PRINCIPLES AND PRACTICES OF THE FINANCIAL MANAGEMENT OF METROPOLITAN'S DISCRETIONARY PARTICIPATION PRODUCTS

Client summary

Smoothed Bonus Portfolios

This document summarises how Metropolitan manages its smoothed bonus portfolios, and explains where and how we invest, how we smooth and what bonuses we declare. It focuses on the management of the pooled investment portfolio and not on all the finer details of the different policies.

Metropolitan follows the obligations stated in the policy contract and complies with any legal and regulatory requirements. If there are any differences between this summary document and the policy contract and legal requirements, the contract and legal requirements will be considered final and correct.

What are discretionary participation products?
These are products that rely on the ability of the insurer to use its discretion (decide what is in the best interest of the policyholder) to manage them with regards to investment, smoothing and bonus declaration.

Managing discretionary participation products requires trust between policyholders and Metropolitan. Metropolitan takes decisions that are in the best interests of policyholders and the sustainability of the portfolios. Sustainability of the portfolios means that Metropolitan will use and invest the policyholders' money wisely.

What is a smoothed bonus portfolio?
A smoothed bonus portfolio is an investment in which your money is pooled with other policyholders' money. The returns to policyholders are 'evened out', or smoothed, over a number of years. This means that the bonuses paid in one year may be higher or lower than the actual investment returns in the stock market.

How does a smoothed bonus portfolio work?
Metropolitan invests the pool of money contributed by you and other policyholders in a range of suitable assets such as shares, bonds, property, cash and offshore assets, and we manage the portfolio for all the policyholders. The actual investment returns in the market earned on the pool of assets may vary from year to year, and may sometimes even be negative.

Metropolitan divides the smoothed bonus portfolio's returns to policyholders by a process known as a bonus declaration. Metropolitan declares bonuses that are more stable than the actual investment returns in the stock market, which is why the bonuses we pay within a given year are likely to be higher or lower than the actual investment returns in the stock market in the same year.

Who should invest in a smoothed bonus portfolio?
A smoothed bonus portfolio is a suitable choice for policyholders who are looking for long-term (more than five years) growth on their investments, and who also want protection against sudden and unpredictable changes in the equity, property and bond markets.

How does smoothing affect my policy?
Your policy has an investment account that works similarly to a bank account. Your investment account balance grows as you pay your premiums. It also grows with the bonuses that Metropolitan declares. It shrinks when money is paid out to you in claims and when Metropolitan charges fees.

What fees does Metropolitan charge?
Metropolitan charges you to administer the policy and in some cases to pay shareholders for providing guarantees (see below). The charges depend on the type of policy you have. Your policy contract will explain this in more detail.

What are the guarantees?
On some types of policies, Metropolitan guarantees a minimum payout when your policy reaches its end date as stated in your policy contract, or when it matures. When your policy matures, you will receive the higher amount of your investment account and the guaranteed maturity value. Your policy contract explains the guarantees that apply to your policy.

How does smoothing affect my payout?
Metropolitan pays you the benefits from your policy if you were to die or to retire, or when your policy matures. Because of smoothing, the payout may be higher or lower than the market value of your policy's share of the assets in the portfolio at the time. This will work in your favour if stock markets are down, but it may be less favourable to you if stock markets have performed well before we pay out.

What will happen to my investment account if I decide to cash it in before the end date or retire early?
Your payout may be subject to a market value adjustment, or MVA (see below), which means that the money in your investment account will be reduced. You will also be charged an 'early termination' fee, in line with South African Law. Please speak to your adviser for more information about the 'early termination' fee.

What is a market value adjustment?
When markets are down, the value of the assets in the pooled smoothed bonus portfolio is often lower than the value of all the policyholders' investment accounts that share in the pool. If this is the case, we may reduce the investment accounts of policyholders who cash in their policies early by a market value adjustment, or MVA.

If Metropolitan did not reduce the investment accounts by the MVA of those policyholders who cancel their policies early, these policyholders would receive more than the actual value of their policies at that time. This would mean that the policyholders whose policies stay invested would receive lower bonuses in future, which is not fair to those policyholders.

An MVA will not apply on a contractual claim event such as death or maturity.

How does Metropolitan decide on the bonuses to declare?
Depending on the economic outlook and interest rate forecasts, Metropolitan decides what a long-term, sustainable level of bonus would be. We may use returns that were earned in previous years, but which have not been distributed as bonuses, to increase the bonus rate in the current year or in future years. Similarly, we may hold back part of the returns earned in the current year and use these to increase bonuses in future years.

Returns not distributed as bonuses in a particular year stay in the pool of assets, and Metropolitan will distribute these to policyholders at a later stage. Metropolitan may not keep any of these undistributed returns.

When we declare bonus rates, different groups (called a bonus series) of policyholders may receive different bonuses. The bonus series that your policy falls into depends on when you took out your policy, the type of policy (for example, whether it is an endowment or a retirement annuity), the fee structure and the tax treatment of your policy.

The Board of Directors declares bonus rates based on advice from the Statutory Actuary.

When are bonuses declared and applied?
Metropolitan declares bonuses once a year shortly after the end of its bonus year. The date on which bonuses are declared is called the declaration date. Metropolitan applies the bonuses retrospectively for the bonus year just completed up until the declaration date.

The payment date for benefits to your policy often is not the same as the declaration date. For this reason, Metropolitan adds an interim bonus to your investment account from the last declaration date to the date of the claim event (e.g. death, surrender, maturity or retirement) to make sure that your policy also receives the benefits of investment returns since the last bonus declaration. We can revise the interim bonus rates during the year.

Can bonuses be taken away?
Metropolitan declares two bonuses each year: a total bonus and a vesting bonus.

The total bonus is the sum of the vesting bonus and the non-vesting bonus.

The vesting bonus applies to the vesting fund and cannot be taken away at policy maturity or earlier death, however it is not guaranteed in the case of full surrenders, partial surrenders or other withdrawals of funds before the policy terminates.

The non-vesting bonus is the difference between the total bonus and the vesting bonus. This is the portion that Metropolitan can take away. Therefore, if the value of the assets in the smoothed bonus portfolio drops significantly, and the investment returns in the market are unlikely to recover soon, Metropolitan may take away part or all of non-vested bonuses to protect the portfolio and make sure all policyholders are treated fairly. But this only happens in extreme cases.

How are the underlying assets invested?
The pool of money is invested in a balanced portfolio of different assets to make the most of the expected returns, while at the same time limiting the risk of a large drop in the value of assets.

How can I get more information?
You can view a more detailed document called Principles and Practices of Financial Management of Metropolitan discretionary participation products (PPFM) at www.metropolitan.co.za or request it from your financial adviser or from our head office.

Metropolitan head office:
PO Box 2212, Bellville, 7530
Tel: 0860 724 724
Fax: 021 940 6142
Email: info@metropolitan.co.za