



**The Federated Employers'
Mutual Assurance Company
(RF) Proprietary Limited**

**INTERIM REPORT
30 JUNE 2018**

Non-executive directors

NF Maas (Chairman)
H Walker (Lead Independent Director)
JR Barrow
JRT Headbush
MG Ilsley
K Imathiu
CS Jiyane
APH Jammine
MA Letshele
K Moodley
H Ngakane

Executive directors

NF Manyonga (Chief Executive Officer)
A Daya (Chief Financial Officer)
GM McIntosh (Chief Information Officer)

Company secretary

EJ Willis

Head office and registered address

2nd floor
Oxford & Glenhove
114 Oxford Road
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Private Bag 87109
Houghton
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Company registration number

1936/008971/07

www.fema.co.za

The Federated Employers' Mutual Assurance Company (RF) Proprietary Limited

(Registration No. 1936/008971/07)

INTRODUCTION

The Federated Employers' Mutual Assurance Company (RF) Proprietary Limited ("the Company") has pleasure in presenting its Interim Report for the six months ended 30 June 2018.

Basis of preparation and approval

This interim report has been prepared in compliance with IAS 34, "Interim Financial Reporting" and has been presented using the same accounting policies applied for the latest annual financial statements. These included a change in accounting policy on reserving for incurred but not reported (IBNR) claims introduced at the 2017 year end. This required a restatement of the previously reported claims expense and reserves for the comparative interim period ended 30 June 2017. The net effect was a decrease of R3 million in the previously reported net profit for the period ended 30 June 2017 with a corresponding increase in the IBNR component of the claims reserve at 30 June 2017. In addition, there was a reclassification between premiums raised on final and initial wage declarations for the comparative interim period ended 30 June 2017. This increased premiums raised on final wage declarations by R41 million and decreased premiums raised on initial wage declarations by the same amount with no net effect on the previously reported gross premium income for the period.

There have been no material post balance sheet events subsequent to 30 June 2018 up to the date of approval of this report. The interim report has not been subject to any audit or review by the Company's independent auditors.

The interim report was approved for issuance by the Company's board of directors on 28 August 2018.

Company profile

The Company is a short term insurer registered in terms of the Short Term Insurance Act. More specifically, the Company operates as a mutual association licensed under the Compensation for Occupational Injuries and Diseases Act ("COID Act") to carry on the business of insurance of certain classes of employers within the construction industry against their liabilities to employees in terms of the COID Act.

Owing to the mutual shareholding structure of the Company, it is classified as a private company under the South African Companies Act. However, the provisions of the Company's Memorandum of Incorporation ("MOI") make it subject to the same extended accountability provisions as are applicable to a public company. In addition, the MOI contains unalterable provisions designed to protect policyholders' interests by entrenching the mutual status of the Company.

The Company operates solely in the Republic of South Africa, however a portion of its investment income is earned from foreign investments.

FINANCIAL REVIEW

This review of the Company's financial performance is focused on the Company's underwriting and investment results and cash flows for the six months ended 30 June 2018 and its overall financial position at 30 June 2018. Unless otherwise specifically indicated, all comparisons made are to the prior half year ended 30 June 2017.

Highlights

- Gross premium income decreased by 3% to R915 million; net earned premium increased by 2% to R353 million
- Net claims and benefits increased by 14% to R216 million
- Administration expenses increased by R11 million to R76 million
- Accident prevention expenses and grants totalled R21 million, an increase of 33%
- Net investment income totalled R111 million, representing an annualised return on average investments of 3,7% (2017: 6,4%)
- Net profit decreased by 48% to R147 million for the period.

Financial results and cash flows

Gross premium income decreased by 3% to R915 million mainly as a result of the decrease in assessment rates as gazetted by the Compensation Fund.

Net claims and benefit expenses increased by 14% to R216 million, this increase was mainly attributable to an increase in the medical claims expenditure which was partly offset by a reduction in the pension valuation charge and reinsurance recoveries.

Accident prevention expenses and grants increased by 33% to R21 million, this increase includes an 8% increase to existing grant recipients and a timing difference in the payment of regulatory fees totaling R5 million.

Net investment income decreased by 47% to R111 million. This decrease has resulted from a lower annualised investment return of 3.7% (2016: 6.4%) on average assets.

Administration costs include R6 million for the newly established pensioners beneficiary project.

The Company continues to generate cash from operating activities with R213 million (2017: R530 million) generated during the six months.

Financial position

Total assets increased by R511 million over the interim period (i.e. from 31 December 2017 to 30 June 2018).

The Company's net asset value has increased from R3.110 billion at 31 December 2017 to R3.257 billion at 30 June 2018 and represents a very healthy capital position. The Company has also met its target of achieving a breakeven underwriting result of R37 million (2017: R73 million).

The accompanying interim financial statements for the six months ended 30 June 2018 were prepared under the supervision of the Chief Financial Officer, Mr A Daya (CMA, MBA)

STATEMENT OF FINANCIAL POSITION ("SOFP")

at 30 June 2018

	Note	6 months to June		December
		2018	2017	2017
		R'000	Restated R'000	R'000
ASSETS				
Property, equipment and motor vehicles		71 610	5 927	72 780
Reinsurance assets		13 087	1 742	20 027
Financial assets at fair value through profit or loss	1	6 552 946	6 739 544	6 260 077
Other financial assets measured at amortised cost				
Insurance receivables		148 208	76 199	10 487
Other receivables		41 855	27 567	17 448
Cash and cash equivalents		107 745	61 498	43 310
Total assets		6 935 451	6 912 477	6 424 129
EQUITY AND LIABILITIES				
Ordinary share capital		10	10	10
Retained income	SOCE	3 257 049	2 828 658	3 109 606
Total equity		3 257 059	2 828 668	3 109 616
Insurance liabilities		3 554 815	3 303 674	2 957 234
Pension liabilities	2	1 716 669	1 574 268	1 697 661
Unpaid claim liabilities	3	588 820	522 750	567 764
Unearned premium liabilities		567 110	578 414	146 975
Premium rebate liabilities	4	682 216	628 242	544 834
Financial liabilities measured at amortised cost				
Trade and other payables	6	123 577	780 135	357 279
Total liabilities		3 678 392	4 083 809	3 314 513
Total equity and liabilities		6 935 451	6 912 477	6 424 129

STATEMENT OF COMPREHENSIVE INCOME ("SOCI")

for the six months ended 30 June 2018

	Note	6 months to June		December
		2018	2017	2017
			Restated	
		R'000	R'000	R'000
Gross premium income		915 258	944 156	985 699
Premiums raised on initial wage declarations for the current year		858 429	867 509	909 011
Premiums raised on final wage declarations for the previous year		56 829	76 647	76 688
Annual rebates to policyholders		(137 419)	(142 262)	(320 627)
Unearned premium		(420 133)	(450 254)	(18 815)
Gross earned premium		357 706	351 640	646 257
Insurance premium ceded to reinsurers		(4 363)	(4 517)	(9 689)
Net earned premium		353 343	347 123	636 568
Gross claims and benefits		(228 911)	(191 792)	(526 374)
Gross claims expense		(210 630)	(169 368)	(427 170)
Claims recoveries		4 709	6 122	12 317
Pension valuation charge	2	(22 990)	(28 546)	(111 521)
Claims recovered from reinsurers		13 226	2 094	27 611
Net claims and benefits		(215 685)	(189 698)	(498 763)
Underwriting profit before operating expenses		137 658	157 425	137 805
Administration expenses		(75 560)	(64 138)	(137 494)
Impairment of insurance receivables		(4 495)	(4 174)	(10 814)
Accident prevention expenses and grants		(21 102)	(15 901)	(26 251)
Underwriting profit / (loss) before investment income		36 501	73 212	(36 754)
Net investment income	5	110 941	208 703	599 617
Investment income		121 576	220 347	618 539
Investment expenses		(10 635)	(11 644)	(18 922)
Net profit for the period		147 442	281 915	562 863
Other comprehensive income		-	-	-
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		147 442	281 915	562 863

STATEMENT OF CHANGES IN EQUITY ("SOCE")

for the six months ended 30 June 2018

	Stated capital	Retained income	TOTAL
	R'000	R'000	R'000
Opening balance at 1 January 2017 as previously stated	10	2 742 926	2 742 936
Effect of change in accounting policy	-	(196 182)	(196 182)
Opening balance at 1 January 2017 as restated	10	2 546 744	2 546 754
Net profit for the period as restated	-	281 915	281 915
Closing balance at 30 June 2017 as restated	10	2 828 659	2 828 669
Net profit for the period	-	280 947	280 947
Closing balance at 31 December 2017 as presented	10	3 109 606	3 109 616
Net profit for the period	-	147 442	147 442
Closing balance at 30 June 2018	10	3 257 049	3 257 059

STATEMENT OF CASH FLOWS ("SOCF")

for the six months ended 30 June 2018

	<u>6 months to June</u>		<u>December</u>
	<u>2018</u>	<u>2017</u>	<u>2017</u>
	<u>R'000</u>	<u>R'000</u>	<u>R'000</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Net profit for the period	147 442	281 915	562 863
Adjustments for depreciation and other operating activities:	(23 949)	(133 921)	(469 877)
Depreciation	3 032	1 370	3 293
Impairment of insurance receivables	4 495	4 175	10 814
Net foreign currency gain on financial assets	(36 791)	(55 204)	(65 104)
Net valuation loss / (gain) on financial assets measured at fair value	5 326	(85 126)	(419 751)
Net profit/(loss) on disposal of furniture, equipment and motor vehicles	(11)	864	871
Net movements in operating assets and liabilities	212 124	489 961	264 550
Reinvestment of interest and dividend income	(122 730)	(107 619)	(220 443)
Cash generated from operating activities	212 887	530 336	137 093
Net payments to FEM Education Foundation	-	-	(465 510)
Cash generated / (utilised) from operating activities	212 887	530 336	(328 417)
CASH FLOWS FROM INVESTING ACTIVITIES			
Net (investment) / disinvestment in financial assets measured at fair value	(146 600)	(669 346)	240 002
Purchases of furniture, equipment and motor vehicles	(1 872)	(1 262)	(70 305)
Proceeds on disposals of furniture, equipment and motor vehicles	20	-	260
Cash applied to investing activities	(148 452)	(670 608)	169 957
Net increase / (decrease) in cash and cash equivalents for the period	64 435	(140 272)	(158 460)
Cash and cash equivalents at beginning of period	43 310	201 770	201 770
Cash and cash equivalents at end of period	107 745	61 498	43 310

Notes to the statement of financial position

	<u>6 months to June</u>		<u>December</u>
	<u>2018</u>	<u>2017</u>	<u>2017</u>
	<u>R'000</u>	<u>R'000</u>	<u>R'000</u>
1. Financial assets at fair value through profit or loss			
Local:			
- Listed equity securities	1 394 590	1 527 105	1 469 527
- Listed debt securities: fixed interest rate	279 544	278 192	302 544
- Listed debt securities: inflation linked	1 125 502	1 254 824	1 123 754
- Corporate debt securities with derivative overlay (note 1)	458 797	372 399	457 958
- Money market investments	1 415 180	1 423 826	1 014 587
	<u>4 673 613</u>	<u>4 856 346</u>	<u>4 368 370</u>
Foreign:			
- Listed equity securities	1 546 355	1 492 873	1 539 045
- Corporate debt securities with derivative overlay (note 1)	119 470	162 196	117 178
- Derivative foreign exchange contracts	(17 436)	(3 447)	18 975
- USD cash	12 569	61 299	13 419
- Pooled unlisted equity securities	186 628	140 959	172 950
	<u>1 847 586</u>	<u>1 853 880</u>	<u>1 861 567</u>
Accrued income	10 541	9 273	9 480
Assets under management	<u>6 531 740</u>	<u>6 719 499</u>	<u>6 239 417</u>
Enterprise development fund	21 206	20 045	20 660
Total financial assets at fair value through profit or loss	<u>6 552 946</u>	<u>6 739 544</u>	<u>6 260 077</u>

Note 1

The Company has invested through investment-linked insurance policies into illiquid, unlisted and listed local and foreign corporate bonds with maturity dates of up to 7½ years. As part of the so-called “credit opportunities/alpha transport” product structure:

- interest rate duration and currency risks on the bonds are immunised through interest rate swaps into short term rates and currency swaps into Rands; and
- the Company purchases equity forward contracts for the same nominal value as the aggregate value of the corporate bonds.

Thus the Company effectively receives a local equity market return (based on an approximation of the JSE SWIX Total Return Index) plus the credit and liquidity spread on the bonds. Note that the corresponding capital amount invested is exposed to both equity pricing risk on the relevant market indices and credit default risk on the separate corporate bonds.

Notes to the statement of financial position

	<u>6 months to June</u>		<u>December</u>
	<u>2018</u>	<u>2017</u>	<u>2017</u>
	<u>R'000</u>	<u>Restated R'000</u>	<u>R'000</u>
2. Pension liabilities			
Opening balance	1 697 661	1 546 935	1 546 935
Movement for the period:	19 008	27 333	150 726
Pensions paid during the period	(53 615)	(47 026)	(95 914)
New pension awards (transferred from unpaid claims liabilities)	49 633	45 813	135 119
Net valuation charge to profit or loss	22 990	28 546	111 521
Closing balance	<u>1 716 669</u>	<u>1 574 268</u>	<u>1 697 661</u>
3. Claims Provisions			
Unpaid reported claims	254 126	209 408	254 422
IBNR Provision	265 214	248 249	248 249
Claims handling expenses	69 480	65 093	65 093
	<u>588 820</u>	<u>522 750</u>	<u>567 764</u>
<i>The movement in claims provisions is analysed as follows:</i>			
Opening balance	567 764	504 560	504 560
Gross claims and benefits expense for the year	228 911	191 792	526 374
Claims paid	(158 222)	(127 789)	(328 050)
Pensions awarded	(49 633)	(45 813)	(135 119)
Closing balance	<u>588 820</u>	<u>522 750</u>	<u>567 764</u>
4. Premium rebate liabilities			
Annual premium rebate liabilities relating to:			
Underwriting year ended February 2016	249 205	236 797	-
Underwriting year ended February 2017	295 629	249 205	249 205
Underwriting year ended February 2018	137 382	142 240	295 629
Total premium rebate liabilities	<u>682 216</u>	<u>628 242</u>	<u>544 834</u>

Notes to the statement of comprehensive income

	<u>6 months to June</u>		<u>December</u>
	2018	2017	2017
	R'000	R'000	R'000
5. Net investment income			
Investment income	121 576	220 347	618 539
Interest income	98 354	77 491	168 678
Dividend income	28 090	30 128	49 637
Net foreign currency gain on financial assets	36 791	55 204	65 104
Net valuation (loss) / gain on financial assets measured at fair value	(37 945)	85 126	419 751
Investment income attributable to FEM Education foundation	(3 714)	(27 602)	(84 631)
Investment expenses	(10 635)	(11 644)	(18 922)
Asset management and reporting fees	(7 084)	(11 308)	(18 052)
Performance fees	(3 551)	(336)	(870)
Total net investment income	110 941	208 703	599 617

The net valuation gain on financial assets measured at fair value incorporates any interest and dividends earned on pooled funds.

Certain of the Company's mandated asset managers offset their investment fees and transactional costs in unit pricing and, consequently, these expenses are incorporated in the net valuation gain on financial assets measured at fair value. Where investment expenses are explicitly disclosed by asset managers, these are included in the investment expense line item.

6. Trade and other payables

Trade and other payables includes the following balances in respect of the amount to be paid to the newly established FEM Education Foundation NPC:

Opening balance	280 882	746 392	750 000
Movement for the period:			
Financial assets transferred	(225 264)	-	(518 017)
Beneficiary payments made	-	(35 000)	(35 197)
Directors Fees	(39)	-	(21)
Asset consulting and legal fees incurred	(333)	(381)	(514)
Accrued investment income	3 714	27 602	84 631
Closing balance	58 960	738 613	280 882

As previously reported on 19 October 2016, the Company's Shareholders approved the payment of R750 million to an educational fund that was established as a corporate social investment initiative by the Company and, by association, its policyholders and the wider construction industry.

7. Income tax

The Company is exempt from income tax in accordance with section 10(1)(t)(xvi)(cc) of the Income Tax Act.