S1 2013 Earnings Call

Company Participants

- Adrian Gore, Group CEO
- Barry Swartzberg, Executive Director
- Herschel Mayers, Executive Director
- Jonathan Broomberg, CEO, Discovery Health
- Ricky Farber, CFO, Finance Director, Executive Director
- Unidentified Speaker, Unknown

Other Participants

- Brian Mushonga, Analyst
- Mike Christelis, Analyst
- Unidentified Participant, Analyst

Presentation

Unidentified Speaker

If I can be a little bit more formal, Mr. Adrian Gore, the Executives of Discovery, members of the Board, the investment analysts aside, we all once again thank you for presenting to us today for the period ended December 2012.

Discovery is an enterprise that comes to us once in every generation, where an enterprise rises above the rest. And Discovery has risen head and shoulders above the rest in South Africa, not only adding shareholder value, that's only one aspect of it. But also as a Group and as a Company. And as an enterprise adding to the quality of life and also to the quantity of life of all South Africans and all those that participate in their products.

So Mr. Adrian Gore it's, once again, we thank you for giving up the time and for the energy that's gone into this presentation, thank you.

Adrian Gore {BIO 3068929 <GO>}

Peter, thank you very much for the very kind introduction. And you really touched on something close to our hearts and it's really trying to make a difference to the people that we serve. And I do want to make that point.

It's an absolute honor and a pleasure to be here and to present to you today. It is the interim results of Discovery to December 31, 2012. It has been -- I'm trying to find my way around this very complicated -- it's like a NASA launch pad here . There we go.

It has been a very, very exciting period for us. And I think it's been excellent and it's been important. It's excellent in the sense that I think our results have been strong and rigorous. You'll see later in the presentation operating profits up 21%. Our established business has grown by 15% and our emerging businesses, particularly in the UK, had a fantastic time, up 70% in total.

So it has been an excellent year for us. But I would say it's an important period, important in the sense that our business model is taking shape. We're learning more and more about its ability to scale, to repeat, to penetrate in the South African market. And I think across our 10 business units in core countries, as you can see on the chart, I think we're alive to all of them and there's a very, very strong push in that regard. We're excited about what's been achieved and I think we're very confident about what we can do going forward.

I think it's important to contextualize once again. I need to restate it. What we're trying to do, what our purpose is and what is our ambition? And our purpose is clear, build an organization that makes people healthier. Build an organization that through doing that builds products and structures and solutions for our customers that enhances their lives and protects them in the right way. And that's what we're focused on doing.

Our ambition is to build the best-in-class global organization that is renowned for strength, financial strength and innovation. It makes a difference to the societies in which we operate.

Now I've been talking about this core purpose for many, many years and often times I get the feedback it sounds kind of soft and a bit fleeting in the rough and tough bottom line role of financial services. But I will contextualize to you today in a sense how fundamentally the purpose is, the methodology is, in a world that's changing around us.

And there are a number of global trends, I think mega-trends that are becoming clearer and clearer that make our model directionally, I think, fundamentally important.

The first is, I think, quite an obvious issue, something we've been speaking about for a long time. But the simple idea that diseases of lifestyle are fundamental in driving mortality and morbidity. And we know this. There are many different ways of cutting this. The one that I like that's the most descriptive on the left hand side of the chart is the Oxford Health Alliance view of what they call 3-4-50. Three lifestyle choices; smoking, poor nutrition, lack of exercise, lack of physical activity lead to four conditions, diabetes, cancer, heart and lunch diseases that drive 50% of mortality. It's quite remarkable.

And these are modifiable through behavior change. Now we've known this for a long time. But it's becoming a bit of a fever pitch. The United Nations had a summit last year. The World Economic Forum in Davos just a few weeks ago brought out a charter for healthy living. There's a strong focus on this in every respect.

And I think there's a wave coming our way, a wave around nutrition; a wave around how food companies from Nestle to PepsiCo, how they make their food, the salt content, the trans fats; a wave around physical activity leading to policy change. That's happening.

But at our level, an institutional level, an organization that can create behavior change could price that into insurance, can make people healthier and somehow integrate that into insurance models I believe has a competitive advantage and has the ability to offer better products to customers. And that's what we've focused on.

The second import trend is a world of uncertainty. And we know this well. But we are in a very volatile world in every respect, geo-politically, power shifts from west to east, the multi (inaudible) with all kinds of complexity. From a financial perspective, the global financial crisis has meant, if you look at any index, there's been a lost decade to an extent. People have lost faith in the stability of markets and the ability --the investment markets the ability to really deliver.

It's amazing that almost accepted dogma 10 or 15 years ago that you should opt out of a defined benefit pension scheme and go into a defined contribution one. It was a terrible choice to make if you did do it, essentially a world shift from individuals to companies that's what has happened. And it is problematic. But people have lost faith in a sense in that regard.

At the same time, we have recession in different parts of the world. And you have other things, climate change, demographic shifts. We live in a very complex world.

Now not to be pessimistic. And that's not the point of my comment, I'm simply making the point that people are risk averse and concerned. And, therefore, the protection industry, the life insurance, the health insurance industry, those industries that can create certainty, can create predictability are very, very relevant.

But the fascinating issue is that the innovation has been largely in the investment space, the investment markets, hedge funds, ETS, whatever it might be, complicated innovations, sub-prime mortgages, dare I say. But be that as it may, life insurance markets largely are commoditized. There hasn't been much innovation.

If we look on the right hand side of the chart, there's just a -- I'm sorry, it's not very clear. But just to show you a portal in the UK. Life insurance is about commodity, it's about price. There's very little innovation.

And once again, I'd say to you, given the relevance of this industry, if we can innovate. And I believe we can, if we can, in fact, innovate for our mortality and our morbidity, the very input costs that drive these things, our ability to compete, be relevant is real. And so I say to you the global uncertainty is good for what we are doing.

And then the final trend I wanted to mention and I just want to explain this to you very carefully is the issue of healthcare. Healthcare's massive. It's probably the largest industry in the world. And it's going to grow, it's robust.

And that might sound against the run of play, wherever you go in any country, there's a sense that healthcare's unsustainable. In our country here, the doubts about the NHR; the doubts about whether private healthcare can sustain itself. Same in the US, same in the UK, those are the feelings about healthcare.

But there's seeming contradiction between the robustness of healthcare and the fact that people can see that it's unsustainable. It's because, in a sense, its cost inflated above inflation. That is what disarms people. How can you have an industry that continues to cost more in real terms. It's not possible. But I think it is.

And there's some fascinating work by an economist call Baumol, a great book called the Cost Disease that I think it makes it absolutely obvious when you think about it. You see his thesis and we've seen it play out is that certain industries drive efficiencies down through technologies. The manufacturing, automotives, electronics, they're getting more efficient over time.

But industries like healthcare, education, the Philharmonic Orchestra is an example, rely on skilled labor, doesn't respond to technology. Healthcare is full of technology all over. But, in fact, we see healthcare technology, ironically, makes things more expensive. Biological drugs mean we can do more; scanners cost more, we can do more.

Technology at this stage is not driving down cost. And, therefore, you will accept those industries that don't have efficiencies through technology will inflate higher than those industries that do.

Now the simple epiphany is that CPI is the arithmetic average. So, therefore, you have to accept healthcare will always inflate above inflation. And other industries are always, in fact, below inflation. And that's how it is, right?

Now the interesting thing that you have to ask and you see from the chart there, I think that came out of one of the Baumol studies, if you look at the US over the last 30 or 40 years, you can see how healthcare and education have dramatically outstripped price inflation. In fact, they're at CPI plus 2% to 5% across the world. If you read some of these studies, it's quite remarkable.

The question is how do they sustain it? And the obvious answer is because the other industries inflate below inflation, they make way for these industries that inflation above inflation.

Now, not to say that they continue forever and hopefully we can bring technology to health in a way that brings costs down. But the point I'm trying to make is healthcare's likely to grow. And we have to fight, as Discovery and others, to keep costs under control. That's our fundamental role. And so I'd say here at a strategic level, in an industry that's going to grow. But if we can bring costs down for our customers and we must, our relevance is fundamental. And I'd to say to you that's one of the directions we're focusing on.

So to an extent, I would say to you that these three trends contextualize our core purpose of making people healthier. It's not a soft idea. It's not a fleeting idea. It's very, very fundamental. And to an extent, in the period under review, we've restructured our business, focused very hard on building out the chassis, Vitality at the base; building best of breed companies in every regard; being meticulous in how we structure them in our different geographies, in different industries, to make sure we capture the value that we think we can.

If we get it right. And I believe hopefully you'll see in these results, in many cases we do, fundamentally we have the opportunity to make people healthier. That's the core of what we do.

But from a competitor position, our price points are lower; our selection is better; our selective lapsation is better; our products are different; and the performance is fundamentally better. And that's what we're trying to do.

What I think is exciting and hopefully you'll see that, in our establish businesses we are learning more and more how to do this. But I think we're learning how to scale and repeat this into different markets. And I think that is the great opportunity that I think we have. So the fundamental benefits of the model, I think, hopefully are self-evident as I go through the presentation.

So let me begin by just giving you a bit of an overview of the results. I then want to go into just showing you a few analyses of the earnings very quickly. I hope in the disclosure that's much more detailed. I'm not going to get bogged down in that.

And then what I thought I would do, as I usually do, is try and give you a bit of strategic insight into some of the businesses. I can't do all of them. And some of the thoughts of where they've come from, where I think they are, where I think they are going.

Let me start with just giving you a bit an overview. Discovery itself, operating earnings up 21%; headline earnings per share up 20%; embedded value of 18%. And I think robust new business of a higher base up 12%.

Discovery Health had a fantastic performance in every regard. And the Discovery Health medical scheme under that has performed remarkably well for its members and I think that's important.

Operating profit up 12%; despite a cut in our administration fees, we continue to do that. We reduced them by ZAR70 million over this period; despite the size of the base. The base grew by 6% in total off the back of strong new business and very low lapses. And I think in every dimension of what Discovery Health is doing, it's done remarkably well, as has the Discovery Health Medical Scheme.

Discovery Life had a very pleasing performance, operating profit up 17%. New business up 7%, I'll show you later the development of that. I think the real story around Discovery Life has been quality. We focused hard on getting the model to pricing, the lapses, how that interplays with mortality, how it works with Vitality in different ways. And critically, Discovery Life is now cash positive, I think it's very, very important; so a very good period for Discovery Life.

Discovery Invest, a rather pleasing performance, operating profit up 22%; assets under management up 42%; the business is relatively young, great potential going forward.

Vitality had a tremendous period; growth up, lapses down. But the real story of Vitality. And I going to make a few points a bit later, has been the learnings we're getting about engagements, about what programs work in the context of Vitality and how we can scale them out. And that really forms a foundation for what we are doing. We're deploying a number of different ideas into different markets.

Discovery Card continues to perform well, over 9% market share; the book is over ZAR2.6 billion; excellent credit experience. I think it continues to provide a foundation for growth.

And then finally, Discovery Insure, in the local context, new business up 56%; a very, very strong growth in new business. We estimate at the end we're capturing around 9%, at the new business run rate, of the market. It's pretty good after 18 months; we're pleased with it. We've invested a considerable amount in the period, about ZAR100 million/ZAR102 million. And I'll take you through that a bit later in the presentation.

Turning to some of the international new businesses, in UK, by a long shot, a star of the show. The UK businesses have been absolutely remarkable. I'd say it's the best period we've had; a lot of work that's been done in PruHealth and in PruProtect have really paid off. You can see there that the combined new business grew by nearly 50% to ZAR727 million. Operating profit up nearly 70% to ZAR347 million. The business is throwing out huge amounts of cash at the same time.

So I think that, to me, has been one of the seminal events of the period. PruHealth itself operating profit up nearly 90%. As you can see, every aspect inside the PruHealth business I think is very strong; lapses, mortality rates up, claims rates and loss ratios. And I'll show you a bit later how that's played out.

PruProtect, I think, by the long shot the star of the show. Operating profit up over 100%; strong new business growth up nearly 60%. It's navigated a very complex environment like gender equality, tax changes. But you'll see every aspect of the business is tight, the distribution is excellent and very pleased with the performance.

Our stake in China we've reached first base. I'm going to take you through some of the thinking there. We really have focused hard on building the business; building up a very good quality health insurance business in China. I think it's reached first base and it's, really, we've refocused the business towards core, proper health insurance products in both the Group and individual market. And we're pleased with the progress.

And in the US, the Vitality Group with Humana I think has grown tremendously; up to 2 million lives. Post the reporting period, Humana has now opened up Vitality to their Medicare book. So they're adding on -- they've added on 700,000 lives now. We've transacted a deal with Wal-Mart together with Humana around offering HealthyFood in the US that I think has great, great potential.

So across the Group I think the performance has been very, very strong and I think the innovation is very much alive.

Let me just say this about the business model on a financial level; what we've tried to do. And I hope it's clear, is a build a business on innovation; a business on IP; a business on a different business model; and, to an extent, one that is capital light. Our view is if you have sufficient IP and knowhow and expertise you can grow organically and you can grow in a sense and the ability of the team. And I think we're managing to do that.

The methodology has been around incubating new businesses, spending 5% to 7% of our operating profit on new businesses, at the same time. And strong organic growth. And then those businesses become established and they then fund the growth. You get, hopefully, this virtuous cycle. That's what we set out to do.

So, to an extent, if we're successful I would argue what you should see is robust, established businesses, throwing out cash, funding new businesses with new platforms. And you get this kind of virtuous cycle. I think. And I hope you'll see, in the period under review that I think that methodology has been very, very sound and has played out, I think, very, very well.

Going through just some of the numbers. I've just told you about these. But I'd like to just contextualize them. If you look at the operating profit, up 21% to just under ZAR2 billion; the established businesses, Discovery Health, growing by 12%; Discovery Life growing by 17%; both of them off a very, very large base. The established businesses together then collectively growing by 15%.

You can see the emerging businesses in the UK and Discovery Invest growing by a very strong 71% collectively. You can see PruProtect over 100% growth; PruHealth nearly 90% growth. And Discovery Invest up 22%.

We spent slightly more on incubating new businesses in the context of the Vitality Group, Discovery Insure and Ping An. The real driver there is Discovery Insure; we spent over ZAR100 million on Discovery Insure. It's growing quickly; significant new business during bad weather during the period. And I'll touch on that a bit later. So we spent about 10% of operating profit on that. We're not concerned. I think with the platforms we're building we are confident of great potential going forward.

When you add it all together you find that headline earnings per share up 20%. And we've declared a dividend of ZAR0.60 per share, up 20%; very consistent. So a very simple flow-through from operating profit to headline earnings to the dividend declaration. I think quite straightforward and quite simple.

Let me turn to new business; quite an interesting set of dynamics in the new business side illustrating a number of issues. We're pleased with the new business performance; up 12%, as you can see, to around ZAR5.1 billion; made up of different pieces of it.

The established businesses, Discovery Health off a very high base, growing by 9%; Discovery Life growing by 7%. That trend is escalating. I'd like to take you through that a bit later.

Vitality is getting great acceptance. It's growing into the base at a rapid rate; you can see it growing by 42%.

In the UK the points I made, you can see PruProtect and PruHealth going very strongly; 58% and 36% respectively. I'd say to you the 58% is slightly flattering, because the gender equality and tax changes in the UK at the end of the year, there was a bit of a rush of new business in December. So it's slightly bloated. But I would still argue that that -- it would have probably ended up not that far from there anyway. The kind of momentum and the pace of the business, I think, is quite remarkable.

Discovery Invest up 6%; we slowed down capital bonds in that period. So not overly concerned about that. You can see on the new business side the Discovery Insure performance quite remarkable, up 56% to ZAR184 million.

Vitality is a bit lumpy. We did very little in the second part but, in fact, post the reporting period we had 700,000 lives join. So, it's a bit difficult to get consistent growth, because our big client is Humana. So you're going to get lumps of business coming over from period to period.

In the case of Ping An, I will show you a bit later that there's a refocus of the business away from what they call service and fun products; more towards the insurance products. So, to an extent, the 6% growth that you see there doesn't tell the full story. We kind of slowed down the other business. And you can see that we're focusing more on the proper, bona fide health insurance business, per se, which is growing quite nicely and will continue to grow very strongly into the future.

If you look at the performance in both earnings and new business in a graphical form, I think you see clearly how we've progressed. I think the earnings have grown nicely. The earnings per share we've managed to add 28% per annum, compound, over the decade and more since we listed in 1999. And I will point out that we've managed to achieve that growth without recourse to much capital. And I think that tends to show the virtuous cycle and how it's playing out.

You can see the new business will fluctuate from period to period depending on how we play out. We are pleased with the 12% growth. And I think, more importantly, we built very good foundations, I think, to go forward from that.

A few points about the earnings I thought I'd make, just to give you a sense of quality, the first is earnings are becoming more diverse. So if you go back a couple of years, the organization was really Life and Health, to an extent. If you wind forward to this period, which you can see is a much more diverse set of earnings by industry, by country, 13% of the earnings are now offshore through the Pru ventures. And I think that's going to grow. So to an extent I think the earnings have become more robust and more diversified.

The second important point I wanted to make is cash flow. The organization is throwing out considerable amounts of cash. During the period we generated ZAR2.3 billion in cash from the business.

Amazingly, you'll see. And it's an important point to understand, I hope I make it clear later in the presentation, you can see Discovery Health threw out about ZAR1.5 billion of cash on its existing book. Discovery Health threw out some cash. The Pru businesses in the UK are throwing out quite a bit of cash. We're investing a lot of it back into Discovery Life new business, into Discovery Invest. And in fact, most of it locally.

So if you actually look at the use of cash on the right-hand side, you'll see that only 6% or so is being spent offshore. So despite the ambitions of globalizing a lot, what we're doing is still taking a very prudent approach and a very careful approach to the deployment of capital outside of South Africa. We remain very optimistic and committed to our country and we think we can do both, in a sense, at the same time. And I think that's played out in the cash and capital allocation.

And then, finally, in terms of quality. The embedded value has grown very nicely, up 18%, as you can see, to just over to ZAR59.26 per share, as you can see.

And I think maybe more important than the actual just quantum of the embedded value, it's interesting to look at the build-up of the embedded value from ZAR30.2 billion to ZAR33 billion on the right-hand side of the slide. What I want to show you is the controllable build-up; in other words, where we can have an influence from the ZAR30.2 billion to the ZAR32 billion or so, the two blue charts.

And the point I wanted to make is if you look at the build-up, of course, there's the unwind of the expected return that you see coming through. But the real drivers of that growth is new business and positive experience variances. And I think that's fundamental.

We've achieved the highest positive experience variance I think we've seen, certainly in Discovery Life, as well. So, to an extent, the growth in embedded value is a function of ability to transact and attract quality new business. And at the same time, I would argue, that it's a function of the organization outperforming the expectations set for it at the -- within the embedded value assumptions. And so to an extent I think illustrates the quality of the earnings and I think the quality of the business that I think we are building up.

In terms of the positive variances, just to make the point, the organization over six months generated over ZAR600 million positive experience variances across a wide range of different metrics. You can see the very strong performance in terms of lapses on the left-hand side of the chart, in addition to mortality and morbidity. So, I would just argue that I think quality of earnings is very strong; cash flow generative diverse, great quality in terms of the embedded value. And I think we're pleased with that.

Let me turn to some observations. As I said, I cannot comment on all the businesses; there just isn't the time. But I want to make a few, hopefully, interesting comments and give you a sense of our strategy and give you a sense of where we're going.

Firstly, I want to talk about Vitality generally. I've made the point about Vitality in the local environment. It's growing strongly and it's really a powerful foundation for what we do. You can see the membership growth is very strong. Lapse rates are remarkably low. So, they were always low at 3% and have come down to Vitality-only lapses of about 3%. So it's very, very, sticky.

The engagement levels are quite remarkable. If you look at this we're generating 2 million gym visits a month from our client base. People are flying 70,000 flights a month. That's like 12 737s packed every single day of people using their Vitality benefits. There is frenetic activity in the context of them. And, of course, that bodes well for people doing to actually earn those benefits. We're driving population health better. And I think that's fundamental.

But, at the same time, I would say to you that we're learning about programs that can be repeated and scaled, not only here. But in the other markets. One thing I'd mention to you is the HealthyFood benefit that is a tremendously simple idea; give 25% discount on healthy foods. It addresses the very thing that people are concerned about; trying to create the difference in price between healthy things and unhealthy things.

I've mentioned this to you before. It's simple to the customer. It's very complex what is healthy, what isn't healthy, how you filter out these foods. The joint venture with Pick n Pay is something that has been remarkably strong. You can see the cumulative spend. Our clients are spending about ZAR2.5 billion a year now through this benefit; this is remarkable.

And we're starting to see, on the right-hand side of the chart, differences in lifestyle-related illness, incidence of it, by people that are buying more healthy food, those that are buying less. Now, of course, we don't have the causality of it. But it's quite fascinating what we've started to see; we need to understand it better.

But the point of this benefit is it's amazingly crisp; we need to make it bigger. And we need to scale it into other markets. So some work has been done on a number of things. The first thing we did during the period we transacted a deal with Woolworths, which you may have heard of. That's rolling out next month. So, in fact, expanding the HealthyFood network in the South African context, will be available to certain parts of membership of the Discovery Health plan.

It's very much on the same line, a very crisp idea, 25% HealthyFoods, the same kind of physicality of the benefits. It's leading to the till splits; it's leading to the shelves of

Woolworths. So, you'll be able to see on the different Woolworths shelves the Vitality HealthyFood tick, as you can see.

So we're going through a process of rigorously building up the infrastructure together with Woolworths. And I think we have a fantastic set of, what's the word, goals and excitement about this particular development, excited about what it can do.

At the same time, we're scaling it into other markets. We've done a lot of work with Sainsbury's in the UK. I think that's in its infancy. And we need to push that out.

Something notable during the period I make the point Humana together with Vitality. And Wal-Mart have got a joint venture now on HealthyFood. So we're playing this out into the US market at the same time. We have taken a bit of a soft step into that market. We're giving a 5% discount; the US is a complicated place. We need to field that out. But I think quite quickly, over time, we're going to, in fact, escalate their Vitality status.

I thought I'd show you Humana's now matters actively promoting this as part of a Vitality rollout to Medicare clients, etc. I thought I'd tell you what they're saying, hope this comes through.

(video playing)

Quite interesting, because Humana is the biggest Medicare player in the US and, in fact, Wal-Mart is a distribution point for the Medicare products as well. So there's the potential to link it all together and I think it's very, very, powerful. So this is -- this really is in its infancy and I'm trying to illustrate the ability of these programs to scale and to be repeated. The customer message is simple but the technology behind it is not that simple. And I think it's a competence that we're developing.

The other important point is we're learning more about how to build the Vitality brand in different markets. So, in the UK, for example, one of the things that we're doing. And it's actually working remarkably well, is the idea of a Vitality ambassador, Jessica Ennis, who, you may remember, won the gold medal for the decathlon for the UK. She's a remarkable role model. In fact, research shows she's the number 1 role model in the UK. She's a remarkable, clean-living, smart, successful individual. And she's now a Vitality ambassador.

And the power of it is quite remarkable. So it does illustrate to us the ability to use people. It's such a positive message. There's no downside to Vitality. And the ability to use ambassadors to get that above the line I think is great, great, potential.

At the same time, what's interesting about Vitality is, it helps build the brands of our partners. And I hope you can see this. This is an amazing thing, what Ping An has done. Ping An, as I think you know, is the second and third largest insurer in the world. They are only active in China. But they're desirous of building their brand outside of China. And ironically, they believe building it outside of China will support their efforts in China, with Chinese people.

So in the Chinese New Year, last week or the week before, essentially on Times Square played a video of Ping An on a continuous basis. And most of the video is about Vitality. So, as you can see, now Vitality, new (inaudible) about health insurance, there's interviews on it, it's quite remarkable to see. You can see on the right-hand side, we only spotted this now, if you look above the screen you can see a weeping Pistorius to give you a sense of the time of this.

But the point I'm trying to make is it's such a positive powerful message. And it's beside us building brand, our partners find it as a pivotal way to build their own brands. And I think that bodes well for a much more global approach to what Vitality can do.

But ignoring the soft stuff, the hard reality is we're growing Vitality significantly. You can see the growth through Humana. We've only just rolled it out in China. We launched it six months ago. It's taken us six months to go through the regulatory process to get out there to market it. So, to an extent, we're only starting to get some traction in China. It's going to take us some time. But despite that you can see the rapid growth of Vitality.

And then the ultimate thing about it is it really is competitive advantage. We've done a lot of work on mortality rates, by Vitality status. It's remarkable. What you can see in the left-hand chart is different mortality curves by Vitality status. We can now effectively price life insurance by status, which is critical. And it gives us more rating factors. And that is a powerful competitive advantage. It also gives us the way life insurance products are developed; gives us ability to have dynamic rating factors, as people engage their premiums flex. That's remarkably powerful in the world of life insurance. I think it has global potential in the sense of what we're doing.

On the right-hand side, you know well, we've done a lot of work on the healthcare base to understand the effect on admission rates, on chronic illness and a cost-per-member per life for hospitalization. So essentially, ignoring all the soft, fluffy stuff about Vitality, the fact is it does make people healthier. It is a fantastic selection tool. And it does give us the potential to offer products that are simply better, priced better. And perform better. And that's what we're focusing on.

Let me go to the UK. And talk about the PruHealth, PruProtect, JV; it's had a remarkable period. I need to just state our ambition here of building a business along the lines of the Discovery business model; the best protection business in the UK. I think that opportunity's there. I think we're on the way to doing it. I think the potential is there.

The UK life insurance industry has typically been focused on savings, products, investments. As I've said before protection is, in a sense, commoditized based on price. The PMI market is very commoditized. We have a great opportunity.

And I think the period under review has seen this JV grow significantly. I made the point about some of the numbers. But I think if you look at them graphically, the performance is strong. You can see collectively new business growing by nearly 50% to over ZAR720 million; operating profit at 68%, very strong to ZAR350 million for this six-month period;

embedded value up to over ZAR4 billion over that period, up 30%. You can see the quality I think of the business that, to an extent, has been built.

And from a cash-flow perspective, you can see how the business is playing out. Over the comparable periods of the last three years, you can see break-even at a cash-flow level, throwing out now nearly ZAR0.25 billion in cash that, I think, has the ability make us grow, or has the ability to give us real power in the UK market and elsewhere.

So the performance at a combined level has been absolutely tremendous. The UK itself is an interesting market. It's a complex market. Firstly, the considerable headwind the market itself is experiencing, as you know well, the recession; austerity from Government. This is a very depressed environment and difficult. And I think that's exciting for a company that's innovating and changing. And trying to offer value for money.

At the same time, there are massive policy changes that are affecting both health and life insurance, that are significant. I think all of them are directionally good for us.

In the first case, the Retail Distribution Review that looked at distribution of insurance products is fairly profound. One of the important by-products of it is that independent advisers cannot earn commission on savings and investment products; they can only earn fees. And what that means is they're shifting their focus towards protection. And potentially selling private health insurance. That means a much greater distribution channel for us. And I think that's very good.

At the same time, wealth managers tend to be high advice, right at the top of the pass, absolutely perfect for the PruProtect vision and target market. But the gender neutrality is fascinating. The UK, following the EU, now has banned inability to differentiate premium rates by gender.

Complicated issue in life insurance, because women live longer than men, right. And it's quite remarkable. So what's happened now is prices for women have gone up. And prices for men, to an extent, have gone down to equalize. Complicated thing to navigate as a life insurer, there are all kind of lapse and re-entry problems. But the truth of it is for a competitor that's innovating. With Vitality the ability to attract women, we're in a very competitive position. I think that's important for us.

And then also important for the protection market, changes to the tax base to an IFRS basis of taxing life insurance, keeps prices up; again, good for a new entrant and good for a differentiator and good for someone competing at the top of the market. So we've had to, in a sense, navigate very complicated changes, all them I would argue directionally good for the business.

And then finally from a Health perspective, NHS continues spending reviews and complexity. The NHS is here to stay. That's why it is a fantastic asset. The UK, it's deep in psyche. I did see a saying once that there is a national religion in the UK, it's called the NHS. And I think it's very, very true.

But the truth of it is, under austerity, under the growing healthcare stent, it is going to battle. And, therefore, we are very confident of a growing, robust private health insurance market. And so we continue to innovate and our clear role is to outdo our competitors. And I think we have the ability to do that.

So if you look at the actual businesses themselves, I think they illustrate how we're navigating through this market. The PruProtect numbers are very strong. I've made the point about new business, about profitability. But I think if you look at policies in force up 53%; the value of new business significantly up to ZAR388 million; significant margins. We're increasing the profitability to an extent of the business.

The actual focus is on what we do here, innovate and offer better products. So we're focusing on a number of different areas, improving the critical illness products; getting Vitality to integrate properly with the protection products. And you can see the half-year by half-year development of the new business, very strong.

And on the right-hand side, I think it's a remarkable chart of the policyholders in force. You can see the rapid and consistent growth of what we've managed to achieve. And I think we're very pleased with that.

If you analyze the market share, it's really, really interesting. I think the business is doing amazing stuff. In the intermediated market, you can see looking quarter 3, that's the latest data we have, 2010/2011/2012, you can see how quickly we've taken market share. So I think we were seventh or eighth position in 2010. We jumped a spot, 2011. We jumped another two or three spots in 2012. And the period under review, in the Third Quarter, we captured 10% of the market.

I think when the quarter 4 stats come out you'll see further increase in market share. But illustrating just how quickly this business is starting to make headway in the context of the UK.

And then I think fundamentally the quality of the business is remarkable. You can see the lapse rates have come down dramatically, below our expectation. In the middle of the slide, you can see that the claims to expected are dramatically lower than -- sorry, the claims are lower than expected. And the value of in-force is growing very, very strongly.

So the focus on the top of the market, high premiums, quality business, careful pricing and underwriting and the quality of distribution that we're doing is paying great dividends in the UK. I believe that we're scratching the surface of some of the opportunities that we're looking at. And there's a number of very exciting innovations that the team have planned for PruProtect.

If you go to PruHealth, the performance I think has been staggering. There are two pieces of PruHealth that are important. One is that we made this acquisition Standard Life Healthcare two years ago or so. And it's about digesting that and making that pay. The acquisition was done for strategic reasons to give us scale. And I think that's worked.

The other strategy is growing new business and differentiating, bringing new products out and driving Vitality. I would say to you that in both of these we've done remarkably well. If you look at the numbers, I think they're fairly clear. The loss ratio is stubbornly low and coming down, I think that's to us probably the biggest asset; the operating profit up strongly; new business up strongly.

But, importantly, if you look at the actual acquisition and the effect of it, all the metrics are positive. If you recall a couple of years ago, our real worry was the loss ratio, how we keep that, how we manage that. We've worked incredibly hard on the pricing integrity, on the underwriting, on the risk management, on every aspect.

We've been absolutely focused on pricing bad groups up and out and making sure we maintain good groups. You can say that play out in the diminishing loss ratio. And when you compare that to the industry, it is quite remarkable. We are dramatically lower than the rest of the industry.

On the lapse rate side, we've brought the lapse rate down. And I would argue we're lapsing out the right kind of groups. So the performance of the plan at the base level has been incredible.

The acquisition of Standard Life Healthcare, we've been very careful in this acquisition. When we did the acquisition, we were careful about setting a roadmap for both loss ratios and lapse rates. So we set out that roadmap in the blue on both sides. What you'll see is the actual performance is far better in both cases than expected.

And our calculation is that the internal rate of return on the acquisition is about 33% over a 10-year period. So despite the strategic imperative to do the acquisition, the reality from a pure financial perspective has been exceptionally good. And I'm very pleased with where I think it's got to.

In terms of driving the business forward, there's been a huge focus on innovation, on new products, on the base of what we've created. There's a number of different pathways of innovations. We're really pushing around lines that our competitors aren't; driving benefits for not smoking; driving a focus on obesity with Vitality and bariatric surgery; wrapping around products all kinds of different issues.

You can see that's paying off on the new business side. In 2010, we did a lot of new business, quite a bit of corporate stuff. We're back to that level on higher post the acquisition. And, in fact, you'll see a lot less corporate, much more individual where the loss ratios are much, much lower.

So I'd say to you the new business is really growing, 36% growth in new business. But the quality of the business has been quite exceptional.

On the Vitality side, we're getting great traction. One thing we've done on Vitality, I think, is very smart in the UK, the regulations allow us to do that, we've broken up into two components; the core product, Vitality; and then a Plus, the outer ring, where companies and individuals can buy up to Vitality Plus, who offer richer benefits.

And the key thing for us then is to get the buy up to happen, we've introduced a whole range of new benefits in that structure. What you see on the right-hand side is the take-up level. A year ago, we're sitting at about 40% of new business buying Vitality Plus. Today we've climbed that to about 70%. So we're getting great traction, I think, in the context of Vitality.

And then we're focusing very much above the line in the UK on a number of different initiatives. I made the point about Jessica Ennis and I think we're using it in a whole lot of different ways. We're pushing things like the pharmas of the world triathlon, ultra tri -- the world triathlon series. The final is in London this year; it will be a PruHealth Vitality event. We need to think about how to get that ahead. It's on the same course as the Olympic Games. It's going to be quite fascinating.

We've also learned about things that we've done in this market. The healthiest companies to work for, we're doing it in the UK, together with the Sunday Telegraph and Mercers. And we're getting fantastic participation of companies in this initiative. Tesco's is there. Amazingly BUPA is part of our competition, I don't know why. And they've been remarkably active in it and we're very grateful. But it's really an exciting initiative.

Trying to make the point that we're pushing hard above the line to get the Vitality message out there. And I'm very pleased, I think, where both PruHealth and PruProtect have got to.

I want to turn to China. I wanted to give you a sense of the progress made in China. China is complex. And it looks opaque from the outside. And I think you can get stymied with the view of this massive explosive growth. It's the biggest market in the world. It's a complex market. And we're aware of it. And I don't think we're fooled by it. We've been quite clear that we have to build a Company brick by brick, life by life and let that market emerge. And we need to be at the front of that market.

We are pleased with the progress made. We're focusing very carefully on the kind of quality of new business. You can see new business up by 6%. I made the point about focusing on insurance business. But I want to just remake the case for China in the context of the health insurance.

It is a very big market in terms of healthcare. It's one of the biggest markets in the world in terms of total healthcare spend, more than 10 times the size of our market and I expect it to grow as China per capita becomes much more prosperous. But it's amazing that only 3% of expenditure is through private health insurance. The health insurance market is nascent; it's just starting to form.

On the right-hand side, you can see, amazingly, that 37% of expenditure is out of pocket. So you have this unbelievable combination of a rapidly emerging middle class, very big healthcare market, very big exposure out of pocket with very little insurance. And I think that is our opportunity and so we're pushing very, very hard.

But the point I wanted to make is we're not bamboozled by the scale of the market. We're focusing on building a quality Company. And I do believe we've got to first base. We've an organization of 371 people; we've got, I think, skill and structure in every part of the business.

And on the bottom side of the chart, I wanted to give you a sense that we've migrated a number of our systems, risk management; claims systems; customer service; systems into China; our head office in Shanghai, together with Ping An is strong, great people. We're focused hard in that respect.

We built a very strong branch network across China that gives us great potential to grow into China. At the same time, we have about -- we have seven branches. The core of the business is in Shanghai, Beijing and Guangdong. But we're growing out further than that. And I think that's a great asset going forward. The ability to penetrate the Ping And distribution channel is fundamental in this branch network.

And then from a product perspective, we've refocused the business into two distinct markets, what they call the group high-end market, what McKenzie might be buying or Goldman Sachs for their staff in China. We think that's a fundamental market. We need to compete and win there. I think that's in terms of scale and it's in terms of status, etc. And then on the individual mid-market, giving individuals the ability to buy state-of-the-art health insurance products, give them access to better healthcare.

And so we've refocused the market away from fund business and service business and the kind of stuff that they've been doing towards a very careful focus on brilliant products on the basis of Vitality. That has taken us some time to achieve. I must say, we're pleased with the results. In the high-end market, in the group high market, you can see there's been a very strong growth of business. I think we said explosive. I think it's very strong growth and I think we can take that number one position.

The quality of clients, you can see in the middle of the chart, is very strong; Goldman Sachs, Pricewaterhouse, Accenture, ICBC, etc. So I think we're penetrating very nicely.

And in the right-hand side of the chart, we're number two now in that space, ahead of Cigna, ahead of AXA, who need to capitalize on that. So the team knows there's a clear goal of being number one in that space. And that space will grow.

On the individual side, it's a very complex place. Chinese culture doesn't play well to products that you pay risk premiums to and if you don't pay them you get nothing back. There's a very strong savings culture. And so we've been very careful trying to understand how we can interpret the products in a way that will give people a sense of payback. So at the moment people are buying riders on their life insurance critical illness products to get into to pay for healthcare. It's a pretty blunt instrument.

We have the opportunity to offer. And we've called it CHP, the Comprehensive Health Protector, a product that's more comprehensive, focused, indemnity-based on the back of Vitality. And that's what we've developed over the last year. We rolled it out in November. It's now being actively marketed. I'm excited about what its potential is.

Just to give you a sense, it's actually very interesting in China. In the same hospital, you have a VIP section and that is what people buy insurance for. They want to avoid the normal piece and go for the VIP section.

This is a pictorial description; same day, same hospital, five minutes apart. You can see the general section; crowded, lot of people waiting. You can see the VIP section; quite remarkable the difference. In addition, there's, in both sections obviously, massive out-of-pocket exposure. So the ability to offer product to give people access to better quality care, better quality hotel settings as well, is in incredible demand. And we think the potential there is huge.

At the same time, Ping An has hundreds of thousands of agents selling across China. So, for us, this is a key strategic requirement.

We built a product, as I said to you before, the CHP product. We rolled out Vitality. That's a very comprehensive base, I believe, with partners like Adidas, Sinopec, offering cheaper fuel; some of the learnings we had from Discovery Insure.Travel benefits. We've done a whole range of things to pivot it.

And very importantly on the right-hand side, we have developed a product that's not inexpensive. But if you manage your health, on the right-hand side, you can see you can get a lot of your money back. You get all of it back, in fact, if you don't claim and you, in a sense, get the Vitality benefits out of it.

So we're trying our best to interpret the kind of healthcare needs of individuals. But, at the same time, play to the desire of people getting money back out of their product if they don't use it. And so I'd argue it's embryonic. But I think we're quite excited about what can be achieved.

So we have refocused the business; number 1 in the high-end market. We set a very clear goal of getting to 100 cases a day in the individual market, penetrating the Ping An health distribution channel. And I'm excited by what I think has kind of got to first base. And I think the team feels a sense of confidence of our ability to grow.

Let me make another point that, for us, is very important. At the outset of the Ping An relationship we tried to acquire 25% of Ping An Health. We couldn't quite do that; we got to 20%. But we agreed with Ping An that, if it became possible, we'd like to buy up the additional 5%. It was an agreement in good faith to do so.

I'm very pleased to tell you we're in the process of acquiring that 5%. We've agreed all the terms of Ping An. We're just waiting for regulatory approval by FIA and from the

Chinese authorities. So, essentially, I think it's a done deal. We're going to move up from 20% to 25% of Ping An Health. We're going to push particularly hard in the year ahead to get to our goals.

Let me turn to Discovery Insure; fascinating business. I think a very exciting six months. I've made the point many times about the scale of new business. We invested ZAR100 million into the business over the six-month period. You can see we invested ZAR74 million in the previous period.

It's largely in line with plan. The one factor we didn't factor in was the most ludicrous hailstorm on one day in October, on October 20. This is our claims register, how it looked; ticking along quite nicely and suddenly one of the worst hailstorms ever. I know that, from a short-term insurance industry, it has been one of the worst storms in 30 years, as you can see some of the research that we've done. So this massive spike in claims, that cost us ZAR20 million in the process; that's the nature of the business. I'm not overly concerned about that.

But the business itself is developing nicely; if you look at the new business, climbing very strongly half-year by half-year. You can see that we launched the business in 2011. It had a very, very fast start.

We spent the first part of this calendar year, of the 2012 calendar year, restructuring the product around Vitality, how it integrated with Discovery Insure. It took us a couple of months to get that right. We flattened out during the period. We weren't as much above the line. We weren't marketing much. And then we put our foot on the gas. So to speak, in the second part of the year.

During this period you can see the rapid growth in new business. And the business is growing quickly. You can see the in-force premium income is approaching ZAR0.5 billion now. So the business, really, I think is gaining scale very quickly. We estimate at a run rate we're catching close to 9% of the market. And I think we're excited by the potential.

Something that I think is very important in this market, when we're setting out to enter the motor insurance market one of the warnings in some of the research we saw was that often a new player gets selected against. The people that leave the existing players and move to a new player tend to be the worst risks that have been priced out. And therefore, you can get this massive bad run on the loss ratio.

We're not seeing that. We're seeing quite the opposite. We're seeing quality clients. If you look at the distribution of our client base, close to 60% have three or more Discovery products. We are tracking Discovery disciples, to an extent, into Discovery Insure. And I think that that means that the value should be good going forward. And we're focusing very hard on that.

The other point I'd make is that really the distribution channels are really embryonic. Close to 80% of the new business is from almost a direct process. Our broker channels, we're building very, very carefully. We don't want to work with a channel where we give away the underwriting pen, we lose the administration. That's a very important Discovery principle. So we're developing broker leasing channels to use our existing broker network. That will take us some time. But I think the potential is quite remarkable.

If you look on the right-hand side, our estimation in embedded value between these different channels is stark. So we're focusing hard, investing a lot to build out that broker channel in the right way.

But I do need to tell you we are learning a lot about how to make people safer drivers. And that's the core proposition behind Discovery Insure. Our global vision has created a nation of safe drivers. That's what we're trying to do. So we're tracking people, incentivizing them. They come in at a neutral level. They can go to the advanced level and they get 50% off their fuel if they do the right things. It's remarkably powerful.

And the way people change their behavior is quick. So what you're seeing is by duration, over 17 months the distribution of people from the base all the way to advanced. And you can see how people are getting better over time very quickly. Our death rate, the fatality rate for motor vehicle accidents we see is a fraction of the national average.

I do believe, with these kind of incentives, with the structure, you have the ability -- forget about loss ratios and profitability; we can change people's behavior and make them better drivers. And that's the desire behind Discovery Insure.

What is very interesting as well is the technology we've built has unbelievable applicability. So we're tracking every single driver, as you can see, around, in this case, Johannesburg. And what it gives us the opportunity to do is some strange things.

So some of the learnings we had in that hailstorm is we know where people are driving and when. And, at the same time, we have access to the weather systems. So if you superimpose the two, what you see on that terrible day is a storm descending on our cars; terrible sight. But we can match the two. And that's what's exciting.

So what we're doing now is building the technology to be able to actually SMS individuals, based on our weather predictions, based on where they're driving. And warn them; move out or go under cover or whatever. It's good for us and good for them. No one wants to see their car destroyed in a hailstorm.

So it's these kind of permutations, of having that embedded technology, that give us such incredible opportunity.

In addition, I might have mentioned this before. But we're trying to bring the whole loop into the Discovery Health world as well. We track people how they drive, their g-forces. We know the statistical distribution of our people driving individually. We're developing a lot of statistical methodologies to do that.

And so we know if the g-force is out of range, probability is they've had an accident. So we can reach out to them. We can dispatch an ambulance to them, because we know they've had an accident. It's quite remarkable.

And then some technology we're in the process of developing, we've just sent out, over the last number of months, these new Discovery car stickers with a QR code per individual. And the idea, we haven't quite got there yet, is that paramedics, at the point of the accident, just simply use their smartphone, the QR code and all the health records of health ID appear on their phone.

So we can dispatch help immediately proactively. We can get at the point of care, from Discovery Health, all the health records, all the issues about that individual. The opportunities, I think, to save lives and to make differences is limitless. So the real potential is there.

So the business really is embryonic and I think the potential is quite remarkable. So we're excited and I think we will continue to invest. I see that business taking a number of years to get to scale.

Let me turn, then, to the big businesses in South Africa; Discovery Health and Discovery Life. I think Discovery Health and, by implication, the Discovery Health Medical Scheme, performed unbelievably well over the period, no matter how you cut the data. The new business was robust off a very hard base; up 9%.

The lapse rates inside the Discovery Health Medical seem remarkably low. They have come down further to 3.2%. So people are joining us in big numbers and they're not leaving. I don't know a health insurance system anywhere where you have lapse rates of 3%. If you look at the UK or the US they're typically 15% to 20%. I think it's remarkably sticky. And the function of new business and low lapse rates means that our very large base of members has grown by 6% in total, period to period.

Discovery Health itself grew its operating profit by 12%, despite a cut in administration fees by ZAR70 million over that period. And if you look at the Discovery Health Medical Scheme, the performance has been remarkable. It continues to grow in terms of its membership.

And amazingly over the last number of years that rate of growth has tended to escalate. The reserves built up inside the Discovery Health Medical Scheme for its members is now topping ZAR8 billion. It's a remarkably strong entity. I don't know how many corporate entities are out there that have ZAR8 billion -- no liabilities, over ZAR8 billion in cash or near cash sitting in the Discovery Health Medical Scheme. If you compare it to the absolute quantum of our competitors, it's awesome.

So the Discovery Health Medical Scheme I think has done remarkably well. And done remarkably well for its members. So, in every respect, I think the system is very, very strong.

But I must say to you. And at every presentation I need to make this point, given our scale, our responsibilities collectively are not just for our members; we have to build a better healthcare system for all South Africans. So we are strong supporters of the NDP. We're strong supporters of plans to evolve in NHI. We think that that is fundamental. We think that that is a plus -- a responsible and robust execution of NHI is fundamental for our country.

And as an organization, Discovery Health is working very close in every respect. We're part of the pilot projects. We've got our people working on data, on groupers. Some of the systems that we use we're trying to make available. I think we can add real value.

At the same time, Discovery Health has been very active in forming a social contact, together with many actors in the private sector. And with government and the Minister of Health. And I think the opportunity to use that that contact is remarkable in terms of building the system.

Having said that, I don't believe that the NHI is going to be disruptive to our core business model. It would be fantastic if, as a country, we could afford to provide healthcare for everyone. But we can't. And so, from a business perspective, from a strategic perspective, we are focusing on building our industry. And we need to do that.

It's important to say, getting back to the trend that I said at the outset, healthcare inflates. And that's our challenge. It's very, very difficult. We have a shortage of doctors, as you can see from here to other countries. And, if you look over time, medical inflation's outstripped other industries. It forms exactly the Baumol effect I spoke about at the outset in our country. And it's our role, with every fiber to fight against that. And to make healthcare affordable to our customers.

But it must be said that our system is remarkably stable. Despite all the noise about healthcare inflation and all the difficulties, people are not leaving. As I said to you before, the lapse rate has come down. Our lapse rate for the calendar year 2012 was 4.2%. In the last six months it was down to 3.2%, as I previously showed you.

The other measure I think is critical to look at is the buyer buy-down process. If people find healthcare completely unacceptable they would buy down their benefits to exit. But they're not. If you look on the right-hand side of the chart, 94% to 95% of people are constantly keeping benefits unchanged and a further 4% or so have tended to buy up, if anything.

So the system is remarkably robust. And I think that gives us confidence to say that we have to invest considerably. So despite all the noise, we believe strongly we're an industry that's likely to grow; and there is nowhere to hide. We have to be excellent for our customers. We have to be excellent for the Discovery Health Medical Scheme in a sense in every regard.

So if you look around this virtuous cycle, we know what we have to do. We've got to minimize costs for our members. We've got to maximize benefit. We've got to make sure that the healthcare system is excellent, improve the patient journey into the system. We need to be able to give a promise that, if you're covered by Discovery Health and the Discovery Health Medical Scheme, you will be healthier; that's what we have to do.

And then importantly in the bottom left-hand side, we've got to build a healthcare system for all South Africans. And we need to run around this wheel continuously. There is no compromise. And I would argue in the period under review, I think we've done remarkably well.

In terms of the administration fees we continue to drive them down. You'll see on the right-hand chart, they're around the 15% level, we brought them down to close to the 11% level over the last number of years. And I think we can get to the 10% level, which is an important milestone, in the next two or three years. And I think we see that as a reality.

Amazingly, in the left-hand side we often get these debates about the value for money of the administration fees. We've done a lot of studies around that. And we can illustrate strongly that the fees journey to 2 to 1 ROI in sense, ignoring the administration the kind of the effect on healthcare all the issues on growing the scheme, etc., etc.

And I'll tell you something that's very, very interesting. I think we are doing reasonably well. We can always do better in terms of keeping costs under control. We're fighting hard in every respect across every single discipline. And if you look on the left-hand side of the chart, what you'll see is our rate of inflation across hospital costs, specialists' costs, wherever you look is dramatically lower than our competitors.

On the right-hand side of the chart what you'll see is the rate increases over time. Our rate of inflation is around CPR plus 3%. Our competitors tend to be CPR plus 4% to 5%. The cumulative effect in that is dramatic. Our analysis shows that benefit-for-benefit now Discovery Health Medical Scheme options are 15% cheaper than our competitors. That is very, very material. So I'd say to you working hard in every respect of the healthcare system to bring prices down to bring inflation down. And I think we're getting on top of many that we need to do, we need to keep fighting there.

But it's interesting, when you bring together this debate about administration fees in healthcare costs you get a very interesting dynamic. If you look at the healthcare costs of our competitors. And you set them at 100 units or 100%, we estimate that per unit to benefit we're 15% cheaper.

In other words, what costs our competitors 100% costs us 85%. If you then bring together the administration fees, you'll find when you add up our healthcare costs plus the administration fees, we are still less than our competitors. And I think it's a very simple way of seeing the return on investment of the Discovery Health Medical Scheme is getting from that process.

If you then look at the administration fees that our competitors have to add you get a difference in exit price. And it's that difference in exit price that's creating, that's sucking sound to an extent, that really is driving the new business and holding in the lapses. And I believe, given the sophistication, the continued investment, our ability to do that is very, very real. So I think Discovery Health is pushing hard on the cost side.

In the case of benefits, we are focused hard on increasing benefits. This is a very difficult battle to win out there in the hearts and minds of people. People perceive benefits based on limits. What's the spectacle limit? What's the limit on this? What's -- and there are those limits. We acknowledge it. We have to fight hard to lift those.

But the real actuarial view of benefits is per unit of sickness, how much are people getting out of the system? So things like oncology, biological drugs, scanners, all the technology that drives up cost, if you look actuarially, we've increased benefits by 10% over the last number of years. We plan to do that, going forward.

So we're focusing very hard on not skimping on benefits. And making sure that the promise of Discovery Health and the Discovery Health Medical Scheme is, you get access to the best-quality healthcare. And we need to do that at the same time as controlling costs.

We would argue -- and it's a point we made at our launch for the 2013 year, we would argue that benefits trumps austerity in healthcare. And therefore, we're focusing very hard to make sure benefits stay real.

You can see on the right-hand side of the chart the cover ratio. Hospital costs, what percentage are covered by the Scheme to the claimants. In the case of a heart plan it's close to 100%, even in the case of the less expensive plans 96% to 97% are covered. So I think on balance, benefits we are doing relatively well. And we'll continue to do so.

At a previous presentation I spoke about the patient journey. And this is a very, very exciting opportunity for us. We brought out this fantastic piece of technology for HealthID; it really puts on an iPad, for doctors, everything. So when patients of the Discovery Health Medical Scheme come to see them, they have all of their patient records. They can scrip medicine. They can see everything. You can look at pathology results.

We've had tremendous take in this regard. You can see that nearly 100,000 of our members have already given their doctors consent to use it. On the right-hand side you can see in the last number of months the number of doctors. We estimate 15% of doctors who should be using it are now using it. We're going to drive that up, going forward. So we really are trying to digitalize the healthcare system. And I think that provides a fantastic opportunity.

At the same time, what we've done over the year. And we launched into the 2013 year, is made available a whole set of technology for our members to use. So effectively, we made the health plan actually exist, to an extent, on an iPhone.

The idea here is to try and get away from this very clunky idea of phoning up your medical aid. And claims being submitted. And making a health plan exist here, that's where we have to go. So the technology platform that we're trying to create is not only at the doctor level. But at the member level as well.

And I think the power of this is quite remarkable. I wanted to show you this. In Discovery Health, just to show you a few things, I don't want to waste your time. But there's some really powerful things that you can do.

The first is as an individual, you can see your health records. You can just page through, through any date, like a carousel, see what you saw, who you saw. So everything is there for you; your entire health record is kind of dumped into this capability.

You can if you want to submit a claim through the 'phone. So I select a patient, in this case I'm John Smith. And I have a claim in paper, I want to submit it. What I do is just take a photo of it, just take a picture of it, excuse my poor photography, saving photo. And I submit it. It's gone. It's in our system.

So it takes away the hassle factor. And then you can do things that I think are quite remarkable. You can -- if you want you can buy medicines through our courier system in a way. So if you really have a -- in this case a re-order of Cataflam that this person has, I must just get the details which are already in there; confirm it. I want it in the morning. Submit it; gone. And through our Medical Scheme system it will be delivered.

So moving the health plan onto the 'phone. And I think the potential of that is quite remarkable. Now, even things like Medical Scheme details, what you can do is have your membership card on the 'phone. So you go and see a doctor, it's all there, etc.

So to an extent that digital interfaces as I think we've managed to create for doctors, with HealthID. And the ability for patients and members to use this kind of technology's getting rid of the clunkiness of the healthcare system.

And I'd argue beside obviously the convenience factor, it makes people healthier. The ability to really, at the point of care, give the caregiver all the information, the client is better informed, as everything on his or her desktop or phone has fantastic potential.

And we're pushing this a lot further. One of the initiatives we're busy with now, it's an amazing opportunity. See Discovery Health and the Medical Scheme's big enough to straddle the healthcare system. So a lot of the telemetry that's coming out, we have the potential, in fact, to execute across our client base.

We have, for example, 55,000 diabetics inside the Discovery Health Medical Scheme. Making sure they're compliant, making sure you know their readings, is a critical issue. So what we've done now, we have a pilot running with these telemetry devices that a pilot test has, when they check their readings goes through their 'phone, like this. And it comes to us and to their doctor.

So quite quickly over time the doctor through their HealthID will be notified continuously of those readings. And if they get out of kilter. We're going to be running that out of the whole diabetic basis and other conditions will follow. So this suite of technology has the ability to really drive the quality of care. And I'd argue that's where we're focusing on.

And then the final point of the wheel that I showed you is building the healthcare system; we are intent on making sure that the South African healthcare system is excellent. So the Discovery Foundation currently has about close to 200 recipients of grants, of excellent doctors specializing in the right kind of areas. That's 4% of the specialists in our country. We need to do more of that.

We're doing things like working with Murchison Hospital of trying to bring super specialties into the country, educating our best people at places like Harvard and bringing them back to train the trainer. We have the ability to build a healthcare system. We need to do that.

So I would argue, in the context of Discovery Health, the performance is strong; that our responsibility is much more macro. We have to control costs. We have to maximize benefits. We have to improve quality of care for doctors and our patients. And we need to build a healthcare system. I believe that's a reality.

Let me end off with Discovery Life. I've taken much too much of your time. But I think Discovery Life performance has been very, very pleasing over the period. New business grew by 7%; the revenue grew by 18%. But you can see the quality of the business. Operating profit growing by 17%; and the value of in-force growing over ZAR16 billion, by 28%, really reflecting a lot of progress made in a number of areas. It's interesting that the new business grew by 7%; we'd like it to be higher. It's off a very high base and 7%, I think, is robust.

But we were slightly late in terms of getting new products into market. You can see if you compare this period's new business, in terms of the bar charts, to the previous period, in terms of the straight line, once we got our new products into the market, you can see that things started to escalate. And many of the structures in those products we're going to try and bake in, over time. So we grew by 7%, new business. But I believe we can escalate that, going forward.

The real story of Discover Life is the quality of the model; it really is fundamental. It's integration with Vitality, the ability to bring prices down, the ability to dynamically price with dynamic rate indicators, through Vitality, means that we have better benefits, lower price, more dynamism, better lapses, lower mortality. And that's exactly the progress that I think we saw in the case of Discovery Life.

Lapses have come down dramatically, as you can see. The mortality experience continues to outperform expectations. I think that's remarkable.

In the middle of the chart what I'm trying to show you there is the embedded value assumptions of mortality. As you can see in the gold line we keep bringing it down. And the actual performance in the blue line. So we keep outperforming and reducing share. We're better -- we're increasing hurdle around mortality. And I think that's important.

The lapse rate performance is staggering. We went through the financial crisis with an elevation in lapse rates that's come down to the lowest levels ever. And the effect of that is positive experience variance. So you can see on the right-hand side Discovery Life generated nearly ZAR300 million in positive experience variances; dramatically higher than any period in the past. So to an extent, I would argue that the virtual cycle of how the model works is paying significant dividends in the context of Discovery Life.

The other point I want to make. And some work we're starting to do, is about life expectancy. I've made the point we're here to make people healthier. In the case of Discovery Life, it's difficult to strip out selection from behavioral change. But if you look at the experience what we've seen, it's quite remarkable.

South African insured life expectancy is about 67 years; we're seeing ours at about 80. And people inside Vitality -- policyholders in Vitality are typically 82 to 88 years old life expectancy; it's remarkable. So if you're a Gold or Diamond Vitality member with Discovery Life, our expectation is you could live to 88. And we're trying to understand the drivers and causality of that. That's just for -- to our core purpose again about what we're trying to do.

I want to end off with a very important point about Discovery Life. We've made the point, over many presentations, that we invest a lot of capital in Discovery Life. It's a fantastic investment. The returns, we think over time, will be tremendous. It's a better mortality which we believe in, very strongly. But I think one of the critical things about Discovery Life is it's throwing out a lot of cash. And in fact, the business in total, despite the new business, is cash flow positive.

So what you see if you actually go through the cash flow progression over the six months, Discovery Life attracted about ZAR3 billion of premiums. In terms of claims and reserves, they have consumed about half of that. You can see expenses and commission further amount, leaving just ZAR1 billion in cash that's been generated by the existing block.

We then invested, just progressing it, about 80% of that into new business, into the new business strain, leaving about ZAR200 million thereabout as free cash.

Our belief very strongly is that investment is worthwhile. The margins inside the Discovery Life new business are remarkable, about 10%. And in fact, they've gone up to 10.6% over the period. But the point I'm trying to make is the Life businesses is about throwing out cash. And I expect it to grow, hopefully, strongly, going forward.

We're using that cash to build Discovery Invest and to build other things in the Group. But I think the Company has performed remarkably well. And that's it on that.

Let me wrap up by saying, I think it has been an excellent period for us. I tried my best to illustrate the context in which we operate. It's a global context in which I would argue that our business model is actually directionally perfect and fundamental.

I said to you that we're trying to build the best organization, globally; I think we can do that. Our Board and our Company has articulated that, in terms of methodology, return on capital, diversity, the effect on society and I think we have the ability to do that. And I'm very confident that we can continue to grow at this rate, without recourse to capital.

Let me end there. And just thank our staff, our people, the 11,000 people that work in Group, who've done a remarkable job over this period.

I appreciate you listening. And we have all our executives here for questions. I'm going to ask Ricky Farber, our CFO, to come up and join me. Thank you, very much.

Questions And Answers

A - Adrian Gore {BIO 3068929 <GO>}

If you're okay, I'll just direct questions. If we go here, where's the mic? Just wait one sec. Sorry, I missed.

Q - Mike Christelis {BIO 15233664 <GO>}

Mike Christelis, UBS. Just one question, if I can? On your PruProtect business, clearly gender neutral pricing coming in towards the end of December provided a boost to sales. Can you give me a sense of what the January and February to date run rate looks like? In other words, how much of that is just an acceleration of January sales into December? And how much is actually being boosted by things like the change to RDR, etc?

A - Adrian Gore {BIO 3068929 <GO>}

Herschel, do you want to comment on that? Just wait for a mic there; there we go.

A - Herschel Mayers {BIO 3614988 <GO>}

Mike, as Adrian showed, the December number was dramatically up; January has come down a bit; and February is starting to pick up to normal rates. So overall, it was an acceleration. But I think that the average increase is probably 5%/10% above previous values.

Q - Mike Christelis {BIO 15233664 <GO>}

Herschel, it's not clear, because you would expect males would wait to buy insurance as parts are going down. So the dynamic is not clear; interesting.

A - Herschel Mayers {BIO 3614988 <GO>}

Well, there were obviously two factors. It was the gender neutrality changes and the tax change, which increased prices by about 10%/15%; just because of a tax change.

A - Adrian Gore {BIO 3068929 <GO>}

A question over there.

Q - Brian Mushonga {BIO 16209522 <GO>}

Brian Mushonga, Credit Suisse; two questions. If there was a return to collective bargaining of medical schemes, versus the hospital groups, do you think you'd still be 15% lower on costs? That's the first question.

The second question relates to the additional investment in Ping An. Could you just remind me if that's on the same terms as the original investment? And I guess, maybe related to that, who actually owns the hospital that you showed in the pictures? The Chinese Government, I assume so.

A - Adrian Gore {BIO 3068929 <GO>}

Barry, do you want to deal with this? Maybe the Ping An question first. And maybe, Johnny will you talk to the --?

A - Barry Swartzberg {BIO 3296824 <GO>}

Most hospitals -- I'm assuming that hospital question on hospital is government owned, including the VIP ward. And there are private hospitals. But they are not of that scale in the market.

In terms of the premium that we paid, we paid about a 20% premium on the original price.

A - Jonathan Broomberg {BIO 16688888 <GO>}

Brian, on the centralized bargaining, it's a complicated issue. The first point to make is that it -- to the extent that we ever get there, it may apply only to individual professionals, rather than hospitals and corporates. But assuming it applied to everything, I think there is some chance that the pricing advantage we have in the hospital space would be narrowed. We would expect pricing to come down towards our level.

But I think it's critical to understand that that 15% lower cost of healthcare that we see is made up of many different parts. Pricing advantage in the hospital sector is an element. But we have price advantage in many others areas.

And, more importantly, we have different pricing structures, alternative reimbursement, which would not be impacted by collective bargaining. And we have a wide range of risk management tools and assets, fraud and forensics. And a whole lot of other areas that contribute to that gap that wouldn't be impacted by a narrowing of the pure price gap.

Q - Brian Mushonga {BIO 16209522 <GO>}

Excellent.

A - Adrian Gore {BIO 3068929 <GO>}

(inaudible).

Q - Unidentified Participant

(inaudible) I have a few questions, please. Firstly, regarding your proposed additional investment in Ping An of a further 5%. Some roughly two months ago it was announced that HSBC had sold their, I think, 10% share, I might be wrong with the percentage, to a Thai tycoon; I had to get that in.

A - Adrian Gore {BIO 3068929 <GO>}

Is that a stutter? (Laughter).

Q - Unidentified Participant

Does this in -- I would think that this in no way concerns you, given that your proposed additional 5% purchase came after the announcement of HSBC's sale.

A - Adrian Gore {BIO 3068929 <GO>}

No, no, it didn't concern us. Obviously, Ping An. And its ability to succeed is important to us. Ping An's strength in China, I think, is remarkable. That particular transaction, I think HSBC was trying to offload that for a long time and that whole complexity around that particular transaction is nothing to do with operational integrity of Ping An. So to speak. So, it's not an issue.

Q - Unidentified Participant

All right. Now, you referred, a number of times. And quite correctly, to. And justifiably, about the amount of cash that's been generated. Your last few slides highlighted this. However, it's only when one looks in some detail at the balance sheet to see what extent this has impacted. And I think I need to ask Mr. Farber to give me the secret of how the equity securities level has increased in six months, by 165%. The increase is of the order of ZAR8.5 billion.

Now, we're all aware that the stock markets worldwide have done particularly well in this period. But an increase of 165% is something staggering. Does it also include an adjustment for currency movements with the weakening of the rand? Or have you just purchased the right shares all the time?

A - Ricky Farber {BIO 5884718 <GO>}

It's a little bit of luck and the right shares. But fundamentally, you have to understand that there are two pieces sitting in there. The first piece is what we call available for sale financial assets, that's the shareholder funds. And that has gone up. It went up from ZAR5.3 billion to ZAR6.1 billion. So an increase of ZAR800 million over the period.

Now, Adrian spoke about the cash we generated. And that cash ends up in the money market instruments and the big part of that driver is that.

The second bit is the currency that you spoke about. And then a little bit of the rising market and the right shares.

To be fair, we don't have a great, or a large equity exposure relative to, I guess, what we would have liked over this period. Our investment style is much more cautious. And particularly because a fair amount of the equity is sitting supporting the UK business, which hasn't had the same stock market performances as we've had here.

The other bit. So the balance of what's now ZAR26 billion. So ZAR20 billion is sitting in policyholder assets. And fundamentally, that's the money that we get from Discovery Invest policyholders. There, the biggest driver is really new products that we've sold. And our policyholders benefitting from gray markets.

So we're pleased to say that, that equity security is the biggest part of that increase is for our policyholders. And the performance of the Discovery equity fund has been quite good. And the overall investment return that it had over the six-month period has been great.

Q - Unidentified Participant

Income statement there are two items I'd like explained a little bit, please. The first one is the item net fair value gains on financial assets. That is now standing at ZAR1.6 billion; a massive increase from the previous comparable period. How did that come about?

And secondly, also from the income statement, acquisition costs of ZAR1.7 billion, nearly, what is that a reference to?

A - Adrian Gore {BIO 3068929 <GO>}

Do you want to handle that?

A - Ricky Farber {BIO 5884718 <GO>}

The net fair value gains ties exactly back to the point that I just spoke about. That's the gains on policyholder liability. So the money that we hold for our policyholders in Discovery Invest. And that big gain, from ZAR252 million in the comparable to ZAR1.6 billion, is the stock market performance that I spoke about a few moments ago.

The second item which you asked about is acquisition costs. Primarily, that's commission. So we, as a Group, have paid out ZAR1.6 billion commission over this period. It's split -- the two biggest parts are, obviously, Discovery Life in South Africa, which Adrian spoke about;

and then the life business in the UK, PruProtect, where you saw the phenomenal growth in this period. Obviously, that has quite a high commission burden.

A - Unidentified Speaker

Thank you, Mr. Gore.

A - Adrian Gore {BIO 3068929 <GO>}

Thank you. Are there any other questions? We have taken a lot of your time. If you are okay, I'm going to wrap it up. And thank you all, here. If you have questions. Once again, thank you. Greatly appreciate you listening. Thank you.