Further commentary on 30 September 2013 Interim results

Transcript of Conference call

Held via teleconference on November 5, 2013 at 16h00 (South African time)

Conference leader: Ryan McDougall – Group Financial Director (RM)

RM: Good evening and thank you all for attending this conference call on the Trustco Group Holdings 2014 Interim results. My name is Ryan McDougall, group financial director and also currently also acting in an investor relations capacity.

The order of the call will be as follows:

1. brief introduction;
2. A summary of the results and also highlighting in a bit more detail the key changes from previous results;
3. I will then respond to the questions emailed to me;
4. And finally I will open the floor to questions from the participants.

The 2013 results, published on SENS and the Trustco website show favorable growth in NPAT, Assets, NAV, Loan book, Gross profit and Revenue but the question many would as is why hasn't this translated in Headline Earnings? I will seek to address this divergence by highlighting some of the key changes to the results since previous announcements and hopefully this will lead to a better understanding of where the business is at the moment.

I. Properties:

RM: The progress of Phase II of the Lafrenz is as follows:

Layout for LaFrenz phase 2 has been received by municipality and the town board will sit later in the month or early in 2014 to finalize and approve our development, at which stage we can begin sales.

Phase II is 369,000 m2, but only about 65% will actually be able to be subdivided based on geography and requirement to install roads etc.

We expect average selling price to be approximately R1500/m2 and costs to develop approximately R300/m2. The carrying amount of the land, previously residing in investment properties on the statement of financial position is to be transferred at approximately R300/m2; this will form a part of cost of sales as the land is sold.

The properties division has also informed me that sales price may be higher or lower depending on demand.

A revaluation gain recognized in profit and loss on Investment properties of R45million reflects 50% of a recent independent valuation on land held by the IFC as security for the bond program. We expect to recognize at least the same in the second half of the 2014 FY as the group also holds other investment properties both in South Africa and Namibia. Investment property is accounted for under the fair value model with transfers to inventory for development purposes done at carrying value (i.e. fair value).

II. Rest of Africa Insurance segment (including start up insurer in South Africa)

- Legacy business

RM: All operations relating to the legacy business are now confined to brokerage for current Yambu products and IT support for the systems, which is supported by a Royalty charge.

- Yambu Legal Protect

Q: Why is Yambu Legal (South Africa) referred to in the Micro-Insurance (Namibia) segment commentary? Shouldn't this be included in the" Rest of Africa" segment?
A: Yes, this is a bit ambiguous as Yambu legal is an insurance product but the revenues do form part of the Rest of Africa segment.

Q: How long does the group expect the Insurance segment In SA to take to get to a break-even level? Please can you talk a little more around this? This is clearly the segment that is detracting from the overall results and the sooner this shows some signs of life the better for everyone.
A: At current rates sales are between 2,000 and 3,000 per month. At this rate break-even on a month-to-month basis will occur between 12 and 24 months time

Q: When would you expect to recoup the losses from the investment in South African Yambu?
A: Overall timespan to achieve positive return on Investment from inception is 3 years, with full repayment expected in 5 years.

Q: What has been the total cash burn for the South African operations related to Yambu in total? What was the cash burn of the South African operations related to Yambu in the 6 month period just reported on? What would be the expected total cash burn for South African Yambu by the time break even is reached?
A: Cost of running the operations are currently ZAR6m per month. Expect this to reduce by ZAR2m every 6 months. Total investment in South Africa is capped to ZAR110m but this includes an allocation for the winding down of the legacy business.

Q: Should we expect further impairments of the indefinite life intangible asset for F2014?
A: No the ZAR3.8m impairment is a once-off impairment on the indefinite life intangible is due to the finalisation of transfer of existing back-office insurance functions at a lower Royalty rate than initially built into the valuation model. The model has been updated and the resultant decrease in fair value has been fully recognised.

Q: Why don't you disclose the number of Yambu customers?
A: It is generally not Trustco's policy to disclose customer numbers. However given the new venture we will likely disclose an audited number at year end.

- Rest of Africa

RM: The group continues to negotiate with other insurers and Telco's in Africa. For now Shoprite roll-out in countries other than Namibia has been put on hold, but not shelved completely. The Shoprite product in Namibia continues s to generate revenues and good press for both Shoprite and Trustco.

Q: In the Business Day results announcement it mentioned "A continuing commitment to launch micro-financial products in both South Africa and the rest of Africa has produced favourable results in terms if policy numbers and presence, but a great deal of work still needs to be done to make these ventures both profitable and relevant in terms of contribution to Group revenues." What this statement fails to do is to quantify what management views as favourable results.

A: Managements targets are to create a Trustco presence in rest of Africa via licensing, mobile partnerships or partial management of Trustco micro-insurance products for at a minimum number of countries by end 2014. South Africa has only a single insurance product at the moment and it is envisaged that we will roll out more innovative products to replicate the success of Namibia in future.

Q: What is the current status of litigation with Econet?

A: It was determined on appeal that the Supreme court of Zimbabwe are of the opinion that Econet validly terminated the agreement. This means that our claim for damages is now rendered moot as the arbitrator will have to give accord to the judgment. We have lodged an appeal with the Constitutional Court in Zimbabwe to appeal this finding. We will however still be entitled to our claim for revenue based on amounts unpaid prior to cancellation. Arbitration is set for December.

III. Insurance segment and Microfinance segment in Namibia

RM: The insurance division in Namibia launched Yambu Life, a term life offering which so far has been well received by the market and is being accepted by banks as security on asset lending. Shoprite customers continue to participate in the product whilst the group has made use of the client demographic profiling to actively target spenders who were previously not approached for other term products.

The Educational loan book continues to grow at healthy rates with NPL remaining below 5% throughout the period. The group has been prudent in its provisioning to ensure that new loans with longer emergence periods do not impact future earnings.

Q: In Q2 FY2014, N$99m was added to the gross loan book, whereas N$133m was added in Q1 FY2014. However the loan book profitability was only N$5.6m versus N$15m respectively. Understand the endowment effect, but what explains the divergence?

A: Loan book growth is dependent on student demand, but also note that actual book growth in Q3 FY2014 will again be skewed as disbursement to Students was temporarily delayed due to funding and finalising 1st tranche of bonds in Q2 FY2014. Overall the profitability of the division is also not a linear pattern and operates on a sliding COI.

IV. General

Q: The admin expenses have risen by 64% compared to the comparative and are also already 58% of the total for 2013. What are the major contributors to this increase?
A: In SA in 2013, the SA operations were continuing to capitalise development costs to software, but now as this is a fully licensed product those developers spend all their time on maintenance etc. which is fully expensed. The 52 branches acquired from Real People substantially increased rental and staff costs in SA. In Namibia cost increases have been in line with revenue growth for insurance and finance segment. The only once-offs in this admin line related to impairment of intangible asset and disposal of PP&E.

Q: The put option with RenCap is due to expire this month - what is the situation there?
A: The collar Expires mid-Jan2014 Group's view is that we will exercise the call if the strike price is above market but Trustco may also exercise the call should the group have a positive view of future earnings at that stage, note that a buy-back shrinks the size of equity of the group and is in effect a disbursement to existing shareholders and value per share increases.

Q: Trustco's dividend policy is to pay 4-5 times cover. TTO is paying 2 cents now; does it mean a no dividend at year end?
A: Should the second half of the year be similar to the first half it is likely that a dividend will be paid, although exceeding the stated policy of an earnings coverage ratio will need board approval. The impact of not paying a final dividend in 2013 was felt both on major investors as well as the share price in the market, and the group would like to avoid this in future.

RM: Thank you everyone for taking the time out to attend this call. The transcript will be available online shortly.

Call ended: 16h24