Annual Results Presentation Transcript

16 March 2020

ANNUAL RESULTS

Iain Williamson

Good morning ladies and gentlemen and thank you for taking the time to be with us today especially given the growing concerns about the coronavirus. Welcome to Old Mutual's 2019 Annual Results Presentation. Our first full year set of annual results since listing in 2018. As we've just reminded you, Old Mutual is celebrating 175 years of existence. If ever a South African company can be said to have stood the test of time, that company has to be Old Mutual and 2019 was certainly the most testing of times. My name is Iain Williamson and I'm the interim group CEO. Joining my today are our group CFO, Casper Troskie, and members of our executive committee, some of which are attending from Cape Town due to the coronavirus.

Please allow me to welcome new members to our exco, Kerrin Land, who's taken over Personal Finance, Prabashini Moodley, our new MD of Corporate, and Maserame Mouyeme, our Corporate Affairs Director. Clement Chinaka is now wearing his new hat as MD of Africa. In a moment I will give you a brief overview of our results for the year before handing over to our group CFO, Casper Troskie who will go into more detail on our financial performance. After Casper has filled you in on some of the underlying numbers, I will share a few thoughts on our prospects for 2020.

While you digest some of the detail in this slide, let me say a few things about our 2019 results. These results largely reflect an extraordinarily difficult macro environment, an environment which has impacted not only Old Mutual but all of our competitors. Under extremely challenging conditions our results speak to the resilience and strength of a well-diversified business, one that really understands and looks after its customers, the way we've been doing business for the better part of two centuries. Adjusted headline earnings were up 5%. It was largely due to relatively strong investment returns in South Africa. As you can see, our results from operation was down 2% impacted by higher catastrophe claims from Old Mutual Insure and a net positive impact of assumption changes at group level.

Progress we've made on improving our operating effectiveness in a tough environment for revenue growth was a key highlight of 2019. So I'm delighted to report that we were able to exceed our cost savings target of R1 billion delivering R1.2 billion of recurring savings from our comparable 2017 cost base. Also pleasing this year was the progress we continued to make on optimising our balance sheet to a number of corporate actions including share buybacks and ongoing management of our debt position. The board has declared a final dividend of 75 cents per share. This brings our total cash returns to shareholders to R2.20 per share for the year when you include share buybacks.

The South African economy performed poorly in 2019, we ended the year in a technical recession. The employment picture was just as bad and our customers' ability to save and invest came under unprecedented pressure. When times are tough people, particularly those in the Mass and Foundation segment, save less and are more cost conscious. This is a reality we can't fight but one which we can and did manage. By December, equity market levels were up almost 6% on those in 2018 but for most of the year, market levels were lower than they were for the previous year. In fact, it was only towards the end of Q3 that we saw an upswing relative to 2018 and these gains have already been reversed the first two months of 2020.

In our interim results we noted that we had decided to manage Zimbabwe on a ring-fenced basis given that country's hyper-inflationary economy and our inability to access capital [unclear]. As such, Zimbabwe has been excluded from our headline earnings from the 1st of January 2019. With inflation reaching over 500% by year end, Zimbabwe's economy continued to be battered in 2019. As were our customers in that country who have endured the very real challenge of making ends meet in hyper-inflationary environment. The economic conditions of the other Southern African countries in which we operate with were mixed with Namibia continuing to experience recessionary conditions. Nigerian inflation easily outpaced pedestrian GDP growth and equity market there dropped by 15%. More positively, Kenya which is a key building block in our rest of Africa strategy with GDP growth of nearly 6% and at almost 8% growth, Ghana has the best GDP growth of all the countries in which we operate.

In 2019 the board and the executive team spent a great deal of time refreshing our strategy. Together we agreed our high level strategy and set a good foundation for the future. We remained focused on our eight strategic battlegrounds which are how we measure current success. In developing our five pillar strategy, we agreed that our overarching objective is to ensure that Old Mutual becomes customers'first choice to sustain and grow their prosperity. And we agreed that to deliver on that outcome we would need to deliver on five pillars. We started to execute against these pillars as indicated on this slide. For example under always present first, across the group we're rolling out and improving digital, easy to use, value adding tools like an enhanced My Old Mutual Insure platform and our new MyOldMutual website, tools which save both us and our customers' time and money.

And under Rewarding digital engagement, our Old Mutual Rewards programme was a brilliant success story for mass [?] Mass and foundation and Personal finance while, for the first time, we interacted with more than 3 million customers in South Africa this year and grew the number of active money accounts to 300 000 and counting. On Engaged employees, we significantly advanced our Pulse Culture intervention and rolled out our new cloud based employee self-management tool Workday in six countries. Under Solutions that lead, we've made significant enhancements to our Wealth proposition, rolling out Old Mutual Protect nationally and have a new savings and income proposition coming. These solutions will significantly enhance our intermediate experience and competitiveness in a very tough market. In demonstrating what we mean by Old Mutual Cares, this year we disbursed R80 million from the R500 million Enterprise Supplier Development Fund in support of emerging businesses. We agreed to this as part of our managed separation. I would just like to add at this point, that this last Friday that we were formally advised that an independent verification has confirmed that we have achieved Level 1 BBBEE accreditation for the first time.

Now if you're not an Old Mutual rewards customer I'd like to give you an idea of what you're missing out on. [Plays video].

[Over half a million South Africans have joined since the program launched in 2018. Our objective, to reward customers for taking steps towards achieving their goals and dreams. A great outcome has been that Old Mutual rewards members are saving more. Our members in total have completed 1.6 million actions towards financial wellness adding to their financial wisdom and helping them stay committed to their financial plans. The more our members learned about managing money better and the more they engaged with the program, the more points they earned. With every 10 points equalling R1 and with over 500 million points being earned since launch, plus exciting new ways to earn in 2020. Swipe, save, earn with money account. Old Mutual Insure coming soon. Our members earned and spent points with a wide range of partners that offer something for everyone. And it just keeps getting better. [Music playing]. 2019 was amazing. Here's to an epic 2020.]

Iain Williamson
Here we have a quick overview of the results from operations of each of our segments with their relative contributions on the right. Segmental RFO was impacted by various assumption changes and modelling improvements in the year. The non-economic assumption changes you see were the result of experience reviews we conducted across our Life business in 2019 and largely related to persistency and mortality across Personal Finance and Mass and Foundation Cluster. We are satisfied that the actual basis has been appropriately adjusted but will continue to monitor this relative to our actual experience. At the same time, improvements to our economic modelling resulted in a reduction in our investment guarantee reserves. At a group level, non-economic changes had a negative net impact of R81 million and improvements our economic generator modelling to align with our hedging methodology, a R1 billion impact. As you can see, impacts on the segments were varied so please bear this mind when considering the year on year performance of the various segments.

Mass and Foundation Life APE sales fell by 4% as we took steps to improve the quality of our foundation market group funeral business. I might mention, however, that sales momentum picked up in the second half. Lower sales volumes and the launch of our new value for money savings product reduced the Value of New Business by 10%. Positively, in a tough environment our risk margins improved but not enough to offset the impacts I've just described. Financial constraints also impacted our Banking and Lending business which experienced worsening credit losses to 8.9%. The H2, to address the deterioration in our credit quality, we deliberately slowed growth and applied appropriate price increases for specific categories of higher risk customers. Not only was Mass and Foundation an increasingly important profit contributor, it succeeded in defending its market penetration. This is partially due to adding 57 ATMs at 20 new branches bringing our physical footprint to 368 branches. Overall, a commendable result for this segment but the outlook remains challenging.

Corporate returned a pleasing result this year with Life APE sales rising by 16% to over R3.6 billion, largely driven by strong, recurring premium umbrella sales. Gross flows reduced by 7% to under R40 billion, mainly due to lower pre-retirement single premium flows. The sharply poorer net client cash flow was all about the state of the economy with, regrettably, retrenchments and termination increasing. Results from operations rose by 7% helped by 14% improvement in the value of new business and VNB benefitted from a substantially improved H2 sales performance. It's worth mentioning that Old Mutual corporate consultants had a good year securing 10 new consulting appointments. Our market leading umbrella offering SuperFund delivered an outstanding performance in 2019. We succeeded in converting standalone funds to umbrella funds as well as winning transfers from competitor umbrella offering. That performance would have been even better were it not for delays we continued to experience in getting our healthy pipeline of single premium deals through the section 14 regulatory approval process.

Moving to Personal Finance. Here you will note the decline of 14% in the result from operations which was mostly down to mortality basis changes. In the second half of the year we observed a further deterioration in our mortality experience against the first half of the year. To reflect this experience, we made a mortality assumption change which strengthened the basis but negatively impacted RFO. Excluding the assumption changes, RFO would have been up by 19%. As you would appreciate Personal Finance's performance and particularly the performance of its distribution channels should not be viewed in isolation. In 2019, these channels generated R35.9 billion in gross flows for Wealth and Investment, R5.2 billion for Corporate. Our new MD for this segment, Kerrin, has already put in place measures to improve productivity and the effectiveness of our distribution channels. To this end, last week we announced that the Wealth business will in future report operationally to Kerrin.

Wealth and Investments result from operations declined by 10% in 2019, a result which was driven by flat revenue as a result of lower average equity market levels. We also incurred additional one off costs by rationalising our boutiques to improve the competitiveness of our offering. As with much of the group's business adverse economic factors weighed on gross flows which fell by 9% in 2019. Compared to 2018, Net Client Cash Flow at R3.5 billion remains positive, although that result should be seen in the context of buoyant previous year when Old Mutual International accounted for some very large flows. For 2019 we acknowledge that our macro stance favouring South African assets negatively impacted our short term investments. Overall, annuity revenue was 1% up as credit spreads contracted. While specialised finance saw a 17% decline in its RFO and a drop off in non-annuity income, encouragingly it booked some R8.6 billion in new credit assets. A market which saw fewer deals than in 2018.

At the outset I mentioned the effect which Old Mutual Insure's catastrophe claims had on our bottom line. Several of the most important indicators pointed to real success in our battleground of turning this segment around. One of these indicators was the top line gross written premium, up by a commendable 11% and another the gross underwriting result which up 281% year on year. Our net underwriting result, at 0.4% however, was impacted by our worst catastrophe claims experience since 2015. Several of those claims crop related. Better guaranteed underwriting results also disappointed. Encouraging was Speciality which includes its underwriting margins from -12.9% in 2018 to a positive 6.5%. Our underwriting target remains unchanged at 4% to 6% and the medium term outlook was positive.

We are understandably pleased with our Rest of Africa segment's performance which saw it grow results from operations by 15% with both Southern and East Africa's Banking and Lending businesses making solid contributions. This despite some very challenging economic conditions on the ground. Southern Africa we recorded strong profit growth, banking and lending particularly in Namibia where we successfully penetrated state-owned payroll-linked disbursements. As you would appreciate, these are relatively low risk. East Africa, lending growth was driven by retail disbursements, similarly lower risk. Overall East Africa disappointed in 2019 and while I'm satisfied that the fundamentals there will improve, a R40 million loss was regrettable. This arose mostly from a poor claims experience in our medical insurance business as well as from lower new business volumes. In West Africa, we have renewed confidence as the newly strengthened leadership team has right-sized the cost base and laid a foundation for the future. This year the new MD of Rest of Africa, Clement has begun a thorough strategic review process. This review will clearly articulate how this segment can maximise its standing and strengths in its various markets to the year 2030. It will also address meaningful opportunities cost rationalisation. I'm now going to hand over to Casper to take you through more financial stuff.

Casper Troskie
Thank you Iain and good morning everyone.

Our financial delivery in 2019 was impacted by a number of headwinds and uncertainty. The most notable being the lack of GDP growth in South Africa, the reduction in the value of our Zimbabwe business and ongoing uncertainty regarding our regulatory capital position. Despite this we have made good progress on financial delivery with adjusted headline earnings per share up 7%. Our RoNAV exceeding the cost of equity at 15.2%. An ongoing strong cash generation supporting dividend flow with growth in embedded value of 12.7%. Our group solvency ratio remains well within target at 161% after taking into account foreseeable dividends. We have adjusted our dividend cover range of 1.75 times to 2.25 times to a range of 1.5 times to 2 times to reflect exclusion of Zimbabwe's earnings from our adjusted headline earnings.

Iain has taken you through our operating segment results which were down 3%. Net expenses from central functions reduced relative to the prior year following the increase in expenses being more than offset by interest earned on short term working capital balances. Shareholder operational costs rose by R260 million as this was the first full year of being standalone listed entity as well a result of one off costs related to staff restructuring. This was more than offset by interest received on higher cash balances. These balances compromised the proceeds of our Latin America disposal and remittances from Residual Plc which were used to fund share buybacks and dividends. Shareholder investment returns reflect mark-to-market gains in Q4 offset by the reduction in fair value of property assets in East Africa on the back of lower property yields and occupancy levels. The increase in finance cost is mostly from the inclusion of these costs in East Africa. The decline in associate income is as a result of the reduction in Nedbank's results of 7% whereas our China joint venture recorded an increase in earnings.

We have exceeded our cost target by delivering cost savings of R1.2 billion. The biggest driver of cost savings was operating model improvements in East Africa, West Africa, Zimbabwe and in the central functions in South Africa. This was supported by focussing on efficiencies in IT processes, reduction in consulting spend and improved space utilisation. Cost efficiency leadership was a key part of our financial objectives for the last two years and excluded increased incremental listing and other once off costs related to managed separation, also excluded commission related expenses. A key focus going forward will be on acquisition cost effectiveness as well as focussing on driving efficiencies through group structure optimisation, the simplification of our operating model, IT infrastructure and processes over the medium term.

On this slide we provide you with sources of income by lines of business. This is to assist investors in valuing our business and is not how we run the business. You'll notice that results from Life and Savings, Asset Management and Banking and Lending were largely in line the previous year. This disguises fairly large offsetting changes in the components making up these lines of business. In Life and Savings, increased new business strain and lower operating experience were offset by an increase in economic experience. The higher new business strain, lower operating experience was impacted by pressure on volumes, lower persistency and lower positive expense variances.

Iain has taken you through the impact of basis reviews that we concluded during the year. It had substantial impacts on our Life and Savings segment. Asset management earnings were up with the increase in profits from the Rest of Africa, more than offsetting lower earnings in South Africa. Banking and Lending profits were flat with higher profits in East Africa offsetting the lower profits from Old Mutual Finance and Specialised Finance. The biggest impact year on year has been the reduction in Property and Casualty profits following the increase in catastrophe losses in South Africa and increased claims in the medical insurance business in East Africa. Part of this slide gives you a brief reminder of the impact of the unbundling of Quilter and Nedbank on prior year profits which results in a comparable base of R7 billion. There has been substantial improvement in the OML perimeter profits from the base of R7 billion, with the improvement in Residual plc more than offsets the reduction in Zimbabwe profits. The Residual PLC improvement resulted from the effective implementation of managed separation and the reduction in risk provisions held.

Devaluation of the Zimbabwean currency reduced profits by R1.7 billion. Lastly, this year we incurred R1.8 billion in the reduction in the carrying values of Nedbank following a lower outlook on dividends and the reduction in value of Rest of Africa properties. We have set out on this slide the group's solvency position for OMLACSA and OML. The OML group has not been formally designated as an insurance group in terms of the insurance act and the solvency position remains a pro-forma view using the same basis approved by the regulator for managed separation. The OMLACSA solvency ratio has been impacted by the reduction in own funds due to increased policyholder participations which results in a technical mismatch in policyholder assets and liabilities with the assets included at tangible net asset value as opposed to share value.

Prescribed equity shocks during the increasing market levels from the prior year increased capital requirements. This was partially offset by the additional issue of R2 billion in subordinated debt. At the OML level, our ratio also reduced because of the OMLACSA reduction. There was a bigger negative impact on own funds for Nedbank due to the change of treatment of shares held on behalf of policyholders and a reduction in the capital ratio on a Basel III basis. A higher equity shock for own regulated entities also increased the capital requirement. Our capital position remains sound with certainty around the group position which allows for more deliberate capital decisions. Our capital position at the group level remains well within our target range at 161%. We are expecting a substantial uplift in our group capital ratio on a relative basis once we are designated as an insurance group.

We’ve set out on this slide the key movements in our covered business embedded value. New business value of R1.9 billion contributed 2.9% towards embedded value growth. Experience variances were slightly negative with negative persistency and in tax variances exceeding part of those risk and expense variances. Our trading model and model changes highlighted by Iain and results from operations basis was substantially more positive on an embedded value basis at R1 billion. Economic variances were R844 million which included the positive economic assumption noted by Iain. Operating variances related mainly to restructuring costs in Old Mutual International which are included in embedded value but fall outside of adjusted headline earnings as defined. The overall growth in embedded value of 12.7% was competitive and up from the prior year.

Here, we show you our estimate of the equity value of the business. We have set out for each key component the basis we have used for arriving at the value. The group equity value excludes the multiple for the value of new business which should be added to get to a fair or appraisal value. Group equity value declined by R6.1 billion from the prior year but cash remains largely flat on a per share basis. Key drivers of the reduction in group equity value include share buybacks of R4.9 billion and dividends paid R5.4 billion. A reduction in the value at which Nedbank is included of R3 billion following a lower dividend growth outlook. The devaluation of our Zimbabwe business of R1.5 billion. This was offset by an increase of R8.7 billion, the value of our operating businesses and other, which include the holding company net asset value.

I will now hand back to Iain to conclude on our outlook.

Iain Williamson
Thank you, Casper. Now, to the future.

In October our best projections for South African GDP growth in 2020 were that it would come in at a touch above 1%. By January we had revised this outlook down. Now, here we are in March 2020 facing a pandemic which has spread fear across the world, the spectre of global recession is growing stronger by the day. One of our founding values at Old Mutual is to be a certain friend in uncertain times. For our staff who are the lifeblood of the organisation, we have implemented measures across all of our operations to minimise their exposure to this virus. We believe that taking proactive actions ed by the executive team will further protect our customers, their families and the communities we are honoured to serve. However, even with the best measures downside risks remain.

What we do know, however, is that in 2019 Old Mutual once again proved its resilience. Our performance under trying circumstances demonstrated the strength of our balance sheet and our diversified operations’ ability to weather these storms. We also know that our stress testing has demonstrated that we have sufficient capital and liquidity to withstand a perfect storm scenario. Our balance sheet remains strong and our cash generation ability remains strong. We follow a prudent capital management philosophy and our invested shareholder portfolio is biased towards cash and hedged equities. We remain humble about our history and look forward with excitement at the next 175 years.

Over the medium term we expect that meeting several of our most important targets will be challenging. Taking out further costs in a time of lower revenue growth will continue. We will remain very closely focused on our operational results, digital enablement and exploiting opportunities for growth. The investments we've made in enhancing our customer and intermediary experience will no doubt be essential to remaining competitive and winning in our markets. We also anticipate that our healthy solvency ratios will continue to support returns to shareholders.

Thank you very much for attention. We will now be only too happy to take any questions that you may have. Our executive team are either here in the room or on the audio link to do that.

Male speaker
Do we have any questions on the conference call? In the interim while we wait for questions to come through on the conference we do have one question that's come through. It is from Londiwe Buthelezi at Fin24 and she asks, can you give us some colour on your Banking and Lending business? How many customers hold OM money accounts now and seeing that you are aggressively marketing the accounts and OM rewards and the rollout of more ATMs. Do you plan on getting your own banking licence any time soon?

Iain Williamson
Clarence do you want to take that one?

Clarence Nethengwe
Thanks for the question. We have 400,000 money account customers, with over 270 thousand of them as primary account holders. In terms of the question around whether we will be getting our own banking licence, that is something that will be determined and e communicated later in the year whether we are going that route but so far we have got a relationship with Bidvest and that relationship has been very sound and there's no need for us to make any changes.

Male speaker
Do we have any questions on the conference call?

Operator
We have question from Francois du Toit from Renaissance Capital. Please go ahead.

Francois du Toit
Firstly, I want to know about the impact of the release of investment guarantee reserves, it added a R1 billion to just operating profits. In the light of market conditions now do you think that was a prudent thing to do? Obviously also, I think you mentioned also in the EV footnote that part of the release reflected lower volatility assumptions marked forward with the assumptions. Maybe if you can give us a sense of what would happen to those reserves at these levels of volatility? That's the one question. The second question relates to Nedbank. Nedbank share price down 40% year to date. What impact would that have on your SCR ratio given that Nedbank is cap accounted at market value towards capital.

I assume that given… that there will be some relief in the system and given that the equity shock is also aggressive and a significant impact on your SCR ratio but related to that as well, is it not maybe advisable to either hedge that exposure or to have more diversified, in other words, not so much exposure to your Nedbank share price, reliance on Nedbank for capitalisation in the life business. The second question.

Then, the third question. In Personal Finance your mortality experience and lapse experience have been consequently changed which had a big negative impact, but it was offset by the allowance for potential positive impact of future premium increases. I just want to get a sense of what is that guarantee period and you've launched Greenlight back in 2004, so it's 15 years old. Have you got a lot of experience now in terms of policies that's gone through that guarantee period? Have you been able to increase premiums and what has been the impact of those premium increases on lapse experience for example. I just want to get a sense of whether premium increases really help and whether you're comfortable with that. That you're able to get some of the money back through premium increases on own risk policies.

I think just also last question related to the coronavirus. If you can maybe give us a sense or point us in the direction where we can see what is your longevity risk and whether that is higher than your mortality risk. Maybe just give us a sense in terms of what would be the impact if people at, say let's say ages over 65, there's a very meaningful increase in mortality. Would you have, probably a fairly offsetting release from the annuity book which would impact a higher mortality on risk only policies? Given that the experience or the mortality experience is most severe at older ages is it fair to say that your annuity book would give you a meaningful offset to the mortality risk there?

Iain Williamson
Okay, so there are four questions there. I'll start with a very high level overview on the IGRs. The main change we've made is to bring the economic scenario generator model outcome closer to the way that we actually hedge the book. So it was really just an improvement in the accuracy of the ESG scenarios to what we are doing in reality. So we don't feel that was a relaxation in prudence as it were. And I'll perhaps ask Nico to comment on what we've done since then to test the situation.

Nico van Der Colff
Hi, it's Nico here. I think it's useful to also realise that our IGRs currently consist of two components. One, we do a best estimate calculation and then we hold a discretionary margin over and above that. And we've been managing that discretionary margin very carefully over many years to accumulate a material discretionary margin on IGRs. A material change in this process was that we realised that our discretionary margins were starting to get excessive and didn't need to be quite so large to provide the level of protection we were looking for from the discretionary margin. So there's a best estimate component that you can see when you look at EV but the profit release mostly came from leading smaller discretionary margin in addition to the best estimate APN1-10 liability we were holding. We're comfortable that it's been holding up reasonably well through this very noisy period at the start of 2020 with the hedging behaving reasonably compared to what this model suggests and therefore we're not uncomfortable with what was done at the end of last year.

Iain Williamson
Casper wants to add, can we get a mic here for Casper.

Casper Troskie
Francois, on the Nedbank Holding your capital requirement is the function of the value. So as the value reduces, the capital requirement reduces. So there's no volatility on your ratio, it's just a diversification impact. So the volatility of the ratio is very stable whether you have big or low [market shocks.

Iain Williamson
And then on the PF side, Kerrin, can we check if you got the question and are able to respond?

Kerrin Land
I did Iain. Can you hear me?

Iain Williamson
Thanks, we can hear you well, yip.

Kerrin Land
So in response to that question, we have different periods where we can review the premium. Spread across 5 year, 10 year and 15 year terms and we actually started this review in H2 last year. So we sent our first sets of letters out in July and August. The first set of increases took place in October. It is a nuanced review so it's not equal across all different cohorts but together it's a very material lever for our future profitability and so far we haven't seen lapses increasing materially.

Iain Williamson
Are there any further questions on the line?

Male Speaker
We do have one more question.

Operator
The next question is from Warwick Bam from Avior, please go ahead.

Iain Williamson
Warwick, would you like to ask your question?

Operator
Unfortunately, we are not getting a response from Warwick so there are no further questions.

Iain Williamson
Okay well then ladies and gentlemen thank you very much for your attendance. We look forward to engaging with you one on one in the coming days. Thanks very much for coming and I hope you found the presentation useful.

END OF TRANSCRIPT