CEO's report

The Peregrine group produced an acceptable set of results, under very difficult market conditions, for the year under review. Notwithstanding the highly uncertain environment, the group's operating subsidiaries produced an aggregate operating profit of R355,9 million after accounting for all minority interests and deducting group head office costs of R16,7 million. All of the group's divisions remained comfortably profitable for the period.

This level of operating profit includes minimal performance fees for the year under review, in contrast to the previous year in which record performance fees were earned. The absence of performance fees is the principle reason why profit from the group's existing South African operations was 47% lower than the previous year.

The group's earnings were further dampened by negative returns on its proprietary investment portfolio as well as a swing from net interest received to net interest paid for the year.

A feature of the year was the acquisition of a controlling interest in international wealth and asset manager Stenham Limited, effective 4 April 2008. This helped boost both the annuity and foreign currency component of the group's earnings as well as increase its assets under management by 87% to R80 billion at year end.

Results

Whilst operating revenue increased by 41% (boosted by the acquisition of Stenham), total income of R1,45 billion was only 9% higher than the previous year as a result of the negative returns earned on the group's proprietary investments.

The 72% increase in operating expenses primarily resulted from consolidating the Stenham operations for the first time. If the Stenham expenses are excluded, operating expenses (including profit participation) declined by 11%.

Interest costs on external funding raised at the beginning of the year resulted in the group moving into a net interest paid position for the year of R49,1 million from net interest received of R64,5 million in the previous year.

Attributable earnings were reduced by the amortisation of intangible assets resulting from the Stenham transaction in the amount of R19,5 million. By excluding the effect of this amortisation, basic earnings per share decreased by 71% to 64.6 cents per share.

Headline earnings per share decreased by 85%, the principle adjustment between basic and headline earnings being the deduction of the surplus on the sale of the group's Sandton head office property as required by Circular 8/2007 "Headline earnings".

Operating highlights

Due to the substantial minority interests which exist in both the asset management and group investments results, the operating highlights are presented on a pro forma "after minorities" basis as set out below. The results are reflected at the operating profit level, on a pre-tax basis. This is considered to be the most appropriate basis on which to assess the results. In addition, these pro forma earnings are shown before the amortisation of intangible assets in order to most closely represent the cash generation of the underlying subsidiaries. Minority interests in the income statement are accounted for on an after-tax basis.

	Profit from ordinary activities as per the income statement		Pro forma profit from ordinary activities before intangible amortisation adjusted for minorities		% of profit from ordinary activities		% of profit from ordinary activities before intangible amortisation adjusted for minorities	
	2009 R'000	2008 R'000	**2009 R'000**	2008 R'000	**2009**	2008	**2009**	2008
Wealth and asset management	**115 201**	317 460	**102 676**	265 638	**24**	60	**28**	55
Wealth management	**82 810**	165 251	**84 294**	166 735	**17**	31	**23**	35
Asset management	**32 391**	152 209	**18 382**	98 903	**7**	29	**5**	20
Broking and structuring	**152 594**	216 020	**152 594**	216 020	**32**	40	**41**	45
Stenham	**215 098**	-	**117 347**	-	**44**	-	**31**	-
Profit from operating subsidiaries	**482 893**	533 480	**372 617**	481 658	**100**	100	**100**	100
Group	**(215 014)**	202 043	**(205 798)**	127 390				
Operations	**(16 735)**	(23 497)	**(16 735)**	(23 497)				
Investment returns	**(78 577)**	225 540	**(69 361)**	150 887				
Cost of funding	**(119 702)**	-	**(119 702)**					
	267 879	735 523	**166 819**	609 048				

Profit from ordinary activities of private client wealth management firm, Citadel, decreased by 49% to R84,3 million, contributing 23% to profit from the group's operating subsidiaries for the year. Performance fees dwindled to almost zero during the course of the year as a result of the difficult market conditions coupled with a high inflation rate. In spite of gross inflows of approximately R130 million per month and a solid relative performance manifesting in a client retention ratio exceeding 98%, assets under management ended the year 10% lower at R13,6 billion. The business remains well placed as a leader in the private client wealth management market but is unlikely to earn meaningful performance fees within the ensuing financial year.

The contribution from the asset management division fell by 81% to R18,3 million as a result of minimal performance fees generated. This constituted 5% of the group's profit from operating subsidiaries. The bulk of this contribution came from the group's hedge fund flagship Peregrine Capital. The business experienced its first year of negative returns in 10 years, leaving a high watermark which will have to be caught up before performance fees can be earned by the business. The business also experienced a level of redemptions in the second half of the year in line with the contraction in the South African hedge fund industry. These two factors were equally responsible for assets under management contracting from R3,6 billion to R2,9 billion during the course of the year. There were also changes to the Peregrine Capital management team during the course of the year which nonetheless left the original founding team in place.

Notwithstanding positive returns from several funds for the year, assets under management in the group's range of hedge funds housed within Peregrine Investment Managers (PIM) declined from R1,1 billion to R600 million. The major decline in assets resulted from the closure of a fund where the manager emigrated during the course of the year. The top performing fund, Big Rock, won the AfricaHedge Fund of the Year Award with a return of 19.8% for 2008. Peregrine remains the country's largest single strategy hedge fund manager, managing R3,5 billion in single strategy hedge funds.

Caveo, the group's fund-of-hedge funds joint venture with Investment Solutions, made no material contribution to group earnings for the period. Investment performance for the funds managed by Caveo, which are aimed at institutional investors, was positive for the period and ranked very competitively in its market space. The business achieved net inflows for the year with assets under management growing by 30% to R2,2 billion.

Peregrine Quant, the group's institutional asset manager with a quantitative focus, made a small contribution to profitability. The business experienced a 32% reduction in its assets under management to R14,9 billion at year end.

Peregrine Securities was the largest contributor to group earnings for the year. The broking and structuring activities housed within this division contributed R152,6 million or 41% of profit from the group's operating subsidiaries. The focus on growing the division's operations and on maintaining profitability momentum quickly switched to a focus on risk management and risk mitigation in the wake of the fallout precipitated by the international banking crisis from September 2008 onwards. The business did extremely well to weather the ensuing precarious market conditions without suffering any losses on its contract-for-difference or prime broking book.

The deliberate downsizing of the business combined with a meaningful reduction of market trading volumes in the second half of the year resulted in the division's earnings being 29% lower than the previous year. Earnings pressure is expected to continue in the ensuing year as trading volumes continue to decline and the business continues to feel the full impact of last year's shake out across the inter-bank, hedge fund and asset management industries.

Stenham, the group's offshore wealth and asset management subsidiary, included in the group's results for the first time, produced a level of profitability in line with expectations, notwithstanding the difficult market conditions. Profit from ordinary activities of R117,3 million which excludes the amortisation of intangible assets in the amount of R19,5 million, constitutes 31% of profit from the group's operating subsidiaries. The asset management division of Stenham which houses its fund-of-hedge fund business produced a record level of annuity profitability for the year. Assets under management peaked at $3,1 billion in August 2008 before a combination of redemptions and adverse currency movements took their toll during the course of the latter half of the financial year.

Returns for the year (which were single digit negative) on the flagship funds were substantially ahead of industry averages. The business had no investments in underlying funds that "blew-up" or closed during the period and the funds themselves remained open for client withdrawals throughout. As a result, the business remains extremely well placed relative to competitors and off a year end base of $2,1 billion is anticipating healthy growth in assets under management in the foreseeable future.

The property division, with £2 billion of property assets under management, continues to face the challenge of reduced valuations on existing property funds and investments, together with very tight conditions in the financing and re-financing market. At the same time, this presents tremendous opportunity to invest into distressed or "value" opportunities at very attractive yields and valuations. New funds are being rolled out to take advantage of these opportunities in the current climate.

We believe that the acquisition of a controlling interest in Stenham will materially impact the nature and composition of the Peregrine group going forward. We are particularly pleased with Stenham's long-term growth prospects, its annuity flows and its diversification benefits to the group both in geographical terms and from a currency perspective. The Stenham acquisition, combined with existing offshore income already earned by the group, should result in more than one third of the Peregrine group's net income being earned offshore in ensuing years.

As a result of the negative return earned on the group's proprietary investments, group investments yielded a loss of R69,4 million compared to a positive return of R150,9 million in the previous year. Whilst mark-to-market losses on the group's hedge fund and investment banking portfolios had no direct impact on the group's cashflow, they served to substantially diminish the group’s reported earnings for the period.

During the course of the year, an offer was made by a third party to purchase the property portfolio which housed the minority interest in the group’s head office building in Sandton. The group elected not to exercise its pre-emptive right to purchase the 40% interest it did not already own and as a result was obliged to exit its 60% holding at the same valuation. The consequent uplift in valuation relative to book value has not been recognised for headline earnings purposes.

Core costs at the group level decreased by 29% year on year largely as a result of lower executive bonuses reflective of the decline in reported earnings.

In the interest of presenting more meaningful disclosure, interest costs incurred on external funding of R119,7 million have not been allocated to the divisions carrying the interest but have been aggregated at a group level. Accordingly, return on group investments (net of group costs and external funding) reduced earnings by R205,8 million for the period.

With a lower level of consolidated debt outstanding, a lower interest rate applicable to the outstanding debt and a low likelihood of the negative returns on the proprietary portfolio being repeated, it is envisaged that the return on group investments for the year ahead (net of group costs and external funding) should be materially improved relative to the year under review.

Prospects

The Peregrine board has always maintained that the group’s overall financial performance will be closely linked to the investment performance of the underlying businesses, investment markets generally and the ability of the group to continue to attract and retain key members of staff.

The group has proved its ability to generate an acceptable level of profitability and cash flow even under the most arduous conditions of the last year. In contrast, the group was able to generate exceptional profits under favourable conditions in the previous year. Given prevailing market conditions and the low likelihood of material performance fees being earned within the group, the year ahead is likely to be one of consolidation for the group.

Dividend

In keeping with the stated dividend policy of paying out a minimum of 25% of each year’s earnings, the directors resolved to declare a dividend of 13 cents per share for the year. Details for the dividend can be found on page 25.

Leadership changes

On 31 December 2008, Keith Betty stepped down as group CEO in order to relocate with his family to Australia. We would like to thank Keith for the valuable contribution he made to the group in over a decade with us and for the role he fulfilled as group CEO in his final two years.

I assumed the role of acting group CEO from 1 January 2009, whereafter a number of board changes were announced, giving effect to a new leadership structure.

Effective 1 April 2009, I stepped down from the position of chairman in order to take on the group CEO role again. The board appointed Leonard Harris to the position of group chairman. Leonard is the group’s longest standing independent non-executive director and we look forward to his continued contribution in his new role. Jan van Niekerk was nominated to the position of deputy group CEO at the same time effectively assuming the role of CEO designate. Jan is now working closely with me in running the group on a day-to-day basis.

Appreciation

At the end of a particularly challenging year I would like to commend and thank our full staff complement for the steadfast way in which they have continued to look after the interests of our clients. To the various leadership teams within our underlying businesses, thank you for the passion, dedication and focus with which you run your respective businesses, regardless of market conditions.

To our board of directors, a sincere thank you for your guidance and support, both in terms of your contribution to the leadership debate as well as to all matters considered over the year.

To our clients, I would like to offer special thanks for your confidence and support. I trust that you have found us to be as engaging and available in the difficult times as in the good. Above all I hope that your experience with the group over the past year has been one which is reputation endorsing.

Sean Melnick
Chief Executive Officer
3 June 2009