



*Chairman's and  
Managing Director's Report*

## Insurance Market Overview

The short term insurance sector has delivered positive results in recent years, as it experienced favourable underwriting conditions. However, 2005 has seen a downturn in the insurance cycle as a result of softer market conditions and a return to a normalised claims trend. General market premium growth has been limited and insurers may soon be facing further pressure on rates as companies seek to increase market share.

Although South Africa has not been adversely affected by any major weather-related losses recently, our counterparts abroad have been severely impacted. The occurrence of natural disasters world wide, such as hurricanes, fires and floods have increased of late, both in severity and frequency, and this development will place the industry under enormous pressure. Whilst the true impact of global warming is not yet known, climatic change looms ever larger as a market concern following a second year of unparalleled hurricane losses with an even more severe season being forecast for 2006.

In light of the above the reinsurance market remains firm and rate increases are expected. Locally, there was evidence of customers containing reinsurance costs through higher retentions. In a globalised context the impact of international reinsurance losses has a significant influence locally and reinsurers will have to take this into consideration as they adapt their business models to meet the needs of a changing market.

The South African market has lately been characterised by a relatively low inflation and a low interest rate environment. This has resulted in strengthened property prices, increased vehicle sales and levels of disposable income. Any abnormal rise in inflation during the course of 2006 will impact interest rates and consequently could result in a depreciation of the rand which has the potential to significantly affect average claims settlement values.

2006 promises to be a challenging year for the industry. A year that will again require industry players to concentrate on maintaining a strict underwriting discipline, appropriate pricing and rigorous risk assessment in order to remain relevant and competitive.

## Group Results

Growth in premium revenue continued with an increase of 10% to R3,509.7 million (2004: R3,191.1 million - restated). Investment income increased by R114.4 million to R353.5 million (2004: R239.1 million - restated). The bond portfolio performed positively and the continued equity disposal programme resulted in realised gains of R172.9 million (2004: R70.1 million - restated).

An increase in the incidence of accidents and higher repair costs impacted the motor account and certain weather related events and a number of large fires impacted the fire account. Most other underwriting accounts performed satisfactorily during the period. However, we will continue to focus on rigorous risk assessment and appropriate corrective action going forward.

Whilst earnings per share increased by 24.2%, headline earnings per share, which excludes net realised gains on disposal of investments, have decreased to 1,933.4 cents per share (2004: 2,037.4 cents per share). The solvency margin has decreased to 52.9% (2004: 57.0%), after payment of the special dividend in March 2005. This remains above the stated



MC South  
Chairman



NV Beyers  
Managing Director

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policy of maintaining solvency in the 40% to 50% range. The Company remains financially sound and continues to enjoy an AA+ claims paying ability rating by Global Credit Rating.

In line with current dividend policy, the Directors declared a final dividend of 600 cents per share (2004: 470 cents per share) bringing the total dividend to 800 cents per share (2004: 650 cents per share).

### **Regulatory Developments**

Regulation has had a major impact on the insurance sector in South Africa. The Financial Advisory and Intermediary Services (FAIS) Act has necessitated a number of changes that impact insurers and brokers alike. The cost of compliance could be a potential barrier to entry for new brokers and existing brokers will have to re-examine the way they do business in order to integrate the regulatory framework into their business processes. It is expected that FAIS will ultimately result in the broker market undergoing major transformation and consolidation.

Heightened scrutiny of the insurance industry by public authorities and regulators following the Spitzer enquiry may impact the local market.

The Financial Sector Charter has resulted in financial services businesses, including the short term insurance industry, concentrating on ownership and empowerment issues and procurement. Although ownership issues were addressed, resulting in several equity transactions being concluded during the year, procurement poses challenges. Industries that serve short term insurers are themselves generally not empowered and this issue needs to be addressed. The insurance industry will need to collaborate and focus its efforts on empowering the supplier chain in order to meet the BEE targets.

### **BEE Transaction**

In April, SA Eagle announced that Royal Bafokeng Finance (RBF) had acquired a 10% interest in the Company from its Swiss parent the Zurich Financial Services Group. As part of the agreement, RBF were able to nominate one Director to the SA Eagle Board and the company has an option to increase its shareholding in line with the ownership requirements. Moreover, SA Eagle undertook to fund specific projects nominated by RBF in areas such as corporate social investment, enterprise development and empowerment financing, subject to approval by the Board.

### **Looking Forward - The Year Ahead**

As a result of the transformation of our business model SA Eagle has realised significant improvements over the last three to four years. Now we intend to consolidate these improvements into a strategic plan that will enable us to become a leading insurer.

In order to facilitate this process we interviewed a cross section of senior management and conducted a business excellence survey amongst all staff to test perception of our progress in a number of key areas. This research was used to plan the content of a strategic planning workshop that was held in the last quarter with a view to commence the planning process required to take the business forward enabling us to meet key operational objectives. Several workstreams have been identified as a priority.

This included reviewing our Sales and Marketing strategy by line of business as well as our personal lines and SMMEs strategy. We will be looking especially at opportunities that emerging markets provide for increased innovation and product development for both personal insurance as well as SMMEs. In this regard we will be collaborating closely with Royal Bafokeng Finance, our empowerment partner, to leverage opportunities to distribute low income insurance products within this community.

We also plan to strengthen our corporate customer business. This will require creating an organisational framework to develop and execute an agreed corporate business strategy ensuring effective value added service for corporate customers in line with Zurich's Global Corporate value proposition.

Operational excellence is of paramount importance as we strive to become a leading insurance company. To this end we will remain focused on continuous improvement across our processes and service levels. With the aim of achieving certain cost savings, we will develop a procurement strategy in line with the Financial Sector Charter. Claims leakage will continue to be vigilantly monitored. In this regard we hope to leverage benefits afforded to us by The Zurich Way – the Zurich Group's initiative to drive operational excellence and best practice across the Group, to the benefit of our customers.

Leading edge technology remains a critical driver of our business processes and we are in the process of upgrading our workflow capabilities. The policy administration and credit control applications have been completed and implemented and work has commenced on the claims system enhancements. We will also be embarking on an initiative to improve our data mining capability. This will include a focus on simulation and modelling tools, analytics and data integrity.

Planning for a more integrated people management approach has commenced. This will encompass the areas of leadership assessment, employee recruitment, job grading and remuneration, performance management and succession planning. Proactively managing our talent will be an important factor in our success.

Over the last two years we have established a clear commitment to operational excellence as a foundation for sustained profitability. Underwriting discipline will be a key

focus enabling us to deliver consistent operating results and shareholder returns. We aim to develop greater synergies within the context of the Zurich Group and benefit from global best practice. We will also continue to identify and prioritise opportunities for sustainable profitable growth as part of our aspiration to become a leading insurer.

### *Acknowledgements*

We would like to extend our thanks to employees for the effort they have made towards achieving another set of excellent results. We would also like to thank all our business partners and customers for their continued support and our Board for their ongoing guidance and advice.

During the year we bade farewell to Board Members Geoff Riddell, Jim Carter and Joe Pamensky. We would like to welcome Stuart Morris, Steve Phiri, Al Paas, Dennis Burton and Clifford Zungu as new members of our Board.

**Martin South**

*Chairman*

**Nick Beyers**

*Managing Director*