MCEV disclosure for covered business in Emerging Markets

For the six months ended 30 June 2014

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1. Analysis of covered business MCEV

The following section provides a summary of the components of MCEV for the covered business in Emerging Markets.

Components of MCEV for covered business

			Rm
	At 30 June 2014	At 30 June 2013	At 31 December 2013
Adjusted net worth	28,466	28,169	28,262
Free surplus	8,769	9,150	8,854
Required capital	19,697	19,019	19,408
Value of in-force	24,140	20,776	23,210
Present value of future profits	30,193	25,816	28,934
Frictional costs	(3,679)	(3,116)	(3,603)
Cost of residual non-hedgeable risks	(2,374)	(1,924)	(2,121)
MCEV	52,606	48,945	51,472

MCEV increased by 2% compared to 31 December 2013 due to higher operating earnings, mainly as a result of a strong existing business contribution, the value of new business and good investment performance, partially offset by net transfers in the form of dividend payments and other capital transfers.

Analysis of change for covered business for the six months ended 30 June 2014

Rm

	Six months ended 30 June 2014				
	Free surplus	**Required capital**	**Adjusted net worth**	**Value of in-force**	**MCEV**
Opening MCEV	**8,854**	**19,408**	**28,262**	**23,210**	**51,472**
New business value	**(1,392)**	**995**	**(397)**	**1,215**	**818**
Expected existing business contribution (reference rate)	**228**	**450**	**678**	**915**	**1,593**
Expected existing business contribution (in excess of reference rate)	**32**	**77**	**109**	**137**	**246**
Transfers from VIF and required capital to free surplus	**2,936**	**(1,227)**	**1,709**	**(1,709)**	**-**
Experience variances (excluding development costs)	**261**	**(28)**	**233**	**18**	**251**
Experience variances - development costs	**(106)**	**-**	**(106)**	**-**	**(106)**
Assumption changes	**-**	**-**	**-**	**-**	**-**
Other operating variance	**(116)**	**-**	**(116)**	**(215)**	**(331)**
Operating MCEV earnings	**1,843**	**267**	**2,110**	**361**	**2,471**
Economic variances	**573**	**14**	**587**	**543**	**1,130**
Other non-operating variance	**-**	**-**	**-**	**-**	**-**
Total MCEV earnings	**2,416**	**281**	**2,697**	**904**	**3,601**
Closing adjustments	**(2,501)**	**8**	**(2,493)**	**26**	**(2,467)**
Capital and dividend flows	**(2,518)**	**-**	**(2,518)**	**-**	**(2,518)**
Foreign exchange variance	**17**	**13**	**30**	**22**	**52**
Other	**-**	**(5)**	**(5)**	**4**	**(1)**
Closing MCEV	**8,769**	**19,697**	**28,466**	**24,140**	**52,606**
Return on MCEV (RoEV)% per annum[1]					**10.2%**

[1] Return on MCEV is calculated as the annualised operating MCEV earnings after tax divided by opening MCEV. The operating assumption changes and other operating variances are not annualised.

Rm

	Six months ended 30 June 2014		
	Adjusted net worth	**Value of in-force**	**MCEV**
Experience variances (excluding development costs)	**233**	**18**	**251**
Persistency	**9**	**21**	**30**
Risk	**448**	**34**	**482**
Expenses	**(43)**	**(10)**	**(53)**
Other	**(181)**	**(27)**	**(208)**

New business: VNB decreased by 17% compared to the first six months of 2013 despite higher sales volumes due to a reduction in new business margins. Margins have decreased as a result of a higher new business strain (larger salaried sales force in Mass Foundation Cluster without an equivalent increase in sales volumes at this stage), a less profitable mix of business (particularly in Namibia, due to strong high margin Corporate Segment smoothed bonus sales in 2013 which have not been repeated, as well as within Mass Foundation Cluster) and the negative impact of the operating assumption changes implemented at the end of 2013 (including the increase of lapse assumptions in Mass Foundation Cluster and an expense allocation change in Mexico).

Experience variances: Experience variances (excluding development costs) were a positive R251 million, mainly due to positive mortality and disability experience on protection and annuity business. In addition, persistency profits have emerged (positive experience in Corporate Segment and Retail Affluent was partially offset by negative variances on Mass Foundation Cluster risk products which were less negative than experienced in the 2013 half year following the assumption changes made at the end of 2013). Other experience variances include the impact of the decision to reduce certain product fees in Retail Affluent to provide better value for money to clients and improve competitiveness, as well as higher than anticipated taxation.

Development costs: These costs are mainly in respect of initiatives relating to new product offerings and establishing distribution capabilities in Africa.

Operating assumption changes: No operating assumption changes were made during the reporting period.

Other operating variances: This includes modelling changes and improvements. The most significant impacts relate to updates to the capital requirements used in the calculation of the cost of non-hedgeable risks and modelling improvements in Africa (including South Africa) and Mexico.

Economic variances: Positive economic variances are mainly due to favourable investment performance on policyholder and shareholder funds, which include growth in local equity markets, particularly in South Africa and Namibia.

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Closing adjustments: Significant net transfer items relate to net dividends paid (after allowing for dividends received from Nedbank and the Property and Casualty business), accounting more appropriately for the purchases of subsidiaries in prior years and the purchase of the Faulu operations in Kenya.

Analysis of change for covered business for the six months ended 30 June 2013

					Rm
	Six months ended 30 June 2013				
	Free surplus	Required capital	Adjusted net worth	Value of in-force	MCEV
Opening MCEV	7,231	18,074	25,305	20,367	45,672
New business value	(1,194)	990	(204)	1,186	982
Expected existing business contribution (reference rate)	184	381	565	729	1,294
Expected existing business contribution (in excess of reference rate)	26	73	99	120	219
Transfers from VIF and required capital to free surplus	2,574	(1,046)	1,528	(1,528)	-
Experience variances (excluding development costs)	(164)	55	(109)	(206)	(315)
Experience variances - development costs	(33)	-	(33)	(1)	(34)
Assumption changes	-	-	-	-	-
Other operating variance	(202)	100	(102)	(33)	(135)
Operating MCEV earnings	1,191	553	1,744	267	2,011
Economic variances	841	172	1,013	98	1,111
Other non-operating variance	(18)	-	(18)	-	(18)
Total MCEV earnings	2,014	725	2,739	365	3,104
Closing adjustments	(95)	220	125	44	169
Capital and dividend flows	(356)	93	(263)	-	(263)
Foreign exchange variance	261	127	388	44	432
Other	-	-	-	-	-
Closing MCEV	9,150	19,019	28,169	20,776	48,945
Return on MCEV (RoEV)% per annum[1]					9.1%

[1] Return on MCEV is calculated as the annualised operating MCEV earnings after tax divided by opening MCEV. The operating assumption changes and other operating variances are not annualised.

			Rm
	Six months ended 30 June 2013		
	Adjusted net worth	Value of in-force	MCEV
Experience variances (excluding development costs)	(109)	(206)	(315)
Persistency	(27)	(145)	(172)
Risk	268	(8)	260
Expenses	(172)	(15)	(187)
Other	(178)	(38)	(216)

Analysis of change for covered business for the year ended 31 December 2013

Rm

	Year ended 31 December 2013				
	Free surplus	Required capital	Adjusted net worth	Value of in-force	MCEV
Opening MCEV	7,231	18,074	25,305	20,367	45,672
New business value	(2,349)	1,822	(527)	2,570	2,043
Expected existing business contribution (reference rate)	311	736	1,047	1,506	2,553
Expected existing business contribution (in excess of reference rate)	51	147	198	254	452
Transfers from VIF and required capital to free surplus	4,813	(1,959)	2,854	(2,854)	-
Experience variances (excluding development costs)	170	103	273	10	283
Experience variances - development costs	(257)	-	(257)	5	(252)
Assumption changes	143	(34)	109	(295)	(186)
Other operating variance	(296)	25	(271)	343	72
Operating MCEV earnings	2,586	840	3,426	1,539	4,965
Economic variances	2,064	242	2,306	1,316	3,622
Other non-operating variance	13	-	13	(137)	(124)
Total MCEV earnings	4,663	1,082	5,745	2,718	8,463
Closing adjustments	(3,040)	252	(2,788)	125	(2,663)
Capital and dividend flows	(2,921)	98	(2,823)	-	(2,823)
Foreign exchange variance	258	154	412	110	522
Other[1]	(377)	-	(377)	15	(362)
Closing MCEV	8,854	19,408	28,262	23,210	51,472
Return on MCEV (RoEV)% per annum					11.0%

[1] Other relates to the impact of including certain African entities (Zimbabwe, Kenya, Malawi, Swaziland and Nigeria) on an MCEV basis and an adjustment to allow for non-controlling interests in Zimbabwe.

Rm

	Year ended 31 December 2013		
	Adjusted net worth	Value of in-force	MCEV
Experience variances (excluding development costs)	273	10	283
Persistency	(82)	(46)	(128)
Risk	527	75	602
Expenses	(243)	(10)	(253)
Other	71	(9)	62

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2. New business results

The following section provides a summary of the new business information for Emerging Markets.

Value of new business and new business profitability

The tables below set out an analysis of the value of new business (VNB) after tax. New business profitability is measured by both the ratio of the VNB to the present value of new business premiums (PVNBP) as well as to the annual premium equivalent (APE), and shown under PVNBP margin and APE margin below. APE is calculated as recurring premiums plus 10% of single premiums.

Rm

	Annualised recurring premiums	Single premiums	PVNBP	PVNBP capitalisation factors[1]	APE	APE margin	VNB	PVNBP margin
Covered business								
30 June 2014	**2,885**	**12,378**	**27,644**	**5.3**	**4,123**	**20%**	**818**	**3.0%**
30 June 2013[2]	2,432	11,348	24,972	5.6	3,567	28%	982	3.9%
31 December 2013[3]	5,360	22,843	51,470	5.3	7,645	27%	2,043	4.0%

[1] The PVNBP capitalisation factors are calculated as follows: (PVNBP - single premiums)/annualised recurring premiums.

[2] New business figures for Rest of Africa, other than Namibia, were not included in the June 2013 information reported above as no value of new business and PVNBP calculations were performed for these businesses.

[3] New business figures for Rest of Africa, other than Namibia, were included for the first time at December 2013.

Rest of Africa life business premiums

The following amounts are included in respect of the life businesses in Zimbabwe, Malawi, Kenya, Swaziland and Nigeria in the June 2014 information reported above (June 2013: excluded; December 2013: included).

Rm

Emerging Markets - Rest of Africa (excluding Namibia)	**Six months ended 30 June 2014**	Six months ended 30 June 2013	Year ended 31 December 2013
New business single premiums	**278**	350	739
Annualised recurring premiums	**119**	141	232
APE	**147**	176	306

The new business figures in the table above include minority interests and renewal premiums for the six months ended 30 June 2013 and the year ended 31 December 2013. As from June 2014, these new business figures are reported excluding minority interests and renewal premiums.

Additional new business written by Emerging Markets

New business single premiums of R1,629 million, annualised recurring premiums of R258 million, and APE of R421 million, in respect of the life business in India and China for the six months ended June 2014 have been excluded from the above tables, as these businesses are not modelled on an MCEV basis.

The value of new individual unit trust linked retirement annuities and pension fund asset management business written by the Emerging Markets long-term business of R7,289 million (June 2013: R7,433 million; December 2013: R15,263 million) is excluded from VNB (as well as APE and PVNBP) above as the profits in this business arise in the asset management business.

The new business figures presented in this section exclude premium increases arising from indexation arrangements in respect of existing business, as these are already included in the value of in-force business.

Drivers of new business value for covered business (PVNBP margin)

			%
	30 June 2014	30 June 2013	31 December 2013
Margin at the end of comparative reporting period	**3.9**	3.5	4.1
Change in volume	**(0.5)**	0.2	0.1
Change in country and product mix	**(0.3)**	0.1	-
Change in operating assumptions	**(0.2)**	-	(0.2)
Change in economic assumptions	**0.1**	0.1	0.1
Change in tax/regulation	**-**	-	(0.1)
Margin at the end of the reporting period	**3.0**	3.9	4.0

The decrease in new business margins compared to 30 June 2013 is mainly due to higher new business strain (larger salaried sales force in Mass Foundation Cluster), a less profitable business mix in Mass Foundation Cluster and Namibia, and the impact of the operating assumption changes made at the end of 2013 (including the increase of lapse assumptions in Mass Foundation Cluster and an expense allocation change in Mexico).

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3. MCEV sensitivity information

The tables below show the sensitivity of the MCEV, the value of in-force business at 30 June 2014 and the value of the new business for the six months ended 30 June 2014 to the following:

- **Economic assumptions 100bps increase/ decrease**: Increasing/ decreasing all pre-tax investment and economic assumptions (projected investment returns and inflation) by 100bps, with credited rates and discount rates changing commensurately.
- **10 bps increase of liquidity spreads:** Recognising the present value of an additional 10bps of liquidity spreads assumed on corporate bonds over the lifetime of the liabilities, with credited rates and discount rates changing commensurately.

For each sensitivity illustrated, all other assumptions have been left unchanged except where they are directly affected by the revised conditions. Sensitivity scenarios therefore include consistent changes in cash flows directly affected by the changed assumption(s), for example future bonus participation in changed economic scenarios.

			Rm
MCEV	**30 June 2014**	30 June 2013	31 December 2013
Central assumptions	**52,606**	48,945	51,472
Value given changes in:			
Economic assumptions 100bps increase	**51,941**	47,926	50,738
Economic assumptions 100bps decrease	**53,189**	49,900	52,013
10bps increase of liquidity spreads	**52,714**	49,052	51,577

			Rm
VIF	**30 June 2014**	30 June 2013	31 December 2013
Central assumptions	**24,140**	20,776	23,210
Value given changes in:			
Economic assumptions 100bps increase	**23,475**	19,757	22,464
Economic assumptions 100bps decrease	**24,723**	21,731	23,765
10bps increase of liquidity spreads	**24,248**	20,883	23,315

			Rm
VNB	**30 June 2014**	30 June 2013	31 December 2013
Central assumptions	**818**	982	2,043
Value given changes in:			
Economic assumptions 100bps increase	**779**	900	1,962
Economic assumptions 100bps decrease	**855**	1,048	2,085
10bps increase of liquidity spreads	**822**	985	2,054

4. Reconciliation of IFRS net asset value to MCEV adjusted net worth for the covered business

The table below provides a reconciliation of the IFRS net asset value (NAV) to the MCEV adjusted net worth for the covered business.

			Rm
	At 30 June 2014	At 30 June 2013	At 31 December 2013
IFRS net asset value	**22,494**	20,405	21,121
Adjustment to include long-term business on a statutory solvency basis	**2,782**	2,480	2,738
Inclusion of Group equity and debt instruments held in life funds	**3,882**	5,404	5,106
Goodwill	**(134)**	(120)	(134)
Other[1]	**(558)**	-	(569)
Adjusted net worth attributable to ordinary equity holders of the parent	**28,466**	28,169	28,262
Value of in-force business	**24,140**	20,776	23,210
MCEV	**52,606**	48,945	51,472

[1] Adjustment to allow for non-controlling interest in Zimbabwe.

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5. MCEV Methodology

The following section provides information on the methodology used to calculate MCEV results. The methodology used to calculate 30 June 2014 MCEV results is consistent with 31 December 2013 unless explicitly noted in this disclosure.

Basis of preparation and coverage

MCEV is a measure of the consolidated value of shareholders' interests in the covered business and consists of the sum of the shareholders' adjusted net worth in respect of the covered business and the value of the in-force covered business.

The Market Consistent Embedded Value Principles (Copyright © Stichting CFO Forum Foundation 2008) issued in June 2008 and updated in October 2009 by the CFO Forum (the Principles) have been used as the basis for preparing the MCEV disclosure information for the covered business in Emerging Markets.

The CFO Forum announced changes to the MCEV Principles in October 2009 to reflect inter alia the inclusion of a liquidity premium. These changes affirm that the risk free reference rate to be applied under MCEV should include both the swap yield curve appropriate to the currency of the cash flows and a liquidity premium where appropriate.

The Principles have been materially complied with in the preparation of MCEV information for the Emerging Markets business at 30 June 2014. Note however that detailed consolidated disclosure information has not been prepared for the Old Mutual Group as required by the Principles.

For the Emerging Markets business, covered business includes, where material, any contracts that are regarded by local insurance supervisors as long-term life insurance business, and other business, where material, directly related to such long-term life assurance business where the profits are included in the IFRS long-term business profits in the primary financial statements. For the life businesses in entities where the covered business is not material, the treatment within this supplementary information is the same as in the primary IFRS financial statements (i.e. expected future profits for this business are not capitalised for MCEV reporting purposes).

Some types of business are legally written by a life company, but under IFRS are classified as asset management because 'long-term business' only serves as a wrapper. This business is excluded from covered business, for example individual unit trusts and some group market-linked business written by asset management companies in South Africa through the life company as profits from this business arise in the asset management and asset administration companies.

The detailed methodology and assumptions made in presenting this information are set out in the following sections. The MCEV for Emerging Markets is presented after an adjustment to include the market value of life fund investments in Group equity and debt instruments.

Methodology

(a) Required capital

Required capital is the market value of assets that is attributed to support the covered business, over and above that required to back statutory liabilities for covered business, whose distribution to shareholders is restricted.

For Emerging Markets, capital is determined with reference to internal management objectives. The required capital in respect of OMLAC(SA)'s covered business is partially covered by the market value of the Group's investments in banking and Property & Casualty in South Africa. On consolidation these investments are shown separately.

The table below shows the level of required local capital expressed as a percentage of the minimum local regulatory capital requirements.

			Rm
	At 30 June 2014	At 30 June 2013	At 31 December 2013
Required capital (a)	**19,697**	19,019	19,408
Regulatory capital (b)	**14,390**	13,111	13,983
Ratio (a/b)	**1.4**	1.5	1.4

(b) Cost of residual non-hedgeable risks

The cost of residual non-hedgeable risks (CNHR) is calculated using a cost of capital approach, i.e. it is determined as the present value of capital charges for all future non-hedgeable risk capital requirements until the liabilities have run off.

A cost of capital charge of 2.0% has been applied to residual symmetric and asymmetric non-hedgeable capital at a business unit level over the life of the contracts.

The amount of diversified economic capital held in respect of residual non-hedgeable risks in Emerging Markets is R15,256 million at 30 June 2014 (R13,196 million at 30 June 2013; R14,041 million at 31 December 2013).

(c) Taxation

A change to the tax relief on expenses became effective as from 1 January 2013, which had the effect of increasing the Expense Relief Ratio (ERR) from 8% in 2012 to 11.5% in 2013 and 2014 (approximate effective rates). The effect of the change has not yet been allowed for in the MCEV assumptions.

In addition, the new draft Tax Laws Amendment Bill issued in 2014 has proposed that protection business should be taxed in the corporate (shareholder) fund from 1 January 2016, applying to new protection business written after this date.

6. MCEV assumptions

The following section provides details of the economic and non-economic assumptions used in the MCEV calculations. The assumptions have been derived in a consistent manner to 31 December 2013 calculations unless explicitly stated as a change in this disclosure note.

Economic assumptions

The following sections relate to the economic assumptions in South Africa. In other territories, economic assumptions are determined with reference to local economic conditions.

(a) Risk-free reference rates and inflation

The risk free reference rates, reinvestment rates and discount rates are determined with reference to the swap yield curve appropriate to the currency of the cash flows. For Emerging Markets the swap yield curve is sourced internally (using market data provided by the Bond Exchange of South Africa) and is checked for reasonability relative to the Bloomberg swap yield curve.

At 30 June 2014, a liquidity premium adjustment has been applied to OMLAC(SA)'s Immediate Annuity business and Fixed Bond business. A liquidity premium adjustment is applied to OMLAC(SA)'s Fixed Bond business as OMLAC(SA) holds a portfolio of non-government bonds which have a market yield in excess of the risk free rate and the duration of the asset portfolio and the liability duration are a good match (meaning the asset portfolio is held to maturity). Cash flows on this product are also predictable and the company has adequate liquidity to withstand a substantial increase in lapses at all durations without having to sell bonds which further strengthens the case for applying a liquidity premium.

It is the directors' view that a proportion of non-government bond spreads at 30 June 2014 is attributable to a liquidity premium rather than only to credit and default allowances and that returns in excess of swap rates can be achieved, rather than entire spreads being lost to worsening default experience. For OMLAC(SA)'s Immediate Annuity business the currency, credit quality and duration of the actual bond portfolios were considered and adjusted risk free reference rates were derived at 30 June 2014 by adding 50bps of liquidity premium for this business (June 2013: 50bps; December 2013: 50bps) to the swap rates used for setting investment return and discounting assumptions. For OMLAC(SA)'s Fixed Bond products 40bps of liquidity premium was added to the swap rates (June 2013: 45bps; December 2013: 40bps). These adjustments reflect the liquidity premium component in non-government bond spreads over swap rates that are expected to be earned on the portfolios. The liquidity premium was derived by comparing the yields of South African government bonds with bonds of similar duration issued by state-owned enterprises.

The risk free reference spot yields (excluding any applicable liquidity adjustments) at various terms are provided in the table below. Expense inflation rates have been derived by comparing real rates of return against nominal risk free rates, with adjustments for higher anticipated inflation rates where appropriate.

Risk free reference spot yields (excluding liquidity adjustments) and expense inflation

		%
	Risk-free rate	**Expense inflation**
At 30 June 2014		
1 year	6.6	6.6
5 years	7.9	7.4
10 years	8.7	8.0
20 years	9.3	8.3
At 30 June 2013		
1 year	5.7	7.0
5 years	7.5	7.5
10 years	8.5	8.2
20 years	9.0	8.4
At 31 December 2013		
1 year	5.7	6.8
5 years	7.7	7.6
10 years	8.8	8.3
20 years	9.7	8.9

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(b) Volatilities

The at-the-money annualised asset volatility assumptions of the asset classes incorporated in the stochastic models are detailed below.

ZAR volatilities[1]

Option term	1 year swap	5 year swap	10 year swap	20 year swap	% Equity (total return index)
At 30 June 2014					
1 year	25.3	22.7	21.0	20.0	15.9
5 years	21.1	20.0	19.2	19.7	25.0
10 years	19.2	18.8	19.3	20.7	28.2
20 years	22.6	23.8	24.8	24.3	28.3
At 30 June 2013					
1 year	32.4	26.3	23.8	22.8	21.3
5 years	23.9	22.5	21.5	22.1	28.1
10 years	21.3	21.1	22.3	23.1	29.5
20 years	25.3	24.9	26.9	26.8	30.0
At 31 December 2013					
1 year	31.7	26.2	23.8	22.2	20.7
5 years	23.6	22.6	21.0	21.4	26.2
10 years	21.3	20.1	21.0	21.5	29.0
20 years	24.6	25.0	24.4	23.2	29.6

[1] Due to limited liquidity in the ZAR swaption market, the market consistent asset model has been calibrated by extrapolating swaption and equity implied volatility data beyond a term of one year and 5 years respectively.

(c) Expected asset returns in excess of the risk free reference rates

The expected asset returns in excess of the risk free reference rates have no bearing on the calculated MCEV other than the calculation of the expected existing business contribution in the analysis of MCEV earnings.

Pre-tax real-world economic assumptions are determined as follows:

- The equity risk premium is 3.7%.
- The cash return equals the one year risk free reference rate.
- The property risk premium is 1.5%.
- Returns on corporate bonds reference actual yields from assets held.

(d) Effective tax rates

The weighted average effective tax rate that applies to the cash flow projections in OMLAC(SA) at 30 June 2014 is 29% (June 2013: 28%; December 2013: 29%).

Non-economic assumptions

The appropriate non-economic projection assumptions for future experience (e.g. mortality, persistency and expenses) are determined using best estimate assumptions of each component of future cash flows and have regard to past, current and expected future experience where sufficient evidence exists (e.g. longevity improvements and AIDS-related claims), as derived from both entity-specific and industry data where deemed appropriate.

The management expenses attributable to life assurance business have been analysed between expenses relating to the acquisition of new business, maintenance of in-force business (including investment management expenses) and development projects.

- All expected maintenance expense overruns affecting the covered business are allowed for in the calculations.
- The MCEV makes provision for future development costs and one-off expenses relating to in-force covered business that are known with sufficient certainty, based on three year business plans. The provision is reduced to the extent that projects have associated benefits that are directly quantifiable and are considered to emerge within a reasonable timeframe (e.g. over the business plan period).
- Unallocated Group holding company expenses have been included to the extent that they are allocated to the covered business. The future expenses attributable to the long-term business in Emerging Markets at 30 June 2014 are R82 million (R56 million at 30 June 2013; R136 million at 31 December 2013). The allocation of these expenses is based on the proportion that the management expenses incurred by the covered businesses bears to the total management expenses incurred by the Group.