Conference Call Transcript

14 September 2018

PRE-CLOSE BRIEFING

Stephen Koseff
Good morning everybody. Welcome to our pre-close briefing. Most of you would have already seen that we made an additional announcement this morning which I will deal with at the end of the briefing. This is to give you some guidance to the end of September. And some of the asset management and balance sheet figures are up to the end of August. If we look at the operating environment we are still operating with a lot of uncertainty in both our core geographies, notwithstanding the fact that the global world when you look at the macro picture is doing okay, particularly the US. The South African economy is very weak as you would have seen with GDP figures released last week where they talk about a technical recession. You can argue whether it's a recession or a technical recession, but confidence is weak as a consequence of policy uncertainty and that is having an impact on overall business confidence.

I think both the SA equity market and the UK equity market have been okay during this period, particularly in the last few months. SA is supported by Rand hedge stocks, the UK also by a weakish Sterling. If you look at our overall business for the period ended 30th September I think our Asset Management business should report results well ahead of the prior period while the Investment business is expected to report results behind the prior period. Both divisions however have had high levels of funds under management and reasonable equity markets and good net inflows. If we look at the Specialist Banking business the UK specialist bank is expected to report results well ahead of the prior period. The South African banking business is more or less in line with the prior period.

The exchange rate has had a negative effect with the Rand at this point in time depreciating approximately 3.5% on average against the Sterling over the equivalent period. We do expect revenue to be moderately ahead of the prior period. Recurring revenue will be approximately 78% of our total revenue, and that will say that the weakness in our results will have been investment income. Otherwise all the other factors we saw growth. The total income statement charge is less than the prior period. I think obviously we have dealt with legacy so we expect our bad debt charge to be between 0.21% and 0.25% compared to 0.54% last year. Costs are higher, and that is growth in head count to support both activity levels and increased regulatory requirements, in particular in the UK where we had MiFID II and GDPR. So we do expect our adjusted operating profit to be ahead of the prior year.

Looking at our core growth drivers I think third party assets under management increased 4% in Sterling, 8.7% on a currency neutral basis. Customer accounts are down 5.5% in Sterling. That's really the Rand. 2.5% on a currency neutral basis. And loans and advances down a similar number, but an increase of 2.5% on a currency neutral basis. We maintained a very sound balance sheet. Liquidity is retained at very strong levels. Loans to customer deposits at the end of August were 79.6%. Our capital ratios are expected to be in line with our group target. We have got permission to do a parallel run – still subject to regulatory approvals – to implement foundation IRB in South Africa by the end of the 2019 year. And we expect that to have a 1.2% improvement in our core tier one ratio in South Africa. So that is a pre-step towards where there would be further improvement. Our leverage ratio was sound. They are running at

over 7% so they are comfortably ahead of our target. So overall we believe the balance sheet remains very sound.

If we look at the individual business units in Asset Management I think very strong inflows. I think perhaps a feature of these results, £4.4 billion to the end of August 2018. Again we've had a competitive investment performance over the long term notwithstanding challenging markets, particularly emerging markets where there has been outflow from emerging markets. I think the leadership transition is well underway with an orderly and well executed plan. If you look at funds under management they are up 4.9% in Sterling to £109 billion, which is 9.7% on a currency neutral basis, which we believe is very strong underlying performance.

On the Wealth & Investment business we expect to be behind the prior period. We have got higher funds under management. We had net inflows of £600 million. That is mainly discretionary inflows. We did have some discontinued services as a consequence of MiFID and obviously we have had some outflows as a consequence of that. I think on the South African side underlying profitability is impacted by lower activity levels because of lack of confidence. There is an element of activity that always comes through in the wealth numbers. On the UK side I think we've had higher costs driven by IT initiatives, implementation of MiFID II and GDPR which have had an effect on this business. So overall funds under management up 2.4% in Sterling to £57.4 billion, 7.1% on a current neutral basis.

Looking at the Specialist Bank we are expecting to be reasonably ahead of the prior year. Net interest income driven by book growth in both the UK and South Africa is up. Fees and commissions driven by good performance from our UK corporate advisory business as well as our South African private and business banking activities are up. Investment income is well behind the prior year due to weaker performance from listed and unlisted equities relative to the past year, and partially offset by improved trading income. Costs in the UK are up in line with revenue and flat if we compare to the second half of last year. You are aware that there were a lot of investment costs in that business. That has now flattened and tapered off. So we expect that we will not see cost rises of any kind of material form going forward. In South Africa costs are increasing at below inflation which I think is well under control.

I think on other information our expected tax rate is effectively 18%. Last year it was at 14.5%. So it is starting to normalise. And then our non-controlling interests of £35 million is profit relating to Asset Management business and ten consolidation of the Investec Property Fund. And then weighted number of shares in issue of approximately 937 million shares. So overall I think the environment has been challenging. We have still got a lot of uncertainty around the type of Brexit we're going to have, which has some impact on confidence in certain sectors.

Our activity levels in the UK have however been supporting profitable growth and have been acceptable. I think on the South African front there has been negative emerging market sentiment. There is continued policy uncertainty. Hopefully that starts getting dealt with. We're in an election year so that also encourages populist rhetoric. But that has hurt investment confidence and we've had a significant weakening of the currency particularly in the last few months. So growth in that environment is challenging and is being reflected in overall activity levels and performance.

So when we look at the overall group results I think they have been supported by good growth in funds under management, positive net inflows and an improving performance by the UK specialist bank. And that's the nub of the issue. So what we told you before was once we get through this legacy – which I haven't mentioned here, but it is behind us – we will start seeing a strong uplift in the UK specialist bank which is what we're seeing in these numbers. So that's the trading update. I don't know if anyone wants to ask questions. I will start in London before I go onto the next story. No questions. Can I go to Johannesburg? I can't see Johannesburg. Are you still connected?

Male speaker
We are here.

Stephen Koseff
Are you there? Are there any questions? No, okay. So we also announced this morning the proposed demerger and listing of Investec Asset Management. I think since we made the succession announcement in Feb 2018 we've focussed on orderly transition of leadership. Fani and Hendrik will assume their roles as joint CEOs on 1st October as was previously planned. In conjunction with this leadership transition the board together with the executive directors, old executives and new incoming executives, did have a strategic review of the group. The strategic review has focussed on ensuring that the group is positioned to enhance long-term interests of shareholders, clients and employees.

I think through the strategic review we concluded that the group comprises of a number of successful businesses operating across two core geographies with different capital requirements and growth trajectories in those businesses. We see there are compelling current and potential linkages between the Specialist Bank and the Wealth & Investment business which deal with private individuals. Elements of the Specialist Bank and the Wealth business do deal with private individuals. However there are limited synergies between those businesses and the Asset Management. So post that review I think the board has concluded that it is now appropriate to demerge and publicly list Investec Asset Management.

The Specialist Bank and Wealth & Investment business will continue to remain part of the dual listed company structure and it is intended that Asset Management will be listed on the London exchange with an inward listing into Johannesburg. We believe that this transaction simplifies the group and focusses both Asset Management and the remaining group on their respective growth paths. We also believe that this will enhance the long-term prospects and potential of both businesses for the benefit of all stakeholders. The transaction is subject to regulatory approval, shareholder approval and other approvals and is expected to be completed within a 12 month period.

The Asset Management team's management stake will be retained by them so they will end up with shares in the listed entity. And the remaining group will maintain a minority stake in Investec Asset Management. I think post the implementation of the transaction shareholders of Investec Group will have a direct shareholding in Asset Management in addition to their shareholding in the remaining group. Following the implementation Fani Titi will lead the remaining group and Hendrik du Toit will lead Investec Asset Management. The precise mechanics of the demerger and listing will be communicated in due course. So we are not here to talk about the mechanics because that's a process and we will come back to the market as soon as that process is clearly defined.

So we believe that our individual businesses are well positioned strategically with strong market positions and good prospects and it is now the right time to demerge the Asset Management business. It wasn't possible in the immediate past. So I think we believe it is now the right time. We have made very good progress on expanding our banking and wealth management franchises in our two key markets over the years and we are focussing and have improved the operational and financial performance. I think the transaction does allow these businesses to reach their full potential and shareholders we believe will benefit from future value creation having a direct ownership of two separately listed companies.

People ask me why, and I relate it to when my daughter left home and got married. First it was very hard and then I had three grandchildren and now it's easy. So she was also allowed to go on and develop as an individual. I think we have been building Investec Asset Management together with Hendrik and his team for 28 years. It's like letting one of our children go, but we are giving it its own wings to fly. So I think this is where we've come to as a firm and we believe that both businesses should flourish in the ongoing future. And there will be a much greater degree of focus and much more simplicity. And we understand you guys in the market like simplicity. You don't like complexity. So that's the end of the story. Thank you. Questions. Questions here in London? Richard.

Richard
We are here. Any questions in Jo'burg?

Operator
There are no questions from the lines.

Richard
There is one.

Stephen Cranston
Hello. It's Stephen Cranston. So does that mean obviously John Green and Mimi Ferrini go back to their old jobs? They must be a bit disappointed.

Stephen Koseff
You have to be cynical hey.

Hendrik du Toit
Stephen, I tried to avoid your questions for a long time. I even went into banking not to deal with them, and now you catch me. No, absolutely not. There is an executive transition happening in the group and in the Asset Management business on 1 October as announced. Mimi and John become joint CEOs of the Asset Management business and Fani and I take up the group and we have to navigate this. And after that we each go our different ways. But only after that is executed. So no, John and Mimi remain exactly as announced and they have to start work. So there actually grandchildren already. Any more questions, Richard?

Richard
No. Stephen can't ask more questions. [Inaudible background chat].

Stephen Koseff
Is that is, Rich?

Richard
Looks like it, Stephen.

Stephen Koseff
Okay. I hope they've got food. Thank you. Okay, thanks very much. Thanks everybody for attending and we will see you soon. Next time Fani and Hendrik will present. Cheers.

END OF TRANSCRIPT