

Investor Call Transcript

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Q1 2023 OPERATIONAL UPDATE

Old Mutual Limited	External Participants
Iain Williamson , Group CEO	Andrew Baker , Citi Group
Casper Troskie , Group CFO	Andrew Sinclair , Bank of America
Bonga Mriga , Interim Head of Investor Relations	Michael Christelis , UBS
Ranen Thakurdin , GM: Group Reporting and Insights	Larissa van Deventer , Barclays
Sanesh Albert , Head of Capital	Baron Nkomo , JP Morgan
	Chris Logan , Opportune

Operator

Good day, ladies and gentlemen, and welcome to the Old Mutual Q1 2023 operational Update. All attendees will be in listen-only mode. There will be an opportunity to ask questions when prompted. If you should need assistance during the call, please signal an operator by pressing * and then 0. Please note that this event is being recorded. I'd now like to hand the conference over to your host, Bonga Mriga. Please go ahead, sir.

Bonga Mriga

Thank you. Thank you, Judith. Good day, ladies and gentlemen, and thank you for joining us on the call following the release of our voluntary operational update earlier today. I am Bonga Mriga, as it has been announced. I'm the Interim Head of Investor Relations. On the call, we are joined by our CEO, Iain Williamson, together with our CFO, Casper Troskie. We also have Ranen Thakurdin, who is our General Manager in Group Reporting and Insights, together with Sanesh Albert, who is our Head of Capital. Iain will take us through the call, and we will open for Q&A after Iain has concluded on what he has to tell us today. The operator will then guide you on how to queue up your questions. And with that, I'll hand over to you, Iain. Thank you.

Iain Williamson

All right. Thanks, Bonga, and good evening, everybody, and thanks for taking the time to join the call this evening. Our business has shown great resilience overall in the first quarter of the year, and demonstrated, I think, the continued momentum that we saw last year, despite economic pressures experienced across all of our markets, and in particular in South Africa. Just looking at some of the key performance indicators, life APE sales were down 1%, mainly on the back of lower sales in China following the withdrawal of a particular product in the Chinese business. But life APE sales when you exclude China were up 7% with the momentum particularly in our retail businesses being maintained.

Mass and Foundation Cluster life APE sales grew 15% on the prior year driven by credit life sales. In Personal Finance and Wealth Management, life APE sales were up 11%, mainly on the back of improved productivity in the channels and with a good contribution from guaranteed annuity sales, which should be encouraging for VNB and margins. This was strong growth both in the single and recurring premium arena. In our Africa Regions, life APE sales are up 10% driven by new business secured by renewals and by improved productivity in the East Africa region.

Persistency does remain under pressure, despite the strengthening of our persistency basis at the end of last year, and particularly in the Mass and Foundation Cluster business, as you would expect in this economic climate. We remain focused on deploying an identified set of management interventions, which we believe will continue to improve our retention outcomes.

Turning to gross written premiums (GWP) on the short-term insurance side, GWP was up 19% with a strong showing across both the Africa Regions businesses and in Old Mutual Insure. With Africa regions up 32% and Old Mutual Insure up 15%. Growth in the Africa Regions was driven by the health and general insurance business in East Africa and by corporate new business in Southern Africa. Genric, which has been included in Old Mutual Insure's numbers for the first time in this quarter, contributed to the growth in GWP there, with the other channels also showing positive momentum.

Gross flows were up 22% on the prior year and in Old Mutual Investments, gross flows are up 90% boosted by money market flows, fixed income and corporate cash inflows into Futuregrowth. But we have seen some drawdowns from an investment perspective from our alternatives, ideas and A4 fund, so that's the fourth infrastructure fund. We've seen strong growth in gross flows resulting in stronger performance in net client cash flow as well.

Loans and advances are flat on the year end position at December 2022, but if you look back to the equivalent end of March last year, we're up 3% on the prior year. The business in the Mass & Foundation cluster is up 6% in line with the constrained economic environment. And the Africa Region's loan book is down 8% due to lower disbursements given the tough economic climate, and in particular in Kenya.

I'm going to move now from the operational to some more strategic matters. We will be hosting an investor update on 28 July 2023 in Cape Town, and we will include a hybrid option for that meeting. We will update you in detail on our strategy for the medium to long term. In that session, we will also include detailed content on both the progress on the bank build, as well as the impacts from IFRS 17. And we will include a teaching session on IFRS 17 over and above what we have already taken you through at our annual results in March this year.

From a capital perspective, we have now received approval from the regulator for our share buyback, which we announced in March, and we are happy to confirm that we will be aiming to conclude a buyback of R1.5 billion. The share buyback, the Genric acquisition and the Old Mutual Finance Namibia acquisitions have resulted in discretionary capital decreasing to R1.4 billion from R3.5 billion at the end of December. We continue to monitor group solvency and our group solvency ratio remains stable and within our target range of 170% to 200%.

As you all know, one of the main contributors to the tough operating environment at the moment is that the energy crisis in South Africa has worsened over time, and that's been coupled with strong depreciation of the Rand against major currencies and particularly against the US Dollar. These present grave concerns around consumers' ability to handle additional financial pressure in an already financially stressful environment. We continue to call on the South African government to demonstrate leadership and take decisive action to address the concerns faced by the business community and by the citizenry of the country.

We will strive to continue to balance the interests of all our stakeholders, including customers and shareholders. The time has come for our government to implement concrete, actionable steps to reverse the recent negative events. And to achieve this, we believe the government needs to engage in a much more open dialogue with the business community, fostering a relationship of trust and collaboration. The willingness from the business community to assist is certainly there, but the ability to attain any traction in initiatives has proved to be incredibly difficult. So, with that I will stop talking and ask the operator to help us manage the Q&A process. Thank you very much.

Operator

Thank you, sir. Ladies and gentlemen, we will now be conducting the question-and-answer session. If you would like to ask a question, please press * and then 1 on your telephone keypad or the keypad on your screen. A confirmation tone will indicate that your line is in the question queue. You may press * 2 to exit the question queue. In the interest of time, we ask that you please limit yourselves to maximum of three questions. Thereafter, you are welcome to re-join the queue for any additional questions. Just a reminder, if you would like to ask a question, you are welcome to press star* and then 1. This first question comes from Andrew Baker of Citi.

Andrew Baker

Great. Thanks so much for taking my questions.

- The first is just on the persistency pressure that you're seeing. Should we read into what you're saying today that you are expecting further strengthening of your basis in the first half, or are you just flagging for experience variances purposes? And then, related to the same topic, are you beginning to see any early signs of the benefits from the management actions that you've been referencing or that you referenced in the full year results around persistency?
- And then secondly, just on China and the regulatory changes that you mentioned. Are you able just to give a little bit more detail on what they were, and then potentially maybe a percent of the 2022 China AP that was contributed to from the products that are now ceased? Thank you so much.

Iain Williamson

Okay, thanks, Andrew. On the persistency, we have seen some positive indicators from some of our management actions in the sense that our first premium collection success rates have improved, NTU rates have got a bit better etc. But the pressure on the longer dated in force book remains a concern and something that we will continue to monitor. I think it's too early to say whether this pattern is something that would result in an assumption change

being required. Obviously, three months of data is not very much. And historically, as you may know, our practice has been that we mainly revisit basis at the end of the year. Although it is possible, we could review a short-term provision at the half year, but I think it would require quite a significant variation from experience.

As far as the China piece goes, we actually withdrew a product from our own product set in advance of the regulator, then essentially clamping down on a similar kind of product range across the market. And that was for reasons of concerns around essentially the adequacy of pricing for risk in the way that that product was constructed. It was a single premium universal life type product. As you can see, it was a fairly material contribution to total sales last year. But I don't have the percentage off the top of my head to help you with, so we would need to come back to you with that number. Thanks.

Andrew Baker

That's great.

Casper Troskie

Casper, anything to add? No, Iain, I don't have anything to add. We've started to work on experience investigations between now and the year concluding on what we're going to be doing for the half year. So, it's too early to give you any guidance on that. Thanks.

Operator

The next question which comes from Andrew Sinclair of Bank of America.

Andrew Sinclair

Evening everyone. Thanks for the time today. Three for me please:

- First is on the buyback. Great to hear it's been signed off. I just really wondering if you can give us some colour on the timescale and format of the buyback, please.
- Second, just going back on persistency. I mean it's just over two months since you last updated the market and announced the persistency provisions that have been taken. And what's been said today leaves quite a bit of uncertainty until the next update in September. I just really wonder if you can give us a bit more context on potential impact and potential for more provisioning. I'm sure we'd all like to get ahead of this debate and feel we can do one and done.
- The third question is on China. On the products, given that you withdrew it even before the regulatory changes, can you give us any details on concerns on the back book of products that have been written there? Are there any risks on that? Any thoughts there. Thanks.

Iain Williamson

Sanesh, can you deal with the buyback process and issues, please?

Sanesh Albert

Yeah, sure. Thanks, Iain. So, it all happened at once in terms of getting prudential authority approval over the line and getting through our board steps. So, AGM is also coming up, so we will effectively get that vote count into the AGM and then we will execute basically imminently. I think the results are expected by tomorrow afternoon. So, you can effectively say we will start early next week. The timing obviously, just looking at the trading volumes, we do expect that we will conclude over towards the end of let's say Q3, Q4, but just depending on trading volumes. But we will definitely execute before the end of 2023.

Andrew Sinclair

And that would just be the full R1.5 billion.

Sanesh Albert

Yes. We did note a range of R1 billion to R1.5 billion. We have now confirmed it will be R1.5 billion that we will execute.

Andrew Sinclair

Excellent. Thank you very much.

Iain Williamson

Okay, Andy, on persistency here, I don't have much to add to the way that we answered the question earlier. Unfortunately, this is a bit early to call it. And I realise that everyone would like clarity. We would too. The truth of the matter is, I think that with the way that the economy has played out in South Africa – and we saw another 50bps interest rate hike today – I think we are seeing pressure on that lower income consumer group. And I think it is really just too early to answer how that's likely to pan out.

On the China product, essentially the crux of the issue was that the early termination values on the product had to earn returns from a yield perspective that were tight. Not ridiculous, but very tight. And so, I don't expect material exposure. But equally, the product was not going to pass profitability return on capital criteria from our perspective. So, that was why we terminated it. But I don't anticipate that it should result in any sort of material big loss problems or anything like that.

Andrew Sinclair

Thank you very much.

Operator

Thank you. The next question comes from Michael Christelis of UBS.

Michael Christelis

Afternoon guys. Thanks for the time. Just maybe three from me as well.

- You called out the Genric impact on South African GWP. Can you just give us a sense of what the size of that is, how much of the 15% is Genric? In other words, what has the rest of the book done?
- The second one, maybe a bit of comment on the credit quality in Old Mutual Finance and how that's tracking in the current environment. We've seen some of the finance businesses locally take quite a bit of strain in the last couple of months.
- And then the third one is a question around maturities and withdrawals from affluent market savings products. Are you seeing a pickup there in terms of outflows from those products at all? And maybe any colour you can give us on trends there. Thank you.

Iain Williamson

Thanks, Mike. Cassie, do you have the Genric picture off the top of your head and the OMF credit bit?

Casper Troskie

Yeah, on the Genric I'll just look it up. I don't have it off the top of my head, but I'll try and find it quickly, Iain. And then on the credit piece, we have seen that tick up to top end of our range, so there has been pressure on credit. Just to remind you that our range is 6% to 8%, so we feel comfortable with where that's sitting and we're obviously watching that closely. I'll obviously be able to give you an update at the end. Obviously, our growth in that book has been a lot slower than the market growth, so you shouldn't see the same level of impairments writing elsewhere.

Iain Williamson

And then finally on the maturities and withdrawals piece, I don't think we've seen anything specific to write home about in terms of problematic issues. We keep quite a close eye on that top end on things like impact of emigration and things like that. But I don't think we've seen anything that I would call out as a material issue worthy of noting in terms of impact on outflows and things like that at this stage.

Michael Christelis

Right, thanks very much, guys. If you can get that Genric back, it'll be great.

Iain Williamson

Sure. Look, off the top of my head, Michael, and don't hold me to it, but off the top of my head, I think the core book is around circa 9% growth, and then the balance would effectively be a Genric impact. But let us confirm that number.

Michael Christelis

Thank you.

Operator

Thank you. The next question comes from Larissa van Deventer of Barclays.

Larissa van Deventer

Good afternoon. Two questions from my side though. To circle back on China, it's a two-part question, so I suppose that makes it three.

- First question is can you give us a little bit more colour on what exactly the regulatory change is that is pending and whether you expect any more? And would you give an indication of the degree of profitability of the China product and what impact that may have on VNB?
- And then second, it appears that the growth in South African sales has been tending towards risk sales. Is it fair to assume that the current trend suggest an improvement in the new business margin for the half year? Or how should we think about margins as the current economic scenario plays out?

Iain Williamson

Thanks, Larissa. Just to be clear on the Chinese regulatory piece, it's not a forthcoming change. The regulator essentially clamped down on a particular product construct that was prevalent in the market, which was essentially, in our language, a universal life endowment with early surrender value guarantees embedded into the product. That was essentially the structure of it. So, that's done. All players in the market have effectively withdrawn the product from the beginning of this year. It's not a forthcoming thing. So, as I've described, the impact that I've described really is the appropriate impact to think about. I think the main impact on us will be simply on sales because it was a popular product in the channels.

And there's a regulatory timeline, lead time to effectively constructing and getting approved the replacement product to fill the gap that leaves in your product range in terms of your ability to sell. So, China's very granular in its regulation around product. Every product you construct, which we would regard as just a change in features or even a launching the same product into a different channel, requires a separate regulatory approval. So, there's quite a lot of lead time involved in getting that right.

I think your statements around the mix and the probable impact on margin are likely to be correct. So yes, the growth in risk sales both in MFC and PF has been encouraging. And the mix, as I indicated in my voiceover earlier, the mix of guaranteed annuity sales in PF has picked back up again in this environment. And I would expect both of those features of the volume and the mix to be supportive of margin.

Larissa van Deventer

Thank you. And the contribution to the bottom line roughly of the Chinese product?

Iain Williamson

I don't know off the top of my head the answer to that question. I mean, our Chinese business broadly breaks even. I don't expect the picture of that to change as a consequence of the product change. It is primarily going to be a question of, is there pressure on the expense ratios as a consequence of the volume issue. That's going to be the main consequential item.

Larissa

Okay thank you very much.

Ranen Thakurdin

Just to confirm that the growth rate in Insure without Generic on GWP was 9.5%. Thanks.

Iain Williamson

That sounds pretty close. Okay. Thanks, Ranen.

Operator

Thank you. Ladies and gentlemen, just a reminder, if you'd like to ask a question, you're welcome to press * and then 1 to place yourself in the question queue. The next question comes from Baron Nkomo of JP Morgan.

Baron Nkomo

Hi guys. Just two quick questions from me.

- Just on the discretionary capital, can I just confirm if you intend to use the entire R1.4 billion that's remaining for the Two Mountains equity acquisition, or will that only be part of it?
- And then secondly, are you able to give any commentary or guidance around your actual operating profits or results from operations?

Iain Williamson

Thanks. Casper, can I hand those ones to you?

Casper Troskie

No, the Two Mountains transaction won't be more than a third of that discretionary capital. It's probably a little bit less than that. So, it's only a portion. And obviously the rest will be used for growth initiatives for the time being. And then we'll give you an update on discretionary capital at the half year. We don't normally comment on profitability at quarter ends. And in this quarter in particular we're just firming up on our IFRS 17 numbers. We'll give you more colour on the IFRS 17 comparisons, as we said, at the half year. And then we'll obviously give you an update on where we land as we normally do as part of the trading updates once we've had approval from our audit committee on the results. So, we're not giving any guidance on operating profit at this stage.

Iain Williamson

Thanks, Casper.

Operator

Thank you. Ladies and gentlemen, just a final reminder, if you'd like to ask a question, you're welcome to press * and then 1. The next question comes from Chris Logan of Opportune.

Chris Logan

Yes. Iain, thanks very much for the update. Obviously, the elephant in the room is how the SA economy pans out and how amenable government becomes in enacting necessary changes. Did I catch you right in that you said you were trying to engage with government on a host of things and it was proving very difficult?

Iain Williamson

Yes, look, it's not just us.

Chris Logan

No, sure.

Iain Williamson

There's an extensive amount of goodwill in the business sector towards trying to assist. And there's actually an initiative that's been going for some time where essentially organised business has identified some priorities to assist with. And they include energy, logistics, and crime and corruption, essentially, if I theme it. There is some traction on getting it moving. There have been meetings with the President and cabinet and what have you, and there has been a little bit of traction. But it is frustratingly slow and it is very difficult. Essentially you get a lot of willingness from particular ministers and from particular individual actors in the conversation, but once it gets into the collective, it seems to just get bogged down.

So, that's the best way I can describe it. I think there's a combination of ideological issues and different camps that just make it difficult to navigate through decisively. But I do think that if the political will can be solved, then actually things could move a lot faster than people realise. I think we know what the solutions are. We know what needs to be done. It requires a certain amount of political will to remove the barriers to those things getting moved ahead.

Chris Logan

No, sure. Thanks for that. It fits in with the... I'm sure you saw the Economist article of a couple of days ago, where CEOs have realised that running the country cannot be left to the ANC. That was its title. But, obviously trying to assess the SA assets at the moment is very difficult until this decline is arrested. So, very good luck.

Iain Williamson

Yeah, thanks.

Operator

Thank you. It appears we have no further questions in the question queue. I will now hand over back to Iain Williamson for closing remarks.

Iain Williamson

Okay, thanks very much. So, nothing really further to say from me, guys, other than I am actually really encouraged by the performance and the resilience of the business in the first quarter. As I said in my opening remarks, it is

tough out there. But we seem to have a knack of thriving in this kind of an environment. So, I look forward to updating you again at the investor day in July and then at our interim results. And until then, best of luck to everybody out there. Thanks for the time this evening.

Operator

Thank you, sir. Ladies and gentlemen, that concludes today's event. Thank you for joining us, and you may now disconnect your lines.

END OF TRANSCRIPT