Conference call transcript

17 May 2012

RESULTS FOR THE YEAR ENDED 31st MARCH 2012

Stephen Koseff

Good morning everybody. Welcome to Investec and our annual analyst presentation. I'm going to start off by reminding people of what we are and what we do as a firm. And I think this has been a very tough period and it's important for us to go back to our roots and say what we are. Since our inception as an organisation we've built our business through organic growth and strategic acquisitions. We started internationalising our business in 1992 and our primary strategy in terms of internationalising our business was to follow our customer base, gain domestic competence in a particular environment and then build scale in those geographies, at the same time facilitating cross-border flow.

We believe for the type of organisation we are and the type of clientele we deal with who have become very international as South African opened up to the rest of the world we would lose our client base if we did not follow that path. We have tried to build a diversified portfolio of businesses and geographies to support our clients, institutional, corporate and private individuals, through varying markets and economic cycles. And at the end of the day what we've tried to create is a meaningful balanced portfolio with proper foundations in place which can gain traction over time.

If you look at our core geographies at this point in time, if we start off with the UK it is a tough and competitive place with many banks and asset managers around the world opening offices and building businesses in that part of the world. We have over the 20 years that we've been there established a brand and gained traction in most of the businesses we operate within. I can still recall about eight years ago when we went on road shows people were telling us to sell our asset management business in the UK because it had not gained traction. These things take time, and it takes time to build up a shop.

Australia we originally struggled to gain a foothold. We spent a lot of time reshaping our business model and making sure that we get the right people in the right place so that we can build that business going forward. And we do see strong links between that part of the world and what we do in South Africa and Africa.

To remind people what we are in South Africa, we're not a high street bank. We don't have branches. We operate in a niche environment. We target specific client communities, and we have got scale in all three of our businesses, in our banking businesses, our wealth and investment business and in our asset management business.

The industry that we've operated in over the last while notwithstanding the fact that is has not been so bad in South Africa has been very tough. There was a recent article in The Economist which articulated that the banking industry at the moment is a not-for-profit sector. It's a social responsibility industry at the moment. It has been a very tough industry to operate, and obviously that has an impact on us because we have businesses in that part of the world.

For those of you who think that return on equities in this environment and this world with this kind of regulation that we face – again read the article – are going to be 20% plus are actually living in a

delusional state, particularly when interest rates around the world, long-term bonds in most main countries that are stable are below 2%.

I think one has to factor that into account. You will accuse me of being defensive, some of you. I will try not to be defensive today. So I will carry on telling you what we're doing and what we stand for as a firm. I will deal a lot more about strategy than about numbers. Numbers, you can phone Ursula, look in the book or go onto the website. The information is all out there.

If we look at the year in review it has been a very difficult operating environment. As we stood here last year this time the world looked like it was in a much better place. It looked like it was recovering and getting on to some kind of sustainable growth path. I think that turned upside down when Europe started running into trouble again. That was around about June last year. I think all hell broke loose during the period. We've had ups and downs in this last year that has been like a roller coaster ride. In our industry when you have a roller coaster ride certain activity levels stop. You can be in the middle of transactions for clients and you can't get them away because shareholders have all gone into hibernation. They say they're not in this game. So it does affect levels of activity.

You've seen interest rates at very low levels in all the geographies we operate within. That also has an impact on earnings, because if you earn nought on your surplus cash or on your capital it has a big difference to earning 5%. And obviously in this particular period the Rand weakened quite substantially, on average about 6% or 7% against the Sterling which we report in. The other two were more or less flat in the year. At the balance sheet date it was about 13%.

So I think the world we're in actually masked the significant realignment that has taken place in our business over many years. As we've said, banking is a different game. Regulators want you to be a utility. Politicians want you to give your money away. They're not in synch with what they want you to do. The one wants you to have a lot more capital. The other one wants you to lend a lot more. As a consequence of that we have had to re-think this over the last number of years how we reshape our business model. That has been something that we have been doing, and we think the environment does really mask the success that we perhaps have had.

We have realigned our business model quite substantially. We've held our revenues. They were down marginally this year. If you strip out the debt buyback of last year they were flat. Despite the difficult markets our quality of earnings has increased substantially, which I will deal with in a moment. And I think many of our businesses have continued to deliver. We do have some under-performing businesses that we do believe are turning the corner, with gross levels of defaults down quite substantially, notwithstanding the fact that impairments overall are flat and down in our core businesses.

Integration also has been a focus of what we've been doing across the group. If we look at our core businesses again, in Wealth and Investment we integrated Rensburg which had to integrate our private banking operation into its activity. We have made substantial progress in the integration of Williams de Broë. That will only be complete towards the middle of this financial year for us. So these things take time. They involve integration of systems, processes and people. It is not something that is easy to do and it does take time, as I've pointed out.

We have already integrated Evolution Securities both into our investment banking activities and into what we used to call capital markets, and we have rationalised them into one entity. Then we have been on a medium-term path of putting all of our banking businesses onto single platforms with clearly defined target markets. We believe that over time that strategy will improve our offering to our clients as well as we will get significant cost and revenue synergies, not short term but over the long term.

And then we’ve also increased our cross-border activity to service our local client base and are creating global communities across our various geographies to ensure that our clients get access to those communities. Then we have also significantly restructured our Australian business and realigned our credit portfolio in that market so it looks a lot more like the rest of our organisation. We will deal with that in a moment.

So looking at our business mode, I think 49% of our revenue in this particular season came from what we would call capital light activities, the bulk of that from fees and commissions. And 51% of our revenue came from capital intensive activities, which is lending and some of our investment activities and to a lesser extend our trading activities. We are not a big trading bank as you will notice. We generated £109 million from trading revenue, which is not massive. It is 5% of our total revenue. So our model is quite different and a lot more defensive as a consequence to the US investment bank or a major global investment bank.

I think we have created these three distinct businesses and we’re going to report in this format going forward. Asset Management and Wealth and Investments made 48% of our operating profit. Specialist banking 52% of our operating profit. Obviously that number is a lowish number from specialist banking because we still had elevated impairments in this particular year. That should align itself back to probably 60/40, the target that we would set ourselves over time.

Impairments were down in two key geographies. Our credit loss ratio in South Africa is down to 0.61% from 0.71% last year. We would say a normal number for that business is about 0.4%, so it is not quite normalised yet, but it is normalising. In the UK it was down to 1.2% or 1.3% from 2%. That is also not quite normal yet. That should normalise in time at a lower level. And in Australia we had a big clean-up and we had an impairment charge of 3%. That will normalise again down at 0.4% or 0.5% and hopefully we will see that in the not too distant future. We can’t have that kind of write-off again. We just don’t have that kind of book left.

So we are seeing that unless the world blows up and there is some big drama out there we will see normalisation of this number quite quickly. I know you say we said that before, but we didn’t know Ireland would blow up and we didn’t know there would be floods in Queensland that would wipe out a whole coastal region for a while. We can’t predict the future, but where we stand right now that’s what we believe.

Costs relative to revenue did deteriorate slightly, and that was partially as a consequence of acquisitions and restructuring that is taking place in the organisation, and also as a consequence of a very difficult revenue environment. If you look at this chart since 2003 when we listed in London you can see the strong growth over this period in revenue, which has grown much faster. Revenue grew by 16% and costs by 13%. And that head count, if you exclude Evolution, is pretty flat. Obviously we’ve had adjustments in some areas where life is pretty tough and we see them as being tough for a long period ahead. But otherwise our head count is pretty stable. We’ve had in some of the areas that are growing an absorption of heads into the organisation.

So overall I would regard this as disappointing. It was a very disappointing year for us. At the start of the year we thought we would do a lot better. Our operating profit is down 17%. If you strip out impairments that's down 9%. Part of that would be the debt buyback, but part of that would be difficult revenue environment. And then attributable earnings down 21% and EPS down 26%. Obviously we have some more shares in issue which I know a lot of you guys are shouting about.

We've decided to keep our dividend flat. For the South African shareholders that is a big bonus because the Rand is a lot weaker. I don't see Louis, who used to complain about the dividend, or Ruby here today. And then we've also embedded in the dividend our STC credit, so that dividend for individuals which will be tax-free is another big boost. So you shouldn't be upset about the dividend. You can be upset about the earnings.

Then net tangible assets per share are down 8.3%. That's all in Rand. Because we translate into Sterling the Rand took about £200 million out of our net asset value. And then you can see our shareholder equity relatively flat, and that would be bolstered by earnings and some of the shares that we had to issue. Loans and advances were down 2.8%, but in stable currency they're actually up. In South Africa they're up about 5% or 6%. Australia down and UK pretty flattish.

So that's an overall summary of the story. If we look at our financial targets we did adjust our ROE target. We're way below it. 7.8% is not a happy number for us or for you. Very clearly we have to get the number back to within our targets in the not too distant future, and that is what we will strive to do. Obviously it is reflective of the results that we have just delivered.

Our EPS growth I have covered and our cost to income ratio I've covered. Our dividend is just within our target range at 1.9. The bottom end of our range is 1.7. And our capital adequacies for Investec Ltd up slightly at a total level, 16.1. Tier one down slightly in South Africa. That is after the implementation of Basel 2.5 which added about R6 billion of risk-rated assets. And the UK a similar sort of number. Flat on tier one and total capital up slightly again after the implementation of Basel 2.5. So we did get extra risk-rated assets from just a change in regulation. That would have affected those ratios, but still in our opinion pretty solid.

If we look at our divisions I think specialist banking has had a pretty torrid time over the last five years. We have some businesses doing well and others that have battled. If we went back into old-style terminology, private banking has battled and is still not profitable after this Australian write-off, but it will start coming back now. And what we used to call capital markets has continued to do quite well. So it is a tale of two cities inside that specialist bank.

Asset Management have doubled their earnings since the start of the financial crisis. That is a pretty strong achievement with pretty strong net inflows over the last few years. And wealth and investments is down slightly, but it is masked by two things. One is that we had to consolidate the [unclear] business in there which is still loss-making and needs to be fixed up. That is part of something that we're busy doing. And we sold the Asset Management piece of Rensburg, so we lost that revenue stream, which was about £1.7 million. So overall that business was up probably about 8% in this particular period. So that's just a headline summary.

If we look at Asset Management I think they maintained very competitive performance. They more than doubled their funds under management. They've had three years in a row of £5 billion of net inflows. And the momentum has been positive. I think they have good clarity on what they want to do in life and where they're going, and they just have to do more of the same. Obviously like all these businesses they are subject to the risks of volatile markets.

Their cost to income ratio slightly up, 64%. And at one stage the ROE was quite low because we'd made acquisitions. Now you can see through building off the back of some of our acquisitions, which was really the London business, the South African business has been grown entirely organically, the ROE is coming through at 84% and on tangible at 288%. So a well run business and continues to perform.

The wealth and Investment business, this is where we have spent money making acquisitions. The South African business has been the consolidation of a whole lot of little platforms. And the UK business has been a consolidation of a number of UK wealth managers. And we do cover with the Williams de Broë acquisition almost the whole of the UK in this business. It is a prop for our play in the UK and it is a substantial business. As I said results were adversely affected by the operation in Switzerland and the sale of the fund management business, which we got a fair amount of money for at the time. So I think the short-term prospects are supported by a lot of synergies that we expect to come through once the rationalisation is complete. So a lot of work to still do there, but with £35 million worth of funds under management globally it is a sizeable business for us.

Then we get to the Specialist Bank. Obviously this is where performance was down. Again it is a tale of two cities. The debt buybacks were not repeated. Last year we made £32 million on debt buybacks and some other money from closing out hedges which would have added to that £32 million. And then we had a weaker performance from our principal investment portfolio which was mainly listed assets which we hold in the mining sector where the shares came down quite substantially in this particular year, whereas in our private equity assets we still seem to have done reasonably okay.

So those were the two big reasons why the operating profit was down. We saw quite a good turnaround in our private banking operations in South Africa and in the UK. I think the legacy issues in Australia and in Ireland would have also clouded this overall performance. We also in our property group launched our property fund in South Africa. They had a very strong first year of performance with a return to shareholders of about 28%. At least they can say nice things about their performance. We can't. Well done to Sam and his team on that.

If we look at the outlook, we're in a tough macro environment and that does impact on activity levels. There are seasons when you think it is coming right, and there are seasons when you think will this ever come right. And I suppose we've seen the elections that took place in Europe over the last two weeks and the consequences of that. There is still a lot of tidying up to do in that part of the world. On the other side America looks like it's doing a lot better. So this is still going to be a tough space but we do see that impairments are starting to normalise. And certainly if you have a world as it is today these impairments will normalise over the next year or two. Cost to income ratio in that business at about 62%. I suppose that is reasonable when you think of the various business activities that we have.

Moving on to strategy. I think last year we spoke about three distinct different business units. They have different profiles. They do different things. Two of them deal with corporate, institutional and government, the Asset Management business. And they provide investment management services. And then the specialise bank, which deals both with private clients and corporate, institutional and government, provides advisory, transactional banking, lending, treasury and trading and investment activities to a fairly narrowly-defined client base starting with high-income individuals all the way

through to government. And then our Wealth and Investment business provides wealth management services to private clients.

Asset Management. This business has been organically built by and large into an international platform. Its focus is institutional and its client base is global. It has a strong culture and a very stable and experienced management team. And I think that its emphasis is on long-term sustainability and on quality and depth across its business, at all times maintaining cost discipline. It wins numerous awards. I think last year Hendrick himself won the award of European Fund Manager of the Year. It has really migrated from a South African business to a global business, and its brand is well established all around the world. That is part of a reward for the internationalisation strategy of our organisation.

So to answer the fellow in Business Day yesterday, explain why you went to London, explain all these things, here is a result of making our business a lot more international than just a South African business. And we think that long term we get lots of benefits from that. The same applies to this business. We've created a global platform with very strong regional capability. Our focus is on internationalising this business because many of our clients want an international offering. As in South Africa exchange control has been relaxed quite significantly. We don't want to lose all our money that we look after in South Africa to global wealth managers. We have to have products and capability to offer them.

So this was a very important step that we took in terms of building up this particular business. Clearly the focus is on the successful integration of Williams de Broë, and then the development of the international and UK resident non-domiciled business via our Guernsey and Swiss platforms. That's very important for us as an organisation, to maintain our presence. We operate in a number of different markets and we have sales and distribution in those markets. It is very important that we create this global platform.

So we have very well-established platforms in both South Africa and the UK. We believe we have spent a lot of money in building good systems which enable us to do things at a lower cost and that our offering is a very good offering. You can see again in this business also strong growth in funds under management, but obviously we spent money buying these businesses and now we can build off the back of buying these businesses organically. And that is our key, to drive this business organically.

If we look at the specialist banking business I've got here three areas but we're probably really four. We're an investment business where we invest in property, private equity and other investment opportunities. We have an advisory business where we advise large corporate and mid-corporate clients around the world on cross-border transactions or local transactions. Those are the two activities that we do inside the corporate advisory and investment business.

Then we have our corporate and institutional banking business which we always called capital markets. People get confused as to what you are because it is a banking business. You can see we don't make a lot of money trading, so we're not a big trading house. And then we have our private banking business that looks after private clients. And there we've got transactional banking, lending, deposits, advice and we offer our clients investments as well, often a lot of the investments from our other channels, which may be from the asset management business or the wealth and investment business.

So on our corporate advisory businesses I think what we have built are good domestic platforms. In South Africa mid to large cap. In the UK a very strong mid-cap space. And in Australia we're building a mid-cap franchise which we are having quite a lot of success at. Again the issue for us here is globalising this business so we're able to offer our clients links between the developed world and the emerging world and between the different geographies that we've got. And we have been spending time now putting these platforms together in global forums.

We're building a global resource capability. We have resource expertise in a number of the geographies that we operate within, and we're really starting to see good flow from that. It is important for us as a firm to have this capability so that we link the emerging world with the developing world. And it goes both ways. This is something that we have been building over many years. We have very good advisory platforms in place and we think that we are in a strong position in this particular market.

If we look at corporate institutional banking the bottom slide shows the capability in the Australian market. As you all know we have very good platforms in South Africa. The business has done very well in this particular year. We have a very strong capability in the UK and a developing capability in the Australian market. Our strategy here is focus more on capital light activities, go deeper into our core markets and we need to as a firm continue to lengthen our deposit bases as we contend with Basel III.

And then again the same principle of connecting Africa, India and China to our core geographic offerings. And I think that in my 30 years of being a banker, going around the world and talking to investors and the investment community I've never seen a more interesting Africa than we have now. I think it is the continent that people are having a massive interest in, thinking it is the next wave. We have to have the ability to deal, because people will see us naturally as an organisation that has a capability to do cross-border transactions into the African continent.

We have built a very good international platform. We do rely on traditional customer bank flow. We believe we've got very sustainable businesses in this place, and we continue to balance our business model and build our business depth.

Then we get on to our private banking business. I think a lot of you would know this business, certainly in South Africa, because many of you are clients. Our value proposition is we offer a high touch service to facilitate the creation of wealth and the management of wealth for our clients. We also provide transactional banking products. This is something we hadn't yet done in the UK and Australia. They're in trial at the moment launching it in both markets by the beginning of July.

There are a whole lot of banking, credit, investment type products to two distinct client bases: the high income individual and the high net worth individual. We offer advice and tailored solutions to the high net worth individual. We're focussing on back to basics. I think we lost our way a bit here. We became very property-orientated in two of our core markets. That obviously didn't work out so well because that's where a lot of our impairments come from. We're focussing on growing our client base and ensuring the product offering is delivered to our global client base.

So we also try and enhance some of our offerings because some of them need continual enhancement, and there is a lot of work taking place on systems and product integration. If you look back to 2009 you can see that our loans exceeded our deposits by over £3.5 billion. We've had a strong drive to build our deposit franchise in our core geographies, and you can see now the two match each other. So we have had some success in building our deposit franchise, particularly in the UK and Australia. Clearly in South Africa we always had a franchise, and it is a different market and different system where a lot of things are just wholesale and there is just not a lot of retail out there.

And then just to come back to Australia, I know that we've taken a lot of heat. Why did you go there? We went there in 1997 and again the reason was we were following clients and trying to create a business that supports our global client base. We also found that there is a lot of flow between Australian corporates and South Africa. Australians have big interest in resource capabilities in Africa. And 30% of our cross-border transactions for our South African corporate finance team were together with our Australian corporate finance team, as an example.

But we have re-orientated this business in its entirety. The private banking is focussed on professional finance and high income finance. This is what we started out in life, dealing with doctors and accountants. They have a very strong franchise and that business over the last four years has built itself into a profitable channel for us. And we have been reshaping the high net worth business strategy to focus on a focussed lending and advisory offering to our clients as opposed to being a property lender which we were.

So it is at this point in time just a specialist bank. We do have asset management people on the ground there, and they fall directly into the global Asset Management business but they look after the greater region. And I'm not talking about Australia; I'm talking about the greater region which is the Asia-Pacific region. They're going to shoot me for saying this, but Hendrick manages about $5 billion in the greater Asia-Pacific region. I'm disclosing it. So it does help you build. The fact that we've been pioneers, built a business, built a brand, established our platform, does help us in terms of other business activities that we offer the global group. We're going much more for alignment between what we do there and what we do in the rest of the world because it is important we align all of our business globally. Otherwise you just have a shop there that is not linked to what you do and not worth having.

And then if you look at the bottom slide it shows you the migration of the loan portfolio. You can see that at least 40% of what we did was property lending. The colour is like a greyish colour and a dark blue colour. The dark blue colour was the non-core book. And you can see that has come to a very low level at March. And the greyish colour is what we do in high net worth property finance, which is to a core client base that we're happy to service and look after. And you can see that 60% of what we do is a professional banking business. The whole business has been dramatically realigned and transformed over the last year. It has had a very problematic year because we've had to deal with the legacy stuff.

I think if I conclude we clearly believe that we have a well-developed brand. Our brand is well known and well accepted in the geographies in which we operate. Some of you will say you spend a lot of money on marketing. Yes, we have spent money and we have gained traction. People have got to know us and therefore they are comfortable depositing money with us, which is a very important thing for us. Now it is up to us to start offering them a greater degree of products.

I think we have continued to invest in people and a sustainable future. There is lots of stuff that we do as an organisation to develop our own people and to develop our societies at large. And I think that often we don't get recognition for this, but we win lots of awards and we're very active in this particular space. I know that doesn't help shareholders because it costs money, but it helps us in our communities at large.

I think what I want to go back to is where we started out in life when we listed in London back in 2003, what we have done in this period, because in this bad year you think we have gone back in life. We probably have, but not materially. I think in the last ten years we've had very strong growth in our revenues from £500 million to just under £2 billion. Some of that came from acquisition, but I can strip out acquisitions. It won't be big numbers, £200 million.

I think you have seen in this last year very strong growth in fees and commissions, up 12.3% in Pounds. In a stable currency it is up a lot higher. I don't have the number in my head. And net interest up 2.6%. Again in stable currency that would be probably 7% or 8%. And then we suffered this year because we didn't have the debt buybacks so our trading income came down. And then our income from investments came down for the reasons I quoted earlier.

But still a long track record of building a better quality earnings base. If we look at what we've done to our earnings drivers, we've grown our third party funds under management in Pounds by 17%. So if you start in 2003 and end in 2012 there is no exchange rate difference because they're almost the same. They were R12.30 against R12.50 in 2003. So a little bit of a difference, but not material. And if you look at our growth in loans obviously that has flattened since the financial crisis, but we grew loans by 19% since 2003 as we built our franchise around the world. You might say you shouldn't have done that, you wouldn't have taken the bad debt. Obviously part of that is correct. We maybe ran them up too high in the back end of the bull market. And we grew our customer deposits by 17%. And that would have been a big shift from wholesale to retail.

I think this number, a lot of people probably haven't worked out that our compound growth in intangible asset value per share was 17% in Sterling. That excludes dividends, if you go from 2003 to where we are today. If you take all the goodwill into account, which a lot of analysts like to do, it was 23%. But a lot of that has come from the issue of shares or acquisitions. So stripping it out and saying per share what is the number is was 17% over the last ten years. If I add dividends to the number if you invested at NAV in 2003 and you exited at NAV in 2012, and you took the dividends on the way, you would have earned 31%. If you went into the share at 2003 which was the bottom of the last cycle, took all the dividends on the way and exited at 2012, which is again a low point in our history, 22.5%. And then if you exited at NAV, which includes goodwill, in at 2003 and out 2012, and took dividends on the way, the return was 22%.

So if you look at our business over a long time there has been performance. Yes, the last year has been a bad year which we accept and we take responsibility for part of it. The crisis side we can't take responsibility for. That's life. We have also had to build our capital up in this same period and we have grown our capital base by 21% since 2003, which again is a consequence of needing more capital in particular environments where we operate, more capital from a regulatory perspective and more capital from a counter party perspective. So we have had to do this over the years. Most of it has been internally generated. Some of it we have done shares for cash to buy back debt, which would have helped us no the way. These are things we believe we had to do because we had to manage our balance sheet.

Over the last four years what was important for us was to build businesses that have got momentum and to manage the balance sheet, make sure that we have the capital and liquidity to navigate a very difficult crisis which can limp along for years to come. Some people think this thing can go on for another five years, this up down up down that we've been living with over the last while. But anyway, we live in an emerging market so hopefully it won't be so bad in South Africa.

So in summary our strategic focus is still building low capital intensive revenue, managing the capital side of life very well, making sure we keep the business tight from a cost perspective, but we still need to invest for the future, always maintaining the appropriate levels of capital and liquidity because that helps you get through difficult storms. I remember [unclear] from New Republic Bank said that you build your boat so that it can navigate through very rocky waters, because that's the kind of world we live in. Then we want to continue implementing our single bank structure so that we get the right operational efficiencies and offer the right product to our client base. We just want Hendrick to maintain momentum in Asset Management. He doesn't have to do anything else. He must just keep going. And then we have to complete our integration in Wealth and Investments and continue internationalising our offering. And we need to capture the opportunities between the developed and the developing world because that's what we're positioned to do as a firm.

So our outlook, we're in a very challenging environment and we will continue to pursue the strategy of aligning our business model. We believe that our competitive position is strong. And I certainly believe in Europe where we operate – we don't really operate much in Europe, but certainly in the UK – we have very good competitive positioning because we are still open for business. We don't have to de-leverage our balance sheet by 40% as some of the European banks have to do. They have all gone home. They have all had to go home because they had to slow down their internationalisation strategy.

So there is a lot of opportunity for us as a firm with our platforms in place. We believe we have very good people and we have good skills in our organisation and we believe we can continue to take advantage of opportunities in our core niches. Our focus is on winning new clients and servicing existing clients in the best possible way. I think we have dealt by and large with our legacy issues and we can concentrate now on clients. But again environment remains unpredictable, but we will continue to build on our solid foundations.

I think in closing I've got a little story to tell. What people fail to understand about us is we're an organisation that has developed a unique culture which encourages our people to be transparent through open and honest dialogue. This results in the organisation receiving a massive amount of feedback which is often very robust. The last few years have taught us many lessons and reminded us of lessons we learnt in the past but may have forgotten. I think if you were a lender in South Africa in 1998 when rates went up to 25% you learnt some lessons on what not to do. Unfortunately by 2006 we'd forgotten and repeated some of the mistakes. Now we hard-code them so we don't repeat them again. But we are an organisation that accepts feedback from all our stakeholders. That's not only our shareholders but all our stakeholders, which includes government, employees and society at large. And we believe our ability to understand and act on such feedback can only help us create a more powerful organisation in the future.

So from where we stand as a firm we navigated a storm. We know we haven't done well this year. We know we haven't performed well this year. We know that a return on equity of 7.8% is no good and that we have to get it back to the number that we lived with. We will never get back to 20% unless the asset management and wealth management become a much bigger part of our business. And that just depends on how life is out there. We know we have a lot to do as a firm. We think we have done a massive amount of work to ensure that tidy, that we deal with our legacy issues and make sure that we can go forwards as opposed to go backwards.

And if we show you what we've done over the long term we have a business that is maybe a hundred times better than the one that was on a 35 multiple about 12 years ago. So we can't help where share prices are. We've got to run our business and manage our business in the best way we can. There are times that will be positive and times that will be negative. So we take the feedback, we understand what shareholders are saying. We're out there trying to build value, trying to look after our clients. And obviously we're trying to do the best we can. We really believe we have the platforms to succeed. So again on that note I thank you all for attending. I thank you for your feedback over the last while and look forward to any questions that you may have. I will start in London. James, you're almost like Ruby and Louis.

James
Good morning. I promise not to ask about the dividend. Two if I may. Firstly on the balance sheet. Will you be happy for customer deposits to yet again outstrip loans and advances to customers this year? And secondly, can you tell us how much of your loan book is [unclear] loan to value is 85% or more?

Stephen Koseff
On the second question you will have to ask Ursula. I haven't got the details in my head. You will have to ask her that question online. The first question is our strategy is to diversify our customer base, and therefore we did slow down the deposit growth for a while and then we let it run again. But we're still going to diversify our customer deposit base, and therefore you may see continual growth but obviously we have a loan deposit ratio of below 70% and it is more about diversification than growth at this point in time. Any more questions?

Male speaker
No more questions here, Stephen.

Stephen Koseff
Okay. I will come back to South Africa. I don't see Ruby or Louis here. Stefan.

Stefan
Just a question on the ROE for the bank. Do you think you will be able to exceed cost of equity over the next few years? And if not shouldn't one consider being a bank in the UK, maybe exit the UK and just run the bank in South Africa and an asset manager in the UK?

Stephen Koseff
We get that question quite often. We believe that we have built a franchise and we do believe that cost of equity will adjust for risk. It hasn't adjusted for risk. You've still got very high expectations of what cost of equity should be for that type of business. But as people get more comfortable with... If you look at the slide I put on from The Economist you can see where bank returns were until the late 80s. They were always below 10 ROE. And if you don't have 20 years rates or 30 year rates or three and ten year rates at two to say that we've got cost of equity above that sort of number is delusional. We think we can get a reasonable return in that business. That business is not only about being a bank. I think it adds value to other businesses that we have, particularly the wealth business as we capture the client from either side. It's the same question you guys asked us in 2004, why don't you sell asset management because you're not getting a good return from it? We think strategically it is right for us to be there. We've got a good platform. That part of the world is going through a particular difficult time and we will manage our way through. We don't manage the business for today. We manage it for the long term. Mike.

Mike
Stephen, I know your presentation is more on the macro stuff, but just to ask some questions focussing on one area. A few years ago you spent quite a bit of time talking about your exposure to residential

and commercial property loans in the UK. I don't think you've mentioned it today. I'm sure that business hasn't disappeared and I hope it's not part of your social security or charity businesses you were talking about in your first slide. But perhaps just a mention on how that's doing, that residential property business.

Stephen Koseff
The mortgage business.

Mike
The mortgage business in the UK. Then turning to South Africa. We hear a lot about Investec Bank's exposure to certain property developments and golf courses and things like that. Presumably you've taken a lot of assets onto your book. Are you in a position to give us some sort of number and some strategy on how you're working your way out of that?

Stephen Koseff
You saw our South African net defaults are 2.7% of our book. So I will start off with that question. We had relative to the size of our book our residential property was less than R1 billion. So you're not talking a massive number on a R130 billion book. Some of those things we have taken in. We've got one that changed their name to Copperfield. Some of them we've actually sold. We built the club house and we're selling the stuff out. It will take us three years but we'll have all our money back plus some change. There are some that are more difficult than that, but they're small in our life at the moment. And we haven't done that kind of lending for five years. So I don't know if that deals with that side of life. So I think those are little pimples. Yes, they were stupid, because if I went back to ten years earlier I would never have done any of them, but some crept into our system and said okay, we can do this stuff because we've got pre-sales and risk is de-risked.

If you get to the UK business I think you're talking specifically about the mortgage business. We bought Kensington in 2007. I think on the UK stuff it has been going fairly well. Obviously we had big write-offs as we told you at the trading update. We had a write-off in Kensington of £99 million. So it basically broke even this year as opposed to other years that it has been profitable. And that book is in run-down mode. We've changed that business completely. We want to deal with only prime clients and clients we're happy to have as private clients of our group as we move forward. So we have shifted that business completely. The other thing is we have been reducing our exposure to commercial property. I don't know what the exact number is and what has happened to it relatively speaking, but certainly in the UK we're doing much better quality deals because a lot of banks are not doing anything. And we are managing our legacy stuff out. We're doing reasonably well there. Clearly we have the little business in Ireland. We haven't done any lending in Ireland for four years or three years. And we had to deal with the consequence of the bubble, and that was the big write-off last year. The write-offs in this year have been relatively moderate compared to the write-offs last year. So I hope that answers your question. If you want more detail you'll have to ask Ursula. I don't know if off by heart. More questions.

Ben Cantor [?]
Of the banks that you compete with in the UK how many of them are either emerging market-based banks such as HSBC, Standard Chartered, alternately state-owned? How many are truly independent banks in the UK?

Stephen Koseff
You’ve got Standard Charter which is an emerging market bank. That has had a very successful strategy by focussing on the developing market. HSBC is mixed, so it has got both developed and developing world, a lot more like us. And then you’ve got Barclays which is independent. And then the two big ones, RBS and Lloyds, obviously still have significant shareholders. And then you’ve got a whole lot of others that were banks that are in run-down mode like Northern Rock. Alliance & Leicester is part of Santander. There is Santander as well in the UK, which is owned by Santander, the Spanish bank. And then you’ve got Rothschild and a few guys, but they’re not as active in our space. They are more advisory operations. The competitive landscape has shifted dramatically there. Is that the point you’re trying to make to respond to Stefan’s point?

Ben Cantor
Sure.

Stephen Koseff
Which is an opportunity, not a threat actually for us. And we’re a fresh brand. People were unhappy with what was going on there, all their banks.

Barry
I don’t know if you can hear me. If you had to benchmark Investec, against which...? That’s what I think the question is.

Stephen Koseff
I can’t see you. Where are you? Oh, Barry. You can’t benchmark us. That’s why I’ve given you three firms, three income streams. You’ve got wealth and investment where there are boutiques like Rathbone or a whole host of guys in the UK we would be very similar to. Or Julius Baer in Switzerland. We’ve got Asset Management where you can compare us in South Africa to Coronation. And in the UK you’ve got to compare us to Schroeder [?], Aberdeen. I wouldn’t compare us to Man Group because they’re more a hedge fund type operation. And then you’ve got the Specialist Bank where we’re a different type of animal. There is the Close Brothers in the UK which is a specialist bank but also has some asset management and wealth management. There is Macquarie in Australia, but they’re much more investment banking. Goldman’s we’re not the same as. So it is hard to find a peer. And you guys don’t value the bank at much anyway. More questions? Nothing. Okay. That took a long time. There should be something to eat for those of you who are hungry. I’m pretty hungry. I’m here to answer any questions you guys didn’t want to ask online. Thank you.

END OF TRANSCRIPT