IFRS* 17: Insurance Contracts

Investor presentation

12 October 2022

* International Financial Reporting Standard

Financial Planning | Investments | Insurance | Health | Retirement | Wealth

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Currency

Unless otherwise noted, all amounts are in South African Rand.

CONTENTS

PURPOSE OF PRESENTATION

- Introduce the investor community to a high-level impact of IFRS17 on Sanlam’s reporting
- Flag areas of significant difference between IFRS 4 and IFRS17 as relates to Sanlam’s reporting
- Advise on Sanlam's readiness for Day 1
- Provide a platform to address some of the FAQs

IMPACT ON FINANCIAL REPORTING

KEY MESSAGES

What is NOT CHANGING	What IS CHANGING

What is NOT CHANGING

- **No impact on** investment management operations, investment contracts, retail credit and other **non-insurance businesses**
- **Sanlam's business strategy** with the key financial performance focus remaining on value creation and dividend growth
- Reporting will continue to focus on **the same key performance metrics. GEV** to be **retained as primary measure of shareholders' value creation**
- **Free cash flow generation** for dividend purposes
- The **financial strength** of the Group

What IS CHANGING

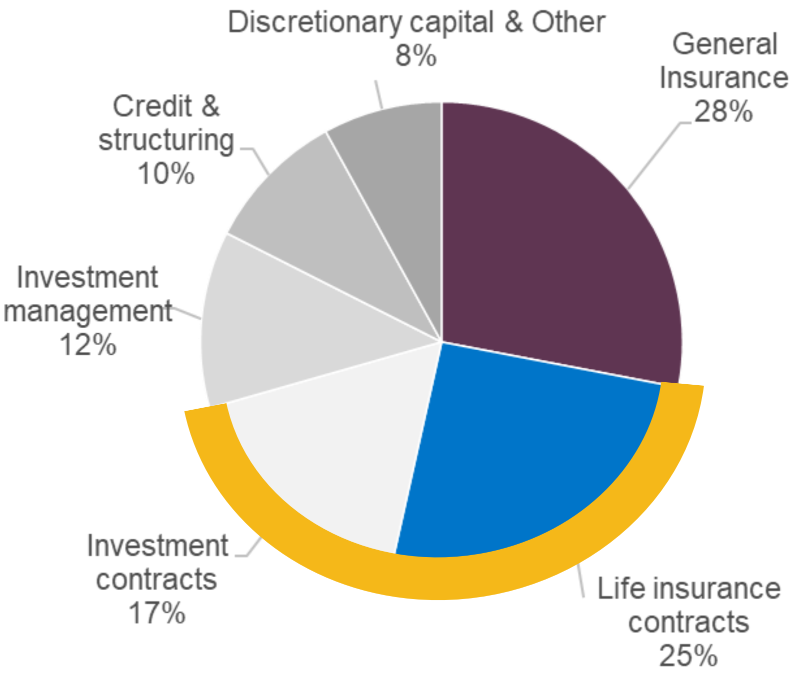
- **Measurement, presentation and disclosure** of Sanlam's **life and general insurance businesses**
- **Earnings recognition in the income statement may accelerate marginally**, but impact on free cash flow generation is expected to be limited
- **Amendments to the South African tax legislation for insurers**
  - Acceleration of tax in respect of transition amount, time value of money impact with no impact on earnings (income statement)
  - Funded from reserves released on transition

SHAREHOLDERS' FUND INCOME STATEMENT VS IFRS INCOME STATEMENT

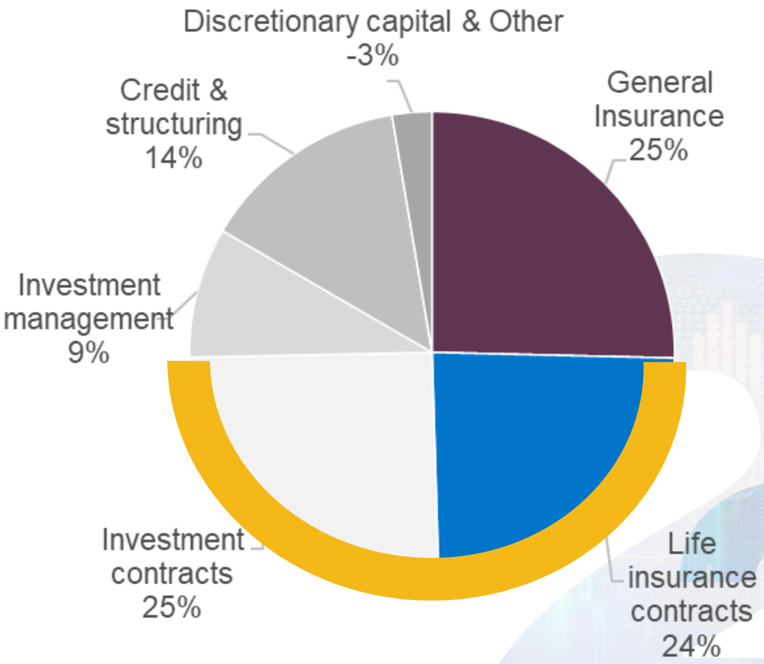
- In line with past practice, we will continue to prepare a Shareholders fund income statement in addition to the IFRS statement of comprehensive income
- Attributable earnings in the Shareholders fund income statement is equal to Profit after tax attributable to Shareholders in the IFRS income statement
- The Shareholders fund income statement is a different presentation of the IFRS information and reflects:
  - Earnings from operations – how we manage the business
  - Investment return earned on shareholders fund / capital
  - One-off expenses (project expenses)
  - Non-economic mismatches on a separate line
  - Amortisation of intangible assets and other income and expenses
- GEV remains the primary measure of value creation (53% relates to life and general insurance contracts) with reconciliations to IFRS

ANALYSIS BY LINES OF BUSINESS[1]

Group Equity Value



Net Result from Financial Services



= Covered business

[1] At 31 December 2021

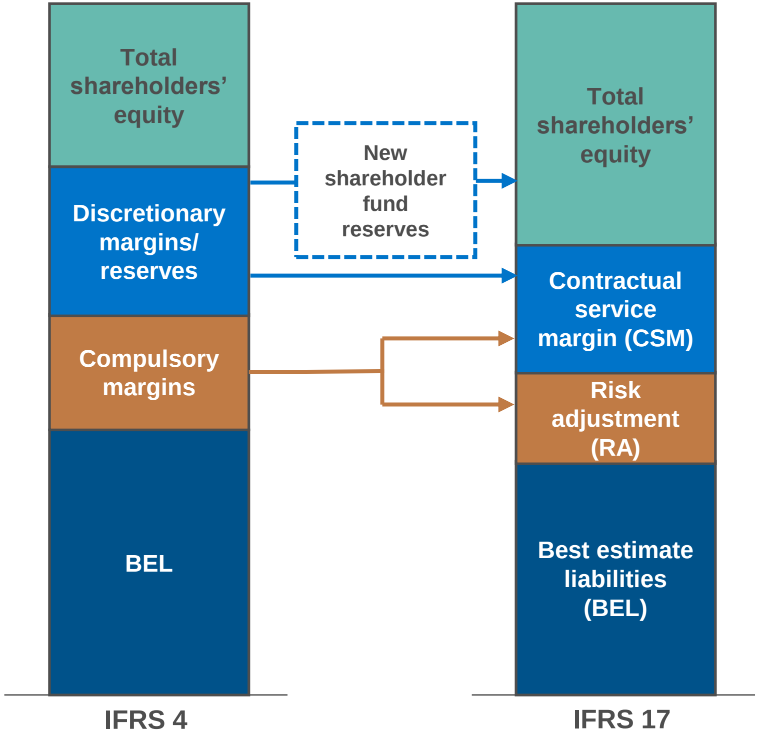
IMPACT ON KEY PERFORMANCE INDICATORS

KPI's	Notes	Expected impact for the Group
Earnings • Net result from financial services • Net operational earnings • Headline earnings	• Initial acceleration in earnings on new business expected (mainly due to deferral of acquisition costs) • For the in-force book future profits are reduced. Overall impact depends on the mix and volume of new business relative to the in-force book	Marginally positive for life insurance Limited impact is expected on general insurance net earnings
Cash earnings	• Cash generation will be very similar to the current experience	Limited impact
Group Tax (South African businesses)	• Tax payments will be accelerated in phasing-in period (6 years) of transition amount for life insurance • Not material for general insurance • Tax is provided for in current reserves	No impact on earnings / dividends (additional tax payments funded from balance sheet)
Business volumes	• New business volumes and net client cash flows not impacted	Value of New Business: limited impact
Group Equity Value **Return on Group Equity Value**	• GEV based on Discounted Cash Flows (DCF) of future cash flows	Limited impact
Group dividend	• Group dividend policy is unchanged	Limited impact
Solvency cover[1]	• No change in own funds. Change in composition between net asset value and value of in-force. • Assets released from policyholder funds to be retained in shareholder funds for solvency purposes	Limited impact

[1] Review of target solvency cover ranges – update to be provided with 2022 year-end results. Continue to investigate opportunities for further balance sheet optimization.

TOTAL EQUITY AT TRANSITION

Illustrative example of impact of IFRS 17 on the balance sheet at transition[1]



The Group expects a net reduction in policyholder liabilities at transition

1. **BEL**:- best estimate of policyholder cash flows
   - excludes expense cash flows not directly attributable to insurance contracts; and
   - includes impact of discounting incurred claims on general insurance business.

2. **RA**:- compensation required for future changes in non-financial risks

   Provisions for financial risks included in the CSM

3. **CSM**:- unearned future insurance profits

   Discretionary (e.g. zeroisation) margins will be released

4. **Total equity**:- increase in equity from release of policyholder liabilities, partly offset by the derecognition of insurance-related Value of business acquired.

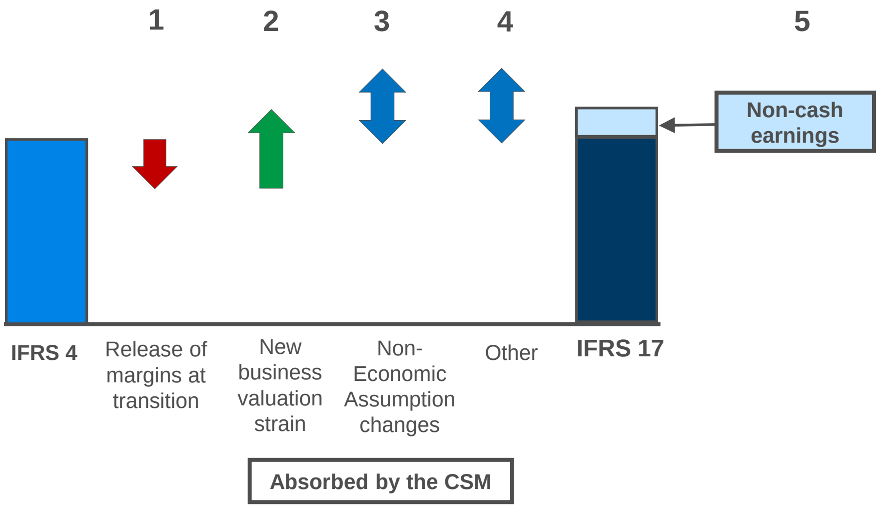
   Asset mismatch reserve will be released from insurance liabilities and held as new shareholder fund reserves

[1] This is an illustrative example, the respective sizes of the bars do not represent actual transition impact

NET RESULT FROM FINANCIAL SERVICES POST TRANSITION

Illustrative example of IFRS 17 impact on net result from financial services[1]

Sanlam expects an acceleration in the recognition of profits



[1] This is an illustrative example, the respective sizes of the bars do not represent actual profit impact.

1. **The net reduction in policy liabilities (including margins)** at transition will reduce subsequent profits from the in-force book.
2. **Net new business valuation strain** under IFRS 4 is eliminated and absorbed by the CSM.
3. **The impact of changes in best estimate assumptions** will be deferred over the lifetime of the contracts.
4. **Other changes impacting** the **expected timing of earnings:- frequency of zeroisation** and **pattern of releasing profits.**
   - Under IFRS 4, Sanlam elects to zeroise the insurance liabilities in each reporting period – this results in some deferral of profit recognition for in-force business compared to IFRS 17.
   - The pattern of CSM recognition and RA release is expected to be more predictable and based on when services are provided.
5. There will be an adjustment to reported IFRS 17 earnings to determine **cash earnings / free cashflow generation for dividend purposes**

CONCLUSION AND NEXT STEPS

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Overall, the Group is **well positioned for the adoption of IFRS 17** on 1 January 2023:

- Opening transition balances have been calculated and is currently under review by external audit.
- All system build activity is complete and is currently being used to calculate interim (June 2022) IFRS 17 results.
- Although there is an acceleration of future profits and taxes, the expected impact on the Group's KPI's (RoGEV, dividends, solvency) is not material.

Next Steps

- Finalise audit review of opening balances.
- Q1 2023 Operational update based on IFRS 17 will be communicated in May 2023.

ADDITIONAL INFORMATION

CHANGES TO INCOME STATEMENT PRESENTATION

Illustration of condensed shareholders’ fund income statement

IFRS 4

Financial services income
Sales remuneration

Income after sales remuneration
Underwriting policy benefits
Administration costs

Net result from financial services
Net investment return
Project expenses

Net operational earnings
Net other earnings

Normalised attributable earnings
Net other earnings

Attributable earnings[2]

IFRS 17

Result from life/general insurance contracts1
    Insurance revenue 1
    Insurance service expenses 2
    Insurance investment result 3
    Non-attributable expenses 4
Result from other operations 4

Net result from financial services
Net investment return
Project expenses

Net operational earnings
Net movement in asset mismatch reserve 5
Net other earnings

Normalised attributable earnings
Recognition of changes in CSM at locked-in interest rates 6
Net other earnings

Attributable earnings[2]

[1] Result from life and general insurance contracts are presented separately in the income statement. The income or expenses from reinsurance contracts are shown separately as a single amount in the income statement.

[2] Attributable earnings in the Shareholders fund income statement is equal to Profit after tax attributable to Shareholders in the IFRS income statement

CHANGES TO INCOME STATEMENT PRESENTATION (continued)

Illustration of condensed shareholders' fund income statement

Changes in presentation

1 2 **Insurance revenue** and **insurance service expenses** based on services provided (insurance service result)

3 **Insurance investment result** reflects difference between actual investment returns earned on policyholder fund assets and discount rates used in insurance liabilities (after SHF adjustments)

4 **Non-attributable expenses** and **earnings from other operations** presented separately (e.g. related to investment contracts and non-insurance operations)

SHF adjustments

1 3 **CSM accretion at locked-in rates vs current rates** transferred from insurance investment result to insurance revenue, with no impact on total earnings

3 Current **asset mismatch provisions** in policy liabilities replaced by SHF asset mismatch reserve

Artificial accounting mismatches removed, e.g. recognition of changes in CSM at locked-in interest rates

5 6 Net **movements in mismatch reserves offset** the **SHF adjustments in net result from financial services**

COMPONENTS OF INSURANCE PROFITS

1 Insurance revenue

Long-term insurance business[1] includes:
- Recognition of CSM
- Release of RA for risk expired
- Release of expected incurred[2] claims and admin expenses from BEL

Short-duration insurance business[3] includes:
- Earned revenue

2 Insurance service expenses

- Actual incurred claims and admin expenses
- Expected future losses recognised immediately
- Actual acquisition expenses incurred (short-duration insurance business only)

3 Insurance investment result

- Investment variances (after SHF adjustments)
- Amortisation of asset mismatch reserves

4 Non-attributable expenses

- Actual expenses not directly attributable to insurance contracts

[1] Long-term insurance business is measured using either the General Measurement Model or the Variable Fee Approach
[2] This excludes acquisition expense cash flows. The acquisition expense cash flows are deferred over the lifetime of the insurance contracts and presented separately in insurance revenue and insurance service expenses (no impact on earnings).
[3] Short-duration insurance business is measured using the Premium Allocation Approach

OVERVIEW OF IFRS 17 IMPACT ON FINANCIAL REPORTING

Measurement

- Consistent principles for level of aggregation and measurement of insurance contracts
- Unearned future insurance profits (CSM) and provisions for non-financial risks (RA) are measured and disclosed separately

Timing of profit recognition

- Consistent principles for recognition of profits as insurance services are provided, including:
  - no up-front recognition of unearned profit; but
  - immediate recognition of expected losses arising from non-profitable groups of insurance contracts

Presentation

- Insurance and reinsurance contract assets and liabilities presented separately in the balance sheet
- Amounts for insurance and reinsurance contracts presented separately in the income statement

Disclosure

- Additional disclosures expected to provide more transparency and provide more granular information to the users of financial statements, e.g.:
  - Reconciliations of the movements in the components of insurance and reinsurance liabilities during the reporting period

FREQUENTLY ASKED QUESTIONS

Some of the questions encountered over the past few months in preparation for day 1

Question	Answer
Impact on pattern of cash earnings (business level as opposed to product level)	IFRS 17 is not expected to have an impact on free cash flow generation.
Impact on dividend policy	No change in dividend policy – continue to be based on free cash flow generation.
What happens to positive experience variances of the past?	IFRS 17 is not expected to have an impact on the level of experience variances relative to our best estimate assumptions. Amounts related to non-attributable expenses are not reserved for under IFRS 17 and will be presented separately in the income statement.
Will you be changing your approach to best estimate assumptions?	The only notable change is the reduction in unit expense assumptions to: • exclude non-attributable expenses not directly attributable to insurance contracts; and • allow for the expected growth in the SEM businesses still building scale (where relevant).
Changes to sources of profits?	Main sources of IFRS 17 profits have been covered in the Annexure (‘Components of insurance profits’).
How will the new JV with Allianz be reflected	Equity accounted, reflecting Sanlam’s economic interest in the JV’s earnings and net asset value. Continue to reflect line of business information for Shareholders Fund reporting.

IFRS 17 GLOSSARY

Term	Abbreviation	Description
Carrying amount of a group of insurance contracts	n/a	The total IFRS 17 liabilities comprising the sum of the liability for remaining coverage (LFRC) and the liability for incurred claims (LIC). The LFRC is equal to the fulfilment cash flows (FCF) related to future service allocated to a group of insurance contracts, plus the Contractual Service Margin (CSM) where relevant. The LIC comprises the fulfilment cash flows related to past service allocated to a portfolio of insurance contracts.
Fulfilment cash flows	FCF	The fulfilment cash flows of a group of insurance contracts are equal to the current estimate of future cash flows (related to future and past service) plus the Risk adjustment (RA) for non-financial risk (covered below).
Current estimate of future cash flows	n/a	The discounted present value of the unbiased, probability-weighted estimate of future cash flows. It is a component of the carrying amount of the asset or liability for a group of insurance contracts. This is commonly referred to as the 'best estimate liability' or BEL.
Risk adjustment for non-financial risk	RA	The risk adjustment for non-financial risk is the compensation an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk as the entity fulfils the insurance contracts.
Contractual Service Margin	CSM	A component of the carrying amount of the asset or liability for a group of insurance contracts representing the unearned profit the entity will recognise as it provides insurance contract services under the insurance (or reinsurance) contracts in the group. The CSM is determined for groups of contracts and recognised in profit or loss when services are provided to the policyholders in that group.

IFRS 17 GLOSSARY (Continued)

Term	Abbreviation	Description
Loss component	LC	A negative CSM is not permitted for insurance contracts – where this is applicable for a group of insurance contracts, a nil CSM is included for measurement and an LC is recognised immediately as an expense in the income statement.
General Measurement Model	GMM	The GMM is the default measurement model under IFRS 17 and should be applied to any insurance contract, including reinsurance contract held, that is in the scope of IFRS 17 unless an entity chooses to apply the premium allocation approach for short duration contracts, or if the insurance contracts meet the eligibility criteria to apply the Variable Fee Approach.
Premium Allocation Approach	PAA	The PAA is a measurement model under IFRS 17 for (re)insurance contracts issued and reinsurance contracts held. It is considered a simplification of the GMM and is mainly relevant to short-duration insurance business, such as general insurance. One of the following criteria should be met before an entity can elect to apply the PAA: 1. the coverage period of each contract in the group of insurance contracts is one year or less; or 2. the entity reasonably expects that the PAA would produce a measurement of the LFRC for a group of insurance contracts that would not differ materially from the measurement that would be achieved by applying the GMM.
Variable Fee Approach	VFA	The VFA is a variation of the GMM and is relevant to savings business if certain criteria are met. These contracts provide substantial investment-related services with the entity promising an investment return based on the underlying items managed on behalf of the policyholder. The entity's share of the fair value returns on the underlying items is reflected in the CSM.

IFRS 17 GLOSSARY (Continued)

Term	Abbreviation	Description
Portfolio (related to level of aggregation of contracts)	n/a	Portfolios include insurance contracts with similar risks that are managed together. There is no explicit definition of “similar risks” or “managed together” in the IFRS 17 standard.
Cohort (related to level of aggregation of contracts)	n/a	IFRS 17 requires a portfolio of contracts to be divided into 'cohorts' based on inception date. A cohort may not include contracts issued more than one year apart.
Group (related to level of aggregation of contracts)	n/a	Portfolios and cohorts of insurance contracts need to be further disaggregated into the following groups based on the contracts’ expected profitability at initial recognition: 1. Onerous contracts; 2. Profitable contracts with no significant probability of becoming onerous; 3. Remaining contracts, i.e. profitable contracts with a significant probability of becoming onerous.

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