Investment Policy Statement for the Nedgroup Investments MyRetirement Portal

NEDGROUP INVESTMENTS

1. INTRODUCTION

Retirement poses unique and complex financial challenges

Most of us look forward to our retirement. We see it as the opportunity to finally do all the things we never had time for while we worked and to enjoy life to the full. Diligently saving for your retirement throughout your career is the first step to achieving some of your retirement goals. But the decisions you make about your savings at and during retirement can be just as critical.

Managing your money during retirement involves different questions, risks and complexities that all affect one another:

Questions to answer

- Will your savings last for the rest of your life?
- Will you get enough income to live the lifestyle you want to live?
- Will you be able to accommodate changes in your circumstances?

Risks to mitigate

- **Investment risk** – the risk of your savings not growing enough because of poor returns
- **Longevity risk** – the risk of outliving your money
- **Inflation risk** – the risk of your money not keeping up with inflation, which means it's worth less and less
- **Consumption risk** – the risk of drawing too high an income and/or underestimating your expenses in retirement

Complexities to consider

- Choosing between different investment options with different pros, cons and features
- Understanding the impact of what you do today, e.g. how much income you draw, in 10 or 20 years' time
- Calculating the impact of fees and costs on your savings

In addition, developments and trends in the retirement industry in recent years add to these challenges

❶ South Africans are ill-informed about retirement	Statistics show that only 6% of South Africa's population can enjoy a comfortable retirement without extra financial support.
❷ There are more older people	In South Africa, the percentage of people over 65 has increased from 3.5% in 1980 to 5.5% today.
❸ People are living longer	It is estimated that by 2100, South Africans' life expectancy will increase by 12 years.
❹ Regulation requires that retirement funds provide guidance to retirees	Retirement funds must provide retirees with access to guidance on how their retirement savings may be applied.

The MyRetirement Portal is an easy-to-use online automated advice portal that helps you make the most of your retirement savings It enables you to complete a needs analysis, with the support of a personal retirement coach, and then provides a custom retirement plan based on the information you provided.

The portal:

- provides information on your options at retirement;
- helps you make sensible decisions about your retirement savings so that you make the most of these during your lifetime;
- provides solutions to challenges like accessing savings in the case of an emergency.

It's important to understand that the MyRetirement Portal focuses on assessing your income and liquidity needs as a retiree. It does not conduct an exhaustive needs analysis covering all your financial needs or provide a comprehensive financial plan.

The MyRetirement Portal is supported by a personal retirement coach that you can access for life.

What you can expect from the coach

Your retirement coach can be either of the following:

Someone who provides retirement benefit counselling services

This includes:

- guiding you to create and refine a retirement plan based on your needs using the MyRetirement Portal – the online automated advice tool;
- helping you to implement your retirement plan with Nedgroup Investments (if appropriate);
- helping you review your retirement plan once a year and guiding you on any decisions you need to make such as choosing your income for the next year, if you are able to change this;
- being available to explain concepts and terminology used on the portal that you don't understand; and
- sharing articles that may be of interest to you throughout your retirement.

OR

A registered financial planner

The planner provides holistic advice on all your financial needs in retirement and uses the MyRetirement Portal to support their advice process.

2. SCOPE AND PURPOSE

This investment policy statement (IPS) maps out the investment strategy used by the MyRetirement Portal. The IPS defines the investment framework and how your needs are taken into consideration in arriving at the recommended investments. The IPS also defines the governance framework of the investment recommendation, for example the setting of an appropriate asset allocation, monitoring the retirement plan, risk management and reporting. It also assigns accountabilities to all the different parties and entities involved in implementing the retirement plan. One of the most important functions of the IPS is to provide objective guidance and a course of action during times of market turmoil when your emotions may drive you not to act prudently. It is therefore the document that can always be referred to when you are uncertain so that you can stay on course.

3. GOVERNANCE

Nedgroup Investment Advisors Proprietary Limited (NIA) is responsible for all stages of the investment policy development and implementation. NIA will continuously monitor the appropriateness of the investment policy for the MyRetirement Portal and make changes where necessary. A key part of the investment policy is setting an appropriate asset allocation to sustain the recommended income over your expected lifetime. NIA will continuously monitor the appropriateness of the strategic asset allocation and all the assumptions that goes into determining this allocation.

The implementation of the recommended retirement plan will utilise different Nedgroup Investments risk profiled unit trust portfolios. NIA is also responsible for ensuring that these portfolios are managed in accordance to their mandates and will monitor the relevant fund managers on an ongoing basis, whether they are internal or external.

The MyRetirement Portal allows you to update your financial needs such as back-up plans and dependants that you support. If your circumstances change and are updated into the MyRetirement Portal, your recommended retirement plan will be reassessed.

4. INVESTMENT, RETURN AND RISK OBJECTIVES

4.1 OVERALL INVESTMENT OBJECTIVE

The MyRetirement portal recommends taking some your retirement savings as a cash lump sum and investing the remainder in a compulsory annuity which provides an income. We recommend allocating your cash lump sum to various needs (such as debt repayment, emergency savings) and that you invest any excess cash after meeting these needs in a unit trust. If there is no excess cash then there won't be a unit trust recommendation. From the unit trust, you can make regular withdrawals to supplement your income. Any reference to income includes the regular withdrawals from the unit trust and the income from your annuity.

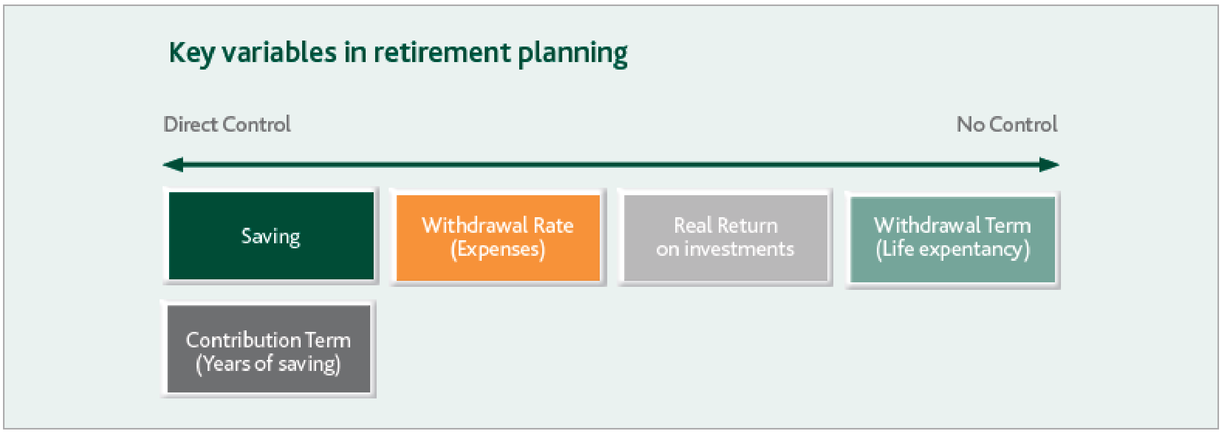
The MyRetirement Portal will focus on two different investment objectives:

- Providing a sustainable income for life;
- Saving for an emergency

We will cover each of these objectives separately below.

4.1.1 PROVIDING A SUSTAINABLE INCOME FOR LIFE

In order to set the investment objective to determine whether an income is sustainable for life the MyRetirement Portal sets a confidence level that is determined by inputs in the tool. Our definition of a sustainable income is an income that will keep pace with inflation over your lifetime.



(Source: Daniel R Wessels, Make-or-break retirement planning, 2011)

Determining a sustainable retirement income is difficult as it is influenced by variables that you have limited control over, such as your real investment returns and withdrawal term (life expectancy). Given that both returns and term influence the outcome, we developed a model that accounts for a range of different investment outcomes and lifetimes. The simulated returns are real returns, so inflation risk is implicitly accounted for. These simulated lifetimes take account of your age, gender and whether you have a serious medical condition. The results are a number of scenarios; in some scenarios the income will be sustainable for life and others not.

Our aim is to recommend an income where there are more sustainable scenarios than unsustainable scenarios. On the extreme, we could be very conservative and target 100% confidence level. This would mean you need to either invest your money in a guarantee product called a *life annuity* or take a very low income that in the majority of scenarios is far below what you could have sustained. So, you can see that there is a trade-off between the level of income and the confidence level. For people that feel a guarantee is very important, the MyRetirement portal will recommend a guaranteed annuity.

Therefore, we have aimed to balance these competing objectives of income and confidence level. The appropriate balance will depend on whether you have a back-up plan. If you do not have a back-up plan, then a higher confidence level is appropriate as you are fully reliant on this income. However, if you have a back-up plan you are able to target a lower confidence level as you have another means of providing an income.

Based on this model, the MyRetirement portal will make an income recommendation which includes:

- The Rand value of any excess cash that should be invested in a unit trust (if applicable)
- Which unit trust to invest in (if applicable)
- The monthly withdrawal that you should take from your unit trust (if applicable)
- The Rand value that should be invested in a compulsory annuity and the compulsory annuity that best meets your needs according to your survey answers
- The unit trust where you should invest your annuity savings. Note that this does not apply when the recommendation is a life annuity.
- The recommended monthly income to draw from your annuity.

Once the recommendation has been made, you will be allowed to change some of the retirement variables such as your cash needs, monthly income, unit trust monthly withdrawal, the percentage you leave to dependants (if applicable) or the underlying investment portfolios to see how they impact your chances of having a sustainable income for life.

4.1.2 SAVING FOR AN EMERGENCY

If you indicated that do not have sufficient money set aside for an emergency, we recommend setting aside some of your cash lump sum for unexpected expenses in the event of an emergency. We recommend investing this in an enhanced cash investment portfolio. We recommend an enhanced cash portfolio as it is expected to provide you with a higher return than a money market portfolio but still provide adequate liquidity in terms of limiting the risk that the timing of your withdrawal may be when markets are down, resulting in a loss.

4.2 INVESTMENT STRATEGY AND CONSIDERATIONS

The Investment framework employed in the MyRetirement Portal will have the following characteristics:

Designed with the investment objective in mind

The portfolios were each designed with a clear objective which incorporate the purpose of the investment, the retiree's income, their expected life time and the risk-return profile of the various asset classes. These factors were combined to determine the appropriate asset mix and a reasonable long-term strategic asset allocation was set for each of the portfolios to achieve their respective investment objectives.

Diversification for risk management

The portfolios offer retirees exposure to a range of domestic and offshore asset classes, which include equity, listed property, bonds, inflation – linkers and cash. Diversification across and within asset classes help reduce the risk within each portfolio.

Unit trust portfolios

Collective Investment Schemes such as unit trust have many benefits such as:

- Governance since they are regulated, and daily compliance is done on portfolios to make sure that they are managed according to their mandates
- Tax efficiency as Capital Gains on winners and losers are netted off within the portfolio and all fees are first deducted before income and dividend are declared.
- Daily liquidity.

The investment framework can be implemented through different types of investment strategies: Low-cost passive, or multi-manager strategies. As the target audience of the MyRetirement Portal includes the end client (retiree) and intermediaries such as financial planners, our recommendations will be into the Low-cost passive or multi-manager strategies.

The reasons for using the *Nedgroup Investments Core range* as the low-cost passive option within the MyRetirement Portal are:

Low costs

The investment management fees charged in the MyRetirement Portal when using these portfolios is 0.40% (including VAT) for the unit trust and 0.58% (including VAT) for compulsory annuity. The portfolios use a cost-efficient rebalancing strategy to maintain the strategic asset allocation and underlying asset class benchmarks weightings This leads to an Estimated Annual Cost (EAC) of just under 1% which includes investments, automated advice and administration. This amounts to a total cost saving of between 1% to 2% per annum.

Simplicity and transparency

The Core portfolios are rules-based portfolios which means that their asset allocation and stock selection are determined by pre-defined rules and indices. This removes the complexity of manager selection, especially to the MyRetirement Portal target market of non-professional investors who are not in the position to pick the next top performing portfolio manager.

Investor behaviour

Numerous international studies have shown that low cost rules-based portfolios (passive funds) typically deliver better investor returns because of investor expectations [1].

The reasons for using the *Nedgroup Investments XS Select range* as the multi-manager option within the MyRetirement Portal are:

Access to external fund managers

[1] For example, the *Morningstar 2016 Global Asset Flows Report* showed that passive funds have not just outperformed on an absolute return basis over the past 10 years, their investor returns have also been higher.
In fact there is a high correlation between costs, fund returns and investor returns.

Many investors and intermediaries prefer to diversify their investments across different fund managers. The XS Select range caters for this need by investing across four actively managed funds and one passive (the Core range described above).

Ongoing monitoring

There is continuous evaluation of external managers' ongoing performance and period re-evaluation of their process. A complete due diligence is also completed bi-annually.

Cost and tax efficient structure

The XS Select range offers investor a fund of fund structure where the underlying funds could be changed if required without the tax implication of standalone funds.

A list of additional investment options across different risk profiles and investments strategies will be made available to investors wishing to opt of the recommended portfolios, for example where financial advisor have performed a comprehensive needs analysis.

4.2.1 RETURN, DISTRIBUTION AND RISK REQUIREMENTS

The Nedgroup Investments unit trust portfolio ranges described above have been designed to cater for different return and risk requirements so that they can be easily incorporated into the needs analysis within the MyRetirement Portal. The risk and return characteristics of the Core and XS ranges are as follows:

1. **Growth portfolio**: A traditional balanced portfolio that targets returns of inflation + 4 to 6% p.a. over rolling five-year periods. The combined strategic equity and listed property allocation is 75%. This portfolio distributes income bi-annually and will typically be recommended for investment horizons of 5 years and longer.
2. **Moderate portfolio**: A moderate balanced portfolio that targets returns of inflation + 3 to 5% p.a. over rolling four-year periods. The combined strategic equity and listed property allocation is 58.5%. This portfolio distributes income bi-annually and will typically be recommended for investment horizons of 4 years and longer.
3. **Conservative portfolio:** A conservative balanced portfolio that targets returns of inflation + 2 to 4% p.a. over rolling three-year periods. The combined strategic equity and listed property allocation is 42%. This portfolio distributes income quarterly and will typically be recommended for investment horizons of 3 years and longer.
4. **Income portfolio:** An income portfolio that targets returns of inflation + 1 to 3% p.a. over rolling two-year periods. The combined strategic equity and listed property allocation will be limited to 21%. This portfolio distributes income quarterly and will typically be recommended for investment horizons of 2 years and longer.
5. **Cash portfolio:** An enhanced money market portfolio that targets returns of inflation + 1 to 2% p.a. over rolling one-year periods. The portfolio only invests in cash instruments. This portfolio distributes income monthly and will typically be recommended for investment horizons of between 0 – 2 years.

4.2.2 CAPITAL AND INCOME RISK

The primary risk a retiree faces is that their income is not able to keep pace with inflation for life. Investment returns and the volatility thereof play a big part in whether a retiree can sustain their income or not.

It is important to bear in mind that although a retiree is drawing a regular income from their savings, the income we recommend is a relatively small portion and the majority of the savings remain invested in any given year. Therefore, retirees are still typically long-term investors with the life expectancy of a 60-year old female being approximately age 90 and the life expectancy of a 60-year old male is approximately age 85[2].

[2] Based on South African life expectancy of compulsory annuity policyholders

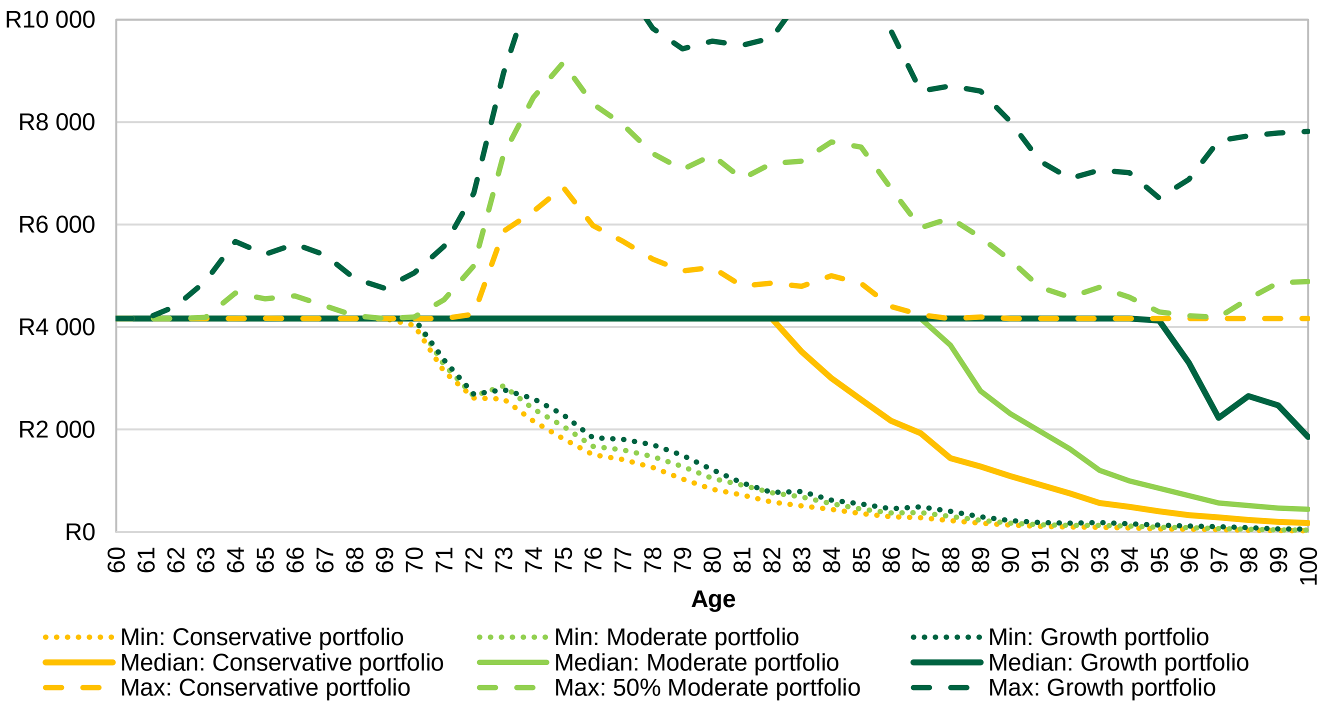
The implication of this is that a retiree should ideally be invested in a portfolio that is designed for a longer time horizon. To illustrate that this is a valid assumption in the context of drawing an income, we have included charts that show the range of income and capital in real terms for a 60-year old male with R1 million and a starting income of R4,167 (5% pa drawdown). These charts are shown for both annuities where an investment recommendation is appropriate; a *Living Annuity* and the *Living Annuity Plus*[3]. The charts contain the outcomes for 3 different portfolios.

Risk Profile	Portfolio	Real return target (net of fees)	Minimum required time frame
5	Growth portfolio	5%	5 years
4	Moderate portfolio	4%	4 years
3	Conservative portfolio	3%	3 years
1	Cash Portfolio	1%	1 year

You will notice that the capital risk of all three portfolios in the worst outcomes are fairly similar, but the median outcome and best outcomes are considerably better for the Growth portfolio than for the Moderate and Conservative portfolios. Similarly, the median outcome and best outcomes are considerably better for Moderate portfolio than for the Conservative portfolio.

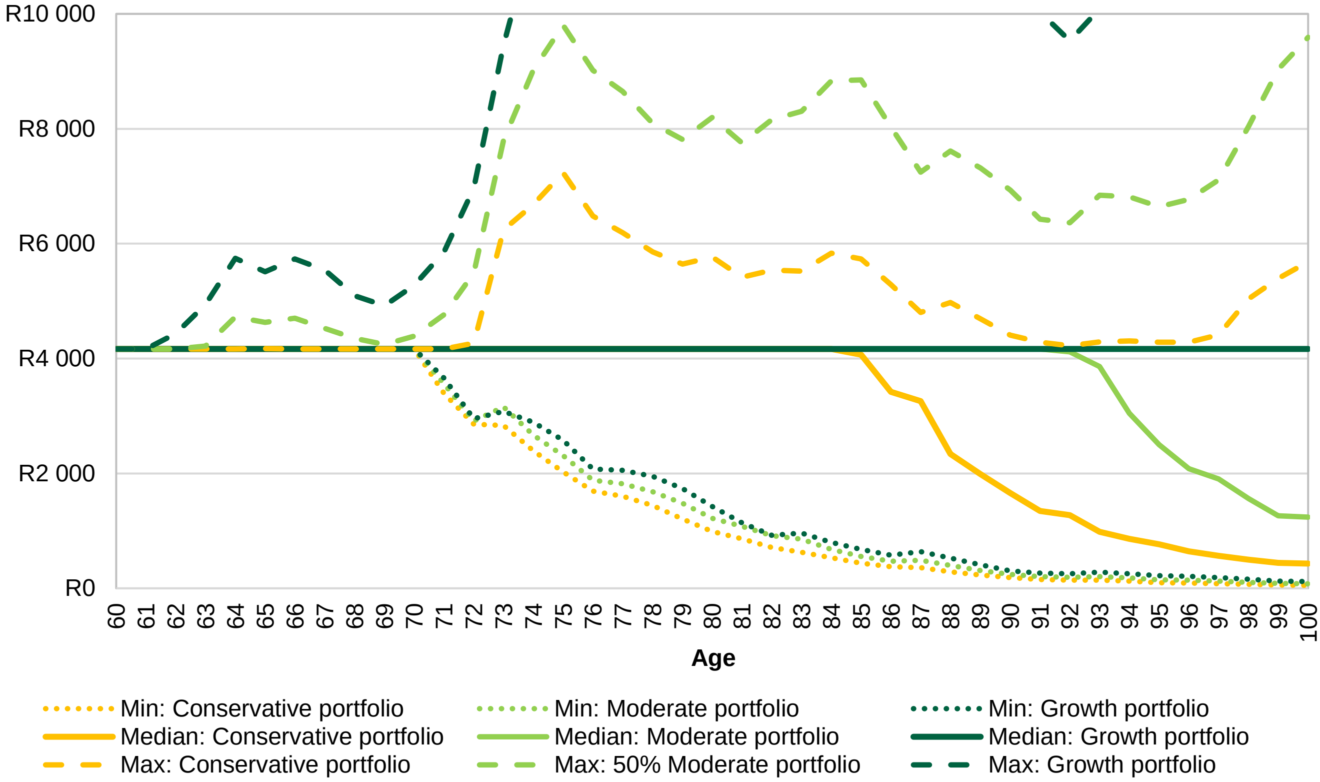
The same principles are observed in the income charts. For this reason, our recommendation is to invest both the unit trust (if applicable) and the annuity savings in the Growth portfolio.

Living Annuity: real income per month

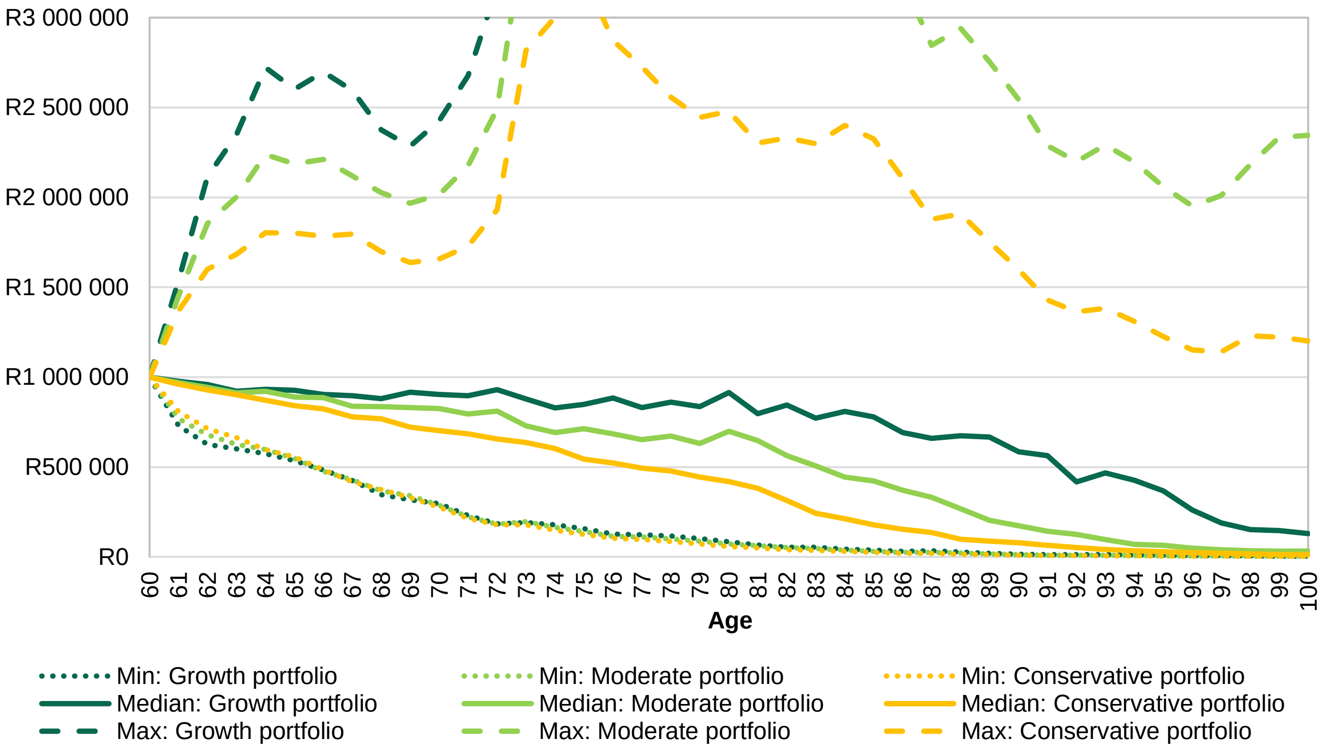


Living Annuity Plus: real income per month

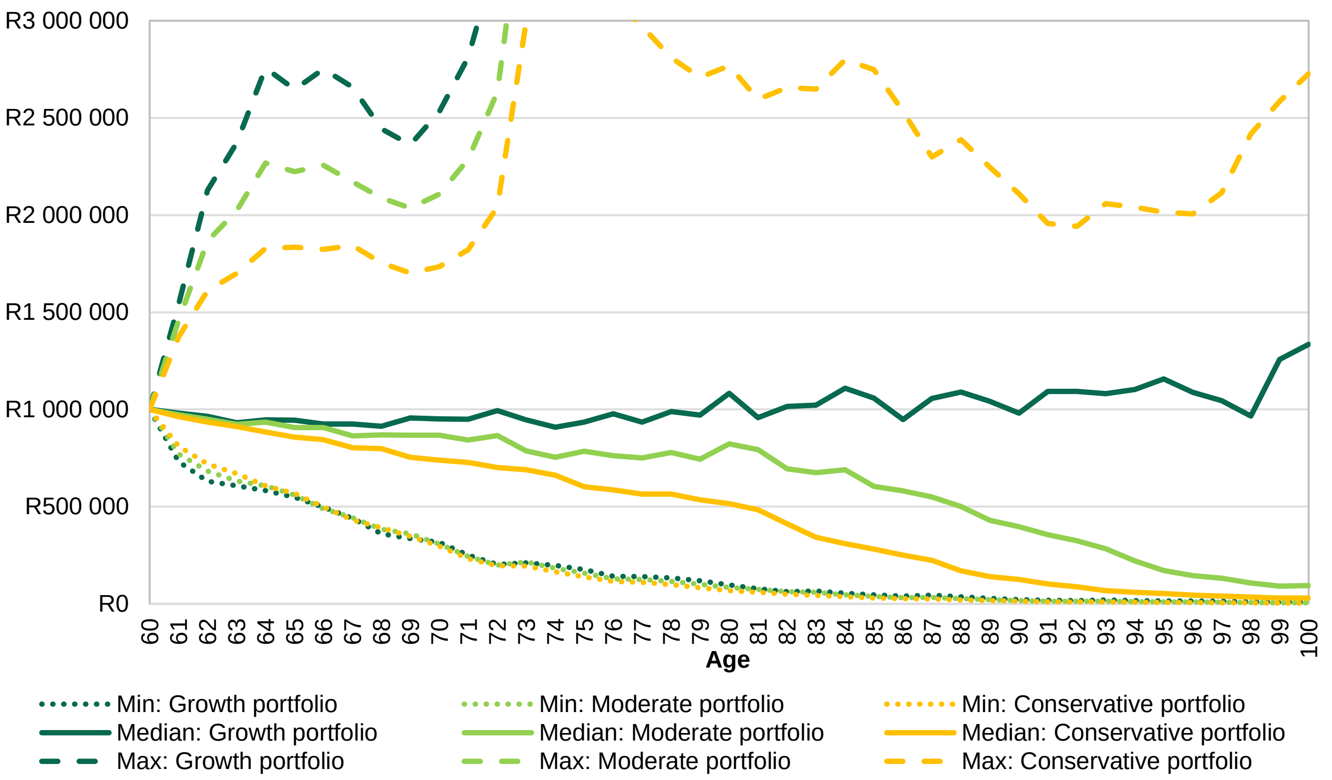
[3] The elected % to dependants is 70% in the charts



Living Annuity: real capital



Living Annuity Plus: real capital



4.3 INVESTMENT CONSIDERATIONS AND CONSTRAINTS

The MyRetirement Portal will use unit trust portfolios in three different investment vehicles:

- Living Annuity or Living Annuity Plus
- Directly for unit trust component of retirement savings
- Directly for discretionary emergency savings

Each of these three have different tax treatments and are subject to various rules and constraints. The different tax treatments are summarised in the table below:

Investment vehicle	Entry: Contribution	During: Investment term	Exit: Withdrawal/ termination
Living Annuity & Living Annuity Plus	Tax-free transfer in	Not taxed	Income: taxed at your marginal rate of tax Death benefit: taxed as a retirement lumpsum
Discretionary	After-tax contributions	Subject to tax: interest and dividends	Subject to tax: capital gains

Living Annuity and Living Annuity Plus

Living annuities can only be purchased from an approved retirement fund (ie. Pension fund, provident fund and a preservation fund). You cannot purchase a living annuity with discretionary funds. You can choose an income every year of between 2.5% and 17.5%. On death any remaining benefit will be paid out to you nominated beneficiary. A living annuity can only be fully accessed if your fund value is less than R50 000 (if you have not taken a lumpsum on retirement) or R75 000 (if you have not taken a lumpsum on retirement).

Discretionary Investments (unit trusts)

Discretionary investments for emergency funds are liquid and can be accessed at any time. The investor must take cognisance of annual tax exemptions on interest and capital gains taxes.

4.3.1 LIQUIDITY AND TAX CONSIDERATIONS FOR LIVING ANNUITIES

The liquidity is covered in the section above. Your investment in your Living Annuity or Living Annuity Plus is tax free. However, any income taken from these annuities will be taxed as per the income tax tables.

4.3.2 LIQUIDITY AND TAX CONSIDERATIONS FOR UNIT TRUSTS AND EMERGENCY SAVINGS

Savings for an emergency and the unit trust component of your retirement savings are a liquid investment vehicle. The investors may use either savings to pay for unforeseen expenses. Discretionary investments are therefore the most suitable investment vehicle for these forms of savings.

The investor must take cognisance of annual tax exemptions on interest and capital gains taxes.

5. RISK MANAGEMENT

5.1 PERFORMANCE MANAGEMENT AND REPORTING

The MyRetirement Portal uses the Nedgroup Investment Core and XS Select ranges for its investment recommendations as these unit trust portfolios have been designed to fit into a financial planning process. These ranges are continuously monitored to ensure that they continue to deliver in line with their stated objectives. There are two primary facets of the monitoring process:

- Firstly, Nedgroup Investments Advisors (NIA) continuously evaluate the fund managers' ongoing performance and periodically re-evaluate their process. NIA also do a complete due diligence of all potential managers on regular basis.
- Secondly, NIA reviews the strategic asset allocation and asset class benchmarks of the portfolios on a regular basis.

The Nedgroup Investment Core and XS Select Ranges are unit trust portfolios so their performance, latest asset allocation and distributions are published monthly on a Minimum Disclosure Document (MDD or factsheet) while the detailed portfolio holdings are published quarterly. All these documents are available from the Nedgroup Investments website www.nedgroupinvestments.com.

The performance of the retiree's investment vehicles and that of the underlying unit trust portfolios are available once the retiree registers on the Nedgroup Investments website and reflected in an investment statement that is sent to the retiree on a quarterly basis.

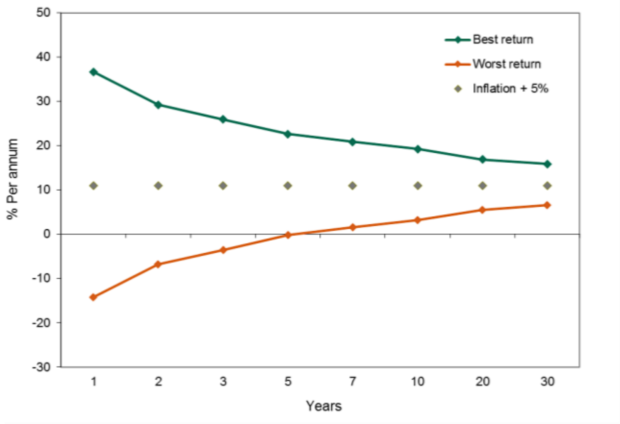
5.2 RISK METRICS FOR MEASUREMENT AND EVALUATION

There are a number of risk metrics used to evaluate the risk within the investors' portfolios. The most common risk measure is the standard deviation of returns over statistically meaningful periods of 3 years or longer. The range of volatility which the portfolios may experience is summarised below.

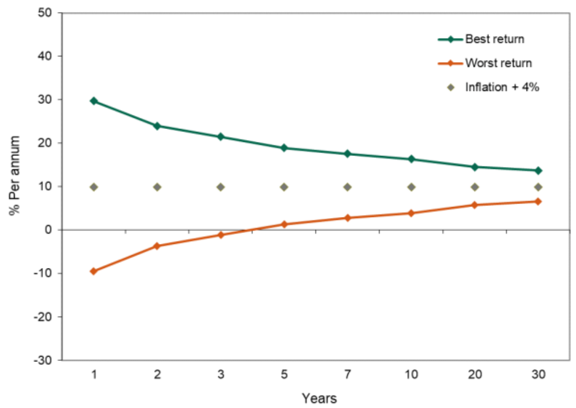
Table 5.1

Portfolio	Rolling 3 year annualised standard deviation using monthly returns from 1960 – 2017			
	Median	67% confidence range	Maximum	Minimum
Growth Portfolio	12.5%	8.7% - 16.3%	19.4%	5.2%
Moderate Portfolio	9.5%	6.4% - 12.5%	15.5%	4.0%
Conservative Portfolio	7.0%	4.8% - 9.3%	11.6%	2.8%
Cash portfolio	0.5%	0.1% - 0.8%	1.6%	0.1%

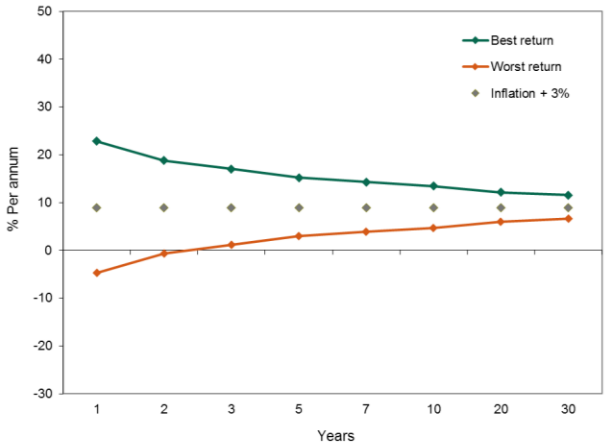
GROWTH PORTFOLIO RANGE OF RETURNS



MODERATE PORTFOLIO RANGE OF RETURNS



CONSERVATIVE PORTFOLIO RANGE OF RETURNS



CASH PORTFOLIO RANGE OF RETURNS