Q4 2018 Earnings Call

Company Participants

- Adrian Gore, Founder, Chief Executive Officer & Executive Director
- Mike Brown, Chairman

MANAGEMENT DISCUSSION SECTION

Mike Brown {BIO 6995397 <GO>}

All right. So, good morning, ladies and gentlemen. I think everybody's in now, including myself as the very latecomers. I apologize for that. I'm Mike Brown from the Investment Analysts Society. We'll be hosted today by Discovery Limited for their annual results for period ended 30th of June.

This is a presentation I think we all greatly look forward to. And one of the unique things about Discovery is that it's a company that's chronologically and you guys back about 25, 26 years and we listed 18 years. So, many of the founding fathers, the original team, are still here. They started this business.

One of them, if I can just pass a very brief tribute to, is John Robertson who is the Chief Information Officer who's now retiring. John and I went to school together, so I know he is past retirement age. And the last thing John did here was to effectively deliver this building as an operational asset for Discovery to house the entire Discovery head office. So, we wish John a long and happy retirement.

Thank you. Somebody hopefully won't be retiring as Chief Executive Officer, Adrian Gore - and I've - it's a great privilege that Adrian is going to address us this morning on the results of the group, and I'd like to ask him to come up and to thank you on behalf of the Investment Analysts Society and all the other stakeholders that are listening to this presentation.

Over to you, Adrian. Thank you.

Adrian Gore {BIO 3068929 <GO>}

Mike, thank you for that introduction, and thank you to the Investment Analysts Society for the opportunity, and to all of you, thanks for the time. We greatly appreciate it. Maybe it's a good segue, Mike, just to thank our staff. It's been a most remarkable year, and people have worked incredibly hard to get to where we have got to. I get the pleasure of delivering the results, but it really is a team effort of remarkable people. And also, to - just highlighting John Robertson. I think it's an amazing thing to do. He's the most wonderful guy. He's one of the founders and builders of the entire organization. So, this is not his farewell yet, John, wherever you are, but we will celebrate with you.

So, let me get to the actual results. And as you heard, it's for the June 30, 2018, our full financial year. It's been a remarkable year. It's been a very, very complex year. I think it's been a fundamental year in our growth. I think the numbers are fairly clear, strong growth in operating profit, up 17%, new business up 10%, headline earnings up 32%, and normalizing them down to what we think is the appropriate measure, up 16% year-on-year. There's been considerable activity across all of our businesses. And I hope I give you a sense of that. There's just a lot of moving parts, and we try our best to get across the stuff that really makes a difference.

There're really four themes I'm going to try and get across, and this framework is going to follow through the presentation. So, I'm hoping I'm not going to be too verbose. We get across the issues to you. The first I think is context. We set out this 2018 ambition of being best globally. It was a bold ambition. And I think what's important about it is it really reflects where we came from a core purpose of make people healthier. That kind of it over time manifested into, we think, a globally relevant, repeatable model of Shared-Value Insurance model that's unique and very powerful.

And on the back of that, the deep conviction of its applicability, I believe that we could be best globally. And so, we set this 2018 ambition. The truth of it is that strength is in the actual operating models and discipline that I think it put onto us. This was five years ago. And throughout the results, I hope you'll see the context of that ambition and the framework for it.

Secondly, the financial performance has been a particularly strong year for us. We saw operating profit up 17%, normalized earnings up 16%, and we generated ZAR 10.6 billion of cash, we invested a lot in new businesses. All of our businesses are profitable. All the emerging businesses turned to profitability. We earned a return on capital just under risk-free plus 10%, and our experience variances are positive. So, the organization as a whole outperformed the actuarial assumptions. And I'll take you through the financial performance I think in quite a bit of detail through the framework of the 2018 ambition.

The Discovery Bank, I'm going to talk about it to make the point upfront. There's been a considerable amount of work on the bank. There's been a slight delay in it in the context of our licensing approval that was conditional, and I'll tell you now publicly on FirstRand over time moving down their shareholding from 25% down to zero over a five-year time. That was the licensing conditions. We made a decision collectively with FirstRand that they would exit as soon as possible, so I'm here to tell you that we're acquiring the 25% now subject to regulatory approval, and we'll be issuing equity in order to fund that acquisition. And I'll take you through that process and I hope that becomes clear.

And then I'm going to take you through the businesses themselves, the established, the emerging. The new initiatives gives you insight into them. I think the dynamics between them has been quite fundamental and powerful. I hope I'll give you insight. It's very, very difficult given the scale of where we've got to try and cover everything. We've tried our best to look at those (00:05:24) issues and I think and hope are relevant.

At the outset, I kind of thought before we get into strategy and the whys and how we operate, just put the numbers out there in the most kind of naked form. What you'll see is the operating profit up 17% to ZAR 8.3 billion. If you cast your mind down or your eyes down, you'll see that I think there's strong robust growth across the entire group. New business up 10% to ZAR 16 billion. Very good new business growth. There's been a focus on profit. A very strong focus on internal rate of return of new business. The numbers I think are strong. Good performance in the UK despite a very difficult economy. And our three start-ups have grown really, really well. And that's one of the features of – our three emerging markets have grown very, very well, one of the feature of the results.

We spent, as you can see at the bottom of the table, on operating profit, 7% on our new initiatives including the bank, so well within the guidance. But, over time, that, of course, will change as the bank is launched, and I'll touch on that a bit later.

What you see is net cash flow across the business, I think very strong. Our established businesses beside Vitality Life generating positive cash flow. Return on capital, nearly risk-free was 10%. You can see the risk-free was 9.6%. And across the business, I think, a very, very good performance. And experience variances, in other words, how each of the companies in the group performed against the actual expectations, I think very, very positive.

So, we are pleased, I think, overall with kind of how the results and how the group has played out. So, although maybe upfront, just kind of put the numbers out there so you can see it. And I thought it's important then for me to give it a bit more context.

And kind of let me start with the why, the how, and the what. And that framework that is really framed, I think the evolution of Discovery. Our core purpose of make people healthier has been an incredibly powerful kind of North Star for us. It has evolved into this very disciplined Shared-Value model, incentivizing behavior change, (00:07:13) insurance, and that created this virtuous cycle, they're good for society, good for us, and fundamentally good for our customers. And, of course, that is important.

The core capability is at the bottom of the slide, this ability to take the Vitality methodology and to kind of mix it, integrate it within institutional capability to get to the right kind of traction. And then we apply it to a whole range of things: life insurance, health insurance, long-term savings, property and casualty insurance, and then ultimately, of course, banking. And that's the intention.

But to make the point, I think the conviction of its applicability is that we kind of strongly feel that the world is changing. And I think you will have seen this from us many times that I do believe that there's three mega-trends that are really framing what we do. Of course, technology and more of it, whether it's fintech, digital therapeutics, all of the stuff, is accelerating at a considerable rate, so we know that the enabling disruptive issue are technology.

On social purpose, we've been here saying we're here to make people healthy. In early years, it was seen as almost bizarre. But that's become a bigger and bigger thing since

2008. And I was really amazed to see Larry Fink, CEO of BlackRock, sent a note out to the top 1,000 CEOs making the point that they strongly are urging and forcing social purpose on the companies they invest in on the back of the idea that governments can't deliver all that, and of course (00:08:33) private sector actors like ourselves have to do that.

So, there is an increasing push towards companies standing for a social purpose. And I think the great thing about Discovery, our purpose of making people healthier is entirely authentic. That's how we started. We never had a mission statement. That's what we do. And our business model is entirely and totally consistent with that. But it's really the nature of risk that I think is critical. We've made the point, you know this that we're an organization that believes in behavior change. And what's really becoming clear is that in financial services, healthcare, and other stuff that we're involved in, most of the risk is about the simple choices people make and their behavioral biases. And if you can affect that, you can make a real, real difference.

And I kind of wanted to show you this interesting analysis. It's kind of – it's maybe provocative, but I think it makes a point. Now, just to make this maybe strange analog, turns out that the DNA of a human and a pig is actually very, very simple, extremely simple and very similar as far as I know. So, no – no – I'm not suggesting anything. It's a biological fact. But it turns out that there's kind of a DNA strand running through our industry. So, it's definitely as (00:09:42) life insurance is to motor insurance is to banking. It turns out like in health, 4-4-60, four behaviors lead to four conditions that drive 60% of mortality: smoking, eating badly, physical inactivity, alcohol drives four conditions. Cancer, diabetes, lung and heart disease drives 60% of mortality. Turns out those behaviors are consistent across everything: so aggressive driving, harsh braking, saving too late, corrosive spending in the banking space, these simple behaviors have the same effect.

So, if you look at banking, four – our analysis shows that four simple behaviors drive 90% of defaults: semi long-term savings, semi-motor insurance. So, as different as these things are from a human to a pig, there is a very similar DNA strand that's running. I wouldn't say which one is a pig incidentally. I'm just going to – (00:10:30) taking this analogy way too far. But just to make the point that the behavioral piece drives a huge amount of the risk, and in fact increasing amounts when it comes to long-term savings and to banking.

And so, this interpretation of make people healthier, make them drive safer, make them manage their money better, et cetera, is entirely consistent in a pure play, a purely authentic play on the core purpose of make people healthier. And you'll see throughout the presentation – I hope I get it across – that this virtuous cycle is true in every single case because we are completely aligned with our customers, right? We monetize better behavior, better decisions. So, if customers make their decisions, we are more profitable, we can find the incentives. So, we have this ability to kind of circulate this model. So, it really is a consistent simple play.

So, when you look at the results of Discovery, I think you need to be clear that in fact it's entirely a consistent adjacent move, but it's exactly the same DNA strand, exactly the same model. As soft as it sounds, it has a hard edge actuarially. So, if you look at this from a kind of a veer and weave (00:11:31) point of view, or a margin point of view, the effective Shared-Value of this model is tremendous. It creates a sales effect, so we get an uplift in sales. Critically, it creates a selection effect, the kind of people that buy products like what we're doing (00:11:46) which is important. There's a behavioral change once they're with us. They behave better. And then critically reach people often as I understand the selective lapsation effect in our industry is critical. Most insurance, the better lives tend to scatter and you keep the worst risks because their lives tend (00:11:59) to see value for money. In our model, it's quite the opposite.

The lives that we're engaging tend to stay and the lives that aren't tend to leave. And so, you get a positive selective lapsation cycle. And this table comes from all of our different bits of data, but just to make the point, if you get the model right in the life insurance space and give you a double kind of value of new business, your margins in health and property and casualty insurance are dramatically high through a lower loss ratio. And the semi long-term savings, VoNB's dramatically higher if you get that right.

So, to make the point that our conviction kind of comes from the soft idea of make people healthier, but it siphons through a much more disciplined environment to one that actually translate actuarially into better value for us and, of course, bettering lives for our customers. And so, on the back of that, we set this 2018 ambition.

I've shown this to you before, and I'm not going to be laborious with it. But it's based on the hypothesis that we can attract the best people according to a set of values, technology capabilities, they will build great businesses on the back of this Shared-Value model in life, health, and other, and that will flip into an impact ZAR 10 billion of pre-tax earnings, growing our earnings by CPI plus 10%, achieving a return on capital of risk-free plus 10%, and touching 10 million people through the Vitality program, and that's what we've set out five years ago.

I think you will see through the presentation, and I hope it's clear we still have six months to run, we're actually fairly close to achieving this ambition. I believe we're going to miss it in certain areas, I think we're maybe too South African. We haven't globalized quick enough I think to claim the relevance I think we need to do, but we're well on the way. And I think this ambition has proven to be remarkably – how can I say – just instructive as in setting up exactly what we need to do.

So, let me deal with the financial results, and I'm going to deal with them in the context of this third dimension of the financial and social impact of the organization and just bear those metrics in mind. And, over time, we've developed, I think, a pretty sophisticated and disciplined model around growth, cash, and capital. And the important point to say at the outset is, I think we are quite unique in the fact that we've build our businesses organically. It doesn't mean that we can't make acquisitions but, simply put, I think intellectually if you have a unique model like ours, we're having it figured out how to do it into a back-book, we're working on that. But, in truth, this is about building businesses from the ground-up, building anew according to this basis and, therefore, this is an organic model.

So, if you accept, then let me take you around the cycle so you'll see what we're trying to do. On the left-hand side is the growth model, businesses start new. Over time, they become emerging. Over time, they become established, and we've metrics for those. We see that phasing typically five years and another three to five years. That's what we see. (00:14:36) To build an institutional business, it takes five to eight years in our experience, and that's what you get.

The growth, what we spend is - (00:14:39) our earnings should be 90%, 20%, minus 10%. Now, those established businesses should be 90% of our profit, the emerging 20%, and we spent 10% of our profit on funding new initiatives. If we get that all right through the relative growth rates, that should spell out a growth of CPI plus 10%. That growth funds - or generates cash and we invest that cash in tax, dividends, finance cost, but then in new businesses. And kind of intellectually, we should fund as much of it as possible at the right rate of return provided we don't breach our risk parameters, and that's really the model.

So, that leads to the capital model which is made up of four components: regulatory capital, making sure that all of our entities are soundly capitalized; allocated capital, making sure we can wind through five years of growth without recourse to additional capital; the use of debt and its quantum; and then a buffer of cash at the center that can be there to manage growth.

And the two - if we get that right, we should run (00:15:34) risk-free plus 10%. That's the target. But the two critical kind of controlling variables are at the bottom. The leverage should never exceed 28%, and that was that financial leverage ratio should never exceed 28% if insurers hold a buffer of ZAR 1 billion to ZAR 2 billion in cash at the center. If you accept that this kind of washing machine, we call it, should spin around and we should do it as fast as we can provided we don't violate those two kind of optimizing variables at the bottom of leverage and cash at the center, and that's really how this model has been played out.

So, the central question, of course, then is how have we done. So let me deal firstly with the growth engine and go through the numbers kind of with you. Very quickly on new business, you can see it's grown 10% on the previous year. If you kind of look at it graphically, it's actually not unlike previous years. A few comments to make, firstly, Ping An at the bottom. We used to show it as 100%. We only own 25% of it given its scale, we now show 25%, which you can see it's growth is staggering at over 80%. Really it's growing quickly.

The Vitality Group above that showing 2%, but in fact that includes our U.S. corporate business. When you look at the partner market, that's growing at 40%. I'll take you through that later. So, those two for us are really strong growth areas. The rest of the growth I think has been strong. I made the point about the UK growing nicely in a very staggering market. Discovery Life, the individual business grew by 3%. It was a focus on profit, on quality, and I'll take you through a lot of that later.

And then Discovery Health continues to grow nicely despite the scale of the base. I think the robust growth in new business, if you look at that and combined with the back-book, we had a kind of a target of 10 million. Today, we cover close to 18 million lives across the globe. You can see how they're made up of insured lives, Vitality lives giving you a total of 18 million, and you can see them across the various countries.

I'm quite proud of the fact - I think the team has done remarkably well, that we cover 1.1 million fully insured lives in the UK. So, that business really is getting I think considerable scale. You can see the rates of growth in China in Ping An, quite amazing and then the Vitality Group approaching 1 million lives. So I think the growth has been fairly strong.

Let me turn to the operating profit, up 17%. The performance has been, I think, excellent over the period. If you look at the various businesses and the growth, it's just strong and robust across all of it. For the first time, all of our emerging businesses have flipped to profitability. The established businesses are a ramp of ZAR 8.6 billion of profit, as you can see, and has grown by 14%. So, a very strong growth in the rate of - in the established businesses. And then I made the point that we spent about 7% of earnings on new starts, et cetera. There's more spend on that. What's coming through, of course, is as you capitalize a lot, it doesn't come through the income statement yet, but I'll touch on that a bit later.

We thought may be appropriate on the right-hand side to break it down - I'm not sure if this is instructive - by industry, by business unit, by growth model. You can see what it shows. You can see Discovery Health at the top, (00:18:37) less than a third of the earnings, I think. You can see by industry: health, life, property and casualty, the growth is actually quite strong across the board. And, in fact, they're kind of mixes of start-ups and whatever, so it's hard to draw conclusions, but I think that is pleasing. And then, the growth model itself, the existing businesses are growing at CPI plus 14%. That has implications, and I'll touch on a little bit later.

Maybe just to just reconcile some of the accounting stuff - Deon, our CFO is with us. So, any questions later, we will be here to take. But profit from operations, I've made the point, up 17%, just under ZAR 8.3 billion. If you take out finance costs and some other issues, you get profit before tax up 28% to ZAR 7.4 billion, after-tax and a few other issues, headline earnings up 32%. We normalize out the - there's been a considerable deferred tax asset that emerged as the businesses turned to profitability. (00:19:30). So, taking that out brings that 32% down to 16%. As we published it, we're declaring a dividend today of ZAR 1.14 per share, up 16%, very much in line with the increase in normalized headline earnings. So, that is kind of the - a recall of the headline earnings down to the normalized headline earnings and the dividend declaration.

I want to just touch briefly on the building we're sitting in. It has been really good for us, I must say. Our people I think are motivated. We've got a fantastic deep space. I think the culture is working remarkably well. This is not a group of separate companies; it's an integrated organization. We like people to see each other, work with each other, be integrated, and I think we've done well doing that. But, of course, the question is how much does it cost, right?

And what I want to show you here is, in fact, in the accounts we've taken I think the appropriate approach. The accounting standards now require a finance lease accounting approach. So, in effect, what you're seeing on the chart there is the green line is the cash cost of the rental, right? So, kind of the monthly cost of the building. What the accounting standards do is require to – account for it as if you've acquired the building and you're depreciating it over time. So, you kind of get a lease cost that's made up of interest and depreciation.

So, in the accounts, we've actually taken the finance lease accounting, and that's what we've got in our normalized headline earnings per share. So, to an extent, there's a significantly higher charge than the actual cost of the building. It's fairly flat and comes down. So, we're over penalize us (00:21:02) in early years, but in the later years, it will actually be a boost to our operating profit.

Why is this relevant? Well, it is relevant because I think when you compare one year with the other, it is important to understand that in the previous period, we're in about five or six buildings with old leases, et cetera, et cetera. We moved all of these – everyone into one massive building and flattened out the rental cost. So, it's a pretty penal approach. Our board had quite a debate around whether we should normalize (00:21:29) compare like with like and decided not to do that, because if we did that, every year, we would have to normalize, and that didn't make sense.

But just to show you the reconciliation, our headline earnings is up 32%. I showed you right at the bottom, our normalized headline earnings is up 16%. So that includes this flat line (00:21:43) treatment of the rental cost. If you looked at the actual rental cost in the green, it would have been a 20% growth year-on-year. So, comparing like with like, you do get a 20% growth, but we're not going to show that. We've settled on this accounting convention, and that's what we will show, and so you get the normalized headline earnings up 16% year-on-year.

So, let me just wrap up on the growth model, making the point that headline earnings – sorry, that operating profit is up 17%, trying to show you how it's broken down. And I think the critical thing to do is to look at it how it's evolved, 7% on new initiatives. Our emerging businesses all profitable, growing considerably. I think the growth is ridiculous (00:22:21) because you've gone from negative to positive, but the growth of the established businesses had been at CPI plus 9%.

And this is an important kind of strategic consideration because kind of the linearity of the growth model is starting to break down. If you've got a ramp of established businesses, nearly ZAR 9 billion in scale, it is largely impossible to have a start-up that linearly grows and makes a massive impact unless you take big bets and do things that have blue-sky potential. And that really is, I guess, the question.

On the right-hand side of the chart in those graphs, just showing you that we're trying to get you 20% of earnings from the emerging businesses. At this stage, they're a slither. They are earning – to be fair, that just turned around, but with small earnings compared to the established. But if you look at it on an embedded value basis, we don't publish an embedded value for our new starts, but an estimated EV that's around 10% of the group EV, so in fact, the value being created is very, very considerable.

And so I'll put it to, this is really where I think the – not a level where I think we (00:23:15) kind of heading is that the established businesses we think are very well positioned. It's about making sure the emerging businesses have real blue-sky potential and investing in new initiatives that really can make a difference over time. And I think with things like the Discovery Bank, Vitality Invest and other stuff that we're doing, we think that is in the belly of the strategy that you will see.

So, the growth model, I think, has worked well. It's generated better than CPI plus 10%, but I'd argue that its linearity is probably breaking down and we need a more exponential approach, I think, to new starts as we go forward. And I do think we are doing that.

Maybe turn to the cash and how we've applied the cash, and we've tried our best here to be absolutely, how can I say, detailed in giving you whatever you need. We've tried our best I think to reconcile all these numbers, so all of the stuff is absolutely visible for you. But to make it clear, the group generated ZAR 10.6 billion in cash over the period. We spent ZAR 7.8 billion of that on new business. We spent ZAR 2 billion of that on new businesses, and we spent ZAR 3.4 billion on tax, dividends and finance costs. And that's really how the model has played out.

If you look at the net cash flow, again, I'm repeating it for you, (00:24:24) I think did well. Vitality Life is in a growth phase, it requires a lot of capital. The return or the internal rate of return on new business is very strong, mainly risk-free plus 10% or better if we can achieve that in the UK which is a much lower rate interest rate environment. Risk-free plus 7% to 9% is embedded in the new business. And, in fact, the period of how they come out is fairly consistent. We're trying to get our cash back over 5 to 8 years, earn risk-free of about (00:24:47) 8 to 10 years, and then risk-free plus 10%, I would say 13 to 15 years. That's really how the business tends to play out.

So, all of the new business models have the same requirements in them. All of them have to meet the hurdles set for them both in terms of duration and return on capital. So this then flips into the capital model. As I've said to you before, risk-free plus 10% and exactly how it plays out. I think if you look at the period, I think performance has been very, very strong.

On the left-hand side, you can see that we actually earned risk-free plus 9% from a 6%, (00:25:16) very close to what we set out to do. The regulatory capital in the businesses is strong. So, each of our entities is I think very strongly capitalized. We have sufficient capital – I mean, allocated capital to grow despite the diversity of growth strongly over the next five years. The debt levels, in fact, the financial leverage ratio has come down, so it was closer to 28%. You can see it's come down to 25.8%. And the cash buffer's increased to about ZAR 1.7 billion. So, if anything, the capital plan I think is more intact and strengthening. And our desire is to keep that financial leverage ratio coming down slowly and building out cash at the center while we continue to grow.

On the right-hand side, just showing you graphically the return on capital of the businesses. Now, all doing I think fairly well. Even on the extreme right-hand side, our new businesses are starting as they make positive profitability, starting to offer reasonable returns on capital. We expect that profit growth to increase over time.

Maybe if we could segue to the embedded value, just touching on those briefly, I think fairly straightforward, return on embedded value is 17%. You can see the growth in the EV, new businesses adding ZAR 2.9 billion, the unwind of the discount rate adding nearly ZAR 6 billion, positive experience variances overall of ZAR 300 million, some changes to methodology and that's in the detail that we hand out giving a total EV of ZAR 67.5 billion, a few reductions, new initiatives, changes in capital and dividends paid, getting it down to ZAR 65.6 billion or an increase of 15%, not very dissimilar to the rate in operating profit.

So, putting them all together, that's how this kind of cycle has played out. I would argue very, very well it's created the right discipline. The growth rate of CPI plus 12%. I think we've generated a lot of cash. I believe used it judiciously and actually have cut off (00:27:03) in the future. The organization is well-capitalized for growth with leverage coming down. Buffer is going up, and we expect that to increase over time. So, it's in a very solid position. And despite kind of the diversity of growth from the Vitality Group – from Vitality Group globally to Ping An Health in China, to a new bank over here, we believe we're well-capitalized and positioned well for growth.

But I wanted to make the point, I guess, just on this dilemma around how we grow and the kind of exponential nature of organic growth that we need to achieve. So, if you look at the established businesses, just to make the point, they are ramp-up over (00:27:38) ZAR 8 billion growing at CPI plus nearly 9%. I'm not convinced we can continue to do that kind of growth, but it's a massive, massive ramp-up for us. And if you look at them, they all are growing strongly and have continued to grow strongly. And the UK itself had a particularly good year.

So, these are all great businesses and we think that can continue to grow. But we do think that there is real blue-sky potential in the emerging business, and I've made the point that they're all profitable: Discovery Insure, the Vitality Group and Ping An (00:28:05) profitability should dramatically grow. But I would argue, these businesses offer quite unique opportunities each and on itself running (00:28:12) exactly the same model, but they kind of have – each of them has a different case.

Discovery Insure is the fastest-growing short-term insurer in the country. I'll show you a bit later that the dynamics of the Shared-Value model of changing behavior is dramatic, and the embedded value building up is really, really powerful. So, the value that we think can be – the profit growth and value we think can be substantial.

The Vitality Group with its partners and what it's doing has just amazing potential. It's in its infancy. We are getting tremendous results. I'll take you through that. Really it's open sea for us. We've built the largest global platform globally around behavioral change linking it into financial services and the potential for that is tremendous. And then Ping An Health needs no case to be made. It is the leading specialist health insurer and its (00:28:50) growth just tends to be tremendous and the quality, I'll take you through that.

So, we do believe that these three opportunities are starting to mature. They offer considerable capability and despite the scale of the established businesses, these emerging businesses can be very, very substantial. Anyone who opens a fizzy water at the podium is an idiot. Sorry (00:29:15).

And then, I guess at the bottom of the growth model, just turning to the new initiatives, we've been very busy over the period. We rolled out our Discovery Business Insurance into the commercial market, offering companies - and I'll take you through that, some of the skills of Discovery Insure. Umbrella Funds were launched during the period as well. And then, a very important launch for us in the UK, Vitality Invest, I'll take you through, that was launched just about a few months ago, just before the summer holidays in the UK. And then, the Discovery Bank, a huge amount of work is taking place, and we intend on launching it before the end of 2018.

So, these are substantial initiatives. Maybe to summarize then, I think where the group is now is a very strong set of established businesses, a strong set of emerging business offering real blue sky potential, and a set of new initiatives that are in and of themselves really large bets of real potential going forward.

So, just to summarize before we turn to the actual businesses, I think the Shared-Value model has proven to be remarkably efficient and powerful. And to an extent, for us it feels like it's in its infancy. There's so much we can do with this model. The businesses are well positioned, as I've said. And, critically, the capital plan is robust, intact, generating cash, strengthening, if anything. And so, all the disciplines applied in the past of what we've tried to achieved are largely intact now in the model.

So, maybe it's a very good place to start talking about the business. I want to talk about the Discovery Bank first, I mean, and just tell you what we are doing. There's been a considerable process of work as you would imagine in building the bank, just a timeline down there, the left side of the chart, just to show that we started the process in 2015, acquiring 55% of the Discovery Card. By October 2016, our provisional banking license had been granted. We began the bank build in January 2017. A considerable work has been done since that day of October 2017, our bank license was obtained and we made this public that the license was granted by the regulator subject to certain conditions.

Well, the fundamental condition of where it has taken us a year or two kind of unraveling work through has been the fact that while the entire architecture of this bank has had FirstRand owning 25% of it, the regulatory approval was subject to the fact that FirstRand would have to reduce their share from 25% down to zero over a five-year period.

So, this presented considerable complexities I think for both parties and we kind of collectively quite quickly decided that the best way forward for us and for FirstRand would be for us to acquire their 25% outright (00:31:57) as soon as possible. FirstRand has its own objectives about the long-term value creation and that's their decision. From our perspective, we need to own our bank fully, we need to control it fully, we need no competitive forces within it, et cetera. So, for both parties, it seemed to be the right decision.

But extricating out the card and its migration and how that will work legally and pacing was not a simple thing. And we worked through (00:32:22) to agree now that we've agreed with FirstRand all the terms and conditions subject to regulatory approval. We'll be acquiring 25% of the bank and the remaining card and we'll be issuing equity in order to fund that. The purchase price is largely formulaic. It's ZAR 1.8 billion for it. There's the balance of the card that is really the previous valuation with interest. And then we had a contractual price of the balance in the bank, the 25% of the bank rolling up with interest, giving ZAR 1.8 billion to acquire the balance of the card and the 25% of the bank that we didn't own.

So in effect, that is what we're doing. And I wanted to make a few points in this regard. It is important to understand the asset ready in the belly of the bank as it grows. The Discovery Card is performing really, really well.

So if you look at operating profit, it's grown by 17% to ZAR 414 million over the period. And so to make the point immediately, if you look at the valuation of the price of the card versus the profitability, it's about a post-tax P/E of, I think, around a 10 times multiple. So in effect, the purchase price embedded in this is kind of a 10 P/E.

And if you kind of place the entire cost of this on the card, it's kind of buying the card at a 15 P/E. So to an extent, you could argue it could be value accretive to us, but bear in mind, that's inside the belly of FirstRand. We have to bring that across. We have to get it into our systems with our costs. So, there's a lot of work to be done. So, it's not hubris or (00:33:45) whatsoever, but I do think the price is fair to both parties but the card has performed well.

You can see the scale of the card. There's a book of ZAR 4.3 billion, and I think critically for us, in the middle of the chart is just how well the book has done. Non-performing loans are about 3% of the base, that compares to the kind of 8% average of the banking market. So, it's substantially better quality book than other banks.

And the important point for us is just how integrated to the behavioral model the Discovery Card is. So, if you look on the left-hand side as people engage in Vitality, they tend to spend more on the card. As they engage in Vitality, their closure rates or their propensity to leave us goes down. So, spend more, become more sticky.

And then if you look at the kind of bad debts are going into arrears as they engage in Vitality that goes down, we'll have more Discovery products with us, bad debts go down, and amazingly this kind of (00:34:42), these things are all correlated. People who drive better have lower default rates. Right? Not sure why but that's how it is. So, it's kind of like all of the stuff interlinked. And for us of course this has been behind the impetus of the bank, the data, the segmentation, the correlations, and more, and that gives us the ability to build the bank.

Dealing with the decision about how we fund the purchase price, and this has been quite a considerable debate of our board over time over the year. If you look at the capital plan and you look at the white line of how the financial leverage is coming down, we've put a self-imposed limit of 28%.

We're coming down nicely. Were we to fund acquisitions of bank with internal resources? It's doable but it pops us right to kind of that limit. And our feeling was given the rate of growth of the group, China, the Vitality Group, the stuff that we're doing (00:35:33) at all. We've made it clear in our guidance that our capital is sufficient for everything that's on the table. This is a new acquisition. It offers considerably something (00:35:42) for us so we felt an equity raise to do that is fairly insignificant in the market capital of the group, but the right way to acquire it.

This is all subject to regulatory approval. The deal has been agreed with FirstRand, and that's the process we're going forward. So, expect more from us in the next few weeks, so I would guess, Deon, around this issue as it plays out, but that is our preferred approach.

So, let me go back to the businesses. And, now, I'm going to move through them and I'm hopefully not going to be too laborious. I will deal with the international stuff first, the (00:36:12) markets in China and the Vitality Group elsewhere around the world.

The Vitality Group has really had a tremendous period. You can see the rate of growth here. The integrated products with our partners like AIA, Generali, John Hancock has grown by maybe 80% to nearly $400 million of new business. Our revenue has grown by 40% to nearly $52 million – just over $51 million of revenue and that business is now profitable.

It's very much a fixed cost business. There's a lot of fixed costs at the center. And as it grows, we should actually start seeing good (00:36:43) profit emerge out of it. We are still investing considerably in it. So, it's going to take us a bit of time. We are not rushing the profitability. This is not something that's dragging us at all, but the potential is just so remarkable. If you look at the growth of the business over the last few years, it has been tremendous. And the number of membership as it's grown, it's really accelerating exponentially.

And to make the point on the right-hand side of the chart, we really have got the largest platform globally around behavior change and how it integrates into financial services. And the Vitality Group is learning its repeatability and scalability. So, the different product designs from dynamic processing to enhanced yield, we're learning how that applies to different markets. We're learning how to optimize the partner mix from healthy food partners to germs (00:37:26) and all the like, learning how to deal with regulators in different markets and then we're repeating and scaling it I think particularly well.

One of the notable aspects over the period has been technology in Vitality One. We spent nearly ZAR 0.5 billion on building this piece of technology. In the first iterations of the Vitality Group with AIA, we're using our own South African Vitality system bent into shape and we did this around the world. The decision made by the Vitality Group that we should really globalize, one platform, cloud-based, multi-tenancy, multi-language can be deployed very quickly per partner, a very, very substantial rollout. It's taken us years to do this, 105 developers around the world working on this. And it's been a very, very powerful capability. That's just been rolled out with Sumitomo Life in Japan and with AIA in Korea. And it offers considerable ability to take the platform and really scale it quickly to make it much more flexible. So, that's a very important step for us. And over time, the group will fall onto this platform in different shapes and sizes.

The other point I wanted to make is that the actual performance for our partners is remarkable. So, I made the point up-front about the effect of this model. You should get better selection, better growth, better behavior change, better lapsation. These are three use cases across three markets. We can't divulge the names of our partners, but we chose them. They are quite unique in each case.

In case one on the left-hand side, this is a very large market that's fairly stagnant. Our partner has managed to grow its new business by 10% in a stagnant market, but by growing the Vitality integration by 14%, so it's giving a really strong new business effect.

In the (00:38:59) market, it's hard to get customer interaction using Apple Watch and Active Rewards. On the chassis, we're seeing considerable uplift in engagement. And then the right-hand side, I think a fantastic example. A market that has annually renewable premiums in life insurance, so that the prices go up every year, we get considerable lapse rates and that's the biggest challenge in the market, keeping clients on the books.

You can see on the right-hand side of the chart how correlated the lapse rates are. So, as people engage, their lapse rates go down by 30%, down to a sum of about (00:39:29) further 30%, et cetera. So, the actual stickiness is remarkable. So, the ability to get the sales effect, behavioral change, lapsation effect is real. So, the data coming out of our partners is incredibly powerful.

And so, we remain very excited about how we can grow this business. The profit I think will follow strongly and you will see that. Three distinct areas of growth. We have amazing partners in Ping An, Generali, John Hancock, and more. We need to exploit that latent potential. There's a whole lot of ways to do that. More products attached to the chassis. More penetration in the product. Better engagement. We had our infancy there, and the ability to do that I think is substantial.

The second point is our joint venture with Hannover Re where we kind of have boxed this together with the reinsurance offering and offering this in many smaller markets. You can see the pipeline is building up strongly. We signed up four companies across Asia and Latin America. We've got three that have signed letters of intent and a very long pipeline building up. And then, importantly, the considerable adjacencies. Our motor insurance business has applicability internationally. The VitalityInvest capability, using this platform for long-term savings has applicability. We're working really well with Apple on a number of adjacencies, and I hope you have the time to see how that will play out. So, there's considerable potential.

But one thing I did want to show you, it's the only video I have in the entire deck, but our launch of Sumitomo Life in Japan, this has taken us a few years. It's probably the best example of repeatability and scalability. The team worked on all the learnings, worked with the regulator that the product is set right. And the actual launch itself has Sumitomo play this out in terms of partners like Apple, Garmin and others in exactly the way it was structured is kind of the model placed and how this can work out. It's just a few months old, taken us two years to launch. We launched I think early July, June-July we did the formal launch. Let me give you a bit of insight into the launch itself in the process.

[Video Presentation] (00:41:16-00:42:24)

So, early days but really exciting stuff. Barry and I had to learn a bit more formality about standing on a stage and bowing, which is new for us, Barry, but really, really exciting stuff and offers great potential.

Then we turn to China at Ping An. Again, there's a lot to say here and I just want to be pretty clear. It's been a tremendously positive period. New business grew by 95%. You can see the scale of growth to nearly $450 million. The written premium because of the rate of growth also grew by nearly 90% as you can see. The profitability is just starting to emerge, but this business is full of new business strain, tax on commission. We've been growing at this rate (00:43:01) the profitability emerges very slowly. Our profitability is 25% of it less our costs. We have quite a strong team under Barry and his team driving the Ping An Health capability.

So, if you turn to profitability and we expect that to be muted for a year, but then to grow really strongly thereafter as you look at the effect of new business strain (00:43:19) of these specific dynamics of the Chinese market.

I'm not going to make the case for how big the Chinese private health insurance market will be, but this is coming out of the Ping An, their own analysis. I mean the market really is emerging. On the left-hand side, you can see private health insurance penetration is tiny. It's kind of non-existent. In the middle, out-of-pocket expenses are very high, like 35%. And therefore, the insurance opportunity is really, really substantial. On the right-hand side, the actual addressable market, they believe, will kind of be 7x quite quickly. So, this is a market of considerable scale. But issue really (00:43:52) is the quality of the business that Ping An is building in Ping An Health.

Firstly on the distribution side, Ping An Health itself now has its own branch network that covers large cities in China, covering nearly 230 million people by the end of this year in some of the major centers including Beijing, Shanghai, Shenzhen and more. In the middle of the chart is just the agency force of 1.4 million agents. And amazingly, 21% of them are now actively selling Ping An Health. And then on the right-hand side, something that I think is kind of a seminal (00:44:23) issue for the period under review is the power of technology. And in China, as you know, it's the highest rate of adoption of technology, people live online and a different distribution channels. The third-party platforms that are selling our product.

And then critically on the top, we have our own app, our own Ping An Health app that's – that people are using and buying health insurance through it, and it's proven itself to be remarkably powerful. So, the Ping An Health app now has over 4 million users. We've done over RMB 100 million of business through this. So, the trend has been remarkable. And amazing this app out of I think a couple of hundred thousand financial services apps has been ranked, on the (00:45:02). So, it's an amazingly powerful piece of real estate. So, the business itself has just tremendous distribution capabilities directly online through the Ping An distribution capability.

The product strategy I think is working well. We have three real product lines that are getting real traction. Our group high-end business is truly the (00:45:21) group market. We've got a fantastic set of clients Goldman, GAP, McKinsey, et cetera. But the real breakthrough in this business has been selling individual business through the agency force.

The mid-market products of Ankang and Anxiang have really got traction and sold through the Ping An Life agents and then importantly, over the last year, the really notable thing has been E-sheng Bao, which is sold online. It's a lower level product, a RMB 10,000 deductible and really sold online promoted by the Ping An agents. And you can see how their revenue grow off, it's just exponential. I think importantly on the right-hand side, our loss ratios and our lapse rates are very much in line and below the premium assumptions which is of course very, very important and the stability is there. So, the quality of the business there I think is quite tremendous.

The team, I believe, is interpreting the environment correctly. While intellectually, you accept the market is big and it's going to grow. There's certain kind of catalyst that may change. This is a very interesting thing that happened this year. You might have read about it in The Economist, but a movie, Dying to Survive, about a kind of a parody about an individual suffering from leukemia in China who's smuggling drugs into China from India. Cancer drugs are not available in China, highlighting the deficits in the system and the dangers not having access to these drugs became like a viral hit. And you can see generated over ZAR 5 billion of box office sales in two weeks illustrating kind of a continuing interest in healthcare and fears about things like cancer.

So, our team has launched – they're doing it anyway but they launched a cancer product that has just been rolled out, fairly low premium. We're selling about ZAR 3 million a day of new business online through this approach. Trying to illustrate that in fact I think the team is interpreting how the market is kind of developing and how our product shows you – you should follow that.

The other important point to say is that there is a considerable investment in technology, digitalization. This is a fascinating chart that kind of shows the capability of the company. I do remember this and you may – if you've attended our presentations, a few years ago, we were trying to get to 100 cases a day. We developed this individual product and the aim is trying to get to 100 cases a day. We're now writing 25,000 a day, right? So, when you get growth like that, the ability of organization to actually handle it from an administrative perspective is very difficult.

So, there's been a considerable focus in digitalization. You can see the capacity to handle applications was about 100 per minute. That's now 4,000 per minute. The ability to process claims per day has gone up dramatically. Operating cost has come down. So, the ability to grow and manage that growth is quite substantial.

And then, finally, from a Discovery perspective, we are shifting as much IP as possible as quickly as possible from all the data capabilities that work with quantum (00:47:57) on the data side. All of our analytics, all of our product development tools, our Vitality capabilities, as fast as we can, we're putting them into the Ping An capability.

I thought I'd end with this slide, it kind of brings it all together, kind of illustrates the growth of what's happening. This is a month-by-month revenue slide of Ping An Health, 2017 in grey and 2018 in orange. I guess it's obvious, if you're doubling in size, you have double revenue, right, pretty obvious. But I just wanted to show you, by June, we've done the same revenues we did in the entire year last year. So, this really is growing on the back of the power of the Chinese market and the distribution capabilities, the product sets, et cetera. So, we are excited about Ping An Health. It is profitable. That profit is likely to stay where it is for a year or so because of the new business strategy but they're off to a - (00:48:44) confident it will grow quite significantly.

Let me turn to the UK. And the UK, I think, had a very, very good period. We've built, I think, a composite capability in the UK, new business up 12% to quite substantial and it's just under ZAR 2.3 billion of new business. Operating profit, really in the back of the incredible performance of Vitality Health, up 44%.

In the last comment I made the point before, total lives covered climbing by 11% to 1.1 million lives in the UK. The (00:49:18) is fantastic and when we launched the VitalityInvest, it's starting to look more and more like Discovery so, you've got the ability to integrate. We haven't done any of that stuff yet. The truth of it is this has been a business both Health, Life in the belly of Prudential initially and then brought across, and that really is a composite capability. We can focus more on integration. There is no cross-sell between them at all. There's like 0.5 million lives in Life, 0.5 million lives in Health. The two don't cross. We haven't cross-sell-ed anything with either of the base. So, there really is potential. You can see the quality of the Vitality platform. The levels of integration and the levels of engagement on the right-hand side are absolutely tremendous. So, it's a very, very tight - very tight capability.

Vitality Health had a absolutely tremendous period. I want to just take you through what has driven this. As you know, it's had not an easy evolution and the team is focused very hard on quality. New business is up 14% to just over ZAR 1.1 billion while operating profit is just a remarkable growth and I'll show you why.

Lives for the first time is going to grow. You can see at the right-hand side of the chart the lives we've kind (00:50:21) we felt the right kind of lives to rightsize the business and now we're growing I think strongly again. But the real driver has been the quality. All the factors of the model have worked. We're selecting better lives. If you look at the actual quality of the health of the people that are joining, dramatically different to the UK average. In the middle of the slide, if you look at behavior change, we're getting tremendous correlations to engagement in lower claims. In the left side, we are retaining the better lives, losing the worst lives.

And so, mathematically over time, the book gets better not worse and that's important. But I think there's two other aspects as well. For a given life, we're developing considerable sophistication on our premiums. It's an amazing market. There are no community rating requirements guarantee issue. You could rate any factor you like in the UK market. So, there's literally over 100 million possible combinations of risk factors, Health status, Vitality status, the postal code where people live. If you know, the UK insurance market is highly, highly sophisticated. Our team has developed fantastic AI machine learning models and they developed really good ability to price premiums.

And then, on the right-hand side, our joint venture with Aviva where we operate in a purchasing alliance buying healthcare, has given us as you can see on the right-hand side of the chart, we can't give, of course, the granular amounts, but you can see the inflation on hospital oncology cost has, in fact, come down, so keeping those costs relatively stable.

So, you add together great demography, the effect of all of those effects, great pricing, and lower cost of healthcare when you buy it, you get a fantastic effect. The loss ratio has just decreased over time by 21%. It's remarkable. The business has flown out. The back book has flown out ZAR 1 billion from ZAR 5 billion of cash. We spent ZAR 1 billion of it on acquiring new business and other developments and throwing out a net ZAR 0.5 billion of free cash into the center.

And so, the performance, I think, has been absolutely tremendous. If you look at the return on capital, it has climbed from a kind of 3% close to nothing to exceeding now risk-free plus 10%. So, that's pretty great performance, I'd say, together with some of the other with Ping An and with Vitality Group, really a standout performance of what we've set out to do.

If we turn to Vitality Life and make the point, this business has been a very difficult environment with low rates of interest. We've been clear over the last number of presentations. If we're rightsizing - not rightsizing, getting the business configured correctly in terms of a low interest rate environment, I think it had a great period in that context. New business up 10%. Operating profit up 6% in a pretty tough market. Lives covered growing by 15%. The interest rate environment is difficult. You can see that rates came down dramatically with real rate of interest now like minus 2%. We don't think that's sustainable. I mean you point out negative real rates of return forever, but they're low.

The other factor that is really the devil that's been is considerable volatility in interest rates. And how we were operating before was - we've made this point clearly was we're using the interest rate for IFRS calculations at the point in time that our (00:53:11) finished, so, whatever happened, kind of potluck that would determine our earnings. And I think we've made this point of how we're trying to deal with it. In working with a regulator, with our auditors, we now shifted to a passive approach. So, what we're using in our IFRS numbers is really a 12-month average of GILTs (00:53:26) and other rates that are appropriate with (00:53:28) 25 basis points above and below. Should rates break out of that, then we'd – have to relook at that calculation. And so, we stabilize the volatility by changing the accounting approach that provides much more stability and predictability to the earnings, and you should see that going forward.

But I think in the dynamics, I think the team has done a great job in shifting to its business that operates better in a low-interest rate environment away from Whole Life business now meeting (00:53:51) 96% term insurance, more and more towards the index business, which is naturally immunizing in a low-interest rate environment giving a 38% index as opposed to 24% just a few years back. The effect of that I think is good. You can see the new business has grown. The margin went down to 2%. It's climbed back up to 5%. And the internal rate of return on new business has climbed to kind of about 8%. Not bad in the environmental risk-free is like 2% or thereabouts. So, we are pretty comfortable with the performance of Vitality Life, and we strongly as rates are going to just go up (00:54:22) the inherent profitability and value will increase.

Let me turn to VitalityInvest, I hope I'm making sense. I hope I'm not running out of time. Let me just tell you that we are excited about what has been launched in the UK. I want to just – give me a moment to explain the hypothesis here that it's very, very interesting. And the UK is one of the most competitive commoditized long-term savings markets in the world with just hundreds of fund managers and choices and you know the stuff as well as I do.

But this is an amazing issue. As the market has shifted from defined benefit to defined contribution environment, there's just been a considerable sophistication in a number of funds, passive, active, all kinds of innovation. You can see from the chart the expense ratios, platform fees, asset management fees have come down. So, it's a highly, highly sophisticated market. And it's a considerable scale. It's a market of in total £180 billion of flows every single year. So, it's a market of just considerable scale.

But our hypothesis is that we want to harness all of that sophistication and we can and we have, I believe. But the key issue that we want to offer is the idea of the demography side, people managing the mortality. It's kind of quite mad in a sense that you plan so well on the asset management side with fund choices but you have no idea what your life expectancy is, you have no idea how long you're going to live and what planning horizon you're planning for, how sick you're going to be and what it means to your retirement income. So, kind of our value add is the Vitality share value model. And so, we've rolled that in the UK. I think a very, very sophisticated product set. I'll try to show you in the left-hand side that's from our team's marketing. But effectively, the currency we use in this shared value model came from Discovery Invest, idea of boosting people's funds.

So, if you save earlier, you manage your health, you drawdown less, all of the stuff leads to boosting your fund, boosting your retirement income, reducing your platform or asset management fees. So, giving you more money. And the strategy that we invoked (00:56:18) has got all the technology, all the asset management choices. We have a JV with Investec, with Vanguard on the passive fund side, access to all of the third-party fund managers, so, trying to bring together this capability. We've increased dramatically our distribution footprint through our franchises and our advisors on the ground but I think, close to 25% or 50%. It's a dramatic number that we've increased. And we saw – you can see traction in that regard.

The actual value proposition is interesting. I just want to show you this tool. Just bear with me. I find it fascinating. Forget about all the asset management complexity. The question is when you're retiring, how long are you going to live at and are you saving up enough money? So, what we're doing is we've done a lot of work on that, signs of aging, and we're giving our clients and advisors tools to actually work this out.

So, this tool, which is available online, allows based on individual risk factors to tell them their life expectancy; in this case, a 35-year-old male is expected to live to 75. We give a confidence band from 67 to 81 in this particular case. And then, we propose through Vitality what lifestyle (00:57:20) they should do. If they do that, their confidence band goes from 77 to 91 with an expected life expectancy of 85. The problem then is with their retirement savings, they're only going to make it to 83. So, the whole idea is that if you do the things we say, we're going to boost your retirement income, therefore push you out to 88. So, we're trying our best to give all the kinds of tools to people to make decisions about the kind of mortality demography side of the choices they make, life expectancy, and to give them the ability to boost those savings as they go forward.

It's early days. I think the traction we will see in the next few months, literally, the market is only starting as people come back from the summer break, but you can see we're using the same kind of approach of Vitality, Stanley our dog (00:58:02). And we've had really good traction in the press. So, in The Financial Times, you can see they're linking this idea of health to long-term savings and that's the link we're trying to – we try to get. So, early, early days, but we're excited about what we think we can achieve in the market that is quite substantial.

To make the point, addressable market we see, I think, is £29 billion where the accumulation of drawdown products are which is ZAR 0.5 billion of – ZAR 500 billion of potential market for us. So, if we get the chart to scale it's I think considerably different to what we're used to.

Let me move on and just try and end off with the South African businesses, if I can, just talk to them one by one. I think it has been a very good period. In the South African business, our deal with Discovery Health, growth remains very strong. New business up 8%. Membership now climbing over 3.5 million. Operating profit continues to grow by 11% in this regard. If you look at Discovery Health, it's doing better with restricted schemes as well. So, of the last 17 tenders, we've won 16 of them and Engen just joined the Discovery Health platform. The total market share of private healthcare lives is 40%. And you can see on the right-hand side the quality of restricted schemes with one open scheme, the Discovery of medical scheme that we saw right at the start of Discovery today. It makes up 56% market share of the entire open scheme market covering 2.8 million lives.

The Discovery Health Scheme itself and I show the slide at every presentation is remarkably strong. They pay 16% less for health care than its competitors. It has administration fees paid to us in the lowest quartile. It is remarkably stable. Buy ups and buy downs are very small from year-to-year as 27% or more in solvency. ZAR 16 billion in cash in reserves and it's AAA rated. So, it's incredibly robust. I think the performance is really, really strong.

And I don't like the point with any sense of hubris or in any way blasé. I mean the issue really is given that strength, how do we navigate the way forward. And I think to make it clear, we kind of know our social mandate. We have to make – keep healthcare affordable. That's our fundamental issue. And keep access to quality healthcare, not just for our members but for all South Africans. We have to help the country build its health care system both public and private. So that's a very, very big mandate.

There are only three things we can – it's one of most complex businesses you can think of politically, economically, actuarially, it has everything in it. But I wanted to make three points, navigating regulation, trying to deal with medical inflation that is really our nemesis, and then just building the service digital environment that is superior. On the regulatory side, we have heard a lot from us. I mean this is a lot of stuff in the pipeline, the NHI Bill, the Medical Schemes Amendment Bill around macro (01:00:46) regulation medical schemes, the competition health market inquiry. I think we are pretty focused on what we think we need to do. The NHI Bill is lacking detail but pretty rational by creating a fund in its governance.

We don't see growth from (01:01:00). Discovery Health is committed to helping build the NHI. On the (01:01:05) Health Market Inquiry, there are a lot of findings in every single side of the healthcare system. We think they're in the large or rational and appropriate. And as they get implemented, they probably have a very good effect on the healthcare system. I don't think though you should hold your breath for a dramatic cuts in the cost of health. I just don't think it's possible.

And maybe it's – the next slide, they may be makes it a point. Clearly, our biggest issue and always will be is medical inflation, how you keep it under control. I wanted to show you these slides they're kind of changed from year-to-year, but the points are the same. Trying to keep healthcare cost under control is extremely difficult. So, people often get misconstrue inflation for tariffs and doctors' fees. Those things are largely under control. So, CPI and tariffs are like 6% to 6.5%. That's not the issue. The issue is the utilization factor. That is growing at like 4% to 5% a year. It's dramatic.

So, the inflation or the increase in utilization is almost in scale the same size as underlying inflation of tariffs. It's dramatic. And it's driven by what we call both supply side factors and demand side factors. And the one point I wanted to mention on the right-hand side, the increase in VAT of 1% is costing the Discovery Health Medical Scheme in excess of ZAR 300 million. So, if you study that in the budget, I think the cost to – in total of that 1% increase in debt is ZAR 30 billion. So, fully 1% of the country's entire increase in VAT will be carried by the Discovery Health Medical Scheme. It's a very big number. That means that we have to put our rates up 1% to fund for that.

But let me come back to the issue of the utilization increase and there are many things that drive this. I thought I'd mention one that remains for us always something difficult to deal with that's increase in the number of hospitals. That's well-known in health care. You get the (01:02:51) supply-induced demand. The more supply side you get, instead of prices going down, they tend to go up. So, when you open up a hospital, see on the right-hand side the case study in Pietermaritzburg, hospital beds went up, immediately our utilization went up 23%. So, you can see in the middle of the chart, 52 new facilities were opened up, and it created a spend of nearly ZAR 1 billion to fund these facilities. You can also take to your left-hand side where medical scheme lives have grown by 7%, hospital beds have grown by 40%.

Is this a bad thing? Probably not. A lot of these new hospitals are black owned (01:03:26). There's new quality. These are things that we should encourage and we should try to fund. But you're going to get supplier-induced demand when you track up everything always. And at some point, we need to start making choices about how we deal with that and what and where we restrict. So, this is something that I think is difficult to fund, but something that we need to deal with in the appropriate way and something we are supportive of, but we need to deal with judiciously.

On the demand side, we often get asked about cancer. And given the richness of our statistics, I want to show you these quite scary numbers. This is coming out of the Discovery Health Medical Scheme, just illustrating on a risk-adjusted basis the kind of incidence of cancer – the increasing incidence of cancer, males and females, you can see, over 2,000 and acts in a kind of a 10-year period, the incidence rate has almost doubled as you can see, one from 8.5 times in the case of females, over 2 times in case of males. You can see the different kinds of cancers and what those incidence rates are. In males, colon cancer is up nearly 3 times. Why is it happening? We don't know. Earlier diagnosis may trigger some of the statistics, but the really (01:04:31) obesity or lifestyle choices, other factors we're not sure.

Of course, the effect on the price of healthcare is dramatic. As you all know, that each of these cancers, amazing immunotherapies and biological drugs are coming at considerable, considerable costs. So, you put this together with supply-induced demand, all these things together create considerable medical inflation. I'm not here complaining about it. I'm making the point that we know what we have do and that's our mandate. And we will do it. We have to keep costs under control. Just to make sure we'll be releasing our rate increase and other product enhancements into 2019. And all of these factors have to be priced in. We know where we have to go.

We're at the end, so very quickly just telling you we continue to focus on the administration fees and our 10.1% and they're in the lowest quartile. In the middle of the chart, just showing you the core administration fees has come down quite a bit below the average. But on the right-hand side, you can actually see the scheme gets considerable value out of those fees. So, we are acutely aware of what we need to.

Discovery Health has built incredibly sophisticated integrated digital ecosystem. I've demonstrated here DrConnect, HealthID. These things are all together with all of our data management population management tools. And I do believe that Discovery Health has the ability to tremendously manage health care costs, add value to our customers, and add value to society as we go forward.

Let me talk to Discovery Life. I think a very good period. And the focus really was on quality and robustness. New business grew by just 1%, but that was – we had a very large group scheme in the previous period. The individual life new business grew by 4% in a pretty stagnant market. You can see on the right-hand side our market share continues to grow. So, the fact we're now over 30% of the new business, (01:06:15) life insurance market, nearly 60% bigger than our nearest competitor. Operating profit growing by 7%, on the individual block by about 9% of the period with just over ZAR 3.8 billion.

Discovery Life really has been the kind of catalyst of the shared value modeling in long-term insurance, and we continue to see most remarkable results. So, if you look at selection, mortality correlations, lapsation, the value we're sharing with customers is remarkable. We're getting better lives in than we expected. The mortality correlations are amazing. People heavily engaged in Vitality are exhibiting 20% to 25% lower mortality levels. And we're getting lapses in excess that we like to see. People are engaged of staying. People are opting (01:06:53) to be in the book over time should get better.

But I thought of showing you the shared value, the top-right hand chart because our customers get value from us, obviously in their life cover, fundamentally. But they need to die for that, which is one of the stays of the product we offer, right? But they get value in terms of premiums coming down as they engage. But one of the benefits has been the sort of paybacks. If you engage with Vitality, every couple of years, every five years, you get a payback benefit, a function of the number of factors. You can see the scale of the paybacks (01:07:19) borrowing we can.

We paid back this year, this period under review, nearly ZAR 1 billion to our customers. And in fact, cumulatively over the years, we've paid ZAR 5 billion back to our customers in terms of engaging in Vitality, so really illustrating kind of the shared value at work. The company continues to innovate, Global Education Protector, I think won a (01:07:41), Global Award for Innovation around covering education, the whole range of issues. We've segmented our market where we cater our (01:07:48) Purple Life plan for coverage about 10 million. All of that stuff has added considerably to our market competitiveness.

A lot (01:07:55) on the left-hand side, some of the technology we're using are using data. So, for example, if you have a rare disease or a severe illness policy today, typically you get a severe illness, after you've had treatment, you try to figure out with your adviser, do you qualify, don't you, if you think about that and then you make the claim. We now more and more are being proactive using the data. We know from the data whether you qualify for a claim, even if you or your adviser doesn't know it. When we pick up the data from your claims, we actively reach out and tell you that you qualify for a claim out of your policy.

So, we've done a lot through that. This is still – and you can see a bit more of that kind of use of technology and data will follow. So, I would argue that the competitive frontier of Vitality Life is particularly strong. But I wanted to just change gear, and you will know this,

this considerable noise around the accounting standards, the dynamics in Discovery Life. It is a very, very complex business. And I wanted to deal with it kind of head on and tell you the choices we've made and why. We've done a considerable amount of work that would be available to you, a whole bunch of papers that illustrate all of these factors of exactly the profit emersions of Vitality Life, the assumptions and why we've made these choices.

So, let me just go through this quickly and just give you the rationale of our thinking and hopefully that will make clear all the choices we are making in building Discovery Life. The first point to make is Discovery Life is very different to its competitors. Number one, it only sells one class of business unlike our competitors that sell all kinds of different policies. We have sold protection business, long-tail, whole of life, up-front acquisition cost from the day we started. It creates a financial dynamic that is quite unique. You get this up-front cost and over a long period of time, you recoup that.

The second point is that it's a young business. It started 18 years ago or thereabout. The midterm of a businesses is 6.3 years old. If you look at our competitors, they are typically 100 to 150 years old and, therefore, there's a very different scale of maturity. The third point is that the growth has been rapid. We've grown about 25% per annum compound over the entire duration of the business. So, as you acquire business, you get more and more acquisition costs that kind of go through. And then, finally, the Shared-Value model, the Vitality model means you got dynamic pricing. Your premiums are flexing from year to year based on how people engage in Vitality.

So, from this kind of - this complexity, the question is how do you recognize profits? Well, there're two extremes. You could just do it on a cash flow basis, right? As you spend the money, you just kind of - whatever goes through, you account for it. The problem with that is that given the rate of growth, you'd have a kind of minus ZAR 20 billion cumulative profit when the business (01:10:29) profitable.

At the other extreme, you could do a full kind of EV accounting (01:10:35) embedded value created. The approach we've taken, which is consistently we offer is 17 (01:10:37), is going will take us is a prudent emergence of value, setting up a negative reserve that reflect, hopefully prudently, what the outstanding acquisition loadings are and trying to get the profit to emerge throughout the journey illustrates inherent profitability of the business. And that's been the accounting standard we've taken. We think it's appropriate given how the business is positioned. And if that is appropriate according to IFRS, we'll send that. But it has a number of consequences and it creates kind of a controlled cycle that I wanted to just demonstrate to you.

The first is once you've set the accounting policy at that, you create a large negative reserve. So this is the point 2. You need to check the assumptions behind that negative reserve and make sure it's resilient. Once you have those assumptions that leads to point 3, you've got to make sure every year the experience is in line with what you expected, else your assumptions are wrong. And then finally, whatever happens, you've got to manage your cash and capital given the nature of this business with high up-front cash requirements and a long tail associated with it. We've done a lot of work on this and I probably won't do it justice, but I did want to kind of touch the tops of this and leave you with papers that deal will all of these.

On the issue of the negative reserve, you will see on the face of our balance sheet, there's a negative reserve, I think ZAR 27 billion, attributed to Discovery Life. That's a massive asset on the face of our balance sheet. The question is how resilient is it. Well, you will see in the paper that the ZAR 27 billion has margins above it, first and second year margins of a further ZAR 24 billion. We've tried our best to illustrate to you that if you stress this asset with lapse rates, interest rates, higher claims, you'll find that in 1 in 200 of your stresses, the margins actually survive, so you never really penetrate through to the underlying asset. So that's an important issue.

On the actual experience variances, even if you assume the asset is resilient, the question is are we performing in line with the assumptions. Well, this is a very important point. You will know if you follow us closely that over the years - I'm sorry, it's a complicated slide - over the years, we've had positive experience variances. For the first time for the last two years, we've had negative experience variances. And that creates a concern, are you performing in line with what you said you would do? I am pleased that the work done by the team has lifted positive experience variances for this year and work done. We've strengthened the bases by a further ZAR 1 billion to make sure that the experiences going forward are positive.

But if you look at the key areas, claims, lapses, and policy alterations, we've done considerably good work. So, claims are better than expected despite the first half being quite a bit worse. They turned around dramatically. Lapse has continued to be dramatically better than expected. And even our policy alterations, we've actually made the second half as positive, a lot of work done on a number of structures. So, in total, the experience variances are positive for the period. I think that, together with the strengthening of the basis, we are confident will lead to positive experiences going forward.

And then, finally, managing the cash. I've made this point. Discovery Life was cash-generative to the tune of ZAR 540 million - just over ZAR 0.5 billion (01:13:24) you can see it there playing out, generated ZAR 12.7 billion of revenue. After claims and other expenses throughout about ZAR 3.5 billion of cash. We invested ZAR 2.9 billion of that in new business and to a few other changes. You can see that the net cash is fairly strong, and the company's remarkably well capitalized. Our solvency cover is about 170% on the new same basis. So, it's kind of self-perpetuating and growing on this basis, and gives us confidence that the company will grow, innovate and continue, I hope, to eat market share on a sustainable basis. Its fundamental proposition, of course, is making people healthy in addition to its social role of providing coverage.

Let me move quickly, Discovery Invest had a very good period. It actually - new business was down 10% at the half year. We clawed back somewhat in the second half. Not a simple market, but the net flows were up 10%. So, reflecting surrenders and withdrawals better than we expected. Assets under administration continue to climb 18% to just under ZAR 82 billion, profitability reflecting both scale and efficiency, and maintaining margins up 19% to just over ZAR 885 million.

I wanted to make a point really borrowing out of the Vitality Invest part of the presentation that we've simplified our thinking around what we're trying to do is get people to save earlier, manage their health, and draw down less in retirement. And all of the incentives are aimed at doing it. So, the currency here like we're using in the UK is simply the idea of boost. We boost people's funds. We boost their retirement funding, provided they do what we're trying to incentivize them to do and to kind of avoid those corrosive behaviors.

We're actually getting fantastic results as you can see. People are saving on average two to three years earlier. Fantastic engagement in Vitality. And on the bottom right-hand side of the chart, we're seeing 3 percentage points lower on average drawdown levels. So the actual – the product in that sense, I think, are working well.

At the same time, the dynamics of the business are strong. We've managed to bring down the platform fees, 90% or more of the choices of our customers are on our own funds. The Discovery Balanced Fund has performed remarkably well. And then, we've managed to maintain margins despite a very, very difficult market.

During this period, we rolled out the Umbrella Fund business. That's a pretty complicated – very, I think, comprehensive offering based on Vitality, but the fundamental issue is we boost your retirement funding if you do what we are trying to get you to do (01:15:43) preservation funds across, we boost and provided you manage your health, you saved early, et cetera. So, it really offers, we think, strong, strong value for money.

Let me turn to Discovery Insure and end off on this and just make a few comments. I think a great period. New business up 17%. Written premium up nearly 30%, reflecting the scale of new business slices just adds to the revenue flow. The number of cars we cover over 200,000 and the business is now turning to profitability. I think the exciting thing behind Discovery Insure is just the model works unbelievably well. The selection of lives is remarkably good, so we're getting really good quality lives joining.

The behavior when people drive is – behavior changes quicker. We can see a 17% improvement in one month. So when people know they're being monitored, they're getting incentivized for change, they change quickly. Lapses are better for our better drivers. And, again, we're getting fantastic correlations. People that manage their health tend to drive better. People that manage their health and their wealth drive even better. So, it turns out it's the same kind of behaviors. Wherever you cut the data across our group, you get the same stuff.

We're getting remarkable data coming out of Discovery Insure, but I wanted to show you this kind of hot off the press. I want to make this point to you. There's all kinds of sensitivities in these slides. And let me just try to get it across to you in a – I hope, a fairly simple way. We live in a country with considerably dangerous roads. Our road fatalities are known to be absolutely terrible. But the fundamental question is how well do our drivers drive and are we seeing a lot of fatalities as you engage in our incentives.

And what you see on the left-hand side is the South African average of fatalities for 100,000 motor vehicles. You can see our population is dramatically lower, second from the left. So, the fatalities we see in our covered base is dramatically lower than the South African averages you would expect. But the important thing you see is that those that are with us that on to the Vitality drive program are not that dissimilar to the South African average. But as you engage, if it goes down dramatically, and I think what's interesting is our silver class drivers are dissimilarly in danger to what they see in the U.S.

So, it's kind of – I don't know if it's an intuitive result or not despite the danger in our roads, it turns out that people that are driving on our roads, as our silver drivers and higher due are exhibiting similar kinds of danger levels to those driving around in the U.S. You can see it tails off in Australia, et cetera.

One last statistic I like is we haven't had one death of a gold member yet, right? So, our gold members will live to 300 or something. I know what this means. They never die. But we haven't had one death yet of gold members. So, there's a lot of potential applications for understanding fatality rates and how the correlation between driving fatality rates play out.

I want to make one point just before I end off, on just the quality of the business being built up. It's turned to profitability. But the exciting thing about Discovery Insure is the value being built up. Everything is durational. People behave better over time, the better they'll stay with us. So, in fact, the back book gets better and better. And if you look at the back book in this period, ignore the acquisition cost, the back book, ZAR 324 million of profit and cash and had a margin of about 11%.

And if you look at all of the factors, you've got the extreme right-hand side of the chart, you can see the combined ratio of this business mathematically should drift down quite dramatically over time. So, if we can keep doing what we're doing, that 11% margin on the back book, it's going to grow and grow as the business gets bigger and the expense levels come down, and it will add to the combined ratio coming down. So, our deep believe is while the business turn to profitability, its power over time I think is quite dramatic.

Let me end off by just making the point that we rolled out Discovery Business Insurance during those period. I think the product offering is absolutely remarkable. It really does interpret the idea of Shared-Value in a business perspective, that's around focusing not on the big corporates, but on the commercial side of the market, which is not insignificant. We're making available all of our driving technology. So small SMEs, for the first time, can operate their own fleets and the same day have the ability as an owner to see where your drivers are, how they're driving, incentivize them to drive better, so making those fleets run better. The coverage itself covers things like intangibles, like reputation or cyber risk. So, things that are modern. So, the coverage itself is powerful.

And then, the interpretation of Shared-Value also extends to the business itself. Our belief is that a well-run business is probably a low-risk. So we used learnings from Endeavour in building businesses to try and help companies who join us. And the simple idea is we kind of curated a bunch of partners and working with Endeavour, trying to help companies be better companies. If you join Discovery Insure, we can offer you access to diagnostic test of how well you're running your business; access to capital, do you need technology, do you need financial reporting tools, et cetera, et cetera.

The idea is using our buying power and our learnings to make the companies we cover better. We think in that process, the whole selection, behavioral effect will come out. A very deep conviction that a well-run small business is probably a lower risk to us, so interpreting Shared-Value I think, in a slightly different way, we have a great hopes for the business insurance model and quite confident that it's going to do well for the business.

So, I've been going here way, way too long. Let me end off where I started and just say it's been a remarkably good year. The context remains has been the 2018 Ambition. The performance of the group, I think, has been strong with a 16% increase in headline earnings.

All of our businesses are profitable. All, I think, are well positioned. Discovery Bank, we hope to launch during this year. Slight delay in some of the work we've done the first year, and I think the joint decision between us to acquire the equity is the right one. We'll be issuing our own equity in order to fund that transaction.

And then, finally, I think our businesses are very well positioned, South Africa, the UK, international, and by established, emerging, and new. I'm very excited about where we are. To make the point that we are – everything we do I hope is clear, we are strongly a South African company despite our globalization, great belief is in our countries.

These are difficult times for the country, but we are optimistic, building, investing. It's worthwhile saying some of the steps that over the last five years we've created net 5,000 new jobs within the Discovery head office capability and we're investing considerably buildings, banks, new business. So, we are optimistic and excited and moving forward. We urge you to do the same. Exciting times.

Can I end off by thanking you and maybe making the point – we've actually set half an hour, I think we're spot on time for Q&A session, have our CFO...

[Abrupt End]