Representative:

- Mr. James Starke – African Alliance
- Mr. Colm Patterson – CFO, Letshego Holdings
- Mr. Chris Low – Group Managing Director, Letshego Holdings
- Mr. Shawn Bruwer – Deputy Group MD, Letshego Holdings
- Ms. Mythri Sambasivan-George – Head of Corporate Affairs, Letshego Holdings

START OF TRANSCRIPT

Operator

Good day, ladies and gentlemen, and welcome to the Letshego Botswana conference call hosted by African Alliance Capital Markets. All participants are in listen-only mode and there will be an opportunity to ask questions after today's presentation. If you should need any assistance during the conference please signal an operator by pressing star and then zero. Please also note that this conference is being recorded. I would now like to hand the conference over to James Starke. Please go ahead.

James Starke

Thank you, Dylan. Good afternoon and good morning depending on where in the world you're dialling in from. Joining us today from Gaborone is Mr Chris Low, the CEO of Letshego Holdings, Mr Colm Patterson, the CFO, Mr Shawn Bruwer, COO, and Ms. Mythri George, Head of Corporate Affairs. We are very grateful to the management of the Letshego team for making time available to us to speak about their six months results to 31 July. Just a reminder, there is a presentation accompanying this call. It was circulated with the email sent out earlier today. Without much further ado I would like to hand over to Mr Low and his team. Thank you, Chris. You may go ahead.

Chris Low

Thank you, James, and good morning or good afternoon everybody. As James said, there is a presentation that we've sent out ahead of this call. So what I would really like to do is to walk through some key insights to our strategy and then hand over to Colm to give you some highlights on our performance. So if you do have the slides available my insights will follow those lines. And as James has again indicated we will have some questions at the end.

Strong performance, growth and returns

In summary, the first half of 2014 Letshego delivered a good set of results. We are gaining momentum with our transformational strategy and we remain committed to strong performance, growth and returns. When we look at our strategy I'd like to highlight a few points around "our house" as we call the one page vision and strategy slide. Our strategic intent is to become a broader based financial services company. And we have an aspiration to be a leading financial services group in Africa. That's not to say we want to become a commercial bank. We want to be a broader based financial services company operating at the segment space below commercial banking. Today we are already a top 40 Sub-Sahara African company by market cap ex. South Africa.

Our vision and strategy

We are, through our brand promise, committed to improving lives. I will come back to our focus on health, education and business loans. Our uniquenesses or values as listed are key and underpin our business model. They are there to drive how we engage with customers and our stakeholders while at the same time they will drive our service processes and documentation. And I would like to come to talking about the five sustainable competitive advantage capabilities that we're looking to build.

Core business

Our core business remains payroll lending, using deduction at source for collections. This still accounts for more than 90% of our book and our profit. Our biggest businesses continue to be Botswana and Namibia, while Mozambique is growing fast. We continue to find ways to improve our offering as well as to enter new segments. I will talk to this later on Botswana. And a key part of our risk management is through credit and life assurance.

Three approaches to transformation strategy

Turning to our country strategy, our country transformations. We have three approaches for country franchises. To grow, diversify or defend. South Sudan sits in the hold and divest. And as you will note from the slides and our half year announcement we are looking to exit South Sudan and are in discussions with a potential interested party who happen already to be a board member and who lend to our business in South Sudan. Exit of a country is clearly not an easy decision, and we thought long and hard about this. But, as you will recall we did provide against our book at the end of last year, and in our view conditions have, if anything, got worse. We see little prospect of turning this business into a profit making operation and in the short to medium term we see no obvious signs that we can make this a significant contributor to group. Hence the decision to exit, but to exit ideally through handing over the business on a going concern basis to an NGO.

Other key things before I come to illustrating the transformational strategy. Our provisional licence in Namibia was granted in July, and just this week Shawn and myself were there to meet the central bank to finalise a number of conditionalities that this provisional licence comes with. We are hopeful that our proposals will be accepted by the Bank of Namibia so that we can complete central bank sign-off in first quarter next year and go live shortly thereafter.

I also draw your attention to Kenya where we’re seeing significant increase in our low income housing products. This generally involves individuals or businessmen borrowing money to add an extra room to their existing premises to that they can rent it out. Clearly security over rental proceeds and/or title can be used there. And lastly I will mention Tujijenge in Tanzania. This is a minority holding that we have in the micro finance business that was acquired when we bought Micro Africa in 2012. This business makes very little money, approximately $10,000 per month. However we see no prospects for that growing significantly, so one of the other minorities, Progression Capital, has agreed to purchase that from us. Neither the exit from South Sudan nor the sale of our Tanzania micro finance business will have a material impact on our results.

Grow strategy: Mozambique

Turning to the first of the transformational strategies, using Mozambique to illustrate this, Mozambique is a relatively new business to the group started approximately three and a half years ago. It is a pure payroll business today. During those three years we have invested heavily in the branch network and today we have 11 branches. All but one of those is outside of Maputo, giving us a footprint across all regions within the country.

We obtained, as you will be aware, a deposit taking licence at the end of last year. And we launched in February of this year. However, those who have looked at the notes will quickly see that that deposit gathering process has not yielded any significant results as yet. This is because we are still rolling out the technology to open an account, a fixed deposit account. We are using biometric technology. This gives added protection to those individuals who open accounts, because in some cases their written capability is limited.

The product has been launched under the brand of ”Xitique”, which in Portuguese means savings. There is a group savings culture in Mozambique that this is designed to address. Further investment there is ongoing. We are working with the regulator as the only non-commercial bank there on mobile and agency banking frameworks. This will enable us next year to roll out the third module of our IT infrastructure, the financial inclusion module which will enable full agency and mobile banking accessibility and will complement the footprint that we have already established.

Our “invest to grow” strategy places Mozambique as our first full service operation, and we are very excited about those prospects. I hope to be able to report back on that when we do our year end report early next year.

Diversify strategy: Rwanda

Turning to Rwanda, this is a “diversify” strategy. It is one of our smaller businesses, but those of you that know the country will know the Rwandan government is being very supportive of infrastructure investment. And as with many governments they have a financial inclusion, skills deepening and rural financial services access policy. Today we have six branches of which two are in rural locations and we are looking to open several more next year. Our focus today is on low income housing. Rwanda has a well established electronic title deed registry and micro and small enterprise business loans which are mostly secured by assets, primarily property but also vehicles and other chattel. As there is no payroll deduction, we do not do payroll lending there. And last year we phased out group lending as it is too labour intensive and therefore difficult to gain sufficient momentum at a reasonable cost.

Within the next month we will be launching a current account savings transactional product. This is the diversification which will enable us to drive the beginnings of the financial inclusion agenda there. It also will enable us to start to offer rural services. Once Mozambique is live we will then roll out the full financial inclusion module to Rwanda. So a small business, but a growing one that again aligns with our strategic agenda.

Defend strategy: Botswana

The last country, Botswana, is a “defend” strategy. You will be aware it is still our largest business and it is where we started Letshego’s operations. Unlike other markets banks compete strongly in our space for payroll business. And there is a limited entry of banks into MFC here. That said, in this first half we have had a strong performance with a growth in profit before tax of 20% year on year.

Our defence strategy is focussing on finding new customer segments and introducing new products that align with the government’s agenda. We have already started working with the mining sector offering payroll loans to unionised staff and most recently we’ve launched a home improvement loan in line with the government’s policy on low income housing.

To ensure we have successful growth in our business we are growing our direct sales force. And we are piloting our call centre as an outbound sales unit as well as an inbound service centre. This is enabling us to pull back in customers who used to borrow from the banks and today our offering is well trusted in this market. So we are building on our existing business.

Sustainable competitive advantage

So our franchise growth strategy is quite clear. To enable that to happen effectively and successfully we believe we have to invest and build sustainable competitive advantage in five key areas. In the customer experience side of things, to give you a flavour for that, we have established a set of standards. The photograph you can see on the right there (slide 10 of the results presentation) is our new Dar es Salaam main branch which has just been completed. And in addition we are in the process of expanding our brand research with a view to identifying where we need to improve our product offering to ensure that we are living our uniqueness and additionally we are rolling out additional sales and service training for micro and small enterprise lending.

Interestingly in a number of countries – Rwanda and Uganda come to mind immediately – because of our focus on financial inclusion the strategy is being funded on the training side through technical service providers. They lend us money and often will offer up to 10% in a grant towards delivery of our strategy.

Under innovation this covers primarily our rollout of banks. This year we've rolled out Lesotho, Namibia, Botswana and Mozambique (earlier this month). We also have an integrated communications network across our footprint and our data centre is based near OR Tambo in South Africa.

Risk management I will come to on the next slide. On people development we are investing heavily in leadership, management, facilitation and communication skills. We have now an extended leadership below the CEO level and we are in the process of rolling out a one-day programme to all staff covering our vision and strategy. We have also introduced talent management and an enhanced performance management programme to align behaviours with delivery of our strategy.

And lastly on stakeholder engagement, meeting with government and regulators is now part of our regular group management committee visits to countries. We have tested experiential marketing with our customer base in Tanzania using the World Cup as a basis for that. And we really do believe we have to do much more to ensure that our messaging as to both our vision and strategy as well as our customer focus and product set are clearly understood by all segments.

Effective and prudent risk management

Risk management, briefly. I'm sure many of you are aware of our end-to-end holistic approach to this. We have to be highly effective and prudent in our risk management and there has been absolutely no change in that since our last six monthly update.

Our payroll business I've already mentioned. Credit and life insurance policy. And in the slide (slide 11 of the results presentation) you can see some of the other elements of ensuring that our staff is suitably equipped to run and effective risk management framework. Our provisions I will mention at this stage – Colm will come back to impairments a little later – are in line with IFRS and we are studying the latest prudential guidelines which will become effective in 2018 to establish whether additional provisioning may or may not be required. At this stage, as the graph shows, we have achieved good strong asset growth without compromising on asset quality.

Progressing diversification and leverage

Two more slides before I hand over to Colm. Balance sheet diversification and leverage is another key leg to our strategy. We are finding it is a successful strategy to increase the number of funders who will provide local currency funding. This is particularly important. As you will be aware one of the volatilities in our P&L has been foreign exchange risk. Colm will talk to that a little more in the numbers. And also interestingly development financial institutions are increasingly interested to lend to us. About 10% of our funding now comes from them, and as I indicated before that often comes with technical assistance grants to lower our cost of doing business.

Moving to the last slide, I talked about improving lives. Research to date has shown that most of our loans are being used for education purposes, for health reasons and for business and livelihood. The current brand research will further confirm that I'm sure, as well as offer alternative areas that we might find we can finance. For example, we are doing research into the education and health sectors and we are starting some research into the agricultural opportunity. In my view, by virtue of our focus in those business and consumer segments below where banks go offers us huge potential. However, we have to ensure that we understand all the mechanics of it, all the opportunities there to keep costs to a minimum, because we want to introduce this new diversification of our business in a sustainable manner.

And as you will be aware this space is usually occupied by not for profit NGO businesses. However, we have cost and technology advantages that they do not have, and in this way I do believe we will be able to establish mechanisms by which we can enter this segment.

So I'm going to now hand over to Colm. He is going to present some more granularity behind the results we have achieved. Hopefully what I've given you now gives you some more granularity and insight into our transformational strategy. Thank you.

Colm Patterson

Okay. Thank you Chris and good afternoon, good morning, good day to everybody. Let me just take you through some of the figures in terms of where we are. Overall I think we're very happy. We think this is a very positive performance for the six months to July. Chris has spoken about some of the things that we're doing in terms of looking to diversify the business. And there are a number of other things happening in terms of system changes. Notwithstanding those things that were going on we were still able to produce what we think are a very positive set of figures.

Growth in assets

In terms of growth on the balance sheet side of things the big three were still the main contributors, which is Botswana, Namibia and Mozambique. They preformed very well for this period again. Notwithstanding that there was, albeit off a lower base, very good growth from Kenya, Rwanda and Lesotho, and to a lesser extent from Swaziland. However, we have touched on it a little bit earlier on, and we are going to touch on it again and again, that the growth hasn't compromised the quality of the book. And that's a very important fact. It's not growth for the sake of growth. It's growth where markets allow under competitive environments, but also that has to be good quality.

Revenue mix

From a revenue side of things we are satisfied that the revenue is growing at a faster pace than costs. We are investing where we need to invest in terms of our costs, but the revenue side is growing faster. Yields on the overall loans and advances to customers remain consistent period on period. And we have indicated in the past that there has been a downward trend slightly in those yields, and that is likely to continue going forward, however that is coupled with the introduction of other revenue lines that can compensate for that slightly. Period on period we were able to keep the overall yields fairly consistent. So net interest income if we strip out the impact of foreign exchange gains and losses period on period increased by 22%, which was close to the increase of 21% in loans and advances to customers. So, overall, we were quite satisfied with that.

Efficiency and profitability

In terms of efficiency and profitability, we touched on the revenue lines' yields remaining consistent. From a cost of funding perspective our cost line has remained consistent. When you look at the income statement the interest expense line fluctuates a bit, but that is due to some open forex positions that we made a gain on last year but a small loss in this period. We're not in the business of predicting forex rates, so we do want to close them off as soon as possible. We have made reasonable progress in that. Our two main open forex positions are a position in Meticais, Mozambique Meticais, and a net Rand position. So we have been able to take some steps to address those and further steps will be taken during the course of this year. We won't fully close them out this year but we should be able to mitigate to a large extent.

Expenses have increased, albeit it a lower rate than revenue. And we are investing in terms of the overall franchise, and that has resulted in a cost to income ratio of about 28% which is slightly lower than last year. And it is in the sort of range we would expect going forward, maybe slightly higher going forward. All of that gave a reasonable increase in profit before tax. Because our profitability is being generated more outside of Botswana than inside of Botswana that has resulted in a tick-up in the overall taxation expense. Previously our blended tax rate was closer to 22%. It has ticked up to about 26% and we are looking at options and ways of trying to address that. Obviously that has to be in the context of transfer pricing rules to be adhered to, thin capitalisation rules etc. But there are some opportunities we have to try and look at containing or slightly reducing going forward the tax rate. But that is something we are working on.

All of that results in earnings per share increasing slightly, just 1% period on period. however, going forward we are not expecting any further dilutive impact, so profit after tax and earnings per share should be reasonably aligned going forward.

Asset quality

Asset quality, again just to stress that the expected range is between 1% and 3%. We have given guidance on that in the past, and we did come within that range. It is very much an area of focus. We are looking to explore opportunities that we have to grow, but not at any cost. It has to be good quality growth. So we were satisfied with the quality of the assets that we have on our balance sheet.

Capital and liquidity

From a capital perspective we do have a very strong balance sheet. We are very well capitalised and we are looking to increase our level of debt going forward. We did see the debt to equity ratio increase from 25% to 39% period on period. That is an area that is getting a lot of focus, and we will continue to do so.

And finally before I hand back to Chris, the Board did look at our dividend policy and we are pleased to report that the board decided that we would increase our dividend payout ratio from 25% of profit after tax to 50%. That is effective now from the interim dividend that has been declared, and we will look to maintain that going forward. So hopefully that will be seen as a very positive signal in our confidence in the business and our prospects going forward. So with that I think I will hand back over to Chris to wrap up.

Chris Low

Thanks, Colm. Just to summarise, we clearly remain committed to delivering strong performance, growth and returns. Our transformation strategy focuses on growing our core payroll business, on diversifying through invest to grow, diversification or defend approaches in our key countries. We are building technical assistance and other partnerships to drive and support our businesses, and we will continue to build capability to enhance our sustainable competitive advantages.

Effective balance sheet, risk and cost management will remain key to our operating model, and it is our intention looking forward to ensure that revenue growth can support the investment side of our cost equation. We want to have “positive jaws”, faster growth in revenues than cost growth and on an underlying basis we have achieved that in these six months results. Lastly our strategic commitment is to financial inclusion, financial deepening and good ESG principles. Thank you very much. Back to you, James.

James Starke

Okay. I think all that remains is to thank Chris and the team for their time. Just to let everyone know we will have a note out earlier next week on our updated views on Letshego. Wishing everyone a happy weekend.

Chris Low

Thank you. Goodbye.

Operator

Thank you very much. On behalf of Letshego Botswana and African Alliance Capital Markets that concludes this conference. Thank you for joining us. You may now disconnect your lines.

END OF TRANSCRIPT