NAMFISA
NAMIBIA FINANCIAL INSTITUTIONS SUPERVISORY AUTHORITY

EXPLANATORY MEMORANDUM

TO : PUBLIC

DATE : 16 FEBRUARY 2024

SUBJECT : PROPOSED AMENDMENTS TO THE LONG-TERM INSURANCE REGULATIONS

1. INTRODUCTION

1.1 This Explanatory Memorandum pertains to the proposed amendments to the regulations under the Long-term Insurance Act, 1998 (Act No. 5 of 1998) (“the Act”) and is issued by virtue of the functions and powers of the Namibia Financial Institutions Supervisory Authority (“NAMFISA”) and those of its Chief Executive Officer, in his capacity as the Registrar of Long-term Insurance (“the Registrar”) in terms of the Act, read with the Namibia Financial Institutions Supervisory Authority Act, 2001 (Act No. 3 of 2001).

1.2 The purpose of this Explanatory Memorandum is to serve as an explanatory note to the proposed draft amendments to the regulations under the Act as well as to solicit comments on the proposed amendments.

1.3 Should you have any queries pertaining to this Explanatory Memorandum, kindly contact Mr. Floris Fleermuys at ffleermuys@namfisa.com.na or via Tel: 061-290 5110 or Ms. Irene Shebo at ishebo@namfisa.com.na or via Tel: 061-290 5119.

2. EXPLANATION OF MAIN PROPOSED AMENDMENTS

2.1 BACKGROUND TO REGULATIONS 15 AND ANNEXURE C

2.1.1 Section 72(1)(n) of the Act empowers the Minister of Finance to make regulations relating to minimum or maximum or both minimum and maximum amounts which a registered long-term insurer or reinsurer may invest in particular assets or in particular kinds or categories of assets whether in Namibia or elsewhere, and prescribing the basis on which the amount shall be

determined and defining the kinds or categories of assets to which the amount applies.

2.1.2 The aim of Regulation 15 is to ensure that assets backing policyholders liabilities are invested in a prudent manner that not only protects the policyholders interest, by offering protection from the effects of poorly diversified investment portfolios, but is channelled in ways that achieve economic development and growth. To achieve this, the regulation limits the extent to which registered long-term insurers and reinsurers may invest in particular assets or asset classes.

2.1.3 Since its introduction, the regulation and the annexure thereto, have been amended several times after Namibia gained independence from South Africa on 21 March 1990. The investment universe has drastically changed over the last 3 decades, while permissible asset classes and prudential limits for institutional investors, specifically insurers, have largely remained somewhat stagnant, not considering the evolution of risks and new, more innovative, products in the financial markets. As a result, insurers and reinsurers find it more difficult to comply with regulation 15, because of its archaic nature.

2.1.4 The various amendments to the regulation and the annexure thereto over the last 30 years have failed to cater for new and innovative instruments in the investment landscape, both locally and internationally. In this regard, these proposed amendments aim to review the regulation and the different asset classes it prescribes, considering investor needs as well as government objectives.

2.1.5 NAMFISA carried out a study to establish the adequacy of the current investment asset classes for the pension funds industry. The said study resulted in a finding that additional asset classes must be introduced to broaden the current investment framework. In light of the fact that the long-term insurance industry is exposed to similar risks as pension funds, it was deemed appropriate to propose the same amendments in regard to additional asset classes for long-term insurers as for pension funds. Therefore, the references made to the pension funds industry in this Circular is on the basis of the aforesaid.

The current regulation

2.1.6 Regulation 15 prescribes the maxima for various types of investment that may be made by a registered long-term insurer or reinsurer. They are intended to guide insurers or reinsurers who invest assets backing policyholder liabilities.

These maxima relate to the market value of the assets, backing policyholder liabilities, which are held by insurers and are broadly:

(i) No more than 90% may be invested in credit balances;
(ii) No more than 50% may be invested in corporate bonds;
(iii) No more than 75% may be invested in shares;
(iv) No more than 25% may be invested in property;
(v) No more than 90% may be invested in a combination of equities and property;
(vi) No more than 10% may be invested in a large capitalization listed equity, and 5% in a small capitalization listed equity;
(vii) No more than 25% may be invested with any single bank;
(viii) No more than 2.5% may be invested in “other assets”; and
(ix) No more than 3.5% may be invested in unlisted investments.

2.1.7 Furthermore, structured products like derivative instruments, hedge funds and private equity funds are not explicitly catered for in the regulation, leaving them to be categorized under the category of “other assets”, and no guidance is provided as to how such products may be employed.

2.1.8 The evolution of capital markets across the world and the recent financial crises brought about key lessons in ensuring that investment portfolios of long-term insurers and reinsurers are well diversified. In this regard, many jurisdictions have reviewed their regulations in terms of portfolio limits for long term insurers and reinsurers.

2.1.9 Long term insurers’ current exposures are well below the existing asset class prudential limits apart from the “other assets” category, for which some long-term insurers and reinsurers have exceeded the ceiling limit. This is mainly owed to investments in instruments that are not explicitly catered for in the regulation, and thus reported as “other assets”, which resulted in the limit being exceeded.

2.1.10 It is, therefore, deemed appropriate to introduce additional asset classes, and in some cases to adjust the limits of existing asset classes, to ensure entities’ ability to invest within a broader framework for diversification.

2.2 PROPOSED AMENDMENTS TO REGULATION 1 - DEFINITIONS

Regulation 1 is amended by the insertion of and/or amendment of the following definitions (amendments illustrated by underlined italics and strike outs):

2.2.1 Amendment of paragraph (b) from regulation 15(3)(a)(ii) to regulation 15(17)(b), which is the correct reference.

2.2.2 Amendment of the definition of "banking institution" to clarify that these make reference to the new banking institutions Act, which is the Banking Institutions Act, 2023 (Act No.13 of 2023).

2.2.3 Amendment of the following paragraph of the definition of "domestic asset":

(h) item *9* (associated companies and joint ventures) where such investment constitute shares in, loans to and convertible debentures of associated companies in Namibia;

2.2.4 Insertion of the word "currencies" in the following definition of "exchange traded fund":

"exchange traded fund" or "ETF" means a listed investment product that tracks the performance of a group or 'basket' of underlying shares, currencies, bonds or commodities;

2.2.5 Insertion of the following definition of "derivative instrument":

"derivative instrument" *means any financial instrument or contract that creates rights and obligations and –*

(a) that derives its value from the price or value of; or

(b) the value of which may vary depending on a change in the price or value, of; some other particular product or thing;

2.2.6 Amendment of the following paragraphs of the definition of "domestic asset":

(a) Item 1 (credit balances) where such balances are held in Namibia *and denominated in Namibian currency;*

(b) item 2 (Namibian Government and Bank of Namibia Bonds) where such bonds are denominated in any currency, and wherever issued and purchased;

(c) item 3 (Multilateral development bank Bonds) where such bonds are denominated in Namibian currency, and issued and purchased in Namibia;

(d) item 4 (State owned enterprises, statutory body, public enterprise, local authority and regional council bonds) where such bonds are denominated in Namibian currency, and issued and purchased in Namibia;

(g) item 8 (shares) where such shares are in a company incorporated in Namibia and, subject to regulation 15(4) and (5), includes shares in a company incorporated outside Namibia if such shares assets have been acquired on a stock exchange licensed under the Stock Exchanges Control Act;

(h) item 9 (associated companies and joint ventures) where such investment constitute shares in, loans to and non-convertible debentures of associated companies in Namibia;

(i) item 11 (commodities) where such commodities are listed on a stock exchange licensed under the Stock Exchanges Control Act;

(j) item 13 (other structured products) where such investments are held in Namibia;

(k) item 14 (other claims) where such claims are against natural persons resident in Namibia and companies incorporated in Namibia;

(m) item 15 (other assets) where such other assets that are classified under item 12 are held in Namibia;

2.2.7 Insertion of the following definition of "*exchange traded fund*":

"exchange traded fund" or "ETF" means a listed investment product that tracks the performance of a group or 'basket' of underlying shares, bonds or commodities;

2.2.8 Insertion of the following definition for "exchange traded note":

"exchange traded note" means an exchange-traded debt instrument that grants investors access to a wide spectrum of assets;

2.2.9 Insertion of the following definition of "foreign unit trust scheme":

"foreign unit trust scheme" means any scheme or arrangement, in whatever form, including an open-ended investment company, carried on in a country other than Namibia, in pursuance of which members of the public are invited to acquire an interest or undivided share (whether called a unit or by any other name) in one or more unit portfolios and to participate proportionately in the income or profits derived therefrom, whether the value of such interest, unit or undivided share which may be acquired remains constant or varies from time to time;

2.2.10 Insertion of the following definition of "fund of hedge funds":

"fund of hedge funds" means a portfolio that invests only in hedge funds, but may also hold notes, coins and a balance or deposit in a savings, current or money market account with a banking institution, and subject to conditions as may be prescribed;

2.2.11 Insertion of the following definition of "fund of private equity funds":

"fund of private equity funds" means a portfolio that invests only in private equity funds, but may also hold notes, coins, and a balance or deposit in a savings, current or money market account with a banking institution, and subject to conditions as may be prescribed;

2.2.12 Insertion of the following definition of "hedge fund":

"hedge fund" means an asset which-

(a) *uses any strategy or takes any position that could result in the portfolio incurring losses greater than its fair value at any point in time, and which strategies or positions include but are not limited to leverage and net short positions; and*

(b) *is subject to conditions as may be prescribed;*

2.2.13 Insertion of the following definition of "investment manager":

"investment manager" means an investment manager as defined in the Determination of conditions in terms of section 4(1)(f) of the Stock Exchanges Control Act;

2.2.14 Insertion of the following definition of "investments":

"investments" for purposes of regulation 15(6), means assets or items acquired or held with the goal of generating income or appreciation.

2.2.15 Insertion of the following definition of “leverage”:

“leverage” means the use of securities, including derivative instruments, short positions or borrowed capital to increase the exposure beyond the capital employed to an investment;

2.2.16 Insertion of the following definition of “long position”:

“long position” means the situation in which a person holds or will hold more securities than such person has contracted to sell or, in respect of options, where such person has bought rights which exceed the rights sold;

2.2.17 Insertion of the following definition of “management company”:

“management company” means a management company as defined in the Unit Trusts Control Act, 1981 (Act No. 54 of 1981);

2.2.18 Insertion of the following definition of “multilateral development bank”:

“Multilateral development bank” means the World Bank Group, the International Monetary Fund and the African Development Bank;

2.2.19 Insertion of the following definition of “over-the-counter instruments”:

“over-the-counter instruments” means securities traded between two counterparties executed outside of a licensed exchange;

2.2.20 Insertion of the following definition of “private equity fund”:

“private equity fund” means a pool of capital that-

(a) has as its main business the making of equity, equity orientated or equity related investments in companies incorporated outside Namibia and not listed on an exchange to earn income and capital gains; and

(b) is subject to conditions as may be prescribed;

2.2.21 Insertion of the following definition of “short position”:

“short position” means a bear sale as defined in the Stock Exchanges Control Act;

2.2.22 Amendment of the following definition of “state-owned enterprise”:

"State-owned enterprise" means an entity that is named in Schedule 1 to the *Public Enterprises Governance Act* State-owned Enterprises Governance Act, 2006 (Act No. 2 of 2006);

2.2.23 Insertion of the following definition of "uncovered position":

"uncovered position" means a position in which an asset needed to settle a derivative contract is not held for the duration of the contract

2.3 PROPOSED INSERTION OF NEW SUB-REGULATION 2

Insertion of new sub-regulation (2) of Regulation 15 to clarify that the investment limits in Annexure C only apply to policyholder assets as opposed to shareholder assets;

2.4 PROPOSED DELETION OF SUB-REGULATION 8

Deletion of Old Regulation 15(8) requirement to obtain approval from the Registrar to re-classify an investment. The rationale for this deletion is that an insurer found wanting (not complying with the limits imposed by the Regulations) will naturally alter the portfolio and change investment strategies where necessary in order to comply with the investment limits. Thus, requiring the Registrar's approval for the reclassification of an investment is not very practical to enforce for the insurance industry.

2.5 PROPOSED AMENDMENTS TO REGULATION 15 – LIMITS OF INVESTMENT

2.5.1 Due to the insertion of additional provisions in regulation 15 and the introduction of additional asset classes to Annexure C to the regulations, the numbering and referencing of certain provisions have been amended accordingly.

2.5.2 Regulation 15(1) is amended as follows (amendments illustrated by underlined italics and strike outs):

15 (1) The value of the assets which every registered insurer and every reinsurer is, subject to the provisions of sub-regulation (~~5~~*6*), required to hold ~~in respect of its long-term insurance business~~ in terms of sections 26 and 27 of

the Act, shall not, in respect of the kinds or categories of assets set out in Column 2 of Annexure C, exceed the percentage set out opposite each such

kind or category of asset in Column 3 of that Annexure, which percentage expresses a maximum percentage of the aggregate liabilities of the ~~long-term insurance business~~ of the registered insurer or reinsurer, except for assets of the kind or category referred to in item 10 where the percentage expresses a percentage of the market value of the investments of the registered insurer or reinsurer, but -

(a) assets of the kinds or categories referred to in items ~~6~~, *7, 8* ~~to~~, 9, *14*, *15* inclusive, in Column 2 of that Annexure ~~held in respect of long-term insurance business~~ shall not exceed 95 per cent of the aggregate liabilities of the ~~long-term insurance business~~ of the registered insurer or reinsurer;

(b) assets of the kinds or categories referred to in items ~~6~~ ,*7* ~~and 7~~*8, 13* and *14* in Column 2 of that Annexure ~~held in respect of long-term insurance business~~ shall not exceed 90 per cent of the aggregate liabilities ~~of the long-term insurance business~~ of the registered insurer or reinsurer; *and*

(c) *assets of the kinds or categories referred to in items 11, 12 and 13 in Column 2 of that Annexure ~~held in respect of long-term insurance business~~ shall not exceed 15 per cent of the aggregate liabilities ~~of the long-term insurance business~~ of the registered insurer or reinsurer*

2.5.3 Regulation 15(6) is amended by increasing the upper limit for unlisted investments from 3.5 per cent to 5 per cent. The 5 per cent limit is also in line with those of regional peers (other SADC jurisdictions, namely Botswana, Kenya, South Africa, Tanzania and Uganda).

2.5.4 Insertion of new subregulation (7) of Regulation 15 to clarify that all the unlisted investments an insurer or reinsurer makes pursuant to subregulation (6) must solely be used to finance activities of portfolio companies within Namibia for purposes of local economic development and that such investments may not be transferred directly or indirectly out of Namibia in any form or manner.

2.5.5 Insertion of new subregulation (9) of Regulation 15 to clarify that an insurer or reinsurer will only be considered to have complied with the unlisted investment requirement if it has actually made investments in an unlisted company and such investments fall within the limits prescribed in subregulation (6);

2.5.6 With the introduction of new asset classes to Annexure C, such as hedge funds, private equity funds and derivative instruments, regulations 15(9), 15(10), 15(11) and 15(12) were inserted to address, to a certain extent, any additional risks which the new asset classes may pose to registered insurers or reinsurers:

15(10) A registered insurer or reinsurer must not invest or contractually commit to invest in an asset, including a hedge fund or private equity fund, where the registered insurer or reinsurer may suffer a loss in excess of its investment or contractual commitment in the asset.

15(11) Hedge funds and private equity funds that may expose the registered insurer or reinsurer to liability must be held in a limited liability structure.

15(12) A hedge fund must be operated by a management company registered under the Unit Trusts Control Act, 1981 (Act No. 54 of 1981) and must be managed by an investment manager approved under the Stock Exchanges Control Act, 1985 (Act No. 1 of 1985).

15(13) Despite subregulations (10) and (11), a registered insurer or reinsurer may invest in derivative instruments, subject to the following conditions –

(a) the investment is made solely for purposes of reducing investment risk or various liability risks, or for efficient portfolio management, and may not be used for purely speculative purposes;

(b) no leverage may be used;

(c) at no time must there be uncovered positions, taking the registered insurer's or reinsurer's liability position into consideration;

(d) long positions must be fully covered by cash and short positions must be fully covered by the actual underlying asset;

(e) exposures may only be offset to the extent that they are exact and the reasonable correlation of assets is not enough to offset exposures;

(f) over-the-counter instruments should also be appropriately collateralized and a registered insurer or reinsurer must require high quality assets as collateral, which is measured and adjusted regularly;

(g) the use of derivatives that involves the possibility of unlimited commitments are prohibited; and

(h) the board of the registered insurer or reinsurer must have the relevant reporting structures in place to monitor such

investments and must understand the use of derivatives to prudently manage risks associated with their use.

2.5.8 Regulation 15(14) is inserted to provide for the procedures to be followed by a registered insurer or reinsurer when it breaches any of the limits prescribed by regulation 15 due to market movements.

2.5.7 Regulation 15(15) is amended to include investments in foreign unit trust schemes. It appears as though this provision only applies to investments in local unit trust schemes and there appears to be no justification for the differential treatment;

2.5.8 Regulation 15(19) is amended to delete the reference to Annexure D and to provide that the form may be determined by the Registrar.

2.5.9 Regulation 15(22) is amended to provide that the Registrar is not required to obtain approval from the Minister to decline an application for exemption.

2.6 PROPOSED AMENDMENTS TO ANNEXURE C TO THE REGULATIONS – LIMITS OF INVESTMENT (REGULATION 15)

2.6.1 Insertion of Item 3 (Multilateral development bank Bonds)

Current provision

The current Annexure C to the regulations does not specifically provide for multilateral development bank bonds.

Proposed amendment

‘Multilateral development bank Bonds’ are added to the Annexure to the same degree and treatment as that afforded to Namibian Government security issuances, with a similar maximum limit of 95%.

Rationale for including ‘Multilateral development bank bonds’ as an asset class

An international financial institution (IFI) is a financial institution that has been established (or chartered) by more than one country, and hence is subject to international law. Its owners or shareholders are generally national governments, although other international institutions and other organizations occasionally figure as shareholders. The most prominent IFIs are creations of multiple nations, although some bilateral financial institutions (created by two countries) exist and are technically IFIs. The best known IFIs were established

after World War II to assist in the reconstruction of Europe and provide mechanisms for international cooperation in managing the global financial system.

The IFIs include Multilateral Development Banks (MDBs) which are institutions created by a group of countries that provides financing and professional advice to enhance development, and the Bretton Woods Institutions, the World Bank Group and the International Monetary Fund (IMF). IFIs have played a role in supporting domestic capital markets by issuing local currency bonds and setting up guarantee facilities.

According to the IMF (2021), local currency marketable debt as a share of total government debt has increased in emerging market and developing economies over the past decade. Better macroeconomic conditions and increased perception about the importance of developing domestic debt markets have created the conditions for this increase. However, despite considerable growth of local currency bond markets (LCBMs) in recent years, LCBMs in emerging market and developing economies continue to remain relatively underdeveloped compared with advanced economies, in which the local currency share of total government debt is about 95 percent.

Alongside growth in LCBMs, issuance policies have improved. Emerging market and developing economies have adopted new issuance policies and procedures as their government debt portfolios have grown, advisory efforts among international financial institutions (IFIs) and global and regional actors have increased, and knowledge sharing on debt management and debt management best practices have improved within the international community. In addition, progress has been observed in developing economies as primary market practices have become more transparent and more countries have started to issue benchmark securities.

Despite the observed progress, there is still significant scope for countries to further develop their LCBMs. Although many emerging market and developing economies have regularly promoted and adopted policies to develop their domestic markets for several years, different crises—for example, banking sector and macroeconomic dysfunctions in some countries have deterred LCBM improvements. In other cases, the lack of underlying enabling conditions or appropriate policies related to LCBM development has prevented further progress. Thus, it is important to understand the factors that are hindering the government LCBM development process so that appropriate measures and steps, targeted to the specific country, can be developed.

LCBM development can help to diversify government funding sources, safeguard sovereign portfolios from currency and maturity mismatches, and prevent financial crises in emerging markets (IMF 2002). In particular, the IMF says that Silva, and Velandia-Rubiano (2010) find that some emerging markets that shifted the composition of their public debt portfolios toward local currency debt issuance and improved their macroeconomic fundamentals avoided being buffeted by the global financial crisis.

The Group of Twenty (G20) has also recognized the importance of LCBMs in improving the resilience of the domestic economy and financial systems. In November 2011, the G20 endorsed an action plan to support LCBM development. As part of this commitment, several multilateral institutions developed a diagnostic framework to identify general enabling conditions, key components, and constraints for successful LCBM development in emerging market and developing economies (IMF, World Bank, EBRD, and Organisation for Economic Co-operation and Development 2013).

Considering LCBMs' integral role in sovereign debt portfolio management, the IMF affirms Jonasson and Papaioannou (2018) maintaining that LCBM development can be viewed in terms of three main stages with different priorities. In the initial stage, the focus should be on establishing a functioning primary market and creating the enabling conditions for secondary market development. In the deepening stage, where basic elements of the primary market and secondary market are established and functioning, the focus should be on improving liquidity on the secondary market. Finally, in the maturing stage, where elements of the market are, in general, well-functioning, the focus of policy makers should be on the development of sophisticated instruments and segments such as derivatives and making the market internationally competitive.

The International Finance Corporation (IFC), a sister organization of the World Bank and member of the World Bank Group is the largest global development institution focused exclusively on the private sector in developing countries. The IFC issued a bond in Namibia, the IFC21 that matured on 5 April 2021. The bond was approved and listed on the Namibian Stock Exchange. The bond was afforded the same degree of treatment as a Namibian Government issuance.

Due to the importance and critical roles that IFIs play in global development, it is recommended that these institutions be granted the same preferential status as that of the Namibian Government in relation to their issuances of securities to support Namibia's developmental agenda. By granting these institutions the same status as the Namibian Government in relation to security

issuances should encourage them to issue more securities in Namibia. This would as a consequence enhance the Namibian financial market development and skills transfer.

2.6.2 **Amendment of Item 4 (Statutory body, public enterprise, local authority and regional council Bonds)**

Current provision

The current Annexure C to the regulations does not specifically provide for Bank of Namibia bonds.

Proposed amendment

Item 4 is amended by including 'Bank of Namibia' as an issuer of bonds under column 1.

2.6.3 **Amendment of Item 5 (Corporate Bonds)**

Proposed amendment

Item 5 is amended by deletion of reference to "loans" in the second column of Item 5. The rationale for this deletion is that these loans are typically unsecured and secured loans are provided for in Item 14 (Other claims).

2.6.4 **Insertion of Item 9 (Associated companies and joint ventures)**

Background

Challenges have been identified regarding the correct treatment of investments in subsidiaries, especially where such subsidiaries are unlisted. There is increased incidences reported quarterly of non-compliance with Regulation 15 limits of investments by insurers who breach the 3.5 percent upper limit of unlisted investments. Investigations into the non-compliance showed that insurers combine the unlisted investments and investments in subsidiaries and other related entities as one item in Annexure C. Insurers have reported that the reason they combine the two types of investments together under unlisted investment is that the Annexure C does not provide separately for investments in subsidiaries and other related entities. Further that, since investments in subsidiaries and other related entities is mainly to local unlisted companies, it qualifies as unlisted investments.

Current provision

The current Regulation 1 defines the term “associate”, which includes a subsidiary. There is however no provision under Annexure C for investments made in subsidiaries, associated companies and joint ventures. This has resulted in insurers reporting such investments in subsidiaries under unlisted investments even though the objective of unlisted investment was intended to achieve the government’s economic development agenda (stimulation of the local economy).

To introduce investments in subsidiaries and other related entities as a class and to set the limit under Annexure C, it must be ascertained from the submitted quarterly returns whether insurers invest in subsidiaries and associates or other related entities such as joint ventures and how much is invested in these entities. The review of the five-year (2016-2020) quarterly returns indicated that life insurers hold material investments in subsidiaries and other related entities within the same group of companies. Since 2019 though, investments in subsidiaries is reported under the class unlisted investments on the returns. The calculations show that investment in subsidiaries constituted on average 5.5 percent of total industry investments.

In addition, a similar review of a few other jurisdictions; namely, Kenya, Mauritius, Nigeria and the United States of America, revealed that investments in subsidiaries is a permitted type of investment for long-term insurers and allowable limits range from 0 to 10 percent. To strike a balance between the range observed in other jurisdictions of up to 10 percent and the results from the review of data submitted to NAMFISA between 2016 and 2020, a limit of of atleast 5 percent is proposed.

Proposed amendment

The review concluded that unlisted investment class does not by nature or character adequately align to the nature and objectives of investments in subsidiaries and hence a split should be adopted. There is a need to create an additional new class to cater for investmentd in subsidiaries and other related entinties.

It is therefore proposed that an additional new class ‘‘associated companies and joint ventures“ with a limit of 5 percent is added to Annexure C to permit insurers to hold investments in subsidiaries and joint ventures.

2.6.4 **Amendment of Item 10 (Unlisted investments)**

Current provision

The current limit of 3.5% seems adequate as investments in domestic unlisted investments has not breached this limit, indicating that investors are experiencing challenges in finding suitable unlisted investment opportunities.

Proposed amendment

It is however proposed to increase the ceiling to 5%, which would render the limit consistent with regional peers (other SADC jurisdictions, namely, Botswana, Kenya, South Africa, Tanzania and Uganda).

Furthermore, adjustment is made to the exclusions contained in the second column due to the introduction of new asset classes and deletion of reference to “loans” in item 5 (corporate bonds).

2.6.5 Insertion of Item 11 (Commodities)

Current provision

The current Annexure C to the regulations does not specifically provide for commodity investments, and these types of investments are currently categorized under “other assets” for which a 2.5% ceiling is allowed.

Proposed amendment

It is proposed that commodities be added to the list of permissible asset classes, with a ceiling of 10% in line with similar limits in the SADC region (Botswana and South Africa).

Rationale for adding ‘Commodities’ as an asset class

Commodities are raw materials that are used to produce finished goods. Commodities include agricultural products, mineral ores and fossil fuels. They are basically any kind of natural resource that is consumed by companies and individuals. There are four main types of commodities:

i. **Energy.** The energy market includes oil, natural gas, coal and ethanol—even uranium. Energy also includes forms of renewable energy, like wind power and solar power.
ii. **Metals.** Commodity metals include precious metals, like gold, silver, palladium and platinum, as well as industrial metals, like iron ore, tin, copper, aluminum and zinc.
iii. **Agriculture.** Agriculture covers edible goods, such as cocoa, grain, sugar and wheat, as well as nonedible products, such as cotton, palm oil and rubber.
iv. **Livestock.** Livestock includes all live animals, such as cattle and hogs.

Commodities are physical goods that are bought, sold and traded in markets that are distinct from securities such as shares and bonds that exist only as financial instruments or contracts. There are several ways to invest in commodities.

- **Physical ownership.** This is the most basic way to invest in commodities. But unless these are small, transportable assets like precious metals, it can be impractical. Storing bales of cotton, steers or barrels of frozen orange juice concentrate or barrels of oil can be quite problematic for those not specifically dealing in those sectors, a pension fund for instance. Owning these types of commodities is usually best left to those who will be turning that commodity into a finished product.

- **Futures contracts.** Futures originated as a way for farmers to set a price for future delivery of goods. These contracts are perhaps the most well-known method for investing in commodities. While it can be risky, trading in futures can help protect against swings in other parts of a portfolio investment. Futures contracts have price-mechanism transparency, and one can access a commodity futures contract for a small fraction of its value. Buying and selling futures contracts, however, requires skill and experience. If the forward price, or what one paid for the contract is higher than the spot price when the contract comes due, one could lose money on that investment.

- **Individual securities.** Shares of commodity-producing companies grant indirect access to the commodity markets. If the commodity rises in price, the companies producing that commodity may experience increased revenues and profits. This is achieved through a regulated exchange.

- **Collective investment schemes (CISs), exchange-traded funds (ETFs) and exchange-traded notes (ETNs).** These securities can provide a wide exposure with relatively low investment minimums.

- **Alternative investments.** Structured investments, hedge funds or investments specialising in commodities are an option. These are highly speculative and leveraged investment strategies, carrying a high degree of risk and volatility. Enhanced returns are a possibility, but there is no guarantee of success.

Although commodity exposure may take the form of various instruments, including physical commodities, commodity derivative contracts, exchange traded funds (ETFs), exchanged traded commodities (ETCs) and commodity-linked notes, due the complications that can be experienced in direct ownership of commodities by pension funds, it is recommended that ownership of these assets be through a regulated exchange. This serves the purpose not only of practicalities, but also ensures instant price discovery of the specific commodity.

2.6.6 **Insertion of Items 12 and 13 (Private Equity Funds and other structured products)**

Current provision

The current Annexure C to the regulations does not specifically provide for private equity funds or other structured products, and these types of investments are currently categorized under “other assets” for which a 2.5% ceiling is allowed.

Proposed amendment

In line with global trends, many pension funds, especially larger ones, have an increased appetite for alternative investments. Various alternative investment structures are available to institutional investors, although it is difficult to classify these into specific asset classes. These structures include, but are not limited to, exchange traded funds (ETFs), exchange traded commodities (ETCs), exchange traded notes (ETNs), derivative instruments, private equity funds and hedge funds.

It is proposed that “Private equity funds” be added as an additional asset class with a total exposure limit of 5%, including a 2.5% limit per private equity fund and 5% limit per fund of private equity fund.

Furthermore, it is proposed that “other structured products” be added as an additional asset class for the inclusion of hedge funds, ETFs, ETNs and derivative instruments, with a total exposure limit of 5% and further limits of 2.5% per hedge fund, ETF, ETN or derivative instrument, as well as 5% per fund of hedge fund.

Although this might initially attract foreign exposure (a result of already well-developed private equity markets outside Namibia), it may pave the way for developing the alternative investment market in Namibia.

2.6.7 **Amendment of Item 14 (Other claims)**

2.6.7.1 Proposed amendment

Deletion of reference to “natural persons”. Although these are secured claims, there remains a risk in granting loans to individuals and there is no rationale for granting such loans.

2.6.7.2 Proposed amendment

Deletion of reference to “outstanding premiums” because it is inadmissible in terms of section 26, read with section 29 of the Act.