



COMPANY NAME: ASSUPOL HOLDINGS
SHARE CODE: - TRADES OTC VIA OTC EXPRESS-
PRICE: 510CPS
RECOMMENDATION: BUY BELOW R6

DESCRIPTION OF THE BUSINESS

Assupol is a financial services provider offering funeral, life, savings and retirement annuity products. The company's main business is Assupol Life which was established in 1913 and accounts for the bulk of the Group's profits. Assupol Life's client base is predominantly employed in the public sector, with a particularly strong presence in the South African Police Services (SAPS).

Assupol currently only trades on the OTC market via OTC Express. Anglorand Securities is a registered broker with OTC Express and is therefore entitled to trade Assupol shares listed on the platform on behalf of clients. (See Trading Assupol VIA OTC for further details).

BACKGROUND

In 2010 Assupol began demutualising the original structure with the process completed in February 2013. The demutualisation resulted in 228,263 policyholders redeeming shares while approximately 12,000 policyholders elected to retain their shares and become ordinary shareholders in the group. The funding of the R890mn redemptions was achieved by utilising R293mn of earnings retained from Assupol Holdings in the 2012 financial year, a R30mn investment by BEE company WDB Investment Holdings, a R300mn investment by Investec as well as a R132mn bridging loan facility from Investec. The banking arm of the World Bank, the International Finance Corporation, also invested R170mn. The shareholding at present is as follows.

- Investec 35%
- Management and staff 20%
- International Finance Corporation 20%
- WDB Investment Holdings 10%
- Free float 15%

RESULTS AND REVIEW FOR FINACIAL YEAR TO JUNE 2016

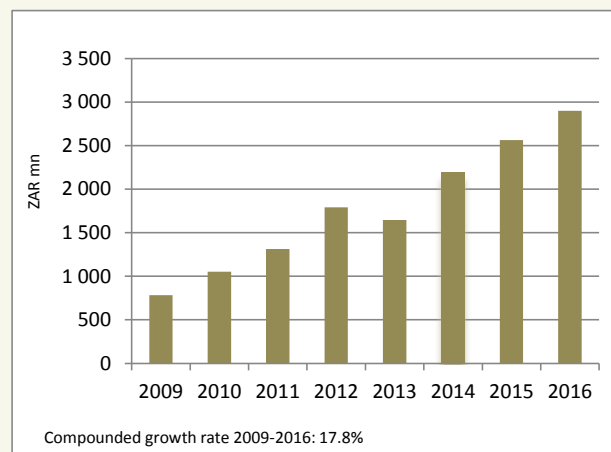
Gross premium revenue generated for the period increased by 20% to R2.44bn boosted by an expanded branch network and sales force. Adjusted operating profit (excluding the impact of changes in investment financial assets) increased by 19.3% to R466mn while the value of new business increased by 22% to R221mn. The group achieved

investment returns on total assets of just 3.7% (2015: 2.7%) for the year under review largely due to high volatility and the subpar performance of SA financial markets. Diluted EPS increased by 2.8% to R1.36 per share. A dividend of 53cps was declared during the year, down from 99cps in 2015. The decline in the dividend payment was a result of a drop in the special dividend paid, with 2015's 61cps far larger than the 13cps paid in 2016. The ordinary cash dividend component totaled 43cps up from 38cps in 2015.

Despite R305mn of dividends paid out in 2016, embedded value (EV) increased by 13.7% to R2.9bn or R7.07 per share. As a reminder, EV is an actuarial measure of the present value of all future profits expected to be earned from the existing policies that an insurance business has written, plus the value of the assets of the business. We also believe that it represents the best measure of intrinsic value for life insurers.

VALUATION

FIGURE 1: ASSUPOL EMBEDDED VALUE



Although facing economic headwinds over the last several years, Assupol management has consistently shown their ability to grow EV, with a CAGR 17.8% achieved over the last 8 years. In addition to successful strategy execution, we attribute this ability to grow EV to the fact that the majority of Assupol policy holders are employed in the public sector where employment is not as sensitive to downturns in the economic cycle.

Given this relatively sticky public sector policyholder base, coupled with increasing penetration into the non-government sector as well as new product offerings, management still sees significant growth opportunities.



With Assupol currently trading at a 28% discount to its current E, we believe that the company offers compelling value especially when one considers that the company is likely to exhibit further growth going forward. Further evidence of its attractive valuation is revealed when one compares Assupol to its closest JSE-listed peer, namely Clientele Life.

TABLE 1: ASSUPOL VS CLIENTELE LIFE

	Assupol	Clientele Life
Gross Premium Inc (R mn)	2448	1852
Net Profit (R mn)	472	415
P/EV	0.73	1.06
PE	3.75x	13.5x
ROE	21%	51%
DY (excl special div)	8.40%	6%
Market Cap (R mn)	2100	5600

As is evident from Table 1, Assupol's market capitalisation is 62% less than that of Clientele, this despite the company writing more premiums and generating higher operating profits. Clientele also trades at a significantly higher rating (higher PE and P/EV), and although it could be argued that this is justified due to its superior returns as well as due to the fact that it trades on the JSE, which is a far more liquid market, we feel that the rating differential is too wide. Given Assupol's history of growing EV at over 15% per annum and generating returns on equity (ROE) in excess of 20%, we believe that a 30% discount to EV is excessive. Although growth and returns appear to be more than acceptable we do however believe that a discount should exist due to the fact that Assupol currently only trades on the OTC market and as such have applied a 10% discount to our fair value price. Applying this discount would value Assupol at around 636cps, which represents a 25% premium to the current share price of 510cps.

RISKS

Although Assupol clients are primarily employed in the public sector where employment is generally more stable, the government employee target market will also come under pressure from an ongoing squeeze in rising living costs which is impacting disposable income.

Additionally, rising interest rates will negatively impact the discount rate used in calculating embedded value.

RECOMMENDATION

Overall, we believe that Assupol is a high quality business especially given its high penetration levels in the less volatile public sector space. Given this fairly unique position we feel that the company is likely to grow even in the face of economic headwinds, which coupled with the attractive valuation (as highlighted by the steep discount to current EV), should see Assupol deliver healthy returns with the added potential for significant unlock should the company decide to list on the JSE. As such we recommend that long term investors look to **buy Assupol at R6 per share or lower**

TRADING ASSUPOL SHARES VIA OTC

Assupol currently only trades via the OTC Express platform where investors must choose who they want to contact and engage with in independent bilateral negotiations. As opposed to placing orders via the normal bid offer system as is the case on the JSE, investors are required to place adverts to buy and adverts to sell with quantity only, so as not to constitute a bid or offer which would be a contravention of the current Financial Markets Act. Parties who trade on the platform now load a trade agreement on OTC Express on conclusion of an independently bilaterally negotiated transaction. Settlement is then automatically effected only after the parties to a concluded transaction have loaded a trade agreement on OTC Express and have both accepted the trade agreement. Clients who wish to trade Assupol should please email desmonde@anglorand.com.

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