

Cognizant

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THE RELENTLESS PURSUIT
OF RELEVANCE

FROM CODE TO CLOUD:
UNVEILING MICROSOFT'S
COMPETITIVE ADVANTAGE

SHOPRITE: WINNING
WHERE IT MATTERS

NAVIGATING FOREIGN
INHERITANCE AS AN
SA TAX RESIDENT

BEYOND GEOGRAPHIES
AND GENERATIONS



Private Clients

by  Old Mutual Wealth

Contents

THE RELENTLESS PURSUIT OF RELEVANCE

4

FROM CODE TO CLOUD: UNVEILING MICROSOFT'S COMPETITIVE ADVANTAGE

8

SHOPRITE: WINNING WHERE IT MATTERS

11

NAVIGATING FOREIGN INHERITANCE AS AN SA TAX RESIDENT

14

BEYOND GEOGRAPHIES AND GENERATIONS

16

The Relentless Pursuit of Relevance

ANDREW DITTBERNER, CHIEF INVESTMENT OFFICER AT PRIVATE CLIENTS BY OLD MUTUAL WEALTH



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emaining relevant in today's fast-paced, technology-driven

world is increasingly challenging. This is evident in the decreasing lifespan of S&P 500 companies. According to consulting firm Innosight, the average company lifespan has declined from 61 years in 1958 to just 18 years today. In

this increasingly Darwinian corporate landscape, it is crucial to understand how effectively a business allocates its finite capital and resources.

The full impact of the COVID-19 pandemic is still slowly playing out in consumer and market behaviour, as pre-pandemic trends sharply accelerate. For example, the number

of industrial businesses in the S&P 500 has dropped from 166 in 1969 to about 75 today, while technology-related businesses have increased from 16 to 65 (excluding the likes of Alphabet, Amazon and Meta, listed under separate industries).

This shift creates significant challenges for company management teams. As

industry boundaries blur and hybrid industries emerge, management must consider how to stay relevant. They need to assess whether they have the necessary technology, and if not, decide whether to build or acquire it. If this is not a priority, they then face the choice of whether to return excess capital to shareholders through dividends or share buybacks; alternatively, they can pay down debt, or hold on to idle cash on their balance sheets.

Alongside rapid technological advancement, companies also face the challenge of becoming more sustainable in their operations and products. In the face of these challenges and the evolving landscape, capital allocation has become increasingly critical for a business' survival and relevance, and remains the CEO's top responsibility.

Renowned capital allocator Warren Buffett put it succinctly when he addressed the most important role

of a CEO and why so many fail at it: "Once they become CEOs, they face new responsibilities. They now must make capital allocation decisions, a critical job that they may have never tackled, and this is not easily mastered." The reason for this is that the skills required to become a CEO often focus on general management rather than capital allocation decisions.

UNPACKING CAPITAL ALLOCATION

Investing can seem relatively straightforward: capture the fundamentals, tick the necessary boxes, arrive at a valuation, and construct a sensible portfolio. However, the complexity lies in understanding the industry a company operates within and identifying its competitive advantages. The most subjective aspect of an investment decision is determining whether the management team can allocate capital prudently to ensure that the business strategy is well executed.

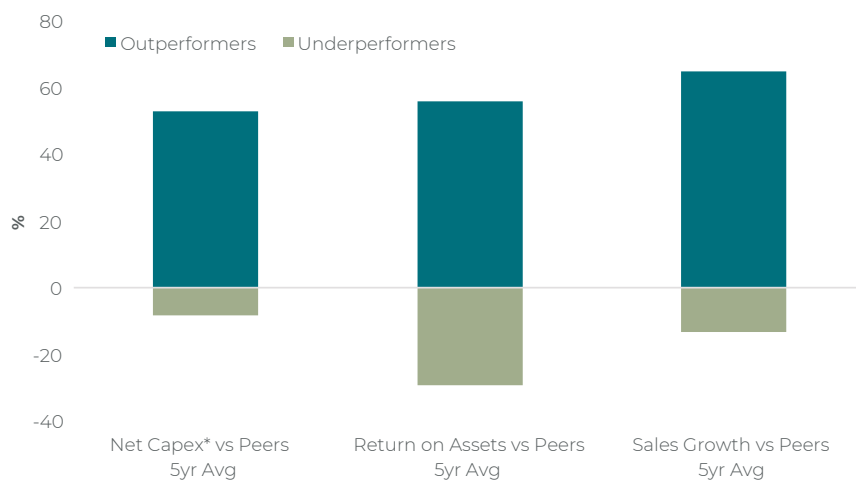
Capital allocation is not about building an ivory tower or fancy headquarters

decorated with expensive art. Every capital expense comes with an associated opportunity cost – i.e. the potential return that could have been earned elsewhere. Capital allocation decisions that do not generate returns above the cost of capital destroy shareholder value and jeopardise a company's future.

Interestingly, despite the need for substantial investments in digital and sustainability transformations, a recent Boston Consulting Group (BCG) report shows that over the past decade, capital expenditure relative to revenue in the US has dropped by around 10%. Meanwhile, capital returned to shareholders through buybacks and dividends, along with cash balances, have risen by about a third. This indicates a reluctance to spend capital, which is not due to a lack of opportunities. Persistently low interest rates and bond yields have certainly played a role, as has the financial engineering of buying back shares at face value only to reissue them to management or employees through share-based compensation schemes.

The evidence, however, is clear: companies making smart investments are winning. BCG's report shows that the top performing companies – those in the top third of market valuation growth relative to peers – invested about 50% more in capital expenditure (capex) than their peers. As shown in graph 1, these outperformers achieved 56% higher returns on assets and approximately 65% higher sales growth over the five-year period to 2023.

Graph 1: Outperformers Invest More and Achieve Higher Returns and Growth



Source: Boston Consulting Group: The Art of Capital Allocation (Nov 2023)
 *Net capex is defined as total capex relative to the asset base.

OPTIONS FOR ALLOCATING CAPITAL

Capital can be generated or raised in several ways. The most important source is operational cash flow, which is what is left over once operating expenses are covered. Other capital raising avenues include disinvestments, issuing new shares or borrowing money.

Management teams then have various options for allocating their companies' capital:



1. Reinvesting in the business:

This can drive organic growth by either expanding or optimising current operations to increase growth, efficiencies, and ultimately profitability.



2. Acquisitions:

While growing inorganically through acquisitions are viewed as quick wins, they can lead to the downfall of many businesses given the risks involved. These are discussed in more detail below.



3. Paying down debt:

This is a particularly attractive option for businesses that have stretched balance sheets. Ensuring that the business is healthy by maintaining an adequate debt-to-equity ratio is viewed favourably among investors.



4. Returning capital to shareholders:

This can be done either through share repurchases or by paying dividends to shareholders. Both options are generally viewed positively by investors when done under the right conditions.

WHAT WE LOOK FOR

At Private Clients, we have specific preferences for how the businesses we invest in should allocate capital.

Many companies adopt a dividend policy and rigidly adhere to it, allocating a percentage of earnings to shareholders annually. While this approach is common, it often overlooks other capital allocation options.

A set dividend policy poses two main problems. Firstly, investors become reliant on the dividend payment and any sign of the dividend being at risk, for whatever reason, can lead to a significant drop in the share price. Secondly, management may prioritise maintaining the dividend over better capital allocation options, sometimes even increasing debt to ensure the dividend is paid.

We believe that dividends should be considered only after exploring other capital allocation options. For more income-reliant investors, fixed income securities such as cash or bonds may be more effective as opposed to relying on dividend income. Warren Buffett, for example, has a philosophy of not paying dividends, believing that he can allocate capital more effectively (and this has proven to be the case) than Berkshire Hathaway shareholders. Although Berkshire's cash reserves are steadily growing, and pressure is mounting for him to do something with it, Buffett remains prudent, ensuring the cash is not hastily spent.



Another concern we have regarding capital allocation involves companies that initiate share buyback programmes and then rigidly adhere to them, regardless of price. This practice is akin to setting a monthly budget and ensuring that it is met, even if the expenditure is not necessary. Companies often end up buying back shares at inflated prices due to a buyback programme being in place. A more significant concern arises when companies issue some of the repurchased shares to management or employees as part of share-based compensation.

Acquiring and disinvesting from businesses is common. Our preference is for acquisitions where the acquired business either aligns with or complements the current business operations. While the allure of new ventures can be enticing, they often come with significant risks. It also goes without saying that management should not overpay for acquisitions, which is easy to do when using shareholder capital. Another preferable criterion for acquisitions is that they should be funded from internally generated cash, as opposed to raising debt or issuing shares. Finally, we advocate for a strategy of

making smaller, bolt-on acquisitions rather than betting heavily on a single, massive acquisition. This is referred to as firing bullets, not canons.

LOOKING BACK AT TRACK RECORDS

The landscape is littered with examples of both superb and poor capital allocation decisions. Articles later in this edition will explore two examples of companies staying relevant through prudent capital allocation decisions. However, Xerox provides a stark example of how ill-considered and poorly timed capital allocation decisions can lead to a company's demise.

After listing on the New York Stock Exchange in 1961, Xerox achieved great success. It became one of the Nifty Fifty stocks in the 60s, with its share price soaring from US\$0.77 in January 1962 to \$8.30 by the end of 1969. Riding on this stellar share price growth and eager to enter the burgeoning computer industry, then CEO Peter McCollough sought to acquire a computer capability. Developing their own capability was deemed unfeasible given how fast the field was growing, raising concerns that they would never catch up. Consequently, Xerox decided to acquire

Scientific Data Systems (SDS) in 1969. With Xerox's share price at astronomical levels, the acquisition was concluded at a ratio of one Xerox share for every two SDS shares, totalling close to US\$1bn. SDS was quickly renamed Xerox Data Systems (XDS).

Nearly half of XDS's business was linked to the space programme at the time. The first astronauts landed on the moon shortly after the acquisition was concluded, and since the computers needed for that programme were already in place, the growth of that market could only decline. The recession of 1970 was the death blow for XDS. Facing US\$250m in operating losses on top of the US\$1bn acquisition cost, Xerox opted to sell XDS to Honeywell in 1975. This deal remains one of the costliest acquisitions in American business history.

Xerox's downfall can be attributed to several factors: the euphoria of a rising share price, the glamour of the exciting new computer field, the allure of the unfamiliar, inadequate research, overoptimism, and groupthink. Many lessons from Xerox's experience can be applied in today's market.

MAINTAINING RELEVANCE THROUGH CAPITAL ALLOCATION

Investing involves both science and art. Identifying companies that align with our investment philosophy is relatively straightforward. Building a valuation model requires a little more art. However, the real challenge lies in assessing whether an industry is facing disruption, whether the management team has the strategic vision and skills to navigate the environment, and whether the required opportunities are present. This requires careful consideration and critical thinking that is not prone to groupthink.

At Private Clients, each of our model portfolios has a subcommittee dedicated to discussing such issues. While it is ultimately the portfolio managers' responsibility to make investment decisions, no decision is made hastily or without vigorous debate. While it is highly uncommon for the sub-committee to reach unanimous agreement, it is vital that all views are thoroughly considered. We believe that this robust framework, supported by years of experience, ensures sensible decision-making. It is essential that the businesses we invest in for our clients demonstrate continued relevance through prudent capital allocation decisions.

From Code to Cloud: Unveiling Microsoft's Competitive Advantage

NADINE CHETTY-KHAN, RESEARCH ANALYST AT PRIVATE CLIENTS BY OLD MUTUAL WEALTH



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n the fast-paced world of technology, Microsoft is a titan known not just for its innovative prowess, but also for its strategic capital allocation strategies that have steered the business through evolving market conditions. From its humble beginnings in 1975 to its status as a global leader, Microsoft's journey is marked by a keen focus on research and development (R&D)

investment and strategic acquisitions, all underpinned by a commitment to long-term shareholder value.

Since its inception, Microsoft has focused heavily on software development and has consistently set aside a significant portion of its capital for R&D and strategic acquisitions, driving its continuous pursuit of innovation. This strategic

reinvestment back into the business has been instrumental in laying the foundation for a suite of globally integral products such as the Windows operating system, Microsoft Office suite and Azure cloud platform.

Microsoft's financial prudence is evident in its balanced approach to capital allocation and increasing return on invested capital. While

R&D investments drive innovation, the company maintains a robust balance sheet, which ensures stability and enables strategic investments. Its dividend has grown at an annual compounded rate of 19.3% since 2003 and, together with its share buybacks, reflects the company's commitment to rewarding long-term investors while pursuing growth opportunities. Maintaining a balance between organic growth and strategic acquisitions ensures that Microsoft remains nimble without compromising its financial strength.

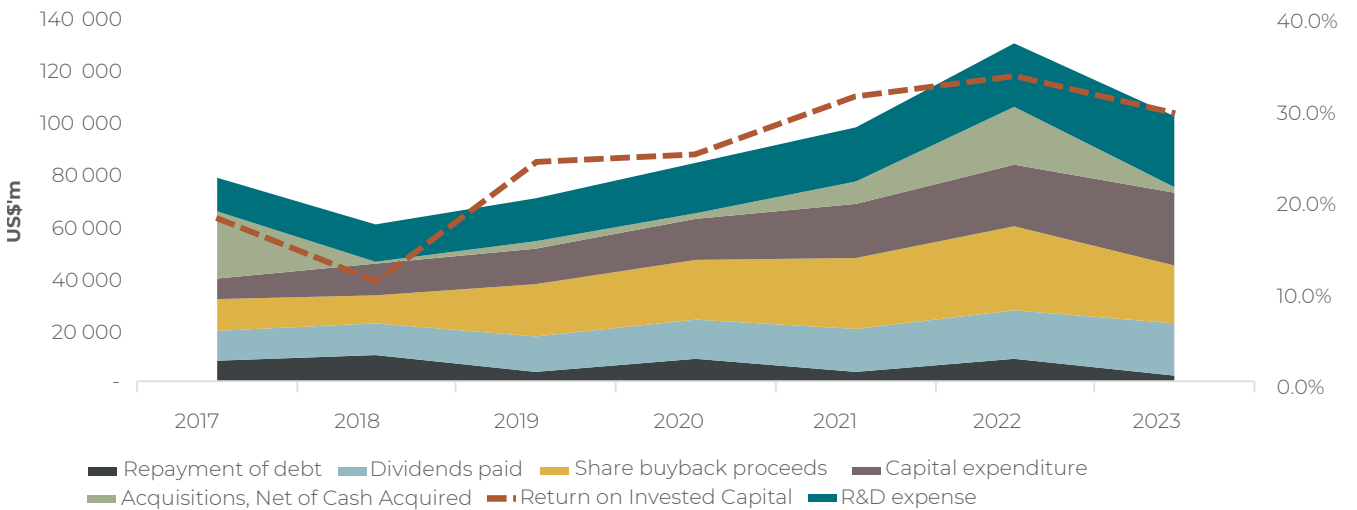
LEARNING FROM MISTAKES AND DRIVING TRANSFORMATION

Microsoft encountered challenges along the way. Under Steve Ballmer's leadership from 2000, the company faced scrutiny for some capital allocation decisions. While paying dividends showed a commitment to shareholder value, the acquisition of Nokia's mobile business received mixed reactions. However, the real transformation came with Satya Nadella's appointment as CEO in 2014

and is testament to the company's effective management of capital, which involves learning from mistakes and taking corrective action.

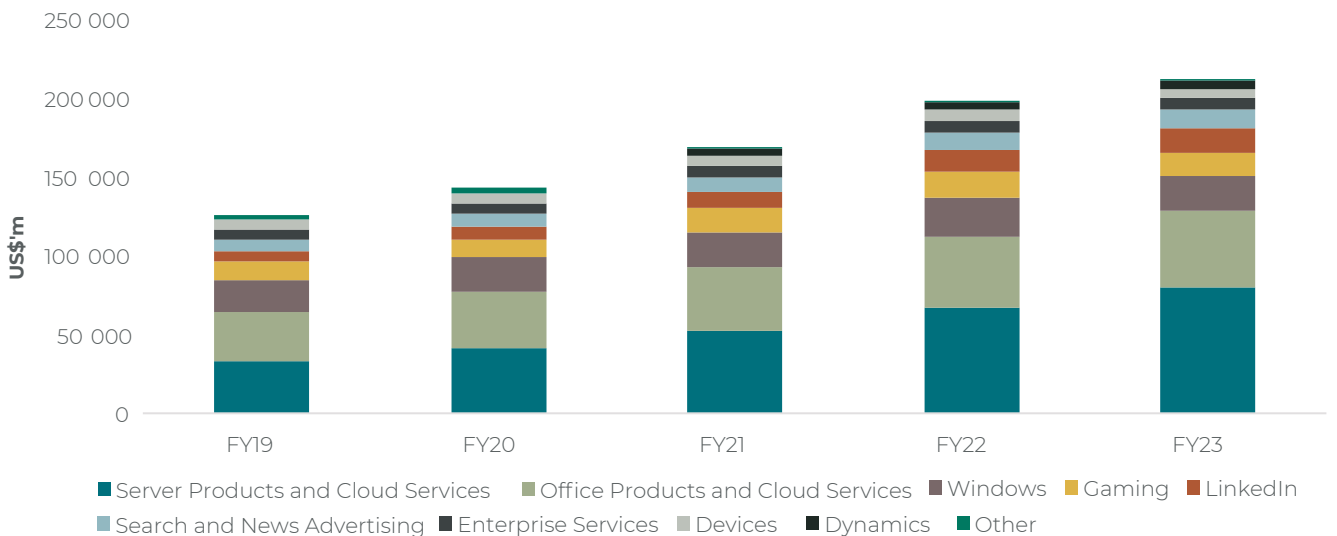
Under Nadella's leadership, Microsoft shifted its focus towards cloud computing, artificial intelligence (AI) and other emerging areas. Azure showcases this strategy, with substantial investments in infrastructure and services leading to impressive growth and positioning Microsoft as a strong competitor to Amazon Web Services (AWS).

Graph 1: Microsoft's capital allocation



Sources: LSEG and Private Clients

Graph 2: Microsoft's revenue by product



Sources: LSEG and Private Clients

Azure's revenue surged by an impressive 30% in the last financial year, highlighting its rapid expansion and growing competitiveness in the cloud market. The shift was facilitated by strategic acquisitions like LinkedIn in 2016 and GitHub in 2018, which seamlessly integrated into Microsoft's ecosystem and bolstered its competitive edge. The acquisition of LinkedIn strengthened Microsoft's position in professional networking, while GitHub provided a platform for open-source collaboration and enriched Microsoft's developer community.

ADAPTING IN AN EVER-EVOLVING ENVIRONMENT

Microsoft has demonstrated remarkable flexibility in response to changing market dynamics and technological advances. In its formative years, Microsoft faced fierce competition, including Apple's Mac and Lotus 1-2-3, which dominated the spreadsheet software market in the 1980s. However, Microsoft's pivotal strategic move came with the development of Windows, which solidified its position as a software powerhouse, as its applications were able to seamlessly integrate with the platform. While competitors were slow to adapt, Microsoft flourished.

As technology evolved, new challenges emerged, including Apple's resurgence with its design-centric approach to electronics and ecosystem integration and Google's entry into search engine and cloud-based services. Additionally, Android OS emerged as a competitor in the mobile space, while Amazon Web Services (AWS) disrupted the cloud computing market. In response, Microsoft has consistently invested in

innovation, ensuring that its offering evolved to meet customer needs, thereby defending its market share.

THE ERA OF APPLIED TECHNOLOGY

Applied Technology – which leverages knowledge and technology to create, design or improve products and processes – is seen as the new frontier of the 21st century. This field incorporates AI, gene and cell therapy, robotics, and the Internet of Things. At Private Clients, we recognise Applied Technology as a key long-term investment theme, and Microsoft provides us with significant exposure to this growth area.

Microsoft has prioritised cloud computing and AI as strategic growth areas. Investments in Azure have positioned Microsoft as a leading player in the cloud computing market, challenging competitors like AWS. While Amazon dominated the public cloud services market with a 40% share in 2022 as per Gartner (vs Microsoft's 21.5% market share), its revenue growth was slower, at a 33% compounded annual growth rate compared to Microsoft's 60% between 2016 and 2023. Gartner predicts that the cloud computing market will grow by around 20% annually from 2001 to 2027, with over 70% of businesses using cloud

platforms by 2027, up significantly from 15% in 2023.

By seamlessly integrating AI into its product lines and developing Azure AI services, Microsoft has positioned itself at the forefront of the AI revolution. A key aspect of the company's AI growth strategy lies in its partnerships, including its collaboration with OpenAI, a leader in AI research, which aims to accelerate AI breakthroughs and make AI more accessible globally. After partnering with Microsoft in 2019, OpenAI successfully launched ChatGPT in 2022 and gained over 100 million monthly users in just two months. Looking ahead, this partnership holds immense potential for both companies.

By leveraging OpenAI's expertise, Microsoft can further differentiate itself in the competitive AI landscape and capitalise on new growth opportunities. Similarly, OpenAI benefits from Microsoft's extensive reach and resources, enabling it to scale its efforts and bring AI technologies to a broader audience. Gartner predicts that by 2026, 80% of businesses will use generative AI applications, up from just 5% in 2023. As AI continues to reshape industries and drive innovation, Microsoft and OpenAI are well positioned to lead this change.

INVESTING IN MICROSOFT'S LEGACY AND FUTURE

Microsoft's strong track record of effective capital allocation and competitive success is a testament to its strategic acumen and financial discipline. The company's solid financials, strategic vision and commitment to innovation make it an attractive investment. As a leader in technology with a clear path forward, we believe that Microsoft is poised to continue its legacy of creating shareholder value, and the company therefore remains a key holding within our Private Clients Global Equity Portfolio.

Shoprite: Winning Where it Matters

VICTOR MUPUNGA, HEAD OF RESEARCH AT PRIVATE CLIENTS BY OLD MUTUAL WEALTH



"T

he best decisions have little to no immediate payoff.

The best choices compound. Most of the benefits come at the end, not the beginning. The more patient you are, the bigger the payoff." – Shane Parrish

The vastly divergent performances of South African food retailers over

the past 20 years are one of the best illustrations of how management decisions affect long-term success.

Back in 2004, with a market value of R11.2bn, Pick n Pay was the largest food retailer on the JSE. The business was 60% larger than its closest competitor Shoprite (R7.1bn) and more than three times Spar's size (R3.6bn). Today, Shoprite

is worth around R152.5bn, making it 12 times larger than Pick n Pay, while Spar's value has increased six-fold to R20.1bn. Meanwhile, Pick n Pay's value has barely changed, currently at around R12.3bn. Given that Pick n Pay and Shoprite have similar business models and operate within the same challenging local economy, it is worth considering why their fortunes have been so different.

HOW DID WE GET HERE?

At Private Clients, free cash flow is a key metric we use when analysing a company, as it shows how much capital is left within the business after funding essential activities, such as interest payments and maintenance capital expenditure (capex). Essentially, management can use this leftover capital for any opportunity they believe will generate superior returns. This often includes acquisitions, dividends or reinvestment into the business.

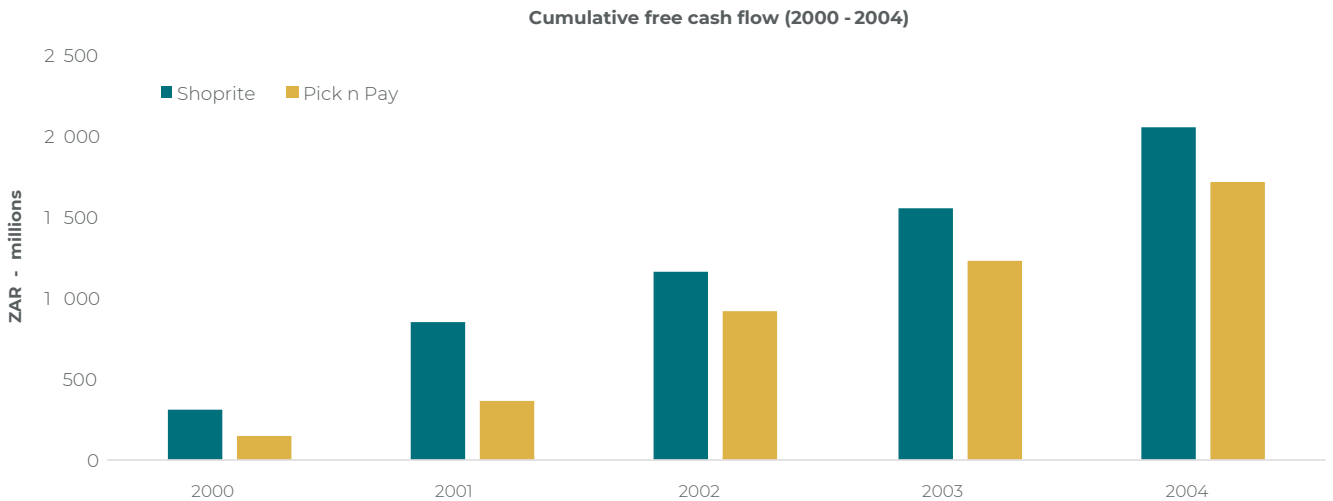
Notably, between 2000 and 2004, Pick n Pay and Shoprite generated similar

free cash flow, with both companies accumulating around R2bn at the end of 2004. But despite starting from the same point, their trajectories have been vastly different since then.

The priorities of Pick n Pay and Shoprite's management teams are evident in how they allocated capital between dividends and capex between 2000 and 2010, as shown in graph 2. For the first half of the decade, Shoprite matched its dividend growth with a similar level of reinvestment into the business, slowing down its capex only during the 2007/2008 Global Financial

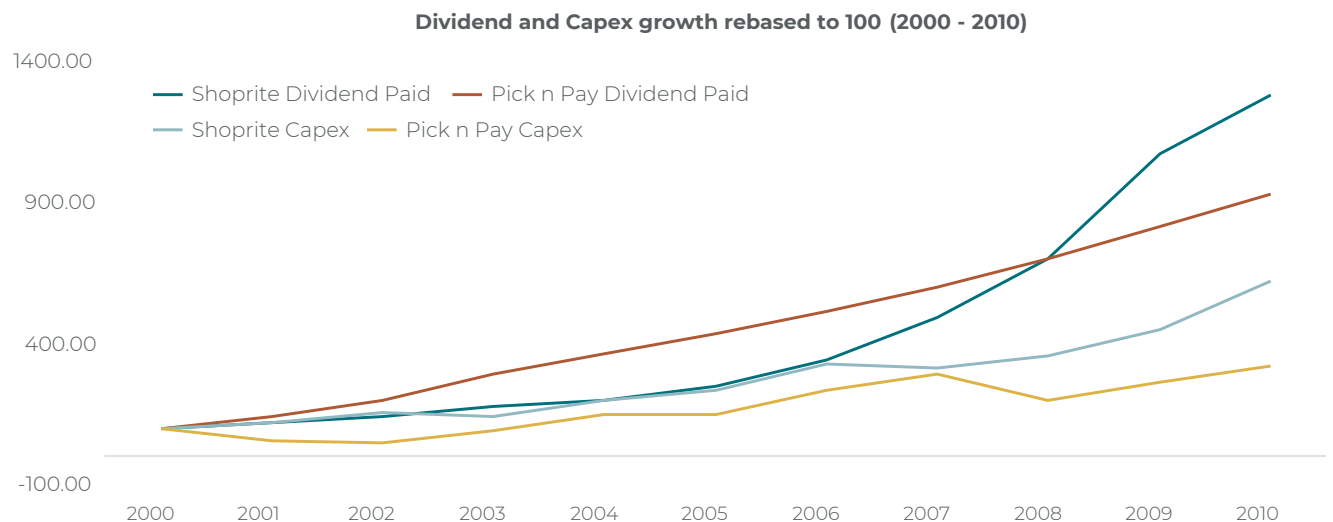
Crisis and then quickly picking up again. In contrast, Pick n Pay increased its dividends at a compound annual growth rate of 25% over the period, more than double the 12% growth rate of its capex. On average, Pick n Pay paid 76% of its earnings as dividends, while Shoprite's dividend was less than half of its earnings. In what at that time was a fast-growing economy, this focus on short-term gains rather than reinvesting into the business allowed smaller competitors like Spar, Woolworths and Shoprite to flourish. We believe that this capital allocation

Graph 1: Cumulated free cash flow generated over the period*



Sources: LSEG and Private Clients

Graph 2: Growth in dividends versus capital expenditure



Sources: LSEG and Private Clients

mistake has been Pick n Pay's biggest error over the past two decades, and the company has not yet fully recovered from it.

In the early 2000s, Shoprite built an extensive distribution network, store footprint and IT systems. As its market share and bargaining power with suppliers grew, Pick n Pay could not keep up with Shoprite's capex scale. By the time Pick n Pay realised this, its market share, earnings and cash flow were declining. By the end of the decade, Shoprite's astute capital allocation allowed it to spend more than three times what Pick n Pay could on capex. This gave Shoprite a strong and hard-to-replicate leadership position based on offering consumers lower prices. Like all good decisions, the benefits of Shoprite's superior historic capital allocation strategy have continued to compound. The gap between the two businesses has further widened, as shown by Shoprite's recent annual dividend of R3.5bn, while Pick n Pay had to suspend its dividend in a bid to strengthen its balance sheet.

FAILING FAST

Apart from the Covid-19 period, 2018 and 2019 were likely the toughest years for Shoprite in the last two decades. During this time, the group's share price declined by nearly 60% due to a sharp increase in foreign-denominated debt taken on to expand across Africa. Adverse currency moves, difficulty in repatriating cash to SA and weak commodity prices saw the group's rest of Africa operations – once viewed as a key differentiator – become a burden rather than an advantage. However, actions taken by Shoprite's management team turned out to be another example of effective capital allocation.

In a short time, the group exited its loss-making non-SA operations, closed poorly performing stores, and launched Checkers Sixty60 and its Xtra Savings rewards programme. Furthermore, the group also sold some of its distribution centres and leased them back. From an incentive perspective, the board enhanced executive remuneration by including performance hurdles that ensured stricter capital allocation. The result was an increase in free cash flow from a negative R2.4bn in 2019 to an average of R4.3bn per year over the next four years. This highlights that while capital allocation errors will happen, it is crucial to fix them quickly. As the late Charlie Munger once said, "Mistakes never get better while you wait, fix them quickly." Ideally, such errors should arise from making "small bets" rather than large acquisitions that could devastate the business if they fail.

MAKING MANY "SMALL BETS"

Since closing its loss-making non-SA operations, Shoprite has focused on providing a wide range of value-added services for local consumers. This includes its mobile network K'nect, which offers one of the cheapest data packages in the country (R19.50 per GB) for Shoprite account holders. The group is also expanding into adjacent categories such as baby clothing (Little Me), pet products (PetShop Science), clothing (UNIQ) and outdoor equipment (Checkers Outdoor). Given that these ventures are often located near existing stores and benefit from Shoprite's scale and cost advantages, they require minimal capital cost and offer competitive pricing.

While none of these small bets alone will drastically transform the group in the short term, they present an

opportunity to increase Shoprite's share of consumer spending in a low-growth economy. Furthermore, with the increased investment in Checkers Sixty60 through the launch of its R99 monthly subscription for unlimited delivery, the group is aiming to boost long-term customer value rather than immediate profits from its fast-growing delivery business. We regard these as prudent capital allocation decisions that diversify the business without risking too much. Coupled with the group's strong data analytics that are supported by the largest loyalty programme in the country (28 million Xtra Savings members), Shoprite has a significant advantage that competitors will find hard to match.

WINNING OVER THE LONG TERM

Given that few businesses are as dependent on the macro economy as retailers, it is interesting to observe the divergent performances within the sector. While economic conditions certainly affect companies, especially over the shorter term, we believe that management decisions on where to invest capital matter more in the long run. Shoprite has excelled in this regard and has shown adaptability over time, unlike many of its peers. We expect the group's current capital allocation strategy of investing in adjacent categories to steadily increase its share of consumer spending. This will drive returns and ultimately compound over the long term, as all good decisions tend to do.

Navigating Foreign Inheritance as an SA Tax Resident

GODWIN MAGOSHA, FIDUCIARY SPECIALIST AT PRIVATE CLIENTS BY OLD MUTUAL WEALTH



Inheriting assets from abroad can be both a blessing and a challenge for South African residents. Consider, for example, an SA resident inheriting a flat in the UK from a relative who emigrated long ago. Suddenly, the resident now has a worldwide estate that includes an offshore asset. If the resident decides to rent the flat out, they will need to register as a UK taxpayer and include the foreign rental in their SA tax

return. What are the estate planning considerations and options?

A BRIEF OVERVIEW OF SA LAW ON FOREIGN INHERITANCE

SA law offers specific provisions for handling foreign assets inherited from tax non-residents. These include exemptions from Exchange Control Regulations and Donations Tax, as well as certain deductions under the Estate Duty Act.

In a nutshell, an SA resident does not have to disclose an inheritance received from a non-resident if the inheritance is located outside SA. Furthermore, this foreign inheritance can also be disposed of without reporting the disposal to the SA Reserve Bank's Financial Surveillance Department. However, local tax disclosures and compliance will apply to the disposal.

While the foreign property inherited will form part of the resident's total

estate, it is excluded by way of a deduction under section 4(1)(e) of the Estate Duty Act. Moreover, the foreign property inherited can be donated without triggering donations tax in South Africa, due to the exemption from donations tax under section 56(1)(e) of the Income Tax Act.

If the foreign property is sold, the base cost used in the calculation of capital gains is the market value of that property at the death of the non-resident plus costs incurred in respect of the foreign property by the executor, in the process of winding down the estate.

If the foreign property is donated to a foreign trust, resulting in income distributions to a non-resident, the attribution rules apply, and the income distributed to the non-resident is included in the resident's income.

ESTATE PLANNING OPTIONS

One of the main objectives for residents inheriting foreign properties might be to avoid becoming subject to tax in foreign jurisdictions. Alternatively, they may seek to hold the property in a manner that reduces estate planning complexities. Whatever the objective, making an informed decision requires a thorough understanding of both SA law and the laws governing the jurisdiction where the property is situated.

Within the scope of SA law, residents have several options when dealing with inherited foreign assets, including:

- **Direct ownership:** Holding the property and renting it out may subject the resident to taxes in both SA and the foreign jurisdiction, requiring annual tax filings in both countries. A Section 6quat rebate may apply to foreign rental income taxed in SA. At death, there will be no estate duty on the foreign property in SA. However, capital gains tax may be payable due to deemed disposal. As a result of a foreign estate created by the inheritance, the resident may need a will dealing with that offshore property. However, there should be no foreign tax rebate if there is a wealth tax on the foreign property – because the value of the foreign property never formed part of the dutiable estate in SA.
- **Immediate disposal:** Selling the inherited property upon acquisition can minimise capital gains tax exposure, though careful consideration of market value and base cost is essential. The proceeds could be invested anywhere in the world, without applying for Financial Surveillance Department permission, and the replacement property is excluded from the SA estate – for estate duty purposes.
- **Transfer to a foreign company:** Transferring the property to a foreign company within which the resident is a majority shareholder could create a controlled foreign company, requiring compliance with the controlled foreign company provisions of the Income Tax Act.
- **Donation to a foreign trust:** The property could be donated to a foreign trust without triggering South African donations tax, but may result in income tax obligations for distributions from the trust to non-resident beneficiaries.
- **Sale to a foreign trust on a loan account:** Selling the property to a foreign trust on loan account can provide tax-efficient income streams, though careful structuring is necessary. Since the loan is based on foreign currency, market-related interest may be significantly lower than what could have been charged on an SA rand loan. The loan account will remain level over the lifetime of the resident taxpayer. At death, there is no capital gains tax on the disposal of a loan account and the loan account will not attract estate duty in SA. The foreign interest income will be included in the SA tax return, and if there are interest payments by the foreign trust to the resident taxpayer, the receipts should be sufficient to pay domestic tax. The tax payable to the tax authorities in the foreign jurisdiction could be reduced by claiming tax treaty benefits between SA and that foreign jurisdiction.

Each of the above options carry their own tax and legal implications, requiring careful evaluation based on individual circumstances and objectives. Professional advice is recommended to navigate both SA and foreign tax laws effectively. In conclusion, while inheriting foreign assets as an SA tax resident presents complexities, understanding the legal landscape can facilitate informed decision-making and optimal estate and tax planning.

Beyond Geographies and Generations

SARETTE VAN DEN HEEVER AND WAYNE SOROUR, WEALTH DIRECTORS AT PRIVATE CLIENTS BY OLD MUTUAL WEALTH



Crafting and managing a well-structured portfolio of investments in one geography, for one family can be challenging. In today's ever-shrinking world, where families are scattered across the globe and uncertainty reigns supreme, these challenges become even more significant.

While previous generations might have initially focused on accumulating assets and building wealth predominantly within South Africa, the next generation is being compelled to plan and manage

their affairs globally from the outset, says Sarette van den Heever.

“For most South African families, it has now become the norm to have multiple family members living, earning, accumulating assets, and paying tax in at least one other country. Where you choose to live, no longer determines where you earn income and where you build assets – these can all be in different and multiple countries. Our clients with young families are considering the reality of their children studying abroad and most probably settling there

permanently. In that case, they are actively exploring options to live abroad themselves, if only for part of the year, and to have assets and funds available in the local currency,” she says.

But this brings with it a host of complexities. Once investments are made offshore, navigating the different laws and regulations across different countries and currencies can become a minefield. This complexity also extends to owning property, setting up trusts and managing tax and estate duties.

There's no doubt that effectively managing assets across

various jurisdictions demands a comprehensive understanding of the respective financial, legal and structural considerations. “Before making any significant decisions, such as investing, acquiring alternative citizenship, emigrating or taking any unconventional steps outside South Africa, it’s essential to seek expert advice timeously to understand the implications, avoid potential pitfalls and ensure a successful outcome,” says Wayne Sorour.

“Many people try to cut corners to avoid investing in professional advice to understand the implications, which often leads to costly consequences,” he says.

These days, many investors’ children live, work and study abroad, often in different countries. Others work overseas for 10, 20 years, earn money in that country and then come back. “In such a situation, questions about the efficiency of your investments and the future of your wealth become crucial. Are you getting the best returns on your investments, and should the assets be held in a more tax-efficient legal structure? Most of these structures should be put in place before one leaves and/or returns to South Africa. If you have created a business, will it continue to thrive after you are gone and will your loved ones be properly cared for?

“Therefore, effective planning and revisiting your investment portfolio and structures several months ahead of your departure or return can save you a lot of tax, both here and in the country where you have worked. I often see how clients assume laws and regulations regarding tax, property, investments and estates work the same across the world. This can lead to

immediate or future losses of millions or prevent their loved ones from accessing money or assets after they have passed on,” Wayne says.

ACCESS TO GLOBAL EXPERTS

Apart from advising clients about the best offshore investments and structures that would make the most sense for their specific circumstances and needs, Private Clients by Old Mutual Wealth also assists with cross-border tax and fiduciary services, advising individuals with business interests and investments in multiple countries. Complementing its highly experienced in-house family office, investment management and fiduciary services teams, the business has also established strong relationships with lawyers, tax consultants and other specialist experts outside South Africa.

“If a client has a particular need in, say, the US where they want to emigrate to, I know who to call. We make sure that the client gets the right advice so when they settle in the US, they’re not going to get any surprises from the tax authorities,” Wayne explains.

Planning for the future also involves considering how your estate will devolve to your children and loved ones and, where applicable, how your business will be managed into your retirement and after your death,

says Sarette. This calls for careful and effective succession planning.

This may sound like too many different experts are needed to successfully manage your wealth and everything that goes with it, including what happens to it once you’re gone. Dealing with multiple financial advisers could potentially pose a risk because there isn’t one cohesive picture and structure.

“Indeed,” says Sarette, “that’s why we have a ‘family office’ that is responsible for overseeing the entire family, not just the individuals who have been generating the wealth. This includes managing various structures such as trusts and companies, whether they are operating businesses or other entities created to manage wealth. The family office also assists all family members within this structure, including children and grandchildren,” she explains.

“The real benefit of having this type of structure is having one office that manages all your affairs and understands how everything is interconnected, including the links between different family members, risks and opportunities. On a practical level, it is invaluable to have one point of contact to sort out anything from complex global tax structures to simple tasks like making payments or arranging insurance assessments,” she says.

“The family office in Private Clients by Old Mutual Wealth was established in 1925 and it has looked after some of the families for four generations. With this comes significant learnings and established professional relationships across the globe, all managed from South Africa. In addition to our skilled in-house team, we work closely with families’ existing advisers, accountants, lawyers and investment managers and we call on a wide network of well-established professional firms to assist us in the management of our clients’ affairs,” Sarette says.

The Authors



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Andrew joined Private Clients in 2017 and was previously employed at Cannon Asset Managers. He joined Cannon in 2007 as a Research Analyst and during his tenure, he rose through the ranks to become a Portfolio Manager in 2011 and was then appointed CIO in 2014. Andrew has extensive knowledge of and insight into valuing businesses across multiple industries and identifying suitable investment opportunities. He holds a Master's degree in Economic Science from the University of the Witwatersrand, where he lectured for a while. Andrew also holds a PhD in Investments and Securities from the University of Pretoria.



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Nadine joined Private Clients in March 2024 and was previously employed as an Equity Analyst at Investment Managers Laurium Capital, Mazi Global and Old Mutual Titan. Prior to that, she was an Old Mutual Chartered Accountant Trainee and worked with various departments within the business, including Private Clients' Finance team. Nadine qualified as a Chartered Accountant at the end of 2017 and has also completed CFA Level 2. She also completed a Marketing and Entrepreneurship course with StartUp School.



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Victor joined Private Clients in 2016 and is responsible for conducting research relating to all aspects of our investment portfolios, including top down, bottom up, idea generation, macro and asset allocation research. He also serves as Portfolio Manager of the Private Clients Equity Income Model Portfolio. Victor was previously employed as an Investment Analyst at Maestro Investment Management, where in addition to equity research, he was responsible for managing a number of private client equity portfolios. Prior to that, he was a Fund Accountant at Investment Data Services where he prepared and reviewed valuations and accounting records of hedge funds. Victor graduated with an MBA from Stellenbosch Business School as well as a Business Science Finance (Hons) degree from the University of Cape Town. He is also a CFA Charterholder.



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Godwin joined Private Clients in 2024 as a Fiduciary Specialist. He started his career with Old Mutual in 2006 with Personal Financial Advice (PFA) as a Financial Analyst. He worked for Succession Financial Planning as a Broker and joined Liberty South Africa as a Legal Adviser, before returning to Old Mutual in 2021. Godwin is an admitted attorney of the High Court of South Africa. He holds LLB (Unisa), BCom (Hons) (UCT), MPhil Tax Law (UCT), Postgraduate Diploma in Financial Planning (UFS) and Postgraduate Diploma in Estate Planning (UFS). He has over 15 years' experience in the financial services industry.



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Wayne obtained his BProc LLB at the University of the Free State and is an admitted attorney. He joined Old Mutual as a Legal Adviser and has spent many years in the financial services industry where he gained vast experience in sales, wealth management and the distribution side of asset management. Before joining Private Clients as Wealth Director, Wayne held the position of Head of Old Mutual International: Sales and Distribution in South Africa where he worked in the offshore market for over 15 years. He also holds a CFP®.



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Sarette has spent over 15 years in the wealth management industry, holding numerous positions within Old Mutual Wealth as a Business Development Executive. In 2016, she moved into the Fintech industry where she fulfilled a strategic consulting role. In 2023, Sarette joined Private Clients as a Wealth Director and assisted the business in developing and building its high net worth client proposition. She holds a BCom in Actuarial Science and an MBA.



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