

Liberty Financial Solutions
Operations and Strategic Direction
Giles Heeger, CEO

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Agenda

Why LibFin?

Achieving our strategic focus

- Managing to risk appetite
- Refining strategic objectives
- Infrastructure build
- LibFin now

Financial Performance

2011 and beyond

Why LibFin?

A changing industry

- **Regulatory changes**
- **Capital requirements and improved capital efficiency** necessitates tighter risk management
- **Complex product set**
- Financial accounting - **mark to market financial liabilities**
- **Financial markets**
 - more sophisticated and integrated
 - participants becoming increasingly sophisticated at pricing, managing and distributing risk
- **Solvency II on the horizon**

Driving significant change to how risk is viewed and managed at Liberty

Why should Liberty manage market risk

Significance of market risk in generating group profits



Managing risk should be a team's day job

Liberty's market risk is complex in nature - components of risk volatile and asymmetric

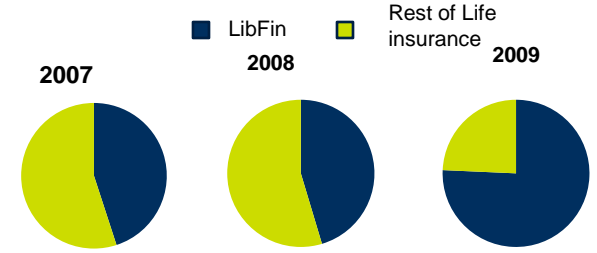


Specialist skill and infrastructure required to manage

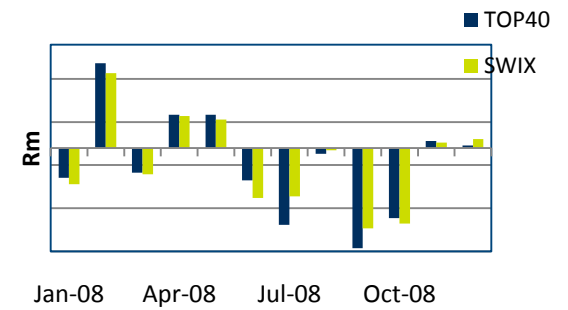
Opportunities to enhance product design



Leveraging capability of specialist team



Monthly P&L on R8 billion long position: TOP40 and SWIX



A specialist team focused on asset liability management and investment risk management is critical for the group to deliver on long term strategic objectives and remain competitive

Introducing a specialist capability

Pre - 2008

- Investment capability and infrastructure to manage market risk (asset liability management) significantly lags shifts in nature and complexity of risk and international best practice

2008

- Limits placed on the amount of earnings, economic capital, Return on Embedded Value, and CAR to be placed at risk in any given year – **Introduction of Risk Appetite Statement**
- Adoption of three manager model – middle manager comprises Group Risk and Capital Analytics (GRaCA) and Liberty Financial Solutions (LibFin)

2008 /
2009

- Shifting exposure to market, credit and liquidity risk in line with market risk appetite
- LibFin resourced

2009
onwards

- Appropriate risk management function in place

Achieving our strategic focus

LibFin's strategy: January 2009

Strategy

- Build excellence in the management of the balance sheet

Manage to risk appetite

- Outside risk appetite

Refining strategic objectives

- Retain and hold capital?
- Versus sell or dispose?
- Versus manage, if so to what objective, earnings or capital or EV, within what guidelines?

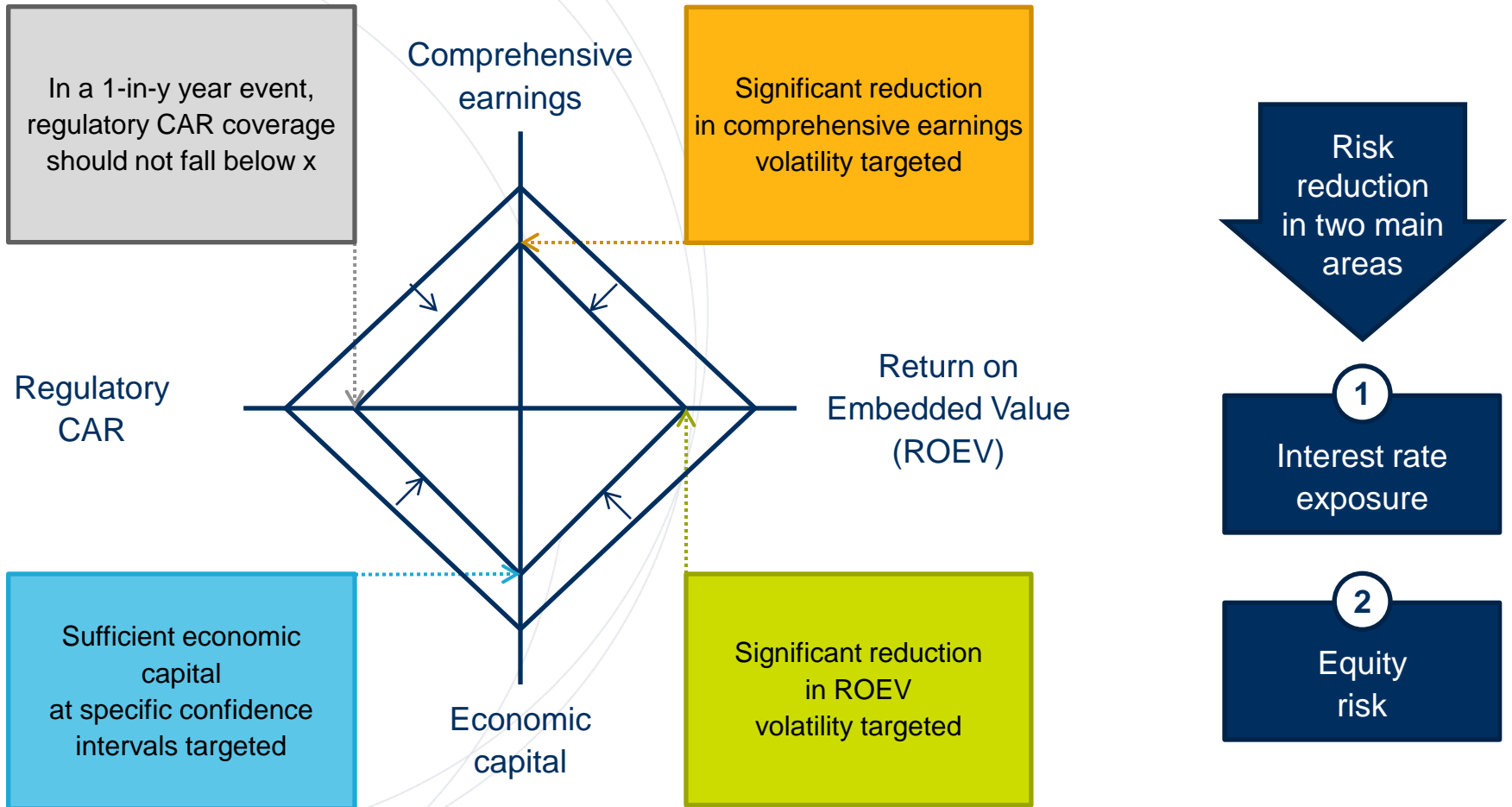
Infrastructure build

- Eg: Some positions not known (interest rate curve shape)
- Eg: Some positions can't be disaggregated into components(e.g. Volatility)
- Eg. Most position data stale and inaccurate

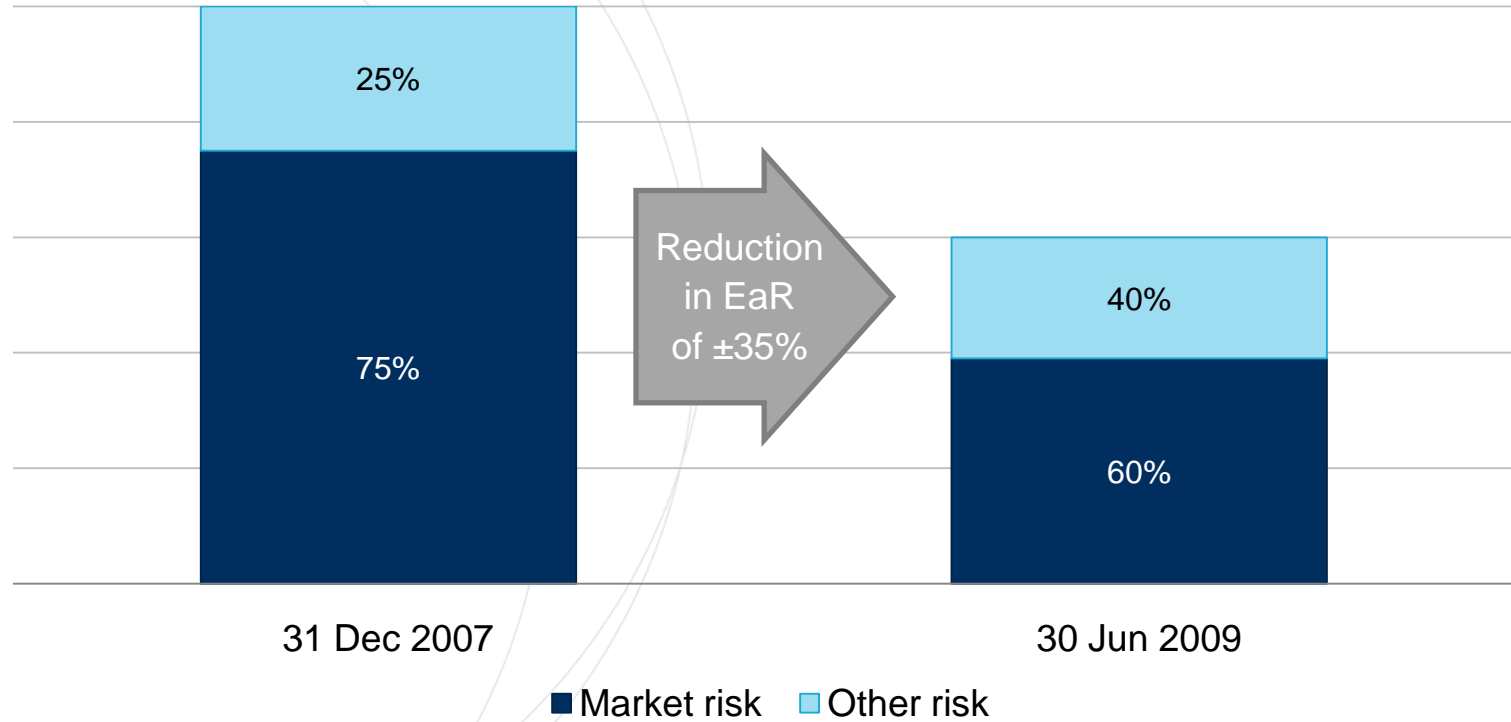


Managing to risk appetite

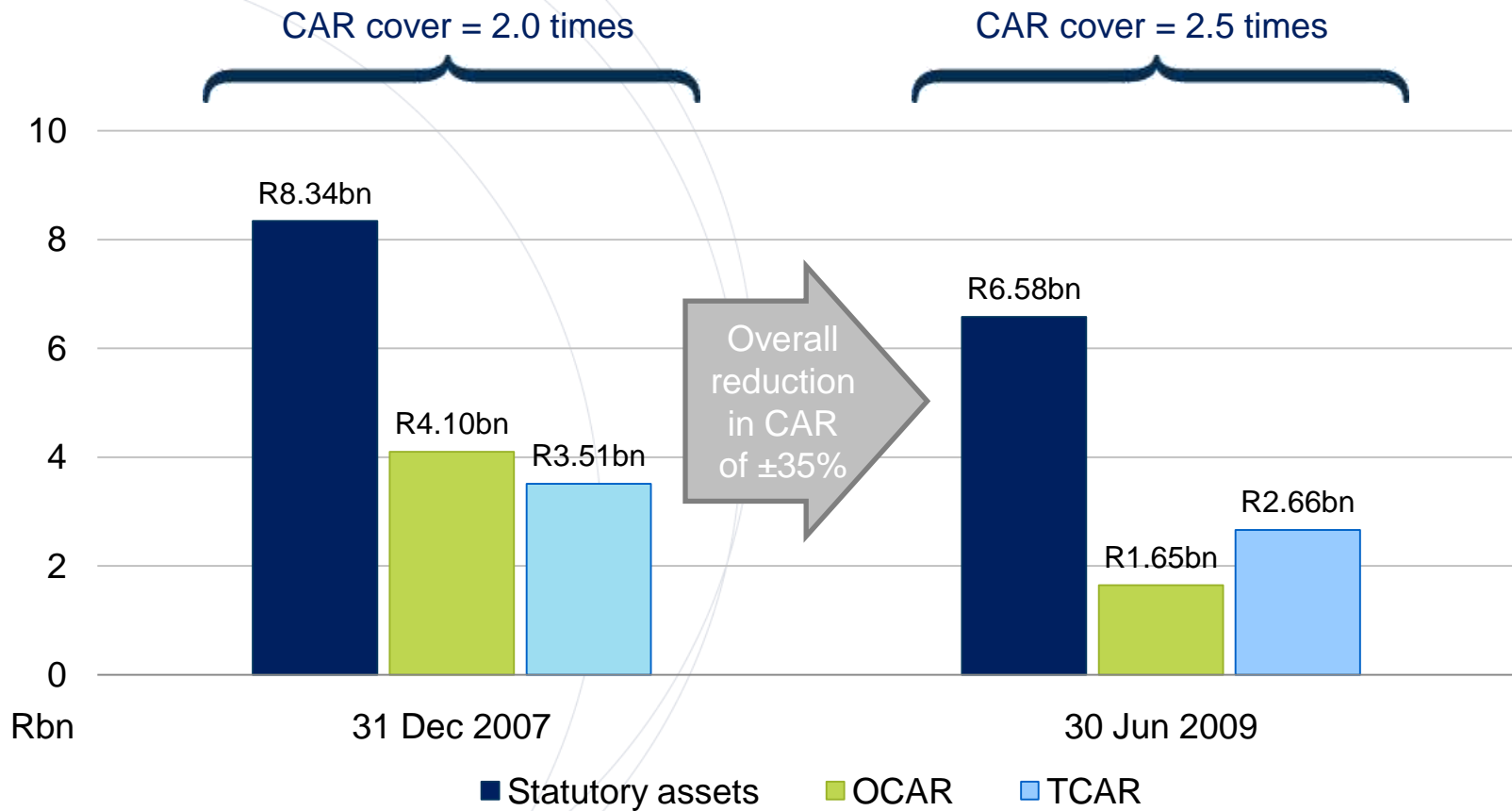
The de-risking strategy – achieving stated risk appetite framework



Impact of de-risking activities on earnings at risk



Impact of de-risking activities on CAR





Refining strategic objectives

Distinguishing between management strategies

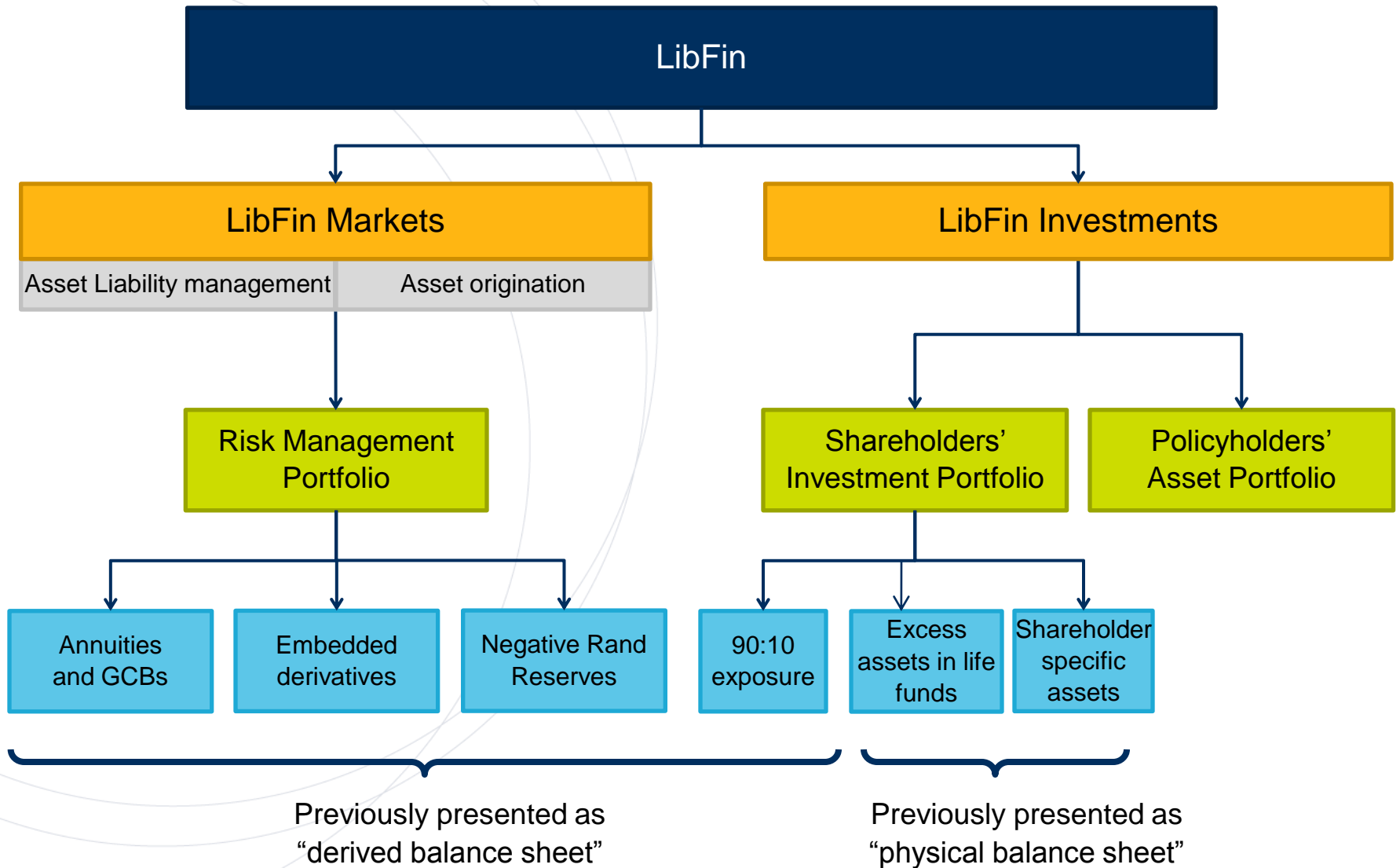
Market risk management (Asset Liability Management)

- Disposal of market risk originated by the insurance business at point of sale, which is not attractive to the organisation on a risk-to-reward assessment
- Risk is often complex and non-linear in nature and can be very capital intensive
- Profitable management of such risk requires a skill set usually found in Investment banks requiring: trading type skills, comprehensive risk management structures and daily position management

Investment management

- The business of being an insurer also generates opportunities to invest in market risk which is attractive on a risk-to-reward assessment in the long term, despite possibly exhibiting short-term volatility
- Such risk is usually linear and not particularly complex to quantify (although potentially more complex to forecast directionally)
- Profitable management of such risk requires a skill set usually found in asset managers or asset consultants requiring: portfolio management type skills, and long-term investment mindset, strategic asset allocation, tactical asset allocation and stock picking skills

LibFin structure



LibFin Markets: Objectives

- Manages market risk exposure from complex and long dated asset liability mismatches
 - Represented in Risk Management Portfolio and arising from:

Product book	Behaviour similar to
Annuities and Guaranteed Capital bonds (GCBs)	Fixed income and credit exposures
Embedded Derivatives (ED)	Exotic written options book
Negative Rand Reserves (NRR)	Accounting asset with bond like characteristics

- Extracting value by investing underlying annuity and GCB funds in a well diversified portfolio of government and corporate instruments

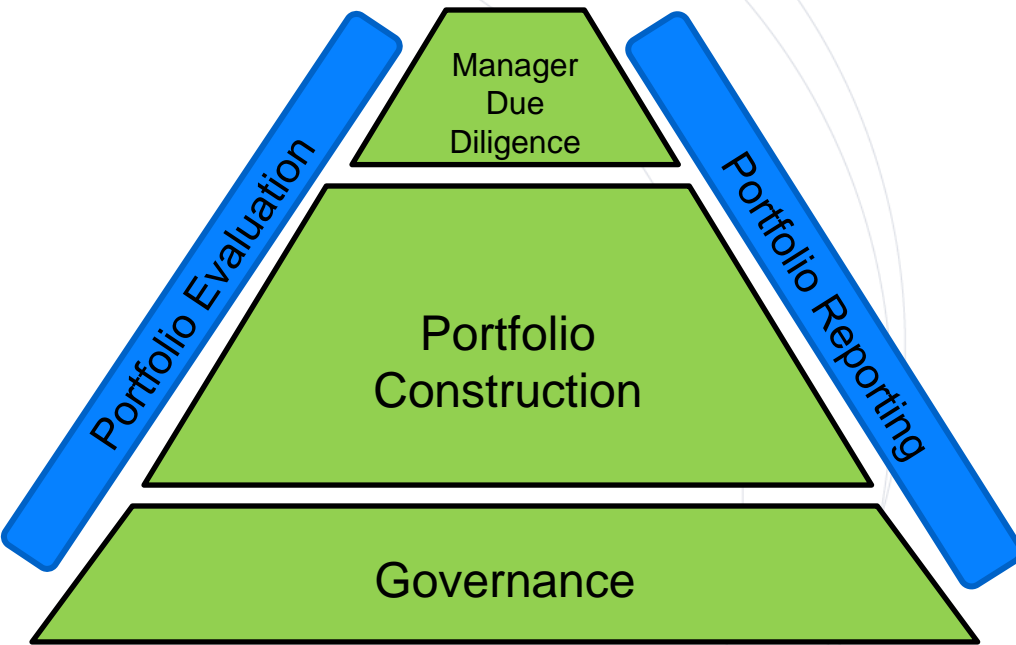
LibFin Markets: Implementation of objectives still in progress

Products	Key risks	De-risking level achieved	Market risks still inherent in business	Aim
Annuities, GCBs	<ul style="list-style-type: none"> • Interest rates • Credit spreads 	<ul style="list-style-type: none"> • Parallel and non-parallel movements in interest rates 	<ul style="list-style-type: none"> • Bond/swap basis • Credit spreads 	<ul style="list-style-type: none"> • Reduce basis risk • Remain strategically invested in credit risk
Embedded Derivatives	<ul style="list-style-type: none"> • Long dated interest rates • Equity funds • Property funds • Foreign asset funds • Volatility 	<ul style="list-style-type: none"> • Parallel movements in interest rates • Moderate equity moves • Moderate property moves • Moderate foreign moves 	<ul style="list-style-type: none"> • Non-parallel movements in interest rates • Basis (esp. bond/swap basis together with NRR) • Large equity moves • Large property moves • Large foreign moves • Volatility 	<ul style="list-style-type: none"> • Continue to reduce all of these market risks where : <ul style="list-style-type: none"> a) risks are quantifiable, and b) appropriate hedging instruments are available
Negative Rand Reserves	<ul style="list-style-type: none"> • Interest rates • Equity funds • Property funds • Foreign funds 	<ul style="list-style-type: none"> • Parallel movements in interest rates • Equity moves • Property moves • Foreign moves 	<ul style="list-style-type: none"> • Basis (esp. bond/swap basis together with ED) 	<ul style="list-style-type: none"> • Reduce basis risk

LibFin Investments: Objectives

- Responsible for ensuring asset managers deliver **investment performance** for policyholders and shareholders (R200 billion of assets)
- **Dedicated and skilled team** - competency leveraged across policyholder and shareholder funds
- Focusing on generating optimal risk adjusted returns over the long term on market risk exposure the group wishes to retain

Libfin Investments: Growing competency to ensure investment performance



■ 2008
■ 2009 / 2010

Adding rigour and accountability to this process

- Ensure appropriate risk / return objectives for both shareholders and policyholders
- Extract optimal value from asset managers through appropriate
 - **portfolio construction**
 - **performance evaluation**
 - **fee negotiations**
- Relevant governance over asset managers through
 - **due diligence**
 - **mandates**
 - **relationship management**
- Ongoing evaluation and monitoring of the portfolio performance – reporting back to the business
- Assisting with product innovation



Infrastructure Build

Libfin Markets: Build work and systems required

- Complete 2009
- Underway 2010
- To complete 2011



Annuities and GCB's



Embeddded derivatives



Certain information LibFin now receives daily would have taken one year to calculate under original process



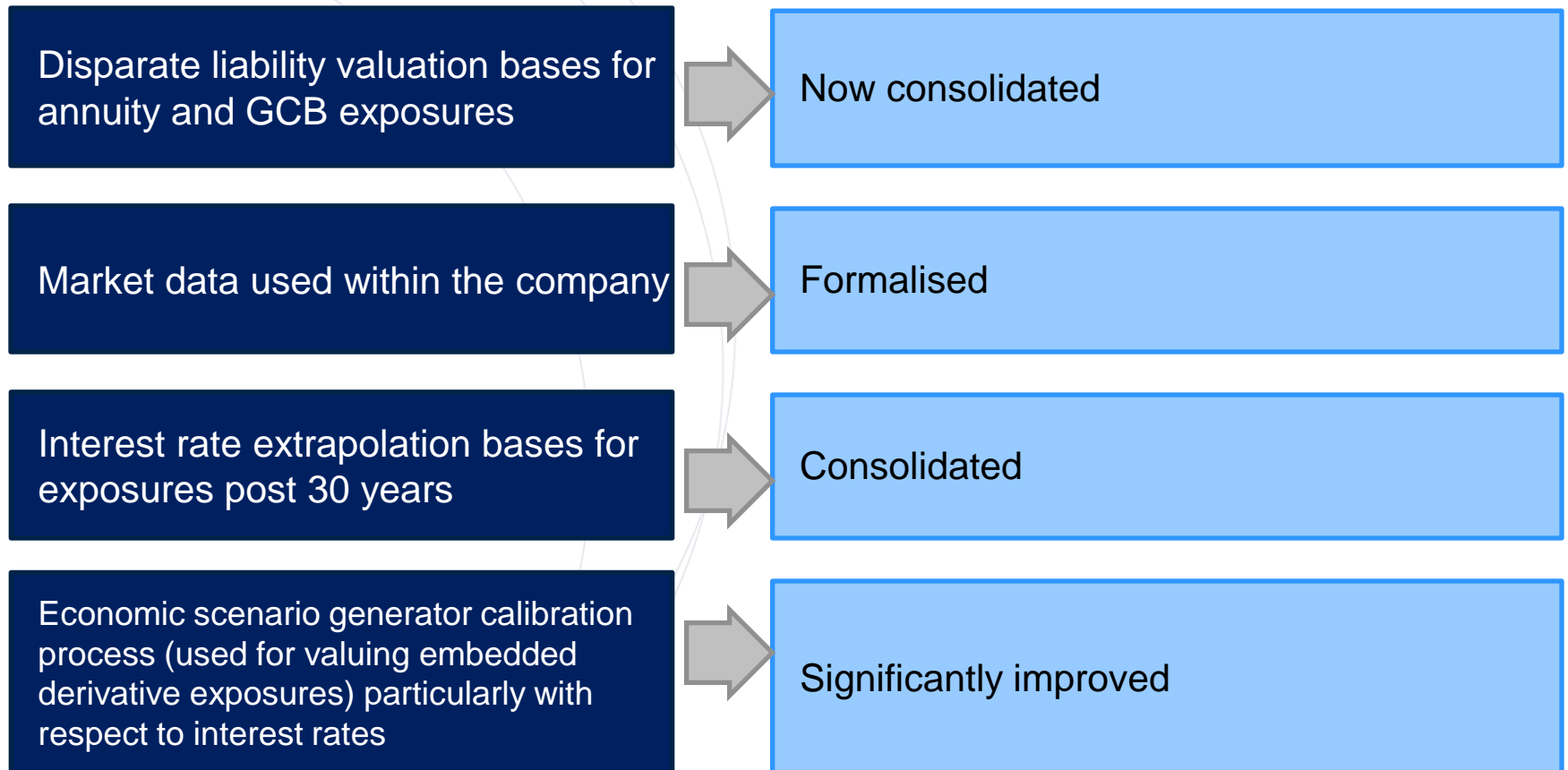
Process Re-engineering

Less reliance on skilled resource, more frequent and accurate data through automation

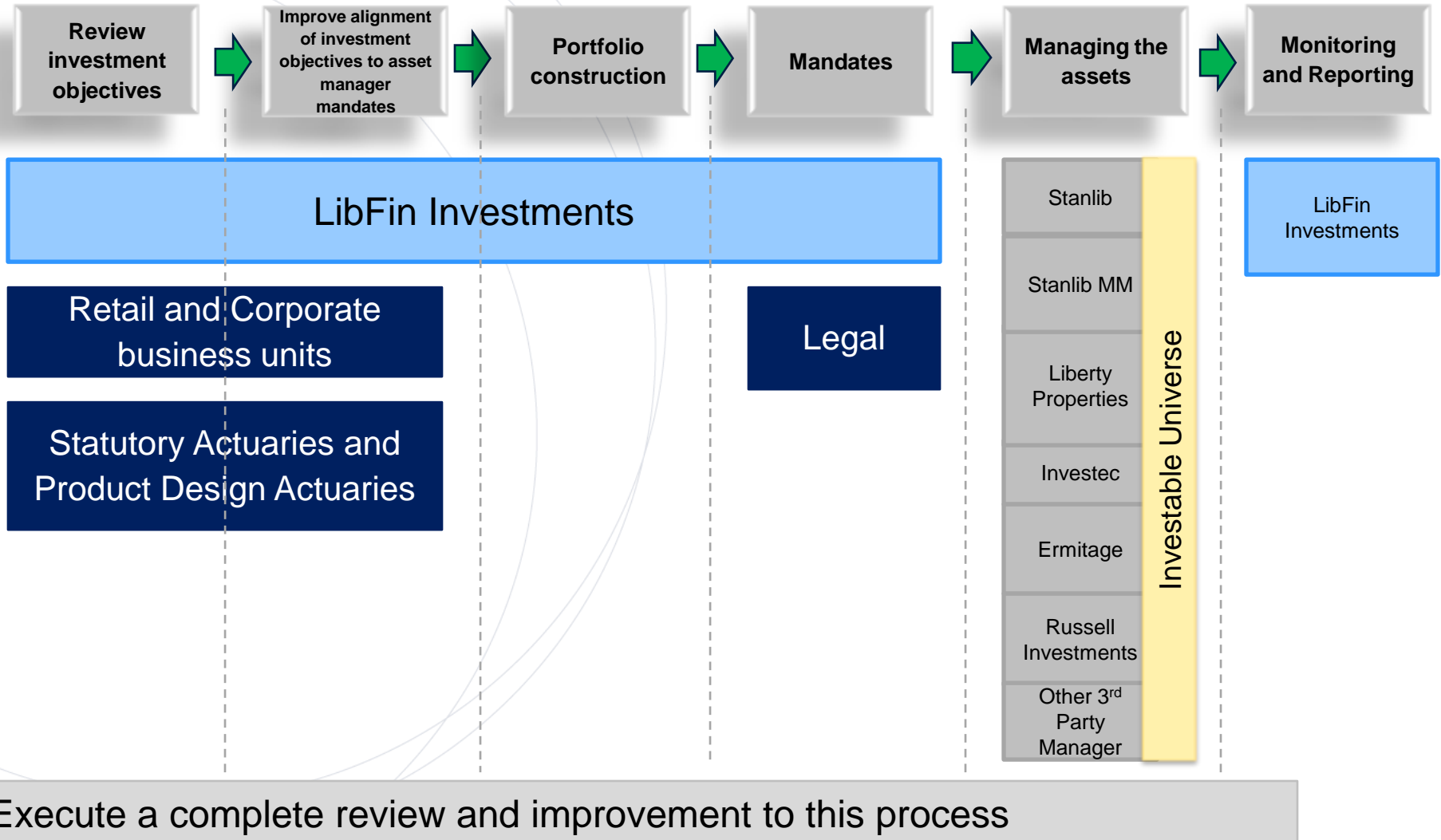
Valuation model improvement work

Significant build of infrastructure and systems already achieved – more to achieve before optimal functionality

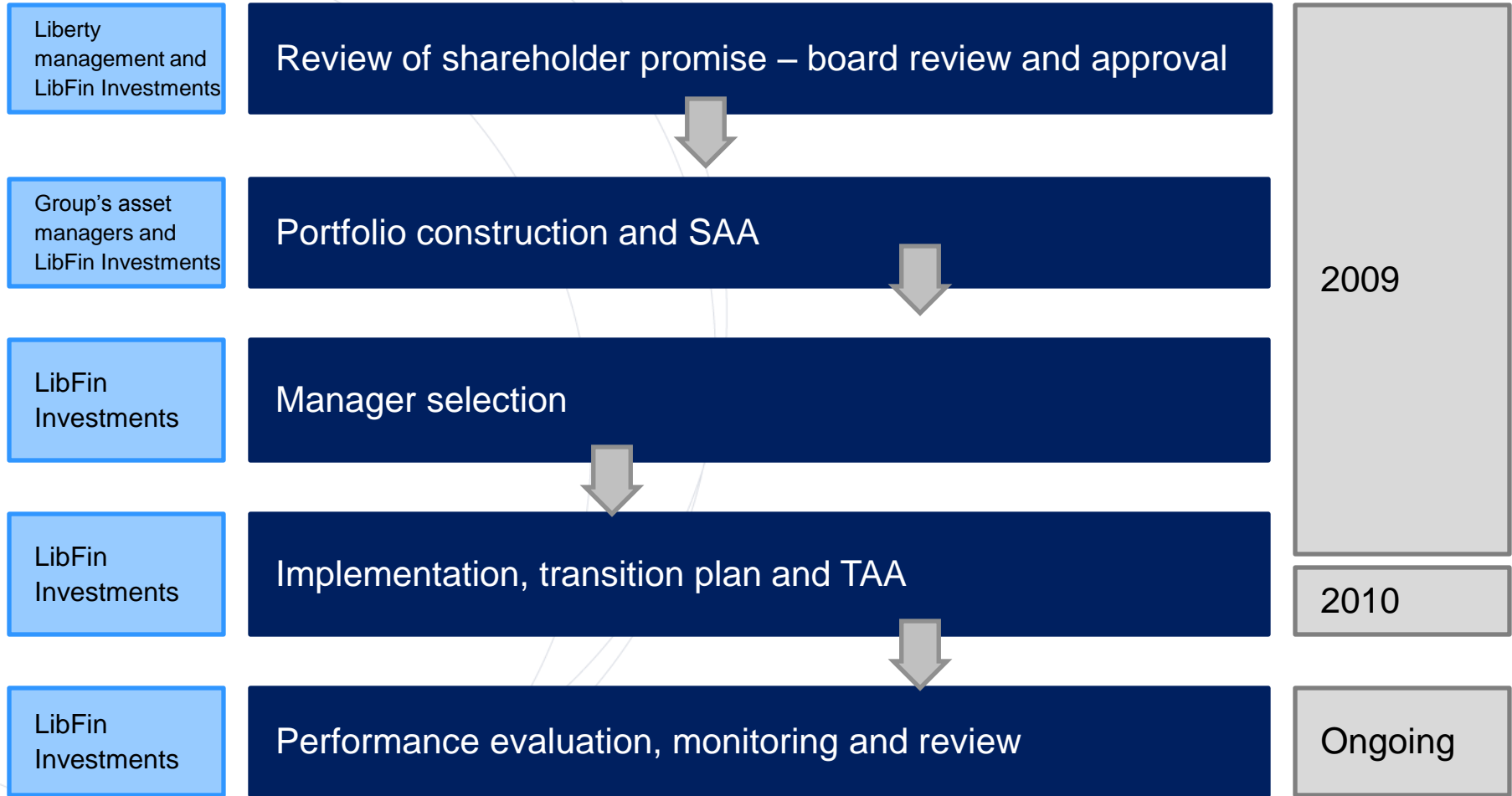
LibFin Markets: Valuation model improvements



LibFin Investments: Efficient and ongoing investment governance process required

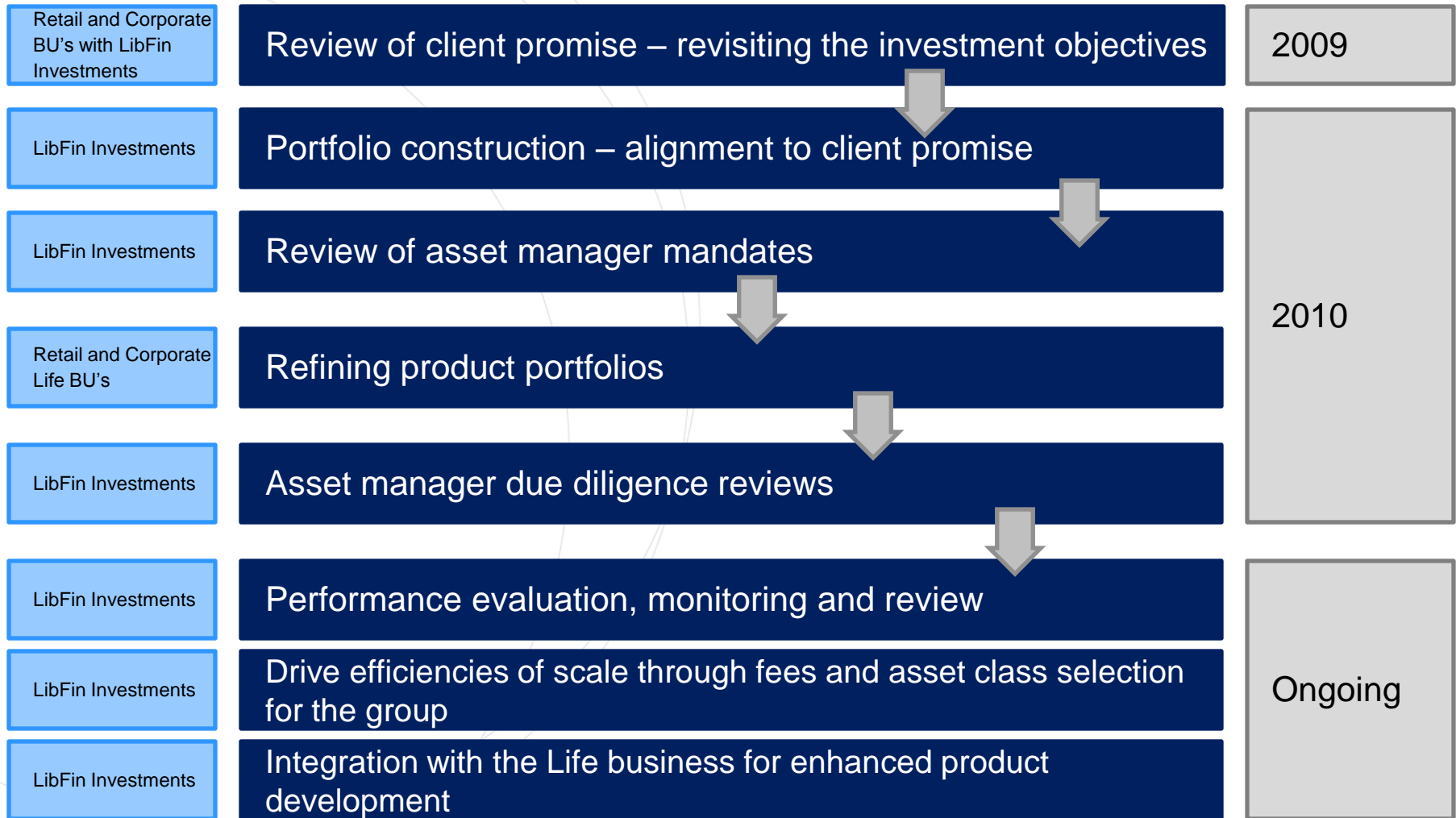


LibFin Investments: Management of Shareholder Investment Portfolio “SIP”



Management of SIP to improved process substantially addressed in 2009

LibFin Investments: Policyholder Investments



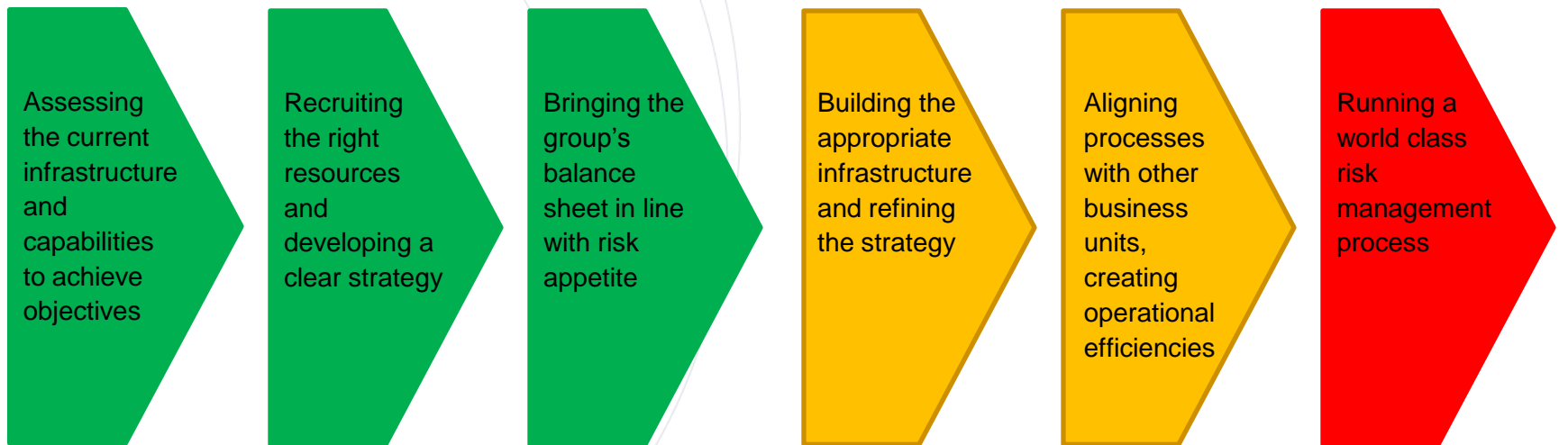
Management of Policyholder investments to improved process to be substantially addressed in 2009



LibFin now

Achieving our commitments

Asset liability management



Ensuring investment performance

2008



2009



2010



2011

Financial performance

LibFin – headline earnings by portfolio

Rm – net of tax	2H09	1H09	Dec 09	Dec 08	% Δ
Shareholders' Investment Portfolio	676	(462)	214*	564	-62
Risk Management (ALM)	473	(176)	297	(313)	>100
Equity de-risking	-	(519)	(519)	-	n/a
	1 149	(1 157)	(8)	251	n/a
Transfer to Retail SA Insurance: 90:10 planned margins	(98)	(142)	(240)	(318)	24
Headline earnings	1 051	(1 299)	(248)	(67)	n/a

* Includes 90:10 planned margins

LibFin – Shareholders' Investment Portfolio

Rm	Dec 09				Jun 09
	Shareholder specific assets	Excess assets in life funds	90:10 exposure	Total	Total
Local equities	686	562	2 250	3 498	2 590
Preference shares	1 450	10	-	1 460	1 460
Local cash, fixed income, property and other	5 644	2 134	1 125	8 903	9 070
Foreign currency holdings	1 565	281	805	2 651	3 080
Total	9 345*	2 987*	4 180	16 512	16 200

* Shareholder assets before deduction of callable bond and net current liabilities

Manage these assets

Taker of this exposure

Managing the portfolio requires a focus on the total position

Modelling LibFin Markets



Model now

	Whats different	Earnings stream impact	Sensitivities / Remaining risks resulting in earnings variability
Annuities and GCB's	Increased focus on managing rates risk and asset accumulation	<ul style="list-style-type: none"> • Small uplift in income from credit spreads • Minimal income from interest rates – managed within limits 	<ul style="list-style-type: none"> • Significant changes in credit spreads
Embedded Derivatives	Hedging out first order risks (rates equities, forex etc)	<ul style="list-style-type: none"> • Reduces income statement volatility 	Second order risks <ul style="list-style-type: none"> • Basis • Rates term structure • Large changes in asset prices (Gamma) • Volatility
Negative Rand Reserves	Hedging out first order risks (rates equities, forex etc)	<ul style="list-style-type: none"> • Reduces income statement volatility 	<ul style="list-style-type: none"> • Basis

Modelling LibFin Markets continued..



To model

	What could be different	Earnings stream / impact	Sensitivities / Remaining Risks
Annuities and GCB's	Nothing material in pipeline	• Growth of credit book	• Changes in credit spreads
Embedded Derivatives	Hedging out second order risk (basis, rates term structure, gamma, volatility)	• Further reduces income statement volatility	• Function of what is practically achievable
Negative Rand Reserves	Hedge basis	• Further reduces income statement volatility	• Not material

Modelling Libfin Investments

Portfolio definition	Whats different	Portfolio objective	Sensitivities / Risks
<p>Shareholder Investment Portfolio = Shareholder specific assets + 90:10 exposure + excess assets in life fund</p>	<p>Formalised strategic asset allocation for the entire Shareholder Investment Portfolio with set portfolio objectives resulting in a well diversified balanced portfolio</p>	<p>Maximise after tax returns on the SIP for a Board mandated level of risk appetite</p>	<ul style="list-style-type: none"> • Market performance of local and foreign asset classes • Currency movements • Asset manager performance

Model as a single portfolio which is similar to a conservative balanced asset portfolio

Conclusion – 2011 and beyond

Conclusion

- We remain committed to a strategy which we believe is appropriate best practice to manage risks of this nature in the current environment
- We believe in the longer term this strategy will deliver
 - Greater earnings stability
 - Ability to leverage product innovation without increasing capital consumption
 - Better investment performance for our life insurance customers
- Substantial infrastructure build is still required to deliver this strategy. Our build projects are on track and being well managed

A specialist team with world class infrastructure and rigorous processes



Questions?