OLDMUTUAL

Presentation transcript

10 May 2022

BULA TSELA BROAD-BASED BLACK ECONOMIC EMPOWERMENT TRANSACTION

PARTICIPANTS	
OLD MUTUAL LIMITED	**Q&A**
Iain Williamson, CEO **Casper Troskie,** CFO **Sizwe Ndlovu,** Head of Investor Relations **Taskeen Ismail,** Head of Corporate Finance **Ranen Thakurdin,** GM Group Reporting & Insights	**Michael Christelis,** UBS **Craig Gradidge,** Gradidge-Mahura Investments **Larissa van Deventer,** Barclays **Andrew Sinclair,** Bank of America **Cornette van Zyl,** ABSA Asset Management **Sarine Barnard,** Ninety One

Operator

Good day, ladies and gentlemen, and welcome to the Old Mutual Ltd investor call on the proposed Bula Tsela Broad-Based Black Economic Empowerment transaction. All participants will be in listen-only mode. There will be an opportunity to ask questions later during the call. If you should need assistance during the call, please signal an operator by pressing * then 0. Please note that this call is being recorded. I would now like to hand the call over to Sizwe Ndlovu. Please go ahead, sir.

Sizwe Ndlovu

I am Sizwe Ndlovu, Head of Investor Relations. Good afternoon to everybody. Welcome to all those who are joining the call. This afternoon we'll be hearing from our Chief Executive, Iain Williamson, and CFO, Casper Troskie, on both the rationale for the proposed transaction, as well as some indicative financial impacts following the SENS that we released on the 20th April 2022. Please note that the presentation has been emailed to all participants who had registered as at the close of business yesterday and will be available on the homepage of our investor relations website as well.

If you have not seen it, I would encourage you to access it. For those who have received it, please follow using that during this presentation. Once Iain and Casper have concluded, we will be happy to field any questions you have for the remainder of the call. Over to you, Iain.

Iain Williamson

Thanks, Sizwe, and good afternoon, everyone. We are also joined on this call by Taskeen Ismail, who is our new Head of Corporate Finance, as well as by Ranen Thakurdin, who is our General Manager of Group Reporting and Insights. For those of you who are following on the slides, I am going to start on slide three. We mentioned at the announcement of our year-end results on the 15th March that achieving the empowerment targets we had set for ourselves at listing in 2018, which was to be *best-in-class*, was something that we had taken and continue to take seriously and have been working on achieving.

As of 2018, *best-in-class* amounted to 30% Black ownership of our business. And we are pleased to be bringing an impactful transaction to the market that has a wide set of participants with employees, communities and the general public included. The proposed Bula Tsela B-BBEE transaction will allow us to reach just over 33% Black ownership, subject to all necessary approvals, assuming of course that our current B-BBEE ownership percentage of between 28% and 29% remains at that level. Bula Tsela is a Sesotho phrase that means ‘paving a way’ and we are indeed paving a way for the transformation of the financial futures of those who participate in the scheme. We are also the first insurer to facilitate a share offer to the black South African public and based on the share price at the end of March 2022, we expect the transaction to be valued at R2.8 billion.

I am moving on to the next slide, slide four, for those of you who are following. The proposed transaction gives life to the commitment that we made in 2018 and goes beyond that. We believe that it will give us an enhanced competitive advantage, particularly in the key Old Mutual Corporate and Old Mutual Investments businesses. And the development of South Africa is at the core of what we do. The more equal and inclusive our society becomes, the more opportunity there is for us to achieve sustained growth and unlock value for shareholders. The transaction aligns with both our responsible business and shared value approach, and it is deliberately truly broad-based. The benefits, we believe, far outweigh and will outlive the costs of the implementation.

On slide five, the rationale for the transaction is that we firmly believe it makes business sense to drive real empowerment. The more equal and inclusive our society becomes, as I said before, the more opportunity there is to achieve sustained growth and unlock value. The way that we’ve constructed the deal is deliberate to achieve genuinely broad-based transformation. There are three groups of participants: i) our employees, ii) the black South African public and iii) our communities. On employees, we want all of our employees to share in the success of the Old Mutual Group. This will in this case include non-black South Africans and the rest of our employees in the rest of Africa. However, we will materially tilt towards black South African employees in entry level positions in our company.

In the communities, we aim to support community development and specifically the development of Black people and Black-owned entities through financial and other educational and digital skills development programmes. We aim to help create jobs in the SME sector and develop the skills to fill those jobs. In including the black public, we are broadening our shareholder base and specifically including Black South Africans at lower income levels, which has not been done before. The deal will be good for Old Mutual and should improve our B-BBEE ownership credentials, enhancing our ability to compete successfully in our chosen market segments.

We did a substantial amount of work on analysing business at risk from our current lack of empowerment, and this deal together with the sale of 21% of Futuregrowth to AIH, as we announced earlier this year, will help move both Futuregrowth and the Old Mutual Investment Group (OMIG) towards becoming majority Black-owned businesses, which will help those businesses to remain preferred service providers for institutional investment mandates. It also helps the Old Mutual Corporate business to be more competitive in its offering to institutional counterparties.

On slide six, the salient terms of the deal, as you would have seen in our terms announcement, we are proposing to issue just over 205 million new Old Mutual shares to be allocated to the employee scheme, retail scheme and the community trust. Detailed funding plans for this will be outlined in the shareholder circular that will be released in due course. At a high level, we anticipate that individual group companies will contribute to fund their respective employee schemes with the remainder to be funded by Old Mutual Ltd through notional vendor funding. For the retail scheme, Black members of the public including Black-owned entities will be invited to apply for shares and will contribute some equity to do so, with the remainder to be funded through preference share funding from Old Mutual. For the community scheme, notional vendor funding will be provided by Old Mutual.

Other key points worth noting are that the allocation of value in this deal is largely tilted towards the Black population and towards Black women in particular. There is no strategic equity partner to ensure that the deal remains broad-based. Non-executive directors of Old Mutual will not be participating in the transaction. The scheme will be in place for ten years, with the community scheme to continue operating beyond the ten-year period. We will not be providing any specific business updates and we will communicate these in the normal course of our investor calendar and via SENS. I will now hand over to Casper for a brief overview of the indicative financial impacts of the transaction, and we will then take any questions at the end. Casper, over to you.

Casper Troskie

Thanks, Iain. I hope you can all hear me well. I am referring now to slide eight, if investors want to follow. In terms of the terms announcement, we showed the indicative pro-forma impacts of the transaction. And we referred to total costs of R917 million which is made up as follows:

- In terms of the scheme cost for the employee scheme, the accounting treatment is similar to our existing employee schemes, with the only difference between the vesting period, which for this transaction is four, six and eight years. And the IFRS 2 cost of approximately R377 million will be incurred over the duration of the scheme.

- In terms of the community scheme, the expenses represent the use of trickle dividends in the community trust to be paid out to various qualifying initiatives on a discretionary basis. And we assumed that we will be paying out the full trickle dividend for purposes of the financial impacts.

- In terms of the retail scheme, this represents the upfront IFRS 2 charge of R174 million calculated as the equity-settled cost of the scheme less the contribution from retail participants. This amounts to R305 million as the equity-settled cost less the contribution of R131 million, which gets you to the R174 million.

- The once-off implementation costs consist mainly of consulting and implementation fees and further detail will be provided in eth forthcoming circular. Should the retail scheme be listed in year five, we estimate an additional once-off listing cost of R10 million.

- The annual administration cost represents the ongoing costs that will be incurred to manage the administration of the schemes. The costs contained in the terms announcement are based on assumptions at 31 December 2021 and final costs incurred will be impacted by changes to both the market and the market assumptions.

We have used the Black-Scholes model to set specific assumptions for the deal over a ten-year period. We have made conservative assumptions of value in our model for share price volatility, dividend yield and risk-free rates amongst others. These assumptions give us additional confidence that value indeed can be created through the proposed transaction. We will provide further detail on these assumptions in the circular which will be distributed to our shareholders in the coming months. We are firming up with our auditors the exact dilution impacts, and in particular around the retail scheme, as well as the impact to net assets and will provide further detail in the circular once we have alignment with our auditors on these items.

I think the most critical points that we have been very clear on as a management team is that the benefits to Old Mutual Ltd of this deal far outweigh the cost of its implementation. And we have used fairly conservative assumptions in terms of what the deal would cost. And we then have quantified internally what we expect the benefits to be of the scheme. We have thought about this in three ways:

- We have looked at current funds at risk where we are managing funds where those are at risk because we are not above the 50% ownership in our asset managers. So that's the listed equity franchise, Futuregrowth as well as Old Mutual Corporate that are affected.

- We have looked at the ability to source additional funds from existing clients, and

- We have looked at the ability to increase our win rate in new proposals both for the asset management businesses as well as Old Mutual Corporate. And in that case, we've looked at our pipeline to try and quantify what the impact would be.

And taking that into account, the actual annual benefits are material that we've calculated and are expected to fairly quickly exceed the costs of the transaction.

So back to you, Iain.

Iain Williamson
Thanks Casper. Just in terms of process and next steps, we will issue a circular that will provide additional information regarding the transaction in due course. And we expect that will be in the next couple of months. Following the release of the circular, we will schedule a shareholders' meeting where we will be seeking approval of the proposed Bula Tsela B-BBEE transaction and its terms, and we will issue a prospectus for the retail scheme. And we anticipate that we would want to schedule all of that such that we can conclude this transaction, subject to regulatory approvals, by the end of the year.

I will hand back to Sizwe to take any questions that you may have on the line. Sizwe, over to you.

Sizwe Ndlovu
Thanks, Iain. I see we already have some people lining up. I will hand over to the operator from Choruscall. We have Michael, Craig and Larissa. Over to you.

Operator
Thank you. Ladies and gentlemen, if anyone would like to ask a question, you're welcome to press * and then 1 on your touchtone phone or on the keypad on your screen. If you, however, wish to withdraw the question, you may press * and then 2 to remove yourself from the question queue. Our first question is from Michael Christelis of UBS. Please go ahead.

Michael Christelis
Good afternoon, guys. Thanks very much for the time and thanks a lot for the detail around the costs of the scheme and how you expect this to come through. Two questions if I can, one related to those costs. Presumably, these costs will be shown in your central cost line. Is that right? Just for my modelling. And that 2022 cost presumably all gets incurred in H2 if you're hoping to do this by year end. If you could just clarify that for me. Secondly, on a higher level just around new business over the last two or three years, have you actually lost business purely on the basis of your B-BBEE ownership, or do you think this is more of defensive move? Is it something you can actually quantify how much business you've lost in the last couple of years, and it is material or not?

Iain Williamson
I will let Casper answer the first question around the accounting treatment. Regarding the second one, we can point to specific transactions and mandate losses in the asset management space have been attributed by the clients that have moved the business specifically to the issue of majority Black ownership in asset managers. So, the answer to that is yes.

Casper Troskie
Michael, on your first question, the once-off costs will be treated as a transaction cost which we exclude from our adjusted headline earnings. We have agreed that treatment with our audit committee. The once-off costs that you see in year one, the R150 million for the transaction plus the retail scheme, that once-off cost will go outside of adjusted headline earnings. So, it will sit in the centre. The rest of the costs relating to the employee scheme we will allocate to the business units. And then obviously the community scheme will sit in the centre. And you can see that's not really material. Hopefully that gives you a sense. We shouldn't see the employee scheme solely sitting in the centre. Some of that will be allocated to the business units.

Michael Christelis
That's very clear. Thanks very much.

Operator
Our next question is from Larissa van Deventer of Barclays. Please go ahead.

Larissa van Deventer

Thank you. Good afternoon gentlemen. Three questions please. On the lock-in, on the slide you specified that it's ten years. Does that mean after ten years all the shares are fully free to trade? The second question is on the funding. Could you please help me understand the extent to which the funding is effectively just a loan that will be repaid, or is there a free element to it? I am not clear on that.

Also, is the attractive funding cost included in the cost, or does that come in addition, the differential between that and market rates? Then the last one is, Casper, you mentioned the benefit and you mentioned where they would come from, but I'm not clear as to how. Are you expecting to get all the benefits from additional business, or how did you quantify those benefits please?

Iain Williamson

Thanks Larissa. If we start with your last question, as I've said, we've looked at funds at risk in our existing client base where there is an empowerment mandate. That's one part of the answer. These are the fees we can lose if we don't do this. Then we've also looked at our existing clients where we have current allocations to us where we think by having a higher empowerment or being above 50% – let's be blunt about it – will give us the ability to attract additional funds from those clients. And we've quantified what we think that number is.

And we also then looked at proposals we're currently excluded from because we're not majority Black-owned. So, we've looked at potential additional pipeline that we can source because we would be Black-owned. And we've put a number to that opportunity, and we've calculated what that would mean from an assets under management, a revenue and a profit perspective. I hope that helps, Larissa.

In terms of the notional funding there is obviously interest charged on the funding, depending on which scheme it is, and it will be as a percentage of prime. And how the notional funding works, whatever the cost of that build-up of the funding is including the interest, taking off the dividends, excluding the trickle dividends. Whatever that ends up at the end of the day, you then cancel enough shares to pay for the outstanding funding and the interest rollup on that at the end of the scheme so that you get to the amount of shares that actually vest for each of the participants. For the community scheme it remains post the ten-year period. And those will be treated as treasury shares on an ongoing basis. And you will see the trickle dividends coming through as a cost. I hope that helps, Larissa.

Larissa Van Deventer

I'm not sure that I'm entirely clear but let me think about that one. Thank you. So, the lock-in for everything is ten years, and then it's completely free float. Is that right?

Iain Williamson

For the employee scheme there is a four-, six- and eight-year lock-in. For the other schemes there is a five-year period for the retail scheme. We then intend listing the retail scheme shares on a B-BBEE exchange which then preserves that B-BBEE nature of those shares for longer than the ten-year period because they are listed on that exchange.

Larissa Van Deventer
Okay. Thank you.

Operator
Our next question is from Craig Gradidge of Gradidge-Mahura Investments. Please go ahead.

Craig Gradidge
Thank you. Good afternoon gentlemen. I think my first question was partly answered. It was around the retail scheme. I see it's a ten-year funding term but there is the intention for it to be an evergreen scheme by staying listed on an exchange. And I think you've answered that, so I'll go to my second question, whether the staff shares will also be listed on the same exchange so that if members of the public wanted to get a bigger exposure to Bula Tsela, they could, or to at least improve the liquidity.

Iain Williamson
We're intending to treat the staff shares, except for the difference in the vesting period, in exactly the same way as we're dealing with our current employee share allocation. So those will not be listed on the B-BBEE exchange. That's the current thinking.

Craig Gradidge
Okay. And then the last question. The selection criteria, it looks like you will be favouring smaller investors. Do you have selection criteria that you can disclose now, or do we just wait for the prospectus for that?

Caser Troskie
I think we'll be detailing all that detail in our circular. But there will be a substantial skew both in the staff scheme – and when we say substantial, we mean substantial – towards our lower paid employees at lower levels of management. And equally there will be a skew in the actual retail scheme. Taskeen, I don't know if you want to give a bit more detail on that.

Taskeen Ismail
Thanks, Casper. That is accurate. On the retail scheme selection criteria, it really does depend on the level of applications that we get. But the intention is to try and build that book with as broad an allocation base as possible.

Craig Gradidge
Thank you.

Operator
Our next question is from Andrew Sinclair of Bank of America. Please go ahead.

Andrew Sinclair
Thanks everyone. Two from me if that's alright. Firstly, do you expect this to be a one-off transaction, or do you think there will be any further such transactions in the future? *Best-in-class* is clearly a moving target. And the second question was just on the benefits. On what timeline should we start to see the benefits that you've been talking about? Thanks.

Iain Williamson
Andy, I think on your first question our view is that at this stage this is a one-off in the sense that we made a particular commitment as part of managed separation which we are honouring. I think any decisions around future transactions will be driven by essentially a business case for that transaction in terms of understanding what we believe the cost benefit equation looks like. So, at this stage we don't necessarily plan anything else, but it's an evolving story over time depending on the business case at that point in time.

Andrew Sinclair
And a timeline for the benefits?

Iain Williamson
Casper, do you want to elaborate at all?

Casper Troskie
I think based on my understanding of the work that we've done, actually we've been able to keep some clients because of the fact that we are going ahead with the empowerment transaction at a Futuregrowth level and the intention to get Old Mutual Investment Group to 51% Black ownership. So, there is almost immediate benefits starting to accrue. But I expect the timeline for the benefits to accrue and for us to be on the front foot on the benefit side versus the cost to be within the ten-year period timeframe.

Andrew Sinclair
Thank you.

Operator
Our next question is from Cornette van Zyl of Absa Asset Management. Please go ahead.

Cornette van Zyl
Good afternoon, guys. My Black Scholes and IFRS 2 knowledge is a bit rusty, but in terms of the cost assumptions that you put out here under current share price – because obviously we've seen quite a significant correction in your share price along with the rest of the market – what type of impact would it have on these cost numbers and your cost estimates if we see material either upside or downside movements on the share price?

Casper Troskie

So obviously the scheme is dependent on how the share price performs over the period. The starting share price is an input, and then obviously what happens to the return over the ten-year period. If there is a higher return, more shares will vest. So, we've based our financial impacts at this stage on a set of assumptions which we will be disclosing as part of the circular. And obviously if interest rates are higher, if there is a change in volatility, if the dividend yield that we've assumed in the model is higher or lower, it will impact on the ultimate number of shares that are vesting. The IFRS 2 cost is fixed. Because it is equity-settled, it's fixed on day one. And that will move around until we actually do the deal. So, it depends on what happens to the market.

So, you will calculate that on the day of implementation of the transaction using the various inputs at that point in time. Then you will calculate the IFRS 2 cost, and that will then be your cost that you use for accounting purposes. The actual number of shares that then vest at the end of the day, if there is no growth in the share price, there will be no shares vested. So, the share price actually has to perform for participants to get value out of this transaction. I hope I've understood your question correctly and I hope you're happy with the answer.

Cornette Van Zyl
Would you be publishing a sensitivity analysis to your costs once you have all of the details?

Casper Troskie
Taskeen, I'm not sure if we're doing it as part of the circular. I think we will be doing some scenario analysis. We'll certainly have two scenarios I know of. But once we've made the announcement, we can certainly provide you with sensitivities as part of the updates to investors when the circular has gone out around some of the key assumptions like share price growth and so forth so you can have a better understanding of what the sensitivities are.

Cornette van Zyl
Thank you.

Operator
Ladies and gentlemen, just a reminder, if anyone else would like to ask a question, you're welcome to press * and then 1. We have a question from Sarine Barnard of Ninety One. Please go ahead.

Sarine Barnard
Hi everyone. I just want to find out how do we think about the impact on the embedded value (EV)? Casper, as you said, initially the notional loan will have to be paid off through the appreciation of the share price. Will it initially be zero, and as the share price appreciates, the ones that seem to vest will be taken into account? Or how do we think about that?

Casper Troskie
So, the impacts on the balance sheet are actually quite small because IFRS 2 is effectively a charge through the income statement, but the credit is taken to reserves. So, we will be providing you with the detailed impact on the net asset value and the EV will be much the same.

Sarine Barnard
So, what happens to the shares in issue for the EV?

Casper Troskie
So, the shares in issue because they're treated as treasury shares until such time as they vest, you won't have any impact in the near term. And when those shares then vest, we will be providing you with detailed disclosure on the dilution impact of the shares. What the accounting rules require us to do is to show the negative side only. So, we need to take the costs into account, and the additional shares that we think might be issued, but we don't take the benefits into account. Obviously for this to be a complete picture, one actually has to understand what benefits you derive from this transaction, which I've spoken through before.

Just to be 100% clear, shares are treated as treasury shares and there is no impact over the term until you get to a vesting date. Then dependent on how many shares get issued, there will be a dilution impact. And we feel confident as management that the benefits that should accrue should more than make up for the dilution impact in the shares. But the way we have to account for or report this from an IFRS perspective requires us to only take the costs into account and the additional shares that we will issue.

There will be detailed disclosure, Sarine, on the expected dilution impact. Once again, that could change quite materially depending on whether the share price underperforms or overperforms. So, you will have a much smaller dilutive impact of the share price underperforms, and vice versa if it overperforms. But all those details we'll have in the circular.

Sarine Barnard
Okay, great. In the circular. So, is the EV going to anticipate the expected dilutionary impact, so make assumptions on the share price accretion over the ten-year period and then take the dilution into account immediately, like putting a value on it?

Casper Troskie
Because you've effectively calculated on day one the value of what you're giving the shareholder. That's what your IFRS 2 charge represents, the cost to the shareholder of this transaction.

Sarine Barnard
Yes. Not the dilution. So, basically if everything goes according to plan and say you issue 50% of the shares of the 205 million shares at the end of the scheme, then in year nine you will have everything still treated as treasury shares and in year ten all of those shares will come into issue, and you will see the dilution in the EV only in that year.

Casper Troskie
Just remember you've built up the reserves through the IFRS charge to effectively pay for those shares. So, I think what we'll do is we'll try and provide a bit more detail on that as part of the circular so it's very clear.

Sarine Barnard

That will be great. That will be very helpful. And then I just wanted to ask on the share scheme. Iain was saying that the funding will be provided by the different business units. I wasn't clear. So, the ESOP scheme also has a notional funding attached to that. Will that notional funding be the liability of the business units or the liability of the participants?

Casper Troskie

No, it will be the liability of the participants for repaying the funding, but the funding to the participant is provided by… it is not so much the business unit, it is more the legal entity that provides the funding.

Sarine Barnard

Okay. So, the hurdle for the ESOP scheme is substantially higher because the notional funding is based on the net fair value, 80% net fair value instead of the VWAP which obviously you still have to disclose to us. But I assume the notional fair value will be quite a bit higher than the VWAP.

Casper Troskie

I didn't quite follow that, Sarine.

Sarine Barnard

My understanding for the ESOP scheme is that the notional funding talks about the subscription price will be 20% VWAP and 80% fair value. So, is my understanding there incorrect? That's what needs to be paid back by selling shares at the end of the period.

Ranen Thakurdin

Can I add? Sarine, we just used the word fair price because it's not the VWAP. We will use the share price we use in the option pricing model for the fair value calculation. But I think for your intents and purposes, just think of it as the share price.

Sarine Barnard

Okay, great. Thanks. I couldn't understand.

Ranen Thakurdin

It's more an accounting/tax technical issue that we have to refer to it that way.

Sarine Barnard

Okay, great. Thanks so much. Thanks for that, guys.

Operator

Ladies and gentlemen, just a final reminder, if anyone else would like to ask a question, you are welcome to press * and then 1. We will pause a moment to see if we have any further questions. It seems we have no further questions on the lines. I would like to hand back to Sizwe for any closing remarks.

Sizwe Ndlovu

Thank you, and thanks everybody for participating in today's engagement. We do still invite you to contact the investor relations team should you have any specific matters you wish to discuss with the company. And finally, we will be making a transcript available on our website of this call very shortly. Thank you and goodbye.

Operator

Ladies and gentlemen, that concludes this call. Thank you for joining us. You may now disconnect your lines.

END OF TRANSCRIPT