Discovery

Integrated ANNUAL REPORT 2013





MAKING PEOPLE HEALTHIER



Discovery was founded in 1992 by the current Group Chief Executive Officer, Adrian Gore, and Group Executive Director, Barry Swartzberg. The vision was to create a different business that would be guided by a clear core purpose – that of making people healthier and enhancing and protecting their lives.

Underpinning this core purpose was the belief that through innovation we could be a powerful market disruptor that could change the way insurance works. At the time, the South African environment provided a powerful incubator for innovation. South Africa's healthcare system was highly fragmented with double-digit healthcare inflation affecting the private sector. Discovery's approach was to offer innovative health and wellness solutions to address these challenges, and change the face of medical schemes in South Africa. Later in 2000, we entered the life assurance market – a highly commoditised industry – and added value through differentiation and structural change in how insurance products were designed.

Vitality, our science-based wellness programme, which is recognised as one of South Africa's leading innovations, is the pioneer in behavioural-based insurance – an insurance model that uses behavioural economics insights to understand and influence consumer behaviour. This unique capability enables us to structurally reduce the cost of insurance for our clients. Today, our business model is increasingly relevant and responsive in a world where the burden of chronic diseases of lifestyle is growing, healthcare costs are persistently increasing and risk-averse consumers are seeking greater certainty and protection.

Contents

Introduction

About this report 04
Our performance during the year 06
CEO's report – Adrian Gore 08
Q&A – Richard Farber, Discovery Financial Director 12

About Discovery

How our business works 14
Vitality: a global wellness innovator 16
Our medium-term strategic framework 18
Our stakeholders 20

We describe how our business model creates value for our stakeholders, according to our stated ambition and the issues that are material to our business and stakeholders.

Performance reviews 2013



Discovery Health

Key facts and performance highlights 24
Performance against key strategies 26
Our focus areas during 2013 and strategic priorities for 2014 28
Q&A: Dr Jonathan Broomberg, Discovery Health CEO 32
Case study: Improving quality of care through the Discovery Health Care Coordination Programme 35



Discovery Life

Key facts and performance highlights 36
Performance against key strategies 38
Our focus areas during 2013 and strategic priorities for 2014 40
Q&A: Herschel Mayers, Discovery Life CEO 42
Case study: Creating value through behavioural life insurance 44



Discovery Invest

Key facts and performance highlights 46
Performance against key strategies 48
Our focus areas during 2013 and strategic priorities for 2014 49
Case study: Using innovative products to maximise retirement savings 51



PruProtect

Key facts and performance highlights 82
Performance against key strategies 84
Our focus areas during 2013 and strategic priorities for 2014 86



The Vitality Group

Key facts and performance highlights 88
Performance against key strategies 90
Our focus areas during 2013 and strategic priorities for 2014 91
Case study: Vitality recognised at the World Economic Forum 93
Discovery opinion: Derek Yach, Head of the Vitality Institute 94



Ping An Health

Key facts and performance highlights 96
Performance against key strategies 98
Our focus areas during 2013 and strategic priorities for 2014 99
Case study: The increasing burden of chronic disease in China 100
Case study: Ping An Health's operating model is based on the Discovery Health integrated model 101

Corporate Governance

Discovery Limited Board of Directors 118
Corporate Governance Committees and Secretary 122
Corporate Governance report 123
Enterprise Risk Management report 128
Group Compliance report 131
Remuneration report 133

Annual Financial Statements

Our annual financial results for the financial year 138
Embedded value statement and additional information 266



Discovery Vitality

Key facts and performance highlights 52
Performance against key strategies 54
Our focus areas during 2013 and strategic priorities for 2014 56
Q&A: Gidon Novick, Discovery Vitality CEO 60
Case study: Furthering public debate about health promotion and wellness issues impacting our society 62



Discovery Insure

Key facts and performance highlights 64
Performance against key strategies 66
Our focus areas during 2013 and strategic priorities for 2014 68
Q&A: Anton Ossip, Discovery Insure CEO 70
Case study: Fewer accidents and lower claims cost for Discovery Insure 72
Case study: Telematics – the insurance industry game changer 73



PruHealth

Key facts and performance highlights 74
Performance against key strategies 76
Our focus areas during 2013 and strategic priorities for 2014 77
Case study: Britain's Healthiest Company 80



Discovery People

Key facts and performance highlights 102
Our focus areas during 2013 and strategic priorities for 2014 105



Discovery's socio-economic impact

Key facts and performance highlights 108
Our focus areas during 2013 and strategic priorities for 2014 111
Discovery opinion: Dr Ayanda Ntsaluba, Discovery Limited Executive Director 113

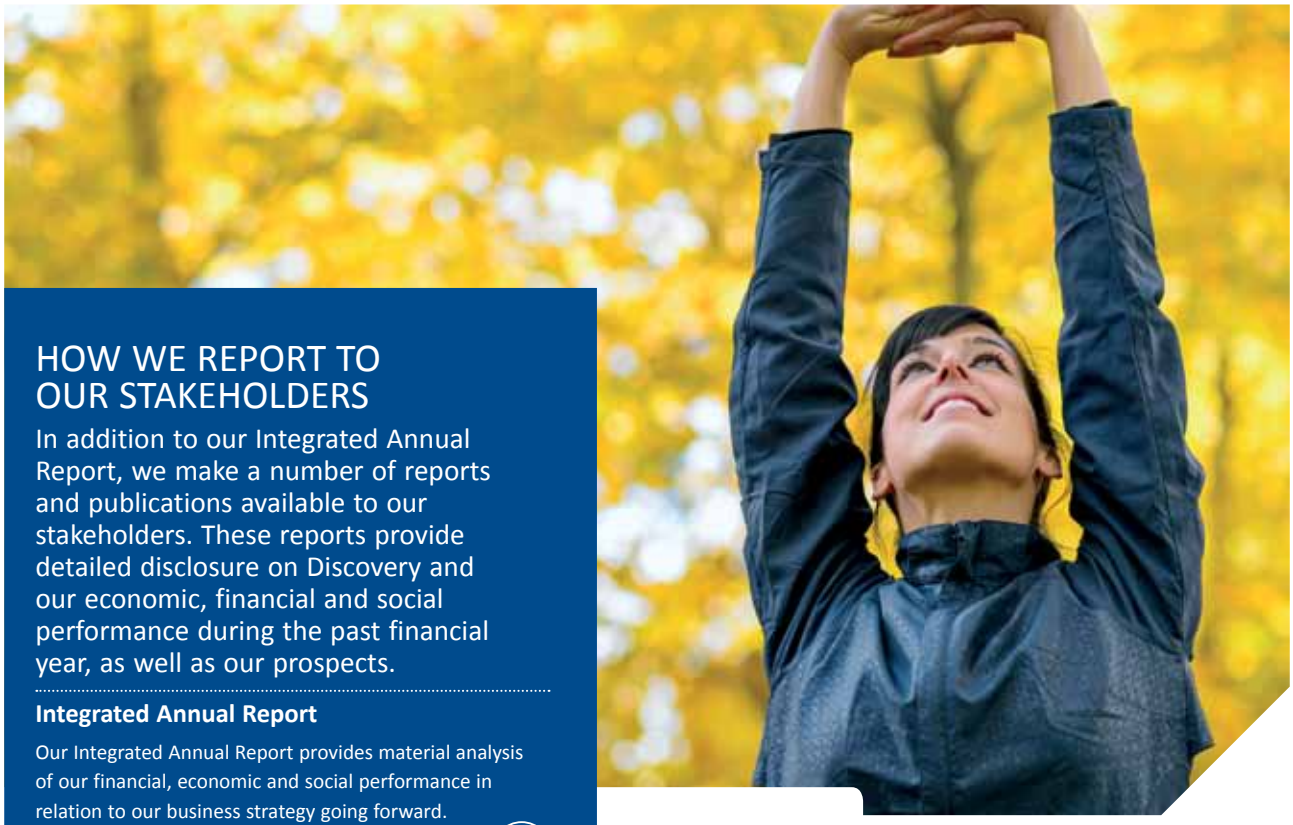
Discovery Opinion

Who is best placed to reduce the long-term impact of non-communicable diseases 94

Discovery Opinion

Calling for a multi-sector compact 113

ABOUT THIS REPORT



HOW WE REPORT TO OUR STAKEHOLDERS

In addition to our Integrated Annual Report, we make a number of reports and publications available to our stakeholders. These reports provide detailed disclosure on Discovery and our economic, financial and social performance during the past financial year, as well as our prospects.

Integrated Annual Report

Our Integrated Annual Report provides material analysis of our financial, economic and social performance in relation to our business strategy going forward.

Available online at www.discovery.co.za/info/annualreport

Annual Financial Results Presentation

A presentation of Discovery's annual financial results to investors.

Available online at www.discovery.co.za/info/annualresults

Summarised Annual Financial Statements

Presents summarised financials and administration requirements (AGM notice, proxy form).

Available online at www.discovery.co.za/info/summarisedfinancials

Sustainable Development Report

An overview of Discovery's performance according to our Framework for Sustainable Development.

Available online at www.discovery.co.za/info/sustainabledevelopment

Discovery's 2013 Integrated Annual Report covers the financial year period from 1 July 2012 to 30 June 2013, and is our primary report to our stakeholders.

This is our third integrated annual report. It provides an overview of our business model and strategy to achieve our stated ambition, as well as an integrated view of the past year's performance as it relates to the financial, economic and social factors that impact our business. It also addresses our expectations for growth and performance in the year ahead.

We aim to confine our report to the material issues that impact on our business and our stakeholders. Materiality is determined according to our business objectives, strategy, the important stakeholders we engage with and the macro-trends in our operating environment.

This report covers the operations of Discovery Limited, including Discovery Health, Discovery Life, Discovery Invest, Discovery Vitality, Discovery Insure, PruHealth, PruProtect, The Vitality Group and Ping An Health. All data reported on relates to the past financial year, unless otherwise indicated.

YOUR COMMENTS

We value feedback and comments from our stakeholders on our Integrated Annual Report, as well as our other publications. Please send your comments to **askthecfo@discovery.co.za**

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Approval by the Discovery Board of Directors

The Discovery Board of Directors approved the 2013 Discovery Integrated Annual Report on 30 September 2013, based on the recommendation of the Discovery Audit and Risk Committee.

Signed by the Chairperson of the Discovery Board of Directors

Monty Hilkowitz

Statement from the Discovery Social and Ethics committee

The Social and Ethics Committee assists the Board in meeting its responsibilities for social investment, transformation, ethics management and sustainable development within Discovery.

The committee has reviewed and provided input into this year's Integrated Annual Report as well as the Sustainable Development Report and is satisfied that our reporting provides an accurate and integrated view of Discovery's performance during the past financial year, and its prospects.

Signed by the Chairperson of the Social and Ethics Committee

Sindi Zilwa

Preparation of Discovery's Annual Financial Statements

The Annual Financial Statements for the year ended 30 June 2013 were prepared by B Mill FFA, FASSA; L Capon CA(SA); and L van Jaarsveldt CA(SA). The preparation of the statements was supervised by R Farber, CA(SA), FCMA and was audited by PricewaterhouseCoopers Inc.

Global Reporting Initiative (GRI)

Our information is reported in accordance with the Global Reporting Initiative's guidelines for sustainability reporting, which are available at www.globalreporting.org.

We declare a GRI application level B+ for the Discovery 2013 Integrated Annual Report and Sustainable Development Report. We received third-party verification from Indeybo Incorporated of this application level.

View our Global Reporting Initiative Index in our 2013 Sustainable Development Report.

View Indyebo Incorporated's statement in our 2013 Sustainable Development Report.

Statement from Discovery Group Internal Audit

Discovery Group Internal Audit performed a limited review of the statements and quantitative data contained in the Discovery 2013 Integrated Annual Report, with the exception of the Annual Financial Statements.

Based on the results of our work performed, in our opinion, the report:

- Provides confidence in the information presented. The level of data accuracy was found to be within acceptable limits. Additional improvements were recommended to Discovery management to reduce the potential for minor anomalies and misstatements, which were subsequently amended. Data trails selected were easily identifiable and traceable, and the persons responsible were able to reliably demonstrate the origin(s) and interpretation of data.
- The report appropriately reflects the environmental, social and economic performance achieved during the period.
- The report represents a fair statement of Discovery's sustainability initiatives.
- The report contains quantitative data which is free from material misstatement.

Overall, Group Internal Audit is satisfied that the report is an appropriate representation of the relevant aspects during the reporting period, based on the audit procedures applied during this review.

OUR PERFORMANCE DURING THE YEAR

Normalised headline earnings

↑ 20% to R2.8 billion

Embedded value now over **R35.7 billion,** with return on embedded **value exceeding 20%**

Global Vitality membership base in five countries reached 5.5 million

New business API

↑ 15% to R10.8 billion

Excellent actuarial dynamics across the business with **positive trends in lapses and loss ratios**

Vitality Institute launched in the US to advance debate and thought leadership on wellness and health promotion

R18 155 666 committed to medical specialist training and clinical research projects in South Africa through the Discovery Foundation

R11 million committed to support public and primary healthcare organisations in South Africa through the Discovery Fund



Normalised return on capital of
21.5%,
13%
above the risk-free rate

21% improvement
in driver behaviour
for Vitalitydrive clients within
12 months of joining

Normalised cash generated from operations **up 45%** to over **R2 billion**

12%
of operating profit invested in new initiatives

Discovery Foundation MGH Fellowship Award launched

in partnership with Massachusetts General Hospital in Boston US, enabling South African healthcare professionals to conduct cutting-edge medical research



CEO'S REPORT

Adrian Gore

Group Chief Executive Officer
Discovery Limited

The period under review has been a highly successful one for Discovery, with strong performance across all our businesses.

A key feature of the past year has been the continued investment in Discovery's business model to ensure that it is scalable and repeatable in different markets globally. Our business model, which is built on the use of behavioural science underpinning insurance systems, is unique and disruptive, and more importantly, highly relevant in a world where three global megatrends are rapidly coalescing and impacting social security and financial systems.

Chronic diseases of lifestyle can, and will, be modified

One of the most important societal trends emerging is the relevance of wellness and lifestyle choices, and the global realisation that these have a major impact on mortality, morbidity and healthcare costs. This is being fueled by a less optimistic view of the power of curative care, the implications of ageing populations and the view that non-communicable diseases are now more relevant than communicable diseases. Research from the Oxford Health Alliance – the 3-4-50 model – reveals that three poor human behaviours (smoking, poor nutrition, lack of exercise), lead to four diseases (cancer, diabetes, lung and heart diseases), resulting in over 50% of deaths worldwide. Concurrently, not only is the burden of mortality attributable to the increase in non-communicable diseases, people are living longer in poorer health. In this regard, the science of behavioural economics is highly relevant in understanding the individual behaviour leading to lifestyle diseases and offers insight as to why people frequently make choices that are inconsistent with their long-term welfare. Individuals are unaware of their health risks, over-optimistic about their health status and they generally discount the value of a healthy lifestyle. Given the unique behavioural dynamics of lifestyle choices, encouragement and the use of incentives are increasingly being seen as acceptable and effective policy responses. This is in contrast to legislation and regulation, which may infringe on individual freedom.

The increased cost of healthcare will remain a challenge

The negative impact of poor wellness and lifestyle choices on governments and healthcare funders worldwide is particularly severe given the stubborn increase in healthcare costs globally – a function of scarce skills and the emergence of new and expensive medical technology. Industries that depend heavily on scarce skills (for example, doctors in the healthcare industry) do not benefit from cost-efficiencies gained through the introduction of new technologies. This characteristic – termed the Baumol effect – explains why the healthcare industry experiences cost inflation far higher than Consumer Price Inflation.

New business API

15% to R10.8 billion

Normalised headline earnings

20% to R2.8 billion

with 12% of earnings invested in new initiatives

The insurance industry is receptive to innovation

The combination of global shifts in power and the financial crisis has created an environment in which consumers have less faith in financial markets and where they seek greater certainty. The intense focus on, and innovation in, investment products over the last two decades, has left the protection industry relatively static and commoditised, and competition is based almost entirely on price. Concurrently, the financial crisis has given rise to increased capital requirements, leading to a potential erosion of margins. Innovation and the ability to manage and price risk more accurately are crucial for relevance and profit. Despite this, underwriting practices have evolved very little, remaining focused on selection and pricing factors at inception. This is despite the fact that risk flexes over the life of the policyholder. This risk can also be influenced at will by the policyholder, based on the lifestyle choices they make.

Discovery's business model is resilient and responsive to these global trends

Brilliant and disruptive insurance businesses are built on top of the Vitality behavioural chassis, resulting in a distinct competitive advantage. In health insurance, integration incentivises healthier behaviour and reduces healthcare costs, and in life insurance, it introduces dynamic rating factors through wellness behaviour. These factors enable consumers to extract better value from their protection policy and improve actuarial dynamics for the insurer.

This unique wellness-integrated insurance model is scalable – with applicability in short-term insurance as seen with Discovery Insure, and repeatable – with manifestations in the US, UK, China and recently Singapore, with the launch of AIA Vitality. Ultimately, across all social security systems, integration aligns our interests with that of our members: we both benefit from better member behaviour.

The dynamics of the business model and strong performance from the individual businesses manifested in high growth in new business and earnings as well as excellent loss ratios and lapse level trends across the portfolio.

The established businesses of Discovery Health, Discovery Life and Discovery Vitality and the emerging businesses of PruProtect, PruHealth and Discovery Invest, increased earnings by 15% and 54% respectively. In addition, 12% of earnings was invested in building out the new businesses of Discovery Insure, The Vitality Group, Ping An Health and AIA Vitality.

Observations on Discovery's performance during the financial year

New business API: Up 15% to R10.8 billion, improving on Discovery's 10-year average Annual Premium Income

Earnings: Normalised headline earnings up 20% to R2.8 billion with 12% of earnings invested in new initiatives

Cash: Normalised cash generated from operations up 45% to over R2 billion

Return on capital: Normalised returns of 21.5%, 13% above the risk-free rate set internally

Quality of business: Excellent actuarial dynamics – with positive trends in lapse rates and loss ratios

Embedded value: Embedded value of over R35.7 billion with return on embedded value exceeding 20%

Market position: Market leadership and industry recognition

Social impact: Positive impact of Vitality in encouraging wellness, evident globally

In reviewing the individual business performance, the following are notable:

Discovery Vitality

Vitality forms the fundamental underpinning of the Discovery business model and this was strengthened over the period, with membership growing to 5.5 million lives in five markets. Given the structure's ability to change member behaviour – and the evidence from Discovery's base of engagement leading to significantly lower hospital admission rates, healthcare costs, and levels of dread disease and mortality – investment was made into the science, scale and infrastructure of Vitality. This enabled the success of the existing businesses and supports continued expansion, such as with the AIA joint venture in South East Asia – as the ability to incentivise healthier behaviour and dynamically price risk in life insurance becomes even more powerful.

In addition, progress was made in globalising the Vitality capabilities, such as the HealthyFood benefit structure, which was extended to Woolworths in South Africa, and rolled out to Walmart in the US and Cold Storage in Singapore. The period was also significant with the launch of the Vitality Institute in the US and the Vitality Advisory Board in the UK – with a mandate to strengthen the science of disease prevention and health promotion to further secure Vitality as the thought leader in the rapidly-growing wellness industry.

Discovery Health

Discovery Health performed excellently during the year under review. Across all metrics – new business, lives under management, operating surplus, and lapses – Discovery Health and Discovery Health Medical Scheme (DHMS) performed above expectation. New business API increased by 13% to R4 820 million and operating profit increased by 13% to R1 688 million. The Scheme also showed excellent financial strength, ending the 2012 calendar year with a strong surplus of R789 million and total reserves of R8.2 billion. A key development during the period was an independent review of DHMS's governance and operating model, as well as the value generated by Discovery Health as the administrator of the Scheme. The independent review, conducted by Deloitte Consulting, validated the value delivered by Discovery Health and ranked DHMS as the best-performing scheme among all its benchmarked peers.

Discovery Health has become the dominant player in the medical scheme market with a 52% share of the open scheme market and unrivalled brand recognition and awareness among consumers. The recent Sunday Times Top Brands survey ranked Discovery Health as the top brand with no reference to alternative brands. From Discovery Health's perspective, this highlights the vast social responsibility we have to contribute to the private healthcare system in South Africa. In this regard, Discovery Health's vision is to ensure that the medical schemes under its management offer the broadest and best benefit choices, at the lowest cost per unit of benefit, inside a healthcare system that is seamless, accessible and excellently-serviced. During the period, Discovery Health continued to deliver on this vision, with work done on every aspect of the business; to control healthcare costs, enhance scheme benefits, digitise the Discovery Health ecosystem, and strengthen the long-term sustainability of the schemes under management.

In addition, the business must also exist within a broader sustainable healthcare system for all South Africans. In our view, collaboration is required from all stakeholders to ensure its sustainability. The Discovery Foundation continued to address the shortage of specialist skills with an R18 million commitment in medical training grants and fellowships. I am also excited about a partnership with one of the leading teaching hospitals in the US, the Massachusetts General Hospital, that will afford South African academic specialists the opportunity to conduct groundbreaking research. In addition to this, we recently launched a set of new Foundation awards recognising excellence and innovation among private-sector doctors.

Discovery Life

Discovery Life made excellent progress during the year: new business API increased by 8%, further strengthening our position as the number-one writer of risk business in the broker market. Mortality and morbidity experience continued to improve and lapses were down from 11.2% in 2012 to 10.1% in 2013. This resulted in an increase of 16% in operating profit, while a stronger cash position allowed for further investment into the business.

Since its launch in 2001, Discovery Life's business model has evolved from separating risk from investment products to dynamic underwriting and now, to behavioural life insurance, which enables more accurate underwriting and more value for consumers. For Discovery Life, the model is highly successful in the sense that the more consumers engage with Vitality, the healthier they get and the less they claim; while at the same time the higher a client's Vitality status, the better benefits and incentives become – a value aspect that encourages customers to remain with us.

Importantly, we are increasingly coming to understand why members lapse their policies. These insights are critical for our product and benefit design as it allows us to target incentives at the optimal level to ensure both engagement in Vitality – resulting in better mortality and morbidity experience for Discovery Life – and customer retention. To this end, we enhanced the PayBack Benefit during the year to give clients more immediate rewards. We also introduced an integration product with Vitalitydrive that gives clients additional opportunity to lower their premium through better driving behaviour.

Discovery Invest

During the year under review, we made progress in achieving greater scale in the Invest business. Our assets under management increased to R30 billion, up 20% from the previous year and a strong indicator of the market's receptivity to Discovery Invest's approach. We launched Discovery Invest on the premise that the business would offer investors the same Linked Investment Service Provider (LISP) offering, combined with the open architecture platform that is available in the South African investment market, but with the additional value of benefit integration and unique protection. The result is a product range based on a unique efficiency that is made possible by integrating Discovery Life and Discovery Invest products. An example of this product design is the Discovery retirement Optimiser, the only retirement product in the South African market that converts unused life cover at retirement age into additional retirement savings. During the year, we worked to enhance the benefit for consumers – making it simpler to understand and introducing a benefit that allows clients to use their Life PayBacks to boost their retirement savings. The market responded very positively to the product offering, resulting in increased new business and profitability from this product.

PruHealth and PruProtect

Our vision for the UK is to build the best protection business with clear market leadership in both the Private Medical Insurance (PMI) and protection markets. Achieving scale has therefore been imperative for Discovery and we are extremely pleased with the way in which the combined business is progressing. The performance has been exceptional with the business today mirroring the Discovery Health and Discovery Life model in South Africa. Over the period, operating profit grew by 57% to R472 million; new business API grew by 48% to R1 573 million; and the customer base measured around 710 000 lives at the end of June 2013.

In PruHealth, the focus has been on further advancing operational efficiencies in terms of the service platform, as well as ensuring quality across all performance metrics: increasing new business, and managing loss ratios as well as lapse levels. The PMI market in the UK is highly sensitive to economic cycles and working alongside the National Health System, requires PMI providers to deliver unique benefits and high levels of

protection to consumers. PruHealth's strategy has been, firstly, to offer higher levels of cover and secondly, to address the value-gap perception in the market through Vitality. To this end, we focused on creating higher market awareness of the Vitality offering with UK sporting personalities, Sir Sebastian Coe and Jonny Wilkinson joining Jessica Ennis as Vitality Ambassadors. The response from the market was immediate: the average calls from individuals interested in a PruHealth policy increased from an average 40 in the first quarter of 2013 to over 130 in the second quarter. In addition, we also launched the Vitality Advisory Board in the UK, which is aimed at bolstering the scientific capability and application of Vitality in the UK market.

PruProtect posted a remarkable performance, taking into account that the business was built organically since its launch in 2007. The work done over the past number of years in building out the quality of the business in terms of claims experience and lapse rates is now resulting in an excellent operating and financial performance. This is evident from the 40% growth in policies in force, 40% increase in new business API and a 56% improvement in operating profit during the reporting period. The excellent levels in new business were supported by a continued investment in building out our Franchise Channel, with 18 franchises now operational across the UK. In terms of sales by channel, this segment increased their production by 33%, accounting for 72% of total sales. Our focus now turns to evolving the PruProtect model into a robust integration model, with the first Vitality-integrated protection product launched in the UK in September this year.

AIA Vitality

Earlier in July, we launched an exciting joint venture in Singapore with one of pan-Asia's most prominent insurance groups, AIA Group. The joint venture is a manifestation of Discovery's ability to apply the Vitality offering in a life insurance environment, and to transform a traditional insurance model into a behavioural life assurance model. We are very excited to be partnering with AIA – a highly credible partner with an extensive distribution footprint and tremendous brand equity.

The joint venture will see the Vitality product made available to all AIA Singapore clients with a life insurance product, with dynamic underwriting principles being applied to create more value for consumers. The Vitality programme mirrors its South African counterpart, reflecting the work done during the year to ensure the philosophy and efficacy of Vitality remains standard. In Singapore, we have contracted with quality partners such as Cold Storage, a leading retailer, Air Asia as well as Emirates and adidas.

Discovery Insure

Discovery Insure had an exceptional year with strong progress across all performance metrics – a continuous increase in new business API (up 53%) and improvements in lapse rates and loss ratios. We estimate that Discovery Insure has captured 10% of the personal lines market, only two years since its launch. The market continues to respond well to the product with Discovery Insure being ranked the second-most recognised short-term insurance brand in the 2013 Sunday Times Top Brands survey, despite our spend on advertising being one of the lowest in the market. More encouraging, however, is how people are responding to incentives and how quickly they adapt their driver behaviour. Our data shows that there is a 21% improvement in driver behaviour, from the lowest level to the highest status level, as tracked through a status-level system, within 12 months of joining Discovery Insure. The ability to improve driver behaviour through Vitalitydrive, positively influences the claims experience in Discovery Insure. Clients on the higher driver status have a 34% less chance of claiming and the severity of their claims decreases by 19%. The early results of the model have therefore been very encouraging.

A key strategy for us has been to differentiate Discovery Insure based on innovative product design that delivers more value and protection to consumers. Traditionally, short-term insurance products have been focused on distribution – insurers would either compete in the direct-to-consumer market on price, or in the high-advice broker market. Discovery Insure competes in both distribution channels, but with the emphasis on a differentiated product with potential for integration with other Discovery businesses. During the year under review, we continued to focus on building out Insure's product range with several benefit enhancements, as well as its unique protection capability made possible through telematics technology.

Ping An Health

The private health insurance market is only starting to emerge in China and its potential is significant. While total healthcare expenditure per person is significantly lower in China compared to the US, UK and South Africa, the percentage spend on private expenditure continues to rise. More relevant for insurers competing in this space is the percentage out-of-pocket expenditure (37%) where current insurance options in the market are not providing adequate cover. Against this background, Ping An Health made good progress over the period, with a deliberate refocus of its strategy away from the Fund and Service base, and towards mid-end and high-end insurance products. These markets, while embryonic, are growing rapidly and total approximately RMB 1 billion of premium income – of which Ping An Health has captured in the region of 30%. Insurance business was characterised by strong new business growth levels over the period (up 58%, excluding Ping An employees) and a low loss ratio in line with expectation. Ping An Health sustained its position as the number one writer of new business in the Group high-end market. Importantly, the individual market remains the key growth opportunity for the business, and the integrated health insurance and Vitality offering will powerfully position Ping An Health to capture this potential.

Concluding thoughts

A key factor in our success has been the contribution of Discovery's more than 8 000 employees. At Discovery, we have a deep and unequivocal belief that talented employees, liberated to do their best and achieve their potential, are what makes and keeps our business successful. In the context of Discovery's expanding global footprint and our goal to become the world's best insurance organisation, innovation is essential; and to achieve sustained innovation, it is necessary to attract and retain the best talent.

Apart from the indisputable business benefits of a talented workforce, it is personally fulfilling to work with so many inventive, capable and driven individuals. I thank each member of the Discovery team for their individual contributions in making the past year as successful as it has been, and I look forward to continue building Discovery with this remarkable team.

Q&A: Richard Farber, Financial Director, Discovery Limited



Q&A

Richard Farber

Financial Director, Discovery Limited

Describe the past year's performance.

We are extremely pleased with this set of financial results. We've made good progress across all metrics and all the businesses are well positioned for future growth in their respective industries. The UK business continues to go from strength to strength and profitability levels are very good. Discovery Life also delivered good results with low lapse rates and increased new business volumes.

What were the highlights and disappointments?

Specific highlights include the launch of our joint venture (JV) with AIA Group in Singapore. This JV is particularly exciting for us as it shows the relevance of the Vitality model to insurance – not only in health insurance but also in life insurance. We've been working on this JV for over two years and the challenge is now to build a business of scale in the Singapore market. Another important milestone for us was the 25% acquisition of the Hollard stake in Discovery Insure. Having full ownership of the Insure business makes it possible for us to create more innovative and integrated products with other Discovery products. We recently launched the first Discovery Insure-Discovery Life integrated product and we're excited to explore more opportunities in this area. A disappointment to some extent has been the relatively slow rate of growth of Ping An Health into the mid-level individual market. We have always made it clear that due to the nature of this market segment, Ping An Health will take some time to gain traction. Having said that, we have put a lot of work into developing a quality product for this market and we have now launched Vitality as well. I am optimistic about the potential of the private health insurance market in China.

How do you see the material issues that may potentially impact the sustainability of Discovery?

There are a number of broad issues that will not only have a long-term impact on the success of Discovery, but also our clients and economy. Rising healthcare costs remain a critical challenge in South Africa as well as globally. It has a huge knock-on effect for businesses and a country's economy at large. Related to this is the increasing burden of chronic diseases of lifestyle and its impact on quality of life, productivity and healthcare costs. The government's recently-published Strategic Plan for the Prevention and Control of Non-communicable diseases estimates that around 50% of all deaths in South Africa are caused by non-communicable diseases. This is expected to increase unless the problem is addressed.

Economic cycles in the sense of a recessionary environment, are a risk for all insurers. The rate of policy lapses closely follows difficult economic conditions and so it is important to design products that are relevant and meet people's needs. Products must offer protection and value to clients.

A third material issue is regulatory developments which impacts on how we do business. Current regulatory developments include the National Health Insurance system in the healthcare sector and the Solvency Assessment and Management Framework in the long- and short-term insurance sectors.

Lastly, an immediate material issue for Discovery specifically is our international expansion and how we implement our strategy. The Vitality model is proving to be highly pertinent in addressing high insurance costs. The challenge for us is to ensure the model is relevant for each target market and that it is scalable and repeatable. Linked to this is the issue of people capacity. The business is growing rapidly and we need to ensure that we have enough talent and skills to meet business needs. Discovery has built a very unique culture over the years; an aspect that is very important for our ability to innovate. The challenge is to ensure that our unique culture, values and drive to innovate are transferred internationally.

Was it part of your strategy to purchase the Hollard stake, just two years after the launch of the company? In terms of this acquisition, did you pay a fair price?

The original shareholding structure for Discovery Insure involved the possibility of purchasing the 25% Hollard stake. Although we have agreed to the acquisition earlier than anticipated, we view the future growth prospects of Discovery Insure as very positive.

"Discovery produced a strong set of financial results during the past financial year." Richard Farber, Financial Director of Discovery Limited, explains the key aspects of our performance and reflects on key challenges for the Group.

The acquisition will allow us to realise the full benefits of this growth. We have agreed to acquire the shareholding at a premium to the invested capital. The premium takes into account the excellent progress made by Discovery Insure and the future growth prospects of the business, as well as recent capital investments made by Hollard in the business. The transaction is currently pending regulatory approval.

Discovery is following an aggressive growth strategy; specifically in terms of its international growth. How do you foresee the financial implications of this strategy, especially in diverse markets such as Asia?

Our international expansion strategy is a low capital-intensive strategy. We team up with excellent partners who are market leaders in their respective industries. Partners such as Ping An in China, AIA Group in Singapore, Humana Inc in the US and Prudential in the UK, all bring major scale, distribution expertise and brand equity to the partnerships. In turn, we provide intellectual expertise and product innovation.

Discovery at times receives criticism for the extent of its investment in the Discovery Life business. What is the reason for this?

We have been criticised that we are too aggressive in our reinvestment in developing new business for Discovery Life. Our view, however, is that Discovery Life offers products that are valuable for our clients and provide suitable returns for our shareholders, and our strategy is to invest in growing the business. The Life business delivered strong results during the past financial year with new products and benefits launched, good new business growth and importantly, low lapse levels. The quality of the business is very good, so we are satisfied that we are following the correct strategy for Discovery Life.

You mentioned the new Solvency Assessment and Management Framework. What are the implications of this legislative development for Discovery?

The proposed Solvency Assessment and Management Framework (SAM) addresses three areas (termed "pillars"). Firstly, it proposes a new risk-based methodology for the calculation of required capital. Secondly, it introduces a number of new requirements on how insurance companies and groups are governed and manage risk. Finally, it includes an array of new disclosure requirements – both to the regulator and to the wider public.

Based on our own internal research, combined with participation in the South African Financial Services Board's quantitative impact studies, we expect to meet the new solvency standard with our current capital resources and with relatively little practical impact from the first pillar – statutory capital requirements. South Africa already has a risk-based capital requirement, and while the calculation is quite different, we believe we are adequately capitalised under both our current requirements and the SAM proposal. We reached a similar conclusion for the PruHealth business in the UK, based on the current statutory requirements and the expected transition to Solvency II and SAM. The biggest impact of SAM will be the second pillar – governance and risk management processes. While we believe that the Group is already well governed and the risks adequately managed and reported, additional processes and documentation will be required under SAM. Additionally, we will need to quantify a number of items which we have been addressing qualitatively up to now. A fair amount of this work will be required under the Insurance Laws Amendment Bill, which we anticipate to come into effect in 2014. We are currently preparing for this. While the third pillar will require an element of additional disclosure, much of which is still to be finalised, I am confident that we will put in place processes to provide for this in line with the statutory requirement once it is clarified.

At the time of your annual results announcement in September, you released a cautionary trading update about the expected performance. The market reacted negatively to this trading update and your share price took a knock – what was the reason for the market reaction?

Prudential has a put-option on the 25% shareholding in the JV with Discovery, meaning that they can sell their shareholding to Discovery in future. Accounting requirements make it mandatory for a company to account for this and raise a liability in their statements. Following the UK businesses' excellent performance, we were required to re-evaluate Prudential's 25% shareholding. We also recaptured a portion of the outstanding reinsurance balance in PruHealth, resulting in a five-year interest saving of R52 million. These accounting transactions impacted the earnings per share, and the market misunderstood our trading update as an indication of poor underlying business performance. These transactions are not representative of the underlying performance of the business and we exclude them from our normalised operating results. The market has subsequently understood our position.

HOW OUR BUSINESS WORKS

WHAT DRIVES US

OUR CORE PURPOSE
To make people healthier and enhance and protect their lives

Where we are heading
Our **ambition** is to be the **best insurance** organisation in the world and a powerful force for social good

WHAT WE DO
We offer products that span the personal financial needs spectrum

Discovery Health | Discovery Life | Discovery Invest | Discovery Insure | Discovery Vitality
the vitality GROUP | PRUHEALTH | PRUPROTECT | 中国平安 PINGAN | AIA Vitality

Vitality

Vitality: a world-class behavioural science platform

Vitality is a comprehensive wellness solution that helps our clients become healthier by giving them the tools, personalised wellness programmes and motivation to improve their health. We have clinically proven that Vitality members who actively use the programme live longer and have lower healthcare costs than non-Vitality members.

In our business, Vitality creates significant value in the following areas:

Wellness catalyst: consumers actively improve their health

Reduces the cost of insurance: positive impact on healthcare costs and mortality and morbidity experience in life insurance

Big data analytics capability: a wealth of wellness, credit card and health data enables a big data analytics advantage and insight into understanding how clients respond to incentives

Dynamic underwriting: allows for dynamic risk assessment and more accurate risk pricing for individual clients

Product integration: enables consumers to gain more value from efficiencies as products are integrated

What makes us different to our competitors

We design innovative insurance products that use insights from behavioural economics and our capability in analysing big data to drive positive behavioural change. This impacts risk and the cost of insurance positively and creates sustained shared value for all stakeholders.

OUR VALUE DRIVERS

We develop best-of-breed products that offer more value and efficiency through product integration, resulting in higher levels of new business.	**We retain clients through high-quality products and additional health value gained through Vitality.**	**A sophisticated and robust risk management model enables us to better manage risk.**
New business API up 15% to R10.8 billion	Low levels of lapses across the business **Increased engagement levels in Vitality**	Claims experience is **within expectation across the business**

A pioneering market leader with **uniquely positioned businesses**

ORGANICALLY-GROWN BUSINESSES

Healthcare cover



Discovery Health

Largest open medical scheme in South Africa

Life insurance



Discovery Life

Largest pure risk writer in South Africa in the intermediary market

Long-term savings and investments



Discovery Invest

Number one writer of **endowment and voluntary purchase annuities** in South Africa

Short-term insurance



Discovery Insure

Attracted 10% of new business written in the personal lines insurance market in South Africa

Wellness solution



Discovery Vitality

Membership in South Africa close to **1.7 million**

JOINT VENTURES

Wellness solution



THE vitality GROUP

Recognised as a **best-in-class wellness solution** provider in the US

Healthcare cover



PRUHEALTH

Top four Private Medical Insurance provider in the UK

Life insurance



PRUPROTECT

Top four risk provider in the UK Independent Financial Adviser channel

Healthcare cover



中国平安 PING AN

Number one in the group high-end insurance market in China

Wellness-based life insurance



AIA Vitality

Launched in **Singapore** in July 2013

Performance highlights

8 220
employees

7 million
clients worldwide

Normalised headline earnings of
R2 787 million

Embedded value of
R35.72 billion

VITALITY: A GLOBAL WELLNESS INNOVATOR

Vitality is Discovery's internationally-recognised, science-based wellness programme.

Built on the principles of behavioural economics, the programme encourages positive, sustained behaviour change by offering individuals a combination of knowledge tools, access to wellness partners and financial incentives that increases proportionally as they engage with the programme. Initially developed in response to a growing wellness trend – a trend that is highly relevant today in light of the major global challenge to economic and social progress that non-communicable diseases pose – Vitality has evolved into an innovative business model that is changing the way insurance works.

THE CHALLENGE

A growing social and economic problem: chronic non-communicable diseases

Chronic non-communicable diseases such as cardiovascular disease, diabetes, lung diseases and some cancers are the greatest global causes of death and disability, accounting for more than 50% of deaths worldwide. The number of deaths from these diseases is double the number of deaths that result from nutritional deficiencies, infectious diseases such as HIV and AIDS, tuberculosis and malaria, as well as maternal and perinatal conditions. Three preventable lifestyle behaviours – physical inactivity, poor nutrition and smoking – lead to an increased risk of getting a chronic illness. Pre-emptive measures to address these lifestyle behaviours can significantly reduce the impact of such illnesses.

THE INSIGHT

Behavioural insight: the healthcare-wellness paradox

A paradox exists in how people view the value of healthcare with its immediate results, and wellness where the value of preventive measures is only realised in the future. While the long-term benefits of wellness and preventive care are well-documented and known, sustained wellness behaviour is difficult to encourage. A lack of information, over-optimism about health status and the fact that the benefit of wellness and preventive care are only realised later in life, are all factors leading to an under-consumption of preventive care.

For Vitality, understanding this aspect of human behaviour is important in how we design incentives to encourage healthy behaviour.

THE Vitality SOLUTION

Groundbreaking techniques to encourage healthy lifestyle modification

Vitality was designed to engage individuals in the management and improvement of their health through the use of incentives. At the heart of the programme lies Vitality's innovative approach that:

1| Offers members access to a network of health and wellness providers, which not only lowers the burden of access and cost to members, but also provides data linkage for Vitality to measure and verify health behaviour and engagement

2| Customises a wellness solution based on an individual's risk factors

3| Rewards engagement in activities to maintain and improve health through a broad reward set that addresses different behavioural motivators.

The Vitality programme integrates health behaviour and covers the complete healthcare spectrum – ranging from lifestyle modification and preventive care to disease management. Key to the programme is its simplicity – it is not difficult to engage with. Moreover, it is personalised for individuals to ensure it is appropriate for and relevant to all members, regardless of their health status.

The results

Evidence for the efficacy of the Vitality programme – in terms of improved clinical outcomes, reduced healthcare costs, increased productivity at work and improved mortality rates – has been profiled in numerous academic journals. The programme has also gained international recognition in leading publications such as The New York Times, The Economist, and Harvard Business Review, as an innovative health and wellness promotion methodology.

EVIDENCE THAT VITALITY WORKS

in changing behaviour

Vitality published the results of its first research projects in 2008 when we revealed the positive outcomes of three preliminary studies conducted to determine the efficacy of Vitality in improving members' health and reducing healthcare costs.

Vitality has since grown, both locally and internationally, with the programme offered in the UK, US, China and recently, Singapore. The success of the programme is largely due to its efficacy. Research has shown that simple, accessible and inexpensive lifestyle interventions that address tobacco use, unhealthy diet, physical inactivity and excessive alcohol intake, are the most effective in dealing with the growing burden of chronic diseases of lifestyle.

Over the years, Vitality has incorporated evidence-based interventions drawn from a diverse range of disciplines, including medicine, dietetics, sports science, psychology, behavioural economics and epidemiology, into benefits and incentives to address each of these unhealthy behaviours.

CHANGING THE WAY INSURANCE WORKS

Integrating Vitality with insurance products

Insurers traditionally use the following rating factors to access and underwrite risk: age, gender, socio-economic status as well as smoker status and medical history. These risk factors are mostly static and provide a limited view of a person's risk. A person's health behaviour, however, provides a more accurate risk indication.

Vitality, with its 16 years of wellness data and its comprehensive understanding of wellness behaviour, adds an additional dynamic rating factor. It takes into account the impact of chronic diseases and lifestyle factors, such as smoking, level of exercise, diet, alcohol consumption, blood pressure and cholesterol on a person's risk profile.

By integrating Vitality with insurance products, we have developed a scientific and dynamic underwriting model that uses high-quality data about a person's health, wellness, credit card spend and driving behaviour to assess their risk more accurately over time. This results in:

- **Better benefits**
- **Lower and more accurate risk pricing**
- **Better selection**
- **Lower lapse rates**
- **Better mortality and morbidity experience.**

VITALITY RECOGNISED INTERNATIONALLY

- The development of groundbreaking techniques to encourage healthy lifestyle modification and ongoing research support has propelled Vitality to the forefront of **innovative global healthcare**. The model is being successfully replicated in the UK, the US, China and Singapore. Vitality now impacts the lives of over five million people globally.
- Discovery is now acknowledged as a **global thought leader** in the use of behavioural economics and incentive-based wellness.
- Vitality has attracted **international recognition** and has been the subject of much press coverage. Over the past few years, it has received coverage in the Wall Street Journal, The New York Times and The Economist in the US; The Guardian, The Telegraph, Financial Times of London and BBC News in the UK; and Folha de Sao Paolo in Brazil.
- In the US, The Vitality Group received recognition as the **best corporate wellness provider** from broker houses AON-Hewitt and Mercer.
- Most recently, in a report released by the **Workplace Wellness Alliance at the World Economic Forum** held in January 2013 in Davos, Switzerland, Vitality was acknowledged as a global case study on wellness and a gold standard for incentivising healthy behaviour and outcomes.

OUR MEDIUM-TERM STRATEGIC FRAMEWORK

OUR AMBITION

Our ambition is to be the best insurance organisation in the world and a powerful force for social good.

We must be known for our excellence, financial strength and innovation

In addition, we must be a powerful force for social good – whether through the way we do business, the products and services we deliver or through the impact our business has on the broader society.

To achieve our ambition we use our unique business model to make a tangible difference in people's lives. By using powerful financial and behavioural structures that meet people's needs in sustainable ways, we are able to provide superior returns for shareholders.

Our strategic priorities

We measure our success against the following strategic priorities:

People

Recognition as an employer of choice for all critical skills with excellent levels of employee satisfaction and retention

Our performance during the past year

The Discovery Graduate Programme, which targets IT and actuarial skills, has been extended to include pharmaceutical and marketing skills. During the past year, we **hired 17 graduates through the Graduate Programme,** across the Discovery business.

At the time of writing the report, we had initiated the Adrian Gore Fellowship Awards, a three-year fellowship programme aimed at actuarial students. The programme was launched at four South African universities.

Return on capital

Group-wide return on capital of risk-free + 10% over the long-term

Our performance during the past year

Normalised return on capital of 21.5%, 13% above the risk-free rate.

Earnings

CPI + 10% sustainable growth in operating earnings

Our performance during the past year

Normalised headline earnings up **20% to R2.8 billion.**

Our social footprint

Regarded by all stakeholders as a force for social good

Our performance during the past year

Vitality recognised globally as **a solution to the growing burden of chronic diseases of lifestyle.**

Continued investment in training specialists for South Africa's public healthcare sector through the Discovery Foundation.

Discovery as a force for social good



Dr Mergan Naidoo is an obstetrician and lecturer in Family Medicine at the University of KwaZulu-Natal in South Africa. He received a grant from the Discovery Foundation to complete a PhD on ways to improve obstetrical surgical safety in public hospitals in KwaZulu-Natal.

Discovery's core purpose and ambition extends further than our immediate clients or our financial performance.

We are acutely aware of the escalating complexity of a globalised world; and the increasingly connective role business can and must play in society. Along with important macro-trends that impact society, such as the rise of chronic diseases of lifestyle and its impact on society as well as difficult economic circumstances globally, the relationship between business and society has changed. Businesses must not only navigate social change successfully, but must also contribute to building the stability necessary for a thriving society. For Discovery it is equally important to have a positive impact on society and to be a force for social good – not only through the products and services we offer, but also in our engagement with people and the social partnerships and collaborations we build to benefit society as a whole.

We provide more information about our performance as it relates to sustainable development in our Sustainable Development Report, which is available at www.discovery.co.za/info/sustainabledevelopment

Our stakeholders

Discovery impacts the lives of over **seven million clients**, over **8 000 employees** and many more stakeholders in the **industries, communities** and **countries** in which we operate.

We understand that the continued growth and success of our business is fundamentally linked to understanding and addressing our stakeholders' concerns, needs and insights. The method and frequency with which we interact with our stakeholders and how we conduct our business are key aspects of Discovery's long-term sustainability strategy.

Our engagement with stakeholders centres on the following principles:

- Honesty and integrity
- Inclusivity and responsiveness
- Transparency and accountability
- Complete, timely, relevant, accurate and accessible information.

We manage our stakeholder engagement through:

- Proactive management and regular communication
- Our stakeholder engagement framework and guidelines
- The Board's governing role in the monitoring of our stakeholder engagement.

Discovery delivers value to our stakeholders through constant innovation aimed at creating more value and protection for consumers. For this reason, we have a product launch every year in each business, ensuring a disciplined focus on creating value for our customers.

We also investigate and appropriately respond to material stakeholder concerns, the most significant of which are detailed below.

Stakeholder group	Key concerns during the year	Our approach and response
Our employees	**To understand the level of employee engagement in our business, Discovery runs the Towers Watson engagement survey on a bi-annual basis.** **While the 2012 survey (which had a participation rate of 74%) showed that the company performed extremely well when compared to the South African norm, it also highlighted a few employee concerns as areas for improvement, namely:** • **Some employees were unsure whether there would be follow-through on the survey results.** • **A few employees believe that management style does not always encourage employees to give their best.** • **There is also some concern over personal wellbeing.**	Based on the results of the survey, we have and will continue to address these concerns in the following ways: • We analysed the results by division and provided feedback on the results and actions to all employees on platforms such as departmental meetings, performance conversations, the Discovery intranet and employee newsletters. Further actions include implementing an online tracking mechanism with quarterly updates from managers on employees' progress against commitments. • Survey feedback has been rolled out across all businesses and support was given to the various business units in running focus groups with employees and managers to co-create solutions and further reinforce leadership excellence. Survey results will also be fed into the broader leadership development strategy which will serve to support leaders in the delivery of business objectives. • We have renewed our focus on strategic leadership development within our Leadership Charter and company values as well as on developing potential long-term career paths. Various members of management have been enrolled in leadership training sessions to give them insight into their personal management styles and equip them with tools to increase their awareness and efficacy in their roles. • Discovery continues to encourage wellbeing activities to promote a healthy work/life balance, support financial wellbeing by catering for financial advisers for employees as well as lifestyle partners.

Stakeholder group	Key concerns during the year	Our approach and response
Our clients	**Whether Discovery Health Medical Scheme (DHMS) is well-governed and well-managed and whether DHMS members receive value for money from the administration fees paid to Discovery Health** **Whether Discovery Health and DHMS offers value-for-money healthcare benefits**	• To ensure best practice governance, DHMS' governance model is subject to periodic review. DHMS commissioned Deloitte to perform an independent governance and performance review, the results of which were communicated at the 2013 Scheme annual general meeting. The Deloitte Report documented the following findings: a) DHMS is led by a strong, competent and independent Board with no governance failures; b) DHMS outperforms all benchmarked schemes in the Deloitte Performance Model and c) DHMS members obtain significant value-for-money for the administration fees paid to Discovery Health. • The findings of the Deloitte Report were also distributed through press releases and newsletters as well as posted on the Discovery website. • Discovery is dedicated to investigating every single consumer query or complaint brought to us in a timely and satisfactory manner. Cases are always reviewed by the appropriate business unit. We engage with our members during this process to resolve any further queries or outstanding issues.
Healthcare professionals	**Fair reimbursement** **The quality of care in the private healthcare system** **The overwhelming shortage of skilled healthcare workers and medical specialists in the country** **The impact of administrative requirements of their patients and medical schemes, on their practices**	Discovery Health has, over the past year, advanced its work on alternative models of reimbursement, particularly ones that include a shift away from fee-for-service towards risk-sharing payment systems that better align incentives for efficiency and quality of care. Discovery Health is engaged in various active interventions on supply-side cost drivers, as well as changes in reimbursement methods in order to reduce cost and increase the quality of care. We have been developing integrated healthcare teams, better integration between health professionals and hospitals, and better coordination and sharing of vital clinical information across the healthcare system. We are working with healthcare professionals on various targeted initiatives to improve healthcare quality, such as the Paediatric Governance Project, our Senior Care Coordination Programme, and the Best Care Always Programme. There is much engagement around issues of sustainability in the industry and projects to strengthen the healthcare system: • The Discovery Foundation invested over R18 million during the reporting period to help train healthcare specialists in South Africa. • The MGH Fellowship Award, a new award category in the Discovery Foundation Awards, was launched in May 2013. The award is intended to fund an established South African healthcare academic to either undergo specialist training or take part in ground-breaking research in their chosen medical field at the Massachusetts General Hospital, one of the leading academic hospitals in the USA.

OUR STAKEHOLDERS continued

Stakeholder group	Key concerns during the year	Our approach and response
Regulators and governments	**The imbalance of resources, particularly those in healthcare, between the public and private sectors** **A desire for universal healthcare coverage for all citizens** **Rising healthcare costs in the private healthcare sector** **The need for a more rigorous solvency framework in insurance** **A review of commission structures for investment and insurance products in South Africa**	Discovery Health continued to provide leadership in the launch of the Social Compact with the Department of Health. The compact is an initiative aimed at bridging the divide between the public and private sector. Participating private-sector health companies, which so far includes 23 leading representatives from the pharmaceutical, hospital, pharmacy and medical scheme industries, have pledged a fixed annual contribution to ensure the delivery of various healthcare initiatives. In 2013 alone, the partnership committed R40 million to prioritising key projects, in addition to the work individual companies continue to do as part of their Corporate Social Investment (CSI) programmes. In terms of the National Health Insurance (NHI) system for South Africa, we are working with the government in one of the NHI pilot districts, in which we are sharing our software assets and experience to develop better information systems for public hospitals. Discovery strongly supports the Competition Inquiry into the South African healthcare system, which seeks to investigate means of managing rising costs by reviewing components of the healthcare system for wastage, inefficiencies and other potential drivers of healthcare costs. Discovery will collaborate fully with the Inquiry. Discovery is actively participating in various working groups and initiatives focused on the development of the Regulatory Frameworks around Solvency both in South Africa and the UK. In South Africa, we are also involved in work initiated by the Financial Services Board and the South African insurance industry that aims to improve the risk-based supervisory regime for the regulation of long-term and short-term insurers. We have also established internal working groups to discuss relevant technical papers and proposals, both in South Africa and the UK. During the year, the Financial Services Board continued the review of broker remuneration in the South African financial services environment. This is mainly focused on investment and insurance products and the commission structured and payments around these products. We provided our input and views to the regulator when information was requested at the onset of their review. We will participate in any projects around the development of the regulatory framework and its implementation.
Financial advisers	**Whether they are offering the best products, services and financial advice, so as to retain and grow their client base**	To equip financial advisers with the knowledge and skills they require to provide comprehensive, appropriate financial advice to their clients (and through the quality of their services, grow their client base). Discovery supports them proactively and extensively in the following ways: • Information by means of the Discovery Insights Series • Invitations to product launches • Provision of supporting marketing material and tools • Ongoing communication through electronic newsletters and website articles • The use of the Intermediary Advisory Forum • Training material and support, as well as financial adviser roadshows • Continuous Professional Development days that form part of quarterly training • Recognition of high performers in Discovery's proprietary distribution channels. Discovery's support for financial advisers has been consistently recognised by the Financial Intermediaries Association (FIA), with Discovery Health, for example, being voted as South Africa's Product Supplier of the Year in the 'Healthcare' category for six consecutive years. Together with Discovery Life winning the top award in the "Long-term insurance" category and Discovery Invest in the "Investment products" category this year, 2013 marks the first year ever in which a single company won FIA awards in three separate categories. A survey conducted among AON-Hewitt's brokers in the US revealed that Vitality is considered the wellness provider that provides the best wellness services in the US.

Stakeholder group	Key concerns during the year	Our approach and response
Investors and analysts	**Understanding Discovery's long-term growth strategy and the company's short-term financial outlook, so as to support more informed decision-making on their part**	Discovery acknowledges the importance of more clarity in explaining our strategy and business model to investors and analysts to assist them in gaining an accurate and realistic view of the company's strategy. To keep investors up to speed, Discovery's investor relations team attends international conferences and holds one-on-one meetings with institutional investors and sell-side analysts after results announcements, and periodically during the year.
The media	**Investigating newsworthy, publishable stories that are accurate and informative** **Consumer advocacy and the fair treatment of members** **Specialised training and recognition in the niche segment of healthcare journalism**	Information in the finance and healthcare sector is often specialised and complex. Discovery therefore makes a significant amount of quality content available to journalists to assist them in producing quality media stories. We ensure that material we supply is intelligently written, beneficial to readers, and importantly – always reviewed by the relevant company CEO to ensure transparency, consistency and accuracy. The media has constant access to spokespeople through our media relations team. Being available for comment is a priority. We also hold regular engagements with the media, including editor forums and round-table discussions as well as media meetings with the Discovery leadership team. Discovery demonstrates our commitment to raising the overall standard of health reporting and journalism in the country through training and the proactive approach in engaging with health journalists. Excellent health reporting is a crucial public service and Discovery believes in the integrity of well-researched and balanced articles. As such, we host the annual Discovery Health Journalism Awards, which aim to recognise excellence in healthcare reporting and also encourage journalists to raise the standard of healthcare reporting in South Africa. The Discovery Centre for Health Journalism (DCHJ), a partnership by Discovery Health and Rhodes University School of Journalism and Media Studies, enables in-depth studies in health journalism within the school's Honours Degree (one-year) and the new Masters (two-year) specialisations in Health Journalism. Discovery Health also hosts one or two Health Summits each year, at which we present key healthcare trends and information to health journalists.
Community and public healthcare organisations (PHOs)	**Globally, governments, NGOs and corporates are starting to realise the huge negative impact of chronic diseases of lifestyle on society.** **Primary healthcare organisations that typically rely on donor funding, are concerned about the sustainability of their projects.** **Discovery Foundation recipients, especially past recipients, wish for increased engagement with the Discovery Foundation.**	Discovery's business model positions it strongly as a key contributor to address the global challenge of non-communicable diseases. Earlier this year, we launched The Vitality Institute in the US to encourage debate around health promotion and policy in the US. Having identified fundamental skills required for the ongoing success and viability of non-governmental organisations, Discovery continuously offers support in training and development of key individuals and representatives of the primary healthcare organisations we support through the Discovery Fund. These workshops aim to improve their knowledge and skills in areas such as communication, report-writing, basic IT skills, administration and corporate governance. This empowers them to manage their projects well and thus increases their likelihood of sustaining themselves. While we conduct mid-term evaluations of the Discovery Foundation, manage Discovery Foundation roadshows at universities and host the Foundation Awards, Discovery Foundation recipients have communicated a desire for ongoing engagement with us. Discovery is currently investigating different ways in which we can best provide consistent and continuous support to our recipients.



DISCOVERY HEALTH

Our vision

To be an organisation that makes people healthier; offering them the broadest and best benefit choices at the lowest cost per unit of benefit in a healthcare system that is seamless, accessible and brilliantly serviced and that operates within a broader sustainable healthcare system for all South Africans.

New business API up **13%** to
R4 820 million

Normalised operating profit for Discovery Health up **13%** to
R1 688 million

Total medical scheme membership for all schemes under management **increased by 6%**

Key facts about Discovery Health

Administers Discovery Health Medical Scheme, the **largest open medical scheme in South Africa, and 12 closed schemes.**

Number of lives covered
(including DHMS and all closed schemes under management) at 30 June 2013:
2 792 236.

Market share:
31% of total medical scheme market.

More than
50 000
hospital admissions authorised every month, covering 96.9% of hospital costs in full.

35 300
calls handled in Discovery Health's call centre every working day and 80% of queries resolved during the first call.

Key facts about Discovery Health Medical Scheme

R789 million
net surplus earned
for the year at 31 December 2012.

2 517 000
lives covered
at 30 June 2013;
52%
of the open medical scheme market.

6%
average increase in principal members.

4.1%
annualised lapse rate
at 31 December 2012.

R8.2 billion
in reserves
at 31 December 2012.

AA+
credit rating from international credit rating agency, Global Credit Rating.

DHMS pays
R35 billion
in healthcare expenses annually.

PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

DISCOVERY HEALTH

Discovery Health's performance during the past financial year exceeded expectation. New business increased by 13% to R4 820 million and the number of lives covered increased to over 2.7 million. DHMS continued to build on its excellent financial strength – ending the year with a strong surplus of R789 million and total reserves of R8.2 billion.

Key strategy for 2013

Ensure that Discovery Health Medical Scheme (DHMS) and other medical schemes under our management **continue on a healthy growth path, as well as a strong financial trajectory.**

Our progress

- DHMS contribution increases for 2013 were set to maintain and enhance the value proposition of the Scheme while ensuring its long-term sustainability.
- **Contributions are on average 15% cheaper for a family of four across all plan types, compared with similar plans in the open medical scheme industry.**
- 6% year-on-year growth in the number of principal members.
- R8.2 billion in reserves, which is equal to 41% of all open medical scheme reserves.
- Lowest lapse rate in the industry of 4.1%.

Key strategy for 2013

Empower and enrich our members through education and tools to navigate the healthcare system and improve their quality of care.

Our progress

- **Launch of a series of educational and information videos for members, addressing various aspects of the Discovery Health Plans. These are available on the Discovery smartphone app, YouTube or through the Discovery website.**
- We developed procedure information guides that advise members what to expect when they go to hospital for a surgical procedure. These are also available on the Discovery app, YouTube or through the Discovery website.

Key strategy for 2013

Use our health analytic assets to improve the quality of care and eliminate inefficiencies in the healthcare system, ensuring that scheme members obtain the richest benefits at the lowest premiums in the market.
Health analytics refer to the use of data and analysis to understand issues that impact the cost and quality of healthcare.

Our progress

- Positive impact of the Discovery Health Coordinated Care Programme:
  - 2 200 members
  - Average age 68 years
  - Engagement with 13 facilities
  - Three home nursing companies
  - R30 000 saving a year for every member enrolled on the programme.
- **Discovery Health Renal Care programme, providing care for 1 065 members on Chronic Renal Dialysis and increasing both quality of care and efficiency.**
- Discovery Senior Care Coordination Programme aims to improve the quality of life for seniors by minimising avoidable hospital admissions. A pilot of the programme has been launched in Johannesburg with 54 members enrolled. Elements of the programme include outpatient management, extensive evaluation and management of common geriatric syndromes associated with an increased risk of hospitalisation as opposed to single disease management; in-home assessment, and validation of screening tools for accuracy of identifying individuals at risk for hospitalisation.
- Savings attributed to forensics and fraud management: estimated at R250 million for 2012.

DHMS contributions are on average **15% cheaper** compared with similar plans in the open schemes market

Two new health plans introduced for **2013**

Discovery Health is one of the signatories to the industry **Social Compact**

Key strategy for 2013

Leverage our scale and the latest mobile technologies to change the way our clients, doctors and financial advisers experience the healthcare system.

Our progress

- Launch of the Discovery app for Discovery Health members.
- **Rollout of telemetry-enabled glucometer and associated smartphone app for members with diabetes, which helps members and their treating doctors manage the condition immediately and more effectively.**
- Launch of SmartAdvisor app for financial advisers.
- Further enhancements to HealthID application for doctors to access Discovery Health members' health records.

Key strategy for 2013

Continuous innovation in benefit design to ensure the broadest benefit choices and provide access to the latest medical technologies for those with the greatest clinical needs.

Our progress

- Two new plans were introduced for the 2013 benefit year:
  - **Classic Comprehensive Zero – a new health plan that offers the same security as the Classic Comprehensive plan for in-hospital treatment and chronic medicine, but with the flexibility of funding day-to-day expenses without a Medical Savings Account (MSA).**
  - KeyCare Access – a new, very low-cost entry point for lower-income earners that provides cover in the healthcare areas members value most: private GP visits, emergencies and accidental trauma, childbirth and cover for newborns and certain elective procedures in a network of private hospitals.

Key strategy for 2013

Strengthen the Discovery Health brand through continuous, **proactive and positive engagement with all stakeholders.**

Our progress

- Discovery Health, together with other private-sector stakeholders, is one of the key signatories to the Social Compact for the healthcare industry established by the Minister of Health in November 2012.
- **Engagement with the National Department of Health and Council for Medical Schemes on the use of high-cost drugs, including private-sector pricing, international price benchmarking, pharmaco-economics, bargaining council funding strategies, access to state pricing, risk-sharing models and implications for Prescribed Minimum Benefits.**
- Discovery Health continues to provide support and expertise in improving public-sector pilot sites for the NHI rollout.
- Engagement with approximately 90 pharmaceutical companies to reduce the single-exit price of over 1 200 products for scheme members.
- **Continuous engagement with all health professional groups to ensure cooperation and alignment, resulting in improvements in the cost and quality of healthcare.**
- Discovery Health brought together 43 leaders of GP and specialist societies and associations at the annual Discovery Health Thought Leadership Summit. The aim of the summit is to debate future trends and strategies to ensure a sustainable private healthcare system.

OUR FOCUS AREAS DURING 2013

DISCOVERY HEALTH

Our focus areas during 2013

During the year, we continued to deliver on our vision; with work being done on every aspect of the business to control healthcare costs, enhance scheme benefits, digitise the Discovery Health ecosystem and strengthen the long-term sustainability of all the schemes under our management.

FOCUS AREA 1

Ensure strong financial performance and sustainability of Discovery Health Medical Scheme (DHMS) and restricted schemes under management.

A number of factors impact a medical scheme's financial performance and long-term sustainability, and these must be balanced to ensure continued growth and sustainability.

Contribution increases

Reflect effective management of a scheme and its competitiveness.

DHMS's contribution increases have been 15% lower than its competitors over the past five years.

Medical scheme pricing

The surplus year-on-year reflects contribution levels that are in line with expected membership and claims experience.

DHMS continues to produce a consistent, healthy surplus. During 2012, the net surplus was R789 million.

Growth

Continuous growth improves the risk profile of a scheme due to new joiners typically being younger than existing scheme members. It also reflects the competitiveness of a scheme and the attractiveness of its products.

DHMS has had positive membership growth since inception. Over the past 12 months, the Scheme grew by 6% (growth in principal members).

Average age of membership base

The average age of a scheme is a primary indicator of the risk pool. For every year's increase in the average age, contributions must increase by between 1.5% and 3% to absorb higher claims costs.

The average age of DHMS members is 32 compared with the industry average of 35.7. Since 2009, the average age of members has increased by 4.8 months, while the rest of the open medical scheme market has aged by 21.6 months.

Membership size

Larger schemes have a more stable risk pool, resulting in more predictable claims experience and accuracy in pricing.

- DHMS covers over 2.5 million lives and has a 51% share of the open medical scheme market.
- The Scheme continues to show significant growth relative to competitors: 220 000 lives were added in 2011 and 2012 compared with 100 000 members lost by the next 11 largest open medical schemes over the same period.

Absolute reserves

This demonstrates the Scheme's ability to meet large, unexpected claims as well as variations in expected claims experience.

- DHMS outperformed all benchmarked peers in the Deloitte Medical Scheme Performance Model.
- During 2012, Discovery Health Medical Scheme added more funds to its reserves than the next nine largest schemes combined. In December 2012, reserves were at R8.2 billion.
- DHMS solvency plan expected to increase statutory reserve levels to 25% by 2015.

Plan movements

Indicate product satisfaction, stability in benefit design and appropriate pricing.

In 2012, 93.7% of DHMS members remained on the same plan with only 3.1% downgrading or upgrading to a higher plan.

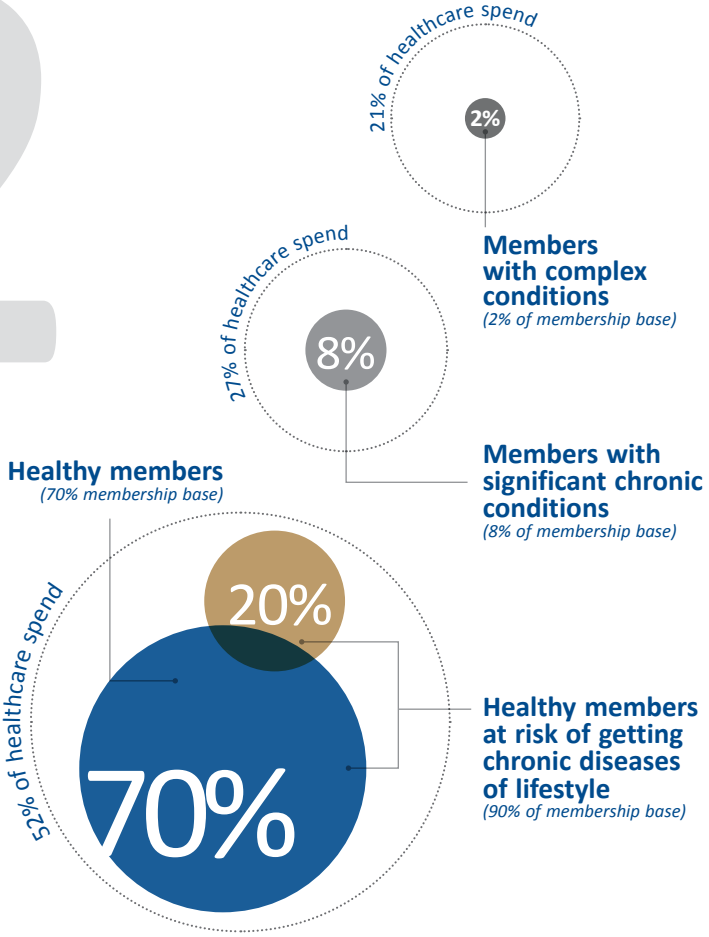
FOCUS AREA

Make members healthier.

A strategic approach to managing the population risk in a medical scheme is essential to proactively manage and reduce healthcare costs. A medical scheme population can be segmented into four sub-populations with varying degrees of healthcare risk and associated claims expenses:

- Members with complex conditions – 2% of the membership base, accounting for 21% of healthcare spend
- Members with significant chronic conditions – 8% of the membership base, accounting for 27% of healthcare spend
- Healthy members at risk of getting chronic diseases of lifestyle – 20% of the membership base, accounting for 52% of healthcare spend with the next sub-group of healthy members
- **Healthy members – 70% of the membership base, accounting for 52% of healthcare spend with the previous group who are healthy but at risk of developing a chronic condition.**

Various targeted initiatives to help improve health and reduce costs in each population segment have been implemented, thereby managing claims risk. The Vitality programme, to which over 65% of DHMS members belong, forms an integral part of Discovery Health's approach to making members healthier.



Read more about Vitality as a global wellness innovator on page 16 of this report, and our Vitality Performance Review on page 52).

FOCUS AREA

Ensure richest benefits for scheme members across a wide spectrum of plan choices.

A wide range of plan choices means that consumers are able to choose a plan that meets their needs. At the same time, engaging with healthcare providers in payment arrangements and provider networks improves a scheme's benefit coverage, and limits co-payments by scheme members. Discovery Health has invested considerably in developing network assets that ensure high levels of coverage and enables us to reduce scheme costs, as well as reduce member co-payments. Our most important network assets are the pharmacy networks, KeyCare and Delta hospital networks, the GP network and the KeyCare GP network, as well as three different specialist Direct Payment Arrangements. These networks and payment arrangements cover approximately 90% of all DHMS members' consultations and procedures by specialists and GPs. Our data indicates that the Discovery Health Direct Payment arrangements result in annual savings to members of approximately R1 billion in reduced co-payments and assisted the Scheme in meeting its obligations to fund Prescribed Minimum Benefit treatments in full.

DISCOVERY HEALTH

FOCUS AREA

Ensure the lowest cost and best value in the industry

Discovery Health has demonstrated the ability to manage cost inflation more effectively than industry competitors. This is as a result of superior price and contract negotiation with hospitals and other health service providers, superior claims risk and actuarial management, as well as the impact of Vitality on the health of members.

DHMS funds over R35 billion of healthcare expenditure, including R14.2 billion paid to GPs and specialists; and R10.9 billion to hospitals. Due to the size and scale of DHMS, the network assets developed by Discovery Health and Discovery Health's risk management expertise, schemes managed by DHMS are able to purchase healthcare at significantly lower costs per member than other schemes. In the case of DHMS, we estimate that healthcare costs are approximately 19% lower than other open medical schemes, on a benefit-adjusted basis. This results in significantly lower annual premium increases for DHMS and other schemes managed by Discovery Health. Over the past five years, annual premium increases for DHMS have averaged 3.30% above Consumer Price Inflation (CPI) – the lowest among all other open medical schemes.

In addition, the administration and managed care fees charged by Discovery Health to DHMS have been reducing in real terms as the Scheme has grown, resulting in a 5.5% (27% in nominal terms) real reduction between 2008 and 2012.

Since then, administration fees have reduced further, and will continue to do so as DHMS continues to grow.

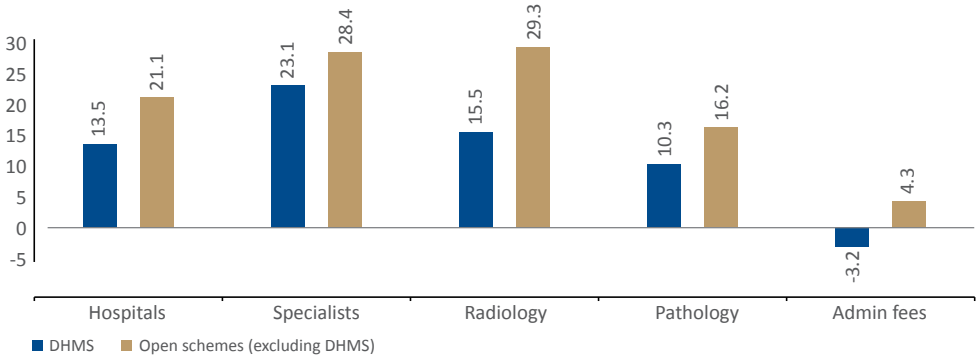
The DHMS Governance and Operating Model Review, which was commissioned by DHMS Board of Trustees and concluded by Deloitte, assessed the operating and governance model, as well as the performance of the Scheme and the administration fees and value delivered by Discovery Health. The review found that:

- The governance processes and structures of DHMS were of a very high standard, and the relationship between the Scheme and the administrator is effectively governed
- **DHMS is led by a strong and competent Board of Trustees with no governance failures**
- The Scheme outperforms all benchmarked schemes in the Deloitte Performance Model
- The administration and managed care fees paid by the Scheme to Discovery Health are 7% above the industry average, equivalent to R11.43 (per average beneficiary per month relative to the average of the open medical schemes industry)
- The members of the Scheme gain significant value from the services provided by Discovery Health, reflected primarily in the fact that members pay on average R158.24 less per beneficiary every month in contributions than the members of other open schemes on a benefit-adjusted basis
- **In terms of total value obtained by DHMS members, the review found that for every R1 spent by the Scheme on administration and managed care fees, the Scheme obtains a return of between R1.77 and R2.02. The growth of DHMS over the past five years could be predicted to lead to administration fees reducing by approximately 28% due to economies of scale; and the actual finding was that these fees have reduced by over 27% during this period. The review thus found that the Scheme is effectively obtaining all of the benefits of its growth over this period in terms of reduced administration fees**
- The Scheme's model of integrated outsourcing of all administration and managed care services to Discovery Health costs 15% less than the rest of the industry, and delivers better performance for the Scheme relative to all other open schemes.

The results of the Deloitte review were made public at the Discovery Health Medical Scheme Annual General Meeting on 20 June 2013.

DHMS has a lower cost inflation than all other open schemes

% Growth in pabpm costs (2008 – 2011)



4

FOCUS AREA

Ensure seamless access to the healthcare system underpinned by best-in-class service.

The scale of Discovery Health's operations is unparalleled in the industry, with over 35 000 calls answered each working day, and 80% of queries resolved during the first call. More than 50 000 hospital admissions are approved every month. Despite the scale of our operations, we achieved an average 8.85 out of 10 in customer satisfaction surveys.

Discovery Health was also recognised as the top and only recognised medical aid brand in the 2013 Sunday Times Top Brands survey, as well as by the Financial Intermediary Association (FIA) as the Healthcare Product Supplier of the Year – an accolade we have consistently received since the FIA Awards were initiated in 2008.

5

FOCUS AREA

Help build a better healthcare system for all South Africans.

6

As one of the leading role-players in South Africa's healthcare sector, we have a responsibility and opportunity to help build a better national healthcare system. As such, we have invested in various large-scale projects and initiatives over the past few years to strengthen the healthcare system. These include a comprehensive 10-year programme in which we are investing more than R150 million in training additional specialists, a R55 million investment in various public healthcare organisations with a focus on primary healthcare and a R15 million investment in immunisation services in under-resourced areas of South Africa.

DISCOVERY FOUNDATION TO INVEST OVER **R150 MILLION IN TRAINING MORE THAN 300 MEDICAL SPECIALISTS**

R102 million

IN GRANTS COMMITTED TO 237 RECIPIENTS (2007 – 2013)

DISCOVERY FOUNDATION MGH AWARD:

- Grant for cutting-edge medical research in collaboration with Massachusetts General Hospital in Boston, US; one of the leading academic hospitals in the US.
- Two-year fellowship period.
- Award valued at **R2.1 million**.
- Granted to a top healthcare professional pursuing an academic medical career after obtaining a PhD.

Strategic priorities for 2014

Continue to provide benefit and contribution stability across the DHMS product range.

Ensure that all schemes under our management provide the broadest benefit choices at the lowest cost, with outstanding service to members.

Drive further service and benefit innovations for members, healthcare professionals and financial advisers.

Continue to leverage our scale, resources and partnerships to stimulate and incentivise improvements in the efficiency, quality and coordination of care delivered to members managed by Discovery Health, including the development of innovative, low-cost models of care delivery.

Continue to use innovative product solutions to meet the needs of the lower-income market.

Improve the quality and efficacy of Discovery's Corporate Wellness offerings to clients as part of a strategy to improve the health and wellness of our members.

Implement a framework for Treating Customers Fairly.

As part of the objective of strengthening and sustaining South Africa's private healthcare system within the broader national healthcare system, introduce award categories to recognise key contributors in the private sector.

DISCOVERY HEALTH



Q&A

Dr Jonathan Broomberg

Chief Executive Officer, Discovery Health

What are some of the key trends and challenges facing the private healthcare sector today? How are you addressing these?

South Africa's healthcare system is highly complex with various factors impacting access, quality and cost. These challenging factors include the rapidly rising cost of healthcare that outstrips consumer inflation, an increased burden of disease, a lack of skilled medical professionals, particularly specialists, and areas of inconsistent quality and fragmentation of care. These factors all contribute to the rising cost of private healthcare which, in turn, leads to a trend in the medical schemes environment known as adverse selection. Simply put, it means that younger and healthier members may choose not to be on a medical scheme because they do not see the value in it. But the way medical schemes work makes it critical for schemes to attract healthier and younger members who help to keep the schemes viable over the long-term. In addition, there is huge disparity between our public and private sectors. Over 42 million South Africans rely on the public sector, with 8.7 million beneficiaries in the private sector, resulting in an overburdened public sector.

At Discovery Health, we navigate this complex environment through an integrated model that proactively addresses each of these challenges. We work closely with the healthcare system – specialists, hospitals and other healthcare professionals – to improve quality of care and reduce costs over the long-term. This involves innovative new reimbursement models that encourage healthcare providers to optimise quality and efficiency. A second important area to consider is the fragmented nature of care in our healthcare system. Healthcare providers tend to work in silos when in fact, the complexity of patients' conditions require multi-disciplinary teams that are able to manage diagnostic uncertainty and clinical ambiguity. By introducing programmes that facilitate greater teamwork and coordination of care we are able to impact quality of care positively.

A third important trend in healthcare is the importance of big data and analytics capability. Health analytics is a critical skill and asset for healthcare funders as it enables us to better understand and manage risk over time. We estimate that good risk management saves Discovery Health Medical Scheme (DHMS) in the region of R3 billion each year. This equates to nearly 10% of total claims. Health analytics also enable data analysis and interpretation of a range of issues that impact the quality and cost of healthcare.

New digital technology provides more opportunity to improve quality, cost and consumers' experience in the healthcare system. During the past year, we introduced a diabetes device pilot programme that uses telemetry to assist patients to monitor their condition with the use of a smartphone app. We gave 50 members with diabetes a glucose monitoring device that measures their blood

"At Discovery Health we navigate the complex healthcare environment through an integrated model that proactively addresses challenges in the healthcare sector."



sugar four times a day. The results were then relayed to their doctor through their mobile phones. Alerts were triggered when readings were out of range. Initial feedback from our members has been very positive – 82% of patients rated the pilot experience eight or higher out of 10. We are now rolling out the programme to around 55 000 Discovery Health members with diabetes.

These initiatives contribute to our vision of being an organisation that makes people healthier and offers them the broadest and best benefit choices at the lowest cost per unit of benefit in a healthcare system that is seamless, accessible and brilliantly serviced and that operates within a broader sustainable healthcare system for all South Africans.

As elsewhere in the world, there are various regulatory changes currently being implemented in South Africa. What are your views on these changes, for example the Competition Commission Inquiry into the private healthcare system? Do these regulatory changes pose a risk for private healthcare funders?

There are currently two key areas of regulatory reform – the National Health Insurance (NHI) system and the Competition Commission Inquiry into the private healthcare system. Certainly, one of the most topical areas is NHI, with the current emphasis being on improving the public-sector system in the 11 pilot districts.

Discovery Health continues to strongly support the vision and objectives of the proposed NHI system. We view it as a critical part of building our healthcare system to make quality healthcare a reality for all South Africans. To this end, we have a dedicated team assisting and supporting the Department of Health in the rollout and implementation of one of the pilot districts. While some of the progress may have been slow and uneven, we remain optimistic that the Department of Health is focused on the appropriate issues, and that we will see systematic improvements in the quality and efficiency of the public healthcare system over time. We are also eagerly awaiting further details on the structure and approach to be taken in relation to the NHI and its financing. As the emergence of the NHI will be very gradual over many years, we do not envisage any material impact on the private funding environment for the foreseeable future. In terms of the Competition Commission Inquiry, we fully support this process, and we believe that it has the potential to increase the information available to policymakers, and heighten understanding of the challenges and opportunities facing our healthcare system. We expect that the focus of the Inquiry will be on hospitals and specialists, with attention also being given to financial advisers, as well as medical schemes and administrators.

Discovery Health has received its share of negative publicity from unhappy customers during the past year. Do you think consumers still perceive value in belonging to a private medical scheme?

Creating value in healthcare, and ensuring that consumers understand and recognise this value, is a challenging task. The reality is that healthcare costs around 15% of household income, but 80% of people claim less than they contribute in any one year. However, the 20% that do claim consume most of the premium income of a scheme.

This is the essence of the medical scheme "contract" – it will be there for you when you or your family has significant healthcare expenses, but over many years, members may feel resentful that they paid in more than they have claimed. An added factor is that healthcare is becoming more complex for both healthcare professionals and funders. Advances in medical treatment means that new treatment regimens and technology are brought to market fairly quickly and medical schemes are often required to make complex funding decisions that balance the issue of cost and clinical efficacy. There is a tremendous responsibility to make the correct funding decision that protects both the individual member as well as the Scheme.

It is important that we act in the best interests of every member as well as the entire Scheme at all times. I believe we do so on a fair and consistent basis. However, when an individual is impacted by these processes, they often don't perceive the wider process, and understandably focus only on their specific issue. It is our responsibility to respond fairly and consistently to each of these members, and not to make exceptions when there is significant media or other pressure to do so.

Q&A: Dr Jonathan Broomberg continued

DISCOVERY HEALTH

Having said all of that, there is no doubt that the general public still believes in the critical importance of having medical scheme cover if they can afford to. It is also clear that Discovery Health and DHMS are the standout choices for employers and individuals relative to all other schemes. Over the past six years, over 890 000 members have left other open schemes – 600 000 of these have joined DHMS, and the majority of the remainder have joined the Government Employees Medical Scheme. So, while we do experience negative media coverage in isolated cases, we work incredibly hard to service our close to 2.8 million members brilliantly every day, and I believe that we do that very well and consistently.

The impact of non-communicable diseases on quality of life and productivity as well as healthcare costs, has been high on the global agenda during the past year. How should healthcare funders deal with this risk?

Chronic diseases of lifestyle are increasingly impacting medical schemes. It is estimated that four major chronic diseases – diabetes, heart disease, lung diseases and some cancers, caused by three risk factors being tobacco use, poor diet and a lack of physical activity, together account for over 50% of deaths worldwide.

The impact on medical schemes is severe. The Council for Medical Schemes estimates that the burden of chronic diseases of lifestyle grew by 12% between 2008 and 2011. Healthcare funders must have a robust strategy in place to address this risk. Discovery Health's data shows that of all our members, the sickest 2% account for 21% of the total healthcare cost spend, while the next tier members with a significant chronic condition account for 27% of the total spend. The third group consists of members who are healthy, but their lifestyle may put them at risk of developing chronic conditions in future. This group accounts for 90% of our member base.

It is clear that a population of this size offers both a challenge and an opportunity to contain healthcare costs and significantly improve the sustainability of the Scheme. Discovery's wellness programme, Vitality, plays an important role in encouraging healthy behaviour and reducing healthcare costs. Our research into the impact of Vitality has found that the longer members are on the programme, the more active they become. This is important, as physically active members have a 7% lower chance of being admitted to hospital than less active people. Their healthcare costs are also lower.



Discovery Health



Improving quality of care through the Discovery Health Care Coordination Programme

The Discovery Health Care Coordination Programme supports **the recovery of members with highly complex clinical needs**.

These members often need complex rehabilitation, including home-based care. However, a lack of coordination in the care of these patients often results in longer recovery periods as well as recurring re-admittance to hospital. The Discovery Care Coordination Programme helps members to move to a participating care facility where they can regain their health once they are discharged from hospital. We appoint a care coordinator who is a registered nurse to guide members through their rehabilitation process. After members are discharged from the facility, they continue to receive treatment at home and in their communities for as long as is necessary. The range of services includes rehabilitation, disease education, psycho-social support and nursing services.

There are currently 11 facilities and 400 providers involved in the programme in five regions across South Africa. A total of 2 384 members were enrolled in the programme by June 2013.

KEY FACTS AND PERFORMANCE HIGHLIGHTS

First integrated product launched with Discovery Insure

Improved levels of Vitality engagement resulting in **lower claims** and **lower lapse rates**

Discovery Life was voted **the top life insurance brand** by South African consumers in the 2013 Sunday Times **Top Brands survey** and received the 2013 Financial Intermediaries Association of Southern Africa (FIA) award for **best long-term insurer**



DISCOVERY LIFE

Our vision

To become the best life insurer in the world with superior actuarial dynamics, offering unique products that enhance the lives of policyholders.

PERFORMANCE HIGHLIGHTS

Embedded value of Discovery Life and Discovery Invest increased by **20%** to
R16.9 billion

New business API increased by **8%** to
R1 896 million

Operating profit increased by **16%** to
R2 106 million

Key facts about **Discovery Life**

Launched in
2000,
Discovery Life is South Africa's fastest growing major life insurer in the risk market.

First **South African life insurer to separate risk from investment,** leading to significant change in the industry.

372 288
policyholders.

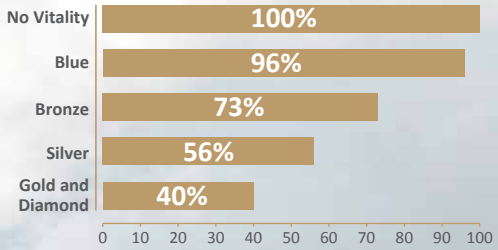
Discovery Life addresses the problem of under-insurance through its **unique integrated operating model and innovative product development.**

Discovery Life is the **first life insurer to reward clients for safe driving behaviour.**

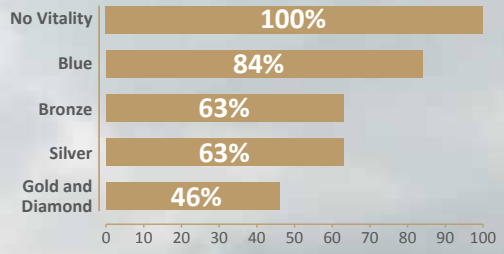
Discovery Life has **25%** **of the overall risk broker market.**

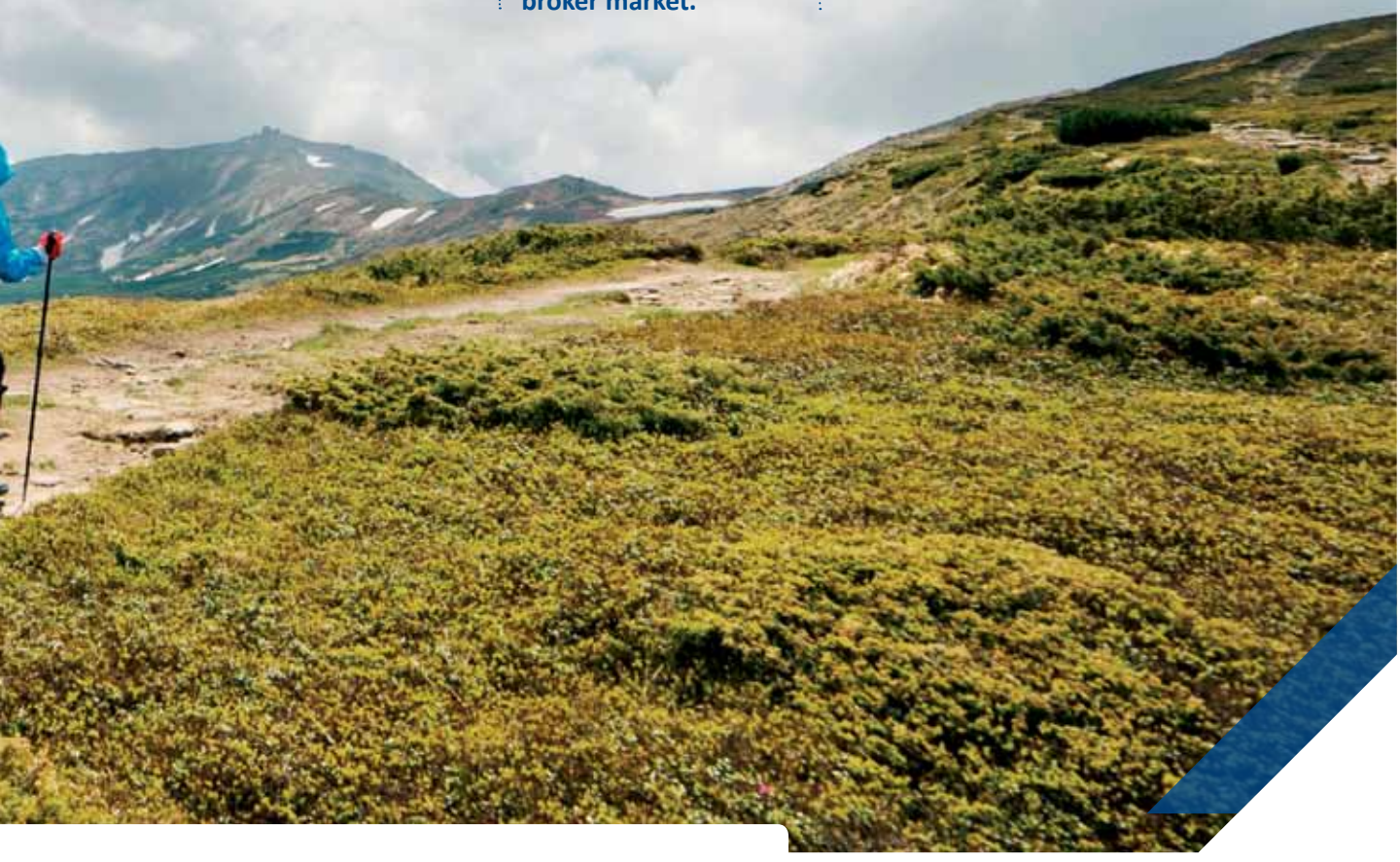
Excellent actuarial dynamics of the model

Lapse rates by status (Expected indexed to 100)



Claims experience by status (No Vitality indexed to 100)





PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

DISCOVERY LIFE

Discovery Life is the only insurer to offer the ability to claim in excess of the benefit amount and multiple related claims regardless of whether a subsequent claim is of a higher, lower or same severity as the previous claim.



Discovery Life delivered a positive performance during the past year. New business API increased by **8% to R1 896 million**, with Discovery Life gaining market share and being the number one writer of new business in the broker risk market.

Operating profit increased by 16% to R2 106 million and we continued to reinvest cash to strengthen and grow the business. We also developed the first integrated product with Discovery Insure that allows us to add driving behaviour as a risk-rating factor to our dynamic pricing model. A second important development during the past year has been the separation of short-term and long-term behavioural elements through a restructure of PayBack and Cash Conversion Benefits. This improves the value proposition for consumers as paybacks at an earlier stage are made possible, resulting in increased engagement levels in Vitality, better lapse rates and improved morbidity and mortality experience.

Discovery Life

To date, Discovery Life has paid out over
R528 million
to policyholders in the form of PayBack benefits

Total claims paid to
1 129 policyholders
between April and June 2013 was
R489 021 066

Key strategy for 2013

Continue to develop innovative solutions for consumers, including the lower-income market, **to address the trend of underinsurance in South Africa.**

Our progress

We launched the following key products and benefits during November 2012 and May 2013:

- Re-pricing of the Income Continuation Benefit for professionals
- A new funding plan option, Flexrater, which gives clients more flexibility and choice in how their premiums are structured
- Enhanced Financial Integrator Benefit that allows earlier payouts to clients by moving Cash Conversion Benefits earlier in a policy's term
- Enhancements to the PayBack Benefit in the form of three new features:
  - Annual Guaranteed paybacks of up to 30% for the first 10 years
  - Cumulating PayBack option which increases certainty by paying higher guarantees at years five and 10
  - Vitality Memory – a benefit that enables a guaranteed PayBack percentage to clients who have built up a health asset through regular engagement with Vitality
- A new integrator with Discovery Insure and Vitalitydrive
- Various special offers to clients.

Key strategy for 2013

Manage financial risk for Discovery Life.

Our progress

The lapse rate continues to improve, with the experience over the financial year at 10.1%, above the expected lapse rate of 12.6%.

Key strategy for 2013

Improving the servicing of existing clients while maximising expense efficiencies.

Our progress

We have introduced new educational and information tools that give financial advisers the opportunity to provide better quality advice to their clients. This includes the Policyholder Return on Premium calculator – a tool that enables financial advisers to calculate the return on premium that their clients will experience as a result of good health management. It also highlights the increased value generated through engagement in Vitality and the associated health benefits.

OUR FOCUS AREAS DURING 2013

DISCOVERY LIFE

We were the first life insurer in South Africa to separate risk from investment products, a change that has led to a structural change in our insurance industry. Since then, we have continuously evolved the Discovery Life product offering by changing the underlying structure of risk policies to generate more value where it previously did not exist. Behavioural life insurance today optimises a client's return on premium by rewarding them for managing their health.

Our focus areas during 2013

In 2013, we focused on evolving the Discovery Life product offering further from the one-size-fits-all approach to one that is dynamic and empowers consumers to derive more value from their life insurance.

1

FOCUS AREA

Re-engineering key integration benefits to enhance short-term benefit for clients as well as long-term sustainability.

During the past year, we restructured three key Discovery Life benefits – the DiscoveryCard Integrator, Financial Integrator Protectors and CoverBooster – to give clients more immediate rewards as well as long-term sustainability in gaining additional value. The funding for these benefits, which was made possible by improved health behaviour and accurate risk pricing gained through the dynamic underwriting model, has now been channelled to enhance the PayBack Benefit and the Cash Conversion Benefit. Both these benefits, which are highly valued by consumers, are two of the most successful drivers of behaviour change for policyholders.

2

FOCUS AREA

Introducing the first integrated product with Discovery Insure and Vitalitydrive.

Motor vehicle accidents are one of the major causes of deaths in South Africa. Behavioural data from Discovery Insure – Discovery's short-term insurance company – shows that the majority of motor vehicle accidents are preceded by poor driving behaviour such as harsh braking and cornering as well as driving over the speed limit. An improvement in average driving behaviour can result in fewer fatalities on South African roads.

The effect of motor vehicle accidents is not only detrimental to society at large, but is also a substantive cost for life insurers. In 2012, motor vehicle accidents accounted for one in five deaths on the Discovery Life book, which amounted to over R245 million in claims. A significant reduction in Discovery Life's liabilities can be achieved by improving the driving behaviour of policyholders. Vitalitydrive is highly effective in improving driving behaviour and consequently, the mortality rate related to vehicle accidents. Our data from Discovery Insure shows that Vitalitydrive clients have one-third less fatal car accidents compared to the national average.

It also shows a direct correlation between driving behaviour and the incidence of claiming. Clients with high levels of harsh acceleration, harsh braking and speeding have much higher claim ratios than clients with low levels. The potential existed to link the Discovery LIFE Plan with Vitalitydrive to give clients who drive well, initial premium discounts based on how well they drive.

3

FOCUS AREA

A focus on benefit enhancements to drive new business.

During November 2012, we launched several enhancements and special offers to expand the value offered on key Discovery Life products and benefits. The introduction of these benefits resulted in a marked increase in daily activations of over 20%, compared to the same period during the previous year. We also worked on launching targeted product initiatives during the first half of 2013, with the aim of further driving new business.

FOCUS AREA

Ensuring Discovery Life is prepared for the requirements of the Solvency Assessment and Management Framework.

The Financial Services Board and the South African insurance industry started a project in 2009 to establish a solvency framework for the South African short- and long-term insurance sectors. This process follows the global trends in insurance supervisory regimes such as Solvency II developments in Europe. The Solvency Assessment and Management (SAM) Framework project – consisting of industry representatives as well as representatives from the Financial Services Board in South Africa – is responsible for establishing a risk-based supervisory regime for the regulation of long-term and short-term insurers.

Discovery Life is taking part in the industry initiatives and we have also established internal working groups to discuss technical papers and proposals regarding various aspects of SAM requirements. At the time of writing, a Discovery working group had completed work for an industry survey for the Financial Services Board. The Economic Impact Study survey aims to gather an assessment from industry role-players on the likely first and second order impacts of the SAM regulatory regime change on all insurance stakeholders and to predict the broader macro-economic impact of this change.

Strategic priorities for 2014

Drive take-up of recently-launched Life products and features (Severe Illness Benefit, Financial integrator, Vitality Memory).

Continue our preparation for the Solvency Assessment and Management Framework.

A continuous focus on enhancements to the Discovery Life product offering, including further integration opportunities with other Discovery businesses.

Expand into the emerging market.



DISCOVERY LIFE



Q&A

Herschel Mayers

Chief Executive Officer, Discovery Life

What are some of the trends in the protection market in South Africa?

There are four important trends that are impacting the insurance industry globally. The principles behind behavioural economics are increasingly becoming relevant as we start to understand how mostly irrational human behaviour impacts our everyday decisions and most importantly, our decisions about health and wellness. A well-documented behavioural economics concept, which is highly relevant in life insurance, is the concept of hyperbolic discounting. It means that individuals will often place more value on short-term gratification instead of long-term rewards. This is an important concept for us specifically, as we provide our clients with short-term and medium-term tangible rewards that drive long-term behaviour change and ultimately, long-term benefits.

A second important trend is that of continually increasing healthcare costs. Various factors contribute to this increase, with non-communicable diseases (NCDs) one of the contributors. NCDs are estimated to cause more than nine million deaths

"The life insurance industry in South Africa is one of the most competitive in the world and we therefore need to continue offering our clients unrivalled value."



worldwide each year for people under the age of 60, with obvious knock-on effects on productivity and development. The problem is not limited to the insurance or health sectors only, but is fast becoming one of the national agenda points. It was a key topic at this year's World Economic Forum meeting. The impact of NCDs can be reduced by making the necessary lifestyle changes that incorporate a healthy diet, an active lifestyle and stopping smoking.

The third important trend has to do with the financial crisis and consumers becoming more risk averse in their financial behaviour. Consumers today are drawn towards financial products that give them certainty as opposed to products that carry a higher financial risk.

Lastly, a trend in the life insurance industry, both locally and globally, has been the distinct shift towards products that are transparent and understandable to consumers. The responsibility to treat customers fairly spans all aspects of the business, including the way in which products are designed, marketed and distributed. There has been an industry-wide shift towards more objectivity and certainty in products and processes.

What have been the key risks and challenges for Discovery Life during the past financial year? How do you address and manage these risks?

A key challenge for Discovery Life is to continuously innovate and meet clients' needs in a highly complex environment. The state of the economic environment impacts how consumers behave financially. In difficult economic circumstances, lapses tend to track higher as consumers experience more financial pressure. The key is to find ways to address gaps and needs in the market and offer additional value to consumers. At the same time, we must also deliver excellent return on capital, so it is a fine balance to manage. In terms of Discovery Life's sustainability and continued success, managing our financial exposure, especially with regards to lapses and claims experience, is critical as an improved performance across these metrics enhances the profitability for the business. The way we address these risks is through a relentless focus on product innovation that uses the integration opportunities across the business as a platform to create more value for our clients. This process is formalised as we have product launches every year during which products and benefit enhancements are introduced to the market.

Competition in the life insurance industry is strong – how do you see your competition and what are you doing to address the competition?

The life insurance industry in South Africa is one of the most competitive in the world and we therefore need to continue offering our clients unrivalled value. Vitality gives us a unique advantage in the market as it generates value in a number of areas – it enables us to create unique benefits that offer clients better value for money, it enables more accurate risk pricing as it introduces dynamic risk-rating factors and lastly, it improves the actuarial dynamics in the business.

CASE STUDY

DISCOVERY LIFE



Creating value
through behavioural life insurance

The frequency of life insurance claims for clients who are highly engaged in Vitality, is **68% lower than for clients who do not actively manage their health.**

The additional accuracy created through dynamic risk assessments enables discounts – both upfront and over time – to be offered, resulting in improved premium efficiency.



For decades, life insurance has been a stagnant industry with little innovation. A new phase in life insurance, with dynamic underwriting and wellness management as the underpin, has resulted in more accurate underwriting and long-term value for consumers. Traditionally, life insurers only collect information about a policyholder's risk once at the start of the policy and then predict what the person's risk for mortality or morbidity is likely to be. This prediction is based on static risk-rating factors such as age, gender, smoker status, level of wellness, hazardous pursuits and socio-economic circumstances. Since this is the only information available to the insurer throughout the policy, the insurer will base the price on the average experience of existing policyholders with similar rating factors. During the initial period – when the insurer is able to assess the policyholder's health – the premium will be lower for healthier individuals. However, as the policy period continues, the insurer will base the policyholder's premium on the average experience of initially similar policyholders. This static model penalises healthier clients over average clients as it is unable to assess risk continuously.

A new phase in the life insurance industry has emerged with a model that moves away from an inflexible, one-size-fits-all approach, to one that is dynamic, empowers the consumer and creates value. This model acknowledges that people often behave irrationally in terms of their health status and risk – foregoing long-term positive outcomes for immediate benefits – and this aspect influences how insurers assess mortality and morbidity risk. A dynamic underwriting model that measures behaviour and rewards healthy behaviour adds a new dimension to the consumer's value equation: Policyholder's Return on Premium.

Dynamic underwriting models that use health status and behaviour as a risk-rating factor can price risk more accurately. While some risk factors such as age cannot be controlled, factors such as smoker status and physical activity can be influenced and measured. By assessing health and wellness information throughout the term of the policy, a more accurate risk assessment can be done. It enables discounts on premiums – both upfront and over the term of the policy. For insurers, health and wellness management reduces expected liabilities and releases surplus assets. Life insurers are required to hold a certain amount of funds to ensure they are able to meet their liabilities in the form of future expected claims. The extent of liabilities depends on the benefits and health of the insured lives. An improvement in the health status of policyholders will have a direct positive impact on the liabilities for insurers. Traditional underwriting models are unable to measure and quantify this impact, and can therefore not maximise additional reserve funds for the benefit of healthy policyholders.

By managing their health, policyholders can earn health and financial benefits.

KEY FACTS AND PERFORMANCE HIGHLIGHTS

Operating profit increased by **46%** to
R221 million

Assets under management increased **20%** to
R30 billion

In 2013, **5 000** financial advisers selected **Discovery Invest** for their clients



DISCOVERY INVEST

Our vision

To become a brilliant savings business that delivers superior returns for clients by offering innovative products and access to superior asset management.

New business API increased by **11%** to
R1 070 million

In-force business increased **28%** to
R2 194 million



Key facts about Discovery Invest

Assets under management exceed **R30 billion.**

Launched in **2007,** **90 758** policyholders.

The company offers consumers a unique and comprehensive product range that addresses the current gaps in the market by offering **greater protection against poor investment choices.**

To date, Discovery Invest clients have saved approximately **R133 million** in investment fees because of the As and When Investment Integrator, an integration product that pays back investors up to **100%** of all administration fees, policy fees, asset management fees and financial adviser initial advice fees.

In 2013, Discovery Invest received the Financial Intermediaries Association of Southern Africa (FIA) **award for best recurring premium business.**

PERFORMANCE AGAINST KEY STRATEGIES AND OUR FOCUS AREAS FOR 2013

DISCOVERY INVEST

Discovery Invest delivered a strong performance during the past year, supported by sustained product resonance and an improved performance of the investment markets. We further developed the integration model to enable Discovery Invest to offer investment products with unique features to consumers.

Key strategy for 2013

Continued product innovation to **offer a comprehensive range of investment products to consumers.**

✓

Our progress

- We enhanced the Discovery retirement Optimiser Benefit to enable clients to use their LIFE Plan paybacks to boost their retirement savings. Our enhancement of the product offering resulted in increased new business and profitability.
- **We extended the Upfront Investment Integrator to make Discovery Endowment products more competitive in the market as it also benefits investors who invested in External Funds or investors without a Discovery LIFE Plan. Previously, the benefit was only available to clients who had a Discovery Fund. The extended product attracts larger volumes of new business and appeals to a larger array of financial advisers.**
- We redesigned the Discovery Invest website portal to give investors more information and easy access to their portfolio details.
- A special offer to investors – the Offshore Limited Tranche – was made during May 2013. Through this special offer the upfront integration boost on the Offshore Endowment Plan was enhanced from 10% to 15% for specific Discovery LIFE Plan members, with a 10% boost for all other clients. The product was marketed through a direct email campaign.
- We launched the Tax-free Corporate Endowment Plan for corporate investors that offers tax-free interest and capital gains growth for five years.
- Product enhancements were introduced to the Croci Funds to make this product offering more competitive in the market.
- We designed a Portfolio Review to assist financial advisers in analysing investments for their existing clients.

Key strategy for 2013

Continue to build scale with a **focus on achieving cost efficiencies.**

✓

Our progress

We introduced new distribution channels, Independent Consultants and Group Independent Consultants. At the end of July 2013, 211 individual Independent Consultants and 209 Group Independent Consultants joined the current Discovery distribution channel.

Discovery Invest's objective is to provide innovative products and investment solutions that address gaps in the market by offering greater protection against poor investment decisions.

The investment industry was largely efficient at the time of Discovery Invest's launch in 2007 – consumerism had driven costs lower and more product choices were available to investors while specialist asset managers started to emerge. While the industry is focused on generating value for consumers through more choice and flexibility, our strategy has been to combine the breadth and skill of the asset management industry with the product integration capability of Discovery Life and Discovery Vitality to create more efficiency in investments.

Discovery Invest

Discovery Invest is the **largest** writer of endowment policies in South Africa, with **one in every four** endowments being invested with Discovery Invest

Through the Upfront Investment Integrator, we expect to boost our clients' investments by over **R1 billion** by 2015

Our focus areas during 2013

During 2013, our focus has been on developing new products and benefit enhancements that give investors a more comprehensive range of investment choices. The new products and benefits that were launched are aimed at driving new business for Discovery Invest to reach greater scale.

1

FOCUS AREA

Introduced benefit enhancements and special offers on products to give clients more financial protection and certainty.

- We introduced enhancements to the Discovery retirement Optimiser in November last year, which gives clients further opportunities to save for retirement. It addresses the challenges investors face when saving for retirement – challenges that are not addressed by traditional retirement products. Through the benefits of integration with other Discovery products such as Discovery Life and Discovery Health and Vitality, clients gain significant value. The enhanced product is simpler to understand for consumers and more cost-effective as the addition of the Retirement Investment Integrator provided extremely large fee discounts, making it the cheapest in the market. The Life PayBack Booster allows clients to reinvest their Life PayBacks in the Discovery retirement Optimiser and have them doubled in retirement, making saving automatic and more valuable for consumers. The take-up of the enhanced Discovery retirement Optimiser has been excellent with a 58.8% increase in Annual Premium Income.
- In March 2009, following the global financial crisis, we launched the Upfront Investment Integrator, a product that provided an opportunity for investors to experience an immediate recovery from investment losses as a result of the crisis. This product used the tax assets created by a client's Discovery LIFE Plan to direct additional funds to a client's endowment policy, effectively a 26% boost. Since its launch, we have enhanced the contributions of our investors by R660 million.
- We also ran a range of special offers to encourage clients to invest in Offshore Endowment plans, endowment plans for corporate clients or other lump sum investments. These special offers were aimed at increasing the cost-effectiveness of investing for clients, by reducing fees. The special offer on the Offshore Endowment Plan allowed investors to invest their money offshore at lower exchange rates, an additional advantage in the current market where the South African Rand has depreciated dramatically.

Our example shows how product integration can benefit a client by enabling the client to effectively retire for free:

- R1 000
Monthly contribution to the Discovery retirement Optimiser

+ R400*
Tax deduction refund

+ R187.50
Discovery Life PayBack of 20%**

+ R75
Additional tax deduction refund from Discovery Life PayBack

+ R187.50
PayBack reinvested using the Retirement PayBack Booster, the amount is boosted by up to 100% at retirement age

R150
Discovery LIFE Plan Optimiser adds a tax-free boost to the retirement fund (15% assumed)

R0 effective contribution

* *assuming a marginal tax rate of 40%*

** *assuming a PayBack included on the client's Discovery LIFE Plan, Health Integrator and a premium of R937.50*

OUR FOCUS AREAS DURING 2013 continued

DISCOVERY INVEST

FOCUS AREA

Enhanced communication tools for our financial advisers that provide additional support.

In May this year, we launched PortfolioReview, which creates a personalised investment portfolio report for financial advisers. It covers various aspects of investment performance that includes a consolidated overview of investments, a breakdown of the client's allocation to various sectors and the internal rate of return on each investment.

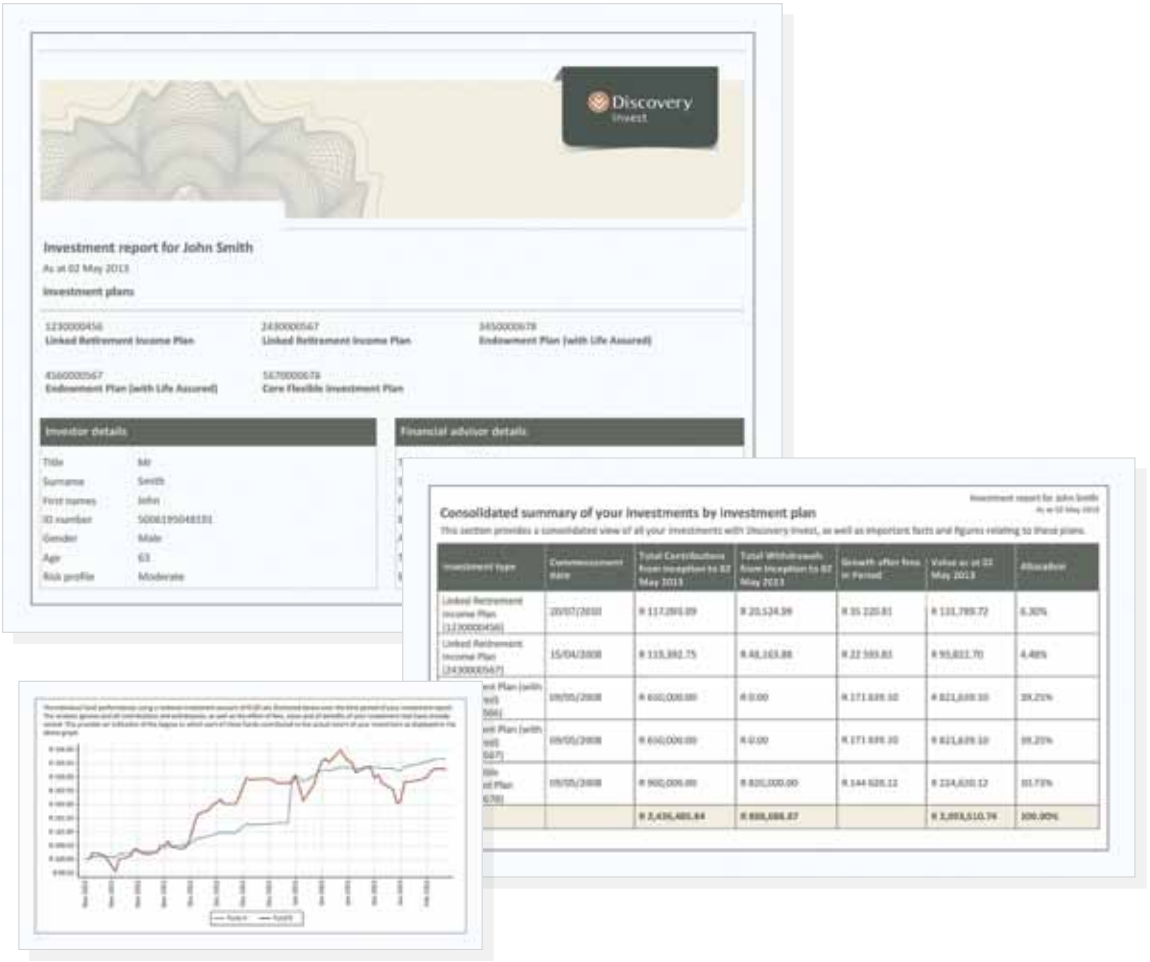
2

Strategic priorities for 2014

Drive take-up of new products and benefits launched for Discovery Invest.

Further strengthen our distribution channel.

Redesign the Discovery Invest website portal with additional functionality for clients and financial advisers.



CASE STUDY

Discovery Invest



Using innovative products to maximise retirement savings

South Africa traditionally has a low savings culture and many South Africans are **not able to retire** comfortably, having to rely on **state welfare** or having to continue working well after retirement age.

The challenges facing people saving for retirement are:

- High fees eroding investment returns
- Low levels of savings from the time a person starts working mean insufficient savings at retirement
- Advances in medical technology and longer life expectancy mean people are outliving their retirement savings and income
- High levels of inflation mean no sustainable real income after retirement
- People often have to postpone their planned retirement date. In addition to making poor investment decisions, consumers are also at a disadvantage as a lack of innovation in the savings industry does not make optimal use of financial products to gain the maximum benefits for retirement.

The Discovery retirement Optimiser is an innovative product that allows consumers to use other existing Discovery products more optimally. It provides clients with a tax-efficient savings vehicle that when combined with a Discovery LIFE Plan, allows them to reduce the cost of investments, giving them additional funds to invest in retirement savings. It also gives consumers the opportunity to convert unused risk cover from a Discovery LIFE Plan into tax-free instalments in retirement.

The Discovery retirement Optimiser benefits consumers in the following ways:

- Unused life cover becomes an asset to enhance retirement income
- It helps reduce the risk of a person outliving their retirement income as it effectively doubles the number of years a retirement income can last
- Its cost-efficiency enhances a person's retirement fund as it can effectively provide additional return every year
- It provides a sustainable and real retirement income
- It makes it possible for a person to retire earlier than the typical retirement age of 65.

KEY FACTS AND PERFORMANCE HIGHLIGHTS

Vitality members in South Africa increased to almost
1.7 million

Vitality points awarded to members in 2013 for getting active with fitness devices
23 630 600

Vitality members booked over one million discounted flights, filled up 19 planes every day, covered over three million kms and saved themselves
R231 million



DISCOVERY VITALITY

Our vision

To make people healthier by incentivising our members globally to improve their health with compelling rewards that are based on proprietary science-based interventions.

More than **320 000** families registered on the **HealthyFood Benefit**

Better behaviour from members in terms of healthy nutrition – engagement with the HealthyFood

Benefit increases the ratio of healthy to total food expenditure by 9.3% and decreases the ratio of less desirable food items by 7.2%

Engagement levels up across all wellness and screening categories

Key facts about **Discovery Vitality**

The Vitality value offering is enhanced by the

DiscoveryCard
Discovery's unique Visa credit card which gives members status-based rewards.

The first Vitality Fittest City Index was launched in 2013.

Vitality is the largest wellness programme of its kind in the world, with more than **1.6 million** members in South Africa, and a global membership base of 5.5 million.

DiscoveryCard is South Africa's largest status-based rewards credit card in issue, with a market share of point-of-sale spend of over **9%.**

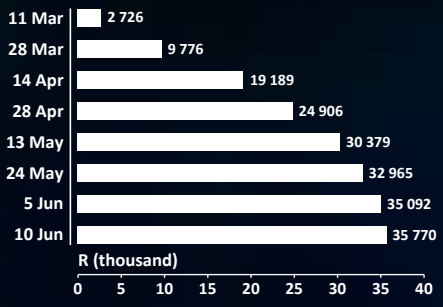
DiscoveryCard has over **240 000** primary cardholders.

The HealthyFood Benefit delivers **positive outcomes** for the Vitality partner, the insurer and the policyholder.

Members have spent over R10 billion, of which R2 billion has been on HealthyFood (Pick n Pay)



Over 35 000 activations since launch (Woolworths)



PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

DISCOVERY VITALITY



Our sedentary lifestyles impact significantly on the current global epidemic of chronic diseases. Being physically active lowers the risk of several of these life-threatening conditions, like type two diabetes, hypertension, cardiovascular disease and certain cancers.

Over 35 000 HealthyFood activations
since Woolworths was added as a HealthyFood retail partner

1 288 Vitality members
are finding out their Vitality Age every day

Key strategy for 2013

Continue to develop the clinical efficacy of the Vitality programme by using the **latest thinking on behavioural economics to incentivise healthier lifestyles.**

Our progress

- Various research projects ongoing in partnership with RAND Corporation and other leading academic institutions.
- **Research paper on HealthyFood published this year.**
- Vitality Fittest City Index results released this year, which ranks South Africa's major metropolitan areas according to its health and fitness-promoting infrastructure.

Key strategy for 2013

Introduce powerful new benefits **that enhance the lives of our members.**

Our progress

- **HealthyFood Benefit extended through our partnership with Woolworths, giving members a broader range of retailers from which to buy HealthyFood items.**
- VitalityMobile introduced, with the aim of reducing financial barriers to mobile communication and building a community around wellness.

Key strategy for 2013

Use evolving technology and social media **to increase engagement and expand the scope of fitness-related activities available to members.**

Our progress

We introduced new ways to track and earn points in 2013, using a range of new devices such as Garmin, Polar, adidas miCoach and Fitbug. By recording their data, members can earn rewards for any regular physical activity they choose.

Key strategy for 2013

Build on the benefits of DiscoveryCard as a further incentive to members to live healthier lives and advance their Vitality status.

Our progress

New DiscoveryCard partners introduced: Builders Warehouse and Builders Express, Incredible Connection and Sunglass Hut; as well as the new discovery/mall online shopping experience.

OUR FOCUS AREAS DURING 2013

DISCOVERY VITALITY

Non-communicable diseases are increasingly becoming a global challenge that governments, businesses and communities grapple with.

The Oxford Health Alliance 3-4-50 model is based on the understanding that more than 50% of all deaths worldwide are caused by chronic diseases of lifestyle that are preventable if poor lifestyle behaviours are changed. Vitality, as a science-based wellness intervention founded on behavioural economics insights, has been proven to help change people's health behaviour over the long-term, thereby reducing their health risks. Our success has been built on a comprehensive clinical understanding of the factors influencing a person's health risk and how people respond to rewards and incentives.

Our focus areas during 2013

Important areas of focus for Vitality have been the further evolvement of the programme in terms of its ability to change people's health behaviour. Sustained behaviour change, as reflected by increased engagement levels, impacts positively on an individual's health status and risk. Vitality's ability to incentivise healthy behaviour and enable product integration opportunities across the Discovery business contributes to a powerful business model that uses dynamic underwriting to better price risk and generate more value for consumers.

FOCUS AREA

Further develop the clinical efficacy and thought leadership of Vitality.

Research projects and partnerships aimed at further developing the clinical efficacy and applicability of Vitality in various fields continue to be a focus. There are currently several research projects and papers underway, including various papers on the impact of Vitality on diabetes and diabetes prevention.

During the year, Vitality released the results of a research project done by RAND Corporation on the effectiveness of a discount programme for healthy food items on consumer purchase and consumption behaviour. The research showed that lowering the costs of healthy foods in supermarkets increases the amount of fruits, vegetables and whole grain foods that people eat, while also appearing to reduce consumption of nutritionally less-desirable foods:

- Vitality members buy 9.3% more HealthyFood items and 7.2% less unhealthy food items
- Members who buy 30% more HealthyFood items in relation to unhealthy food items have a 40% less chance of being diagnosed with a lifestyle-related health condition.

1

Vitality research shows that gym membership and usage increase the longer a member remains on Vitality.

Gym usage on average increased from 27% to 33% in five years.

703 non-smoker declarations completed every day

1 619 Vitality members take part in a Discovery Wellness Day every week

Every **1.2 seconds** a Vitality member works out at a gym

2

FOCUS AREA

Enhance the HealthyFood Benefit to increase awareness and behaviour change around nutrition.

Insights from the RAND Corporation research on HealthyFood validated our approach to focus strongly on nutrition as a critical element of the Vitality rewards structure. Since its launch in 2009, the HealthyFood Benefit has fast become one of the most used benefits. Results from the programme shows that people make healthier food choices if these items are more affordable and easier to identify.

The impact on health has been significant: research shows that a person's chance of being diagnosed with a lifestyle-related health condition decreases the more a person buys HealthyFood items. For this reason, we worked on extending the HealthyFood Benefit to make the incentives more rewarding for members in 2014. Building on the success of adding Woolworths as a HealthyFood partner during the past year, we have extended the benefit to all Discovery Health members from 2014.

3

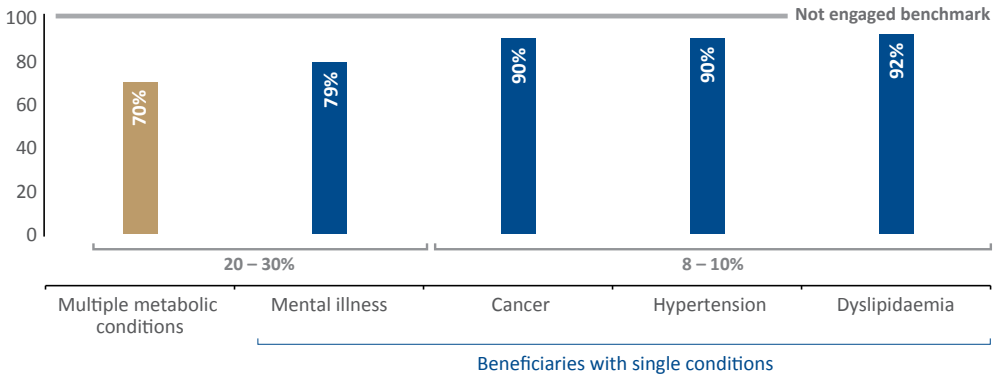
FOCUS AREA

Expand Vitality's fitness platforms to provide members with more opportunities to be active.

- An important feature of the Vitality programme is its approach to changing behaviour, based on the insight that a combination of information, tools and environmental or structural changes are required to change ingrained behaviours such as unhealthy eating and a sedentary lifestyle. Vitality's gym benefit lowers the financial barrier for people to lead an active lifestyle. This benefit forms the cornerstone of the programme and engagement with it continues to increase. This is encouraging as increased engagement in Vitality results in a better mortality and morbidity experience for Discovery Health and Discovery Life.
- During the year, we focused on extending the fitness platform for members in recognition of the need to offer our members more choices to be active and earn points. In June this year, we launched a partnership with parkrun South Africa that enables members to earn Vitality points for taking part in parkruns around the country. Parkrun is a global organisation that, together with sponsors, organises free, weekly 5km timed runs around the world. Over 266 parkruns have been started around the globe in the UK, Denmark, Australia, Poland, New Zealand, the US, Ireland and South Africa.

Engaged chronic members experience lower costs per patient compared to other groups

Risk-adjusted hospital cost for chronic members: engaged versus non-engaged Vitality members



P = 0.001 for multiple metabolic conditions; all single conditions are not statistically significant

DISCOVERY VITALITY

4

FOCUS AREA

Implement new Vitality and DiscoveryCard Benefits for 2013.

At the end of 2012, we introduced enhanced Vitality and DiscoveryCard Benefits for our members for the 2013 calendar year. These benefit enhancements were aimed at enhancing the nutrition element of Vitality through an extended HealthyFood Benefit with Woolworths; benefits that incorporate the latest technology to help members track and improve their fitness; and VitalityMobile, which established a wellness community by reducing the financial barriers to mobile communication.

Social interaction and support are key drivers of positive behaviour change and mobile technology plays an important part in encouraging this type of interaction. The VitalityMobile Benefit, which was launched late last year, aims to remove the financial barriers to mobile communication, thereby creating a unique wellness community. The benefit was rolled out to our members during May this year and allows members to call other VitalityMobile members for free. Over and above the standard contract offer, members also gain a data boost and significantly lower international call rates.

5

FOCUS AREA

Encourage public debate on wellness to help build a healthier society.

The results of another informative survey conducted in partnership with the University of Cape Town were released in June this year. The Vitality Fittest City Index aims to determine how each of South Africa's six major metropolitan areas rank in health and infrastructure that promotes physical activity. The survey intends to raise awareness on the issues of public health, physical activity, urban planning and environmental studies. Data for the Vitality Fittest City Index was collected from reliable, publically-available resources and research and then divided into four categories: personal health indicators; self-reported physical activity; modes of transport; and physical activity-related facilities. Cape Town was announced as South Africa's Fittest City, largely based on the city's attractive outdoor and sporting facilities that encourage physical activity.



"The rapid rise in diseases of lifestyle is a major health concern and we hope that the Vitality Fittest City Index will encourage policymakers and local governments to create supportive environments which will improve the health and physical activity profile of their city. We'd like the Index to act as motivation to encourage people to find opportunities to get active."

– Dr Craig Nossel
Head of Vitality Wellness, Discovery

Discovery Vitality

Every 8 minutes a Vitality Fitness Assessment is completed | **Every 3 seconds** a Vitality member buys HealthyFood | **Over R2 million** is spent on HealthyFood every day



Strategic priorities for 2014

Develop member-specific wellness programmes.

Broaden opportunities for members to participate in physical activity.

Enhance the HealthyFood offering to achieve greater participation and engagement from members.

Develop a corporate wellness offering for employers.

Invest in simplifying and enhancing member service experience and interaction.

BUSINESS DAY (Late Final)
14 Jun 2013, p.2

Capetonians have best opportunity to boost their health

TAMAR KAHN
Science and Health Editor

CAPE TOWN — If you always suspected that Capetonians get a better deal than other South African city slickers, here is proof: new research shows they have more opportunities to get moving and boost their health than anyone else in the country.

A "Fittest City Index" released yesterday by health and life insurer Discovery and the University of Cape Town (UCT) shows the Mother City has better public transport, cycling infrastructure and sports facilities than other big metros. That is good news for its residents and for the officials tasked with marketing the city, said Discovery subsidiary Vitality head Craig Nossel. A similar index is published by the American College of Sports Medicine, which has for the past five years ranked US cities on their health and health potential.

Just as Denver has sold itself to prospective investors as a city with one of the best educated and healthiest populations in the US, so could Cape Town, he said. "The index could also be used to market to tourists, as many visitors want to run, walk, and use public transport."

The index gauges how each of SA's metropolitan areas — Cape Town, Durban, Port Elizabeth, Johannesburg, Pretoria, Port Elizabeth and Ekurhuleni — rank for both physical activity-related health and infrastructure that encourages people to walk, cycle and exercise. It was calculated using research in four categories — personal health indicators, self-reported physical activity, transport and sports facilities.

Cape Town is well known for its seaside promenades, mountain hiking routes and mass exercise events like sponsored walks, but the key reason why it stole the march on other metropolitan areas is its public transport network, which includes a rapidly expanding bus network linked to bicycle routes that aims to have a bus stop within 500m of most people's homes, said Discovery.

The MyCiti bus system is expected to include residents far from the city centre in areas like Khayelitsha and Mitchell's Plain. It allows people to take bicycles on board, unlike the Gautrain, which has barred bikes.

But Capetonians scored below the national average when it came to personal health indicators such as diabetes and high blood pressure.

UCT's Prof Vicki Lambert said there was no direct link between the four areas. The relatively unhealthy Capetonians had the potential to improve their health by making use of their growing opportunities to get physically active, she said.

Dr Nossel said the rapid rise in lifestyle-related diseases posed a growing health burden, and Discovery hoped the index would spark debate about the importance of physical activity for health.

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DISCOVERY VITALITY



Q&A

Gidon Novick

Chief Executive Officer, Discovery Vitality

Vitality has been recognised as one of the most innovative concepts to come from South Africa and Discovery is now exporting this concept to international markets. Why do you think Vitality has become so relevant?

I think Vitality is trying to help solve one of the biggest issues in the world today, and that's the issue of chronic diseases of lifestyle. It is making a significant contribution in this area. Governments cannot afford the persistent increase in healthcare costs. Preventive care and the proactive management of people's lifestyles have become key issues and Vitality is at the forefront of addressing this. It is about creating the right incentives to encourage people to make healthier choices.

What does your competitor landscape look like? Is there any risk that Vitality may lose its appeal to consumers?

This is always a risk and that's why we constantly challenge the way we do things so that the offer to our clients – the incentives that we create to help them to live healthier lives – remain relevant. That is why we are so obsessed with innovation. At the same time, the area of wellness is such a fast-moving space and there are many different entities involved in trying to solve this problem. This is positive and we encourage it. From businesses like us, to governments around the world trying to solve the issues around lifestyle diseases and universities doing research on wellness, we view it as a necessary collaborative effort.

Discovery Vitality

Every 10 seconds a discounted movie is watched at Ster-Kinekor | **Over R5.5 million** is paid in DiscoveryCard cash back every month

"We know that Vitality works incredibly well in the context of an underlying insurance business. That is why Vitality is attracting some of the best insurers around the world who want to partner with us. Our most recent partnership is with the AIA Group in Singapore with the launch of AIA Vitality."



What are the key risks and challenges in managing the Vitality programme? What are you doing to manage and address these risks?

The programme is complex and the decisions that we make have long-term impacts and yet the environment around health and wellness is changing fast. The science is changing fast. Our understanding of the way people respond and react to incentives is changing all the time and that's a tricky thing to manage – to come up with incentives and structures that are really long-term in nature but respond well to a fast-moving external environment. The best way to manage this complexity is to have the smartest team solving these issues, understanding the impact of the interventions that we have and plotting the future of Vitality.

With such a large-scale programme, how do you maintain excellent customer service?

I think there are two dimensions to delivering great customer service. The one is to have great systems, great processes and many different ways customers can interact with us in a slick, effective environment. Whether a customer wants to contact us telephonically, through our website or use one of our mobile apps; these channels must be robust. But at the same time it's our focus on individual members that is most important. On the one hand we look at our metrics, how we're doing in terms of customer service in aggregate; and on the other hand it's about how we deal with each individual customer and the issues they have and understanding that every member is different. It is a balance of those two that helps us focus on our members.

What is Vitality's future business strategy?

Our strategy remains to make people healthier. We are continuously learning about new ways of making people healthier, how people respond to incentives and what really has an impact on health behaviour, risks and status. Vitality is relevant in just about every market in the world because every country in the world has the issue of lifestyle diseases to solve. Therefore a big part of our strategy is to roll out Vitality on a global basis.

Vitality has been very successful for Discovery in terms of engagement, low lapse rates in the Health and Life businesses, customer retention and in managing risk. How do you effectively extend these learnings to a broader population who may not interact with your brand or product?

We know that Vitality works incredibly well in the context of an underlying insurance business. That is why Vitality is attracting some of the best insurers around the world who want to partner with us. Our most recent partnership is with the AIA Group in Singapore with the launch of AIA Vitality. That is one area where we see Vitality having a much broader impact globally than what we currently have. Already we have over five million Vitality members globally and in addition to that, Vitality is creating a platform for the evolution of the science of wellness. We are working with institutions around the world that are using Vitality and the experience and the data that Vitality generates, to evolve the science of wellness.

I also believe that Vitality has a responsibility to society as a whole. Even though we're having a massive impact on our membership base of 5.5 million people around the world, we also have a responsibility to play a positive role in society. We do this by raising awareness and encouraging public debate on the issue of wellness. The Vitality Fittest City Index, which we launched earlier this year, compares metropolitan areas around South Africa and the environment they are creating for people to lead active lifestyles. We're encouraging them to create healthy environments for their residents to live in and adapt their lifestyles. Another initiative that we've been a part of for many years is the Vitality Schools Programme where we are helping schools to create a healthier environment and educate kids on healthy behaviour.

CASE STUDY

DISCOVERY VITALITY



Furthering public debate about health promotion and wellness issues impacting our society

During the year, we worked on bringing together top international experts in health promotion and wellness as part of our commitment to encourage public debate on health issues that impact our society. Hosted in partnership with the Sports Science Institute of South Africa, the Vitality Summit hosted well-known experts in the field of chronic diseases of lifestyle, which is currently regarded as one of the biggest social and economic threats facing modern society. The speakers included: Dr Brian Wansink, John Dyson Professor of Consumer Behaviour at Cornell University; Tyler Hamilton, former professional cyclist and best-selling author; Adrian Gore, CEO of Discovery; Professor Tim Noakes, co-founder of the Sports Science Institute of South Africa; Dr Derek Yach, Senior Vice President of The Vitality Group and Executive Director of the Vitality Institute; and Dan Ariely, James B. Duke Professor of Psychology and Behavioural Economics at Duke University. Over 1 500 delegates attended the Summit, which was held in August 2013.



Participants test their fitness at the 2013 Vitality Summit held in Sandton.



Professor Dan Ariely shares his knowledge of behavioural economics at the Vitality Summit.

KEY FACTS AND PERFORMANCE HIGHLIGHTS

Introduction of new benefits that **offer clients more choice and flexibility** and that increase Discovery Insure's competitiveness

Positive shift in driver behaviour and **lower claims** frequency and severity for engaged drivers

Discovery Insure was recognised by consumers as the **runner-up brand** in the short-term insurance category of the **Sunday Times Top Brand survey**



DISCOVERY INSURE

Our vision

To be an organisation that protects people and their possessions by offering them the most comprehensive and innovative insurance at the lowest long-term cost. We use powerful incentives and telematics technology to reduce risk through improved driving behaviour and advanced safety features, thereby creating great drivers and safer roads for all.

PERFORMANCE HIGHLIGHTS

Annual Premium Income (in force) increased to **R600 million**

New business API of **R366 million** up **53%**

Attracted **10%** of new business written in the **personal lines** insurance market



Key facts about **Discovery Insure**

Launched in May 2011 and has **33 251** policyholders.

Vitalitydrive encourages and rewards better driving behaviour, **as well as vehicle roadworthiness.**

Discovery Insure offers **comprehensive** vehicle, portable possessions and household cover.

Young adults between 18 and 25 can receive further discounts of **up to 25%** on their motor premiums.

Vitalitydrive leverages the behavioural expertise developed over the past decade in the Vitality programme with the **latest telematics** technology in the form of the **DQ-Track** to measure crucial aspects of driving behaviour.

Vitalitydrive provides up to **50% fuel rewards** on clients' monthly BP fuel spend.

Positive shift in driver behaviour leading to lower claims

Driver behaviour shifts positively within 12 months of joining

Lower claim frequency and severity for engaged drivers

PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

DISCOVERY INSURE

Discovery Insure's performance during the past financial year affirmed our view that the business has considerable potential to change the short-term insurance landscape in South Africa.



During the year, we made progress across all areas, including new business growth. We developed our market-leading claims management ability and continued to improve driver behaviour, the result being a continued reduction in our loss ratio.

The business has continued to show great growth potential since its launch two years ago, with mounting evidence of the effectiveness of the behavioural insurance model and opportunities for product linkages across the Discovery product suite. This potential led Discovery to acquire Hollard Insurance Group's 25% share in the Discovery Insure business. Although the transaction was still subject to regulatory approval at the time of writing this report, complete ownership of Discovery Insure will expand the opportunity to develop more innovative products and product integration with other Discovery products.

Key strategy for 2013

Grow our distribution by focusing on potential channels through which to distribute Discovery Insure products; **provide ongoing support and training and use of technology to enhance the sales process.**

Our progress

- We developed a sophisticated portal for financial advisers to fully administer and manage their clients' policies online. This portal enables them to perform fundamental administrative tasks such as adding or removing risks, logging and tracking claims as well as tracking how their clients engage with Vitalitydrive.
- **Our technical marketing team continues to provide ongoing sales support to financial advisers who are new to the product, resulting in the continued expansion of our distribution channel.**
- We have introduced binder agreements for experienced financial advisers, allowing them a greater ability to manage their client base with relevant levels of authority provided.

Key strategy for 2013

A focus on supply-side innovations that **add value and seamless service for clients.**

Our progress

On the back of the success of our Fasttrack claims service that replaces lost portable possession items within 48 hours, we introduced Xpress assessing. All building and content claims will be assessed by a team of experts within 24 hours of a claim being registered, failing which the client's excess will be waived.

Key strategy for 2013

Introduce further safety enhancements that protect clients in high-risk situations.

Our progress

Data on driver behaviour collected through DQ-Track enables us to develop unique driver profiles that can immediately trigger an alert when someone other than the policyholder is driving the vehicle. Discovery Insure can detect if a vehicle has been stolen or hijacked because of the different driver profiles. This ability translates into an added service and safety benefit for clients since Discovery Insure uses this data to immediately contact clients if abnormal driver behaviour is detected.

OUR FOCUS AREAS DURING 2013

DISCOVERY INSURE

South Africa has one of the highest road fatality rates in the world and the magnitude of this critical social problem is illustrated by Discovery Life's claims experience.

In 2012, motor vehicle accidents accounted for one in five deaths on the Discovery Life book. Discovery Insure's vision of creating a nation of great drivers and thus making a positive social impact is therefore particularly relevant. Vitalitydrive, our unique driver behaviour programme, rewards good driving and is key to achieving this vision. It not only measures and changes driving behaviour but also provides unique features that help keep our clients safe. Discovery Insure also offers comprehensive vehicle and home insurance cover.

Our focus areas during 2013

During the past year, our focus has been on further developing the Discovery Insure and Vitalitydrive platform, including our product range, DQ-Track safety features and Vitalitydrive rewards, to provide clients with the best insurance offering in the market. Vitalitydrive, like Vitality, offers unique integration potential with other Discovery businesses. During the year, Discovery Insure worked with Discovery Life to offer an Integrator product that gives Discovery Life policyholders an upfront 10% discount on their life premium if integrated with Vitalitydrive. Annual increases depend on the policyholder's Vitalitydrive status – the higher the status, the better the policyholder's driving behaviour and the less their risk of having a motor vehicle accident, a traditionally high mortality risk for Discovery Life.

FOCUS AREA 1

Enhance our product offering to provide clients with more choice and flexibility.

During the year, we extended the Discovery Insure product range considerably to offer clients more flexibility and choice. We introduced two new plans – the Executive and Essential Plans – that extend our competitive ability in all areas of the short-term insurance market and offers further choice to our clients. The Essential Plan provides a solution for a client looking for comprehensive cover but without some of the added benefits of the Classic Plan at a premium that is approximately 15% to 20% lower than the Classic Plan. The Executive Plan is a new product that offers additional unique benefits and services aimed at high-net-worth clients. In addition, a number of new benefit options were introduced which answer a number of client challenges that exist in the industry following a motor vehicle claim.

These include:

- A write-off accelerator that gives clients the option to write off their vehicles if the damage exceeds 40% or 50% of the retail value; a first for the insurance market
- A car hire extension that increases car hire from 30 days to 60 days to ensure clients are not inconvenienced if the repair process takes more time
- A Retail Value Booster that gives clients 15% above the retail value if their car is stolen or written off
- An Executive Plan allows clients with multiple insured vehicles for one driver, the ability to reduce their premium by covering only one car at a time for accidental damage.

We introduced these new products and benefits to the market during August 2013.

FOCUS AREA 2

Build on the success of Vitalitydrive to reduce road accidents and deaths.

We continued to use Vitalitydrive rewards to encourage better driving behaviour over the long-term. Our data shows that clients change their driving behaviour during the first 12 months after joining Discovery Insure. The number of clients who start off as poor or average drivers reduces by an average of 29% during the first year of membership, while the number of good drivers increases by 36% and the number of excellent drivers surges by 137%. Clients also sustained their improved driving behaviour, demonstrating the long-term positive impact of Vitalitydrive.

Vitalitydrive tracks over
44 000 cars in real time

Over the last 12 months, drivers on the lowest status **improved their driving by an average of 25%**

FOCUS AREA

Manage claims cost and claims loss ratios.

Our data continues to show the positive effect that Vitalitydrive has had on the number of gross claims, as well as on the cost per claim and total claims cost. The programme is helping us to proactively manage our claims loss ratio to achieve targets. Our data shows that good drivers claim half as much as below-average drivers by having fewer and smaller accidents. In addition to the positive impact of Vitalitydrive, we also continued to build our claims infrastructure to optimise the claims process and reduce our loss ratio sustainably.

3

FOCUS AREA

Enhance our claims system and processes to ensure each client experiences excellent customer service.

During the year, we completed the development of key claims processes and a new claims system to enhance operational efficiency. The new system has resulted in service level improvements across all touch points.

4

Strategic priorities for 2014

Gain ubiquitous awareness of the BP fuel benefit – 50% off fuel if you drive well – through above-the-line marketing and other actions.

Deliver powerful new business growth.

Manage loss ratios within the business expectations.

Create a step-change in service quality throughout the service chain.

Clients who join Vitalitydrive have the option of installing DQ-Track in their cars at no extra cost. DQ-Track uses the latest telematics technology, including three-dimensional accelerometers, GPS functionality and GSM capabilities to relay vehicle diagnostics to Discovery Insure. This enables us to measure driving behaviour and provides clients with a range of unique safety features.

Q&A: Anton Ossip

R25 billion
The amount of cover for buildings and households

R31 million
The amount clients have accumulated through the Excess Funder Accounts, an additional facility that lets clients bank their BP fuel cash back to pay for future excess amounts



Q&A

Anton Ossip

Chief Executive Officer, Discovery Insure

How has Discovery Insure performed during the past year?

Discovery Insure has performed exceptionally well during the past year. We continued to develop our service platform, and at the same time almost doubled the number of in-force clients, bringing the total number to more than 33 000 with in-force annual premium income reaching R600 million. All aspects of the business are going according to plan with strong new business, greater awareness of our offering in the market and the continued efficacy of our driver behaviour model.

What are the key risks for Discovery Insure?

As an insurer we are subject to a number of risks – higher incidents of accidents and thefts and worsening weather conditions to name a few. The difference with Discovery Insure is that we are actively involved in protecting our clients from these risks and not only dealing with the consequences. We take a proactive and not only reactive approach to managing risk.

Discovery Insure was one of the first adopters of telematics technology; how do you view your competitors and how will you maintain your competitive advantage?

Many insurers around the world have started piloting and developing telematics programmes and it is likely that the same will eventually happen in South Africa. We have developed a strong skill in understanding telematics and how to apply it to insurance and risk management. Much of this builds on what we have learnt from Vitality over the past decade.

How do you use partnerships to add value to the client offering?

Partnerships are very important as they combine various skills in the offering. At Discovery Insure, we have partnered with a number of companies to make the client journey an exceptional experience. We believe in building long-term, sustainable partnerships that are beneficial to all parties, especially our clients.

Your product is designed on the belief that driver behaviour can be changed. From your experience over the past two years, do you believe this can be achieved?

Definitely – in just two years we have collected meaningful evidence of behaviour change. If clients understand what it means to be a better driver with frequent and clear communication, the necessary tools and appropriate rewards, we are confident that good driving is within everyone's grasp.

Discovery Insure

The amount paid to **Vitalitydrive** clients
R62 million
in fuel rewards

R8 billion
The amount of **cover for clients' vehicles**

Drivers on the higher driver status have **34% fewer claims** than average or poor drivers (as measured by Vitalitydrive)

"The entire Vitalitydrive programme is designed around **incentivising good driving and therefore lowering the rate of accidents**. A remarkable statistic we have recorded is that our client base experiences a rate of fatalities that is one-third of the market average, proof that we are making clients safer."

Your vision is to make clients safer. How does this translate into practice? What are the results of the model?

A big focus is on driver safety. The entire Vitalitydrive programme is designed around incentivising good driving and therefore lowering the rate of accidents. A remarkable statistic we have recorded is that our client base experiences a rate of fatalities that is one-third of the market average, proof that we are making clients safer. In addition to driver safety, our product provides features that reduce the risk of theft and improve the chance of finding a stolen vehicle.

The value of an insurer is often judged by consumers when a claims event takes place. What is Discovery Insure doing to ensure clients experience a hassle-free claims experience?

We have invested significantly in technology to improve the claims journey. Frequent client feedback is a crucial part of the process. Features such as Fasttrack claims and Xpress assessing contribute to making the claims process easier and more convenient.

You recently launched new and innovative benefits to your clients; how do you continue to innovate in such a competitive industry?

As we continue to interact with our clients, we find that there are numerous innovations to be made in the industry. A number of innovations challenge conventional thinking in insurance and are designed to improve the customer journey and experience. We recently introduced the Write-off Accelerator, an industry-first benefit that allows the client to choose a lower level of damage at which a vehicle will be considered written off. This alleviates the repair concerns of vehicle performance and resale value.

How do you see Discovery Insure's future growth in relation to the big industry players?

We believe that with a product as differentiated as ours, and as consumers get to know about the value they could be getting by driving well, the potential is enormous. We fully appreciate that we operate in a competitive industry and this is all the more reason why successful insurers need to offer true innovation that adds value to their customers.

The short-term insurance industry is notorious for poor customer service delivery. What is Discovery Insure doing to deliver service that stands out from competitors?

We are obsessed with measuring all aspects of the service chain and working hard to ensure that every client interaction is exceptional. There is no excuse for anything but that. As a business we are not perfect but we are driven to constantly improve. There are many measures and incentives in place to ensure that in the short-term we will achieve our goal of offering our clients exceptional service in all areas.

Insurance policies are known to have much small print that clients only get to understand when they claim. What is Discovery Insure's approach to this?

We develop marketing material in plain language that makes it clear how a policy works. This serves both our clients' interests and ours. We also go to great lengths to educate financial advisers in all our distribution channels on important aspects to be aware of. All our client service employees are accredited in terms of FAIS legislation and trained to give appropriate advice.

How sustainable is Vitalitydrive in terms of Discovery Insure's profit potential?

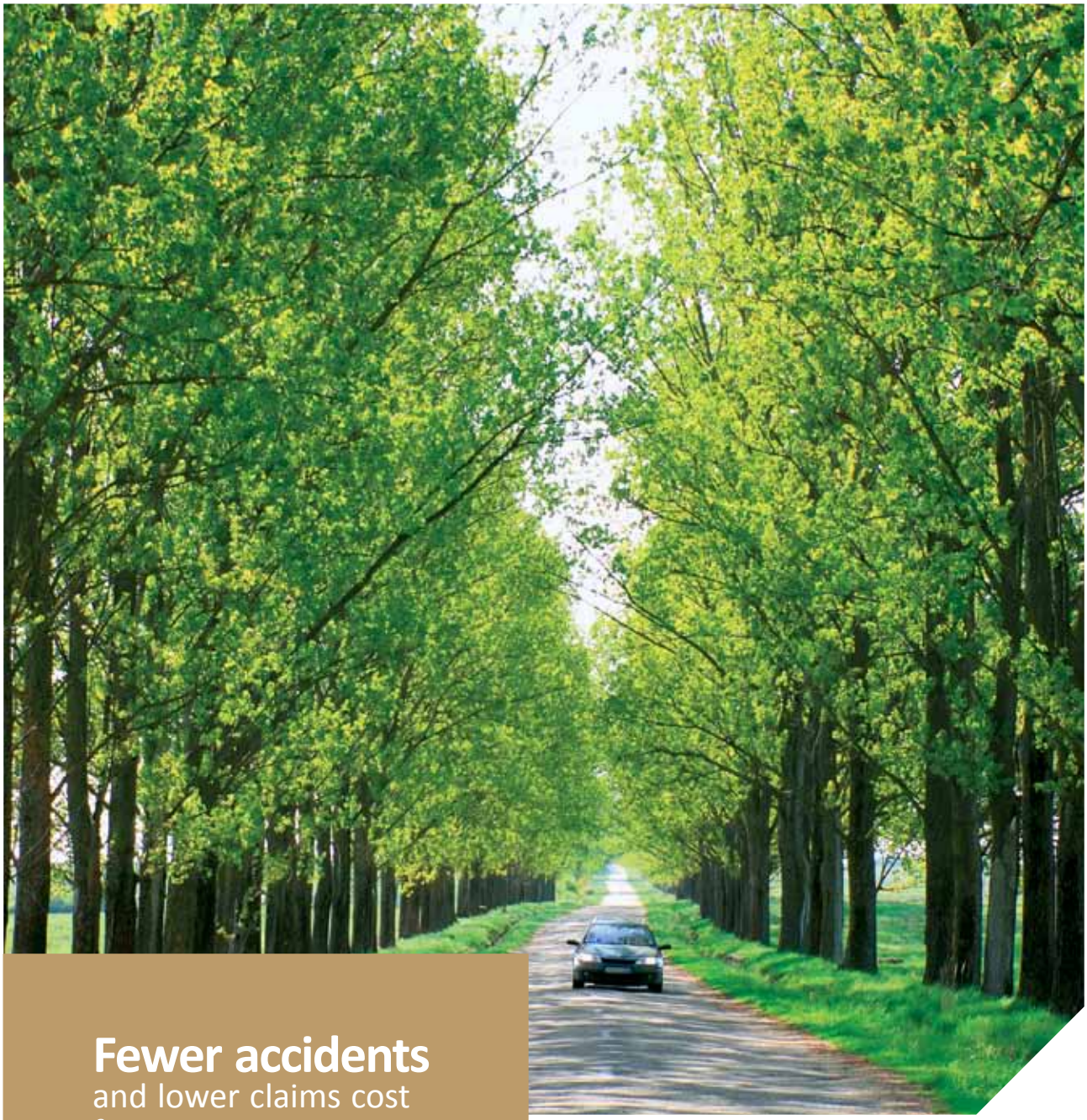
The Vitalitydrive model is very sustainable as it ultimately rewards clients that drive well for their lower insurance risk. It gives us the unique ability to better understand risk and build in proactive measures that benefit both the client and Discovery Insure.

Last year, the short-term insurance industry took a huge knock with unpredictable hail storms in October. What are your views on the impact of climate change in the insurance industry? How do you manage this risk?

Climate change is a huge area of uncertainty and risk for insurers, but we also view it as an opportunity to continuously innovate and differentiate ourselves for the benefit of our clients. One initiative we introduced is real-time weather alerts. We closely monitor weather patterns and predictions and once we know that there is a high chance of adverse weather, we alert our clients who are based in that area. This helped clients stay out of the way of one of the largest hailstorms last year.

CASE STUDY

DISCOVERY INSURE



Fewer accidents
and lower claims cost for Discovery Insure

Analysis of our data shows that the number of claims good and excellent drivers experience is 34% less than that of poor and average drivers. Similarly, the cost of claims for good and excellent drivers is 19% lower than that of poor and average drivers. The combined effect is an overall decrease of 46% in the cost of claims.

Discovery Insure

Telematics – the insurance industry game changer

South African short-term insurers are under pressure. The combined net underwriting margins of the largest insurers with a collective market share of over 60%, deteriorated during 2012. This means that there is a downward trend in the total loss and expense ratio compared with the amount of premium written. Factors that contribute to this trend are: the impact of catastrophic weather events; the higher average cost of car parts – the largest cost contributor; and increased competition from direct insurers who are causing a downward pressure on premiums as companies compete for market share.

In addition, the cost of regulatory compliance is increasing with the introduction of SAM (Solvency Assessment and Management Framework) and other legislative initiatives such as IFRS4 accounting standards and Treating Customers Fairly. For consumers, a difficult economic environment means less disposable income, with food, electricity and petrol inflation outstripping salary increases.

In the absence of value and innovation, consumers will base their insurance purchase decisions solely on price. However, without value-creating mechanisms, insurers will be forced to increase premiums, reduce benefits or develop other internal cost-saving initiatives to improve their financial results.

Telematics is the latest technology with immense potential for insurers to offer consumers better value and, at the same time, contain costs. It enables accurate risk assessment as insurers can charge appropriate premiums for the risk component that is within a client's control. This is because telematics technology gives clients the opportunity to understand individual driving behaviour – the fundamental risk in motor vehicle insurance. By monitoring diagnostics such as the longitudinal and latitudinal forces acting on a vehicle, telematics devices can accurately measure the extent to which a driver's actions will increase the risk of an accident.

Using telematics technology to accurately measure risk can help insurers differentiate their prices. Whereas traditional insurers use static risk factors such as gender and age to rate risk, being able to measure driver behaviour immediately provides a far more accurate risk-rating factor for insurance models. This results in more equitable premiums that are based on the actual likelihood of claiming. Incorporating incentives to improve behaviour also means that clients can reduce their premiums by driving better.

Telematics technology has the added advantage of enhancing safety benefits: it provides the big data solution for insurers to better assess situations where clients may need help. It means that insurers are able to respond to accidents quicker and dispatch emergency medical personnel to an accident scene. It also allows insurers to use location data to alert customers to severe weather conditions.

Telematics makes insurance tangible for the consumer in an entirely new way, increasing the potential for better risk management and more consumer touch points. Motor insurers and financial advisers will gain access to richer individual and collective data than the sector has ever known.

KEY FACTS AND PERFORMANCE HIGHLIGHTS

Operating profit (excluding Transactional Services Agreement) up **23%** to

R270 million

Launch of the **Vitality Advisory Board,** a sub-committee of the PruHealth and PruProtect Board, aimed at contributing to the ongoing strategic development of Vitality in the UK



PRUHEALTH

Our vision

To build the best protection business in the UK based on the integrated Discovery business model, manifesting in a number three market position for both health and protection, and a high-quality, profitable membership base with excellent actuarial dynamics.

PERFORMANCE HIGHLIGHTS

New business API increased **54%** to
R929 million

Continued improvement in lapse rates, at around **25% below industry levels**

One of the lowest loss ratios in the industry, at **12% lower than the industry average**



Key facts about **PruHealth**

Launched in April 2004, **PruHealth is the fourth-largest Private Medical Insurer (PMI) in the UK** and the only one that integrates a comprehensive wellness solution within its health insurance product construct. This differentiated approach has resulted in a product proposition that **provides value** to all members, not only those who need to make a medical claim.

PruHealth has an approximate 9.5% overall market share, covering almost **555 000 lives.** The business model and its approach to the market has resulted in a disproportionate share of the more profitable individual and Small Medium Enterprise (SME) markets.

PruHealth's ongoing focus on **quality of business,** coupled with the positive effects of Vitality engagement, has resulted in a best-in-class portfolio with some of the **lowest loss ratio and lapse rates in the industry.** Importantly, actuarial dynamics continue to show ongoing positive improvement.

PruHealth's product and service innovation continues to resonate strongly with financial advisers and consumers. PruHealth has **won several awards,** including Best PMI Provider and Best Online Intermediary Service at the 2012 Health Insurance Awards, as well as Best Group PMI Provider at the **2012 Cover Excellence Awards.**

PERFORMANCE AGAINST KEY STRATEGIES 2013

PRUHEALTH

PruHealth continued to deliver an excellent performance during the past financial year with a 23% increase in operating profit, excluding TSA, and a 24% increase in embedded value. Most important is the increase in profitable individual new business received in terms of low lapses and loss ratios.

Key strategy for 2013

Enhance margins, quality and profitability **through a continued focus on writing high-quality individual and SME business.**

V

Our progress

- New business API of R929 million, an increase of 54% from the previous year.
- **Sales to individuals and SMEs comprised 89% to total new business over the year.**

Key strategy for 2013

Maintain our leadership position in integrated health and wellness solutions, including the continued rollout of Vitality to the Standard Life Healthcare member base, as well as a continued focus on enhancing the Vitality offering.

V

Our progress

- Vitality Advisory Board was launched and the inaugural meeting held in London in July 2013.
- Launch of the Vitality Ambassador programme, with well-known UK sport personalities Lord Sebastian Coe, Jessica Ennis and Jonny Wilkinson serving as Vitality Ambassadors.
- We made enhancements to the Vitality offering, including 50% off bicycles, free weekly cinema tickets and cash back for non-smokers. These have been highly successful in encouraging increased levels of engagement.

Key strategy for 2013

Extend the PruHealth product proposition through the launch of highly-differentiated benefits that expand the PMI landscape.

V

Our progress

PruHealth's PMI benefit offering was enhanced to offer industry-first coverage in the areas of bariatric surgery, non-elective cosmetic surgery for specific conditions, and assistance at home following hospitalisation.



PruHealth is one of the leading PMI providers in the UK. It offers a differentiated product that focuses on providing wellness interventions through Vitality and healthcare benefits.

This integrated approach serves a dual purpose: providing members with enhanced value compared to traditional PMI policies, as well as institutionalising a comprehensive approach to tackle one of today's most pressing social problems – the epidemic of chronic diseases of lifestyle.

From a market perspective, the UK PMI industry is highly complex, offering supplementary care to the care provided by the National Health Service (NHS). This dynamic means that the PMI market is highly susceptible to economic cycles, with a recessionary environment negatively impacting growth in the PMI market. This was evidenced by the approximate 10% shrinkage of the market in the period following the financial crisis. The volume of demand for private medical cover in the UK moved marginally higher in 2012, increasing by 1.1% to reach a total of 4 033 000 subscribers at the end of the year.

Our focus areas during 2013

The key areas of focus for PruHealth during the past year have been the consolidation of various initiatives and strategies to create a market-leading platform from which to accelerate growth. Much of our emphasis lies in creating additional value through innovative products and benefits; our focus on comprehensive and integrated wellness; and the extension of cover into previously uncovered areas of the market.

FOCUS AREA 1

Reversing the trend of cost containment to offer consumers more value.

Healthcare in the UK is mostly accessed through the NHS, with some individual consumers and corporates choosing to purchase a PMI product. The voluntary nature of the PMI purchase means that PMI providers must offer additional value to consumers who can easily revert to the NHS if their PMI product is perceived to not offer enough protection and value. Our focus has been on reversing the trend of typical cost containment measures – exclusions, restricted network cover and limited follow-up care – to provide extended cover, higher payouts and product innovation that offers additional value for consumers. An example of this approach is the Full Refund promise for consultant fees, resulting in zero shortfalls for our members. We have also introduced the Lifestyle Surgeries and Home Assistance Benefits that extend members' cover. Both are industry firsts in the UK.

PRUHEALTH

FOCUS AREA

Encouraging Vitality engagement with the launch of new Vitality benefits.

Traditional PMI benefit design typically only benefits the sickest members of the population – around 20% – who then consume approximately 80% of healthcare costs. We address this gap through Vitality; using powerful incentives and behavioural tools to engage people in their PMI policy, regardless of their claims level and state of health. One of our key ongoing strategies is to further develop the Vitality offering and its thought leadership position in the UK. An important step in this has been the full integration of our core PMI policy and Vitality – a move to accelerate sustained health behaviour change and positively impact healthcare outcomes. In addition, we have focused on two major lifestyle risks in the UK today by introducing a Non-Smoker Cash Back, which rewards people with cash back on their premium for not smoking, and a Coordinated Obesity Management Programme, which combines wellness, dietary, psychological and surgical interventions to control obesity.

During the year, we also saw a steady increase in how our members use wellness benefits and other rewards. New gym membership and HealthyFood activations for the first six months of the 2013 calendar year measured 15 000 and 7 000 members respectively. We also completed work on Vitality product enhancements, which were launched to the UK market in October this year. These enhancements are aimed at improving access to lifestyle and wellness partners, for example, through a device agnostic physical activity platform, as well as a series of new rewards partners.

FOCUS AREA

Further develop the thought leadership of Vitality in the UK.

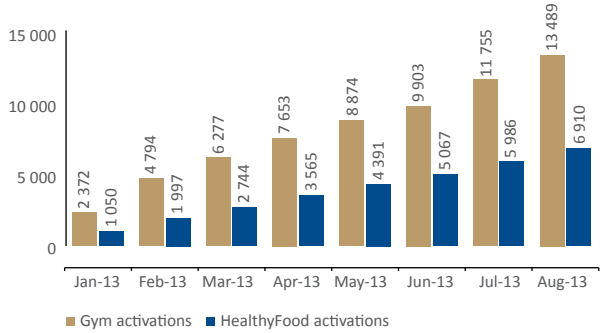
Internationally, Vitality is gaining recognition for its thought leadership in wellness and health promotion, its ability to change people's behaviour and the role it plays in structurally changing insurance systems. During the past year, we concentrated on building awareness of Vitality in the UK market with the appointment of prominent British sport personalities as Vitality Ambassadors.

We also sought to bolster the strategic development of the Vitality programme through the Vitality Advisory Board, a sub-committee of the PruHealth and PruProtect Boards. The Vitality Advisory Board's role is to develop Vitality further in the area of partner and network development and consumer and corporate engagement, as well as to help steer the public policy debate around the importance of preventive health and wellness.



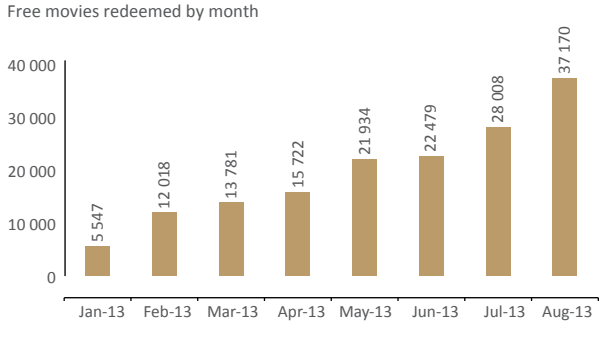
Strong growth in wellness benefit utilisation

Cumulative new activations: CY2013



Resonance of new reward benefits: Free cinema usage

Free movies redeemed by month



42 000 Personal Health Reviews have been completed online

Vitality members in the UK earned over **19 million** **Vitality points** during the past year

Vitality members have made **600 000 gym visits** and around **1 300 members** are joining Virgin Active gyms with Vitality every month

50 000 **Vitality members** have registered on the new PruHealth Member Zone

FOCUS AREA

Investing in new technology to improve operating efficiency.

An important area of focus for PruHealth has been an investment in technology to improve operational efficiency. We invested £23 million to enhance our administration and claims systems and to build PruHealth's digital platforms. The enhancements include improvements to our claims system that enable us to use Discovery Health's big data analytics capability to strengthen our risk management capabilities, as well as enhancements to our digital platforms that provide a customised pre-sales web journey, and mobile and social media platforms.

4

Strategic priorities for 2014

Entrench our new approach to the provision of PMI to increase value and provide a differentiated experience for our members.

Be the smartest users of data, resulting in practical business applications that improve the customer journey.

Develop new online tools that make it easy for our clients and healthcare professionals to engage with us in a transactional capacity.

Collaborate with healthcare professionals to provide our members with ongoing access to the most experienced consultants on a sustainable basis.

FOCUS AREA

A focus on improved service and experience.

During the year, we completed the transfer of our servicing operation from South Africa to the UK. Our customers now have all claims, servicing enquiries and Vitality support actioned by a UK-based team. We also introduced a dedicated distribution services division with a number of operations integrated to offer clients seamless service. Initial results from the new service model have been very positive – lapse rates continue to decrease and client complaints have been reduced by half. Member ratings of our service continue to improve: the highest-ever rating from brokers was given to the new Partner Services team that provides premier servicing for the 17 largest brokers.

5



CASE STUDY

PRUHEALTH



Britain's Healthiest Company

In 2012, **PruHealth launched Britain's Healthiest Company, the first initiative in the UK** aimed at understanding the health status of Britain's workers and the largest survey of workplace wellness in the UK.

In June this year, we announced the results of the companies that performed best in the survey as well as key findings from the survey. An overall winner was chosen as well as winners in four sub-categories: Most Active, Healthiest Active, Most Smoke-Free and Most Healthy Workplace. Quintiles, a clinical research company, was awarded the overall Healthiest Company in the large-sized category, while adidas (UK) Ltd won the highest accolade in the mid-sized category.

Key findings from the survey include:

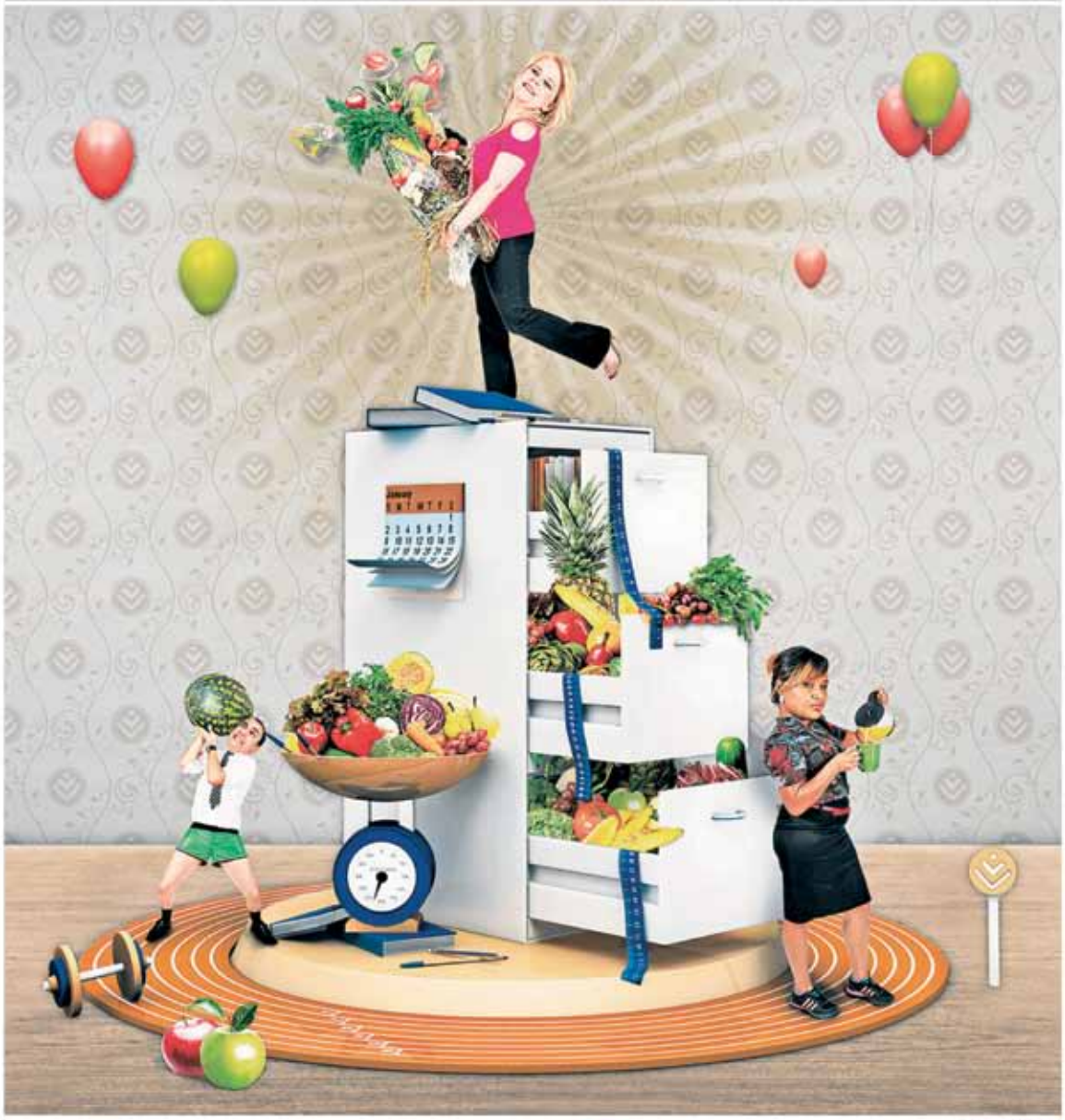
- 86% of respondents have a Vitality Age higher than their actual age, with an average difference of 4.1 years
- Body mass index (BMI) and physical activity were the lifestyle risk factors with the fewest employees in the healthy range
- 87% of respondents have at least one lifestyle or clinical risk factor outside of the healthy range and 11.5% had four or more risk factors outside the healthy range
- 14% reported having a chronic condition of lifestyle, with the most prevalent being high blood pressure and depression.

We are currently in the process of finalising a partnership with Cambridge University and the RAND Corporation to administer Britain's Healthiest Company in the future.

BRITAIN'S

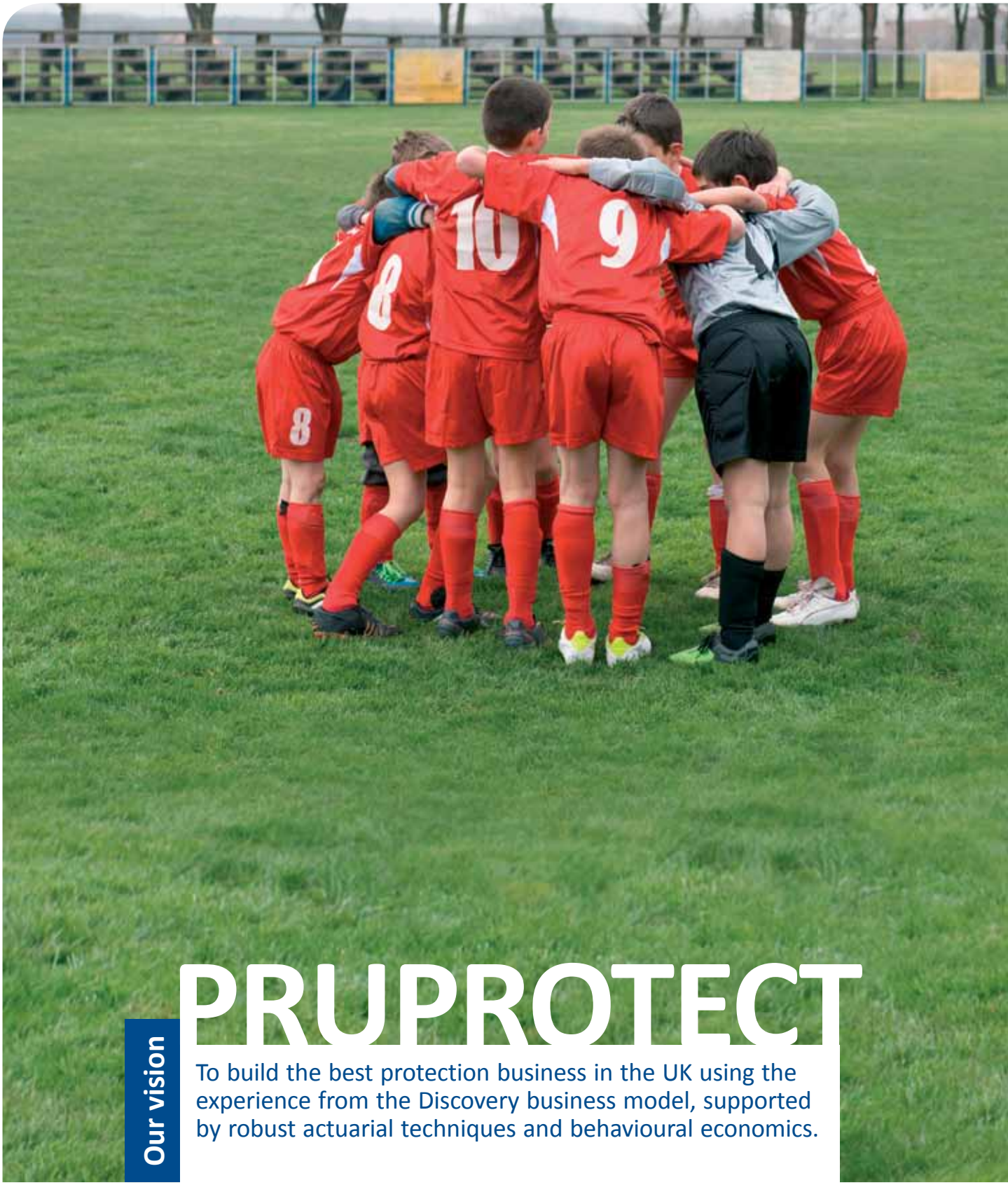
HEALTHIEST COMPANY

The winners in our search for organisations with an outstanding approach to employee health and well-being



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In association with PRUHEALTH MERCER BRITAIN'S HEALTHIEST COMPANY



Our vision

PRUPROTECT

To build the best protection business in the UK using the experience from the Discovery business model, supported by robust actuarial techniques and behavioural economics.

PERFORMANCE HIGHLIGHTS

Operating profit up by **56%** to
R326 million

New business API increased by **40%** to
R644 million

In-force premiums up **46%** at
R1 412 million



Key facts about **PruProtect**

PruProtect was launched in **2007** and markets consumer-engaged protection products to the UK market.

PruProtect has received significant industry recognition, including:

- The Protection Review Innovation Award in 2012
- Financial Adviser Service Awards in 2012
- Award for the best Income Protection Stand-Alone Product in 2012 by Mortgage Strategy Awards
- Best Critical Illness Provider Awards each year from 2009 to 2012 at the Health Insurance Awards
- Since 2007 we have been awarded the Defaqto five-star rating for our Serious Illness Cover and Income Protection Cover.

Currently the fourth-largest writer of **protection** business in the UK in the independent financial adviser segment.

Number of policyholders:
153 671
up 40% from the previous year.

PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

PRUPROTECT



PruProtect experienced a **56% increase in operating profit** to R326 million as well as an increase in new business API – up 40% to R644 million.

The business also saw better-than-expected claims and lapse experience and a 40% increase in in-force policies. The value of in-force business increased by 93% to R702 million (Discovery's 75%). While increased new business was partly driven by legislative factors such as the EU Gender Directive and changes to the tax regime, additional factors contributed to the improved performance, including quality of new business mix; higher average premiums; a reduction in reinsurance rates on life and serious illness cover following sustained positive claims experience; growth in our distribution model as well as more favourable economic assumptions.

Key strategy for 2013

Support holistic financial planning **through continued growth in the franchise footprint while increasing market share in the independent financial adviser space.**

Our progress

Various marketing and support tools were launched for financial advisers.

- **The PruProtect Connect tool supports financial advisers with strong sales and marketing initiatives.**
- The new iPad app that allows financial advisers to view a simple summary of their clients' plans and options to help advisers determine the best cover levels and products to meet their clients' needs.

Key strategy for 2013

Access opportunities to further strengthen distribution through leveraging and developing strategic partnerships with networks, banks and funds platforms.

Our progress

We have increased the number of distribution franchises to 18 with the vast majority writing more than GBP 100 000 worth of **new business** every month.

Key strategy for 2013

Leverage Vitality capabilities to **further differentiate product offerings.**

Our progress

- A marketing campaign was introduced during the year to increase awareness of the Vitality offering.
- **We have revised the remuneration structure for financial advisers in terms of selling the Vitality plans to clients.**
- We worked on enhancing our product offering by embedding Vitality in the protection offering.

Key strategy for 2013

Continued provision of differentiated product and service propositions that meet consumers' needs in a changing regulatory landscape.

Our progress

- Launched an enhanced Income Protection Benefit that integrates with the NHS doctor benefit scheme.
- **Cover Booster was launched, which provides free life cover to eligible policyholders.**
- Special offer introduced to the market that makes serious illness cover free for children on a policy.

OUR FOCUS AREAS DURING 2013

PRUPROTECT



The protection market in the UK is traditionally a highly commoditised, price-sensitive market where innovation is stifled at the cost of competing on price. This results in less focus on meeting customer needs throughout a person's life.

The onset of new digital and mobile technology has also resulted in an increase of online price comparison portals, an industry trend that in many respects is detrimental to meeting genuine customer needs as financial advisers shift their focus from customer needs to scale. A report from The Syndicate, a research initiative focused on the UK life and pensions industry, shows that consumers are becoming more confused and lack clear guidance when it comes to their savings and insurance.[1] The current economic climate is impacting on how consumers react and behave in their financial purchase decisions, highlighting the need for sound financial advice. Against this background, PruProtect's business model of offering comprehensive personal and business protection products with additional value gained through engagement with Vitality, is proving highly relevant.

1 http://www.protectionreview.co.uk/events/event/the_syndicate_press_release_october_2011: a survey of over 3 000 adults in the UK and their perception of savings and insurance

FOCUS AREA 1

Support holistic financial planning through continued growth in the franchise footprint while increasing market share in the independent adviser space.

- During the year, we completed the development of a new underwriting system that enables automated underwriting, quicker turn-around times and feedback to financial advisers. Between 60% and 70% of new business is currently being submitted via the new system, with positive feedback from financial advisers. In addition, we launched various marketing and support tools for financial advisers.
- The PruProtect Connect tool supports financial advisers with strong sales and marketing initiatives by letting them choose a variety of email templates which can be personalised with the broker firm's logo and brand. It allows them to upload their client data and produce targeted marketing campaigns to highlight the need for protection products to their clients. The tool also enables advisers to analyse in real time the outcomes of campaigns.
- We also introduced a new iPad app for financial advisers who are either new to protection or the PruProtect proposition. The app provides a simple summary of plan details and options that advisers can use or help them to determine the cover levels and products to recommend to their clients. These enhancements are all aimed at addressing the need for high-quality financial advice in the protection market.

58% of UK adults had to abandon their plans to save in the current economic climate to **focus on other monthly expenses**

50% of UK adults view life insurance as the **most important** type of insurance, but **80%** of respondents **could not describe** how a **basic life insurance policy works**

Up to 75% of UK adults are less likely **to cancel an insurance policy** if their **loyalty was rewarded**

FOCUS AREA

Access opportunities to further strengthen distribution through leveraging and developing strategic partnerships with networks, banks and funds platforms.

2

PruProtect has 18 financial adviser franchises across the UK with the majority writing more than £100 000 of new business each month and contributing to over 70% of total sales. In total, we have 196 account managers who service these franchises. PruProtect also has a panel representative on all networks in the UK and the objective is to increase our market share through these significant distributors.

3

FOCUS AREA

Leverage Vitality capabilities to further differentiate product offerings.

- During the year, we developed the Vitality Optimiser product that replaces the Accelerator Benefit. The new product has a greater focus on health and wellness as it incorporates Vitality Plus into the core protection offering. We have simplified the premium structure with an upfront premium discount and subsequent premium adjustments that are based on the client's Vitality status. Vitality Plus Benefits include an annual cash back which will double for clients who have both a PruProtect and PruHealth policy. The initial market receptivity to the product has been very positive.
- We have also completed work during the financial year on an enhanced serious illness cover benefit that increases some of the current conditions covered by the benefit. It provides a booster option to increase the benefit resulting in a payout rate for certain conditions of up to 200%. This benefit enhancement was launched to the market during September 2013.

4

FOCUS AREA

Continued provision of differentiated product and service propositions that meet consumers' needs in a changing regulatory landscape.

- PruProtect launched a number of product benefits which include an enhanced Income Protection Benefit that integrates with the NHS doctor benefit scheme. The NHS has a structured sick pay for doctors, which increases each year during the first five years of employment. Should they become ill, injured or disabled and unable to work, they receive full pay for a limited number of months, followed by half pay for a limited time. Advisers may therefore need to produce new quotes, and potentially issue new policies, with new deferred periods, every year. However, this new cover has been designed to automatically change in line with the NHS sick pay structure. This option means payments will automatically tie in with the doctor's NHS sick pay structure, avoiding the potential need to make regular manual changes to the client's policy while meeting the client's specific needs.
- We also launched a cover booster product that provides free life cover to eligible policyholders, and a special offer that makes serious illness cover free for children on a policy.

Strategic priorities for 2014

Grow our market share to be the third-largest protection insurer in the intermediary market.

Launch and roll out new product features that will enhance the integration potential between Vitality and the protection benefits.

Introduce benefit enhancements to the Serious Illness Cover Benefit to reaffirm our market leading proposition.



THE VITALITY GROUP

Our vision

To entrench Vitality as a best-in-class wellness provider and the provider of choice for American corporates.

Vitality has gained high levels of recognition among some of the largest Employee Benefit Consulting Houses in the US.
Industry surveys recognise Vitality as a best-in-breed wellness vendor in the large employer group market

Vitality recognised as the **gold standard in corporate wellness solutions** by the World Economic Forum

Combined membership of **The Vitality Group and HumanaVitality:**
3 196 598



Key facts about The Vitality Group

The Vitality Group was launched in 2007 and offers a stand-alone version of the Vitality programme to self-insured, large employer groups and to members of **Humana Inc, a large national healthcare insurer.**

The direct business is written through The Vitality Group LLC, owned 75% by Discovery and 25% by Humana. The Humana-related business is written through HumanaVitality, owned 25% by Discovery and 75% by Humana.

The Vitality Institute was launched in the US in 2013. Founded by Discovery as part of its commitment to health promotion and wellness programmes that advance social good, the Institute aims to advance knowledge about the evolving science of prevention and health promotion.

PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

THE VITALITY GROUP



Key strategy for 2013

Drive engagement **levels in Vitality.**

Our progress

Engagement levels from members of The Vitality Group continue to be well above industry norms.

Key strategy for 2013

Leverage the thought leadership of **Vitality in the US market.**

Our progress

We launched the Vitality Institute in New York, US, in May 2013.

Key strategy for 2013

Continued product **development and innovation.**

Our progress

- A HealthyFood Benefit modelled on the South African experience was launched with Walmart this year.
- **Various engagement tools were added to the programme.**
- Significant advances were made in providing connectivity to a wide range of devices to track physical activity.

Key strategy for 2013

Build up social networking tools and further mobile device generation.

Our progress

Launch of a new smartphone app aimed at improving the member experience, increasing engagement and differentiating Vitality in the market.

Workplace wellness programmes are increasingly recognised as a means of reducing the impact of chronic diseases of lifestyle on individuals and organisations.

In the US, the Affordable Care Act formalises the conditions of workplace wellness programmes and classifies it into two categories – participatory wellness programmes and health-contingent wellness programmes. The regulations support well-designed workplace wellness programmes to continue motivating people to adopt healthier behaviours. With the rising cost of healthcare and increasing prevalence of non-communicable diseases, employers are looking for wellness programmes focused on verifiable and proven solutions. Within this environment, The Vitality Group is playing an increasingly important role in offering a robust wellness solution to American employers.

1

FOCUS AREA

Drive engagement levels in Vitality.

During the past year, engagement levels of The Vitality Group members in the Vitality programme improved significantly with an approximately 20% increase in the number of average member activities. The increase in engagement follows the rollout of Vitality Squares, enhancements in the HealthyFood Benefit, an increase in member communication campaigns and an increase in members using fitness devices to track and measure their fitness levels.

Vitality published research that shows that if physical inactivity, low fruit and vegetable intake, smoking, obesity, hypertension, hypercholesterolemia and alcohol abuse were lowered to their theoretical minimum, the average annual healthcare costs per working adult would be reduced by 18.4%.

Research reported in The Lancet in January 2013 indicates that a few risk factors – tobacco use, an unhealthy diet, lack of physical activity, mental ill health and poor adherence to treatment – account for the vast majority of preventable chronic disease.

FOCUS AREA

Continued product development and innovation.

Continuous product development and enhancements to the current rewards structure remain key focus areas for The Vitality Group. We launched a HealthyFood Benefit with Walmart this year and added various other tools and product enhancements throughout the year.

2

THE VITALITY GROUP

3

FOCUS AREA

Leverage the thought leadership of Vitality in the US market.

In May this year, we launched the Vitality Institute in New York, US, to advance knowledge about the evolving science and art of disease prevention and health promotion to build healthier societies. The Institute brings together some of the world's leading experts and practitioners in wellness and disease management in a large-scale collaboration to positively impact public debate around health promotion.

Some of the foremost experts and leaders in wellness will be part of The Vitality Institute Commission. The Commission will focus on healthcare policies and actions in the US, as well as on chronic diseases, mental health and related determinants that drive the burden of disease and associated costs. The Commission's work will extend beyond the prevention provisions of the Affordable Care Act and related programmes within federal, state and local government structures to identify multi-stakeholder solutions to non-communicable diseases.

The launch of The Vitality Institute comes at a time when chronic lifestyle diseases are severely impacting morbidity and mortality risk globally. The economic costs associated with ill-health and a loss of productivity in the workplace continue to soar, placing further pressure on governments and policymakers to find solutions to the escalating problem. Overwhelming evidence that lifestyle diseases are a fundamental contributor to mortality and sickness, and that they can be controlled, has prompted a growing global policy movement towards wellness. At the core of healthcare reform, particularly in the US, will be the ability to influence behaviour and improve people's health, reducing the risk of mortality and reducing healthcare costs.

www.thevitalityinstitute.org

Strategic priorities for 2014

Focus on building scale in the US market.

Implement a powerful strategy to rapidly increase engagement levels with the Vitality programme members.

Build up the thought leadership of Vitality through the various research initiatives of the Vitality Institute.

Provide a ready-made wellness solution that assists employers in ensuring compliance with the Affordable Care Act.

4

FOCUS AREA

Build out social networking tools and further mobile device generation.

During the year, we released a new smartphone app that is rich in features and functionality, and aims to improve the member's experience and engagement in Vitality. It enables members to complete a Vitality Health Review on their phones, submit events for points and even "check-in" with their phones at a gym. Members can earn Vitality points based on the GPS location of the phone.

BUSINESS DAY (Late Final)
24 May 2013, p.6

New Discovery body to research lifestyle diseases

TAMAR KAHN
Science and Health Editor

CAPE TOWN — Health and life insurer Discovery on Tuesday launched the Vitality Institute in New York to conduct scientific research to guide both private sector and government attempts to prevent lifestyle-related disease.

There is growing global concern over the threat of non-communicable diseases, which will cause an estimated cumulative output loss of $47-trillion over the next 20 years, according to the Global Charter for Healthy Living released at the World Economic Forum this year.

At the same time, there is growing awareness of the benefits of preventing diseases before they manifest. But while much is known about the lifestyle factors that influence health, from diet to exercise, a lot still has to be discovered about how to persuade the public to change their behaviour, the institute's executive director Derek Yach said yesterday.

"The institute will try to develop better interventions for preventing disease globally. Since Discovery is the main supporter, we are looking at the big markets where it is present — SA, the US, China and the UK," he said.

The institute had established a commission to investigate how to get health prevention higher on the US political agenda, and would also being doing work on obesity, diabetes and tobacco worldwide.

Discovery pioneered the use of incentives to encourage healthier choices among members of the medical schemes it administers in SA, with a programme called Vitality.

The body has published research showing that people who get involved with the programme have lower health bills than people who do not, which translates into savings for the scheme or health insurance company they belong to.

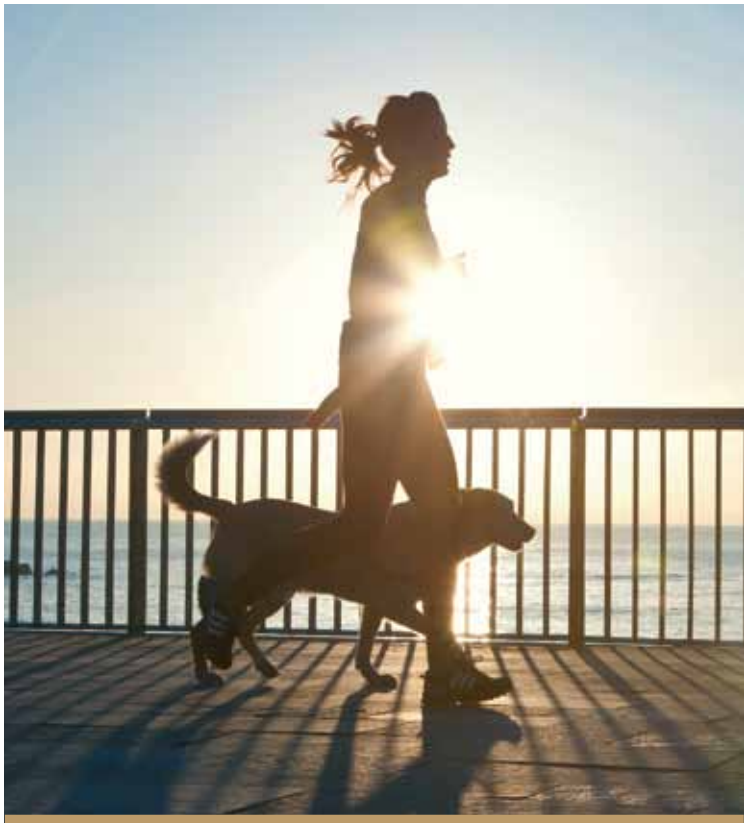
"Tackling the problems of obesity, inactive lifestyles, smoking and other risk behaviours in a way that is cost efficient and effective requires a multi-disciplinary approach. While the Vitality programme is fun and simple for the user, behind it lies a wealth of clinical, actuarial and behavioural science," Vitality CEO Allan Pollard said.

"Keeping our programmes grounded in the sciences is an imperative of Vitality and is one of the reasons we are launching the Vitality Institute."

Research on Americans' health and lifestyle status found their risk-adjusted age was on average five years older than their chronological age, figures that are broadly consistent with similar research in SA, said Mr Pollard.

Last year's South African Healthy Company index found workers from the companies that participated had on average a risk-adjusted age that was 6.4 years more than their chronological age.

kahnt@bdfm.co.za



Vitality recognised

at the World Economic Forum as a gold standard in workplace wellness solutions

The Workplace Wellness Alliance, part of the World Economic Forum, released a report at the Annual Meeting in Davos in January 2013. The report analyses the latest thinking on workplace wellness and metrics and is based on research and data from over two million employees from 25 companies across 125 countries. As one of the Leadership Members of the Alliance, Discovery is recognised for its Vitality programme that incentivises healthy behaviours and outcomes as well as its global collaboration with partners in China, the UK and US.

Find the Workplace Wellness Alliance report here: http://www.weforum.org/reports/workplace-wellness-alliance-making-right-investment-employee-health-and-power-metrics

DISCOVERY OPINION

THE VITALITY GROUP



Who is best placed
to reduce the long-term impact of non-communicable diseases

Derek Yach, Head of the Vitality Institute for Health Promotion in the US, shares his views on the global challenge of non-communicable diseases (NCDs) and possible solutions to address this risk.

Recent global reports have highlighted the importance of tackling a relatively small set of potentially preventable health risk factors that cause considerable ill health and suffering and that lead to most deaths. Unsurprisingly, tobacco, high blood pressure, unhealthy diets, a lack of physical activity and excess alcohol were found to lead to heart disease and stroke, many cancers, lung disease and diabetes. New South African data – gathered from various HIV and AIDS treatment programmes – is starting to reveal that the country's underlying health status is not significantly different from other middle-income countries where these health risk factors are also predominant.

Over the last decade, the US government and the World Health Organization (WHO) – together with a range of NGOs, academic groups and industry – have attempted to formulate ways to reduce the NCD burden. However, they have failed to define who is best placed to do this and to adequately resource the desired actions. In addition, funding for effective health promotion and disease prevention remains dwarfed by costs of treatment and care, and the proponents of health promotion are frequently drowned out by those advocating the latest breakthrough treatment.

WHO proposals tend to focus on taxes, regulations and laws, whereas industries, whose bottom-line depends on increased sales of products and services related to unhealthy behaviours, tend to favour voluntary actions and usually those that can get the widest buy-in from competitor companies. This usually means settling for the lowest common denominator supported by industry, which may not be the best for the public's health. Academic groups, meanwhile, tend to propose a range of innovations based on small community studies often in selected groups, without considering how to reach scale and become financially sustainable. I have had the chance to explore what works from many perspectives. At WHO, we favoured government-led actions to address tobacco, and science-led approaches to define dietary norms. We saw the value of WHO and governments highlighting which behaviours are risky and which are beneficial. At PepsiCo, we favoured voluntary actions to reduce unhealthy marketing and ingredients; and invested significantly in science, innovation and deep consumer insights to develop healthier options. These different approaches represent apparently divergent ways of seeing the world, with WHO focused on accomplishing its mission to improve global health even if this means adopting a paternalistic approach. In contrast, companies are driven by the need to remain focused on the bottom-line and sensitive to what their consumers will buy and consume. Despite these different approaches, the overriding objective remains to reduce the long-term impact of NCDs.

The role of WHO and health departments has served to provide clear leadership and actions on the ground when it comes to infectious disease control, maternal health and treatment programmes. While WHO has effectively advocated for preventive actions to tackle diets, exercise, tobacco and alcohol, its direct role in changing behaviour has not been as successful, with one notable exception: tobacco. The WHO Framework Convention on Tobacco Control, adopted a decade ago, has provided impetus, guidance and technical support to countries. In many countries – developed and developing – tobacco prevalence is declining. While a paternalistic approach to tackling tobacco was successful, applying this approach to other health risk factors is problematic for many reasons. Let's consider unhealthy diets.

Diets and activity patterns are complex, often context- and culture-specific, and demand permanent behaviour change by people over the course of their lives and across a wide range of products. Corporations involved in all aspects of food across the supply chain (from the farm to the fork) balk at regulations that might reduce their short- to medium-term profits, even if they are seen as potentially promoting healthier and more sustainable diets needed for the long-term sustainability of business, the environment and people's health. The costs of implementing taxes on unhealthy foods, prohibiting the sale of unhealthy foods or limiting the size of food and beverage portions, and regulating the salt, sugar and fat levels of foods, are usually very high.

In many developing countries, a lack of strong regulatory and enforcement capacity means that these laws run the risk of remaining on the books and not being implemented. This allows governments to say they have done their job even as the problem persists or grows.

Many people simply reject being told what to eat, when to exercise and how much to drink, since "they know what is in their best interests". This view is being challenged by exciting research that is setting the scene for smarter government policies and more responsive industry actions.

Over the last few decades, research conducted by a group of influential behavioural economists, led by Nobel Prize winner Daniel Kahneman, has shown that we tend to opt for today's immediate pleasures over tomorrow's promised rewards. This applies to whether we eat calorie-laden food, sleep in instead of exercising, or have another drink or cigarette. We generally overestimate our ability to follow and stick with healthy choices, be they a diet, a regular exercise regime or restricted alcohol intake. Likewise we undervalue the role of simple environmental signals that promote unhealthy food purchases and consumption. These built-in human frailties should be seen as such and tackled more effectively.

If many people reject more laws and interference in their lives, what are governments and industry to do, given that the cost of inactivity has been quantified in the workplace in terms of rising healthcare costs and reduced productivity? In some countries, inactivity also explains a significant part of the national debt.

What if we deliberately designed our environment and messages to make the healthy choice the easiest one? Brian Wansink (author of "Mindless Eating" and lead speaker at the recent Vitality Summit) and Cas Sunstein (author of "Nudge" and "Simpler" and former head of regulations in the Obama administration) have shown how to do just this by shifting from a tough-to-understand "healthy pyramid" to a "healthy plate" that is linked to simple key messages actionable by all:

- Make half your plate fruits and vegetables
- Drink water instead of sugary drinks
- Switch to low fat or no fat milk
- Choose unsalted nuts or reduced salt.

Wansink has gone further and demonstrated the power of designing school cafeterias in such a way that they promote healthy eating. He also shows how using smaller plates and thinner glasses helps people reduce portion size – a critical aspect in preventing obesity.

What if we helped people avoid unhealthy choices by rewarding the healthier option today? Vitality's HealthyFood programme does just that by discounting healthy food. Our new intellectual partner, Kevin Volpp, a world leader in applying behavioural economics theory to health, has shown how similar approaches can boost adherence to chronic disease medications and increase the rate of people stopping smoking.

These behavioural economics measures are beginning to permeate government policy and are being seen as invaluable to companies seeking to meet people's health needs. Synergy between government and industry goals could help us move faster. Greater government support for research on healthy diets would stimulate private sector innovation; shifting subsidies away from unhealthy to healthier crops could lower costs for both consumers and food companies; while more effective government-led campaigns to promote simple healthy food messages would complement what the private sector can achieve.

This synergy will see governments shift away from a predominantly paternalistic approach towards innovative partnerships with industry; partnerships that are capable of more effectively and sustainably addressing the burden of chronic diseases. Discovery's Vitality experience places us at the forefront of making this a reality.

Derek Yach is a South African analyst in the field of international healthcare policy. He has served as Executive Director for NCDs at the World Health Organization and as Senior Vice President for PepsiCo for their Food and Agriculture policy. He is currently Senior Vice President of The Vitality Group, part of Discovery Limited, where he heads up The Vitality Institute for Health Promotion in New York.



PING AN HEALTH

Our vision

To be the best health insurer in China, by making people healthier and offering them the broadest and best benefits and services in a system that is seamless, accessible and services clients brilliantly.

PERFORMANCE HIGHLIGHTS

Ping An Health **sustained its position as number one** writer of new business in the group high-end market

New business API in the insurance product line up **58%** to **R109 million** excluding own agents

Expenses and loss ratio **managed within business plan and budget**

Launch of **Vitality to Ping An Health** members: initial take-up has been **positive**



Key facts about **Ping An Health**

Ping An Insurance is **China's leading insurer and one of the largest** insurers in the world.

Ping An Health administers products for 553 900 lives including 149 437 lives for insurance products.

Ping An Health was founded in **2005 as a subsidiary of the Ping An Group and has established itself as a specialist health insurer in China.** Ping An Health has branches in seven major provinces and cities in the country.

Discovery entered into an agreement with Ping An Health in **2009,** after which **Discovery acquired a 20%** share in the business. During the financial year, Discovery increased its shareholding in **Ping An Health to 25%.**

Vitality was launched in China through Ping An Health in **June 2012.**

PERFORMANCE AGAINST KEY STRATEGIES FOR 2013

PING AN HEALTH

The estimated size of the private health insurance market in China is RMB 1 billion, consisting of the RMB 800 million high-end and the RMB 200 million mid-market. The industry has grown by between 40% and 50% each year.



Ping An Health made good progress during the year in terms of its strategy to focus on the product offering for the mid-end and high-end insurance markets.

Although these two markets are in the early stages of development, the combined market size has already reached approximately RMB 1 billion of premium income. Ping An Health has captured 30% of this market. This meant a deliberate move away from Fund and Service products, which are non-insurance administration products and which deliver lower margins.

Key strategy for 2013

Roll out Vitality to the Ping An Health membership base.

✓

Our progress

- Vitality was launched to the Ping An Health membership base during November 2012, and early take-up has been positive.
- **Annual enhancements to the Vitality programme were in progress at the time of writing the report and due to be launched to the market during November 2013.**

Key strategy for 2013

Focus on developing a product **for the individual market and grow this market.**

✓

Our progress

We developed and launched China's first comprehensive health protection product with Vitality embedded in the product structure. This product is aimed at the mid-end individual market, thereby expanding Ping An Health's product offering.

It is offered in addition to comprehensive insurance products for the high-end market and top-up cover products that work alongside the Social Health Insurance system.

Key strategy for 2013

Become the number one provider in the group high-end insurance market.

✓

Our progress

Ping An Health attained the number one position in the group high-end market.

中国平安 PINGAN

The private health insurance market in China continues to show potential for significant growth with the Chinese government specifically setting a goal to actively develop this industry.

The high-end and mid-end health insurance markets are estimated to outperform the life and property and casualty sectors by more than 20%. A report released by McKinsey estimates that gross written premium for the high-end and mid-end private health insurance markets will increase by 40% and 50% respectively, year on year. Against this background, Ping An Health's integrated health insurance and Vitality wellness offering is positioned well to grow market share. Products are being developed for both the group high-end and the individual markets and will be launched in the market during the next financial year.

1

FOCUS AREA

An ongoing focus on gaining traction in the mid-level market.

At the end of 2012, we launched a comprehensive health insurance product to the individual market, and actively promoted the product from March 2013 onwards. Our engagement with Chinese consumers has highlighted new opportunities and we have developed a "second-generation" product offering that was launched during October 2013. Vitality enhancements are to be introduced to the market during November 2013 and includes simplified rewards and increased cash backs.

2

FOCUS AREA

Entrenching Vitality as a key Ping An Health product offering.

Levels of engagement in the Vitality programme among individual members are satisfactory. Engagement among members of employer groups is increasing slowly; during the year we focused on promoting the programme to employer intermediaries and human resources representatives. We also added new partners; increased rewards within the group offering; and expanded the range of physical activity devices through which members can earn points.





PING AN HEALTH

FOCUS AREA

Developing our distribution capability.

Ping An Health uses the distribution footprint of Ping An Group to market both individual and corporate health insurance products. We have selected a group of high-performing agents for further training and development, and are providing technical marketing and sales support to agents.

Strategic priorities for 2014

Retain the number one position in the group high-end market.

Further develop our product offering and distribution capability for the individual market.

Enhance product benefits and services to meet the needs of our clients.



CASE STUDY

The increasing burden of chronic disease in China

A study published by The Lancet in June 2013 provides valuable insight into disease, disability, and demographic-related health trends in China. It indicates that China has achieved marked success in improving life expectancy and reducing death and illness caused by infectious diseases, but the challenge of non-communicable diseases (NCDs) has grown significantly and so has the number of years that Chinese people live in poor health. Although Chinese people are now living longer, the number of years they spend affected by disease and disability has risen by 21% since 1990.

The study further indicates that NCDs account for over 85% of all deaths in China. Cardiovascular diseases (stroke and ischemic heart disease) and cancers stand out as the top killers, causing around seven million of China's annual 8.3 million deaths, with the number of cancer deaths being significantly higher than for other nations.

Ping An Health's data indicates that clients of our group high-end insurance products in China suffer from very similar conditions to the general population, with hypertension, coronary artery disease, type two diabetes and hyperlipidaemia being the most prevalent.

Today, the leading health risk factors in China are related closely to lifestyle choices:

- Poor nutrition, including diets high in salt and low in fruit, whole grains, nuts and seeds, is the leading health risk.
- Second is high blood pressure, which researchers estimate causes two million deaths every year.
- Tobacco use is next, accounting for at least 1.4 million premature deaths.
- Alcohol abuse, high glucose levels, high body mass index and physical inactivity were also among the top 10 risks.



CASE STUDY

Ping An Health's operating model

is based on the Discovery Health integrated model

Ping An Health's operating model leverages Discovery Health's expertise and integrated model to offer a seamless approach to managing healthcare. It allows us to analyse claims and other data to develop detailed, dynamic profiling of risk and cost across the healthcare value chain, resulting in lower prices and more sustainable rates for clients. The following three aspects form part of the operating model:

- **Ping An Health's consumer-directed product construct**
  Ping An Health offers comprehensive health insurance benefits to ensure members have the necessary protection and certainty of cover when they need it. In addition, Ping An Health adds a wellness approach to the product offering through Vitality, which encourages and rewards clients for being healthy. This innovative approach to healthcare funding lowers costs, boosts productivity and reduces absenteeism.
- **HAL*O*: Health Analytic Tools and Capabilities**
  Ping An Health has deployed a number of assets that allows us to manage the risks of funding healthcare. This proprietary technology, called HAL*O*, is a set of health analytic tools and applications used throughout the business. We believe this sophisticated approach to risk management is key in offering competitive and sustainable rates for our clients.
- **The Ping An Health Servicing platform**
  The Ping An Health Servicing platform is a series of servicing assets that we have established to provide a robust service framework:
  - The Ping An Health Client Gateway is the benefit management system that enables all of Ping An Health's services. At the start of 2013, we re-engineered our benefit management system so that all benefit liabilities could be housed in this system. The result is 2.7 million possible benefit configurations, all of which are fully automated, thereby ensuring quicker claims processing turn-around times and fewer errors.
  - Ping An Health Hospital*Direct* is the most extensive direct billing network in China, and an asset that we continue to build on to advance our hospital and claims services.
  - Ping An Health's claims processing system is the first health insurance claims system with auto-adjudication in China.



DISCOVERY PEOPLE

Our vision

To continually grow a high-performance, values-based culture of opportunity where diversity is embraced, innovation thrives, personal wellbeing is valued and individuals are inspired to achieve their potential.

PERFORMANCE HIGHLIGHTS

R90.1 million
Total spend on skills development in South Africa

69% Percentage of skills development spend on Employment Equity employees in South Africa

R4 billion
Total annual employee earnings between July 2012 and June 2013

3 212 The number of employees in South Africa who **participated in the Discovery Employee Volunteer Programme**, an increase from 2 183 in the last reporting period



Key facts about **Discovery People**

8 220
total permanent employees worldwide.

22 109
employment opportunities currently sustained by Discovery worldwide, including financial advisers, employees, contractors and learners.

Critical skills:
Information Technology (IT), clinical and actuarial skills.

DISCOVERY PEOPLE



In support of Discovery's ambition to be the best insurance organisation in the world, we recognise the need to develop our employees and leaders.

While products and technologies can be replicated, unique and talented people enable a company to innovate, differentiate its product offering and succeed in a globalised business environment. In the context of our current economy, Discovery's increasingly global presence makes innovation a non-negotiable. We need the best talent to realise this innovation on a continuous basis. Because we believe that employing talented people leads to indisputable business benefits, talent management is a high priority at Discovery. Effective talent management ensures we have the most appropriate combination of skills to meet our business requirements. This entails:

- Aligning our company's vision, values and strategy with how we manage our employees.
- Identifying critical skills needed in the business to meet both current and future business needs.
- Recruiting, developing and retaining talent, particularly those in core capability areas.
- Integrating the key components of our talent management programmes so they form a coherent whole.

Our focus areas during 2013

In the past year, we have continued to seek ways to leverage our Employee Value Proposition, create a strong employer brand, and establish ourselves as an employer of choice.

1

FOCUS AREA

Targeting critical skills through graduate recruitment drives.

- Discovery has identified core capabilities that will best support our growth ambition, namely: IT, actuarial and clinical skills. We have sufficient depth in these areas currently and we are working on a talent strategy that focuses on these talent pools to ensure maximum contribution, growth and retention.
- In 2013, Discovery employed 17 graduates from our Graduate Programme – a programme aimed at attracting talented individuals at university level – in core capability areas. We aim to increase the number of appointments from this programme to 25 during 2014.
- In August, we launched the Adrian Gore Fellowship Award – a bursary programme that seeks to source and develop some of the country's best actuarial talent to work at Discovery, as well as build our profile at four leading universities in South Africa.

2

FOCUS AREA

Building human resources capacity to support growing business needs.

- We run an entry level Research and Development (R&D) Apprentice Programme targeted at people with a combination of analytical and creative skills. In 2013 we recruited 90 learners and are driving internship intake across the business.
- In addition, we ran two graduate skills programmes for people with disabilities, increasing the number of learners on each by 10 to 25 and increasing the duration of these programmes from four to six months.
- Over the past 10 months, a 360-degree feedback process was rolled out at senior management level, resulting in the establishment of personal development plans. A total of 556 employees completed leadership development programmes at Discovery, up from 506 in the previous period.
- The Group Talent Review included an evaluation of succession plans and readiness for critical roles across the Discovery business.

3

FOCUS AREA

Rolling out an executive development programme aligned to the business strategy.

- In 2013, we launched the Oxford Executive Leadership Programme which runs over a period of nine months. Twenty-one selected senior Discovery leaders participated in the first module at Oxford in the United Kingdom. The intense five-day experience – Breakthrough Skills and Strategies – focused on transforming delegates' perspectives on leadership, innovation and entrepreneurship.
- The Executive Mentoring Process was launched in June and the delegates will be mentored by Discovery senior executives for the duration of the programme. The programme serves as an example of how the output of one talent management process is the input of another, creating an interlocking, self-reinforcing and consistent leadership development approach.

OUR FOCUS AREAS DURING 2013 continued

DISCOVERY PEOPLE

4

FOCUS AREA

Establishing mutually-beneficial partnerships.

- Discovery has joined forces with various agencies, universities and organisations that enable us to attract diverse talent across different career lifecycles, while supporting job growth and career development. For example, in 2013 we were involved in the South African Actuarial Development Programme (SAADP), an independent non-profit organisation whose primary objective is to address the shortage of black actuaries in South Africa. The programme aims to unearth and harness mathematical and analytical skills among black students to help them capitalise on future career opportunities in the field of Actuarial Science.

  Discovery is represented on the SAADP selection panel and helps to fund bursaries for school-leavers to enable their further education. Recipients are also trained through workshops and mentorings, and are offered academic and non-academic support.

- Another example of a partnership aligned to Discovery's objectives is the immersion day we held in March 2013 for selected recruitment agencies. On such days, we invite recruitment representatives to attend workshops and experience a day at Discovery to gain an understanding of our values and culture. This enables them to understand our expectations of potential candidates, thereby allowing them to source the most suitable candidates.

5

FOCUS AREA

Improving the diversity of our workforce, particularly at senior and professional levels.

- Between July 2012 and June 2013, we hosted 188 unemployed black learners on learnerships and skills development programmes; some 52 learners from the 2012 programmes were employed. An additional six disabled black learners from the skills development programme proceeded onto the 2013 learnerships.
- As part of the talent management process, there was a specific focus on identifying black employees who show potential, and are looking for ways to accelerate their development.
- Employment Equity representation at Divisional Manager level increased by 11% as a result of both recruitment and development programmes aimed at building senior leadership skills. Discovery's new Employment Equity Plan, effective from 1 July 2013 to 30 June 2016, is currently being implemented.

Strategic priorities for 2014

Reinforce and grow the unique Discovery culture.

Build a robust talent pipeline that will enable us to achieve our ambition through recruiting, developing and retaining the best people.

Develop outstanding leaders who can deliver on our business ambition.

Continue to improve organisational diversity and achieve our employment equity targets.



Read more about Discovery People in our 2013 Sustainable Development Report at www.discovery.co.za/info/sustainabledevelopment

Occupational levels	SA employees								Foreign nationals		Total	
	Female				Male				Female	Male		
	African	White	Coloured	Indian	African	White	Coloured	Indian			2013	2012
Top management	1	0	0	0	1	18	0	2	1	0	**23**	20
Senior management	22	97	9	30	18	126	13	18	7	10	**350**	315
Professionally qualified and mid-management	91	276	50	124	37	180	22	60	13	7	**860**	847
Skilled technical/junior management	339	444	195	333	304	402	134	287	30	37	**2 505**	2 395
Semi-skilled	825	367	272	312	564	347	199	326	13	11	**3 236**	3 164
Unskilled and defined decision-making	0	0	0	0	0	0	0	0	0	0	**0**	0
Total permanent employees 2013	1 278	1 184	526	799	924	1 073	368	693	64	65	**6 974**	
Total permanent employees 2012	1 157	1 160	546	762	851	997	355	648	113	152		6 741

South African Employment Equity information for Discovery: 1 January 2012 – 31 December 2012



R18 729 546
Investment in Discovery Foundation initiatives

R1 482 201 893
Total preferential procurement spend

DISCOVERY'S SOCIO-ECONOMIC IMPACT

Our vision

To focus and maximise our socio-economic impact by aligning our Corporate Social Investment and Enterprise Development initiatives with Discovery's core purpose as well as national priorities in South Africa, thereby promoting a thriving society.

PERFORMANCE HIGHLIGHTS

R1 204 941
Total spend on youth development projects

R2 823 085
Enterprise development loans granted

R2 000 000 investment in the Laureus Sport for Good Foundation, an organisation that uses sport to bring about social change in communities

R11 186 634
Total investment by the Discovery Fund in various public and community healthcare projects

Key facts about **our socio-economic impact**

The Discovery Foundation is investing R150 million to train 300 healthcare specialists in South Africa.

Discovery's corporate social investment initiatives focus on supporting the delivery of primary healthcare services: HIV and AIDS, immunisation, chronic illnesses, healthcare awareness and the health of women and children.

The Discovery Fund provides ongoing financial support to **34 community healthcare organisations** and projects across South Africa, with many of these organisations and projects situated in remote and rural areas.



DISCOVERY'S SOCIO-ECONOMIC IMPACT

Businesses today must not only navigate social change successfully, but must also contribute to creating the social stability that is necessary for a society to develop and thrive.

As such, we use our resources and skills to support enterprise development and entrepreneurship, which we believe are fundamental in growing our economy and impacting society positively.

For Discovery it is equally important to have a positive impact on society and to be a force for social good – not only through the products and services we offer, but also in our engagement with people and the social partnerships and collaborations we build to benefit society as a whole. This touches on all aspects of our business, be it the innovation that disrupts the market for the benefit of consumers, the building of a healthcare system that contains healthcare costs, incentivising good health through Vitality; or investing in indigent communities.

Specifically, our goal is to use innovative partnerships to strengthen and improve our country's healthcare sector so that more South Africans can access equitable, high-quality and affordable healthcare services. Such partnerships include those with government, as well as non-governmental organisations, universities and the corporate sector. We choose projects where we can respond to national healthcare priorities identified by the government, and support and supplement healthcare delivery in such a way that it results in a positive ripple effect in broader society.

Over the years, we have been involved in numerous projects and initiatives to make people in the broader community healthier.

1| Primary healthcare support

Through the Discovery Fund, an independent trust, we give ongoing support to community healthcare projects around South Africa. These projects often work in remote and rural areas and provide the most critical healthcare services. The projects focus on HIV and AIDS, immunisation, chronic illnesses, healthcare awareness and training, and the health of mothers and children in rural communities.

2| Developing people

We are committed to investing in people in our healthcare sector. We launched a 10-year programme in 2006 aimed at training an extra 300 specialists for South Africa's public healthcare sector. Through a series of grants and scholarships awarded through the Discovery Foundation, talented medical professionals are able to conduct clinical research and undergo specialist training that will help to advance medical care in South Africa.

Discovery also supports skills development programmes and scholarship schemes in rural areas, such as the Umthombo Youth Development Foundation in KwaZulu-Natal. In line with the priority of boosting human resources identified by the government, we are building capacity in the healthcare system by training mid-level healthcare workers. These include community healthcare workers, school health nurses, district clinical specialist teams and pharmacy assistants.

In addition, we address youth unemployment through enterprise development initiatives that invest in youth development projects.

3| Infrastructure development

We support and help develop the infrastructure needed for healthcare delivery through large capital infrastructure investments that help to improve healthcare delivery. Past examples include refurbishing the antenatal clinic at the Alexandra Health Centre and University Clinic near Sandton in Gauteng, and building a new trauma unit at the Red Cross Children's Hospital in Cape Town.

4| Volunteering our time

Being involved with people and communities around us is an important aspect of the Discovery corporate culture. Our volunteers contribute to community development through giving of their time and sharing their skills to support communities in need.

Many departments in Discovery have also adopted and support a chosen charity or project over a longer period. For example, members from our Information Technology department volunteer their time and raise funds for the Refilwe Community Organisation in Lanseria, Johannesburg.

Our focus areas during 2013

During the past year, we have continued to seek ways to contribute to socio-economic development in South Africa by aligning various initiatives with business and national priorities as set out in the National Development Plan.

Key initiatives we undertook to impact broader society included the following:

FOCUS AREA

1

Forming key strategic partnerships to expand access to healthcare for more South Africans.

In the past financial year, Discovery played a leadership role in the launch of the pioneering Social Compact agreed by the Department of Health and business leaders of major health companies operating in South Africa.

The Compact seeks to unite the public and private sector on healthcare issues of national priority. In a further bid to work with the government to broaden access to quality primary healthcare for all South Africans, Discovery is actively engaging with them in support of the National Health Insurance pilot districts.

We are also working with the Council for Medical Schemes in a pilot project that aims to investigate the role of medical schemes in measuring and improving healthcare service quality.

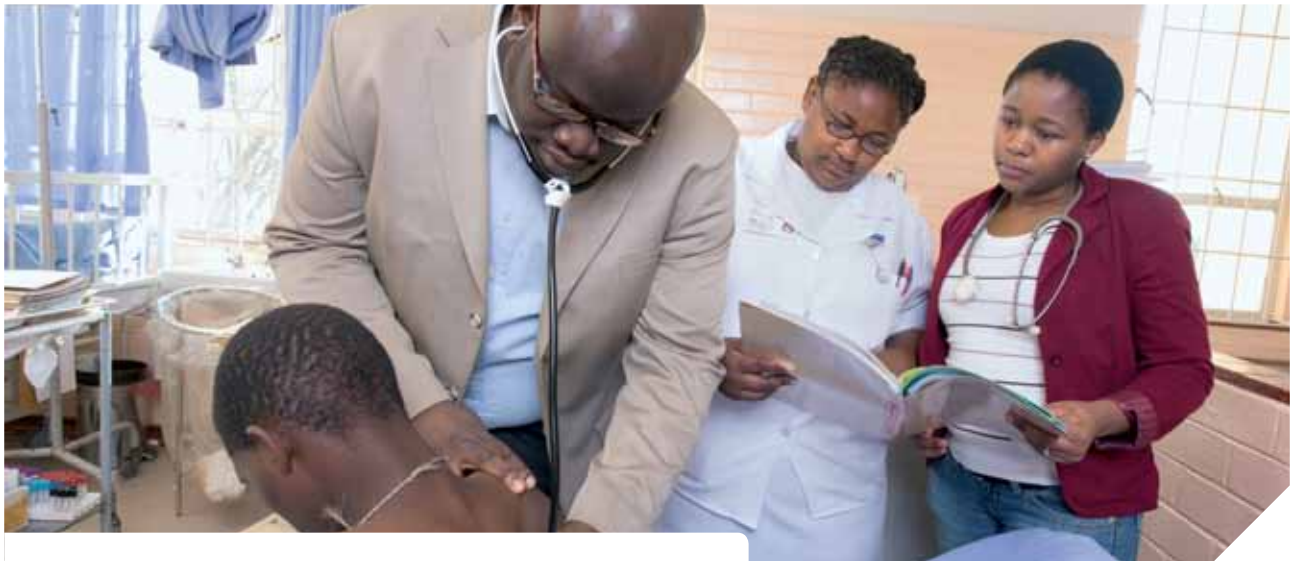
FOCUS AREA

2

Introducing a new award category to the Discovery Foundation Awards to further strengthen specialist medical training in South Africa's public healthcare sector.

The new Discovery Foundation MGH Fellowship Award was launched in May this year. The award will enable an established South African healthcare academic specialist to either undergo specialist training or take part in groundbreaking research in their chosen medical field at the Massachusetts General Hospital, one of the leading academic hospitals in the US.

Dr Neliswa Gogela, a Cape Town physician working towards a PhD in hepatology, was chosen as the award's first beneficiary. Her R2.1 million grant will enable her to join the MGH's research and training programme on liver transplantation. The Foundation trustees have also recently approved the inclusion of the private sector in the overall Foundation Awards programme. Although the Foundation Awards have focused on public-health doctors, it has become necessary to explore the contribution that private-sector doctors can make in strengthening South Africa's healthcare system. These awards will be rolled out during 2014.



DISCOVERY'S SOCIO-ECONOMIC IMPACT

3

FOCUS AREA

Focus our enterprise development strategy on mutually beneficial partnerships to encourage entrepreneurship, with a continued spotlight on transformation in the health sector and partners in our supply chain.

A number of initiatives are underway to achieve this objective. For example, non-profit organisations are often challenged by dwindling donor funding and need to find ways to generate income to sustain their core operations. Discovery seeks to add value to our partners in various initiatives. As such, our enterprise development strategy focuses on helping organisations build their internal capacity, leveraging off our skills and expertise, to become sustainable.

Discovery's enterprise development and corporate social investment teams jointly selected three Discovery Fund projects to support: MES Impilo, the Siyakhana Initiative for Eco-health and Food Security and the Topsy Foundation. By assisting these projects both financially and through the transfer of skills and intellectual property, we were instrumental in assisting them to create income-generating opportunities and to become more self-sustaining.

Discovery is also broadening our enterprise development strategy to include other divisions of Discovery. This has helped us to identify additional areas of focus, including our ongoing efforts in providing healthcare for lower-income groups.

Strategic priorities for 2014

Establish new award categories to recognise key contributors among private-sector doctors, as part of our objective of strengthening and sustaining South Africa's private healthcare system within the broader national healthcare system.

Continue to work with government in support of universal healthcare coverage and with healthcare providers to develop the capacity to deliver it.

Encourage a culture of entrepreneurship and support black-owned franchises in our distribution channel to be sustainable.

Determine the feasibility of current CSI projects becoming enterprise development beneficiaries.



Read more about Discovery's socio-economic impact in our 2013 Sustainable Development Report at www.discovery.co.za



Discovery **Opinion**

Calling for a multi-sector compact:

A view on the relationship between business and society, especially in the healthcare sector

Dr Ayanda Ntsaluba, Executive Director at Discovery, shares his views on how collaboration between businesses and society can create value for all stakeholders.

Some believe that to truly be a force for social good, one must remain untainted, so to speak, by business incentives.

I disagree.

While non-profit organisations do much good, this approach narrowly limits the field of those who can benefit and progress society. My greatest wish for Discovery is that it becomes an example of how it is entirely possible to be a successful business and, at the same time, be socially relevant.

In the realm of social responsibility, we are in a position that is both fortunate and, at times, tricky. We're fortunate because Discovery's core purpose – making people healthier and enhancing and protecting their lives – by definition lends itself to being socially relevant. The tricky part comes into play because the health sector where we are a significant player, as in any country in the world, is politically charged. Society understandably expects those involved in the health sector to display a higher level of social consciousness. As the healthcare system touches us at our most vulnerable moments, I believe, this causes us to judge decisions and consequences in this sector more critically than we would in most other sectors. This expectation is justified and correct.

It is therefore imperative that Discovery remains steadfast in its values and demonstrates that success is not beyond the reach of those who do the right thing. This is particularly important in the South African context, where healthcare is critical to the consolidation of our democracy and restoration of the dignity of many South Africans. Our task lies in forging strategic and tactical partnerships across the public private divide and using the assets that we've built in the process of developing the private sector, to increasingly make a positive impact on society, without undermining our competitive position as a business.

I'm excited that Discovery has clearly formulated this goal and is in many ways already using intellectual and human resources to assist in the process of piloting for the eventual establishment of the NHI – a process that is firmly led by the Minister of Health and his team. I believe that South Africa urgently needs a united vision of where we want to go and what we want to achieve. It is crucial that businesses work with government in order to leverage the country's assets to truly promote our national interests.

While some have criticisms of the National Development Plan (NDP), to me it represents a good starting point from which to create a platform for focused national effort. If embraced by both the public and private sectors, the NDP can help us build consensus around the major societal and economic challenges we face as a nation. This, in turn, will provide great impetus to leverage South Africa's position as a middle-income country with very high ambitions. Like any broad vision, its test surely has to lie in the impact its implementation has on improving the quality of life of ordinary citizens. And like all transformative interventions, it has to be dynamic, living and open to improvement and further elucidation in the context of our lived experiences and insights gained.

DISCOVERY'S SOCIO-ECONOMIC IMPACT

Calling for a multi-sector compact continued

We must recognise and harness the socio-economic power of well-managed Public-Private Partnerships (PPPs), which lend themselves to integration across industries. A case in point is the ground-breaking Social Compact signed in November 2012 by the Department of Health and CEOs of leading healthcare companies. The compact is an initiative aimed at bridging the divide between the public and private sector and agreeing to work together in a focused and targeted manner on those priorities where pooling our resources enables scale to be achieved.

The partnership focuses on human capital and HIV and AIDS, two important elements of the Department of Health's 10 Point Plan. Each participating private sector health company, which so far includes 23 leading representatives from the pharmaceutical, hospital, pharmacy and medical scheme industries, has pledged a fixed annual contribution to ensure the delivery of various healthcare initiatives.

In 2013 alone, the partnership committed R40 million to prioritising key projects, in addition to the work individual companies continue to do as part of their Corporate Social Investment (CSI) programmes. One of the priorities is to strengthen management capability in public hospitals and thus reduce inefficiencies in the system.

Another project, spearheaded by Health Minister Aaron Motsoaledi, is bold and ambitious. It is about turning the adversity of being known for our high HIV/AIDS and TB burden into something beneficial by developing our country as a leading centre of research on the treatment and management of these diseases. Through collaboration with the Medical Research Council, the project supports the training and further education of medical professionals who wish to conduct pioneering PhD research in tuberculosis or HIV and AIDS, in conjunction with the Medical Research Council. The first recipients of these awards will be announced soon.

There is also an urgent need to train enough medical practitioners to address the gaps in the public and private healthcare sectors. According to research collaborated through many sources, there are currently only 5.5 doctors providing care for every 10 000 people in South Africa. To address this shortage, the healthcare system must train 52% more medical professionals than the current standard. The private sector – through the Social Compact – has also agreed to work with the Department of Health and educational institutions to increase the capacity of our country's eight existing medical schools.

Research further reveals that of the 1 200 medical students who graduate annually, only 35 end up working in rural areas in the long-term – areas in which good healthcare is desperately required. Funding from the Social Compact also specifically targets underprivileged students from rural areas to study further, enabling them to return to their communities well-qualified and eager to make a difference. This not only addresses South Africa's undersupply of doctors, but also helps us to build a more equitable healthcare system.

All these initiatives focus on investing deeply in our people by equipping them with skills and knowledge. There is no doubt that such investments will have a ripple effect on society and for future generations. However, as inspiring as this industry-wide compact is, it is still only the start of what needs to be a series of such initiatives. Long-term growth and sustainability require trust and cooperation among businesses, the workforce and government.

Of course this journey will face many challenges. Some of these are inherent in the respective roles of the different partners. The true test of leadership is to resist being paralysed by these challenges but to always seek new vistas for sustained collaboration. After all, it is in the crucible of practical work that we learn more about each other and our mutual interdependence.

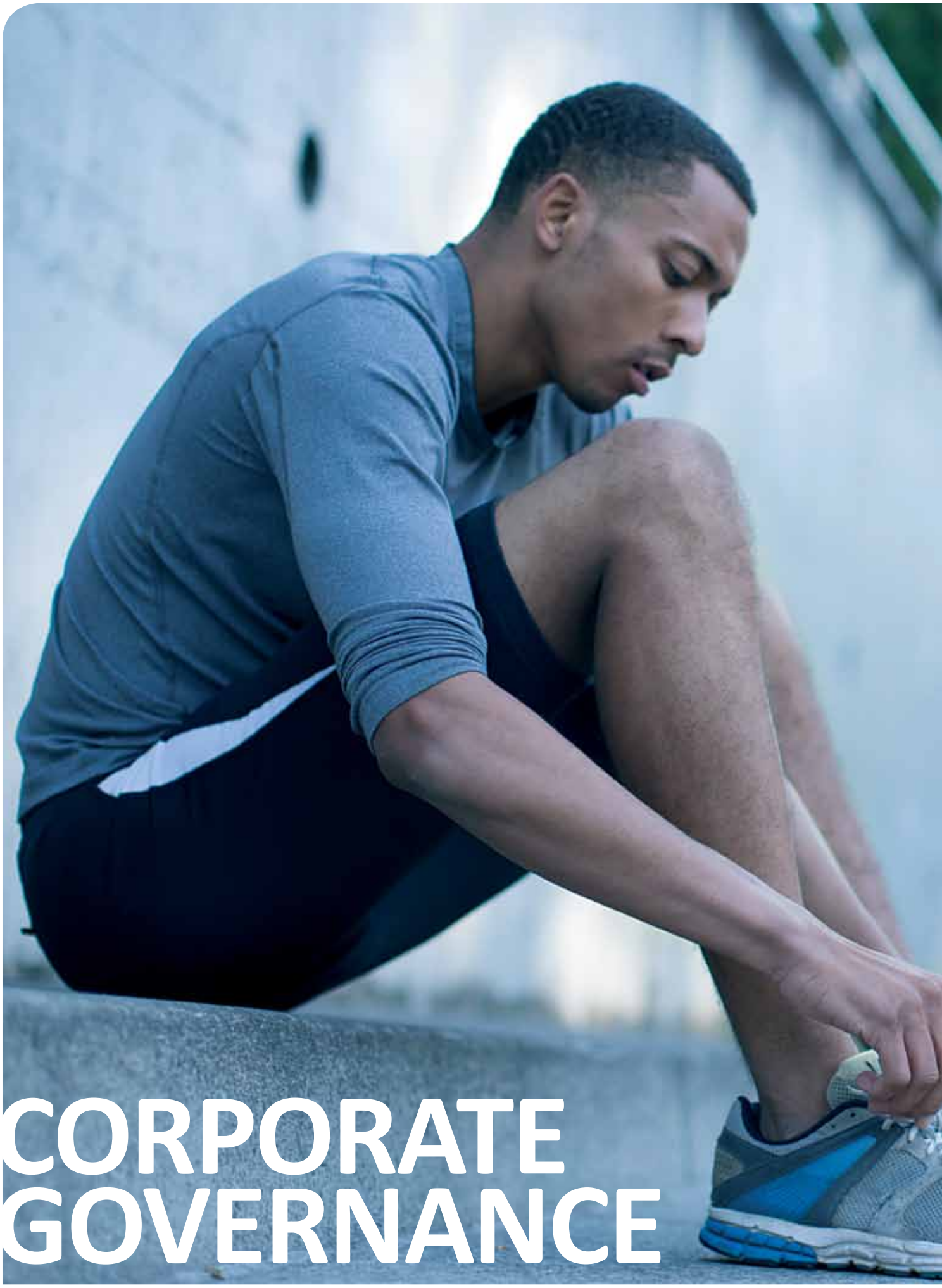
It is important to realise that the challenges facing our country are too big for any one sector working in isolation to resolve. Our growth is inextricably bound to the ability of the public and private sectors to work together to address South Africa's immense socio-economic issues. Credible platforms for regular dialogue across a number of sectors are vital, particularly if these platforms are bolstered by shared goals that represent national interests.

I believe that South Africa truly needs a multi-sector compact aligned with a clear national vision that is both realistic but ambitious, and I'm not the only one. Business leaders like Adrian Gore and Clem Sunter have also been calling for a broader social compact – some sort of economic CODESA, backed up by smaller but strong sectoral compacts. It's a refreshing concept, and it's encouraging to see government and business beginning to realise the necessity of rising above immediate circumstances and personal differences to find common ground. This bold step, together with a move away from simplistic charity-giving to a more sustainable asset-building model, will ensure that our efforts have a wider reach and a lasting impact on the country as a whole.

Dr Ayanda Ntsaluba was the former Director General of International Relations and Cooperation and of Health in South Africa. He is currently an Executive Director of Discovery Limited and also co-chairs the Social Compact in the healthcare industry.



In May 2013, the Discovery Foundation announced an annual grant for leading South African academic doctors to conduct clinical research and training at the Massachusetts General Hospital (MGH) in Boston, US. The first recipient, Dr Neliswa Gogela, from the University of Cape Town, is a physician working towards a PhD in hepatology. She will join a training and research programme in the field of liver transplantation at MGH for two years.



CORPORATE GOVERNANCE



Contents

Discovery Limited Board of Directors	118
Corporate Governance Committees and Secretary	122
Corporate Governance report	123
Enterprise Risk Management report	128
Group Compliance report	131
Remuneration report	133

DISCOVERY LIMITED BOARD OF DIRECTORS – Executive directors



Richard Farber

Executive Director

BCom (Hons), CA(SA), FCMA

Richard was a partner at Fisher Hoffman Sithole (PKF) from 1998 until 2001 before joining Investec Bank, where he was the Group Accountant from 2002 to 2003. He joined Discovery as Chief Financial Officer in 2003 and was appointed as the Financial Director in 2009. Richard is also a member of the Financial Reporting Investigation Panel (FRIP) of the JSE Limited and a Fellow of the Chartered Institute of Management Accountants.



Adrian Gore

Group Chief Executive Officer

BSc (Hons), FFA, ASA, MAAA, FASSA

Adrian founded Discovery Health in 1992 after conceiving the idea of a specialist risk management company that offered clients innovation, flexibility, value and excellent service. Adrian is a Fellow of the Actuarial Society of South Africa, a Fellow of the Faculty of Actuaries (Edinburgh), an Associate of the Society of Actuaries (Chicago) and a member of the American Academy of Actuaries. He was chosen as the Ernst & Young Entrepreneur of the Year in 1998 and in 2004 as South Africa's leading CEO in the annual MoneyWeb CEO of the Year award. In 2010, he was named as the Sunday Times Business Leader of the Year. He is also the Chairperson of Endeavor South Africa, a global organisation that focuses on developing entrepreneurial talent. Adrian also serves on the World Economic Forum Global Health Advisory Board, as well as the Columbia University Mailman School of Public Forum Board and the Massachusetts Federal Hospital Global Health Advisory Board.



Hylton Kallner

Executive Director

BEconSc, FFA, FASSA

Hylton graduated from the University of the Witwatersrand with a BEconSC in Actuarial Science. He was later admitted as a Fellow of the Faculty of Actuaries and a Fellow of the Actuarial Society of South Africa. In 1996, Hylton started his career in the actuarial division at Liberty Life. Later that year, he joined Discovery Health, where he has held various positions in marketing, actuarial and strategic projects. He is currently Chief Marketing Officer for the Discovery Group and plays a key role in the executive committees of Discovery Limited and its subsidiaries.



Neville Koopowitz

Executive Director

BCom, CFP

Neville is Chief Executive Officer of PruHealth, Discovery's health insurance joint venture in the UK. Neville joined Discovery as Marketing Director in 1996 and has played a key role in the development of Vitality, DiscoveryCard and Discovery Health, where he was the Chief Executive Officer. He is passionate about the role of sports in facilitating healthy living and is a past board member of the Sports Science Institute of South Africa and the Board of Trustees of the Laureus Sport for Good Foundation's South African chapter.



Herschel Mayers

Executive Director

BSc (Hons), FIA, FASSA

Herschel qualified as an actuary in 1986 and is a Fellow of the Institute of Actuaries. He joined Liberty Life after qualifying and as a member of their EXCO, he served as the Head of Individual and Group Business, Underwriting and Systems, Technology, Product Development and Finance. Herschel joined Discovery in 2000 as the Managing Director of Discovery Life. In 2001, Herschel was appointed to the Board of the Life Offices Association (LOA) and he currently serves on the Board of the Association for Savings and Investment South Africa (previously LOA). In January 2006, Herschel was appointed CEO of Discovery Life and Discovery Invest. Herschel is a member of the Discovery Limited Executive Committee and is currently also the Chief Executive Officer of PruProtect in the UK.



Dr Ayanda Ntsaluba

Executive Director

MBChB, MSc (Lond), FCOG (SA)

Before joining Discovery in July 2011, Ayanda served as Director General of the Department of International Relations and Cooperation. Before this, he was Director General of the Department of Health. A qualified obstetrician and gynaecologist, Ayanda completed further tertiary education in the fields of health policy planning, international relations and business at eminent universities including Harvard, the University of London and the Moscow Institute of Social Science. He has served on a number of statutory bodies including the Medical Research Council and the Health Professions Council of South Africa. Ayanda is playing an instrumental role in Discovery's overall strategic planning, particularly within the healthcare system, and in Discovery's international expansion strategy.



Alan Pollard

Executive Director

BSc (Hons), FIA, FSSA

Alan joined Discovery Health in 1994 and headed up Research and Development, where he was responsible for the design and development of Discovery Health products. A qualified actuary, Alan was the Chief Executive Officer of Discovery Vitality until 2012. He is currently the Chief Executive Officer of The Vitality Group and is a member of the Executive Committee and Actuarial Committee of the Discovery Group.



John Robertson

Executive Director

BCom, CTA, CA(SA), HDipTax

John joined Discovery Health in April 1993 and was responsible for Information Technology Strategy, systems development, information technology networks and finance. As the Group Chief Information Officer, he is responsible for all Information Technology Strategy, Infrastructure, Corporate Applications, and all Internal Corporate Facilities and Shared Operations at Discovery.



Barry Swartzberg

Executive Director

BSc, FFA, ASA, FASSA, CFP

Barry was a co-founder of Discovery Health in 1992 and was involved in developing the Discovery concept. After Discovery Health was launched, he was involved in setting up the administration and systems infrastructure for the company. Following that, he served as Marketing Director and then Chief Executive Officer of Discovery Health from 2000 to 2005. He is currently the Group Executive Director of Discovery Limited and is responsible for Discovery's international operations. He serves on the boards of Discovery Limited, The Vitality Group in the USA and PruHealth and PruProtect in the UK, as well as Discovery Insure.

DISCOVERY LIMITED BOARD OF DIRECTORS – Non-executive directors



Dr Brian Brink

Non-executive Director (Independent)

BSc (Med), MBBCh, DA (SA)

Dr Brian Brink is a respected thought leader in defining the contribution the private sector can make towards improving health in developing countries. He has served on the board of The Global Fund to Fight AIDS, Tuberculosis and Malaria since its inception in 2002 and is currently the Vice Chair of its Audit and Ethics Committee. Dr Brink has particular interest in strengthening and improving health systems and healthcare delivery in resource-poor settings.



Peter Cooper

Non-executive Director

BCom (Hons), HDip Tax, CA(SA)

Peter is Chief Executive Officer at Rand Merchant Insurance Holdings Limited (RMIH, Discovery's most significant shareholder) and its sister company RMB Holdings Limited. As their representative, he also serves on the boards of certain of their investments, including FirstRand, OUTsurance and RMB Structured Insurance. Peter graduated from the University of Cape Town in 1978. After qualifying as a chartered accountant, he worked in the financial services sector, first as a tax consultant and later specialising in corporate and structured finance. He then joined the RMB group in 1992.



Jan Durand

Non-executive Director (Independent)

BAcc (Hons), MPhil, CA(SA)

Jan is a qualified chartered accountant and Rhodes Scholar, with a BAcc (Hons) from the University of Stellenbosch and an MPhil in management studies from Oxford University. He is the Chief Executive Officer of Remgro Ltd, and before its delisting was the Financial Director and Chief Executive Officer of Venfin Ltd. Jan is a Director of Rainbow Chicken Ltd, Capevin Investments Ltd, SAIL Group Ltd, Capevin Holdings Ltd, RMB Holdings Ltd, RMI Holdings Ltd, Saracens Ltd, Tracker Investments Holdings (Pty) Ltd, InVenFin (Pty) Ltd, Intervid Ltd, Intervid International AG, CommsCo Holdings (Pty) Ltd and CommsCo (Pty) Ltd. He has been a Director of Remgro Ltd since 2009, and served as a Non-executive Director of Alexander Forbes Ltd from 2004 to 2007. Jan brings extensive expertise to the Discovery Board.



Steven Epstein

Non-executive Director

JD (Columbia University Law School) BA (Tufts University)

Steven is the founder and senior partner of Epstein Becker & Green, one of the largest US-based health law firms that support clients in health practice on matters that range from health policy and strategic partnering to complex compliance issues. He sits on the Board of The Vitality Group, a number of healthcare companies and the advisory boards of several venture capital firms. For over 30 years, he has played a unique role in establishing the concept that healthcare organisations need a dedicated form of legal representation.



Monty Hilkowitz

Non-executive Chairperson (Independent)

FIA

Monty worked for Southern Life Association and Swiss Re before joining Liberty Life in 1971, where he was appointed as Managing Director in 1978. He was appointed Chief Executive Officer of Westpac Life in Australia in 1986. He has been self-employed since 1989 and involved in investment management, financial services and insurance interests in several countries. He is currently Director of Acuvest, a specialist financial services company in Ireland. He also serves as Chairperson of Pioneer International. Monty is chairperson of the Discovery Limited Board of Directors.

** Vhonani Mufamadi, non-executive director, resigned in December 2012.*



Dr Vincent Maphai

Non-executive Director (Independent)

BA (Hons), M Phil, D Phil, Advanced Management Programme (Harvard)

Dr Maphai is Director of Corporate Affairs and Transformation at SABS. Previously he was the Southern African Chairperson of BHP Billiton. In an academic career spanning two decades, he taught at various universities both locally and abroad and consulted with several blue-chip companies on a range of transformation and human resource issues. He was also a Research Executive Director of Social Dynamics at the HSRC for three years. He has served on the Boards of various companies as Non-executive Chairperson, and he has chaired the SABC, the Presidential Review Commission into the restructuring of the public sector, and the South African Responsible Gambling Trust. Dr Maphai is also the Chairperson of the Discovery Foundation.



Les Owen

Non-executive Director (Independent)

BSc (Hons), FIA, FPMI

Les is a qualified actuary with over 35 years of experience in the UK and Asia Pacific insurance markets. He was the Group Chief Executive of AXA Asia Pacific Holdings Limited from 2000 to 2006 and Chief Executive Officer of AXA SunLife in the UK from 1995 to 1999. Les brings to the Board extensive experience and expertise in international insurance markets. He is a Non-executive Director of Jelf and Computershare Ltd, Royal Mail, Just Retirement and CPP. He is Chairperson of the Discovery Limited Audit and Risk Committee.



Sonja Sebotsa

Non-executive Director (Independent)

LLB (Hons), MA

Sonja is the founder and principal partner in Identity Partners, an investment firm which makes equity investments, carries out advisory work and provides debt and equity finance for SMEs through the Identity Development Fund. Sonja's areas of study were law, business and economics. Until August 2007, she had been an Executive Director of WDB Investment Holdings where she led the structuring of several of WDB's investment transactions. Before this she was a Vice President in the investment banking division of Deutsche Bank, where she worked in Mergers and Acquisitions and Corporate Finance in South Africa and the UK.



Tania Slabbert

Non-executive Director

BA, MBA

Tania was CEO of WDB Investment Holdings for 10 years, during which time she managed the growth of the company's portfolio of investments. In October 2013 she was appointed CEO of the WDB Trust, the investment company's sole shareholder. In her new role, she continues to further the WDB Group's mission of sustainable economic development for rural women in South Africa by providing them with access to financial and non-financial resources. Before joining WDB, Tania spent four years in the diplomatic corps several years in West Africa working in the non-governmental sector. Her other directorships include BP South Africa, the Bidvest Group and Caxton.



Sindi Zilwa

Non-executive Director (Independent)

BCompt (Hons), CTA, CA(SA), Advanced Taxation Certificate (SA), Advanced Diploma in Financial Planning, Advanced Diploma in Banking

Sindi is the Chief Executive Officer of Nkonki, a chartered accountancy firm. In 1990, she became the second black woman to qualify as a chartered accountant in South Africa. In 1998, she was awarded the Business Women of the Year title by the Executive Women's Club, and in 2008, the Woman of Substance Award by the African Women Chartered Accountants Forum. She serves on the Boards of Aspen, Rebosis, Metrofile, Gijima and Alexkor SOC Limited and Air Traffic Navigation Services Limited. She has recently authored a book, "ACE Model-Winning Formula for Audit Committees."

Corporate Governance Committees and Secretary

	Board of Directors	Audit and Risk Committee	Actuarial Committee	Social and Ethics Committee	Remuneration Committee	Executive Committee
MI Hilkowitz (Chairperson)	6/6◊				2/2	
P Cooper	6/6				2/2	
A Gore (Chief Executive Officer)	6/6			3/3		M◊
BA Brink	6/6			3/3		
A Ntsaluba	5/6			3/3		M
J Durand	5/6				2/2◊	
SB Epstein	6/6					
HD Kallner	6/6			3/3		M
R Farber	6/6		6/6	3/3		M
NS Koopowitz	5/6					M
TV Maphai	6/6					
HP Mayers	6/6		4/6	3/3		M
V Mufamadi**	2/3					
AL Owen	6/6	6/6◊	3/6			
A Pollard	3/6					M
JM Robertson	6/6			3/3		M
SE Sebotsa	5/6	5/6				
T Slabbert	5/6			3/3		
B Swartzberg	6/6		5/6	3/3		M
SV Zilwa	4/6	4/6		3/3◊		
J Broomberg(1)	6/6			2/3		M
KS Rabson(2)	5/6					M
P Tlhabi(1)	6/6			2/3		M
AB Rayner(3)			6/6◊			
S Matisonn(3)(4)			6/6			M
RW Williams(3)			6/6			
R Lee(3)			6/6			
D Govender(4)						M
P Harvey(4)						M
L Izikowitz(4)						M
K Mayet(4)						M
R Noach(4)						M
G Novick(4)						M
A Ossip(4)						M
E Stipp(4)						M
B Sundelson(4)						M
P Thompson(4)						M
R van Reenen(4)						M
S Vyvyan-Day(4)						M
MJ Botha (Company Secretary)						

Key

** *Resigned December 2012*

◊ *Chairperson of the Committee*

(1) Directors of Discovery Health (Pty) Limited only

(2) Director of Discovery Life Limited only

(3) Not directors of Discovery Limited

(4) Executive Management



How we address the recommendations of the King Code on Governance Principles (King III) for Discovery

During the year under review, Discovery complied with the mandatory principles of governance as contained in the JSE Listings Requirements, as well as with the principles of King III. In assessing adherence to the King III principles, a compliance programme is in place whereby the level of compliance across the Group is monitored at regular intervals. The details on the following pages illustrate how we have applied the principles of King III. Where a principle has not been applied, this has been highlighted and explained. For the full King III register, please refer to our website at www.discovery.co.za

Corporate governance forms the foundation of how we conduct our operations. As a values-based organisation, Discovery embraces the four values underpinning good governance: fairness, accountability, transparency and responsibility. Our company values permeate our business operations and form an integral part of Discovery's Code of Conduct. Corporate governance is important because it ensures we conduct business in a responsible, ethical and transparent manner. Discovery's Board of Directors is committed to ensuring that both our local and foreign business operations are run in a responsible manner with a view to maintain sustainable economic, social and environmental performance.

Ethical leadership and corporate citizenship

The Discovery Board governs the organisation in an effective and ethical manner such that the business is synonymous with the qualities of integrity, honesty, fairness, intellectual leadership and tenacity.

These characteristics are manifested in the form of Discovery's values. Our values are embedded in all business operations through a Code of Conduct which is subscribed to by the Board and prescribed and applicable to all employees.

The Code of Conduct sets out Discovery's commitment and approach to conducting business ethically, and in the best interests of all stakeholders. It is regularly communicated to all employees and a number of programmes are in place to create awareness of Discovery's values and ethics standards.

Discovery has established various sustainability initiatives under a Framework for Sustainable Development which incorporates corporate social investment (CSI) initiatives, enterprise development and transformation and environmental issues. These initiatives and projects are aimed at ensuring that Discovery has a positive impact on society and that there is always a correlation between business impact and community benefit. For more information on our sustainability performance and initiatives, please read our 2013 Sustainable Development Report, available online at *www.discovery.co.za/info/sustainabledevelopment*

Board of Directors

The core purpose of Discovery is to make people healthier and to enhance and protect their lives. Discovery has a unique entrepreneurial spirit with a strong emphasis on innovation. The Discovery Board of Directors (Board) has the responsibility to preserve these special attributes while at the same time ensuring that the principles of sound and uncompromising good governance are observed.

The Board is ultimately responsible for the performance and strategy of Discovery. By selectively delegating authority and certain functions to the various committees, the Board does not absolve themselves from their own responsibilities towards Discovery. Each committee operates under written terms of reference, which are approved by the Chairperson of the Board.

Discovery's Board has a clear division of responsibilities between itself and the executive management. During the past year, Discovery appointed one executive director and one non-executive director to the Board. At the time of publishing this report, the Discovery Board consisted of 10 non-executive directors (seven are independent) and nine executive directors.

Board proceedings: The Board meets six times a year, with additional meetings arranged where necessary. Three additional meetings were convened during the year under review.



Figure 1: Overview of the Board and Sub-committees

The long- and short-term strategies of Discovery are discussed and agreed with executive management in an annual strategy day. The focus of these discussions is around the Group strategy and takes into account risks, opportunities and the sustainability of the Group.

Board Charter: A Board Charter, which sets out the roles and responsibilities of the Board, has been adopted and this is reviewed annually. The Charter provides directors full and unrestricted access to relevant information pertaining to Discovery and allows them to access independent professional advice at Discovery's expense to assist them in their duties.

Role of the Chairperson: The Chairperson has been a non-executive director of Discovery for 11 years. The Board of Directors considered the Chairperson's independence and taking into account the independence criteria applied to Board members, found him to be independent.

The roles of the Chairperson and the Chief Executive Officer are separate with each having their own set of duties. The Chairperson is responsible for leading the Board and the Chief Executive Officer for the operational management of the Group. The division of responsibilities ensures a balance of power so that no individual has unrestricted decision-making powers or authority.

Succession plan of the Chairperson and senior executives: Succession plans, which are reviewed and updated annually, are in place for the Chairperson of the Board as well as the senior executives within the Group.

Appointment and rotation of directors: The Board has agreed not to appoint a nomination committee but an ad-hoc sub-committee may be established for the search and vetting of potential directors. To ensure that the mix of skills, experience and technical expertise of the directors remains appropriate, the Board retains responsibility for the appointment of new directors.

Non-executive directors are appointed for three years and re-appointment is not automatic. As per the Board Charter, one-third of the non-executive directors rotate annually by retirement. Executive directors have contracts that may be terminated with one to three months' notice.

Assessment of independent directors: In assessing the independence of non-executive directors, the Board takes into account the personal shareholding of the individual director, the director's own or family involvement in Discovery's business and the fact that the remuneration earned by the directors is not contingent on the performance of the Group.

Assessment of the Chairperson: The Board evaluates the performance and independence of the Chairperson annually by means of a questionnaire. The results of the assessment found the Chairperson to fulfil his role independently and to the satisfaction of the Board as a whole.

Board performance assessment: A collective board-effectiveness evaluation is conducted annually. The Chairperson meets with individual directors on a one-to-one basis throughout the year to discuss matters relevant to their directorship. Overall, it was found that the Board has a wide array of skills and experience required for the oversight of the Group as a whole.

Continuous professional development: Induction and orientation programmes are in place for new directors, including an explanation of their fiduciary duties and responsibilities. They also go on visits to different parts of the businesses for discussions with management on industry-specific issues.

Continuous educational programmes incorporating financial, actuarial, economic and industry-related matters are available to all directors. During the year under review, specific training on Solvency Assessment and Management (SAM) was provided.

Management of directors' interest: A declaration of interest register is regularly updated by the Company Secretary. Directors' interests are disclosed before any Board meeting and directors are encouraged to disclose their interest whenever it arises.

Trading in Discovery shares: Discovery adopted a policy enforcing closed periods prohibiting trading in shares by directors, senior executives and employees a month before the interim and final financial period. All directors trading in shares require the prior approval of the Chairperson of the Board and senior management are required to notify the Financial Director prior to the transaction. The Company Secretary keeps a record of such trading and approvals.

Company Secretary: The Company Secretary is suitably qualified and has the requisite knowledge and skills to fulfil his duties and responsibilities. This is reviewed bi-annually by the Financial Director, in his performance appraisals. He has been the Company Secretary since 2001 and is not a director. Furthermore he has not participated in any share incentive programme or scheme and thus remains impartial. The directors have unlimited access to the advice and services of the Company Secretary, who ensures that all members adhere to the administration protocols of Board and sub-committee proceedings. The Board is satisfied that the Company Secretary is qualified to fulfil his duties and responsibilities to the Group.

Board committees

Audit and Risk Committee

The Audit and Risk Committee is responsible for assisting the Board in terms of the financial reporting processes, internal controls, risk management, compliance with legislation and internal and external audit processes.

The Committee consists of three highly skilled and experienced independent non-executive directors with extensive actuarial, insurance, economics and accounting skills. Members of the Committee are elected at the Annual General Meeting on recommendation of the Board and have the right to consult with specialists or consultants if required. The Chairperson of the Board, Chairperson of the Actuarial Committee, executive management team and Heads of the Finance, Risk, Compliance and Internal Audit Functions, as well as the external auditors, attend the meetings by invitation.

Audit and Risk Committee proceedings: The Audit and Risk Committee meets six times a year with the mandate to convene additional meetings as circumstances require. The Chairperson of the Committee reports at each Board meeting on its activities and attends the Annual General Meeting to answer questions concerning matters falling within the ambit of the Committee. The Committee regularly meets with the internal and external auditors, as well as the Heads of Risk and Compliance, without members of management present.

For more details, refer to the Report of the Audit and Risk Committee on page 140 of the Integrated Annual Report.

Actuarial Committee

The Actuarial Committee assists the Board with actuarial matters and their fiduciary duties towards members, policyholders and shareholders.

The Committee consists mainly of executive directors and non-Board members who provide industry expertise, as well as an independent and unbiased perspective on actuarial matters impacting Discovery. The Committee is chaired by a non-Board member recognised in the industry as a technical leader in his field.

The PruHealth Group in the UK and Discovery Insure have their own Actuarial Committees that are responsible for specific issues relating to the pricing and underwriting of these companies' products. The work of these Committees is overseen by the Discovery Actuarial Committee.

Actuarial Committee proceedings: The Actuarial Committee meets six times a year with the mandate to convene additional meetings as circumstances may require. Two additional meetings were scheduled during the past year.

The responsibilities of the Actuarial Committee are:

- to ensure that all relevant actuarial risks within Discovery are identified and analysed
- to consider the financial soundness valuation results of Discovery, including overall methodology and assumptions used to value the assets and liabilities of the Group
- to consider the embedded value results of Discovery, including the overall methodology and assumptions used in the embedded value calculation
- to review the external disclosure of the embedded value results of Discovery
- to consider the capital position of Discovery
- to review all reinsurance arrangements.

Social and Ethics Committee

The Social and Ethics Committee assists the Board in its responsibilities towards the requirements of transformation, ethics management and sustainable development within Discovery. The Committee's scope covers all South African subsidiaries within the Discovery Group.

The Committee is mainly constituted by executive directors and the Chairperson is a non-executive independent director. Taking into account the objectives of this Committee, the Board is of the view that the skills, experience and knowledge of the current Committee members is appropriate in overseeing the Committee's activities.

Social and Ethics Committee proceedings: The Committee meets three times a year, with additional meetings being held when required. The Committee may invite any directors, professional advisors, or officers whose input might be required at the meeting.

The responsibilities of the Social and Ethics Committee are:

- to monitor the company's standing in terms of the 10 principles set out in the United Nations Global Compact Principles and the Organisation for Economic Cooperation and Development (OECD) recommendations regarding corruption and relevant legislative requirements
- to review and approve for recommendation to the Board the company's stakeholder policy
- to review and approve a framework for stakeholder engagement and the Stakeholder Engagement Policy
- to monitor the company's activities in respect of stakeholder relationships, including the company's advertising, public relations and compliance with consumer protection laws
- to monitor the company's performance in relation to good corporate citizenship as well as the environment, health and public safety

- to review and approve the Enterprise Development Policy, the Employment Equity Plan, the Preferential Procurement Policy, the CSI strategy and projects proposed by management
- to review and approve, for recommendation to the Board, the Sustainable Development strategy and key sustainability indicators
- to consider and review the Ethics Framework, the Code of Conduct and any complaints received by the Group
- to make recommendations to the Board regarding any potential conflicts of interest of a material nature.

Remuneration Committee

The Remuneration Committee assists the Board in terms of the Group's remuneration strategies, principles and employment policies.

The Remuneration Committee consists of three independent non-executive directors. Impartial remuneration experts are invited to meetings to assist in advising the Committee.

Details of the respective directors' remuneration for the year under review can be found on page 258.

Remuneration Committee proceedings:
The Committee met twice during the year. Members of executive management and the Chairperson of the Internal Remuneration Committee also attend the meetings by invitation. Executive directors are not allowed to participate in discussions regarding their own remuneration nor are they entitled to a vote at the meetings.

The responsibilities of the Remuneration Committee are:

- to assist the Board in its responsibility for setting and administering remuneration policies in Discovery's long-term interest
- to ensure that Discovery's employees are remunerated fairly and equitably taking into account Discovery's performance and external market trends
- to make recommendations to the Board on the remuneration structures of non-executive directors
- to ensure that the remuneration of executive directors is sufficient to attract, retain and motivate them
- to approve a policy relating to bonus and share incentive schemes.

Group Executive Committee

The Group Executive Committee is mandated and responsible for implementing the strategies approved by the Discovery Board and for managing the affairs of the Group.

The Group Executive Committee is chaired by the Chief Executive Officer and meets weekly.

The different business units, including the offshore operations, also have Executive Committees that meet regularly. Feedback on the activities of each business unit is given at the weekly meetings of the Group Executive Committee.

Control functions within Discovery

To further strengthen the Board's governance oversight, they have mandated the establishment of Independent Control Functions that operates at a Group level.

The oversight of the activities of these Functions has been delegated to the Audit and Risk Committee.

Group Risk Management

The Discovery Board is ultimately responsible for the governance of risk across the Group. The Board Charter outlines the directors' responsibilities for ensuring there are risk management processes in place to enable complete, timely, relevant, accurate and accessible risk disclosure to all stakeholders. As sub-committees of the Board, the Audit and Risk and the Actuarial Committees have been delegated the responsibility to oversee the operational effectiveness of the risk management system.

The Board maintains and is accountable for the Enterprise Risk Management Policy and implementation of the Risk Management Plan. In conjunction with the Group Risk Management Function, the Chief Executive Officers and executive management teams are responsible for the management of all risks and for implementing the Risk Policy and Plan through a common and integrated Enterprise Risk Management Framework.

The Board reviews and approves the level of risk appetite and tolerance for each category of risk to which each business is exposed. Many factors are considered when setting the appetite and tolerance. Some of these include considerations of business maturity, risk management maturity, Discovery's propensity to take risk, Discovery's ability to control risk, capital and funding constraints and reputational impacts.



Figure 2: Overview of the control functions

An evaluation of the effectiveness of the risk management system is performed on an annual basis by the Group Internal Audit Function. For more information on the Risk Management Report, refer to page 128 of the Integrated Annual Report.

Group Compliance

The Group Compliance Function's primary responsibility is to assist the Board and the Chief Executive Officers to ensure that all local and international business operations are run with integrity, comply with all applicable legal and regulatory requirements as well as comply with international standards of best practice.

The responsibility of Group Compliance is to implement controls ensuring the appropriate management of Regulatory Compliance Risks. Group Compliance works closely with Group Risk Management but operates as a separate division within Discovery. This enables close alignment to the Risk Management Framework while ensuring that the regulatory exposures and opportunities within Discovery receive focused and appropriate attention.

The Chief Compliance Officer reports to the Audit and Risk Committee on all regulatory, legal and supervisory developments and the impact that they might have on other relevant legislation as well as functionally to the Chairperson of the Audit and Risk Committee.

To ensure the identification, assessment and appropriate response to the risk of non-compliance, a compliance framework has been developed and implemented to ensure that regulatory exposures are managed in accordance with Generally Accepted Compliance Standards.

Requests for Information and Promotion of Access to Information Act: During the year under review, we received two requests for information in terms of Promotion of Access to Information (PAIA). Both were refused due to the fact that the requestor was unable to adequately substantiate the nature of the rights that they were seeking to protect. For more information on the Compliance Report refer to page 140 of the Integrated Annual Report.

Group Internal Audit

The Group Internal Audit Function operates within the ambit of a clearly defined charter which has been approved by the Audit and Risk Committee. Their main focus is to provide a systematic, disciplined approach to the evaluation and improvement of the effectiveness of the internal control systems, risk management and governance processes.

Group Internal Audit is staffed with suitably qualified, competent and ethical staff, affiliated to the Institute of Internal Auditors (IIA) and other professional bodies. These employees are not involved in any day-to-day operations of Discovery, nor do they assume the responsibility for the implementation of any internal control systems or direct the activities of any employee.

Group Internal Audit annually prepares a risk-based audit plan in consultation with management, Group Risk and Group Compliance. This plan, as well as the Group Internal Audit Budget, is approved annually by the Audit and Risk Committee and the effectiveness of the function is also assessed. As far as possible, planning is coordinated with the external auditors in order to minimise duplication of audit effort.

The Audit and Risk Committee is also mandated to approve the appointment and dismissal of the Chief Audit Executive (CAE).

The Internal Audit Plan includes capacity for the review of the effectiveness of Internal Financial Controls:

- ***Internal Financial Controls:*** Specific attention is given to testing the control effectiveness and evaluating the results based on the design, implementation and operation of internal controls in the Group. This is done through a formal documented process and the results are reported to the Audit and Risk Committee.
- ***Combined Assurance:*** A Combined Assurance model was adopted as part of the Governance and Control Framework. Group Internal Audit annually provides an estimation to the Audit and Risk Committee on the adequacy of the Combined Assurance approach.

Governance of Information Technology (IT)

The Board is responsible for IT governance and ensuring that IT is aligned to the performance objectives of the Discovery Group. They have appointed a Group Chief Information Officer whom they believe is suitable, qualified and experienced and who reports to the Board on all IT-related matters.

A formal IT Governance Framework consisting of various policies, standards and guidelines have been approved and implemented within the Group. This Framework is fundamental to the operations of Discovery and covers:

- the implementation of a dedicated Information and Data Security Function to ensure that an appropriate Information Security Programme is put into practice within the business
- the establishment of a formal process to oversee and manage all IT investments and capital expenditure
- the establishment of a number of operational and strategic IT Oversight Committees to ensure that the Group infrastructure appropriately supports business objectives and strategy
- the implementation of a Business Continuity Framework to ensure that appropriate plans and controls are in place so that all aspects of business resilience and disaster recovery are adequately dealt with.

Enterprise Risk Management report

Enterprise Risk Management provides a framework for managing risks, which typically involves identifying particular events or circumstances relevant to Discovery's objectives (risks and opportunities), assessing them in terms of likelihood and magnitude of impact, determining a response strategy where necessary and monitoring progress.
By identifying and proactively addressing these risks and opportunities, Discovery's local and international operations are able to protect and create value for its stakeholders.

Our Risk Management strategy

Discovery is committed to being an organisation with a high-quality Enterprise Risk Management capability which encompasses all its activities and tangibly contributes to growth in economic value and the protection of policyholder benefits and shareholder assets. This is achieved by:

- fostering an environment where consideration of risk is embedded in Discovery's culture, business planning, decision-making and day to day business activity
- being risk-conscious, risk-confident and not risk-averse. Risks are considered appropriate if they are well understood, generate the required risk adjusted return (either financially or otherwise) and support Discovery's strategic objectives. Discovery actively seeks to assume appropriate risks, against the background of a clearly articulated risk appetite and business strategy
- seeking to avoid, mitigate and/or transfer those risks for which Discovery has little or no appetite or where the expected risk-adjusted return is inadequate
- actively communicating the effectiveness and business benefits of risk management to all stakeholders
- continually developing and enhancing Discovery's Enterprise Risk Management capability in a manner that yields business benefit
- providing reasonable and independent assurance to Discovery's senior management and Board.

The role of the Risk Management Function

The Risk Management Function aims to:

- assist the Board of Directors, the various Committees and senior management in carrying out their respective responsibilities by coordinating risk management activities across Discovery
- identify the risks Discovery faces and evaluate the internal and external risk environment on an ongoing basis in order to assess potential risks as well as emerging risks as early as possible.

This may include looking at risks from different perspectives, such as by territory or by line of business

- assess, challenge, aggregate, monitor, help manage and otherwise address identified risks effectively. This includes assessing Discovery's capacity to absorb risk with due regard to the nature, probability, duration, correlation, and potential severity of risks, as well as assessing the adequacy of the control environment
- recommend Discovery's risk appetite to the Board for approval, including cascading down to an appropriate level of detail and monitoring the actual risk exposure against the Board-approved appetite
- gain and maintain an aggregated view of the risk profile of Discovery and its individual operations
- set standards and guidelines relating to risk management methodology and techniques of quantification
- conduct regular stress testing and scenario analyses, including those in respect to outliers or issues with a low probability but high potential impact
- regularly report to senior management, key persons in control functions and the Board of Directors on Discovery's risk profile, risk events that have occurred, details of the risk exposures faced and the related mitigating actions required
- incorporate a feedback loop based on appropriate and good quality information, management processes and objective assessments. This enables the Group Risk Management Function to take necessary actions in a timely manner in response to changes in Discovery's risk profile
- conduct regular assessments of the risk management system and ensure that all necessary improvements are implemented
- document and report material adverse changes affecting Discovery's risk management system to the Board of Directors to help ensure that the Framework is maintained and improved.



Enterprise Risk Management provides a framework for managing risks, which typically involves identifying particular events or circumstances relevant to Discovery's objectives (risks and opportunities), assessing them in terms of likelihood and magnitude of impact, determining a response strategy where necessary and monitoring progress.

Our Enterprise Risk Management Process

The Enterprise Risk Management Process at Discovery aims to contribute towards both growth in economic value and the protection of policyholder and shareholder assets.

Discovery Enterprise Risk Management Process

Risk Identification

- The risk identification process seeks to determine those risks that would prevent Discovery from meeting its business objectives and therefore addresses all categories of risk. The risk identification process is performed at all levels of the organisation and follows either a bottom up or top down approach.
- *Bottom up approach* – involves a process of identifying, analysing and evaluating the key operational risks and controls across all entities within the Group.
- *Top down approach* – involves routine risk assessments with executives and senior management who are involved in the strategic planning process and who make decisions about risk and return that could significantly impact the Group's risk profile.

Risk Analysis

- Control Evaluation: Controls are identified, categorised and assessed for each risk that has been recognised during the risk identification process. Controls may either be a single control activity that is capable of mitigating the risk, or a number of control activities that, in combination, mitigate the risks to an acceptable level. Controls include all measures taken to mitigate potential liabilities and exposure to risks.
- *Residual Risk Assessment:* Risks are classified based on the impact and likelihood of them occurring. The residual risk assessment assists in quantifying the exposure that Discovery has to a risk, after taking the control environment into account. A combination of both expert judgment and objective evidence is required to arrive at the appropriate risk rating.

Risk Evaluation

- The purpose of a risk evaluation is to implement or review management action plans to address unacceptable risk exposures, control weaknesses, risk events and key risk indicator breaches. The decision to create an action plan is based on the residual risk rating. Risk evaluation will assist the business in making decisions, based on the outcome of the risk analysis process. The management team at Discovery ensures that actions are tracked, communicated effectively and implemented successfully for maximum benefit to be derived from the process.

Risk Monitoring

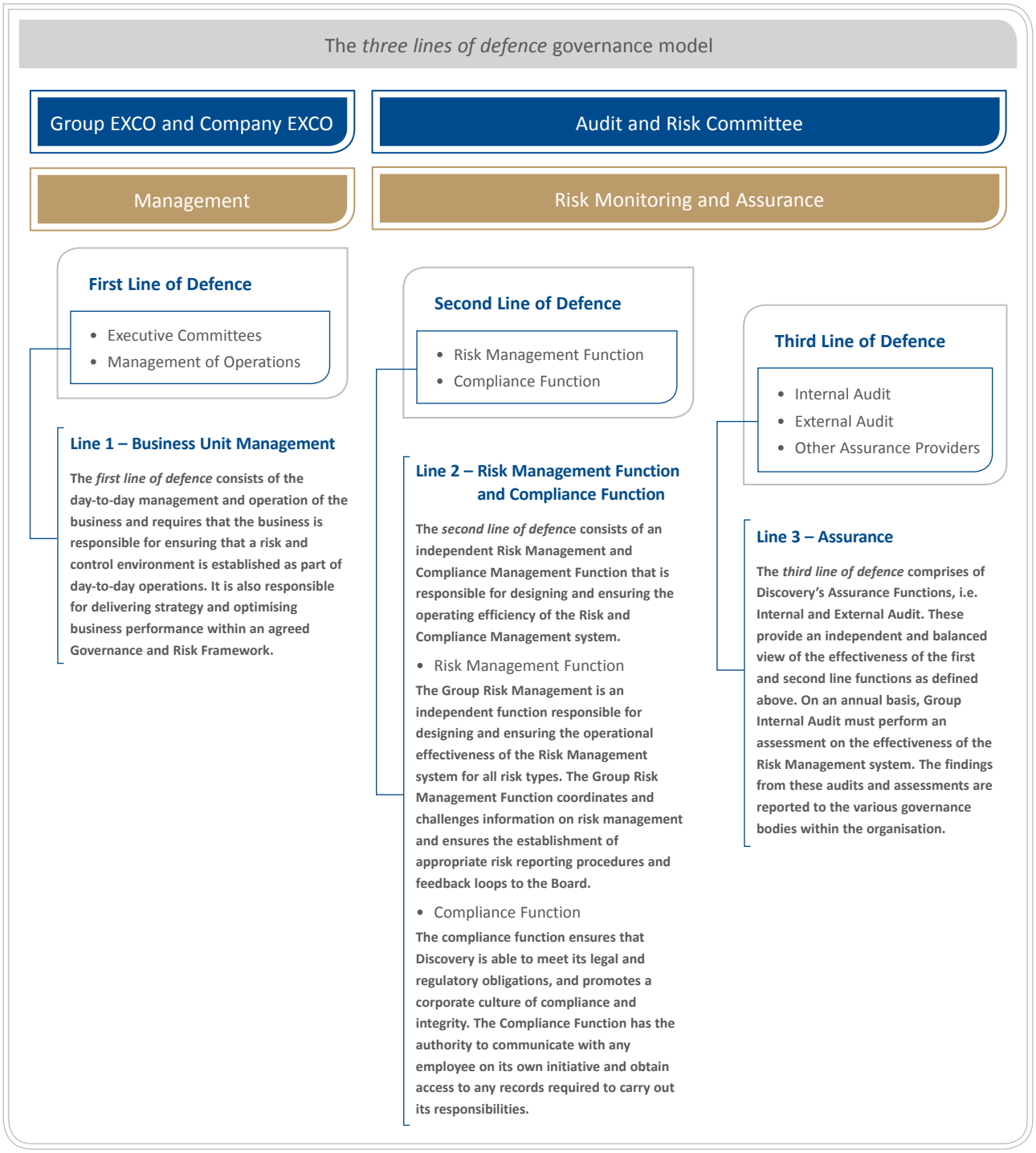
- Risks are continuously monitored. This process involves the planning and tracking of new risks, constantly reviewing existing risks, monitoring action plans and residual risks, as well as reviewing the execution of risk responses while evaluating their effectiveness.

Risk Reporting

- All risk is reported on every two months, with detailed commentary on *medium high* and *high* risks as well as a summary of risk events that have occurred, in line with the Audit and Risk Committee meetings. Risk events and near misses are reported on a weekly basis to the Discovery Holdings Executive Committee. The risk reporting process enables the effective monitoring and reporting of risk and capital management issues across Discovery and provides assurance that the Enterprise Risk Management Framework is operating as intended.

How do we manage risk

Discovery uses the *three lines of defence* governance model as a key principle of operation. It is designed to promote transparency, accountability and consistency within the risk management process through the clear identification of well-defined roles, the clear separation of business management, governance and control structures and the tracking of performance against accountabilities.



Group Compliance report

Compliance Risk refers to the risk that the controls and procedures implemented to comply with laws, regulations, supervisory requirements or industry codes may be inadequate or ineffective, potentially resulting in legal or regulatory sanction, financial loss or loss to reputation.

Given our geographical footprint and the requirement to adhere to various local and international laws, rules, codes and standards, compliance is built into our corporate governance structures and frameworks at Discovery.

Our approach to compliance

The Group Compliance Function's primary responsibility is to assist the Board and the Chief Executive Officers to ensure that all local and international business operations are run with integrity and comply with all applicable legal and regulatory requirements and international standards of best practice. Discovery has no risk appetite to knowingly fail to adhere to any of the regulatory requirements. The Group will seek to avoid any breach of regulation that may result in enforcement action by a regulator. All instances of non-compliance are investigated and the appropriate action taken.

While the South African business operations are supported by experienced compliance officers within the centralised compliance team, our international business areas are supported by dedicated compliance teams in their respective environments. The work of these teams is closely aligned to the standards and guidelines in place within the Group Compliance Function in South Africa.

This allows the Group Compliance Function to set standards and guidelines applicable to both the local and international business operations, to perform independent monitoring and to provide easy access to technical expertise in terms of specific regulatory requirements.

The structure of the Function enforces the independence of the Compliance Function and ensures that dedicated focus is given to compliance matters throughout all business areas in the Group. This is a very important component of good corporate governance and is a requirement of King III and other legislation.

Group Compliance is also responsible for the implementation and monitoring of an Anti-Money Laundering Control Framework within the Group.



Regulatory environment

Discovery is regulated by several local and international regulatory authorities. Contact with our regulators takes place through authorised individuals on both a formal and informal basis. We always seek to maintain a relationship of trust and transparency with our regulators. Our key regulators are:

Financial Services Board (FSB)
The FSB regulates non-banking sectors of the financial services industry, including pension funds, long-term and short-term insurance, collective investment schemes and financial advisory and intermediary services.

National Credit Regulator (NCR)
The NCR was established to regulate the South African credit industry.

Council for Medical Schemes (CMS)
The CMS provides regulatory supervision of private health financing through medical schemes.

Financial Intelligence Centre (FIC)
The FIC was established to identify the proceeds of unlawful activities and to combat money laundering activities.

Department of Trade and Industry (DTI)
The DTI focuses on consumer protection and develops legislation to encourage appropriate business practices and enable consumers to exercise their rights.

National Consumer Commissioner (NCC)
The Office of the Consumer Commissioner was established with the implementation of the Consumer Protection Act in April 2011 and is responsible for promoting consumer rights.

Financial Conduct Authority (FCA, United Kingdom)
The FCA's strategic objective is to ensure that the financial services market functions effectively by:

- securing an appropriate degree of protection for consumers
- protecting and enhancing the integrity of the financial system in the UK
- promoting effective competition in the interests of consumers.

Prudential Regulatory Authority (PRA, United Kingdom)
The PRA is responsible for the prudential regulation and supervision of banking and non-banking institutions in the UK.

The PRA serves to promote the safety and soundness of regulated institutions and contribute to securing appropriate protection for policyholders.

Information Commissioner's Office (United Kingdom)
The independent regulatory office deals with the Data Protection Act 1998 and the Privacy and Electronic Communications (EC Directive) Regulations 2003 across the UK.

Guernsey Financial Services Commission (GFSC, United Kingdom)
The GFSC is the regulatory body for the finance sector in the Bailiwick of Guernsey. The Commission's primary objective is to regulate and supervise financial services in Guernsey.

Discovery's focus areas during the past year

- **Continuing our efforts to ensure the protection of our clients' rights and personal information:** We have made progress over the last 12 months with various projects across the business focused on strengthening controls and procedures to protect our clients' personal information. In line with the recent finalisation of the Protection of Personal Information Bill in Parliament, we plan for a number of initiatives to be completed and delivered over the next 12 months.
- **Establishment of a framework to monitor and report on the fair treatment of customers:** Work around the implementation and embedding of the Treating Customers Fairly (TCF) Framework within our South African operations is ongoing and we have completed a number of initiatives focused on the treatment of customers over the past year. We continue to participate in industry forums as well as in the regulatory process.
- **Implementation of the Solvency and Assessment and Management (SAM) Framework:** Discovery's project to implement the requirements of the SAM Framework is making good progress and is aligned with the proposals initiated by the FSB. We are actively participating in the FSB industry programme in this regard.
- **Continued strengthening of our Information Security Controls:** We have completed a number of projects during the past year focused on formalising and strengthening our Information Security Framework. Information security remains a key element of the Protection of Personal Information (PPI) programme within Discovery. As such, we will continue to focus on this over the next 12 months.

Regulatory developments and focus areas for the coming year

A number of new regulatory requirements will have an impact on the business areas during the coming year. These are:

- **Protecting the rights and personal information of our clients:** Work around the implementation of the Protection of Personal Information Bill requirements is ongoing within local operations and plans are in place to deliver the outstanding projects by August 2014. At the same time, we are monitoring developments around Data Protection that may impact the programmes we currently have in place within the UK environment.

  Work around the formalisation of the Treating Customers Fairly programme within the South African operations is also on track and we are actively participating in various industry initiatives.
- **Solvency Assessment and Management and Solvency II:** During the next year, we will be focusing on the implementation of the Pillar II requirements contained in the proposed interim measures, as set out in the Insurance Laws Draft Amendment Bill. Work around the Capital Requirements as set out in Pillar I of the FSB programme is ongoing and we are actively participating in industry and regulatory initiatives in this regard.

  Work around the implementation of the Solvency II requirements in the UK is also on track and we will continue our participation with programmes and information requests from UK regulators.



Approximately 80% of short-term incentives is paid in arrears – in September each year in respect of the immediately preceding financial year. The remuneration details on page 258 reflect the remuneration paid during the financial year. Accordingly, the details in respect of short-term incentives reflected in the year ended 30 June 2013 substantially reflect the incentives paid in September 2012 in respect of the performance for the financial year ended 30 June 2012.

Remuneration report

Introduction

This report sets out the remuneration philosophy and the salient points of the policies that Discovery has adopted in respect of executive management, employees and non-executive directors.

Remuneration philosophy

The remuneration process is designed to support the successful execution of the organisational strategy by:

- attracting, motivating and retaining quality employees
- encouraging and rewarding employees to achieve or exceed the objectives of the business
- aligning the economic interest of employees with those of other stakeholders
- fostering Discovery's owner-manager culture.

Our philosophy is to balance a flexible approach that recognises differences in individual performance, value and contribution to the organisation, with a consistent framework that ensures equitable pay levels and defensible remuneration decisions. At all levels there is a rigorous objective setting process to ensure that shareholder objectives are met and/or exceeded.

Discovery aims to be an employer of choice. For base pay, Discovery takes cognisance of the 50th percentile of the financial services market. However, Discovery's philosophy is to pay above market where required to attract the best talent, especially for critical skills. In addition, Discovery pays short-term performance-based incentives to its employees that enable the individual to earn above market levels if their performance supports this.

Responsibility for developing and governing remuneration

The Board is ultimately responsible for the Remuneration Policy. To assist the Board in fulfilling its responsibilities, it has appointed and mandated a Remuneration Committee, which consists of non-executive directors and an independent expert.

The primary objective of the Remuneration Committee is to provide input to and approve the reward strategy. It is responsible for:

- approving remuneration packages for executive directors
- approving policy relating to bonus and share incentive schemes
- recommending the non-executive directors' fees
- reviewing the annual salary increase process and the increases of all senior executives; and ensuring alignment of remuneration practices with Discovery's overall remuneration philosophy.

The Remuneration Committee has delegated some of its functions to the Internal Remuneration Committee. This latter body is responsible for:

- detailed analysis and development of research-based recommendations to the Remuneration Committee
- the remuneration packages of management and employees in general (with the exception of directors) in line with the policy
- supervising the increase process and reporting any anomalies to the Remuneration Committee.

The Remuneration Committee uses the services of a number of advisers to assist in tracking market trends related to all levels of employees, including PE Corporate Services, Mabili Reward, Remchannel Financial Reward Survey and 21st Century Business and Pay Solutions.

Remuneration Committee membership

J Durand is the Chairman of the Remuneration Committee. Other Remuneration Committee members are P Cooper and M I Hilkowitz. T Slabbert and M Olivier (independent remuneration expert), who both have experience in this area, attend the meeting by invitation.

Meeting attendance can be found in the table on page 122.

All Remuneration Committee members have the relevant skills and experience to perform their duties.

Remuneration for executive directors

The executive directors on Discovery's Board as at 30 June 2013 were:

- A Gore
- R Farber
- H Kallner
- NS Koopowitz
- HP Mayers
- A Ntsaluba
- A Pollard
- JM Robertson
- B Swartzberg

All executive directors are employed on employment contracts that are cancellable on between one month and three months notice by either the executive or the company.

The remuneration of executive directors for the financial year can be found on page 258.

Remuneration packages for executive directors comprise the following components:

Guaranteed component

All executive directors receive a guaranteed element of remuneration. This is based on cost to company. Cost to company comprises a fixed cash portion and compulsory benefits (medical aid, life cover and retirement fund membership).

Comparative studies of peer groups and similar size companies are used together with market survey data in determining adjustments to the executive directors' guaranteed remuneration to ensure positioning of pay in line with the Group's remuneration philosophy. International benchmarks are considered for HP Mayers, A Pollard and NS Koopowitz, taking into account their international duties. All of Discovery's executive directors receive guaranteed remuneration in line with market levels, taking into account their responsibilities.

Short-term incentives

Short-term incentives are designed to reward executive directors for achieving stipulated strategic annual objectives, thereby ensuring that a significant portion of executive directors' cost is variable.

Executive directors' short-term incentives comprise two components:

- an annual personal incentive linked to individual goals for each director; and
- a "profit pool" element which allows senior management to share in profit if the Group's performance is above certain profit hurdles.

Typically the split between individual and profit pool components is 25% and 50% of salary respectively. In each case, there is a threshold below which no incentive is paid. These thresholds are set strategically based on the business area and level.

Long-term incentives

Long-term incentives aim to encourage executive directors to execute the long-term strategy of the Group successfully to achieve its long-term objectives. Executive directors take part in the Group's share-based incentive scheme. This scheme is described in more detail below, and details of the allocation to executive directors can be found from page 260.

Remuneration for senior management and employees

The aggregate remuneration of the Discovery directors and Executive Committee members for the financial year can be found on page 235.

Remuneration packages for senior management and employees contain some or all of the following components, depending on the individual's level in the Group and contributing to the key initiatives:

Guaranteed component

All permanent employees who are not in a sales function, irrespective of level, receive a guaranteed element of remuneration. This is based on cost to company and comprises a fixed cash portion as well as compulsory benefits (medical aid, life cover and retirement fund membership). The guaranteed portion of the remuneration package is set taking into account base pay at the 50th percentile of the financial services market, and the skills of the specific employee. Increases in the guaranteed component are determined in line with market movements and reflect individual performance.

Employees in a sales function receive a variable monthly remuneration linked directly to their productivity. The level of this remuneration is also benchmarked to the financial services market.

Short-term incentives

At a management level, Discovery uses short-term incentives to encourage achievement of stipulated semi-annual and annual objectives, thereby ensuring that a significant portion of pay is variable and linked to performance.

Senior management's short-term incentives comprise two components (depending on their level):

- a six-monthly personal incentive linked to individual goals for each employee
- a "profit pool" element which allows senior management to share in profit if the Group's performance is above certain profit hurdles.

The Remuneration Committee approves the Group primary bonus pools and oversees the principles applied in allocating these pools to business units and individuals. Typically the split between individual and profit pool components is 25% and 50% of salary respectively. In each case, there is a threshold below which no incentive is paid. These thresholds are set strategically based on the business area and level.

The performance-related pay of employees in many business areas relate directly to their function and is paid monthly, bi-annually or annually. Discovery encourages managers to include an element of performance-related pay in all employees' packages.

On occasion, additional payments are made to employees outside of the formal incentive structure in recognition of exceptional performance or innovation. None of these payments were material in the current year.

Long-term incentives

Senior management, together with executive directors take part in the Group's share-based incentive scheme. The overall individual performance is taken into account when the Remuneration Committee decides on each individual allocation. It is the view of the Remuneration Committee that the incentive scheme is a direct link to the company performance through the share price. In addition, the scheme is intended, primarily to attract and retain competent employees. This scheme is described in more detail below.

Share-based incentive scheme

Discovery operates a share-based incentive scheme that gives employees a bonus that is calculated according to Discovery's share price performance. Discovery pays these incentives in cash. The value of the annual allocation of the share-based incentive scheme at the date of allocation as a proportion of annual guaranteed pay varies between 30% for managers and 60% for executive directors. The final allocation is based on the individual performance. Each year, the Remuneration Committee uses the prior year's allocation and current salary level in assessing the allocation and ensures that final allocation is related to performance.

Discovery implemented this bonus scheme following the introduction of income tax legislation that requires employees to pay income tax on all gains from share options that they receive from their employment. Payments made in terms of this scheme are taxable in the hands of the employee and tax deductible for the company making the payment. Payments are made in equal proportions on the second, third, fourth and fifth anniversaries of allocation.

The participants earn a cash bonus based on the allocation of the bonus scheme units which in turn are linked to the performance of the Discovery share price. Units are issued in September each year; the vesting of the units is equally two, three, four and five years after allocation, subject to the vesting criteria. The cost thereof is then included in the remuneration of the executives in the year of payment. As a result, there is a timing difference between the performance of the company and the reflection of the related remuneration. This is an inevitable consequence of retention being a key objective of the scheme. For example, the units allocated to executives in September 2010 which vest from September 2012 (2013 financial year) will be paid over four years with the first payment in October 2012. This payment will reflect in the executive remuneration in the 2013 financial year.

Discovery has implemented a programme to hedge out the economic risk linked to the share price based on the anticipated payout of the incentive. As the scheme is a phantom bonus scheme, there is no dilution created by these awards.

Further details relating to the share-based incentive scheme can be found in note 34 on page 236.

Allocations under the share-based incentive scheme are made each year, based on the ruling share price at the time of allocation. The units issued in terms of the scheme vest equally and are paid out on the second, third, fourth and fifth anniversary of allocation, based on the share price at the time of payment. Accordingly, if there is a substantial increase in the share price, the payment to the individual will be more than the value at the date of allocation. Similarly, if there is a decline in share price, the payment will decrease accordingly.

Discovery has implemented a programme to hedge this economic risk for the company. Thus, there is a fixed cost to the company and any outperformance is covered through the hedge.

The remuneration details on page 258 reflect the remuneration paid during the financial year. Accordingly, the details in respect of the share-based incentive scheme reflected in the year ended 30 June 2013 reflect payments made in the financial year in respect of units allocated in the previous years, as well as any appreciation in the share price to the date of payment.

Review of long-term incentives

The Remuneration Committee regularly reviews the Group's long-term incentive scheme to ensure alignment to both the Group's long-term objectives and any relevant changes in tax legislation.

Remuneration for non-executive directors

The remuneration of non-executive directors for the financial year can be found on page 258.

Non-executive directors' fees are reviewed annually and benchmarked against industry standards to ensure the fees remain competitive. The Remuneration Committee reviews fees, ensures that professional benchmarking is done and makes recommendations to the Board for consideration. Following recommendations from the Remuneration Committee, the Board proposes for shareholder approval of the fees for non-executive directors.

Non-executive directors receive a combination of fixed and meeting fees for their participation on the Board and Board Committees. Black non-executive directors also participated in the Discovery BEE transaction in 2005. This initiative was approved because the Board believed it highly important to secure the services of black non-executive directors with the relevant skills and experience.

At the AGM held on 1 December 2009, shareholders approved a phantom share scheme for Ms SE Sebotsa, a black non-executive director, to replicate participation in the Discovery BEE transaction.

White non-executive directors do not participate in any share-based incentive scheme.

Non-executive directors' fees

The Board determines the fees for non-executive directors, following a recommendation from the Remuneration Committee. The fees are reviewed annually, taking into consideration the individuals' responsibilities and Board Committee membership. The Chairman is not present when his remuneration is reviewed. In addition, from time to time, the fees are benchmarked to other local and international financial services companies and companies with similar market capitalisation. The fee structure has two components: a retainer and Board or Board Committee meeting attendance fees. For the 2014 financial year, the remuneration of the Board has been split into a fixed retainer and a variable attendance fee to take into account the emerging governance practices. The Chairman of the Board receives a fixed retainer and does not receive any other fees or retainer for attendance at Board or Committee meetings.

The fee structure for the 2013 and 2014 financial years is shown below:

	Financial year 2013	As approved by the Board for the financial year 2014
Retainer for the Chairman of the Board	ZAR 2 662 500	ZAR 2 835 500
SA-based board retainer	ZAR 273 700	ZAR 145 700
SA-based board attendance fees		ZAR 24 280 per meeting
SA-based committee chairperson retainer	ZAR 170 000	ZAR 181 000
SA-based committee members retainer	ZAR 98 000	ZAR 104 000
SA-based committee chairperson attendance fees	ZAR 18 100 per meeting	ZAR 19 300 per meeting
SA-based committee member attendance fee	ZAR 12 500 per meeting	ZAR 13 300 per meeting
US-based board retainer	USD 69 000	USD 35 535
US-based board attendance fee		USD 5 900 per meeting
UK-based board retainer	GBP 52 350	GBP 26 950
UK-based board attendance fee		GBP 4 500 per meeting
UK-based committee chairperson retainer	GBP 24 820	GBP 25 600
UK-based committee chairperson attendance fee	GBP 2 400 per meeting	GBP 2 500 per meeting
UK-based committee member retainer	GBP 7 800	GBP 8 000
UK-based committee member attendance fee	GBP 980 per meeting	GBP 1 000 per meeting

The non-executive directors' fees for the 2013 financial year have been increased by 6.5% for South African Rand-based fees and 3% for Great Britain Pound and United States Dollar-based fees.





ANNUAL FINANCIAL STATEMENTS

Contents

Directors' responsibility statement	139
Certificate by the Company Secretary	139
Report of the Audit and Risk Committee	140
Independent Auditor's Report	142
Directors' Report	143
Group accounting policies	146
Group	
Statement of financial position	168
Income statement	169
Statement of comprehensive income	170
Statement of cash flows	171
Statement of changes in equity	172
Notes to the Annual Financial Statements	174
Company	
Statement of financial position	248
Statement of comprehensive income	249
Statement of cash flows	250
Statement of changes in equity	251
Notes to the Annual Financial Statements	252
Directorate	258
Analysis of shareholders	264

DIRECTORS' RESPONSIBILITY STATEMENT

for the year ended 30 June 2013

DIRECTORS' RESPONSIBILITY TO THE SHAREHOLDERS OF DISCOVERY LIMITED AND ITS SUBSIDIARIES (DISCOVERY)

The directors of Discovery are required by the Companies Act (Act 71 of 2008) (Companies Act), to maintain adequate accounting records and to prepare financial statements for each financial year which fairly present the state of affairs of Discovery at the end of the financial year, and of the results and cash flows for the period. In preparing the accompanying annual financial statements, International Financial Reporting Standards have been used and reasonable estimates have been made. The annual financial statements incorporate full and responsible disclosure, in line with Discovery's philosophy on corporate governance.

The directors have reviewed Discovery's budget and flow of funds forecast for the year to 30 June 2014. On the basis of this review, and in light of the current financial position and available cash resources, the directors have no reason to believe that Discovery will not be a going concern for the foreseeable future. The going concern basis has therefore been adopted in preparing the annual financial statements.

The directors are responsible for Discovery's systems of internal control, which include internal financial controls in the various subsidiaries that are designed to provide reasonable, but not absolute, assurance against material misstatement and loss. Discovery maintains internal financial controls to provide assurance regarding:

- safeguarding of assets against unauthorised use or disposition and
- the maintenance of proper accounting records and the reliability of financial information used within the business, or for publication.

The controls contain self-monitoring mechanisms, and actions are taken to correct deficiencies as they are identified. Even an effective system of internal control, no matter how well designed, has inherent limitations, including the possibility of circumvention and the overriding of controls. An effective system of control therefore aims to provide reasonable assurance with respect to the reliability of financial information and, in particular, the presentation of annual financial statements.

To the best of their knowledge and belief, based on the above, the directors are satisfied that no material breakdown in the operation of the systems of internal control and procedures has occurred during the year under review.

Discovery's external auditors, PricewaterhouseCoopers Inc., have audited the annual financial statements and their unqualified report appears on page 142.

The annual financial statements of Discovery for the year ended 30 June 2013, which appear on pages 143 to 264, have been approved by the Board of Directors on 2 September 2013 and are signed on its behalf by:



Chief Executive Officer



Financial Director

CERTIFICATE BY THE COMPANY SECRETARY

for the year ended 30 June 2013

It is hereby certified in terms of section 88(2)(e) of the Companies Act, that Discovery Limited has for the year ended 30 June 2013 lodged with the Registrar of Companies all such returns as are required by a public company in terms of this Act and that all such returns are true, correct and up to date.



MJ Botha
Company Secretary

2 September 2013

REPORT OF THE AUDIT AND RISK COMMITTEE

for the year ended 30 June 2013

We are pleased to present our report for the financial year ended 30 June 2013. The Audit and Risk Committee (the Committee) is an independent statutory committee. Duties are delegated to the Committee by the Board of Directors of Discovery Limited (Discovery).

The Committee also acts as the statutory Audit Committee of Discovery Life Limited.

AUDIT COMMITTEE TERMS OF REFERENCE

The Committee has adopted formal terms of reference that have been approved by the Board of Directors and are reviewed at least annually. The Committee has conducted its affairs in compliance with its terms of reference and has discharged the responsibilities contained therein.

AUDIT COMMITTEE MEMBERS, MEETING ATTENDANCE AND ASSESSMENT

The Committee consists of three independent, non-executive directors. It meets at least four times per annum as per its terms of reference, and in the year ended 30 June 2013 met six times.

The Chairman of Discovery's Board and non-executive directors are entitled to attend meetings after informing the Chairman of the Committee. The Chief Executive Officer, Financial Director and executive directors attend meetings or parts of meetings by invitation only. The Chief Audit Executive and the external auditor meet with the Committee, or the Chairman of the Committee, before each meeting without management present, and attend meetings or parts of meetings by invitation. The Chairman of the Committee meets regularly with the Financial Director, external audit and the heads of internal audit, risk and compliance.

The membership, qualifications and attendance of the members of the Committee are as follows:

Committee member	Qualifications	Number of meetings held during the year ended 30 June 2013	Number of meetings attended
AL Owen (Chairman)	BSc (Hons), FIA, FPMI	6	6
SE Sebotsa	LLB (Hons), MA	6	6
SV Zilwa	BCompt (Hons),CTA, CA (SA)	6	4

An externally facilitated assessment of the effectiveness of the Committee and its individual members has been carried out within the last three years. An internal assessment was carried out during the year ending 30 June 2013.

ROLE AND RESPONSIBILITIES

Statutory duties

The Committee's role and responsibilities include statutory duties as per the Companies Act and further responsibilities assigned to it by the Board.

The Committee executed its duties in accordance with its terms of reference and applicable laws and regulations in force during the year ended 30 June 2013.

External auditor appointment and independence

The Committee considered the matters set out in section 94 of the Companies Act and nominated PricewaterhouseCoopers Inc. for appointment as external auditor of Discovery. PricewaterhouseCoopers Inc., with the approval of Discovery, worked together with Indyebo Inc. (a black female owned auditing firm) for a portion of the audit.

The Committee has satisfied itself that the external auditor is independent of Discovery, as set out in section 94(8) of the Companies Act. Requisite assurance was sought and provided by the auditor that internal governance processes within the audit firm support and demonstrate its claim to independence.

The Committee ensured that the appointment of the auditor complied with the Companies Act and any other legislation relating to the appointment of auditors.

The Committee, following consultation with executive management, approved the engagement letter, terms, audit plan and budgeted audit fees for the year ending 30 June 2013.

There is a formal policy in respect of the provision of non-audit services by the external auditors of Discovery and its subsidiaries, and a formal procedure governs the process whereby the auditor is appointed to provide any non-audit services, including a limitation on fees for non-audit services which shall not exceed 25% of the audit fees. The Chairman of the Committee approves the nature and extent of any non-audit services that the external auditor provides in terms of the agreed pre-approval policy and a schedule of approved non-audit services is reviewed annually by the Committee. The Committee satisfied itself that the provision of non-audit services carried out by the external auditors during the year was in accordance with the approved policy.

Financial statements and accounting practices

The Committee has reviewed the accounting policies, the consolidated and separate financial statements of Discovery and is satisfied that they are appropriate and comply with International Financial Reporting Standards. A process has been established to receive and deal appropriately with any concerns and complaints relating to the reporting practices of Discovery. No matters of significance have been raised in the past financial year.

Internal financial controls

The Committee is responsible for assessing Discovery's systems of internal financial and accounting control. In this regard the Committee has, inter alia, evaluated the adequacy and effectiveness of Discovery's systems of internal control and made appropriate recommendations to the Board. This has included a formal documented review by the internal audit function of the design, implementation and effectiveness of Discovery's system of internal financial controls. Based on the results of this review, it is the view of the Committee that Discovery's internal financial controls are effective, relative to the fair representation of the annual financial statements.

Evaluation of the expertise and experience of the Financial Director

The Committee reviewed and satisfied itself of the appropriateness of the expertise, resources and experience of Discovery's Financial Director, Mr R Farber.

Whistle blowing

The Committee receives and deals with any concerns or complaints, whether from within or outside Discovery, relating to the accounting practices and internal audit of Discovery, the content or auditing of Discovery's financial statements, the internal financial controls of Discovery and related matters. No such concerns or complaints were received during the year.

Ethics and compliance

The Committee is responsible for reviewing any major breach of Discovery's code of conduct and ethics and relevant legal, regulatory and other obligations. The Committee is satisfied that there has been no material breach of these standards or material non-compliance with laws and regulations. The Committee is satisfied that it has complied with all its legal, regulatory and other obligations during the period under review.

Risk management

The Committee monitors the risk management processes and systems of internal control for Discovery through review of reports from and discussions with Discovery's internal and external auditors and Discovery's risk management function.

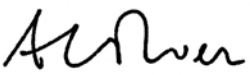
The Committee is satisfied that the system and process of risk management is effective.

OPINION

Based on the information and explanations given by management and discussions with the independent external auditor regarding the results of their audit, the Committee is satisfied that there was no material breakdown in the internal financial controls during the financial year under review.

The Committee has reviewed the consolidated and separate financial statements of Discovery for the year ended 30 June 2013 and based on the information provided to the Committee, considers that Discovery complies, in all material respects, with the requirements of the Companies Act and International Financial Reporting Standards.

The Committee has recommended the annual financial statements to the Board for approval. The Board has subsequently approved the annual financial statements which will be open for discussion at the forthcoming Annual General Meeting.



AL Owen
Chairman: Audit and Risk Committee

2 September 2013

INDEPENDENT AUDITOR'S REPORT

for the year ended 30 June 2013

TO THE SHAREHOLDERS OF DISCOVERY LIMITED

We have audited the consolidated and separate financial statements of Discovery Limited set out on pages 146 to 264, which comprise the statements of financial position as at 30 June 2013 and the income statements, statements of comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

The Company's directors are responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa and for such internal control the directors determine is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated and separate financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated and separate financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of Discovery Limited as at 30 June 2013 and its consolidated and separate financial performance and its consolidated and separate cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Companies Act of South Africa.

Other reports required by the Companies Act

As part of our audit of the consolidated and separate financial statements for the year ended 30 June 2013, we have read the directors' Report, the Audit and Risk Committee's Report and the Company Secretary's Certificate for the purpose of identifying whether there are material inconsistencies between these reports and the audited consolidated and separate financial statements. These reports are the responsibility of the respective preparers. Based on reading these reports we have not identified material inconsistencies between these reports and the audited consolidated and separate financial statements. However, we have not audited these reports and accordingly do not express an opinion on these reports.



PricewaterhouseCoopers Inc.
Director: **AG Taylor**
Registered Auditor

Sunninghill
2 September 2013

The directors present their 14th annual report, which forms part of the consolidated and separate financial statements of Discovery Limited for the year ended 30 June 2013.

NATURE OF BUSINESS

Discovery Limited (the Company) is listed on the Johannesburg Stock Exchange and is an integrated financial services organisation, specialising in health insurance, life assurance, wellness, investments and savings products, short-term insurance and credit card products. The Company is directly and indirectly the holding company of:

- Discovery Health Proprietary Limited (Discovery Health)
- Discovery Life Limited (Discovery Life)
- Discovery Life Collective Investments Proprietary Limited (Discovery Life Collective Investments)
- Discovery Life Investment Services Proprietary Limited (Discovery Life Investment Services)
- Discovery Life Nominees Proprietary Limited
- Discovery Third Party Recovery Services Proprietary Limited (DTPRS)
- Discovery Vitality Proprietary Limited, previously Vitality Healthstyle Proprietary Limited (Discovery Vitality)
- Discovery Investment Management Proprietary Limited (dormant)
- Discovery Insure Limited (Discovery Insure)
- Destiny Health Inc. – This company holds Discovery's interests in Destiny Health Management Company LLC, Destiny Health Insurance Company and Destiny Health Administration Company (dormant), which are incorporated in the United States of America (Destiny Health)
- The Vitality Group Inc. and The Vitality Group LLC, which are incorporated in the United States of America (The Vitality Group)
- Discovery Group Europe Limited, previously Discovery Offshore Holdings Limited, which is incorporated in England and Wales
- Prudential Health Holdings Limited – This company holds Discovery's interest in Prudential Health Limited, Prudential Health Services Limited and Prudential Health Insurance Limited, previously Standard Life Healthcare, which are incorporated in England and Wales (PruHealth)
- Discovery Vitality International Asia Private Limited
- Vitality International Services Asia Private Limited

Discovery Limited and its subsidiaries are referred to herein as Discovery or the Group. The subsidiaries are wholly-owned with the exception of Destiny Health in which the Company has a 99.98% interest, Discovery Insure, PruHealth and The Vitality Group LLC in which the Company has a 75% interest.

In addition to the above subsidiaries, Discovery consolidates unit trusts in which the Group has a greater than 50% economic interest resulting in effective control. The consolidated unit trusts include:

- Discovery Balanced Fund*
- Discovery Cautious Balanced Fund
- Discovery Diversified Income Fund
- Discovery Dynamic Equity Fund*
- Discovery Equity Fund*
- Discovery Flexible Property Fund*
- Discovery Global Balanced Fund of Funds
- Discovery Global Contrarian Equity Feeder Fund*
- Discovery Global Equity Feeder Fund
- Discovery Moderate Balanced Fund, previously Discovery Absolute Return Fund
- Discovery Money Market Fund
- Discovery Target Retirement 2010 Fund
- Discovery Target Retirement 2015 Fund
- Discovery Target Retirement 2020 Fund
- Discovery Target Retirement 2025 Fund
- Discovery Target Retirement 2030 Fund

* *consolidated for the first time in the current financial year.*

DIRECTORS' REPORT continued

for the year ended 30 June 2013

REVIEW OF RESULTS

Profit attributable to ordinary shareholders is R2 063 million, a 6.2% decrease from profits of R2 199 million reported in the prior financial year. Normalised headline earnings increased by 20.3% to R2 787 million.

SHARE CAPITAL

The share capital of the Company at 30 June 2013 was as follows:

Class of shares	Authorised number of shares	Issued number of shares
Ordinary shares of 0.1 cent per share	1 000 000 000	591 872 390
A preference shares	40 000 000	–
B preference shares	20 000 000	8 000 000
C preference shares	20 000 000	–

DIVIDENDS

The following interim dividends were paid during the current financial year:

- preference share dividend of 431,23288 cents per share, paid on 18 March 2013
- ordinary share dividend of 60 cents per share, paid on 25 March 2013

The directors are of the view that the Discovery Group is adequately capitalised at this time. On the statutory basis the capital adequacy requirements of Discovery Life was R455 million (2012: R364 million) and was covered 4.0 times (2012: 4.4 times).

B preference share cash dividend declaration:

On 29 August 2013, the directors declared a final gross cash dividend of 421,50685 cents (358,28082 cents net of dividend withholding tax) per B preference share for period 1 January 2013 to 30 June 2013. The dividend has been declared from income reserves and no secondary tax on companies' credits has been used. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued preference share capital at the declaration date is 8 million B preference shares.

The salient dates for the dividend will be as follows:

Last day of trade to receive a dividend	Friday, 13 September 2013
Shares commence trading "ex" dividend	Monday, 16 September 2013
Record date	Friday, 20 September 2013
Payment date	Monday, 23 September 2013

B preference share certificates may not be dematerialised or rematerialised between Monday, 16 September 2013 and Friday, 20 September 2013, both days inclusive.

Ordinary share cash dividend declaration:

Notice is hereby given that the directors have declared a final gross cash dividend of 64,5 cents (54,825 cents net of dividend withholding tax) per ordinary share for the year ended 30 June 2013. The dividend has been declared from income reserves and no secondary tax on companies' credits has been used. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued ordinary share capital at the declaration date is 591 872 390 ordinary shares.

The salient dates for the dividend will be as follows:

Last day of trade to receive a dividend	Friday, 4 October 2013
Shares commence trading "ex" dividend	Monday, 7 October 2013
Record date	Friday, 11 October 2013
Payment date	Monday, 14 October 2013

Share certificates may not be dematerialised or rematerialised between Monday, 7 October 2013 and Friday, 11 October 2013, both days inclusive.

DIRECTORATE AND SECRETARY

Details of the directors, their emoluments, participation in share incentive schemes and interests in the Company are reflected on pages 258 to 263.

Mr Vhonani Mufamadi has resigned as non-executive director from the Board of Discovery Limited, with effect from 4 December 2012.

Mr P Cooper, Mr JJ Durand and Mr S Epstein retire by rotation at the forthcoming Annual General Meeting of shareholders and are eligible and available for re-election.

Mr MJ Botha continues in office as Company Secretary. His details are reflected on page 258.

DIRECTORS' INTERESTS IN CONTRACTS

No material contracts involving directors' interests were entered into in the current year. The directors had no interest in any third party or company responsible for managing any of the business activities of Discovery.

BORROWING POWERS

The directors may exercise all the powers of the Company to borrow money. In terms of the Memorandum of Incorporation, the borrowing powers of the Company are unlimited. In terms of the Long-term Insurance Act, 1998, Discovery Life may not encumber its assets or directly or indirectly borrow.

INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

The Company entered into agreements to indemnify its directors to the extent permitted by law against all liabilities including legal costs incurred by the director in connection with or as a consequence of the director acting in any capacity, including as an authorised representative of a group company.

During the financial year, the Company paid insurance premiums in respect of a Directors and Officers Liability insurance contract, which insures directors and officers of the Company against certain liabilities arising in the course of their duties to the Company or group companies. Details of the nature of the liabilities covered and the amount of premium paid are not disclosed as such disclosure is prohibited under the terms of the contract.

AUDITORS

It will be proposed at the Annual General Meeting of shareholders, that PricewaterhouseCoopers Inc. continue in office in accordance with section 90(1) of the Companies Act.

SPECIAL RESOLUTIONS

Passed by Discovery Limited

Details of special resolutions passed by the Discovery Limited shareholders are set out on page 257.

Passed by subsidiaries of Discovery Limited

During the current financial year, the shareholders of some of Discovery Limited's subsidiaries passed a special resolution to adopt a new Memorandum of Incorporation. The subsidiaries include:

- Discovery Health Proprietary Limited
- Discovery Life Limited
- Discovery Vitality Proprietary Limited
- Discovery Insure Limited
- Discovery Life Collective Investments Proprietary Limited
- Discovery Life Investment Services Proprietary Limited

GROUP ACCOUNTING POLICIES

for the year ended 30 June 2013

GENERAL INFORMATION

Discovery Limited is listed in the insurance sector of the JSE Limited and is an integrated financial services organisation, specialising in health insurance, life assurance, investments and savings products, wellness, short-term insurance and credit card products. Below is a graphical representation of the material operating companies of the Group:



1. Health

Discovery Health

Discovery Health provides administration services and managed care services to the Discovery Health Medical Scheme as well as 12 closed schemes.

Discovery Health offered the insurance of private ward and overseas cover benefits. Members that had taken up this benefit before the distribution of it ceased, had the option to continue with this benefit. These benefits were written through Discovery Life.

PruHealth

The PruHealth product offers policyholders in the United Kingdom, cover for a range of private healthcare-related claims. The cover is dependent on the plan type chosen and includes hospital and outpatient cover for selected conditions. It specifically excludes emergency cover, maternity cover and cover for chronic conditions.

Policies offered by PruHealth are annual contracts which can be cancelled or the premiums adjusted on renewal.

Ping An Health

Ping An Health offers policyholders in China, cover for a range of private healthcare-related claims.

2. Life

Discovery Life

Discovery Life offers a range of insurance and financial solutions to both individual and group policyholders. The Discovery Life products reflect Discovery's underlying philosophy to make members healthier and to enhance and protect their lives.

Discovery Life offers some unique benefits that integrate with the benefits offered by Discovery Health, Discovery Vitality and Discovery Invest.

Individual life insurance

Discovery Life Plan

The Discovery Life Plan provides protection against a comprehensive spectrum of risks, including life, disability, severe illness and income continuation cover.

Health Plan Protector

The Health Plan Protector will fund contributions to the Discovery Health plans in the event of death, disability or severe illness. It further rewards members for positive health management through the payback benefit.

Discovery Retirement Optimiser

The Retirement Optimiser offers funding for retirement and offers benefits that could together with the Life Plan, capitalise unneeded risk cover to boost retirement funding.

DiscoveryCard Protector

The DiscoveryCard Protector will cover the outstanding balance on the DiscoveryCard in the event of death, disability or severe illness. It further provides a monthly benefit for a defined period equal to the average DiscoveryCard spend in the six-month period prior to the life-changing event.

Global Education Protector

The Global Education Protector funds education costs for children in the event of death, disability or severe illness of the insured life. Cover is provided to the earlier of the insured life reaching age 65 or the child reaching age 24. This benefit can be purchased on a stand-alone basis.

Supplementary Cancer Protector

The Supplementary Cancer Protector provides defined benefits to help cover non-medical costs associated with cancer. Benefits vary based on the severity of the cancer diagnosis.

Funeral Cover

The Funeral Cover benefit will pay out a defined lump sum in the event of death which can be used to cover the costs of a funeral. This lump sum is doubled in the event of accidental death. An education benefit is automatically included at a defined amount which aims to fund the education costs for children upon death of the principal member or spouse. Additional memorial and grocery benefits may be added to the policy as an option.

Group life insurance

Discovery Group Life offers a comprehensive spectrum of protection benefits on a group basis. Life cover, severe illness, disability and income continuation benefits are offered.

PruProtect

PruProtect is Discovery's life insurance offering to policyholders in the United Kingdom. It sells pure protection policies and is based on the Vitality structure that enables dynamic pricing to be employed in the UK life assurance market.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

3. Invest

Discovery Invest

Discovery Invest offers, through a range of investment fund choices, including Discovery managed unit trusts, a comprehensive and flexible range of investment choices. These products are sold through a number of investment wrappers, including Discovery Life policies.

4. Vitality

Discovery Vitality

Discovery Vitality offers the Group's clients health and lifestyle benefits with selected partners. This business includes the DiscoveryCard which is offered to Discovery policyholders within South Africa. The lifestyle benefits offered by Discovery Vitality are subject to change and can be adjusted on a monthly basis.

The Vitality Group and HumanaVitality

The Vitality Group and HumanaVitality offers the Vitality programme in the US on a stand-alone basis by wrapping it around other health plans and employer groups.

AIA Vitality

AIA Vitality offers the Vitality programme in Singapore, which is wrapped around and integrated with life and health insurance products offered by AIA Group Limited.

5. Insure

Discovery Insure

Discovery Insure provides motor vehicle, household and other short-term risk insurance products to the South African market. Discovery Insure product offerings include, but are not limited to, the following benefits:

Vitalitydrive

Discovery Insure encourages safe driving through Vitalitydrive, a programme that gives you rewards for improving your driving. The programme uses the latest motor vehicle telematics technology to develop a scientific measure of driver behaviour. If you drive well, you will earn points and the more points you earn the greater your rewards are.

If a policyholder insures both their car and home with Discovery Insure, and drive well, they can earn up to 50% of their BP fuel spend back every month (fuel cash back). The fuel cash back can be used to either reduce the premium that the policyholder is required to pay for the month in question or alternatively, at the election of the policyholder, have their fuel cash back doubled and paid into an excess funder account (EFA). The fuel rewards will depend on the number of points earned in the month. Furthermore, if the policyholder drives well, up to 10% of their car premiums will be paid into the EFA each month.

The funds in the EFA can be used to pay the excess liability a member incurs as a result of a valid claim for any motor vehicle insured under the policy. After three years, up to 50% of the funds available in the EFA can be withdrawn. If the policy lapses, the member forfeits the amount deferred in the EFA.

Young Adult Plan

The Young Adult Plan is available to drivers younger than 26 years and includes the following benefits:

- 25% of their car insurance premiums paid into a Rewards Fund every six months, which they can spend on whatever they want
- a further R200 paid into the Rewards Fund each month if they avoid driving late at night

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated and separate financial statements are set out below. These policies have been consistently applied to all the years presented, except for the accounting policy relating to Joint Ventures.

Previously, Discovery accounted for interests in jointly controlled entities by proportionate consolidation. In terms of this method, Discovery would include its share of a joint venture's individual income, expenses, assets, liabilities and cash flows in the relevant components of its financial statements.

Discovery has changed this accounting policy and now will recognise its interest in a joint venture using the equity method. Under the equity method, on initial recognition the investment is recognised at cost and the carrying amount is increased or decreased to recognise Discovery's share of the profit or loss of the investee after the date of acquisition. Discovery's share of the investee's profit or loss is recognised in profit or loss.

As this change has no effect on the opening retained income or the comparative numbers, Discovery changed its accounting policy to align with the requirements of IFRS 11: Joint arrangements, which is effective for Discovery's 2014 reporting period.

1. Basis of presentation

The consolidated and separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as well as the South African Companies Act. They have been prepared in accordance with the going concern principle using the historical cost basis except where otherwise stated in the accounting policies below.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying Discovery's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are outlined in note 4.

All monetary information and figures presented in these financial statements are stated in millions of Rand (R million), unless otherwise indicated.

Amendments and interpretations to published standards effective for Discovery's 2013 financial year

The following amendment is mandatory for the current accounting period and has been adopted.

Standard	Scope	Effective date
IAS 1 (Amendment): Presentation of financial statements	The amendment requires that an entity must group together items within other comprehensive income that may be reclassified to the profit or loss section of the income statement in order to facilitate the assessment of their impact on the overall performance of an entity.	Annual periods beginning on or after 1 July 2012

This amendment has not had any material impact on the Group's results but has resulted in changes to disclosure in the annual financial statements.

Amendments and interpretations to published standards effective for Discovery's 2013 financial year that are not significant or applicable to the results of the Group

Discovery has also adopted all other effective amended IFRSs (not previously early adopted), as of 1 July 2012. The following amendment is effective for the current financial year, with no material impact on Discovery's accounting policies or results, and no restatement of prior period results.

Standard	Scope	Effective date
IAS 12 (Amendment): Income taxes	Provides an exemption for the measurement of deferred tax assets or liabilities arising on investment property measured at fair value.	Annual periods beginning on or after 1 January 2012

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

New standards, amendments and interpretations to published standards not yet effective

The following new standards, amendments and interpretations to existing standards have been published and are not yet effective for the current financial year. Discovery has not early adopted them.

Standard	Scope and potential impact	Effective date
IFRS 7 (Amendment): Financial instruments: disclosures	This amendment aims to enhance the existing asset and liability offsetting disclosures.	Annual periods beginning on or after 1 January 2013
IFRS 9: Financial instruments (2009)	This standard introduces new requirements for the classification and measurement of financial assets. All recognised financial assets that are currently within the scope of IAS 39 will be measured at either amortised cost or fair value. *Potential impact*: Currently, Discovery's shareholder investments are designated as available-for-sale financial assets. This results in the realised gains being recognised in profit or loss. If Discovery chooses to continue with this classification, the realised gains will not be recycled to profit or loss. This designation will be reviewed and the appropriate classification will be selected upon adoption of this standard.	Annual periods beginning on or after 1 January 2015
IFRS 9: Financial instruments (2010)	The standard has been updated to include guidance on financial liabilities and the derecognition of financial instruments.	Annual periods beginning on or after 1 January 2015
IFRS 10: Consolidated financial statements	This standard builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements. *Potential impact*: With the application of this new standard, control will not be determined just by reference to the economic interest. An investor will control an investee when: • it has power over the investee • it has exposure, or rights, to variable returns from its involvement with the investee and • it has the ability to use its power over the investee to affect the amount of the investor's returns. This may affect the way Discovery accounts for the following: • Discovery Unit Trusts: Discovery currently consolidates unit trusts in which the Group has a greater than 50% economic interest resulting in effective control. The application of IFRS 10 may lead to unit trusts that were previously consolidated, not being consolidated in future and vice versa. • PruProtect: Discovery currently accounts for the PruProtect arrangement as a subsidiary, but with the application of IFRS 10, it may be classified as a reinsurance contract. • Share Trusts: Discovery currently consolidates its BEE Share Trust. With the application of IFRS 10 the share trust may no longer be consolidated. For all the items mentioned above, certain line items in the income statement and statement of financial position will be affected but there will be no material effect on the profit or loss in the income statement.	Annual periods beginning on or after 1 January 2013

Standard	Scope and potential impact	Effective date
IFRS 11: Joint arrangements	This standard identifies two types of joints arrangements, namely joint operations and joint ventures and focuses on the rights and obligations of the arrangement, rather than its legal form. The standard stipulates the accounting for these joint arrangements and has removed the option of proportional consolidation of joint ventures.	Annual periods beginning on or after 1 January 2013
IFRS 12: Disclosures of interest in other entities	This standard includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles.	Annual periods beginning on or after 1 January 2013
IFRS 10, 11 and 12: Amendment to the transition requirements	The amendment clarifies that the date of initial application is the first day of the annual period in which IFRS 10 is adopted. Entities adopting IFRS 10 should assess control at the date of initial application; the treatment of comparative figures depends on this assessment. The amendment also requires certain comparative disclosures under IFRS 12 upon transition.	Annual periods beginning on or after 1 January 2013
IFRS 10: Consolidated financial statements; IFRS 12: Disclosures of interest in other entities and IAS 27: Consolidated and separate financial statements	The amendment creates an exception to the principle that all subsidiaries must be consolidated. Entities meeting the definition of "Investment Entities" must be accounted for at fair value under IFRS 9: Financial instruments or IAS 39: Financial instruments Recognition and Measurement. Changes have also been made in IFRS 12 to introduce disclosures that an investment entity needs to make.	Annual periods beginning on or after 1 January 2014
IFRS 13: Fair value measurement	This standard aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs.	Annual periods beginning on or after 1 January 2013
IAS 1 (Amendment): Presentation of financial statements	The amendment clarifies the disclosure requirements for comparative information when a third statement of financial position is provided.	Annual periods beginning on or after 1 January 2013
IAS 19 (Amendment): Employee benefits	The amendment makes significant changes to the recognition and measurement of defined benefit pension expense, termination benefits, the definitions of short-term and other employee benefits and to the disclosures for all employee benefits.	Annual periods beginning on or after 1 January 2013
IAS 27 (revised 2011): Separate financial statements	Consequential amendments resulting from the issue of IFRS 10, 11 and 12.	Annual periods beginning on or after 1 January 2013
IAS 28 (revised 2011): Associates and joint ventures	This standard includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11.	Annual periods beginning on or after 1 January 2013
IAS 32 (Amendment): Financial instruments: Presentation	The amendment clarifies that income tax related to distributions is recognised in the income statement and income tax related to the costs of equity transactions is recognised in equity.	Annual periods beginning on or after 1 January 2013
IAS 32 (Amendment): Financial instruments: Presentation	The amendment clarifies some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position.	Annual periods beginning on or after 1 January 2014
IAS 34 (Amendment): Interim financial reporting	A measure of total assets and liabilities is required for an operating segment in interim financial statements if such information is regularly provided to the chief operating decision maker and there has been a material change in those measures since the last annual financial statements.	Annual periods beginning on or after 1 January 2013

Unless otherwise stated, it is not expected that the above new standards and amendments will have any material impact on Discovery's results but may result in additional disclosures in the annual financial statements.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

Interpretations and amendments to existing standards not yet effective and not relevant for Discovery's operations

Standard	Scope	Effective date
IFRS 1 (Amendment): First time adoption	The amendment addresses how a first-time adopter would account for a government loan with a below-market rate of interest when transitioning to IFRS and adds an exception to the retrospective application of IFRS.	Annual periods beginning on or after 1 January 2013
IFRS 1 (Amendment): First time adoption	The amendment clarifies that an entity may apply IFRS 1 more than once under certain circumstances and when an entity can choose to adopt IAS 23: Borrowing costs. It also clarifies that a first-time adopter should provide the supporting notes for all statements presented.	Annual periods beginning on or after 1 January 2013
IAS 16 (Amendment): Property, plant and equipment	The amendment clarifies that spare parts and servicing equipment are classified as property, plant and equipment rather than inventory when they meet the definition of property, plant and equipment.	Annual periods beginning on or after 1 January 2013
IFRIC 20: Stripping costs in the production phase of a surface mine	The interpretation clarifies there can be two benefits accruing to an entity from stripping activity and considers when and how to account separately for these benefits as well as how to measure these benefits both initially and subsequently.	Annual periods beginning on or after 1 January 2013

2. Consolidation

The consolidated financial statements include the assets, liabilities and results of the operations of the holding company and its subsidiaries.

2.1 Business combinations

The acquisition method of accounting is used to account for business combinations by the Group. The consideration transferred for the acquisition of a business is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, Discovery recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

The excess of the consideration transferred, being the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired, is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in profit or loss.

2.2 Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which Discovery has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Discovery considers the existence and effect of potential voting rights that are currently exercisable or convertible when assessing whether Discovery controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to Discovery. Consolidation is discontinued from the date on which control ceases.

Unit trusts, in which the Group has greater than 50% economic interest resulting in effective control, are consolidated. The consolidation principles applied to these unit trusts are consistent with those applied to consolidated subsidiary companies.

Investments in subsidiaries, in the separate financial statements of the holding company, are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable cost of investment.

Gains and losses on disposal of subsidiaries are included in profit or loss as gains and losses resulting from business combinations.

Intra-group transactions, balances and unrealised gains on intra-group transactions are eliminated. Unrealised losses are also eliminated. Subsidiaries' accounting policies have been changed where necessary to ensure consistency with the policies adopted by Discovery.

2.3 Non-controlling interests

Non-controlling interests can be measured at either:

- the proportionate share in the fair value of the identifiable net assets of the subsidiary at acquisition date, or
- fair value.

This measurement choice is not an accounting policy choice and Discovery will apply this at acquisition date per business combination transaction.

Non-controlling interests are treated as equity participants of the subsidiary company. Therefore, all transactions of Discovery with non-controlling interest in their capacity as owners, where there is no change in control, are treated as transactions within equity. In such transactions the carrying amounts of the controlling and non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of Discovery.

2.4 Puttable non-controlling interests

Put options granted to the non-controlling interests of Discovery's subsidiaries entitle the non-controlling interest to sell its interest in the subsidiary to Discovery at contracted dates.

In such case, Discovery has consolidated 100% of the subsidiaries results and has recognised the fair value of the non-controlling interest, being the present value of the estimated future purchase price, as a financial liability in the statement of financial position (Puttable non-controlling interests). In raising this liability, the non-controlling interest is derecognised and the excess is debited to retained earnings in the statement of changes in equity.

Interest is recorded in respect of this liability within finance costs using the effective interest rate method. The estimated future purchase price is fair valued at each reporting date and any changes in the value of the liability as a result of changes in the assumptions used to estimate the future purchase price are recorded in profit or loss.

2.5 Associates and joint ventures

Associates are entities over which Discovery has the ability to exercise significant influence but not control over the financial and operational policies. Significant influence is determined based primarily on percentage voting rights, generally between 20% and 50%, together with other factors such as board participation and participation in the policy-making process.

A joint venture is a joint arrangement whereby the parties that have joint control of an arrangement have rights to the net assets of the arrangement.

Discovery recognises its interest in an associate or a joint venture as an investment and accounts for that investment using the equity method. Under the equity method, on initial recognition the investment in an associate or a joint venture is recognised at cost, and the carrying amount is increased or decreased to recognise Discovery's share of the profit or loss of the investee after the date of acquisition. Discovery's share of the investee's profit or loss is recognised in profit or loss. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in Discovery's proportionate interest in the investee arising from changes in the investee's other comprehensive income. Such changes include those arising from the revaluation of property, plant and equipment and from foreign exchange translation differences. Discovery's share of those changes is recognised in other comprehensive income.

Discovery discontinues equity accounting when the carrying amount of the investment in an associate or a joint venture reaches zero, unless it has incurred obligations, guaranteed obligations or made payments on behalf of the associate or the joint venture. Discovery resumes equity accounting only after its share of the profits equals the share of losses not recognised. Discovery increases the carrying amount of investments with its share of the associate's or joint venture's income when equity accounting is resumed.

As Discovery's investment in an associate or a joint venture includes goodwill identified on acquisition, Discovery assesses at each reporting date whether there is objective evidence that an associate or a joint venture is impaired. If such evidence of impairment exists, Discovery calculates the amount of impairment as the difference between the recoverable amount of the investment and its carrying value and recognises the amount adjacent to "share of profit/loss of associates or joint ventures" in profit or loss.

Profits and losses resulting from upstream and downstream transactions between Discovery and its associates or joint ventures are recognised in Discovery's financial statements only to the extent of unrelated investor's interests in the associate or joint venture. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates and joint ventures have been changed where necessary to ensure consistency with the policies adopted by the Group.

Discovery will discontinue the use of the equity method from the date when its investment ceases to be an associate or a joint venture as follows:

(a) If the investment becomes a subsidiary, Discovery will account for its investment in accordance with IFRS 3 and IAS 27.
(b) If the retained interest in the former associate or joint venture is a financial asset, Discovery will measure the retained interest at fair value. The fair value of the retained interest will be regarded as its fair value on initial recognition as a financial asset in accordance with IAS 39. Discovery will recognise in profit or loss any difference between:
    (i) the fair value of any retained interest and any proceeds from disposing of a part interest in the associate or joint venture and
    (ii) the carrying amount of the investment at the date the equity method was discontinued.
(c) When Discovery discontinues the use of the equity method, it will account for all amounts previously recognised in other comprehensive income in relation to that investment on the same basis as would have been required if the investee had directly disposed of the related assets or liabilities.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

Interest in unit trusts in which Discovery has between 20% and 50% economic interest, therefore providing significant influence, are deemed to be interests in associates and are, on initial recognition, designated as financial assets at fair value through profit or loss, based on the scope exemption in IAS 28 – Investments in associates for investment-linked insurance funds.

Investments in associates and joint ventures, in the separate financial statements of the holding company, are accounted for at cost less impairment. Cost is adjusted to reflect changes in consideration arising from contingent consideration amendments. Cost also includes direct attributable cost of investment.

3. Foreign currency translation

3.1 Functional and presentation currency

Items included in the financial statements of each of Discovery's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in Rand (R), which is the functional and presentation currency of Discovery Limited.

3.2 Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from:

- the settlement of trading transactions are included in the results of operating activities in profit or loss
- the settlement of financing transactions and from the translation at year-end exchange rates of assets and liabilities denominated in foreign currencies are recognised in profit or loss as foreign exchange gains and losses
- qualifying cash flow hedges and qualifying net investment hedges are deferred in the statement of comprehensive income and are recycled to profit or loss in the periods in which the hedged item affects profit or loss

3.3 Group companies

The results and financial position of all Discovery entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at rates at the date of the transactions)
- all resulting exchange differences are recognised as a separate component of equity

On consolidation, exchange differences arising from the translation of the net investment in foreign entities are recognised in the foreign currency translation reserve in the statement of comprehensive income. When a foreign operation is partially disposed of or sold, such exchange differences are recognised in profit or loss as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

4. Property and equipment

Property and equipment are stated at historical cost less depreciation and impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to Discovery and the cost of the item can be measured reliably. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Property and equipment are depreciated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

Leasehold improvements	Shorter of estimated life or period of lease
Computer equipment and operating systems	3 years
Computer software packages	3 years
Furniture and fittings	6 years
Motor vehicles	4 years
Office equipment	5 years

The assets' residual values and useful lives are reviewed at each reporting period and adjusted if appropriate. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value-in-use.

Gains or losses on disposals are determined by comparing the proceeds with the carrying amount. These are recorded in profit or loss.

5. Intangible assets

5.1 Computer software development costs

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by Discovery are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software product so that it will be available for use
- management intends to complete the software product and use or sell it
- there is an ability to use or sell the software product
- it can be demonstrated how the software product will generate probable future economic benefits
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available
- the expenditure attributable to the software product during its development can be reliably measured

Directly attributable costs, that are capitalised as part of the software product, include the software development employee costs and an appropriate portion of directly attributable overheads.

Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

Computer software development costs recognised as assets are amortised over their useful lives, which does not exceed three years. The amortisation is reflected under marketing and administration expenses in profit or loss.

5.2 Deferred acquisition costs – insurance and investment contracts

The accounting policy for deferred acquisition costs relating to insurance and investment contracts is detailed in accounting policy 13. The amortisation of deferred acquisition costs is reflected under acquisition costs in profit or loss.

5.3 Other intangible assets

Discovery does not attribute value to internally developed trademarks, patents and similar rights and assets, including franchises and management contracts and expenses the costs incurred to profit or loss in the period in which they are incurred.

6. Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of Discovery's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or group of cash-generating units that are expected to benefit from the business combination in which the goodwill arose, identified according to operating segment.

7. Financial assets

Discovery classifies its financial assets into the following categories:

- financial assets at fair value through profit or loss
- available-for-sale financial assets
- loans and receivables
- derivative financial instruments at fair value through profit or loss or carried as a hedge

The classification depends on the purpose for which the investments were acquired. Management determines the classification of its financial assets at initial recognition.

Financial assets are derecognised when the rights to receive cash flows from them have expired or where they have been transferred and Discovery has also transferred substantially all risks and rewards of ownership.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

7.1 Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading and those designated at fair value through profit or loss at inception.

A financial asset is classified into the 'financial assets at fair value through profit or loss' category at inception if:

- it is acquired principally for the purpose of selling in the short-term or
- it forms part of a portfolio of financial assets in which there is evidence of short-term profit-taking

Derivatives are also classified as held for trading unless they are designated as hedges.

Financial assets designated as financial assets at fair value through profit or loss at inception are those that are:

- held in internal funds to match insurance and investment contract liabilities that are linked to the changes in fair value of these assets. The designation of these assets to be at fair value through profit or loss eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as 'an accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.
- managed and whose performance is evaluated on a fair value basis. Information about these financial assets is provided internally on a fair value basis to Discovery's key management personnel.

Financial assets carried at fair value through profit or loss, are initially recognised at fair value with transaction costs expensed in profit or loss. These assets are subsequently carried at fair value. Realised and unrealised gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in profit or loss in the period in which they arise.

Discovery recognises interest income, dividends received, realised and unrealised gains and losses of 'financial assets at fair value through profit or loss' category within net fair value gains on financial assets at fair value through profit or loss in profit or loss.

7.2 Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other categories.

Available-for-sale financial assets are initially recognised at fair value plus transaction costs that are directly attributable to their acquisition and are subsequently carried at fair value. Unrealised gains and losses arising from changes in the fair value of assets classified as available-for-sale are recognised in the statement of other comprehensive income. When assets classified as available-for-sale are sold or impaired, the accumulated fair value adjustments are included in profit or loss as net realised gains/losses on available-for-sale financial assets and impairment on available-for-sale financial assets respectively.

Discovery recognises interest income and dividends received from these assets as part of investment income in profit or loss. Dividends are recognised when the entity's right to receive payment is established.

7.3 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than those that Discovery intends to sell in the short-term or that it has designated as at fair value through profit or loss or available-for-sale.

Loans and receivables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method, less provision for impairment. A provision for impairment of loans and receivables is established when there is objective evidence that Discovery will not be able to collect all amounts due according to their original terms (see accounting policy 9 for the policy on impairment). Receivables arising from insurance contracts are also classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables.

7.4 Fair value

The fair values of quoted and listed investments are based on current bid prices. Collective investment schemes are valued at their repurchase price. If the market for a financial asset is not active, Discovery establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models making maximum use of market inputs and relying as little as possible on entity-specific inputs.

8. Derivative financial instruments

Discovery initially recognises derivative financial instruments in the statement of financial position at fair value on the date which a derivative contract is entered into (the best evidence of fair value on day one is the transaction price) and subsequently re-measures these instruments at their fair value. The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Discovery designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge) or
- hedges of highly probable forecast transactions (cash flow hedge).

Discovery documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. Discovery also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are expected to be and have been highly effective in offsetting changes in fair values or cash flows of hedged items.

8.1 Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in profit or loss, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedge item for which the effective interest rate method is used, is amortised to profit or loss over the period to maturity.

8.2 Cash flow hedge

Discovery recognises the effective portion of fair value changes of derivatives that are designated and qualify as cash flow hedges and prove to be highly effective in relation to the hedged risk, in the cash flow hedging reserve in the statement of comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

Non-financial asset or liability

Amounts accumulated in the statement of other comprehensive income are recycled to profit or loss in the period in which the hedged item will affect profit or loss. Where the forecast transaction or a foreign currency firm commitment results in the recognition of a non-financial asset or a liability, the gains and losses previously deferred are transferred from the statement of comprehensive income and included in the initial measurement of the cost of the non-financial asset or liability.

Financial asset or liability

Amounts accumulated in the statement of other comprehensive income are recycled to profit or loss in the period in which the hedged item will affect the profit or loss. Where the forecast transaction subsequently results in the recognition of a financial asset or liability, gains or losses deferred in equity are transferred from the statement of comprehensive income when the financial asset or liability is sold or impaired.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to profit or loss.

8.3 Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of all such derivative instruments are recognised immediately in profit or loss.

9. Impairment of assets

9.1 Financial assets carried at amortised cost

Discovery assesses at each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (a 'loss event') and the loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence includes one or more of the following events:

- significant financial difficulty of the issuer or debtor
- a breach of contract, such as default or delinquency in payments
- it becoming probable that the issuer or debtor will enter bankruptcy or other financial reorganisation
- the disappearance of an active market for that financial asset because of financial difficulties
- observable data indicating that there is a measurable decrease in the estimated future cash flow from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in Discovery, including:
  - adverse changes in the payment status of issuers or debtors of Discovery
  - national or local economic conditions that correlate with defaults on the assets of Discovery

Discovery first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant. If Discovery determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred on loans and receivables carried at amortised cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in profit or loss.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as improved credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in profit or loss.

9.2 Financial assets carried at fair value

Discovery assesses at each reporting period whether there is objective evidence that an available-for-sale financial asset is impaired, including in the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and current fair value, less any impairment loss on the financial asset previously recognised in profit or loss – is removed from the statement of comprehensive income and recognised in profit or loss. Impairment losses recognised in profit or loss on equity instruments are not subsequently reversed. The impairment loss is reversed through profit or loss if, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

Discovery has taken the view that a 30% decline in the fair value of an investment in an equity instrument below cost would be classified as significant and a period of nine months or more would be a prolonged decline.

9.3 Impairment of other non-financial assets

Assets, including intangible assets and deferred acquisition costs, other than those relating to insurance contracts (see accounting policy 13), that are subject to amortisation, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Such indicators include continued losses, changes in technology, market, economic, legal and operating environments.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is measured using the higher of the fair value less costs to sell and the value-in-use. Value-in-use is the present value of projected cash flows covering the remaining useful life of the asset. An impairment charge is recognised as a loss in profit or loss immediately.

10. Offsetting financial instruments

Discovery offsets financial assets and liabilities and reports the net balance in the statement of financial position where:

- there is a current legally enforceable right to set off
- there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously

11. Cash and cash equivalents

Cash and cash equivalents comprise:

- cash in hand
- deposits held at call and short notice
- balances with banks

Cash and cash equivalents only include items held for the purpose of meeting short-term cash commitments rather than for investing or other purposes. Cash and cash equivalents have a maturity of less than three months from the date of acquisition. Cash and cash equivalents are carried at cost which due to their short-term nature approximates fair value.

12. Share capital

Shares are classified as equity when there is no obligation to transfer cash or assets. Incremental costs directly related to the issue of new shares or options are shown in equity as a deduction from the proceeds, net of tax.

Where any Group company purchases Discovery Limited's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Discovery Limited's equity holders. Where such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity attributable to the Discovery Limited equity holders, net of any directly attributable incremental transaction costs and the related income tax effects.

13. Insurance and investment contracts

Discovery issues contracts that transfer insurance risk or financial risk or both.

Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk. Discovery defines as significant insurance risk the possibility of having to pay benefits, on the occurrence of an insured event, that are significantly more than the benefits payable if the insured event did not occur.

Investment contracts are those contracts that transfer financial risk without significant insurance risk. Financial risk refers to the risk of a possible future change in the value of an asset or financial instrument due to a change in interest rate, commodity price, index of prices, foreign exchange rate or other measurable variable.

13.1 Insurance contracts

Discovery developed its accounting policies for insurance contracts before the adoption of IFRS 4. As provided for in IFRS 4, Discovery continues to apply the same accounting policies for the recognition and measurement of obligations arising from insurance contracts that it issues and reinsurance contracts that it holds.

Recognition and measurement

Insurance contracts are classified into four main categories, depending on the duration of the risk and the type of risk insured.

(i) Individual life insurance

These contracts insure against a comprehensive spectrum of risks, including life, disability, severe illness and income continuation cover. These contracts are long-term in nature.

For the published accounts, the actuarial value of policyholder liabilities is determined based on a prospective discounted cash flow valuation basis calculated as the difference between the present value of future benefit payments plus expenses and the present value of future premiums. Best estimate assumptions regarding the future experience of claims experience, premium income, expenses and commission are used. Where the same policy includes both insurance and investment components and where the policy is classified as an insurance policy, the liability for the insurance benefits and investment benefits are separately calculated. These components of the liability are not unbundled for reporting purposes. (Refer to accounting policy 13.2 for the recognition and measurement of investment benefit liabilities).

Where the value of policyholder liabilities is negative in aggregate, this is shown as assets arising from insurance contracts.

Applying the valuation basis on the best estimate basis, described above, results in a gain at initial recognition in excess of initial expenses. Compulsory and discretionary margins are therefore added to the best estimate assumption to avoid the premature recognition of future profits. At initial recognition profits are recognised to the extent of the actual acquisition costs incurred but considering the premium loadings available on the total portfolio to recoup acquisition costs.

Discretionary and compulsory margins are therefore added to the best estimate assumptions within the following framework:

- All margins are at least equal to the compulsory margins prescribed by regulations.
- For the discount rate and lapse rate margins, the direction of the margins may vary based on policy type and duration to ensure that the margin is in the conservative direction, overall.
- Given the level of uncertainty in the best estimate assumptions for lapse, mortality and morbidity margins are added to protect against future possible adverse experience.
- Additional margins are added to allow for the release of profit over the term of the policy.
- Margins are released over the term of a policy in line with the risk borne.
- The best estimate and margins are reset at every valuation date to reflect the underlying profitability of the portfolio.
- Assets under insurance contracts are not used to offset the liability under the pure investment benefits of the policy.

In the valuation of the policyholder liability for South African policies, it has been assumed that all policyholders change to plans with minimum premium increases without changing the cover levels at the valuation date. This is in line with South African actuarial guidance which requires that expected profits in respect of future options that may be taken up by policyholders should not be recognised in the policyholder liability.

The actuarial liabilities are calculated gross of reinsurance. The expected impact of reinsurance is valued separately.

The valuation basis meets the requirement of the liability adequacy test as required by IFRS 4 for individual life insurance and no additional tests are performed.

The liability estimates are reviewed at every reporting period and any changes in estimates to the liability are reflected in profit or loss as they occur.

For these contracts, premiums are recognised as revenue when due. Premiums are shown net of premium discounts received and before the deduction of commission. Premiums exclude taxes and levies.

Insurance benefits and claims relating to individual life insurance contracts are recognised in profit or loss based on the estimated liability for compensation owed to the contract holder. Death, disability and severe illness and surrender claims are accounted for when notified. These claims include claims reported but not yet validated. The estimate is determined taking into account the likelihood of the claim being valid and the expected severity of the claim given that the claim is valid. The proportion to be included is estimated separately for each benefit type. An estimate of the expected claim amount is charged to profit or loss and included in liabilities under insurance contracts. Maturity and income disability are recorded as incurred. Liabilities are held to reflect incurred but not yet reported (IBNR) claims. The IBNR is modified to reflect actual current operating conditions. The liabilities are calculated gross of reinsurance. An asset is then raised to allow for the expected recoveries from reinsurers.

Acquisition costs for these contracts represent commission and other costs that relate to the securing of new contracts and the renewing of existing contracts. The valuation basis for valuing insurance contracts makes implicit allowance for the deferral of acquisition costs and hence no explicit deferred acquisition cost asset is recognised in the statement of financial position. These are expensed in profit or loss.

(ii) Group life insurance

These contracts insure against a comprehensive spectrum of protection benefits on a group basis. Life cover, severe illness, disability and income continuation benefits are offered. These contracts are short-term in nature.

For these contracts, premiums are recognised as revenue when due. Premiums are shown before the deduction of commission and exclude taxes and levies.

Where a claim is reported but not yet validated, an estimate of the expected claim is charged to profit or loss in the period in which it is reported and included in liabilities under insurance contracts. Liabilities are held to reflect IBNR claims. The IBNR is estimated based on the actual incidence of historic reported claims. The IBNR is calculated on the risk premiums net of profit loadings as this represents the best estimate of future claims experience. The IBNR is further modified to reflect current operational conditions or known events. The liabilities are calculated gross of reinsurance. An asset is then raised to allow for the expected recovery from reinsurers.

Acquisition costs for group life insurance contracts comprise all direct costs arising from the sale of insurance contracts. Commissions are expensed as incurred.

(iii) Health insurance

These contracts insure policyholders against healthcare-related claims.

Health insurance premiums received in respect of annual contracts are recognised proportionally over the period of the coverage. The portion of the premium received on in-force contracts that relates to unexpired risks at the reporting period is reported as unearned premiums within liabilities arising from insurance contracts. The unearned premium income is amortised on a straight-line basis.

Benefits payable under health insurance contracts are accounted for as incurred. Liabilities are held to reflect IBNR claims. The IBNR calculation is performed using the chain ladder approach. This allows for the historic patterns of claims payment in determining the likely future emergence of claims. The IBNR is further modified to reflect current operational conditions or known events. The liabilities are calculated gross of reinsurance. An asset is then raised to allow for the expected recovery from reinsurers.

The direct costs (commissions) of acquiring short-term health insurance business which are incurred during the year but which are expected to be recoverable out of future revenue margins are deferred and disclosed as an asset in the statement of financial position, gross of tax. The costs are deferred over the period of the contract and amortised on a straight-line basis in line with unearned premiums.

(iv) Short-term insurance

These monthly contracts insure policyholders against a comprehensive spectrum of short-term risks including, but not limited to, motor vehicle and household cover.

Short-term insurance premiums received in respect of monthly contracts are recognised as revenue when due. Premiums are shown before the deduction of commission, less the fuel cash back rewards described below, and exclude valued-added tax.

Reinsurance commission income is recognised in profit or loss over the period of the related direct insurance business assumed.

Claims are accounted for as incurred and consist of claims paid, movement in the provision for outstanding claims and related claims handling expenses.

The provision for outstanding claims is based on estimates of the cost of settling all claims incurred but unpaid at the reporting date, whether reported or not. Related anticipated reinsurance recoveries are disclosed separately as assets in the statement of financial position and included in recoveries from reinsurers in profit or loss.

Certain short-term insurance contracts allow Discovery to sell property acquired as a result of a claim (ie. salvage). Discovery may also have the legal right to pursue third parties for payment of some or all of the costs (ie. subrogation).

The estimated salvage and subrogation reimbursements are treated as a reduction in the measurement of claims liability.

Acquisition costs for these contracts comprise all direct costs arising from the sale of insurance contracts and are recognised in profit or loss over the life of the contract.

As discussed on page 148, the fuel cash back can be used to either reduce the premium that the policyholder is required to pay for the month in question or can be doubled and paid into an EFA.

Where the policyholder has used the fuel cash back to reduce the monthly premium, the reduction has been shown in insurance premium revenue in profit or loss as incurred.

If the policyholder has elected to double the fuel cash back and paid it into an EFA, an EFA liability is raised. The EFA liability is calculated using a deterministic basis and is disclosed in liabilities arising from insurance contracts in the statement of financial position and the movement is disclosed in the transfer to liabilities under insurance contracts.

Embedded derivatives

A unit-linked insurance contract is an insurance contract with an embedded derivative linking payments on the contract to units of an investment fund purchased with the consideration received from the contract holders. This embedded derivative meets the definition of an insurance contract and is therefore not accounted for separately from the host insurance contract. The liability for such contracts is adjusted for all changes in the fair value of the underlying assets.

Discovery does not separately measure embedded derivatives that meet the definition of an insurance contract or options to surrender insurance contracts for a fixed amount (or amount based on a fixed amount and an interest rate). All other embedded derivatives are separated and carried at fair value if they are not closely related to the host insurance contract and meet the definition of a derivative. Embedded derivatives that are separated from the host contract are fair valued through profit or loss.

Liability adequacy test

At the reporting date, liability adequacy tests are performed to ensure the adequacy of the contract liabilities net of related deferred acquisition costs. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses are used. Any deficiency is immediately charged to profit or loss initially by writing off deferred acquisition costs and by subsequently establishing a provision for losses arising from the liability adequacy test.

Reinsurance contracts

Contracts entered into by Discovery with reinsurers under which the Company is compensated for losses on one or more contracts that meet the classification requirements for insurance contracts are classified as reinsurance contracts. Contracts that do not meet these classification requirements are classified as financial assets.

Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract.

The amounts Discovery is required to pay under its reinsurance contracts held are recognised as reinsurance liabilities (liabilities arising from reinsurance contracts).

Outward reinsurance premiums are recognised as an expense and are accounted in the same accounting period that premiums received are recognised in revenue. The amounts due to Discovery under its reinsurance contracts are recognised as reinsurance assets (classified within loans and receivables). Discovery assesses its reinsurance assets for impairment on an annual basis following the same method used for financial assets.

In certain cases there is a gain or loss at inception of a reinsurance contract:

- Where these amounts relate to a reimbursement of expenses the gain is disclosed as a recovery of expenses from reinsurers.
- Other gains or losses are amortised over the life of the insurance policies on the same basis as the profit is expected to emerge.

Deferred acquisition costs (DAC)

Commissions and other acquisition costs that vary with and are related to securing new contracts and renewing existing contracts are capitalised as an intangible asset (DAC). All other costs are recognised as expenses when incurred. The DAC is subsequently amortised over the life of the contracts.

Receivables and payables related to insurance and investment contracts

Receivables and payables are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders. Discovery assesses its receivables for impairment on an annual basis following the same method used for financial assets.

13.2 Investment contracts

Recognition and measurement

Discovery issues investment contracts without fixed benefits (eg. unit-linked and structured products) and investment contracts with fixed and guaranteed benefits (eg. term certain annuity).

Investment contracts without fixed benefits are financial liabilities whose fair value is dependent on the fair value of the underlying financial assets and derivatives (unit-linked) and are designated at inception as at fair value through profit or loss. Discovery designates these investment contracts to be measured at fair value through profit or loss because it eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases. See accounting policy 7.1 for the financial assets backing these liabilities.

Discovery's main valuation techniques incorporate all factors that market participants would consider and are based on observable market data. The fair value of a unit-linked financial liability is determined using the current unit price that reflects the fair values of the financial assets contained within the Discovery's unitised investment funds linked to the financial liability. The fair value of the financial liabilities is obtained by multiplying the number of units attributed to each policyholder at the reporting date by the unit price for the same date.

For investment contracts with fixed and guaranteed terms, valuation techniques are used to establish the fair value at inception and at each reporting date. Valuation techniques include discounted cash flow analysis using current market rates of interest and reference to other instruments that are substantially the same.

All premiums under investment contracts are recorded as deposits to investment contract liabilities and claims incurred on investment contracts are recorded as deductions from investment contract liabilities.

Deferred acquisition costs (DAC)

Deferred acquisition costs on investment contracts represent the contractual customer relationship and the right to receive future investment management fees. Incremental costs directly attributable to securing rights to receive policy fees for services sold with investment contracts are recognised as an intangible asset where they can be identified separately and measured reliably and it is probable that they will be recovered. An incremental cost is one that would not have been incurred if the Group had not secured the investment contract.

The asset represents the Group's contractual right to benefit from providing asset management services and is amortised over the expected life of the contract on an appropriate basis.

Fees on investment contracts

Service fee income on investment management contracts is recognised on an accrual basis as and when the services are rendered. Fees on investment contracts are included in fee income.

A deferred revenue liability (DRL) is recognised in respect of upfront fees, which are directly attributable to a contract, that are charged for securing the investment management service contract. The DRL is then released to revenue when the services are provided, over the expected duration of the contract on an appropriate basis.

Regular fees are charged to the customer monthly either directly or by making a deduction from invested funds.

14. Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds and the redemption value is recognised in profit or loss over the period of the borrowings using the effective interest rate method.

15. Deferred income tax

Discovery calculates deferred income tax on all temporary differences using the statement of financial position based approach. It calculates deferred tax liabilities or assets by applying corporate tax rates that have been substantively enacted to the temporary differences existing at each reporting date between the tax values of assets and liabilities and their carrying amount, where such temporary differences are expected to result in taxable or deductible amounts in determining taxable income for future periods when the carrying amount of the assets or liabilities are recovered or settled.

Discovery recognises deferred tax assets if the directors of Discovery consider it probable that future taxable income will be available against which the unused tax losses can be utilised.

Temporary differences arise primarily from the difference between accounting and tax balances arising from insurance contracts, depreciation of property and equipment, effect of accounting for leases as a finance lease, effect of straight-lining of operating leases, revaluation of certain financial assets and liabilities, provisions for leave pay, provisions for share-based payments and tax losses carried forward. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable income.

Deferred tax related to fair value re-measurement of available-for-sale investments and cash flow hedges, which are charged or credited directly to the statement of other comprehensive income, is also credited or charged directly to the statement of other comprehensive income and is subsequently recognised in profit or loss when the gain or loss is realised.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. Discovery separately discloses the deferred tax asset and deferred tax liability.

16. Employee benefits

16.1 Post-employment benefits

Discovery operates defined contribution schemes, the assets of which are held in separate trustee-administered funds.

These funds are registered in terms of the Pension Funds Act, 1956, and membership is compulsory for all Discovery employees. Qualified actuaries perform annual valuations.

For defined contribution plans, Discovery pays contributions to privately administered pension insurance plans on a mandatory basis. Discovery has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

16.2 Post-retirement medical benefits

Discovery has no liability for the post-retirement medical benefits of employees.

16.3 Share-based compensation

Discovery operates equity-settled and cash-settled share-based compensation plans.

Equity-settled share-based compensation plans

Discovery expenses the fair value of the employee services received in exchange for the grant of the options, over the vesting period of the options, as employee costs, with a corresponding credit to a share-based payment reserve in the statement of changes in equity. The total value of the services received is calculated with reference to the fair value of the options on grant date.

The fair values of the options are determined excluding non-market vesting conditions. These vesting conditions are included in the assumptions of the number of options expected to vest. At each reporting date, Discovery revises its estimate of the number of options expected to vest. Any changes to the estimated number of options are recognised in profit or loss immediately.

Cash-settled share-based compensation plans

Discovery recognises employee services received in exchange for cash-settled share-based payments at the fair value of the liability incurred and expenses these services over the vesting period of the benefits, as employee costs.

The liability is re-measured at each reporting period to its fair value, with all changes recognised immediately in profit or loss.

16.4 Termination benefits

Discovery recognises termination benefits as a liability in the statement of financial position and as an expense in profit or loss when it has a present obligation relating to termination. Discovery has a present obligation when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal, or providing termination benefits as a result of an offer to encourage voluntary redundancy.

16.5 Leave pay

Discovery accrues in full the employees' rights to annual leave entitlement in respect of past service. This is expensed over the period the services are rendered.

16.6 Profit share and bonus plan

Discovery recognises a liability and an expense for bonuses and profit-sharing in staff costs, based on a formula where there is a contractual obligation or where there is a past practice that has created a constructive obligation.

17. Trade and other payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less from the reporting date. If not, they are presented as non-current liabilities.

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

18. Provisions

Provisions are recognised when, as a result of past events, Discovery has a present legal or constructive obligation of uncertain timing or amount, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provisions are measured as the present value of management's best estimate of the expenditure required to settle the obligation at the reporting date. The pre-tax discount rate used to determine the present value reflects current market assessments of the time value of money. The increase in the provision due to the passage of time is recognised as interest expense.

Discovery recognises a provision for an onerous contract when the expected benefits to be derived from a contract are lower than the unavoidable costs of meeting the obligations under the contract.

19. Contingent liabilities

Discovery discloses a contingent liability when:

- it has a possible obligation arising from past events, the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity or
- it has a present obligation that arises from past events but not recognised because
  - it is not probable that an outflow of resources will be required to settle an obligation or
  - the amount of the obligation cannot be measured with sufficient reliability.

20. Revenue recognition

20.1 Insurance premium revenue

Insurance premium revenue includes individual life insurance premiums, group life insurance premiums, health insurance premiums and short-term insurance premiums. These are accounted for as described in accounting policy 13.

20.2 Fee income on administration business

Administration fees and managed care fees are included in fee income and are accounted for on an accrual basis in the accounting period in which the services are rendered.

20.3 Vitality income

Vitality income includes:

- Vitality contributions received from its members which are accounted for on an accrual basis in the accounting period in which the services are rendered.
- Revenue income from the sale of benefits offered by Vitality which is accounted for on an accrual basis.
- Fee income received from the activation of new gym contracts. These fees are deferred and released on a straight-line basis over the period of the contract.
- Fee income received from FNB in respect of the DiscoveryCard joint venture which is accounted for on an accrual basis in the accounting period in which the services are rendered.
- DiscoveryCard fee income which is deferred and released on a straight-line basis over the period of the contract.

Discovery Vitality operates a loyalty scheme through the DiscoveryCard which allows customers to accumulate miles that entitle them, subject to certain criteria, to use their miles against purchases with Discovery Vitality partners. Income, which is equal to the fair value attributed to the miles awarded, is deferred and recognised when the miles are redeemed or expire. The fair value of the miles is estimated by applying a weighted average cost per mile based on estimated redemption percentages.

20.4 Investment income

Investment income comprises interest and dividends received on available-for-sale investments, interest received from assets held at amortised cost and cash and cash equivalents.

Discovery recognises dividends when Discovery's right to receive payment is established. This is on the "last day to trade" for listed shares and on the "date of declaration" for unlisted shares. Dividend income includes scrip dividends, irrespective of whether there is an option to receive cash instead of shares.

Interest is accounted for on an accrual basis using the effective interest rate method.

20.5 Net realised gains on available-for-sale financial assets

Net realised gains comprise realised gains and losses on available-for-sale financial assets. The accumulated fair value gains and losses recognised in the statement of comprehensive income are accounted for on disposal of the investment in profit or loss as net realised gains and losses.

20.6 Net fair value gains on financial assets at fair value through profit or loss

Net fair value gains on financial assets at fair value through profit or loss include gains arising from interest, dividends and net realised and unrealised gains on financial assets held at fair value through profit or loss.

GROUP ACCOUNTING POLICIES continued

for the year ended 30 June 2013

21. Leases

21.1 Finance leases

Discovery classifies leases as finance leases where it assumes substantially all the benefits and risks of ownership.

Finance leases are capitalised as assets at the fair value of the leased asset at the inception of the lease, or, if lower, at the estimated present value of the underlying lease payments. Discovery allocates each lease payment between the liability and finance costs to achieve a constant rate on the finance balance outstanding. The interest component of the finance cost is recognised in profit or loss over the lease period. The assets acquired are depreciated over the useful life of the assets, unless it is not probable that Discovery will take ownership of the assets, in which case the assets are depreciated over the shorter of the useful life of the asset or the lease period, on a basis consistent with similar owned property and equipment.

21.2 Operating leases

Discovery classifies leases as operating leases where the lessor effectively retains the risks and benefits of ownership. Operating lease payments are recognised in profit or loss on a straight-line basis over the period of the lease. Minimum rentals due after year-end are reflected under commitments.

Discovery recognises as an expense any penalty payment to the lessor for early termination of an operating lease, in the period in which termination takes place.

22. Marketing and administration expenses

Marketing and administration expenses include marketing and development expenditure, all other non-commission related expenditure and benefits paid under the Vitality program. These costs are expensed in profit or loss as incurred.

23. Finance costs

Finance costs are recognised as an expense in profit or loss on an accrual basis using the effective interest rate method.

24. Direct and indirect taxes

Direct taxes include South African and foreign jurisdiction corporate tax payable, as well as secondary tax on companies and capital gains tax. With the introduction of withholding tax on dividends paid to equity holders, effective from 1 April 2012, secondary tax is no longer applicable. Withholding tax on dividends is not a tax for the Company and will therefore have no effect on the profit and losses of the Company. Direct taxes are disclosed as taxation in profit or loss.

Indirect taxes include various other taxes paid to central and local governments, including value-added tax and skills development levies. Indirect taxes are included as part of marketing and administration expenses in profit or loss.

The charge for current tax is based on the results for the year as adjusted for items which are non-taxable or disallowed. It is calculated using taxation rates that have been enacted or substantively enacted by the reporting date, in each particular jurisdiction within which the Discovery entities operate.

Taxation in respect of the South African life insurance operations is determined using the four fund method applicable to life insurance companies.

25. Dividend distribution

Dividend distribution to Discovery Limited's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved.

26. Segment reporting

Discovery's operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-makers (CODM). The CODM have been identified as the Chief Executive Officers of Discovery's businesses, who make strategic decisions regarding these businesses.

An operating segment is a component of an entity:

(a) that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity)

(b) whose operating results are regularly reviewed by the entity's CODM to make decisions about resources to be allocated to the segment and assess its performance

(c) for which discrete financial information is available

An operating segment may engage in business activities for which it has yet to earn revenues, for example, start-up operations may be operating segments before earning revenues.

Discovery will report separately information about an operating segment that meets any of the following quantitative thresholds:

(a) Its reported revenue, including both sales to external customers and intersegment sales or transfers, is 10 per cent or more of the combined revenue, internal and external, of all operating segments.

(b) The absolute amount of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not report a loss and (ii) the combined reported loss of all operating segments that reported a loss.

(c) Its assets are 10 per cent or more of the combined assets of all operating segments.

Operating segments that do not meet any of the quantitative thresholds may be considered reportable, and separately disclosed, if management believes that information about the segment would be useful to users of the financial statements.

Discovery may combine information about operating segments that do not meet the quantitative thresholds with information about other operating segments that do not meet the quantitative thresholds to produce a reportable segment only if the operating segments have similar economic characteristics.

STATEMENT OF FINANCIAL POSITION

at 30 June 2013

R million	Notes	Group 2013	Group 2012
Assets			
Assets arising from insurance contracts	5	**14 407**	11 681
Property and equipment	6	**533**	251
Intangible assets including deferred acquisition costs	7	**1 828**	1 608
Goodwill	8.2	**1 859**	1 542
Investment in associates	9	**402**	341
Financial assets			
– Equity securities	11	**14 710**	5 096
– Equity linked notes	11	**1 281**	6 480
– Debt securities	11	**5 324**	2 835
– Inflation linked securities	11	**172**	257
– Money market	11	**8 114**	5 729
– Derivatives	12	**541**	149
– Loans and receivables including insurance receivables	13	**3 061**	2 197
Deferred income tax	22	**370**	348
Current income tax asset		**32**	18
Reinsurance contracts	14	**237**	201
Cash and cash equivalents	15	**2 062**	1 929
Total assets		**54 933**	40 662
Equity			
Capital and reserves			
Ordinary share capital and share premium	16.1	**1 470**	1 503
Perpetual preference share capital	16.2	**779**	779
Other reserves		**1 253**	670
Retained earnings		**10 204**	8 778
		13 706	11 730
Non-controlling interest		**2**	1
Total equity		**13 708**	11 731
Liabilities			
Liabilities arising from insurance contracts	17	**19 086**	14 319
Liabilities arising from reinsurance contracts	18	**1 508**	1 457
Financial liabilities			
– Puttable non-controlling interests	19	**3 782**	2 893
– Negative reserve funding	20	**2 813**	1 264
– Borrowings at amortised cost	21	**660**	402
– Investment contracts at fair value through profit or loss	22	**6 049**	2 915
– Derivatives	12	**28**	35
– Trade and other payables	23	**3 179**	2 268
Deferred income tax	24	**3 784**	3 075
Deferred revenue	25	**151**	116
Employee benefits	26	**138**	116
Current income tax liability		**47**	71
Total liabilities		**41 225**	28 931
Total equity and liabilities		**54 933**	40 662

INCOME STATEMENT

for the year ended 30 June 2013

R million	Notes	Group 2013	Group 2012
Insurance premium revenue		**17 893**	14 691
Reinsurance premiums		**(2 233)**	(1 755)
Net insurance premium revenue	27	**15 660**	12 936
Fee income from administration business		**4 819**	4 251
Vitality income		**1 958**	1 603
Investment income	28	**324**	261
Net realised gains on available-for-sale financial assets	29	**1**	81
Net fair value gains on financial assets at fair value through profit or loss	30	**2 099**	737
Net income		**24 861**	19 869
Claims and policyholders' benefits		**(8 884)**	(6 702)
Insurance claims recovered from reinsurers		**1 804**	1 200
Net claims and policyholders' benefits	31	**(7 080)**	(5 502)
Acquisition costs	32	**(3 407)**	(2 775)
Marketing and administration expenses	33, 34	**(7 869)**	(6 910)
Amortisation of intangibles from business combinations	7, 9, 33	**(186)**	(152)
Recapture of reinsurance		**(336)**	–
Recovery of expenses from reinsurers		**139**	148
Transfer from assets/liabilities under insurance contracts		**(1 735)**	(1 075)
– change in assets arising from insurance contracts		**2 262**	2 454
– change in liabilities arising from insurance contracts		**(3 953)**	(3 396)
– change in liabilities arising from reinsurance contracts		**(44)**	(133)
Fair value adjustment to liabilities under investment contracts	22	**(600)**	(50)
Profit from operations		**3 787**	3 553
Puttable non-controlling interests fair value adjustment	19	**(133)**	(13)
Finance costs	35	**(347)**	(265)
Foreign exchange gains	36	**40**	78
Share of (loss)/profit from associates		**(22)**	1
Profit before tax		**3 325**	3 354
Income tax expense	37	**(1 194)**	(1 132)
Profit for the year		**2 131**	2 222
Profit attributable to:			
– ordinary shareholders		**2 063**	2 199
– preference shareholders		**68**	23
– non-controlling interest		**–**	–
		2 131	2 222
Earnings per share for profit attributable to ordinary shareholders of the Company during the year (cents):	38		
– basic		**372.2**	396.1
– diluted		**367.1**	395.7

STATEMENT OF COMPREHENSIVE INCOME

for the year ended 30 June 2013

R million	Group 2013	Group 2012
Profit for the year	**2 131**	2 222
Items that are or may be reclassified subsequently to profit or loss:		
Change in available-for-sale financial assets	**195**	35
– unrealised gains	**223**	145
– capital gains tax on unrealised gains	**(27)**	(40)
– realised gains transferred to profit or loss	**(1)**	(81)
– capital gains tax on realised gains	*	11
Currency translation differences	**292**	324
– unrealised gains	**341**	324
– deferred tax on unrealised gains	**(49)**	–
Cash flow hedges	**96**	32
– unrealised gains	**172**	39
– deferred tax on Unrealised gains	**(33)**	(3)
– current tax on unrealised gains	**(4)**	–
– gains recycled to profit or loss	**(54)**	(4)
– tax on recycled gains	**15**	*
Other comprehensive income for the year, net of tax	**583**	391
Total comprehensive income for the year	**2 714**	2 613
Attributable to:		
– ordinary shareholders	**2 646**	2 590
– preference shareholders	**68**	23
– non-controlling interest	**–**	–
Total comprehensive income for the year	**2 714**	2 613

* *Amount is less than R500 000.*

STATEMENT OF CASH FLOWS

for the year ended 30 June 2013

R million	Notes	Group 2013	Group 2012
Cash flow from operating activities		**1 781**	1 457
Cash generated by operations	39.1	**6 230**	5 401
Net purchases of investments held to back policyholder liabilities		**(4 751)**	(3 849)
		1 479	1 552
Dividends received		**238**	115
Interest received		**617**	395
Interest paid		**(182)**	(113)
Taxation paid	39.2	**(371)**	(492)
Cash flow from investing activities		**(1 257)**	(3 222)
Net purchases of financial assets		**(737)**	(2 968)
Net purchases of equipment		**(302)**	(116)
Net purchase of intangible assets		**(181)**	(138)
Purchase of businesses		**(37)**	–
Cash flow from financing activities		**(671)**	202
Proceeds from issuance of ordinary shares	39.3	**1**	28
Proceeds from issuance of preference shares	39.3	**77**	806
Share issue costs		**–**	(21)
Dividends paid to ordinary shareholders		**(670)**	(580)
Dividends paid to preference shareholders		**(68)**	(23)
Non-controlling interest share buy-backs		**–**	(8)
Repayment of borrowings	39.4	**(11)**	–
Net decrease in cash and cash equivalents		**(147)**	(1 563)
Cash and cash equivalents at beginning of the year		**1 929**	3 285
Exchange gains on cash and cash equivalents		**64**	207
Cash and cash equivalents at end of the year	15	**1 846**	1 929

STATEMENT OF CHANGES IN EQUITY

for the year ended 30 June 2013

R million	Attributable to equity holders of the Company		
	Share capital and share premium	Preference share capital	Share-based payment reserve
Year ended 30 June 2012			
At beginning of the year	1 542	–	318
Profit for the year	–	23	–
Other comprehensive income	–	–	–
Total comprehensive income for the year	–	23	–
Transactions with owners:			
Increase in treasury shares	(47)	–	–
Realised gains from treasury shares	8	–	–
Issue of preference shares	–	800	–
Share issue costs	–	(21)	–
Non-controlling interest share issues	–	–	–
Transfer to puttable non-controlling interests liability	–	–	–
Non-controlling interest share buy-backs	–	–	–
Employee share option schemes:			
– value of employee services	–	–	1
Dividends paid to preference shareholders	–	(23)	–
Dividends paid to ordinary shareholders	–	–	–
Total transactions with owners	(39)	756	1
At end of the year	1 503	779	319
Year ended 30 June 2013			
At beginning of the year	**1 503**	**779**	**319**
Profit for the year	**–**	**68**	**–**
Other comprehensive income	**–**	**–**	**–**
Total comprehensive income for the year	**–**	**68**	**–**
Transactions with owners:			
Increase in treasury shares	**(39)**	**–**	**–**
Proceeds from treasury shares	**6**	**–**	**–**
Non-controlling interest share issues	**–**	**–**	**–**
Dividends paid to preference shareholders	**–**	**(68)**	**–**
Dividends paid to ordinary shareholders	**–**	**–**	**–**
Total transactions with owners	**(33)**	**(68)**	**–**
At end of the year	**1 470**	**779**	**319**

* *This reserve relates to the revaluation of available-for-sale financial assets.*

Of the R10 204 million (2012: R8 778 million) held in retained earnings, R3 401 million (2012: R3 092 million) is distributable. The balance is held to meet the capital requirements in various Group companies.

Attributable to equity holders of the Company						
Revaluation reserve*	Translation reserve	Hedging reserve	Retained earnings	Total	Non-controlling interest	Total
23	(70)	7	7 149	8 969	4	8 973
–	–	–	2 199	2 222	–	2 222
35	324	32	–	391	–	391
35	324	32	2 199	2 613	–	2 613
–	–	–	–	(47)	–	(47)
–	–	–	–	8	–	8
–	–	–	–	800	–	800
–	–	–	–	(21)	–	(21)
–	–	–	–	–	34	34
–	–	–	–	–	(29)	(29)
–	–	–	–	–	(8)	(8)
–	–	–	–	1	–	1
–	–	–	–	(23)	–	(23)
–	–	–	(570)	(570)	–	(570)
–	–	–	(570)	148	(3)	145
58	254	39	8 778	11 730	1	11 731
58	**254**	**39**	**8 778**	**11 730**	**1**	**11 731**
–	**–**	**–**	**2 063**	**2 131**	**–**	**2 131**
195	**292**	**96**	**–**	**583**	**–**	**583**
195	**292**	**96**	**2 063**	**2 714**	**–**	**2 714**
–	**–**	**–**	**–**	**(39)**	**–**	**(39)**
–	**–**	**–**	**–**	**6**	**–**	**6**
–	**–**	**–**	**–**	**–**	**1**	**1**
–	**–**	**–**	**–**	**(68)**	**–**	**(68)**
–	**–**	**–**	**(637)**	**(637)**	**–**	**(637)**
–	**–**	**–**	**(637)**	**(738)**	**1**	**(737)**
253	**546**	**135**	**10 204**	**13 706**	**2**	**13 708**

1. SEGMENT INFORMATION

The Group has identified its reportable segments based on a combination of products and services offered to customers and the location of the markets served.

The following summary describes the operations of each of the Group's reportable segments:

(i) **Health South Africa:** administers and provides managed care services to medical schemes and renders administration services to other business segments within the Group.

(ii) **Life South Africa:** offers a range of insurance and financial solutions to the Group's clients against the financial impact of lifestyle-changing events in South Africa.

(iii) **Invest South Africa:** offers, through a range of investment fund choices, including Discovery managed unit trusts, a comprehensive and flexible range of investment choices. These products are sold through a number of investment wrappers including Discovery Life policies and are offered to individuals in South Africa.

(iv) **Vitality South Africa:** offers health and lifestyle benefits with selected partners to the Group's clients. This segment includes the DiscoveryCard which is offered to clients within South Africa.

(v) **Health United Kingdom:** offers consumer-engaged private medical insurance products to employer groups and individuals in the United Kingdom, together with Prudential Assurance Company Limited. All contracts in this segment are short-term insurance contracts.

R million	SA Health	SA Life
30 June 2013		
Income statement		
Insurance premium revenue	16	7 189
Reinsurance premiums	(2)	(1 299)
Net insurance premium revenue	14	5 890
Fee income from administration business	4 061	140
Guarantee received from HumanaVitality	–	–
Vitality income	–	–
Investment income on assets backing policyholder liabilities	–	141
Finance charge on negative reserve funding	–	–
Inter-segment funding[1]	–	(360)
Net fair value gains on financial assets at fair value through profit or loss	–	501
Net income	4 075	6 312
Claims and policyholders' benefits	(2)	(3 648)
Insurance claims recovered from reinsurers	3	1 004
Net claims and policyholders' benefits	1	(2 644)
Acquisition costs	–	(1 497)
Marketing and administration expenses		
– depreciation and amortisation	(164)	(29)
– other expenses	(2 224)	(1 198)
Recovery of expenses from reinsurers	–	–
Transfer from assets/liabilities under insurance contracts		
– change in assets arising from insurance contracts	–	1 189
– change in liabilities arising from insurance contracts	–	117
– change in liabilities arising from reinsurance contracts	–	(134)
Fair value adjustment to liabilities under investment contracts	–	(10)
Normalised profit/(loss) from operations	1 688	2 106

(1) The inter-segment funding of R360 million (2012: R271 million) reflects a notional allocation of interest earned on the negative reserve backing policyholders' funds of guaranteed investment products and hence is transferred to Discovery Invest.

(vi) **Life United Kingdom:** offers a risk-only life assurance product. All contracts in this segment are long-term assurance contracts offered to both employer groups and individuals in the United Kingdom, together with Prudential Assurance Company Limited.

(vii) **New business development:** includes expenses incurred to investigate new products and markets as well as start-up businesses and acquisitions including but not limited to The Vitality Group in the United States of America, Ping An Health in China, AIA Vitality in Asia and Discovery Insure in South Africa.

(viii) **All other segments:** includes those segments that do not meet the quantitative thresholds set out in IFRS 8 and cannot be aggregated with another reportable segment. It includes costs incurred by Discovery Limited and Discovery Group Europe Limited.

The Chief Executive Officers assess the performance of the operating segments based on normalised profit/loss from operations. This measurement basis excludes the effects of business combinations, realised gains from available-for-sale financial assets, puttable non-controlling interest fair value adjustments and finance costs. Investment income and expenditure attributable to equity holders, and foreign exchange gains and losses are not allocated to the segments as this type of activity is primarily driven by the Group treasury function which manages the cash position of the Group. The Group's segments, report their profit or loss based on the Group's accounting policies. Internal charges and transfer pricing adjustments are reflected in the performance of each business.

The segment information provided to the Chief Executive Officers for the reportable segments is provided in the following table.

SA Invest	SA Vitality	UK Health	UK Life	New business development	All other segments	Total
4 520	–	4 744	1 128	296	–	17 893
–	–	(733)	(190)	(9)	–	(2 233)
4 520	–	4 011	938	287	–	15 660
555	–	34	–	11	–	4 801
–	–	–	–	18	–	18
–	1 660	100	–	198	–	1 958
–	–	51	–	–	–	192
–	–	–	(124)	–	–	(124)
360	–	–	–	–	–	–
1 598	–	–	–	–	–	2 099
7 033	1 660	4 196	814	514	–	24 604
(1 538)	–	(3 281)	(192)	(223)	–	(8 884)
–	–	668	111	18	–	1 804
(1 538)	–	(2 613)	(81)	(205)	–	(7 080)
(401)	(73)	(379)	(1 011)	(46)		(3 407)
(1)	–	(20)	–	(15)	(1)	(230)
(256)	(1 552)	(1 166)	(549)	(640)	(54)	(7 639)
–	–	139	–	–	–	139
–	–	–	1 073	–	–	2 262
(4 026)	–	(11)	(10)	(23)	–	(3 953)
–	–	–	90	–	–	(44)
(590)	–	–	–	–	–	(600)
221	35	146	326	(415)	(55)	4 052

NOTES TO THE ANNUAL FINANCIAL STATEMENTS continued

for the year ended 30 June 2013

1. SEGMENT INFORMATION continued

R million	SA Health	SA Life
30 June 2012		
Income statement		
Insurance premium revenue	16	6 085
Reinsurance premiums	(1)	(1 082)
Net insurance premium revenue	15	5 003
Fee income from administration business	3 705	99
Guarantee received from HumanaVitality	–	–
Vitality income	–	–
Investment income on assets backing policyholder liabilities	–	113
Finance charge on negative reserve funding	–	–
Inter-segment funding[1]	–	(271)
Net fair value gains on financial assets at fair value through profit or loss	–	252
Net income	3 720	5 196
Claims and policyholders' benefits	(3)	(2 639)
Insurance claims recovered from reinsurers	–	739
Net claims and policyholders' benefits	(3)	(1 900)
Acquisition costs	–	(1 373)
Marketing and administration expenses		
– depreciation and amortisation	(135)	(26)
– other expenses	(2 083)	(1 122)
Recovery of expenses from reinsurers	–	–
Transfer from assets/liabilities under insurance contracts		
– change in assets arising from insurance contracts	–	1 503
– change in liabilities arising from insurance contracts	–	(281)
– change in liabilities arising from reinsurance contracts	–	(161)
Fair value adjustment to liabilities under investment contracts	–	(17)
Normalised profit/(loss) from operations	1 499	1 819

(1) The inter-segment funding of R360 million (2012: R271 million) reflects a notional allocation of interest earned on the negative reserve backing policyholders' funds of guaranteed investment products and hence is transferred to Discovery Invest.

SA Invest	SA Vitality	UK Health	UK Life	New business development	All other segments	Total
3 683	–	4 193	623	91	–	14 691
–	–	(566)	(102)	(4)	–	(1 755)
3 683	–	3 627	521	87	–	12 936
421	–	20	5	1	–	4 251
–	–	–	–	14	–	14
–	1 454	58	–	91	–	1 603
–	–	19	–	–	–	132
–	–	–	(66)	–	–	(66)
271	–	–	–	–	–	–
485	–	–	–	–	–	737
4 860	1 454	3 724	460	193	–	19 607
(904)	–	(2 992)	(102)	(62)	–	(6 702)
–	–	412	49	–	–	1 200
(904)	–	(2 580)	(53)	(62)	–	(5 502)
(351)	(65)	(282)	(685)	(19)	–	(2 775)
(5)	–	(11)	–	(8)	–	(185)
(270)	(1 384)	(946)	(491)	(359)	(70)	(6 725)
–	–	148	–	–	–	148
–	–	1	950	–	–	2 454
(3 146)	–	37	–	(6)	–	(3 396)
–	–	–	28	–	–	(133)
(33)	–	–	–	–	–	(50)
151	5	91	209	(261)	(70)	3 443

1. SEGMENT INFORMATION continued

A reconciliation of normalised profit from operations to profit before tax is provided as follows:

R million	Group 2013	Group 2012
Normalised profit from operations	**4 052**	3 443
Investment income attributable to shareholders	**132**	129
Net realised gains on available-for-sale financial assets	**1**	81
Amortisation of intangibles from business combinations	**(186)**	(152)
Finance costs	**(223)**	(199)
Foreign exchange gains	**40**	78
Share of loss from associate	**(22)**	(13)
Puttable non-controlling interests fair value adjustment	**(133)**	(13)
Recapture of reinsurance	**(336)**	–
Profit before tax	**3 325**	3 354

2. MANAGEMENT OF INSURANCE RISK

Discovery enters into contracts that carry insurance risk or financial risk or both. The following table analyses the various contracts offered by the Group and the risks these contracts transfer.

Contracts offered by the Group	Contract type	Insurance risk	Financial risk
Discovery Life			
– Discovery Life Plan	Insurance	✓	
– Health Plan Protector	Insurance	✓	
– Discovery Retirement Optimiser: Linked	Unit-linked insurance	✓	✓
– Discovery Retirement Optimiser: Guaranteed	Insurance	✓	
– DiscoveryCard Protector	Insurance	✓	
– Global Education Protector	Insurance	✓	
– Supplementary Cancer Protector	Insurance	✓	
– Funeral Cover	Insurance	✓	
– Group Life	Insurance	✓	
– Destiny Provident Fund	Unit-linked investment		✓
– Destiny Benefit Fund	Unit-linked investment		✓
Discovery Invest			
– Unit-linked contracts without significant insurance risk	Unit-linked investment		✓
– Unit-linked contracts with significant insurance risk	Unit-linked insurance	✓	✓
– Guaranteed return plans	Insurance	✓	✓
– Fixed annuities	Insurance	✓	✓
Discovery Insure			
– Short-term insurance	Insurance	✓	
PruHealth			
– Individual product	Insurance	✓	
– SME product	Insurance	✓	
– Corporate product	Insurance	✓	
PruProtect			
– PruProtect Life Plan	Insurance	✓	
– Over 50's life cover	Insurance	✓	

The risks identified for the contracts above and the management thereof will be discussed as follows:

Management of insurance risks: pages 179 to 196

Management of financial risks: pages 196 to 214

The insurance risk under any one insurance contract is the possibility of a claim arising from that contract and the uncertainty of the amount and timing of the resulting claim. This risk is random and therefore unpredictable.

A large portfolio of independent but similar insurance contracts, allow for the use of probability theory to predict the number and value of claims over a defined period. Insurance risk, when considering a large portfolio of insurance contracts, is thus the probability that the actual amount of claims over a defined period is different to expected. This could in turn result in the value of insurance liabilities being over or under estimated.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome will be. Discovery reduces claims variability by underwriting policies and by using reinsurance to protect against single large claims.

Discovery assumes the following risks transferred from insurance contracts:

- automatic increase take-up rate
- capital adequacy requirements and protection against adverse experience
- concentration risk
- currency risk
- expense risk
- lapse and surrender risk
- liquidity risk
- market and mismatching risk
- modeling and data risk
- operational/implementation risk
- policy wording/legal risks
- regulatory risk
- reputational risk
- tax risk
- underwriting experience risk

The following section will briefly describe the various contracts offered by the subsidiaries within the Group, the insurance risks associated with those products and the way the Group manages these risks.

2.1 Discovery Life and Discovery Invest

2.1.1 Product descriptions

Discovery Life offers policyholders a range of insurance and financial solutions. The Discovery Life products reflect Discovery's underlying philosophy to make members healthier and to enhance and protect their lives.

Discovery Life offers some unique benefits that integrate with the benefits offered by Discovery Health, Discovery Vitality, DiscoveryCard and Discovery Invest.

Discovery Life Plan

The Discovery Life Plan provides protection against a comprehensive spectrum of risks. Discovery Life offers a Classic Life Plan with broad and comprehensive protection for the policyholder and his or her immediate family and an Essential Life Plan which offers cost effective protection for the principal policyholder and his or her spouse.

The Discovery Life Plan covers:

- Life Cover Benefits
- Disability Benefits
- Severe Illness Benefits
- Income Continuation Benefits

The Life Fund forms the base amount of cover insured under the Life Plan, ie. the basic sum assured amount. The Life Fund can be linked to a benefit escalation rate, for example inflation, and will then automatically increase at each policy anniversary. The Life Fund can also be linked to global investment markets and a selection of currencies via the Global Linkage Benefit to provide additional protection in real terms and in foreign currencies. The Cover Integrator allows for an increase in the Life Fund at a significantly reduced premium and further rewards policyholders for managing their health by engaging in Vitality. The Financial Integrator increases the Life Fund and offers protection against adverse financial events such as asset price depreciation, increases in interest rates, rand depreciation and high severe illness claims. The Financial Integrator fluctuates on an annual basis to offer protection against the adverse financial events.

The key risk benefits are then defined as a percentage of the Life Fund. The Life Fund is reduced by the amount of benefits paid from the Life Fund. The Life Fund can be protected against claims by means of the Minimum Protected Fund. Multiple claims are allowed against the Life Fund from the same benefit.

2. MANAGEMENT OF INSURANCE RISK continued

There are a number of risk benefits that are defined in monetary terms or in form of indemnity benefits, rather than being expressed as a percentage of the Life Fund. These benefits include:

- Income Continuation Benefit
- Global Education Benefit
- Global Health Protector

The Life Plan has unique features allowing policyholders to add benefits for other family members. The Global Education Protector, Global Health Protector, Childbirth Benefit, Child Severe Illness Benefit, Parent Severe Illness Benefit and Family Trauma Benefit allow protection for the whole immediate family.

By actively maintaining and improving their health, Discovery Life policyholders, through the Integrator Benefit, could receive premium discounts and refunds of premiums.

The Life Plan provides whole of life cover. Premium guarantees are offered and quantified on most benefits. For example, the premiums for Life Cover are guaranteed not to increase by more than 25% for any 10 year period.

The Life CoverBooster can also be added to the Life Plan. This benefit provides 32% additional life cover at no additional premium for three years. After three years, clients have guaranteed insurability that they can buy up the additional cover at a discount of up to 15%. In addition, the Life CoverBooster provides a 5% cash conversion whereby 5% of the CoverBooster amount will be paid out as a cash lump sum at age 65 to supplement retirement savings.

Premiums are payable monthly. There are four funding methods that allow policyholders a choice of premium funding patterns. A combination of level premium funding patterns, annually increasing premium patterns and ten-yearly stepped premium funding patterns are offered. The higher the compulsory future premium increase, the lower the starting premium.

At 30 June 2013 there were 293 611 Life Plans with an annualised premium income of R5 425 million (2012: 277 355 Life Plans with an annualised premium income of R4 685 million). The annualised premium income is calculated by multiplying the monthly in-force premium at 30 June by 12 months.

Health Plan Protector

The Health Plan Protector will fund contributions to the Discovery Health Medical Scheme in the event of death, disability or severe illness. It further rewards members for positive health management through the payback benefit and Health Dividends. The Health Plan Protector can be added to the Life Plan or can be bought on a stand-alone basis. The Health Plan Protector provides cover up to age 65, however premiums are not guaranteed.

At 30 June 2013 there were 50 139 Health Plan Protector policies with an annualised premium income of R209 million (2012: 50 677 Health Plan Protector policies with an annualised premium income of R195 million).

Discovery Retirement Optimiser

The Discovery Retirement Optimiser offers funding for retirement and offers unique benefits that could together with the Life Plan, capitalise unneeded risk cover to boost retirement funding. Policyholders have a choice of linked investment portfolios or a portfolio that offers a guaranteed return in real terms.

As at 30 June 2013 there were 55 011 Discovery Retirement Optimiser policies of which 49 917 policies are linked to the Life Plan. These policies have an annualised premium income of R1 014 million (At 30 June 2012 there were 51 343 Discovery Retirement Optimiser policies, 47 546 of these policies were linked to the Life Plan, with an annualised premium income of R852 million).

DiscoveryCard Protector

The DiscoveryCard Protector will cover the outstanding balance on the DiscoveryCard in the event of death, disability or severe illness. It further provides a monthly benefit for a defined period equal to the average DiscoveryCard spend in the six month period prior to the life changing event.

At 30 June 2013 there were 12 212 DiscoveryCard Protector policies with an annualised premium income of R12 million (2012: 13 697 policies with an annualised premium income of R13 million).

Global Education Protector

The Global Education Protector funds education costs for children in the event of death, disability or severe illness of the insured life. Cover is provided to the earlier of the insured life reaching age 65 or the child reaching age 24. This benefit can be purchased on a stand-alone basis.

At 30 June 2013 there were 2 673 stand-alone Global Education Protector policies with an annualised premium income of R8 million (2012: 2 650 stand-alone Global Education Protector policies with an annualised premium income of R7 million).

Supplementary Cancer Protector

The Supplementary Cancer Protector benefit will pay defined monthly amounts which can be used to meet costs that arise when a family is affected by cancer.

At 30 June 2013 there were 7 699 stand-alone Supplementary Cancer Protector policies with an annualised premium income of R18 million (2012: 7 358 Supplementary Cancer Protector policies with an annualised premium income of R15 million).

Funeral Cover

The Funeral Cover benefit will pay out a defined lump sum in the event of death which can be used to cover the costs of a funeral. This lump sum is doubled in the event of accidental death. An education benefit is automatically included at a defined amount which aims to fund the education costs for children upon death of the principal member or spouse. Additional memorial and grocery benefits may be added to the policy as an option.

At 30 June 2013 there were 860 stand-alone Funeral Cover policies with an annualised premium income of R2 million.

Group Life

Discovery Life offers a comprehensive spectrum of protection benefits on a group basis. Life Cover, Severe Illness, Disability and Income Continuation Benefits are offered on a group basis. The policies offered under Group Life can be cancelled or the premiums adjusted at the end of the contract term (usually one year).

At 30 June 2013 there were 354 534 lives covered under group policies with an annualised premium income of R1 060 million (2012: 334 454 lives covered under group policies with an annualised premium income of R885 million).

Discovery Invest

Discovery Invest offers investors access to a comprehensive and flexible range of investment solutions which can be tailored to the needs of every investor.

A range of investment wrappers are provided to ensure flexibility and to optimise the investments according to the investment objectives and time horizon of the investor. A wrapper is the legal structure that allows policyholders to make underlying investments with different tax and other legal implications.

The following wrappers are available:

- **Endowment:** A medium-term investment vehicle that provides tax efficiencies for an investor with a five to ten year time horizon.
- **Flexible investment:** A flexible investment vehicle that allows tailor made investments solutions whilst providing immediate access to funds.
- **Retirement plan:** A long-term investment vehicle providing a tax efficient structure for saving towards retirement.
- **Preserver plans:** An investment vehicle that helps to ensure retirement benefits continue to grow on a tax efficient basis once a policyholder has left the retirement plan of an employer.
- **Retirement income plan:** Fixed and linked annuities are provided giving flexibility to meet retirement needs.

A comprehensive range of investment fund choices are provided including unique Discovery Invest funds. The funds include:

- **Discovery Invest funds:** Includes a comprehensive range of Discovery Invest's single and multi-manager funds across a range of asset classes.
- **Dynamically protected funds:** Unique Discovery Invest funds that are designed to protect investors against the major risks associated with investment choice, for example, underperformance by fund, asset class and geographic region.
- **Special purpose funds:** These funds are designed to provide solutions to investors looking to save for specific goals, such as retirement. These funds provide alternative and innovative management expertise.
- **External funds:** Discovery Invest provides a broad range of externally managed funds.

Integrating Invest and Discovery Life products reduces the cost of investment and enhances benefits available under the Invest plans.

- **Investment Integrator:** Uses inter alia the health improvements from Vitality and tax efficiencies created to offer a cost effective endowment and increase the value of the investment. A fee reduction of up to 100% can be achieved on both administration and asset management fees.
- **Annuity Integrator:** By releasing the value of a policyholder's life cover at retirement, the Annuity Integrator creates enhanced benefits for Discovery Retirement Income Plan investors. The benefits include increased retirement income, protection against longevity, protection against ill-health and protection against poor performance of underlying assets.
- **Guaranteed return plans:** Guaranteed return plans include the following:
  - The Guaranteed Growth Plan is a single premium endowment that provides a guaranteed return at the end of five years.
  - The Guaranteed Income Plan provides a guaranteed return at the end of five years on the chosen percentage of the lumpsum contribution. The remainder of the lumpsum will provide a monthly or annual income.
- **Upfront Investment Integrator:** Provide an upfront boost to the investment values provided on the Endowment plan.
- **Life Booster:** Provide a boost to the investment fund value on death of between 5% and 15% depending on the member's Vitality status.

At 30 June 2013 there were 82 854 Invest plans with an annualised premium equivalent of R3 333 million (2012: 65 573 Invest plans with an annualised premium equivalent of R2 549 million). The annualised premium equivalent includes single premiums at 10% of the single premium.

2. MANAGEMENT OF INSURANCE RISK continued

2.1.2 Insurance risks

Market and mismatching risk

Mismatching risk is the risk that movements in assets and liabilities are out of line given changes in market conditions as defined on page 196.

Discovery Life

For Discovery Life, the insurance related cash outflows (eg. benefit payments, administrations expenses, etc.) are covered by expected future cash inflows (predominantly future premiums). This can clearly be seen by considering the future net cash flows arising from insurance contracts. These cash flows are calculated in accordance with the accounting policies. Premium and benefit increases on insurance contracts are recognised in line with the lowest increase option available to the policyholder that will not require any other changes of premiums relative to benefits.

The expected future cash flows utilised in the calculation of assets under insurance contracts were as follows:

R million	Year 1	Years 2 to 5	Years 6 to 10	Years 11 to 20	Years 21+
2013					
Discovery Life	**1 419**	**5 223**	**6 085**	**10 381**	**20 885**
2012					
Discovery Life	1 396	4 430	5 002	8 422	17 359

The value of assets under insurance contracts of R13 461 million (2012: R11 308 million) is calculated by discounting the expected future cash flows shown above. The effect of discounting is R30 532 million (2012: R25 302 million). The discount rate is set with reference to the prevailing risk free SA gilt yield. The value of assets under insurance contracts is subject to interest rate risk.

Reconciliation of the assets under insurance contracts disclosed in the cash flows above to the statement of financial position (note 5):

R million	2013	2012
Assets arising from insurance contracts at end of year	**13 534**	10 838
Adjusted for:		
– Unit-linked policyholder liabilities	**3 437**	2 362
– Assets arising from insurance contracts relating to PruProtect	**(3 510)**	(1 892)
Discovery Life value of assets under insurance contracts	**13 461**	11 308

Discovery Invest

For Discovery Invest, the insurance related cash outflows are matched with a combination of a release of policyholder assets (net of retained fees), investment return on these assets and Discovery Life cash flows.

The expected future cash flows in the calculation of liabilities under insurance contracts were as follows:

R million	Year 1	Years 2 to 5	Years 6 to 10	Years 11 to 20	Years 21+
2013					
Discovery Invest	**(878)**	**(4 613)**	**506**	**776**	**444**
2012					
Discovery Invest	(265)	(4 420)	480	514	196

The value of the liabilities under insurance contracts of R4 286 million (2012: R3 644 million) is calculated by discounting the expected future cash flows as shown above. The effect of discounting is a decrease of R522 million (2012: R148 million). The discount rate is set with reference to the prevailing risk free SA gilt yield.

Reconciliation of the liabilities under insurance contracts disclosed in the cash flows above to the statement of financial position (note 17):

R million	2013	2012
Long-term insurance contract liabilities with fixed and guaranteed terms	**5 540**	4 626
Negative insurance liability included in unit-linked insurance contracts	**(1 254)**	(982)
Discovery Invest value of liabilities under insurance contracts	**4 286**	3 644

There is thus a risk that a change in the risk free SA gilt yield could cause a change in the value of the assets and liabilities under insurance contracts.

The outstanding claims and incurred but not reported claims are mostly short-term in nature and have consequently been matched with cash.

The risk under the Global Linkage Benefit is fully reinsured and Discovery does not face any net direct market risk. In the event of the reinsurer defaulting, the investments held by the reinsurer to hedge their risk relating to the Global Linkage Benefit, will be ceded to Discovery Life. Discovery Life reviews the assets held by the reinsurer on a six monthly basis.

Automatic increase take-up rate

The majority of Discovery Life Plan policyholders have selected policies with automatic premium and benefit increases.

Recurring premium Invest plans have various automatic increase options ranging from 0% up to 20% per annum. A CPI-linked option is also available. The majority of Invest policyholders have selected plans with automatic benefit increases.

The automatic increases increase the profitability of the plans to Discovery over time since the cash flows under the policy are maintained in real terms.

These automatic increases are contractual. However, if a policyholder is no longer in a position to meet the premium increases, they may elect to change their policy to a plan with lower premium and benefit increases. In practice it has been found that most of the policyholders continue with their initial funding plans. However, for valuation purposes it has been assumed that all South African policyholders change to plans with minimum premium increases without changing the cover levels as at the valuation date. This is the worst case scenario and thus acts as a margin.

Lapse and surrender risk

Policyholders have the option to discontinue or reduce contributions at any time.

There is a risk of financial loss due to the withdrawal rate being higher than expected. The risk is highest during the early duration of the policy since the acquisition costs and commission incurred at the inception of the policy will not yet have been recouped. On Invest plans, the surrender value may also exceed the policy value, net of expenses, at early durations.

On Life Plans there is also a risk of lower than expected withdrawals at late durations of the policy since no surrender value is payable on withdrawal from a risk policy even where reserves are positive.

There is a further risk that Life Plan withdrawals are selective from a claims experience point of view. For example, healthy lives may find it easier to obtain cover elsewhere compared to less healthy lives.

Future earnings under Life Plans are dependent on the number of policies remaining in future years and thus future earnings are dependent on the lapse rate. The future expected earnings vary by the premium funding method chosen by the policyholder. In general, the higher the increases, the higher the withdrawal risk to future earnings.

Future earnings under Invest plans are dependent on the value of assets under management and thus future earnings are dependent on the withdrawal and surrender rate.

The lapse risk is managed as follows:

- *Product design*
  Products are designed to be sustainable in the long-term. New product offerings are made available to existing policyholders as far as possible to prevent lapse and re-entry risk.

  Integration between different product offerings across Discovery enhances the value proposition of the overall package of products from Discovery. For example, Vitality provides unique rewards and benefits to members who have proven to be a credible risk differentiator. Premium discounts are available to policyholders who actively engage in a healthier lifestyle and utilise the Vitality benefit. Better terms are thus offered to healthy lives compared to less healthy lives.

  No surrender benefit is offered on risk benefits and thus the loss on withdrawal on Life Plans is reduced.

- *Commission clawback*
  Discovery Life predominantly distributes via independent brokers and tied agents. Commissions are clawed back from intermediaries where a policy lapses within the first two years of inception. The amount of commission clawback depends on the duration of the policy in months and gradually reduces from 100% to 0% over the two year period.

- *Client relationships*
  All premiums are collected via debit order. Clients are contacted after a failed debit order and after notification of a cancellation. The reason for the cancellation is established and wherever possible the policies are conserved.

- *Reinsurance*
  Discovery has reinsurance treaties that protect a part of the assets under insurance contracts against a substantial increase in lapses. The reinsurance protects Discovery Life against the loss of assets under insurance contracts in the event that the aggregate lapse rate exceeds a predefined level.

2. MANAGEMENT OF INSURANCE RISK continued

- *Experience monitoring*
  Lapse experience is monitored on a monthly basis and the data is analysed to establish possible trends for which management action can be taken.

- *Proactive conservation*
  Targeted conservation campaigns are run for example; financial advisors are notified of clients that do not have certain features on their policies that are correlated with good persistency. Financial advisors are thus encouraged to add such features.

Underwriting experience risk

There is a risk that actual mortality and morbidity experience is higher than expected on Life Plans. This could arise as a result of the number of claims or the value of claims being higher than expected.

On guaranteed annuities there is a risk that mortality experience is lower than expected and thus income payments continue for longer than expected. The guaranteed annuity book of Discovery Life was insignificant at 30 June 2013. Discovery Life does not offer any deferred annuities where the annuity rate at a future point in time is guaranteed for new entrants.

Investment products are not directly impacted by mortality and morbidity risks. The Annuity Integrator's Ill-health booster boosts retirement income on severe illness. The Annuity Integrator's Longevity booster boosts retirement income every 10 years. The Life Booster increases the investment fund value by between 5% and 15% on death, depending on Vitality status. The costs of the benefits were allowed for in the product design and pricing of the benefits.

Selection risk is the risk that worse risks than expected are attracted and these risks are then charged inadequate premiums. Selection could also lead to higher than expected mortality and morbidity experience on Life Plans or lower mortality on guaranteed annuity policies.

There is a risk that the emergence of a new disease or epidemic can increase the number of claims.

The risks are managed through:

- *Product design and pricing*
  Products are carefully designed to minimise adverse selection. Rating factors are applied to standard premium rates to differentiate between different levels of risk. For example, premiums are differentiated by income, education level, smoker status, gender, medical history and age. Discovery Life has the unique ability to take additional rating factors into account for example the current medical scheme claims and lifestyle factors.

  All new premium rates are reviewed and approved by the statutory actuary. Product integration between the different product offerings in the Discovery Group helps to attract healthier lives than average in the market leading to positive selection.

  For certain of the product-options offered under the Life Plan, Discovery Life has retained the option to review premium rates annually throughout the life of the contract because of uncertainties underlying the value of the benefits offered. Only premiums that can be predicted with confidence are guaranteed. Where guarantees are offered, Discovery guarantees that premiums can only be reviewed every 10 years and increased by a maximum of 25%. The guarantee provided to the policyholder will, however, be strengthened based on the policyholder's actual annual historic Vitality status.

  Discovery Life predominantly operates in the high end of the insurance market where the risk to AIDS is lower than for the market as a whole. The impact of HIV/AIDS is considered and allowed for during the product development and pricing.

  Group business is reviewed on a contract by contract basis, with the review period never exceeding two years. AIDS risk is specifically allowed for in the pricing of individual groups.

  Overall, Discovery Life has experienced better than anticipated claims experience during every reporting period since its inception in 2001.

- *Underwriting*
  Underwriting ensures that only insurable risks are accepted and that premiums reflect the unique circumstances of each risk. For individual policies with lump sum life cover, the minimum requirement will be an HIV test.

  Financial underwriting is applied to ensure that the policyholder can justify the amount of cover applied for. Premium loadings and exclusions are applied where high risks are identified. For Integrated policies, Discovery Life can dynamically adjust certain premiums using the information from the health claims experience of a policyholder who is also a member of the Discovery Health Medical Scheme and Vitality. This provides Discovery Life with an advantageous position in the market.

  Group business is underwritten on an employer by employer basis and additional allowance is made for the impact of industry class, income and geographic location on expected claims experience. The free cover limit is the sum assured that will be given automatically to a specific life without further specific underwriting. The free cover limits are set separately for each scheme depending on the size and cover chosen by the specific scheme.

  Monthly internal quality assurance audits are performed on underwriting to minimise the risk of incorrect underwriting decisions.

- *Reinsurance*
  Reinsurance protects against volatility in claims experience and against an accumulation of risk. Reinsurance is further utilised on a facultative basis if uncertainty exists over the terms that should be offered to a particular risk.

  In addition, reinsurers provide specialist advice when designing new products.

  Discovery Life utilises surplus reinsurance to reinsure amounts in excess of defined retention levels. Discovery Life is thus protected against large individual claims.

  In addition, catastrophe reinsurance reduces the risk of an accumulation of risk due to a single event. Both individual and group business are covered by catastrophe reinsurance.

- *Experience monitoring*
  Experience investigations are conducted and corrective action is taken where adverse experience is noted. Experience monitoring is done on at least a quarterly basis.

Expense risk

Expense risk is the risk of actual expenses being higher than expected. Expenses could exceed expectations due to an increase in the expense inflation or due to a reduction in the number of in-force policies. A reduction in the assets under management could be an expense risk due to the number of fixed costs. Expenses are monitored on a monthly basis against budgeted expenses. Any deviation from the budget is investigated, reported and where necessary, remedial action is taken.

Modelling and data risk

The actuarial liabilities are calculated using complex discounted cash flow models. There is thus a risk that the model doesn't accurately project the policy cash flows in the future.

The risk is controlled using specialist actuarial software that is widely used and accepted in the life insurance industry throughout the world. This is tailored for Discovery.

The original actuarial model was tested and verified using an independent but identical parallel model. Any changes made are externally and independently reviewed. Parallel models are developed to test any modelling changes.

The model relies on data from the administration system and there is thus a further risk that the data does not accurately reflect the policies being valued.

The data is extracted from modern administration systems and subjected to detailed checks together with high-level reasonability checks. Discovery Life does not have any legacy systems that could impact on the data quality. Data is checked at each valuation date.

Operational/Implementation risk

Segregation of duties ensures multiple checks on processes and further protects against the risk of fraud. Discovery does not have any legacy systems and processes to deal with thereby reducing operational risk.

Regulatory risk

Discovery Life operates in a highly regulated environment which is currently being scrutinised and questioned by both consumers and regulators. This has resulted in the constant review of the in force regulations and the interpretation thereof. The regulatory risk can thus be defined as the potential detrimental impact unexpected changes in regulations (or interpretation thereof) may have on Discovery Life.

Discovery Life is a member of the Association for Savings and Investment SA, an industry-wide body that engages in discussions with policymakers and regulators.

Although Discovery endeavours to design insurance and financial solutions which meet the requirements of the current regulations in force, the risk does exist that changes in the regulations or the interpretation of the regulations, over time may result in the current products not fully complying with the regulations in force in future. This risk is managed through constantly seeking legal advice on new product developments. Further, all insurance products issued by Discovery Life have to be signed off by the independent statutory actuary.

Discovery Life's compliance department enhances regulatory compliance through audits and by monitoring developments in the regulatory environment.

Tax risk

Tax risk is the risk that the actual future tax liability is different to what is currently expected. This could be as a result of an incorrect interpretation or application of tax legislation or as a result of changes to tax legislation.

External tax advice is obtained as required to ensure that products are structured in a tax efficient way. Uncertainty currently exists with regards to potential changes to the taxation of life insurers following the announcement by the Minister of Finance during the February 2013 budget.

2. MANAGEMENT OF INSURANCE RISK continued

Currency risk

All of Discovery Life's insurance benefits are Rand denominated, with the exception of the Global Linkage Benefit, a benefit where the sum insured can be linked to global investment markets or a selection of currencies. The Global Linkage Benefit is fully reinsured. Discovery Life thus does not have significant net currency risk.

Capital adequacy requirements and protection against adverse experience

There is a risk that future premiums, investment returns and estimates used to calculate liabilities are insufficient to provide for variations in actual future experience. Margins are maintained in all insurance liabilities. In addition, Discovery maintains shareholder capital to meet substantial deviations in experience.

In accordance with the Long-term Insurance Act (1998), Discovery Life is required to demonstrate solvency to the Registrar of Long-term Insurance. Discovery Life thus needs to maintain sufficient shareholder assets, over and above the assets required to fund shareholder liabilities, to fund the Capital Adequacy Requirement (CAR).

The CAR is calculated in accordance with the Standard of Actuarial Practice Note (SAP) 104 as issued by the Actuarial Society of South Africa (ASSA). The CAR calculation is intended to approximate a risk-based capital measure and covers the major areas of insurance risk. It explicitly covers the following areas of risk:

- lapse and withdrawal risk
- fluctuations in mortality and morbidity experience
- fluctuation in expense experience
- AIDS risk
- risk of asset liability mismatches
- risk of worse than expected investment returns
- operational risk
- credit risk

Discovery Life regularly reviews the capital position and also considers various new business scenarios. Typically a five-year new business projection horizon is allowed for and the capital position is assessed at each valuation date during the projection to ensure an acceptable capital cover is maintained.

No management action was allowed for to offset adverse conditions.

At 30 June 2013, the statutory capital adequacy requirement was R455 million and was covered 4.0 times (2012: the statutory capital adequacy requirement was R364 million and was covered 4.4 times).

Liquidity risk

Liquidity risk arises due to a timing mismatch between the assets and liabilities.

Discovery maintains sufficient liquid assets to meet short-term liabilities and to allow for the initial cash flow strain when writing new business.

Currently, Discovery Life's expected outflows are mostly long-term and the main liquidity requirement is to fund acquisition expenses on new business and unexpected fluctuations in benefit payments. As discussed in 3.4.3, Discovery invests primarily in liquid financial assets. There is a need to meet liquidity requirements under the growing Guaranteed Plan book. Liquidity requirements are managed to ensure a liquidity buffer is maintained to meet potential outflows if exit rates are higher than expected. The liquidity risk on the existing portfolio is thus relatively small.

Large sums assured above a defined retention level are reinsured, providing stability in claims experience and further reducing the liquidity risk.

The undiscounted expected statutory cash flows under in-force contracts after policyholder liabilities have been met, net of tax and reinsurance, as at 30 June were as follows:

R million	Year 1	Years 2 to 5	Years 6 to 10	Years 11 to 20	Years 21+
2013					
Discovery Life	**650**	**4 176**	**7 901**	**19 246**	**48 017**
Discovery Invest	**349**	**951**	**1 093**	**2 138**	**1 007**
2012					
Discovery Life	800	3 485	6 762	16 436	42 683
Discovery Invest	257	713	881	1 999	584

Note that the cash flows in the table above differ from those disclosed on page 182, since these are based on best estimate free cash flows after meeting policyholder liabilities. Cash flows arising under investment management contracts are also included. No allowance has been made for new business and related expenses.

Policy wording/legal risks

There is a risk that Discovery could be financially exposed to obligations that are different to expected and not adequately provided for. The risk could also arise from legal proceedings.

The risk is managed when new products are developed and all policy wordings are reviewed by legal advisors and external advice is obtained where necessary to ensure that terms and conditions are clearly defined and unambiguous.

Reputational risk

Reputational risk is the risk of negative market reaction towards Discovery Life. Discovery Life may thus not be able to apply management policies to reduce risk.

Reputational risks are controlled in that all decisions to repudiate claims are reviewed by the Chief Medical Officer and legal advice is obtained where necessary.

Marketing material and policy wordings are reviewed and designed to be clear and unambiguous to avoid creating unreasonable policyholder expectations.

Discovery Life offers policies that integrate with the product offerings within the Discovery Group. The reputational risk to Discovery Life is thus extended to the reputational risk of the entire Discovery Group. Discovery Life management reviews all product offerings to minimise the reputational risk. All products are approved by the statutory actuary prior to launch.

Reputational risk may also arise if Invest Plans experience worse investment returns than competitors. This may lead to lower future new business and higher surrenders. This risk is mitigated through the use of reputable experienced fund managers and unique, innovative products covering specific risks.

Concentration risk

- *Claims experience risk*

  There is a risk that a concentration of risk can lead to worse than expected experience. The concentration risk is the highest in group business, since assured lives live in the same geographical location and generally work in the same industry or at the same location.

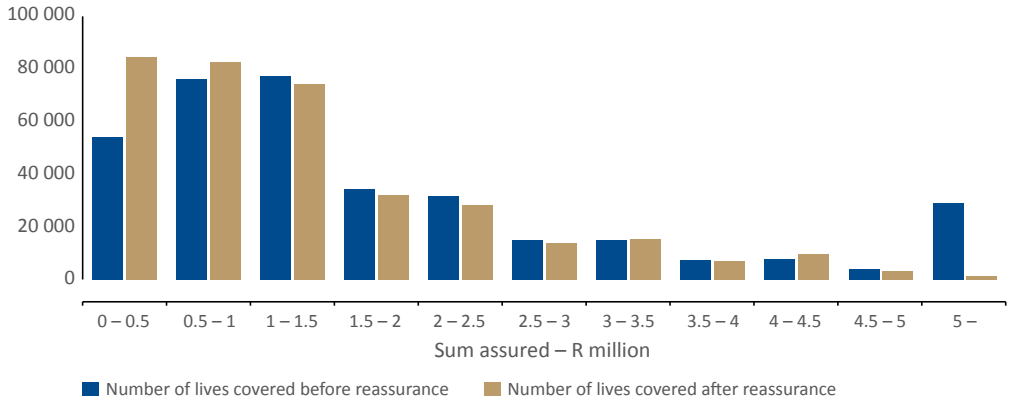
  This risk is mitigated through catastrophe reinsurance.

  Discovery Life maintains a well-diversified portfolio of policies. Reinsurance is further used to protect against the concentration of risk. Catastrophe reinsurance protects against accumulation of claims from a single event, for example an airplane crash. The catastrophe reinsurance covers single event disasters for up to R300 million where the net of reinsurance impact is greater than R30 million.

  Reinsurance removes the exposure to large individual claims. The table below demonstrates that the distribution of policies by sum assured is shifted towards lower sum assured due to the reinsurance cover:

Impact of reassurance on exposure to large claims

Number of lives covered



2. MANAGEMENT OF INSURANCE RISK continued

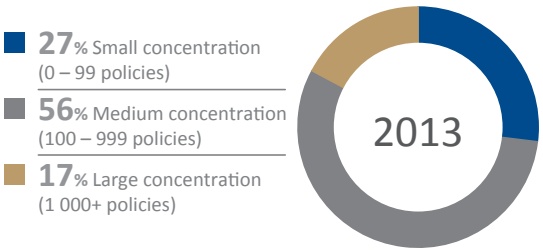
- *Withdrawal concentration risk*
  There is a financial risk of the withdrawal of a block of policies written by a single independent intermediary.

  Discovery Life has a well-diversified book of business by source of new business and spread across more than 7 800 (2012: 7 800) brokers and agents.

  The maximum exposure of Discovery Life to a single intermediary is smaller than 1% and to a group of intermediaries is 2% (2012: 3%) as a percentage of total premium income.

  The distribution of annualised premium income (API) by concentration to an intermediary group is given in the graph below. A large concentration is defined as an intermediary group that has written more than 1 000 Discovery Life policies. A small concentration is defined as an intermediary group that has written less than 100 policies.

API concentration by intermediary



2.1.3 Sensitivity analysis

The financial impact of the key risks that Discovery Life is exposed to, can be demonstrated by considering the sensitivity of the financial results to a hypothetical change in the underlying assumptions or prevailing market conditions.

Although the sensitivities demonstrate the impact of a change in assumption, the results generally cannot be extrapolated to demonstrate the impact on future earnings and earnings forecasts.

For each sensitivity illustrated, all other assumptions have been left unchanged. No allowance has been made for any management action, for example premium increases, to react to the worse than expected experience.

The ranges of sensitivity were chosen for illustration purposes and do not represent the extremes of possible experience.

The sensitivities shown under insurance risks consider a change in the long-term assumption used in the projection model.

The following sensitivities are provided under insurance risk:

- **Lapses:** The lapse, surrender and withdrawal rates are increased or decreased across all policies and investment plans.
- **Renewal expenses:** Renewal expense per policy is increased or decreased across all policies and investment plans.
- **Mortality and morbidity:** The mortality rate, disability rate and severe illness rates are increased and decreased across all policies and investment plans.
- **Long-term investment return and inflation:** A parallel shift is assumed in the yield curve. The investment return, inflation, renewal expense inflation and inflation-linked premium increases are adjusted consistently.

Assets under insurance contracts in the statement of financial position include assets for both Discovery Life and PruProtect. The total assets under insurance contracts less reinsurance recoveries are R13 534 million (2012: R10 838 million) (refer note 5). R3 510 million (2012: R1 892 million) of this relates to PruProtect. The sensitivities in the table below relate to Discovery Life.

	Assets under insurance contracts R million	Change from base assumption %
Base: June 2013 assumptions	**10 024**	
Lapses +10% (eg. From x% to 1.1x%)	**8 698**	**(13.2)**
Lapses -10% (eg. From x% to 0.9x%)	**11 637**	**16.1**
Investment return and inflation -1% (eg. From 5% to 4%)	**11 528**	**15.0**
Investment return and inflation +1% (eg. From 5% to 6%)	**8 759**	**(12.6)**
Expense assumption +10%	**9 820**	**(2.0)**
Expense assumption -10%	**10 228**	**2.0**
Mortality and morbidity +10%	**7 802**	**(22.2)**
Mortality and morbidity -10%	**12 331**	**23.0**
Base: June 2012 assumptions	8 946	
Lapses +10% (eg. From x% to 1.1x%)	7 991	(10.7)
Lapses -10% (eg. From x% to 0.9x%)	10 076	12.6
Investment return and inflation -1% (eg. From 5% to 4%)	10 187	13.9
Investment return and inflation +1% (eg. From 5% to 6%)	7 894	(11.8)
Expense assumption +10%	8 771	(2.0)
Expense assumption -10%	9 122	2.0
Mortality and morbidity +10%	7 025	(21.5)
Mortality and morbidity -10%	10 949	22.4

Liabilities arising from insurance contracts consist of outstanding reported claims, IBNR claims and long-term liabilities relating to fixed and guaranteed contracts and unit-linked contracts. For outstanding reported claims and IBNR claims any deviation from the best estimate liabilities would have a direct impact on profit.

2. MANAGEMENT OF INSURANCE RISK continued

For long-term insurance liabilities relating to fixed and guaranteed contracts and unit-linked contracts (refer to reconciliation on page 182), the sensitivities are detailed in the table below:

	Liabilities under insurance contracts R million	Change from base assumption %
Base: June 2013 assumptions	**4 286**	
Lapses +10% (eg. From x% to 1.1x%)	**4 309**	**0.5**
Lapses -10% (eg. From x% to 0.9x%)	**4 261**	**(0.6)**
Investment return and inflation -1% (eg. From 5% to 4%)	**4 456**	**4.0**
Investment return and inflation +1% (eg. From 5% to 6%)	**4 125**	**(3.8)**
Expense assumption +10%	**4 300**	**0.3**
Expense assumption -10%	**4 272**	**(0.3)**
Mortality and morbidity +10%	**4 296**	**0.2**
Mortality and morbidity -10%	**4 277**	**(0.2)**
Base: June 2012 assumptions	3 644	
Lapses +10% (eg. From x% to 1.1x%)	3 664	0.6
Lapses -10% (eg. From x% to 0.9x%)	3 621	(0.6)
Investment return and inflation -1% (eg. From 5% to 4%)	3 805	4.4
Investment return and inflation +1% (eg. From 5% to 6%)	3 491	(4.2)
Expense assumption +10%	3 658	0.4
Expense assumption -10%	3 629	(0.4)
Mortality and morbidity +10%	3 651	0.2
Mortality and morbidity -10%	3 636	(0.2)

2.2 Discovery Insure

2.2.1 Product description

The policies underwritten by Discovery Insure are as follows:

Motor

Provides cover for loss, damage and liabilities arising from the use or ownership of motor vehicles. The cover includes comprehensive, third party, fire, theft and third party liability cover.

Property

Provides cover for loss or damage from specified events – such as fire, storm, theft etc. – to movable and immovable property belonging to the insured.

Liability

Provides cover for risks relating to the insured incurring personal liability to specified third parties which are not specifically covered under another insurance contract.

At 30 June 2013, 71% (2012: 79%) of the new business API related to motor policies and 29% (2012: 21%) to property policies.

2.2.2 Insurance risks

Discovery Insure covers clients for various short-term insurance risks. Such risks include the perils around property, motor and liability. The principal risk is that the frequency and/or severity of claims are greater than expected. Insurance events are, by their nature, random and the actual number and size of events during any one year may vary from those estimated and experienced in prior periods.

Discovery Insure manages its insurance risk through its reinsurance programme which is structured to protect the company against material losses to either a single insured risk, or group of insured risks in the case of a catastrophe where there would tend to be a concentration of insured risks.

The underwriting of insurance risk and the passing on of excessive insurance risk is further described below.

Underwriting strategy

Discovery Insure aims to manage risk through diversifying the pool of insured risks by establishing a balanced portfolio of insurance risks over a wide geographical area. Short-term insurance risks are priced on an individual basis, therefore a minimal cross subsidy between risks exist.

Premiums are calculated using statistical regression techniques. Insurance risk factors identified would typically include the past insurance history, type and value of asset covered, measures taken to protect the asset, primary use of covered item and various other pertinent factors.

Discovery Insure's quotation and administration system calculates risk on an individual basis based on information captured by brokers and agents for each risk. Individual risks are accepted automatically up to cut-off limits which vary by risk type. Insurance conditions and exclusions are also automatically set at an individual risk level.

Individual risks greater than the limit are automatically referred and underwritten by the underwriting department. No risks are accepted which exceed the upper limits of the reinsurance contracts without the necessary facultative cover being arranged.

Reinsurance strategy

Discovery Insure reinsures a portion of the risk it underwrites to protect the profitability and the capital of the company. A variety of treaties are assumed in order to limit losses resulting from individual and collective insurance risks. Additional facultative reinsurance is purchased for certain individual risks that are in excess of the relevant treaty limits. Discovery Insure only enters into reinsurance arrangements with reinsurers that have adequate credit ratings.

Concentrations of risk

There is a risk that a concentration of risk can lead to worse than expected claims experience. Discovery Insure is exposed to a concentration of insurance risk in the Gauteng province of South Africa where 62% (2012: 66%) of the company's total sum insured is domiciled. In order to manage this concentration of insurance risk, the company has entered into a catastrophe excess of loss reinsurance treaty that would limit the loss of the company to pre-determined levels following the occurrence of a localised catastrophe in this area.

2.3 PruHealth

2.3.1 Product description

PruHealth offers three main product types:

Individual product

This is offered to the retail market either direct or via a broker. The product features include:

- **Private Medical Insurance:** Cover is offered for a range of private healthcare-related claims. The cover is dependent on the plan type chosen and includes hospital and outpatient cover for selected conditions.
- **Starter discounts:** Discounts are available based on answers to healthcare questions.
- **Renewal discounts:** Discounts are offered at renewal depending on claims and Vitality status.
- **Vitality rewards:** A full Vitality package is offered, including gym offering and healthcare-related rewards.

SME product

This is an age-rated product offered to small groups (2–100) either direct or via a broker. The product features include:

- **Private Medical Insurance:** Cover is offered for a range of private healthcare-related claims. The cover is dependent on the plan type chosen and includes hospital and outpatient cover for selected conditions.
- **Renewal discounts for employers:** Discounts are offered at renewal depending on loss ratio.
- **Cashback:** Employees may be eligible for cash bonuses depending on the amount claimed during the period and their Vitality status and depending on the PruHealth cover selected by their employer.
- **Vitality rewards:** A full Vitality package is offered, including gym offering and healthcare-related rewards.

Corporate product

This is a product offered by brokers and employee benefit consultants. The product features include:

- **Private Medical Insurance:** Cover is offered for a range of private healthcare-related claims. The cover is dependent on the plan type chosen and includes hospital and outpatient cover for selected conditions.
- **Cashback:** Companies can select their desired level of cashback with PruHealth. If selected, employees are eligible for cash bonuses depending on the amount claimed during the period and their Vitality status.
- **Vitality rewards:** A full Vitality package is offered, including gym offering and healthcare-related rewards.

At 30 June 2013, there were 553 388 PruHealth members with an annualised premium income of GBP 354.8 million (30 June 2012: 554 430 PruHealth members with an annualised premium income of GBP 332.2 million).

2. MANAGEMENT OF INSURANCE RISK continued

2.3.2 Insurance risks

PruHealth takes a proactive approach to managing its risk and each business unit responsible for the risk groupings identified below have initiated a series of risk management processes to ensure that they are adequately controlled.

The key areas of risk are premium pricing, claims volatility and failing to meet target levels of business. Monthly meetings are held to review recent actual experience against that expected in the financial forecast for sales and lapse rates and all revenue items including premium income and claims incurred. The standard terms and conditions applicable to the company's products mitigate the risk of late reporting of claims. Recent claims experience is monitored against expected to ensure that PruHealth's current pricing assumptions are reasonable and formal pricing reviews are conducted by the Actuarial and Pricing department at least twice each year. On an annual basis, the financial forecast is fully reviewed taking into account both emerging actual experience and anticipated future experience. PruHealth measures profitability and solvency using a financial model of the business that projects in-force and expected new business cash flows.

Excess of loss reinsurance is utilised to mitigate the risk of undue concentrations of insurance risk. Due to the short tail nature of the company's risks all claims are expected to be settled within 12 months of reporting and accordingly, the company has not presented a comparison of actual claims compared with previous estimates. Loss development tables are not provided since all claims are typically settled within a year of the claim arising.

PruHealth currently has quota share agreements in place with three reinsurers with an outstanding balance of GBP 27 million at year end.

Capital adequacy requirements and protection against adverse experience

PruHealth maintains shareholder capital to meet substantial deviations in experience.

At 30 June 2013, the statutory capital adequacy requirement was GBP 74 million (2012: GBP 74 million). PruHealth currently holds capital resources that are 40% in excess of the highest level of capital resources requirement.

2.3.3 IBNR calculation

PruHealth adopts two reserving methodologies. Firstly, the 'chain ladder' approach which assumes that there is stability in the delays from treatment date to payment date and therefore future payments can be estimated using historical experience. Secondly, an 'independent measure' approach applied to the most recent treatment months, which assumes that the total costs arising from each month of treatment can be estimated independent of any payments already made. The Reserving Committee considers both of these independent measures when setting the actual reserves.

The IBNR is GBP 34 million at 30 June 2013 (2012: GBP 31 million), which approximates one and a half month's worth of claims. This is the expected delay in claims reporting estimate by the two approaches discussed above.

2.4 PruProtect

2.4.1 Product description

PruProtect plan overview

The PruProtect plan is a lifestyle protection plan which allows customers to select from a menu of benefits which includes:

- life cover
- serious illness cover
- capital disability cover
- income protection insurance
- family income cover
- education cover
- health cover
- waiver of premium on death, serious illness and/or incapacity
- additional optional serious illness cover for children

Structure

The PruProtect plan has at its basis a Plan Account. The Plan Account defines the amount paid out under any benefit that is attached to it. The benefits that are attached to the Plan Account are expressed as a percentage of the Plan Account's value.

The Plan Account can be structured to provide cover that is level, increasing or decreasing.

The PruProtect plan can be written on a single or joint life basis and cover may be stand-alone or limited to the Plan Account whereby claims would accelerate payment of the Plan Account. Premiums are payable monthly in advance and can be guaranteed or reviewable. Premiums can either be level, increase at a fixed rate or increase at a rate related to Retail Price Index in the UK. The plan doesn't offer any surrender value.

The PruProtect plan provides extensive severity-based cover for serious illness.

At 30 June 2013, there were 153 671 PruProtect policies with an annualised premium income of GBP 101.0 million (30 June 2012: 109 933 PruProtect policies with an annualised premium income of GBP 68.9 million).

2.4.2 Insurance risks

PruProtect takes a proactive approach to managing its risk. Risk management processes are employed to ensure business units identify and control the risks to which they are exposed. Discovery has a 75% interest in PruProtect, with Prudential Assurance Company Limited (PAC) holding the balance of 25%. Innovation is a strong focus of PruProtect and is driven by the combined experience of PAC and Discovery. PruProtect benefits from internal as well as the government structures of PAC and Discovery.

The key insurance risks of the business are driven by the mortality and morbidity of PruProtect policyholders. Claims experience and price competitiveness are reviewed at each monthly Management Committee. Experience analysis motivates changes to the assumptions used in the actuarial model. The same model is used for valuation and forecasting.

The life, serious illness, disability and income protection benefits of the PruProtect product are reinsured with a maximum retention of 50%. The unemployment benefit offered as part of the PruProtect product is fully reinsured.

Market and mismatching risk

The insurance-related cash outflows (eg. benefit payments, administration expenses, etc.) have been matched predominantly with future premiums. The valuation discount rate is set with reference to the prevailing risk-free gilt yield. The value of assets under insurance contracts is subject to interest rate risk. There is thus a risk that a change in the risk-free gilt yield could cause a change in the value of the assets under insurance contracts. PruProtect has no investment or embedded derivative type products.

Lapse risk

Policyholders have the option to discontinue or reduce contributions at any time.

There is a risk of financial loss due to the withdrawal rate being higher than expected. The risk is highest during the early duration of the policy since the acquisition costs and commission incurred at the inception of the policy will not yet have been recouped.

There is also a risk of lower than expected withdrawals at late durations of the policy since no surrender value is payable on withdrawal from a risk policy even where actuarial reserves are positive.

There is a further risk that withdrawals are selective from a claims experience point of view. For example, healthy lives may find it easier to obtain cover elsewhere compared to less healthy lives.

Future earnings are dependent on the number of policies remaining in future years and thus future earnings are dependent on the lapse rate. The future expected earnings vary by the premium funding method chosen by the policyholder. In general, the higher the increases, the higher the withdrawal risk to future earnings.

The lapse risk is managed as follows:

- *Product design*
  Products are designed to be sustainable in the long-term. New product offerings are made available to existing policyholders as far as possible to prevent lapse and re-entry risk.

  Vitality provides unique rewards and benefits to policyholders which have proven to be a credible risk differentiator. Premium discounts are available to policyholders who actively engage in a healthier lifestyle and utilise the Vitality benefit. Better terms are thus offered to healthy lives compared to less healthy lives.

  No surrender benefit is offered on risk benefits and thus the loss on withdrawal is reduced.

- *Commission clawback*
  PruProtect predominantly distributes via independent intermediaries.

  Commissions are clawed back from intermediaries where a policy lapses early on. The clawback period is currently either two or four years. The amount of commission clawback depends on the amount of unearned commission over the period. There is a credit risk associated with clawing back commission from brokers.

- *Client relationships*
  All premiums are collected via debit order. Clients are contacted after a failed debit order and after notification of a cancellation. The reason for the cancellation is established and wherever possible the policy is conserved.

- *Experience monitoring*
  Lapse experience is monitored on a monthly basis and analysed to establish possible trends for which management action can be taken. Data is currently not sufficient to provide credible results, so significant reliance is placed on reinsurers' advice as well as experience from Discovery Life and PAC.

2. MANAGEMENT OF INSURANCE RISK continued

Underwriting experience risk

There is a risk that actual mortality and morbidity experience is higher than expected. This could arise as a result of the number of claims or the value of claims being higher than expected.

Selection is the risk that worse risks than expected are attracted and these risks are then charged inadequate premiums. Selection could also lead to higher than expected mortality and morbidity experience.

There is a risk that the emergence of a new disease or epidemic can increase the number of claims.

The risks are managed through:

- *Product design and pricing*
  Products are carefully designed to minimise adverse selection. Rating factors are applied to standard premium rates to differentiate between different levels of risk. For example, premiums are differentiated by income, education level, smoker status, gender (prior to 2013), medical history and age. From January 2013 onwards, no differentiation of premiums or benefits on the basis of gender is allowed in the UK.

  For certain of the product-options offered, PruProtect has retained the option to review premium rates annually throughout the life of the contract because of uncertainties underlying the value of the benefits offered.

- *Underwriting*
  Underwriting ensures that only insurable risks are accepted and that premiums reflect the unique circumstances of each risk. This is achieved by different levels of medical underwriting, depending on the answers to medical questions on the application form. Financial underwriting is applied to ensure that the policyholder can justify the amount of cover applied for. Premium loadings and exclusions are applied where high risks are identified.

  Quality assurance audits are performed on underwriting to minimise the risk of incorrect underwriting decisions.

- *Reinsurance*
  Reinsurance protects against volatility in claims experience and against an accumulation of risk. In addition, reinsurers provide specialist advice when designing new products.

- *Experience monitoring*
  Experience is monitored on a monthly basis and analysed to establish possible trends for which management action can be taken. Data is currently not sufficient to provide credible results, so significant reliance is placed on reinsurers' advice as well as experience from Discovery Life and PAC.

Expenses

Expense risk is the risk of actual expenses being higher than expected. Expenses could exceed expectations due to an increase in the expense inflation or due to a reduction in the number of in-force policies. Expenses are monitored on a monthly basis against budgeted expenses. Any deviation from the budget is investigated, reported and where necessary, remedial action is taken.

Modelling and data risk

The actuarial liabilities are calculated using complex discounted cash flow models. There is thus a risk that the model doesn't accurately project the policy cash flows in the future.

The risk is controlled using specialist actuarial software that is widely used and accepted in the life insurance industry throughout the world.

Any changes made to the model are reviewed.

The model relies on data from the administration system and there is thus a further risk that the data does not accurately reflect the policies being valued.

The data is extracted from modern administration systems and subjected to detailed checks together with high-level reasonability checks. PruProtect does not have any legacy systems that could impact on the data quality.

Operational/Implementation risk

Segregation of duties ensures multiple checks on process and further protects against the risk of fraud.

PruProtect does not have any legacy systems and processes to deal with thereby reducing operational risk.

Regulatory risk

PruProtect operates in a highly regulated environment. The regulatory risk can be defined as the potential detrimental impact of unexpected changes in regulations (or interpretation thereof).

Although PruProtect endeavours to design insurance and financial solutions which meet the requirements of the current regulations in force, the risk does exist that changes in the regulations, or the interpretation of the regulations, over time may result in the current products not fully complying with the regulations in force in future. This risk is managed through constantly seeking legal advice on new product developments. Further, all insurance products issued by PruProtect are subject to a rigorous sign-off process.

Tax risk

Tax risk is the risk that the actual future tax liability is different to what is currently expected. This could be as a result of an incorrect interpretation or application of tax legislation or as a result of changes to taxation legislation. Tax relief on expenses will not apply to protection business sold from January 2013 onwards.

External tax advice is obtained as required to ensure that products are structured in a tax efficient way.

Currency risk

All of PruProtect's insurance benefits are Sterling denominated as all business is sold in the UK market.

A significant part of operational expenses are Rand denominated as systems and administration are based in South Africa. This creates a potential mismatching risk.

Results are published in Rands in Discovery's annual financial statements creating movement in the values due to currency fluctuations.

Solvency capital requirements and protection against adverse experience

There is a risk that future premiums, investment returns and estimates used to calculate liabilities are insufficient to provide for variations in actual future experience. Margins are allowed for in the calculation of all insurance liabilities.

The Financial Services Authority (FSA) was replaced by two distinct regulators in 2013 namely the Prudential Regulation Authority (PRA) and the Finance Conduct Authority (FCA). The PRA is a part of the Bank of England and responsible for the prudential regulation and supervision of insurers. It sets standards and supervises financial institutions. The FCA regulates the financial services industry in the UK. Their aim is to protect consumers, ensure the industry remains stable and promote healthy competition between financial services providers. The Prudential Sourcebook for Insurers (INSPRU) contains standards for capital management.

Capital requirements are calculated based on the concept of two pillars:

- Pillar 1, which covers public solvency information that appears within the regulatory returns on the basis of prescriptive rules. This includes the statutory valuation of liabilities together with a prescribed measure of additional capital, the Long-Term Insurance Capital Requirement (LTICR).
- Pillar 2, the Individual Capital Assessment (ICA), which covers a confidential company-specific assessment of solvency. This assessment is done on a realistic basis with the aim to protect against risks up to the 99.5 percentile over a one-year period.

The LTICR is a minimum required margin for solvency on the statutory valuation basis and covers the following basic risks:

- death risk
- expense risk
- market risk
- health risk

The ICA is a risk-based capital measure and covers the major areas of insurance risk. It explicitly covers the following areas of risk:

- lapse and withdrawal risk
- fluctuations in mortality and morbidity experience, including catastrophe risk
- expense risk
- mis-selling risk
- credit and default risk
- risk of worse than expected investment returns
- operational risk
- exchange rate risk
- tax risk

The amount of capital that ultimately needs to be held by a life insurance company in the UK is the larger of the Pillar 1 and Pillar 2 results.

Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with insurance liabilities due to insufficient cash being available to meet commitments as and when they become due. Liquidity risk arises due to a timing mismatch between the assets and liabilities.

PruProtect maintains sufficient liquid assets to meet short-term liabilities and to allow for the initial cash flow strain when writing new business.

Currently, PruProtect's expected liabilities are mostly long-term and the main liquidity requirement is to fund acquisition expenses on new business. The liquidity risk on the existing portfolio is thus relatively small.

2. MANAGEMENT OF INSURANCE RISK continued

Policy wording/legal risks

There is a risk that PruProtect could be financially exposed to obligations that are different to expected and not adequately provided for. The risk could also arise from legal proceedings or complaints by policyholders.

The risk is managed when new products are developed and all policy wordings are reviewed by legal advisors and external advice is obtained where necessary to ensure that terms and conditions are clearly defined and unambiguous.

Reputational risk

Reputational risk is the risk of negative market reaction towards PruProtect. PruProtect may thus not be able to apply management policies to reduce risk.

Marketing material and policy wordings are reviewed and designed to be clear and unambiguous to avoid creating unreasonable policyholder expectations and are subject to a rigorous sign-off process.

PruProtect management reviews all product offerings to minimise the reputational risk.

Concentration risk

- *Claims experience risk*
  There is a risk that a concentration of risk can lead to worse than expected experience. PruProtect maintains a well-diversified portfolio of policies. Reinsurance is further used to protect against the concentration of risk. Reinsurance removes the exposure to large individual claims.
- *Withdrawal concentration risk*
  There is a financial risk of the withdrawal of a block of policies written by a single independent intermediary. PruProtect has a well-diversified book of business by source of new business and spread across more than 12 000 (2012: 6 000) brokers and agents. The maximum exposure of PruProtect to a single intermediary is smaller than 3.5% (2012: 2.6%) in annualised premium income.

3. MANAGEMENT OF FINANCIAL RISK

Discovery's activities expose it to a variety of financial risks. Financial risks include market risk, credit risk and liquidity risk.

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices and investment return. Market risk that could impact on future cash flows and hence the value of a financial instrument arises from:

- *Equity price risk:* The impact of changes in equity prices and dividend income.
- *Interest rate risk:* The impact of changes in market interest rates.
- *Currency risk:* The impact of changes in foreign exchange rates.

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

Liquidity risk is the risk that Discovery will encounter difficulty in meeting obligations associated with financial liabilities due to insufficient cash being available to meet commitments as and when they become due.

Financial risks are managed by Discovery as follows:

- Discovery has appointed reputable external asset managers to manage its investments.
- The Actuarial Committee reviews the overall matching of shareholder and policyholder assets to their respective liabilities.
- The Capital, Currency, Investment Committee (CCIC) is a sub-committee of the Executive Committee and meets quarterly to focus on shareholder assets and the performance of asset managers responsible for managing these assets. The CCIC also sets exposure limits for exposures to individual counterparties.
- Discovery periodically engages external consultants to review past investment decisions.
- The Investment Committee is a sub-committee of the CCIC and meets monthly to make practical decisions regarding Discovery's liquidity and foreign currency exposure.

Discovery has not significantly changed the processes used to manage its risks from previous periods.

To assist in the analysis of the financial risks that Discovery is exposed to, the statement of financial position has been divided into the following categories:

- unit-linked investment contracts
- unit-linked insurance contracts
- other insurance contracts
- shareholder financial assets and liabilities
- shareholder non-financial assets and liabilities

The table on page 178 lists the contracts that Discovery offers and the category they are included in for financial risk disclosures.

The following tables reconcile the Group statement of financial position to the classes of risks and the categories listed on the previous page:

At 30 June 2013					Shareholder	
R million	Total	Unit-linked investment contracts	Unit-linked insurance contracts	Insurance contracts	Financial assets and liabilities	Other assets and liabilities
Assets arising from insurance contracts	14 407	–	(2 883)	17 290	–	–
Financial instruments at fair value through profit or loss:						
Listed:						
– Equity securities	13 998	4 315	9 646	37	–	–
– Equity linked notes	502	84	418	–	–	–
– Debt securities	4 533	375	1 224	2 934	–	–
– Inflation linked securities	185	33	48	104	–	–
– Money market securities	896	138	758	–	–	–
Unlisted:						
– Equity securities	9	3	6	–	–	–
– Debt securities	14	12	2	–	–	–
– Money market securities	2 753	857	1 703	193	–	–
Available-for-sale financial instruments:						
Listed:						
– Equity securities	951	–	–	–	951	–
– Equity linked notes	13	–	–	–	13	–
– Debt securities	506	–	–	–	506	–
– Inflation linked securities	46	–	–	–	46	–
– Money market securities	3 665	–	–	–	3 665	–
Unlisted:						
– Debt securities	135	–	–	–	135	–
– Money market securities	1 395	–	–	–	1 395	–
Derivative financial instruments at fair value:						
– Hedges	536	–	–	–	536	–
– Non-hedges	5	–	–	–	5	–
Loans and receivables:						
– Insurance receivables	1 038	–	–	–	1 038	–
– Other	2 023	226	478	2	1 317	–
Reinsurance contracts	237	–	–	237	–	–
Cash and cash equivalents	2 062	144	203	–	1 715	–
Other assets	5 024	–	–	–	–	5 024
Total assets	54 933	6 187	11 603	20 797	11 322	5 024
Liabilities arising from insurance contracts	19 086	–	9 575	9 511	–	–
Liabilities arising from reinsurance contracts	1 508	–	–	1 508	–	–
Puttable non-controlling interests	3 782	–	–	–	3 782	–
Negative reserve funding	2 813	–	–	–	2 813	–
Borrowings at amortised cost	660	82	132	1	445	–
Investment contracts at fair value through profit or loss	6 049	6 049	–	–	–	–
Derivative financial instruments at fair value:						
– Hedges	10	–	–	–	10	–
– Non-hedges	18	1	–	–	17	–
Trade and other payables	3 179	55	88	–	3 036	–
Other liabilities	4 120	–	–	–	–	4 120
Total liabilities	41 225	6 187	9 795	11 020	10 103	4 120

In the statement of financial position, investments in unit trusts are allocated to the security in which the unit trust is predominantly invested. In the table above, the look-through basis has been applied to the unit trust balances to assist in the identification of Discovery's financial risks.

3. MANAGEMENT OF FINANCIAL RISK continued

At 30 June 2012 R million	Total	Unit-linked investment contracts	Unit-linked insurance contracts	Insurance contracts	Shareholder: Financial assets and liabilities	Shareholder: Other assets and liabilities
Assets arising from insurance contracts	11 681	–	(1 947)	13 628	–	–
Financial instruments at fair value through profit or loss:						
Listed:						
– Equity securities	7 242	1 063	6 169	10	–	–
– Equity linked notes	460	225	224	11	–	–
– Debt securities	3 106	289	739	2 078	–	–
– Inflation linked securities	285	71	64	150	–	–
– Money market securities	2 279	410	1 867	2	–	–
Unlisted:						
– Equity securities	455	213	240	2	–	–
– Debt securities	8	8	–	–	–	–
– Money market securities	1 197	499	487	211	–	–
Available-for-sale financial instruments:						
Listed:						
– Equity securities	691	–	–	–	691	–
– Equity linked notes	1	–	–	–	1	–
– Debt securities	327	–	–	–	327	–
– Inflation linked securities	67	–	–	–	67	–
– Money market securities	2 222	–	–	–	2 222	–
Unlisted:						
– Equity securities	53	–	–	–	53	–
– Debt securities	8	–	–	–	8	–
– Money market securities	1 996	–	–	–	1 996	–
Derivative financial instruments at fair value:						
– Hedges	141	–	–	–	141	–
– Non-hedges	8	–	–	–	8	–
Loans and receivables:						
– Insurance receivables	861	–	–	–	861	–
– Other	1 336	16	20	–	1 300	–
Reinsurance contracts	201	–	–	201	–	–
Cash and cash equivalents	1 929	135	139	1	1 654	–
Other assets	4 108	–	–	–	–	4 108
Total assets	40 662	2 929	8 002	16 294	9 329	4 108
Liabilities arising from insurance contracts	14 319	–	6 593	7 726	–	–
Liabilities arising from reinsurance contracts	1 457	–	–	1 457	–	–
Puttable non-controlling interests	2 893	–	–	–	2 893	–
Negative reserve funding	1 264	–	–	–	1 264	–
Borrowings at amortised cost	402	–	–	–	402	–
Investment contracts at fair value through profit or loss	2 915	2 915	–	–	–	–
Derivative financial instruments at fair value:						
– Hedges	20	–	–	–	20	–
– Non-hedges	15	2	–	–	13	–
Trade and other payables	2 268	12	13	–	2 243	–
Other liabilities	3 378	–	–	–	–	3 378
Total liabilities	28 931	2 929	6 606	9 183	6 835	3 378

The financial risks associated with each category are discussed below.

3.1 Unit-linked investment contracts

Unit-linked investment contracts relate to contracts where there is a direct relationship between the returns earned on the underlying portfolio and the returns credited to the contract. The market risk (including equity price, interest rate and currency risk) for these contacts is therefore borne by the policyholder. Discovery holds the assets on which the unit prices are based and as a result, there is no mismatch.

	Investments held at risk of investment policyholders	
R million	**June 2013**	June 2012
Financial assets at fair value through profit or loss:		
Listed:		
– Equity securities	**4 315**	1 063
– Equity linked notes	**84**	225
– Debt securities	**375**	289
– Inflation linked securities	**33**	71
– Money market securities	**138**	410
Unlisted:		
– Equity securities	**3**	213
– Debt securities	**12**	8
– Money market securities	**857**	499
Loans and receivables	**226**	16
Cash and cash equivalents	**144**	135
Total assets	**6 187**	2 929
Total policyholder liabilities	**6 187**	2 929

3.1.1 Market risk

Discovery's primary exposure to market risk from these contracts is the volatility in asset management fees due to the impact of interest rate, equity price and currency movements on the fair value of the assets held in the linked funds, on which the investment management fees are based. A decrease of 10% in the value of the assets would reduce the asset management fees by R13 million per annum (2012: R10 million).

In respect of IFRS-defined investment management contracts there may be an associated deferred acquisition cost intangible asset. There is a risk that in the event of adverse market movements, future expected management fees may reduce and consequently this asset may not be realised and therefore necessitate impairment.

3.1.2 Credit risk

To manage the credit risk, Discovery has appointed reputable external asset managers to manage these investments.

3.1.3 Liquidity risk

Certain contracts can be surrendered before maturity for a cash surrender value specified in the contractual terms and conditions. This surrender value is equal to or less than the carrying amount of the contract liabilities. If all the contracts with this option were surrendered at the financial year-end a loss of R165 million (2012: R113 million) would have been recorded in profit or loss. This loss results from the DAC and DRL relating to these contracts being impaired, but the impact is reduced by the surrender penalties receivable.

A maturity analysis based on the earliest contractual repayment date would present 100% (2012: 100%) of the policyholder liabilities due within one year. The assets held to match these policyholder liabilities are realisable in the short-term.

3. MANAGEMENT OF FINANCIAL RISK continued

3.2 Unit-linked insurance contracts

A unit-linked insurance contract is an IFRS-defined insurance contract with a component that is linked to the units of an underlying portfolio. For this component, Discovery holds the assets on which the unit prices are based. However, the gross unit liabilities are reduced by the present value of future charges less the present value of future expenses and risk claims. Some market risk is therefore retained on these contracts. The unit-linked component is not accounted for separately from the host insurance contract.

	Investments held at risk of insurance policyholders	
R million	**June 2013**	June 2012
Assets arising from insurance contracts	**(2 883)**	(1 947)
Financial assets at fair value through profit or loss:		
Listed:		
– Equity securities	**9 646**	6 169
– Equity linked notes	**418**	224
– Debt securities	**1 224**	739
– Inflation linked securities	**48**	64
– Money market securities	**758**	1 867
Unlisted:		
– Equity securities	**6**	240
– Debt securities	**2**	–
– Money market securities	**1 703**	487
Loans and receivables	**478**	20
Cash and cash equivalents	**203**	139
Total assets	**11 603**	8 002
Total policyholder liabilities	**9 795**	6 606

3.2.1 Market risk

Discovery's primary exposure to market risk from these contracts is the volatility in asset management fees due to the impact of interest rate, equity price and currency movements on the fair value of the assets held in the linked funds, on which the investment management fees are based. A decrease of 10% in the value of the assets would reduce the asset management fees by R31 million per annum (2012: R21 million).

The insurance liability of R2 883 million (2012: R1 947 million) is included in the sensitivity analysis presented on page 189 in respect of assets arising from insurance contracts.

3.2.2 Credit risk

To manage the credit risk, Discovery has appointed reputable external asset managers to manage these investments.

3.2.3 Liquidity risk

A maturity analysis based on the earliest contractual repayment date would present R10 829 million (2012: R6 351 million) of the liabilities as due on the earliest period of the table (between 0 and one year) and R457 million (2012: R255 million) of the liabilities would be due between one and five years. The assets held to match these policyholder liabilities are 100% liquid.

All contracts can be surrendered before maturity for a cash surrender value specified in the contractual terms and conditions. This surrender value is equal to or less than the carrying amount of the contract liabilities. If all the contracts with this option were surrendered at the financial year-end a loss of R1 336 million (2012: R1 007 million) would have been recorded in profit or loss. This loss results from the impairment of assets arising from insurance contracts relating to these contracts, but the impact is reduced by the surrender penalties receivable.

3.3 Insurance contracts

For insurance contracts, Discovery funds the insurance liabilities with a portfolio of matching assets.

R million	June 2013	June 2012
Assets arising from insurance contracts	**17 290**	13 628
Financial assets at fair value through profit or loss:		
Listed:		
– Equity securities	**37**	10
– Equity linked notes	**–**	11
– Debt securities	**2 934**	2 078
– Inflation linked securities	**104**	150
– Money market securities	**–**	2
Unlisted:		
– Equity securities	**–**	2
– Money market securities	**193**	211
Loans and receivables	**2**	–
Reinsurance contracts	**237**	201
Cash and cash equivalents	**–**	1
Total assets	**20 797**	16 294
Total policyholder liabilities	**11 020**	9 183

3.3.1 Market risk

When calculating the liabilities arising from insurance contracts, an increase/decrease in the investments would result in an increase/decrease in the liability but it may not be an equal Rand value movement, resulting in the difference being accrued to the shareholders.

Based on guidance from SAP 104, these movements are captured in the resilience Capital Adequacy Requirement (CAR) and an amount of R74.3 million is included in the CAR at 30 June 2013 (2012: R39.6 million) to protect against potential mismatches between assets and liabilities.

3.3.2 Credit risk

Discovery is exposed to credit risk from the financial investments comprising money market and debt instruments entered to match policyholders' insurance contract liabilities. Discovery is exposed to the issuer's credit standing on these instruments which is monitored by the CCIC by setting a minimum credit rating. Regulations in the various jurisdictions in which Discovery operates have the effect of limiting exposure to individual issuers due to the inadmissibility of assets if specified limits are breached. Discovery has appointed reputable asset managers to manage these instruments. Information regarding the aggregated credit risk exposure for debt and money market instruments categorised by credit ratings is provided below.

R million	Total	AAA	AA+ AA AA–	A+ A A–	Govt	Not rated
At 30 June 2013						
Financial assets at fair value through profit or loss:						
– Debt securities	**2 934**	**101**	**453**	**5**	**2 375**	**–**
– Inflation linked securities	**104**	**–**	**–**	**–**	**104**	**–**
– Money market securities	**193**	**56**	**129**	**1**	**–**	**7**
	3 231	**157**	**582**	**6**	**2 479**	**7**
At 30 June 2012						
Financial assets at fair value through profit or loss:						
– Debt securities	2 077	111	398	4	1 564	–
– Inflation linked securities	150	75	–	75	–	–
– Money market securities	213	58	155	–	–	–
Cash and cash equivalents	1	–	1	–	–	–
	2 441	244	554	79	1 564	–

* *Amount is less than R500 000.*

3. MANAGEMENT OF FINANCIAL RISK continued

3.3.3 Liquidity risk

The liquidity risk for assets and liabilities arising from insurance contracts are discussed in insurance risks on page 186.

The financial investments held at fair value through profit or loss are realisable in the short-term.

3.4 Shareholder financial assets and liabilities

The shareholders are exposed to financial risk through the following financial assets and liabilities:

R million	June 2013	June 2012
Available-for-sale financial assets:		
Listed:		
– Equity securities	**951**	691
– Equity linked notes	**13**	1
– Debt securities	**506**	327
– Inflation linked securities	**46**	67
– Money market securities	**3 665**	2 222
Unlisted:		
– Equity securities	**–**	53
– Debt securities	**135**	8
– Money market securities	**1 395**	1 996
Derivative financial instruments at fair value:		
– Hedges	**536**	141
– Non-hedges	**5**	8
Loans and receivables	**2 355**	2 161
Cash and cash equivalents	**1 715**	1 654
Total financial assets	**11 322**	9 329
Puttable non-controlling interests	**3 782**	2 893
Negative reserve funding	**2 813**	1 264
Borrowings at amortised cost	**445**	402
Derivative financial instruments at fair value:		
– Hedges	**10**	20
– Non-hedges	**17**	13
Trade and other payables	**3 036**	2 243
Total financial liabilities	**10 103**	6 835

3.4.1 Market risk

(a) Equity price risk

Investments

Discovery is exposed to equity price risk because of investments held by the Group and classified on the consolidated statement of financial position as available-for-sale. To manage its equity risk arising from investments in equity securities, the Group diversifies its portfolio.

For shareholder investments, a 10% increase in the equity markets would result in a profit of R51 million before tax (2012: R49 million). A 10% decrease in the equity markets would result in a loss of R37 million before tax (2012: R38 million). This impact would be recognised in the statement of comprehensive income. The sensitivity is based on the assumption that the equity markets had increased/decreased by 10% with all other variables held constant.

Hedge derivative instruments

Discovery is also exposed to equity price risk through its cash-settled share incentive scheme, the details of which is described in note 34. To manage this risk, Discovery has purchased various instruments from BBB+ or A– rated South African banks to hedge a portion of its exposure to changes in the Discovery share price.

Phantom share scheme

As at 30 June 2013, approximately 87.7% (2012: 79.1%) of this exposure is hedged. The hedges were designed to be highly effective, where the terms of the hedge or return swaps substantially match that of the phantom share scheme on a per instrument basis. Combinations of return swaps, call and put options were designated on a unit for unit basis to substantially match the terms of the phantom share and call option units.

The cash-settled call options and cash-settled put options held by the Group at 30 June were:

Maturity date	Strike Price	Number of call options	Number of put options
2012			
30 September 2012	26.40 – 27.72	516 956	516 956
2013			
30 September 2014	**54.75**	**1 050 000**	**–**
30 September 2015	**54.75**	**1 000 000**	**–**
30 September 2016	**54.75**	**950 000**	**–**
30 September 2017	**54.75**	**900 000**	**–**

The fair value of the call and put options are repriced at each reporting date and were calculated on a Black-Scholes model using the same assumptions as tabled in note 34.

The return swaps held by the Group at 30 June were:

Maturity date	Strike Price	Number of return swaps
2012		
30 September 2012	34.21 – 38.37	2 264 850
30 June 2013	39.69	1 400 000
30 September 2013	34.33 – 39.21	2 837 662
30 September 2014	35.08 – 39.21	2 022 678
30 September 2015	38.37 – 39.21	1 314 000
30 September 2016	39.21	680 000
2013		
30 September 2013	**34.33 – 39.21**	**2 837 662**
30 September 2014	**35.08 – 79.69**	**2 642 678**
30 September 2015	**38.37 – 79.69**	**1 864 000**
30 September 2016	**39.21 – 79.69**	**1 160 000**
30 September 2017	**39.21 – 79.69**	**410 000**

The fair value of the return swaps are calculated by discounting the future cash flows of the instruments.

Acquisition share scheme

As at 30 June 2013, approximately 68.9% of this exposure is hedged. The hedges were designed to be highly effective, where the terms of the hedge or return swaps substantially match that of the acquisition share scheme on a per instrument basis.

The return swaps held by the Group at 30 June 2013 were:

Maturity date	Strike Price	Number of return swaps
2013		
30 June 2014	**54.76 – 79.69**	**655 000**
30 June 2015	**54.76 – 84.06**	**695 804**
30 June 2016	**59.00 – 84.06**	**520 500**
30 June 2017	**59.00 – 84.06**	**95 000**
30 June 2018	**84.06**	**32 000**

At 30 June 2013, the fair value of the derivative instruments purchased to hedge the phantom and acquisition share schemes, is R521 million (2012: R141 million). A deposit of R132 million and R343 million (refer to note 23) was received from ABSA Bank Limited and Standard Bank of South Africa Limited respectively, during the current year to secure this receivable.

3. MANAGEMENT OF FINANCIAL RISK continued

(b) Interest rate risk

Sensitivity to changes in interest rates is relevant to financial assets or financial liabilities bearing floating interest rates due to the risk that future cash flows will fluctuate. However, sensitivity will also be relevant to fixed-rated financial assets and financial liabilities that are re-measured to fair value.

The table below details the specific interest rate risk that the Group is exposed to:

R million	Carrying amount	Fixed	Floating	Non-interest bearing
At 30 June 2013				
Available-for-sale financial assets:				
– Equity securities	**951**	**–**	**–**	**951**
– Equity linked notes	**13**	**–**	**–**	**13**
– Debt securities	**641**	**211**	**430**	**–**
– Inflation linked securities	**46**	**46**	**–**	**–**
– Money market securities	**5 060**	**1 250**	**3 806**	**4**
Derivative financial instruments at fair value:				
– Hedges	**536**	**377**	**–**	**159**
– Non-hedges	**5**	**4**	**1**	*****
Loans and receivables	**2 355**	**–**	**86**	**2 269**
Cash and cash equivalents	**1 715**	**–**	**1 715**	**–**
Total financial assets	**11 322**	**1 888**	**6 038**	**3 396**
Puttable non-controlling interests	**3 782**	**–**	**3 782**	**–**
Negative reserve funding	**2 813**	**–**	**2 813**	**–**
Borrowings at amortised cost	**445**	**42**	**403**	**–**
Derivative financial instruments at fair value:				
– Hedges	**10**	**10**	**–**	**–**
– Non-hedges	**17**	**–**	**10**	**7**
Trade and other payables	**3 036**	**–**	**475**	**2 561**
Total financial liabilities	**10 103**	**52**	**7 483**	**2 568**
At 30 June 2012				
Available-for-sale financial assets:				
– Equity securities	744	–	15	729
– Equity linked notes	1	–	–	1
– Debt securities	335	198	137	–
– Inflation linked securities	67	49	18	–
– Money market securities	4 218	1 807	2 408	3
Derivative financial instruments at fair value:				
– Hedges	141	128	–	13
– Non-hedges	8	8	–	–
Loans and receivables	2 161	–	224	1 937
Cash and cash equivalents	1 654	–	1 654	–
Total financial assets	9 329	2 190	4 456	2 683
Puttable non-controlling interests	2 893	–	2 893	–
Negative reserve funding	1 264	–	1 264	–
Borrowings at amortised cost	402	–	402	–
Derivative financial instruments at fair value:				
– Hedges	20	20	–	–
– Non-hedges	13	–	13	–
Trade and other payables	2 243	–	–	2 243
Total financial liabilities	6 835	20	4 572	2 243

* *Amount is less than R500 000.*

Investments

For shareholder investments, a 1% increase in the local interest rate would result in a profit of R7 million before tax (2012: R7 million). A 1% decrease in the local interest rate would result in a loss of R7 million before tax (2012: R5 million). This impact would be recognised in profit or loss. The sensitivity is based on the assumption that the interest rate had increased/decreased by 1% with all other variables held constant.

Borrowings at amortised cost and hedge derivative

Discovery has long-term borrowings at a floating rate which exposes Discovery to cash flow interest rate risk. This risk has been managed by using a floating-to-fixed interest rate swap. This interest rate swap has the economic effect of converting the borrowings from floating to fixed rates. The loan is repayable on 10 September 2017.

The interest rate swaps held by the Group at 30 June were:

	June 2013		June 2012	
R million	**Nominal value**	**Fair value liability**	Nominal value	Fair value liability
Maturity date:				
10 September 2017	**400**	**8**	400	20

Non-hedge derivative financial instruments

Discovery's asset managers use derivative instruments as mandated to limit or reduce risk. The majority of derivatives are exchange traded (SAFEX or Yield-X). Exchange traded derivatives are settled daily by reducing exposures (and hence credit risk) to zero at the end of each day. The market values of these derivatives at 30 June 2013 and 2012 are disclosed below. For derivatives with other parties, credit risk arises only where the instrument has a positive value. Discovery has some interest rate swap agreements and the value of exposure towards these parties was calculated by taking into consideration the ISDA agreements in place which allow for netting off between positive and negative exposures. The total derivative exposure is tabled below.

The table below details the Group's exposure:

R million	**Notional amount**	**Fair value asset**	**Fair value liability**
June 2013			
Interest rate contracts:			
– fixed for floating swaps	**(190)**	**1**	**(10)**
– fixed for fixed swaps	**(1)**	*****	**–**
– floating for fixed swaps	**(80)**	**4**	*****
	(271)	**5**	**(10)**
June 2012			
Interest rate contracts:			
– fixed for floating swaps	(254)	*	13
– fixed for fixed swaps	(18)	1	*
– floating for fixed swaps	(145)	7	*
	(417)	8	13

* *Amount is less than R500 000.*

Puttable non-controlling interests

The puttable non-controlling interest liability is the present value of the estimated purchase price at the expected option exercise date. This exposes Discovery to interest rate risk and the movement in the 10-year bond rate used to discount the liability will be taken to profit or loss.

If the interest rate had increased by 1% with all other variables held constant, the post-tax profit for the year would increase by R149 million (2012: R201 million). If the interest rate had decreased by 1% with all other variables held constant, the post-tax profit for the year would decrease by R161 million (2012: R218 million).

3. MANAGEMENT OF FINANCIAL RISK continued

(c) Currency risk

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar and the UK pound. Foreign exchange risk arises from future commercial transactions and recognised assets and liabilities. The table below segregates the currency exposure by major currency:

R million	Total	Rand	GBP in UK subsidiary	GBP other	USD in US subsidiary	USD other	Other currencies
At 30 June 2013							
Available-for-sale financial assets:							
Listed:							
– Equity securities	**951**	**493**	**–**	**52**	**–**	**108**	**298**
– Equity linked notes	**13**	**13**	**–**	**–**	**–**	**–**	**–**
– Debt securities	**506**	**469**	**–**	**–**	**15**	**–**	**22**
– Inflation linked securities	**46**	**38**	**–**	**–**	**–**	**–**	**8**
– Money market securities	**3 665**	**1 380**	**2 279**	**–**	**–**	**4**	**2**
Unlisted:							
– Debt securities	**135**	**135**	**–**	**–**	**–**	**–**	**–**
– Money market securities	**1 395**	**1 364**	**–**	**–**	**–**	**5**	**26**
Derivative financial instruments at fair value:							
– Hedges	**536**	**523**	**–**	**–**	**–**	**11**	**2**
– Non-hedges	**5**	**5**	**–**	**–**	**–**	**–**	**–**
Loans and receivables	**2 355**	**1 795**	**485**	**–**	**56**	**17**	**2**
Cash and cash equivalents	**1 715**	**1 329**	**224**	**1**	**79**	**11**	**71**
Total financial assets	**11 322**	**7 544**	**2 988**	**53**	**150**	**156**	**431**
Puttable non-controlling interests	**3 782**	**307**	**3 221**	**–**	**254**	**–**	**–**
Negative reserve funding	**2 813**	**–**	**2 813**	**–**	**–**	**–**	**–**
Borrowings at amortised cost	**445**	**445**	**–**	**–**	**–**	**–**	**–**
Derivative financial instruments at fair value:							
– Hedges	**10**	**10**	**–**	**–**	**–**	**–**	**–**
– Non-hedges	**17**	**10**	**7**	**–**	**–**	**–**	**–**
Trade and other payables	**3 036**	**2 231**	**744**	**–**	**55**	**–**	**6**
Total financial liabilities	**10 103**	**3 003**	**6 785**	**–**	**309**	**–**	**6**
At 30 June 2012							
Available-for-sale financial assets:							
Listed:							
– Equity securities	691	512	–	35	–	104	40
– Equity linked notes	1	–	–	–	–	1	–
– Debt securities	327	314	–	–	12	1	–
– Inflation linked securities	67	67	–	–	–	–	–
– Money market securities	2 222	73	2 147	–	2	–	–
Unlisted:							
– Equity securities	53	3	–	–	–	50	–
– Debt securities	8	8	–	–	–	–	–
– Money market securities	1 996	1 985	–	–	–	11	–
Derivative financial instruments at fair value:							
– Hedges	141	141	–	–	–	–	–
– Non-hedges	8	8	–	–	–	–	–
Loans and receivables	2 161	1 680	456	–	25	–	–
Cash and cash equivalents	1 654	1 308	293	–	53	–	–
Total financial assets	9 329	6 099	2 896	35	92	167	40

R million	Total	Rand	GBP in UK subsidiary	GBP other	USD in US subsidiary	USD other	Other currencies
Puttable non-controlling interests	2 893	399	2 152	–	342	–	–
Negative reserve funding	1 264	–	1 264	–	–	–	–
Borrowings at amortised cost	402	402	–	–	–	–	–
Derivative financial instruments at fair value:							
– Hedges	20	20	–	–	–	–	–
– Non-hedges	13	13	–	–	–	–	–
Trade and other payables	2 243	1 322	883	–	38	–	–
Total financial liabilities	6 835	2 156	4 299	–	380	–	–

Financial assets and financial liabilities in respect of the Group's US and UK subsidiaries are accounted for in their functional currency. Foreign currency movements will be recognised in the foreign currency translation reserve.

The exchange rates at year-end are detailed in the table below (quoted as Rand per foreign currency):

	USD	GBP
30 June 2013	**10.01**	**15.22**
30 June 2012	8.19	12.83

Investments

Discovery has offshore assets in its investment portfolios. These offshore investments are made for the purpose of seeking international diversification. There is a risk to future earnings that the value of these assets reduces due to a strengthening in the Rand. Performance of foreign currency assets is benchmarked against the MSCI AC World Equity Index.

Hedge derivative financial instruments

Forward exchange contracts (FECs)

To manage its foreign exchange risk arising from future commercial transactions, Discovery enters into FECs. In the current financial year, Discovery agreed to buy US Dollars from third party banks which are BBB-rated. The fair values of these contracts have been included in financial liabilities. Discovery has entered into these agreements to hedge the foreign currency risk for expenses expected to be paid in the future. The FECs have been designated as a cash flow hedge of a forecast transaction and firm commitment. Gains and losses on the FECs are initially included in equity and once the expense is incurred the gain/loss is transferred to profit or loss.

There were no outstanding contracts at 30 June 2012.

Outstanding contracts at 30 June 2013 are:

Contract	USD	ZAR	Rate	Maturity date
1	**250 000**	**2 492 875**	**9.97**	**15/07/2013**

3. MANAGEMENT OF FINANCIAL RISK continued

Collar options

Discovery purchased collar options from BBB or BBB- rated South African banks to hedge exposure to changes in foreign currency for transactions entered with foreign entities.

In the table detailed below, Discovery bought the right to buy USD (call option) and sold the right to sell USD (put option). Discovery has further sold the right to buy USD (call option) in exchange for Chinese Yuan and has bought the right to sell USD (put option) in exchange for the Chinese Yuan. Discovery has entered into these agreements to hedge the exposure to Chinese Yuan in future transactions with Ping An Health.

The fair value of these contracts has been included in financial assets. Gains and losses on the options are included in equity and once the expense is incurred the gain/loss is transferred to profit or loss.

There were no outstanding contracts at 30 June 2012.

Outstanding contracts at 30 June 2013 are:

Maturity date	Call or Put	USD	Strike price	ZAR	CNY	Fair value R million
31/07/2013	Call	7 000 000	9.106	63 742 000	–	
31/07/2013	Put	7 000 000	9.106	63 742 000	–	7
31/07/2013	Call	5 000 000	9.102	45 510 000	–	
31/07/2013	Put	5 000 000	9.102	45 510 000	–	4
31/07/2013	Call	11 494 253	6.264	–	72 000 000	
31/07/2013	Put	11 494 253	6.264	–	72 000 000	2
31/07/2013	Call	324 823	6.1572	–	2 000 000	
31/07/2013	Put	324 823	6.1572	–	2 000 000	*
31/07/2013	Call	324 670	6.1601	–	2 000 000	
31/07/2013	Put	324 670	6.1601	–	2 000 000	*
31/07/2013	Call	486 208	6.1702	–	3 000 000	
31/07/2013	Put	486 208	6.1702	–	3 000 000	*

* *Amount is less than R20 000.*

Non-hedge derivative financial instruments

Zero cost collar

PruHealth invested in fixed term deposits with a BBB rated bank, which included a zero cost collar arrangement with a cap of 13.70 ZAR:GBP and a collar of 12.75 ZAR:GBP. The deposits are held in GBP until maturity, at which point they:

- mature in ZAR at a rate of 13.70 if the spot rate at maturity is 13.70 or higher
- mature in ZAR at a rate of 12.75 if the spot rate at maturity is 12.75 or lower
- mature, at the choice of PruHealth, in either in GBP or ZAR at the spot rate if that spot rate at maturity is higher than 12.75 but lower than 13.70

The investment structure provides access to the rates of return offered in South Africa, but on a GBP denominated fixed term deposit, and at the same time reduces the PruHealth exposure to changes in foreign currency for ZAR denominated recharges from Discovery group entities.

Contract	Cap	Collar	GBP	Maturity date
1	13.70 ZAR:GBP	12.75 ZAR:GBP	166 809	23/07/2013
2	13.70 ZAR:GBP	12.75 ZAR:GBP	166 809	23/08/2013
3	13.70 ZAR:GBP	12.75 ZAR:GBP	166 809	23/09/2013

3.4.2 Credit risk

Key areas where Discovery is exposed to credit risk are:

- **Financial investments comprising money market and debt instruments entered to invest surplus shareholder funds** – Discovery is exposed to the issuer's credit standing on these instruments which is monitored by the CCIC by setting a minimum credit rating. Regulations in the various jurisdictions in which Discovery operates have the effect of limiting exposure to individual issuers due to the inadmissibility of assets if specified limits are breached. Discovery has appointed reputable asset managers to manage these instruments. Information regarding the aggregated credit risk exposure for debt and money market instruments categorised by credit ratings is provided below.
- **Cash and cash equivalents –** This risk is managed by monitoring exposure to external financial institutions against approved limits per institution. Credit ratings are provided below.
- **Certain accounts within the statement of financial position category of loans and receivables** – The management of this risk is discussed in detail on page 210.
- **Reinsurance assets comprising receivables raised for expected recoveries on projected claims (Discovery's liability as primary insurer is not discharged) and amounts due from reinsurers in respect of claims already paid** – This risk is limited as risk premiums are paid monthly to reinsurers and claims can be offset against risk premiums. Further it is expected that there will be little build-up of actuarial liability on the reinsurers' side. The risk thus mainly arises following a period of higher than expected claims. Credit ratings of reinsurers are taken into account in reinsurance placement decisions. Credit exposure to reinsurers is also limited through the use of several reinsurers. Reinsurance is placed with reputable international companies directly or through their national offices. The reinsurance companies used by Discovery are rated A or higher by A.M. Best.
- **On some investment products Discovery issues a guaranteed policy to the policyholder and the asset is guaranteed by a third party** – There is thus a risk to Discovery in the event of the third party defaulting. Credit risk is reduced by the choice and spread of third party providers.

Credit exposure for debt instruments, money market instruments and cash and cash equivalents

The following table provides information regarding the aggregated credit risk exposure for debt instruments, money market instruments and cash and cash equivalents, categorised by Fitch credit ratings:

R million	Total	AAA	AA+ AA AA–	A+ A A–	BBB BBB+	Govt	Not rated
At 30 June 2013							
Available-for-sale financial assets:							
– Debt securities	**641**	**68**	**301**	**142**	**1**	**129**	**–**
– Inflation linked securities	**46**	**–**	**32**	**1**	**–**	**13**	**–**
– Money market securities	**5 060**	**1 109**	**1 450**	**1 034**	**1 467**	**–**	**–**
– Equity linked notes	**13**	**–**	**–**	**–**	**–**	**–**	**13**
Cash and cash equivalents	**1 715**	**80**	**67**	**310**	**1 236**	**–**	**22**
	7 475	**1 257**	**1 850**	**1 487**	**2 704**	**142**	**35**
At 30 June 2012							
Available-for-sale financial assets:							
– Debt securities	335	51	88	53	–	142	1
– Inflation linked securities	67	10	45	1	–	11	–
– Money market securities	4 218	2 564	146	1 258	240	–	10
– Equity linked notes	1	1	–	–	–	–	–
Cash and cash equivalents	1 654	3	25	394	1 230	–	2
	6 275	2 629	304	1 706	1 470	153	13

3. MANAGEMENT OF FINANCIAL RISK continued

Credit risk relating to loans and receivables

Discovery's loans and receivables including insurance receivables at 30 June comprise:

R million	Ref	2013	2012
Insurance receivables:			
Premium debtors	i	**287**	169
Less provision for impairment of premium debtors		**(37)**	(33)
Reinsurance debtors (refer to page 209)		**788**	714
Other receivables:			
AIA Company Limited		**18**	–
Agents and brokers	ii	**190**	162
Cash-in-transit debtor		**6**	56
Closed scheme debtors	iii	**34**	31
Digicore loan receivable		**35**	–
Discovery Health Medical Scheme	iii	**415**	401
Discovery Unit Trust debtors		**6**	1
FNB joint venture receivable		**45**	33
Humana		**64**	21
Loans to share trust participants		**–**	113
Loans to BEE initiatives		**51**	51
Prepayments		**222**	110
Prudential Assurance Company		**–**	209
Purchased receivables		**33**	5
Road accident fund claims		**11**	28
St Andrew's Group		**57**	68
Vitality partner debtors		**16**	8
Other debtors		**225**	151
Less provision for impairment of other loans and receivables		**(111)**	(137)
		2 355	2 161

Credit risk relating to loans and receivables is managed as follows:

(i) The balance of premium debtors are not rated by Discovery as exposure to any single customer is insignificant. The premium debtors comprise amounts receivable from individuals and corporates. In addition, Discovery suspends benefits when contributions are not received for three months. Premium debtors that are past due are handled by a specialist area in business. Where amounts remain uncollected for more than six months, the debtors are then handed to specialist debt collection agencies.

(ii) Agents and brokers are subject to a comprehensive relationship management programme including credit assessment. Agents and brokers are not rated by Discovery as exposure to any single intermediary is insignificant. The widespread nature of the individual amounts combined with this close management relationship reduces credit risk. Most commission claw backs are offset against future payments and hence the risk of outstanding commission is reduced.

(iii) The Discovery Health Medical Scheme (DHMS) has been rated AA+ by Global Credit Ratings. The closed schemes have not been rated. Payments by DHMS and the other closed schemes are managed by Discovery and are paid by the seventh of the following month.

Discovery ages and pursues unpaid accounts on a monthly basis. The ageing of the components of loans and receivables at 30 June was:

R million	Gross 2013	Impairment 2013	Gross 2012	Impairment 2012
Not past due	**2 208**	**(33)**	2 124	(51)
30 days	**85**	**(8)**	17	(8)
60 days	**32**	**(7)**	19	(8)
90 days	**16**	**(4)**	9	(7)
120 days	**12**	**(4)**	11	(4)
150 days	**6**	**(5)**	6	(3)
>150 days	**144**	**(87)**	145	(89)
Total	**2 503**	**(148)**	2 331	(170)

Discovery establishes an allowance for impairment that represents its estimate of incurred losses in respect of loans and receivables. The allowance comprises a specific loss component, that relates to individually significant exposures and a collective loss component, established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

The movement in the provision for impairment during the year was as follows:

R million	2013	2012
Balance beginning of year	**170**	119
Increase in provision	**19**	56
Amounts utilised during the period	**(41)**	(5)
Balance at 30 June	**148**	170

3.4.3 Liquidity risk

Cash flow forecasting is performed in the operating entities of Group and aggregated by group finance. Group finance monitors rolling forecasts of the Group's liquidity requirements to ensure it has sufficient cash to meet operational needs while maintaining sufficient headroom on its undrawn committed borrowing facilities (note 21) at all times so that the Group does not breach borrowing limits or covenants (where applicable) on any of its borrowing facilities. Such forecasting takes into consideration the Group's debt financing plans, covenant compliance and, if applicable, external regulatory or legal requirements – such as capital requirements.

Cash held by the operating entities is managed by Group treasury. Group treasury invests it in interest-bearing accounts, time deposits and money market deposits, choosing instruments with appropriate maturities or sufficient liquidity to provide sufficient headroom as determined by the above-mentioned forecasts. At the reporting date, the shareholders held money market funds and cash and cash equivalents of R6 852 million (2012: R5 872 million) and other liquid assets of R2 964 million (2012: R2 368 million).

The table below analyses the Group's non-derivative financial liabilities and net-settled derivative financial liabilities into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date.

R million	Ref	Total	< 1 year	1 – 5 years	5 – 10 years	>10 years	Open ended
At 30 June 2013							
Puttable non-controlling interests	i, ii	**4 900**	**307**	**–**	**4 593**	**–**	**–**
Negative reserve funding	iii	**2 813**	**276**	**–**	**2 537**	**–**	**–**
Borrowings net of interest rate swap	i	**624**	**60**	**564**	**–**	**–**	**–**
Derivative financial instruments at fair value:							
– Non-hedges		**18**	**–**	**6**	**7**	**5**	**–**
Trade and other payables		**3 036**	**2 358**	**671**	**–**	**–**	**7**
Total		**11 391**	**3 001**	**1 241**	**7 137**	**5**	**7**
At 30 June 2012							
Puttable non-controlling interests	i, ii	4 399	–	–	4 399	–	–
Negative reserve funding	iii	1 264	119	–	1 145	–	–
Borrowings net of interest rate swap	i	615	41	164	410	–	–
Derivative financial instruments at fair value:							
– Non-hedges		13	2	8	2	1	–
Trade and other payables		2 243	1 971	260	7	–	5
Total		8 534	2 133	432	5 963	1	5

(i) These amounts do not agree to the statement of financial position as these are the undiscounted contractual payments.

(ii) Refer to note 19 for the contractual worst case scenarios.

(iii) The negative reserve funding liability represents the acquisition costs that are funded by the Prudential Assurance Company on behalf of PruProtect. The liability unwinds and is repaid on a matched basis as the cash flows emerge from the assets arising from insurance contracts. In the event that the cash flows do not emerge as anticipated, PruProtect would be required to repay these liabilities from other resources.

3. MANAGEMENT OF FINANCIAL RISK continued

3.5 Capital risk management

Capital adequacy risk is the risk that there are insufficient capital reserves to cover capital requirements. The Group aims to maintain a capital balance that is sufficient to meet its current and projected future obligations and strategic capital requirements.

The Group's objectives when managing capital are:

- To comply with the statutory capital requirements required by the regulators of the insurance markets where the Group operates.
- To maintain a capital buffer in excess of the statutory capital requirements in order to reduce the risk of breaching the statutory requirement in the event of deviations from the main assumptions affecting the Group's insurance businesses.
- To ensure that sufficient capital is available to fund the Group's working capital and strategic capital requirements.

For Group subsidiaries that operate in the insurance and financial services sectors, the regulator specifies the minimum amount and type of capital that must be held by each of the subsidiaries in addition to their insurance liabilities. The minimum required capital must be maintained at all times throughout the period.

Management regard share capital, share premium, perpetual preference shares, retained earnings and other reserves as capital when managing capital.

The table below summarises the minimum required capital across the Group subsidiaries, and the actual solvency capital held for each of them at 30 June 2013:

Insurance operations	Jurisdiction	Statutory solvency requirement	Actual solvency 2013	Actual solvency 2012
Discovery Life	South Africa	1 x Statutory Capital Adequacy Requirement (CAR)	**400%**	440%
Discovery Life Investment Services	South Africa	13/52 x annualised operational expenses (2012: 8/52 x annualised operational expenses)	**229%**	241%
Discovery Life Collective Investments (DLCI)	South Africa	13/52 x annualised operational expenses plus a portion of risk capital on investments held by DLCI	**367%**	205%
Discovery Insure	South Africa	13/52 x annualised operational expenses	**120%**	120%
Prudential Health Limited	United Kingdom	Capital determined under the Individual Capital Adequacy Standards (ICAS) framework	**142%**	134%
Prudential Health Insurance Limited	United Kingdom	Capital determined under the Individual Capital Adequacy Standards (ICAS) framework	**142%**	152%

3.6 Fair value estimation

The Group's financial instruments measured at fair value have been disclosed using a fair value hierarchy. The hierarchy has three levels that reflect the significance of the inputs used in measuring fair value. These are as follows:

Level 1 includes financial instruments that are measured using unadjusted, quoted prices in an active market for identical financial instruments. Quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Level 2 includes financial instruments that are valued using techniques based significantly on observable market data. Instruments in this category are valued using:

(a) quoted prices for similar instruments or identical instruments in markets which are not considered to be active or

(b) valuation techniques where all the inputs that have a significant effect on the valuation are directly or indirectly based on observable market data.

Level 3 includes financial instruments that are valued using valuation techniques that incorporate information other than observable market data and where at least one input (which could have a significant effect on instruments' valuation) cannot be based on observable market data.

For the amounts disclosed in the fair value hierarchy table, the look-through basis has not been applied to the unit trust balances and will therefore agree to the amounts disclosed in the statement of financial position.

R million	Level 1	Level 2	Level 3	Total
30 June 2013				
Financial assets				
Financial instruments at fair value through profit or loss:				
– Equity securities	**8 656**	**5 090**	**–**	**13 746**
– Equity linked notes	**–**	**1 267**	**–**	**1 267**
– Debt securities	**3 633**	**1 151**	**–**	**4 784**
– Inflation linked securities	**162**	**–**	**–**	**162**
– Money market securities	**148**	**2 783**	**–**	**2 931**
Available-for-sale financial instruments:				
– Equity securities	**733**	**231**	**–**	**964**
– Equity linked notes	**–**	**14**	**–**	**14**
– Debt securities	**33**	**507**	**–**	**540**
– Inflation linked securities	**6**	**4**	**–**	**10**
– Money market securities	**2 629**	**2 554**	**–**	**5 183**
Derivative financial instruments at fair value:				
– Hedges	**–**	**536**	**–**	**536**
– Non-hedges	**–**	**5**	**–**	**5**
	16 000	**14 142**	**–**	**30 142**
Financial liabilities				
Puttable non-controlling interests (Refer to note 4.3 and note 19)	**–**	**–**	**3 782**	**3 782**
Negative reserve funding	**–**	**2 813**	**–**	**2 813**
Borrowings at amortised cost	**–**	**445**	**–**	**445**
Derivative financial instruments at fair value:				
– Hedges	**–**	**10**	**–**	**10**
– Non-hedges	**–**	**18**	**–**	**18**
	–	**3 286**	**3 782**	**7 068**
30 June 2012				
Financial assets				
Financial instruments at fair value through profit or loss:				
– Equity securities	682	3 678	–	4 360
– Equity linked notes	–	6 436	–	6 436
– Debt securities	1 928	577	–	2 505
– Inflation linked securities	197	–	–	197
– Money market securities	178	1 359	–	1 537
Available-for-sale financial instruments:				
– Equity securities	543	193	–	736
– Equity linked notes	–	44	–	44
– Debt securities	147	183	–	330
– Inflation linked securities	15	45	–	60
– Money market securities	13	4 179	–	4 192
Derivative financial instruments at fair value:				
– Hedges	–	141	–	141
– Non-hedges	–	8	–	8
	3 703	16 843	–	20 546

3. MANAGEMENT OF FINANCIAL RISK continued

R million	Level 1	Level 2	Level 3	Total
Financial liabilities				
Puttable non-controlling interests (Refer to note 4.3 and note 19)	–	–	2 893	2 893
Negative reserve funding	–	1 264	–	1 264
Borrowings at amortised cost	–	402	–	402
Derivative financial instruments at fair value:				
– Hedges	–	20	–	20
– Non-hedges	–	15	–	15
	–	1 701	2 893	4 594

The financial assets included in level 2 above, consists primarily of investments in unit trusts where the valuation techniques maximise the use of observable market data if available and relies as little as possible on entity specific estimates. There were no transfers between level 1 and level 2 during the current financial year.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

Assumptions and estimates form an integral part of financial reporting and have an impact on the amounts reported. Assumptions are based on historical experience and expectations of future outcomes and anticipated changes in the environment. Assumptions are further regularly reviewed in the light of emerging experience and adjusted where required.

4.1 Goodwill and goodwill impairment

Following the acquisition of Standard Life Healthcare and the related capital restructure of the Prudential joint venture, Discovery allocated GBP 120.1 million to goodwill at 1 August 2010. The goodwill represents the value of future new business expected to be written by PruHealth and PruProtect and has been allocated between PruHealth and PruProtect based on management's estimate of the present value of future new business for each entity as at 31 July 2010.

The value of future PruHealth new business has been calculated as the present value of future after-tax profits of the business expected to be written in future. The after-tax profits in each future period are calculated as the earned premium multiplied by the net profit margin. A long-term net margin of 5% and a terminal growth rate of 2.5% have been used in this calculation.

The value of future PruProtect new business has been calculated using an appraisal value methodology, where the value of future new business is calculated as a 3 times multiple of the value of new business written over the past year.

Based on the above valuations, GBP 96.7 million and GBP 23.4 million of the goodwill was allocated to PruHealth and PruProtect respectively as at 31 July 2010.

Recoverable amount of goodwill at 30 June 2013

Discovery tests each cash-generating unit (CGU) containing goodwill for impairment on an annual basis. An impairment loss is recognised whenever the carrying amount of a CGU exceeds its recoverable amount. The recoverable amount of each CGU is estimated as the present value of future cash flows that are expected to be derived from the asset ie. its value-in-use. The value-in-use is calculated as the present value of the best estimate pre-tax cash flows for each CGU over a 10 year projection period plus a terminal value calculated using a 2% per annum terminal growth rate assumption.

During the reporting period, the recoverable amount for PruHealth was 1.4 times higher than the carrying amount and the recoverable amount for PruProtect was 5.5 times higher than the carrying amount, therefore no impairment is necessary.

4.2 Equity linked notes

Discovery Life has invested in equity linked notes offered by International Banks in order to back certain unit-linked contract liabilities. The calculation of the daily value of the equity linked investments is made by the provider of the note. Discovery Life does, however, have procedures in place to ensure that these prices are correct. Aside from the daily reasonableness checks versus similar funds and movement since the prior day's price, the fund values are calculated with reference to a specific formula or index, disclosed to the policyholders, which is recalculated by Discovery Life in order to check if the price provided by the provider is correct.

4.3 Puttable non-controlling interest liability

During the 2011 financial year, put options were granted to the non-controlling interests of three of Discovery's subsidiaries. The put options entitle the non-controlling interest to sell its interest in the subsidiary to Discovery at contracted dates.

The following put options were issued:

- PAC has the option to sell its 25% shareholding in Prudential Health Holdings Limited to Discovery, five years from 1 August 2010 or after each succeeding one year period, using a formula that is an estimate of fair value.
- Humana has the option to sell its 25% shareholding in The Vitality Group LLC to Discovery, seven years after acquisition or after each succeeding two year period, at the fair market value less a 15% discount.
- The Discovery Insure preference shareholders have the option to sell its 25% shareholding in Discovery Insure to Discovery, four, five or seven years after acquisition, at the fair market value.

In accordance with IAS32, Discovery has consolidated 100% of the subsidiaries results and has recognised the fair value of the non-controlling interest, being the present value of the estimated purchase price, as a financial liability in the statement of financial position (Puttable non-controlling interests). In raising this liability, the non-controlling interest is derecognised and the excess of the liability is debited to retained earnings in the statement of changes in equity.

Interest is recorded in respect of this liability within finance costs using the effective interest rate method. The estimated purchase price is reconsidered at each reporting date and any changes in the value of the liability as a result of changes in the assumptions used to estimate the future purchase price will be recorded in profit or loss.

The puttable non-controlling interest liability is calculated as the present value of the non-controlling interests' share of the expected redemption value, discounted from the expected option exercise date to the reporting date. There are therefore two steps to the put option liability valuation process:

- estimation of the expected redemption value at the expected option exercise date
- discounting the expected redemption value to the reporting date using a discount rate equal to an appropriate cost of debt

Estimating the expected redemption value

Prudential Health Holdings Limited (PHHL)

Prudential has the option to sell its 25% shareholding in PHHL to Discovery, five years from 1 August 2010 or after each succeeding one year period, at the fair market value. For valuation purposes, it is assumed that the option will be exercised in 2020, when the current contractual rights and obligations will be renegotiated with PAC.

The contractual agreement specifies that the redemption value will be calculated as follows:

- The redemption value for PruHealth will be calculated as the projected tangible net asset value plus a value per life insured multiplied by the number of lives insured, at the valuation date.
- The redemption value for PruProtect will be calculated as the projected value of in-force business at the valuation date plus the value of three years' new business.

The Vitality Group LLC

Humana has the option to sell its 25% shareholding in TVG LLC to Discovery, seven years after acquisition or after each succeeding two year period, at the fair market value less a 15% discount. For valuation purposes, it is assumed that the option will be exercised in 2020.

The fair market value is calculated as the projected tangible net asset value at the valuation date plus the present value of the projected future cash flows discounted to the valuation date.

Discovery Insure

The Discovery Insure preference shareholders have the option to sell its 25% shareholding in Discovery Insure to Discovery.

Discovery and the preference shareholders have agreed on the sale of the preference shares to Discovery. Based on the agreed purchase price, the put option has been valued at R307.25 million at 30 June 2013.

Calculating the discount rate

The discount rate is calculated as the cost of debt using an appropriate risk free interest rate plus the Discovery credit spread.

The risk free interest rate is derived from the applicable government bond yield curve (UK government bond curve for PruHealth and PruProtect and US government bond curve for The Vitality Group LLC) based on the number of years between the reporting date and the expected option exercise date. As Discovery and the Discovery Insure preference shareholders have agreed on the sale of the preference shares in Discovery Insure, no discounting has been applied to the Discovery Insure redemption value.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES continued

4.4 Policyholder liabilities assumptions and estimates (including assets arising from insurance contracts)

The insurance policies issued by Discovery Life are valued using various methodologies and assumptions. The methodology is described in the accounting policies on pages 159 to 162. The assumptions used are best estimate assumptions, with the addition of explicit compulsory margins required by SAP 104 of the Actuarial Society of South Africa and the discretionary margins described on page 160 of the accounting policies. The process used to decide on best-estimate assumptions is described below:

Experience investigations

Experience investigations into lapse, mortality, morbidity, expenses and other key accounting estimates are performed at every valuation date.

The data for the months since the previous valuation date forms the basis of each investigation. The experience of prior periods is also considered to establish trends and add credibility to the results.

The most recent experience investigations were performed at 30 June 2013.

Mortality and morbidity

Assumptions of future mortality and morbidity experience are derived based on data from reinsurers and compared to actual past experience. Where appropriate, the assumptions are adjusted to reflect actual past experience or for expected changes in future experience.

The assumptions are modified for each policy based on actual data available from underwriting performed on the policy.

The assumptions are compared against standard industry tables for reasonability. The key mortality and morbidity assumptions are reviewed and benchmarked against the industry by independent actuarial consultants to ensure that the assumptions are reasonable, upon implementation of significant new products.

An allowance is made for the impact of AIDS on South African mortality rates. This is described in detail under the AIDS assumption below.

Surrender and lapse rates

Surrender and lapse rates are based on actual past experience where available. The lapse analysis is done by considering the in-force duration of policies. For durations longer than existing actual data, lapse rates are set based on expectations of future experience based on internal and external expert advice. The lapse experience investigation covers at least the last two years of lapse experience to allow trends to be identified.

Lapse assumptions are varied between different types of policies where the lapse experience is expected to differ significantly. Allowance is made for the estimated impact of the economic environment.

Taxation

Future tax is allowed for according to the current tax legislation and current tax rates.

The current and expected future tax position of each policyholder's tax fund is taken into account in setting the tax assumption.

The individual policyholders' fund (IPF) is currently in an excess expense (XE) position and hence no tax is payable on the interest earned on policyholders' funds within the IPF. Consequently, no allowance is made for tax relief on expenses within the IPF. Current forecasts are that the IPF will remain in an XE position. No deferred tax is raised for the XE position. Tax relief on expenses is allowed for in PruProtect, for policies sold prior to January 2013.

Deferred tax arises on the other temporary differences between the accounting basis and the tax basis.

It is assumed that future tax on statutory profits will be payable at the prevailing company tax rate of 28% (2012: 28%) in South Africa. The prevailing tax rate in the UK is 23% (2012: 24%).

Economic assumptions/Investment returns

The discount rate is set equal to the estimate of the risk free investment return rate. The risk free rate is calculated with reference to the risk free yield curve. A single risk free rate is then derived appropriate to the weighted duration of the cash flows and rounded to the nearest quarter of a percent. The risk free rate at 30 June 2013 was set at 8.5% pa (2012: 8.5% pa).

Other investment returns and economic assumptions are set relative to this yield. The assumptions for Discovery Life are as follows:

Cash:	Risk free -1.5%
Fixed interest:	Risk free
Equity:	Risk free + 3.5%
Consumer price inflation:	Risk free -4%

For PruProtect , the risk free rate is set in line with the market observed investment return of fixed interest assets of appropriate term and nature, less a margin to protect against adverse experience. The best estimate inflation assumption is set in line with long term UK inflation expectations and observed real yields consistent with the term of the liabilities.

The investment fees and tax rates are taken into account in setting the economic assumptions.

Expense assumptions

Renewal expense assumptions are based on the results of the latest expense and budget information.

The allocation of expenses between initial and renewal expenses is based on the latest expense analysis where expenses are directly allocated based on the function performed. Where an expense could relate to both initial and renewal functions, the expenses are allocated proportionately based on estimates of the functions performed.

Per policy expenses are projected to increase in line with consumer price inflation.

Non-recurring expenses are excluded from the expense analysis used to derive the assumption.

HIV/AIDS

For individual South African business a fixed loading is applied to the expected best estimate mortality rates to allow for the expected effect of AIDS. The loading varies based on socio-economic class. An HIV test is required for all individual policies with lump sum life cover. Discovery Life further operates in the high end of the market where the AIDS risk is lower compared to the full market. The additional loading for AIDS is set in consultation with external independent actuaries and reinsurers.

For Group policies a loading is applied at the underwriting stage to allow for the expected effect of AIDS. The loading varies based on the industry and geographic area and composition of the group and is derived from advice received from the reinsurers. The loading then forms the AIDS assumption for Group policies.

Reinsurance

All prospective liabilities are valued gross of reinsurance and then adjusted for the expected effect of reinsurance. For outstanding reported claims and incurred but not reported claims liabilities (IBNR), a specific allowance is made for reinsurance recoveries.

The Global Linkage Benefit is fully reinsured. The cost of the future reinsurance is dependent on the cost at which the reinsurer can hedge the liabilities under this benefit. Assumptions are made around the cost at which the reinsurer can hedge the benefits, based on current and historic costs of the hedging structures.

Automatic premium increases

Automatic premium increases could include both contractual and voluntary increases. No allowance is made for voluntary premium increases when calculating liabilities under insurance contracts in Discovery Life. Contractual premium increases are defined as increases that cannot be cancelled by the policyholder without altering the terms of the benefits provided under the policy. Contractual increases are included in the calculation of policyholder liabilities.

Policy alterations

In the calculation of policyholder liabilities, no allowance is made for policy alterations over time in accordance with actuarial guidance.

Changes in assumptions

Assumptions and methodologies are reviewed during each valuation. The impact of changes in the assumptions is reflected in profit or loss as the changes occur.

Modelling and assumptions changes were made to the valuation at 30 June 2013 to ensure that assumptions are in line with the best estimate of future experience. The total effect of these changes was an increase in the liabilities on the Financial Soundness Valuation basis of R79 million (2012: R199 million increase).

In addition to this, the discretionary margins were reset to reflect the underlying profitability of the overall portfolio. The reset of margins decreased the liabilities on the Financial Soundness Valuation basis by R278 million (2012: R106.6 million decrease). See note 5 for an analysis of these changes.

Sensitivities

The sensitivity of the policyholder liabilities on the Financial Soundness Valuation basis is set out on page 190.

5. ASSETS ARISING FROM INSURANCE CONTRACTS

R million	Group 2013	Group 2012
Long-term insurance contracts – gross	**14 407**	11 681
Less: ceded to reinsurers (refer to note 18)	**(873)**	(843)
Long-term insurance contracts – net	**13 534**	10 838
Current	**2 342**	1 853
Non-current	**14 629**	11 347
Variable[1]	**(3 437)**	(2 362)
	13 534	10 838
Movement in assets arising from insurance contracts		
Balance at beginning of the year	**10 838**	8 316
Movement for the year:		
Expected movement in policyholder liabilities	**(2 686)**	(1 925)
Unwinding of discount rate	**1 039**	1 026
New business written	**3 051**	2 633
Experience variances	**522**	333
Economic	**83**	42
Operational	**439**	291
Modelling and method changes	**94**	199
Benefit enhancements	**–**	(38)
Changes in assumptions	**(201)**	1 512
Economic	**168**	627
Operational	**(369)**	751
Premium and benefit increase assumptions	**–**	134
Changes in margins	**422**	(1 393)
Margins related to premium and benefit increase assumption	**–**	(134)
Other margin changes[2]	**422**	(1 259)
Exchange rate difference	**455**	175
Balance at end of the year	**13 534**	10 838

(1) The variable portion relates to unit-linked policyholder liabilities of the Discovery Retirement Optimiser product which is attached to a Life Plan. The maturity of this liability is dependent of policyholder behaviour.

(2) In line with accounting policy 13.1, the best estimate and margins are reset at every valuation date to reflect the underlying profitability of the overall portfolio. Assumptions and margins are not set on new business in isolation but on a portfolio level.

6. PROPERTY AND EQUIPMENT

R million	Furniture, fittings and equipment	Computer equipment and operating systems	Leasehold improve-ments	Motor vehicles	Total
Year ended 30 June 2012					
Opening carrying amount	60	43	92	5	200
Exchange differences	1	3	1	–	5
Additions	32	41	40	3	116
Disposals					
– Cost	(2)	–	(3)	–	(5)
– Accumulated depreciation	2	–	3	–	5
Depreciation charge	(24)	(19)	(24)	(3)	(70)
Closing carrying amount	69	68	109	5	251
At 30 June 2012					
Cost	189	162	196	20	567
Accumulated depreciation	(120)	(94)	(87)	(15)	(316)
Carrying amount	69	68	109	5	251
Year ended 30 June 2013					
Opening carrying amount	**69**	**68**	**109**	**5**	**251**
Exchange differences	**1**	**26**	**3**	*	**30**
Purchase of businesses	**2**	–	–	–	**2**
Additions	**21**	**308**	**22**	**4**	**355**
Disposals					
– Cost	**(2)**	*	–	**(1)**	**(3)**
– Accumulated depreciation	**2**	*	–	**1**	**3**
Depreciation charge	**(25)**	**(44)**	**(33)**	**(3)**	**(105)**
Closing carrying amount	**68**	**358**	**101**	**6**	**533**
At 30 June 2013					
Cost	**258**	**511**	**221**	**21**	**1 011**
Accumulated depreciation	**(190)**	**(153)**	**(120)**	**(15)**	**(478)**
Carrying amount	**68**	**358**	**101**	**6**	**533**

* *Amount is less than R500 000.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS continued

for the year ended 30 June 2013

7. INTANGIBLE ASSETS INCLUDING DEFERRED ACQUISITION COSTS

		Deferred acquisition costs		Business acquisitions[2]			
R million	Software	Investment management contracts	Insurance contracts[1]	Customer contracts[3]	Prudential brand	Renewal commission	Total
Year ended 30 June 2012							
Opening carrying amount	155	173	124	828	160	–	1 440
Foreign currency adjustment on translation	2	–	24	147	28	–	201
Additions	138	100	192	–	–	–	430
Amortisation charge	(115)	–	–	(129)	(15)	–	(259)
Deferred acquisition costs amortised	–	(38)	(166)	–	–	–	(204)
Closing carrying amount	180	235	174	846	173	–	1 608
At 30 June 2012							
Cost	551	235	174	1 081	201	–	2 242
Accumulated amortisation	(371)	–	–	(235)	(28)	–	(634)
Carrying amount	180	235	174	846	173	–	1 608
Year ended 30 June 2013							
Opening carrying amount	**180**	**235**	**174**	**846**	**173**	–	**1 608**
Foreign currency adjustment on translation	**4**	–	**36**	**144**	**31**	–	**215**
Additions	**224**	**117**	**310**	–	–	–	**651**
Purchase of businesses	–	–	–	–	–	**1**	**1**
Amortisation charge	**(125)**	–	–	**(157)**	**(20)**	–	**(302)**
Disposal	**(43)**	–	–	–	–	–	**(43)**
Deferred acquisition costs amortised	–	**(36)**	**(266)**	–	–	–	**(302)**
Closing carrying amount	**240**	**316**	**254**	**833**	**184**	**1**	**1 828**
At 30 June 2013							
Cost	**760**	**316**	**254**	**1 283**	**239**	**1**	**2 853**
Accumulated amortisation	**(520)**	–	–	**(450)**	**(55)**	–	**(1 025)**
Carrying amount	**240**	**316**	**254**	**833**	**184**	**1**	**1 828**

(1) This intangible asset relates to health insurance contracts only.

(2) Intangibles identified in the acquisition of business combinations are amortised over their remaining useful lives and tested for impairment at each reporting date. There was no indication of impairment for the current reporting period.

(3) Customer contracts represents the value of in-force business acquired in the Standard Life Healthcare business combination.

8. BUSINESS COMBINATIONS

8.1 Insure Your Health

On 25 March 2013, Prudential Health Holdings Limited (PHHL), established a wholly-owned subsidiary named Insure Your Health Limited, and acquired 100% of the share capital for GBP1.9 million.

The activities of this company comprise:

- sales of Private Medical Insurance (PMI) products for a small panel of providers for individual PMI products
- sales of PMI products for PruHealth for SME products on an exclusive basis
- sales of individual protection products for a small panel of providers

To set-up the business, Insure Your Health acquired the assets of the three businesses namely, Insured Health Limited, Insured Limited and Employed Health Limited. The 'assets' include:

- plant and equipment
- leasehold property
- commission debts
- business information
- each other asset which is used in connection with the business
- each right that the business has against another person which relates to the business

The initial purchase price is
(1) GBP 1.9 million plus
(2) an amount equal to the estimated commission debtors, plus
(3) an amount in advance relating to the future renewal commission stream.
Both (2) and (3) are subject to a 13-month true-up process.

Discovery has allocated the purchase price as follows:

	GBP	R million*
Tangible net asset value:		
– Property and equipment	142 367	2
– Commission debtors	325 402	5
– Prepayments	50 888	1
Intangible assets:		
– Future renewal commission stream	100 000	2
Goodwill	2 002 259	30
Deemed consideration paid	2 620 916	40

* *Translated at closing rate at 30 June 2013, which is the rate they are included in the statement of financial position.*

The intangible asset identified in the table above have been included in the statement of financial position of the Group. This intangible asset will be amortised over 12 months from date of purchase.

Goodwill, which represents the future new business expected to be written by PruHealth, is not amortised, but is assessed for possible impairment at each reporting date and the impairment is recorded in profit or loss, if necessary.

Post-acquisition revenue and profit or loss of acquired businesses
The table below discloses the post-acquisition revenue and profit or loss that has been included in the Group's income statement at 30 June 2013:

R million	2013
Revenue	**14**
Loss for the period	**(3)**

8. BUSINESS COMBINATIONS continued

8.2 Goodwill recognised through business combinations

Goodwill, which represents the value of future business expected to be written, is not amortised, but is assessed for possible impairment at each reporting date. The impairment is recorded in profit or loss, if necessary. At 30 June 2013 there was no indication that goodwill is impaired.

Reconciliation of goodwill	Date of acquisition	GBP million	R million
Balance at 1 July 2011			
Goodwill recognised from the purchase of PruHealth Holdings Limited	31 July 2010	86.9	942
Goodwill recognised from the purchase of Standard Life Healthcare	31 July 2010	33.2	360
Net exchange differences arising during the year			240
Balance at 30 June 2012		120.1	1 542
Goodwill recognised from the Insure Your Health business combination	25 March 2013	**2.0**	**30**
Net exchange differences arising during the year			**287**
Balance at 30 June 2013		**122.1**	**1 859**

9. INVESTMENT IN ASSOCIATES

R million	Group 2013	Group 2012
Balance at 1 July	**341**	260
Increase in consideration paid	**16**	23
Included in profit or loss:		
– share of loss of associate	**(22)**	(13)
– amortisation of intellectual property[1]	**(9)**	(8)
Other equity movements:		
– available-for-sale investments reserve	**(1)**	2
Exchange differences	**77**	77
Balance at 30 June	**402**	341

(1) Upon formation of Humana Vitality LLC (HV), TVG Inc. contributed a perpetual royalty-free license to the Vitality IT systems, the Vitality name and associated marks and a perpetual, royalty-free license to the Vitality intellectual property, exclusively for use in the United States, for its 25% shareholding. This contribution was valued at USD 12.5 million and disclosed as an investment in associate in the statement of financial position. HV recognised an intangible asset, being intellectual property, for the same value which is amortised to profit or loss on a straight-line basis over a three-year period. The amortisation has been included in 'amortisation of intangibles from business combinations' in the income statement.

The financial information of equity accounted associates is set out below. The amounts disclosed are 100% of the entities results.

R million	Country of incorporation	Assets	Liabilities	Revenues	Profit/(Loss)	% interest held
30 June 2013						
– Ping An Health Insurance Company of China, Limited	**China**	**1 897**	**1 058**	**316**	**(112)**	**20%**
– Humana Vitality LLC	**USA**	**804**	**213**	**591**	**80**	**25%**
– Healthcode Limited	**UK**	**30**	**21**	**34**	**1**	**20%**
		2 731	**1 292**	**941**	**(31)**	
30 June 2012						
– Ping An Health Insurance Company of China, Limited	China	1 372	604	195	(68)	20%
– Humana Vitality LLC	USA	520	114	255	(101)	25%
– Healthcode Limited	UK	23	18	29	*	20%
		1 915	736	479	(169)	

** Amount is less than R500 000.*

10. INVESTMENT IN JOINT VENTURE

On 10 May 2013, Discovery Vitality International Asia Private Limited (a 100% subsidiary of Discovery Limited), contributed HK$ 1000 for 50% of the ordinary share capital of AIA Vitality Company Limited.

R	Group 2013
Consideration paid	**1 189**
Included in profit or loss:	
– share of loss of joint venture	**(1 189)**
Balance at 30 June	**–**

The financial information of the equity accounted joint venture is set out below. The amounts disclosed are 100% of the entity's results.

R million	Country of incorporation	Assets	Liabilities	Revenues	Profit/(Loss)	% interest held
30 June 2013						
AIA Vitality Company Limited	**Singapore**	**160**	**72**	**–**	**(117)**	**50%**

11. FINANCIAL ASSETS – INVESTMENTS

R million	Group 2013	Group 2012
The Group's investment in financial assets are summarised by measurement category below:		
Available-for-sale financial assets:	**6 711**	5 362
– Equity securities	**964**	736
– Equity linked notes[1]	**14**	44
– Debt securities	**540**	330
– Inflation linked securities	**10**	60
– Money market securities	**5 183**	4 192
Financial assets at fair value through profit or loss:	**22 890**	15 035
– Equity securities	**13 746**	4 360
– Equity linked notes[1]	**1 267**	6 436
– Debt securities	**4 784**	2 505
– Inflation linked securities	**162**	197
– Money market securities	**2 931**	1 537
Total investments	**29 601**	20 397
Listed	**25 026**	14 646
Unlisted	**4 575**	5 751
	29 601	20 397

(1) Majority of the equity linked notes are Rand denominated investments providing equity exposure together with either a floor of 80% of the highest price observed since inception or a return after five years based on the best of three different unit trusts or indices.

Maturity profile:

- It is management's intention to hold the available-for-sale financial assets as a long-term investment but may utilise these funds when required by business.
- Financial assets at fair value through profit or loss are held to back policyholder liabilities. Except for R457 million (2012: R255 million) which will be held to back unit-linked insurance contracts with a maturity profile between one and five years (refer to page 200), the balance can be withdrawn in the short-term.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS continued

for the year ended 30 June 2013

12. DERIVATIVE FINANCIAL INSTRUMENTS

R million	Group 2013 Assets	Group 2013 Liabilities	Group 2012 Assets	Group 2012 Liabilities
Phantom share scheme – cash flow hedge	**259**	**(2)**	55	–
Phantom share scheme – fair value hedge	**264**	**–**	86	–
Collar options	**13**	**–**	–	–
Interest rate swap	**–**	**(8)**	–	(20)
Non-hedge derivatives	**5**	**(18)**	8	(15)
	541	**(28)**	149	(35)
Current	**161**	**–**	51	(10)
Non-current	**380**	**(28)**	98	(25)
	541	**(28)**	149	(35)

Refer to pages 202 to 208 for a detailed description of the derivative financial instruments listed above.

13. LOANS AND RECEIVABLES INCLUDING INSURANCE RECEIVABLES

R million	Group 2013	Group 2012
Receivables arising from insurance and reinsurance contracts:		
– Premium debtors	**287**	169
– Less provision for impairment of premium debtors	**(37)**	(33)
– Reinsurance debtors	**788**	714
Other loans and receivables:		
– AIA Company Limited	**18**	–
– Agents and brokers	**190**	162
– Cash-in-transit debtors	**111**	56
– Closed scheme debtors	**34**	31
– Digicore loan receivable	**35**	–
– Discovery Health Medical Scheme	**415**	401
– Discovery Unit Trust debtors	**607**	37
– FNB joint venture receivable	**45**	33
– Humana	**64**	21
– Loans to share trust participants	**–**	113
– Loans to BEE initiatives	**51**	51
– Prepayments	**222**	110
– Prudential Assurance Company	**–**	209
– Purchased receivables	**33**	5
– Road accident fund claims	**11**	28
– St Andrew's Group	**57**	68
– Vitality partner debtors	**16**	8
– Other debtors	**225**	151
– Less provision for impairment of other loans and receivables	**(111)**	(137)
Total loans and receivables	**3 061**	2 197
Current	**2 919**	1 987
Non-current	**142**	210
	3 061	2 197

The fair value approximates the carrying value of the loans and receivables.

14. REINSURANCE CONTRACTS

R million	Group 2013	Group 2012
Reinsurers' share of insurance contract liabilities	**237**	201
Current	**237**	201

Amounts due from reinsurers in respect of claims paid and reported by the Group on the contracts that are reinsured are included in loans and receivables (refer to note 13).

15. CASH AND CASH EQUIVALENTS

Cash at bank and in hand	**1 521**	945
Short-term deposits	**541**	984
	2 062	1 929

The effective interest rate on short-term deposits was 4.9% (2012: 5.23%) and the average maturity 13 days (2012: 26 days).

Cash and cash equivalents include the following for the purposes of the statement of cash flows:

Cash and cash equivalents	**2 062**	1 929
Bank overdraft (note 21)	**(216)**	–
	1 846	1 929

16. SHARE CAPITAL AND SHARE PREMIUM

16.1 Ordinary share capital and share premium

	Number of shares	Ordinary shares R million	Share premium R million	Treasury shares R million	Total R million
At 1 July 2011	554 975 477	1	1 593	(52)	1 542
Employee share option scheme:					
– Delivered to participants	355 496	*	*	–	*
Treasury share purchases	(961 700)	–	–	(47)	(47)
Realised gains from share trust treasury shares	–	–	8	–	8
At 30 June 2012	554 369 273	1	1 601	(99)	1 503
Employee share option scheme:					
– Delivered to participants	**277 543**	*	*	–	*
Treasury share purchases	**(633 890)**	–	–	**(39)**	**(39)**
Realised gains from share trust treasury shares	–	–	**6**	–	**6**
At 30 June 2013	**554 012 926**	**1**	**1 607**	**(138)**	**1 470**

* *Amount is less than R500 000.*

The total authorised number of ordinary shares is 1 billion (2012: 1 billion), with a par value of 0.1 cent per share.

16.2 Preference share capital

	2013 R million	2012 R million
Authorised		
20 000 000 class B voluntarily redeemable non-convertible preference shares of R100 each	**2 000**	2 000
Issued		
8 000 000 class B voluntarily redeemable non-convertible preference shares of R100 each	**800**	800
Share issue costs	**(21)**	(21)
At 30 June	**779**	779

The preference shares are non-compulsory, non-cumulative, non-participating, non-convertible, voluntarily redeemable no par value preference shares and were issued at a coupon rate of 85% of prime rate. With the introduction of dividend withholding tax on 1 April 2012, the coupon rate on the preference shares was increased to 100% of the prime rate.

16. SHARE CAPITAL AND SHARE PREMIUM continued

16.3 Discovery share incentive trusts and BEE transaction

	2013 Shares	2012 Shares
Number of ordinary shares allocated at beginning of the year	**36 822 849**	36 216 645
Number of ordinary shares purchased by the BEE staff share trust	**100 000**	725 000
Number of ordinary shares purchased by BEE participants	**533 890**	236 700
Number of ordinary shares delivered to participants during the year	**(277 543)**	(355 496)
Number of ordinary shares allocated at end of the year	**37 179 196**	36 822 849

For more details regarding the trusts refer to note 33.

17. LIABILITIES ARISING FROM INSURANCE CONTRACTS

R million	Group 2013	Group 2012
Gross		
Short-term liabilities:		
– claims reported and loss adjustment expenses	**2 566**	1 926
– claims incurred but not reported	**870**	732
– EFA liability	**16**	3
– unearned premiums	**519**	439
Long-term liabilities:		
– unit-linked insurance contracts	**9 575**	6 593
– with fixed and guaranteed terms	**5 540**	4 626
Total liabilities arising from insurance contracts, gross	**19 086**	14 319
Recoverable from reinsurers		
Short-term liabilities:		
– claims incurred but not reported	**(237)**	(201)
Total reinsurers' share of liabilities arising from insurance contracts (refer to note 14)	**(237)**	(201)
Net		
Short-term liabilities:		
– claims reported and loss adjustment expenses	**2 566**	1 926
– claims incurred but not reported	**633**	531
– EFA liability	**16**	3
– unearned premiums	**519**	439
Long-term liabilities:		
– unit-linked insurance contracts	**9 575**	6 593
– with fixed and guaranteed terms	**5 540**	4 626
Total liabilities arising from insurance contracts, net	**18 849**	14 118
Current	**4 570**	3 157
Non-current	**3 450**	3 385
Variable[1]	**10 829**	7 576
	18 849	14 118

(1) There is no maturity profile for these liabilities as this will depend on policyholder behaviour. Contractually policyholders may disinvest on demand.

17. LIABILITIES ARISING FROM INSURANCE CONTRACTS continued

Movements in the liabilities are as follows:

R million	2013 Gross	2013 Reinsurance	2013 Net	2012 Gross	2012 Reinsurance	2012 Net
Claims reported and loss adjustment expenses						
Notified claims	**1 926**	**–**	**1 926**	1 700	–	1 700
Incurred but not reported	**732**	**(201)**	**531**	626	(180)	446
Balance at beginning of the year	**2 658**	**(201)**	**2 457**	2 326	(180)	2 146
Cash paid for claims settled in the year	**(687)**	**89**	**(598)**	(593)	–	(593)
Increase/(decrease) in liabilities:						
– arising from current year claims	**1 791**	**(106)**	**1 685**	1 244	(9)	1 235
– arising from prior year claims	**(430)**	**–**	**(430)**	(397)	–	(397)
Net exchange differences	**104**	**(19)**	**85**	78	(12)	66
Total at end of the year	**3 436**	**(237)**	**3 199**	2 658	(201)	2 457
Notified claims	**2 566**	**–**	**2 566**	1 926	–	1 926
Incurred but not reported	**870**	**(237)**	**633**	732	(201)	531
Total at end of the year	**3 436**	**(237)**	**3 199**	2 658	(201)	2 457
EFA liability						
Balance at beginning of the year	**3**	**–**	**3**	–	–	–
Increase in the year	**14**	**–**	**14**	3	–	3
Cash paid	**(1)**	**–**	**(1)**	*	–	–
Total at end of the year	**16**	**–**	**16**	3	–	3
Provisions for unearned premiums						
Balance at beginning of the year	**439**	**–**	**439**	430	–	430
Release in the year	**(2)**	**–**	**(2)**	(68)	–	(68)
Net exchange differences	**82**	**–**	**82**	77	–	77
Total at end of the year	**519**	**–**	**519**	439	–	439

* *Amount is less than R500 000.*

R million	Group 2013	Group 2012
Long-term insurance contracts		
Unit-linked insurance contracts		
Balance at beginning of the year	**6 593**	4 454
Premiums received	**3 746**	2 656
Fair value adjustment	**1 346**	556
Withdrawals	**(1 567)**	(646)
Fees	**(273)**	(157)
Movement in negative insurance liability	**(270)**	(270)
Balance at end of the year	**9 575**	6 593
With fixed and guaranteed terms		
Balance at beginning of the year	**4 626**	3 411
Expected movement in policyholder liabilities	**(416)**	(305)
Unwinding of discount rate	**257**	245
New business written	**1 028**	1 016
Change in assumptions	**45**	259
Balance at end of the year	**5 540**	4 626

18. LIABILITIES ARISING FROM REINSURANCE CONTRACTS

R million	Group 2013	Group 2012
Lapse risk treaties	**635**	614
Reinsurance recoveries relating to assets arising from insurance contracts (refer to note 5)	**873**	843
	1 508	1 457
Balance at beginning of the year	**1 457**	1 308
Increase in liability	**42**	131
– Accrual	**484**	564
– Net reinsurance premiums	**(442)**	(433)
Exchange differences	**9**	18
Balance at end of the year	**1 508**	1 457
Current	**190**	203
Non-current	**1 318**	1 254
	1 508	1 457

19. PUTTABLE NON-CONTROLLING INTERESTS

During the 2011 financial year, put options were granted to the non-controlling interests of three of Discovery's subsidiaries. The put options entitle the non-controlling interest to sell its interest in the subsidiary to Discovery at contracted dates.

The following put options were issued:

- PAC has the option to sell its 25% shareholding in Prudential Health Holdings Limited to Discovery, five years from 1 August 2010 or after each succeeding one year period, at the fair market value.
- Humana has the option to sell its 25% shareholding in The Vitality Group LLC to Discovery, seven years after acquisition or after each succeeding two year period, at the fair market value less a 15% discount.
- The Discovery Insure preference shareholders have the option to sell its 25% shareholding in Discovery Insure to Discovery, between five and seven years after acquisition, at the fair market value. (Refer to note 44 regarding the exercising of this option.)

The aggregate effects on Discovery's results at 30 June are as follows:

R million	Group 2013	Group 2012
Balance at beginning of the year	**2 893**	2 314
Further share issues to non-controlling interests	**77**	29
Finance costs recognised in profit or loss	**165**	152
Fair value adjustments:	**133**	13
– Resulting from a change in interest rates	**(55)**	164
– Resulting from a change in assumptions	**188**	(151)
Net exchange differences arising during the period	**514**	385
Closing value of puttable non-controlling interest liability	**3 782**	2 893

20. NEGATIVE RESERVE FUNDING

Negative reserve funding	**2 537**	1 145
Finance charge payable on negative reserve funding	**276**	119
	2 813	1 264

The negative reserve funding liability represents the acquisition costs that are funded by the Prudential Assurance Company on behalf of PruProtect. The liability unwinds and is repaid on a matched basis as the cash flows emerge from the assets arising from insurance contracts. In the event that the cash flows do not emerge as anticipated, PruProtect would be required to repay these liabilities from other resources.

21. BORROWINGS AT AMORTISED COST

R million	Group 2013	Group 2012
Bank borrowings	**402**	402
Bank overdraft	**216**	–
Finance lease liability	**42**	–
	660	402
Current	**232**	2
Non-current	**428**	400
	660	402

Bank borrowings

In order to fund the acquisition of Standard Life Healthcare, Discovery borrowed R400 million from FirstRand Bank Limited. The salient terms of the loan are the following:

– Lender: FirstRand Bank Limited
– Type of borrowings: Senior debt
– Interest rate: Floating
– Security: Pledge of shares in Discovery Life Limited
– Maturity date: 10 September 2017
– Callable/Convertible: Not applicable

The borrowings are repayable on maturity and interest is paid quarterly. The interest rate has been fixed through interest rate swaps.

The loan agreement imposes certain restrictions on Discovery's operations, including a limitation on total borrowings. A breach of these restrictions would require immediate repayment of any outstanding balance.

Undrawn borrowing facilities

The Group has undrawn committed floating rate borrowing facilities totalling R800 million, expiring 30 June 2014.

Capitalised finance lease liability

Lease liabilities are not secured as the rights to the leased assets remain with the lessee in event of default.

R million	Minimum lease payments	Finance cost	Present value
30 June 2013			
Due within one year	**18**	**(4)**	**14**
Due between two and five years	**31**	**(3)**	**28**
	49	**(7)**	**42**

22. INVESTMENT CONTRACTS AT FAIR VALUE THROUGH PROFIT OR LOSS

R million	Group 2013	Group 2012
The movements during the year were as follows:		
Balance at beginning of the year	**2 915**	2 063
Premiums received	**8 856**	1 578
Fees deducted from account balances	**(3)**	(5)
Account balances paid on withdrawal and other terminations in the year	**(6 319)**	(771)
Fair value adjustment	**600**	50
Balance at end of the year	**6 049**	2 915
Variable[1]	**6 049**	2 915

(1) There is no maturity profile for these liabilities as this will depend on policyholder behaviour. Contractually, policyholders may disinvest on demand.

The benefits offered under the Group's unit-linked investment contracts are based on the return of selected equities, debt securities and money market securities. The Group communicates the actual performance of these contracts to its contract holders.

23. TRADE AND OTHER PAYABLES

R million	Group 2013	Group 2012
ABSA Bank Limited	**132**	–
Discovery Unit Trust creditors	**165**	26
Due to reinsurers	**116**	103
Payables and accrued liabilities	**1 004**	827
Payroll creditors	**767**	498
Policyholder unallocated funds	**95**	54
Prudential Assurance Company	**94**	458
– Commission refundable to Prudential Assurance Company	**–**	458
– Corporation tax payable	**94**	–
Standard Bank of South Africa Limited	**343**	–
Straight-lining operating lease payments	**46**	38
Value-added tax	**46**	53
Other creditors	**371**	211
	3 179	2 268
Current	**2 500**	1 997
Non-current	**679**	271
	3 179	2 268

24. DEFERRED INCOME TAX

Deferred tax asset	**370**	348
– Current	**85**	32
– Non-current	**285**	316
Deferred tax liability	**(3 784)**	(3 075)
– Current	**(37)**	(37)
– Non-current	**(3 747)**	(3 038)
	(3 414)	(2 727)
Movement summary		
Balance at beginning of the year	**(2 727)**	(2 288)
Income statement charge	**(549)**	(426)
Deferred tax on cash flow hedge charged to other comprehensive income	**(18)**	(3)
Capital gains taxation on market value adjustments and realised gains charged to other comprehensive income	**(25)**	29
Deferred tax on unrealised translation gains charged to other comprehensive income	**(49)**	–
Exchange differences	**(46)**	(39)
Balance at end of the year	**(3 414)**	(2 727)

24. DEFERRED INCOME TAX continued

Deferred taxation comprises:

R million	Opening balance	Charge for the year	Closing balance
Year ended 30 June 2013			
Assessed loss in Company Policyholders' Fund	**41**	**(1)**	**40**
Assessed loss in subsidiaries	**76**	**13**	**89**
Capital gains tax on unrealised gains on available-for-sale financial instruments	**(19)**	**(25)**	**(44)**
Cash flow hedge	**(2)**	**(18)**	**(20)**
Deferred acquisition costs	**(66)**	**(22)**	**(88)**
Deferred revenue	**6**	**2**	**8**
Difference between accounting and tax balances arising from insurance contracts	**(2 780)**	**(629)**	**(3 409)**
Difference between wear and tear and depreciation	**(26)**	**6**	**(20)**
Fair value hedge	**(15)**	**(21)**	**(36)**
Gains on disposal of intellectual property	**(31)**	**(4)**	**(35)**
Intangibles recognised on acquisition of businesses	**(245)**	**11**	**(234)**
Operating leases	**9**	**2**	**11**
Prepayments	**(18)**	**–**	**(18)**
Provisions	**40**	**12**	**52**
Share-based payments	**69**	**41**	**110**
Unrealised forex gain	**(8)**	**(59)**	**(67)**
Unutilised special transfer balances	**240**	**(3)**	**237**
Other	**2**	**8**	**10**
	(2 727)	**(687)**	**(3 414)**
Year ended 30 June 2012			
Assessed loss in Company Policyholders' Fund	41	–	41
Assessed loss in subsidiaries	63	13	76
Capital gains tax on unrealised gains on available-for-sale financial instruments	(58)	39	(19)
Cash flow hedge	1	(3)	(2)
Deferred acquisition costs	(48)	(18)	(66)
Deferred revenue	4	2	6
Difference between accounting and tax balances arising from insurance contracts	(2 222)	(558)	(2 780)
Difference between wear and tear and depreciation	(33)	7	(26)
Fair value hedge	(9)	(6)	(15)
Gains on disposal of intellectual property	(28)	(3)	(31)
Intangibles recognised on acquisition of businesses	(277)	32	(245)
Operating leases	8	1	9
Prepayments	(12)	(6)	(18)
Provisions	36	4	40
Share-based payments	50	19	69
Unrealised forex gain	–	(8)	(8)
Unutilised special transfer balances	194	46	240
Other	2	–	2
	(2 288)	(439)	(2 727)

24. DEFERRED INCOME TAX continued

R million	Group 2013	Group 2012
Discovery did not recognise deferred tax assets in respect of the following assessable losses:		
Discovery Life – Individual Policyholders' Fund calculated in terms of the four funds approach	**13 789**	12 110
Discovery Insure	**399**	200
Destiny Health (will begin to expire in 2019)	**2 131**	1 603
Prudential Health Limited	**1 408**	986
	17 727	14 899

25. DEFERRED REVENUE

Balance at 1 July	**116**	130
Income deferred	**104**	45
Income recognised through profit or loss	**(70)**	(60)
Foreign currency adjustment on translation	**1**	1
Balance at 30 June	**151**	116
Current	**89**	87
Non-current	**62**	29
	151	116

26. EMPLOYEE BENEFITS

Leave pay

Opening balance	**116**	97
Additional provisions raised	**40**	45
Used during the year	**(18)**	(26)
Closing balance	**138**	116
Current	**123**	104
Non-current	**15**	12
	138	116

27. NET INSURANCE PREMIUM REVENUE

Health	**3 835**	3 641
Recurring premiums	**4 760**	4 209
Reinsurance premiums	**(925)**	(568)
Individual life and invest	**10 779**	8 566
Recurring premiums	**8 195**	6 640
Single premiums	**3 678**	2 951
Reinsurance premiums	**(1 094)**	(1 025)
Group life	**759**	642
Recurring premiums	**964**	800
Reinsurance premiums	**(205)**	(158)
Short-term insurance	**287**	87
Recurring premiums	**296**	91
Reinsurance premiums	**(9)**	(4)
	15 660	12 936
Insurance premium revenue	**17 893**	14 691
Outward reinsurance premiums	**(2 233)**	(1 755)
	15 660	12 936

28. INVESTMENT INCOME

R million	Group 2013	Group 2012
Available-for-sale financial assets:	**216**	116
– Interest	**205**	102
– Dividends	**12**	16
– Investment charges	**(1)**	(2)
At amortised cost interest income	**10**	21
Cash and cash equivalents interest income	**98**	124
	324	261
Attributable to:		
– shareholders	**132**	129
– policyholders	**192**	132
	324	261

29. NET REALISED GAINS ON AVAILABLE-FOR-SALE FINANCIAL ASSETS

Realised gains	**13**	132
– Equity securities	**–**	80
– Debt securities	**13**	19
– Inflation linked securities	**–**	7
– Foreign assets	**–**	22
– Money market securities	**–**	4
Realised losses	**(12)**	(51)
– Equity securities	**–**	(19)
– Debt securities	**(9)**	(13)
– Inflation linked securities	**–**	(3)
– Foreign assets	**–**	(13)
– Money market securities	**(3)**	(3)
	1	81

30. NET FAIR VALUE GAINS ON FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

Investment income	**694**	259
– Interest	**468**	160
– Dividends	**226**	99
Net realised gains	**92**	99
Net fair value gains	**1 476**	636
Investment charges	**(163)**	(257)
	2 099	737

31. NET CLAIMS AND POLICYHOLDERS' BENEFITS

R million	Group 2013	Group 2012
Health insurance claims	**2 612**	2 582
Gross claims	**3 283**	2 995
Less: Reinsurance recoveries	**(671)**	(413)
Individual life insurance claims	**1 895**	1 395
Death	**1 374**	888
Disability	**1 182**	914
Payback benefits	**276**	242
Less: Reinsurance recoveries	**(937)**	(649)
Group life insurance claims	**550**	451
Death	**409**	315
Disability	**319**	274
Less: Reinsurance recoveries	**(178)**	(138)
Individual investment benefits	**1 818**	1 011
Surrenders	**1 631**	874
Guaranteed payments	**46**	27
Annuity payments	**141**	110
Short-term insurance claims	**205**	63
Gross claims	**223**	63
Less: Reinsurance recoveries	**(18)**	–
	7 080	5 502
Claims and policyholders' benefits	**8 884**	6 702
Insurance claims recovered from reinsurers	**(1 804)**	(1 200)
Net claims and policyholders' benefits	**7 080**	5 502

32. ACQUISITION COSTS

Commission expenses	**3 532**	2 863
Movement in deferred acquisition costs (refer to note 7)	**(125)**	(88)
	3 407	2 775

33. MARKETING AND ADMINISTRATION EXPENSES

R million	Group 2013	Group 2012
Marketing and administration expenses comprise:		
Employee costs	**3 966**	3 347
Marketing and distribution costs	**460**	493
IT systems and consumables	**565**	287
Building-related and office costs	**496**	454
Depreciation and amortisation	**230**	185
Vitality benefit costs	**1 493**	1 378
Other costs	**659**	766
	7 869	6 910
Marketing and administration expenses include the following:		
Amortisation of intangible assets (refer to note 7)		
Software	**125**	115
Amortisation of intangible assets from business combination(1)	**186**	152
– acquisition of Standard Life Healthcare	**177**	144
– acquisition of The Vitality Group (refer to note 9)	**9**	8
	311	267
(1) The transactions relating to business combinations are not included in marketing and administration expenses as it is disclosed separately in the income statement.		
Auditors' remuneration		
Audit fees		
– current year	**21**	16
– prior year	**1**	–
Fees for other services	**1**	2
	23	18
Depreciation on property and equipment (refer to note 6)		
Furniture, fittings and equipment	**25**	24
Computer equipment and operating systems	**44**	19
Leasehold improvements	**33**	24
Motor vehicles	**3**	3
	105	70
Employee costs		
Salaries, wages and allowances	**3 113**	2 622
Medical aid fund contributions	**158**	135
Defined contribution provident fund contributions	**140**	120
Social security levies	**86**	65
Share-based payment expenses		
– equity-settled	**–**	5
– cash-settled	**450**	262
– gain on fair value hedge	**(250)**	(85)
Staff training	**21**	17
Recruitment fees	**41**	29
Temporary staff	**59**	55
Provision for leave pay	**38**	41
Other	**110**	81
	3 966	3 347

Directors' and prescribed officers' remuneration is included in employee costs. Refer to Directorate for detailed disclosure.

33. MARKETING AND ADMINISTRATION EXPENSES continued

R million	Group 2013	Group 2012
Operating lease charges		
Land and buildings	**192**	181
Computer and office equipment	**59**	73
	251	254
Professional fees		
Actuarial fees	**2**	2
Technical and other	**258**	192
	260	194
Repairs and maintenance expenditure		
Computer repairs and maintenance	**23**	17
Furniture and equipment maintenance	**1**	1
Office repairs and maintenance	**4**	5
Software maintenance	**239**	117
Motor vehicle repairs and maintenance	*	*
	267	140
Other operating costs		
Impairment of receivables	**3**	88
Foreign exchange losses/(gains) on supplier balances	**16**	(10)

* *Amount is less than R500 000.*

34. SHARE-BASED PAYMENT EXPENSES

34.1 Staff incentive schemes

Discovery operates various share-based payment arrangements. The details of these arrangements are described below:

1. BEE staff share trust

5 290 000 Discovery Limited's shares were issued to the BEE staff share trust for current and future employees. 100 000 additional shares were purchased by the BEE staff share trust during the current year (2012: 725 000), for future allocations to employees. The trust consists of two components; the allocation scheme and the option scheme as described below.

Allocation scheme

Shares have been allocated to senior black employees based on level of seniority and length of past service. The shares vest to employees two, three, four and five years after allocation at a rate of 25% per annum. On each vesting date, the trustees shall distribute to the employees the allocated shares to which the employee may be entitled.

Option scheme

Options granted to black employees may be exercised two, three, four and five years after the option is granted at a rate of 25% per annum. Any options not exercised by the end of the fifth year from the grant date shall lapse. On exercise of the option, the employee pays cash to the trust for the full purchase price of the option.

2. The Vitality Group Inc. stock option plan

Options are granted at fair value price at date of grant. The fair value price was USD 0.55 as per the valuation performed at 30 September 2011. Options vest 33.3% per year for three years and must be exercised within three years of the date that 100% vest otherwise the options expire.

3. The Vitality Group Inc. phantom stock plan

Participants earn a cash bonus based on allocation of bonus scheme units which in turn are linked to the performance of the Vitality Group Inc. share price. The bonus is earned if the participant is employed on each vesting date. For units issued in October 2011, the vesting of the units is two, three and four years or two, three, four and five years after allocation of the bonus units, depending upon the length of service of the employee.

4. The Discovery Limited phantom scheme

Participants earn a cash bonus based on allocation of bonus scheme units which in turn are linked to the performance of the Discovery share price. The bonus is earned if the participant is employed on each vesting date. For units issued in September, the vesting of the units is two, three, four and five years after allocation of the bonus units. The bonus may not be carried forward.

In the calculation of the bonus for units issued, the participants could choose to replicate the economics of a Discovery share or a call option over a Discovery share or a combination of both for the 2005, 2006 and 2007 allocations and only that of a Discovery share for the 2008, 2009, 2011 and 2012 allocations. The 2012 allocation was a pre-determined combination of units that replicate the economics of a Discovery Limited share and units that replicate the economics of a call option over a Discovery Limited share.

5. The PruHealth and PruProtect phantom stock plans

Participants earn a cash bonus based on allocation of bonus scheme units which in turn are linked to a notional PruHealth and PruProtect share price calculated by reference to the embedded value. The bonus is earned if the participant is employed on each vesting date. The vesting of the units is two, three and four years or three, four and five years after allocation of the bonus units, depending upon the length of service of the employee.

6. Acquisition schemes

There are various schemes offered to franchise directors, agents and employees where participants are allocated share units which replicate the economics of a Discovery Limited share. The share units are settled as a cash bonus on vesting. The bonus is earned if the participant is employed on the vesting date. The vesting periods on the schemes vary from two to five years. The bonus may not be carried forward.

The share option schemes mentioned in 1 and 2 on the previous page have been classified as equity-settled schemes and therefore a share-based payment reserve has been recognised.

The schemes mentioned in 3,4,5 and 6 have been classified as cash-settled schemes and a liability is raised in terms of IFRS 2.

The following is a summary of the terms and conditions of the share options granted:

Date granted	Option price	Final vesting date	Shares under option at beginning of year	Options granted during year	Options delivered during year	Options cancelled or adjusted during year	Shares under option at end of year
1. BEE staff share trust							
13/09/2005 to 30/06/2006	R21.47	13/09/2010	35 250	–	(35 250)	–	–
13/09/2005 to 30/06/2006	R0.00	13/09/2010	63 960	–	(52 894)	–	11 066
01/07/2007 to 30/06/2008	R27.40 – R30.00	28/02/2013	157 460	–	(157 460)	–	–
01/07/2007 to 30/06/2008	R0.00	28/02/2013	11 875	–	(11 875)	–	–
01/07/2008 to 30/06/2009	R23.99	31/10/2013	60 000	–	(30 000)	–	30 000
01/07/2008 to 30/06/2009	R0.00	01/04/2014	29 616	–	(14 807)	(4 809)	10 000
01/07/2010 to 30/06/2011	R34.90	30/09/2015	47 277	–	(11 819)	–	35 458
01/07/2010 to 30/06/2011	R0.00	30/03/2016	65 326	–	(15 432)	(33 750)	16 144
01/07/2011 to 30/06/2012	R0.00	30/09/2017	319 382	–	–	(17 936)	301 446
01/07/2012 to 30/06/2013	R0.00	30/09/2018	–	105 228	–	–	105 228
2. The Vitality Group Inc. stock option plan							
01/10/2008	USD0.38	01/10/2012	255 000	–	(245 000)	–	10 000
3. The Vitality Group Inc. phantom stock plan							
01/10/2011	USD0.00	01/10/2015	1 548 459	–	(446 029)	9	1 102 439
01/10/2012	USD0.00	01/10/2016	–	2 579 505	–	–	2 579 505

34. SHARE-BASED PAYMENT EXPENSES continued

Date granted	Option price	Final vesting date	Shares under option at beginning of year	Options granted during year	Options delivered during year	Options cancelled or adjusted during year	Shares under option at end of year
4. The Discovery Limited phantom scheme							
30/09/2006	R22.30	30/09/2011	41 250	–	(41 250)	–	–
30/09/2007	R26.40	30/09/2012	483 553	–	(485 616)	2 063	–
30/09/2007	R0.00	30/09/2012	292 594	–	(291 969)	(625)	–
30/09/2008	R0.00	30/09/2013	1 624 075	–	(818 038)	(20 088)	785 949
01/07/2009	R0.00	30/09/2013	2 210 295	–	(736 766)	–	1 473 529
30/09/2009	R0.00	30/09/2014	2 291 426	–	(774 555)	(84 288)	1 432 583
30/09/2010	R0.00	30/09/2015	3 208 790	–	(816 123)	(99 831)	2 292 836
30/09/2011	R0.00	30/09/2016	3 805 500	–	(23 125)	(38 175)	3 744 200
30/09/2012	R54.75	30/09/2017	–	4 969 455	–	(109 170)	4 860 285
30/09/2012	R0.00	30/09/2017	–	1 656 485	–	(36 390)	1 620 095
5. The PruHealth and PruProtect phantom stock plans							
01/03/2012	GBP14.63	31/10/2015	41 012	–	–	–	41 012
01/03/2012	GBP10.00	31/10/2015	15 000	–	–	–	15 000
6. Acquisition schemes							
01/07/2007 to 30/06/2008	R0.00	30/06/2013	16 376	–	(29 233)	12 857	–
01/07/2008 to 30/06/2009	R0.00	30/06/2014	81 651	–	(49 559)	5 904	37 996
01/07/2009 to 30/06/2010	R0.00	30/06/2015	427 364	–	(384 919)	38 865	81 310
01/07/2010 to 30/06/2011	R0.00	30/06/2016	1 183 429	–	(290 989)	(88 805)	803 635
01/07/2011 to 30/06/2012	R0.00	30/06/2017	1 239 197	–	(196 159)	186 224	1 229 262
01/07/2012 to 30/06/2013	R0.00	30/06/2018	–	975 303	(213 127)	(14 990)	747 186

The fair value of options was calculated at year-end on a Black-Scholes model using the following assumptions:

	Spot price	Exercise price	Option term	Volatility	Dividend yield
BEE staff share trust – originally issued on 13 September 2005	R21.47	R21.47	2 to 5 years	32.7% to 35.5%	–
Phantom scheme and Acquisition scheme – issued on 30 September 2012	R84.06	*	up to 4.25 years	32.7% to 35.5%	2.00
Vitality Group Inc. stock option plan	USD0.375	USD0.375	6.25 years	14.1%	–

* *Refer to table on page 239 for detailed option prices.*

The Phantom schemes and Acquisition schemes are cash-settled and are thus repriced at each reporting date. The fair value of shares granted under these schemes during the current financial year, has been calculated using the closing share price on 30 June 2013 of R84.06.

34.2 Black Economic Empowerment (BEE) transaction and IFRS 2

Discovery concluded a BEE transaction in September 2005 pursuant to which 38 725 909 shares were issued to BEE parties as follows:

BEE parties	Number of shares	Subscription price per share
Dlamini SPV	200 000	0.001
Zilwa SPV	200 000	0.001
WDBIH SPV	17 703 273	0.113
Maphai SPV	1 106 455	1.718
Discovery Foundation	14 226 181	0.001
BEE staff share trust	5 290 000	0.001

The shares issued to the Dlamini SPV and the Zilwa SPV were settled on 15 April 2009 and 9 December 2010 respectively, and are no longer outstanding in terms of the BEE transaction.

Mechanics of the transaction with BEE partners other than BEE staff share trust (BEE parties)

The difference between the market value of the ordinary shares issued to the BEE parties of R715 million and the subscription consideration of R3.9 million represents an outstanding funded amount provided by Discovery shareholders (the funded amount). The BEE parties will provide Discovery and its subsidiaries with a right to purchase, at the end of ten years, such number of ordinary shares at 0.1 cent per share (the par value) that will provide Discovery with a notional return on this funded amount (the Discovery repurchase agreement).

In order to allow the BEE parties to retain the full number of Discovery shares originally issued to them, the BEE parties will have a right to simultaneously acquire from Discovery, at the then 30-day volume-weighted average price per Discovery share, the same number of shares repurchased by Discovery in terms of the Discovery repurchase agreement.

Shares acquired by the BEE parties rank pari passu with existing Discovery shares. The BEE parties have undertaken to utilise any dividend or capital distributions made by Discovery to acquire additional Discovery shares in the market within three months of the date of any distribution.

For purposes of IFRS 2, the transaction has been accounted for based on the fair value of a share option with a similar economic effect. In respect of the WDBIH SPV, the Maphai SPV and the Foundation SPV, the transaction was expensed in full in the 2006 financial year. This fair value was determined using a Black-Scholes model with the following assumptions:

	WDBIH	Maphai	Foundation
Spot price	R21.47	R21.47	R21.47
Exercise price	R81.82	R60.55	R64.21
Option term	10 years	10 years	10 years
Volatility	27.3%	27.3%	27.3%
Dividend yield	0%	0%	0%

For details of staff incentive schemes, refer to note 34.1.

35. FINANCE COSTS

R million	Group 2013	Group 2012
Interest expense on:		
– Bank loan	**41**	47
– Finance charge on negative reserve funding	**124**	66
– Finance lease liability	**5**	–
– Accounts payable balances	**12**	*
– Puttable non-controlling interest liabilities	**165**	152
	347	265

* *Amount is less than R100 000.*

36. FOREIGN EXCHANGE GAINS

Net foreign exchange gains	**40**	78

The net foreign exchange gains arise primarily from the settlement of foreign subsidiary intercompany balances.

37. TAXATION

Charge for the year:		
Current taxation	**645**	646
South African normal taxation	**534**	511
Foreign countries normal taxation	**102**	111
South African capital gains taxation	**9**	24
Deferred taxation	**549**	426
Secondary tax on companies	**–**	60
	1 194	1 132
	%	%
Taxation rate reconciliation		
Effective taxation rate	**35.9**	33.8
Prior year adjustments	**(0.4)**	(2.2)
Subsidiary losses not provided for	**(4.1)**	(2.0)
Capital profits and dividend income	**0.4**	0.7
Secondary tax on companies	**–**	(1.8)
Disallowed expenditure	**(4.0)**	(2.1)
Tax rate decrease in the UK	**0.3**	–
Tax rate differences	**(0.1)**	1.4
Other temporary differences	**0.1**	–
Other permanent differences	**(0.1)**	0.2
Standard rate of taxation	**28.0**	28.0

For South African entities that are in a tax paying position, tax has been provided at 28% (2012: 28%) and secondary tax on companies at 10% (up to 31 March 2012) in the financial statements.

Current taxation relating to Discovery Life is determined by applying the four fund method of taxation applicable to life insurers.

38. EARNINGS PER SHARE

	Group 2013	Group 2012
Basic earnings per share		
Earnings per share is based on net profit after tax attributable to ordinary shareholders and the weighted number of ordinary shares in issue.		
Earnings attributable to ordinary shareholders (R million)	**2 063**	2 199
Weighted number of ordinary shares in issue (000's)	**554 165**	554 930
Basic earnings per share (cents)	**372.2**	396.1
Diluted earnings per share		
Diluted earnings per share is calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. Discovery has two categories of dilutive potential ordinary shares namely:		
– shares issued from the staff share trusts which have not been delivered to participants		
– shares issued to BEE parties		
Weighted average ordinary shares in issue (000's) adjusted for:	**554 165**	554 930
– Weighted average ordinary shares in the staff share trusts (000's)	**467**	486
– Weighted average ordinary shares issued to BEE parties (000's)	**7 211**	122
	561 843	555 538
Diluted earnings per share (cents)	**367.1**	395.7
Headline earnings		
Headline earnings per share is based on the net profit after tax attributable to ordinary shareholders adjusted for items of a capital nature and the weighted average number of ordinary shares in issue.		
Headline earnings reconciliation (R million)		
Earnings attributable to ordinary shareholders	**2 063**	2 199
Adjusted for:		
– Realised gains on available-for-sale financial instruments	**(1)**	(81)
– Capital gains tax on realised profit on available-for-sale financial instruments	*	11
Headline earnings	**2 062**	2 129
Headline earnings per share (cents):		
– Undiluted	**372.0**	383.7
– Diluted	**367.0**	383.2
Normalised headline earnings (R million)		
Headline earnings	**2 062**	2 129
– Recapture of reinsurance	**336**	–
– Amortisation of intangibles from business combinations[1]	**186**	152
– Tax on amortisation of intangibles from business combinations	**(55)**	(83)
– Fair value adjustment to puttable non-controlling interest financial liability[2]	**133**	13
– Finance costs raised on puttable non-controlling interest financial liability[2]	**165**	152
– Non-controlling interest allocation if no put options	**(40)**	(14)
– Final dividend accrued for preference shareholders	*	(33)
Normalised headline earnings	**2 787**	2 316
Normalised headline earnings per share (cents):		
– Undiluted	**502.9**	417.3
– Diluted	**496.0**	416.9

(1) Refer to note 33.

(2) Refer to note 19 for detail of puttable non-controlling interests.

* *Amount is less than R500 000.*

39. CASH FLOW INFORMATION

R million	Group 2013	Group 2012
39.1 Cash generated by operations		
Profit before taxation	**3 325**	3 354
Adjusted for:		
Investment income	**(855)**	(520)
Realised investment gains and losses	**(93)**	(180)
Financing costs	**347**	265
Premiums, claims and investment charges for liabilities under investment contracts	**982**	802
Non-cash items:		
Amortisation of software	**125**	115
Amortisation of intangibles from business combinations	**186**	152
Deferred acquisition costs	**(125)**	(88)
Deferred revenue	**34**	35
Depreciation	**105**	70
Gain on fair value hedge	**(250)**	(84)
(Profit)/Loss from associates	**22**	(1)
Operating lease payments in advance	**8**	3
Provision for bad debts	**(22)**	51
Provision for employee incentive schemes	**2**	10
Provision for employee benefits	**22**	19
Puttable non-controlling interest fair value adjustment	**133**	13
Share-based payment expenses	**450**	267
Transfer to liabilities under reinsurance contracts	**44**	133
Transfer to assets/liabilities under insurance contracts	**1 691**	942
Fair value adjustment to liabilities under investment contracts	**600**	50
Translation differences	**32**	(27)
Unearned premiums	**(2)**	(68)
Unrealised gains on foreign exchange	**(35)**	–
Unrealised gains on investments at fair value through profit or loss	**(1 476)**	(636)
Other	**–**	2
Working capital changes:		
Loans and receivables including insurance receivables	**(785)**	156
Trade and other payables	**1 765**	566
	6 230	5 401
39.2 Taxation paid		
Balance at beginning of the year	**(53)**	–
Taxation charged for the year in the income statement	**(1 194)**	(1 132)
Adjustment for movement in deferred taxation	**549**	426
Taxation recoverable from consortium relief – PruHealth	**102**	160
Taxation charged to other comprehensive income	**(4)**	–
Interest received from SARS	**2**	1
Balance at end of the year	**15**	53
Taxation paid	**(583)**	(492)
Taxation received from consortium relief	**212**	–
Net taxation paid	**(371)**	(492)
39.3 Proceeds from issuance of shares		
Preference shares issued in Discovery Insure Limited	**77**	6
Preference shares issued in Discovery Limited	**–**	800
Ordinary shares issued in The Vitality Group LLC to non-controlling interest	**1**	5
Ordinary shares issued in PruHealth to non-controlling interest	**–**	23
	78	834

R million	Group 2013	Group 2012
39.4 Repayment of borrowings		
Balance at beginning of the year	**402**	402
Assets purchased on finance lease	**53**	–
Investments purchased on bank overdraft facility	**216**	–
Balance at end of the year	**(660)**	(402)
	11	–

40. DIVIDENDS PER SHARE

40.1 Dividends per ordinary share

The dividends paid in 2013 totalled R672 million and comprised a final dividend of 53.5 cents per share paid on 15 October 2012 and an interim dividend of 60 cents per share paid on 25 March 2013.

The dividends paid in 2012 totalled R580 million and comprised a final dividend of 48 cents per share paid on 17 October 2011 and an interim dividend of 50 cents per share paid on 26 March 2012.

40.2 Dividends per preference share

The dividends paid in 2013 totalled R68 million and comprised a final dividend of 414,73973 cents per share paid on 25 September 2012 and an interim dividend of 431,23288 cents per share paid on 18 March 2013.

The dividends paid in 2012 totalled R23 million and comprised an interim dividend of 289,23 cents per share paid on 19 March 2012.

41. COMMITMENTS

41.1 Capital commitments

Capital expenditure approved but not contracted for at the reporting date is as follows:		
Property and equipment	**46**	58
Intangible assets	**145**	118
	191	176

41.2 Operating lease commitments

Discovery has various operating lease agreements. Most leases contain renewal options. Lease terms do not contain restrictions on Discovery's activities concerning dividends, additional debt or further leasing.

Discovery leases certain land and buildings under operating leases. The remaining periods of the leases are from nine months to eight years. The future minimum commitments in terms of the leases of land and buildings, including Discovery's operational head office are as follows:

Due within one year	**168**	162
Due within two to five years	**491**	460
Due after five years	**25**	26
Cash flow commitment	**684**	648
Accrued to a liability (refer to note 23)	**(46)**	(38)
Net commitment	**638**	610

Discovery leases certain computer and office equipment under operating leases. The remaining periods of the leases are from one month to five years. The future minimum commitments are as follows:

Due within one year	**65**	77
Due within two to five years	**119**	151
Cash flow commitment	**184**	228

42. CONTINGENCIES

The Group is exposed to the following contingencies at 30 June 2013:

- Discovery Health has provided a guarantee on behalf of Saldosat Investments Proprietary Limited for the amount of R20 million for the purchase of a property in Longlake, Modderfontein, Johannesburg. The advance under the guarantee will be secured, inter alia, by mortgage of the property purchased.
- A claim of USD 14 million has been instituted for fees, ongoing compensation and damages, against The Vitality Group by a consulting company for services allegedly rendered. The Vitality Group believes that the claim is without merit and is defending the matter. Further, The Vitality Group has filed two counter claims totalling USD 2 million in this matter.

43. RELATED PARTIES

List of related parties as defined:

Subsidiaries

Details of subsidiaries directly owned by Discovery are contained in Company note 1.

Associates and Joint Ventures

Details of Discovery's associates and joint ventures are contained in notes 9 and 10 respectively.

Corporate investors

RMI Holdings Limited has a 25.01% shareholding in Discovery Limited. Included in the RMI Holdings group structure are the following subsidiaries which are also considered to be related parties:

- OUTsurance Holdings Limited
- RMBSI Investments Proprietary Limited

Discovery did not enter into any transactions with these related parties during the current or prior financial year.

Key management personnel

Key management personnel have been defined as directors of Discovery Limited, Discovery Health Proprietary Limited and Discovery Life Limited, as these businesses constitute the majority of the Discovery Group.

A list of the directors and prescribed officers of Discovery Limited can be found on page 258.

It is not considered necessary to disclose details of key management family members and their influenced or controlled separate entities. To the extent specific transactions have occurred between Discovery and these related parties (as defined in IAS 24) the details are included in the aggregate disclosure contained below under key management and where significant, full details of all relationships and terms of the transactions are provided.

Transactions with related parties

For purposes of this section Discovery Limited will be referred to as the Company and where relevant, amounts are excluding VAT.

Discovery Health Medical Scheme (DHMS)

Discovery Health administers DHMS and provides managed care services for which it charges an administration fee and a managed healthcare fee respectively. These fees are determined on an annual basis and approved by the trustees of DHMS. The fees totalled R3 714 million (2012: R3 408 million). Discovery offers the members of DHMS access to the Vitality programme.

Interest between Discovery and DHMS is calculated at call rates on the daily outstanding balance. Interest paid to DHMS amounted to R77 016 (2012: R71 722).

Discovery Third Party Recovery Services (DTPRS) paid DHMS R19.8 million (2012: R15 million) to purchase all the risks and rewards of ownership to the claims due from the Road Accident Fund up to 31 December 2012 (2012: up to 31 December 2011).

DTPRS also provides a service to DHMS to recover all claims that are due from the Compensation for Occupational Injuries and Diseases. DTPRS received R9.1 million (2012: R8.7 million) for this service.

DHMS owes Discovery R415 million (2012: R401 million) at year-end.

In the prior financial year, Discovery Health provided a guarantee to DHMS to settle amounts due from members, service providers and brokers in the event that these debtors default. At 30 June 2012 the value of this guarantee totaled R111 million and Discovery Health raised a provision of R40 million in respect of possible defaults. This guarantee has been settled in the current financial year.

Closed schemes

Discovery Health administers the following restricted membership medical schemes:

- Altron Medical Scheme
- Anglovaal Group Medical Scheme
- IBM Medical Scheme (amalgamated with DHMS on 1 July 2013)
- LA Health Medical Scheme
- Lonmin Medical Scheme
- Naspers Medical Scheme
- Quantum Medical Aid Society
- Remedi Medical Scheme
- Retail Medical Scheme
- Tsogo Sun Group Medical Scheme
- TFG Medical Aid Scheme
- University of KwaZulu-Natal Medical Scheme

Discovery Health charges these schemes administration fees which are determined on an annual basis and approved by the trustees of the respective closed schemes. The fees totalled R342 million (2012: R256 million). Amounts due to Discovery at year-end totalled R34 million (2012: R31 million).

Discovery Consulting Services

Discovery has established a network of 27 franchises in order to establish a national footprint for its products. Discovery has paid R227 million (2012: R255 million) in fees to the franchises.

The Discovery Consulting Services participate in the Acquisition Scheme. Refer to note 34 for further details. During the year, R14 million (2012: R7 million) was accrued for in terms of this scheme.

The Discovery Foundation

The Discovery Foundation was launched in 2006 and is an independent shareholder of Discovery, with its own trustees. It forms one arm of Discovery's Black Economic Empowerment transaction. The principal aim of the Discovery Foundation is to invest in the education and training of medical specialists and the development of academic and research centers, with particular focus on those areas with greatest need.

The Discovery Foundation received contributions from Discovery of R15 million during the year (2012: R13.1 million). Discovery also paid a management fee of R2 million (2012: R2 million).

The Discovery Fund

A fund for sustainable non-governmental healthcare projects, especially in primary healthcare. These projects complement the delivery of primary and preventative care in the public sector and help to relieve the burden on state facilities.

The Discovery Fund received contributions from Discovery of R16.3 million during the year (2012: R14.3 million). Discovery also paid a management fee of R1 million (2012: R1 million).

Discovery staff retirement funds

A pension and provident fund has been set-up specifically for the Discovery staff. Contributions made to this fund during the year amounted to R112 million (2012: R120 million). The pension and provident fund has invested R417 million (2012: R345 million) in Discovery Invest Target Retirement Funds.

43. RELATED PARTIES continued

Key management personnel of Discovery Limited, families of key management (as defined in IAS 24) and entities significantly influenced or controlled by key management

(i) Discovery Limited key management personnel's compensation, paid by the Company or on behalf of the Company for services rendered to Discovery Limited, is detailed in the Directorate on pages 258 and 259.

(ii) Aggregate details of insurance, annuity and investment transactions between Discovery Limited, any subsidiary, associate or joint venture of Discovery Limited and key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management:

Insurance contracts

	Aggregate insured cover		Premiums received		Claims paid	
R'000	**2013**	2012	**2013**	2012	**2013**	2012
Life insurance	**473 909**	457 621	**2 822**	2 137	**–**	–
Short-term insurance	**272 584**	247 382	**1 137**	886	**664**	79

Investment contracts

	Investment value		Premiums received		Investment returns	
R'000	**2013**	2012	**2013**	2012	**2013**	2012
Investment contacts	**43 063**	10 368	**28 238**	1 596	**4 458**	657

(iii) Aggregate details of transactions between PruHealth and key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management:

PruHealth health insurance

	Premiums received		Claims paid	
R'000	**2013**	2012	**2013**	2012
Health insurance	**15**	26	**185**	100

(iv) Aggregate details of transactions between Discovery Vitality Proprietary Limited and key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management:

Vitality loyalty programme

	Premiums received		Amounts paid	
R'000	**2013**	2012	**2013**	2012
Vitality benefits	**24**	23	**301**	385

DiscoveryCard

	Card fees received		Discounts paid	
R'000	**2013**	2012	**2013**	2012
DiscoveryCard	**152**	116	**93**	112

Key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management accrued 228 576 Discovery miles as part of the DiscoveryCard loyalty programme for the year ended 30 June 2013 (2012: 235 394).

(v) Loans from subsidiary companies to key management personnel amounted to R15.2 million at 30 June 2013 (2012: R14.7 million). Interest received on these loans amounted to R0.7 million (2012: R0.6 million).

(vi) Aggregate shareholdings of key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management, in Discovery Limited as at 30 June 2013 was 91 561 063 ordinary shares (2012: 101 459 202 ordinary shares).

(vii) Loans from share trusts to key management personnel amounted to R84 million at 30 June 2012. These loans were repaid in full in the current financial year. Interest received on these loans amounted to R2 million (2012: R6 million).

(viii) During the prior financial year, 200 000 ordinary shares were allocated to key management personnel by the BEE Share Trust. The shares issued vest in four equal tranches, two, three, four and five years after allocation of the shares, subject to key management personnel still being employed on each vesting date.

(ix) During the current financial year the following transactions occurred between Discovery and key management personnel, their families (as defined in IAS 24) and entities significantly influenced or controlled by key management:

- Discovery acquired paintings to the value of R1.2 million (2012: less than R500 000) from a company controlled by a family member of key management personnel.
- Sponsorship and enterprise development grants to the value of R1.5 million were made to organisations where members of key management personnel have significant influence.
- Discovery paid R1 million in legal fees to a company in which a non-executive director of Discovery has significant influence.

44. EVENTS AFTER REPORTING DATE

Ping An Health

Subject to exchange control and regulatory approval, Discovery will purchase a further 5% in Ping An Health for RMB 82.2 million.

Discovery Insure

In August 2013, Discovery Insure's preference shareholders agreed to sell its 25% shareholding in Discovery Insure Limited to Discovery Limited for R352 million, relative to R182 million invested by these shareholders to date. The transaction is subject to regulatory approval and is expected to be settled towards the end of 2013.

B preference share cash dividend declaration

On 29 August 2013, the directors declared a final gross cash dividend of 421,50685 cents (358,28082) cents net of dividend withholding tax) per B preference share for period 1 January 2013 to 30 June 2013. The dividend was declared from income reserves and no secondary tax on companies' credits has been used. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued preference share capital at the declaration date is 8 million B preference shares.

The salient dates for the dividend were as follows:

Last day of trade to receive a dividend	Friday, 13 September 2013
Shares commence trading "ex" dividend	Monday, 16 September 2013
Record date	Friday, 20 September 2013
Payment date	Monday, 23 September 2013

B preference share certificates may not be dematerialised or rematerialised between Monday, 16 September 2013 and Friday, 20 September 2013, both days inclusive.

Ordinary share cash dividend declaration

On 3 September 2013, the directors declared a final gross cash dividend of 64,5 cents (54,825 cents net of dividend withholding tax) per ordinary share for the year ended 30 June 2013. The dividend was declared from income reserves and no secondary tax on companies' credits has been used. A dividend withholding tax of 15% will be applicable to all shareholders who are not exempt.

The issued ordinary share capital at the declaration date is 591 872 390 ordinary shares.

The salient dates for the dividend were as follows:

Last day of trade to receive a dividend	Friday, 4 October 2013
Shares commence trading "ex" dividend	Monday, 7 October 2013
Record date	Friday, 11 October 2013
Payment date	Monday, 14 October 2013

Share certificates may not be dematerialised or rematerialised between Monday, 7 October 2013 and Friday, 11 October 2013, both days inclusive.

COMPANY STATEMENT OF FINANCIAL POSITION

at 30 June 2013

R million	Notes	**Company 2013**	Company 2012
Assets			
Investments in subsidiaries	1	**5 271**	4 451
Investment in associate	2	**263**	247
Financial assets			
– Money market	4	**539**	429
– Derivatives	9	**13**	–
– Loans and receivables		**39**	–
Loan to share incentive trust	5	**–**	99
Loan to subsidiary	6	**871**	701
Cash and cash equivalents	13.3	*****	2
Total assets		**6 996**	5 929
Equity			
Capital and reserves			
Ordinary share capital and share premium	7.1	**1 744**	1 744
Perpetual preference share capital	7.2	**779**	779
Other reserves		**319**	298
Retained earnings		**3 144**	1 476
Total equity		**5 986**	4 297
Liabilities			
Financial liabilities			
– Borrowings at amortised cost	8	**402**	402
– Derivatives	9	**8**	20
Deferred income tax	10	**65**	24
Trade and other payables		**530**	1 184
Current income tax liabilities		**5**	2
Total liabilities		**1 010**	1 632
Total liabilities and equity		**6 996**	5 929

* *Amount is less than R500 000.*

COMPANY STATEMENT OF COMPREHENSIVE INCOME

for the year ended 30 June 2013

R million	Notes	Company 2013	Company 2012
Investment income	11	**1 957**	676
Marketing and administration expenses		**(19)**	(39)
Net impairment of investment in subsidiaries	12	**421**	103
Profit from operations		**2 359**	740
Finance costs		**(40)**	(42)
Foreign exchange gains		**135**	110
Profit before tax		**2 454**	808
Taxation		**(46)**	(101)
Profit for the year		**2 408**	707
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss:			
Change in available-for-sale financial assets		**2**	–
– unrealised gains		**2**	–
– capital gains tax on unrealised gains		**	–
Cash flow hedges		**19**	(14)
– unrealised gains/(losses)		**17**	(27)
– deferred tax on unrealised gains/losses		**(1)**	8
– current tax on unrealised gains/losses		**(4)**	–
– losses recycled to profit or loss		**9**	7
– tax on losses recycled to profit or loss		**(2)**	(2)
Other comprehensive income for the year, net of tax		**21**	(14)
Total comprehensive income for the year		**2 429**	693

* *Amount is less than R500 000.*

COMPANY STATEMENT OF CASH FLOWS

for the year ended 30 June 2013

R million	Notes	Company 2013	Company 2012
Cash flow from operating activities		**1 261**	839
Cash generated by operations	13.1	**(613)**	314
Dividends received		**1 896**	606
Interest received		**26**	29
Interest paid		**(40)**	(42)
Taxation paid	13.2	**(8)**	(68)
Cash flow from investing activities		**(523)**	(924)
Increase investment in subsidiary		**(507)**	(498)
Increase investment in associate		**(16)**	(22)
Purchase of financial investment		**–**	(429)
Decrease in loan to share incentive trust		**–**	25
Cash flow from financing activities		**(740)**	176
Proceeds from issuance of preference shares		**–**	800
Share issue costs		**–**	(21)
Dividends paid to ordinary shareholders		**(672)**	(580)
Dividends paid to preference shareholders		**(68)**	(23)
Net (decrease)/increase in cash and cash equivalents		**(2)**	91
Cash and cash equivalents at beginning of the year		**2**	(89)
Cash and cash equivalents at end of the year	13.3	*	2

* *Amount is less than R500 000.*

COMPANY STATEMENT OF CHANGES IN EQUITY

for the year ended 30 June 2013

R million	Share capital	Share premium	Preference share capital	Hedging reserve	Share-based payment reserve	Revaluation reserve*	Retained earnings	Total
Year ended 30 June 2012								
At beginning of the year	1	1 743	–	12	300	–	1 372	3 428
Profit for the year	–	–	–	–	–	–	707	707
Other comprehensive income	–	–	–	(14)	–	–	–	(14)
Total comprehensive income for the year	–	–	–	(14)	–	–	707	693
Transactions with owners:								
Issue of capital	–	–	800	–	–	–	–	800
Share issue costs	–	–	(21)	–	–	–	–	(21)
Dividends paid to ordinary shareholders	–	–	–	–	–	–	(580)	(580)
Dividends paid to preference shareholders	–	–	–	–	–	–	(23)	(23)
Total transactions with owners	–	–	779	–	–	–	(603)	176
Balance at 30 June 2012	1	1 743	779	(2)	300	–	1 476	4 297
Year ended 30 June 2013								
At beginning of the year	**1**	**1 743**	**779**	**(2)**	**300**	**–**	**1 476**	**4 297**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**–**	**2 408**	**2 408**
Other comprehensive income	**–**	**–**	**–**	**19**	**–**	**2**	**–**	**21**
Total comprehensive income for the year	**–**	**–**	**–**	**19**	**–**	**2**	**2 408**	**2 429**
Transactions with owners:								
Dividends paid to ordinary shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**(672)**	**(672)**
Dividends paid to preference shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**(68)**	**(68)**
Total transactions with owners	**–**	**–**	**–**	**–**	**–**	**–**	**(740)**	**(740)**
Balance at 30 June 2013	**1**	**1 743**	**779**	**17**	**300**	**2**	**3 144**	**5 986**

* *This reserve relates to the revaluation of available-for-sale financial assets.*

1. INVESTMENTS IN SUBSIDIARIES

	Issued ordinary capital R million		Effective percentage holding %		Investment in subsidiaries[3] R million		Amounts owing to subsidiary[4] R million	
	2013	2012	**2013**	2012	**2013**	2012	**2013**	2012
Discovery Life	**1 416**	1 416	**100**	100	**1 697**	1 697	**–**	–
Discovery Health	**271**	271	**100**	100	**469**	469	**521**	1 169
Discovery Vitality	*	*	**100**	100	**7**	7	**–**	–
Discovery Vitality International Asia	**32**	–	**100**	–	**26**	–	**–**	–
Discovery Life Investment Services	**3**	3	**100**	100	**3**	3	**–**	–
Discovery Life Collective Investments	**15**	15	**100**	100	**15**	15	**–**	–
Discovery Insure	**411**	181	**100**	100	**111**	29	**–**	–
Destiny Health Inc.[1]	**1 574**	1 438	**99**	99	**–**	–	**–**	–
Discovery Group Europe Limited[2]	**2 943**	2 943	**100**	100	**2 943**	2 231	**–**	–
					5 271	4 451	**521**	1 169

* *Amount is R1 000.*

(1) Incorporated in the United States of America.

(2) Previously Discovery Offshore Holdings Limited, incorporated in England and Wales.

(3) Investments in subsidiaries includes cost less impairments and the value of share options issued to subsidiary staff.

(4) Included in trade and other payables.

Discovery Limited has pledged its share investment in Discovery Life Limited as security for the borrowings raised. See Company note 8 for details of the borrowings.

R million	**Company 2013**	Company 2012
2. INVESTMENT IN ASSOCIATE		
Investment in Ping An Health	**263**	247
Refer to Group note 9 for detailed disclosure of the investment in associate.		
3. INVESTMENT IN JOINT VENTURE		
Refer to Group note 10 for detailed disclosure of the investment in joint venture.		
4. FINANCIAL ASSETS – INVESTMENTS		
Available-for-sale money market investment	**539**	429

The investment portfolio consists of local, listed money market securities and bears interest at a floating rate. This investment has been measured at fair value and is classified as Level 1 using the fair value hierarchy. Level 1 includes financial instruments that are measured using unadjusted, quoted prices in an active market for identical financial instruments.

Maturity analysis

The following table presents a maturity analysis based on the remaining contractual maturities:

R million	Total	<1 year	1 – 5 years	5 – 10 years	>10 years	Open ended
Money market investment	**539**	–	–	–	–	**539**

Credit exposure

The following table provides information regarding the credit risk exposure categorised by credit ratings:

R million	Total	AA+AA AA-
Money market investment	**539**	**539**

5. LOAN TO SHARE INCENTIVE TRUST

R million	Company 2013	Company 2012
Loan to share incentive trust	**99**	117
Decrease in loan	**(101)**	(25)
Interest received	**2**	7
	–	99

6. LOAN TO SUBSIDIARY

Loan to Discovery Group Europe Limited	**701**	563
Exchange differences	**135**	106
Interest receivable	**35**	32
	871	701

The loan consists of two tranches of GBP 35.5 million and GBP 14.5 million, repayable on 7 September 2017 and 23 December 2015 respectively and carry interest at 400 base points above LIBOR.

7. SHARE CAPITAL AND SHARE PREMIUM

7.1 Ordinary share capital and share premium

Authorised		
1 billion ordinary shares with a par value 0.1 cent per share	**1 000**	1 000
Issued		
591 872 390 ordinary shares with a par value 0.1 cent per share	**1**	1
Share premium	**1 743**	1 743
At 30 June	**1 744**	1 744

7.2 Perpetual preference share capital

Authorised		
20 000 000 class B voluntarily redeemable non-convertible preference shares of R100 each	**2 000**	2 000
Issued		
8 000 000 class B voluntarily redeemable non-convertible preference shares of R100 each	**800**	800
Share issue costs	**(21)**	(21)
At 30 June	**779**	779

The preference shares are non-cumulative, non-participating, non-convertible, voluntarily redeemable no par value preference shares and were issued at a coupon rate of 85% of prime rate. With the introduction of dividend withholding tax on 1 April 2012, the coupon rate on the preference shares was increased to 100% of the prime rate.

8. BORROWINGS AT AMORTISED COST

R million	Company 2013	Company 2012
Bank borrowings	**402**	402
Current	**2**	2
Non-current	**400**	400
	402	402

Bank borrowings

In order to fund the acquisition of Standard Life Healthcare, Discovery borrowed R400 million from FirstRand Bank Limited. The salient terms of the loan are the following:

Lender:	FirstRand Bank Limited
Type of borrowings:	Senior debt
Interest rate:	Floating
Security:	Pledge of shares in Discovery Life Limited
Maturity date:	10 September 2017
Callable/Convertible:	Not applicable

The borrowings are repayable on maturity. Interest is paid quarterly. The interest rate has been fixed through interest rate swaps.

The loan agreement imposes certain restrictions on Discovery's operations, including a limitation on total borrowings. A breach of these restrictions would require immediate repayment of any outstanding balance.

Undrawn borrowing facilities

The Company has undrawn committed floating rate borrowing facilities totalling R800 million, expiring 30 June 2014.

9. DERIVATIVE FINANCIAL INSTRUMENTS

R million	2013 Assets	2013 Liabilities	2012 Assets	2012 Liabilities
Collar option	**13**	**–**	–	–
Interest rate swap	**–**	**8**	–	20
	13	**8**	–	20
Current	**13**	**–**	–	8
Non-current	**–**	**8**	–	12
	13	**8**	–	20

Refer to page 205 and 208 for a detailed description of the derivative financial instruments listed above.

10. DEFERRED INCOME TAX

R million	Company 2013	Company 2012
Deferred tax asset	–	6
– Current	–	2
– Non-current	–	4
Deferred tax liability	**(65)**	(30)
– Non-current	**(65)**	(30)
	(65)	(24)
Movement summary:		
Balance at beginning of the year	**(24)**	–
Deferred tax on cash flow hedge charged to other comprehensive income	**(3)**	6
Deferred tax on unrealised foreign exchange gains on loan to subsidiary	**(38)**	(30)
Balance at end of the year	**(65)**	(24)
Deferred taxation comprises:		
Capital gains tax on unrealised gains on available-for-sale financial instruments	*	–
Cash flow hedge	**2**	5
Unrealised forex gain	**(67)**	(29)
	(65)	(24)

* *Amount is less than R500 000.*

11. INVESTMENT INCOME

Available-for-sale interest income	**23**	30
Dividends received from subsidiaries	**1 896**	606
At amortised cost interest income	**35**	40
Cash and cash equivalents interest income	**3**	–
	1 957	676

12. NET IMPAIRMENT OF INVESTMENTS IN SUBSIDIARIES

Destiny Health Inc.	**136**	12
Discovery Insure	**149**	152
Discovery Vitality Asia	**6**	–
	291	164
Discovery Group Europe Limited – impairment reversed	**(712)**	(267)
	(421)	(103)

13. CASH FLOW INFORMATION

R million	Company 2013	Company 2012
13.1 Cash generated by operations		
Profit before taxation	**2 454**	808
Adjusted for:		
Investment income	**(1 957)**	(676)
Finance costs	**40**	42
Unrealised foreign exchange gain	**(135)**	(106)
Non-cash items:		
Impairment of investments in subsidiaries	**(421)**	(103)
Working capital changes:		
Loans and receivables	**60**	–
Trade and other payables	**(654)**	349
	(613)	314
13.2 Taxation paid		
Balance at beginning of the year	**(2)**	(1)
Taxation charged for the year in the statement of comprehensive income	**(50)**	(101)
Adjustment for movement in deferred taxation	**38**	30
Amount due from SARS transferred from subsidiary	**1**	2
Balance at end of the year	**5**	2
	(8)	(68)
13.3 Cash and cash equivalents		
Cash at bank and in hand	*	1
Short-term deposits	–	1
	*	2

* *Amount is less than R500 000.*

14. CONTINGENCIES

Discovery Limited has provided the following guarantees:

- Discovery Limited has provided a guarantee in favour of HSBC Bank in the amount of USD 5 million for the working capital facility of Destiny Health Inc.
- In terms of the shareholders' agreement between Discovery Group Europe Limited, The Prudential Assurance Company Limited and Prudential Health Limited, Discovery Limited has guaranteed the obligations of Discovery Group Europe Limited to The Prudential Assurance Company Limited and Prudential Health Limited in terms of this agreement.
- Discovery Health Proprietary Limited provides certain administration and ancillary services to PruHealth in terms of the Insurance Intermediary Services agreement. Discovery Limited has guaranteed the obligations of Discovery Health Proprietary Limited in terms of this agreement.
- PruHealth has provided certain volume guarantees to its reinsurance providers. Discovery Limited has guaranteed these obligations.
- In terms of the Master Relationship Agreement with Humana Inc., Discovery Limited has guaranteed the obligations of The Vitality Group LLC to Humana Inc.
- In terms of the Joint Venture Agreement with AIA Company Limited, Discovery Limited has guaranteed the obligations of Discovery Vitality International Asia Private Limited to AIA Company Limited in terms of this agreement.

15. SPECIAL RESOLUTIONS

The following special resolutions were approved during the financial year at the Annual General Meeting of shareholders held on Tuesday, 4 December 2012:

Special Resolution Number 1

Basis for calculating the remuneration of the non-executive directors for services as directors of the Company for the financial year ending 30 June 2013.

Special Resolution Number 2

The Company and or any of its subsidiaries are authorised by way of a renewable general approval to purchase the ordinary shares of the Company, upon such terms and conditions and in such amounts as determined from time to time by directors of the Company subject to the Memorandum of Incorporation (MOI) of the Company and limitations of the JSE Listings Requirements.

Special Resolution Number 3

To the extent required by the Companies Act, the Board of Directors of the Company may, subject to compliance with the requirements of the Company's MOI, the Companies Act and the JSE Listings Requirements, each as presently constituted and as amended from time to time, authorise the Company to provide direct or indirect financial assistance as contemplated in section 44 and/or section 45 of the Companies Act by way of loans, guarantees, the provision of security or otherwise.

Special Resolution Number 4

To change the name of the Company from Discovery Holdings Limited to Discovery Limited.

Special Resolution Number 5

To adopt a new Memorandum of Incorporation.

16. EVENTS AFTER REPORTING DATE

Refer to Group note 44 for a detailed list of the events after reporting date.

DIRECTORATE

for the year ended 30 June 2013

DISCOVERY HOLDINGS DIRECTORS AND PRESCRIBED OFFICERS

Executive directors

A Gore
R Farber
HD Kallner
NS Koopowitz
HP Mayers
Dr A Ntsaluba
A Pollard
JM Robertson
B Swartzberg

Non-executive directors

MI Hilkowitz
Dr BA Brink
P Cooper
JJ Durand
SB Epstein
Dr TV Maphai
V Mufamadi (resigned 4 December 2012)
AL Owen
SE Sebotsa
T Slabbert
SV Zilwa

Prescribed officers

J Broomberg
K Rabson
P Tlhabi

Company secretary

M J Botha
155 West Street, Sandton
PO Box 786722, Sandton, 2146

REMUNERATION AND FEES

Payments to directors for the year ended 30 June 2013 for services rendered are as follows:

R'000	Services as directors	Basic salary	Performance bonus	Phantom scheme bonus	Provident fund contributions	Other benefits[1]	Total
Executive							
A Gore	–	3 876	5 163	3 090	581	136	12 846
R Farber	–	3 171	3 463	5 424	158	74	12 290
HD Kallner	–	3 268	4 002	10 022	163	87	17 542
NS Koopowitz	732	10 134	10 887	–	579	163	22 495
HP Mayers	–	5 604	6 361	8 236	661	215	21 077
Dr A Ntsaluba	–	2 920	2 435	–	510	89	5 954
A Pollard	–	3 699	1 731	6 078	169	134	11 811
JM Robertson	–	2 779	4 244	5 021	564	60	12 668
B Swartzberg	–	3 431	4 751	7 979	452	89	16 702
Sub-total	732	38 882	43 037	45 850	3 837	1 047	133 385
Prescribed officers							
J Broomberg	–	3 218	4 382	8 200	241	76	16 117
K Rabson	–	2 703	4 118	10 027	337	217	17 402
P Tlhabi	–	2 378	2 013	3 548	128	58	8 125
Sub-total	–	8 299	10 513	21 775	706	351	41 644
Non-executive							
MI Hilkowitz	2 663	–	–	–	–	–	2 663
Dr BA Brink[2]	409	–	–	–	–	–	409
P Cooper[3]	767	–	–	–	–	–	767
JJ Durand[4]	497	–	–	–	–	–	497
SB Epstein[5]	1 505	–	–	223	–	–	1 728
Dr TV Maphai	273	–	–	–	–	–	273
V Mufamadi	137	–	–	–	–	–	137
AL Owen	1 505	–	–	–	–	–	1 505
SE Sebotsa	557	–	–	2 682	–	–	3 239
T Slabbert[6]	544	–	–	–	–	–	544
SV Zilwa	849	–	–	–	–	–	849
Sub-total	9 706	–	–	2 905	–	–	12 611
Total	10 438	47 181	53 550	70 530	4 543	1 398	187 640
Less: paid by subsidiaries	(10 438)	(47 181)	(53 550)	(70 530)	(4 543)	(1 398)	(187 640)
Paid by holding company	–	–	–	–	–	–	–

(1) "Other benefits" comprise medical aid contributions, travel and other allowances.
(2) R223 000 of the director's fees for services rendered by Dr BA Brink were paid to Anglo American South Africa Limited.
(3) Director's fees for services rendered by P Cooper were paid to Rand Merchant Insurance Holdings Limited.
(4) Director's fees for services rendered by JJ Durand were paid to Remgro Limited.
(5) Included in director's fees for SB Epstein is US$ 100 000 for services rendered as director of TVG Inc.
(6) Director's fees for services rendered by T Slabbert were paid to WDB Investment Holdings Proprietary Limited.

Payments to directors for the year ended 30 June 2012 for services rendered are as follows:

R'000	Services as directors	Basic salary	Performance bonus	Phantom scheme bonus	Provident fund contributions	Other benefits[1]	Total
Executive							
A Gore	–	3 408	4 643	2 673	549	107	11 380
R Farber	–	2 845	3 370	4 413	142	67	10 837
HD Kallner	–	2 835	3 713	4 575	142	78	11 343
NS Koopowitz	–	7 670	4 665	–	131	26	12 492
HP Mayers	–	5 058	4 910	6 172	624	180	16 944
Dr A Ntsaluba	–	2 751	1 495	–	481	69	4 796
A Pollard	–	2 747	3 559	4 817	206	103	11 432
JM Robertson	–	2 491	3 523	3 948	509	56	10 527
B Swartzberg	–	3 236	4 078	6 134	339	80	13 867
Sub-total	–	33 041	33 956	32 732	3 123	766	103 618
Prescribed officers							
J Broomberg	–	3 015	3 962	7 554	226	75	14 832
K Rabson	–	2 533	3 519	4 656	317	206	11 231
P Tlhabi	–	2 240	1 931	2 803	112	53	7 139
Sub-total	–	7 788	9 412	15 013	655	334	33 202
Non-executive							
MI Hilkowitz	2 500	–	–	–	–	–	2 500
Dr BA Brink[2]	419	–	–	–	–	–	419
P Cooper[3]	732	–	–	–	–	–	732
JJ Durand[4]	354	–	–	–	–	–	354
SB Epstein[5]	1 322	–	–	–	–	–	1 322
Dr TV Maphai	257	–	–	–	–	–	257
V Mufamadi	257	–	–	–	–	–	257
AL Owen	1 232	–	–	–	–	–	1 232
SE Sebotsa	570	–	–	1 464	–	–	2 034
T Slabbert[6]	523	–	–	–	–	–	523
SV Zilwa	797	–	–	–	–	–	797
Sub-total	8 963	–	–	1 464	–	–	10 427
Total	8 963	40 829	43 368	49 209	3 778	1 100	147 247
Less: paid by subsidiaries	(8 963)	(40 829)	(43 368)	(49 209)	(3 778)	(1 100)	(147 247)
Paid by holding company	–	–	–	–	–	–	–

(1) "Other benefits" comprise medical aid contributions, travel and other allowances.

(2) Director's fees for services rendered by Dr BA Brink were paid to Anglo American South Africa Limited.

(3) Director's fees for services rendered by P Cooper were paid to Rand Merchant Insurance Holdings Limited.

(4) Director's fees for services rendered by JJ Durand were paid to Remgro Limited.

(5) Included in director's fees for SB Epstein is US$ 100 000 for services rendered as director of TVG Inc.

(6) Director's fees for services rendered by T Slabbert were paid to WDB Investment Holdings Proprietary Limited.

DIRECTORS' PARTICIPATION IN SHARE INCENTIVE SCHEMES

Discovery's directors and prescribed officers participate in the various share incentive schemes offer by the Group and their participation is disclosed below. Refer to Group note 34.1 for a detailed description of the various schemes offered.

Discovery Limited Phantom Share Scheme

Directors and prescribed officers participation as at 30 June 2013:

Directors and prescribed officers	Outstanding shares	Date granted	Strike price R	Final vesting date	Value at 30 June 2013 R
J Broomberg	13 375	30/09/2008	–	30/09/2013	**1 124 303**
	156 138	01/07/2009	–	30/09/2013	**13 125 000**
	16 150	30/09/2009	–	30/09/2014	**1 357 569**
	30 000	30/09/2010	–	30/09/2015	**2 521 800**
	41 400	30/09/2011	–	30/09/2016	**3 480 084**
	17 260	30/09/2012	–	30/09/2017	**1 450 876**
	51 780	30/09/2012	54.75	30/09/2017	**1 884 197**
R Farber	13 375	30/09/2008	–	30/09/2013	**1 124 303**
	111 156	01/07/2009	–	30/09/2013	**8 898 038**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
A Gore	18 750	30/09/2008	–	30/09/2013	**1 576 125**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
HD Kallner	13 375	30/09/2008	–	30/09/2013	**1 124 303**
	133 942	01/07/2009	–	30/09/2013	**10 722 057**
	16 150	30/09/2009	–	30/09/2014	**1 357 569**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
NS Koopowitz	310 598	30/09/2010	–	30/09/2015	**26 108 868**
HP Mayers	18 750	30/09/2008	–	30/09/2013	**1 576 125**
	197 685	01/07/2009	–	30/09/2013	**15 824 684**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
A Ntsaluba	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**

Directors and prescribed officers	Outstanding shares	Date granted	Strike price R	Final vesting date	Value at 30 June 2013 R
A Pollard	18 750	30/09/2008	–	30/09/2013	**1 576 125**
	110 904	01/07/2009	–	30/09/2013	**8 877 865**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	6 184	30/09/2012	–	30/09/2017	**519 827**
	18 552	30/09/2012	54.75	30/09/2017	**675 079**
K Rabson	13 375	30/09/2008	–	30/09/2013	**1 124 303**
	138 560	01/07/2009	–	30/09/2013	**11 091 728**
	16 150	30/09/2009	–	30/09/2014	**1 357 569**
	30 000	30/09/2010	–	30/09/2015	**2 521 800**
	41 400	30/09/2011	–	30/09/2016	**3 480 084**
	17 260	30/09/2012	–	30/09/2017	**1 450 876**
	51 780	30/09/2012	54.75	30/09/2017	**1 884 197**
JM Robertson	18 750	30/09/2008	–	30/09/2013	**1 576 125**
	74 184	01/07/2009	–	30/09/2013	**5 938 429**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
B Swartzberg	18 750	30/09/2008	–	30/09/2013	**1 576 125**
	187 789	01/07/2009	–	30/09/2013	**15 032 509**
	26 284	30/09/2009	–	30/09/2014	**2 209 391**
	32 177	30/09/2010	–	30/09/2015	**2 704 820**
	44 500	30/09/2011	–	30/09/2016	**3 740 670**
	18 553	30/09/2012	–	30/09/2017	**1 559 565**
	55 659	30/09/2012	54.75	30/09/2017	**2 025 348**
SE Sebotsa	39 930	01/12/2009	–	30/09/2017	**3 356 516**
	120 000	01/12/2009	28.23	30/09/2017	**6 699 782**
P Tlhabi	8 000	30/09/2008	–	30/09/2013	**672 480**
	62 275	01/07/2009	–	30/09/2013	**4 985 114**
	16 150	30/09/2009	–	30/09/2014	**1 357 569**
	26 250	30/09/2010	–	30/09/2015	**2 206 575**
	41 400	30/09/2011	–	30/09/2016	**3 480 084**
	17 260	30/09/2012	–	30/09/2017	**1 450 876**
	51 780	30/09/2012	54.75	30/09/2017	**1 884 197**

DIRECTORS' PARTICIPATION IN SHARE INCENTIVE SCHEMES continued

The Vitality Group Inc. phantom stock plan

Directors and prescribed officers participation as at 30 June 2013:

Directors and prescribed officers	Outstanding shares	Date granted	Exercise price US$	Final vesting date	Value at 30 June 2013 US$
SB Epstein	90 910	01/10/2011	0.55	01/10/2014	**50 000**
SB Epstein	163 636	01/10/2012	0.55	01/10/2015	**90 000**
A Pollard	436 364	01/10/2012	0.55	01/10/2016	**240 000**

The PruHealth phantom share scheme

Directors and prescribed officers participation as at 30 June 2013:

Directors and prescribed officers	Outstanding shares	Date granted	Exercise price US$	Final vesting date	Value at 30 June 2013 US$
NS Koopowitz	41 012	01/03/2012	14.63	31/10/2015	**244 928**

The PruProtect phantom share scheme

Directors and prescribed officers participation as at 30 June 2013:

Directors and prescribed officers	Outstanding shares	Date granted	Exercise price GBP	Final vesting date	Value at 30 June 2013 GBP
NS Koopowitz	15 000	01/03/2012	10.00	31/10/2015	**426 966**

BEE share scheme

Directors and prescribed officers participation as at 30 June 2013:

Directors and prescribed officers	Outstanding shares	Date granted	Exercise price R	Final vesting date	Value at 30 June 2013 R
A Ntsaluba	200 000	11/04/2012	21.47	30/09/2016	**16 812 000**

DIRECTORS' INTERESTS IN SHARES

According to the Register of directors' Interests, maintained by Discovery in accordance with the provisions of section 30(4)(d) of the Companies Act, directors and prescribed officers of Discovery have disclosed the following interest in the ordinary shares of the Company at 30 June:

	Direct beneficial	Indirect beneficial	Total 2013	Direct beneficial	Indirect beneficial	Total 2012
R Farber	226 057	–	**226 057**	376 435	–	376 435
A Gore*	–	47 222 951	**47 222 951**	447 095	53 322 788	53 769 883
HD Kallner	167 661	–	**167 661**	167 661	–	167 661
NS Koopowitz	–	676 856	**676 856**	767 856	–	767 856
HP Mayers	312 606	7 724 497	**8 037 103**	602 806	7 724 497	8 327 303
A Pollard	1 633 840	–	**1 633 840**	2 080 935	–	2 080 935
JM Robertson	1 404 639	3 390 481	**4 795 120**	1 404 439	3 390 681	4 795 120
B Swartzberg*	3 484 227	22 624 429	**26 108 656**	3 983 322	24 328 265	28 311 587
J Broomberg	220 175	–	**220 175**	295 175	–	295 175
K Rabson	–	900 000	**900 000**	97 803	900 000	997 803
P Tlhabi	22 140	–	**22 140**	55 890	–	55 890
Dr BA Brink	30 000	–	**30 000**	30 000	–	30 000
P Cooper	55 076	55 016	**110 092**	55 076	55 016	110 092
SB Epstein	19 250	–	**19 250**	19 250	–	19 250
Dr TV Maphai	149	1 253 335	**1 253 484**	149	1 224 635	1 224 784
AL Owen	30 668	–	**30 668**	30 668	–	30 668
SE Sebotsa	39 950	–	**39 950**	21 000	–	21 000
SV Zilwa	–	67 060	**67 060**	–	77 760	77 760
	7 646 438	83 914 625	**91 561 063**	10 435 560	91 023 642	101 459 202

* *During the year ended 30 June 2010, A Gore and B Swartzberg entered into hedging transactions over 12 124 588 and 4 259 990 shares respectively. These hedging transactions have been partially unwound by 30 June 2013, and, as at 30 June 2013, 7 274 754 shares and 2 555 994 remain subject to the hedge for A Gore and B Swartzberg respectively. These shares are still reflected as being owned by A Gore and B Swartzberg. Details of the transactions were announced on the Securities Exchange News Service (SENS) on 30 December 2009, 2 March 2012, 7 March 2013, 6 May 2013, 19 June 2013 and 2 July 2013.*

There has been no change in the directors' interests in Discovery Limited's shares between 30 June 2013 and the date of publication of this annual report.

ANALYSIS OF SHAREHOLDERS

at 30 June 2013

	Number of shareholders	%	Number of shares	%
Shareholder spread				
1 – 1 000 shares	14 649	67.94	5 106 759	0.86
1 001 – 10 000 shares	5 557	25.77	16 702 356	2.82
10 001 – 100 000 shares	1 043	4.84	32 041 952	5.41
100 001 – 1 000 000 shares	246	1.14	73 895 255	12.48
1 000 001 shares and over	68	0.31	464 126 068	78.43
	21 563	**100.00**	**591 872 390**	**100.00**
Distribution of shares				
Corporate holding	1	0.00	148 048 168	25.01
Charity	11	0.05	696 062	0.12
Custodians	24	0.11	3 916 540	0.66
Exchange-traded fund	4	0.02	1 530 671	0.26
Foreign government	4	0.02	233 372	0.04
Hedge fund	1	0.00	57 997	0.01
Black Economic Empowerment	7	0.03	53 287 733	9.00
Pension funds	209	0.97	94 850 115	16.03
Private investor	224	1.04	113 366 562	19.15
Insurance companies	29	0.13	15 938 898	2.69
Investment trusts	6	0.03	2 101 245	0.36
Local authority	2	0.01	167 189	0.03
Unit trusts and mutual funds	298	1.38	77 517 342	13.10
Other managed funds	135	0.63	48 959 943	8.27
Remainder	20 570	95.40	14 188 379	2.40
University	8	0.04	535 173	0.09
Venture capital	4	0.02	414 801	0.07
Sovereign wealth	26	0.12	16 062 200	2.71
	21 563	**100.00**	**591 872 390**	**100.00**
Public/non-public shareholders				
Non-public shareholders	25	0.12	348 368 564	58.86
– Directors of the company holdings	12	0.06	89 058 254	15.05
– Empowerment	7	0.03	53 305 712	9.01
– Own holdings	1	0.01	680 268	0.11
– Key Management Personnel	3	0.01	1 142 315	0.19
– Strategic holdings (more than 5%)	2	0.01	204 182 015	34.50
Public shareholders	21 538	99.88	243 503 826	41.14
	21 563	**100.00**	**591 872 390**	**100.00**

	Number of shares	%
Beneficial shareholders' holding of 5% or more		
Rand Merchant Insurance Holdings Limited	148 048 168	25.01
Government Employees Pension Fund	56 133 847	9.48
A Gore	47 222 951	7.98

EMBEDDED VALUE STATEMENT AND ADDITIONAL INFORMATION

Contents

5-year review	266
Assurance report of the independent auditors	267
Embedded value statement	268
Additional information	276



FIVE-YEAR REVIEW

for the year ended 30 June 2013

	Group 2009	Group 2010	Group 2011	Group 2012	**Group 2013**	Compound growth %
New business API (R million)	5 866	7 618	7 543	9 390	**10 799**	16%
Gross inflows under management (R million)						
Gross inflows under management	33 591	41 235	50 052	56 914	**65 657**	18%
Less: Collected on behalf of third parties	24 576	28 813	32 198	36 369	**40 813**	14%
Gross income of Group	9 015	12 422	17 854	20 545	**24 844**	29%
Income statement extracts (R million)						
Profit from operations	1 854	2 514	2 914	3 553	**3 787**	20%
Headline earnings	1 238	1 545	1 638	2 129	**2 062**	14%
Abnormal expenses	13	6	390	187	**725**	
Normalised headline earnings	1 251	1 551	2 028	2 316	**2 787**	22%
Diluted normalised headline earnings per share (cents)	226.5	278.8	365.5	416.9	**496.0**	22%
Statement of financial position extracts (R million)						
Total assets	14 931	20 994	30 905	40 662	**54 933**	38%
Shareholders' funds	7 013	8 382	8 973	11 731	**13 708**	18%
Embedded value						
Embedded value (R million)	20 040	22 558	26 890	30 246	**35 721**	16%
Diluted embedded value per share (R)	35.83	40.31	47.86	53.78	**63.30**	15%
Key ratios						
Return on average equity (%)	18	22	30	21	**17**	
Return on average assets (%)	9	10	10	6	**4**	
Capital adequacy requirement (times)	7.7	8.0	3.6	4.4	**4.0**	
Exchange rates						
Rand/USD						
– Closing	7.73	7.66	6.77	8.19	**10.01**	
– Average	8.88	7.59	6.96	7.78	**8.94**	
Rand/GBP						
– Closing	12.71	11.48	10.84	12.83	**15.22**	
– Average	14.08	11.96	11.08	12.35	**13.98**	
Share statistics						
Number of ordinary shares in issue						
– Weighted average (000's)	551 043	554 117	554 847	554 930	**554 165**	
– Diluted weighted average (000's)	552 591	556 257	555 056	555 538	**561 843**	
– End of period (000's)	591 953	591 953	591 872	591 872	**591 872**	
Price/diluted headline earnings (times)	11.5	12.6	10.5	12.5	**17.0**	
Share price (cents per share)						
– High	2 840	3 700	4 095	5 233	**8 700**	
– Low	1 814	2 535	3 410	5 174	**5 280**	
– Closing	2 584	3 505	3 855	5 200	**8 406**	
Market capitalisation (R million)	15 296	20 748	22 817	30 777	**49 753**	

ASSURANCE REPORT OF THE INDEPENDENT AUDITORS

for the year ended 30 June 2013

REPORT ON THE REVIEW OF THE EMBEDDED VALUE OF DISCOVERY LIMITED AND ITS SUBSIDIARIES TO THE DIRECTORS OF DISCOVERY LIMITED

Introduction

We have reviewed the consolidated embedded value of Discovery Limited and its subsidiaries (together the Group) for the year ended 30 June 2013 as set out on pages 268 to 275. The Report is prepared for the purpose of setting out the embedded value of the Group for the year as at 30 June 2013. The directors of Discovery Limited are responsible for the preparation and presentation of the Report in accordance with the basis set out on the first page to the Report and for determining that the basis of preparation is acceptable in the circumstances. Our responsibility is to express a conclusion on this Report based on our review

Scope of review

We conducted our review in accordance with the International Standard on Review ISRE 2410, which applies to a review of historical financial information performed by the independent auditor of the entity. A review of financial information consist of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with international accounting standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review of the consolidated embedded value of Discovery Limited and its subsidiaries as included in the embedded value statement for the year ended 30 June 2013, nothing has come to our attention that causes us to believe that the Group embedded value report is not prepared, in all material aspects, in accordance with the embedded value basis set out on the first page of the embedded value statement.

Basis of Accounting and Restriction of Use

Without qualifying our conclusion, we draw attention to the embedded value basis of preparation set out on the first page of the attached report. The report is prepared for the purpose of setting out the embedded value of the Group for the year ended 30 June 2013. As a result the report may not be suitable for any other purpose.



PricewaterhouseCoopers Inc.

Director: **AG Taylor**
Registered Auditor

Sunninghill
2 September 2013

EMBEDDED VALUE STATEMENT

for the year ended 30 June 2013

The embedded value of Discovery at 30 June 2013 consists of the following components:

- the free surplus attributed to the covered business at the valuation date;
- plus: the required capital to support the in-force covered business at the valuation date;
- plus: the present value of expected future shareholder cash flows from the in-force business;
- less: the cost of required capital.

The present value of future shareholder cash flows from the in-force covered business is calculated as the value of projected future after-tax shareholder cash flows of the business in force at the valuation date, discounted at the risk discount rate.

The value of new business is the present value, at the point of sale, of the projected future after-tax shareholder cash flows of the new business written by Discovery, discounted at the risk discount rate, less an allowance for the reserving strain (for Life), initial expenses and cost of required capital. The value of new business is calculated using the current reporting date assumptions.

For Life, the shareholder cash flows are based on the release of margins under the Statutory Valuation Method ("SVM") basis.

The embedded value includes the insurance and administration profits of the subsidiaries in the Discovery Limited group. Covered business includes business written in South Africa through Discovery Life, Discovery Invest, Discovery Health and Discovery Vitality, and in the United Kingdom through PruProtect, PruHealth and PruHealth Insurance Limited (previously Standard Life Healthcare). For The Vitality Group (USA) and Discovery Insure, no published value has been placed on the current in-force business.

In August 2010, Discovery acquired Standard Life Healthcare and increased its shareholding in the Prudential joint venture from 50% to 75%. During 2011, Discovery announced a venture with Humana in the United States and launched a short term insurer, Discovery Insure. Put options were granted to the non-controlling parties in these subsidiaries. The put option entitles the non-controlling party to sell its interest in the subsidiary to companies within the Discovery Group at specified future dates.

For accounting purposes, in accordance with IAS32, Discovery has consolidated 100% of the subsidiaries results and has recognized the fair value of the non-controlling interest, being the present value of the estimated purchase price, as a financial liability in the Statement of Financial Position (Puttable non-controlling interest). For embedded value purposes, the financial liability in excess of the non-controlling interest in the net asset value and the non-controlling share of the profits/losses included in retained earnings are added back to the adjusted net worth.

In August 2011, Discovery raised R800 million through the issue of non-cumulative, non-participating, non-convertible preference shares. For embedded value purposes, the capital raised, net of share issue expenses, has been excluded from the adjusted net worth.

TABLE 1: GROUP EMBEDDED VALUE

R million	30 June 2013	30 June 2012	% Change
Shareholders' funds	**13 706**	11 730	17
Adjustment to shareholders' funds from published basis[1]	**(9 611)**	(8 401)	
Adjusted net worth	**4 095**	3 329	
– Free Surplus	**1 338**	1 208	
– Required Capital[2]	**2 757**	2 121	
Value of in-force covered business before cost of capital	**32 383**	27 493	
Cost of required capital	**(757)**	(576)	
Discovery Limited embedded value	**35 721**	30 246	18
Number of shares (millions)	**554.0**	554.4	
Embedded value per share	**R64.48**	R54.56	18
Diluted number of shares (millions)	**591.2**	591.2	
Diluted embedded value per share[3]	**R63.30**	R53.78	18

(1) The published shareholders' funds was decreased to eliminate net assets under insurance contracts, deferred tax and deferred acquisition costs at June 2013 of R9 458 million (June 2012: R7 660 million) in respect of Life, R190 million (June 2012: R130 million) in respect of PruHealth and PruHealth Insurance Limited and R32 million (June 2012: R38 million) in respect of PruProtect. The shareholders' funds was decreased by R1 983 million (June 2012: R1 738 million) representing Discovery's share of goodwill and intangible assets (net of deferred tax) relating to the acquisition of Standard Life Healthcare and the Prudential joint venture.

The shareholders' funds was increased by R2 663 million (June 2012: R1 851 million) reflecting the value of the puttable non-controlling interest liability in excess of the non-controlling interest in the net asset value and R168 million (June 2012: R93 million) reflecting the non-controlling share of the losses included in retained earnings.

The shareholders' funds was reduced by an amount of R779 million being the net preference share capital raised during August 2011.

(2) The required capital at June 2013 for Life is R909 million (June 2012: R728 million), for Health and Vitality is R553 million (June 2012: R487 million), for PruHealth and PruHealth Insurance Limited is R987 million (June 2012: R708 million) and for PruProtect is R308 million (June 2012: R198 million). For Life, the required capital was set equal to two times the statutory Capital Adequacy Requirement ("CAR"). For Health and Vitality, the required capital was set equal to two times the monthly renewal expense and Vitality benefit cost. For PruHealth, the required capital amount was set equal to 1.25 times the capital prescribed by the FSA under the Individual Capital Adequacy Standards ("ICAS") framework. For PruProtect, the required capital was set equal to the UK Pillar 1 capital requirement.

(3) The diluted embedded value per share allows for Discovery's BEE transaction where the impact is dilutive i.e. where the current embedded value per share exceeds the current transaction value.

TABLE 2: VALUE OF IN-FORCE COVERED BUSINESS

R million	Value before cost of capital	Cost of required capital	Value after cost of capital
at 30 June 2013			
Health and Vitality	**12 405**	**(190)**	**12 215**
Life and Invest[1]	**17 213**	**(340)**	**16 873**
PruHealth[2]	**2 003**	**(167)**	**1 836**
PruProtect[2]	**762**	**(60)**	**702**
Total	**32 383**	**(757)**	**31 626**
at 30 June 2012			
Health and Vitality	11 435	(171)	11 264
Life and Invest[1]	14 346	(274)	14 072
PruHealth[2]	1 316	(97)	1 219
PruProtect[2]	396	(34)	362
Total	27 493	(576)	26 917

(1) Included in the Life and Invest value of in-force covered business is R576 million (June 2012: R425 million) in respect of investment management services provided on off balance sheet investment business. The net assets of the investment service provider are included in the adjusted net worth.

(2) The value of in-force has been converted using the closing exchange rate of R15.22/GBP (June 2012: R12.83/GBP). The values for PruHealth and PruProtect reflect Discovery's 75% shareholding in the joint venture.

TABLE 3: GROUP EMBEDDED VALUE EARNINGS

R million	30 June 2013	30 June 2012
Embedded value at end of period	**35 721**	30 246
Less: Embedded value at beginning of period	**(30 246)**	(26 890)
Increase in embedded value	**5 475**	3 356
Net change in capital	**21**	39
Dividends paid	**717**	593
Transfer to hedging reserve	**(85)**	(32)
Embedded value earnings	**6 128**	3 956
Annualised return on opening embedded value	**20.3%**	14.7%

TABLE 4: COMPONENTS OF GROUP EMBEDDED VALUE EARNINGS

	Year ended 30 June 2013				Year ended 30 June 2012
R million	Net worth	Cost of required capital	Value of in-force covered business	Embedded value	Embedded value
Total profit from new business (at point of sale)	**(1 752)**	**(103)**	**3 715**	**1 860**	1 640
Profit from existing business					
• Expected return	**2 505**	**26**	**295**	**2 826**	2 670
• Change in methodology and assumptions[1]	**699**	**(58)**	**(841)**	**(200)**	(680)
• Experience variances	**(320)**	**(14)**	**1 326**	**992**	(107)
Increase in goodwill and intangibles	**(22)**	**–**	**–**	**(22)**	–
Other initiative costs[2]	**(450)**	**–**	**25**	**(425)**	(386)
Non-recurring expenses	**(19)**	**–**	**–**	**(19)**	(26)
Acquisition costs[3]	**(6)**	**–**	**2**	**(4)**	5
Finance costs	**(35)**	**–**	**–**	**(35)**	(28)
Foreign exchange rate movements	**451**	**(32)**	**379**	**798**	638
Return on shareholders' funds[4]	**357**	**–**	**–**	**357**	230
Embedded value earnings	**1 408**	**(181)**	**4 901**	**6 128**	3 956

(1) The changes in methodology and assumptions will vary over time to reflect adjustments to the model and assumptions as a result of changes to the operating and economic environment. The current period's changes are described in detail in Table 6 below (for previous periods refer to previous embedded value statements).

(2) This item reflects Group initiatives including expenses relating to the investment in The Vitality Group, Discovery Insure and the expansion of the Life and Invest distribution channel.

(3) Acquisition costs relate to commission paid on Life business that has been written over the period but that will only be activated and on risk after the valuation date. These policies are not included in the embedded value or the value of new business and therefore the costs are excluded.

(4) The return on shareholders' funds is shown net of tax and management charges.

TABLE 5: EXPERIENCE VARIANCES

R million	Health and Vitality		Life and Invest		PruHealth		PruProtect		Total
	Net worth	Value of in-force	Net worth	Value of in-force	Net worth	Value of in-force	Net worth	Value of in-force	
Renewal expenses	(39)	–	21	(3)	(15)	–	7	–	**(29)**
Other expenses	–	–	–	–	(81)	–	–	–	**(81)**
Lapses and surrenders[1]	14	428	(4)	309	–	138	8	(4)	**889**
Mortality and morbidity	–	–	(14)	30	109	61	11	–	**197**
Policy alterations[2]	–	26	(373)	339	–	–	1	9	**2**
Backdated cancellations	–	–	(78)	22	–	–	(6)	(4)	**(66)**
Premium income	–	–	(74)	(82)	–	(133)	–	–	**(289)**
Economic assumptions	–	–	(31)	118	–	–	–	–	**87**
Commission	–	–	–	–	(11)	(16)	–	–	**(27)**
Tax[3]	(12)	–	216	(244)	(11)	–	(15)	–	**(66)**
Reinsurance	–	–	(12)	10	–	–	34	(13)	**19**
Maintain modelling term[4]	–	234	–	70	–	14	–	–	**318**
Vitality benefits	67	–	–	–	(4)	1	–	–	**64**
Other	56	(52)	(85)	79	0	(26)	1	1	**(26)**
Total	86	636	(434)	648	(13)	39	41	(11)	**992**

(1) The total Health and Vitality lapse experience variance of R442 million consists of a positive variance of R134 million due to lower than expected lapses and a positive variance of R308 million due to the net growth in existing employer groups (i.e. R966 million in respect of members joining existing employer groups during the period offset by an amount of R658 million in respect of members leaving existing employer groups).

(2) Policy alterations relate to changes to existing benefits at the request of the policyholder.

(3) The tax variance for Life and Invest arises due to a movement in the deferred tax asset which delays the payment of tax.

(4) The projection term for Health and Vitality, Life, Group Life and PruHealth at 30 June 2013 has not been changed from that used in the 30 June 2012 embedded value calculation. Therefore, an experience variance arises because the total term of the in-force covered business is effectively increased by one year.

TABLE 6: METHODOLOGY AND ASSUMPTION CHANGES

R million	Health and Vitality		Life and Invest		PruHealth		PruProtect		Total
	Net worth	Value of in-force	Net worth	Value of in-force	Net worth	Value of in-force	Net worth	Value of in-force	
Modelling changes	–	–	(30)	(14)	–	–	2	15	**(27)**
Expenses[1]	–	(332)	1	(18)	–	(84)	5	(2)	**(430)**
Lapses[2]	–	–	(0)	(149)	–	186	(239)	26	**(176)**
Mortality and morbidity[3]	–	–	–	–	–	150	31	(8)	**173**
Benefit enhancements	–	–	9	(56)	–	–	–	–	**(47)**
Vitality benefits[4]	–	160	–	–	–	(222)	–	–	**(62)**
Tax	–	–	–	–	–	58	–	6	**64**
Economic assumptions	–	92	42	155	–	(38)	117	(12)	**356**
Reinsurance[5]	–	–	811	(826)	(87)	47	–	–	**(55)**
Other	–	–	23	(12)	–	(19)	14	(2)	**4**
Total	–	(80)	856	(920)	(87)	78	(70)	23	**(200)**

(1) The Health renewal expense assumption has been adjusted to reflect increased investment in IT, systems and other strategic initiatives which are expected to create a sustainable long-term competitive advantage for the business.
The PruHealth expense assumption allows for higher than expected expenses related to the transitional services arrangement with Standard Life.

(2) The Invest and PruProtect lapse assumptions were strengthened to reflect uncertainty about long duration experience.
The PruHealth lapse assumption has been reduced in line with recent experience and expected future experience.

(3) The PruHealth morbidity assumption has been reduced in line with recent experience and expected future experience.

(4) The South African Vitality benefit assumption was adjusted in line with better than expected recent experience.
The United Kingdom Vitality benefit assumption has been strengthened following recent benefit enhancements and increased engagement.

(5) The reinsurance item relates to the impact of the financing reinsurance arrangements.

TABLE 7: EMBEDDED VALUE OF NEW BUSINESS

R million	Year ended 30 June 2013	Year ended 30 June 2012	% change
Health and Vitality			
Present value of future profits from new business at point of sale	**396**	399	
Cost of required capital	**(16)**	(16)	
Present value of future profits from new business at point of sale after cost of required capital	**380**	383	(1)
New business annualised premium income[1]	**1 783**	1 798	(1)
Life and Invest			
Present value of future profits from new business at point of sale[2]	**1 033**	974	
Cost of required capital	**(44)**	(40)	
Present value of future profits from new business at point of sale after cost of required capital	**989**	934	6
New business annualised premium income[3]	**1 923**	1 804	7
Annualised profit margin[4]	**6.4%**	6.6%	
Annualised profit margin excluding Invest Business	**10.0%**	10.0%	
PruHealth[5]			
Present value of future profits from new business at point of sale	**54**	21	
Cost of required capital	**(20)**	(9)	
Present value of future profits from new business at point of sale after cost of required capital	**34**	12	183
New business annualised premium income	**525**	273	92
Annualised profit margin	**1.2%**	0.7%	
PruProtect[6]			
Present value of future profits from new business at point of sale	**480**	326	
Cost of required capital	**(23)**	(15)	
Present value of future profits from new business at point of sale after cost of required capital	**457**	311	47
New business annualised premium income	**483**	345	40
Annualised profit margin[4]	**12.8%**	15.1%	

(1) Health new business annualised premium income is the gross contribution to the medical schemes. For embedded value purposes, Health new business is defined as individuals and members of new employer groups, and includes additions to first year business. There have been no changes to the definition of new business from the previous valuation.
The new business annualised premium income shown above excludes premiums in respect of members who join an existing employer after the first year, as well as premiums in respect of new business written during the period but only activated after 30 June 2013.
The total Health and Vitality new business annualised premium income written over the period was R5 036 million (June 2012: R4 453 million).

(2) Included in the Life and Invest value of new business is R14 million (June 2012: -R1 million) in respect of investment management services provided on off balance sheet investment business.
Risk business written prior to the valuation date allows certain Invest business to be written at financially advantageous terms, the impact of which has been recognized in the value of new business.

(3) Life new business is defined as Life policies or Discovery Retirement Optimiser policies which incepted during the reporting period and which are on risk at the valuation date. Invest new business is defined as business where at least one premium has been received and which has not been refunded after receipt.
The new business annualised premium income of R1 923 million (June 2012: R1 804 million) (single premium APE: R614 million (June 2012: R511 million)) shown above excludes automatic premium increases and servicing increases in respect of existing business. The total Life new business annualised premium income written over the period, including both automatic premium increases of R651 million (June 2012: R552 million) and servicing increases of R392 million (June 2012: R354 million) was R2 966 million (June 2012: R2 710 million) (single premium APE: R644 million (June 2012: R537 million)). Single premium business is included at 10% of the value of the single premium.
Policy alterations, including Discovery Retirement Optimisers added to existing Life Plans are shown in Table 5 as experience variances and not included as new business.
Term extensions on existing contracts are not included as new business.

(4) The annualised profit margin is the value of new business expressed as a percentage of the present value of future premiums.

(5) PruHealth new business is defined as individuals and employer groups which incepted during the reporting period. The new business annualised premium income shown above has been adjusted to exclude premiums in respect of members who join an existing employer group after the first month as well as premiums in respect of new business written during the period but only activated after 30 June 2013. There have been no changes to the definition of new business from the previous valuation.

(6) PruProtect new business is defined as policies which incepted during the reporting period and which are on risk at the valuation date. There have been no changes to the definition of new business from the previous valuation.

TABLE 8: EMBEDDED VALUE ECONOMIC ASSUMPTIONS

			30 June 2013	30 June 2012
Beta coefficient				
South Africa			**0.49**	0.53
United Kingdom			**0.49**	0.53
Equity risk premium (%)				
South Africa			**3.50**	3.50
United Kingdom			**4.00**	4.00
Risk discount rate (%)				
Health and Vitality			**10.215**	10.355
Life and Invest			**10.215**	10.355
PruHealth			**4.97**	4.40
PruProtect			**4.97**	4.40
Rand/GB Pound Exchange Rate				
Closing			**15.22**	12.83
Average			**13.98**	12.35
Medical inflation (%)				
South Africa			**7.50**	7.50
United Kingdom			**7.00**	7.00
Expense inflation and CPI (%)				
South Africa			**4.50**	4.50
United Kingdom	–	PruHealth	**3.30**	3.75
	–	PruProtect	**3.30**	1.60
Pre-tax investment return (%)				
South Africa	–	Cash	**7.00**	7.00
	–	Bonds	**8.50**	8.50
	–	Equity	**12.00**	12.00
United Kingdom	–	Risk Free	**3.01**	2.26
	–	PruProtect asset return assumption	**3.85**	2.66
Income tax rate (%)				
South Africa			**28.00**	28.00
United Kingdom			**24.00% reducing to 20.00% in April 2015**	25.00% reducing to 23.00% in April 2014
Projection term				
– Health and Vitality			**20 years**	20 years
– Life value of in-force			**40 years**	40 years
– Group Life			**10 years**	10 years
– PruHealth			**20 years**	20 years

Life and Invest mortality, morbidity and lapse and surrender assumptions were derived from internal experience, where available, augmented by reinsurance and industry information.

The Health lapse assumptions were based on the results of recent experience investigations. The lapse rate for the projection term after 10 years was set above current experience.

The PruHealth assumptions were derived from internal experience, augmented by industry information.

PruProtect assumptions were derived from internal experience, where available, augmented by reinsurance, industry and Discovery group information.

Renewal expense assumptions were based on the results of the latest expense and budget information.

The initial expenses included in the calculation of the value of new business are the actual costs incurred excluding expenses of an exceptional or non-recurring nature.

The South African investment return assumption was based on a single interest rate derived from the risk-free zero coupon government bond yield curve. Other economic assumptions were set relative to this yield. The current and projected tax position of the policyholder funds within the Life company has been taken into account in determining the net investment return assumption. The PruHealth investment return assumption was derived from the sterling swap curve. The PruProtect investment return assumption was set with reference to the expected return on matching assets (or liabilities in the case of negative reserves) held on the Prudential balance sheet. The PruProtect expense inflation assumption was set with reference to the investment return assumption.

It is assumed that, for the purposes of calculating the cost of required capital, the Life and Invest required capital amount will be backed by surplus assets consisting of 100% equities and the Health, Vitality and PruHealth required capital amounts will be fully backed by cash. The PruProtect required capital amount is assumed to earn the same return as the assets backing the PruProtect policyholder liabilities. Allowance has been made for tax and investment expenses in the calculation of the cost of capital. In calculating the capital gains tax ("CGT") liability, it is assumed that the portfolio is realised every 5 years.

TABLE 9: EMBEDDED VALUE SENSITIVITY

		Health and Vitality	
R million	Adjusted net worth	Value of in-force	Cost of capital
Base	4 095	12 405	(190)
Impact of:			
Risk discount rate +1%	4 095	11 699	(214)
Risk discount rate -1%	4 095	13 188	(163)
Lapses -10%	4 095	12 860	(200)
Interest rates -1%[1]	4 095	12 365	(181)
Equity and property market value -10%	3 997	12 405	(190)
Equity and property return +1%	4 095	12 405	(190)
Renewal expenses -10%	4 095	13 650	(176)
Mortality and morbidity -5%	4 095	12 405	(190)
Projection term +1 year	4 095	12 538	(192)

(1) All economic assumptions were reduced by 1%.

(2) The sensitivity impact on the PruProtect value of in-force includes the net of tax change in negative reserves.

The following table shows the effect of using different assumptions on the value of new business.

TABLE 10: VALUE OF NEW BUSINESS SENSITIVITY

	Health and Vitality	
R million	Value of new business	Cost of capital
Base	396	(16)
Impact of:		
Risk discount rate +1%	358	(19)
Risk discount rate -1%	439	(14)
Lapses -10%	423	(17)
Interest rates -1%[1]	397	(16)
Equity and property return +1%	396	(16)
Renewal expense -10%	469	(16)
Mortality and morbidity -5%	396	(16)
Projection term +1 year	403	(17)
Acquisition costs -10%	413	(16)

(1) All economic assumptions were reduced by 1%.

(2) The sensitivity impact on the PruProtect value of new business includes the net of tax change in negative reserves.

The Life and Invest cost of capital is calculated using the difference between the gross of tax equity return and the equity return net of tax and expenses. The Health and Vitality and PruHealth cost of capital is calculated using the difference between the risk discount rate and the net of tax cash return. The PruProtect cost of capital is calculated using the difference between the risk discount rate and the net of tax asset return assumption.

Sensitivity to the embedded value assumptions

The embedded value has been calculated in accordance with the Actuarial Society of South Africa's Advisory Practice Note APN 107: Embedded Value Reporting. The risk discount rate, calculated in accordance with the guidance note, uses the CAPM approach with specific reference to the Discovery beta coefficient. The Discovery beta coefficient reflects the historic performance of the Discovery share price relative to the market and may not allow fully for non-market related and non-financial risk. Investors may want to form their own view on an appropriate allowance for the non-financial risks which have not been modelled explicitly. The sensitivity of the embedded value and the value of new business at 30 June 2013 to changes in the risk discount rate is included in the tables below.

For each sensitivity illustrated below, all other assumptions have been left unchanged. No allowance has been made for management action such as risk premium increases where future experience is worse than the base assumptions.

Life and Invest		PruHealth		PruProtect[2]			
Value of in-force	Cost of capital	Value of in-force	Cost of capital	Value of in-force	Cost of capital	Embedded value	% change
17 213	(340)	2 003	(167)	762	(60)	**35 721**	
15 528	(302)	1 866	(218)	678	(80)	**33 052**	(7)
19 224	(387)	2 154	(109)	865	(34)	**38 833**	9
18 953	(376)	2 304	(178)	799	(66)	**38 191**	7
17 870	(352)	1 989	(218)	999	(65)	**36 502**	2
17 125	(340)	2 003	(167)	762	(60)	**35 535**	(1)
17 345	(341)	2 003	(167)	762	(60)	**35 852**	0
17 410	(339)	2 183	(167)	752	(59)	**37 349**	5
18 316	(332)	2 745	(167)	743	(59)	**37 556**	5
17 290	(342)	2 026	(167)	762	(60)	**35 950**	1

Life and Invest		PruHealth		PruProtect[2]			
Value of new business	Cost of capital	Value of new business	Cost of capital	Value of new business	Cost of capital	Value of new business	% change
1 033	(44)	54	(20)	480	(23)	**1 860**	
825	(39)	39	(25)	443	(30)	**1 552**	(17)
1 279	(50)	71	(13)	525	(13)	**2 224**	20
1 268	(49)	85	(21)	487	(25)	**2 151**	16
1 109	(46)	53	(25)	388	(26)	**1 834**	(1)
1 059	(44)	54	(20)	480	(23)	**1 886**	1
1 060	(44)	78	(20)	494	(23)	**1 998**	7
1 151	(43)	170	(20)	533	(22)	**2 149**	16
1 043	(44)	56	(20)	480	(23)	**1 878**	1
1 125	(44)	66	(20)	507	(23)	**2 008**	8

The following financial information has not been audited and has been provided for information purposes only.

VALUE CREATORS

New business annualised premium income

New business annualised premium income increased 15% for the year ended 30 June 2013.

R million	**June 2013**	June 2012	% change
Discovery Health	**4 820**	4 282	13
Discovery Life	**1 896**	1 749	8
Discovery Invest	**1 070**	961	11
Discovery Vitality	**216**	171	26
Discovery Insure	**366**	239	53
PruHealth*	**929**	605	54
PruProtect	**644**	460	40
The Vitality Group USA*	**514**	564	(9)
Ping An Health	**344**	359	(4)
New business API of Group	**10 799**	9 390	15

* *The comparatives for PruHealth and The Vitality Group USA have been increased to be consistent with the basis used at 30 June 2013.*

New business API is calculated at 12 times the monthly premium for new recurring premium policies and 10% of the value of new single premium policies. It also includes both automatic premium increases and servicing increases on existing policies. For The Vitality Group USA and Ping An Health, new business API is calculated based on the date of policy inception.

Gross inflows under management

Gross inflows under management increased 15% for the year ended 30 June 2013.

R million	**June 2013**	June 2012	% change
Discovery Health	**41 050**	35 963	14
Discovery Life	**7 329**	6 184	19
Discovery Invest	**9 089**	8 231	10
Discovery Insure	**298**	92	224
Discovery Vitality	**1 660**	1 454	14
PruHealth	**4 878**	4 271	14
PruProtect	**1 128**	628	80
The Vitality Group USA	**216**	91	137
AIA Vitality	**9**	–	
Gross inflows under management	**65 657**	56 914	15
Less: collected on behalf of third parties	**(40 813)**	(36 369)	(12)
Discovery Health	**(36 973)**	(32 242)	
Discovery Invest	**(3 840)**	(4 127)	
Gross income of Group	**24 844**	20 545	21

Gross inflows under management measures the total funds collected by Discovery and is an accurate measure of the growth of Discovery.

Normalised profit from operations

The following table shows the main components of the normalised profit from operations for the year ended 30 June 2013:

R million	June 2013	June 2012	% change
Discovery Health	**1 688**	1 499	13
Discovery Life	**2 106**	1 819	16
Discovery Invest	**221**	151	46
Discovery Vitality	**35**	5	600
PruHealth	**146**	91	60
PruProtect	**326**	209	56
Normalised profit from existing operations	**4 522**	3 774	20
Development and other segments	**(470)**	(331)	(42)
Normalised profit from operations	**4 052**	3 443	18

SIGNIFICANT MOVEMENTS IN THE INCOME STATEMENT

Share-based payments

Included in marketing and administration expenses, in employee costs, is R450 million (2012: R266 million) in respect of phantom options granted under the employee share incentive schemes, which is expensed in accordance with the requirements of IFRS 2. Discovery has entered into transactions to hedge its exposure to changes in the Discovery share price arising from these schemes. As at 30 June 2013, approximately 87.7% (2012: 79.1%) of this exposure was hedged. Fair value gains of R250 million (2012: R85 million) relating to the hedge were recognised in profit or loss resulting in a net expense to Discovery of R200 million (2012: R181 million).

Put options in subsidiaries

During the 2011 financial year, put options were granted to the non-controlling interests of three of Discovery's subsidiaries, entitling the non-controlling interest to sell its interest in the subsidiary to Discovery at contracted dates. In accordance with IAS 32, Discovery has recognised the fair value of the non-controlling interest, being the present value of the estimated purchase price, as a financial liability in the Statement of Financial Position (Puttable non-controlling interests). Interest in respect of this liability of R165 million has been recorded in finance costs for the year ended 30 June 2013 (2012: R152 million), using the effective interest rate method. The estimated purchase prices have been reconsidered at 30 June 2013 and a fair value adjustment of R133 million has been captured to profit or loss (2012: R13 million).

Aggregate effects on Discovery's results at 30 June 2013:

R million	Total
Value of puttable non-controlling interests at 1 July 2012	**2 893**
Further share issues to non-controlling interests	**77**
Finance costs recognised in profit or loss	**165**
Fair value adjustments recognised in profit or loss:	**133**
– resulting from a change in interest rates	**(55)**
– resulting from a change in assumptions	**188**
Net exchange differences arising during the year allocated to the translation reserve	**514**
Value of puttable non-controlling interests at 30 June 2013	**3 782**

Taxation

For South African entities that are in a tax paying position, tax has been provided at 28% (2012: 28%) and secondary tax on companies at 10% (up to 31 March 2012) in the financial statements. No deferred tax has been accounted for in respect of the Discovery Insure losses.

No deferred tax has been raised on the assessed losses in PruHealth and The Vitality Group.

Material transactions with related parties

Discovery Health administers the Discovery Health Medical Scheme (DHMS) and provides managed care services for which it charges an administration fee and a managed healthcare fee respectively. These fees are determined on an annual basis and approved by the trustees of DHMS. The fees totalled R3 714 million for the year ended 30 June 2013 (2012: R3 408 million). Discovery offers the members of DHMS access to the Vitality programme.

SIGNIFICANT MOVEMENTS IN THE STATEMENT OF FINANCIAL POSITION

Acquisition of a business combination

On 25 March 2013, Prudential Health Holdings Limited (PHHL), established a wholly-owned subsidiary, Insure Your Health Limited (IYH). IYH acquired the assets of three businesses namely, Insured Health Limited, Insured Limited and Employed Health Limited for GBP 2.6 million. GBP 2 million of this has been allocated to goodwill.

Financial assets

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss have increased by R7.9 billion due to the sale of Discovery Invest products as well as the significant returns on these investments. These returns are reflected in the income statement in 'Net fair value gains on financial assets at fair value through profit or loss'.

At 30 June 2012, R6.4 billion was invested in Equity Linked Notes issued by two providers. To reduce the exposure to these note providers, Discovery has sold approximately R5.7 billion worth of Equity Linked Notes and re-invested the proceeds with various investment managers.

Available-for-sale financial assets

Available-for-sale financial assets have primarily increased due to the transfer of funds from cash and cash equivalents to money market investments.

Negative reserve funding

The negative reserve funding liability on Discovery's Statement of Financial Position represents the acquisition costs that are funded by the Prudential Assurance Company on behalf of PruProtect. The liability unwinds and is repaid on a matched basis as the cash flows emerge from the assets arising from insurance contracts. In the event that the cash flows do not emerge as anticipated, PruProtect would be required to repay these liabilities from other resources.

The increase in the negative reserve funding liability relates to the increase in new business written by PruProtect in the current financial year.

Deferred tax liability

The deferred tax liability is primarily attributable to the application of the Financial Services Board directive 145. This directive allows for the zeroing on a statutory basis of the assets arising from insurance contracts. The statutory basis is used when calculating tax payable for Discovery Life, resulting in a timing difference between the tax base and the accounting base.

EMBEDDED VALUE

The embedded value of Discovery, representing the sum of the shareholders' net assets and the present value of the expected future profits arising from the existing in-force insurance business less an allowance for the cost of capital, was R35.7 billion at 30 June 2013 (2012: R30.2 billion). The embedded value calculation includes the shareholders' net assets at the values reflected in the consolidated statement of financial position on page 168.

The analysis of the main components of the Group embedded value is set out on below.

R million	Health and Vitality	Life and Invest	PruHealth	PruProtect	Other	Total
Value of in-force business at 30 June 2012	11 264	14 072	1 219	362	0	26 917
Expected return (in-force business)	1 127	1 438	81	5	0	2 651
Release of profits (in-force business)	(1 387)	(991)	(83)	(48)	0	(2 509)
Value of new business	621	2 495	228	268	0	3 612
Expected return (new business)	34	118	14	9	0	175
Release of profits (new business)	0	0	0	4	0	4
Experience variances	636	648	39	(11)	0	1 312
Methodology changes	(80)	(920)	78	23	0	(899)
Other	0	13	260	90	0	363
Value of in-force business at 30 June 2013	12 215	16 873	1 836	702	0	31 626
Shareholders' funds per Balance Sheet	723	11 035	2 937	(576)	(413)	13 706
Adjustment to shareholders' funds		(9 458)	(190)	(32)	69	(9 611)
Embedded value at 30 June 2013	12 938	18 450	4 583	94	(344)	35 721

More detail on the components of each of these items, including the methodology and assumptions made in calculating the embedded value of Discovery, can found in the Embedded Value Statement on pages 268 to 275.

Reconciliation of embedded value earnings

The movement in the embedded value in the year under review can be reconciled to the accounting earnings of the Group as follows:

R million	12 months to 30 June 2013	Value of In-force	Cost of required capital	Impact on Income Statement	Adjustment to Shareholders Funds	Statement of Changes in Equity
Total profit from new business (at point of sale)	**1 860**	3 715	(103)	(1 752)	–	–
– Health and Vitality	**380**	637	(16)	(241)	–	–
– Life	**989**	2 539	(44)	(1 506)	–	–
– PruHealth	**34**	248	(20)	(194)	–	–
– PruProtect	**457**	291	(23)	189	–	–
Profit from existing business						
Expected return	**2 826**	295	26	2 505	–	–
– Health and Vitality	**1 161**	(234)	8	1 387	–	–
Expected transfer from VIF to net worth	**–**	(1 387)	–	1 387	–	–
Unwinding of the risk discount rate	**1 161**	1 153	8	–	–	–
– Life	**1 555**	577	(13)	991	–	–
Expected transfer from VIF to net worth	**–**	(991)	–	991	–	–
Unwinding of the risk discount rate	**1 555**	1 568	(13)	–	–	–
– PruHealth	**95**	(12)	24	83	–	–
Expected transfer from VIF to net worth	**–**	(83)	–	83	–	–
Unwinding of the risk discount rate	**95**	71	24	–	–	–
– PruProtect	**15**	(36)	7	44	–	–
Expected transfer from VIF to net worth	**–**	(52)	8	44	–	–
Unwinding of the risk discount rate	**15**	16	(1)	–	–	–
Change in methodology and assumptions	**(200)**	(841)	(58)	699	–	–
– Health and Vitality	**(80)**	(79)	(1)	–	–	–
– Life	**(64)**	(911)	(9)	856	–	–
– PruHealth	**(9)**	125	(47)	(87)	–	–
– PruProtect	**(47)**	24	(1)	(70)	–	–
Experience variances	**992**	1 326	(14)	(320)	–	–
– Health and Vitality	**722**	646	(10)	86	–	–
– Life	**214**	647	1	(434)	–	–
– PruHealth	**26**	44	(5)	(13)	–	–
– PruProtect	**30**	(11)	–	41	–	–
Increase in goodwill and intangibles	**(22)**	–	–	–	(22)	–
Other initiatives	**(425)**	25	–	(450)	–	–
Non-recurring expenses	**(19)**	–	–	(19)	–	–
Acquisition costs	**(4)**	2	–	(6)	–	–
Finance costs	**(35)**	–	–	(200)	165	–
Foreign Exchange Rate Movements	**798**	379	(32)	(5)	164	292
– Intangibles					(317)	
– DAC					(33)	
– Puttable NCI Liability					514	
Return on shareholders' funds	**357**	–	–	162	–	195
– Unrealised gain on investments and realised gain on investments transferred to income statement	**195**	–	–	–	–	195
– Health and Vitality investment income	**16**	–	–	16	–	–
– Life investment income	**106**	–	–	106	–	–
– PruHealth investment income	**40**	–	–	40	–	–
Amortisation of intangibles	**–**	–	–	(125)	125	–
– Amortisation of intangibles from business combinations	**–**	–	–	(94)	94	–
– Minority Interest (Intangibles)	**–**	–	–	(31)	31	–
PruHealth and PruProtect DAC	**–**	–	–	21	(21)	–
Puttable non-controlling interest fair value adjustment	**–**	–	–	(133)	133	–
Other Minority Interest (Discovery Insure, PruHealth and PruProtect)	**–**	–	–	(44)	44	–
Life assets under insurance contracts	**–**	–	–	1 798	(1 798)	–
Embedded value earnings	**6 128**	4 901	(181)	2 131	(1 210)	487

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