CAPITAL REPORTING – YE 2014

ECONOMIC CAPITAL METHODOLOGY AND ASSUMPTIONS

Old Mutual uses its own economic capital model to determine its economic cover ratio which reflects the excess of available financial resources (AFR) over the economic capital at risk (ECaR) requirement.

Economic available financial resources

The Group's AFR is the value of assets held by the Group in excess of its economic liabilities.

More specifically, for insurance entities the AFR is determined as the market value balance sheet based on Solvency II principles but adjusted for an internal view and current interpretation of key methodologies around, for example, fungibility and transferability and tax. The main components of AFR for these entities include the market value of assets, less insurance technical provisions (represented as the sum of best estimate liabilities plus a risk margin) and other liabilities.

The best estimate liabilities correspond to the probability weighted average of future cash-flows taking account of the time value of money. Allowance is made for the potential impact of variability of investment returns (i.e. asymmetric impact) on future shareholder cash flows of policyholder financial options and guarantees. Management and policyholders' actions, where expected, are captured within the liabilities. The technical provisions also include a risk margin in order to ensure that the value of technical provisions is equivalent to the amount that a third party would be expected to require in order to take over and meet the insurance and reinsurance obligations, assuming a 6 per cent per annum cost of capital, in line with current Solvency II rules.

For non-insurance entities, the AFR is determined as IFRS equity with adjustments to eliminate intangible items as appropriate.

Economic capital at risk requirement

The ECaR requirement has been calculated through a detailed process of identifying, quantifying and aggregating the impact of risks across the Group's principal business units. These calculations incorporate exposures to Old Mutual's life insurance, short-term insurance, banking and asset management businesses across diverse regions.

Old Mutual defines its economic capital at risk requirement as the reduction in post-tax economic available financial resources over a one-year forward-looking time horizon that should only be exceeded once in 200 years (99.5% confidence level that the event will not occur).

The Nedbank results within the Group calculations are consistent with the bank's Internal Capital Adequacy Assessment Process (ICAAP) framework where the requirements are derived based on Nedbank's proprietary economic capital methodology and are consolidated in the Group position on a 99.93% basis reflecting Nedbank's more prudent approach in line with its targeted 'A' rating.

Diversification is allowed for between different risks within entities within business units and across business units.

Governance

The methodology, assumptions and results are set with reference to internal capital model governance policies and are subject to review by the Business Unit Risk Committees and the Old Mutual plc Group Executive Risk Committee. The risk frameworks, governance and development of the Group's capital model are overseen centrally but implemented by our businesses locally so that local requirements can be addressed appropriately. The governance at business unit level is reinforced through senior Group executive representation on business unit regulatory boards and is supported with formal dual reporting for all key control functions.

Key assumptions

The key assumptions underlying the economic capital calibration include:

- risk distribution assumptions used to set the level of stresses in determining the 1-in-200 level for the ECaR requirement. These are set with reference to historical market data where available, internal demographic and operating data and the application of expert judgment as appropriate; and
- dependency assumptions to capture the interaction between risks, where these are set with reference to historical market data where available and the application of expert judgment as appropriate.

The Economic Capital position is not an assessment of distributable capital or cash as it includes, for example, the value of future insurance profits which may emerge over time. The calculations assume that there are no restrictions on the transfer of surplus between Group companies.

Old Mutual recognises that the risks quantified within an EC framework cannot capture all possible risks that may impact a Group over the following twelve month period; in particular the risk of capital loss owing to decisions yet to be taken, for example strategic risks, cannot realistically be modelled. The risk of modelling error is also accepted in interpreting the results although this risk reduces as the models become more widely understood, used and embedded. We will continue to consider and implement improvements to the accuracy, consistency and coverage of our analysis, which may impact future results.