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Researching Capital Markets & Financial Services

RESEARCH
REPORT
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THE EMPOWERMENT **ENDOWMENT**

A study of trusts and foundations established from South Africa's black economic empowerment transactions

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About this report

The Empowerment Endowment is a report by Intellidex, funded by FirstRand. Intellidex is solely responsible for the research and content of the report. FirstRand's funding was not contingent on any of the findings contained in this report.

The report is based on a year-long research exercise into the charitable and community components of the 100 largest JSE companies' empowerment deals implemented since 2002, when community schemes started to be included in BEE deals. It follows an earlier research report, The Value of BEE Deals, which considered the top 100 companies' deals overall. The sources for this research included the published documents of the companies, but also extensive interviews and other engagements with various company executives to obtain information. Additionally, we interviewed several other individuals involved in philanthropy who provided background information and context.

Disclaimer

This report is based on information believed to be reliable, but Intellidex makes no guarantees as to its accuracy. Intellidex cannot be held responsible for the consequences of relying on any content in this report.

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Key Numbers

R51.6bn

Value created specifically for charitable recipients through BEE deals, including community trusts, existing charities and newly established foundations.

R32.6bn

In endowments now held by foundations set up as a result of BEE deals that will support charitable activities on a perpetual basis.

R19.0bn

Has been generated in contributions to public benefit beneficiaries, outside of the new foundations, some of which are existing endowments.

67%

Of this value is earmarked for spending on education, with the balance spent on a variety of objectives ranging from community development to sport and conservation.

The figures are based on an analysis of a sample of 35 companies' deals, which includes all those of the 100 largest JSE-listed companies which had a charitable component to their BEE deals.

Executive Summary

- **Of the 100 largest companies on the JSE, 35 conducted empowerment deals that included public-benefit organisations as beneficiaries.** These were mostly made up of trusts whose beneficiaries include the most in need in South African society.

- **In total, these deals resulted in value of R51.6bn of value for beneficiaries,** made up of a mix of endowed assets and cash flows to beneficiaries.

- **Of those deals, 27 involved the creation of new trusts which have been endowed with assets to support foundations.**

- **Collectively, the new foundations have endowments totalling R32.6bn.** We estimate that these endowments should generate funding for philanthropic activities of about 10% per year, resulting in spending of over R3bn per year.

- **Most of the new foundations are structured with independent boards of trustees**. However, the sponsoring companies usually retain some control over the investment strategies for the endowments, usually ensuring that the endowments remain invested in the sponsoring companies' shares.

- **The new foundations support a wide variety of objectives, but education stands out as a priority area.** We estimate that 67% of the financial resources the foundations command are focused on education-related funding objectives. This is followed by community development (10.6%) and entrepreneurship (8.4%).

- **It is clear that the assets and spending power of the new foundations will make a major impact on the overall philanthropic sector in South Africa.** There is little comprehensive research on philanthropic endowments currently in South Africa. One sample of prominent foundations found a total of R12.6bn held in endowments (Gastrow & Bloch 2016). A study of corporate social investment in South Africa estimated annual total spend of R8.1bn (Trialogue, 2015).

- **Most of the new foundations are less than two years old and are still gearing up to launch full activities.** The findings therefore indicate a change that is currently in the making and will have an impact in the years to come.

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Welcome note

Sizwe Nxasana
Chairman,
FirstRand Empowerment Foundation

Many South Africans still live in poverty, unable to access opportunities to make better lives for themselves. A helping hand can have a big impact on their lives and those of their families. One mechanism to extend that hand is the philanthropic legacy of BEE deals. While many are still new, the endowments that have been created as BEE deals have matured represent a substantial long-term resource that can be used to make a big difference.

At FirstRand, the group's empowerment deal has made a substantial contribution to endowments at various broad-based community-focused trusts, including the FirstRand Empowerment Foundation. These have the potential to change the lives of millions of people and exist for many years into the future.

The research that Intellidex has undertaken has helped to make it clear to us that FirstRand is not alone. Dozens of other companies have established similar endowments. Collectively the impact that these could make is far greater than any of us acting alone. This fact calls for innovation and coordination to really maximise the difference this legacy can make in the country. We should aim to develop, share best practice and collaborate where possible. Knowing more about each other and working together can only help. This research helps us to understand the lay of the land. By having a clearer picture of what other companies are doing, we can better shape our own activities to ensure a better overall outcome.

I hope this research contributes to a clearer vision of what is possible. By putting this information into the public domain it may spur creative thinking about ways we can really change the lives of those who need it. I hope too that it provides insights for, and potential coordination with, other social partners including the government and NGO sector. With good research and creativity, we can ensure a better future.

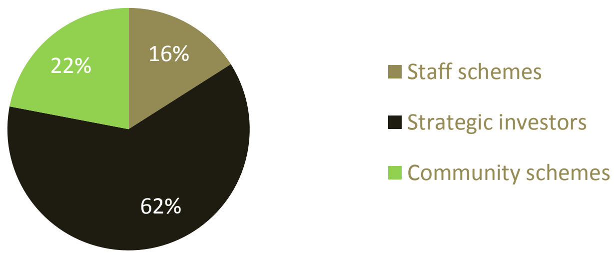
1. Introduction

In 2015, Intellidex undertook a major study of BEE deals to understand the value that had been created for beneficiaries up to the end of 2014 (Theobald et al 2015). We estimated that the total value net of any funding obligations had been R317bn. We divided this amount between strategic partners, consisting usually of established black investment firms and individuals, staff schemes, and finally community or charitable beneficiaries.

One finding from this exercise was that community and other charitable beneficiaries constituted 22% of the total value created from BEE deals (see Figure 1). This implied that R69bn of value had been created for public benefit purposes, broadly defined.

This struck us as a significant finding in the context of the overall philanthropic sector in South Africa. While BEE deals had often been criticised for not being broad-based enough, or for favouring well-connected black individuals and investment firms, this finding indicated that there was some significant benefit for organisations focused on the least well-off in society. We wanted to explore this element of the findings further, to examine the impact this quantum of money would have on the non-profit sector. That led to this research and report.

Graph 1: Value by beneficiary type - 2015 research



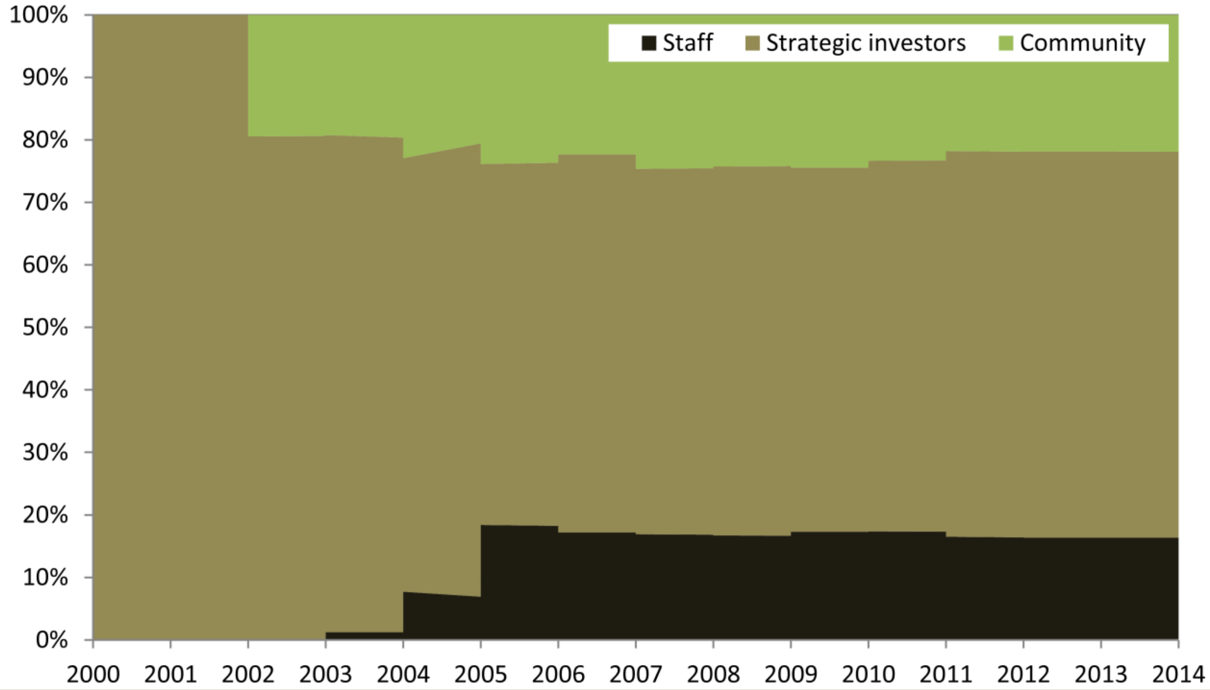
The inclusion of public benefit organisations in BEE deals had evolved over time. The earliest involved mining empowerment deals conducted around 2002, where community trusts were established with a mandate to use the proceeds from deals to develop the communities around mining operations. Subsequently, the idea of using charitable organisations as part of the beneficiary groups for BEE deals gained traction, particularly as they allowed deals to satisfy calls for them to be as “broad-based” as possible. The approaches to this component differed widely across companies. Some focused on established charities, including HIV/Aids charities and educational charities, which companies had previously supported through corporate social investment programmes. Others, however, focused on endowing foundations with assets that would form a long-term source of benefits to support charitable outgoings. Some were existing foundations that had been set up by black investment companies through previous BEE deals. Others set up new trusts with trust deeds that defined the beneficiaries by some or other class, usually black people or people from communities where the companies operated, such that the trusts would qualify as black owners for the purposes of BEE ownership calculations. Trust deeds also usually spell out what types of objectives the foundations should pursue.

Since their establishment, the development of these trusts has varied widely. Some are so far treated as a formality and not yet active. Others have been treated as an opportunity to make a real difference in poorer segments of society. Some are already fully operational with well-thought through strategies and infrastructure, while others still exist on paper only, with nominal assets but still no strategy to deliver to end-beneficiaries.

Most of the foundations are fairly new. BEE deals were struck largely between 2002 and 2005, with most maturing on a 10-year horizon. That means many deals reached

Graph 2: Beneficiary type, cumulative value by date of deal start

This illustrates how different beneficiary groups have evolved over time. It indicates the cumulative value attributable to each beneficiary type as a percentage of the total, according to the date of deal initiation. Community groups were included from 2002 and staff became an increasing part of deals from 2004. (Source: Intellidex 2015)



maturity in 2015, so many of the trusts are only a year or two old. Many of the foundations we considered began operating only after deals were concluded, though others were operational in some form during the lifetime of deals, using the benefits from trickle-through dividends in order to support activities.

In almost all cases, the trust received shares in the sponsoring company or a subsidiary of the sponsoring company. In some cases, the trusts are invested in the domestic subsidiary (for example, South African Breweries) or at the level of a specific operating company (for example, Kumba Iron Ore’s Sishen Iron Ore and Lonmin’s Lonplats). In cases where shares are held in subsidiary companies, it can be difficult to determine a value for these shares because they are not publicly listed. In some cases we had to allocate value proportionately of the holding company’s total value.

The investment strategies open to the trusts are quite narrow. Usually the sponsoring company must approve any disposals of the shares, even though the trusts are otherwise managed by independent trustees. In some cases the trusts are locked in only for a limited period.

The bulk of the impact of the foundations emerging from BEE deals is still going to be felt across the country as they gear up to deliver on beneficiary programmes. This report therefore provides a glimpse into the future as well as a comment on the present. Endowments are fundamentally about the future – they represent the ability of a public benefit organisation to generate returns that can be used to fund activities. Most are

BOX 1

The difficulties of data collection in the non-profit sector

South Africa has no systematic record of financial information about its non-profit sector. This differs starkly from developed markets such as the United States and the United Kingdom, where statistics on non-profits are well curated and made publicly available. The sorts of information we would have liked to access for this report would have included the trust deeds for the trusts that foundations have been set up, as well as detailed balance sheets and income statements. The masters' offices of high courts hold trust deeds, but these have not been digitised and are difficult to access. The non-profit directorate of the Department of Trade and Industry theoretically receives annual returns from registered non-profit organisations, but this information does not seem to be captured or made available for analysis by the public.

Other researchers have conducted research on the sector and parts of it. Trialogue conducts an annual survey of companies' corporate social investment activities, but this is a different aspect of philanthropy to endowments. In its 2015 study, it estimated total annual CSI spend of R8.1bn (Trialogue 2015). Consultancy GastrowBloch Philanthropies undertook a significant study in 2015 of a sample of 21 private sector foundations, but this was not exhaustive of the sector. In its sample, foundations had a total endowment of R12.6bn.

In our case, researching the sector proved more difficult than we expected. Our focus was JSE-listed companies that are required to publish significant financial detail, but once a foundation has been established it is formally independent of the company so there are no longer the same disclosure requirements. We took the approach of trying to speak to every company and foundation to obtain both quantitative and qualitative information about their activities. Some companies were forthcoming, but others proved highly reticent. We put this down to a few factors. Some companies see the foundations as far from their core operations and simply aren't willing to spend time on providing information regarding them. Others are wary of the attention that the foundations may attract, particularly from aspirant funding recipients. One long-standing philanthropy practitioner told us that foundations become the target of thousands of requests and their officers have to deal with invasions of their privacy, so that it is easier to keep out of the public limelight.

To our minds, there is a substantial need for better curating and sharing of data on the non-profit sector that should be led at a government level. This would support better development of the sector and the public understanding of philanthropic activities.

structured as perpetual funds, so they will exist forever onwards. BEE deals have therefore created a long-term legacy. Our findings are that collectively, the 27 endowments that have been set up by the 100 largest companies on the JSE have assets of R32.6bn. If that generates a reasonable return of 10% per year, a significant amount of public benefit activity will be supported by them.

In the remainder of this report we set out our findings in some detail. We examine each of the 35 BEE deals and the 27 new foundations to estimate the financial features of the foundations and spending. We trust it provides some useful insight into the characteristics of BEE endowments and how they have had and still will have an impact on the philanthropy sector in South Africa. We hope the information also serves those foundations in providing insight into each others' experiences.

2. Top-Level Findings

We studied the charitable components of deals undertaken by the 100 largest JSE-listed companies. These companies account for the bulk of economic activity and BEE deals undertaken in South Africa. Of these companies, we identified 35 that had included a public-benefit component in their empowerment deals.

We then calculated the value generated for beneficiaries in these components including three main forms:

1. Assets that had been endowed into trusts set up as part of the BEE deals
2. Assets that had been transferred to pre-existing trusts on maturation of the BEE deals
3. Cash flows that were directed to beneficiaries during the lifetime and at expiry of deals

In the table below, we consolidated all of these different sources of funding in totalling the amount of value that has flowed from BEE deals to public benefit organisations to date.

TABLE 1: Total value created for public-benefit organisations from BEE deals

Sponsoring firm	Total value (Rm)	Main beneficiaries	Effective date	Note
FirstRand	R 16 355	FirstRand Empowerment Foundation, and foundations of Kagiso, WDB Investment Holdings, Mineworkers Investment Company	31-Dec-16	
Assore	R 5 516	Boleng and Fricker Road Trusts	31-Mar-17	1
Sanlam	R 4 334	Sanlam Ubuntu Botho Community Development Trust, and Sanlam Foundation Trust	31-Dec-13	
Kumba Iron Ore	R 3 598	SIOC Community Development Trust	31-Dec-16	
Aspen	R 3 255	Ceppwawu Development Trust	29-Jun-15	
Netcare	R 3 115	Health Partners for Life Trusts	31-Mar-17	2
SABMiller	R 2 511	SAB Inzalo Foundation	31-Dec-16	
Tiger Brands	R 2 275	Thusani Trust/Tiger Brands Foundation Trust	30-Sep-16	
Fortress	R 1 530	Siyakha Education Trust	31-Mar-17	3
Resilient Property Fund	R 1 530	Siyakha Education Trust	31-Mar-17	3
Old Mutual	R 1 200	Old Mutual Black Distributors Trust, Mutual & Federal Black Broker Trust, Old Mutual Education Trust, The Mutual & Federal Community Trust	07-May-15	4
Standard Bank Group	R 1 033	Tutuwa Community Foundation	31-Mar-17	

Pioneer Foods	R 830	The Pioneer Foods Education and Community Trust	31-Dec-16	
Nedbank	R 632	Nedbank Eyethu Community Trust	31-Dec-16	
African Rainbow Minerals	R 490	African Rainbow Trust	31-Mar-17	
Liberty Holdings	R 480	Liberty Community Trust	31-Dec-16	
Sasol	R 450	Sasol Foundation	30-Jun-16	5
JSE Limited	R 397	JSE Empowerment Fund	31-Dec-16	
Distell	R 395	Distell Development Trust	31-Mar-17	
Impala Platinum	R 305	Bafokeng Impala Trust	30-Jun-15	
Italtile	R 277	Ingcube Women Organisation and Italtile Foundation Trust	31-Mar-17	
Santam	R 275	Emthunzini Broad-Based Black Economic Empowerment Community Trust	31-Mar-17	
Bidvest	R 239	Women's Development Trust	30-Jun-16	
Nampak	R 145	National African Women's Alliance and Union Trusts	31-Mar-17	
PPC	R 139	Community Trust, Industry Association Fund, Education Trust	31-Dec-16	
Imperial Holdings	R 76	Imperial and Ukhamba Community Development Trust	31-Mar-17	
AECI	R 63	AECI Community Education and Development Trust	31-Mar-17	
Grindrod	R 44	Adopt-a-School Foundation	01-Jul-14	
Alexander Forbes Group	R 36	Alexander Forbes Community Trust	31-Mar-17	
Barloworld	R 14	Barloworld Education Trust	31-Mar-17	
Invicta	R 12	Humulani Empowerment Trust	31-Mar-17	6
Murray and Roberts	R 9	Khanyisa and Sizwe Trusts	31-Dec-16	5
Emira	R 7	Penreach/Shalamuka Foundation	31-Mar-17	
Lonmin	R 5	Lonplats Marikana Trust	31-Mar-17	
Redefine Properties	R 0	Redefine Empowerment Trust	31-Mar-17	5
TOTAL	**R 51 572**			

Notes
1. The Boleng and Fricker Road trusts act together in most instances so have been classed together for these purposes
2. The Netcare Health Partners for Life trusts include five underlying trusts with differing mandates. Some of these support Netcare's activities in providing services to the indigent
3. Fortress and Resilient Property funds both included the Siyakha Education Trust in their deals. The two companies have a strong relationship. The assets and spending of the trust were divided equally between them in our calculations
4. There were several types of beneficiaries in the Old Mutual deal which are all included here as of the resolution of the Old Mutual BEE deal. We were unable to obtain more fine-grained information from the company
5. At the time of our assessment, the endowments of these companies had negative net asset value. This is because

share prices have underperformed relative to the funding obligations of the entities.
6. These figures only include the latest annual distribution made by the company to the trust. We were unable to determine the value of assets held by the trust due to a lack of information from the company. The trust does have funding obligations, however, so it may have no net asset value

Collectively the total amount of value generated so far for public benefit purposes is R51.6bn. This figure could, and probably will, grow over time, as the asset base of firms increases. This should happen as most trusts aim to generate returns on assets that compensate for inflation. In some cases, firms have indicated that they will continue doing further deals that involve their foundations into the future (for example, Fortress Property Fund and its Siyakha Education Foundation, and the JSE's Empowerment Fund). We have included those firms above whose foundations currently have no net value (see note 6). The value is a function of share prices of those firms, and at current levels these are not sufficient to cover the countervailing funding obligations. In such cases we anticipate one of two outcomes: share prices recover, leading to a higher value in future; or firms restructure new deals that lead to new value creation. Two of the firms involved, Sasol and Murray & Roberts, have experienced difficult conditions as a result of weak oil prices and a depressed construction market, respectively. History tells us that depressed share prices are temporary – the majority of deals found themselves underwater during the 2009 recession, but by 2012 had recovered and have since been able to deliver substantial value.

3. Newly Created Foundations

Of the 35 firms in table 1, 27 included new foundations that were set up specifically as beneficiaries for their empowerment deals. They were not the only foundations which benefited – established foundations like those of the Chemical, Energy, Paper, Printing, Wood and Allied Workers Union, Kagiso, WDB Investment Holdings and Mineworkers Investment Company were also major role players. In the rest of this report, however, we focus on those foundations that were created by BEE deals.

In some cases, these newly established foundations and trusts were initially intended to grow into entities that would become participants in other empowerment deals too. For example, when the Sasol Inzalo Foundation was conceptualised, the vision was that it would gain a life beyond Sasol, building a portfolio of investments by participating in other empowerment deals. That did not end up being the case, in part because the branding clearly aligned it with Sasol, but also because pressure on the Sasol share price meant it did not develop the kind of equity that was initially hoped for. In some cases foundations have ended up with more than one company as sponsors, though this is usually because the companies are related through cross shareholdings, for example the Siyakha Education Trust.

We estimate these foundations now hold a total of R32.6bn. To date they have also distributed R4.5bn to beneficiaries. These distributions include cash that has been allocated but not yet distributed, with some foundations committing to multi-year projects and earmarking cash for later years to ensure cash is available when needed. The distributions have in many cases occurred since the initiation of the BEE deals, with trusts entitled to receive some percentage of dividends every year, with the balance used to pay off funding initially granted in order to acquire the shares. If the sponsoring companies performed well, the funding obligations were often settled early, allowing the trusts to benefit from full cash flows.

TABLE 2: Endowments and spending of newly-created foundations

Rank	Foundation	Endowment value (Rm)	Sponsoring company	Spending to date (Rm)
1	FirstRand Empowerment Foundation	R 5 673.2	FirstRand	R 216.1
2	Boleng and Fricker Road Trusts	R 5 436.0	Assore	R 80.4
3	Sanlam Ubuntu Botho Community Development Trust and Sanlam Foundation Trust	R 3 795.1	Sanlam	R 538.8
4	Siyakha Education Trust	R 2 800.0	Fortress and Resilient property funds	R 260.0
5	Health Partners for Life Trusts	R 2 520.3	Netcare	R 595.0
6	SIOC Community	R 2 506.8	Sishen Iron Ore	R 1 091.6

	Development Trust		Company (Kumba Iron Ore)	
7	Thusani Trust/Tiger Brands Foundation Trust	R 2 241.2	Tiger Brands	R 33.4
8	SAB Inzalo Foundation	R 2 100.0	South African Breweries (SABMiller)	R 411.0
9	Old Mutual Black Distributors Trust, Mutual & Federal Black Broker Trust, Old Mutual Education Trust, The Mutual & Federal Community Trust	R 1 200.0	Old Mutual	n/a
10	Tutuwa Community Foundation	R 932.3	Standard Bank Group	R 100.8
11	The Pioneer Foods Education and Community Trust	R 817.9	Pioneer Foods	R 11.8
12	Liberty Community Trust	R 459.9	Liberty Holdings	R 20.0
13	Nedbank Eyethu Community Trust	R 402.0	Nedbank	R 230.0
14	Distell Development Trust	R 371.3	Distell	R 24.1
15	African Rainbow Trust	R 370.0	African Rainbow Minerals	R 120.0
16	JSE Empowerment Fund	R 349.6	JSE Limited	R 47.0
17	Ingcube Women Organisation and Italtile Foundation Trust	R 273.2	Italtile	R 4.2
18	Bafokeng Impala Trust	R 169.4	Impala Platinum	R 135.7
19	Community Trust, Industry Association Fund, Education Trust	R 139.0	PPC	n/a
20	Alexander Forbes Community Trust	R 31.0	Alexander Forbes Group	R 4.9
21	Imperial and Ukhamba Community Development Trust	R 21.3	Imperial Holdings	R 54.6
22	AECI Community Education and Development Trust	R 0.0	AECI	R 62.9
23	Humulani Empowerment Trust	R 0.0	Invicta	R 11.5
24	Lonplats Marikana Trust	R 0.0	Lonplats (Lonmin)	R 5.0
25	Khanyisa and Sizwe Trusts	R 0.0	Murray and Roberts	R 9.5
26	Redefine Empowerment Trust	R 0.0	Redefine Properties	R 0.0
27	Sasol Foundation	R 0.0	Sasol	R 450.0
	TOTAL	**R 32 609.3**		**R 4 518.4**

Several foundations currently have no net asset value in their endowments. This is because share price performance has not been sufficient to cover the cost of funding received to buy the shares. Usually the shares held by the trusts were issued at some level of discount to the market prices of the shares at the time that the BEE deals were launched. Even so, in some cases share prices fell below the discounted price. However, even when there is no value to the endowment of the foundations, there is usually still some flow of funding to the foundation. For example, the Sasol Inzalo Foundation receives 50% of the dividends paid, with the balance used to pay down debt, irrespective of the amount of debt.

We did not conduct an exhaustive analysis of funding done to date, however we did obtain broad categories of beneficiaries. We then estimated a breakdown of the total value (R37.1bn) between seven main beneficiary types. This is shown in graph 3 below. As is clear, education is targeted for the majority of funding at some two-thirds. Next most significant is community development followed by entrepreneurship. In several cases, the divisions between these priorities is somewhat artificial. For instance, we did not create a specific health category, even though several trusts indicate that their

BOX 2

Innovation in philanthropy

The emergence of so many new foundations from the private sector has also brought a new business-like culture to some kinds of philanthropic activities. Some of the foundations we spoke to have firm intentions of drawing on the entrepreneurial capabilities of their sponsoring companies to innovate new ways of achieving social objectives.

For example, Standard Bank and the Tutuwa Foundation are set to launch the first social impact bond in South Africa. The concept was developed overseas with the first one launched in 2010 in the United Kingdom. The concept is sometimes called “pay for success” financing. A project is identified and specific measurable outcomes are determined. If those outcomes are achieved then the funding for the project is repaid, usually by a government entity. The structure means that there is zero risk to the taxpayer – should the project fail to achieve its intended outcomes, there is no cost.

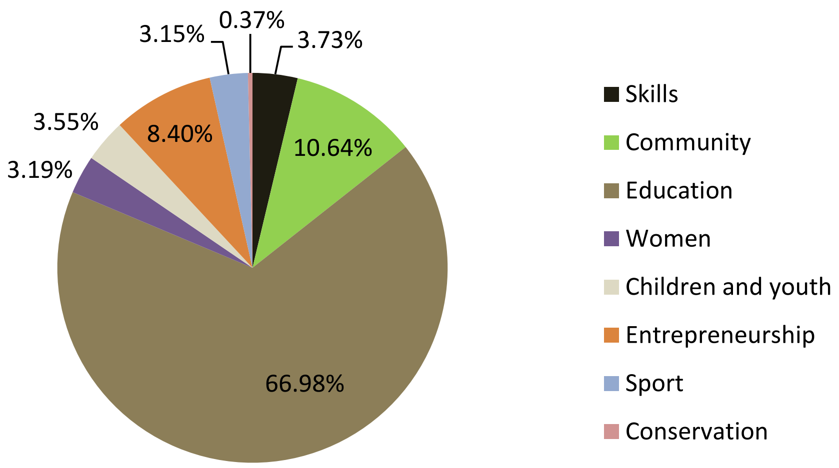
For foundations, social impact bonds are an unusual proposition. They effectively put their capital at risk. If the project fails to meet its objectives, that capital is lost, but it is repaid if the objectives are met. Failure means the funding becomes a grant but success means the funding is an investment. The foundations can provide an initial grant to cover the development of the project idea. Naturally, this shifts incentives for all involved, helping to ensure that the outcomes are achieved.

Standard Bank’s pioneering project will take place in the Eastern Cape and several other foundations will join it in putting up the funding. Two local government departments will act as the guarantors. The projects are all around childhood development from birth to school level within outcomes measured on several health factors and achievements in school readiness tests. The project will run for three years.

We also heard of several other new concepts at earlier stages of development. These could help ensure that the growth of corporate sponsored foundations has a greater impact than money alone.

community or youth investments are health-focused. Also, the distinction between community and education spending can be somewhat arbitrary as some community development work includes schools.

Graph 3: Foundation support priorities



In interviews, representatives of the foundations indicated a range of different considerations in deciding on their priorities for project support. Several were guided by the priorities of the sponsoring companies. For instance, community development spending is focused on their areas of operations, and tend to be focused on enhancing infrastructure that employees and their families will benefit from. Education spending was also often guided by the skills needs of companies, for instance in choosing to support bursaries in subjects that the companies would want new recruits to have studied. However, such company-aligned spending was not the rule. In several cases, foundations told us they had been guided by the priorities of the National Development Plan, choosing early childhood development, for example, because the NDP argued it provided the greatest return in terms of improvement to individuals' life prospects. There were also several examples where foundations have engaged with local government partners in order to work alongside them to invest in schools and other community infrastructure. Such partnerships allow for sustainable projects as local government can take on the running costs after a foundation has funded new infrastructure. In almost all cases, the trustees who oversee the assets and beneficiary strategies are independent and therefore the company-aligned spending policy can be expected to change over time. In older foundations, this has already happened, with the foundations developing independent objectives.

The education focus of many foundations can be in specific segments, for example tertiary education, or cover a wide range. The Tutuwa Foundation, for example, aims to address weaknesses in the full life cycle of youth, beginning with early childhood development and running through to work readiness preparation. This is done with an ambition of supporting the "demographic dividend" that South African could benefit from if its young population is able to take advantage of opportunities. Other foundations have avoided starting new programmes, believing that it is more effective to support established programmes that have already proven their models. For example, the JSE Empowerment Fund has backed a variety of education-related projects such as the Alexandra Education Committee.

The SABMiller Foundation is unusual in having a specific focus on entrepreneurship. Its trust deed defines its objective as: "The provision of funding for small, medium and micro-sized enterprises, in order to contribute to the economic and social empowerment of historically disadvantaged persons, primarily (but not necessarily exclusively) by means of Entrepreneurship Development and with a priority focus on providing opportunities within small, medium and micro-sized enterprises for women and youth in the rural areas, as well as persons with disabilities." The foundation has since set up three programmes shaped around different types of entrepreneurial activity, including mentorship, social innovation and rural enterprises.

In several cases, the strategies of foundations have been aligned with the other corporate social investment strategies of the sponsoring firms. This often allows for increased impact in that the foundations can support activities that are already established. Funding generated by the foundations' endowments can be complemented by the funding from CSI, which is usually determined as a percentage of the sponsoring companies' profits. In some cases, the foundations also work alongside existing foundations. For example, several foundations were created through the Old Mutual BEE deal, but the broader group also includes the Old Mutual Foundation, which was formed from unclaimed demutualisation shares. It has infrastructure that the new foundations can use.

We found a mixed picture when it came to the operations of the foundations. Generally, there were the following types:

- Foundations were still gearing up, appointing staff and creating other infrastructure. In some cases, they had been supporting beneficiaries but the decisions and management had been managed by the sponsoring companies. In several cases we were told that this has been hampered by a shortage of available specialist skills. Examples are the Tutuwa Empowerment Trust, the Alexander Forbes Community Trust and the Liberty Community Trust.
- Foundations that have already established full operational capacity. Examples are the Sishen Iron Ore Company Community Development Trust and the SABMiller Foundation.
- Foundations which outsource some part or all of their management. This can be an efficient mechanism to share overhead costs and access expertise. Examples are the FirstRand Empowerment Trust and Redefine Empowerment Trust.
- Foundations in which the operations will continue to be managed by the sponsoring company, subject to the authority of an independent board of trustees. From the foundations' point of view this can be the most cost effective as the company effectively absorbs all the operating costs. Examples are the

Boleng and Fricker Road Trusts, the Tutuwa Foundation and the JSE Empowerment Fund.

In our discussions with foundation leadership, several indicated that they intend to evolve their operating models over time as their programmes develop. In our view, the indication was that more would establish internal operational infrastructure in order to protect their independence, but still obtain certain support from sponsoring companies "for free", such as accounting and IT services, and office space.

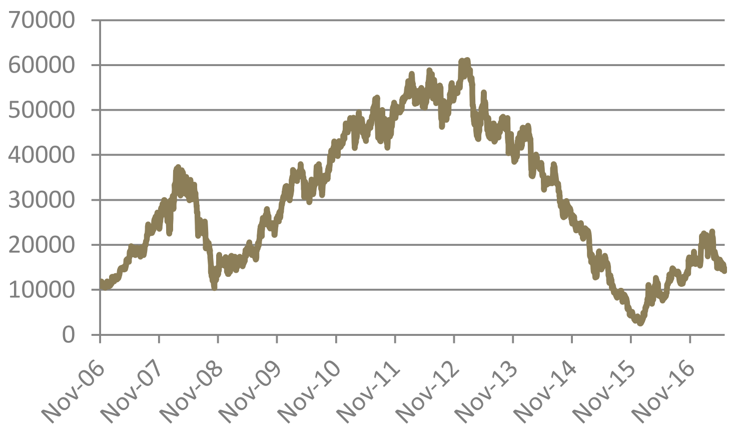
BOX 3

Concentration risk and the Sishen experience

Most of the foundations hold investment portfolios that consist of only the sponsoring company's shares. Most sponsors retain the right to approve any changes to the foundations' investment strategies. This is to ensure that the sponsors can retain the trusts as qualifying black shareholders into the future. This could change as BEE regulations evolve, but for now companies have a clear interest in maintaining the foundations as shareholders.

From an investment management point of view, this represents a highly inefficient investment strategy as it means the endowment is subject to the performance of just a single company. That will inevitably result in a more volatile returns profile than a diversified portfolio would, increasing the risks to the sustainability of the foundations.

Graph 4: Kumba Iron Ore share price (c)



Some foundations have achieved a certain level of diversification by setting aside some of the cash flows earned from dividends and used that to invest in other assets, such as shares that have quite different return characteristics to the sponsoring company. However in our research the greatest degree of diversification we found was for 30% of assets to be invested in a portfolio other than the sponsoring company's shares. One possible solution to better manage these risks would be for foundations to share risks. That could be achieved by structuring return swaps, a kind of derivative, between foundations. Such derivatives would allow one foundation to effectively "swap" a portion of their returns for another's.

A good example of the perils of concentration risk is the Sishen Iron Ore Company Development Trust. Its sponsoring company is the main subsidiary of Kumba Iron Ore, a subsidiary of Anglo American. During the lifetime of its empowerment deal, it experienced both highs and lows as global iron ore prices reached new record before collapsing after the global financial crisis. The share price of Kumba, which mostly reflects the performance of Sishen, rallied six fold between 2006 and 2012, before falling 95% in the next three years (see graph 4).

The company went into cash-conservation mode and ceased paying a dividend. Up to that point, Kumba's BEE deal had resulted in substantial payoffs for beneficiaries, which included the full staff complement of the mine in the Northern Cape. Anecdotally, for a period the town of Katu boasted the highest per capita income in the whole country. But in a flash all that changed. In 2014 the foundation received revenue of R504m, but a year later that fell to R152m and a year after that to R64m. The change was unanticipated and meant that it had to cut back on spending dramatically. It was a dangerous situation that led to significant community tension and security issues. "The austerity was not welcome," says Vusani Malie, the foundation's CEO. "It was very difficult."

In response, the foundation launched a rationalisation programme to reduce costs and prioritise spending programmes. It also set out a strategy to diversify its asset base. The trust had participated in some other BEE deals to gain different assets and it now accelerated those investments. It has borne fruit in that now 35% of the trust's portfolio consists of assets other than Sishen shares, including investments in SA Airlink, Kathu Solar Park and Urban Hotel Kathu. Meanwhile, Sishen has started to recover as iron ore prices have showed some signs of reversing their trend. But the experience has resulted in a trust that is much better prepared to last through the cycle.

4. Conclusion

The endowments created by BEE deals are beginning a journey towards making a substantial difference to the philanthropic industry in South Africa. In many cases, foundations are only now becoming fully operational. With R32.6bn of endowments, most destined to exist in perpetuity, these can make a long-running difference to the lives of millions of South Africans.

The key challenges facing these new entities are a shortage of skills and lack of infrastructure. Many are struggling to find the required staff to run operations. Foundations also have to think through the right operational model, that will balance efficiency with the need to be independent of their sponsoring companies. The use of sponsoring company infrastructure lowers costs, but can come at the loss of real independence in grant making activities.

Foundations also have to find ways to manage the concentration risks inherent in their portfolios. All have major exposures to the shares of their sponsoring companies. This is an outcome of the current BEE regulatory environment which requires companies to maintain BEE-qualifying investment levels. But it leaves foundations with inefficient investment portfolios. Some have begun diversifying by using a proportion of cash flows to diversify their portfolios. But more creative solutions are surely feasible, such as total returns swaps, a form of derivative.

The new foundations also bring a corporate culture, particularly in driving innovation, into the philanthropic sector that could have spin offs for the rest of the sector too. This could result in new innovations such as social impact bonds, philanthropy markets, activist investing, and so on.

There is clear potential for foundations to cooperate, both in dovetailing their programmes to maximise impact, and in sharing best practice, infrastructure and potentially in pooling financial risks and jointly supporting projects. We hope that this report spurs creative thinking that will drive innovation, cooperation and ultimately help increase scale of impact on South African society.

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