

The Private Affairs of Public Pensions in South Africa

Debt, Development and Corporatization

Fred Hendricks



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Acronyms

AIDS	acquired immunodeficiency syndrome
ANC	African National Congress
APF	Administradoras de Fondos de Pensiones (<i>Pension Fund Administrators</i>), Chile
BEE	Black Economic Empowerment
BIG	Basic Income Grant
CENDA	Centro de Estudios Nacionales de Desarrollo Alternativo (<i>Centre for National Studies in Alternative Development</i>)
COSATU	Congress of South African Trade Unions
FEDUSA	Federation of Unions of South Africa
FF	fully funded
GDP	gross domestic product
GEPF	Government Employees Pension Fund
HIV	human immunodeficiency virus
NAPTOSA	National Professional Teachers' Organization of South Africa
NEDLAC	National Economic and Labour Council
NEPAD	New Partnership for Africa's Development
PAYG	pay-as-you-go
PDC	Public Debt Commissioners
PIC	Public Investment Corporation (since April 2005), Public Investment Commissioners (until April 2005)
R	rand
RDP	Reconstruction and Development Programme

Summary/Résumé/Resumen

Summary

Toward the end of its rule, the apartheid government in South Africa converted its contributory pension system for employees in the public sector from one that effectively functioned as a pay-as-you-go (PAYG) scheme to a fully funded scheme. This paper explains the reasons behind this change and reveals its contemporary consequences within the context of the enormous development challenges facing South Africa, and the inadequacy of the social policy responses of the democratic government. The most far-reaching effect of the adoption of a fully funded pension scheme is that it led directly to a dramatic increase in national debt, as the public servants of the previous regime consciously indebted the state in order to safeguard their own pensions and retrenchment packages in retirement. In 1989 the total debt of the South African government stood at 68 billion rand (R), of which R66 billion was domestic debt and only R2 billion was foreign. By 1996 it had grown phenomenally to R308 billion, of which R297 billion was domestic and R11 billion was foreign debt. The servicing costs for these debts rose from about R12 billion in 1989 to more than R30 billion per annum in 1996. During the same period, the assets of the Government Employees Pension Fund (GEPF) grew from R31 billion to R136 billion.

Unlike other indebted governments, the major portion of national debt in South Africa is internal rather than external. In effect, the government is indebted to itself through the fully funded pension system, as the transition from a PAYG system to a fully funded one implied that former contributions to the public pension schemes had to be securitized via government bonds that were deposited in the newly created pension fund. Furthermore, contributions of current employees were directed into the pension fund while current pensions had to be financed out of the budget. This costly transition had detrimental implications for social investment, especially in the areas of education, health and welfare.

This paper argues that the policy choices in respect of the pension system have profoundly shaped the overall economic prospects of the country. In so far as the levels of inequality in South Africa pose the greatest threat to the democracy, these policy choices have had contradictory effects. On the one hand, a progressive agenda involving social spending and dealing with poverty through non-contributory public pensions has certainly benefited many poverty-stricken black South Africans. On the other hand, the fully funded system of contributory pensions for workers in the state sector has had the dual effect of entrenching the deals made with senior public officials of the apartheid government, as well as enriching a very small group of black entrepreneurs who have profited directly from the centralized asset management of public pension funds. There is an inconsistency between solving the problems of poverty and the stated commitment to developing a black capitalist class which, through Black Economic Empowerment, could make inroads into the white stranglehold of ownership and privilege. It is crucial for the government to negotiate this tension in a manner that allows for social policies that encourage economic growth while simultaneously maintaining the social imperative of redistribution. The exigencies of legitimacy and consent demand the latter: in South Africa, precisely because of the extent of inequality and the manner in which the differentiation between rich and poor continues to correspond with the division between black and white, redistribution is all the more urgent.

In broad terms, this paper deals with the interconnections between public debt, contributory pensions in the public sector, the corporatization of the management of these public funds, the contradictions of Black Economic Empowerment, and the failure of South African social policy in respect of contributory public pensions to deal more comprehensively with its development challenges.

The paper starts by describing the political and institutional evolution of South African pension schemes with a special focus on the reform of contributory public pension schemes toward the

end of apartheid. It goes on to examine the governance structure of the pension system in order to establish whether it is transparent and accountable, while ensuring that the pension system is able to pursue its main roles of social protection, redistribution and contribution to economic development and social cohesion. In particular, the paper investigates the institutions that serve public pensions, such as the GEPP and the Public Investment Corporation (PIC). There can be little doubt that the PIC opens up possibilities for accomplishing social goals through an appropriate investment strategy. However, its recent corporatization pushes it toward privatization. While the PIC is still wholly owned by the state, it is an entity that formally exists outside of the public sphere and therefore beyond its oversight. Finally, the paper analyses the investment policy of the public pension fund, paying special attention to whether this fund has been invested to build economic and social infrastructure.

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Résumé

Vers la fin du régime d'apartheid, le gouvernement sud-africain a converti son régime de retraite pour les employés du secteur public, qui était financé par des cotisations et fonctionnait en réalité comme un régime par répartition, en un système par capitalisation totale. L'auteur de ce document explique les raisons de ce changement et expose les conséquences qu'il a actuellement, à un moment où l'Afrique du Sud est confrontée à d'immenses problèmes de développement et où la politique sociale du gouvernement démocratique n'y apporte que des réponses insatisfaisantes. L'effet direct le plus grave a été la hausse spectaculaire de la dette nationale car les fonctionnaires de l'ancien régime ont délibérément endetté l'Etat pour préserver leur retraite et les arrangements conclus pour leur départ à la retraite. En 1989, la dette totale du gouvernement sud-africain s'élevait à 68 milliards de rand (R), dont R66 milliards de dette intérieure et seulement R2 milliards de dette extérieure. En 1996, elle avait explosé et atteignait R308 milliards, dont R297 milliards de dette intérieure et R11 milliards de dette extérieure. Les coûts du service de ces dettes sont passés d'environ R12 milliards en 1989 à plus de R30 milliards par an en 1996. Pendant la même période, les actifs du Fonds de pension des employés du gouvernement (Government Employees Pension Fund – GEPP) sont passés de R31 milliards à R136 milliards.

A la différence d'autres gouvernements endettés, la majeure partie de la dette nationale sud-africaine est intérieure et non extérieure. En fait, le gouvernement a une dette envers lui-même à cause du système de retraite par capitalisation totale car le passage d'un régime par répartition à un système par capitalisation a obligé à sécuriser les cotisations déjà versées aux régimes de retraite publics par des obligations d'Etat déposées dans le fonds de pension nouvellement créé. De plus, les cotisations des employés en service ont alimenté le fonds de pension alors que les retraites devaient être financées par le budget. Cette coûteuse transition a nui aux investissements sociaux, en particulier dans les domaines de l'éducation, de la santé et de l'aide sociale.

L'auteur fait valoir que le régime de retraite choisi a eu de lourdes conséquences pour les perspectives économiques générales du pays. Rien ne menaçant plus la démocratie en Afrique du Sud que l'inégalité, ce choix politique a eu des effets contradictoires. D'un côté, un programme progressiste alliant dépenses sociales et lutte contre la pauvreté par des retraites publiques non financées par des cotisations a certainement été bénéfique pour de nombreux Sud-Africains noirs et pauvres. De l'autre, le système contributif des retraites par capitalisation totale pour les employés de l'Etat a eu un double effet, celui de pérenniser les accords conclus avec les hauts fonctionnaires du gouvernement de l'apartheid, et d'enrichir un très petit groupe d'entrepreneurs noirs qui ont profité directement de la gestion centralisée des actifs des fonds de pension publics. Il y a une incohérence entre l'action menée pour régler les problèmes de pauvreté et la volonté déclarée de développer, par une politique d'autonomisation économique des Noirs (Black Economic Empowerment), une classe de capitalistes noirs qui fasse son entrée dans le cercle, jusque-là réservé aux Blancs, des

propriétaires et des privilégiés. Il est crucial que le gouvernement navigue entre ces deux pôles de manière à ce que ses politiques sociales favorisent la croissance économique sans négliger pour autant l'impératif social de redistribution. Celle-ci est nécessaire pour la légitimité et l'acceptation des politiques gouvernementales et d'autant plus urgente que les inégalités restent considérables et que la différenciation entre riches et pauvres coïncide toujours avec la division entre Noirs et Blancs.

En termes généraux, l'auteur traite des relations entre la dette publique, le régime contributif des retraites dans le secteur public, la transformation de ces fonds publics et leur gestion en sociétés, les contradictions de la politique d'autonomisation économique des Noirs, et l'incapacité de la politique sociale sud-africaine en matière de retraites publiques contributives à s'attaquer pleinement aux problèmes de développement.

L'auteur commence par décrire l'évolution politique et institutionnelle des régimes de retraite sud-africains en accordant une attention particulière à la réforme des régimes contributifs publics vers la fin de l'apartheid. Il examine ensuite la gouvernance du système des retraites afin d'établir si elle est transparente et responsable et veille en même temps à ce que le système des retraites puisse remplir ses principales fonctions de protection sociale, de redistribution et de contribution au développement économique et à la cohésion sociale. Il enquête en particulier sur les institutions qui versent les pensions publiques telles que le GEPF et le Public Investment Corporation (PIC). Il n'y a guère de doute que le PIC pourrait permettre la réalisation d'objectifs sociaux par une stratégie de placements adéquate. Cependant, sa constitution récente en société commerciale le pousse dans le sens de la privatisation. Si le PIC est encore propriété de l'Etat à 100 pour cent, il se situe, par sa forme, hors de la sphère publique, de sorte qu'il échappe à son contrôle. Enfin, l'auteur analyse la politique de placements du fonds public de pensions en se demandant en particulier si les actifs ont été investis dans la construction de l'infrastructure économique et sociale.

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Resumen

En las postrimerías de su mandato, el gobierno del apartheid cambió su sistema de pensiones contributivas para los empleados del sector público sudafricano, al pasar de un sistema que funcionaba en la práctica como un sistema de reparto a un esquema plenamente financiado. En el presente trabajo se explican las razones de este cambio y se dan a conocer las consecuencias contemporáneas de tal medida en el contexto de los enormes desafíos de desarrollo que enfrenta Sudáfrica, así como lo inadecuado que resultan las políticas sociales con las que ha respondido el gobierno democrático. El efecto más transcendental de la adopción de un esquema de pensión plenamente financiado es que condujo directamente a un incremento marcado de la deuda nacional dado que los funcionarios públicos del régimen anterior conscientemente endeudaron al Estado a fin de salvaguardar sus propias pensiones y paquetes de liquidación para su jubilación. En 1989, la deuda total del gobierno sudafricano ascendía a 68 mil millones de rand (R), de los cuales R66 mil millones correspondían a deuda interna y apenas R2 mil millones a deuda externa. Para 1996, la deuda se había disparado a R308 mil millones, de los cuales R297 mil millones eran deuda interna y R11 mil millones deuda externa. Los costos de servicio de estas deudas aumentaron de cerca de R12 mil millones al año en 1989 a más de R30 mil millones en 1996. Durante el mismo período, los activos del Fondo de Pensiones de los Empleados Públicos (GEPF, por sus siglas en inglés) incrementaron de R31 mil millones a R136 mil millones.

A diferencia de otros gobiernos endeudados, la mayor porción de la deuda nacional de Sudáfrica es interna más que externa. En efecto, el gobierno se endeudó consigo mismo a través del sistema de pensiones plenamente financiado, ya que la transición del sistema de reparto a un sistema de pensiones plenamente financiado implicaba que las antiguas contribuciones al sistema público de pensiones tenían que garantizarse con la emisión de bonos públicos que se

depositaban en el fondo de pensiones recientemente creado. Además, las contribuciones de los empleados actuales se dirigían hacia el fondo de pensiones, mientras que las pensiones actuales tenían que ser financiadas con recursos del presupuesto. Esta costosa transición tuvo consecuencias perniciosas para la inversión social, en particular en las áreas de educación, salud y previsión.

Este trabajo argumenta que las decisiones que se tomaron con respecto al sistema de pensiones han afectado profundamente las perspectivas económicas generales del país. En la medida en que los niveles de desigualdad en Sudáfrica representan la mayor amenaza para la democracia, estas decisiones han tenido efectos contradictorios. Por una parte, no cabe duda de que la adopción de una agenda progresista que contempla gasto social y se ocupa de la pobreza a través de pensiones públicas no contributivas ha beneficiado a muchos sudafricanos negros sumidos en la pobreza. Por la otra, el sistema plenamente financiado de pensiones contributivas para los trabajadores del sector público ha tenido el doble efecto de consolidar los arreglos alcanzados con altos funcionarios públicos del gobierno del apartheid y enriquecer a un grupo muy pequeño de empresarios negros que han sacado provecho directamente de la administración centralizada de activos de los fondos públicos de pensión. Existe una incongruencia entre la resolución de los problemas de la pobreza y el compromiso enunciado de desarrollar una clase capitalista negra que, a través del empoderamiento económico negro, pudiera penetrar el dominio de los blancos sobre las propiedades y los privilegios. Es crucial que el gobierno negocie esta tensión de una manera que permita ejecutar políticas sociales que fomenten el crecimiento económico al mismo tiempo de mantener el imperativo social de la redistribución. Las exigencias de la legitimidad y el consentimiento requieren esto último. En Sudáfrica, precisamente debido al grado de desigualdad y la forma en que la diferenciación entre ricos y pobres continúa correspondiendo con la división entre blancos y negros, la redistribución se hace todavía más urgente.

En términos generales, este documento se ocupa de las interconexiones entre la deuda pública, el sistema de pensiones contributivas en el sector público, la corporatización de la gestión de estos fondos públicos, las contradicciones del poder económico negro y el fracaso de la política social sudafricana con respecto a las pensiones públicas contributivas para responder más cabalmente a los desafíos de desarrollo del país.

El documento comienza con la descripción de la evolución política e institucional de los planes de pensión en Sudáfrica, con especial énfasis en la reforma del sistema público de pensiones contributivas a finales del régimen del apartheid. Seguidamente se examina la estructura del sistema de pensiones a fin de establecer su transparencia y rendición de cuentas, y asegurarse de que está en capacidad de cumplir sus funciones principales de protección social, redistribución y contribución al desarrollo económico y la cohesión social. Este documento investiga en particular las instituciones que manejan las pensiones públicas, como el GEPF y la Corporación Pública de Inversiones (PIC, por sus siglas en inglés). No cabe duda de que la PIC ofrece posibilidades para alcanzar los objetivos sociales por medio de una estrategia de inversión apropiada. Sin embargo, su reciente corporatización la empuja hacia la privatización. Si bien la PIC sigue estando en manos del Estado, es una entidad que existe formalmente fuera de la esfera pública, lo que la ubica fuera de su ámbito de supervisión. Finalmente, el documento examina la política de inversión del fondo público de pensiones, con especial atención a si dicho fondo ha sido invertido en la creación de infraestructura económica y social.

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We are limited in South Africa because our democratic Government inherited a debt which at the time we were servicing at the rate of 30 billion rand a year. That is thirty billion we did not have to build houses, to make sure our children go to the best schools, and to ensure that everybody has the dignity of having a job and a decent income.

Nelson Mandela (ACTSA 2002)

The first charge against government revenue is interest on government debt. The bigger our deficit, the more we have to borrow, the higher the interest bill and the less money there is available to invest in social development, in poverty relief and in the development of our human resources.

Trevor Manuel, finance minister (1997)

The bulk of our debt is the domestic debt of ordinary South Africans through the public pension funds.

Trevor Manuel, finance minister (1999)

1. Introduction

Toward the end of its rule, the apartheid government converted its contributory pension system for employees in the public sector from one that effectively functioned as a pay-as-you-go (PAYG) to a fully funded (FF) scheme. This paper seeks to explain the reasons behind this change and to understand its contemporary consequences. It does this within the context of the enormous development challenges facing South Africa and the inadequacy of the social policy responses of the new democratic government. Conceptually, the paper is located within a new trend in development thinking, one that asserts an intrinsic role for the social policies of the state in the development process. In so doing, this approach seeks to shake social policy loose from its moorings to the remedial action associated with the discipline of social work. Instead, it proposes that social policy should encompass a fully fledged developmental and redistribution agenda.

South Africa is currently one of the most unequal countries in the world. The poorest 20 per cent of the population earns a mere 1.7 per cent of total income while the richest 20 per cent earns 72.5 per cent, and the Gini coefficient has grown steadily to reach 0.685 by 2006 (Presidency, RSA 2007:23–24). Inequality is increasing along a wide range of indicators, both among apartheid-defined racial categories and within them. Since the democratic transition in 1994, the benefits of black economic empowerment and affirmation action measures have allowed a significant proportion of previously disenfranchised blacks to change the pattern of social stratification of the managerial and upper classes. However, the main problem confronting the country today remains the problem of black poverty. This is the principal challenge, and the success or failure of social policies for development needs to be assessed against the extent to which they meet it. The costs of the decision to retain the fully funded pension system in South Africa will be considered in this context.

The end of apartheid had a very significant effect on the provision of public non-contributory and contributory pensions. In respect of the former, over a period of merely one decade, there was a dramatic increase in the number of recipients of social pensions and other grants (van der Merwe 2004:312). Non-contributory pensions form a crucial component of the welfare and social security policies of the state because they represent a substantial transfer of state funds to the poor and contribute directly to the well-being of South Africans. Currently, the means tested old age grant of R870¹ per month to those unable to sustain themselves is often the difference between survival and utter destitution. Many families, especially those in rural areas, are heavily dependent on these pensions as a sole source of income, and there can be little doubt that access to pensions has had a substantial influence on levels of poverty. Needless to say, the manner in which race and class continue to coincide in complex ways in South Africa means

¹ \$1= R7 approximately (April 2008).

that the overwhelming majority of people who are poor are black, and those most in need of public protection are elderly rural blacks (Devereux 2001). It is essential to recognize the vital role of non-contributory disbursements made by the state to the poor. However, this paper deals more specifically with contributory pensions in the public sector and the opportunities these funds present for a social policy of inclusive development.

In addition to social non-contributory pensions and contributory occupational pensions in the public sector, there are two further types of funds in South Africa, namely, private occupational pensions and voluntary savings through, for example, retirement annuities. On the face of it, South Africa exhibits the fiscal and institutional capacities for a differentiated system that satisfies the World Bank's multi-pillar requirement for pension schemes (van der Merwe 2004:310). It is important though to emphasize that the differentiation in types of pension schemes still coincides largely, but not entirely, with the racialized divisions of apartheid.

In general, the PAYG system operates on the basis of a zero funding level. The contributions made by current employers and employees go directly to finance the pensions of retired workers. This system implies an ongoing cycle of contributions and benefits between workers and pensioners, and the assumption is that no surplus ought to be generated and no capital accumulated beyond a technical reserve. Nothing is supposed to be saved to pay for the future pensions and other benefits of current contributors. In contrast, the FF system operates along the same lines as a private insurance: individual contributions are deposited into a saving's account and invested in interest-bearing financial instruments or equities. Once retirement age is reached, the accumulated funds (contributions plus investment returns minus administrative and insurance costs) are converted into a retirement benefit, usually an annuity or some sort of programmed withdrawals. Fully funded pension schemes are characterized by a greater exposure to the risks and attendant uncertainties of the market, especially when it involves the purchase of equities (Ribhegge 1999:61).

The conversion to this system in South Africa happened when the National Party regime knew that the end of its rule was imminent, and the consequences of this shift are still felt today. It was a decision that has led directly to a dramatic increase in national debt as the public servants of the previous regime consciously indebted the state in order to safeguard their own pensions and retrenchment packages in retirement. This move was clearly motivated by the perceived political risks associated with the anticipation of a redistributive democratic government.

Unlike other indebted governments, the major portion of national debt in South Africa is internal rather than external. In effect, the government is indebted to itself through the FF pension system as the transition from a PAYG system to a fully funded one implied that former contributions to the public pension schemes had to be securitized via government bonds that were deposited in the newly created pension fund. Second, contributions of current employees were directed into the pension fund while current pensions had to be financed out of the budget. This costly transition had detrimental implications for social investment, especially in the areas of education, health and welfare. The introductory quotations by Nelson Mandela, first President of a liberated South Africa, and Trevor Manuel, the current Finance Minister, graphically illustrate the constraints imposed by this debt on the new state in dealing with the iniquitous legacies of colonialism and apartheid. This paper suggests that these constraints are not immutable. Instead, it argues that policy choices in respect of the pension system have profoundly shaped the overall economic prospects of the country. In so far as the levels of inequality in South Africa pose the greatest threat to the new democracy, these policy choices have had contradictory effects. On the one hand, the non-contributory public pensions have certainly benefited many poverty-stricken black South Africans. On the other hand, the fully funded system of contributory pensions for workers in the state sector has had the dual effect of entrenching the deals made with senior public officials of the apartheid government as well as enriching a very small group of black entrepreneurs who have profited directly from the centralized asset management of public pension funds.

This paper deals with the interconnections between public debt, contributory pensions in the public sector, the corporatization of the management of these public funds, the contradictions of Black Economic Empowerment (BEE) and the failure of South African social policy in respect of contributory public pensions to deal more comprehensively with its development challenges. It does this by:

1. describing the political and institutional evolution of South African pension schemes with a special focus on the reform of contributory public pension schemes toward the end of apartheid;
2. examining the governance structure of the pension system in order to establish whether it is transparent and accountable, while ensuring that the pension system is able to pursue its main roles of social protection, redistribution and contribution to economic development and social cohesion (Mkandawire 2001). In particular, the paper investigates the institutions which serve public pensions such as the Government Employees Pension Fund (GEPF) and the Public Investment Corporation (PIC). This outline of the intricate institutional complexes in respect of contributory pensions in the public sector reveals both the limits and the possibilities for inclusive development; and
3. analysing the investment policy of the public pension fund, paying special attention to whether this fund has been invested to build economic and social infrastructure. Essentially the question to be asked is whether the enormous stockpile of capital (PIC's estimated assets are currently worth about R600billion) is being utilized to promote development or not and how it relates to capital accumulation generally (PIC 2006).

2. The Reform of Contributory Public Sector Pensions

Background

Contributory pensions form a crucial component of compulsory savings. Sociologically, it is possible to view these pensions from two broad perspectives: the individual and the structural. The former refers to the role that pensions play in the lives of pensioners as a form of deferred income, or as a consumption allocation mechanism (Holzmann and Hinz 2005:42). In other words, this system is designed to secure a reasonable livelihood in retirement. There are many uncertainties in this regard, especially related to the fact that individuals do not know how long they will live, and it is therefore always necessary for workers to be finely tuned to their own interests in preparation for their retirement. There are further uncertainties related to the deficits in individual understandings of the wide variety of pension systems and mechanisms for saving. While it is obviously difficult to determine the lifespan of any particular individual, it is easier to establish the life expectancy of large groups of people (Barr and Diamond 2006:16). The structural perspective on pensions refers to the manner in which this form of contractual saving can be utilized as a mechanism for enhancing general welfare in old age, as well as how it opens up possibilities for investments and hence economic growth and development.

Over the past decade there has been a great deal of debate about the viability of PAYG schemes in response to changing demographic patterns, in particular in the developed world. Put bluntly, as the proportion of people in society who are old and retired overtakes that of the working population, the financial viability of schemes such as PAYG, which rely on the current contributions from active workers to finance the pensions of the retired workers, is necessarily threatened (Holzmann and Hinz 2005). The necessity for pension reform is invariably premised on both increasing life expectancy of the population and decreasing fertility levels. The demographics are vitally important. If the population is young (as in most developing countries), a PAYG system may be appropriate, but when the retired population increases relative to that of the active workers, then the financial balance of the scheme can be eroded with a smaller young population providing for a larger retired population. The same problem occurs in a situation of increasing unemployment and informality. As a consequence, public

PAYG systems are characterized by continuous efforts toward parametric reforms regarding contribution rates and entitlement rules, and frequently the state has to cover deficits. This growing challenge for existing pension schemes to meet the promised benefit levels, because of the relative diminution of contributions, has led to the so-called old-age crisis.

The World Bank's report, *Averting the Old Age Crisis* (1994), represented a turning point in the debate on the crisis in social security in developing countries. It proposed a three-pillar system of pensions largely within the framework of neoliberalism: (i) a tax-financed safety pension with defined benefits; (ii) defined contribution pensions based on individual capitalization or occupational pensions; and (iii) voluntary savings earmarked for retirement. In effect, the report recommended that it should be obligatory for all employees to enrol in a pension fund managed by private companies, which in turn would invest the contributions in the financial and stock markets. The World Bank has since altered this initial position to include two further pillars: (i) a non-contributory pension providing minimal protection against utter poverty; and (ii) informal kinship sources of financial and non-financial support for the elderly (Holzmann and Hinz 2005:42). The World Bank has clearly responded to criticisms of its earlier position, recognizing the necessity for poverty relief and redistribution with a more nuanced approach to the feasibility of introducing various schemes in different situations. Yet it has retained the basic precepts of the earlier document, with considerable bias in favour of private provision in prefunded systems. This new approach also extended the rationale for pension reform beyond demographic risks only, to include political and economic risks and in cases where the private model was deemed superior with regard to these risks. Three scenarios are suggested for the transition to a multi-pillar pension system with a strong funded pillar. The first scenario describes countries with a well-developed FF pension system. The second scenario encompasses the shift from a predominantly unfunded system to a multipillar system. South Africa falls squarely into this scenario, which will be described in the next section of the paper. Finally, the third scenario describes poorer countries with low pension coverage (Holzmann and Hinz 2005:44).

In contrast to conventional wisdom on the link between demographic factors and pension reform in favour of funding, Barr and Diamond (2006:33) conclude that "the solution to population aging lies not in funding per se but in output growth". They further debunk the simple connection between the FF system, savings, investment and growth by demonstrating the complex nature of this relationship and by questioning the welfare implications of different policies.

The example of Chile has often been used to indicate the apparent advantages of individual retirement savings in privately managed accounts (Charlton and McKinnon 2001:40; Edwards 1998:55). The evidence from Chile, however, does not support the expectation that the privatization of pension insurance necessarily leads to greater savings and therefore toward economic growth. On the contrary, it has instead led to lower national savings due to high transition costs and greater risks for individual pensioners (Riesco 1999; Singh 1996). The Centro de Estudios Nacionales de Desarrollo Alternativo (CENDA) has recently published two highly critical reports on the privately managed pension system in Chile. In the first, the extremely high administrative costs are exposed with the claim that one out of every three pesos contributed to the scheme was absorbed by the administrators (the Administradoras de Fondos de Pensiones/AFP and insurance companies) between 1981 and 2006, and the second seeks feasible ways of gradually reintroducing the PAYG system.² These reports, together with their recommendations, are currently being considered in the Chilean Parliament. In a similar critical vein, Hujo (1999:137) presents a finely grained analysis of the reform of the Chilean pension system by highlighting its economic objectives and demonstrating how social objectives have fallen far down the list of priorities. More recently, de Mesa and Mesa-Lago (2006:152–155) provide a detailed and critical evaluation of the Chilean pension reform,

² Blackburn 2003:14; CENDA web site, www.cendachile.cl node, accessed on 14 June 2007.

specifically in respect of the high and increasing administrative costs of private pension schemes and the important shortcomings with regard to coverage and equity.

Is there an old-age crisis in South Africa? The World Bank's position on the demographic necessity for pension reform in developing countries is informed by the claim that "while the developed countries got rich before they got old, developing countries are getting old before they get rich". (Holzmann and Hinz 2005:25). This assertion simply does not hold true for South Africa where every single estimate shows a decline in life expectancy from about 50 to 56 years in 2000 to about 45 to 49 years in 2005 (Presidency RSA 2007:28; STATSSA 2005:8). Far from getting older, the South African population is actually dying younger. As with everything in South Africa, these aggregate statistics hide the very wide racialized variations. Whites have a life expectancy of well over 70 years (Kinsella and Ferreira 1997:3). There can be little doubt that HIV/AIDS has had a major impact on the demography of the country. According to the official statistics, about 10 per cent of the entire population is HIV positive, with women between the ages of 15 and 49 years exhibiting the highest prevalence at 18.1 per cent (STATSSA 2005:6). This represents almost five million people with the disease. The South African demographic reality, for the vast majority of the population, is one of lifespan shrinkage due to the effects of the AIDS epidemic, but more generally due to poverty levels. Thus, even though Southern Africa has the fastest growing aged population on the continent, this is a far cry from the extent of ageing of the population in developed countries. The median age for Africa as a whole in 2005 was only 19, yet for Europe it was 39, more than double that of Africa (UN DESA 2007). A recent report, for example, claims that only about half of South Africa's 15-year-old young women will reach pensionable age (Dorrington et al. 2004). The evidence clearly shows that the South African population is still relatively young, with the ratio of retired to employed people only 78 to 1,000, compared to about 300 for every 1,000 in Western Europe and Japan (*Financial Mail* 2005). There is certainly no generalized old-age crisis in South Africa. Yet, the solution proposed and implemented in the country inappropriately assumes the existence of such a crisis. It is an assumption that holds true for white South Africans and for the growing black middle class, who, in the main, are well-covered in retirement. It is entirely unsuitable for the overwhelming mass of the black population who remain excluded and marginalized by their unemployment and poverty.

While the focus of the paper is clearly on the pension funds of public sector workers, it is important to emphasise that pension reform in South Africa has conformed neatly to the World Bank's notion of a multi-pillar pension system and the prescriptions of privatization defined by Orszag and Stiglitz (1999:5) as "replacing...a publicly run pension system with a privately managed one". In line with this thinking, the National Treasury presented a discussion paper on *Social Security and Retirement Reform* with the specific aim of ensuring a multi-pillar system supported by a range of reforms (Treasury, RSA 2007a:3). The Treasury document envisages a compulsory national pension fund to cover about 80 per cent of the working population of South Africans, due to be implemented in 2010. There are currently about 13,500 private pension funds in South Africa, consisting of occupational pension funds, provident funds and retirement annuity funds based on personal plans. Four-fifths of these funds have fewer than 100 members, imposing huge administrative costs and regulatory challenges. The idea is to consolidate these many small pension funds into about 100 large funds to provide retirement benefits for its members. More than nine million people in South Africa are members of retirement funds, but this is an overestimate because some members may belong to more than one fund. About 60 per cent of formal sector employees have some or other form of pension fund (Treasury, RSA 2007a:5). The key to the successful implementation of the plan is obviously the extent of national employment. Membership of a pension fund is only obligatory in the occupations where such a fund exists. Since a large proportion of the population is still not covered by an occupational pension fund for the simple reason that they are not in employment, they will necessarily be dependent upon a social, non-contributory pension.

Together with South Africa's well-developed multi-pillar pension sector goes a well-developed but exclusive financial sector. Bhorat and Cassim (2004:19) claim that this exclusivity is based on

the high levels of income inequality in the country. There can be little doubt that South Africa has a sophisticated multi-tier system of provision of benefits in retirement. However, a very small proportion of the population, only about 6 per cent, is self-sufficient in retirement (van de Merwe 2004:312). The high levels of unemployment obviously feed into the high levels of poverty, and accordingly, there is a high level of reliance upon social pensions and other grants from the state in retirement. There are currently about 11 million recipients of various grants and other forms of social assistance in South Africa (Department of Social Development 2006).

The main development challenge in the country is undoubtedly the problem of black poverty. How the government responds to this challenge raises compelling questions about its legitimacy and the level of consent by the majority, both of which are critical to ensure the sustainability of democracy. In respect of pensions, it is therefore necessary to assess the extent to which this overarching development challenge is met by the policy options of the new democratic government.

Public debt and the fully funded pension scheme in South Africa

In 1989 the total debt of the South African government stood at R68 billion, of which R66 billion was domestic debt and only R2 billion was foreign. By 1996 it had grown phenomenally to R308 billion, of which R297 billion was domestic and R11 billion was foreign debt. The servicing costs for these debts rose from about R12 billion in 1989 to more than R30 billion per annum in 1996. During the same period, the assets of the GEPPF grew from R31 billion to R136 billion.³ The massive increase in national debt stems directly from the government borrowing money from itself in order to secure the pension funds and retrenchment packages of apartheid-era civil servants. This is the single most important variable in the dramatic increase in national debt over such a short period of time, just prior to the possibility of a redistributive democratic government. Currently the national debt stands at R540 billion (of which about R79 billion is foreign debt) and the annual repayments amount to about R50 billion, one of the largest budgetary items in South Africa. The minister of finance, Trevor Manuel, confirms the palpable fact that most of the country's domestic debt is to the pension funds of workers in the public sector. But he proceeds to defend the fully funded pension system on the following grounds:

To invest we need savings. The interest earned from our investment in the Public Investment Commissioners has been one way to save money. Given the existing low savings ratios and high levels of household indebtedness in the South African economy, people must expect the government to take a cautious view on savings, as high levels of savings would better serve the long-term interests of the country (Manuel 1999).

In contrast to this view, Orszag and Stiglitz (1999:9) argue that there is no necessary link between the shift to pre-funded individual accounts and an increase in national savings. Instead, they move away from the simplistic "one-size-fits-all" model to present a range of different options appropriate for particular circumstances. Barr and Diamond (2006:30) reiterate this view but go even further: "[T]he process of building a fund may add little or much to national savings. There are two questions: does the fund increase saving, and if so, is the result welfare enhancing?" They go on to argue that there could be a relative decrease in voluntary savings to offset the effects of a mandatory occupational savings in a pension scheme. Likewise, public dissaving in order to cover transition costs can offset increased private saving in pension accounts. In other words, there is plethora of scenarios which may or may not have the effect of increasing savings.

Manuel's position avoids all these nuances. Instead, it argues that the state will exchange its indebtedness for the savings of the pensioners, without any consideration for the broader welfare implications of the funded option.

³ Treasury RSA 2007b:190–193; AIDC web site, www.aidc.org.za, accessed on 20 September 2004.

In his address to the Federation of Unions of South Africa (FEDUSA) in 2002, Manuel put forward the following defence in favour of the fully funded system:

[S]ome have argued that we should change to a pay-as-you-go system and to use some of the accumulated funds for government spending. I have resisted this push. Government should spend what it raises in taxes and what it borrows to fund the deficit. The pension fund does not belong to government; it belongs to the beneficiaries. If worker representatives want the fund to be managed differently it is their right (Trevor Manuel, speech to FEDUSA, 2002).

There is one patent flaw in this argument, a point to which Manuel himself referred earlier. The government has set up the institutions from which it has borrowed money. Since it has incurred the debt by allocating money to the fully funded pension schemes, it is entirely within the purview of government to reverse such a trend, reducing the level of national debt and consequently opening up possibilities for inclusive social development.

The union movement was not unanimous in its opposition to the fully funded pension system. The National Professional Teachers Organisation of South Africa (NAPTOSA) held a view very similar to that of the government. According to its annual general meeting minutes:

[I]t seems that, in this regard, the Task Team will not find it difficult to make a recommendation, as the disadvantages of a PAYG pension scheme for public servants are sufficiently clear enough to convince them NOT to part with their current fully funded private individual's savings pension fund where workers' own money plus the employers' contribution are invested and grow, and where an actuarial interest is accumulated as retirement protection. The funded pension system, where one can see one's own money grow and can exactly calculate one's own share, has obvious advantages which enable one to accountably plan and to supplement an exactly calculable amount that will be received upon retirement. This clearly would be the best insurance against potential disaster and of having to depend on the 'goodwill' of others (including one's ex-employer, who might be bankrupt) for hand-outs after retirement (NAPTOSA 2001).

The question at stake was how to balance the interests of the workers in the public sector with national developmental goals. In respect of pensions, the government has been consistently in favour of the former. The shift toward a FF pension scheme for workers in the public sector indebteded the state by billions of rand just before a democratic government took power, but there are other related causes for this indebtedness. In the 1980s the funding level of pensions in the public sector had collapsed, precipitously compelling the government to make regular disbursements to the fund. There are two main reasons for this collapse. First, workers in the public sector were permitted to buy back their service at ridiculously low rates to the age of 16, irrespective of when they were employed. In effect, this meant that workers could artificially lengthen their periods of service and hence substantially increase their pension benefits. Wassenaar (1989:84) referred to this as an "outrageous provision, which resulted in a lavish squandering of taxpayers' funds...to acquire fictitious pensionable service". The costs of this largess toward civil servants were obviously unsustainable. In fact, the retirement benefits for workers in the public sector were far better than those in the private sector at the time. In addition to the practice of purchasing additional years of service, pension benefits were calculated on the basis of the earnings on the last day of service, instead of an average over the last few years of service. Wassenaar (1989:84) points out that this system was regularly abused as workers were given a raise toward the end of their service for no other reason but to provide them with a better pension. In effect, these were "free gifts from taxpayers to civil servants" (Wassenaar 1989:87). The financial impact of these benefit costs were reflected in the deficits incurred, and they were compounded by the second reason for the collapse of funding levels, namely the low returns on government bonds in which most of these funds were invested. While there was pension fund, it operated on the same basis as a PAYG scheme.

In the PAYG system the debt of the government to the pensions of its employees is implicit, in the sense that it is clearly a liability, but not one that can readily be called upon in total as with private assets or savings. In contrast, the FF system converts this implicit debt to an explicit or actual debt. Thus, the transition to a FF system corresponded with a massive injection of government funds in order to comply with the exigencies of a possible pension payout for all state sector workers in the scheme. This was because the assumption in an FF system is that the enterprise must at all times have as much money as may be needed for pensions to be paid out in full in the event of the enterprise going insolvent and closing shop. Of course, this is a spurious assumption to make in the public sector. After all, even if a government is bankrupt, as many undoubtedly are, it obviously cannot simply close shop. There is very little prospect indeed of all the pensions of all the state employees suddenly being paid out at once. Yet, this assumption underlies the FF system. It is an assumption that has very direct effects on the amount of reserves accumulated in the public pensions sector and consequently on the levels of domestic debt. The government clearly did not have the money readily available to fund the pensions, and it therefore issued government bonds. These so-called transition costs are inevitable because the FF system compels collected revenues to be shifted away from its availability to pay current pensions and accumulates them in the newly created pension accounts (Hujo 1999:132). Baker and Weisbrot (2002:2) provide evidence of how these transition costs in the privatization of Argentina's social security system played a direct role in its economic crisis.

In South Africa, the transition to democracy provides a vital backdrop for understanding the transition to an FF scheme. The civil servants of the apartheid regime feared that the new democratic government would fail to honour pension arrangements made under apartheid. The perceived risks were of a political nature, and the reasons for the shift were clearly not based on any actuarial calculations. The expectation of government intervention in the allocation of pensions was very real. But, ultimately, these fears were unfounded. One of the major compromises made at the negotiating table toward democratic majority rule involved the protection of the pension benefits of workers in the state sector. The new democratic government had legitimized the debt incurred by apartheid in its dying days and entrenched the shift toward privatization through the corporatization of the investment portfolio manager of the pension funds (the subject of corporatization is dealt with in greater detail in the following section of the paper). It goes without saying that this debt has had a crippling effect on the economy as a whole and on the poor in particular.

The PAYG and the FF systems are not necessarily polar opposites because PAYG systems can be partially funded and FF schemes can include redistributive features. Thus there may be adaptations of either system which allow for benefits to accrue to members. Breyer and Stolte (1999:80) make this point very forcefully: "Each pension system is characterized by an infinite sequence of benefit levels and the corresponding contribution rates". They offer the hypothesis that "all members of a cohort will vote for a certain reform option if it reduces their net payment as comparable to the status quo system". There can be little doubt that this hypothesis holds true for South Africa. The switch to an FF system was clearly a choice prompted by the perceived political risks of a redistributive democratic government.

The bonds issued by the government to finance the transitional costs of shifting to the FF scheme are held by the Public Investment Corporation (formerly known as the Public Investment Commissioners), the investment manager for the GEPPF. In effect, the government is the borrower and the PIC the lender in this transaction. In so far as the PIC is a public entity, the government was borrowing and lending from itself. The entire operation was artificially circular. On the face of it, the government borrowed money from the PIC in order to finance the pensions. Yet, the PIC did not have money to lend to the government. Instead, it managed the assets that were due to the members of the pension fund. The government transfers and interest payments on these bonds has permitted the PIC to accumulate a massive stockpile of capital in direct correspondence to increasing government debt. The correlation is unmistakable.

Commenting on the effects of the debt, Thabo Mbeki, then deputy-president, offers the following political explanation:

To finance the expenditure associated with efforts to buy space for the apartheid regime during its last days, the ruling group went on a borrowing spree to finance a level of spending that could not be sustained on the basis of the extant revenue base...the apartheid ruling group imposed on the country an unprecedented debt burden whose acquisition had to do exclusively with shifting the balance of forces during the period of transition from apartheid to democracy, so that this anti-democratic group would not be as weakened politically as it would otherwise be, in contradistinction to the democratic movement (ANC 1996).

In analysing one of the effects of a transition from a PAYG system to a FF system, the World Bank reluctantly concedes that “debt repayments of this size create a major cost for current (and future) generations, and, despite the potential advantages, the net benefits of a major move toward funding may not be positive” (Holzmann and Hinz 2005:50). It could be argued that these transition costs could have been avoided in the South African case by reverting to the PAYG system.

The structure of pension fund management

The Government Employees Pension Fund

The fragmentation and segregation of apartheid resulted in a highly differentiated system of pensions. Each *bantustan* government and every quasi-department had its own pension fund. For example, the South African government had its own pension scheme, the separate so-called independent states had their own pension scheme, the self-governing homelands had their own pension scheme and so on. There were ten such separate pension funds for various arms of the government, with no uniformity at all.⁴ Since there was a wide variation in the benefits of each of these funds, a Task Team on Restructuring Pensions was appointed by the democratic government to make recommendations on ways in which the benefits could be standardized. The task team was representative of a range of constituencies, including members of the government, the security services, the education sector, other employer organizations and an actuary (GEPF 2004).

Following the recommendations of the Task Team on Restructuring Pensions, the government amalgamated a range of public sector pensions (including the pension funds of Transkei, Venda, Bophutatswana, Ciskei and the Government Service Pension Fund) into a huge Government Employees Pension Fund, directly accountable to the South African national assembly. This rationalization of the various apartheid-era pension schemes followed a provision of the Interim Constitution of the Republic of South Africa (Act No. 200 of 1993), which entitles all public servants to a fair pension and provides for the establishment of a pension fund to manage them. It was also directly related to the establishment of one public service for the country as a whole through the passage of the Public Service Act in 1994.

The GEPF was founded by the Government Employees Pension Law in 1996, consolidating ten separate pension funds into one, standardizing the benefit structure for all government employees, and in so doing formally eliminating the discriminatory practices of apartheid. According to the 2006 Annual Report of the GEPF, it now has a membership of 1.37 million, of whom about 300,000—or 18 per cent—are pensioners (GEPF 2007:44). The average age of members is 40 years and the average past service is 12.2 years (GEPF 2002). It is the twenty-first largest fund in the world, the seventh largest outside the United States. Only the Malaysian

⁴ The following pension funds were involved in the investigation: Government Services Pension Fund, Temporary Employees Pension Fund, Authorities Services Pension Fund, Authorities Services Superannuation Fund, Ciskeian Civil Servants Pension Fund, Transkeian Government Service Pension Fund, Government Employees Pension Fund of Transkei, Government Pension Fund of Bophutatswana, Government Pension Fund of Venda and the Government Superannuation Fund of Venda.

national pension fund is bigger than it in the developing world (*Financial Mail* 2005). Besides making provision for the merger of government pension funds, the GEPF was supposed to be managed by a Board of Trustees with equal representation of fund members and employers. For almost a decade after the passage of this legislation, the board of trustees was not established. The Minister of Finance remained the sole interim trustee until 2005. This was clearly an unsatisfactory state of affairs and various contradictory reasons were provided for the long delays in establishing the board.⁵

Box 1: The South African Transport Services

The South African Transport Services provides an interesting case study of how the pensions system was intertwined with an apartheid workplace regime, and how things have changed since 1994. Up until 1974, black workers were not part of the Transnet Pension Fund. Instead, there was a separate arrangement operated for blacks on the basis of a savings account. This meant that there were contributions from black workers toward their own retirement, but the company contributed nothing. To make matters worse, black widows were excluded from the pension benefits paid in by their husbands. It was only in 1990, with the establishment of Transnet out of the former South African Transport Services, that the black workers were fully integrated into the pension fund of this huge parastatal (Radebe 2000). In its submission on the Transnet Pension Fund Amendment Bill, Congress of South African Trade Unions (COSATU) made the following appeal:

[T]he employees of Transnet were not classified as full employees...[O]ur understanding is that these people have been severely discriminated against purely on the basis of race, and up to today are in a significantly worse position than white...employees in otherwise similar circumstances. This is an untenable position and needs to be addressed as part of dealing with the apartheid legacy (COSATU 2000).

The individual experience of pensions was deeply racialized. In terms of the structures, the debt situation inherited by Transnet mirrored the broader South African problem in stark and obvious ways. Properties, such as the prestigious Cape Town V&A Waterfront, were transferred to the Pension Fund in 1994 to deal with its crisis-ridden deficits. In the process, the asset base of Transnet was significantly eroded. In the case of Transnet, also, the demographics played a role, since according to minister of public enterprises, Jeff Radebe, there were more pensioners receiving benefits than active workers contributing to the fund. In effect, the amendment created an entirely different system, a defined contribution pension fund which transferred the risk to the members rather than to the company. Since this required the consent of the employees, a major incentive was instituted, awarding R7,900 to each worker who agreed to convert to the new system (Radebe 2000). It would appear that the debt crisis of Transnet necessitated this restructuring simply for the purposes of survival. Radebe reiterates just how the Transnet case of debt and pensions reflects that of the rest of South African national debt: "[A]s of March 1999, 43 per cent of Transnet's total debt was due to its pension fund obligations" (Radebe 2000). In response, it was envisaged that the restructuring of the pension fund would have a significant impact on Transnet's "ability to fulfil its *developmental role* in our country" (emphasis added).

Pension privatization has taken on a variety of different forms in South Africa. It encompasses the private management not only of employees' benefits, but also of a whole range of interlocking private controls over the investment of public funds. In confirming this trend, the Annual Report of the GEPF (2002:8) states quite clearly that "the GEPF has grown and now operates...very much like any large private sector business". It employs 427 people, of whom more than 70 per cent are female. There is an intimate connection between the GEPF and the PIC as the two main institutions in respect of the management of public pensions. It is the prerogative of the GEPF trustees to appoint the PIC as its asset manager, but the Board of Trustees was formed only after the corporatization of the PIC.

The Public Investment Corporation

The PIC has a long history that can be divided into three broad periods. Firstly, from 1911 to 1984 the Public Debt Commissioners (PDC) was established with a mandate to control investments on behalf of the state sector. The Public Debt Commissioners Act of 1911 was one of the first pieces of legislation to be passed by the parliament of the Union of South Africa, which came into effect a year earlier through the merger of the four colonial provinces of the Cape, Natal, Orange Free State and Transvaal. Its main objective was to act as a source of

⁵ COSATU 2004b; personal communication with Ben Turok, 2004.

funding for the new government's budget deficits. It was supposed to hold state assets in a transparent manner and be accountable to parliament in order to inspire public confidence. The idea was that control over government funds would be vested in a single authority. In the early stages of its development, the PDC invested trust funds of the government and the South African Railways and Harbours, but by 1924 this included the funds of the provincial administrators. The PDC slowly but surely extended its power, acquiring more and more responsibilities over the funds attached to government. By the mid-1920s it was given the responsibility of granting loans to local governments. It was also charged with the responsibility of establishing the Government Sinking Fund which provided for "unproductive debt" to be redeemed over 40 years (SA Financial Sector Forum 2001). In effect, the PDC created a pool of government money, most of it from government pension funds, from which the government could borrow from itself.

The second phase (1984–2004) in the evolution of the PIC was initiated by the passage of the Public Investment Act (No. 35 of 1984). This piece of legislation gave the early expansion of the PIC a major boost because it allowed for the appointment of commissioners (then called Public Investment Commissioners) with the power to invest funds on behalf of public bodies. By 1991, the PIC started to invest in equities as opposed to fixed interest government bonds only. The overall role of the PIC may be likened to an amalgam of three broad categories of institutions. It is a pension fund manager, a short-term insurer and a manager of trust funds (SA Financial Sector Forum 2001). In terms of its legal framework, the scope and responsibility of the commissioners were closely associated with the minister of finance, who automatically acted as the chairperson. The entire operation of the PIC took place within the Department of Finance, and there was a close link between the PIC and the South African Reserve Bank.⁶ The situation was obviously not frozen since the organization and management of pension funds in particular respond to a changing environment. For example, some government departments, such as the South African Transport Services and the Department of Posts and Telecommunications, were granted the right to function as public companies, and they have subsequently withdrawn their pension funds from the GEPP. Similarly, universities and libraries, also former members, have started their own independent pension funds. While it has lost these, the GEPP has acquired the pension funds of the former homelands. During this period, the PIC played a central financial role for the apartheid regime, especially in a context of the imminent defaulting on debt.

Since 1994 there has been a wide-ranging restructuring of the PIC. Initially, its primary function was to control and invest funds entrusted to it from various sources within the government, most notably the pension fund. It did this by investing primarily in government stocks without submitting any competitive tender. The budgetary allocation to the PIC was determined by the government on the basis of its calculations of the PIC's expected requirements. In 1994, this cosy relationship was changed so that the PIC now buys all its stocks on a competitive basis. These changes paved the way for the third phase of the PIC from about 2004 onward, a phase characterized by the Finance Committee of the South African Parliament passing the Public Investment Corporation Act in 2004. The Memorandum on the Objects of the Public Investment Corporation Bill (2004)⁷ suggests some of the reasons for its establishment. The Public Investment Commissioners were not legally registered as asset managers, although that is how they had been functioning. The bill thus proposed to allow the *de facto* situation to become *de jure* as well.

This piece of legislation was passed in the teeth of opposition from the Congress of South African Trade Unions (COSATU) and other organs of civil society. The controversy over the passage of the Public Investment Corporation Act revealed major schisms over development policy options in South Africa, especially in relation to how the social goals of equity and poverty eradication should be tackled. One of the primary objectives of the Act was to replace

⁶ Public Investment Commissioners (PIC). 2004. www.pic.gov.za/main.htm, accessed on 14 June 2007.

⁷ Memorandum on the Objects of the Public Investment Corporation Bill. 2004. www.pmg.org.za/bills/040511picbill.htm, accessed on 14 June 2007.

the Public Investment Commissioners by the Public Investment Corporation and to transfer all the assets of the existing commissioners to this corporation. The critical aspects of the debate concerned the relationship between the corporation and the state. While COSATU and other organs of civil society called for public scrutiny over the management of pension funds, the clause of the Act (No. 23 of 2004) dealing with the establishment of the corporation, explicitly states that “there is hereby established a juristic person, an *institution outside the public service*, to be known as the Public Investment Corporation Limited” (emphasis added). Yet, in respect of the share capital of the corporation, the Act made equally explicit that the “state is the sole holder of shares in the corporation. The rights attached to the shares in the corporation, of which the State is the holder, must be exercised by the Minister [of Finance] on behalf of the State”. The idea is that the management of government money will reside outside of government. It is a case of the separation of ownership and control over state assets. The draft legislation gave the minister of finance wide-ranging powers in that he “may decide at any time to dispose of all or any part of the shares held by the state in the corporation”.⁸ The subsequent Act gave parliament a greater oversight role. It would not be entirely in the hands of the minister to decide whether the corporation should be fully privatized or not, but the Act (No. 23 of 2004) has a ring of almost ineluctable privatization. The Act exempts the corporation from certain sections of the Companies Act as long as the state is the sole or majority shareholder of the corporation, and in anticipation that at some point it will be out of the hands of the state, it mentions that the corporation will be subject to the provisions of the Public Finance Management Act (No. 1 of 1999) for only as long as the state holds shares in the corporation.

The Public Investment Corporation operates very much like a privately owned asset management firm. In other words, corporatization has blurred the distinction between the public and the private, so that the oversight role of the former is muted and the possibilities for private gain enhanced. There are some obvious contradictions here. While the corporation is akin to a privately managed company, it is still wholly owned by the state, with the minister of finance as the sole shareholder. This arrangement gives rise to a duality of interests. In the first instance, the PIC is obviously accountable to its shareholder, the government. Yet, more than 90 per cent of its funds derive from the GEPPF, and the PIC also has to act in the interests of the pensioners, the ultimate “owners” of the fund. In sum, the corporation is privately controlled but publicly owned, with the use of assets belonging to pensioners. One example will reveal the huge conflicts of interest inherent in this relationship. If the PIC decides to sell shares at a discounted price to BEE partners, then this sale necessarily represents a net loss to the GEPPF and therefore to the pensioners, but it will be a massive gain for a few private individuals (see the example of Telkom below). This scenario raises a whole host of questions around the necessity for the PIC to exist at all. If the GEPPF appointed its own asset managers, it would obviously have far greater control over the management of its funds.

The question of accountability lies at the heart of the problem. If the PIC were a public entity, it would be accountable to parliament and thus to the people of South Africa. As a statutory body outside the public sector, the PIC has very limited accountability, especially since it is removed from government and public scrutiny. Gumata and Magadze (2005:65) confirm this change in status in respect of monetary analysis: “[T]he Public Investment Commissioners was treated as part of the government sector. The corporatization of the Public Investment Commissioners necessitates a re-classification in the monetary analysis from the government sector to the ‘private and other domestic sectors’ category”.

The new PIC has an entirely free hand in the kinds of investments it makes, and there is no evidence that these investments will be at all developmentally orientated. Instead, the investment policy points in the direction of profit maximization for the few through more and more speculative investments in equities. In a speech to the FEDUSA Congress, Trevor Manuel (2002) made the following remarks: “[P]ension funds must hold their fund managers accountable. Pension fund trustees must be active guardians of their members’ interests”. Yet,

⁸ Draft Public Investment Corporation Bill. 2004. www.pmg.org.za/bills/040511picbill.htm, accessed on 20 August 2004.

in respect of the GEPP this is impossible against the backdrop of the corporatization of the PIC, its asset manager.

The minister of finance has the power to authorize the sale of shares in the corporation. This appears to suggest that the PIC is well on the road to thoroughgoing privatization. But this is privatization with a difference. It encompasses the use of state indebtedness for the purposes of private gain for a few. Cynics may point to the fact that the delays in the establishment of the board of trustees of the GEPP, which includes members of COSATU, as per the legislation, were designed to ensure a smooth passage for the Public Investment Corporation Bill. COSATU's opposition to corporatization is very well known, and it goes without saying that if COSATU had representatives on the board of the GEPP, it would have done its level best to have blocked this proposed legislation. Instead, the minister of finance now has wide-ranging powers. Not only can he preside over the possible sale of state assets, he also influences the appointment of the Board of Directors of the PIC. Although the minister is supposed to consult the cabinet in this appointment, it still provides Manuel with great scope in determining the composition of the board.

In its submission on the Draft Public Investment Corporation Bill, COSATU put forward a forceful argument on a range of extremely important issues on both the process of policy making in respect of pensions and on the content of the new policy as it relates more broadly to the development agenda of the state. First, the group voiced strong objections to the manner in which the proposed Draft Public Investment Corporation Bill was introduced to Parliament (COSATU 2004a). There was less than one month for public comment on the bill, certainly not a process of widespread consultation and transparency. The bill was not discussed at the National Economic and Labour Council (NEDLAC),⁹ the body consisting of organized labour, capital and the state on crucial policy decisions, nor was it placed on the agenda of the Board of the GEPP. In short, COSATU complained that the bill was rushed through parliament and that it was not consulted on the proposed corporatization of the management and control over the pension funds, notwithstanding the fact that very many of its members are also members of the fund by virtue of their employment in the state sector. More broadly, COSATU's position is that the lack of accountability in the management of the fund runs counter to the public interest. In response, the government, through Brian Molefe, then newly appointed chief of the PIC, has accused the union federation of "a petulant refusal to face the facts" (Dawes 2004). The director general in the Treasury was even more pointed in his remarks: "[H]e was at a loss to understand how the union could give up the gains made by workers in controlling their pension funds" (Dawes 2004). Former NEDLAC chief, Phillip Dexter's response is revealing: "There is a particular constituency that does not like NEDLAC, but those are fundamentally anti-democratic people who don't see consultation as a worthy application of time".¹⁰ The process is anything but transparent. In response to a range of questions¹¹ the GEPP responded in the following bland manner: "Note: The GEPP is unable to comment on questions 6, 8, 9 and 10".¹²

COSATU defines corporatization as being "inextricably linked to the broader processes of privatization and commercialization of state assets" (COSATU 2004a). In its view the PIC

⁹ NEDLAC is a statutory body of organized labour, business, government and community for social dialogue on issues of social and economic policy.

¹⁰ *Sunday Times*, 8 August 2004. www.suntimes.co.za/2004/08/08/business/news/news18.asp, accessed on 15 August 2004.

¹¹ These were the questions sent electronically by the author to the GEPP's Hilton Fisher:

(vi) Could you please provide a rationale for opting for a funded system instead of the pay-as-you-go system?

(viii) What is the response of the GEPP in respect of the draft Public Investment Corporation Bill? Here I would like a comment on both the process (was there adequate consultation and engagement) and the content (what the Bill entails in respect of the funds of the GEPP).

(ix) Is there any possibility of a merger between the GEPP and the PIC?

(x) How does the GEPP view the corporatisation of its fund management? I would like a comment on the philosophy behind the decisions taken—what ideas about economic development this entails and so on?

¹² Hilton Fisher, email communication with author, 2004.

should be a vehicle for social investment to deal with the huge development problems in South Africa. Instead, the main shift in investment strategy in the PIC has been away from government bonds toward greater exposure to the equity market, following the well-known World Bank view against the public management of pension funds and more generally, against the role of the state in development (Charlton and McKinnon 2001:169).

It was to be expected that an organization with such a huge amount of capital under its management would become a significant force in the South African economy. The chief executive of the PIC, Brian Molefe, was nominated by the *Financial Mail* in 2005 as the second most powerful and influential figure in the economy, after Tony Trahar, head of Anglo-American. Molefe has promised to link the appointment of external asset managers with their record of black economic empowerment. Thus the black-owned Metropolitan Life stands to gain, while others may lose out on the amount they manage, depending on the extent of transformation (defined in this instance to mean black membership on boards) that has taken place. In Molefe's own words:

We will use our investments in the [Johannesburg Stock Exchange] to accelerate transformation. You can't do it by legislation or dictatorship as this is a capitalist economy. We plan to use our rights as a shareholder to have a say...It's dangerous to leave the management of the economy to chief executives whose interests aren't aligned with the people who invest their cash in these companies.¹³

Molefe's threats were not idle. The PIC withdrew R22 billion from its private asset managers, including Old Mutual Asset Managers, Sanlam Investment Managers, Stanlib Asset Management, Futures Growth Asset Management and Rand Merchant Bank Asset Management. The withdrawal sent a powerful message of the necessity for transformation in the sector, and it is no accident that each of these concerns now has an empowerment partner. Molefe has constructed his role in the PIC to primarily promote black executives at the board level using the corporate channel of the AGM to accelerate change in the upper echelons of the corporate world. Last year, two prominent companies, SASOL and Barloworld, have felt the impact of Molefe's style of boardroom activism through a major change in their executive directorships.

The PIC has about R250 billion invested in the stock exchange. There are huge opportunities for utilizing this economic muscle to foster black share ownership and to ensure black partnership as senior executives. Molefe (2007) has made it clear that his aim is to transform the top 40 companies in South Africa by making their executive directors more representative of the demographic realities in the country. After more than a decade of democracy, according to Molefe (2007), there are 33 executive directors in the top ten firms in the country, only three of whom are black, and all from one firm.¹⁴ He goes on to say that of the 92 executive directors in the top 20 firms, only 10 are black. At a conference celebrating a decade of democracy, the distinguished African scholar Ali Mazrui described South Africa's transition in the following metaphoric terms: "The whites decided to hand over the crown to blacks but to keep the jewels." The new government, he concluded, inherited a crown with no jewels. As with all metaphors, Mazrui's captures part of an unfolding narrative. It is clearly not the whole story, but it certainly captures a vital part of it, and nowhere is this more evident than with the executive directors of the top companies.

Currently, about 3.5 per cent of the total portfolio of the PIC is managed by the Corporate Finance and Isibaya Fund unit, an amount of about R13.2 billion (PIC 2006). The stated purpose of this unit is to "pursue the transformation of the economic landscape of the country by contributing to infrastructural development and economic transformation initiatives, while

¹³ Sunday Times, 1 October 2004. www.suntimes.co.za/zones/sundaytimesNEW/business/business1096606460.aspx, accessed on 13 June 2005.

¹⁴ The firm is MTN.

ensuring positive real rates of return on funds invested”.¹⁵ Toward the end of 2003, however, there had been a disaster in the management of these funds especially in respect of BEE deals. Admitting that the PIC had “burnt its fingers”, the then deputy minister of finance, Mandisi Mpahlwa, announced that there was a loss of nearly R300 million over a period of six years, with the value of many of the companies that were targets of investment reduced to zero or almost zero.¹⁶

Box 2: The case of Telkom

There has been a great deal of controversy over some of the BEE deals in which the PIC has been involved, many of which, especially in the early years, were hopeless economic failures. Of these, the Telkom deal has provoked the most wide-ranging criticism because it is so clearly emblematic of the contradictory roles of the PIC. The Elephant Consortium, a black-owned company, wanted to purchase a 15.1 per cent stake in South Africa’s monopoly telephony company, Telkom (also Africa’s largest communications company), from the Malaysian-American company, Thintana. When the Elephant Consortium could not find the funds, it approached the PIC, which in turn bought the shares at R78.74 each, using money from its Isibaya Fund (discussed above). The PIC warehoused these shares and eventually sold 6.7 per cent of them to the Elephant Consortium at R92.50 each, while they were listed at R109 each. The PIC has since decided to place 5 per cent of these shares in the GEPP portfolio and a further 3.4 per cent is earmarked for future broad-based black empowerment (PIC 2006). The government remains the major shareholder in Telkom, but this deal in particular, precisely because of the connections of the individuals involved, has resulted in COSATU’s protesting that “the hard earned money of the poor has been used without their permission to facilitate a deal that will pour millions of rands into the pockets of a few very rich people” (cited in *Business Day* 2005). Instead of enriching a few, the labour federation argued that the shares should be sold back to the government. This deal is the clearest illustration of the private affairs in the use of public funds, especially pensions. Not only did it represent a substantial loss to the members of the GEPP, both pensioners and active workers, whose money was used to finance the deal, but it also reveals the parasitic nature of narrow-based black economic empowerment.

Since September 2003, the Isibaya Fund has undergone substantial restructuring. Having learned from the errors of risky investments, the fund is now mandated to allocate separate amounts for three broad categories of investment:

1. The Fund of Funds: This fund, which amounts to about R3.4 billion, provides loans to BEE deals. Transformation of the ownership structure of the South African economy lies at the heart of this fund, and it allocates loans of R100 million to black-owned or partnered firms. It has outsourced the allocation of loans of between R5 million and R50 million to cater for small, medium and micro black-owned enterprises.
2. Private Equity: This fund amounts to about R6 billion and is used to finance big business owned by blacks or huge deals in which black-owned firms purchase shares in big companies. Cyril Ramaphosa and Tokyo Sexwale have benefited from this type of loan. Offered at an interest rate of 8.6 per cent, this form of loan has been part of the broader change in class stratification of South Africa with the emergence of a hugely wealthy black elite.
3. Infrastructural Fund: This is a long-term fund amounting to about R2.5 billion. It has been used in projects such as the Gautrain, several toll roads and so on.

Out of the enormous portfolio of the PIC, only the minute proportion of 3.5 per cent is directly attributed to the transformation of the economic landscape in favour of the twin objectives of black ownership and the creation of employment through socially responsible investments. While the former objective has evidently been implemented to some degree, the latter has been woefully neglected. In response to popular sentiment, the PIC has recently embarked on a joint venture to create a large socially responsible investment fund, to be called the Community Property Fund, with the aim of focusing on retail property investments in townships and rural

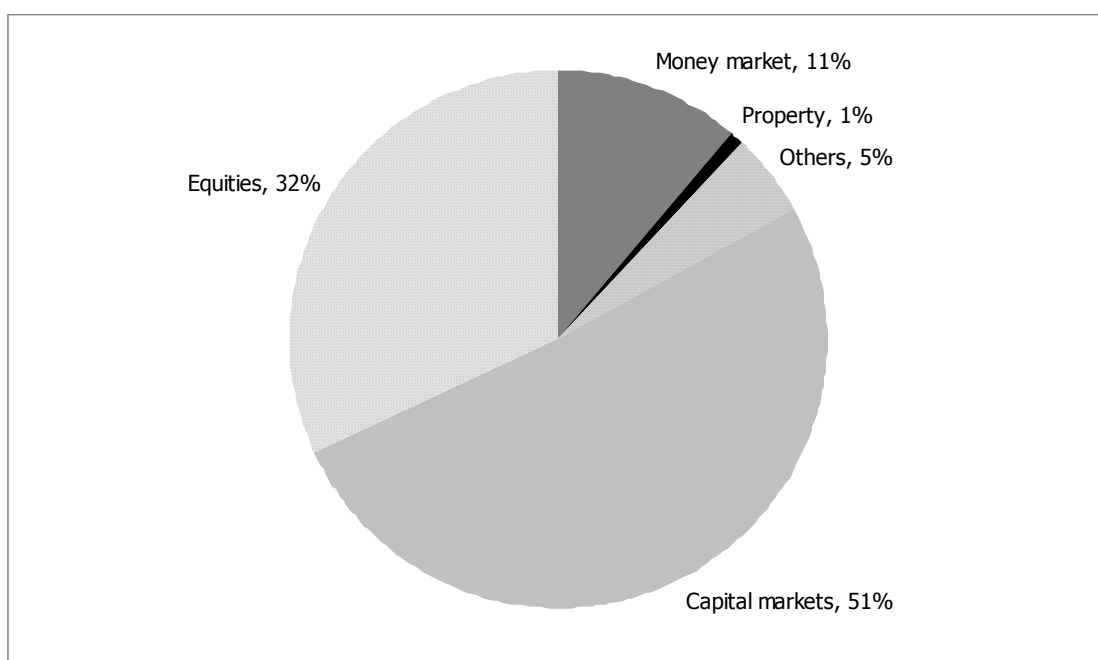
¹⁵ Public Investment Commissioners (PIC). 2004. www.pic.gov.za/main.htm, accessed on 14 June 2007.

¹⁶ The following examples were provided: R13 million investment in Macmed reduced to zero, R100 million investment in PQ Africa reduced to R21 million, R70 million in Carewell Group reduced to R2.3 million, R61 million invested in Midi TV and Penta Publications also reduced to zero (News24.com 2003).

communities (PIC 2006). While such a move should obviously be supported, it does not begin to address the enormity of the problem at hand in South Africa.

A growing amount of the funds of the PIC are invested in equities. Accounting for 32 per cent of the total portfolio of the PIC, equities represent almost 10 per cent of the total market capitalization of the Johannesburg Stock Exchange. By far the largest proportion of the PIC's portfolio is in fixed income with government bonds accounting for 51 per cent, and money market instruments accounting for 11 per cent. With the corporatization of the PIC, it seems inevitable that more and more funds will be managed directly by the corporation itself. There can be little doubt that corporatization opens the way for the PIC to become a profit-making company in its own right. Currently, the property portfolio as well as the capital and money market investments and a portion of the equities, are handled internally within the PIC. The bulk of the equities are externally managed by the five private asset management firms mentioned above (see figure below).

Figure 1: Asset allocation, 2003



Source: Public Investment Commissioners 2003.

The GEPP provides more than 90 per cent of the assets managed by the PIC, its biggest client by far. It could be said that the PIC is merely the investment arm of the GEPP, but this would fail to reveal the full picture of the complex institutional arrangements that have emerged to accommodate a variety of public and private objectives. Nor will it tell us very much about the particular manner in which the PIC and the GEPP relate to each other.

There can be little doubt that the PIC opens up possibilities for accomplishing social goals through an appropriate investment strategy. However, its recent corporatization pushes it toward privatization. While the PIC is still wholly owned by the state, it is an entity that formally exists outside of the public sphere and therefore beyond its oversight. The real debate in respect of the corporatization of the PIC concerns divergent conceptions of development in the country. Broadly speaking, these positions are polarized on the appropriate role for the state in the development process. There is genuine concern about the welfare possibilities of corporatization. But in practice, the debate has now been settled in favour of a diminished role for the state and for the autonomous management of pension schemes through the corporatization of the PIC.

3. Debt, Social Spending and Development

The option to persist with a FF pension scheme has necessarily undercut the capital available for social spending and undermined the possibility of the state to contribute toward an inclusive development agenda. When such an enormous amount of money (about 30 per cent of the South African gross domestic product/GDP) is tied up in government debt to itself, then there are obviously fewer social investment opportunities, as illustrated by none other than former president Nelson Mandela.

Table 1: State debt costs (interest payments) in R billion 1999/2000–2005/2006

Type of debt	1999/2000	2000/2001	2002/2003	2005/2006
Domestic debt	42.8	44.1	45.3	46.5
Foreign debt	1.4	2.0	4.3	4.3
Other	0.1	0.1	0.05	0.05
Total	44.3	46.2	49.7	50.9
Per cent of GDP	5.5	5.1	4.9	3.5

Source: AIDC 2001; Treasury, RSA 2007a:96.

The link between government debt and the shift toward a FF pensions system was made in 1998 by COSATU in a submission to the Parliamentary Committee on Finance (COSATU 1998). In COSATU's view:

[T]he decision to prioritize the move to a pre-funded public sector pension fund, instead of prioritizing expenditure on housing, education, welfare etc., constitutes a misallocation of the scarce resources of the state and runs counter to the stated policy of reprioritizing expenditure in favour of basic needs. We therefore continue to rally support for the restructuring of the GEPP's financing mechanisms with the objective of expanding the resources available for RDP [Reconstruction and Development Programme] delivery in a manner which does not undermine the sustainability of the public sector pension system.

The minister of finance makes the same point in a more hedged manner: "[T]hus, even though I would rather be spending money on improving the quality of life of people by upgrading rural roads, urban areas, and school facilities than on debt interest repayment, as a government we have an obligation to savings and the payment of pensions" (Manuel 1999). It is difficult to estimate just how debt has influenced savings and investment in South Africa. But it is well known that the country has a very low savings rate, about 15 per cent of GDP down from about 24 per cent of GDP in the 1970s (Bhorat and Cassim 2004:24). There are always choices that have to be made in budgets and in policies. These are obviously limited in a small country seeking a place in the global investment scene. However, even within these constraints, the policy and budgetary preferences provide a clear indication of government priorities. Trevor Manuel makes the unambiguous statement that the obligation to pay pensions to public servants overrides the broader national concerns of poverty, ill-health and illiteracy. Certainly, the big apartheid bureaucrats, like director generals and other highly paid members of the civil service, have been given their golden handshakes and early retirement packages, and the apartheid criminals, many responsible for death squads, have taken early retirement on full pension (Bizos 1998).

Rhetoric and reality rarely coincide. In a presidential speech on the occasion of the budget vote in the national assembly, Thabo Mbeki made the following telling remarks. Citing Will Hutton's book, *The World We're In*, at length, he concludes:

[T]here can be no doubt about where we stand with regard to this great divide. It is to pursue the goals contained in what Hutton calls the 'broad family of ideas that might be called left' that we seek to build the system of

governance we indicated today and in previous Addresses. The obligations of the democratic state to the masses of our people do not allow that we should join those who 'celebrate individualism and denigrate the state.' We would never succeed to eradicate the legacy of colonialism and apartheid if we joined the campaign to portray the social, the collective and the public realm...as the enemies of prosperity and individual autonomy...opposed to the moral basis of society, grounded as it should be, (in terms of right wing ideology) in the absolute responsibility of individuals to shoulder their burdens and exercise their rights alone...The advances we must record demand that we ensure that the public sector discharges its responsibilities to our people as a critical player in the process of the growth, reconstruction and development of our country (Mbeki 2004).

Mbeki's sentiments are in direct contrast to the individualizing realities of the Public Investment Corporation Act. The emphasis in this piece of legislation is very clearly toward the possibility of privatization and explicitly away from the responsibilities of the public sector in development. There can be little doubt about the worth of using such an enormous amount of capital as leverage for black empowerment among the asset managers. However, even this is problematic, especially in the light of the manner in which black empowerment has led to the enrichment of very few individuals. The Secretary General of the African National Congress (ANC), Kgalema Motlanthe launched a frontal attack on black economic empowerment as "narrow based".¹⁷ Appropriately addressing the Black Management Forum, he argued, "[I]t seems that certain individuals are not satisfied with a single bout of empowerment. Instead, they are the beneficiaries of repeated bouts of re-empowerment. We see the same names mentioned over and over again in one deal after another".¹⁸ Commenting on a possible solution, he proposed that the ANC should not regard those who had benefited from empowerment deals as historically disadvantaged: "In other words, perhaps it is time to move to a situation which limits a person to one empowerment deal, at least where this involves significant quantities of state resources".¹⁹

At the National General Council of the ANC held in 2005 in Pretoria, a discussion document was tabled, with the following statement:

A difficult issue to broach, but one that must be confronted, is the capital requirements of financing black economic empowerment. ...As an illustration, suppose a black company borrows from a bank to buy 10 per cent of shares in a mining company. The mining company cannot invest in the sector for a number of reasons including domestic regulatory and policy constraints. Their only option is to buy a mine in Chile or Ghana. The financing of BEE deals that do not necessarily raise productive investment levels in the domestic economy is therefore a drain on scarce capital assets and will impact on the medium term investment level. This is just one example where policy decisions in South Africa sometimes contradict each other resulting in the failure to meet our most important objectives (ANC 2005).

The PIC very clearly involves huge quantities of public resources. Yet it is also clear that these resources are not being used productively to cater for the development needs of South Africa. The FF pension system is decidedly deleterious in terms of its role in the ongoing national debt. There can be little doubt about the extensive evidence on the direct link between the fully funded system and debt. Therefore, it appears that a state-driven design is more appropriate to meet the needs of the overwhelming majority of the population, without undermining the interests of the public sector workers and pensioners. In short, it is possible to ensure that the interests of the pensioners are met while dealing with the social challenges of unemployment and poverty.

¹⁷ Sunday Times, 1 October 2004. www.suntimes.co.za/zones/sundaytimesNEW/business/business1096606460.aspx, accessed on 13 June 2005.

¹⁸ Sunday Times, 1 October 2004. www.suntimes.co.za/zones/sundaytimesNEW/business/business1096606460.aspx, accessed on 13 June 2005.

¹⁹ Sunday Times, 1 October 2004. www.suntimes.co.za/zones/sundaytimesNEW/business/business1096606460.aspx, accessed on 13 June 2005.

4. Conclusion

This paper has provided an account of contributory public pensions in South Africa because the issue of pensions raises vital questions about the appropriate role of the state in the development process. There are contradictory pieces of evidence regarding the manner in which the democratic state in South Africa has positioned itself in terms of the development policies that it has adopted and the practices it has prioritized. In the particular case of this paper, the redistributive thrust of non-contributory pensions lies awkwardly next to the personal gain model in contributory pensions. While the former marks an unambiguous responsibility and role for the state in dealing with the vulnerable aged population through redistributory social spending, the latter points in a diametrically opposite direction toward less public accountability over the use of public funds, ostensibly in order to create an environment favourable for investment and saving.

As one of the most unequal countries in the world, South Africa faces enormous challenges, especially because of the manner in which race and poverty continue to coincide more than a decade after the demise of apartheid. One is far more likely to be poor, to be infected with HIV, to be illiterate, to be unemployed, if one is black. In a situation of such extreme disparities between wealth and poverty and between black and white, the pensions policy adopted for workers in the public sector is singularly inappropriate. The effectiveness of social policy in South Africa depends very much on the extent to which it reduces the disparities and tackles poverty. There are, of course, many different ways in which this could be done, and Mbeki's remark that "as part of the realization of the aim to eradicate racism in our country, we must strive to create and strengthen a black capitalist class" (Mbeki 1999), is an unambiguous statement of priorities in this regard.

It would be misleading to view this statement in isolation. At a recent conference of Progressive Governance held in Johannesburg, Mbeki (2005) made it plainly clear that the neoliberal paradigm was incapable of solving the problems of Africa, that market fundamentalism held many dangers for the continent and that substantial state intervention was necessary for a progressive agenda of redirecting resources from the rich to the poor. Commenting specifically on the necessity to mobilize capital and on the possible use of pension funds, Mbeki said:

When you talk about development in Africa to reconstruct and build the African economies to defeat poverty, that means capital. Obviously, as African countries, we have got to do what we have to do to make sure that we mobilize and generate capital domestically on the African Continent for these purposes. And indeed, as a project that is ongoing now, some of our people looked, for instance, at the public sector pension funds, in a number of African countries, and they found, I think it is about twelve African countries, that those pension funds, they actually manage something in the order of \$130 billion. And we have this absurd situation that some of that money is invested in stock exchanges outside of the African Continent, because it is said that there is a lack of capacity to absorb these large volumes of capital here. That is something we are working on, to say that, but yes, capital, savings of the working people of the Continent that are being used to develop countries that are already developed. We must do something about that (Mbeki 2005).

Following this line of thinking, Mbeki has recently placed the issue of repatriating African-owned capital on the agenda of the New Partnership for Africa's Development (NEPAD), especially in relation to the development of infrastructure in Africa and to encourage trade. To be sure, there are some misgivings in South Africa about the use of public sector pension funds on questionable infrastructural development where the only certainty is the massive dividends to a small coterie of extremely wealthy entrepreneurs. But the idea of a Pan African Infrastructure Development Fund that aims to raise \$1 billion from civil servants pension funds in Africa toward the building of roads, ports and telecommunications networks on the continent is a compelling one. The problem lies not in the idea itself, but in its implementation (PIC 2006).

There is an inconsistency between the progressive agenda involving social spending and dealing with poverty, on the one hand, and on the other, a commitment to developing a black capitalist class and making inroads into the white stranglehold of ownership and privilege via the route of black economic empowerment. It is crucial that the government negotiates this inconsistency in a manner which allows for a social policy that encourages economic growth while simultaneously maintaining the social imperatives for redistribution. The exigencies of legitimacy and consent demand the latter. In South Africa, precisely because of the extent of inequality and because of the manner in which the differentiation between rich and poor continues to correspond with the division between black and white, the necessity for redistribution is all the more urgent. In this regard, Mkandawire (2001:19) argues forcefully that, "states...have had to be concerned with reconciling the exigencies of accumulation with those of legitimacy and national cohesion. Consequently, the pursuit of social policies that enhance accumulation while securing the state the necessary legitimacy for political stability has constituted the cornerstone of development management". In short, it is a question of how to manage public goods and services on behalf, and in favour, of the people so as to enhance both economic growth and social inclusivity.

In this respect, there can be little doubt that an opportunity was lost concerning the management of the public pension funds. The conversion of the Public Investment Commissioners, an entity within the public sector, into the Public Investment Corporation, a corporate entity outside the public sphere, has undoubtedly closed off opportunities for redistribution through social spending. Instead, it has safeguarded the pensions of apartheid-era public workers and has enhanced opportunities for substantial benefits for a very small black bourgeoisie. This, in turn, has had the effect of widening the gap between rich and poor in the country as a whole and among blacks in particular. The entrenchment of the FF scheme has imposed an enormous debt burden on the state. It is a burden that substantially undermines the capability of the state to implement social policies designed for long-term development. In South Africa, the state has shown its hand, as the practice of corporatization of public sector pension funds batters down the rhetoric of progressive governance and concerns for redistribution to the poor.

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Interviews

The following people were interviewed:

- Patrick Heidemann, Independent Financial Consultant, East London, South Africa.
- Hilton Fisher, Communications Manager, Government Employees Pension Fund (GEPF), Pretoria, South Africa. Mr Fisher also agreed to answer written questions.
- Hylmie Daniels, Former member of the Standing and Advisory Committee on Company Law, Sub-Committee on Close Corporations, Committee on Accounting Standards and Legal Committee reporting to the Ministers of Finance, Justice and Trade and Industry, King Williamstown, South Africa.
- Ntato Mbingeleli, Principal Financial Advisor, Isibaya Fund, Public Investment Commissioners, Pretoria, South Africa.
- Tenjiwe Lucas, Investment Office, Isibaya Fund, Public Investment Commissioners, Pretoria, South Africa.
- Nicholas Biekpe, Head, Africa Centre for Investment Analysis, University of Stellenbosch, School of Business, South Africa.

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