



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

INTERIM REPORT

30 JUNE 2020

Non-executive directors

NF Maas (Chairman)
H Walker (Lead Independent Director)
JR Barrow
MG Ilsley
K Imathiu
CS Jiyane
MA Letshele
A Moiloa (Appointed 01 July 2020)
H Ngakane

Executive directors

NF Manyonga (Chief Executive Officer)
Y Bodiat (Chief Financial Officer)

Company secretary

EJ Willis

Head office and registered address

2nd floor
Oxford & Glenhove
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Company registration number

1936/008971/07

www.fem.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 2020.

Basis of preparation

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, with the following classification changes having been made to line items in the Statement of Comprehensive Income:

1. The pension valuation charge has been moved below the underwriting results to provide a more meaningful measurement of underwriting performance in relation to the Company’s stated objective of achieving a breakeven result.
2. Investment management expenditure has been moved from operating expenses to be deducted from investment income to provide a clearer presentation of net investment performance.

The above classification changes had no net impact on reported results nor any effect on the presentation of the Company's financial position or cash flows. Consequently, it has not been necessary to present a third balance sheet as would otherwise be required by IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors.

Company profile

The Company is a short-term insurer, and more specifically, 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 Insurance Act make it subject to the same extended accountability provisions as are applicable to a public company. In addition, the Company’s Memorandum of Incorporation 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 2020 and its overall financial position at 30 June 2020. Unless otherwise specifically indicated, all comparisons made are to the prior half year ended 30 June 2019.

Key performance indicators

- Gross premium income decreased by 7% to R773 million
- Gross claims and benefits decreased by 36% to R139 million
- Operating expenses increased by 4% to R87 million
- Accident prevention and grant expenditure was maintained at R22 million
- Underwriting profit before investment income of R60 million
- Net investment income of R221 million despite challenging markets
- Overall net profit for the half year of R357 million (2019: R293 million)

Financial results and cash flows

Gross premium income decreased by 7% to R773 million. This is mainly as a result of the significant challenges facing the construction industry in recent years, which has been exacerbated by the nationwide lockdown resulting from the COVID-19 pandemic where a large portion of the industry was unable to operate. Given that the gross premium income comprises of both financial adjustments for 2019 and initial estimates for 2020, the real impact of COVID-19 may only become apparent in 2021 when policyholders submit their actual wage returns for 2020.

Net claims and benefit expenses decreased by 36% to R139 million, which was mainly attributable to the reduced business activity caused by the nationwide lockdown.

Operating expenses increased by R4 million to R87 million for the half year.

Net investment income decreased to R221m, attributable to strong performance on offshore equities compensating for negative returns on local equities. This represents an annualized return on average assets of 6.6% and is a most satisfactory result given the challenging investment market environment.

There was a net pension valuation gain of R98 million which resulted largely from changes in the economic assumptions applied in the actuarial valuation of the pension liabilities.

The Company remains cash generative, recording positive operational cash flows of R10 million for the half year. This is much lower than the cash generated in the prior half year as a result of the decision to allow policyholders to settle their annual premiums on a monthly basis for 2020. This deferral is reflected in the significant increase in insurance receivables.

Financial position

Total assets increased by R691 million over the interim period, totalling R7.5 billion at 30 June 2020.

The Company's net asset value increased in line with net profit to R3.9 billion at 30 June 2020. This represents a healthy capital position aligned to the Company's long-term strategic objectives.

The Company is required to hold sufficient capital to meet the regulatory solvency requirements in terms of the Insurance Act of 2017 and the Prudential Standards set out by the Prudential Authority. As at 30 June 2020, the Company's Solvency Capital Requirement (SCR) cover ratio was calculated at 1.93x. This represents a healthy solvency position.

The accompanying interim financial statements for the six months ended 30 June 2020 were prepared under the supervision of the Chief Financial Officer, Mr Y Bodiat CA (SA).

Events after the reporting period

As a result of the COVID-19 pandemic and its negative impact on the construction industry, FEM has embarked on initiatives to assist the industry during these challenging times. This includes a Board-approved initiative to grant loans to the industry for an initial amount of R200 million, which is to be administered through a newly incorporated subsidiary. Loan funding from FEM to this wholly owned subsidiary requires approval from both shareholders and the Prudential Authority. The approval from shareholders was obtained at a Special General Meeting held on 12 August 2020, with the approval from the Prudential Authority still pending at the date of approval of this interim report.

There have been no other material events from 30 June 2020 up to the date of approval of this report.

Approval

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 27 August 2020.

STATEMENT OF FINANCIAL POSITION ("SFP")
at 30 June 2020

	Note	6 months to June		December
		2020	2019	2019
		Rm	Rm	Rm
ASSETS				
Property and equipment		73	69	75
Computer software		12	0	5
Reinsurance assets		2	4	4
Financial assets invested through asset managers	1	6 737	6 158	6 390
Investments at fair value through profit or loss		6 709	6 132	6 361
Cash held in bank accounts operated by asset managers		28	26	29
Other financial assets at fair value through profit or loss	2	135	736	294
Other financial assets measured at amortised cost		572	211	72
Insurance receivables		475	117	0
Other receivables		31	30	39
Cash and cash equivalents	SOCE	66	64	33
Total assets		7 531	7 178	6 840
EQUITY AND LIABILITIES				
Stated capital		0	0	0
Retained profit	SOCE	3 888	3 331	3 531
Total equity		3 888	3 331	3 531
Insurance liabilities		3 581	3 800	3 238
Pension liabilities	3	1 763	1 901	1 876
Claims provisions	4	673	639	677
Unearned premium liabilities		485	552	141
Premium rebate liabilities	5	660	708	544
Financial liabilities measured at amortised cost				
Trade and other payables		62	47	71
Total liabilities		3 643	3 847	3 309
Total equity and liabilities		7 531	7 178	6 840

STATEMENT OF COMPREHENSIVE INCOME ("SOCI")
for the period ended 30 June 2020

	Note	6 months to June		December
		2020	2019	2019
		Rm	Rm	Rm
Gross premium income		773	833	857
Premiums raised on initial wage declarations for the current year		725	812	837
Premiums raised on final wage declarations for the previous year		48	21	20
Annual rebates to policyholders		(120)	(125)	(250)
Unearned premium		(344)	(409)	2
Gross earned premium		309	299	609
Insurance premium ceded to reinsurers		(6)	(5)	(10)
Net earned premium		303	294	599
Gross claims and benefits		(139)	(217)	(503)
Gross claims expense	4	(145)	(233)	(528)
Claim recoveries from Road Accident Fund		6	16	25
Claims recovered from reinsurers		5	13	33
Net claims and benefits		(134)	(204)	(470)
Underwriting profit before operating expenses		169	90	129
Operating expenses		(87)	(83)	(162)
Impairment of insurance receivables		0	(5)	(26)
Accident prevention expenses and grants		(22)	(21)	(27)
Underwriting profit/(loss)		60	(19)	(86)
Net investment income	6	221	453	652
Investment income		233	464	674
Investment expenses (where separately identifiable)		(12)	(11)	(22)
Pension valuation release/(charge)	3	98	(132)	(58)
Finance costs		(58)	(57)	(125)
Pension valuation gain/(loss)		156	(75)	67
Net profit for the year before special payments		379	302	508
Special payments		(22)	(9)	(15)
Pensioner beneficiary assistance program		(9)	(9)	(15)
Lump sum payment to pensioners		(3)	0	0
Donations - COVID-19 relief measures		(10)	0	0
Net profit for the year		357	293	493
Other comprehensive income		0	0	0
PROFIT AND OTHER COMPREHENSIVE INCOME		357	293	493

**STATEMENT OF CHANGES IN EQUITY ("SOCE")
for the six months ended 30 June 2020**

	Stated capital*	Retained profit	Total
	Rm	Rm	Rm
Balance at 1 January 2019	0	3 038	3 038
Loss and other comprehensive income for the period (SOCl)	0	293	293
Balance at 30 June 2019	0	3 331	3 331
Profit and other comprehensive income for the period (SOCl)	0	200	200
Closing balance at 31 December 2019	0	3 531	3 531
Profit and other comprehensive income for the period (SOCl)	0	357	357
Closing balance at 30 June 2020	0	3 888	3 888

* Stated capital totals R10 000 rounded to R0m

**STATEMENT OF CASH FLOWS ("SOCF")
for the six months ended 30 June 2020**

	Notes	6 months to June		December
		2020	2019	2019
		Rm	Rm	Rm
CASH FLOWS FROM OPERATING ACTIVITIES				
Net profit for the year	SOCI	357	293	493
Adjustments for depreciation and other non-cash items:		3	7	32
Depreciation		3	2	6
Impairment of insurance receivables		0	5	26
Reinvestment by asset managers of net investment income	6	(221)	(453)	(652)
Net movements in operating assets and liabilities		(129)	638	177
Cash generated from operations		10	485	50
CASH FLOWS FROM INVESTING ACTIVITIES				
Net disinvestment/(investment) of financial assets		33	(443)	(34)
Purchases of equipment and computer software		(10)	(1)	(6)
Cash generated from/(utilised in) investing activities		23	(444)	(40)
Net increase in cash for the period		33	41	10
Cash and cash equivalents at beginning of period		33	23	23
Cash and cash equivalents at end of period	SOFP	66	64	33

Notes to the interim financial statements

	<u>6 months to June</u>		<u>December</u>
	<u>2020</u>	<u>2019</u>	<u>2019</u>
	Rm	Rm	Rm
1. Financial assets invested through asset managers			
Investments designation at fair value through profit or loss			
Local financial assets	3,355	3,340	3,370
Listed equity securities	694	824	811
Listed debt securities: fixed interest rate	781	624	697
Listed debt securities: inflation linked	1,682	1,592	1,618
Money market funds	198	300	244
Foreign financial assets	2,629	2,067	2,257
Listed equity securities	2,379	1,840	2,023
Derivative foreign exchange contract	(2)	1	2
Pooled unlisted equity securities	252	226	232
Corporate debt securities with derivative overlay *	709	645	715
Local assets	481	460	537
Foreign assets	228	185	178
Accrued investment income	16	18	19
Total investments at fair value through profit or loss	6,709	6,070	6,361
Cash held in bank accounts operated by asset managers	28	88	29
Total financial assets invested through asset managers	6,737	6,158	6,390
2. Other financial assets at fair value through profit or loss			
Enterprise development fund	9	9	9
Supplier development fund	12	13	13
Money market funds	114	714	240
Total other financial assets at fair value through profit or loss	135	736	262

* The equity forward overlay on corporate debt securities was removed during the current period, however a derivative programme remains in place that is designed to immunise the effects of foreign currency and interest rate duration, such that the corporate debt securities provide a Rand cash return plus credit and liquidity spread.

Notes to the interim financial statements

	<u>6 months to June</u>		<u>December</u>
	<u>2020</u>	<u>2019</u>	<u>2019</u>
	<u>Rm</u>	<u>Rm</u>	<u>Rm</u>
3. Pension liabilities			
Pension liabilities	1 763	1 901	1 876

The movement in pension liabilities is analysed as follows:

Opening balance	1 876	1 760	1 760
Release of risk margin	(122)	(113)	(114)
Opening best estimate liability	1 754	1 647	1 646
Best estimate charge to profit or loss	(81)	120	50
Finance costs (unwind of discount rate)	58	58	125
Change in economic assumptions and modelling	(130)	13	(57)
Actual versus expected experience and other adjustments	(9)	49	(18)
New pensions awarded	56	70	195
Pensions and expenses paid	(71)	(64)	(137)
Closing best estimate liability	1 658	1 773	1 754
Reinstatement of risk margin	105	128	122
Closing balance	1 763	1 901	1 876

Reconciliation of pension valuation charge to profit or loss:

Best estimate charge to profit or loss	(81)	120	50
Movement in risk margin	(17)	12	8
Pension valuation (release)/charge	(98)	132	58
Less: Finance costs (Unwind of discount rate)	(58)	(57)	(125)
Pension valuation (gain)/loss for the year	(156)	75	(67)

4. Claims provisions

Unpaid reported claims	191	249	231
IBNR provision	402	324	374
Claims handling expenses	80	66	72
	673	639	677

The movement in claims provisions is analysed as follows:

Opening balance	677	618	618
Gross claims expense for the year	145	233	528
Claims paid	(93)	(142)	(274)
Pensions awarded	(56)	(70)	(195)
Closing balance	673	639	677

Notes to the interim financial statements

	<u>6 months to June</u>		<u>December</u>
	<u>2020</u>	<u>2019</u>	<u>2019</u>
	<u>Rm</u>	<u>Rm</u>	<u>Rm</u>
5. Premium rebate liabilities			
Premium rebate liabilities relating to:			
Underwriting year commencing March 2020	116	0	0
Underwriting year commencing March 2019 (2019: March 2019)	257	125	257
Underwriting year commencing March 2018 (2019: March 2018)	287	287	287
Underwriting year commencing March 2017 (2019: March 2017)	0	296	0
Total premium rebate liabilities	660	708	544
6. Net investment income			
Investment income	232	464	674
Interest income	74	87	192
Dividend income	29	23	31
Net foreign currency gain/(loss) on financial assets measured at fair value	524	(18)	(51)
Net valuation (loss)/gain on financial assets measured at fair value	(395)	372	502
Investment expenses	(11)	(11)	(22)
Asset management and consulting fees	(10)	(6)	(16)
Performance fees	(1)	(5)	(6)
Total net investment income for the year	221	453	652
7. Income tax			

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