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Trustco Group Holdings Limited

Namibia Financial Institution Analysis **July 2014**

Security class	Rating scale	Rating	Rating outlook	Review date
Long term	National	BBB-(NA)	Stable	07/2015
Short term	National	A3(NA)	Stable	07/2015

Financial data:

(US$'m Comparative)

	31/03/13	31/03/14
NAD/US$ (avg.)	8.50	10.11
NAD/US$ (close)	9.24	10.58
Total assets	165.9	239.8
Total capital	104.8	115.7
Total borrowings	35.7	69.0
Net advances	39.0	66.2
Liquid assets	5.1	12.4
Operating income	46.7	80.5
Profit after tax	4.6	25.0

Market cap.*	NAD1,536m/US$144m
Market share	n.a.

**Valuation on 30/6/2014 (price: 199c/share, US$/NAD: 10.64).*

Rating history:

Initial rating (July 2012)
Long-term: BBB-(NA)
Short-term: A3(NA)
Rating outlook: Stable

Last rating (July 2013)
Long-term: BBB-(NA)
Short-term: A3(NA)
Rating outlook: Stable

Related methodologies/research:

Banking Criteria (updated April 2014)
Glossary of Terms/Ratios (February 2014)
Trustco Group Holdings Limited Reports (up to 2013)

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Summary rating rationale

The ratings are based on the following key factors:

- The ratings of Trustco Group Holdings Limited ("Trustco" or "the Group") reflect an established/expanding franchise in the group's main areas of operation (education, student/mortgage finance, insurance and property), and markets (Namibia and South Africa). Sound capital structure, low/moderating credit risk and improving profitability support the rating, which excludes the prospect of systemic support, given its low likelihood.
- The rating/s outlook considers Trustco's enhanced prospects and strategic focus, viewed in the context of divergent macroeconomic trends in its core markets: Namibia's sound economic growth and a stable inflation/interest rate environment supporting consumer health contrasts with South Africa's negative macroeconomic trends which impact consumer confidence and the credit cycle.
- In F14, growth in property and lending balances resulted in capital coverage of assets declining from 63.2% (FYE13) to 48.3% (FYE14), and net debt to capital rising to 48.9% (FYE13: 29.3%), while interest coverage is generous at 14.2% (F13: 14.3%). Swift asset/debt growth without a commensurate increase in profit may place strain on capital resources and leverage. Nevertheless, to date, Trustco has managed growth/dividend policies to maintain adequate capital, while remaining within covenanted levels.
- Credit metrics on student loans (representing 80% of finance segment loans) improved. The impairment ratio on student loans fell from 4.7% (FYE13) to 3.5% (FYE14) with all impaired loans provided for. There were no impaired mortgage loans at FYE14.
- In F14, group income grew 54.6% and net profit rose 6.4x to NAD252.6m (F13: NAD39.4m). The South African insurance operations posted losses (related to business closure/setup costs), and all Namibian businesses performed well. The property segment contributed NAD215.5m to the bottom line.
- Earnings prospects seem positive in all business segments. Sales of educational courses are gaining momentum; consequently growth in student finance has a strong outlook. More consistency in property sales should result in meaningful/consistent segment contributions to earnings going forward, supported by mortgage lending. Insurance is entering an expansion phase, with new products/capacity likely to yield benefits in F15 and beyond.

Factors that could trigger a rating action may include:

Positive change/s: Positive earnings evolution across all business segments, combined with stability in the operational business structure and conservatism in capitalisation/leverage metrics.

Negative change/s: The ratings will be impacted by declining asset quality, integration challenges relating to new acquisitions, increased debt levels in contravention of covenants, or adverse macroeconomic developments in key markets.

Organisational profile

Business overview[1]

Trustco is a diversified financial services holding company incorporated in Namibia, with a primary listing on the Johannesburg Stock Exchange ("JSE") and a secondary listing on the Namibian Stock Exchange ("NSX"). A brief description of the business units (each of which comprises one or more reporting segments), and their main focus areas and operating entities, is tabled below.

Business unit	Description of services offered
Education	Distance-learning courses (Namibia), offered through the Institute for Open Learning ("IOL").
Finance	Student loans (Namibia) to finance courses provided by IOL, through Trustco Finance; and Mortgage loans (Namibia) to finance the sale of Trustco properties, through Trustco Capital.
Insurance	Mass-market insurance offering (life and short-term) in Namibia, South Africa, and (to a lesser extent) other emerging markets, through: • Trustco Life, Trustco Insurance (Namibia); and • New Adventure Insurance Brokers, t/a Yambu Legal (South Africa).
Property	Sales of serviced residential, commercial and industrial properties (Namibia), through Trustco Property Holdings.
H/O and support	Support services, fleet management, air charter services and brand awareness. Support assets /costs are allocated to business units listed above.

Trustco continues to develop its business in Namibia and South Africa, and to evaluate possible pan-African and other emerging market opportunities. Selected acquisitions/divestures in F13 and F14 (to date), which are expected to contribute positively to the group's growth trajectory, deserve mention:

- Property (Namibia) – purchase of Elisenheim Property Development Company Limited ("EPDC"), which owns a 6,000-Erf residential development, for NAD300m;
- Insurance (South Africa) – closure of the legacy insurance business at a cost of c.NAD60m. Purchase of 55 branches and a call centre (including staff and operational infrastructure) from Real People (Proprietary) Limited for c.NAD10.4m, through which "Yambu" branded legal/funeral insurance is being sold; and
- Namibia (Finance) – in May 2014, Trustco's announcement of its acquisition of FIDES Bank (subject to regulatory approval).

Ownership structure

With the exception of Quinton van Rooyen, the group's founder and controlling shareholder, and the treasury shares held through Trustco Life Limited, the ownership structure represents diversified, portfolio shareholdings.

Table 1 provides a breakdown of the group's major beneficial shareholders as at 31 March 2014.

[1] For a detailed breakdown of the group, refer to past rating reports.

Table 1: Shareholding composition	%
Q van Rooyen (founding director)	50.8
Trustco Life Limited*	9.8
Pershing, LLC (custodian for 2 large portfolio shareholders)	9.6
Snowball Wealth	3.5
Other investors (all ≤ 3% max.)	26.3
Held by public investors	37.9
Held as treasury shares, and by directors and staff	62.1

* Treasury shares – repurchased in F14 for NAD74.3m, pursuant to the exercise of a put option held by the Renaissance African Master Fund.
Source: Trustco.

Governance

Table 2 summarises the composition of the board of directors ("Board") and the group's adherence to selected aspects of the King III Code of Corporate Governance. The Board has indicated that Trustco materially complies with King III principles, JSE and NSX rules, and other relevant regulatory requirements.

Table 2: Corporate governance summary	
Number of directors	8
-Independent non-executives	5 (at least 1/3 retire annually, and may be re-elected)
-Executives	3
Separation of the chairman	Yes
Frequency of Board meetings	Quarterly. 5 meetings held in F14.
Board committees	Audit and Risk Committee ("ARC"); and Remuneration and Nominations Committee ("REMCO"). All members are non-executive.
External auditors, rotation policy	BDO. Appointed annually, with 5-year partner rotation.
Internal control and compliance	Yes, reports to ARC.

Source: Trustco.

The performance of the Board (and its subcommittees) was self-assessed during F13. In F14 the Company Secretary's performance was assessed by the Board. Directors recommended by REMCO, are approved by shareholders in the annual general meeting.

Trustco's diversified financial services offering and countries of operation attract oversight from several regulatory bodies. The group is subject to oversight by the JSE and NSX, while the Namibian non-bank financial services (microfinance and insurance operations) are regulated by the Namibian Financial Institutions Supervisory Authority ("Namfisa"). In South Africa, the Financial Services Board is Trustco's primary operational regulator. Finalisation of the FIDES Bank acquisition will add the Namibian central bank (Bank of Namibia) as a regulator.

Control structure

Trustco's layered group structure is designed to optimise the balance between swift implementation of group strategy, ease of executive management and the quality of governance and oversight, reflecting both its listed status, and the fact that the managing director ("MD") who is also the CEO and heads the executive committee ("EXCO"), is the group's majority shareholder. The Board (supported by internal audit, compliance, ARC and REMCO) interfaces with EXCO, which is responsible for the execution of strategy, and functional oversight of business operations. EXCO receives input from the business segment heads, while the country heads for the Namibian and South African operations provide additional management oversight and feedback regarding operations in their respective markets.

The ability of the group to act swiftly on market opportunities and integrate/develop new product lines quickly and profitably (complemented by the high quality/timeliness of management information available) evidences an efficient and appropriate management feedback loop. The analysis of business unit operations conducted was high-level.

Recent developments
In March 2014, the MD, decided to reduce his involvement in day-to-day operations of the group, and it was decided that the separation of the MD and CEO roles would improve executive efficiency. From April 2014, the MD has taken the role of Group Executive Director, heading up the newly-established Trustco Innovation Hub together with a handful of senior executives. The sitting Group CFO (who will retain this role until a suitable replacement is found) has assumed the role of acting Group CEO. A Group Company Secretary has also been appointed from within, and an external appointment for the position of MD of the bank acquisition, has been made.

Human resources and staffing
The executive and senior management teams have relevant experience, enabling them to effectively manage Trustco's diversified financial services and property interests. The staff complement is considered adequate to support and/or maintain the group's operations and short-term development goals.

Table 3: Staffing breakdown

By management layer:	Avg. int. tenure	Avg. experience
Executive team	6.7 years	19.5 years
Senior management	5.0 years	16.7 years
Middle management	5.6 years	15.5 years
Servicing employees	2.8 years	14.3 years
By business function:	**# of employees**	**Avg. experience**
Business management	750	14.6 years
Financial control	25	15.0 years
Legal and compliance	14	12.0 years
IT and operations	30	16.4 years
Human resources & admin.	9	14.1 years

Source: Trustco.

Reporting structure and access to information
The group's accounts are prepared based on International Financial Reporting Standards and the annual/interim financial reports are detailed, transparent and released on a timely basis. BDO issued an unqualified audit opinion on the group's F14 financial statements. Investor communications covering performance, risk, corporate developments and other relevant matters are regularly disseminated via the group's website, the stock exchanges' news services, by e-mail, and through regular conference calls with investors and shareholders.

Operating environment
Trustco's operations in the microlending and personal insurance markets (and its focus on lower-income customers) imply that growth will be impacted by consumer vitality in its chosen markets, as well as competitive forces. In addition, the Namibian property development prospects are strongly linked to property price growth and demand in and around the capital, Windhoek. What follows is a brief discussion of the external factors affecting the group's main areas of operation.

Macroeconomic environment (Namibia)
Y/y real gross domestic product ("GDP") growth softened to 4.2% in 2013, relative to 5.0% in 2012. GDP growth drivers in 2013 included mineral production, agriculture, and property development (signalled by the rising real value of approved building plans). These segments are expected to continue to support GDP growth in 2014, with the construction sector also expected to contribute, supported by investments by the private sector (in mining) and public sector (for construction works). Services also bolstered GDP growth, with wholesale and retail trade, and the transport sector, growing well. Inflation has moderated from 6.5% (2012) to an estimated 5.8% (2013), mainly as a result of lower inflation for food, non-alcoholic beverages and housing, while prices for transport rose. Recent weakness in the Namibian Dollar, which is pegged to the South African Rand, is likely to put upward pressure on inflation. In addition, the depreciation of the local currency generally improves external price competitiveness of Namibia's export commodities in the international market, although weakness in key trading partners (in particular the Euro area) may soften demand for Namibian exports. Other economic indicators also point to corporate and consumer health in Namibia, those being stong growth in new vehicle sales and private consumption expenditure, while credit extension in an environment of stable interest and non-performing loan ("NPL") rates suggest a healthy macroeconomic and consumer environment.

Macroeconomic environment (South Africa)
Real GDP growth weakened to 1.9% in 2013 (2012: 2.5%), driven by labour market instability, infrastructure backlogs and continued weakness in key trading partners, amongst others. Moreover, rising inflationary pressures, particularly from necessities such as food and petrol, and administered costs such as electricity and rates, has seen growth in disposable income and consumption expenditure slow. Employment rates remain depressed, and are declining in the private sector, placing strain on employed

borrowers. Thus, while consumer confidence was strong during 2012 and in 1H 2013, it deteriorated in 2H 2013 to levels lower than those posted during the 2008 financial crisis. This has been exacerbated by severe Rand depreciation (prompting the South African Reserve Bank to raise the repo rate by 50 basis points to 5.5% in January 2014). Slower income growth, low confidence and expectations of monetary tightening have led to reduced sales volumes of durable and semi-durable goods, negatively affecting credit demand. Debt to disposable income levels (74.3% in 4Q 2013) have started trending downward, but debt is unaffordable for many at this juncture. Already high levels of consumer stress and an anticipated slowing in economic growth leave little room for discretionary expenditure.

Property market overview (Namibia)

Namibia's healthy macroeconomic prospects, and buoyant mining, construction and financial services sectors, are attracting investment and human capital to Namibia's coastal belt, and the central region around Windhoek. Demand for quality commercial/industrial and residential property is on the rise in these regions. In addition, property supply remains constrained, in part due to the long lead times for obtaining necessary zoning and development permissions.

In Windhoek, an increasing population, exacerbated by a housing backlogs of c.27,000 units (mainly in affordable/mid-level housing) per FNB Housing Index ("FNB HI") data, is placing increasing upward pressure on house prices. February 2014 FNB HI data indicates that the median house price in Windhoek rose 7% y/y, 53% over 3 years, and 121% over 5 years. The figures for Namibia as a whole were 9% y/y, 46% over 3 years, and 83% over 5 years. In general, house prices in the Northern and Southern regions have not shown such strong upward trends, and high-end luxury housing did not experience the same pricing support as mid-level housing. Excluding the effects of inflation, Namibian real house price growth has been 86.4% since January 2008 (vs. 17.9% in South Africa).

Given excess demand and constrained supply, it seems unlikely that prices of quality Namibian property will decline strongly in the foreseeable future. That being said, support for property prices at current levels is strongly linked to supply constraints, regional economic prospects, and could also be sensitive to changes in Namibian, pan-African and global economic drivers.

Financial profile

Likelihood of support

To date, the group has been well supported by its shareholders, primarily through a dividend policy which reflects business expansion objectives/capital requirements.

Funding composition

The group supports its growing business (in particular its lending operations) by accessing a broad range of funding providers. That said, development finance institutions ("DFIs") have been particularly interested in providing secured funding for education and the provision of student loans, which satisfies the development objectives of providing both educational and financial upliftment to rural and/or marginalised populations. Further, Trustco also monetises portions of its property portfolio as a source of funding, in addition to accessing traditional unsecured channels, including the listed bond and interbank markets. In F14, the majority of net new funding (c.NAD400m) was debt (mostly from DFIs such as the International Finance Corporation ("IFC"), Norfund, and African Development Bank). Property sales tended to be cash neutral in F14 as Trustco provided mortgage finance for the properties it sold. c.NAD237m was added to reserves during F14.

Table 4 highlights the quantum and diversification of the group's funding envelope.

Table 4: Funding base (by term & type)	F13		F14	
	NAD'm	%	NAD'm	%
Short-term funding	**41.4**	**12.6**	**277.5**	**29.5**
Current portion, long-term†	*40.8*	*12.4*	*133.6*	*14.2*
Vendor acquisition loan	*-*	*-*	*143.7*	*15.3*
Other loans	*0.6*	*0.2*	*0.2*	*<0.1*
Long-term funding	**288.7**	**87.4**	**662.5**	**70.5**
Term loans and other†	*288.7*	*87.4*	*304.9*	*32.4*
Vendor acquisition loan	*-*	*-*	*65.8*	*7.0*
Debt securities in issue	*-*	*-*	*291.8*	*31.1*
Total	**330.1**	**100.0**	**940.0**	**100.0**

† Secured to varying degrees by sureties and share pledges from the controlling shareholder, and cession of the Student Advances book held in Trustco Finance.
Source: Trustco.

Secured term/other loans (comprising mainly loans from DFIs, mortgages and instalment sale finance) have risen 33.1% to NAD438.5m from NAD329.5m between FYE13 and FYE14, while at the same time declining from c.100% to 46.6% of overall funding. During F14, the group issued listed bonds of R300m under its R1bn Domestic Medium Term Note ("DMTN") Programme – all tranches of which were privately placed with Norfund and the IFC – which comprised 31.0% of total funding at FYE14. In December 2013, Trustco purchased the Elisenheim residential development (through EPDC), with the sellers providing a vendor acquisition loan of NAD209.5m (contributing 22.3% of group debt funding at FYE14), to be settled in tranches between 1 April 2014 and 1 April 2016.

Capital adequacy and leverage

In the past, the group's internal capital generation exceeded capital consumed to support organic growth. However, after a challenging F13 from a profitability perspective (retained earnings only grew by NAD9.5m), the group's internal capital coverage declined. While income retained in F14 increased substantially to c.NAD237m, continued swift asset expansion without a commensurate increase in profit may place strain on capital resources. Historically

Trustco has tempered its growth and/or dividend payout policies to maintain comfortable capital levels.

The group's available capital is considered adequate relative to the levels of business risk assumed. While the ratio of group capital/assets has declined from 63.2% at FYE13 to 48.3% at FYE14, mainly as a result of balance sheet growth (in property and advances), this ratio remains adequate.

Table 5: Capitalisation	F13 NAD'm	F14 NAD'm
Total reported capital	**977.7**	**1,270.6**
Paid up common shares	*194.1*	*223.9*
Eligible reserves	*783.6*	*1,046.7*
Add: Net capital instruments	28.3	31.5
Total primary capital	**1,006.0**	**1,302.1**
Less: Net capital instruments	(37.8)	(54.0)
Total available capital	**968.2**	**1,248.1**
Total balance sheet assets	**1,532.9**	**2,537.3**
Selected ratios:		
Total capital: Total assets†	63.2%	48.3%
Annual dividend pay-out rate	75.9%	6.1%
Total borrowings: Total capital	34.1%	59.7%
Net borrowings: Total capital	29.3%	48.9%

† Minimum level of 25% required under DFI/IFC funding agreement.
Source: Trustco.

Following the substantial increase in debt funding relative to reserves retained in F14, leverage has increased: total and net debt to capital ratios have risen to 59.7% and 48.9%, respectively (FYE13: 34.1% and 29.3%). Trustco is subject to a group-level covenant governing leverage capacity. At FYE14, this ratio was within but close to the covenant, implying that net debt growth will be determined by the combination of earnings retention/debt reduction at this stage. In this regard we note that with the exception of the finance segment, the group's debt requirements are modest, and that the current leverage level (while close to the covenant) is conservative. In addition, the group's higher liquidity levels, which retain the net debt to capital ratio below 50%, add additional comfort. Gross interest cover in F14 is generous at 14.2x (F13: 14.3x). For a financial services business, Trustco's capitalisation/leverage metrics remain conservative, but the large property component on the balance sheet implies that restraint is warranted. Trustco was in compliance with statutory requirements/covenants (for the group and regulated subsidiaries) in F14.

Strategic outlook and risk management

During F14, the group determined its primary strategic intentions for the medium term. These include:

- Education and student finance – duplicating the successful Namibian "education and finance" business model in other jurisdictions, while maintaining educational content sales and loan book growth in Namibia;
- Insurance – reaching profitability in the South African business (including optimising branch network/operational capacity), and maintaining the current growth trajectory/product range expansion in Namibia;
- Property – structuring operations to contribute regularly to group earnings, focussing on the sale of Elisenheim erven, and LaFrenz Phase 2/3; and
- Organisational – streamlining activities to match business units, and decentralising management.

The group's strategic intentions appear to be realistic, and progress towards their achievement is underway.

Risk management

Trustco's enterprise risk management framework framework sets out the processes in place for risk identification, assessment and measurement, response and action, monitoring and review, and risk reporting. The risk management duties of executive management, internal audit and ARC, are clearly defined. Risk management embodies all categories of risk faced by the group and includes setting key control standards, together with continuous review and monitoring. Based on a limited review of the ARC minutes and external auditor's report, the risk management process process appears to comply with the framework, and be operating as intended, with control breaches identified/remedied on a timely basis. Within the context of the group's operating environment and business, credit risk, market (property price) risk, liquidity risk, interest rate risk, regulatory risk, and operational risk are most significant.

Operational profile

Table 6 shows that net advances plus investment property totalled 62% of Trustco's group balance sheet at FYE14 (FYE13: 45.9%), illustrating increased its focus on lending and real estate. FYE14 fixed/intangible assets, receivables and inventory balances remained broadly in line with FYE13 figures. Liquidity rose from NAD46.9m (FYE13) to NAD131.6m or 5.2% of the group's balance sheet at FYE14, reflecting improved short-term liquidity and balance sheet conservatism.

Table 6: Asset breakdown	F13 NAD'm	F13 %	F14 NAD'm	F14 %
Cash and equivalents	46.9	3.1	131.6	5.2
Net advances	360.7	23.5	700.0	27.6
Investment property†	344.2	22.4	873.4	34.4
Fixed & intangible assets	411.9	26.9	415.5	16.4
Receivables	271.2	17.7	293.6	11.6
Other assets	98.0	6.4	123.2	4.8
Total B/S assets	**1,532.9**	**100.0**	**2,537.3**	**100.0**

† Includes NAD331.6m related to residential property stock purchased in the Elisenheim transaction.
Source: Trustco.

The section which follows highlights key risks inherent in the group balance sheet, while also placing asset allocation and revenue/profit generation into the appropriate segmental/business unit context.

Balance sheet risk focus

Market risk

Falling property prices would have a negative impact on Trustco's ability to profitably sell its property portfolio, which is focussed in the central (Windhoek) and northern areas of Namibia. Based on recent trends in property prices, demand/supply dynamics and the macroeconomic outlook, a substantial decline in property prices in the areas where Trustco has its main investments, is considered unlikely.

Credit risk

Credit risk in the balance sheet remained at similar levels (as a proportion of balance sheet) to prior years, but became more concentrated in the loan book, with smaller relative allocations to other receivables.

Table 7: Credit risk Exposure	F13		F14	
	NAD'm	%	NAD'm	%
Loans and placements	**407.0**	**26.5**	**831.6**	**34.8**
Net customer loans†	*360.7*	*23.5*	*700.0*	*27.6*
Bank loans/deposits	*46.3*	*3.0*	*131.6*	*5.2*
Other receivables*	**279.6**	**18.2**	**293.6**	**11.6**
Property sales	*155.6*	*10.1*	*213.8*	*8.4*
Trade and other	*124.0*	*8.1*	*79.8*	*3.2*
Total B/S assets	**1,532.9**	**44.7**	**2,537.3**	**46.4**

† Net of impairments of NAD39.2m (FYE13: NAD30.9m)

* Including NAD75.4m (FYE13: NAD193.1m) which is more than 6 months past due but not impaired at FYE14.

Source: Trustco.

The loan book comprises student advances (FYE14: 80% of gross advances, FYE13: 90%), with the remainder mainly mortgages. Other advances relate to historical business acquisitions, and are almost fully provided. Loans showed improving credit quality, with impairments relative to gross loans decreasing from 7.8% at FYE13 to 5.3% at FYE14, (the quality of the individual credit books will be discussed in more detail in the segmental reviews which follow).

While receivables' contribution to aggregate credit risk has diminished from 18.2% of the balance sheet to 11.6% between FYE13 and FYE14, it remains qualitatively substantial, given that receivables past due more than 6 months but not impaired at FYE14 were NAD75.4m – 6.7% of credit assets and 25.7% of receivables (FYE13: NAD193m, or 28% of credit assets and 69% of receivables). Notwithstanding the above, overdue receivables primarily relate to properties sold, where transfer has not yet taken place, and are not considered to be impaired.

Liquidity risk

The group maintains a conservative liquidity profile in order to ensure that liabilities can always be settled as they become due, in normal and stressed scenarios. Net liquidity rose from 3.1% (FYE13) to 5.2% (FYE14) of the balance sheet. In addition, the group's contractual liquidity profile illustrates positive liquidity gaps in all maturity buckets less than 4 years. The large property portfolio, which would be difficult to sell quickly, is the main source of unmitigated group liquidity risk.

Operational segment focus

Table 8 illustrates the allocation of assets between reporting segments, and by geography. Namibia remains the primary repository for assets and driver of revenue/earnings, with Namibian business interests accounting for c.90% of group assets, and 94.8% of external revenue in F14.

Table 8: Segmental asset mix	F13		F14	
	NAD'm	%	NAD'm	%
Education (Namibia)	**110.2**	**7.2**	**70.3**	**2.8**
Finance (Namibia)	**345.4**	**22.5**	**740.3**	**29.2**
Insurance	**402.2**	**26.3**	**368.2**	**14.5**
Namibia	*170.6*	*11.1*	*122.5*	*4.8*
South Africa	*181.7*	*11.9*	*233.3*	*9.2*
Emerging Markets	*49.9*	*3.3*	*12.4*	*0.5*
Property (Namibia)	**675.1**	**44.0**	**1,358.5**	**53.5**
Total B/S assets	**1,532.9**	**100.0**	**2,537.3**	**100.0**

Source: Trustco.

Table 9 highlights that all profitable business segments in F14 were Namibia-based, whereas the insurance segments in South Africa and emerging markets were loss-making, mainly as a result of costs of closing the legacy business in South Africa, and the c.NAD42m write-off in irrecoverable receivables (Zimbabwe).

Table 9: Segmental profit	F13		F14	
	NAD'm	%†	NAD'm	%†
Education (Namibia)	**4.0**	**3.5**	**22.0**	**5.7**
Finance (Namibia)	**23.8**	**21.0**	**47.0**	**12.1**
Insurance	**(13.3)**	**n.a.**	**(31.8)**	**n.a.**
Namibia	*67.0*	*59.0*	*103.1*	*26.6*
South Africa	*(79.2)*	*n.a.*	*(86.2)*	*n.a.*
Emerging Markets	*(1.1)*	*n.a.*	*(48.7)*	*n.a.*
Property (Namibia)	**18.7**	**16.5**	**215.5**	**55.6**
Total profit*	**113.5**	**100.0**	**387.6**	**100.0**
Total profit	**39.4**	**-**	**252.7**	**-**

† Calculated as a percentage of profit-making businesses only.

* Relates to total of profit-making businesses only.

Source: Trustco.

The section which follows provides additional detail on Trustco's business units/segments, detailing relative size, main activities, and performance.

Education

This unit focuses on providing access to distance learning courses and materials through IOL, which sells courses and supports students through 7 regional offices in Namibia (and a mobile office for reaching outlying areas). Trustco Education had 26,600 active students studying over 700 courses at FYE14. IOL is regulated through the Ministry of Education, while courses also require accreditation from various authorities.

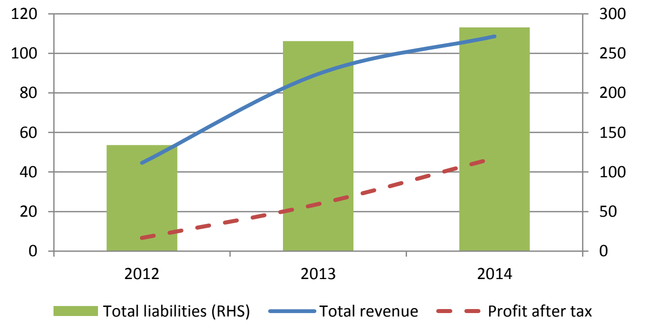
IOL's contribution to group profits rose from NAD4.0m in F13 to NAD22.0m in F14, but remained a modest contributor to group profits. However, the business' declining asset base (NAD70.3m at FYE14 relative to NAD110.2m at FYE13), boosted returns, and contributes indirectly to group profit through the link to student finance.

Competitive position and prospects – Education provision competitors include traditional universities which do not offer distance learning, and smaller distance learning institutes which lack IOL's ability to offer in-house developed, accredited (vocational to tertiary level), and bespoke courses. The complementary student finance offering results in Trustco's business being unique in Namibia, implying no direct competition. Trustco's dominant market shares in distance learning and student finance, and ability to provide relevant courses and student support through the use of technology, makes this business relevant and scalable, with good growth prospects in Namibia (which is burdened with high unemployment /skills shortages) and other emerging markets.

Finance

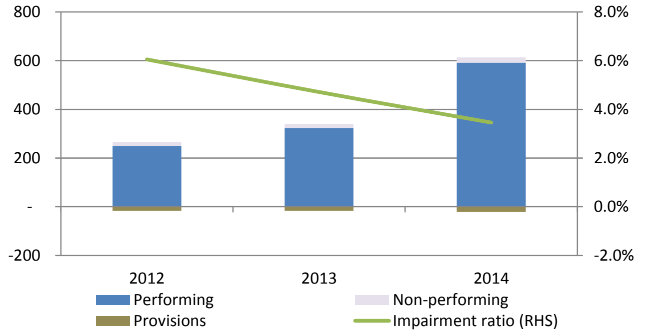
This business unit includes the student and mortgage loan books. Student advances are inextricably linked to the Education business. Trustco Finance provides loans to IOL students to finance their studies, with c.58,000 loans outstanding at FYE14. As a microloan provider (loans <NAD50,000, term <60 months), Trustco Finance is regulated by Namfisa. Mortgage advances have been provided through Trustco Capital since 2013, and essentially provide financing for sales of Trustco properties.

Finance segment performance (in millions)



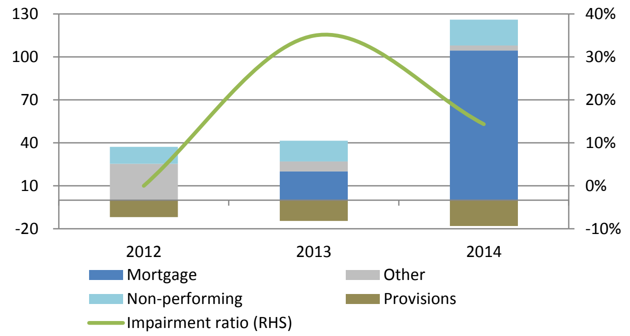
Between F13 and F14, finance segment assets have grown 114.3% from NAD354.4m (22.5% of assets) to 29.2% of assets, or NAD740.3m (NAD592.0m of which are student advances). In F14 the segment contributed NAD47.0m or 12.1% of group profit (F13: NAD23.8m, 21.0%) gross of loss-making segments.

Student advances, asset quality (in millions)



Student loans performed well, with a modest increase in impairments relative to loan book growth. The impairment ratio fell from 4.7% (FYE13) to 3.5% at FYE14, with all impaired loans (90+ days overdue) fully provided for. Loans with balances outstanding >30 days totaled NAD33.7m or 5.5% of gross loans at FYE14. Credit risk appears modest, with the portfolio well diversified geographically (rural 35%, urban 65%) and by gender, and with c.80% of loan repayments (70% government, 10% private enterprise at FYE14) by payroll deduction.

Mortgage loan portfolio, asset quality (in millions)



Mortgages, which are extended by Trustco Capital to support property sales (of Elisenheim Phase 1 in F14), increased from NAD21.4m (FYE13) to NAD104.5m (FYE14). No mortgage loans are impaired. However, other loans (which relate primarily to historical business purchases) of NAD21.6m at FYE14 have provisions of NAD18.1m against them.

Competitive position and prospects – Trustco Finance has a 23% market share of Namibian microlending (by value, at 31 December 2013, per Namfisa data), and provides only student finance for IOL courses. While other Namibian microlenders also offer student finance, this is not their core focus, and they do not compete to finance IOL courses. The purchase of FIDES Bank provides Trustco with the opportunity to upscale and streamline its lending capabilities through a full-service bank infrastructure. In addition, the banking license may provide Trustco with additional (deposit) funding in future.

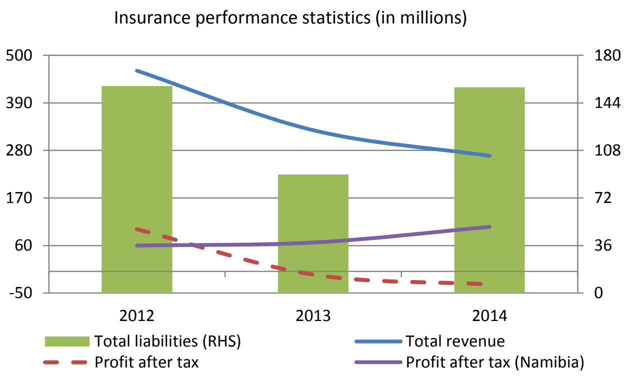
Insurance

This business unit provides a suite of short- and long-term insurance products, in Namibia and South Africa.

Product category	Description, legal entity
Namibia	
Short-term insurance	Legal, medical and salary protection cover (through Trustco Insurance)
Funeral-related insurance	Funeral cost, transport cost, and family support cover (through Trustco Life)
Term life	'Yambu' branded, with health risk-linked premium (through Trustco Life)
'Free' life insurance	Life cover which expires if not renewed through retail spend (through Trustco Life and Trustco Mobile)
South Africa	
Short-term insurance	'Yambu'-branded legal/funeral cover (via New Adventure Insurance Brokers)
'Free' life insurance	Life cover which expires after a period

In Namibia, the premium-based short-term, funeral-related and term life products (insurance products, which target the "working poor" who earn between USS$2 and US$20 per day) are distributed through Trustco's branch network, as well as its mobile units servicing outlying/rural areas. At present, Trustco has issued at least one policy from this suite to 56% of the c.630,000 employed people in Namibia. The short-duration 'free' life cover operates on the basis of a loyalty programme, with distributors paying a 'premium' to Trustco based on a customers' airtime/retail spend. This product is distributed through Trustco Mobile (airtime) and the 'Shop 4 Life' programme in a chain of retail stores in Namibia. The 'free' life cover products, while having limited profitability, act as a means of introducing a new client base to the concept of life insurance.

The 'Yambu'-branded legal and funeral products are being rolled out in South Africa through its network of 55 branches purchased in 2013. 'Free' life cover linked to the purchase of airtime has also been launched.



Trustco's insurance business assets remained constant in F14, but fell as a proportion of group assets from 26.2% (FYE13) to 17.1% (FYE14). In F14 the Namibian insurance contribution to group profit rose 26.6% to NAD108.3m reflecting good take-up of existing and new products, but costs relating to the closure of legacy South African and Zimbabwean business interests, plus costs of purchasing and re-purposing the recently acquired branch infrastructure – together a loss of NAD134.9m (F13: loss of NAD74.1m) – resulted in the insurance segment reporting an overall loss of NAD27.8m (F13: NAD7.1m loss).

Competitive position and prospects – Trustco dominates the Namibian microinsurance market, with the range of its products having broad appeal, while opportunities for cross-selling remain. The 'free' life insurance product, which targets lower LSM groups than traditional term life, has been subscribed to by at least c.200,000 customers in Namibia, and has shown encouraging take-up rates in South Africa (Trustco has first arriver advantage with its currently unique product) where there is a much larger consumer base. Although low profit, 'free' life cover represents a compelling client acquisition strategy, and is suitable for roll-out in other emerging markets (a pilot project in Brazil is currently running, in conjunction with local partners).

In Namibia, Trustco has substantial competition in the term life market, but its 'Yambu'-branded product has attractive features, and market penetration is positive. Life cover can be obtained without submitting to a medical test, but a customer willing to submit to medical tests will obtain higher cover at lower cost than the untested equivalent. It is anticipated that this business will become highly profitable in 3-5 years, once regulatory capital has been built up.

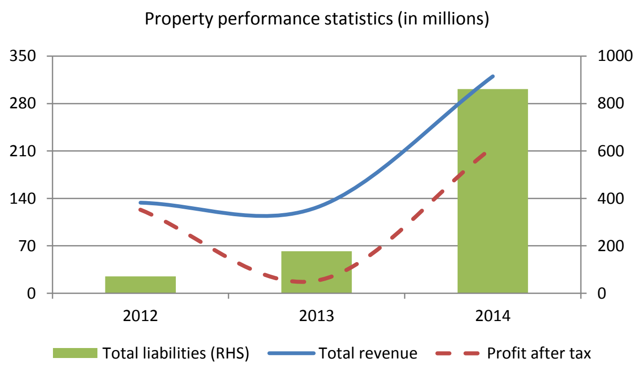
Trustco has traditionally focused its insurance offering on niche markets, or offered unique products. Despite high market penetration in Namibia, opportunities exist for selling more than one product into the existing client base, and offering products which meet different customer needs. In South Africa, Trustco's legal/ funeral cover is not unique, but the market size and niche targeted offer substantial upside.

Property

Over several years, Trustco Properties has built its property investment portfolio, opportunistically acquiring parcels of undeveloped land in and around Windhoek, and elsewhere. The group's strategy is to divide land into development phases, and sell serviced land when market demand is supportive of sales.

Property assets grew from NAD675.1m to NAD1.35bn in F14, rising from 44.0% of group assets at FYE13 to 53.5% at FYE14. While little property-related activity took place in F13, F14 saw Trustco purchase EPDC for a consideration of NAD300m, and subsequently sell Elisenheim Phase 2 at a profit of c.NAD147m. In addition, property transfers from Phase 1 of the LaFrenz industrial development contributed c.NAD92m to income.

In F14, property revenue grew 152% to NAD320.2m, generating a profit of NAD215.5m (10-fold higher than the NAD18.7m recorded in F13).



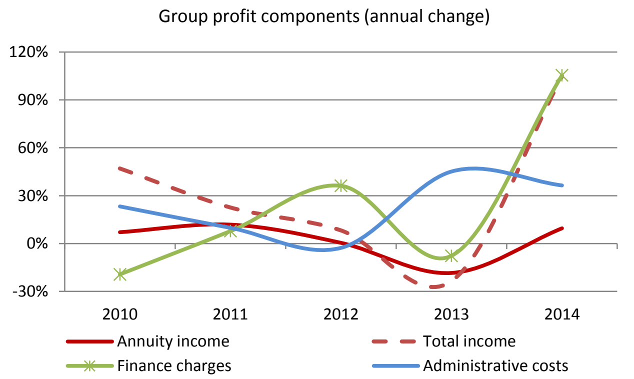
External debt (vendor acquisition finance and DMTN proceeds) appear to have supported the NAD673.8m increase in property segment assets, with segment liabilities increasing from NAD177.5m (FYE13) to NAD861.0m (FYE14). While real estate sales are expected to contribute more stable revenues/profits in future, the investment property portfolio also serves as security/collateral in respect of secured funding arrangements.

Competitive position and prospects – Increasing demand for quality residential land in and around Windhoek has driven up the median house price by 53% over the past 3 years, per the FNB House Price Index data. As Trustco has been adding to its investment property portfolio opportunistically over many years, the purchase cost of the land is modest relative to current values (estimated at NAD3bn vs. balance sheet carrying value of NAD537m). This gain is expected to be realised over the next 20 years (to match demand), with development phases sold on a timeline which will bring greater consistency to revenues and profits, without impacting margins.

Trustco optimises margins by selling serviced land to developers. La Frenz phases 2/3 are expected to be prepared and sold in the next 2 years. The quality of the investment properties, latent demand for land, and Trustco's experience in marketing desirably formatted property indicates good prospects for sustainable, high-margin returns from this business segment.

Financial performance and prospects

A 5-year financial synopsis is shown at the back of this report, supplemented by the commentary below.



The 6.4x increase in F14 income to NAD252.6m (F13: NAD39.4m) has been driven by:

- A 9.6% recovery in annuity income (mainly insurance premiums, net interest income/fees from lending operations, and educational course sales) to NAD558.9m;
- Substantial property-related earnings in F14. Revenue from land sales (NAD306.3m) and investment property revaluations (NAD120.4m) exceeded F13 revenue (NAD127.4m combined);
- Declining administrative cost growth (36.4% in F14 vs. 45.1% in F13). Economies of scale/ infrastructure investment are starting to bolster the bottom line. Cost-to-income ratios remain high at 49.3% (F13: 74% due to abnormally low earnings), reflecting write-offs on business closures taken in F13 and F14, and the capacity-building phase in which the business finds itself; and
- Increasing finance charges, reflecting substantial debt-funded balance sheet growth.

While Trustco continued to redefine its position in its diverse markets in response to opportunities and competitive pressures, the group's strategy appears to be cohesive and achievable. Unsuccessful businesses have been culled, and new ventures appear to receive high levels of operational/management support. Group focus on the long game appears to be supported by F14 results, F15 budgets and long-term anticipated income levels, but reflects an increase in financial risk. Debt levels have risen to match equity funding at FYE14, and the quantum of net new debt which can be raised will be linked to retained earnings growth to support ongoing compliance with leverage covenants.

That being said, the group's earnings prospects are positive across all business segments.

- Sales of educational products are gaining momentum, and the accreditation of high-profile tertiary courses should boost demand. The related growth in student finance also has a strong outlook, albeit with some regulatory risk;
- Property sales generated substantial profits in F14, and Trustco's more consistent, measured approach to extracting value from its investment property portfolio is likely to contribute meaningfully and consistently to earnings going forward. Mortgage lending will gain momentum and add an additional element of annuity revenue as property sales increase; and
- The insurance business appears to be entering an expansion phase, with new products and cross-selling in Namibian markets being supplemented by investment in new markets, particularly South Africa. Extensive costs relating to closure of unprofitable businesses in South Africa and Zimbabwe will not drag into F15. F14 has seen substantial capacity building in insurance, the benefits of which should be reaped in higher income in F15 and beyond.

Trustco Group Holdings Limited

(NAD in millions except as noted)

For the year ended: 31 March

Income Statement	**2010**	**2011**	**2012**	**2013**	**2014**
Insurance premium revenue	108.4	111.5	126.3	150.7	225.1
Broker commissions and fees	291.7	263.1	309.2	174.6	24.9
Microfinance income (interest and fees)	34.5	39.2	44.5	56.3	100.7
Education (tuition fees and related)	70.1	52.0	70.0	85.3	144.6
Trustco Mobile	-	45.3	29.1	0.5	0.0
Investment income	7.9	29.3	24.5	3.8	3.1
Other	43.7	81.9	21.6	38.9	60.5
Total annuity type income	556.3	622.3	625.2	510.1	558.9
Realised Fair value gains/(losses)	25.9	59.1	117.3	101.1	306.3
Unrealised Fair value gains/(losses)	88.3	63.5	97.1	26.3	120.4
Total income	**670.5**	**744.9**	**839.6**	**637.5**	**985.6**
Cost of sales	(279.1)	(265.1)	(320.3)	(240.2)	(172.0)
Total income (excl. cost of sales)	**391.4**	**479.8**	**519.3**	**397.3**	**813.6**
Administrative expenses	(189.6)	(208.3)	(202.7)	(294.2)	(401.4)
Insurance benefits and claims	(16.9)	(21.4)	(18.9)	(26.7)	(33.0)
Transfer to policyholder liabilities	(2.4)	(3.4)	(2.4)	(5.9)	(21.9)
Change in unearned premium provision	(0.4)	(0.6)	(0.5)	1.0	-
Finance charges	(20.5)	(22.1)	(30.1)	(27.8)	(57.1)
Profit before tax	**161.6**	**224.0**	**264.7**	**43.7**	**300.2**
Taxation charge	(24.0)	(12.4)	(25.0)	(4.3)	(47.6)
Attributable earnings	**137.6**	**211.6**	**239.7**	**39.4**	**252.6**
Dividends paid	(14.1)	(10.2)	(25.8)	(29.9)	(15.4)
Retained earnings	**123.5**	**201.4**	**213.9**	**9.5**	**237.2**

Cash Flow Statement					
Cash generated by operations	**82.7**	**185.4**	**178.1**	**96.9**	**321.1**
Working Capital (increase)/decrease	(9.0)	(169.3)	(79.0)	(76.3)	(159.6)
Net loans advanced - Educational	(45.3)	(29.4)	(42.2)	(83.7)	(265.1)
Net loans advanced - Mortgage & other	-	-	-	(3.7)	(13.3)
Proceeds from funding for Educational advances	-	-	-	-	240.0
Net interest/dividends received	7.9	29.3	24.5	3.8	3.1
Finance costs	(20.5)	(22.1)	(30.1)	(27.8)	(57.1)
Taxation paid	(0.4)	(5.5)	(12.8)	(13.6)	(16.1)
Net cash flow from operations	**15.4**	**(11.6)**	**38.5**	**(104.4)**	**53.0**
Dividends paid - Ordinary shares	(14.2)	(10.2)	(25.8)	(29.9)	(15.4)
Net cash retained	**1.2**	**(21.8)**	**12.7**	**(134.3)**	**37.6**
Net investment (cost)/proceeds	**(31.3)**	**(76.3)**	**8.9**	**(28.2)**	**(21.4)**
Acquisitions/Additions to assets	(40.3)	(77.2)	(42.0)	(36.9)	(28.6)
Proceeds on sale of assets/investments	9.0	0.9	50.9	8.7	7.2
Decrease in policyholder under insurance contracts	2.4	3.4	2.4	5.9	21.9
Shares issued/(redeemed)	0.5	-	17.9	37.0	(39.2)
Net cash available/(consumed)	**(27.2)**	**(94.7)**	**41.9**	**(119.6)**	**(1.1)**
Borrowings raised/(repaid)	3.0	66.9	5.8	76.7	86.3
Net increase/(decrease) in cash and cash equivalents	**(24.2)**	**(27.8)**	**47.7**	**(42.9)**	**85.2**

Balance Sheet					
Total shareholders' interest	478.6	732.8	913.3	968.1	1,224.4
Total interest-bearing debt	168.9	247.8	257.8	330.1	730.4
Policyholders liability under insurance contracts	4.9	8.3	10.7	16.6	38.5
Income tax liabilities	59.1	35.4	59.7	62.3	216.3
Accounts payable	187.6	167.3	256.3	129.2	95.0
Other liabilities	22.0	30.7	22.2	26.6	232.7
Total liabilities & equity	**921.1**	**1,222.3**	**1,520.0**	**1,532.9**	**2,537.3**
Fixed assets	139.4	129.7	160.5	179.3	203.1
Intangible assets	194.7	240.9	261.5	232.6	212.4
Advances	178.3	207.8	275.3	360.7	700.0
Investment property	143.2	232.8	318.0	344.2	537.3
Receivables	46.5	197.5	317.4	271.2	293.6
Cash and cash equivalent	91.0	82.7	101.0	46.9	131.6
Other assets	128.0	130.9	86.3	98.0	459.3
Total assets	**921.1**	**1,222.3**	**1,520.0**	**1,532.9**	**2,537.3**

Ratios					
Cash flow:					
Operating cash flow : total debt (%)	9.1	(4.7)	14.9	(31.6)	7.3
Operating cash flow : Interest bearing debt (%)	9.1	(4.7)	14.9	(31.6)	7.3
Profitability:					
Annuity income growth (%)	7.1	11.9	0.5	(18.4)	9.6
Total income growth (%)	28.1	11.1	12.7	(24.1)	54.6
Effective tax rate (%)	14.9	5.5	9.4	9.8	15.9
Cost to income (%)	34.1	43.4	39.0	74.0	49.3
Coverage:					
Dividend cover	9.8	20.7	9.3	1.3	16.4
Interest coverage (Total income excl. cost of sales)	19.1	21.7	17.3	14.3	14.2
Capitalisation:					
Equity : Total assets (%)	52.0	60.0	60.1	63.2	48.3
Retention rate (%)	89.8	95.2	89.2	24.1	93.9
Total debt : equity (%)	35.3	33.8	28.2	34.1	59.7
Net debt : equity (%)	16.3	22.5	17.2	29.3	48.9

GLOSSARY OF TERMS/ACRONYMS USED IN THIS REPORT

Accounting	Recording and reporting of financial transactions, including the origination of the transaction, its recognition, processing, and summarisation in the financial statements.
Agreement	A negotiated and usually legally enforceable understanding between two or more legally competent parties.
Balance Sheet	Basic financial statements, usually accompanied by appropriate disclosures that describe the basis of accounting used in its preparation and presentation of a specified date the entity's assets, liabilities and owners' equity. Also known as a statement of financial position.
Basis Points	A basis point is 1/100th of a percentage.
Capital Adequacy	A measure of the adequacy of an entity's capital resources in relation to its current liabilities and also in relation to the risks associated with its assets. An appropriate level of capital adequacy ensures that the entity has sufficient capital to support its activities and that its net worth is sufficient to absorb adverse changes in the value of its assets without becoming insolvent.
Collateral	Asset provided to a creditor as security for a loan.
Corporate Governance	The manner in which an entity is governed and decisions are undertaken.
Covenant	A clause in loan agreements that promises or obligates and/or restricts the borrower. If violated, a breach has occurred, which may cause the loan to become immediately due.
Credit Rating Agency	A party that provides an opinion on the credit quality of assets, debt securities and companies.
Credit risk	Risk that a party to a contractual agreement or transaction will be unable to meet their obligations or will default on commitments. Credit risk can be associated with almost any transaction or instrument such as swaps, repos, CDs, foreign exchange transactions, etc. Specific types of credit risk include sovereign risk, country risk, legal or force.
Default	Failure to make loan payments on a timely basis or to comply with other terms/requirements as stipulated in the loan agreement.
Depreciation	Expense allowance made for wear and tear on an asset over its estimated useful life.
Diversification	The principle that a portfolio in which assets are separated into different industry sectors, geographic regions and firms will embody less overall risk than one in which assets are concentrated into a few sectors, regions and firms.
Dividend	A portion of the after-tax profits paid out to the owners of an entity as a return on their investment.
Expenditure	Payment, either in cash, by assuming a liability, or by surrendering an asset.
Financial Institution	An entity that focuses on dealing with financial transactions, such as investments, loans and deposits.
Financial Statements	Presentation of financial data including balance sheets, income statements and statements of cash flow, or any supporting statement that is intended to communicate an entity's financial position at a point in time and its results of operations for a period then ended.
Franchise	Business or banking franchise; a bank's business.
Impairment	An amount set aside for expected losses to be incurred by a creditor.
Income Statement	Summary of the effect of revenues and expenses over a period of time.
Intangible Asset	Asset having no physical existence such as trademarks and patents.
Interest Rate	The amount paid by a borrower to a lender in exchange for the use of the lender's money for a certain period of time. Interest is paid on loans or on debt instruments, such as notes or bonds, either at regular intervals or as part of a lump sum payment when the issue matures.
Interest Rate Risk	Interest rate risk in the banking book is the risk that earnings or economic value will decline as a result of changes in interest rates.
Internal Audit	Audit performed within an entity by its staff rather than an independent certified public accountant.
King III	The King Report on Governance for South Africa 2010.
Liquid Assets	Assets, generally of a short term, that can be converted into cash.
Liquidity Risk	Liquidity is the ability fund increases in assets and meet obligations as they become due, without incurring unacceptable losses.
Market Risk	The risk of loss (in both the banking and trading book) as a result of unfavourable changes in foreign exchange rates, interest rates, equity prices, credit spreads and commodity prices.
Mortgage Loan	A loan made by a lender to a borrower to finance real estate.
Non-performing loan	When a borrower is overdue, typically 90 + days in arrears or as defined in the transaction documents.
Operational Risk	The risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This includes legal risk, but excludes strategic risk and reputational risk.
Primary Capital	Primary capital consists of issued ordinary share capital, hybrid debt capital, perpetual preference share capital, retained earnings and reserves. This amount is then reduced by the portion of capital that is allocated to trading activities and other regulatory deductions.
Rating Outlook	A rating outlook indicates the potential direction of a rating over the medium term, typically a one to two year period.
Regulatory Capital	The total of primary, secondary and tertiary capital.
Retained Earnings	The accumulation of an entity's profits less any dividends paid out.
Reputational Risk	The risk of impairment of an entity's image in the community or the long-term trust placed in it by its shareholders as a result of a variety of factors, such as performance, strategy execution, the ability to create shareholder value, or an activity, action or stance taken by the entity.
Risk Identification	The ongoing recognition and discernment of risk.
Risk Management	Process of identifying and monitoring business risks in a manner that offers a risk/return relationship that is acceptable to an entity's operating philosophy.
Risk Reporting	The communication of risk information in all phases of the risk management process, namely identification, measurement, management and monitoring.
Sovereign Risk	The risk of default by the government of the country on its obligations.
Strategic Risk	The risk of an adverse impact on capital and earnings due to business policy decisions (made or not made), changes in the economic environment, deficient or insufficient implementation of decisions, or failure to adapt to changes in the environment.
Tertiary Capital	Tertiary capital means accrued current-year uncapitalised net profits derived from trading activities; and capital obtained by means of unsecured subordinated loans, subject to such conditions as may be prescribed.

SALIENT POINTS OF ACCORDED RATINGS

GCR affirms that a.) no part of the rating was influenced by any other business activities of the credit rating agency; b.) the rating was based solely on the merits of the rated entity; c.) such rating was an independent evaluation of the risks and merits of the rated entity; and d.) the validity of the rating is for 12 months, or as indicated by the applicable credit rating document.

The ratings were solicited by, or on behalf of, Trustco Group Holdings Limited, and therefore, GCR has been compensated for the provision of the ratings.

Trustco Group Holdings Limited participated in the rating process via face-to-face management meetings, teleconferences and other written correspondence. Furthermore, the quality of info received was considered adequate and has been independently verified where possible.

The credit ratings above were disclosed to Trustco Group Holdings Limited with no contestation of/changes to the ratings.

The information received from Trustco Group Holdings Limited and other reliable third parties to accord the credit ratings included the audited annual financial statements as at 31 March 2014 (plus four years of comparative numbers), latest internal and/or external reports to management, full year detailed budgeted income statements (to 31 March 2015), corporate governance and enterprise risk framework, reserving methodologies, capital management policy, Industry comparative data and regulatory framework and a breakdown of facilities available and related counterparties at 31 March 2014.