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from the editor

JANA JACOBS

Sixty-four years ago, 20 000 women marched on the Union Buildings to protest apartheid pass laws for women. On 9 August we will again commemorate that historic day in 1956 as we celebrate National Women's Day during National Women's month. I will certainly celebrate the incredible fortitude of those women and I think commemorating this day is extremely important. But when it comes to Women's Month, I am more inclined to feel that instead of dedicating a month to recognising women, we should be fostering a society daily, throughout the year, that does so. A society that challenges entrenched patriarchy, among other things, in order to effect true change, instead of placing women in the spotlight for a month, only to return to the status quo on 1 September, as it were. Many may find this belief incredibly cynical.

Be that as it may, I find Women's Month particularly difficult to reconcile with the current circumstances faced by women in this country. A year ago, in this very month, 19-year old Uyinene (Nene) Mrwetyana was raped and murdered at a Claremont post office. Her brutal death galvanised South Africans, who protested against gender-based violence.

The fact is, Nene was just one of thousands of women that fall victim to horrific violence yearly in this country. Daily, we learn another name. On 31 July, the police released SA's crime statistics for 2019/2020. While these stats affirm that our society as a whole remains ravaged by crime – 21 325 people were murdered in 2019/2020, a rate of 58 people murdered daily – a total of 2 695 women were murdered in SA, meaning a woman is killed every three hours, as reported by Africa Check. The police recorded 42 289 rapes over the last year, which equates to 116 daily. And those are just the cases that are reported.

The government responded to the nation's protests in September 2019, with Cabinet releasing a statement lamenting the scourge of gender-based violence in the country. Between 1 October 2019 and 31 March 2020 The Emergency Response Action Plan on Gender-based Violence and Femicide (ERAP) was implemented. In May of this year, a report was released to detail a R1.6bn emergency action plan to combat this crisis. Perhaps it is the cynic in me, but government reports and action plans inspire little confidence.

Then, in June, addressing the nation during the lockdown, President Cyril Ramaphosa called gender-based violence SA's second pandemic. This after another horrific spate of brutal killings of women and children in the two weeks preceding his address. In his speech, the president named the 21 victims. Certainly a stark moment, and an acknowledgment of the crisis that was welcomed by many. But the reality is, a year after the protests that arose from Nene's murder – and those of countless other women – not much has changed.

As we remember the brave and inspiring protest of those 20 000 women, we face a societal crisis that I fear will require far more protests demanding change, due to a lack of action. ■

contents

By Johan Fourie

ECONOMY

Everyone should count

Johan Fourie explains why scrapping Stats SA's income and expenditure survey is a mistake.

We live in a world where information is available at the click of a button. Only three decades ago, a trip to the local library was the only way to know the population size of Portugal or Papua New Guinea. Acquiring information was expensive.

Much of that has changed in the information era. Google processes about 3.5bn internet searches a day, providing a valuable service, but also generating valuable and timeous information. One new research paper shows how Google searches for the loss of smell in eight countries predicted a rise in Covid-19 deaths. Another one shows that Google searches for unemployment insurance in the US predicted the massive rise in job losses and unemployment claims.

Big data allows for 'nowcasting' – the prediction of present trends, providing up-to-the-moment information that can be used in decision-making. While traditional data collection on gross domestic product, for example, takes at least three months to process, scraping price information, sales figures, electricity usage or light density from satellite imagery in real time can produce a close approximation of what is happening in the real economy. The question is: Do we still need the expensive data collection methods of yesteryear?

The answer is an unequivocal yes. Sure, nowcasting is valuable in many settings – faster and cheaper (and sometimes even more reliable) than earlier methods. But there are questions that nowcasting fails to answer – often to do with sampling and representativity; things at the heart of the scientific method.

Take the recent CRAM survey, run by Stellenbosch University economist Nic Spaull and his team of SA's leading development economists. This nationally representative panel survey of 7 000 South Africans will run in five waves and attempts to assess the impact of Covid-19 and lockdown. Participants are asked questions about their health and income. Results from the first wave were published on 13 July.

Are there other ways to identify the effects of the pandemic? Sure. Daily, the minister of health reports the number of Covid-19 infections and fatalities, providing valuable and timely information about the spread and severity of the disease. But not only do these numbers depend on test strategies and hospital reports of varying quality, they also can't answer questions that require a representative sample: Do South Africans know the symptoms of Covid-19? Did they change their behaviour? Can they access medication? CRAM tells us that only one in ten South Africans knows that tiredness is a symptom, only a third reported avoiding large groups and only a quarter have access to medication.

And effects on livelihoods? The indications that lockdown has had devastating consequences on the economy are many, but only a representative survey can tell us just how bad it is and who is most likely affected. CRAM shows employment declined by 18% between February and April, that one in three income earners didn't earn an income in April and that job losses – an estimated 3m in total – were concentrated among the already disadvantaged.

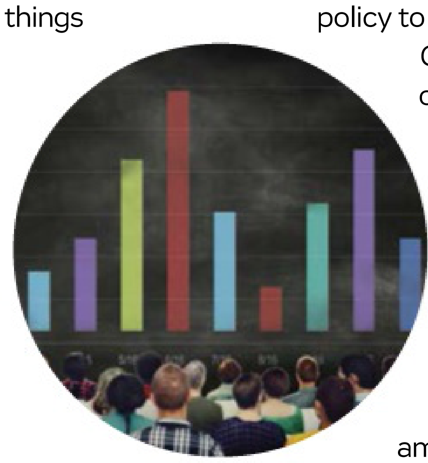
The point is that representative surveys like CRAM allow us to understand the extent of the crisis, enabling us to design better-targeted interventions. The richer the information, the smarter the decisions.

This makes the news that Stats SA, the government's official data collection agency, will scrap the income and expenditure survey this year all the more upsetting. It has been key to understanding the extent of poverty and inequality, and would have provided deeper insights into the devastating effects of Covid-19. But repeated budget cuts have now undermined Stats SA's ability to do its job.

> Shelving surveys is equivalent to burning books. It unjustly amplifies one voice over another.

Amid the escalation of Covid-19 cases, the Stats SA news caused little uproar. That was a mistake. Shelving surveys is equivalent to burning books. It unjustly amplifies one voice over another. It promotes the opinions of the privileged – the powerful, or favoured, or popular – over those of the poor. And it reduces the scientific process to a shouting match.

In *The Sum of the People*, Andrew Whitby explains that surveys or censuses are often considered an instrument of power. And indeed, in the chapter "Paper people", he describes the tragic abuses of census records in Nazi Germany, to give one example. But surveys and censuses, as he notes, can be a tool of the powerless too. In fact, in a world of information overload, the opinions of those with access to power and privilege – the urbanites, the upper classes, the intellectuals, the Twitterati – are preferred above the needs of the uncharted, and often sway public policy to the detriment of society at large.



Consider the case of SA's schools: for months, 'public' opinion has suggested that schools should remain closed, to protect kids and teachers. But CRAM results indicate that 20% of South Africans went hungry in April. Many of those were children. Schools provide essential meals to hungry children. If schools stay closed, child hunger will increase rapidly, with devastating long-term consequences for an entire generation. Many are willing to pay these tragic costs, despite there being no evidence that schools lead to above-average Covid-19 infections among teachers or pupils.

Whereas the privileged can voice their opinions in court filings, newspaper columns and social media – another CRAM finding is that affluent South Africans have exaggerated infection risk perceptions – a voiceless generation of hungry kids can only speak through numbers.

That is why representative surveys and censuses, over and above attempts at nowcasting, are so important. Quantitative social science, with its tools of causal inference, is necessary to test the efficacy of government policies and prescribe more appropriate ones. Treasury's decision to shrink Stats SA's budget – a meagre sum compared with what it will dole out to save SAA – is probably the most fatal blow to poverty alleviation and economic development this country has seen in recent history.

Information is power; to be counted is to count. ■

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Johan Fourie is professor in economics at Stellenbosch University.

Photo: Shutterstock

OLDMUTUAL

STEWARDING A SUSTAINABLE AND RESPONSIBLE FUTURE IN CORPORATE SOUTH AFRICA

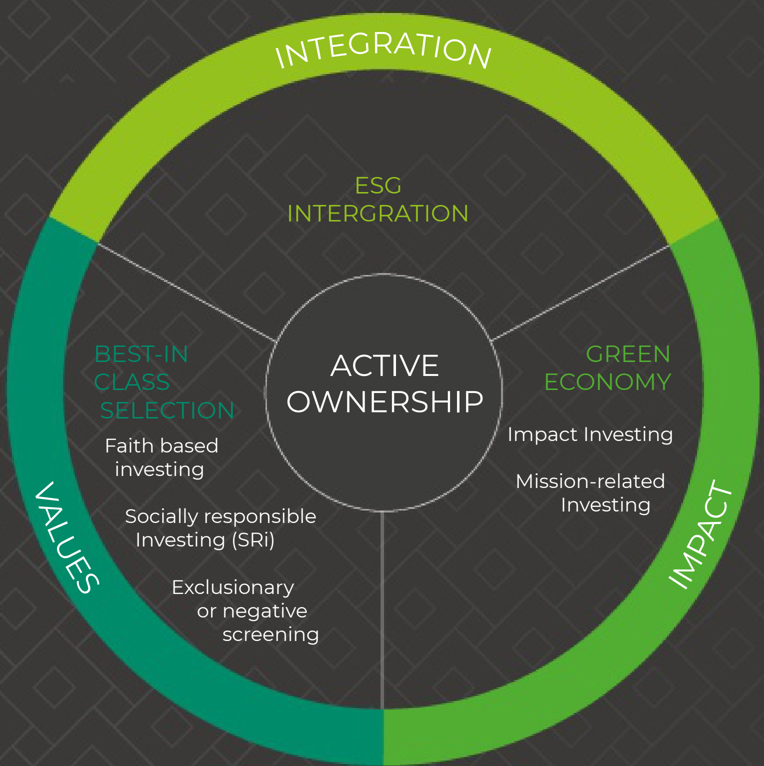
By Robert Lewenson, Head of ESG Engagement, and Jon Duncan, Head of Responsible Investment

After managing Old Mutual Investment Group's (OMIG) stewardship programme over the last five years, the end of 2019 not only marked an important personal milestone for our team, it also gave us the opportunity to reflect on the importance of and the need for stewardship as a solution for our clients' listed equity capabilities. However, there is still much to be learnt and we're working hard to spread clarity and understanding on the solution, beginning with some common questions:

What exactly is stewardship?

Stewardship represents the science of meaningful corporate engagement and aims to promote ESG management practices that encourage long-term value creation for shareholders. Considering the intersection between all the various types of ESG investment strategy –whether an integration, values or impact approach to investment decision-making – active ownership is at the centre; as illustrated in the below diagram.

APPLYING SUSTAINABILITY TO INVESTMENTS



Globally, we have seen an increasing number of large asset owners consolidate their stewardship activities to ensure a consistent outcome. South Africa is no different and we expect more active investors, bigger societal voices and stronger legislative enforcement, to support greater demand for stewardship services. OMIG's engagement activities with companies focus on key strategy and performance issues such as: remuneration policy, climate change, audit quality, board succession, corporate governance, risk management, privacy and data security, to name a few. In 2019 alone, we interacted with 31 companies on 93 material ESG issues.

Why should investors care about stewardship and what solution does OMIG offer?

We are seeing mounting evidence showing increased performance from successful stewardship activities that are collaborative, and with participation from large pension funds/ long-term capital entities. In addition, practicing effective stewardship empowers clients to take action on key ESG issues affecting their listed equity holdings. This is lowering the ESG risk in their portfolio and driving positive change, both at a company level and in terms of market resilience.
With these benefits in mind, we have recently launched our Listed Equity Stewardship service to "crowd in" like-minded collaborative engagement participants, making the industry -competitive stewardship service at OMIG an agent of change. Clients are given access to an experienced team that actively stewards assets in a consistent and transparent manner for scalable impact. Portfolio level reporting is enhanced to meet FSCA requirements and these clients are able to evidence their commitment to responsible investment practices.

What is the total opportunity?

The global investment ecosystem represents US$91 trillion, of which currently about a third is managed in some form of ESG strategy. Therefore, there is still a great opportunity to develop stewardship practices on a global scale.
With approximately R300 billion in listed equity under management, we are excited by the opportunity this service has to effect real change. Looking ahead, we will work tirelessly to allow all our listed equity clients to receive the benefit of a stronger market system, better investment performance and more voices on material ESG issues that impact their portfolios.

By Andile Ntingi

POLICY

What about all the plans?

The ANC's half-hearted economic policies fail to make an impact.

The ruling ANC has an illustrious career in producing policy proposals that never see the light of day. Occasionally, some proposals are implemented half-heartedly, resulting in no meaningful impact being achieved by them.

I was reminded of the ANC's lacklustre track record in implementing its policies when the political party released a 51-page policy document on 10 July, which spelled out proposals aimed at kickstarting the Covid-19-battered South African economy.

Interestingly, the document has a page dedicated to proposed measures that could be undertaken to boost production and investment in the ailing mining sector.

However, the page does not mention anything about the African Exploration Mining and Finance Corporation (AEMFC), the state-owned mining company established in 2011 with the intention to develop strategic minerals with private investors in order to supply them as feedstock to local manufacturers at competitive or discounted prices.

This intervention was necessary to drive the beneficiation of SA's raw materials to help the country make headway in industrial export markets.

In February 2012, the ANC released a research report that recommended that the state-owned mining company (SMC) be used as a main vehicle for increasing government participation in mining, whereby the SMC would hold exploration rights to minerals by having a first-sight of all new state-financed geo-data.

The report was compiled by a group of researchers who studied 12 countries with SMCs, where it was found that some of these countries were moving towards privatising or corporatising their SMCs. These countries provided the lens from which to investigate models of state participation in mining, including nationalisation, which was a hot topic at the time due to left-wing politician Julius Malema clamouring for the seizure of mines without state compensation.

One of the key recommendations of the 2012 report involved the placement of AEMFC under the Industrial Development Corporation (IDC) until legislation was developed to make it standalone.

The researchers felt that the IDC was best-positioned to nurture the company, owing to its vast experience in investing in new mining projects and nurturing them into giants. At the time when the recommendation was made, the IDC held stakes in coal miner Sasol Mining, iron ore producer ArcelorMittal SA, ferrochrome producers Hernic and Merafe, platinum miners Impala and Wesizwe, and aluminium maker Hillside Aluminium.

Although the research paper never spelled out what the strategic minerals are, experts have always considered them to be coal (used for power generation), iron ore (for steel production), and platinum (for use in manufacturing of jewellery, electronics, and automobiles).

While the SMC was introduced in the form of AEMFC, its implementation has been half-hearted, with many of the recommendations in the ANC's research paper having never been pursued.

For example, AEMFC was never moved to the IDC where it could have been pushed to greater heights. Instead it was made a subsidiary of the Central Energy Fund, a parastatal reporting to the department of mineral resources (DMR), where under the then political leadership of minister Mosebenzi Zwane the department allegedly focused on helping the politically-connected Gupta family to buy a coal mine supplying Eskom.

It appears that since its inception, the AEMFC was neglected and as a result degenerated into a laggard, only managing to invest in three operations supplying coal to Eskom.

While Zwane allegedly assisted the Gupta-owned Tegeta to acquire the Optimum Coal Mine from Glencore in 2015, the AEMFC was placed under the leadership of Sizwe Madondo. In March this year, *City Press* reported that Madondo was dismissed by AEMFC after he was found guilty of dishonesty, nepotism, and failing to act in the interests of the company following a disciplinary hearing.

He has been banned from occupying any senior positions at state-owned enterprises after he participated in an attempt to buy Optimum Mine for R1bn, which was liquidated after the Guptas moved to Dubai following allegations of the family's involvement in state capture and grand-scale corruption, facilitated by former president Jacob Zuma.

The AEMFC has been stagnant. In 2016, its three operations, Vlakfontein, Klippoortjie, and T Project employed a total of 320 people. The workforce dropped to 285 in 2019. In 2016, the company generated a profit of R82.4m from a revenue of R376m. In 2019, a profit of R106m was achieved from revenue of R634.9m.

In the policy document the ANC released in July this year, the party is decrying the lack of mining investment and a decline in exploration activity, especially early-stage exploration. But it created the AEMFC to take a lead in facilitating investment alongside private investors. The company does not feature anywhere in the document. Instead, the party is proposing the review of tax policies and fiscal instruments to make the SA mining industry attractive to investors.

The party is also talking about the need to increase mining income to the sovereign wealth fund. Output in the sector is expected to decline by between 20% and 30% this year and 30 000 jobs are at risk of being lost.

On the same day that the ANC released its 51-page document, business lobby group Business for South Africa (B4SA) released its own 111-page document, in which it argued that the decline in mining could be arrested if the government addressed bottlenecks in rail and ports infrastructure. B4SA said if SA's mining laws were simplified and ailing Eskom fixed, the industry could create 70 000 jobs by 2024, contribute R30bn to GDP and R10bn to tax revenues annually.

The AEMFC must be positioned to participate in this growth envisioned by B4SA. ■

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Andile Ntingi is the chief executive and co-founder of GetBiz, an e-procurement and tender notification service.

Photo: Shutterstock

in brief

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"VOLUNTARILY STEP ASIDE."

David Masondo
Deputy finance minister

— **The ANC's integrity committee** wrote to party national executive committee (NEC) member and deputy finance minister David Masondo, asking him to "voluntarily step aside" from his responsibilities in government and the party. Masondo is alleged to have abused state resources to resolve a domestic dispute. The chairperson of the committee, George Mashamba, said Masondo allegedly showed poor judgment in involving the Directorate of Priority Crime Investigations (Hawks) in a domestic matter, which opened him up to accusations that he abused his power and access to state resources. He added that Masondo should have known that the mandate of the Hawks is to probe corruption and offences that fall under the Prevention of Organised Crime Act.

"I've enjoyed the challenge of leading AngloGold Ashanti over these past two years."

— **Kelvin Dushnisky will step down as the chief executive of AngloGold Ashanti,** effective 1 September, according to the gold miner in a statement. A reason was not stated for the sudden change in leadership. The company said Dushnisky leaves AngloGold Ashanti in solid shape, with robust cash flows aiding ongoing debt reduction. Christine Ramon, who is the current chief financial officer, has been appointed the interim CEO while the board of AngloGold Ashanti embarks on a recruitment process to find a new CEO.

"We've seen incremental vaccine improvements, but the market seems to have priced that in for the medium term."

– **Edward Park, deputy chief investment officer (CIO) at Brooks Macdonald Asset Management,** told *The Wall Street Journal* that the mixed picture for global equities reflects a continuing tug of war in markets with push-pull factors remaining the same. The ongoing volatility is viewed as a partial reflection of big institutional investors sitting on the side lines. The Fund Evaluation Group's CIO, Greg Dowling, told the publication that institutional investors are waiting for stimulus, the election and earnings clarity. He said this has contributed to thin trading volume and volatility in stock prices.

THE GOOD

Eskom and the Special Investigating Unit obtained summons in the North Gauteng High Court to recover R3.8bn from former Eskom executives and board members, Gupta family members, their associates, and others. The power utility said the delictual claim for damages suffered relates to the recovery of funds which were allegedly illegally taken from it to help the Guptas and their associates buy a mine that supplied Eskom with coal – including payments to Trillian by Eskom executives. The announcement follows a High Court ruling that found energy regulator Nersa acted illegally when it deducted a R69bn equity injection into Eskom. The ruling allows Eskom to implement a phased recovery of these funds over a three-year period.

THE BAD

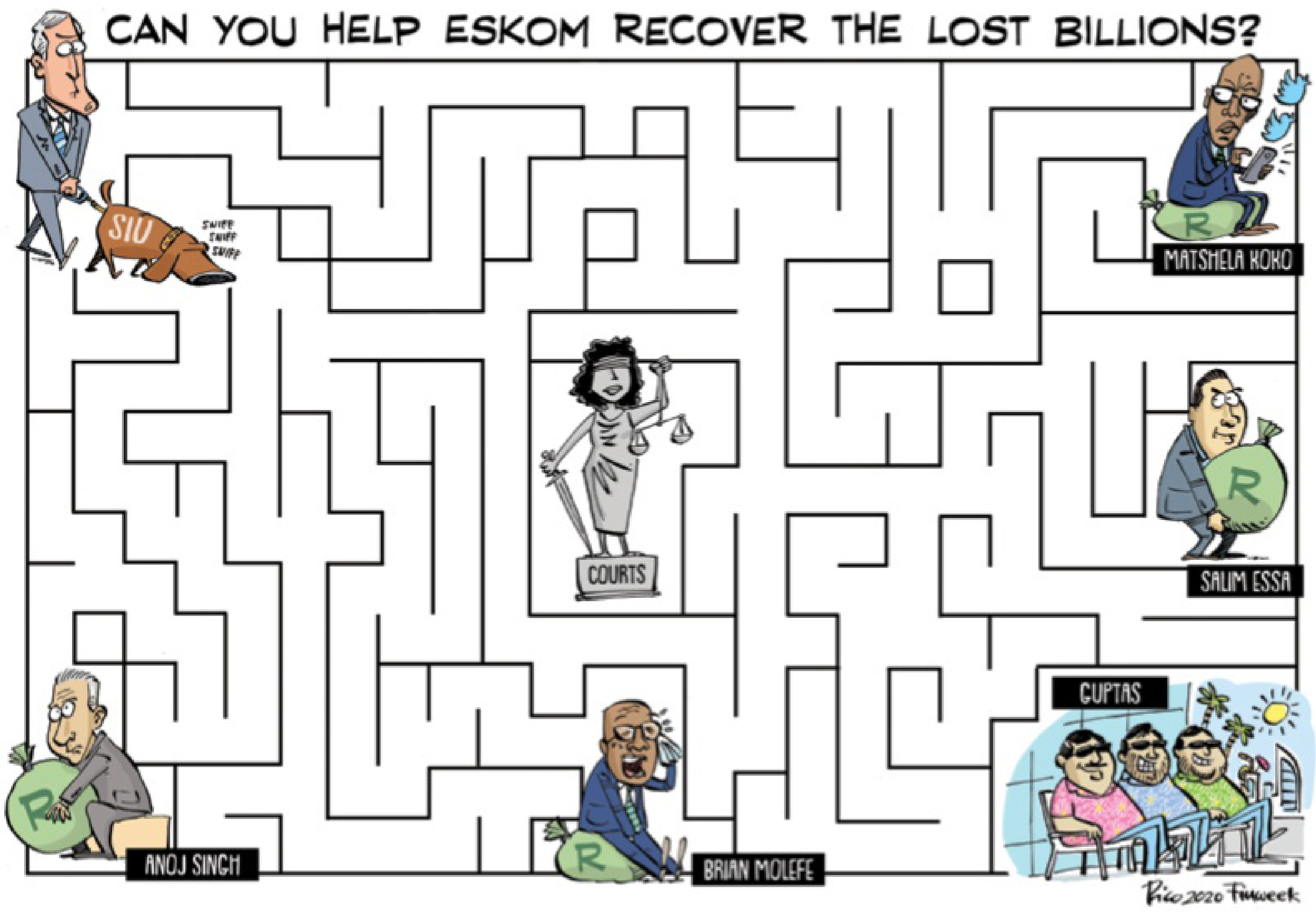
AB InBev-owned South African Breweries (SAB) announced it's scrapping R2.5bn in capital and infrastructure upgrades for 2020 and reviewing another R2.5bn for 2021. The cancellation is attributed to having lost 12 full trading weeks (at 3 August 2020), which effectively equates to some 30% of SAB's annual production, said Andrew Murray, vice president of finance. AB InBev said its SA business was significantly impacted by the lockdown and ban on alcohol sales that began in late March and lasted to end-May. Revenue and volume declined by more than 60%. The second ban on alcohol sales from mid-July will impact results in the third quarter of 2020.

THE UGLY

Murders in South Africa remain high, with a 1.4% increase in 2019/2020, to 21 325 reported cases, according to the latest national crime statistics. The increase works out to 58 people murdered every day, at a rate of 36 people per 100 000 population. Most murders were recorded in KwaZulu-Natal, followed by Gauteng and the Western Cape. Gareth Newham of the Institute for Security Studies told *Daily Maverick* that this increase was the lowest recorded for eight years. The number of murders steadily declined between 1994 and 2012 before continually rising since then. He said this year's figures might suggest murders have plateaued and could decline further if the SAPS makes the necessary interventions.

Photo: Gallo/Getty Images

DOUBLE TAKE BY RICO



BIGGEST EMERGENCY FINANCING YET

R72bn

South Africa was granted a $4.3bn (R72bn) loan from the International Monetary Fund (IMF), the single biggest allocation of emergency financing from the fund yet for a pandemic-hit country. The loan is to help fill urgent balance of payments needs due to the pandemic and to contain the economic disruption and its regional spill-overs. SA also borrowed R5bn from the African Development Bank and $1bn from the New Development Bank. Sars Commissioner Edward Kieswetter told Bloomberg that the national lockdown led to a tax underrecovery of R82bn for the fiscal year through 15 July, meaning the tax shortfall takes up over 80% of the combined three loans.

QUARTERLY LOSS

-$1.1bn

Exxon Mobil, the largest US oil company, posted a quarterly loss (of $1.1bn) for the second consecutive quarter for the first time this century, compared with a profit of $3.1bn a year ago, reported *The Wall Street Journal*. Exxon Mobil's chief executive, Darren Woods, said the global pandemic and oversupply conditions significantly impacted second-quarter financial results with lower prices, margins, and sales volumes. Royal Dutch Shell and Total also reported significant second-quarter losses as the impact of the pandemic and a worsening long-term outlook for commodity prices spurred them to write down the value of their assets.

MOST DOWNLOADS EVER

315m users

Microsoft is in advanced talks to acquire the US operations of the Chinese-owned video app TikTok, people with knowledge of the discussions told *The Wall Street Journal*. The publication reported that the sale to Microsoft (likely for billions of dollars) would make the software giant a major player in social media. TikTok, known for its catchy dancing and lip-syncing videos, has soared in popularity during the pandemic. About 315m users downloaded it in the first quarter of 2020, the most downloads ever for an app in a single quarter, according to research firm Sensor Tower, bringing its total to more than 2.2bn globally.

GOLD MINING INDEX SURGES

100%

Investors continued to flock to gold stocks as a safe haven. The JSE's gold mining index, which represents South Africa's top five gold mining companies, surged over 100% since the beginning of the year to the end of July. The spot price of gold broke through $2 000/oz for the first time on 4 August. According to a report by Renaissance Capital, the price could average $2 000 per ounce during 2021. The authors said the sector's earnings growth is largely driven by margin expansion due to higher gold price expectations and aided by weaker producer currencies.

By David McKay

MINING

Women step out of the shadows on Kumba exploration project

Kumba Iron Ore is drilling at two new sites in a bid to extend the lives of two of its largest assets in the Northern Cape. And there's an all-women drilling crew on board.

In early 2018, JSE-listed Kumba Iron Ore said it was considering a 'step-out' strategy, having in the previous year restructured its Sishen mine in the Northern Cape – a move that cut the operation's life to 13 years from 17 years previously.

The strategy was about exploring for new resources and included possible acquisitions that Themba Mkhwanazi, CEO of Kumba, said at the time would be opportunistic. That strategy is now bearing some fruit following the announcement in July of its R7bn Kapstevel project – an exploration project that will extend the life of Kolomela, another of Kumba's mines.

Members of the all-female Kapstevel South project drilling exploration crew at Kumba Iron Ore's Kolomela mine.

The company also disclosed it was drilling on two other projects – Ploegfontein and Heuningkrans in the Northern Cape. These are recent property acquisitions that, if developed, will help Kumba take the average life of its Sishen and Kolomela mines from their current 13 years to 20 – an effort that will absorb R200m in exploration budget annually.

Extending the life of iron ore – a commodity the price of which is soaring amid major supply interruptions in Brazil – is a shuddering no-brainer for Kumba and its 70% shareholder, Anglo American.

The Northern Cape is rich in iron ore, which is used in making steel, not to mention other minerals, which Mkhwanazi intriguingly said might also fall in the remit of Kumba, in time. So, it makes sense to be securing the firm's future, given the health of iron ore's economics and the type of iron ore Kumba produces. This is high-value, so-called 'lumpy' iron ore that burns more efficiently in furnaces with a better carbon footprint than 'fines' iron ore that is supplied by much of the firm's competitors.

So, with the admittedly unglamorous activity of drilling such a central part of Kumba's future, it's fascinating to see the establishment of the firm's – and possibly SA's – first all-women drilling crew, handed the responsibility of solving the mining firm's existential questions by Kumba's drilling contractor, Rosond.

According to Stuart MacGregor, head of exploration for Kumba, the mechanisation of drilling has helped women step out of the shadows because it has removed some of the heavy lifting that may have been a deterrent in the past.

While the all-women crew comprise just four of some 100 employees that Rosond has on the Kumba project team, there's an aspiration to have women represent 25% to 30% of the total drilling team in time.

"There's quite a bit of competitiveness between the women and the men. You know the men don't want to be outdone," said MacGregor in an interview with *finweek*. But there are already clear benefits: women operate the machines with more care. This confirms a finding of the SA chapter of 'Women in Mining', which said women in mining tend not to break machines; that makes them more capital efficient than their male counterparts.

"The work they are doing is diamond drilling, pressure drilling ... the first stage of finding resources. There are currently 32 drilling teams working on one project, so this is a major push drilling thousands of metres," said MacGregor.

Exploration drilling doesn't require tertiary education, which means there's reach into the community at exactly the level where new employment has the most benefit for SA. "It's great to see," said MacGregor. "The women are coming in, drawing a salary and growing in confidence." For Kumba, women comprise about 24% of total employees. ■

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While the all-women crew comprise just four of some 100 employees, there's an aspiration to have women represent 25% to 30% of the total drilling team in time.

Photo: Supplied

By David McKay

MINING

‘The approach is to make hay now’

Royal Bafokeng Platinum’s chief financial officer explains that the miner’s minimum-dividend policy, among other things, aims for sustainability in an uncertain environment.

Royal Bafokeng Platinum’s Styldrift is a mechanised underground mine located in the North West Province.

Hanré Rossouw, chief financial officer of Royal Bafokeng Platinum (RBPlat), knows a thing or two about dividend disappointment.

As a former portfolio manager for Investec Asset Management, he recalls the train smash that was the mining sector in 2015/2016. One by one, the world’s mining majors dropped the notion of ‘the progressive dividend’, a belief that payouts could be sustained on the evergreen, double-digit growth of China.

“That kind of thing breaks so much trust,” says Rossouw of how investors responded to that mining industry crisis. It could be argued that investor trust was only truly won back last year, and only after mining firms bore down on billions of dollars in debt, a painful process of restructuring.

And then came Covid-19.

In the current environment, where uncertainty is the watchword, it doesn’t make sense to invest in long-lead projects or incur heavy capital costs.

It’s for this reason that he thinks the 10% of cash flow dividend policy adopted at the beginning of RBPlat’s 2020 financial year in March is the best route. He disagrees that as a policy it marks the company out for undue conservatism at a time when buckets of money are being dished out by other mining firms.

“We chose 10% as a bare minimum. We’ve gone for sustainability. Come hell or high water, we will always pay that. We can increase the proportion of cash paid out to 20% or 30% and if there’s surplus we can also declare a special dividend. We aren’t boxed in,” he says.

The expectation raised by RBPlat is, in fact, that it’ll exceed the 10% payout ratio. The company’s R12bn Styldrift expansion, having been completed last year, is currently in ramp-up mode and – for the first time – made a contribution to interim earnings (it made an earnings before interest, tax, depreciation and amortisation contribution in the previous reporting period).

Some 45 days lost to the Covid-19 national lockdown called by the government in March and then the failure of Anglo American Platinum’s refining facilities, which buys RBPlat’s concentrate production, has also created some capital build-up of R3.3bn yet to flow through to the balance sheet, which ended the six months with R1.5bn in cash and about R700m in net cash – a R1.2bn period-on-period turnaround.

Hanré Rossouw
Chief financial officer of Royal Bafokeng Platinum

> The expectation raised by RBPlat is, in fact, that it’ll exceed the 10% payout ratio.

“We’re looking for a really good dividend then,” said Arnold van Graan, an analyst for Nedbank Securities. Rossouw managed a sheepish grin in reply. Said Rossouw: “We’ve come out of some difficulties; we’re coming out of project-mode to cash-return-mode.”

RBPlat may look at “small optimisations” it could make to the way it operates such as an expansion of its concentrator facilities, or to get more volume from Styldrift by accessing the shaft held in Maseve, a mine acquired from Platinum Group Metals in 2018, principally to access its concentrator capacity. These are not big-ticket capital projects, but they may widen the margin.

Set against this is the volatility in the platinum group metal (PGM) markets. Platinum, once the revenue staple, comprised only 28% of RBPlat’s revenue in the six-month period compared with 41.3% in the first half of 2019.

It has been overtaken by both palladium and rhodium, previously a small constituent of the PGM family but with a track record for suddenly lurching into massive deficit, as it has now against tightening emission standards in China. Rhodium’s role in the production of auto catalysts, therefore, has presented it with a key role.

Who knows where the PGM market is heading in the long term? How will electric vehicles change demand for metals primarily set up to supply traditional combustion engines?

“That is why the approach is to make hay now,” says Rossouw. ■

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Photos: bafokengplatinum.co.za

Transformation is a business

Isuzu Motors South Africa has received an industry-leading level 1 on its B-BBEE scorecard for 2020. transformation to be embraced beyond this scorecard as well.

Billy Tom officially assumed full responsibility as Isuzu Motors South Africa CEO and managing director on 1 July 2020.

Isuzu Motors South Africa's third broad-based black economic empowerment (B-BBEE) audit ended on a high note for the automotive manufacturer, with it attaining an automotive industry-leading level 1 on the scorecard for 2020.

This is a remarkable achievement, considering that Isuzu Motors South Africa was only launched in January 2018, says Billy Tom, newly-appointed chief executive officer and managing director of the company.

"We have embraced transformation as a business imperative and our new scorecard reflects the good business practices that we have implemented in support of this. We regard transformation as critical to ensuring the sustainability of our business, while at the same time it reflects our commitment to being part of the transformation of our country."

According to Tom it is important that transformation is adopted by businesses as a pragmatic growth strategy geared towards realising the country's full potential by bringing more South Africans into the economic mainstream. "Furthermore, to help drive this change, South Africans should support businesses that are actively contributing towards the transformation and growth of our local economy."

He emphasises that while he was pleased with the company's performance to date, the company's transformation journey was only just starting. "The focus going forward will be to continue to implement initiatives which will further transform our business and also that of our entire value chain. We must all operate in line with the demographics of South Africa and be tuned in to the needs of our diverse customer base."

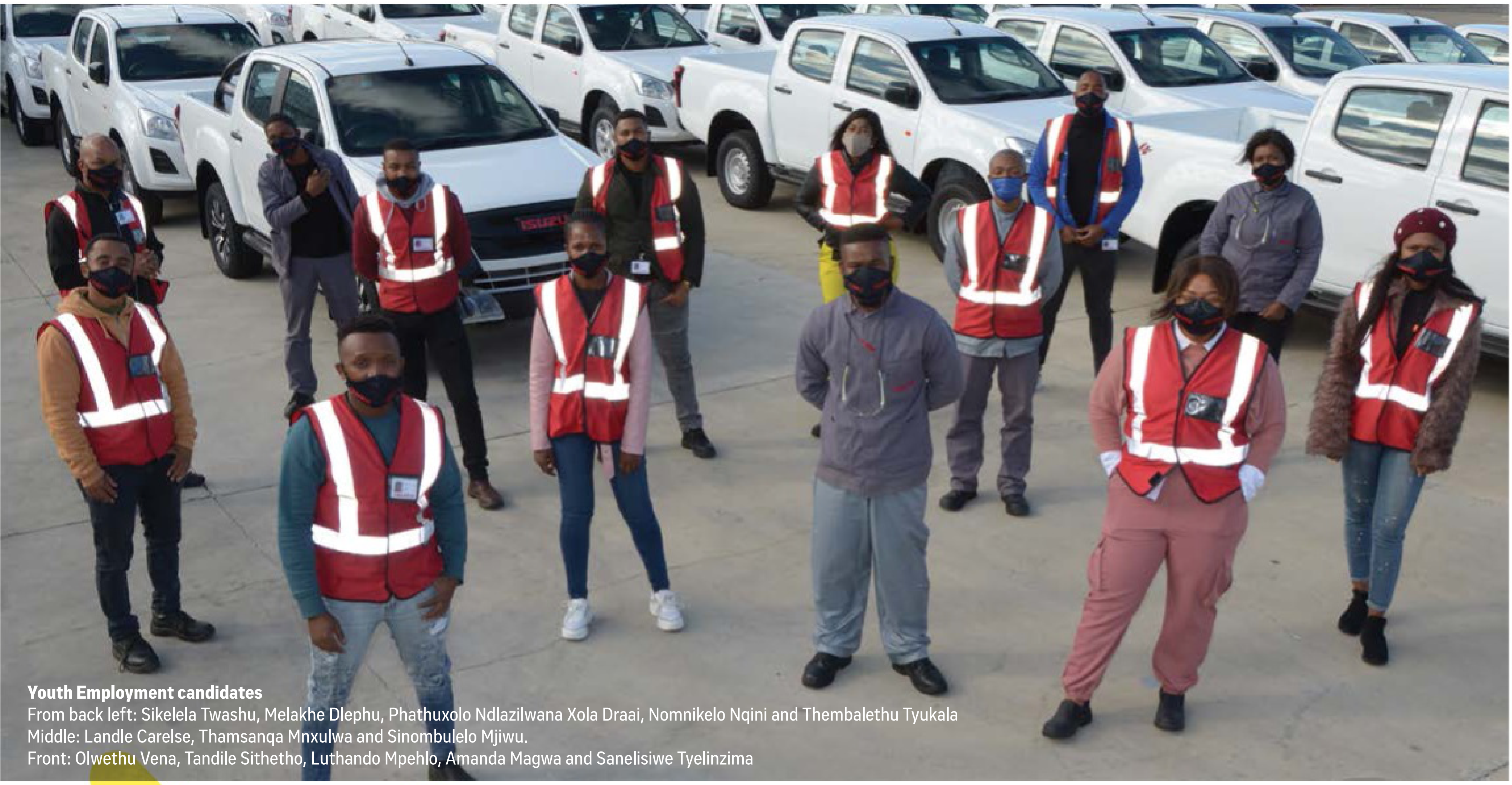
Elvis Hermans, Isuzu's senior vice president for human capital and corporate services, says this achievement is the result of a number of critical actions and decisions taken over the last 12 months to ensure Isuzu's alignment to the country's transformational and economic progression goals. "We are committed to the growth and development of our people, our dealers and our suppliers. To this end we set ourselves rigorous goals and have acted swiftly in implementing the right strategies to achieve these goals," says Hermans.

Isuzu recently became a participant in the Automotive Industry Transformation Fund (AITF), which was established by the department of trade, industry and competition to support the transformation of the automotive industry value chain. "We will be working closely with the AITF to further support supplier and dealer transformation initiatives, as well as the deepening of the localisation of components, which is a pillar of the Automotive Industry Master Plan," emphasises Hermans.

As a first, the company supported the Youth

imperative for Isuzu

Newly-appointed CEO and managing director Billy Tom reflects on this and why it is important for



Youth Employment candidates
From back left: Sikelela Twashu, Melakhe Dlephu, Phathuxolo Ndlazilwana Xola Draai, Nomnikelo Nqini and Thembalethu Tyukala
Middle: Landle Carelse, Thamsanqa Mnxulwa and Sinombulelo Mjiwu.
Front: Olwethu Vena, Tandile Sithetho, Luthando Mpehlo, Amanda Magwa and Sanelisiwe Tyelinzima

"We must all operate in line with the demographics of South Africa and be tuned in to the needs of our diverse customer base."

Employment Service (YES) Programme this year with the placement of 72 candidates, thus offering young South Africans paid work experience, while creating a pipeline of talent for the future. "We will continue to place emphasis on this important initiative, which is already resulting in tangible benefits for these young people and our business," says Hermans.

Furthermore, Isuzu's community development programmes are similarly aimed at the development of young South Africans, especially in the fields of mathematics, science and engineering and the preservation of our natural resources and the environment, while providing disaster relief to communities in crisis.

Tom feels passionate about the company's responsibility to help uplift and grow the economy. "We should always remember that an economy cannot grow by excluding people and that an economy which is not growing, cannot integrate all of its citizens in a meaningful way."

He added that it was important that transformation was also embraced beyond the B-BBEE scorecard to adopt an approach of greater flexibility, adaptability and openness in responding to the rapid changes happening in our environment due to Covid-19.

"Given the seismic shift happening around the globe, and within our industry, we need to rethink and reshape how we do business going forward. Alongside this, we need to ensure that we understand how our customers' needs are changing and how we have to respond to this." ■

market place

FUND IN FOCUS: MOMENTUM TRENDING EQUITY FUND

By Timothy Rangongo

Withstanding adverse market conditions

Aiming for high, long-term capital growth by applying a momentum-based investment strategy to JSE-listed shares.

FUND INFORMATION:	
Benchmark:	FTSE/JSE Capped SWIX Index
Fund managers:	Loftie Botha and Imtiaz Mohammed Alli
Fund classification:	South African – Equity – General
Total investment charge:	0.69%
Fund size:	R2.87bn
Minimum lump sum/ subsequent investment:	R2 000/R250
Contact details:	0860 111 899/ci.clientservice@momentum.co.za

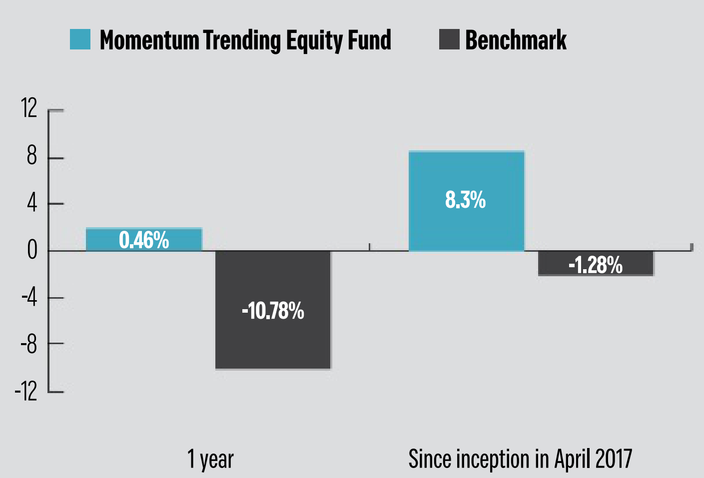
TOP 10 HOLDINGS AS AT 30 JUNE 2020:

1	Naspers*	12.79%
2	British American Tobacco	6.31%
3	Anglo American	6.26%
4	Prosus	5.23%
5	Bidcorp	4.69%
6	BHP	4.22%
7	Impala Platinum	3.94%
8	Gold Fields	3.88%
9	Anglo American Platinum	3.80%
10	Clicks	3.72%
	TOTAL	**54.84%**

*finweek *is a publication of Media24, a subsidiary of Naspers.*

PERFORMANCE (ANNUALISED AFTER FEES)

As at 30 June 2020:



Fund manager insights:

Momentum's Trending Equity Fund comprises a South African equity portfolio with no restrictions on how much exposure the fund can have to different sectors. As at end-June, the top three sectors in terms of equity allocation were resources at 37.59%, followed by technology at 18.02%, and financials at 15.95%.

The fund's objective is to achieve high, long-term capital growth by applying a momentum-based investment strategy to shares listed on the JSE through a smart beta investment methodology. Momentum explains this as an investment style where the manager captures market factors to take advantage of perceived systematic biases or inefficiencies in the market.

The portfolio targets stocks that exhibit robust price momentum, which is defined in terms of a composite of price momentum and earnings momentum as measured by analyst revisions. The universe of listed shares is screened on these momentum parameters; a portfolio with strong momentum factors is then constructed on this basis.

It is this investment process that helped the fund outperform its benchmark amid a volatile local investment climate this year, according to Loftie Botha, one of the fund's managers. "We continuously tilt the portfolio towards shares that have positive price and earnings momentum. This strategy works due to herd behaviour," he says.

"Some investors and analysts lead and act first on new information while others follow. This creates trends that our investment process capitalises on."

One of the equity holdings that proved the most challenging to manage thus far, for instance, has been Sasol, the share price of which collapsed from R303 in December 2019 to a low of R37 in March 2020 (down 88% over the first quarter), says Botha.

"We were underweight Sasol, which served us well over the first quarter, but we missed out on the second quarter's spectacular price movement. However, Sasol is still down 56% over the first six months of the year, meaning our underweight position still added value to our clients."

Although blue-chip stock Naspers performed well and remains a considerable holding for the fund, the position was reduced to 12.79% in June, because "from a risk perspective, its weight had become too large in the fund", says Botha.

Due to its momentum-based investment process, the fund is presently underweight on financial stocks, of which Botha says fundamentals will eventually improve. The fund's approach is to wait for prices and consensus earnings forecasts to trend upwards before they increase the portfolio's weight to the sector.

Why *finweek* would consider adding it:

The fund provides access to high-quality local stocks that held up well during the first quarter's market sell-off, including a strong rebound by resources as the demand outlook for commodities improved due to a resurgent Chinese economy and the easing of restrictions elsewhere. ■

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SHOPRITE

BUY SELL HOLD

By Simon Brown

Still staying true

The Shoprite* trading update for the year ending June was decent. Headline earnings per share (HEPS) from continuing operations are expected to range between 1.6% lower and 6.4% higher than a year ago. The update includes a R327.2m expenditure towards Covid-19 safety preparations and Covid-19 bonuses to staff. It also notes 66 days of no liquor sales and an ultimate 29.5% decline in this sector in the second half of the financial year. Liquor sales had been growing at over 20% prior to the government-imposed ban on alcohol trading and represents some 5.8% of the group's South African sales.

The share has been struggling lately but, taking HEPS at the mid-range results in a price-to-earnings (P/E) ratio of around 13.5 times. For Shoprite this is cheap, albeit that for a large food retailer it's probably around where it should be trading at.

As an investor you hold a large food retailer because people will always have to eat. Shoprite's scale enables aggressive pricing and customer loyalty with new innovations, such as 60-minute deliveries proving extra helpful during a pandemic. I've held Shoprite for almost 20 years and will add on any price weakness ahead of their next results in September. ■

**The writer owns shares in Shoprite.*

Last trade ideas

- BUY — Pan African Resources, *30 July issue*
- BUY — Purple Group, *16 July issue*
- CAUTION — Banks, *25 June issue*
- CAUTION — Hospital Groups, *4 June issue*

MTN

BUY SELL HOLD

By Moxima Gama

Regaining its losses

Mobile operator MTN expects its HEPS for its six months to end-June to rise by as much as 125%, thanks to favourable foreign currency gains. MTN Ghana also grew its after-tax profit by 52.3% to R2bn in its year to end-June, from strong growth in data demand and digital revenue. This is due to an increase in smartphone usage and new gaming offerings.

Active digital subscribers in Ghana grew 44.5% to 2.2m – performance supported by the expansion of the company's digital portfolio, including the renewal of their MyMTN app and launch of the Ayoba messaging app, which allows non-smartphone users to communicate with smartphone users via the app.

How to trade it:

MTN has been steadily regaining its previous losses since testing an all-time low at 2 625c/share. Upside above major resistance at 5 825c/share would indicate an increase in buying appetite. MTN is currently trading close to that level.

Long positions should be initiated at any level above 5 825c/share as the current recovery uptrend formed within its major bear trend could be extended. In March, MTN gapped downwards and since gaps are usually closed at some point, continued upside should see MTN retest resistance at 7 875c – thereby closing the gap. It could even retest the resistance trendline of its bear trend. Breaching that should prompt further gains to 9 075c/share.

Refrain from going long if MTN should capitulate below 5 825c/share. Support at 4 980c/share could be retested. Next support would be at 4 200c/share. ■

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Active digital subscribers in Ghana grew

44.5%

to 2.2m – performance that was supported by the expansion of the company's digital portfolio.

Last trade ideas

- BUY — South32, *30 July issue*
- BUY — Woolworths, *16 July issue*
- BUY — Telkom, *25 June issue*
- BUY — Distell, *4 June issue*

Photos: Archive | Shutterstock

By Moxima Gama

ASTRAL FOODS

Is a bear on the horizon?

South Africa's largest listed poultry producer, Astral Foods, saw its share price decline by 36% since the beginning of the year. The company recently said that it bought a 6.4% stake in listed egg producer Quantum Foods in a bid to protect its long-term broiler supply agreement with the latter.

52-week range:	R129.76 - R222.52
Price/earnings ratio:	8.3
1-year total return:	-12.18%
Market capitalisation:	R6bn
Earnings per share:	R16.77
Dividend yield:	3.04%
Average volume over 30 days:	183 218

SOURCE: IRESS

ASTRAL FOODS

SOURCE: MetaStock Pro (Reuters)

Outlook: In May the company opted to hold on to its interim dividend as it braces for the economic fallout from the Covid-19 pandemic. Already the company faces an oversupply of fresh chicken in the market, which is expected to dampen demand for higher-margin products.

Despite being an essential service as a food producer, the group faces the prospects of higher input costs as global supply chains were disrupted, and local load-shedding problems have also increased costs in its six months to end-March.

On the charts: Astral has turned bearish in its primary bull trend. It has formed a head-and-shoulders pattern and has breached the neckline (red trendline), which is a bearish formation. The support trendline of its major bull trend (black bold trendline), which takes precedence, may, however, curb a sell-off – thereby retaining the primary trend. Failing which, Astral would fall further.

Go short: If Astral defies the support trendline of its primary bull trend, the objective of the head-and-shoulders pattern may well be fulfilled. The trendline would be breached below 11 480c/share – start reducing long positions. A negative breakout of the trend would be confirmed below 7 300c/share and downside to 3 130c/share would be possible.

Go long: The head-and-shoulders pattern would be negated above the final shoulder at 22 255c/share. Such a move could see Astral's share price recover its losses towards its all-time high at 33 520c/share. Upside through 17 100c/share would mean Astral is retaining its long-term bull trend. ■

TIGER BRANDS

Look out for breakout

Tiger Brands, South Africa's largest listed food producer, has lost more than half its value over the past five years as a disease outbreak, linked to some of its processing plants, and troubles at its former Nigerian unit, hit investor confidence. The stock is down 17% this year.

52-week range:	R143.81 - R240.00
Price/earnings ratio:	16.2
1-year total return:	-19.26%
Market capitalisation:	R32.8bn
Earnings per share:	R10.61
Dividend yield:	2.52%
Average volume over 30 days:	549 245

SOURCE: IRESS

TIGER BRANDS

SOURCE: MetaStock Pro (Reuters)

Outlook: Tiger Brands is in the process of selling its value-added meat products business. This unit was at the centre of the world's largest listeriosis outbreak a couple of years ago. The company is facing legal claims after several people died. Tiger Brands received offers from two parties for the acquisition of separate parts of the business, it said in May.

On the charts: Tiger Brands' share price is currently teetering on the resistance trendline of its bear trend. If the three-week relative strength index (3W RSI) continues to form rising bottoms (refer to blue arrows), a positive breakout will most likely be confirmed soon.

Go long: A positive breakout of the current bear trend would be confirmed above 19 825c/share – thereby ending two years of bearish sentiment. Upside to 24 000c/share would be possible and breaching that level should extend gains further towards 29 350c/share.

Go short: Refrain from going long if Tiger Brands should fail to trade above 19 825c/share and falls through the 14 380c/share key level instead. Support at 9 025c/share could then be targeted. ■

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Moxima Gama has been rated as one of the top five technical analysts in South Africa. She has been a technical analyst for 12 years, working for BJM, Noah Financial Innovation and for Standard Bank as part of the research team in the Treasury division of CIB.

By Simon Brown

STOCK MARKETS

Where did all the listings go?

As stocks continue to slide off exchanges across the world, new ways of start-up investing are popping up. But they're still few and far between.

For the past year or so there's been a tweet that frequently pops up in my Twitter timeline, stating that in 1999 the JSE had 668 listed companies and now has 351. I haven't verified the information, because it makes sense to me. It's not a regulation or a red tape issue. It's not even a South African issue. It's a global phenomenon.

In November 2017, research by the US-based Vanguard Asset Management – with $6.2tr under management at the end of January – found that in 1996 the US had over 7 000 listed companies, but by 2016 this number had fallen below 3 800. (You can access this research on this link: https://bit.ly/listingsPDF.)

It may be different timelines, but it shows the same trend. A trend that has accrued for several reasons.

The first was the listing boom and the dotcom bubble at the end of the previous century that led to an expansion, which meant the Nasdaq doubled in value in 1999. Even locally we saw a flood of listings that were not just tech stocks. We even had a second-tier banking boom that ultimately ended in tears.

But there are other reasons, such as companies' easier access to cash. Typically, a listing is a way to raise capital or a chance for the company's founders and early investors to exit their investments. But as I have written before, we're seeing listings happening later in a company's life and in many cases no longer happening at all.

The easy access to cash is in part driven by low interest rates that existed even before we saw the quantitative easing by central banks in response to the global financial crisis of 2008 and 2009, albeit those interest rates were not nearly as low as we've been seeing over the last decade.

The tech bubble, and tech sector in general, has over the last two decades created a vast pool of extraordinarily rich individuals who could easily sell a business for $100m (or in some cases even for billions of dollars). These sellers have now ventured into their own angel and venture funding setups. We also have a few individuals with unimaginable wealth, which has enabled them to fund new ventures from their own pockets.

The space ventures by Jeff Bezos (who funded the start of Blue Origin 20 years ago) and Elon Musk (who started SpaceX 18 years ago) have largely been funded out of their own pockets. If they'd started these businesses back in the 1980s or 1990s, they most likely would have had to go to the stock market to raise the capital required. By doing so, they would have given investors the opportunity to invest into these businesses.

Today, we also have a huge pool of private equity funded by banks, individuals and states – such as Norway and Japan – that are pouring money into new start-ups and even more mature ventures.

We also see large companies who now run venture-capital type investment pools. Naspers*, for example, has its own Naspers Foundry, which recently invested $5.6m into a start-up called Aerobotics. A decade or two ago, to raise that sort of capital, Aerobotics would likely have had to list on the stock exchange. Now it's just one of many examples of beneficiaries of private funding.

The concern of the original tweet does, however, remain. Our investable markets are shrinking, and this reduces investment options for investors.

Even worse news is that there's not very much we can do about it. Most private investors are not able to invest in venture-capital funding companies now that we do have enough capital to do undertake our own risk-adjusted venture-capital funding.

There are, however, companies that allow for co-investing in venture-like funds. For example, there is the Sygnia Oxford Sciences Innovation Fund that has rights to intellectual property coming out of Oxford University. This fund gives investors some level of access to start-up investing. But, in general, there are few good options like this.

At the end of the day, as an investor who only invests in listed investments, I have fewer options. Hopefully, we'll see some more innovative investment options such as the Sygnia fund, but I fear the trend of fewer listings is only likely to worsen. ■

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Photo: Shutterstock

Our investable markets are shrinking, and this reduces investment options for investors.

By Schalk Louw

GOLD

A dollar-driven rally

The price of gold continues to surge as the US prints money to stave off economic hardship. Schalk Louw explains what this means for investors – and South Africa.

For thousands of years the glamour of gold has attracted and captivated humans and even caused conflict. But during the 19th century, the role of gold changed dramatically by becoming the world's official means of payment – not necessarily via direct trade, but in the form of "promises". The gold standard basically meant that you could redeem this promise in the form of a note at any central bank for its weight in gold, which, at the time, was linked to a specific currency.

The role of gold in developed economies changed with the outbreak of World War II. By the end of the war, the Bretton Woods monetary system was implemented, which came to an end in 1971 when the US decided to no longer convert dollars to gold. The fiat currency has since replaced the gold standard.

Recently, however, gold has made headlines for the first time in nearly ten years by exceeding all-time highs last reached in 2011. When the US found itself in a financial predicament along with the rest of the world during the great recession in 2008, the first economic stimulus (later known as quantitative easing) was implemented by then president George W. Bush. The M2 money-supply growth reached new highs (of more than 10% year-on-year), as with the 2001 recession, and as more US dollars came into circulation, the value of the dollar started to decline. Even though the great recession came to an end in the US in 2009, the repercussions of the credit crisis were still noticeable in other countries around the world for years to come.

Various European countries, including Ireland, Greece, Portugal and Cyprus were not able to service their government debt between 2010 and 2014 and this forced the EU to rush to their aid. As fears surrounding this crisis mounted, the safety of gold came back into favour. This caused the gold price to reach a high of $1 921/oz on 6 September 2011.

Printing all this new money and lowering taxes and interest rates were not long-term solutions, and while government debt continued to rise, these measures, much like a painkiller, only provided short-term relief. Gold was no longer necessary and by 2015, its price declined to just above $1 000/oz.

One thing that remained clear, was that even though the dollar was no longer linked to gold, they still moved hand in hand. For the US, this was largely beneficial, and it probably would have stayed that way, but then Covid-19 broke out. With economies under lockdown, the US is yet again forced to borrow trillions of dollars to fund its stimulus package. By June this year, the US budget deficit has only experienced a greater shortfall on five prior occasions in history. They are back to printing more money, but that's not all – for the third month in a row, this money-supply growth has reached new heights.

Now the M2 money supply isn't growing by 10.5% year-on-year as it was during the recession of 2001, nor is it growing by 11% as it was during the credit crisis of 2009. It was growing by more than 24% year-on-year up until the end of June 2020. As more and more dollars are being circulated, the dollar is again starting to lose its value, as happens with most things that there's too much of. And as much as people would like to point out that the dollar is no longer linked to gold, the gold price keeps on running as the dollar's value declines.

Where does this leave us? When we look at the gold price relative to the euro-dollar exchange rate, we will see that similar movements were experienced in 2011, even though the past is never an indicator of the future; those with a more technical approach might tell us that now is a good time to say goodbye to our gold investments.

The fact is that Fed chairman Jerome Powell already promised that the central bank will "do whatever we can, for as long as it takes", and he admitted that they were working on another stimulus package, which will probably see trillions more being borrowed, and will cause even more dollars to come into circulation. Do I think that gold is in overbought territory? Definitely. But I also think that it's dangerous to jump in front of this gold train now and call it a peak. It still has a few more legs to run on before it completes the race. It has breached an important psychological level of $2 000/oz, taking its gains for this year to almost 33%.

If gold shines even brighter, it can also cause the rand to shine. After all, as at the end of 2019,

7.25%

of the total SA GDP consisted of mining operations in general.

But where does this leave South Africans? In terms of worldwide gold production, South Africa was still the eighth-largest gold producer in 2018 and accounted for roughly 4% of worldwide production. Aside from the dollar's decline (which means a strengthening of the rand's value), this environment will be positive for SA gold mines, which will mean further inflows for the country, and which can bring about further strengthening of the rand.

Along with calling the current gold price a peak, investors also must be careful of calling the recent rand strengthening nothing but short-term luck. If gold shines even brighter, it can also cause the rand to shine. After all, as at the end of 2019, 7.25% of the total SA GDP consisted of mining operations in general. ■

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Schalk Louw is a portfolio manager at PSG Wealth.

Photo: Shutterstock

finweek
COLLECTIVE INSIGHT
INSIGHT INTO SA INVESTING FROM LEADING PROFESSIONALS
AUGUST 2020

IMPACT INVESTING

HOW TO BETTER MEASURE THE VALUE AND IMPACT OF YOUR INVESTMENTS

Inside

By Deslin Naidoo

INTRODUCTION

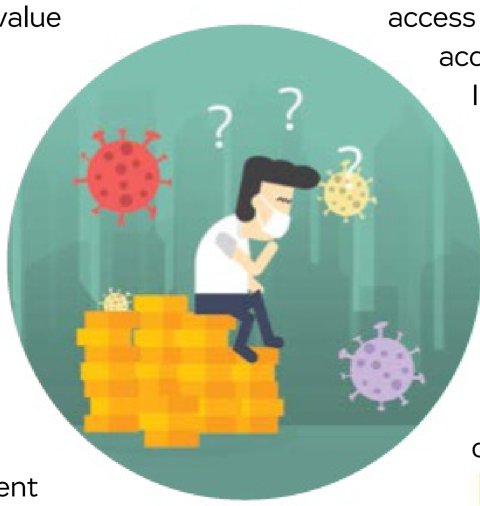
Impact investing: Not a tick-box exercise

The importance of investing for sustainability has been brought to the fore by the coronavirus pandemic.

There is no easy answer when forced to choose between life and living; and it is this choice that has resulted in 3m jobs being lost in the last three months.

The economic lockdown has created a plethora of emotions within all of us – despondency, frustration, mistrust, anger and rage. However, our emotions will not wash away the challenges that now face all of us. South Africa's greatest task right now is to create a functioning economy again, which has sparked innumerable debates across government, business and citizens.

At the beginning of this year, the *Collective Insight* team did not realise how apt the chosen topic, "How to better measure the value and impact of your investments", would be right now. In the absence of the current crisis, this edition would have highlighted that SA needs more focus on impact investing – a global trend where investments are made with the intention to generate a positive, measurable societal impact alongside a financial return. Most of this edition's authors consider this now a fait accompli – investment decision-making needs to transform, not for the sake of a quick economic recovery, but for a long-term sustainable society.



SA is a country with one of the highest financial inequality measurements in the world, with widespread levels of poverty, and one in ten children going to bed hungry at some point during the year. In 2015, the United Nations announced 17 interconnected global sustainable development goals that leaders across the world had committed to address and eradicate by 2030. These global challenges relate to poverty, inequality, climate change, environmental degradation, peace, and justice. Investing for the purpose of impact should generate similar financial returns but make a considerable difference on the ground. Several authors have highlighted investments made locally that have achieved or exceeded such targets.

Our investment decisions allocate much-needed capital resources to various sectors in our economy. Now, however, the long-term investor has high allocations to secondary market assets, in part due to legislation, liquidity and governance. When you buy listed shares or bonds on an exchange, you are only paying the existing owner to transfer ownership to you, and your investment decision has no effect on the capital and management of that company. Billions deducted from salaries every month is allocated to this pursuit of changing ownership within the same set of securities.

It is easy to understand why the intention to mobilise investments towards companies and projects that make a positive difference is very appealing. Yet, there are several challenges to access these projects and to maintain accountability regarding their impact. Investing for impact cannot be a marketing gimmick. Stating an intention against executing the intention requires good governance and an alignment of regulation and stakeholders. All investments theoretically have an impact, but the impact must be clearly defined and the outcomes measurable.

Understanding the impact of your investments – and then doing something about it – is possibly the panacea needed for the challenges that we face today. It is therefore extremely important that we get the framework, guidelines and associated regulation correct.

There are several risks that could materialise over the short term as the industry seeks to bring it to life. First, it becomes a simple tick-box exercise, which marginalises the impact. Or, second, it becomes overtly complex and over-regulated, creating cost and other access issues. Third, it could become conflated with prescribed assets, ESG (environmental, social and governance) concerns and other strawman debates.

Doing good without sacrificing financial returns is possible; it is here and needs champions and long-term investors to ensure that it delivers on its promise. ■

Deslin Naidoo, CFA, is the founder of NEBULA SI, a savings and investment start-up integrating traditional finance with artificial intelligence.

PLEASE SEND ANY FEEDBACK AND SUGGESTIONS TO CABOTA@AFORBES.CO.ZA.

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FRAMEWORK

By Elias Masilela

The worst of times ... is it absolute?

The Covid crisis is making way for impact investing as a much-needed default consideration.

The pandemic is unequivocally unprecedented. In response, we've all voiced, in a chorus of lament, that "it is the worst of times". After much observation and thought, I wonder whether there's a case for seeing the existence of the best alongside the worst of times.

As we search for lasting solutions to the pandemic, a daunting question arises: Will Covid-19 defer the UN's Sustainable Development Goals (SDGs) and the National Development Plan (NDP) permanently, or will it offer an opportunity to accelerate their implementation?

This is a difficult question. When both the SDGs and NDP were adopted, global inequality was already at unsustainable levels. The biggest concern was that, after acknowledging failure with the Millennium Development Goals, we cannot fail again.

Several second-order, yet pivotal, questions also arise. Does Covid-19 offer an opportunity for a closer working relationship between government and the private sector? Are we going to see a narrowing of the trust gap between the two? Is this an opportunity for the realisation of the much-elusive social compact, as emphasised in the NDP?

There are robust reasons for answering 'yes'. Certainly, from an impact viewpoint, an opportunity for the quick adoption of impact as a key implementation tool, both in policy and business, is being observed. We are seeing unprecedented collaboration between government and business in South Africa. Business in SA is starting to lead from the front. Gone are the days when business waited for government before they could act.

Elias Masilela

Rightly so; business has identified an opportunity in the Covid-19 crisis. Not only that, business has reiterated the need for visible urgency, joint action, building on the country's macroeconomic potential, improving confidence, growing investments, ensuring inclusive growth and speeding unemployment reduction. Lastly, business highlights the need to identify and address key constraints, many of which predate the Covid-19 crisis. The catalytic intervention identified is infrastructure – correctly so.

The future of social compacting in SA is bright. It has undoubtedly been given the first significant boost in the history of our democracy. Impressively, this is the closest intervention in dealing with the concerns of the world's heads of state when they adopted the SDGs – namely that inequality is the biggest risk for global growth. Therefore, we must respond and invest differently. In the SA context it is in line with the bold conclusion of the National Planning Commission that the economic imbalances identified at the time when the economic diagnosis was undertaken – in 2010 and 2011 – are too big to be resolved by the government alone. Now, these imbalances have widened multi-fold.

While current observations suggest it is the worst of times, it is also the best of times for impact investing. The pandemic has made this movement a natural default consideration for taking the world economy out of the mud it finds itself in. ■

Elias Masilela is the founder of DNA Economics.

By Andrew Dittberner

An alternative to GDP

Questioning the fixation on growth as a measure for success.

The single most powerful ideology of our time is the fixation on growth. Irrespective of whether it is growth at a macro or micro level, if entities can demonstrate some form of growth, they are perceived to be on the road to success. The time, however, may be fast approaching for modern society to rethink the growth ideology.

Economics Nobel laureate Simon Kuznets developed and presented the modern concept of gross domestic product (GDP) in 1934 and a decade later, it formally became the tool for measuring a country's economy. Interestingly, in his original report, Kuznets warned against the use of GDP as a measure of economic welfare. His concern centred on the simplicity of quantifying economic welfare in a single measure. He warned that oversimplification opens the potential for misleading results on matters that are at the centre of conflict for opposing social groups. Clearly, his warning fell on deaf ears.

The evidence seems clear. Life expectancy has improved significantly, fewer people live in poverty, and education and healthcare are more readily available around the world. These examples push us to the simple conclusion that economic growth results in a higher quality of life.

Until recently, New Zealand's budgetary process involved fiscal discipline and promoting fiscal transparency, government efficiency and economic growth. Yet, despite initial success, overall income and productivity in New Zealand has been low in recent years, coupled with rising inequality.

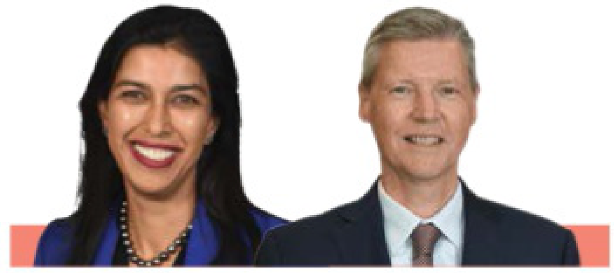
Andrew Dittberner

The net result is that the current government announced a first Wellbeing Budget at the end of 2018. Policy priorities include transitioning to a low-emission economy; supporting tech innovations that unlock social and economic opportunities; increasing income, skills and opportunities for previously marginalised groups; reducing child poverty and family violence; and supporting mental health. Still in its infancy, the success of the budget remains to be seen. However, what is clear is the realisation that a new approach is required.

Wellbeing needs to be one of the central focuses of the new economy to reconcile differences between social groups, between the economy and the environment, and to reconnect people to their greater communities. Behind the challenge of getting this right lies the chance to close the many gaps the fixation on economic growth has created. ■

Andrew Dittberner is the chief investment officer at Old Mutual Private Clients Securities.

By Nazmeera Moola and Simon Howie



INVESTMENT

New initiatives to combat the crisis

How to mobilise the long-term savings pool to help restore SA's economic health – and achieve a positive return.

South Africa's GDP looks set to contract by 8% in 2020. In an ideal scenario, we would see a sharp V-shaped recovery in 2021, resulting in an expansion of 8% or more. For this to occur, we need two things.

Firstly, we need a return of confidence. Remember, SA entered the Covid-19 pandemic in recession. A decade of former president Jacob Zuma's economic mismanagement means that private sector fixed investment has been contracting since 2014. To boost confidence, we need to see three or four tangible reforms (not just talk about reforms) in the next six months.

The second requirement is for SA to protect as much productive capacity as possible. This will be partially met by the wage support measures and loan guarantees that have been implemented. However, even if the loan guarantees begin to function as envisioned, that won't be enough. They are targeted at helping companies with turnovers of up to R300m per year. There are many large private companies and small listed companies that turn over more than that – but could still struggle to find appropriate funding during this crisis.

SA faces a dire capital shortage. The government will run a budget deficit of around 14.5% of GDP in the current year – this is one of the largest in the world. Unfortunately, the bulk of this is due to a collapse in tax revenue as economic activity looks set to contract by the greatest amount since the 1920s.

Given the constraint, it is critical that the long-term savings industry plays a role in protecting the country's productive capacity during the next two years to support the long-term economic recovery, preserve jobs and protect a permanent loss of equity value.

There are, however, structural factors that limit the long-term savings industry's ability to contribute to the current crisis.

First, long-term savings are typically managed by investment managers in specific mandates or funds that are constrained by asset class or credit ratings. Second, most funds managed by investment managers allow clients to withdraw at short notice, requiring a bias to liquid investments. Third, most investment managers are measured on short-term performance, creating a bias towards current momentum and thus limiting the exposure to investments with a strong SA exposure when other markets are outperforming. Finally, most investment managers' funds have limited liquidity to contribute meaningfully.

Within these constraints, local managers can provide some support. Equity funds can participate in rights issues to help businesses that require additional capital. Fixed-income funds can provide debt to companies through the listed bond market and there are a handful of niche private market strategies that can provide some unlisted debt and equity. But this support is clearly not enough and is likely to reflect poorly on the long-term savings industry. Supporting SA businesses through the current crisis should not be the sole responsibility of the banking sector and the government.

The long-term savings industry needs a more flexible approach to help mitigate the economic impact of Covid-19. In this respect it has been encouraging to note that some investment managers are coming to the market with initiatives aimed at tackling this challenge. These initiatives aim for more flexibility than traditional mandates typically have allowed them to help businesses – thus achieving a positive impact while providing a commercial return. Initiatives like these provide a tangible, scalable impact investment vehicle.

However, they have prompted a rethink for many institutional asset owners, as they require them to consider an allocation to unlisted investments across the capital structure in a locked-up structure – a clear departure from their standard asset-allocation decisions. This longer time horizon is critical as companies that are viable on a three- to five-year basis may present too much risk for a manager of listed equities, or credit, with a one- to two-year time horizon.

The companies that would fit the bill would be those that entered Covid-19 with strong fundamentals, have a solid management team, have the ability to contribute to SA once the economic recovery commences, and have a clear path to recovery after the pandemic with the necessary financial resources.

The increased flexibility in mandates is key to the success of these new initiatives as there will be an element of finding the right solution in different circumstances. Some businesses may simply require short-term liquidity to support them through the crisis while others may take longer to recover and will need more patient capital in the form of equity or subordinated debt with easier repayment terms.

> The government will run a budget deficit of around 14.5% of GDP in the current year – this is one of the largest in the world.

The key to the success of such impact initiatives will be the balance between financial returns and socio-economic imperatives. There is a clear impact goal: protect productive capacity, jobs and the country's tax base. While it would be naïve to assume that these funds can ensure no job losses in the companies in which they invest, providing support to businesses and helping them through the current crisis will have a direct benefit to both job preservation and the protection of productive capacity, which should help with employment growth as the economy recovers. Therefore, performance reporting on these funds will include both commercial and impact outcomes.

The Covid-19 pandemic presents an economic situation never experienced – the lockdowns were effectively an induced coma. Unfortunately, the businesses' revenues were in a coma, not their costs.

To mitigate the effect, long-term savings capital has a material role to play to help in the rebuild. Importantly, early action will have a large positive impact and provide solid potential returns. ■

Nazmeera Moola is the head of SA investments at Ninety One.
Simon Howie is co-head of fixed income for SA and Africa at Ninety One.

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By Tanya van Lill

MEASUREMENT

Can we get on the same page?

For many investors wanting to implement impact investing, a challenge is the lack of a standardised set of metrics across multiple stakeholders.

The conversation is shifting from environmental, social and governance (ESG) to impact investing. ESG is characterised as good risk management practices and defined by the UN as development that meets the needs of the present without compromising the ability of future generations.

The Global Impact Investing Network (GIIN) defines impact investments as investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return.

Impact investing considers both the financial return and the intentional positive social and environmental change, while ESG is viewed as sustainable investment. Although ESG and impact investing may overlap on the spectrum of investments, they each offer unique benefits. Whether one chooses good ESG practices or impact investing depends on the requirements of the investor and the types of investments.

> Although ESG and impact investing may overlap on the spectrum of investments, they each offer unique benefits.

In South Africa, due to the pivotal role development finance institutions (DFIs) have played in the development of the private equity sector, good ESG practice has traditionally played a fundamental part in the investment decisions and reporting process. In the *SAVCA 2020 Private Equity Industry Survey,* it was reported that 98% of fund managers consider, at a minimum, ESG factors when making an investment decision. However, recently, more investors are not only demanding ESG, but also the incorporation of impact investing principles as part of the investment process, which calls for four key elements: intent, a positive contribution, measurement and a financial return.

On offer?

There are numerous societal changes that can be met through impact investing, which has the potential to alleviate poverty, hunger and unemployment. Especially in SA, where unemployment figures surged to 30.1% during the first quarter of 2020, according to Stats SA.

The SAVCA survey showcases a few examples of social impact because of direct funding into an investee company. One example is the online platform SweepSouth, where the social impact of this investment has seen the company grow from 2 to 44 permanent employees and, through its platform, created the ability for more than 8 000 SweepStars to earn a regular income.

The *Africa Impact Report* offers a series of cases linked to the UN's sustainable development goals (SDGs). With all the evidence showing what impact investing can offer, the question begs, how do we measure the impact of investments, and is there a standardised set of metrics?

Measurement

Many investors say that when it comes to the implementation of impact investing, a challenge is the lack of a standardised set of metrics across multiple stakeholders. There is a level of complexity to agreeing to a standardised set of metrics to measure impact, as different investors have different target objectives.

The benefit to some level of harmonisation on metrics is that investors will be better placed to mobilise capital and scale up impact investing if asset owners are able to determine a framework to compare the impact of their investments – in the same way as they are able to compare financial performance.

Phatisa, which operates a sector-specific private equity fund aligned towards investments in food, uses core metrics aligned to the SDGs, including zero hunger and reduced inequalities. However, because of the different types of companies they invest in, it is difficult to make meaningful comparisons between investments in their portfolio. Phatisa developed an internal measurement system that enables them to compare the impact across investments.

Actis, which manages various private equity funds and invests across Africa, devised a framework that measures and quantifies the positive impact from the initial investment through to exit. They aim to report on the impact as objectively as possible, so that it could sit alongside financial measures. Using a six-step process, Actis measures the impact of their investments, including examining the expected impact of investments, how much social or environmental impact is likely, and assessing the risk of the investment failing to achieve its intended impact.

It seems that not everyone is yet on the same page, and the difficulty with agreeing on an industry metric is the fact that each investment makes a unique contribution.

What does this mean for investors?

For investors who are looking at investing for impact, part of your due diligence process is to engage with managers that have a proven, demonstrable track record in delivering positive societal impact – along with financial returns that are transparent and aligned on key principles.

According to Mergence Investment Managers, investors should aim for alignment between their objectives and the target impact objectives of a fund and discuss the level of granularity of the metrics and reporting of impact. What is clear, aside from financial returns, is that investors should ask questions about intent, look for evidence of positive contributions to society, and, lastly, enquire about measurement processes to ensure that everyone is on the same page prior to making the investment. ■

Tanya van Lill is CEO of the Southern African Venture Capital and Private Equity Association.

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How to shift the focus

An overview of the evolving asset management industry, from responsible investing to inv

HOW TO SHIFT RESPONSIBLE INVESTING FROM ESG MONITORING TO MAKING A MEANINGFUL IMPAC

	RESPONSIBLE INVESTING WITH ESG AWARENESS	RESPONSIBLE INVESTING WITH ACTIVE ESG
MEASUREMENT CRITERIA	Performance reporting relative to asset allocation benchmark. May show ESG score for portfolio	Performance reporting relative to asset allocation benchmark (may be ESG benchmark) along with reports on select ESG metrics, active engagements with company management and proxy voting
REGULATORS	Regulation 28 of the Pension Funds Act: • Sets out responsibilities of fiduciaries to fund members • Prudent investing should consider factors that affect the sustainable long-term performance of a fund's assets, including ESG risk factors • Sets out class constraints Collective Investment Schemes Control Act	Apply the United Nations Principles of Responsible Investing (PRI) or the CRISA guidelines, or provide an explanation as to why they would not be applicable Apply B-BBEE Codes of Good Practice: legislative framework set out by the department of trade and industry for transformation of SA's economy to enhance economic participation of black people
INDUSTRY GUIDELINES	General governance – King Codes Code for Responsible Investing in South Africa (CRISA) – local body where signatories voluntarily ascribe to responsible investment principles and incorporating ESG considerations Industry sector charters that address local inequalities and other issues (optional)	PRI – international body promoting accountability, transparency and good governance, incorporating ESG considerations and promoting industry participation. Signatories voluntarily ascribe to a set of responsible investment principles and have access to training, research, best practice and networking opportunities
ASSET OWNERS	Formulate an investment policy statement that defines prudent investing alongside performance targets and risk budgets	Set stewardship guidelines to underlying managers around ESG and B-BBEE (where applicable) Commit to PRI and CRISA Select managers on the same criteria
ASSET MANAGERS Investment decisions	Structure portfolios for highest return at client's level of risk ESG measurement would be coincidental or after the fact	ESG ratings integrated into valuations Structure portfolios for highest return at a level of risk after ESG integrated into valuations Some managers would be active shareholders engaging on key ESG issues
CORPORATES, ENTERPRISES AND SOEs Reporting and other commitments	Annual financial reporting – IFRS JSE listing requirements – additional disclosures King Codes on Corporate Governance	Separate reporting on sustainability performance Disclosures of ESG policies

esting for impact.

CT IN SOUTH AFRICA (CONTENT REQUIREMENTS ARE ADDITIVE AS YOU MOVE FROM LEFT TO RIGHT)

RESPONSIBLE INVESTING WITH ACTIVE ESG AND IMPACT MEASUREMENT	RESPONSIBLE INVESTING WITH ACTIVE ESG AND ACTIVE IMPACT INVESTMENT
Report on performance of financially material impacts (positive and negative outcomes) in addition to benchmark relative performance	Relate impact performance to measurable contribution to local and global targets of sustainable development goals (SDGs)
No guideline regulation exists at present. These are potential changes to regulations to include impact measurements: **i.** Expand the definition of prudent investing **ii.** Change the definition of members' liability **iii.** Expand asset class definitions **iv.** Adjust reporting requirements for funds CRISA would need to become more expansive regarding impact measurement guidelines	No regulation or national framework exists at present. This may require National Treasury or the International Finance Corporation (IFC) to set standards and direction in relation to SA's National Development Plan (NDP) and global SDG thresholds to align SA's SDG requirements to investor activities (such as green taxonomy)
International Finance Corporation: a World Bank operation that offers financial guidance for private sector projects in developing countries: • Anticipated impact measurement and monitoring frameworks for 25 sectors • IFC operating principles for impact management to assist the capital providers – for both negative and positive outcomes Global Impact Investing Network (GIIN) provides detailed positive impact measurement details through its IRIS+ system Impact Management Project (IMP) has developed consensus-driven norms providing uniform impact measurement and management logic across all asset classes and organisations	**Sustainable development goals (SDGs): UN-sponsored project to establish basic development standards for 193 countries, including SA:** • UNDP – provides impact measurement guidance to SDGs for different asset classes • UNEPFI – provides principles and tools for financial intermediaries to ensure they are driving positive impacts • UNGC – provides corporate-level guidance, such as the CFO principles PRI – Impact outcomes framework linking to SDG management IMP aims to harmonise the measurement and management of organisations' and investors' contribution to global sustainability targets
Set criteria and expectations for contributions from impact and financial returns Select managers based on an IMP mapping framework of their portfolios to impact outcomes (intentional or unintentional)	Set criteria and expectations for specific impact and financial targets Distingguish between local and non-local impact Select managers based on IMP mapping of portfolios
Portfolio construction to optimise risk/return/impact (requires new benchmarks) Primary capital investments demand intentional impact measures Active engagement on reporting and delivery of impact outcomes	**Portfolio construction should optimise risk/return/impact/SDG outcome (requires new measures)** Identify economic gaps that require filling and identify or structure targeted vehicles to fill gaps
Integrated reporting on financially material impacts on people, the planet and economy **Boards adopt impact outcomes as part of their balanced scorecard measures** Global Reporting Initiative (GRI) frames the impact organisations are having on the world Sustainable Accounting Standards Board (SASB) looks at companies' impact on the world (SASB and GRI will become integrated) CDP: Carbon disclosure project	**Integrated reporting on clearly defined measures of the impacts of non-financial and financial outcomes** Hierarchical measures of global and local SDG initiatives Boards take accountability to shareholders on impact outcomes as part of their balanced scorecard measures

SOURCE: Anne Cabot-Alletzhauser, Colin Habberton and Monique Mathys-Graaff

By Monique Mathys-Graaff

METHODOLOGY

Survival of the fittest

How to probe a company's commitment to sustainability.

For years, the campaign to hold companies – and not just their shareholders, but the societies and economies in which they operate – more accountable, moved at a modest but resolute pace. This past year, though, the Covid-19 crisis laid bare the necessity of getting capitalism and financial systems working on behalf of society, the stakeholders, and planet we inhabit – and not just for pure self-interest. As such, we now have a virtual tsunami of initiatives from any number of international agencies determined to deliver that transformation at record speed.

That leaves investors and asset owners in somewhat of a quandary. Which initiative or methodology should they align with?

The starting point for getting this transition right will be the companies themselves. And if they won't report clearly on where they stand, then it is up to us, the asset owners and the fiduciaries, to probe more effectively. Here is a simple checklist to determine whether the investment you are considering is aligned with your interests:

1. Assess the leadership:
What seniority does the company's head of "ESG" (environmental, social and governance) concerns or "sustainability" or "shared value" or "impact" hold? If they are not part of the C-suite with a direct link to the CEO or MD, there may be a problem. Does the board have sufficient sustainability expertise?

2. Interconnectedness of impact, sustainability, and strategy:
Are you convinced that the core strategy of the organisation has been appropriately linked to the various sustainability topics relevant for its broad stakeholders? Look for clear materiality frameworks linked to their sustainability reports and integrated annual reports. Cross-check this with the strategy and KPIs of the company – there should be a clear link between the materiality of the business and incentives and remuneration for sustainability. A sustainable development goal logo or reference does not cut it.

3. Capital allocation approval process:
Does the ESG or impact report receive due authority for sign-off in the process? Can management give an example of an investment or business decision prevented due to an ESG, sustainability or impact consideration? Where are the sustainability or impact strategy components being assessed in the process before approval? If they say the CEO decides, run.

4. Search the company online and then check community-level operation or product names:
Bad press doesn't necessarily disqualify a company. However, many negative articles, left unaddressed, could point to long-term issues. Also, holding companies sometimes change their names, but local communities tend to stick with the operations' original or local name.

5. Sustainability initiatives reflected in company strategy:
While it's impossible to expect of every organisation to participate in every initiative purporting to change the world for good, it is reasonable that they have some awareness. They should have some form of participation at all three of the following levels: one or two relevant global initiatives, sector-level organisations, and local-level initiatives.

Whatever your role in the capital markets system, as an asset allocator picking portfolio managers or companies, ignoring the long-term sustainability impacts of your decision is likely to compromise your survival. Don't concern yourself with trying to determine which of the impact measurements will survive. That will work itself out over time. Right now, focus on honing your skills to identify the long-term sustainability and impact themes which will prove your investments to be the fittest. ■

Monique Mathys-Graaff is a senior adviser at the Impact Management Project.

INNOVATIVE FINANCE

A spurt for econ

SPACs and mezzanine debt can play a pivotal

South Africa's fiscal position, with its gross-debt-to-GDP expected to exceed 100% between 2021 and 2022, severely limits the government's room to drive economic recovery, therefore the current emphasis on an investment-led recovery.

To stimulate economic activity, there is a need to specifically focus on sectors that enable the country to address the challenges of joblessness and inequality. Investments that yield positive financial returns without any benefit to society could widen the inequalities that are already unsustainable. For the private sector to lead inclusive growth, one of the critical enablers will be access to finance – more so considering the eroded reserves of corporates currently. Without access to finance, the private sector's plans to reactivate the economy would be hamstrung.

Financing options for the private sector are traditionally dominated by equity and senior debt. Both options tend to be unsuitable during times of economic crisis, such as the current one. This mismatch between the capital available (through traditional sources such as commercial banks), and the capital required by corporates, should steer us towards designing new financial instruments, and scaling up those that already exist at a relatively smaller scale that are aligned to a new economic construct. Two examples of such products that are opportune include raising capital through a special purpose acquisition company (SPAC) and mezzanine debt.

A SPAC is a listed investment vehicle that is an alternative platform for raising capital for acquisitions and is led by an experienced management team. A SPAC is defined in the JSE's listing requirements as being a special purpose vehicle established for the exclusive purpose of facilitating a primary capital raising process to enable the acquisition by the SPAC of viable assets in pursuit of a listing on the JSE's main board or AltX.

SPACs tend to invest in businesses that are in a high-growth phase, giving an opportunity for good returns on invested capital. SPACs typically appeal to an investor who is looking for new asset classes, access to investment opportunities in new industries and with a long investment horizon. In the current economic context, it would be

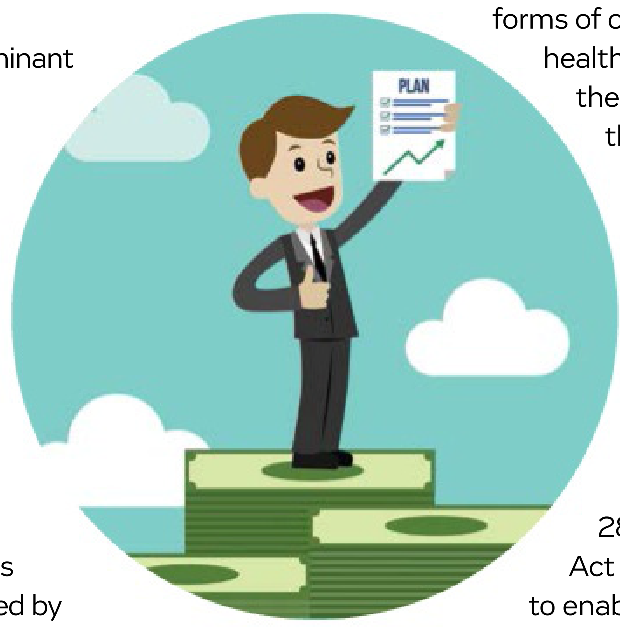
By John Oliphant and Dinao Lerutla

omic revival

role in unlocking inclusive growth.

important that the SPAC also addresses the objectives of inclusive growth to be a relevant form of capital raising.

In the US, SPAC listings accounted for 19% of the total initial public offering market by value in 2017, up from just 12% in 2007. Since the beginning of 2016, ten SPACs have raised more than $500m each, enabling them to effect larger transactions, including several multibillion-dollar deals. Two recent successful case studies of SPACs in SA are Capital Appreciation and RH Bophelo. Capital Appreciation is predominantly invested in fintech companies, and fintech has been at the forefront of financial inclusion for low- and middle-income households in SA. RH Bophelo invests in enabling access to affordable healthcare.



Interestingly, the dominant companies on the JSE do not represent much investment in local information technology (Naspers* has started investing in SA entities in this segment), life sciences or clean energy. These are the new industries poised for growth, and the demand for their services has now been accelerated by how the effects of Covid-19 have shifted consumer spending.

SPACs are akin to a listed private equity vehicle, and typically illiquid in their early years of listing. Asset managers have shown limited understanding of SPACs or, alternatively, mandates from pension funds limit their ability to participate in these opportunities. Our recommendation is for retirement funds to explicitly allow for SPACs in their mandates to asset managers.

Similarly, mezzanine debt offers an alternative to traditional finance instruments. Mezzanine financing most commonly takes the form of preferred stock or subordinated and unsecured debt. Mezzanine debt also has a relatively better cash-flow profile relative to equity investments. It offers investors an amortising profile such that the invested capital is returned during the term of finance. The common traits between SPACs and mezzanine debt is that both have strong criteria on management teams and companies that are cash-flow generative.

One of the success stories of a growing company that was enabled by mezzanine finance is Vumatel. In its earlier stages, banks had limited appetite to finance the company. Six years later, the company today is one of the leaders in providing fibre-to-the-home in SA.

Given the challenges in deploying the stimulus funding provided through the government's bank guarantee scheme (just above 5% of the R200bn has been disbursed to date), it is fair to anticipate that corporates will struggle to raise the traditional forms of capital unless they have healthy layers of equity in their capital structures. In this instance, mezzanine debt and SPACs provide an opportunity to unlock capital for investment and economic recovery. To enable more mezzanine debt to be made available in the market, regulation 28 of the Pension Funds Act needs to be reviewed to enable increased capital flow from retirement funds into mezzanine financing institutions and funds.

The impact of mezzanine debt and SPACs, when directed to investments that address societal challenges, can be multiplied to not only yield a competitive financial return but a multitude of positive social returns too, and therefore enabling the emergence of an inclusive economy.

Our assertion is that impact investing is critical to realising economic recovery, and without access to appropriate financing instruments such as SPACs and mezzanine debt, our efforts as the private sector will yield limited results. ■

*finweek *is a publication of Media24, a subsidiary of Naspers.*

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Dinao Lerutla is the managing partner at Maia Capital Partners.

A SPAC is defined in the JSE's listing requirements as being a special purpose vehicle established for the exclusive purpose of facilitating a primary capital raising process.

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By Ngoku-Sakhile Mazwi

INFRASTRUCTURE

Why pension funds should support GDP

Pension funds could support the knock-on effects of more money flowing into infrastructure projects to assist in South Africa's economic recovery.

The correlation between investment in capital infrastructure and GDP has been shown by IMF and World Bank data collected between 1960 and 2019. These studies demonstrate that 54% of all GDP performance can be explained by a country's investment levels. At this juncture in South Africa's economic history, given the contraction of the economy and the added impact of Covid-19, it is increasingly important to prioritise investment as a stimulant for GDP growth and economic development.

Specifically, infrastructure investments have been empirically proven to have a significant impact on economic growth and to also reduce inequality, according to the *International Journal of Critical Infrastructure Protection.* Aschauer's seminal paper, published in 1989 in *Industry Week,* triggered a voluminous amount of research into the sector by noting strong links between infrastructure investment and economic growth. Belloumi and Achour later proved a causal relationship between transport infrastructure, energy consumption and GDP. In sum, what these studies demonstrate is that a 1% increase in a country's infrastructure stock is directly correlated to a 1% increase in GDP. It is therefore the impact of infrastructure that makes its investment case compelling.

The recently held Sustainable Infrastructure Development Symposium (SIDS) and attendant sustainable infrastructure development methodology are thus a recognition, on the part of government, of the benefits of an infrastructure-led growth plan. What SIDS asserts is that SA needs an investment target of at least 30% (from our current 16% to 18%) to transform into an investment-led economy. Stimulating private sector infrastructure investment, then, forms part of this strategy.

But what is infrastructure?

There is no dominant, singular understanding of what infrastructure is. Most definitions share an overlapping view of infrastructure as a reference to: power plants, power distribution networks, oil and gas pipelines, roads, bridges, railways, harbours, airports, water purification and treatment plants, water pipelines, potable water supply, dams, telecommunications and communication networks, sewage facilities, housing services and human settlement, urban services, and irrigation networks.

The Organisation for Economic Cooperation and Development (OECD) defines infrastructure simply as "the system of public works in a country, state or region, including roads, utility lines and public buildings".

In the investment industry, we typically group and differentiate between economic infrastructure and social infrastructure assets. Economic infrastructure is a reference to power, transport, water and information and communications technology (ICT) assets; and social infrastructure refers to student housing, schools, human settlements, clinics, hospitals and wellbeing.

Furthermore, investors identify quality infrastructure assets based on their economic and financial investment characteristics, which include high barriers to entry, economies of scale, inelastic demand, lower volatility or correlation to economic swings and listed markets, predictable cash-flow yields based on long-term agreements, as well as public-goods attributes linked to a tendency towards monopoly, according to a paper by Inderst.

SA has historically under-invested in infrastructure, achieving infrastructure investment levels of only

4.7%

of GDP.

It is because of these public-goods attributes that government regulation is required to ensure that infrastructure is appropriately priced. However, infrastructure assets do not all behave the same. ICT, as an example, has sufficient attributes to incentivise competitive private participation and therefore does not require too much government involvement.

Nevertheless, infrastructure projects typically have network-effects benefits and address spatial inclusion. Thus, the net public benefit or economic gross value-add from infrastructure investments exceeds their private sector return. For this same reason, some infrastructure sub-sectors, such as social housing, get underprovided for by the private sector and need blended finance solutions to attract the private sector.

SA has historically underinvested in infrastructure, achieving infrastructure investment levels of only 4.7% of GDP, according to the McKinsey Global Institute. In comparison, India and China, SA's bigger BRICs associates, have been investing between 8% and 13% of GDP in infrastructure consistently since the 1990s, according to the Reserve Bank of Australia.

As a way forward, then, there is a requirement to amend policy to enable more private investment in infrastructure. Regulation 28 (the regulation governing pension fund asset allocation) has the potential to unlock an estimated R120bn for direct investment in infrastructure, according to estimates by the Association for Savings and Investment SA (Asisa) and National Treasury. The impetus to amend regulation 28 comes from the requirement to use the regulatory framework to provide clearer guidance to the pension fund market on its role in the nation's infrastructure-led growth strategy and, more generally, the National Development Plan.

As demonstrated, infrastructure investment is a proven path to economic recovery, but perhaps more importantly, it concurrently delivers much-needed socio-economic value by enhancing the lives of the excluded and underprivileged. ■

Ngoku-Sakhile Mazwi is the managing director at Bayakha Infrastructure Partners.

Photo: Shutterstock

By Sawa Nakagawa

METRICS

Choosing the best fit

Asset managers' impact measurement practices should be tailored to the resources they have at their disposal.

All investments have an impact – either positive or negative. A positive impact can be generated deliberately or unintentionally. Selecting the right metrics is an important tenet of the impact measurement and management process. But simply measuring impact does not necessarily lead to creating impact.

Rather than focusing on what we want to measure, we need to shift our discussion to the purpose of implementing our impact investing strategy, and what changes we want to create and how. The newly published *Impact Investing Handbook: An Implementation Guide for Practitioners* by the Rockefeller Philanthropy Advisors, talks about the importance of articulating 'why' investors pursue impact investment. The 'why' – which is often said to be underappreciated – "establishes the values, goals, and parameters". It leads to a "more thoughtful and consistent strategy."

Asset managers can develop a unique competitive advantage through embracing impact measurement and management as a strategic tool. By not treating impact measurement and management as a compliance exercise that happens once a year, you can create a more solid investment strategy for your clients. By investing the time upfront to carefully develop the impact investing goals, you ensure that funds are allocated to meet clients' financial and social or environmental goals.

This is not necessarily sophisticated, but perhaps requires a mindset shift. In many ways, it is like creating an infrastructure to set the expected financial return, evaluate financial performance and report to the asset owners, which form part of a standard operating procedure for any asset manager. By implementing the same rigour to measuring and managing impact, clients will value transparent and insightful reporting, while asset managers can increase their accountability. As Warren Buffett famously said, "It is not necessary to do extraordinary things to get extraordinary results."

Is there such a thing as the 'best' measurement framework?

Given the plethora of impact measurement standards and frameworks available, how do we decide which framework to use? According to the latest Global Impact Investment Network (GIIN) survey, the average investor uses at least three frameworks or tools or systems such as the UN's Sustainable Development Goals (SDGs), Integrated Risk Information System (IRIS), IRIS+, and so forth. That seems excessive. It must be particularly daunting for those that are new to the industry or small fund managers with limited resources.

In the meantime, the best approach is to use what aligns with your impact-creation approach and philosophy. It is not about rushing to adopt the most popular methodology or choosing the most complicated framework. You should invest time and effort in selecting what best supports your theory of change. What works for others may not work for your internal capacity, asset class, or the size of the fund. By taking an open-minded approach, the lessons learned can help you sharpen your competitive advantage over time.

Opportunity in the time of crisis

Interestingly, history tells us that crisis tends to foster innovation. One famous example is the US accounting standards, Generally Accepted Accounting Principles (GAAP), which were established as a response to the stock market crash of 1929 and the subsequent Great Depression.

The current crisis can be an opportunity for the investment community to accelerate the use of capital to support not just the economic recovery, but also the long-term sustainable growth of a country and the world.

Each of us can elevate the impact measurement management practice to the same level of priority as other performance-related tracking systems. We can share our data responsibly with our stakeholders to hold the industry accountable. By treating it as a tool to enhance our value proposition, we increase our return on investment (ROI) on measuring impact, which ultimately helps us to deliver more positive impact on people and the planet. ■

Sawa Nakagawa is a founder and partner of ThreeArrows Impact Partner.

Asset managers can develop a unique competitive advantage through embracing impact measurement and management as a strategic tool.

Photo: Shutterstock

By Rirhandzu Sithole and Angelique Kalam

SUSTAINABILITY

Make your intent clear

Being explicit about the impact goal of an investment to ensure alignment between investors, investee organisations and beneficiaries will go a long way to successful sustainable investing.

Why is impact measurement and reporting such a challenge for investors? After all, they have the necessary frameworks, tools, and metrics to support this process. Could this be a function of the fact that in some instances, the effect cannot easily be captured into a metric and that the human element involved requires subjectivity?

There is also a wide divergence of opinions on what is meant by meaningful impact and where priorities should be focused. One investor might place a bigger preference on affordable housing to address the backlog in the country, whereas another might prefer to invest to address the infrastructure backlog, believing that this achieves a broader-scale impact. How does one rate the social value of one project over another?

A good place to start is to see if we can align broader-impact goals and outcomes to South Africa's National Development Plan (NDP). As an emerging economy, the government has outlined several areas that are intended to promote economic, social, and environmental impacts and stimulate the economy to eliminate poverty and reduce inequality by 2030. We need to identify the areas or sectors of focus that align with our impact goals and objectives. We then need to identify investable opportunities (through debt or equity or a combination of both) to deploy capital.

The impact goal and intent are what differentiates impact investors from so-called ordinary investors.

Clear intent outlines what we expect to achieve by facilitating investment in a specific sector or company. Being explicit means that social outputs and outcomes can then be defined upfront. Specific indicators and metrics can then be used to measure the "success" of the investment and be reported to stakeholders as evidence of the outcome and impact achieved.

The International Finance Corporation (IFC) Operating Principles for Impact Management require impact considerations to be integrated into investment decisions throughout the investment lifecycle. The four steps of this approach include strategic intent, origination and structuring, portfolio management, and impact at exit. It also entails independent verification of these steps.

A case study may help to illustrate how these steps might play out in practice. This is a study of our investment in Retail Capital, a merchant cash advance business that focuses on funding SA's SME market.

Access to working capital is attributed as the biggest challenge faced by SMEs in SA. This exclusion has consequences for a country's economic growth and transformation. Accordingly, the government has prioritised the acceleration of financial inclusion in the NDP, with plans to increase financial inclusion to 90% by 2030. In 2016, SA was 1% away from attaining this goal, but financial systems remain underdeveloped when compared with other developing economies, according to the Banking Association of South Africa.

METRICS USED IN DETERMINING INVESTMENT ACHIEVEMENTS

Number of SMEs funded	Provided funding of over R3bn to date with 10 000 active clients	47% of businesses are women-owned or involved
Number of jobs created	Employing approximately 50 000 staff	4 500 direct jobs created as a result of funding
Innovation	Innovative business funding solutions	Flexible secured and unsecured funding solutions
Regional impact	Geographic diversification across provinces	Reporting on enterprises in urban, semi-urban or rural areas

SOURCE: Futuregrowth

In addition, the research paper *Achieving the Sustainable Development Goals: The Role of Financial Inclusion*, published by CGAP and the UNSGSA, emphasises how including SMEs in the financial system can play a major role in achieving many of SA's sustainable development goals.

Both studies prompted us to consider "promoting inclusive growth and financial inclusion" with the strategic intent to "seek opportunities to close the existing gaps in access to finance for SMEs in SA".

Such an opportunity arose in 2017 when, on behalf of our clients, we took a non-controlling stake in the shareholding of Retail Capital. We used a range of metrics and indicators to assess the outcomes and impact of our investment in this company.

Photo: Shutterstock

In addition, we monitored the impact against our predetermined metrics to assess whether we are achieving the desired outcome and impact as illustrated in the accompanying infographic.

Any number of financial and non-financial risks could have an impact on the long-term sustainability of such an investment. This element should form part of the investment lifecycle and be embedded as part of the investment process. The potential risks associated with the Retail Capital business were researched, debated and deliberated at length prior to investment and priced for accordingly based on the materiality of the risks. In this way, we felt comfortable that we were honouring our fiduciary responsibility in the use of our clients' funds.

Each investment is likely to be unique, with its own idiosyncrasies and metrics, which will vary from sector to sector. Clearly defining our intent, objectives and measurements upfront, so that there is alignment between investors, investee organisations and beneficiaries, can go a long way to making this a meaningful and sustainable process. ■

Rirhandzu Sithole is an impact investment analyst at Futuregrowth Asset Management.

Angelique Kalam is the manager for sustainable investment practices at Futuregrowth Asset Management.

By Jon Duncan

REPORTING

Exploring impact metrics

Determining the standards of reporting on impact investing remains a challenge.

Globally, much work is underway to translate our understanding of impact reporting to the listed equity markets, where issues such as intentionality, type of impact, data, investment horizon and benchmarks require further interrogation. However, setting clear guidelines still requires more effort and acceptance of standards in reporting.

To illustrate the challenge of reporting on "impact" for a local listed equity portfolio, two impact categories were selected: transformation and climate change.

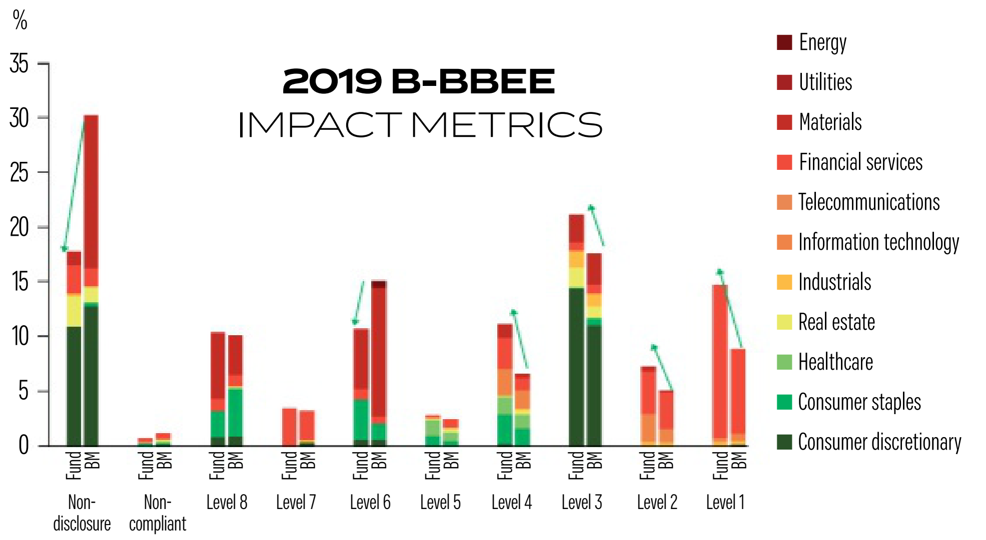
In respect of reporting on transformation impact, broad-based black economic empowerment (B-BBEE) contribution levels were used as the main measurement metric. The graph presents the 2019 B-BBEE data for a fund relative to the Capped SWIX Index. Sector contributions to each of the eight B-BBEE contribution levels are graphed along with non-disclosure and non-compliance. The data is presented by market capitalisation, as opposed to "by count", to reflect the contribution larger players make in the areas of skills and supply chain development (60% of the B-BBEE score card weight). It could just as easily be argued that the data should be represented by count to reflect the idea that participating in the South African transformation journey should not only be a function of size.

We calculated a rolled-up market cap weight score using all B-BBEE levels, including non-disclosure and non-compliance. Lower scores out of 10 indicate a better B-BBEE contribution level. On a rolled-up basis the Capped SWIX scores 6.14 while the fund scores 5.06, an 18% improvement in B-BBEE contribution level relative to the benchmark.

In respect of reporting climate change impact, the following carbon metrics were assessed: carbon footprint reported as total annualised emissions per $1m invested; carbon intensity as the sum of the portfolio emission on an equity share basis reported per $1m of revenue; and weighted carbon intensity – the sum product of the emission on a weighted portfolio basis reported per $1m revenue.

Depending on the metric, the carbon reduction to the benchmark could be reported as either 70% or 40%. For the purposes of comparison to other markets, the weighted average carbon intensity metric was reviewed against a set of global benchmarks. The local benchmark is roughly double the weighted average carbon intensity of the MSCI World benchmark and above the emerging markets benchmark. Notwithstanding, the global benchmarks provide no indication of being aligned to a global 2-degree ambition as required by the Paris Agreement.

Important to recognise is that both transformation and climate impact had more than one potential metric. Depending on the metric, the narrative related to impact would be slightly varied, thus highlighting the importance of understanding how the metric is calculated and what it is evidence of. In both cases, impact metrics are point-in-time measures that will fluctuate as portfolio weights change and, additionally, provide little insight in the forward-looking practises of the companies in the fund.



SOURCE: OMIG RI Team + publicly reported data

Investors need to decide whether they seek a reduction of negative risk, an enhancement of positive contribution, or both. With both, calibrating the scale of contribution requires reporting against specific targets and benchmarks. Here the debate needs to focus on absolute or relative measures. For example, defining the transformation impact for a fund, whether absolute or relative, would require in-depth research on underlying components of the B-BBEE score in order to align with specific investor goals. On the other hand, setting climate impact targets is potentially easier due to the global efforts in this regard.

Investors should also satisfy themselves that their fund manager is intentionally targeting specific B-BBEE or carbon outcomes. Without this intentionality, the buyer of the fund would have no way of targeting their own impact efforts. Lastly, listed equity investors need to grapple with the way they would like to achieve impact. Options include targeting change on a measurable metric over time against a target or benchmark, or through the application of hard exclusions, or through active stewardship.

> To illustrate the challenge of reporting on "impact" for a local listed equity portfolio, two impact categories were selected: transformation and climate change.

Given the scale of asset allocation to domestic listed equity markets, it's important that the asset-owner community considers how this capital contributes to long-term ecosystem resilience. For asset managers, it's no longer enough to provide appropriate risk-adjusted returns, excellent client servicing and competitive fees – the type and scale of impact will also become an important consideration when selecting a service provider.

With what's at stake, it makes good business sense for asset owners, consultants, asset managers, regulators and issuers to work collaboratively on solving for listed equity impact reporting. Industry alignment on impact outcomes has the potential to create a virtuous circle that connects the RI practises of the investment community with the aspirations of SA savers and the long-term sustainability strategies of listed companies. ■

Jon Duncan is head of responsible investment at Old Mutual Investment Group.

CONCLUSION

By Susan de Witt

What will it take?

Flexible impact investment guidelines are preferred to rigidity.

Impact Investing South Africa is tasked with accelerating the adoption of investing for impact into SA's investment community. It interacts with stakeholders across the financial sector, generating action points and sharing local findings with the Impact Investing Global Steering Group.

Globally, international organisations have made significant strides to ensure a shared language and an array of global measurement standards. Locally, though, progress has been slower. The task force keeps an ongoing dialogue with more than 40 practitioners across the SA investment spectrum so we can identify any impediments to the process. Their feedback has been insightful.

What seems to be holding South Africa back? To start with, this imperative is not being driven by senior leadership and has still not become a core consideration for the strategic processes of either asset managers or SA companies. If every enterprise and investment strategy has an impact – whether positive or negative – then harnessing and measuring that impact can lead to far more effective deployment of funds. This is a sophisticated process demanding appropriate resourcing. At best, it is currently relegated to a subordinate team or conflated with ESG (environmental, social and governance) reporting.

This transitional process will demand fluidity and agility. Setting rigid standards too early on could stifle innovation. What we can't have are companies and asset managers holding back until there is certainty, though.

Our practitioners also make it clear that alignment frameworks for measurement need to be robust, yet dynamic. They need to be relevant to SA and the impact needs to be linked to the objectives of the National Development Plan and the UN's Sustainable Development Goals (SDGs), which appear to provide the most compelling set of goals around which international and local enterprises and investors can coalesce.

Impact appears to be a strong indicator of ESG resilience, which means that those companies developing aligned strategies are signalling that they are ahead of the curve when it comes to resilience to future challenges. The return on investing in this process can be exponential to all shareholders. ■

Susan de Witt is the co-lead secretariat of Impact Investing South Africa.

By Anne Cabot-Alletzhauser

Changing one sentence in Reg 28

We don't need a pushback against sustainable investing. We need backing.

On 12 July, the *Financial Times* published this article: "Fund industry prepares to fight Trump curbs on socially responsible investing". The curbs being proposed were to address the question of whether investing for societal impact would hamper returns for members, or worse, introduce political agendas.

At a time where a Covid-stricken world desperately needs to find ways to close the funding gaps for delivering a basic quality of life, pension fund investments would provide a welcome supplement. But what about "value for members"?

For decades we've accepted that long-term savings play a critical role in stimulating economic growth. But, as Deslin Naidoo said in our introduction, the bulk of pension fund assets are invested in listed companies. Investing in stocks simply moves money from buyer to seller – not to the company or the economy.

Yes, there's some trickle-down impact when pensioners spend their pensions – but real economic impact only occurs if pension funds invest in infrastructure bonds or impact investments. If we want impact from listed shares, shareholders would have to persuade companies to be more intentional with corporate policies on creating economic and societal impact.

Here, then, is the point about value to members. "What is the use of a CPI + 5% return if our members need to buy the air they breathe or the water they drink? … If members are forced to rebuild our homes because climate change is increasing veld fire incidents? If they are unable to address meaningful education, affordable housing, food security and health considerations?"

What our members require is to see their savings do more than just bring them a financial return. It needs to bring them a quality of life.

We can do that if we first address:

• Regulation 28 of the Pension Funds Act – clearly spell out that members' funds should be invested not just to generate returns, but to create meaningful impact for their future.

• Company leadership needs to integrate considerations of impact on the broader economy in their planning, with their KPIs aligned to both this and financial targets.

• Asset managers need to understand that their mandate is to create portfolios that are optimally aligned to risk, return and impact and are rewarded for achieving that. ■

Anne Cabot-Alletzhauser is head of the Alexander Forbes Research Institute.

By Simon Brown

CORPORATE FINANCE

Is selling and leasing back the way to go?

Simon Brown probes a form of corporate asset disposal, weighing its benefits and pitfalls. He cautions that investors should take note if a company they hold goes this route.

Sasol has announced the sale of 16 air-separation units located in Secunda to Air Liquide for R8.5bn. The market very much liked the deal, pushing the share up over 12% at one point on the day before closing over 8% higher. Sasol needs to reduce its debt by some R100bn through cost savings and asset sales (and ultimately maybe even a rights issue). This R8.5bn helps a fair bit with reducing that debt.

But there is another side to the story that is less positive. The only customer of these air-separation units is Sasol, as it is an important part of its processes at the Secunda plant. But when Sasol owned these units, the plants either ran at cost, or, if they made any profit, that profit would flow to Sasol. The new owners will now undoubtedly want their newly-acquired plants to be profitable and, as such, Sasol will now pay more for the products. In other words, Sasol's costs have gone up and profits will be lower – a permanent situation after the disposal.

Sasol needs to reduce its debt by some **R100bn** through cost savings and asset sales (and ultimately maybe even a rights issue). This **R8.5bn** helps a fair bit with reducing that debt.

In a sense, this is a sale-and-lease-back type of arrangement that we often see, which solves short-term problems, but creates long-term issues.

For example, a company may own its corporate head office (or any other plant, property, and equipment). It saves money, even if there is outstanding debt on the asset. It's a not-for-profit arrangement: the company pays the debt and associated costs to maintain and run the asset – but that's all. There is no third party owning the assets also looking to make a profit.

On the balance sheet the building, for example, sits as an asset. There is, however, also likely a debt sitting on the liability side of the balance sheet. Ideally, the value of the building exceeds that of the associated debt, especially if the company has owned the building for some time.

Now, if the company needs some cash, either to pay down debt, or perhaps for an expansion, it can look to a sale-and-lease-back arrangement.

This would entail selling the building to a third party, which removes the building from their balance sheet, but generates a pile of cash that can be used by the company to pay debt or expand operations. Seemingly a win-win situation.

But now they must lease the building back from the new landlords and that landlord will also demand a profit, much like the Sasol example. The costs for the company have increased, thus in the long term it hurts. But it does plug an immediate cash need.

I used the example of a corporate head office, but as the Sasol deal shows, this sort of arrangement could be an operational plant or even equipment or any other asset sitting on a balance sheet.

The bottom line is that investors should view these sale-and-lease-back arrangements with some scepticism as the gains are short term, while the increased cost is not. Sure, it solves an immediate problem, but at a cost that will go on forever.

So, keep an eye out for these deals and always ask: Why is the company doing it? It may just be a new board or CEO who wants a cleaner structure and decides building management is not their speciality, which is a fair idea. But as a rule, it is seldom a great long-term solution and is rather undertaken due to a stressed balance sheet that almost certainly requires closer scrutiny, as this is a red flag being raised. ■

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Photo: Gallo/Getty Images

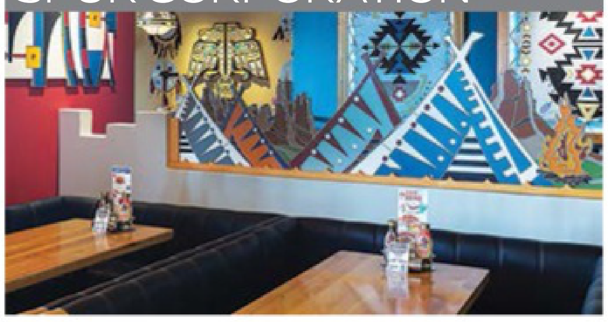
Sasol's costs have gone up and profits will be lower – a permanent situation after the disposal.

By Simon Brown

Simon's stock tips

Founder and director of investment website JustOneLap.com, Simon Brown, is *finweek*'s resident expert on the stock markets. In this column he provides insight into recent market developments.

SPUR CORPORATION



Bite to the earnings

Spur Corporation's trading update for the year through 30 June, which was released at the end of July, gives details of the impact of the hard government-imposed lockdown. Spur's system-wide sales were 5.8% higher for the period to the end of February but for the full 12 months through June this plummeted by 21.7% as sales during the lockdown months were almost 90% down before "improving" to a decline of 79% in June. July and the following months will see more improvements as lockdown regulations are being relaxed, but earnings will remain hard hit.

STEINHOFF

Calming the litigants

Steinhoff is looking to settle the many legal claims (amounting to about R136bn) it is facing with a proposed R16.5bn deal. The deal, announced on 27 July, would see impacted investors and other claimants receiving a mixture of cash and Pepkor shares. If shareholders approve this settlement, it would be an elegant solution to what otherwise will likely be years of expensive legal battles. The Pepkor part of the payment is also clever as it's an attractive asset. One issue, however, is that the Pepkor shares are valued at 1 500c for the deal, whereas they're trading at around 1 000c each. But I still think this is a preferred solution and would enable Steinhoff to continue without the costs and burden of the legal claims.

VIVO ENERGY

The Moroccan headache

Vivo Energy is a stock I write about often and while I like the business model (selling fuel in Africa), I have stayed away due to concerns about possible regulation in Morocco that could hurt profit in its largest market. One of the attractions of fuel sales is the fact that it is very inelastic. But recent results show just how a pandemic can turn everything on its head, as volumes at Vivo decreased by 7%. We are going to see a lot more pandemic pain, but we can also view this as an opportunity. Fuel sales will recover in time, albeit maybe not to pre-pandemic levels. In the meantime, however, I still want clarity on Morocco.

But I wonder if 2% will be the ceiling in this crisis. I suspect not.

CHOPPIES ENTERPRISES

Finally up to date

Choppies Enterprises has finally released its delayed results and, after having to clarify the December 2019 financials, the company is now up to date with outstanding statements. June 2020 results are due at the end of October. At the time of writing, the company remains suspended from trading on the JSE, but this should change soon. The results for continuing operations weren't bad. But considering the boardroom fights, and delayed results, I still don't consider this company to be one I would look at to invest in.

STANDARD BANK

Burgeoning bad debt

Standard Bank is the first of the big commercial banks to issue a trading update for six months ending June, and it's expecting headline earnings per share (HEPS) to be between 30% and 50% lower. The financial results are expected to be released on 20 August and what I will be looking for is the impairment charge. Basically, how aggressive are they? Ideally, they will be taking a large charge now that will cushion much of the pain over the next year or two, as people continue to default on their debt. Extracting from the update and research on the earnings that I have seen, this update suggests impairments ballooning to 2% of the total loan book, which is above the levels of the global financial crisis of 2008 and 2009. But I wonder if 2% will be the ceiling in this crisis. I suspect not.

NEWGOLD ETF

Enjoying the ride

The NewGold exchange-traded fund (ETF) closed July at an all-time high, which is exactly what one would expect to see during a pandemic. Over the last decade NewGold jumped 400%, but half of that gain has been in the last year. Holding gold in the long term is seldom a great investment. One needs to be tactical, hence me holding gold stocks for the first time in my investing life. The question is: How high will gold and its miners go? Truthfully, nobody knows. For me, the bigger, and more important question in terms of a trade rather than a long-term investment is: When do we need to sell? For now, I'm enjoying the ride, but I am also giving lots of thought as to my exit strategy. This is especially important, as not having a clearly-defined exit plan bothers me.

CITY LODGE

An expensive journey

City Lodge announced the details of its rights offer, which even the JSE refers to as a highly dilutive one. There will be 13 new shares for every one share currently in issue. This is a dilution on a scale we usually only see for companies on their knees. The new shares will be issued at 212c each in a bid to raise R1.2bn, of which most will be used to bail out the company's beleaguered BEE deal. The big question the group will subsequently face, is whether it will need more cash for operational reasons. This as occupancy levels remain severely depressed, even as leisure travel starts to reopen and business travel – the company's main market – slowly returns. The bottom line is that City Lodge will survive, but it will be an awfully expensive journey, as this rights issue shows investors.

INVICTA HOLDINGS

Profitable units sold to pay debt

Invicta Holdings has announced the sale of four business units in its Capital Equipment Group to CNH Industrial. The proceeds of the sale will be around R507m and will go to paying down debt. This is, however, a nice profit centre for the company and while lower debt is a good idea, it will result in a permanent loss of income for the company. The problem they face is getting the balance sheet into shape – this is the more important focus for them. We'll see many other listed companies selling profitable assets to repair their balance sheets as nobody wants to buy unprofitable ventures. What this also highlights is that the balance sheet remains hugely important for companies and while good times mean we pay less attention to this financial statement, we shouldn't. The reality is that the next downturn is always just around the corner – even if we have no idea exactly when, how bad it'll be or what will be its cause. Strong balance sheets with manageable debt and strong cash generation is the cornerstone of a solid company.

The new shares will be issued at 212c each in a bid to raise R1.2bn, of which most will be used to bail out the company's beleaguered BEE deal.

BRITISH AMERICAN TOBACCO

Smoking hot profit

British American Tobacco's half-year update through 30 June saw a 0.8% rise in revenue and HEPS 23% higher as it sells more premium cigarettes, according to a 31 July statement. The dividend will increase 3.6%. Overall, it is a good update, but the market was unimpressed and sold the stock down. The share continues to trade under pressure, albeit some 25% higher than 2019-lows. On a dividend yield of over 7%, paid in pounds sterling, it's being priced like a classic defensive and largely ex-growth stock, which is fair. Investors probably want more upside, but I think the current price, coupled with the dividend yield, fits the company profile and makes it an attractive investment.

INDUSTRIAL LOGISTICS

Online shopping boom

One of the property sectors that has been largely ignored is industrial logistics. In simple terms it refers to warehousing for online businesses, but it's often a lot more than that – and in many cases they're highly technical. So far, during the pandemic, this sector has performed very well while other property sectors have taken a knock. Stenprop has acquired an industrial estate in the UK for just under £20m. Its share price jumped by about 46% over the past year. On the other side, Equites, another UK and SA logistics player, has seen its share price drop by 18% over the last year. Modern logistic facilities have been a strong and positive trend for several years. With consumers using online shopping for more and varied purchases, it will likely impact our shopping habits over the long term. It is a space that investors should certainly be looking into. On a yield of almost 16% Equites must be one of the few attractive property stocks on the JSE? ■

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Photos: www.spurcorporation.comcom | Gallo/Getty Images

By Maarten Mittner

TECH STOCKS

Up and up and up and . . .

Why current market distortions can lead to further social instability.

Equity markets are usually efficient allocators of capital. But there may come a time when markets get distorted, usually due to changes in the macroeconomic environment.

Now may be such a time.

High-tech companies have grown strongly since the beginning of the year, partly justified by excellent earnings growth in the second quarter. But this has largely been achieved amid criticism that they ruthlessly undercut competitors and pay workers below-average wages. The rest of the market is losing out while the coronavirus pandemic is rapidly spreading through the US, with unemployment at the highest level in decades.

The civil unrest in the US has many causes, but rising inequalities in the country are a real ancillary factor. When wealth is created, and people feel left out, history has shown it is bound to create circumstances of instability.

Only two years ago Apple had a market cap of less than $1tr. On 4 August it was worth over $1.8tr and already there is talk of it hitting $2tr soon. It has been joined by Microsoft and Amazon in the trillion-dollar league, both also with market caps of around $1.6tr, and with Alphabet, the parent company of Google, not far behind at $1tr.

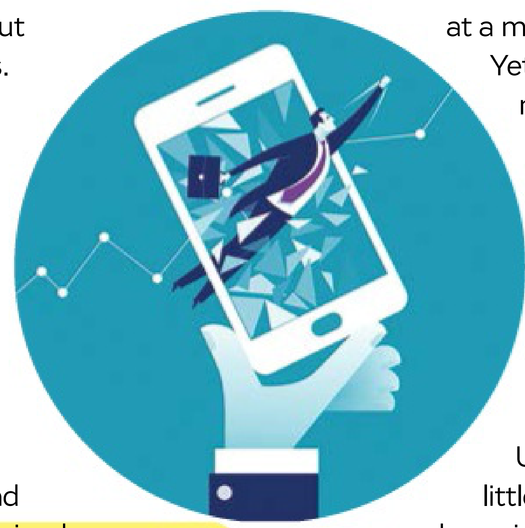
Together these trillion-dollar behemoths already comprise almost a third of the Nasdaq's total market cap of approximately $21tr, and incredibly, represent half of the value of the Dow Jones index, the venerable measure of value of old-time American companies. Their advance is equally noticeable on the S&P 500, where the top tech companies are now rapidly advancing to a third of the total value of the index.

High-tech companies are clearly riding the wave of the fourth industrial revolution, in which digital processing, robotic automation and cloud computing hold the promise of lower costs and so, greater profits.

Easy-money policies of central banks have also helped, with the US Federal Reserve being the greatest proponent of low interest rates for more than three decades now. Conditions have been created whereby capital accumulation on equity markets can continue in an uninhibited way. The boom-bust scenarios have become something of the past.

This has placed huge pressure on the traditional big brick-and-mortar companies. Most can only compete by taking on debt or reducing their number of employees. It is much more profitable for high-tech companies to perform share buybacks, or accumulate cash, than to pay workers a higher wage. All this is happening against the backdrop of a favourable tax dispensation.

Probably the most extreme example of this distortion has been Tesla. Despite concerted efforts by short sellers to benefit from a lower Tesla share price, Tesla has rocketed 300% this year to a market cap of around $300bn at one point, making founder Elon Musk immensely wealthy. Although not only manufacturing cars, it is bigger than Volkswagen, Toyota and Honda's combined market capitalisation. It has grown to become within striking distance of Warren Buffett's Berkshire Hathaway A shares, which trade at a market value of around $486bn, built up over decades. Yet Tesla sold only 367 200 cars last year. Toyota sold more than 10m units.



Only two years ago Apple had a market cap of less than

$1tr.

On 4 August it was worth over

$1.8tr

and already there is talk of it hitting $2tr soon.

Market dominance means market power, and that is where the distortions come in as competition is curtailed.

It is true that Amazon's lowest wages for its employees at $15 an hour is double that of the official minimum wage in the US of $7.25 an hour. This is what most Amazon workers earn, including delivery drivers. The average salary in the US is around $38 per hour, with Amazon showing little incentive to increase wages further and so create a booming middle class in the US. At these wages, US workers not only are not sharing in the wealth created, they remain under the pressure of little disposable income after deducting high educational and healthcare costs.

It seems unlikely that tech companies will be reined in soon. The EU Commission recently lost its anti-competitive case against Apple for additional tax assessments of $15bn, while anti-trust legislation in the US is a notoriously blunt instrument. This despite acknowledgement in recent Congressional hearings that a breakup of the big tech companies will be beneficial to the economy.

However, two developments might cause the tech bubble to die down. The one is a market correction. At a price-to-earnings (P/E) ratio of 120, Amazon looks ripe for a correction. Already there are signs of some market pullback, but the reality is that tech companies all still have massive pricing power.

Greater competition is another threat, not from inside the US, but from China, where tech companies remain strong and, importantly, very innovative. This may undercut US companies, with Intel a probable early casualty.

However, that will bring little consolation to average investors or asset managers, who are standing on the sidelines, rueing that they missed benefitting from the tech surge. Unless, of course, there is a belief that tech companies are edging toward representing on average half of the overall value of all US market caps. ■

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Photo: Shutterstock

By Lucas de Lange

JSE

Be wary of gold shares

Market experts warn they are overbought and could suddenly reverse.

With two-thirds of the JSE's 100 largest shares by market cap lying below their 200-day exponential moving averages (EMAs), the bear is no doubt continuing to dominate most of the JSE. That both the All-Share Index and the Top40 are lying above their 200-day EMAs is therefore certainly not an indication of the true state of the market.

As is apparent from the table of the strongest shares, it is mining companies, with gold shares in the lead, that are towering above the rest. That a risky group such as Harmony is the strongest share confirms how active speculators have been with regard to gold shares. It is, therefore, also understandable why so many experienced market experts are warning that gold shares always require agile footwork to prevent investors from burning their fingers. The JSE's gold index increased by 207% over the past 12 months and is highly overbought. The gold price rose by 41%. As one commentator puts it: It's time to lock in profits to protect your capital.

As far as the rest of the JSE is concerned, pessimism reigns and a report of 150 pages produced by the Organisation for Economic Cooperation and Development clarifies why this is the case. It suggests that the South African economy is in tatters, mainly owing to years of mismanagement, although Covid-19 has of course also taken its toll. Something that is especially highlighted is the high cost of the public service. These officials' salaries and wages are equal to 12% of the gross domestic product – one of the highest percentages in the world. As usual, the pain caused to SA by insolvent state enterprises is also highlighted.

An interesting phenomenon that has garnered a lot of commentary is that there is, as *The Economist* puts it, a new army of retail speculators that have become active on stock exchanges. They are, among others, chasing after shares which in their opinion may recover strongly. In the US, they are very active in technology shares, while in China potential recovery situations are also avidly being pursued.

Some of the newbies have been inspired by the success Warren Buffett had with shares such as American Express (Amex). This group was in deep trouble some years ago owing to a scandal widely reported in the media. What happened was that a major subsidiary, which owned a huge supply of vegetable oil – mainly used in salads – misled everyone. Its storage tanks were filled with sea water and only had a thin layer of oil on top. Although Amex was an iconic group (established in 1850), it was generally avoided.

But Buffett dug deeper. He liked the potential shown by Amex credit cards and also the travellers' cheques it marketed. Buffett went and sat in a restaurant in Omaha for a whole day to see how many people used Amex credit cards. It was evident that the man in the street was not worried about the scandal and continued using the cards.

Buffett made huge investments in Amex in 1964 and today it's one of his four biggest investments. The share has increased more than a thousand times in value and makes a large contribution to his personal fortune of some $68bn.

That things are going badly at Nampak, Africa's largest packaging group and currently the weakest share among the top 100, is evident from its latest interim report. Nigeria and Angola, which have been heavily affected by weak oil prices, remain a serious problem. But investors are also wary of companies that depend on SA consumers. Nampak dropped by about 88% over the past 12 months.

In the break-out column there is not a single share that grabs attention. However, it is notable that Mediclinic, JSE, Clicks and Sanlam are all trading close to their 200-day EMAs, which could mean they have a good chance of breaking through were there to be good news about the economy for a change. ■

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WEAKEST SHARES*

COMPANY	% BELOW 200-DAY EMA
NAMPAK	-67.6
HAMMERSON	-53.2
FORTRESS B	-48.1
HYPROP	-42.4
MASSMART	-41.9
MOTUS	-39.0
VUKILE	-38.3
MPACT	-37.8
INVESTEC LTD	-35.7
REMGRO	-32.4
TFG	-32.3
EMIRA	-30.4
REDEFINE	-30.3
MERAFE	-30.0
DISTELL	-27.7
PEPKOR HOLDINGS	-24.2
NEDBANK	-22.7
ASTRAL	-22.0
ABSA GROUP	-21.9
DIS-CHEM	-20.4
OLD MUTUAL	-20.3
KAP	-20.0
EPP	-20.0
PICK N PAY	-19.7
TELKOM	-19.0
GROWTHPOINT	-19.0
IMPERIAL	-18.5
TRUWORTHS	-17.5
BARLOWORLD	-17.0
MAS	-16.8
FORTRESS A	-16.0
BIDVEST	-15.9
INVESTEC PROPERTY	-15.9
WOOLWORTHS	-15.3
MR PRICE	-14.6
SASOL	-14.5
FIRSTRAND	-14.3
VIVO ENERGY	-12.4
RCL	-11.7
SHOPRITE	-11.3
LIBSTAR	-10.9
PSG KONSULT	-10.9
NEPI ROCKCASTLE	-9.6
ADCOCK INGRAM	-9.5
STANDARD BANK	-9.3
NETCARE	-9.0
RESILIENT	-8.2
SUPER GROUP	-8.2
LIFE HEALTHCARE	-7.3
SAPPI	-7.3
SPAR	-6.9
CAPITEC	-6.7
BAT	-6.4
EQUITES	-6.4
MTN GROUP	-6.0
ALTRON A	-6.0

WEAKEST SHARES*

COMPANY	% BELOW 200-DAY EMA
AB-INBEV	-4.5
PSG	-4.4
TIGER BRANDS	-4.3
RICHEMONT	-3.1
MEDICLINIC	-2.8
JSE	-2.7
MOMENTUM METROP	-2.6
CLICKS	-1.9
SANLAM	0

STRONGEST SHARES*

COMPANY	% ABOVE 200-DAY EMA
HARMONY	85.1
GOLD FIELDS	80.0
PAN AFRICAN RESOURCES	73.6
ANGLOGOLD ASHANTI	52.2
SIBANYE-STILLWATER	49.0
IMPALA PLATINUM	33.1
KUMBA IRON ORE	31.3
NORTHAM PLATINUM	30.9
ROYAL BAFOKENG PLATINUM	23.4
AFRICAN RAINBOW MINERALS	21.8
PROSUS	21.7
RMI HOLDINGS	16.6
ANGLO AMERICAN	14.1
REINET	13.4
QUILTER	12.3
STENPROP	12.2
TRUSTCO	11.9
BHP	11.6
ASPEN	11.4
THARISA	10.9
NASPERS	10.2
OCEANA	9.5
SOUTH32	7.3
CARTRACK	7.1
VODACOM	6.4
EXXARO	6.1
DISCOVERY	5.2
ZAMBEZI PLATINUM PREF	2.5
BIDCORP	2.5
CORONATION	2.1
MC GROUP	1.9
GLENCORE	1.7
TRANSACTION CAPITAL	1.3
INVESTEC AUSTRALIA PROP	1.2
MONDI	0.3

BREAKING THROUGH*

COMPANY	% ABOVE 200-DAY EMA
MC GROUP	1.9
GLENCORE	1.7
TRANSACTION CAPITAL	1.3
INVESTEC AUSTRALIA PROPERTY FUND	1.2

*Based on the 100 largest market caps.

CAN SASOL
ACID TEST?

To understand Sasol's recent travails, it is important to consider the company's 70-year history. With the industrial behemoth's results due in August, Jaco Visser takes a deep dive into the company from its birth as a parastatal and considers the outlook for the share as the group tries to move beyond the Lake Charles fiasco.

By Jaco Visser

Photo: Gallo/Getty Images

PASS THE

?

back in the infancy of chemistry, chain reactions were unstable and sometimes deadly. For chemical producers today, the stakes are still high, and they need to focus not only on the stability of their operations on the ground, but also on the stability of their finances to ensure shareholders are rewarded for placing trust in them. And, as with any listed company, management must clearly demonstrate this duty and commitment to its shareholders.

The severe consequences of a disconnect between company management and shareholders couldn't be more clearly illustrated than by the sorry saga of Sasol over the past decade. In embarking on new ventures, such as the much-analysed and criticised Lake Charles Chemicals Project (LCCP) in the US state of Louisiana, the energy and chemical company management's aspirations lacked due regard for shareholders. And Sasol shareholders can attest to the resulting monetary losses and subsequent near-complete erosion of trust in one of South Africa's industrial behemoths.

Fortunately, the outlook for this legacy company (remember that it was started with taxpayer money in 1950) seems brighter with Fleetwood Grobler having taken up the reins as CEO in November last year.

Sasol has had to endure harsh criticism in the past. When the company was created as a parastatal – to industrialise the pioneering technology whereby coal was turned into fuel – critics questioned why taxpayers should foot the bill of constructing the Sasol One plant in Sasolburg in the 1950s.

At present, shareholders want to know whether the Louisiana-based mega-project, which comes at a cost of $12.8bn (or R216bn, which is just a couple of billion lower than the construction cost of Eskom's R230bn Medupi coal-fired power station, although confirming the latter figure is more onerous than splitting carbon compounds by hand in the dark) is worth losing out on dividend payments and capital appreciation.

The LCCP was borne from former CEO David Constable's tenure. The Canadian took over the helm of the company in 2011 and stepped down after only five years at the group, during which, as reported by *Business Day* in 2016, "he performed radical surgery on Sasol, restructuring its operations and making deep cuts in its cost base at the same time as he streamlined its growth strategy to focus on the ambitious Lake Charles project in Louisiana, US".

Constable was succeeded by joint CEOs Bongani Nqwababa and Stephen Cornell, who were then forced to resign in 2019 after an independent review into the disastrous LCCP venture.

It's perhaps important to place the travails of Sasol in the context of its myriad moving parts. As fund manager Mike Lawrenson from Tantalum Capital puts it: When Constable took over, the company was viewed as cumbersome and in dire need of organisational change. Sasol was privatised and listed on the JSE by a cash-strapped apartheid government in 1979 and its history, former size and structure as a parastatal are important to consider when analysing the issues the company has grappled with in recent times.

The route from parastatal to the present

The birth of Sasol in 1950, by ramping up the conversion of coal to oil (a German technology employed by the Nazis to support their war effort), was South African industry's second attempt to capitalise on the nation's abundance of cheap coal. That is in addition to how cheap the labour was to get it out of the ground.

The Anglo-Transvaal Consolidated Investment Company (Anglovaal) discovered torbanite (bitumen shales) near Ermelo and in 1934 set up the South African Torbanite Mining and Refining Company (SATMAR), writes Stephen Sparks from the department of historical studies at the University of Johannesburg, in a 2016 article titled "Between Artificial Economics and the Discipline of the Market: Sasol from Parastatal to Privatisation" in the *Journal of Southern African Studies*. Sparks scoured government and Sasol archives in the research for his article.

Anglovaal then appointed Dr Hendrik van Eck (later the head of the Industrial Development Corporation) to probe the establishment of an oil-from-coal plant in SA, writes Sparks. Van Eck, together with another engineer at Anglovaal, took the then-minister of commerce and


Bongani Nqwababa
Former joint CEO of Sasol


Stephen Cornell
Former joint CEO of Sasol


Mike Lawrenson
Fund manager at Tantalum Capital

industries, Adriaan Fourie, in October 1936 to Nazi Germany to visit one of the Fischer-Tropsch factories – the latter name refers to the process of turning coal to oil, according to Sparks. Anglovaal's torbanite operation "depended on subsidy through elevated customs duty and rail tariffs on imported petrol".

By the mid-1940s Anglovaal had acquired a more advanced version of the Fischer-Tropsch process from the Americans, and government officials seemed more enthusiastic about the technology and the prospect of utilising SA's abundant coal reserves. Anglovaal, however, diverted its capital and attention to the Free State gold fields around the same time, writes Sparks.

And so, in April 1950, an industrial adviser to the state convinced Van Eck, who was then heading the IDC, to fund the coal-to-oil project which should be controlled by the state, according to Sparks' research. Taken by Sparks from the National Assembly's *Hansard* on 10 April 1951, MPs were jubilant about Sasol's start as it wouldn't be "controlled from abroad or by international monopolies and cartels but by the South African state". Thus, no outside monopoly capital would be employed. But the taxpayer, in post-war SA, had to pay up.

In this context, the words of Etienne Rousseau, first managing director of Sasol, (taken from Sparks' article) ring rather ominously today: "When we think of oil from coal we must think in terms of artificial economics and government protection."

As the price of oil remained low during the 1950s and 1960s, Sasol started to diversify its activities energetically, writes Sparks. "Sasol moved aggressively into chemical production and the provision of gas."

And then the oil shocks of the 1970s came about. When SA's oil supply from Persia was cut off following the Iranian revolution in 1978, Sasol's existence and transformation of coal to oil became a necessity. Plans were approved to construct Sasol 2 and Sasol 3 at Secunda, but the public purse couldn't afford it, writes Sparks. This led to Sasol's privatisation in 1979 – the first parastatal that went this route, according to him.

Lake of tears or of joy?

Thus, the LCCP, which was announced in October 2014 at an initial cost of $8.9bn, might sound familiar to long-time watchers of this company. It signalled another huge undertaking for the company. However, this time it would be the shareholders' and not SA taxpayers' problem.

In the market announcement, Constable, then still CEO, promised: "In spite of a largely volatile macroeconomic outlook, we are confident that we will deliver this project successfully, by drawing on our experience of executing world-scale fuel and chemical facilities, and enlisting the best employees and industry partners." The announcement also stated: "Site

Photos: Supplied | Gallo/Getty Images

"It seems that the improved share price is reflective of the company's solvency rather than its expected earnings."

preparation is underway, and the company expects that the facility will achieve beneficial operation in 2018."

Almost $12.8bn, six years and three CEOs later, and the plant is still not fully operational. And this time around, Sasol must bear the backlash of shareholders and banks, rather than the grunts of taxpayers and a benevolent government, in explaining why the company should be trusted.

The loss of confidence can be seen in Sasol's share price: ten years ago, on 30 July 2010, the share price closed at R289; six years ago – just before the Lake Charles announcement – the stock traded above R600. From there, the value destruction started. It reached an intra-day low of R20.77 at the height of the oil price plunge at the end of March this year. Add to this banks' uneasiness with Sasol's covenants (or terms at which they are willing to lend money to it), which existed prior to the oil price crash. The stock had risen back to R139 at the time of writing.

"The higher share price is reflective of the improved outlook for the company's solvency rather than its expected earnings," Richard Cheesman, a senior investment analyst at Protea Capital Management, tells *finweek*.

The stock is trading at a forward price-to-earnings (P/E) multiple of 56.14 and a historic one of 10.86 – meaning that analysts expect lower earnings in future. At this forward multiple, the company is priced dearly.

These multiples, however, may seem a bit disjointed as the LCCP – although beset by overruns – may just as well (as back in the day when SA's foreign oil supply dried up) be its saving grace. And here we need to crack open the workings and offtake markets of this multibillion-rand plant.

The Lake Charles plant firstly consists of an ethane cracker. The word "cracking" refers to the chemical process of breaking down the hydrocarbon compounds of the feedlot stocks (in this case ethane). The ethane cracker is designed to produce just over 1.5m tonnes of ethylene per year.

In addition to the cracker, the plant also consists of a low-density polyethylene (LDPE) plant, a linear low-density polyethylene (LLDPE) plant, and an ethylene oxide (EO)/ethylene glycol plant, which together will use two-thirds of the ethylene produced by the cracker, according to Sasol.

Almost
$12.8bn,
six years and three CEOs later, and the plant is still not fully operational.

Richard Cheesman
Senior investment analyst at Protea Capital Management

There are also three smaller plants that will produce higher-value chemicals: a Ziegler alcohol unit, an Alumina unit and a Guerbet alcohols unit.

Sasol is banking on the sales of the polyethylene and specialised chemicals (called performance chemicals by the company) to justify its investment in Lake Charles. The plant's construction didn't go unnoticed by some other global chemical companies.

It was reported in the financial media on 28 July that Hanwha Solutions (which formed after a merger of Hanwha Chemicals, Hanhwa Q SELLS and Hanwha Advanced Materials) of South Korea is interested in a 50% stake in the Lake Charles ethane cracker – not the whole chemicals project. Hanwha Chemicals produces polyethylene, polyvinyl chloride (PVC) and chlor-alkali. Hanwha is reportedly offering between $1.7bn and $3bn for this stake.

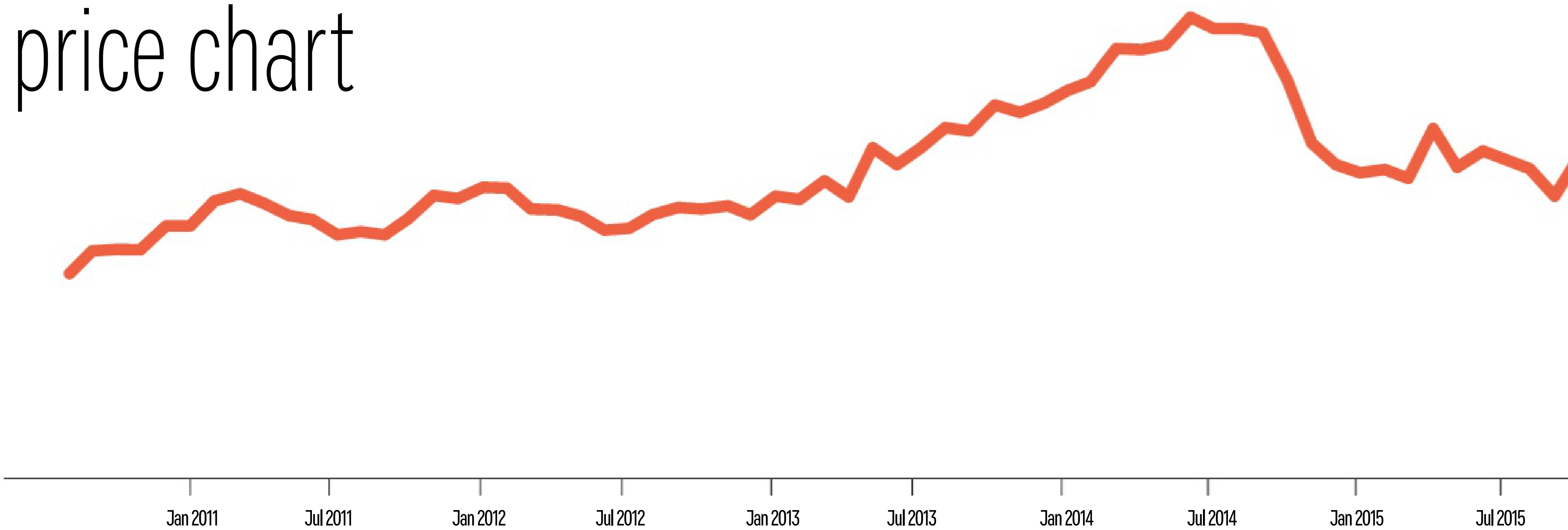
According to Lawrenson, on the assumption that Sasol only intends selling a 50% stake in the base chemicals component of Lake Charles, this rumoured sale would imply that Sasol is effectively disposing 30% of the economic interest in the whole Lake Charles project. Using the reported bid range, this would imply the value of Lake Charles at between $5.7bn and $10bn – less than the anticipated $12.8bn construction cost. "It is unlikely that others will pay for your inefficiencies," says Lawrenson, referring to the almost 50% cost overrun on the original $8.9bn budget for Lake Charles.

The chemistry of Lake Charles

Let's, then, consider the global market for polyethylene. The consultancy group Wood Mackenzie, in a March report, describes the market for this plastic ingredient bluntly: "Wood Mackenzie's base-case global ethylene outlook over the coming industry cycle to 2025, can be summarised in one word – overcapacity." And the reason for this conclusion is "a large and sustained build of capacity relative to underlying demand growth levels". That means that too much polyethylene production facilities (such as Lake Charles) have come into operation recently.

Wood Mackenzie generated two cash-cost production curves from around 300 ethylene producers across the world: one when the oil price trades at $60 a barrel and another at $30 a barrel. At the time of writing it traded at $43.48 – almost midway. At both these oil price levels, North

Sasol **10-year** price chart



American ethylene producers dominated the quartile of lowest-cost producers in the world. Their costs range from $180/t to just under $300/t. And Sasol, according to a statement in 2016, falls within this first quartile of production costs.

The current gross margins at which Sasol sells ethylene are around $150/t, explains Tantalum's Lawrenson. For polyethylene, Sasol's gross margins rise to between $400/t and $500/t, he says. The successful start-up of the final LDPE unit (delayed to October) is key to enabling Sasol to bank these higher margins on the total installed polyethylene (LLDPE and LDPE) capacity of about 900 000t per year.

And these figures are for a distressed chemical market, as Lawrenson explains. "Chemical demand growth is closely correlated with economic growth. Chemical prices have collapsed this year and are well off their highs of 2018. They have, however, bounced off their recent May lows." Thus, the chemical products from Lake Charles will not have a defensive quality in times of economic hardship.

Photo: Shutterstock

The outlook

To fund the Lake Charles construction, Sasol turned to external funders. This included a $3.9bn revolving credit facility with a syndicate of banks, according to its financial statements through 31 December 2019.

The debt issued by the banks came with a condition (or covenant) that Sasol's debt-to-ebitda (earnings before interest, tax, depreciation and amortisation) ratio be less than three times. By the end of December this ratio was at 2.9 times and Sasol was close to breaching it, which would have triggered the banks to call in their loans. The company has negotiated a waiver of the covenant to June 2020 and an increase in the covenant to four times for the December 2020 half-year.

"In some ways the banks are running the business," says Lawrenson referring to Sasol's drive to rectify its balance sheet.

Sasol came up with what seems to be a "magic bullet" to reorganise its finances, as Lawrenson puts it. It is referred to by analysts as the "2+2+2" $bn-plan. Sasol aims to lower its net debt-to-ebitda ratio from the 2.9 times at the end of December 2019 (and likely higher at financial year-end on 30 June) to below 3 times, according to a market update in March. This would be done by improving its working capital by $1bn in the year through 30 June 2020, a cost reduction plan of $1bn in the current fiscal year, selling assets worth $2bn and possibly raising $2bn through a rights issue.

At its current share price of R139 a share, a share raise would mean issuing 241m new shares and diluting those shareholders who don't participate in the rights offer by 38%. Apparently the appetite for this is low

among management, hence the focus on asset sales.

"You couldn't choose a worse time to do an asset sale than now," says Lawrenson, attesting to the depressed global macroeconomic outlook.

In addition to the Hanwha rumours, Sasol said on 29 July that it will sell its air separation units at Secunda to Air Liquide for R8.5bn (around $500m). This also removes a big carbon-emissions headache for Sasol, as Air Liquide will now endeavour to cut the greenhouse gas emissions at the plant. Sasol will buy back the products under a long-term agreement and by doing this, the company is basically outsourcing these production costs.

On 1 July, Sasol said it is divesting from the Escravos gas-to-liquids plant in Nigeria by selling its stake to Chevron. On the same day, the company said "divestment processes are well underway with respect to Sasol's equity interests in the Republic of Mozambique Pipeline Investment Company (Pty) Ltd (ROMPCO) pipeline and the Central Termica de Ressano Garcia (CTRG) gas-fired power plant in Mozambique". These selling prices were not disclosed.

If you take the Hanwha sale's rumoured $1.7bn (rather err on the low side) together with the Air Liquide deal's $500m (subject to regulatory permissions), Sasol could well be on the way to reaching its asset-disposal target of $2bn and may delay a rights offer.

"They had very little choice, they were forced to sell," says Lawrenson. "I am happy if they can sell these assets at 'fair' value rather than doing a deeply discounted rights offer."

Sasol said at the end of May that it expects its headline earnings per share for the year ended 30 June will be at least

20%

lower than the comparable period a year ago.

Protea's Cheesman says Sasol may elect not to do the rights offer. "If you look at how Anglo American and Glencore got through their troubles a couple of years ago, a rights issue may not be necessary."

The final issue that Sasol is being pressed on, is its working capital. By the end of December last year, the company's net working capital was 14.6% of turnover, or R29bn. That is an improvement from the 18.8%, or R34bn, recorded at the end of June 2018. With inventory kept at roughly R30bn and creditors at between R21bn to R22bn over this timeframe, management succeeded in reducing its debtors' book from R26bn to R21bn. To enhance the company's working capital by $1bn (R16.75bn) a year, will mean that either debtors and inventory are lowered, or trade creditors increased. It's a tough one.

Nevertheless, Sasol said at the end of May that it expects its headline earnings per share for the year ended 30 June will be at least 20% lower than the comparable period a year ago. Shareholders and the string of bankers who lend to the company are awaiting the full-year financial results, expected to be released early August.

Shareholders have waited six long years for the Lake Charles project to deliver tangible benefits. In the same way as in the 1950s, South Africans are talking about Sasol. Only this time around there is no national imperative to soothe stakeholders' uneasiness. ■

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By Amanda Visser

The Covid rework: From leases to

The coronavirus pandemic has seen a shift in the substance of lease agreements. It has also necessitated a change

Words like 'force majeure', 'vis major' and 'casus fortuitous' have special meaning in a time when a pandemic causes health and financial crises.

The Covid-19 pandemic forced retailers to close their doors for weeks on end and are now only allowed to serve a limited number of customers at a time. More people than anyone thought possible are working from home.

However, tenants are stuck with the excess office space, and their lease agreements. Cash flows have either dried up or slowed to a mere trickle.

Law firm Werksmans' head of property law and real estate, Fátima Rodrigues, says most retail and commercial lease agreements contain force majeure clauses. This is defined as an unforeseeable event or circumstance that prevents a party to fulfil his obligations under a contract.

"However, the manner in which an event of force majeure has been defined in the particular lease agreement must be closely examined in order to assess whether a pandemic, such as Covid-19, meets the requirements," she says.

Rodrigues says that even if a pandemic is included in the requirements, it may not excuse payment while the pandemic continues. "Any non-payment by the tenant will result in a breach under the lease agreement."

But landlords are not necessarily in the strongest of positions. They need tenants and cannot under current circumstances require "absolute compliance" with the tenant's obligations under lease agreements.

"I have experienced that landlords are quite accommodating towards their tenants," says Rodrigues. "Landlords have either reduced rentals, suspended payments for a period or they have deferred payments. This is certainly not something tenants are used to."

When the lease agreement is not clear on the consequences of an event of force majeure, then common law principles can be relied on.

The common law principle of "supervening impossibility of performance" means that due to an unforeseeable or unavoidable event it has become "objectively impossible" to comply with the obligations in an agreement.

Supervening impossibility of performance can occur due to a vis major (major force) or casus fortuitous (accidental occurrence) – events emanating from nature or from man and are irresistible and outside the control of the ordinary person, explains Rodrigues.

Fátima Rodrigues
Head of property law and real estate at Werksmans Attorneys

There are limited options for tenants who may find it "objectively impossible" to adhere to the terms of their lease agreements.

Richard Debonnaire
Regional manager at office furniture retailer Cecil Nurse

The options

There are limited options for tenants who may find it "objectively impossible" to adhere to the terms of their lease agreements. They can sublet if it is allowed in their agreements, but they must find someone who wants to sublet, and the landlord must be happy with the replacement tenant.

The landlord will obviously consider the financial liability of the sublessee. Although the new tenant will pay the rental and operational costs, the original tenant remains responsible for rental and costs for the duration of the lease period, should the sublessee default.

Most leases do not allow for accession and assignment, since it completely relieves the tenant from all obligations the minute the landlord agrees that the tenant can assign the lease for the rest of the period to someone new.

"Landlords will not negotiate a new lease but may be willing to change some of the clauses to assist tenants. It is unlikely that they will cancel the lease and enter into a lease agreement with someone else, unless a tenant becomes insolvent or the company is liquidated," says Rodrigues.

Pandemic designs

Office design has also been impacted, says Richard Debonnaire, regional manager at office furniture retailer Cecil Nurse. "Covid-19 has increased our awareness of how much we touch and the danger that poses for spreading the virus."

There is a host of automated aspects to an office that can and has been introduced. Doors are not being opened by a handle anymore, sensors now open doors automatically. Proximity switches allow lights to go on when there is movement in the office. Many companies have also introduced automated access control to ensure as little as possible contact with surfaces.

Debonnaire says companies will have to consider the space required for employees who will have to work at the office. The square metre per person allocated to their workspace will have to increase due to social distancing requirements.

Many office areas had to be refurbished to take proper hygiene into account. Easy-to-clean surfaces such as perspex, glass, tiles, vinyl and anti-microbial fabrics are now uppermost in mind when "remaking" the office. Passages with floor-based signage directing the "flow" of movement may become a common feature of the office after Covid-19.

Better use of open spaces

Desk structures must be reconfigured. "Flexible

office space

in office space layout.

furniture cluster-desks (a combination of workstations in a two-way, four-way or six-way cluster) can be reconfigured into two-way clusters," says Debonnaire.

He says even before Covid-19 office designs catered for informal meeting spaces in open areas. The seats are surrounded by screens to offer some privacy to employees. He says the design of these "collaborative spaces" will become more crucial to create an environment where people can feel safe when they meet face-to-face.

To prevent offices from looking deserted, with less people occupying the same space, informal "collaboration" spaces will increase. Companies will also provide more private areas for video calls and more focused work. "Some of these spaces can even be hired out to generate some additional income," says Debonnaire.

A key feature of the modern office after Covid-19 will be dedicated outdoor air systems that extract stale air out of the building and bring in fresh air. Centralised air-conditioning systems pose a real threat for the recirculation of germs.

Covid-19 will not cause the death of the open-office concept. The office environment will, however, change to allow for separated desks, safety screens in front and next to each other, more collaborative informal spaces and private areas for video calls, notes Debonnaire.

The pandemic has certainly forced businesses to be more focused on their office space and work environments, while placing their staff's wellbeing at the top of their list of priorities, he notes.

The future

Tenants are going to be far more aware of their space requirements and the type of rentals they will be willing to pay. It is not a landlord's market, says Rodrigues.

"Rentals are likely to decrease with new lease agreements, and the periods are likely to be shorter. Force majeure clauses will include pandemics. Currently a lot of the leases do not have these clauses, mainly because we have not had a pandemic in the last century."

She suspects landlords may require tenants to take out additional insurance to cover them for events when they are unable to conduct business.

Rodrigues also foresees a slowdown in investments in new retail and office developments. Many developments that were in the pipeline have been placed on the backburner or scrapped altogether. ■

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Photos: Supplied

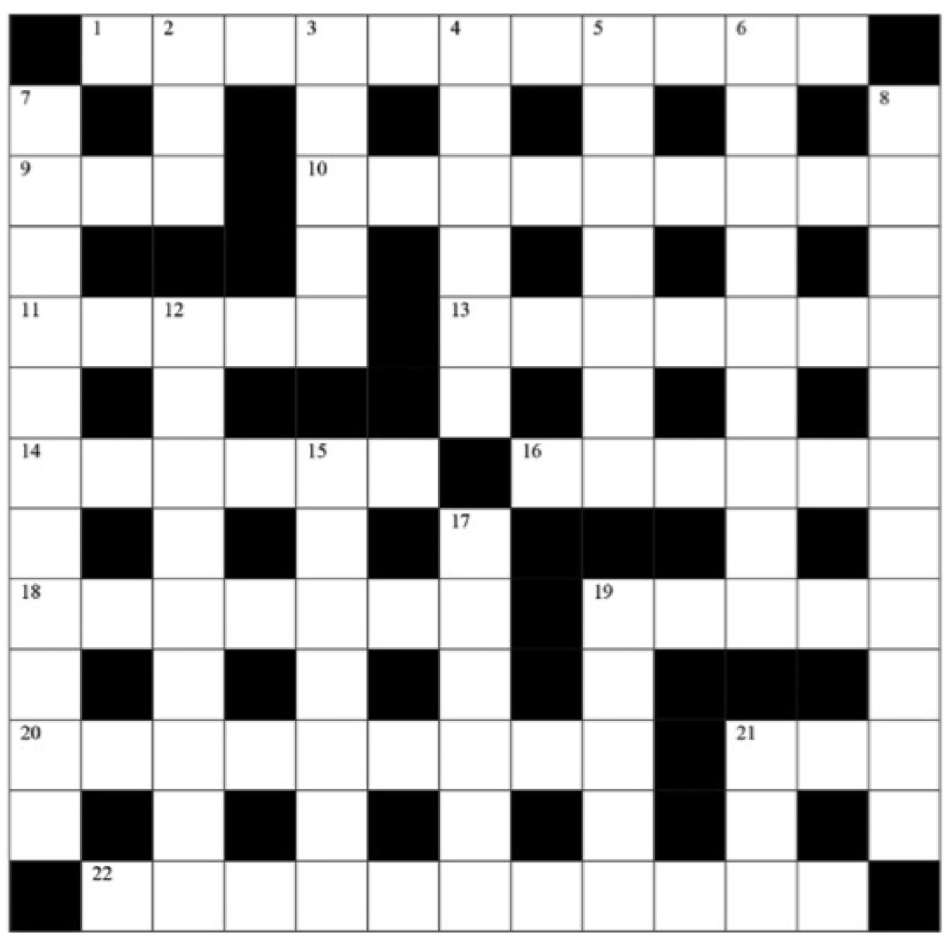
How up to date are you with current affairs? Take our quiz to find out. It will be available online via fin24.com/finweek from 10 August.

1. Fill in the missing name: As of 1 October, __________ will be the new chief financial officer of Tiger Brands.
2. **True or False?** Intra-provincial travel for leisure is allowed under South Africa's advanced lockdown level three.
3. Nominations for the 72nd annual Emmy Awards were announced at the end of July. Which series received the most nominations?
   - Game of Thrones
   - Ozark
   - Watchmen
4. **True or False?** In June, the High Court denied Eskom the right to recover around R69bn over the next three years from customers in the form of higher electricity tariffs.
5. At what age did South African anti-apartheid campaigner Andrew Mlangeni pass away?
6. **True or False?** ArcelorMittal is a supplier of iron ore to the global steel industry.
7. Name the current CEO of Sasol.
8. Cape Town is South Africa's second-most populated city. Which city is the third-most populated?
9. **True or False?** The African Development Bank is headquartered in Johannesburg.
10. In June 2020, South Africa recorded a budget deficit of:
    - R15.7bn
    - R22.3bn
    - R31.5bn

CRYPTIC CROSSWORD NO 758JD

ACROSS
1 Mark of opponent's indignation (11)
9 A cutting alternative to a blade (3)
10 Legal man railing about the station (9)
11 Organised close support (5)
13 The old man's gone nuts! (7)
14 Embellish Her Majesty's food store (6)
16 Deluged with shoals at sea (6)
18 You'll freak out when you go off with the answer! (4,3)
19 Uniform rise (3,2)
20 Final part of story still to be recorded (9)
21 Introduction to history of English garden (3)
22 Get arranged specially for high risk (5,6)

DOWN
2 Slip up halfway through the task (3)
3 Claim to be first in queue, without that French flavour (5)
4 Acknowledged all there (6)
5 Trims US outlay on disease (7)
6 Achieved total with two wickets down? (3-3-3)
7 Girl badly isolated by group (11)
8 Shop holder about to knit jumper (11)
12 Male stays fitter (9)
15 Models from ample characters under review (7)
17 No hesitation with extra number added to another number (6)
19 Gain information on Golf List (5)
21 Hurry upstate (3)



Solution to Crossword NO 757JD

ACROSS: 1 Abut; 3 Banality; 9 Truncal; 10 Umpty; 11 As understood; 13 Legume; 15 Arista; 17 Knocks it back; 20 Horde; 21 Egotist; 22 Celerity; 23 Neep

DOWN: 1 Actually; 2 Uhuru; 4 Allure; 5 Adulteration; 6 Impious; 7 Yo-yo; 8 Academic year; 12 Backstop; 14 General; 16 Assent; 18 Afire; 19 Chic

On margin

Covid corruption

This issue's isiZulu word is *mi*. *Mi* is "here, take this".

I have been trying to wrap my head around the figures being bandied about in relation to personal protective equipment (PPE) corruption. So, the government just said "*Mi*, *ama* billion"? It must be nice.

With the figures that have been mentioned, it sounds to me like we should have an oversupply of PPE then. There should be people just walking around handing out PPE. Let's call them PPE genies.

For instance, you're in your room, crying about the state of the economy, when a PPE genie pops up, hands you a disposable mask and says, "*Mi*, dry your eyes and get into politics. That's where the money is."

A different situation would be if you're rushing to the Shul, but in your haste to be one of the 50, you have forgotten your yamaka. Worry not. A PPE genie would pop up, hand you a N95 mask and say, "*Mi*, Brother."

In another scenario, you're shooting a hip-hop music video but your stylist fell ill so you don't have cool outfits. A PPE genie pops up and gives you hazmat suits, saying, "*Mi*, my friend."

You've run out of lockdown games to play with your kids and are pulling your hair out, trying to come up with something. Without warning, a PPE genie pops up, hands you a mask and says, "*Mi*, use this for awesome blindfold games."

Or it's your birthday, but you have no balloons because you are scared to go to the shops. I don't blame you. The PPE genie pops up and hands you a bunch of latex gloves for you to blow up and use as balloons.

Well, none of the above is going to happen, even though the money is gone. Poof.

– *Melusi's #everydayzulu* by Melusi Tshabalala

"I think you may have found the *'how many is too many people in a Zoom meeting'* threshold."

Verbatim

Rico Schacherl @ricoschacherl
I swear, that maniac weaver bird in our back garden is a townhouse developer ... he's now building nest #6.

I A M M M A P U L A @Mmaps_ThePro
Corruption in Eastern Cape issa sport.

Malehloenya Tsoaeli @iTsoaeli
I bought Choice Assorted today because we don't know if we'll see Christmas 2020.

Tito Mboweni @tito_mboweni
A tender is an ethical contract. It is not a blank cheque to deceive and steal. And stealing from unwell people! During a Covid-19 pandemic! Please people. What kind of people are these criminals?!

Pierre de Vos @pierredevos
Colleagues.

Dr Dirk Donkerbal @dirkdup69
Am I the only one who thinks the SIU (special investigate unit) is just one dude sitting at a desk in a basement somewhere?

Kananelo @kaysexwale
I asked for coffee half an hour ago and was ignored. I switched off the Wi-Fi and coffee has suddenly materialised. Kids!

Tom Eaton @TomEatonSA
Respect to the Cape Town police officer having a smoke in his car. It must have taken the most incredible willpower to ration your supply from March until now.

Shauna @goldengateblond
This woman at Whole Foods is choosing a bundle of asparagus more carefully than I chose my husband.

"Be yourself; everyone else is already taken."

– Oscar Wilde, Irish poet and playwright (1854 - 1900)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