

OLD MUTUAL PLC: TRADE IDEA

KEY FIGURES (# in British pence)

Current Price	206.90
Price target	300.00
Trading period	1 Year
Low	149.40
High	225.50
Average	188.006
1 Year Beta	1.714
Dividend Yield	5.02%



Old Mutual PLC (ODMUF) is an international long-term savings, protection and investment Group. The Company provides life assurance, asset management, banking and general insurance to customers in Africa, the Americas, Asia and Europe. Last week the insurer released the interim results for the first half ended 30 June 2016, in which they reported that the profit after tax rose to £425 million from £419 million a year earlier. The company announced an interim dividend of 2.67 pence, and stated that the final dividend is likely to be at the “mid-to upper-end of cover range of 2.5 to 3.5 times adjusted operating profit.

Value Unlock

Old Mutual Plc's decision to break the 170-year-old company into four units aims to boost shareholder value by cutting the conglomerate discount, debt and central costs. The split into Old Mutual Emerging Markets, Old Mutual Wealth, Nedbank and Old Mutual Asset Management follows a strategic review by CEO Bruce Hemphill, who joined in November last year. The insurer's exposure to hard currency earnings (dollars and pound) gives it a unique diversifier. The group is also growing faster in Africa through acquisitions, although it stated in the recent report that it does not plan to expand aggressively through acquisitions before separation. We expect the group to list Old Mutual Emerging Markets (which is 48% of group revenue).

Insurance business accounts for just under half of Old Mutual's pretax profits. The group has life and savings businesses in Africa, the U.K., Italy, Latin America and Asia, and underwrites property and casualty business through Mutual & Federal. Life premiums have fallen following the disposal of businesses in Scandinavia, Poland, Germany and Austria as Old Mutual focused on emerging-market expansion. South Africa accounts for most of the company's insurance income, leaving revenue sensitive to rand weakness.

SEGMENTS

Bolstering Emerging Markets growth

Old Mutual Life and Savings aims to develop in emerging markets beyond South Africa. Emerging markets account for 34% of the insurer's pretax operating profit. Old Mutual has businesses in Botswana, Ghana, Kenya, Malawi, Namibia, Nigeria, Swaziland and Zimbabwe. Its Latin American presence includes Colombia, Mexico and Uruguay. The company has a joint venture with Guodian in China and a 26% stake in Old Mutual Kotak Mahindra in India. South Africa still accounts for 86% of life and savings emerging-market profit. The group's Emerging Markets announced on May 5 that it had entered into an agreement with Lloyd's of London to offer insurance coverage for commercial property, energy, construction, political risk and trade credit, mining, kidnap and ransom, terrorism, cargo, transit, delay in start-up and general aviation. Since this segment is largely dominated by the South African operations, we compared the segment to its local peers in the life insurance industry. The average multiple is depicted in the figure below:

Life insurance peers (Price to Sales ratio)	
MMI Holdings	0.79
Sanlam	1.55
Clientele	2.62
Liberty Holdings	0.50
Average	1.37

Source: Bloomberg

OM Wealth Management

Old Mutual transformed its UK wealth business by buying the Intrinsic adviser network in July 2014 and discretionary fund manager Quilter Cheviot in February 2015. The group's aim is to build a vertically integrated platform-based retail investment business offering wealth-management solutions. This also includes Old Mutual Global Investors, the UK-based investment manager. The group recently announced the sale of OM Wealth Italy to Cinven for a total consideration of about £323 million, this transaction is part of the group's commitment to divest from continental European businesses allowing it to focus on its core UK and cross border markets. The group's adviser platform rank may be hurt by Standard Life's pending M&A of Axa's "Elevate" platform. To value this segment we compared the company's price to sales ratio with some of it listed wealth management peers;

Wealth management peers (Price to sales ratio)	
Julius Baer	2.82
Ashmore	10.37
Magellan Financial	11.43

Jupiter Fund	4.76
Average	7.34

Source: Bloomberg

Nedbank's contribution

Old Mutual holds 54% of South Africa's fourth-largest bank, Nedbank. On a consolidated basis, the bank accounts for about 48% of Old Mutual's pretax operating profit. The bank operates in the domestic South African market, which is dominated by four companies. It is one of the top-two corporate banks and market leader in commercial property finance. Like Old Mutual's insurance businesses, Nedbank is expanding in Africa. In 2014, it took a 20% stake in Ecobank, which operates in 39 countries across the region. To value Old Mutual's stake in the bank we use the current price of Nedbank as of the 11th of August 2016, R214.50. The value of that investment is about £3.24 billion.

Old Mutual Asset Management

OM Asset Management, Old Mutual's US asset management arm, has seven affiliated boutique investment firms that offer a diverse range of strategies. The Boston-based company has £166.7 billion in assets under management, as of 30 June 2016. Old Mutual said on May 24 that it had received approaches from third parties to buy its stake, but said there's no certainty of a deal. Old Mutual sold 18.3% of the business in an initial public offering in October 2014 and cut its stake to 65.8% with a June 2015 share sale. Including the pre-offer dividend, Old Mutual's share sale in June 2015 raised £543.4 million and helped fund the purchase of Quilter Cheviot. OMAM announced economic net income of £27.4 million in the second quarter of 2016, which is down by 4.7% year-over-year.

On 14 June 2016, OMAM announced that it would acquire a 60% equity interest in Landmark Partners, a leading global secondary private equity, real estate and real asset investment firm.

The value of the stake, as of this writing, is £807.64 million. The full valuation on the segments is outlined below in the sum-of-the-parts model.

Valuation and conclusion

Old Mutual SOTP Valuation

SEGMENTS	2015 FISCAL NUMBERS			VALUE (million pounds)
	(million pounds)	METRIC	MULTIPLE	
OMEM	6 497.00	PS	1.37	8 900.89
OM Wealth	615.00	PS	7.34	4 514.10
Nedbank	6 000.85	Market cap	54.00%	3 240.46
OMAM	1 227.42	Market cap	65.80%	807.64

Segment valuation	17 463.09
Net debt	996.00
Total	18 459.09
# of shares	4 929.60
Value per share	£3.74
Discounted value per share (20%)	£3.00

Source: Bloomberg, our estimates, company data

We value the business using a discounted SOTP basis. We apply an upper-end discount of 20% to all parts in our SOTP valuation for the conglomerate nature of the business. While we believe this discount will be removed over time as the business delivers on its break-up strategy, we believe it is too early to remove or reduce this discount due to the uncertainties that exist surrounding the process and costs of the break up. The managed separation will be effected in a manner that maximises value to shareholders over time, however, the management expects the process to be materially complete by the end of 2018. According to our valuation the current price presents about 45% upside on a 12-18 months view.

On the 28th of June, the CEO - Bruce Hemphill, said that management has started executing the “managed separation” and they are pleased with the progress that they have made since announcing the break-up. He also mentioned that the increased market volatility following the referendum decision to leave the EU does not affect their strategy although it may impact the key performance of the underlying businesses. The firm cut 15% of its workforce at its headquarters and will see further job losses ahead of the separation. Head office will have lost 50% of its staff by the end of the year, cutting jobs to 140 from 275 and leading to savings of £10 million by next year.