

Pension-Secured Loans

Facilitating Access to Housing in South Africa?

Prepared for FinMark Trust by Linda Sing

A WORD OF APPRECIATION

Many thanks to everyone who agreed to be interviewed for this research and who so openly shared their invaluable experience and insight with the author.

Appreciation also goes to the participants of the workshop who assisted in refining the final product through robust debate.

Special acknowledgement must go to Kecia Rust, Jessica Naicker and Rob Rusconi for their generous intellect, challenging discussions and passionate interest. Their contribution has made this research richer.

Any omissions or errors remain the responsibility of the author.

TABLE OF CONTENTS

1. INTRODUCTION	4
2. RESEARCH METHODOLOGY	6
3. THE PENSION-SECURED LOAN MARKET	7
3.1 The South African Retirement Fund Market	7
3.2 Alternative Models of Pension Backed Housing Finance	9
3.3 The Pension Funds Act (No. 24 of 1956)	11
3.4 The South African Pension-Secured Loan Market	12
3.5 Financial Sector Charter Context – Market Potential	16
4. THE PENSION-SECURED LENDING VALUE CHAIN	27
4.1 Overview of the Process	27
4.2 Supply-Side Participants – Roles and Responsibilities	29
5. MYTHS, ISSUES AND OPPORTUNITIES IN PENSION-SECURED LENDING – RECOMMENDATIONS FOR THE FUTURE	33
5.1 Appointment of Loan Provider – Conflict of Interest	33
5.2 Multiple Loan Providers and Fund Members’ Freedom of Choice	34
5.3 Pricing – The Interest Rate Debate	36
5.4 Fees	46
5.5 The “Use of Funds” Conundrum	49
5.6 Product Enhancements	52
5.7 Awareness and Education	55
5.8 Escalating Costs - Administrative and Operational Challenges	56
5.9 The Impact of the Global Economic Downturn of Retirement Savings	61
6. CONCLUSION	63

LIST OF FIGURES

- Figure 1: Central Provident Fund – Singapore
- Figure 2: Housing Finance By Income
- Figure 3: Financial Sector Charter Average Loan Values
- Figure 4: Pension-Secured Loans – Market Potential
- Figure 5: Total South African Mortgage Advances – 2003 to 2008
- Figure 6: Retirement Fund Membership
- Figure 7: A Macro View – Estimating Market Potential
- Figure 8: Pension Secured Loans – Estimated Market Size
- Figure 9: Pension-Secured Loans – Direct Loans
- Figure 10: Pension-Secured Loans – Third-Party Loan Provider
- Figure 11: Supply-Side Participants (Third-Party Loan Provider)
- Figure 12: So...Are Pension-Secured Loan Interest Charges Too High?
- Figure 13: “Use of Funds” Management – Upfront Monitoring
- Figure 14: “Use of Funds” Management – Private Label Card
- Figure 15: Pension-Secured Lending Value Chain

LIST OF TABLES

- Table 1: Privately Administered, Underwritten and Parastatal Retirement Funds (excludes Government Employees Pension Fund)
- Table 2: Government Employees Pension Fund
- Table 3: South African Retirement Fund Industry
- Table 4: Third Party Pension-Secured Loan Providers – Market Share Estimates
- Table 5: Pension-Secured Lending – Estimated Market Size
- Table 6: Financial Sector Charter – Housing Finance Extension – Value of Housing Finance
- Table 7: Financial Sector Charter – Housing Finance Extension – Number of Housing Loans
- Table 8: Average Housing Loan Values Over A 5-Year Period
- Table 9: Housing Finance Products – Interest Rate Comparison
- Table 10: Mortgage Loans vs. Pension-Secured Loans
- Table 11: Factors Influencing the Cost of Providing Pension-Secured Loans
- Table 12: Pension-Secured Lending – Revenue vs. Cost Comparison
- Table 13: Pension-Secured Lending – Summary of Costs and Fees

1. INTRODUCTION

Pension-secured housing loans¹ are increasingly forming a critical part of the financial sector's housing finance armoury with some 257 000 loans, valued at R 4.8 billion having been extended in the five-year period since inception of the Financial Sector Charter (FSC) in January 2004². Proponents of the product see pension-secured housing loans as an integral part of the private sector's housing finance solution, which offers an opportunity for low-income earners to release equity "trapped" in pension/provident funds to satisfy immediate housing needs and as a means to ultimately create wealth over the long-term. Others view these loans as the first step on the road to penury, putting people's retirement savings at risk and in the long-term compounding the State's burden of having to provide adequate social support for an aging population.

With the prevailing shortage of housing stock amongst South Africans who can afford housing finance estimated as affecting some 625 000 households³, coupled with the current contraction in the development of new residential property, indications are that pressures on housing supply will be exacerbated.

Generally, pension-secured loans (and unsecured housing loans) have predominantly been applied to home improvement projects, rather than for the purchase of new homes, as the average size of these loans are relatively small. With increasing numbers of South Africans not being able to afford to purchase new homes⁴, it is not inconceivable that the market will reflect a shift from individuals seeking mortgage finance for the purchase of existing or newly-built homes, to seeking funding for home improvements or enhancements to already-occupied properties, in the form of pension-secured or unsecured personal loans. Therefore, it is reasonable to assume that the pension-secured housing product will continue to exert influence on the affordable housing market as a financing option for incremental housing.

In addition, with the financial services industry having concluded the first measurement period of the Financial Sector Charter at the end of 2008, and the anticipated continuance of the sector's commitment to expanding South African's

¹ The terms "pension-secured loans", "pension-supported loans", "pension-backed loans" and "fully guaranteed loans" are used interchangeably throughout this study. They refer specifically to loans provided by financiers to individuals for housing purposes, where the collateral for the loan is some percentage of the borrower's accumulated retirement savings

² Banking Association of South Africa, September 2008.

³ Matthew Nell and Associates undertook research in 2005 on behalf of the Banking Association South Africa to quantify the size of the housing backlog for those households that could afford housing finance. The research specifically excluded those South African households that were dependent on the State to provide fully subsidised housing. – Housing demand and supply research is presently being undertaken and updated information is expected to be available by mid-2009. The importance of this study cannot be stressed enough, as it incorporates an investigation into the type of housing finance the FSC market will require, e.g. to purchase an existing property or newly-built home; to extend or improve one's current dwelling, and consequently the projected growth in pension-secured lending.

⁴ Recent research undertaken by Eighty20 (February, 2009) indicates that interest rate increases, the rising cost of construction, the introduction of more stringent affordability assessment criteria by the National Credit Act and tightening credit markets which have seen banks requiring bigger cash deposits, significantly reduces the number of people who would be eligible for mortgage finance.

access to housing finance, pension-supported, loan products are expected to remain an integral part of the array of housing finance products.

Pension-secured loan providers and the product itself have, from time to time, been the subject of public scrutiny and heated discussion, on issues ranging widely from accusations of conflicts of interest amongst parties involved throughout the process of appointing providers of finance, to the “leakage”⁵ of borrowed funds and non market-related pricing of loans. Questions have also been raised about the effectiveness of the product distribution channels in reaching the consumer, the competitive dynamics of the industry and the efficacy of the pension-supported loan as an appropriate mechanism for housing finance.

Thus, whilst the pension-secured loan industry has been in existence for close to twenty years, as a result of the closed nature of the industry (with few loan providers and relatively low loan take-up), the low levels of product awareness amongst the general public and non-industry players, relatively little is known about the mechanics and significant influencers of the business.

Against this backdrop, the objectives of this study are to:

- i. Describe the pension-secured personal loan industry in South Africa – identifying the numerous actors, attempting to gauge the magnitude of the market and discussing the market potential.
- ii. Charting the entire value chain of the pension-supported loan – from the initial establishment of the loan scheme to the eventual payout of loan proceeds to the borrower.
- iii. Identify issues impeding the effectiveness of the pension-secured loan from facilitating access to housing and recommend potential solutions. The discussion will situate the pension-supported loan within the suite of available housing finance products and evaluate its effectiveness as a financing mechanism that facilitates access to housing for lower income earners⁶.

⁵ “Leakage” refers to the phenomenon where the proceeds of pension-secured loans are applied for purposes other than that stipulated in the Pensions Fund Act (No. 24 of 1956). The Act stipulates that where a loan is secured by the retirement fund member’s accumulated pension/provident funds savings, the proceeds can only be used to purchase, upgrade or renovate a dwelling which is the member’s primary place of residence.

⁶ For the purposes of this study, “low income” or “affordable housing” borrowers are defined in terms of the definition encapsulated in the Financial Sector Charter, i.e. individuals in their personal capacity or a household, earning between R 1 500 and R 7 500 per month. The table below details the FSC qualifying income bands.

YEAR	LOWER LIMIT	UPPER LIMIT
2003	R 1 500	R 7 500
2004	R 1 610	R 8 010
2005	R 1 680	R 8 190
2006	R 1 730	R 8 440
2007	R 1 810	R 9 080
2008	R 1 930	R 9 670
2009	R 2 145	R 10 760
Source: Banking Association South Africa (2009)		

2. **RESEARCH METHODOLOGY**

The terms of reference, and limited scope and duration of this study, obviates the ability to undertake broad-based, quantitative research. Therefore, a qualitative approach has been adopted. Information and data have thus been gleaned from multiple sources and varied interested parties participating in the pension-secured personal loan industry. The qualitative methodology used in this investigation encompasses the following data sources:

- Literature review – High-level review of available South African and international literature.
- In-depth interviews with industry role-players – Representatives of commercial banks, other financial services participants who are active providers of pension-supported loans, government and/or regulatory bodies, housing practitioners, retirement fund trustees and retirement fund administrators.
- Industry workshop – A presentation was made to industry participants based on a draft version of this work⁷. Feedback from the workshop has been incorporated into the final version of this study.

A word of caution must be raised about an important limitation of this study in that neither retirement fund members nor individuals who had taken up pension-secured loans were directly interviewed. Information on borrowers' views on pension-secured loans is based on input and comments from industry representatives interviewed⁸.

The scope of this research is also limited to the extent that it only refers to the retirement fund industry as it pertains to the provision of housing loans. Whilst this research recognises the importance of retirement savings for the long-term, personal risk management of all South Africans and its associated benefits for the overall growth of the national economy, it does not attempt to investigate or address the broader challenges inherent in the retirement savings sector⁹.

⁷ The workshop was held on 26 March 2009 and included loan providers, regulatory officials, members of the Ministry of Housing, and retirement fund, housing and credit risk specialists.

⁸ There is an opportunity to commission in-depth research to ascertain whether pension-secured loans currently satisfy the housing finance requirements of borrowers and to determine what needs remain unserved.

⁹ For a more comprehensive overview of the retirement savings industry and a discussion of its broader challenges, see Rusconi, R. (2008) – South African Institutional Investments – Whose Money Is It Anyway? – A Discussion Document available on www.tresconsulting.co.za

3. THE PENSION-SECURED LOAN MARKET

3.1 The South African Retirement Fund Market

In order to contextualise the pension-secured lending market, it is useful to understand the size of the retirement fund industry in South Africa.

Privately administered, underwritten and parastatal (Transnet, Telkom and the Post Office) retirement funds constitute two-thirds of the South African retirement fund industry, whilst the Government Employees Pension Fund (GEPF) makes up the remaining third.

PRIVATELY ADMINISTERED, UNDERWRITTEN AND PARASTATAL RETIREMENT FUNDS¹⁰		
(excludes the Government Employees Pension Fund)		
	31 December 2005	31 December 2006 ¹¹
Number of Retirement Funds	13 390	13 325
Net Assets	R 1.28 trillion	R 1.45 trillion
❖ Privately administered and underwritten funds	❖ R 805 billion	❖ R 846 billion
❖ Transnet, Telkom and Post Office	❖ R 477 billion	❖ R 607 billion
Number of Members	9 271 000	9 342 000
❖ Privately administered and underwritten funds	❖ 7.7 million	❖ 7.6 million
❖ Transnet, Telkom and Post Office	❖ 1.6 million	❖ 1.7 million
Table 1 Source: Financial Services Board (2008)		

¹⁰ The FSB only has remit over retirement funds that are supervised under the Pension Funds Act, i.e. privately administered funds, underwritten funds and foreign funds. Retirement funds not supervised under the Act include official funds (Government Employees Pension Fund, Temporary Employees Pension Fund, Associated Institutions Pension Fund and Associated Institutions Provident Fund), Transnet Funds, Telkom Pension Fund, Post Office Pension Fund and Bargaining Council Funds.

¹¹ At the time of writing, the latest available financial statements from the FSB are as at 31 December 2006.

Privately administered, underwritten and parastatal (Transnet, Telkom and the Post Office) retirement funds service 9.3 million members and have net assets of R 1.45 trillion¹². (See Table 1)

As at 31 March 2008¹³, GEPF, South Africa's largest retirement fund, catered to 1.4 million members¹⁴, with net assets of R 707 billion. (See Table 2)

GOVERNMENT EMPLOYEES PENSION FUND (GEPF)		
	31 March 2007	31 March 2008
Net Assets	R 658.8 billion	R 707 billion
Table 2 Source: Government Employees Pension Fund (2007/8)		

Combining data from the FSB and GEPF (see Table 3), the size of the South African retirement fund industry is therefore estimated to be in the region of R 2.2 trillion¹⁵, covering some 10.7 million contributors (see footnote 10 which explains that the true number of members is lower).

The retirement funds industry represents the majority of formally employed South Africans¹⁶ and a significant portion of the nation's savings. Consequently, it stands to reason that effective leveraging of this national asset to facilitate access to housing, a national imperative, could potentially yield a productive synthesis of common objectives.

¹² It is important here to point out that there may be an element of double counting as individuals could, for example, be contributing to an employer-based fund (privately administered), as well as towards a retirement insurance policy (underwritten fund). Rob Rusconi, a retirement industry specialist, indicates that published estimates of true member numbers range from as low as 5.5 million individuals but seldom higher than 7 million members.

¹³ Information on the Government Employees Pension Fund (GEPF) is not included in reports published by the Financial Services Board. At the time of writing, the latest available GEPF report is as at 31 March 2008.

¹⁴ GEPF has 1.1 million contributing members and 330 000 pension recipients.

¹⁵ In the absence of current data from the FSB, 2006 figures have been used as a proxy to combine with the more up-to-date information from GEPF to derive an industry estimate.

¹⁶ South Africa has 9 million formally employed people, of which 2 million earn less than R 1 000 per month. (Mail and Guardian Business, 7 November 2008)

SOUTH AFRICAN RETIREMENT FUND INDUSTRY	
Total Net Assets	R 2.2 trillion
Net Assets <ul style="list-style-type: none"> ❖ Privately administered and underwritten funds ❖ Transnet, Telkom and Post Office ❖ Government Employees Pension Fund 	<ul style="list-style-type: none"> ❖ R 846 billion ❖ R 607 billion ❖ R 707 billion
Total Number of Members	10.7 million
Net Assets <ul style="list-style-type: none"> ❖ Privately administered and underwritten funds ❖ Transnet, Telkom and Post Office ❖ Government Employees Pension Fund 	<ul style="list-style-type: none"> ❖ 7.60 million ❖ 1.78 million ❖ 1.40 million
Table 3 Source: Financial Services Board (2008) and GEPF (2008)	

3.2 Alternative Models of Pension Backed Housing Finance

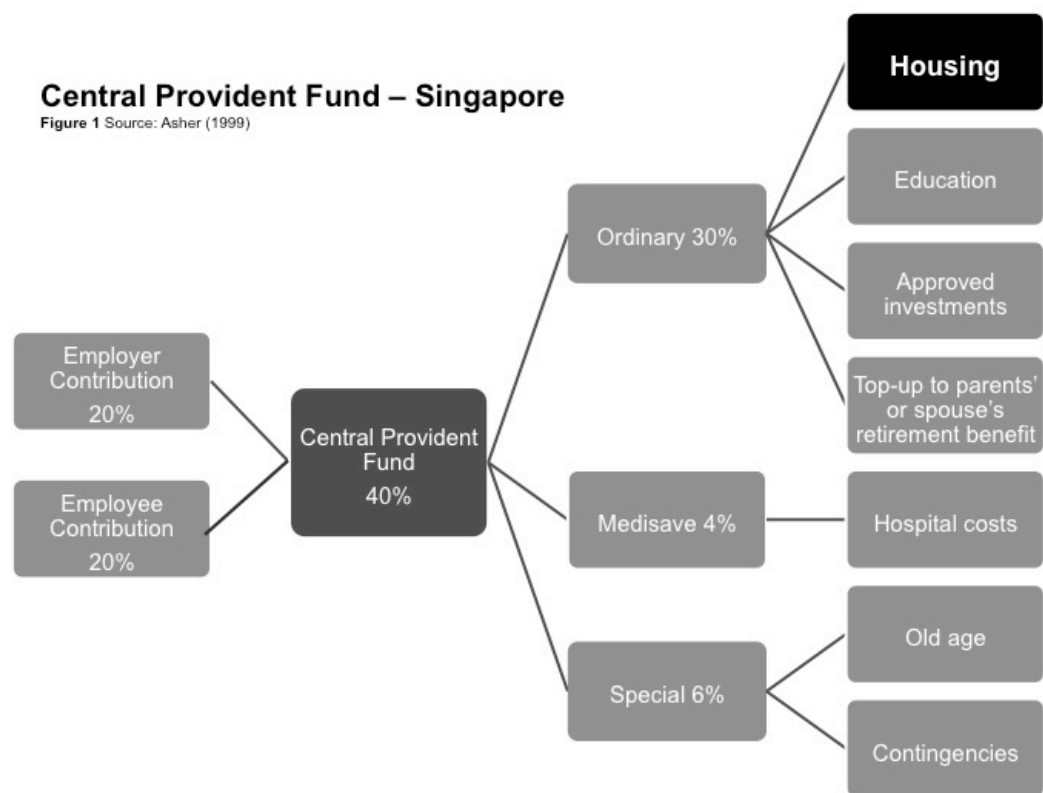
Mobilising retirement benefits to enable scheme members to attain and expand home ownership or to improve their housing conditions provides the means to accelerate an otherwise deferred retirement benefit to meet immediate housing needs. There are examples of countries that have introduced different models and several broad approaches can be identified:

- ❖ Where retirement funds choose to, or are compelled through legislation, to **invest a portion of the fund's asset portfolio in collective financing vehicles** that either finance residential property development or which offer scheme participants access to mortgage loans on favourable terms. – Since the 1980s, in the United States, a number of public pension funds have funded developers who construct homes at substantially reduced costs or who can offer lower income earners mortgage loans at subsidised interest rates. Some schemes have even participated in renovating old, abandoned houses, which are sold to members at below market prices (Chirchir, 2006).
- ❖ Where retirement funds choose to, or are compelled through legislation, to **invest in the direct construction of housing units, or to make loans directly available to their members**. – In Mexico, certain retirement funds earmark a larger relative portion of fund contributions as housing loans to members who fall below a specific income threshold. This policy achieves a level of cross-subsidisation between higher-salaried company executives and

regular fund members. - Mauritian schemes¹⁷ also offer below-market, fixed interest rates to its members. These types of funds, which deplete asset (cash) holdings to make direct loans to members, have become severely under-funded, as there are no limits to the amount of direct loans that the fund can make available (Chirchir, 2006).

- ❖ In Singapore, the State plays a pivotal role in managing a ***national retirement fund***¹⁸, allowing members to access accumulated benefits or even in some instances, to use future payment streams for specified purposes, i.e. housing, medical expenses and education.

Singapore's Central Provident Fund (CPF) was created in 1955, strictly as an instrument for old age savings. The model has since evolved into one that uses retirement benefits to cater to the nation's housing, education, medical and investment needs¹⁹.



¹⁷ The model adopted in Mauritius is an arrangement covering private retirement funds and the benefits are therefore, restricted to the members of the fund.

¹⁸ The Singaporean model bears further discussion, especially in light of recent policy discussions in South Africa where consideration is being given to the establishment of a national savings fund.

¹⁹ Industry commentators are of the opinion that non-formally or self-employed South Africans could be encouraged to contribute to a national, central retirement fund if the fund can offer them access to housing finance, healthcare benefits or education.

It is mandatory that employers and employees alike each contribute 20% of employees' income to CPF. The total contribution of 40%²⁰ is allocated, in turn, by CPF to "ordinary", "Medisave" and "special" accounts. The allocation is based on a ratio of 30%, 6% and 4%, respectively. Accumulated savings in the "ordinary" account can be used for housing, education, insurance premiums, approved investments and to top-up the member's parents or spouse's retirement savings. The "Medisave" portion can only be used for medical expenses, and the "special" account savings is set aside for old age or for specified contingencies. (McCarthy *et al*, 2001)

With home ownership in Singapore in excess of 90% (Singapore Department of Statistics, 2005), there is little doubt that the CPF programme has contributed to this laudable achievement. However, one of the drawbacks highlighted about the CPF scheme is that the physical withdrawal of member's accumulated savings from CPF to purchase a home has resulted in some 60% of Singaporeans not being able to replenish their old age savings by the time they reach retirement age (Chirchir, 2006).

3.3 **The Pension Funds Act (No. 24 of 1956)**

In South Africa, Section 19(5) of the Pension Funds Act (No. 24 of 1956), permits a retirement fund to grant a direct loan to its members or to furnish a guarantee for a member's loan from a third party (e.g. from a bank or another home loan provider). The loan must be used for the following housing-related purposes:

- To purchase a house;
- To buy land and to erect a dwelling on it²¹;
- To make additions or alterations to, or to maintain or repair an existing dwelling, or;
- To repay a third-party loan which is secured by mortgage bond over a property.

The maximum loan amount cannot exceed 90% of the fund member's accumulated retirement savings.²²

Financial assistance (in the form of a direct loan from the retirement fund or a guarantee to secure a third-party loan) is conditional on the property actually belonging to the member (or to his or her spouse) and the house being occupied by

²⁰ The percentage contribution has fluctuated quite widely over time to reflect the financial fortunes of Singaporeans. At inception in 1955, contributions were 10% and gradually increased to 50% by 1984. However, during the East Asian economic crisis in 1997, for example, the CPF contribution rate was reduced from 40% to 30%.

²¹ The escalating price of serviced land, and existing or new homes has put the prospect of first-time homeownership or property upgrading for poorer households out of reach. Section 5.6 "Hybrid Housing Loans" discusses in greater detail why, for most lower income earners, the pension-secured loan is generally not sufficiently large to purchase a house or land.

²² The Pensions Fund Act (No. 24 of 1956) specifies that "A loan...shall not exceed...90 per cent of the market value of the hypothecated property concerned...(or) the amount of the benefit which the member would receive if he were to terminate his membership of the fund voluntarily...whichever is the lesser amount." - This percentage can be increased to 100% if the employer provides an irrevocable guarantee for the difference (section 19, paragraph 5 (c) of the Pensions Fund Act No. 24 of 1956).

the member (or dependants of the member). The retirement fund cannot grant (or secure) a loan for more than one property²³. (Moodley-Isaacs, 2008)

The Financial Services Board, which is mandated to regulate retirement funds, has made it clear that there must be every intention to repay the pension-secured housing loan and that it should not be used as a means to accord members premature access to their retirement benefits. The intention should be to have reinstated the full value of benefits by the time the member retires.²⁴

3.4 **The South African Pension-Secured Loan Market**

There is little doubt that early access to accumulated retirement benefits is a viable means to facilitate access to housing. Quantification of the magnitude of the pension-secured lending industry would indicate to what extent and how many households have already, and would potentially, benefit from expanding access even further. However, it has proven difficult to ascertain the magnitude of the pension-secured lending industry as there is no standardised reporting to a central repository and some finance providers interviewed were reluctant to divulge details of their business for competitive reasons. Therefore, any attempt at gauging size of the pension-supported loan is based on a series of proxies gleaned from available information sources and on information that interviewees were comfortable to share.

The Financial Services Board indicated that, based on financial information to hand as at December 2005, that pension-secured loans granted by retirement funds directly to their members total some R 1.7 billion and third-party loan providers extend pension-secured loans of about R 3.7 billion²⁵. The total pension-secured lending industry is therefore estimated at R 5.4 billion.

In the absence of published figures, there seems to be uncertainty about the value of direct loans, with some industry players believing this figure to be closer to R 7 billion.

²³ As is often the case with regulation, whilst the underlying intent is admirable (in this instance to facilitate access to housing finance but to preclude members from speculative behaviour), there are unintended consequences. The "one property" restriction prevents retirement fund members from potentially amassing a property rental portfolio, which could substantially augment wealth and generate additional income.

²⁴ The FSB clearly states their position in regulatory guidelines (Circular PF No. 92, 1997) issued to the retirement fund industry. - "In terms of section 1 of the Act, the purpose of pension funds is to provide annuities or lump sum payments on retirement to members or to the dependants of members upon the death of members. Permitting housing loans was not intended to offer a means of reducing these benefits by allowing a set-off to take place. Accordingly there must be a real intention to repay a loan so as to reinstate the benefits to full value by the time they become payable on retirement of the members."

²⁵ This information was shared with the researcher during an interview with Mr. Jurgen Boyd, Deputy Executive Officer: Pensions, at the Financial Services Board on 7 October 2008. The figure of R 1.7 billion represents only direct loans granted by funds to its members and was gleaned from financial statements submitted by retirement funds as at December 2005. Pension-secured loans disbursed by third-party loan providers are estimated at R 3.7 billion. Retirement fund regulators do not monitor the value of pension-secured loans granted by third parties. Therefore, the true extent of retirement funds' contingent liabilities in respect of guarantees provided to collateralise members' loans from third parties is not known.

External (non-retirement fund) finance providers interviewed during this study estimate their industry to be in the order of between R 8 billion and R 10 billion in book value.

Using market share estimates embodied in a public submission by Alexander Forbes²⁶ and assuming market size to be in the region of R 10 billion, the size of larger pension-secured loan providers' operations has been approximated (Table 4).

THIRD-PARTY PENSION-SECURED LOAN PROVIDERS – MARKET SHARE ESTIMATES		
NON-RETIREMENT FUND LOAN PROVIDERS	ESTIMATED MARKET SHARE (%) (Alexander Forbes estimate)	ESTIMATED BOOK VALUE (assuming market size of R10 billion)
ABSA	10%	R 1 billion
FirstRand	16%	R 1.6 billion
Glenrand	4%	R 400 million
HomePlan²⁷ (Alexander Forbes)	20%	R 2 billion
NBC	13%	R 1.3 billion
Nedbank	4%	R 400 million
Standard Bank	30%	R 3 billion
Other	3%	R 300 million
TOTAL	100%	R 10 billion

Table 4 Source: Alexander Forbes estimate of market share and information from loan providers interviewed for this study (2008/2009)

In the absence of accurate financial information, the high-side, estimated magnitude of the pension-secured loan industry is in the region of R 17 billion (see Table 5).

²⁶ Market share estimates are based on information submitted by Alexander Forbes to the Competition Tribunal in the process of acquiring Absa's remaining stake in HomePlan (Pty) Ltd, the joint venture pension-secured loan business originally established by Alexander Forbes and Absa (SAFLII, 2008).

²⁷ Joint venture between Alexander Forbes (50%) and Absa Bank (50%). Alexander Forbes is in the process of acquiring Absa Bank's share of the pension-secured loan business. – Absa also has a proprietary in-house pension-secured loan unit. (See footnote 21)

This approximation incorporates all pension-secured loans extended to retirement fund members of all income bands²⁸.

PENSION-SECURED LENDING – ESTIMATED MARKET SIZE			
VALUE ESTIMATES	DIRECT LOANS	THIRD-PARTY LOANS	TOTAL ESTIMATED MARKET SIZE
High	R 7 billion	R 10 billion	R 17 billion
Low²⁹	R 1.7 billion	R 3.7 billion	R 5.4 billion

Table 5 Source: Sing (2009)

If it is assumed that the existing pension-secured lending market is valued at some R17 billion (based on the views of industry participants), then the market constitutes less than 1% of the total assets of R 2.2 trillion of the retirement fund industry.

Whilst there are inherent imbalances in the structure of retirement savings³⁰, it appears that a relatively miniscule number of contributors to retirement funds access pension-secured loans to finance their housing needs. This points to the significant potential to grow the pension-secured lending market.

It would be useful to profile fund members who do avail of pension-secured loans. Figure 2 compares the take-up of the different types of housing finance products, i.e. mortgage, pension-secured and unsecured loans. It appears that poorer households make less use of mortgage finance and more use of pension-secured or unsecured loans. This can be attributed to the fact that lower income households generally cannot afford repayments on the larger mortgage loan but can afford to take up the smaller pension-secured loan (or unsecured loan) to finance their housing requirements.

The higher incidence of pension-secured loans in the lower income market could also be an indication of there being lower qualifying criteria to access the loan. For example, with a mortgage loan, the lender has to be satisfied with the location of the property and its market value, as well as the borrower's ability to repay the loan. Whereas with a pension-secured loan, once confirmation is obtained that the

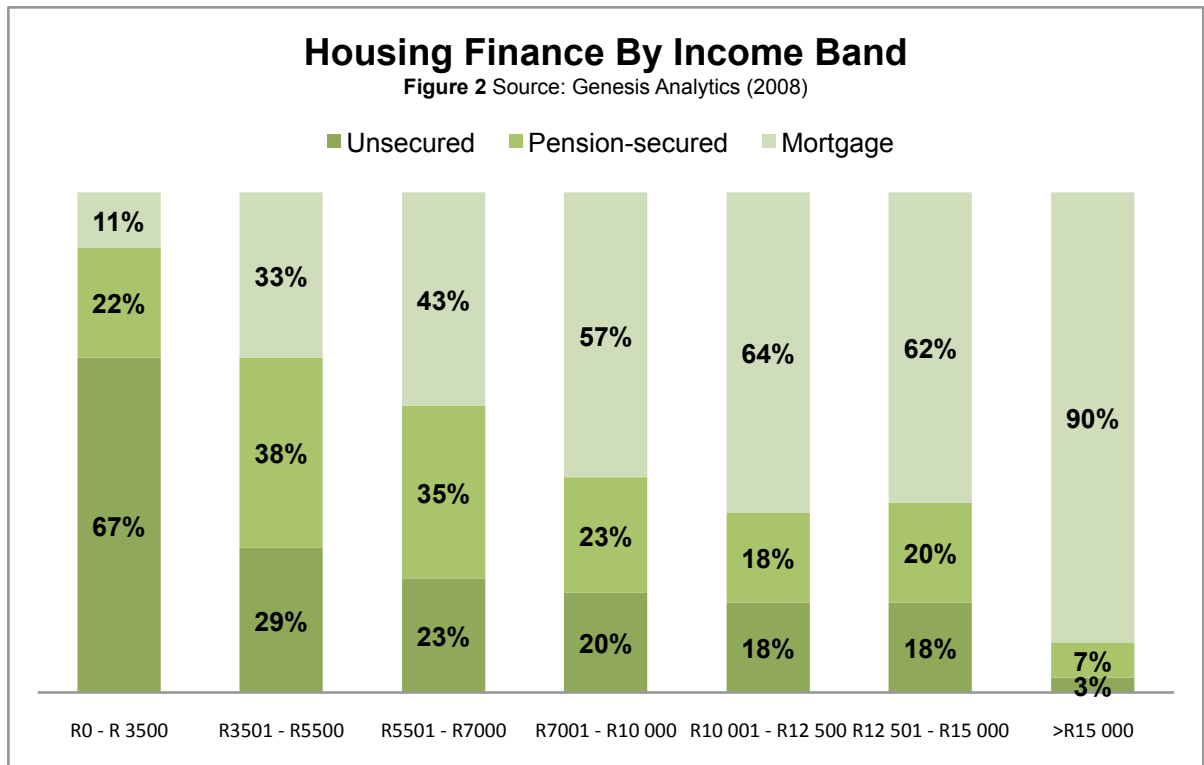
²⁸ Loan providers have indicated that, though the exception, pension-secured loans have also been extended to higher income individuals. Therefore, the pension-secured loan product should not be viewed as only catering to lower income individuals.

²⁹ This Financial Services Board estimate is based on the 2005 financial statements of retirement funds.

³⁰ Having said this, it must be borne in mind that South African's *apartheid* past has resulted in fundamental skews in asset accumulation. Historic income inequality and restricted access to investment vehicles (e.g. home ownership) significantly limited black South Africans' retirement savings. Therefore, a significant portion of the total value of retirement savings tends to be found in the hands of relatively few individuals.

borrower's retirement savings exist and can afford repayments, there is little focus on the value of the property or its potential to appreciate in value.

Banking Association has indicated that they intend seeking approval to align the upper income limit of the FSC market with government's definition of the "inclusionary housing"³¹ market. The upper income limit of this market is R 15 142 per month. According to Figure 2, this would position the pension-secured loan squarely as a product targeted at the FSC market.



³¹ There is no commonly accepted definition of the "inclusionary housing" market. It generally refers to those households who do not qualify for fully subsidised housing (i.e. households earning more than income ceiling of R 3 500 per month) but who also do not earn sufficient income to be able to afford the finance to purchase an entry-level house.

3.5 **Financial Sector Charter Context – Market Potential**

Over the last five years, the Financial Sector Charter³² commitments in respect of expanding access to loan finance to more South Africans, has contributed to a growth in credit extension in the lower income market and more specifically, has had a significant catalysing affect on the housing sector. The Banking Association South Africa reports that (unaudited) figures indicate that since January 2004, their members collectively extended some R 44.8 billion in housing finance to low income earners as at 31 December 2008.

Of the R44.8 billion in housing finance extended to the FSC market by the originating banks (i.e. Absa, FNB, Nedbank and Standard Bank), R36.9 billion (i.e. 82%) of the financing was made directly to the consumer in the form of mortgage bonds, pension-secured loans and unsecured personal loans. Financing of R 8.0 billion (i.e. 18%) was provided to residential property developers and wholesale loan providers. (See Table 6)

A total of 984 730 housing-related loans were disbursed in the same 60-month period (see Table 7). Of the 984 730 housing loans extended to the FSC market, 807 935 loans (i.e. 82%) were made by the originating banks (i.e. Absa, FNB, Nedbank and Standard Bank) directly to the consumer in the form of mortgage bonds, pension-secured loans and unsecured personal loans. The remaining 176 795 loans (i.e. 18%) were loans made to residential property developers to finance affordable housing developments or other loan providers who on-lend to the FSC market.

In the last 5 years, 257 345 pension-secured loans have been extended to the Charter market, valued at R 4.836 billion, i.e. 26% of the total Charter achievement by number of loans disbursed and 11% by value.

³² The Financial Sector Charter (FSC) is a voluntary commitment made by representative organisations operating in the financial services sector, with the intention of achieving Black Economic Empowerment (BEE) objectives. The Charter was signed in October 2003 and incorporated obligations related to ownership and control of businesses, organisational transformation, extending access to financial services to lower income groups, augmenting empowerment financing, focused on enterprise development and enhanced corporate social responsibility. The Charter measurement period commenced on 1 January 2004 and runs until 31 December 2014. The first, five-year measurement period ran from 1 January 2004 to 31 December 2008.

FINANCIAL SECTOR CHARTER – HOUSING FINANCE EXTENSION

VALUE OF HOUSING FINANCE (R m)

(Unaudited figures as at 31 December 2009)

	Mortgage	Pension secured	Unsecured	Residential Development	Wholesale & Social	TOTAL (R m)
2004	7 262	1 013	338	131	658	9 402
2005	6 045	1 083	552	573	828	9 080
2006	6 319	1 181	216	997	1 016	9 729
2007	5 775	795	1 221	1 254	906	9 951
2008	2 946	764	1 341	1 354	260	6 665
TOTAL	28 346	4 836	3 668	4 309	3 668	44 828

Table 6 Source: Banking Association South Africa, March 2009

During 2007, required compliance with the National Credit Act³³ from 1st June, coupled with a growing degree of saturation of previously under-served Charter markets, had a dampening effect on participating banks' performance³⁴. By the end of 2008, the banks breached the R 42 billion housing finance target³⁵. However, the

³³ The primary objective of the National Credit Act (NCA) is to protect consumers' interests from unscrupulous lenders. It places greater accountability on lenders to ensure that their lending practices are not reckless and protects the consumer from overindebtedness. To ensure compliance with legislation, lenders introduced additional checks and balances, e.g. income and expenditure analyses, self-certification of affordability, more comprehensive verification of information. This resulted in increased administration and labour intensive procedures that significantly increased the time taken to process loans. In some instances lenders imposed more stringent affordability criteria on borrowers. The overall impact of the NCA was to reduce the number of successful loan applications. – Loan providers indicated that the initial impact of NCA was to reduce loan volumes by 30% to 40%. However, it is difficult to accurately determine whether the reduced volumes were a result of administrative burden or systems problems, or if they were directly linked to affordability issues.

³⁴ With the commencement of the FSC, originating banks invested aggressively in resources and significantly heightened focus on the lower income market. Through 2004 to mid-2007, this resulted in historically pent up demand for housing finance being satisfied through a frenzy of marketing initiatives, amply bolstered by a generally booming property sector. Towards the end of 2007, however, the effects of the subprime crisis and the shortage of housing stock finally began to take effect, and the sector's performance was only salvaged by a few, exceptional property finance transactions. The apparent spike in unsecured housing loans is mainly due to previously unavailable data being included in the report, following upgrades to banks' measurement systems, rather than an actual increase in the number of loans granted.

³⁵ In terms of the FSC, the financial services sector has, in fact, two separate (but interlinked) targets it has to achieve with respect to housing finance. (i) An **origination** target of R 42 billion, which represents the total value of all housing finance loans disbursed; and (ii) a **targeted investment** target of R32 billion, which represents the growth in the net book value of housing finance during the measurement period.

value of mortgage loans and pension-secured loans originated fell by almost a third. This decrease can be attributed to liquidity constraints and tightening credit extension in the face of the global economic turmoil, further saturation of existing affordable housing markets and delays in new residential housing developments coming on stream (thus further exacerbating the housing stock shortage).

FINANCIAL SECTOR CHARTER – HOUSING FINANCE EXTENSION						
NUMBER OF HOUSING LOANS						
(Unaudited figures as at 31 December 2009)						
	Mortgage	Pension secured	Unsecured	Residential Development	Wholesale & Social	TOTAL
2004	57 324	56 106	40 660	2	35 124	189 216
2005	53 159	58 787	51 720	39	45 974	209 679
2006	43 721	59 635	30 736	166	53 677	187 935
2007	55 287	38 212	94 265	88	33 023	220 875
2008	25 147	44 605	98 571	107	8 596	177 025
TOTAL	234 638	257 345	315 952	402	176 393	984 730

Table 7 Source: Banking Association South Africa, March 2009

Worldwide recessionary conditions and continued housing stock shortages will undoubtedly constrain banks' Charter achievements over the next five-year measurement period (from 2009 to 2014). Pending the outcome of the housing demand and supply research presently underway³⁶, which will reveal the size of the FSC market still requiring housing finance, the Charter signatories will be negotiating new housing finance targets to 2014. It, therefore, remains to be seen what the magnitude of the pension-secured loan component of this target will be.

The exercise to estimate potential market growth in pension-secured lending is based on a series of "informed extrapolations" flowing from three different sources. These include:

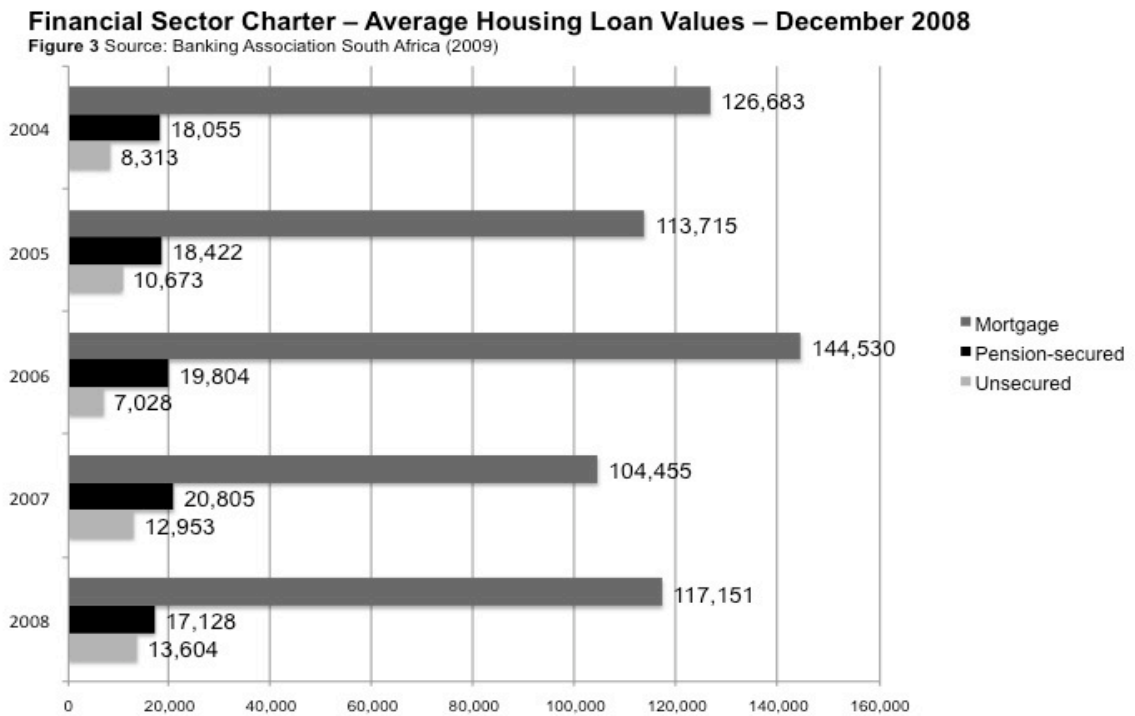
- i. Banking Association South Africa provides a banking industry view from a demand-side perspective, taking into account the existing demand for housing and translating the information into the eventual contribution to the achievement of Financial Sector Charter commitments.

³⁶ Housing demand and supply research has been commissioned by the Banking Association South Africa. (See footnote 3)

- ii. Independent research by Eighty20 (2009) is based on South African household census and demographic data.
- iii. Loan providers estimating short-term market growth potential based on a “scheme penetration factor”.

A Demand-side Estimate (Banking Association South Africa, 2008)

Banking Association South Africa has collated data up to December 2008, which reveals the average size of consumer housing loans originated by banks over a 60-month period (Figure 3).



The average value of mortgage loans is R 121 000, whilst the average value of pension-secured loans is in the region of R 19 000³⁷ and that of unsecured housing loans is R 10 500 (Table 8).

The lower average values of pension-secured and unsecured loans point to them being more appropriate to finance home improvements or to effect extensions to an existing dwelling. With pension-secured finance of R 19 000, there is little likelihood that fund members would be able to purchase a house.

³⁷ Non-bank loan providers interviewed for this report advise that during 2008 and 2009, the average pension-secured loan amount has risen to between R 35 000 and R 40 000.

AVERAGE HOUSING LOAN VALUES OVER A 5-YEAR PERIOD TO DECEMBER 2008

TYPE OF HOUSING FINANCE	AVERAGE LOAN AMOUNT
Mortgage Loans	R 121 000
Pension-Secured Loans	R 19 000
Unsecured Housing Loans	R 10 500

Table 8 Source: Banking Association South Africa, March 2009

Using the assumption that pension-secured and unsecured loans are more suitable to effect enhancements to an existing property, Banking Association South Africa has estimated the potential demand for home improvement finance.

Figure 4 follows the rationale for the projected growth potential in pension-secured loans.

Pension-Secured Loans – Market Potential

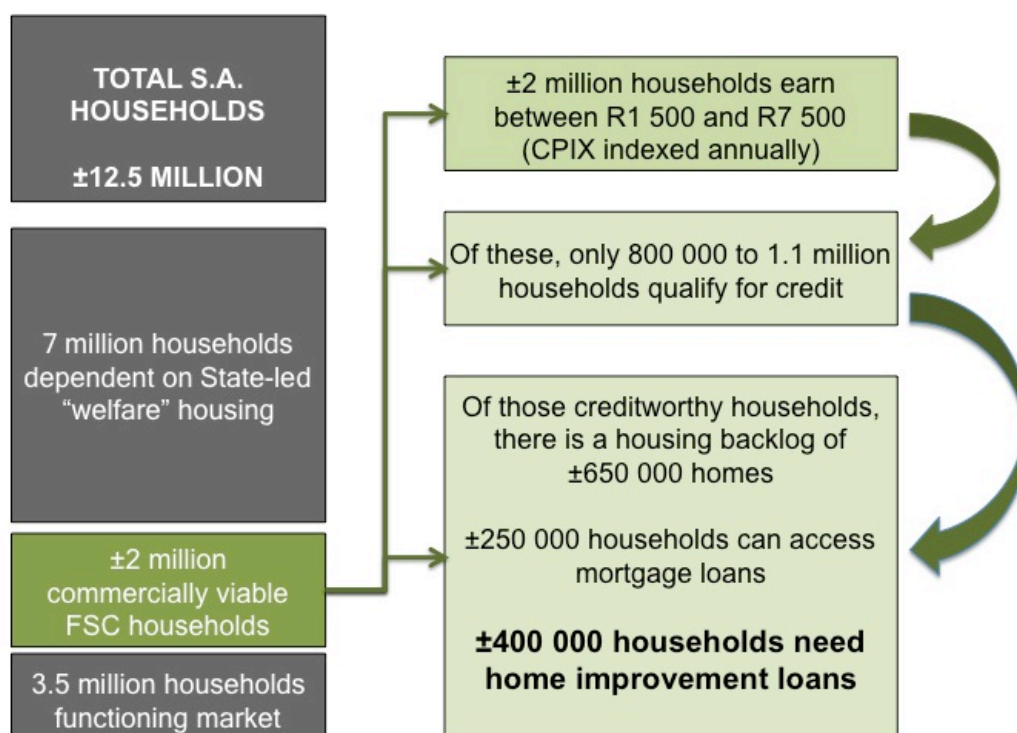


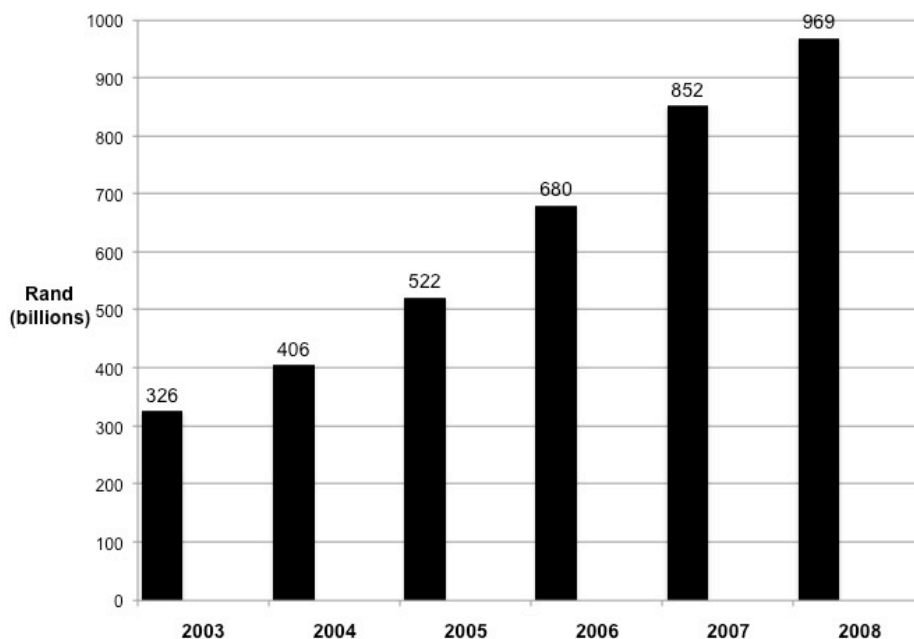
Figure 4 Courtesy of Banking Association South Africa estimates

Of the approximately 12.5 million households in South Africa, it is estimated that some 3.5 million households can access housing finance (or have already done so) with relative ease and are being serviced by the existing mortgage loan market.

The South African mortgage advances market was valued at R 969 billion as at December 2008 (Figure 5). Between 2003 and 2007, the mortgage market had been growing at an average rate of 27% per annum. During 2008, the rate of growth almost halved to 14% compared to the preceding five years, an indication of the massive global economic contraction.

Total South African Mortgage Advances – 2003 to 2008

Figure 5 Source: South African Reserve Bank Quarterly Bulletin, March 2009



Another 7 million households³⁸ would be reliant on the State to provide some form of subsidised housing and/or cannot afford housing finance. These households are potential recipients of fully-subsidised homes or beneficiaries of monetary subsidies³⁹.

The remaining 2 million households that fall within the ambit of the Financial Sector Charter definition⁴⁰ are described as “commercially viable” as these house are able to afford housing finance. Within this category, however, are “dysfunctional”

³⁸ The 7 million households requiring State housing assistance include (i) households that fall below the minimum income threshold of the FSC, i.e. households earning less than R 1 500 per month; (ii) as well as households which do fall within the FSC target market (i.e. households earning between R 1 500 and R 7 500 per month) but who nevertheless earn too little to afford housing finance.

³⁹ The South African government provides various housing subsidies for individual households. (i) People earning less than R 3 500 per month are eligible for a “fully subsidised” house (previously known as a “RDP house”). Subsidy beneficiaries receive ownership of a serviced site (approximately 250m²) and a top structure (minimum size of 45m²). Industry experts value the fully subsidised unit at R 110 000 (with serviced site valued at R 70 000 and the house at R 40 000). (ii) First-time homebuyers earning between R 3 501 and R 7 000 per month are eligible for a cash subsidy in terms of the Finance Linked Individual Subsidy Programme (FLISP). The intention of FLISP is that the state subsidy should be linked with a loan from a financial institution to purchase a house. FLISP works on a sliding scale with higher income beneficiaries receiving less of a cash benefit than lower income families.

⁴⁰ The definition of FSC qualifying households is the base income band of R 1 500 to R 7 500 per month. In practice, this base income band should be escalated annually by CPIX to determine the qualifying FSC income band for a particular year. – For the sake of simplicity and for the purposes of this high-level illustration, the FSC base income was not been adjusted by CPIX.

households that may experience impediments to access housing finance due to, for example, a poor credit history or a lack of savings to contribute to a deposit. These impediments approximately halve the number of households that would qualify for credit or who would meet the affordability criteria. This leaves between 800 000 and 1 000 000 households.

Using the 2005 research on effective demand, the Banking Association further deduces that of the housing backlog, only 40% of housing finance will be required to purchase existing or newly-built properties. This estimate is somewhat optimistic given the current shortage of affordable housing stock. Nevertheless, this leaves in the region of 60% of households requiring home improvement loans, i.e. a market potential of 400 000 pension-secured or unsecured housing loans.

Some of the prospective borrowers will not be able to access pension-secured loans because they:

- Do not belong to a retirement fund, or;
- Belong to a retirement fund that has not negotiated a pension-secured lending facility, or;
- Do not qualify in terms of affordability.

Therefore, if it is assumed that only half of the projected home improvement loans would be funded via a pension-secured loan vehicle, i.e. 200 000 loans, and that the average loan size is in the region of R 20 000, then a high-level estimate of market potential for pension-secured loans is **R 4 billion**⁴¹.

A Macro View (Eighty20, 2009)

Recent research undertaken by Eighty20 (2009b) adopts a macro-environmental view of the pension-secured market using various data sources⁴².

It found that the lower the household income, the less the likelihood that the household contributed to a pension or provident fund (see Figure 6). Only 15% of households earning between R 1 600 and R 3 500 per month contribute to a retirement fund, whereas 48% of households earning between R 5 000 and R 8 200 belong to a retirement fund.

⁴¹ Banking Association South Africa-based estimate of the value of the pension-secured loan market → 200 000 x R 20 000 = R 4 billion

⁴² Using principally the 2007 Finscope™ survey and the 2005/2006 Income and Expenditure Survey (IES), which was conducted by Statistics South Africa. The IES survey sample consists of 21 000 households countrywide.

Retirement Fund Membership

Figure 6 Source: Eighty20, 2009b



There is a degree of irony in this. It has been shown that pension-secured loans are utilised predominantly by lower income groups (see Figure 2). However, if a significant number of lower income earners do not contribute to a retirement fund, then they will be unable to access pension-secured loans. Allowing non-formally employed or self-employed individuals to contribute to a retirement fund (for example, a national savings programme) could significantly expand access to housing finance to more South Africans.

The Eighty20 (2009a) report found that of the estimated 5.2 million FSC households:

- 451 000 households were “too poor”⁴³ to afford housing finance.
- 3.4 million households do not contribute towards formal retirement savings and would therefore not have access to pension-secured loans.
- 200 000 households already had pension-secured finance.

⁴³ Using Finscope (2007) and IES (2005/6) data, Eighty20’s (2009) research defined households as being “too poor” when respondents indicated that they (i) often go without cash income; (ii) sometimes or often go without enough food to eat; (iii) often go without medicine or medical treatment.

A MACRO VIEW – ESTIMATING MARKET POTENTIAL		
Total FSC households		5.182 million
Less: "Too poor" to afford housing finance	451 000	
Less: Do not contribute to retirement fund	3.402 million	
Less: Already have pension-secured loan	200 000	4.053 million
Sub-total		1.129 million
Less: National Credit Act (NCA) restrictions		216 000
Potential market for pension-secured loans		913 000*
Are able to access pension-secured loans and who own homes		283 000
Qualify for pension-secured loans and live in informal dwelling		157 000
Qualify for pension-secured loans but do not own dwelling		471 000
Estimated Market Growth Potential = Potential Households x Average Loan Amount		
Estimated Market Growth Potential = 911 000* x R 20 000		
Estimated Market Growth Potential = R 18 billion		
Figure 7 Source: Eighty20, March 2009a		
*Discrepancy in values due to rounding		

Excluding the households that cannot access pension-secured loans (i.e. those who are "too poor" and those who do not contribute to a retirement fund) and households that already have a pension-secured loan, some 1.13 million households can access pension-supported housing finance (Figure 7).

The introduction of the National Credit Act, however, further reduced the number of people who can access housing finance as they would not meet the more stringent affordability criteria. Eighty20 (2009) estimates that 216 000 households would be disqualified from accessing pension-secured loans on these grounds.

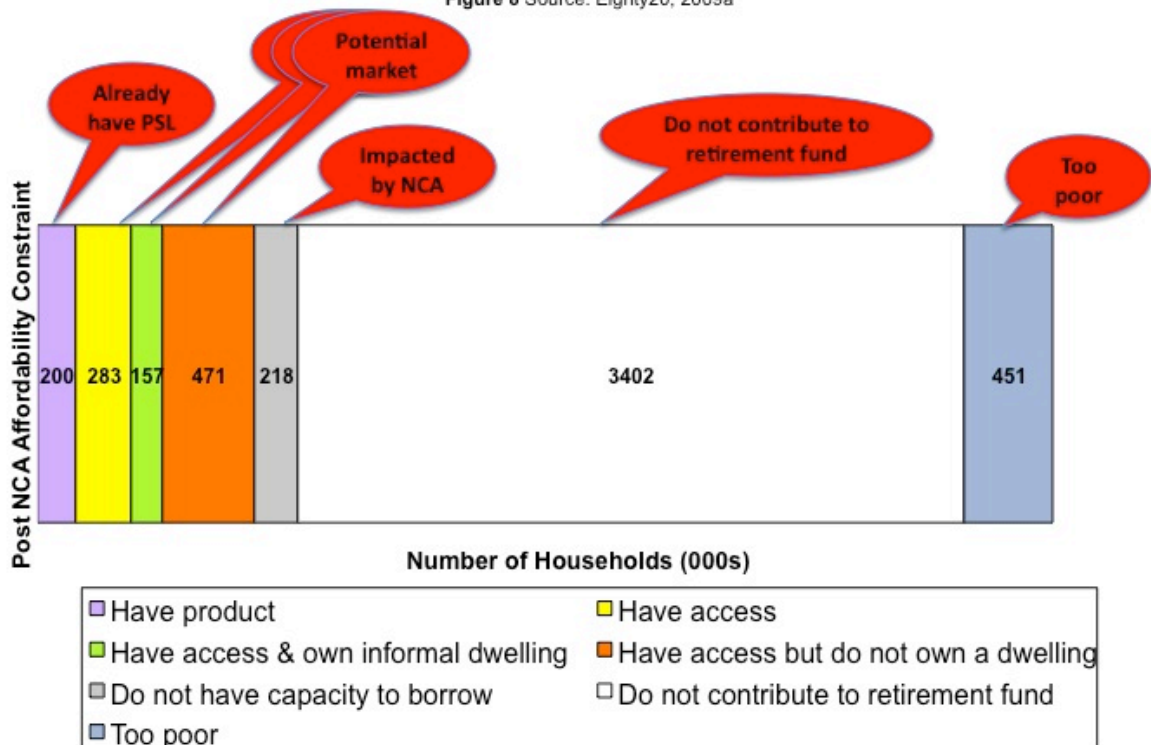
This leaves a potential market for pension-secured loans of 911 000 households. At an average loan amount of R 20 000, the estimated market growth potential is **R 18 million**.

Figure 8 graphically illustrates the potential market, which comprises the following sub-segments:

- i. 283 000 households who would be able to access pension-secured loans and who own homes.
- ii. 157 000 households who would qualify for pension-secured loans and who are presently living in an informal dwelling.
- iii. 471 000 households who would qualify for pension-secured loans but who do not currently own a dwelling.

Pension-secured Loans – Estimated Market Size

Figure 8 Source: Eighty20, 2009a



It was noted in the research that the 471 000 households who do not own their own homes have no use for a pension-secured loan and therefore, should be excluded from the calculation. Whilst this is a valid observation, there could be instances where loans could be used to build structures onto rented property or to build a home on land over which the fund member has no legal title (for example, in an informal settlement).

If these households are indeed excluded, then the estimated market potential is halved to **R 9 billion**.

Eighty20 (2009b) suggests other reasons that may further reduce the number of households who use pension-secured loans.

- Survey data may understate household indebtedness. Many households may, therefore, be unable to absorb additional credit.
- The overall low levels of awareness about credit products would similarly hold true for pension-secured loans, resulting in lower usage.
- Loan providers may be reluctant to extend finance due to expected job losses and to funding constraints.
- The historic origination of pension-secured loans by banks is relatively low compared to market potential. Based on these trends Eighty20 (2009b) estimates an annual origination amount of R 400 million.

An Industry Perspective

Loan providers interviewed for this study venture, in their opinion, a more practical method for quantifying the potential market opportunity for pension-secured loans. They suggest a “scheme penetration factor”. Loan providers advise that the take-up of pension-secured loans by fund members per scheme currently ranges between 10% and 15%⁴⁴.

The reasons given for the low levels of “scheme penetration” are that:

- There is a low level of product awareness amongst fund members.
- For the majority of loan providers the pension-secured lending business is not a core activity. For banks, the pension-secured loan is but one of a large range of loan products and a negligible portion of the banks advances. Pension-secured loans constitute, for example, 0.5% of Standard Bank’s total loans and advances to customers⁴⁵. For the larger non-bank loan providers, pension-secured lending is also not a core business. For example pension-secured loans constitute 0.5% of Alexander Forbes’ total asset base⁴⁶. NBC is primarily an employee benefits company focusing on administration, consulting, actuarial and investment consulting services (listing home loans as their second to last offering on their website). Even with a collective market share of 63% between them (Alexander Forbes, NBC and Standard Bank), the pension-secured loan business nevertheless constitutes only a relatively small component of these organisations’ overall operations. Therefore, it comes as no surprise that fewer resources (management focus, capital, people, marketing spend) are dedicated to the pension-secured lending businesses, ultimately contributing to low consumer awareness about the product and therefore, low take-up.

Participants in the pension-secured loans business are acutely aware that if they actively tried to increase the number of loans sold to members, whose funds already have pension-secured loan facilities in place, origination could increase significantly with relatively little marketing or sales effort.

Loan providers envisage that “scheme penetration” could be increased by at least 20% in the short-term. Based on an estimated market size of R 17 billion (Table 5), another **R3.4 billion** of pension-secured loans could be originated.

In summary, it would seem that, over the next five-year, Financial Sector Charter measurement period, loan origination in the region of R 2 billion to R 4 billion is eminently achievable.

⁴⁴ Say, a retirement fund has 10 000 members. Its board of trustees approves a pension-secured loan scheme with a loan provider. Lenders indicate that only between 1 000 and 1 500 members actually take up a loan, i.e. “scheme penetration” is between 10% and 15%.

⁴⁵ As at 31 December 2008, Standard Bank’s total “loan and advances to customers” stood at R 658 billion, compared to the pension-secured lending book which is estimated to be in the region of R 3 billion (see Table 4).

⁴⁶ Alexander Forbes’ financial statements as at 31 March 2008 report R 750 million of “housing loans secured by retirement fund assets” compared with “financial assets held under multi-manager investment contracts” of R 143.5 billion (the company’s core business) and “total assets” of R 165.7 billion.

4. THE PENSION-SECURED LENDING VALUE CHAIN

There is a misapprehension that the disbursement of the pension-secured loan to the borrower constitutes a significant portion of the pension-secured loan value chain. In fact, the lengthy supply-side of the value chain makes up for the bulk of the process and poses the principal challenges (and costs) inherent in the present environment.

In trying to appreciate the complexity and seeming inefficiencies in the value chain, this section of the study will:

- Provide a brief overview of the pension-secured lending value chain.
- Describe the roles and responsibilities of the supply-side participants in greater detail.

The rationale for focusing on the supply-side dynamics is to achieve a more consumer-centric approach to the delivery of pension-secured loans.

4.1 Overview of the Process

Pension-backed loan schemes generally follow one of two financing models:

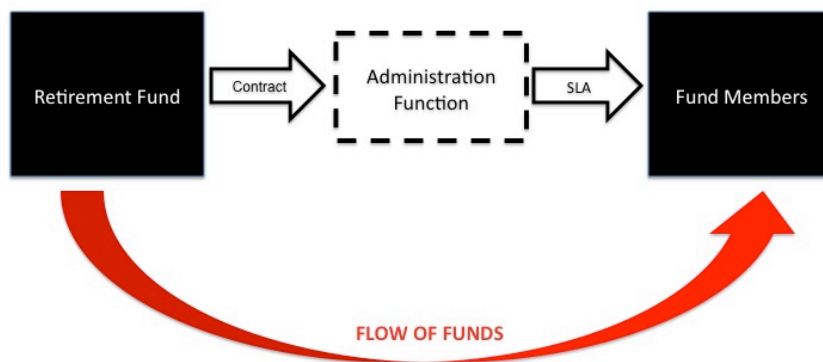
- Direct loans* to members financed by the retirement fund itself. Financing for the loans comes directly from the fund's coffers and represents an opportunity cost to the fund, i.e. the cost of not investing members' savings in some other wealth-generating vehicle. (Figure 9)

±30% of all pension-secured loans are direct loans from the retirement fund.

Trustees can choose to provide loan administration, fulfilment and management functions internally or to outsource the process to a third party.

PENSION-SECURED LENDING – DIRECT LOANS

Figure 9 Source: Sing (2009)



- Third-party loan providers* include commercial banks and other non-bank financial institutions. Trustees appoint the lender and negotiate the scheme

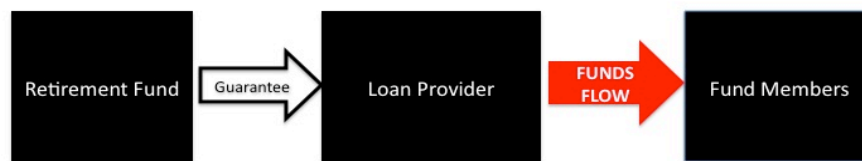
arrangements (for example, interest rates, loan terms and conditions, loan fulfilment process). Funding for the pension-secured loans is furnished by the loan provider. Retirement fund assets remain intact. (Figure 10)

±70% of all pension-secured loans are from third-party loan providers.

Lenders are responsible for all loan administration, fulfilment and management functions.

PENSION-SECURED LENDING – THIRD-PARTY LOAN PROVIDER

Figure 10 Source: Sing (2009)



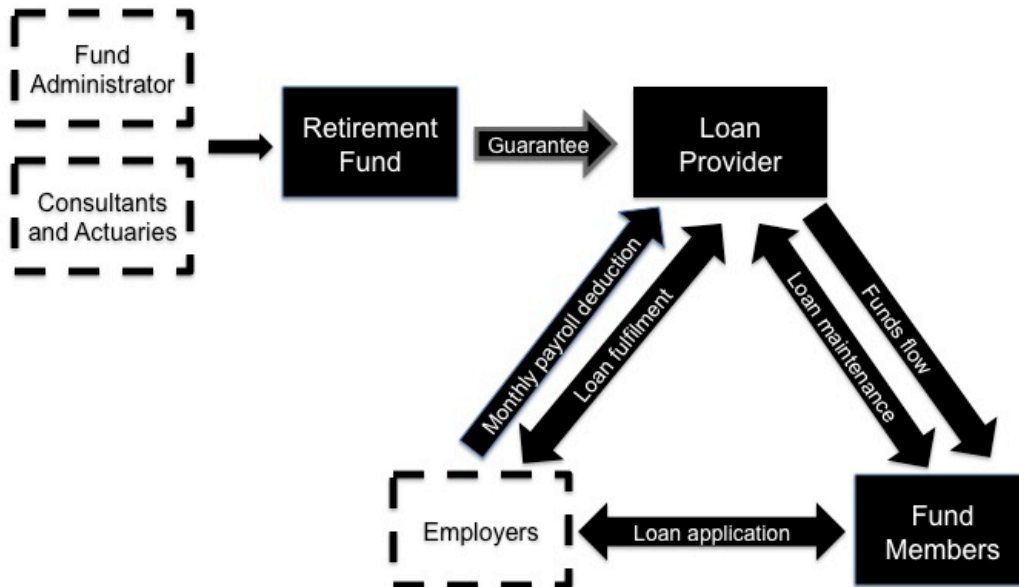
The advantages of funds appointing a third-party loan provider over offering loans to members directly are:

- Funding for loans is furnished by the loan provider. This allows trustees to invest fund assets in the most appropriate investment vehicles that generate market-related returns for their members.
- Trustees do not have to be concerned about eroding fund assets (and investment returns) in order to finance the loan book. There are examples of loan books being allowed to grow so large that fund assets have been diverted to finance the book instead of being directed towards generating long-term investment returns.
- Trustees are able to ring-fence the depletion of members' retirement savings at individual member level in the event of members defaulting on their loans. The entire fund does not have to carry the cost of bad debts (as it would have to do if direct loans were given). The risk of bad debts lies with the loan provider.
- Fund trustees do not have to concern themselves with operating a loans business, supporting infrastructure costs and developing core competencies in lending. The advent of the National Credit Act further burdened funds offered direct loans with increased compliance requirements.

For the purposes of illustration, the pension-secured loan value chain is described assuming that a third-party loan provider has been appointed. Figure 11 is a diagrammatic representation of the process.

SUPPLY-SIDE PARTICIPANTS (THIRD-PARTY LOAN PROVIDER)

Figure 11 Source: Sing (2009)



- The board of trustees of a retirement fund (sometimes with the advice and assistance of the fund administrator or specialist consultant) appoints a loan provider.
- The trustees (on behalf of the fund) provide a guarantee undertaking to the loan provider to repay the member's loan in the event of default.
- Fund members (employees) approach their employers to apply for a pension-secured loan.
- The employer submits the loan application to the loan provider.
- Once the loan is approved, the loan provider pays out the loan proceeds to the fund member.
- The employer effects monthly deductions from the fund member's salary to repay the loan.

4.2 Supply-Side Participants – Roles and Responsibilities

This section describes the roles and responsibilities of the supply-side participants in greater detail.

Retirement Fund Trustees

Retirement funds are managed by a board of trustees on behalf of the fund members. With respect to pension-backed loan schemes, the board of trustees is ultimately responsible for:

- Making the decision to afford their members access to housing finance, using their accumulated retirement savings to guarantee the loan, i.e. deciding to introduce a pension-backed loan facility for members.
- Trustees can opt to either provide loans directly to their fund members using the fund's resources or outsource the scheme to an external loan provider.
- Evaluating and selecting providers of finance, i.e. negotiating the best housing finance deal on behalf of the fund members. Depending on factors such as size of the membership base and estimated growth in the loan book, trustees should be negotiating competitive pricing, and loan terms with third party loan providers. Trustee boards should also consider negotiating attractive associated financial services packages with loan providers. For example, lower premiums for credit life insurance, preferential transactional banking rates, loyalty benefits for members, reduced fund administration fees.
- Determining what percentage of a member's accumulated retirement savings can be used to guarantee a housing loan. – Regulation stipulates that no more than 90% of a member's accumulated retirement savings (at current market values) can be put up as collateral. A fund's board of trustees is mandated to resolve the maximum amount that can be borrowed by the member.

In practice, loan providers indicate that maxima range between 60% and 80%. According to trustees interviewed for this study, a major determinant of the maximum loan amount is to protect members' interests by limiting the percentage of retirement savings "potentially at risk". It appears, however, that this determination is based more on intuition than on data modelling or on actual default experience in most instances.

- Ensuring that the contracts, service level agreements and processing capabilities are in place to operate the loan programme (or that these functions are being provided by third parties).
- Communicating the details of the pension-secured loan scheme to members.
- Ensuring that the pension-backed loan proceeds are, in fact, applied for housing purposes as required in terms of the Pension Funds Act. Accountability for this regulatory requirement falls squarely on the shoulders of the board of trustees. – In discussions with regulators, it would appear that no change to this fiduciary responsibility of the trustees is envisaged in the near future.
- Providing and honouring guarantees to external loan providers on behalf of members who have taken up pension-secured loans.

Fund Administrators

Retirement fund administrators are generally external suppliers that support the board of trustees in the day-to-day administration and management of the retirement fund.

- On being advised that the fund member has applied for a pension-supported loan, the fund administrator's role is to verify that the retirement fund member

has sufficient retirement savings to guarantee the loan amount that has been requested.

- The fund administrator is also responsible for “flagging” the member’s retirement savings account. Once the pension-supported loan is granted and the necessary approvals obtained, the loan provider requests the administrator to “flag” the member’s record to indicate that the retirement savings have been earmarked to secure the pension-supported loan.
- Should the member leave his/her employment before the pension-supported loan is repaid, the administrator should ensure that the outstanding loan amount is deducted from the member’s retirement savings and paid to the loan provider, prior to the accrued benefit being paid out.
- In some instances, where the fund administrator has an in-depth knowledge of the pension-backed lending industry through close associations with potential loan providers, the administrator has been known to provide advice to the trustees to assist in their selection of a loan provider.

Consultants and actuaries

These are specialist advisors⁴⁷ who advise the fund trustees on investment strategies and operational direction. This guidance, sometimes, extends to assisting the board of trustees with the identification, evaluation and selection of the loan provider.

Employers

- Depending on whether companies have established their own retirement fund for their employees or if they participate in an umbrella fund⁴⁸, employer representatives on the board of trustees or trustees selected to represent the umbrella fund, are involved with the selection of the loan provider and with the structuring of the pension-backed loan scheme.
- Once the pension-backed loan scheme is in place, the participating employers’ role is to inform the fund member (employee) about the availability of the housing loan facility. Employers assume the role of interfacing with employees about the pension-secured loan facility on behalf of the retirement fund trustees as they are often the most convenient point of contact. However, the employer is often also keen to position the pension-secured

⁴⁷ Specialist advisors are either smaller independent service providers or, as is more often the case, closely affiliated to larger players in the retirement fund industry. These larger groups offer the full gamut of services to retirement funds, ranging from the provision of advisory and actuarial services, asset management expertise, fund administration and pension-secured loans. The close link between the different business offerings has raised questions about the independence of the advice provided to fund trustees. The potential conflicts of interest are discussed further in section 5.1 of this document.

⁴⁸ An umbrella fund is a collective retirement fund sponsored by a financial services institution, which allows employees from different employers, organisations, industries or trade unions to invest their retirement savings in a single fund. The intended benefits of umbrella funds are to offer affordable retirement fund infrastructure to smaller companies with relatively small workforces.

loan as an “ employee benefit” that they (the employer) have procured for their employees’ advantage.

- In some instances, employers have even assumed responsibility for providing some level of education around the loan product features, terms and conditions.
- Should the employee wish to avail himself of the pension-supported loan, the employer can use their knowledge of the member’s circumstances (personal and financial) to assist the employee to make an informed decision. The extent to which employers are equipped to perform this function is not known but it can be assumed that unless the loan provider and/or trustees have provided specific training, technical capabilities would be low.
- In the vast majority of cases, employers act as the distribution channel for the pension-supported loan. The employee generally approaches the company’s human resources function to complete the loan application.
- A company representative is required to sign off an undertaking (during the loan approval process) to effect monthly deductions from the employee’s wages/salary to repay the pension-backed loan.
- It was reported that several employers have applied their corporate social responsibility funding towards ensuring that employees are using their pension-secured loans for housing. This positive action assists in preventing leakage and ultimately in preserving employees’ retirement savings.

Employees (Pension Fund Members)

The employee is responsible for:

- Ensuring that his/her financial circumstances are not compromised by taking up the pension-secured loan⁴⁹.
- Submitting evidence of a purchase offer if the fund member intends purchasing land or property.
- Providing proof of ownership (or right of tenure) of the land or of the property if home improvements are to be made.
- Providing proof of purchase and delivery of building materials, and confirmation that payment was made for labour, in the event that the fund member has undertaken home improvements.

⁴⁹ Whilst the National Credit Act compels loan providers to take every reasonable precaution to ensure that the borrower is not over-indebted, this does not absolve borrowers from conducting their financial affairs in a responsible manner.

5. MYTHS, ISSUES AND OPPORTUNITIES IN PENSION-SECURED LENDING – RECOMMENDATIONS FOR THE FUTURE

During the course of this study, interviewees highlighted a range of aspects within the pension-secured lending value chain that merit discussion as they point to opportunities to better position the pension-secured loan as a mainstay of housing finance in the lower income sector.

5.1 Appointment of Loan Provider – Conflict of Interest

In making the decision as to whether to offer fund members a pension-supported loan scheme or not, trustee boards often approach their scheme consultants or fund administrators for guidance. The advice would also include suggestions as to which loan provider to appoint, the recommended terms and conditions of the loan scheme and input on operational matters.

The impartiality of the advice has, however, been called into question as certain consultants/fund administrators have proprietary pension-secured loan businesses within their company groupings or have extremely close relationships with specific loan providers.⁵⁰

Unverified reports also refer to the unsavoury practice of loan providers offering financial incentives to trustees to favour their company. It is also alleged that fund trustees request some financial benefit for swinging business to particular loan providers. No incidences of this practice have been made public nor has it been proven. On this basis, it can only be assumed that these instances are the exception rather than the rule.

A counter argument from loan providers interviewed for this study, who are part of employee benefits organisations point out that the integration of loan provision, together with the full service of actuarial consultancy, investment advice and fund administration offers a seamless product that minimises the risk of errors and achieves process efficiencies, which standalone providers (for example, banks and independent loan providers) cannot match. This perspective is valid in as far as these loan providers:

- Can offer loans at a relatively cheaper interest rate than that offered by standalone providers. The touted efficiencies should enable these loan providers to reduce the costs of distribution, administration and communication.
- Can demonstrate transparency in their charging models. There needs to be a clear distinction between fees charged for the various services and that no cross-subsidisation to the detriment of fund members occurs. For example, that lower fund administration charges can be offered to secure the fund

⁵⁰ Recent media coverage about the issue of “secret profits” (Cameron 2009a; 2009b) potentially has relevance here. Not necessarily because there are independently verified reports or proven allegations that retirement fund advisors/administrator have profited from undisclosed commissions for encouraging trustees to direct business to particular loan providers (although industry representatives have confidentially indicated that they believe this practice takes place) but because the process of sourcing, evaluating and appointing loan providers is not regulated and generally not a transparent one.

business but savings from process efficiencies in the loans area not being passed on to the fund member.

However, until such time as either the retirement fund industry self-regulates and adopts a more transparent and accountable approach to appointing loan providers, or regulations are introduced to govern the decision-making process, perceptions of abuse and unethical profiteering (whether or not they prove to be valid) will prevail.

It is recommended that:

- Regulators publish guidelines to trustee boards regarding the process of selecting loan providers.
- Regulators stringently enforce these guidelines.
- Trustees communicate the basis of supplier selection to their members. The growing use of open tenders to solicit loan providers is a positive development and contributes to dispelling concerns.
- Trustee boards as part of their internal governance procedures set policies governing board members' behaviour and address the issue of the giving or receiving of gifts in their capacity as board members.
- Advisors and administrators to recuse themselves from providing advice should there be potential conflicts of interest.
- Loan providers to publicly declare their varied business interests as part of their proposal.

These recommendations suggest ways to incrementally improve the current challenges regarding potential conflicts of interest. Section 5.2 below, however, outlines a more aggressive approach to addressing the issues of conflicts of interest and the need to offer fund members' freedom of choice in loan provider. These sweeping changes would do away with the involvement of fund trustees altogether.

5.2 **Multiple Loan Providers and Fund Members' Freedom of Choice**

Usually trustee boards select only one (at most two) loan providers to service the fund⁵¹. This restricts fund members' choice of provider and adversely impacts on market competitiveness.

There are two ways to addressing this concern. A conservative approach that involves tinkering with the *status quo*, which would involve the regulator issuing guidelines suggesting that board trustees appoint more than one loan provider. Another approach would result in a radical restructuring of the industry and would include recommendations such as:

- Doing away with the regulation that requires individual boards of trustees having to pass a resolution to allow their members to access pension-secured loan finance. – It has been argued that the Pension Funds Act already permits members of retirement funds to utilise their savings for housing purposes (or as collateral to secure housing finance), what further value do

⁵¹ The reason given for this by interviewees is that most fund administrators' information technology systems were historically unable to interface with multiple loan providers. – The majority of loan providers interviewed, however, indicate that electronic communication and multiple interfaces have already been incorporated or are in the process of being developed.

the trustees' deliberations add to the process? After all, consumers already have the ability to approach any loan provider of their choice to access mortgage bonds or unsecured personal loans. In addition, pension-secured loan providers are regulated by the NCA, which gives the borrower (and trustees) the assurance that the borrower's affordability has been taken into account. Furthermore, a proper assessment of affordability should give trustees a measure of comfort that, on a balance of probability, the fund member's retirement savings should remain intact (barring some unforeseen occurrence)⁵².

- Members of defined contribution funds should, therefore, be permitted to approach loan providers of their choice directly, pledge their retirement savings as collateral for a pension-secured loan and to simply advise their fund administrators (and trustees) of the fact.
- In the same way, members of defined benefit funds should be permitted to obtain a guarantee undertaking from their fund (via the administrators) and to be able to offer the undertaking to the loan provider of their choice as collateral for a loan.
- The regulation setting the maximum pension-secured loan amount at 90% of members' retirement savings should be retained to build some level of protection for the member. However, loan providers (and not the fund's board of trustees) should ultimately determine what loan amount the fund member can access based on an assessment of each member's personal circumstances.

Implementing these recommendations would benefit fund members by:

- Releasing members from being "at the mercy" of trustees, who currently decide on members' behalf as to whether having access to pension-secured loans (and by default, housing finance) is appropriate for them or not.
- Giving members the freedom to choose their preferred loan provider⁵³.
- Being able to customise their housing finance based on their individual needs. Members have the assurance that their loan application is assessed based on better information than would be available to the trustees. In addition, loan providers are compelled by the National Credit Act to ensure that the lending is financially responsible.
- Affording members the opportunity to negotiate loan terms (and interest rates) in a competitive environment, safe in the knowledge that pricing is risk based and not arbitrarily pre-agreed to by the board of trustees.

A possible drawback of fund members negotiating individually on interest rates is that they could possibly lose out on the benefits of volume-driven pricing. For example, loan providers would be more amenable to offering multiple borrowers better interest rates if they are secure in the knowledge that they can expect large numbers of loans to be written from a single retirement fund. The lone borrower would not have this bargaining advantage. However, the experience in the mortgage bond market points to competitive

⁵² Trustees, even with their best efforts to preserve members' retirement savings, can not mitigate against retrenchments, dismissals, significant changes in members' financial positions, etc.

⁵³ If members were able to choose their preferred loan provider in a competitive market, trustee boards would be absolved from any suspicion of conflicts of interest with regard to loan providers. Flowing from this, it would also be possible to shift responsibility for the appropriate "use of funds" from the trustees to the loan provider.

forces compelling loan providers to drive down interest rates in order to secure greater market share.

Trustees would, in turn, be secure in the knowledge that they have fulfilled their responsibility for oversight by:

- Empowering fund members to access customised housing finance tailored to suit each individual's financial circumstances and giving them the freedom of choice of loan provider. A wider choice of provider also gives fund members more convenient geographic access.
- Being assured that "use of funds" is more closely monitored by loan providers who are *au fait* and closer to the transaction, and who have the ability to better management the flow of loan proceeds (e.g. paying building materials suppliers directly).
- Ensuring that their members are assessed individually in terms of affordability and in line with the National Credit Act. With the burden of responsibility falling on the loan provider to ensure that the member can afford the loan, the trustee is indirectly ensuring that the member's retirement savings remain intact.

Retirement industry specialists have pointed out⁵⁴ that in terms of current legislation, fund members do not legally "own" their retirement savings until they reach retirement age or until they resign from the fund. Therefore, fund members are not legally entitled to cede their retirement savings as collateral for a pension-secured loan without the express consent of the fund trustees.

There are two possible solutions:

- Retirement and/or housing industry participants should lobby for a change in legislation. This is obviously the more difficult and longer term option.
- Regulations to be amended to permit trustees to guarantee a pension-secured loan on notification by the loan provider that a fund member has been granted a loan.

5.3 **Pricing – The Interest Rate Debate**

A perennial issue plaguing the pension-secured lending industry surrounds the interest rate charged on loans. There is a strong perception in some quarters that fund members are not enjoying the most competitive interest rates, in spite of the secured nature of the loan.⁵⁵

To unpack the elements of this debate, the study will:

- i. Firstly attempt to get an indication of prevailing interest rates in the industry.
- ii. Compare interest rates charged for other housing finance products.

⁵⁴ Input from attendees of a workshop held on 26 March 2009 to discuss the preliminary findings of this study.

⁵⁵ This situation has been exacerbated by several complaints that have been received by the FSB regarding instances where borrowers believe that they have been charged higher than market-related interest rates.

- iii. Introduce a rudimentary model to test whether average interest rates can be considered market related.
- iv. Discuss the specific circumstances surrounding pricing related complaints received by the Financial Services Board (FSB).

Pension-Secured Loans – Prevailing Interest Rates

In an informal poll taken amongst banks active in the pension-secured lending industry, the reported average interest rate charged on pension-secured loans is Prime⁵⁶ minus 1%.

In 2007, the Banking Association South Africa requested FSC originating banks to indicate the average interest rate charge for pension-secured loans. – No updated data is currently available. However, no significant deviation from the “Prime minus 1%” average is anticipated. The reasons for this are:

- Interest rates are set at retirement fund (scheme) level at the outset of the scheme arrangement and all subsequent loans enjoy this Prime-linked rate until renegotiation takes place or unless a new loan provider is engaged. Therefore, the vast majority of new loans written will be at the pre-agreed rate.
- Competition amongst the largest loan providers is fierce. Therefore, there is little scope for loan providers to increase rates without the risk of losing business to competitors or of alienating trustees whose primary motivation is to negotiate the lowest interest rate on behalf of their members.
- Churn of fund business from one loan provider to another is low due to the high cost (financial and administrative) of switching. Therefore, average interest rates will remain stable over the short- to medium- term.

One of the loan providers interviewed indicated that tight liquidity conditions, which has affected the provider’s cost of funding, has forced the provider to price new schemes (not “loans”) at higher interest rates. The average interest rate has risen to Prime plus 0.5%. This represents a significant interest rate differential of 1.5% from the prevailing average. However, in the short- to medium- term, no change in the industry average is expected for the following reasons:

- i. Only one out of five loan providers interviewed (albeit with a significant market share) has confirmed that they are quoting higher interest rates. It remains to be seen whether market forces will compel the loan provider to re-align its pricing with competitors or if competitors will take the opportunity to similarly adjust their pricing upwards, taking advantage of tight credit conditions.
- ii. Tight credit conditions have also resulted in very few new (large) schemes being signed up.
- iii. The vast majority of new loans currently being written are governed by interest rates agreed for existing (old) schemes, i.e. at the historic average of Prime minus 1%.

The change in pricing policy of one loan provider will have little or no impact on industry averages in the near term. However, the situation bears observing as it may herald a significant change in future pricing policy.

⁵⁶ As at 6 February 2009 the prevailing Prime interest rate in South Africa is 14%.

Banks interviewed for this study confirm that there has been no change in average interest rates for existing schemes. Furthermore, they advise that market information gathered on their non-bank competitors, point to comparable average interest rates being in place. Similarly, non-bank loan providers with significant market shares confirm that their business is written at similar average interest rates because they have had to remain competitive with the commercial banks.

Therefore, based on interviews with banks and large non-bank loan providers, there appears to be independent and mutual verification that average interest rates charge by banks and non-bank loan providers are comparable for the time being.

Housing Finance Products – Interest Rate Comparisons

In 2007, the Banking Association requested some of their member banks to submit indications of the relative average interest rates charged across consumer housing finance products.

Table 9 (column 2) shows the results of this informal poll to benchmark average interest rates. The unsecured personal loan is the most expensive financing option both from the perspective of monthly repayments and from a relative interest bill. This reflects the higher risk that loan providers are exposed to when granting unsecured loans.

A comparison of the monthly repayments (Table 9 – column 3) on a loan of R 20 000 and the total interest charge over the period of the loan (Table 9 – column 4) have been included to highlight the affordability requirements and total cost of finance.

The unsecured loans stands out as significantly more expensive with respect to monthly repayments than the pension-secured or mortgage loan. Monthly repayments on the pension-secured loan are higher than that for mortgage loans but the overall total interest cost is significantly lower.

Including the mortgage loan in the comparison is somewhat misleading as it is a patently inappropriate financing product for smaller loan amounts. Comparisons between the pension-secured and unsecured personal loan are, therefore, more useful to evaluate financing for smaller home improvement/home extension projects.⁵⁷

⁵⁷ Mortgage, Pension-secured and Unsecured loans represent the high-level categories and the most popular types of housing finance products currently available in South Africa. – Reviewers have mentioned an innovative housing finance product targeted at lower income earners from Nedbank. This product is an enhancement to the existing Mortgage Loan product. Essentially, overseas grant funding of R 8 500.00 per loan has been made available to pay for half of the legal costs and initiation fees. The remaining portion of the grant is applied directly to the principal loan amount. The maximum loan amount is R 250 000 (at present) and the qualifying income level is determined by the prevailing interest rate from time to time. The ongoing availability of this subsidy is restricted to the total amount of grant funding. Once the grant funding has been exhausted, new sources of similar funding would have to be found.

HOUSING FINANCE PRODUCTS – INTEREST RATE COMPARISON				
Housing Finance Product	Average Interest Rate⁵⁸	Monthly Repayments*	Total Interest Paid Over Normal Loan Term	Total Interest Paid Over Average Actual Repayment Period
Mortgage Loans	Prime	R 248.70	R 39 689	R 18 718
Pension-Secured Loans	Prime – 1%	R 298.62	R 15 835	R 11 042
Unsecured Personal Loans	Prime + 5%	R 518.81	R 11 129	R 8 969

Table 9 Source: Banking Association South Africa informal poll, 2007

*Monthly repayment calculations were based on the following assumptions:

- Loan amount = R 20 000
- Prime = 14% (as at February 2009)
- Repayment periods for Mortgage Loans, Pension-secured Loans and Unsecured Loans were assumed to be 240 months, 120 months and 60 months, respectively, based on the normal loan terms offered to consumers. Obviously the actual repayment period varies from product to product. On average, the repayment periods for Mortgage Loans, Pension-secured Loans and Unsecured Loans are 84 months, 60 months and 36 months, respectively.

Table 9 (column 4) illustrates the total interest charge for the different loan types if calculated over the full loan term, i.e. the official loan tenure offered by the loan provider. For pension-secured loans, the loan period can technically extend to a maximum of 30 years or until the member retires, whichever is the earlier date. In practice, loan providers limit the period to between 10 and 15 years, with an option to extend the period on request. On this basis, the pension-secured loan is the least expensive option and from an ongoing affordability perspective, most appealing for the borrower.

If the total interest charge is recalculated over the average, actual repayment period, i.e. the period over which the loan is repaid based on actual experience, the cost of finance reduces dramatically for all loan types. The pension-secured loan remains the best option for smaller loan amounts.

⁵⁸ During 2007, the Prime lending rate ranged between 13% and 14.5%.

MORTGAGE LOANS VS. PENSION-SECURED LOANS				
Housing Finance Product	Average Interest Rate	Monthly Repayments*	Total Interest Paid Over Normal Loan Term	Total Interest Paid Over Average Actual Repayment Period
Mortgage Loans	Prime	R 2 238.34	R 357 200	R 168 463
Pension-Secured Loans	Prime – 1%	R 2 687.59	R 142 511	R 99 376

Table 10 Source: Sing (2009)

*Monthly repayment calculations were based on the following assumptions:

- Loan amount = R 180 000
- Prime = 14% (as at February 2009)
- Repayment periods for Mortgage Loans and Pension-secured Loans were assumed to be 240 months and 120 months, respectively, based on the normal loan terms offered to consumers. Obviously the actual repayment period varies from product to product. On average, the repayment periods for Mortgage Loans and Pension-secured Loans are 84 months and 60 months, respectively.

If a similar exercise is undertaken for larger loan amounts, say, R 180 000, which could enable the borrower to purchase a serviced site and build a top structure or perhaps to purchase an existing house, the versatility of the pension-secured loan is apparent. Obviously, monthly repayments on the pension-secured loan are higher but the total finance charge reduces substantially.

In addition, pension-secured loans, unlike mortgage loans, do not incur assessment/valuation fees and legal fees for registering a bond. These cost savings alone sways the preference in favour of pension-secured loans.

In practice, the biggest drawback to pension-secured loans is that lower income fund members are not in a position to accumulate large pools of retirement savings because their monthly contributions (a percentage of their income) are low and/or income constraints preclude the member from being able to afford the higher monthly repayments.

The pension-secured loan nevertheless, if accessible to the borrower, remains a much better option than the unsecured (microfinance) loan.

Determinants of Interest Rate Charges

Critics argue that the pension-secured loan, as a relatively “risk free” product, collateralised by the borrower’s retirement savings, should enjoy more competitive (i.e. lower) interest rates. To test the foundations of this argument, it is useful to derive a rudimentary costing model (from the loan provider’s perspective) for the pension-secured loan product.

FACTORS INFLUENCING THE COST OF PROVIDING PENSION-SECURED LOANS		
COST VARIABLE	COST (%)*	COMMENT
Cost of Funds (fixed)	10.5%	Based on the prevailing Repo Rate** as at 6 February 2009.
Cost of Origination - Via Employer (variable)	0%	Currently, the bulk of loans are originated through employers, which adds negligible (but not zero) costs to loan providers. Lenders provide communication, administrative and technical support to employers. However, loan providers are increasingly using proprietary distribution channels or outsourced loan fulfilment services. Added costs range from 0.25% (call centre) to 0.75% (bank branch) to 2.5% (outsourced). This translates to an origination transaction cost of R 50, R 150 and R 500 via a proprietary call centre, branch and outsourced originator, respectively.
Cost of Servicing (variable)	1.2%	Includes account set-up costs, NCA credit checks and income verification, FICA compliance, "flagging" fees, systems support, account maintenance, customer communication (enquiries, account statements), etc. For a loan of R 20 000, this translates to a cost of R20 per month.
Cost of "Use of Funds" Management – Liaising with Supplier (variable)	0.5%	Assuming that the retirement fund picks up the cost of monitoring "use of funds", the once-off cost to the loan provider of managing the administration and relationship with the "use of funds" supplier is about R100. However, if the loan provider contracts for the "use of funds" management on behalf of the trustees <u>and</u> manages the relationship, this cost could rise to 2% of the loan, i.e. R 400.
Cost of Risk (variable)	0.2%	Credit losses are minimised as the loan is guaranteed by the fund. The industry average is said to be 2%. However, several factors could increase the cost of risk (i) individually based default collection increases costs; (ii) the economic downturn giving rise to massive job losses in hard hit sectors (e.g. mining, motor industry) increases the risk of default; (iii) and to a lesser extent, the worsening equity markets has reduced the value of security as retirement savings are eroded. The cost of risk could increase to 1%.
Opportunity Cost of Capital (fixed)	0.2%	The cost of choosing to allocate scarce funding to pension-secured loans instead of alternative investments.
Required Return on Equity (profit)	1.1%	Investors' required return on capital invested.
TOTAL ESTIMATED COST	13.7%	This represents the costs that the loan provider must cover to ensure that the business is profitable (and therefore, sustainable over the long term).
<p>Table 11 Source: This model is based on similar work done by the Housing Work Group at the Banking Association South Africa and uses the same "opportunity cost of capital" and "return on equity" variables as those used for the mortgage lending product.</p> <p>*Cost estimates are calculated on an average loan size of R 20 000. Variable costs are effected by the volumes of loans processed (economies of scale).</p> <p>**The Repurchase (Repo) Rate is the rate at which private sector banks borrow Rands from the South African Reserve Bank (central bank).</p>		

Taking into account the various components contributing to loan providers' costs of offering pension-secured loans, Table 11 reveals that the estimated total cost amounts to 13.7%.

PENSION-SECURED LENDING – REVENUE vs. COST COMPARISON

	COST (%)	COMMENTS
TOTAL ESTIMATED COST	13.7%	This represents the costs that the loan provider must cover to ensure that the business is profitable (and therefore, sustainable over the long term).
AVERAGE INTEREST RATE (Calculated at Prime-1%)	13%	Based on a prevailing Prime rate of 14% (February 2009), this is the reported average interest charged by lenders.
“MARGIN FOR MANOEUVRE”	-0.7%	The negative result (for lenders) effectively means that loan providers are forfeiting 0.7% their required rate return, earning just 0.4% on each loan.

Table 12 Source: Sing (2009)

Table 12 shows that if the Prime rate is assumed to be 14% then the interest rate paid by borrowers is 13%, i.e. the prevailing industry average of Prime-1%. Using the lender’s cost estimates detailed in Table 11 which totalled 13.7%, loan providers face a negative result of 0.7%. This means that in order to break even, loan providers have to forfeit 0.7% of their required rate of return, earning just 0.4% on each loan. Essentially, there appears to be very little margin for loan providers to reduce interest rates.

Loan providers are able to improve their margins by:

- i. Seeking cheaper sources of funding. As funding costs constitute more than 75% of total costs, this would be the most effective approach.

Recent discussions with loan providers revealed that loan providers are already actively seeking cheaper, alternative sources of funding. The global downturn has resulted in liquidity shortages, which are putting pressure on margins and together with the need to comply with Basel II⁵⁹ requirements, lenders are searching for innovative funding models⁶⁰.

Other providers indicate that capital market conditions have tightened to such an extent that even internally sourced funding⁶¹ can cost in the region of 12%.

- ii. Maximising the productivity of existing technology systems, people and processes to “sweat the assets”.

⁵⁹ Basel II incorporates international banking laws and regulations governing banks’ capital and risk management practices and are aimed at protecting the international financial system from major banking collapses.

⁶⁰ Prior to the recent liquidity crisis, securitisation had become a popular avenue of raising funding in the capital markets. With this avenue now essentially closed or too expensive, loan providers (bank and non-bank) are actively seeking cheaper, alternative sources of funding with very limited success.

⁶¹ Bank business units usually source funding from in-house treasury operations. There may be a nominal internal charge between business areas within the same operating entity, which is added to the cost of funding. This is equivalent to including an opportunity cost of capital. Essentially it would be a “compensating” charge levied by the treasury operations for allocating capital towards a particular business unit as opposed to lending the funds out to a corporate or retail client, or to an alternative investment, e.g. acquiring a new business.

- iii. Generating higher loan volumes to benefit from economies of scale. The introduction of NCA regulations has, however dampened loan approvals and the scarcity of funding has largely compromised this avenue.
- iv. Optimising on cross-selling opportunities by offering borrowers related financial products. For example, credit life insurance, which ensures that the loan is paid off in the event of the borrower's demise⁶².

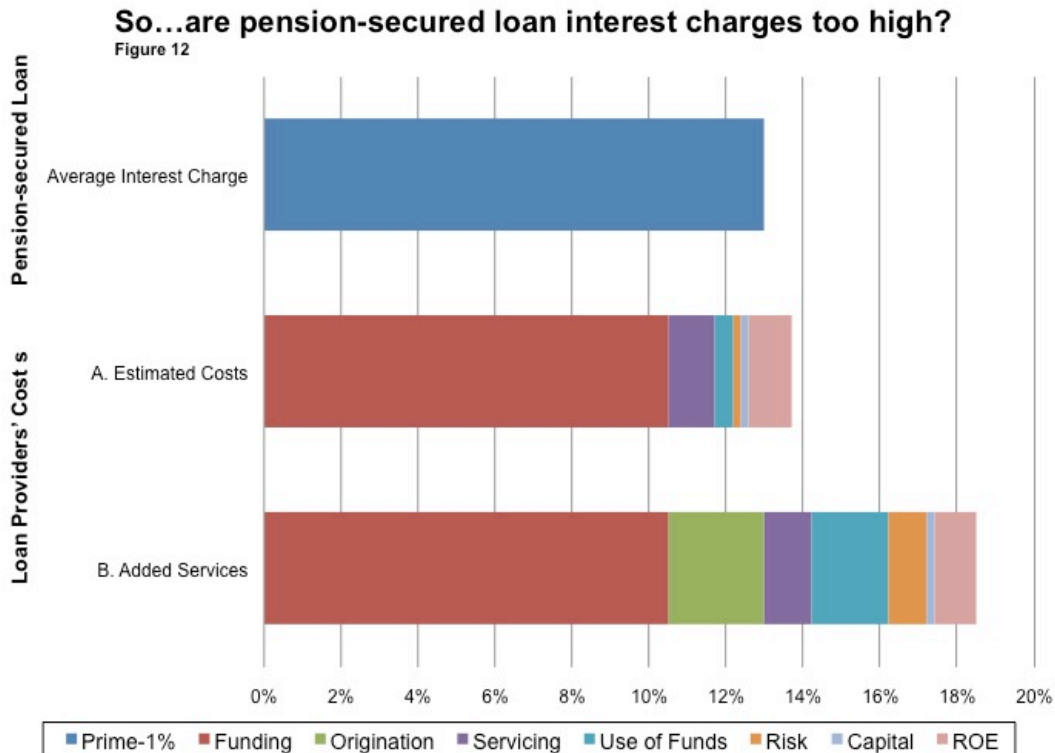


Figure 12 graphically illustrates the thin margins on pension-secured loans. Scenario A depicts the cost estimates of 13.7% as detailed in Table 12. It is worth noting that industry representatives⁶³ were of the opinion that the assumptions made to derive the cost estimates were too conservative. More specifically, they indicated that:

- *Cost of funds* – As discussed previously, some lenders advise that their cost of funds is above the prevailing repo rate. The inclusion of an “opportunity of cost of capital” at 0.2%, in their view, does not compensate for the true cost of funds.

⁶² Some critics question the need for credit life insurance, believing that its sale is exploitative. They argue that in the event of the death of a fund member, the deceased's retirement savings have already been made available as collateral and the house could potentially be sold as an asset to repay the loan. – A counter argument is that it is more detrimental to a surviving family to forfeit a pension payout or their home to repay the outstanding loan. - Comber's (2005) research indicates that 95% of respondents (industry representatives) agreed that it was essential to package credit life insurance with housing finance - "...it should be done responsibly with choice and options provided, and costed reasonably...AIDS and retrenchment cover (are) critical and should be catered for in product designs."

⁶³ Industry representatives attended a workshop on 26 March 2009 to discuss the draft version of this study.

- *Cost of origination* - Even when loans are originated by the employer, it is not a “costless” process to the loan provider. Lenders incur the cost of training employers to complete the loan application and providing them with product knowledge. They also provide ongoing liaison and support services to the employer. Increasingly, loan providers cannot rely on employers to generate sufficient loan volumes and they are forced to introduce alternative distribution channels to ensure that required growth is achieved.
- *Cost of servicing* – The assumption of R 20.00 per loan per month was viewed as too low.
- *Cost of “use of funds” management* – Trustees are increasingly passing on the responsibility for compliance to lenders.
- *Cost of risk* – There were mixed opinions as to whether the occurrence of bad debts are set to escalate significantly or not. However, there was consensus that loan defaults are looming in the mining and automotive sectors.

As loan providers choose to assume greater degrees of operational responsibility (for example, establishing proprietary distribution channels, introducing individualised default collection strategies, managing “use of funds”), costs will increase concomitantly, putting upward pressure on interest rates.

Scenario B illustrates the situation where loan providers contemplate providing more value added services or taking on additional operational responsibilities. Total costs subsequently balloon to 18.5%, resulting in a negative impact on the lender of 5.5%. Under these circumstances, the cost-benefit gap would become so wide that it would render the business unviable.

In this scenario, seeking cheaper sources of funding (which constitutes 55% of total costs) would contribute to reducing lenders’ costs but the non-funding costs (constituting 45% of total costs) would prove to be an equally significant drain on profitability.

In summary, with margins on the pension-secured loan under pressure, there is little likelihood of interest rate cuts. Present liquidity constraints will simply exacerbate the situation. There is little incentive for loan providers to seek to acquire new business.

Allegations of Over-charging – Complaints to the Regulator

These allegations are dealt with separately as they pertain to a particular set of circumstances.

For retirement funds that elected to provide loans directly to their members, Regulation 27 (of the Pension Funds Act No. 24 of 1956) prescribes an interest rate of no less than 15%. This stipulation only applies to retirement funds providing direct loans to their members. Other pension-secured loan providers are exempt from this regulation but fall under the auspices of the National Credit Act (NCA).

According to the FSB, the rationale for setting this prescribed minimum interest rate was to ensure that interest earned on loans to members would yield a similar (minimum) average return as the retirement fund would have enjoyed had it invested its funds in a diversified portfolio (government bonds, money market funds or the equity market). This regulation was thus introduced to obviate the beneficial cross-subsidisation of borrowers by other fund members. – However, it is apparent that the inflexibility of the prescribed rate potentially creates distortions if it is not synchronised with the markets, and that unscrupulous lenders have taken advantage

of the fixed rate to “overcharge” borrowers in relatively low interest rate environments, i.e. when Prime was below 15%.

The Financial Services Board (FSB) had received complaints that third-party loan providers were taking advantage of the Regulation (even though they are exempt) and levelling interest rates of 15% (or higher), at a time when prevailing Prime interest rate was lower⁶⁴.

With the recent increases in the Prime lending rate since 2005, however, this issue has become moot, as the gap between the regulated prescribed rate and the Prime rate has closed. However, to avoid similar problems in the future, it is recommended that regulators should:

- Consider adjusting this stipulated minimum more frequently in line with market movements to ensure parity with the market, or;
- Link the minimum rate to a regularly quoted rate, e.g. Prime, Repo rate, JIBAR, or;
- Scrap the minimum prescribed rate altogether and allow competitive markets to find their own levels.

With the larger loan providers (banks and non-banks) confirming that interest rate charges are quoted on a “Prime linked” basis, then there is a high likelihood that complaints reaching the regulator can be ascribed to isolated cases of unscrupulous loan providers taking advantage of borrowers. Perhaps of greater concern is that these rates are being levied presumably with the full knowledge and acquiescence of trustees.

In conclusion, without more accurate data, it is difficult to evaluate the “appropriate” interest rate for pension-secured loans. A comparison of current average interest rates with a rudimentary analysis of loan providers’ total costs reveals that there does not appear to be extraordinary margins being earned. Discussions with loan providers also indicate that markets are competitive and robust. Most fund trustees are highly attuned to negotiating preferential rates on behalf of their members and loan providers are pressured to offer their most competitive rates in order to secure the business.

Within the broader housing finance context, the average interest rates charged for pension-secured loans are the least expensive. In some respects this is counterintuitive as property values (underlying a mortgage bond) are generally less volatile than capital market/equity values (underlying a pension-secured loan). If it is assumed that higher volatility implies higher risk, then pension-secured loans should be relatively more expensive than a mortgage loan to compensate for the higher perceived risk.

On balance, the information suggests that pension-secured loans, in spite of being administratively intensive (relative to its small loan size) and its collateral value inherently more volatile, are competitively priced compared to other housing finance products.

⁶⁴ The Prime interest rate in 2005 was 10.5%. During 2006 it range between 11% and 12.5%. In 2007, the Prime interest rate ranged from 13% to 14.5%, and in 2008 reached 15%, peaking in June 2008 at 15.5%. Since December 2008, the Prime has decreased and is presently (February 2009) at 14%. – It appears that at the time of the complaints made to the FSB that the Prime interest rate was lower than the prescribed 15% minimum.

To overcome any vestige of negative perceptions about the interest charges, it is recommended that:

- Market forces be allowed to compete to set pricing levels. There are sufficient numbers of loan providers emanating from different sectors (bank and non-bank) to ensure that pricing is robustly and finely negotiated with retirement funds.
- Fund trustees, employers and loan providers should inform members of the pricing components (i.e. interest rate, fees, other charges) of the pension-secured loan on application.

5.4 **Fees**

Pension-secured loans have been subject to a wide variety of fees over time. Some commentators view the fees simply as yet another gambit to extract even more revenue from the fund member. Yet others argue that the pension-secured loan remains a cheaper housing financing instrument, as there are no legal fees or valuation fees as would be the case for a mortgage loan.

Initiation Fees

Commencing with the loan application process. Some loan providers (with the agreement of fund trustees) have expanded their distribution channels to include third-party “loan fulfilment” suppliers. “Loan fulfilment” comprises some or all of the following functions:

- Liaison with employer representatives to arrange to meet with fund members (employees) who have indicated that they wish to apply for a pension-secured loan.
- Advising the employer representative or the fund member as to what personal and financial documentation is required to accompany the loan application.
- Travelling to the worksite⁶⁵ to assist the fund member to complete the loan application and to perform the FICA⁶⁶ verification requirements. The need to obtain the borrower’s original signature to the loan documents requires face-to-face interaction.
- Submitting the completed loan application together with all the supporting documentation to the loan provider.
- In need, to follow up on any outstanding issues with the fund member.

“Loan fulfilment” providers are charging between R 200.00 and R 500.00 per loan application. This cost can be absorbed by the loan provider⁶⁷, capitalised to the loan

⁶⁵ A key business challenge for “loan fulfilment” providers is to have national representation and to be able to reach fund members at remote sites.

⁶⁶ Financial Intelligence Centre Act (FICA) aims to prevent money laundering and requires financial services institutions to gather, verify and store of documents that confirm clients’ identity and place of residence.

⁶⁷ Loan providers are not permitted to charge loan assessment or loan initiation fees in terms of the National Credit Act.

or paid for by the fund. In the majority of instances, the “loan fulfilment” fee is capitalised to the loan⁶⁸.

“Flagging” Fees

Once a loan is approved, fund administrators are requested to annotate the fund member’s retirement savings account is held as collateral for the pension-secured loan.

Loan providers advise that some fund administrators charge a “flagging” fee each time they are requested to annotate the retirement savings account. Reports vary as to the amount of the charge, ranging from anything between R 40.00 and R 200.00. This charge is usually absorbed by the loan provider and recouped as a “cost of servicing” (see Table 11).

There is debate as to whether fund administrators are justified in levying this charge, over and above their monthly administration fee, as “flagging” requires minimal effort, simply entailing a once-off notation on the fund member’s retirement savings account.

Monthly Administration Fee

The National Credit Act (NCA) permits loan providers to charge a monthly fee to cover the costs of maintaining the loan account and servicing the borrower’s needs.

Banks charge fees ranging between R 6.00 and R 12.00 per month. Other loan providers have been known to charge up to R 25.00 per month. Yet other lenders choose to waive this fee for loan schemes to gain a competitive advantage.

Redraws and Further Advances

Common practice amongst sub-contracted providers of loan fulfilment services is to contractually agree a “loan initiation” (or “loan fulfilment”) fee with the borrower, to cover the administrative costs of processing, accessing and disbursing a new loan and to add the fee to the capital portion of the loan. This fee generally applies to the first time a loan is taken up.

Interviewees, however, relay instances where an “initiation fee” is levied each time the borrower redraws on an existing loan. So, each redraw is treated as if it were a new loan. The capitalisation of the “initiation fees” adds to the overall cost of the loan to the borrower and in instances where there are multiple redraws over time can add substantially to total costs over time. Amongst the larger loan providers, there is consensus that this recurring fee is not justified and exploitative.

It may be useful to diagrammatically illustrate the costs associated with providing a pension-secured loan in relation to the fees and charges levied. Table 13 shows how certain loan costs are priced into the interest rate, whilst other costs are recouped

⁶⁸ The “loan fulfilment” fee is contracted directly between the borrower and third party service provider and thus falls outside of NCA regulations.

through fees levied over and above the interest rate charge. The table also shows which of the supply-side participants bear the costs and which of the participants receive the revenue for providing the service.

PENSION-SECURED LENDING – SUMMARY OF COSTS AND FEES				
COST/FEE (per application)	LOAN PROVIDER	THIRD PARTY SUPPLIER	FUND MEMBER (Borrower)	RETIREMENT FUND
Cost of funds	Cost borne by lender		Recouped via interest rate	
Origination/ Loan fulfilment				
• Via employer	Negligible cost borne by lender			
• Call Centre (proprietary)	Cost = R 50		Recouped via interest rate	
• Branch (proprietary)	Cost = R 150		Recouped via interest rate	
• Outsourced origination		R 200 to R 500	Capitalised or paid upfront	Seldom pay
Loan servicing	Cost = 1.2%		Recouped via interest rate Monthly fee between R6 & R25	
“Use of Funds”				
• Monitoring (upfront disbursement)	Borne by lender	R15 to R30 per transaction Earn 2% to 5% “business introduction fee paid by materials supplier	Recouped via interest rate	
• Monitoring (on-site)	Borne by lender	R250 to R500 per inspection	Recouped via interest rate	Sometimes paid for by the fund or employer
• Management (liaison with 3 rd party)	Cost = 0.5%		Recouped via interest rate	
Credit risk	Cost = 0.2%		Recouped via interest rate	
Opportunity Cost of Capital	Cost = 0.2%		Should be recouped via interest rate	
Required ROE	1.1%		Should be recouped via interest rate	
Flagging fee	Borne by lender	R40 to R200 (fund administrator)	Recouped via interest rate	

Table 13 Source: Sing (2009)

It is recommended that to simplify the types of fees levied and to protect borrowers' interests, coordinated action by overseers of the retirement fund industry and the National Credit Regulator⁶⁹ to determine what fees can legally be levied and the maximum amount that can be charged would go a long way to closing any loopholes. Consumers would benefit from greater transparency regarding the total cost of the pension-secured loan. Unscrupulous loan providers would be prevented from passing on operational costs through the interest rate and again through fees. Alignment with the existing National Credit Act would be a simple solution to this problem.

5.5 The "Use of Funds" Conundrum

Incidences of fund members not using the proceeds of pension-secured loans to acquire, upgrade or extend their primary dwelling, have, according to industry sources, reduced dramatically. Historically, estimates of "leakage" were significant, with reports ranging between 30% and 70%. Loan providers put more recent estimates of "leakage" at less than 30%. Based on the reported value of pension-secured loans disbursed by the banks in terms of the Financial Sector Charter, the banks have, on average, extended R 1 billion in pension-backed loans annually. "Leakage" estimates of 30% (or less) translate to about R 300 million of loan proceeds being spent on non-housing products or services.

While the monetary value of this "leakage" amount cannot be ignored, the real concern is that lower income earners, who are already at risk of not being adequately provided for when they reach retirement age, could be increasing their risk by putting their existing retirement savings in jeopardy. Conversely, others argue that whilst the risk of depleted retirement savings (without concomitant property asset acquisition/growth) should be avoided if at all possible, the pension-secured loan is serving a real (and immediate) need for households that would otherwise have to resort to relatively extortionate microloans in order meet essential expenses to survive.

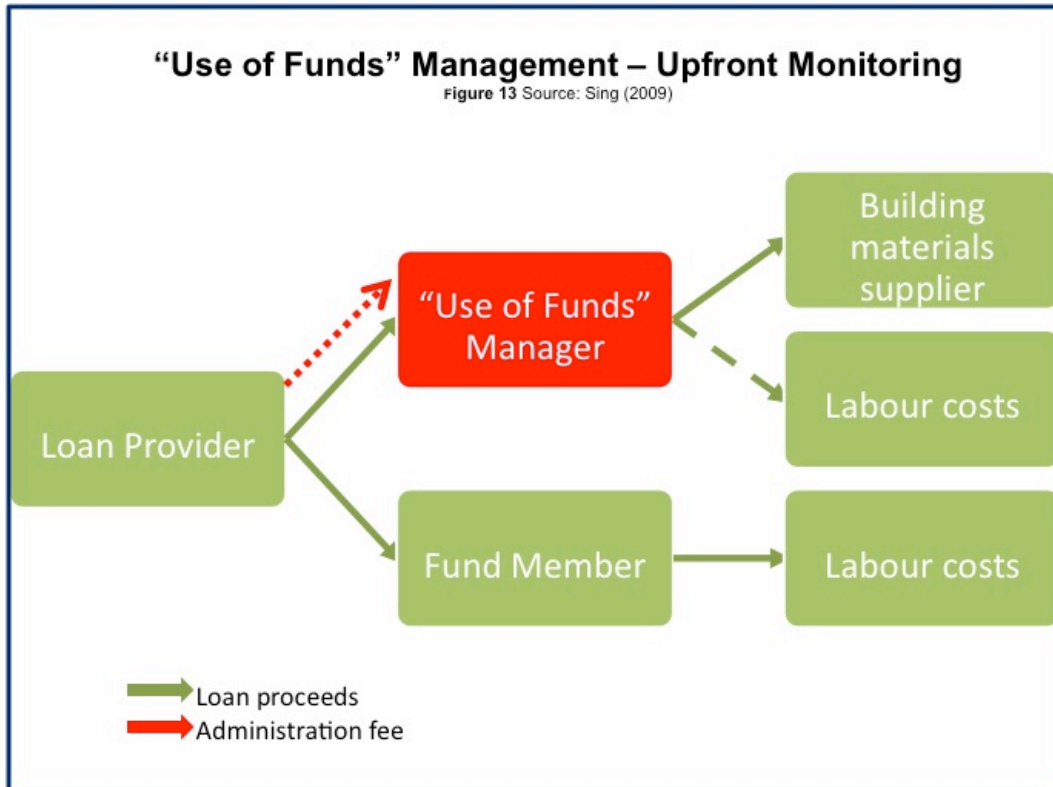
In terms of regulations, the onus remains on fund trustees to ensure that pension-secured loans are only used for housing purposes. Some trustees view this regulation as so onerous that they would rather forgo offering the pension-secured loan benefit to members than have to assume responsibility for adherence to the regulations. Loan providers are actively pursuing solutions to the problem. They believe that assisting the board of trustees to enforce compliance with the regulations forestalls trustees' objections to adopting pension-secured loan schemes and facilitates their marketing efforts.

Monitoring and managing the "use of funds" is usually outsourced to specialist service providers. These providers are generally either involved in the upfront disbursement of loan proceeds or make on-site inspections after a property (or a piece of land) has been purchased or on completion of construction work.

⁶⁹ The need to involve both retirement fund and National Credit Act regulatory authorities is due to their differing mandates. Whilst the FSB has jurisdiction over retirement fund regulation insofar as it allows funds to provide loans to members (or to guarantee members' loans), the National Credit Regulator is responsible for enforcing legislation pertaining to the broader consumer credit market, e.g. prescribed interest rates, allowable fees.

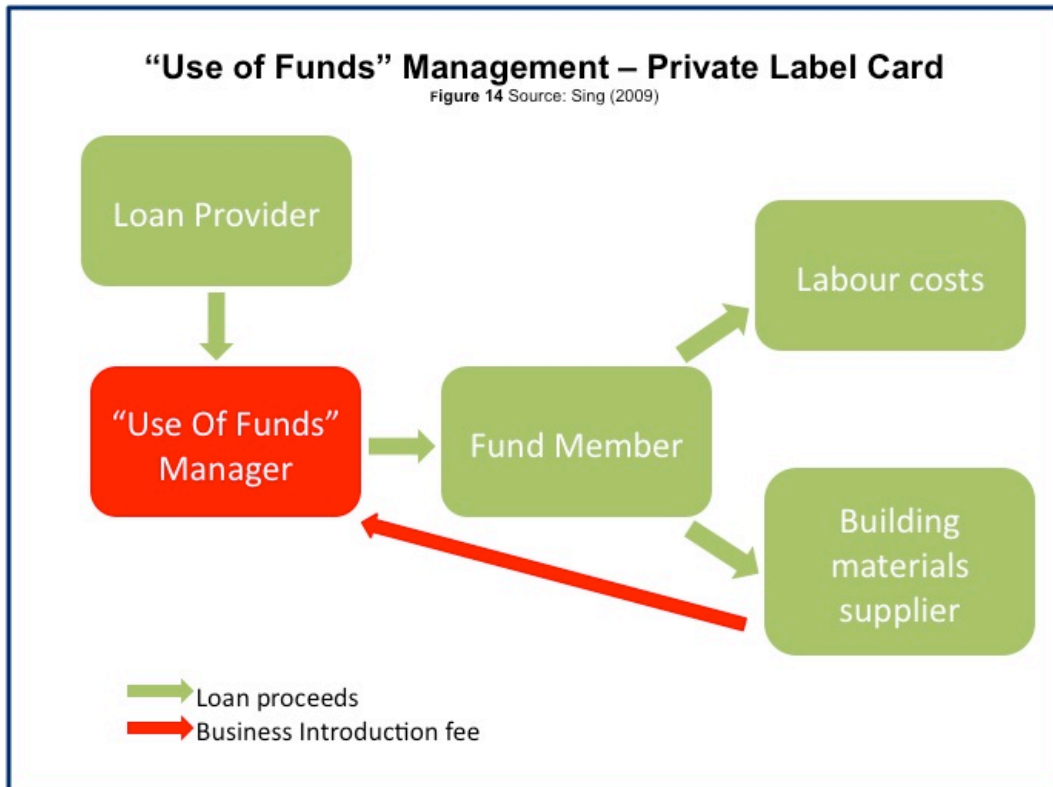
Upfront Disbursements

With upfront disbursements, the “use of funds” service makes payments directly to a building materials supplier against an invoice and/or proof of delivery. Sometimes, direct payments are also made for labour costs (Figure 13).



In the main, upfront monitoring of disbursements is electronically, mass administered and is priced on a “per transaction” basis. Such systems entail relatively high, upfront set-up costs (which the third party supplier generally incurs in anticipation of high volumes of transactions) and relatively low transaction charges. It is difficult to estimate the upfront, systems development costs. They are dependent on such factors as whether a new system has to be built or if enhancements simply have to be made to an existing process; the administrative complexity of the process; the level of technology interface required between the loan provider, the “use of funds” monitor and the building materials outlet. The “per transaction”, administration charge ranges between R 15.00 and R 30.00. This charge is either paid by the fund or incorporated in the loan provider’s pricing.

Another version of monitoring disbursements has recently been developed using private label card technology. The borrower is restricted to only spending the loan proceeds (whose value has been loaded onto the private label card) at designated building material suppliers (Figure 14).



In this business model, the service provider earns income by negotiating a “business introduction” fee with the building materials supplier based on projected business volumes. Some concerns about this model are that:

- Borrowers have a restricted choice of building materials supplier, with respect to geographic access, product range and product price comparison;
- Building material suppliers may pass on the cost of the “business introduction” fee to the borrower;
- The borrower incurs interest charges as soon as the value of the loan proceeds have been loaded on the private label card and not when payment has been made for goods received.

Indications are that the “business introduction” fee is in the range of between 2% and 5% of the total cost of building materials.

Neither of these disbursement monitoring models are foolproof as there could be “leakage” as loan proceeds are usually paid directly to the borrower to pay for labour costs. Lenders have also mentioned building material suppliers who have produced fictitious quotations or invoices for fraudulent borrowers. These materials suppliers pay over the loan proceeds to the fund member after taking a cut for themselves.

On-site inspections

On-site inspections to ensure that the borrower has, in fact, purchased a house or undertaken building work to an existing property is a relatively expensive exercise as it entails a physical inspection by a trained individual. Depending on the geographic location of the property and on assessment volumes, the charge per physical

inspection ranges between R 250-00 and R 500-00. Due to the cost, assessments are normally carried out on a random basis to ensure adherence to regulations.

No intervention has proved to be completely effective in preventing “leakage”. Whatever approach is adopted, the cost of managing the “use of funds” ultimately is passed on to the borrower. Costs are either recouped through higher interest rates if the loan provider includes the monitoring service as part of their product offering or more directly, as an actual expense to the retirement fund.

Managing the “use of funds” may be a necessary intervention to protect fund members from making poor financial decisions. However, borrowers need to be reminded that they are responsible for any adverse consequences to their poor choices. It is recommended that regulators should:

- Insist that all approved pension-secured loan schemes must include a “use of funds” management mechanism.
- Visibly enforce “use of funds” compliance.
- More importantly, however, regulators should shift the emphasis from introducing punitive interventions to proactive consumer awareness programmes⁷⁰, which highlight the dangers of squandering retirement savings on non wealth-creating expenditure.

5.6 **Product Enhancements**

This section identifies several areas where enhancements to the pension-secured loan itself, broadening its usage for different housing types or financing options, would contribute to expanding access to housing and wealth creation opportunities.

Hybrid Housing Loans

The average size of bank-provided pension-secured is in the region of R 20 000. Non-bank providers, on the other hand, advise that the average size of their loans range between R 35 000 and R 40 000. Loan amounts remain patently inadequate to purchase a house.

Some loan providers are addressing this problem by augmenting the pension-secured loan, where the borrower can demonstrate affordability, with additional mortgage or unsecured personal loans to enable the fund member to buy “more house”. Fund members would borrow up to the maximum allowable loan amount as determined by the trustees (and the value of their accumulated retirement savings). The remaining portion would then be financed via a mortgage and/or an unsecured loan.

Concerns that these hybrid loans potentially place borrowers at higher risk of overextending themselves are largely unfounded. The National Credit Act puts the

⁷⁰ Investment in consumer awareness programmes could be funded as part of the FSC commitment to raising financial product awareness.

onus on lenders to ensure that the borrower's financial position is properly evaluated and that he/she is able to afford the loan.

Any additional risk of hybrid housing loans lies more with borrowers who default on their loans. As the property purchase is collateralised using their retirement savings (pension-secured loan) and a mortgage bond is registered over the property, the defaulting borrower could lose both their retirement savings, as well as their home. To prevent this, borrowers should be strongly encouraged to take up insurance⁷¹ to mitigate this risk.

Incremental Housing and Self Build

The pension-secured loan can also be used as a mechanism to finance incremental housing projects. Fund members can begin with a basic structure and add on to these existing dwellings, in small increments, over a period of time.

Anecdotal evidence suggests that this model is more popularly applied for home improvements in rural areas, where formally employed, urban sojourners direct the proceeds of pension-secured loans towards improving traditional, family homesteads. Generally, borrowers (or their dependents) already have title over these rural homes and construction work can be undertaken more cheaply than would be the case in urban areas. This observation supports Tomlinson's (1998) findings where respondents indicated that they have an aversion to bank finance⁷² and prefer buying building materials and effecting improvements or additions to their homes when they can afford to do so, i.e. incremental or self-build housing.

It has also been suggested⁷³ that the pension-secured loan could be an ideal vehicle to purchase land in order to kick-start an incremental housing process.

Small-Scale Landlords

Research undertaken by Shisaka (2006) found that small-scale landlords⁷⁴ are making substantial contributions to the supply and management of affordable rental housing for lower income people. At the same time these landlords are accumulating a portfolio of assets, contributing to wealth creation and national economic growth.

Most of the rental accommodation in South African townships is in the form of units built in the backyard of the landlord's property. The units may be formal (i.e. a traditional brick and mortar dwelling) or informal (i.e. a shack). In some instances, the landlord rents out a piece of land on which the tenant builds their own house. This

⁷¹ For example, borrowers could take up insurance, which covers their loan repayment obligations in the event of loss of income due to unemployment or physical disability. Credit life insurance settles the outstanding liability in the event the borrower dies.

⁷² The reasons given were that people feared losing of control over their finances and their homes being repossessed in the event of default.

⁷³ By Kecia Rust at the workshop held on 26 March 2009 to discuss the preliminary draft of this study.

⁷⁴ Small scale landlords were defined in the research (Shisaka, 2006) as "...someone who has the rights to property and rents it to another person for regular payments which may be in cash or in kind (such as food or services)... individuals and small companies who rent out anywhere between one and one hundred units, or who rent out units in up to three buildings."

innovative arrangement raises questions regarding legal ownership of the top structure and the legal recourse available to the parties in the event that there are any changes to the living arrangements. Housing authorities should be focused on designing flexible legal frameworks to accommodate evolving forms of housing tenure. Existing institutional frameworks only reflect the practices of established housing markets and not the needs of the nascent housing market amongst lower income households.

With the dearth of housing supply in South Africa, promoting small scale landlord-ism is an attractive solution to addressing the housing problem⁷⁵. The pension-secured loan, which admirably serves the home improvement and self-build market, could play a pivotal role in financing rental accommodation.

In terms of the current regulations, fund members are not permitted to purchase secondary investment properties using their retirement savings as collateral. As discussed, earlier in this report (see footnote 20), consideration should be given to doing away with this restriction as it potentially closes off an attractive avenue for wealth creation.

Permission To Occupy (PTO)

Historically, it has been a challenge to provide mortgage finance to prospective homeowners operating under a Permission To Occupy (PTO) issued by tribal authorities⁷⁶. Whilst the homeowner is conferred the right to reside on the property and owns the top structure, the land remains the legal possession of the tribal authority. As such, a financial institution cannot register a mortgage bond over the property and is not entitled to claim possession of the property in the event of default.

The pension-backed loan, however, is secured not by the property but a claim over the borrower's retirement savings. The product may prove to be an appropriate vehicle to finance property governed by a PTO. Anecdotal evidence suggests that this mechanism is already in limited use. Raising consumer awareness about this option has the potential to significantly expand this traditional form of home ownership.

⁷⁵ The Shisaka (2006) research found that just under one-third of South Africans (3.5 million households) live in rental accommodation. Of this 1.85 million households rent their accommodation from small scale landlords. Some 60% (1.1 million households) are formally housed, whilst 40% (740 000 households) live in informal dwellings.

⁷⁶ "Permission To Occupy (PTO) (was) issued either by a communal or tribal authority on state land within the former Homelands (in South Africa). PTO's provided the bearer with a recognised right of occupation and utilisation of an identified portion of land but the land remained the ownership of the state. PTO's are not recognised for purposes of security by financial lending institutions. This situation is responsible for low levels of investment by the private sector in such areas...All land holders share the same obligations, including payment of tribal levies and observance of traditional practices. All members enjoy equal access to the communal areas and these rights are not documented. Exclusive rights to residential stands or arable plot cannot be sold and can only be exchanged with the approval of the headman or the chief. Anyone wishing to leave the area may sell any remaining structures to a new occupant, but the new occupant must have the stand allocated to them by the Tribal Authority before taking occupation." – From Mogale (2001) Changes in residential tenure security in South Africa - shifting relationships between customary, informal and formal systems, Draft Paper, April 2001, University of the Witwatersrand's Graduate School of Public and Development Management. Available on http://www.ucl.ac.uk/dpuprojects/drivers_urb_change/urb_infrastructure/pdf_land%20tenure/NAERUS_ESF_Mogale_tenure_security_sth_Africa.pdf

An Alternative to Microloans

Microloans have traditionally been a significant source of home improvement finance in South Africa, with a leading microfinance business confirming that some 30% of loans are used for housing purposes. The pension-secured loan, which is generally more finely priced as it is guaranteed by retirement savings, is a more attractive option than an unsecured microfinance product (see Table 9).

To give more South Africans access to this cheaper source of funding, all contributors to formal retirement funds should be given the opportunity to directly approach loan providers to access a pension-secured loan, without requiring the “approval” of their fund trustees. Trustees’ role insofar as pension-secured loans are concerned should merely be to set the maximum amount that can be borrowed relative to the member’s retirement savings.

A Boost to Home Ownership

The economic downturn has resulted in a tightening of mortgage lending credit criteria. Mortgage lenders are insisting that borrowers contribute a deposit to reduce the loan-to-value (LTV)⁷⁷ ratio in order to qualify for mortgage finance. Reports suggest that mortgage lenders are requesting deposits of between 10% and 20%. With the majority of lower income earners and first-time homebuyers struggling to come up with the deposit, many more South Africans are being excluded from the property market. A pension-secured loan, prudently granted, after assessing the member’s ability to repay, could be an option to assist the homebuyer to access mortgage finance. Once again, however, there is the danger that in the event of default, borrowers stand to lose both their retirement savings and the property.

A variety of product enhancement opportunities have been identified to further expand access to housing. The pension-secured loan is both a useful instrument to facilitate the purchase of traditional housing (e.g. hybrid housing finance) and as an innovative means to develop alternative housing types (e.g. PTO, small scale landlords).

5.7 Awareness and Education

Industry players have bemoaned at length the low levels of awareness about the pension-secured loan product. Market research undertaken in 2008 by a loan provider⁷⁸ revealed that fund members did not know about product features, the availability of the facility and did not understand how the pension-secured loan can facilitate access to housing. This lack of awareness is thought to permeate

⁷⁷ Loan-to-value (LTV) refers to the ratio between the mortgage bond and the assessed value of the property purchased. For example, if the purchase price of a property is R 100 000 and the purchaser contributes R 20 000 as a deposit, then the mortgage bond of R 80 000 would be at an 80% LTV.

⁷⁸ Unfortunately, this research is not publically available.

throughout the housing value chain, and is seen as a key factor in limiting the growth of the sector.⁷⁹

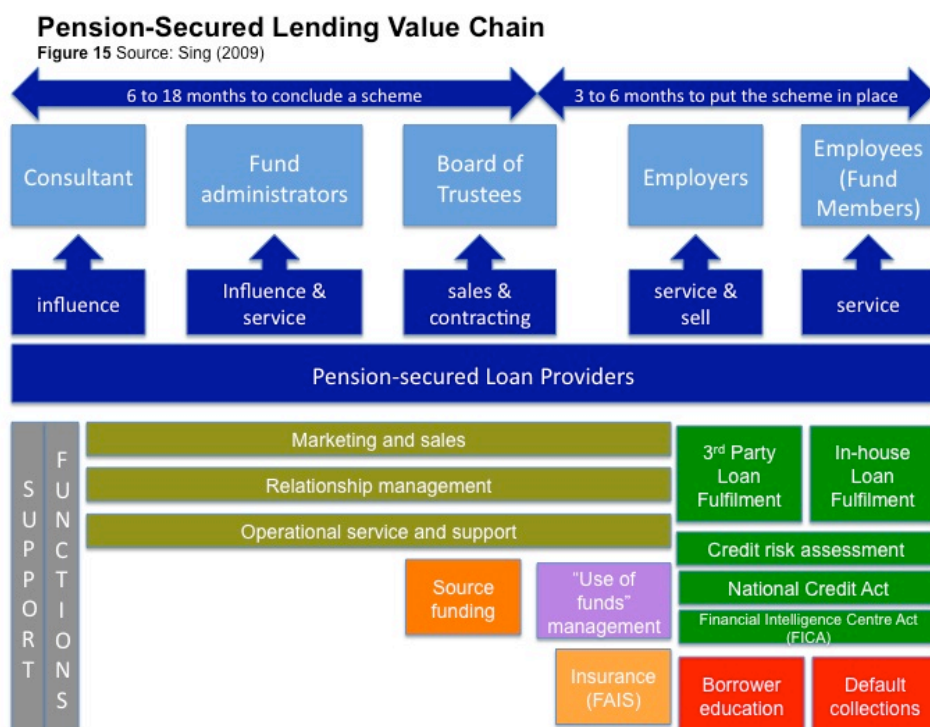
Another aspect of the pension-secured loan not well understood is the risk to fund members' retirement savings in the event of default.

In addition, providing potential consumers with the appropriate product and pricing knowledge empowers potential borrowers to make more informed choices, addresses the prevailing information asymmetry in the market and ultimately enhances the borrower's negotiating power.

The importance of creating public awareness about the product appears to be gaining momentum. Several interviewees mentioned that they would be launching a proactive communications campaign, as well as more targeted initiatives at the workplace directed at fund members. The format of the communication will be in the form of generic consumer education, augmented subsequently with more specific borrower information.

5.8 Escalating Costs - Administrative and Operational Challenges

The pension-secured value chain is fraught with complexity and potential inefficiencies. (Figure 15) This section will highlight areas of escalating costs along the value chain that potentially have implications for the pricing of loans.



⁷⁹ This view is partially supported in research (albeit dated) undertaken by the National Housing Finance Corporation (NHFC) in 2003. This study found that only some 30% of respondents were aware that retirement savings can be used to guarantee a housing loan and that only 8% had actually taken up a loan using their retirement savings as collateral. Comber (2005) highlights that these low levels of product take-up highlight potential opportunities to expand the pension-backed loan market.

Marketing to the Fund

The marketing process is usually initiated by the loan provider targeting a retirement fund that is:

- Providing direct loans to its membership.
- Using the services of another third-party loan provider to offer pension-secured loans to their members.
- Not currently offering a housing finance benefit to its members.

Lenders need to establish solid relationships with influential trustees and the fund's advisors (e.g. fund administrators, consultants).

The marketing and sales process acquiring the loan business can be a protracted one, taking up to between 6 to 18 months before the final decision to establish the loan scheme is ratified.

The long marketing timeline and vagaries of the decision making process add unnecessary costs for relatively little value-add for the fund member. If anything, loan providers may be inclined to price in the marketing costs into the final interest rate. Allowing fund members the freedom to choose their loan provider without the need for the board of trustees' approval facilitates access to housing finance.

Contracting and Establishing Operational Processes

To initiate the pension-secured loan scheme for fund members, multiple contracts have to be concluded between:

- *Retirement fund and the loan provider* - The loan provider agrees to extend a globular loan facility to the retirement fund. In return, the fund provides a financial guarantee to the loan provider warranting that the fund will make good any outstanding amounts in the event of default.
- *Loan provider and the fund administrator* – The administrator agrees to earmark fund members' retirement savings as security for loans and undertakes to repay the outstanding liability should a member retire or resign from the fund.
- *Loan provider and the employer* - Employers undertake to deduct the repayment amount from the members' salary and to pay the proceeds over to the loan provider.⁸⁰

Retirement funds that already have a direct loan operation in place or who are switching the loan facility from another third-party loan provider have to authorise cession of the existing loan book to the newly appointed loan provider. The National Credit Act (NCA) requires each loan to be re-evaluated from a credit risk perspective.⁸¹ This entails up-to-date personal and financial information being obtained from existing borrowers.

⁸⁰ For umbrella funds, a separate contract has to be concluded with each participating employer. In the case of municipal funds, contracts have to be signed with each municipality.

⁸¹ Newly appointed loan providers have cited instances of delaying tactics being employed by the existing loan provider. In order to continue earning interest revenue, existing loan providers will "lose" loan documentation, be unable to provide settlement figures and throw up various forms of bureaucratic hurdles to delay the transfer of loans.

Lenders point to this phase taking between 3 and 6 months to complete.

Allowing fund members the freedom to choose a loan provider and introducing regulation that does away with the need for multiple contracts to be concluded would reduce origination and management costs.

Distribution and Loan Fulfilment

For loan providers, the challenge of introducing comprehensive but cost effective distribution channels remains a high priority. The traditional distribution channel for pension-secured housing loans is via the employer.

Employers typically fund the resources involved in the loan application and management process. For example, some large companies have a dedicated payroll resource attending to loan administration and processing. With pressures on operating margins, offering this service to employees is viewed as non-core to the business and have not played a role in actively marketing loans to employees.

Consequently, loan providers have increasingly taken on the role of communicating and marketing to fund members, as well as the loan application process. Loan providers have also established in-house loan fulfilment capabilities, e.g. call centres.⁸²

The loan application process is heavily influenced with the need to comply with the Financial Intelligence Centre Act (FICA)⁸³ and the National Credit Act (NCA).

The advent of the NCA has brought about a welcome and heightened era of responsible lending (and borrowing) in the industry. There is a view, however, that historically responsible lenders have introduced additional measures to ensure compliance, resulting in increased administration and higher associated costs, whilst those loan providers who have traditionally flouted the tenets of responsible lending continue to exploit borrowers. Time will tell what the net effect of this piece of legislation will be.

Some loan providers have outsourced the loan fulfilment function. This has added costs to operations⁸⁴ and required additional management resources⁸⁵. Others have chosen to leverage off their extensive retail distribution networks. For example, banks are encouraging fund members to apply for pension-secured loans at their

⁸² With NCA having put more responsibility on loan providers, a lender has created an internal loan origination team, which charges R 100 per application. The borrower has the option of capitalising the fee or paying it together with their first instalment. By the loan provider's own admission, this fee does not cover costs, as the team members have to be given cars, laptops, printers and enjoy the benefits of being full-time staff members. To address the challenges of servicing remote areas, a pre-approval system is in place to vet applicants prior to making contact with them.

⁸³ Compliance with FICA requirements to obviate money laundering, necessitates the gathering, verification and storing of documents which verify the borrower's identity and place of residence.

⁸⁴ Loan fulfilment operations have had to establish adequate, national coverage for metropolitan and rural areas, and have to provide the service whether there is one applicant or a thousand applications, precluding them from benefitting from economies of scale.

⁸⁵ Sub-contracted loan fulfilment activities have had to be closely managed as poor service standards and lack of delivery has resulted in reputational risk (and even loss of business) for some loan providers.

proprietary outlets. Optimising on existing infrastructure reduces the cost of distribution. However, some loan providers have pointed out that the cost of systems enhancements to enable branch staff to be able to assist borrowers could increase the cost of loan fulfilment.

To reduce the cost of loan fulfilment, it has been suggested that retirement fund administrators be obliged to perform this function. There are several reasons why this approach would not reduce costs.

- The processing of pension-secured loan applications falls outside the scope of what is normally undertaken by fund administrators and they would, therefore, not have the infrastructure or resources to perform these functions without some investment in infrastructure.
- Fund administrators do not benefit from interest revenues flowing from loans. There is, thus, no incentive for them to perform this function unless they can charge for it.
- Even fund administrators who have loan providers within the same organisational stable, operate the businesses as separate revenue-generating units (giving rise to intra-organisational, nominal cross charges) and as areas with fundamentally different skills, systems and resources.
- Fund administrators cannot compete with loan providers with extensive retail distribution networks.

In summary, no doubt fund administrators could build the capacity to perform the loan fulfilment function but the set-up costs would ultimately have to be borne by the fund members.

Indications are that most loan providers will be adopting a hybrid distribution and loan fulfilment model that is a combination of using employer resources, outsourcing of the function to third-party suppliers and leveraging off existing distribution networks. Loan providers are acutely aware that in an environment where the pension-secured loan competes with a wide array of alternative housing finance options, consumer-centricity⁸⁶, which focuses on bringing the product closer to the client, in the most convenient way, is the primary means of consolidating customer relationships and to optimise profitability.

Default Collections

The original low-cost, business model for pension-secured loans was premised on cost effective default collections. Fewer resources are required to execute default collections as the loan is secured by fund members' retirement savings and guaranteed from the fund. Should borrowers default, the remedy would simply be to call on the fund to repay the loan from the borrower's retirement savings.

Of late, boards of trustees have demanded that loan providers exhaust all avenues of recovery with individual borrowers, before calling on upon the fund guarantee. While this may be a laudable effort to protect members' retirement savings, for loan

⁸⁶ Presently, the loan application process takes between 10 to 21 days before actual disbursement of the loan proceeds takes place. A commitment to consumer-centricity would require a dramatic reduction in this timeline.

providers, instituting default collections procedures with multiple individuals is more expensive than approaching a single guarantor to honour their commitment.

Loan providers thus have to weigh up the costly pursuance of defaulting borrowers on an individual basis, against simply calling upon the fund to honour their guarantee and to risk undermining the relationship with the board of trustees. Trustees and employers could be called upon to assist in recovering the outstanding amounts but there is often neither the incentive nor the experience to effect default collections. There is no simple solution. Legally and contractually, the fund is obliged to repay the outstanding obligation. Loan providers, if compelled to affect this fundamental change to the business model will have to recoup costs by adjusting the overall pricing of pension-secured loan schemes.

Two of the larger loan providers interviewed report that their current bad debt experience is very low, ranging between 0.1% and 0.2%, compared to an industry average of 2%. For the time being, therefore, the low levels of bad debts indicates that there no imminent increase in the cost of risk is anticipated.

There are reports, however, from these same loan providers that they are noticing an escalation in financially distressed borrowers (increasing numbers of administration orders⁸⁷ in place and more individuals undergoing the debt counselling⁸⁸ process). For loan providers, this development warrants careful observation as circumstances deteriorate quickly.⁸⁹

Loan providers cite operational and process challenges as their greatest obstacle to streamlining the pension-secured loan value chain. The concern is that escalating operational and administrative costs will ultimately impact on the borrower. Organisations with the most robust and cost effective operational competencies will flourish.

⁸⁷ If a person is unable to pay their debts (subject to the total debts not exceeding an amount prescribed by law and the individual not having sufficient income or attachable assets to pay such debts), s/he can apply for an Administration Order. The Order temporarily protects the individual from legal proceedings by their creditors. The court decides how much is needed for basic necessities and appoints an administrator to collect surplus income, who, in turn, distributes it on a *pro rata* basis at least once a quarter to creditors.

⁸⁸ The National Credit Act allows over-indebted consumers to approach debt counsellors whose role is to review the credit obligations of every application to assess whether the credit agreements entered into were reckless and/or whether the debt of the consumer should be restructured to make it more affordable. Debt Counselors negotiate restructuring proposals on behalf of over-indebted consumers with credit providers.

⁸⁹ A loan provider relayed a story that puts a spin on a potential “moral hazard” concerning default in the industry. A fund member defaulted on his loan repayment. At the loan provider’s request, the trustees agreed to settle the outstanding amount using the member’s retirement savings. Other fund members with loans and experiencing financial pressure got to hear about this and threatened to go on strike unless the trustees settled their liabilities from their retirement savings. To prevent industrial action, their demands were acceded to (with the regulator’s approval). – This is the only incident of this nature that was shared. However, the real concern is that borrowers, when experiencing financial distress, abandon rational decision-making relating to their retirement savings.

5.9 The Impact of the Global Economic Downturn of Retirement Savings

“...the decline in the All Share Index of around 30% since January 2008 means that some PBLs may be ‘under water’ to borrow a phrase from the mortgage market. Aside from triggering a reassessment of the value of existing guarantees and a revision of loan to market value ratios, given that the value of the underlying assets backing the guarantee has declined the value of loans will decline in tandem.” (Eighty20, 2009b)

The global economic downturn, specifically the significant erosion of value in equity market investments, has raised questions regarding the impact on retirement savings. A recent study (Eighty 20, 2009b) infers that the value of the collateral (i.e. the retirement savings) securing pension-backed loans has diminished in line with plummeting share prices.

This line of thinking, at this juncture, overstates the threat for the following reasons:

- i. Loan providers believe that the net negative effect on retirement savings has only been in the region of 10% - 12%. The muted impact is attributed to Regulation 28 of the Pension Funds Act, which regulates the investment asset classes of retirement funds. These parameters which err on the conservative, limits retirement funds' exposure to market volatility.
- ii. Lower income fund members generally have very limited investment choice and have not been exposed to the magnitude of market volatility that high net worth individuals, who have been able to choose more risky investments, may have been exposed to.
- iii. Retirement fund members continue to contribute to the fund (through good times and bad), resulting in any equity shocks or volatility being smoothed out over the longer term.
- iv. Loan maxima generally hover around 70% to 80% of accumulated savings. Therefore, even if the security value is eroded, there is sufficient coverage relative to the loan amount.

Barring a massive depreciation in equity market values or significant downward adjustments to other investment asset classes, at an aggregate industry level, there is no threat of imminent or catastrophic risk to the value of collateral underlying pension-secured loans in the short-term.

In isolated cases, however, there may remain some risk at an individual borrower or individual fund level. Individual borrowers whose outstanding loan may exceed the collateral value of the retirement savings, would in most instances, simply continue to repay the loan. Only in the event of the borrower being unable to effect monthly repayments (for example, due to loss of employment or over-indebtedness) would fund trustees be requested to release the retirement savings to settle portion of the loan. In the normal course, arrangements would then be made with the borrower to repay the remaining liability. It is difficult to quantify the magnitude of the shortfall as it is dependent on individual circumstances. However, given that the original loan amount would only be some percentage (on average, 70%) of the retirement savings amount and that there is only a small likelihood of the accumulated savings being severely depleted, then the shortfall should be minimal. If the fund member is unable to repay the shortfall, s/he runs the risk of having an impaired credit record, which jeopardises the chances of accessing finance in the future.

Without a crystal ball in these turbulent times, it is difficult to predict the impact of the economic downturn on the value of retirement savings. In the short-term, however, there appears to be no significant risk to the pension-secured lending industry's reliance on retirement savings as collateral.

The more likely risk to the pension-secured loan industry is an escalation in loan defaults as a result of mass retrenchments⁹⁰ due to sectoral pressures. With many loan providers having concluded pension-secured loan scheme arrangements with some of the largest mining and automotive industry-based retirement funds, where job losses appear to be most prevalent, the danger of runaway credit losses is not inconceivable. In addition to the threat to the fund of depleting retirement savings to settle defaulting loan obligations, the associated costs of bad debt administration and write-offs will translate into higher average interest rates being charged for pension-secured loans over the longer term.

⁹⁰ "South Africa is on the brink of a "jobs bloodbath". Between 200 000 and 300 000 people stand to lose their jobs this year on top of the more than 112 000 who have already been laid off since November...The losses could push the unemployment rate – pegged at 22% by the government and 40% by various research units – up by "roughly 3%"...The worst-hit sectors are automotive, mining and clothing and textiles." – Rowan Philp (2009) "Jobs Bloodbath", Sunday Times, 29 March 2009.

6. CONCLUSION

The pension-secured lending industry is estimated to be valued at R 17 billion. Reports put potential market growth ranging between R 3.4 billion and R 18 billion. The wide differential in growth estimates can be ascribed to the uncertainty regarding the magnitude of *effective* demand for housing finance in South Africa. Effective demand refers not only to the demand-side dynamics of the affordable housing market (i.e. the number of lower income households wanting to purchase property or wanting to effect home improvements) but incorporates other dimensions that impact on what can actually be achieved. For example, the available supply of affordable housing and housing-related inputs (services infrastructure, land, etc.) and the macroeconomic determinants of households' ability to afford housing finance (e.g. interest rates, inflation).

This study found that the industry, although fundamentally sound, is stagnating in moribund thinking, policies and processes. Chapter 5 summarised the issues and opportunities prevalent in the market, and recommends possible approaches to addressing the challenges.

- The process of appointing a loan provider is said to be lacking in transparency (**conflict of interests**) and fund members precluded from choosing their loan provider of choice (**freedom of choice**). – Amending the regulations to do away with the need for the board of trustees to allow fund members to access pension-secured loans and to select loans providers resolves these issues. Fund members would be able to access housing finance as and when they require it, and would have the freedom to choose loan provider and to negotiate loan terms that suit their personal circumstances.
- The perennial issue of the pricing of pension-secured loans (**interest rate debate**) is examined. The average interest rate charge of Prime minus 1% is found to be reasonable in relation to the loan providers' costs of offering the product. Pension-secured loans are reported as being the least expensive of the housing finance products (compared with mortgage bonds and unsecured personal loans). More crucially from the borrower's perspective, it appears that amongst the largest loan providers, competition for business is fierce, resulting in market-related pricing carrying the day.
- To prevent "leakage" of loan proceeds into non-housing related expenditure requires more stringent regulation (**use of funds management**). However, proactive and positive action to increase awareness of the pension-secured loan as an option to finance housing and to caution fund members against jeopardising their retirement savings by defaulting on their loans (**awareness and education**).
- Loan providers are on the one hand choosing to provide additional levels of service to grow their business and to enhance client relationships (e.g. convenient loan application outlets), and on the other are being compelled to take on more functions by fund trustees (e.g. individual default collections). The pressure on loan providers is to maximise operational efficiency in the face of **escalating costs**.
- Concurrently, to prevent additional costs from simply being passed onto the borrower, regulators (retirement fund and National Credit) should be combining forces to specify what **fees** are allowable and to set the maximum amount that can be charged. Alignment with the existing National Credit Act would be a simple solution to this problem.

- The pension-secured loan can potentially be structured to cater to a myriad of opportunities to meaningfully expand home ownership, self build and home improvement, and rental accommodation for the affordable housing market **(product enhancement)**.

The pension-secured loan product, properly codified by the regulators and innovatively repackaged by loan providers, should retain its place within the array of housing finance products.

The challenge facing the sustainability of the pension-secured loan is that it is a product delicately juxtaposed between the real need for access to housing and governed by first world regulation. It has been positioned as a vehicle to achieve the developmental imperatives of an emerging economy, whilst constrained by an institutional framework that was designed to satisfy more sophisticated tastes. - For example, the pension-secured loan should technically not be used to improve a shack in an informal settlement. It is argued that it is tantamount to trading a future asset (the retirement savings) for a “worthless”, temporary structure⁹¹. However, if the pension-secured loan has helped to provide a family with shelter to survive a bitter winter, should the “use of funds” regulation be strictly enforced? – Prudent regulation emphasises the need to preserve retirement savings for fund members’ old age. However, what is the use of being assured of a comfortable retirement without a roof over one’s head today? – Unless the regulatory, institutional and operational structures governing pension-secured lending are adapted to meet the real housing finance needs of the community, it is destined to remain a niche product, unable to achieve its true potential as a mechanism to expand access to housing.

The impact of the global financial downturn on the pension-secured lending industry is of greater (and more immediate) concern and far less easy to predict or solve. There is a possibility that with funding at a premium, profit margins extremely thin and the spectre of higher credit risk due to looming job losses, loan providers may choose to severely curtail their lending activities or more drastically (but less likely) to exit the industry altogether. From a housing access perspective, this would prove to be a significant setback, putting the brakes on the momentum generated by the Financial Sector Charter.

⁹¹ The rationale is that the borrower does not have legal title over the property and because the structure is not of a permanent nature, it is perceived as having no tradable value.

REFERENCES

Asher, M.G. (1999), The Pension System in Singapore, Social Protection Discussion Paper Series, No. 9919, Social Protection Unit, Human Development Network, The World Bank, August 1999.

Cameron, B. (2009a), Administrator to oppose paying back secret profits, Saturday Star Personal Finance, 17 January 2009.

Cameron, B. (2009b), NBC, funds still in talks over R200m payback, Saturday Star Personal Finance, 17 January 2009.

Chirchir, S.L. (2006), Promoting Home Ownership Using Retirement Benefits, Kenyan Retirement Benefits Authority, Research Paper Series 01/2006, June 2006. Available on the website www.rba.go.ke

Comber, L. (2005), An Analysis of the Housing Finance Industry in Lower Income Groups in South Africa, Focusing on Pension Backed Lending as a Potential Solution to the Credit Gap Problems. Research project submitted to the Gordon Institute of Business Science, University of Pretoria, November 2005.

Eighty20 (2006), How Low Can You Go? Charting the Housing Finance Access Frontier: A Review of Recent Demand and Supply Data, research undertaken on behalf of FinMark Trust, 25 April 2006.

Eighty20 (2007), Access to Housing Finance in the Financial Sector Charter Target Market, research undertaken on behalf of FinMark Trust, August 2007

Eighty20 (2009a), Access to Housing Finance in South Africa – February 2009, research undertaken on behalf of FinMark Trust. Slide presentation given on 4 February 2009.

Eighty20 (2009b), Access to Housing Finance – Considering the Next Phase of the FSC Targets, research undertaken on behalf of FinMark Trust, March 2009.

Financial Services Board (1997), Pension Funds Act, 1956: Housing Loan Administration, Circular PF No.92, September 1997

Financial Services Board (2008), FSB Annual Report 2008

Government Employees Pension Fund (2008) Government Employees Pension Fund – 2007/2008 Annual Report. Available on www.gepf.gov.za

McCarthy, D., Mitchell, O.S. and Piggott, J. (2001) Asset Rich and Cash Poor: Retirement Provision and Housing Policy in Singapore, Pension Research Council, The Wharton School, University of Pennsylvania, May 2001

Moodley-Isaacs, N. (2008), Act sets out how your fund may help you with a home loan, Personal Finance, 20 September 2008. Available on <http://www.persfin.co.za>

Ntingi, A. (2008), Pension Fund Scheme Shocker, City Press, 8 June 2008

Pension Funds Act No. 24 of 1956

Rust, K. (2006), Analysis of South Africa's Housing Sector Performance, report prepared for FinMark Trust, December 2006

Shisaka Development Management Services (2006), Small Scale Landlords, research undertaken on behalf of FinMark Trust, 2006

Singapore Department of Statistics (2005), Home Ownership and Equity of HDB Households 2003, www.singstat.gov.sg, October 2005

South African Legal Information Institute (SAFLII) (2008), HomePlan (Pty) Ltd - Submission to the Competition Tribunal case No. 4/LM/JAN08, document available on <http://www.saflii.org/za/cases/ZACT/2008/17.html>

Tomlinson, M.R. (1998), Mortgage Bonding? South Africa's Financial Institutions and Low-Cost Housing Delivery, Housing Finance International, June 1998, Volume 12, Issue 4, pp.3-7.

Tomlinson, M.R. (2005), South Africa's Financial Sector Charter: Where From, Where To?, Housing Finance International, December 2005

LIST OF INTERVIEWEES AND ADVISORS

Interviewee	Designation	Organisation	Date of Interview
Jurgen Boyd	Deputy Executive Officer: Pensions	Financial Services Board	7 October 2008
Corlia Buitendag	HOD: Pension Surveillance and Enforcement	Financial Services Board	2 October 2008
Stephanus Burger	Head of Homeplan	Alexander Forbes	29 October 2008
José Da Fonseca	Divisional Manager for Business Development	NBC Home Loans	27 February 2009
James De Smidt	National Marketing Manager – Pension Backed Lending	Standard Bank of South Africa	Telephonic discussion
Allan Greenblo	Editor	Today's Trustee	18 November 2008
Michael Gresty	Head of Research: Financials Analyst	Deutsche Bank	Telephonic discussion on 14 October 2008
Jeff Lawrence	Head of Affordable Housing	Nedbank	Telephonic discussion on 13 March 2009
Illana Melzer	Director	Eighty20 Consulting	Telephonic and e-mail discussions – October 2008, January 2009 and February 2009
Esh Naidoo	Head - Pension Backed Lending	Standard Bank of South Africa	18 September 2008
Glenn Pratt	Pension backed lending practitioner	Standard Bank of South Africa	16 September 2008
Peter Standish	Product Owner	First National Bank	October 2008
Pierre Venter	Housing Co-ordinator	Banking Association South Africa	23 September 2008 and subsequent discussions
Pieter Vorster	General Manager – Home Loans Operations and Production, and Pension Supported Housing Loans	Absa Bank	17 September 2008

A special word of appreciation to the Retirement Fund Trustees who agreed to be interviewed and who contributed invaluable to this study but who preferred to remain anonymous.