

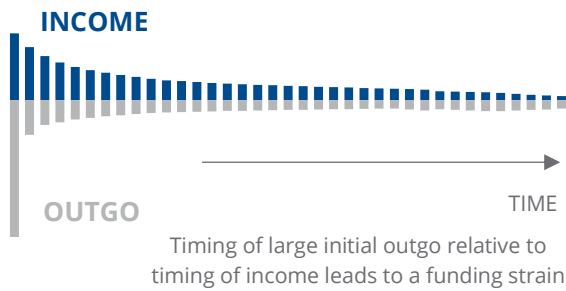


# NEGATIVE RESERVE PRINCIPLES

This is an illustrative note to provide supplementary information regarding the negative reserve on a principles basis and is not intended to provide any specific reconciliations to the accounts

Discovery Life's Individual Risk policies are characterised by large initial acquisition cost outflows followed by a stream of expected **net inflows** (Premiums less Claims, Expenses and PayBacks)

Discounted future income and outgo expected on sample Discovery Life policies



**RESERVE**  
Discounted **future** outgo less discounted **future** income

**NEGATIVE RESERVE**  
**FUTURE OUTGO < FUTURE INCOME**



**POSITIVE RESERVE**  
**FUTURE OUTGO > FUTURE INCOME**



Overall, Discovery Life sells **profitable** new business policies where discounted future income is expected to exceed discounted future outgo, resulting in a negative reserve.

## 1 NEGATIVE IFRS RESERVE

→ **Portion of expected future net cash flows recognised in IFRS income**

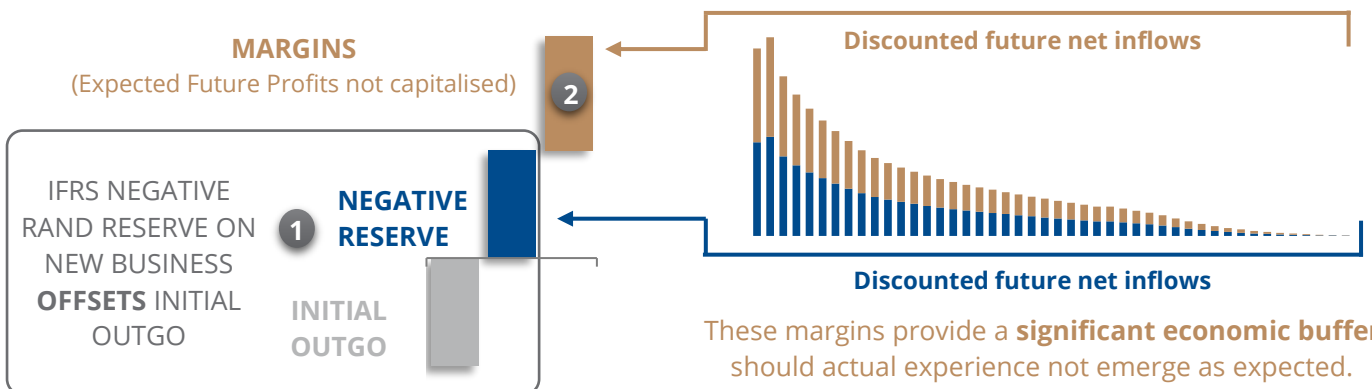
To offset the initial funding strain, a portion of future net inflows are capitalised at the outset of the new business policy to reflect the fact that a **portion** of future premium is earmarked to repay the initial outgo. This is done in line with Discovery's Accounting policy at a portfolio level.

## 2 MARGINS

→ **Portion of expected future net cash flows not recognised in IFRS income statement**

→ **Over time, margins will emerge as IFRS profit**

A large portion of the expected future inflows on new business are not recognised, instead being deferred to emerge as profit in the future through the addition of explicit compulsory and discretionary margins.



JUNE 2018

**-c.R31bn**

NEGATIVE RAND RESERVE ON RISK AND INVEST RECOGNISED ON THE IFRS BALANCE SHEET

**c.60%**

EXPECTED FUTURE NET CASH FLOW RECOGNISED ON THE IFRS BALANCE SHEET

**c.40%**

UNREALISED PROFITS EXPECTED TO EMERGE ON BEST ESTIMATE ASSUMPTIONS