COMPETITION TRIBUNAL
REPUBLIC OF SOUTH AFRICA

Case no: 32/LM/May05

In The Large Merger Between:

Santam Ltd & Kagiso Newco Acquiring Firm

And

Nova Group Holdings Ltd Target Firm

Reasons for Decision

APPROVAL

1. On 29 June 2005 the Competition Tribunal issued a Merger Clearance Certificate unconditionally approving the merger between Santam Ltd and Kagiso Newco and the Nova Group Holdings Ltd.

THE TRANSACTION

2. The parties to this merger are Santam Ltd ("Santam") and Kagiso Newco and the Nova Group Holdings Ltd ("Nova Group").[1] Sanlam holds approximately 53% of the issued share capital in Santam.[2] Kagiso Newco is a wholly owned subsidiary of Kagiso Treasury Services (Pty) Ltd ("KTS").

3. The Nova Group together with its shareholders and Santam entered into a shareholders agreement in terms of which Santam acquired the entire issued share capital and claims against the Nova Group, and Santam sold the entire issued share capital of its wholly owned subsidiary Santam Risk Finance Limited ("SRFL") to the Nova Group. In turn, Kagiso Newco acquired 33.3% of the entire issued share capital in and claims against the Nova Group. Post-merger, Santam and Kagiso Newco would hold 66.7% and 33.3% in the Nova Group respectively.

RATIONALE FOR THE TRANSACTION

4. The stated commercial rationale for the proposed transaction is the creation of synergies between the merging parties' businesses as they complement each other. Nova Group's shareholders are currently exiting their non-core investments hence the present deal.[3]

The merging parties' activities

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[1] Nova Group's shareholders are the Munchener Ruckversicherungs-Gesellschaft Aftiengsellschaft ("Munich Re"), Munich Reinsurance Company of Africa Ltd ("MroA"), Capital Alliance Holdings Ltd ("CAL") and Share Incentive Scheme.
[2] See page 2 of the transcript of 29 June 2005.
[3] Paragraph 3 at page 4 of the Commission's Competitiveness Report.

5. Santam provides short-term insurance policies for all classes of business including alternative risk transfer ("ART"). It provides its ART business which consists of both cell-captive[4] and rent-a-captive products,[5] through SRFL. It also controls underwriting managers. Santam's parent company, Sanlam, is a registered long-term insurer which provides long-term insurance polices and also some ART based long-term insurance products.

6. Kagiso Newco is a newly formed company not trading at the moment. However, there exist a number of firms within the Kagiso Group offering a diverse range of products. Both Kagiso Treasury Services and Kagiso Treasury Solutions provide treasury services. Kagiso Risk Solutions is the current holder of a short-term insurance licence which permits it to provide cell captive and rent-a-captive product, but it has never traded. Kagiso Trust Investments (Pty) Ltd ("KTI") has a 10% shareholding in Metropolitan Life ("Metropolitan"), a long-term insurer. However, KTI does not have control of Metropolitan.

7. The Nova Group, a target firm, is a holding company which provides goods or services through its subsidiaries Nova Risk and Nova Life. The former is a short-term insurer which primarily offers cell captive products and underwriting management of various classes of insurance. It also provides rent-a-captive products to a limited/lesser extent. The latter company provides cell captive life assurance products in terms of the long term insurance licence.

COMPETITION ANALYSIS

Relevant Market

Product market

8. Both firms operate in the short and long term insurance markets. Within the short-term insurance market, in addition to the provision of insurance business through underwriting managers, they both offer ART (cell captive and rent-a-captive) products. Within the long-term insurance, they offer some ART based long term insurance products, i.e., cell captive products. It is therefore clear that product overlaps exist in respect of the provision of cell captive and rent-a-captive short term ART products, underwriting management, and in the provision of cell captive ART based long term insurance products.

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[4] According to the Commission, a cell captive insurer operates on the basis that each client is issued with a cell and each cell carries a different dividend entitlement relating to the insurance business of a particular cell and is issued to the cell owners with appropriate and negotiated level of share premium that provides the requisite solvency of the cell captive insurer to underwrite. The issued share capital, share premium and retained earnings comprise the solvency capacity of each cell to fund the particular insurance business of the particular cell owner and will differ across the cells. Further to this, Cell owners can use separate cells to separate cells to sell third party insurance.

[5] We were told that rent-a-captive is a variation of captive insurer and entails a large corporation insuring its aggregate deductible where it believes that only a continued bad claims experience will result in the deductible being exceeded. In this case, deductible is paid to a rent-a-captive as a premium. The corporation will then pay its deductible responsibilities up to the amount of the aggregate deductible out of the rent-a-captive; thereafter the insurer bears the losses up to an agreed limit.

9. As previously defined by the Tribunal,[6] ART products are a specialised form of short term insurance, a non-conventional, more creative and flexible method of financing risk. The Commission contended that short-term cell captive and rent-a-captive constitutes a market on its own in that an insurer is required to have a licence to provide short-term ART cell captive and rent-a-captive products. Both the Commission and the merging parties contended that ART, which is another form of short-term insurance, is a separate market from the traditional short-term insurance.[7]

10. The merger filing reflected that both Santam and Nova Group conduct insurance business through underwriting managers. Although they are involved in the underwriting management business, there seem to be some differences between them. Santam controls underwriting managers who underwrite specialist classes of insurance business on its behalf whereas Nova Group does not control these underwriting managers. The Commission contended that underwriting agencies operate in a particular line of short-term insurance to the extent that their operations can only substitute each other if they operate in the same niche. According to the Commission, if an underwriting agent has developed expertise and specialised knowledge in crop insurance his skills will not be applicable in marine work and vice versa. In light of this, the Commission viewed the relevant underwriting management market as peculiar to the specialised niche services offered by the parties, such as motor, transportation, accident, health and property guarantee, liability, engineering and miscellaneous.

11. Insofar as the long-term ART product is concerned, the Commission defined the relevant market as the long-term cell captive market.

12. We need not make a definitive finding on the relevant product market because, in our view, the transaction would not result in the substantial prevention or lessening of competition regardless of any market definition adopted.

Geographic market

13. According to the parties, the ART products are structured in a global environment. We were told that about 50% of the worldwide ART business is generated in New York. The parties contended that South Africa's ART market is relatively new although it has grown significantly in recent years. The Commission argued that the relevant geographic market appears to be international.

Market shares

14. According to the market share data submitted by the Commission and the merging parties, both Nova Risk Partners Ltd and Santam Risk Finance Ltd would have a combined market share in short-term cell captive and rent-a-captive market of 22% on par with that of RMB Structured Insurance Ltd. Guardrisk Insurance Company was the top market leader with 40% market share whilst M&F Risk Financing Ltd enjoys only 9%. In the long-term cell captive insurance market, the merged entity (i.e., Nova Life Partners and Sanlam Customised Insurance) would have about 12% market shares. The other significant players are Momentum Mobility (36%), AIG Life South Africa (33%) and

[6] See the Tribunal's previous decision: *Santam Ltd and Allianz Insurance Ltd*, Case No.: 28/LM/May02.
[7] See the Commission's Report, page 6.

Guardrisk Life (20%). Also apparent from the market share figures is that Nova enjoys a relatively low market shares in the underwriting management of various classes of insurance.[8]

Public Interest

15. According to the merging parties seven (7) employees would be affected by the proposed transaction as it would result in the duplication of services within Nova Group and Santam. They contended that these affected employees are very marketable in the financial sector and would be likely to find alternative jobs. The parties gave an undertaking at the hearing that the affected employees would not be more than five (5) and that they would try to absorb them into Santam[9] They further submitted that the deal was pro-BEE as it created an opportunity for Kagiso Trust, a pre-eminent empowerment investment banking services group, to obtain shares in the insurance market.[10]

Conclusion

16. The Tribunal is satisfied that it is unlikely that the merger will lead to lessening or prevention of competition in the relevant markets. There are no significant public interest issues which would alter our conclusion.

Y Carrim **04 August 2005**

Concurring: U Bhoola, M Mokuena

For the merging parties: Ms Coreen Fouché (Jan S De Villiers Attorneys).

For the Commission: Edwell Mtantato (Mergers and Acquisitions).

8 Paragraph 7.3, page 8 of the Commission's Competitiveness Report.
9 See page 5 of the transcript, 29 June 2005.
10 Page 15 and 46 of the record.