PHOENIX GROUP

Q3 Interim Management Statement **5 November 2010**

Jonathan Moss
Chief Executive

Thank you. Good morning everybody and welcome to the Analysts Investor call for Phoenix Group Holdings Q3 Interim Management Statement. I am Jonathan Moss, Group Chief Executive and I have with me today, Ron Sandler our Chairman and Jonathan Yates the Group Finance Director.

I am going to speak for a few moments then Ron, Jonathan and I will be very happy to answer any questions that you have.

As you know, about a year ago we were delivering the first IMS after the Liberty transaction and are very pleased with the progress we have made since then. We have successfully dealt with some very big legacy issues and hence completed the premium listing on the LSE and in addition we have achieved inclusion in the FTSE 250 and the FTSE 350 high yield indices.

The broad theme today is one of continued delivery against our strategic objectives. Our business model is highly cash generative as policies run off and as we implement different ways of utilising our capital more efficiently so capital is released. As a result the cashflow from the business reflects both the profits we make and the capital from our capital management measures.

At the end of September the Group had received £364 million cash from the operating subsidiaries and we have a strong expectation that there is sufficient further free cash within those businesses to enable us to hit the top end of our target range of £725 million of cash generation by the year end.

In addition, we have achieved £157 million of increases in embedded value through our management actions and that exceeds the full year target of £145 million.

From a regulatory capital point of view, we continue to have an estimated surplus of £1.2 billion over the IGD requirement which is coverage of 127%. That ratio falls as equity markets rise due to the impact on the denominator. We are discussing a more sensible basis of measurement with the Regulator and they fully acknowledge the peculiarities of the existing test.

The business is actually managed as you know on an ICA basis, looking at economic capital and IGD is not a good proxy for how the ICA is moving over time. The free surplus within the life companies remains comfortably in excess of the ICA plus our capital policies.

Ignis, our asset management business has also performed well. Assets under management have increased by £4 ½ billion since the year end, up to £71.4 billion. And I am particularly pleased that a billion of that arises from net new business. It is very much part of the strategy for Ignis to build out its third party franchise.

The balance of the growth comes from repatriation of some externally managed money and from investment growth.

As a result of the agreement we reached with Tier I bondholders in April, it was necessary to undertake a share placing to settle the 2009 deferred coupon. That is going to be paid in November. For regulatory reasons because of the ATSM, the Group could not use its own cash to meet the coupon and that meant that we had to place approximately £33 million of new shares

which we did at a discount of just 3%. And although the issue was small, we are very pleased it provided an opportunity that was attractive to a number of new investors.

Operationally we continue to make good progress on the consolidation of our operations into Wythall. And in addition we have done further rationalisation of our outsource arrangements. Unisys was until recently one of our major suppliers of outsource services. During 2009 they indicated their intention to withdraw from that activity in the UK. We worked with Unisys to transfer over a million policies to Diligenta another of our providers. That insured continuity of service for our policy holders and will also in due course provide access for them to the modern administration platform BaNCs, which is a proprietary Diligenta system. We have already transferred 2 million existing Phoenix policyholders onto BaNCs.

A number of important issues remain for the Group over the coming months and in particular we recognise that the current dividend cap which is a feature of the banking arrangements continues to limit our ability to pay dividends at a level that we believe is supported by the inherent cash generation from the business. As a result, we will continue to engage with our lenders to both identify banking arrangements and to lift the dividend cap. And I expect I will be able to report on progress against that objective during Q1 2011.

So to finalise, we are the leaders in the consolidation of closed UK life funds. We believe there are many external factors which will point to the need for further industry consolidation. We believe that we have the operating model and the experience to provide the best solutions for potential vendors of those businesses and we believe in doing so we will also play a role that is very important and desirable for policyholders in fulfilling our consolidation role.

At that point I will finish and if we may operator, we will move to questions.

Question and Answer session

Question 1: James Pearce – UBS
Morning two questions. First of all can you give us a feeling for how close the internal model will be to the ICA? And second, can you just tell us how confident you are that the £2.7 billion in the bank debt will stay outside the Solvency II computation like it has been kept outside the Solvency I computation?

Answer: Jonathan Moss
Thanks James. So the internal model ultimately we are still in the process of developing the internal model. All of the work that we have done so far in terms of quantification and calibration have been in support of the standard model that obviously the European regulators have asked us to participate in. And as you will also know, we have been undertaking most recently QIS5 numbers are being submitted to the FSA and then onwards to the European Regulator even as we speak and during the course of November. The results coming out of QIS5, as we have indicated before, are pretty consistent with where we anticipated that they would be given that we already use an economic model. So there are no significant surprises emerging at this stage. But I think that is probably as much as I will say for now.

The £2.7 billion as you know is outside of the IGD Group currently, it is our expectation that that will continue to be the case. Clearly there is a level of uncertainty attaching to that because it is going to be a function of where both the European Regulator and the FSA end up. But again there is nothing we are aware of which would suggest the position would change.

James Pearce
Okay, that's great. Thank you.

Question 2: Kevin Ryan – Investec
Thank you. I would just like to explore a bit further your statement on cashflow acceleration through management actions. Could you just clarify what the remaining action is that will boost from £30 million at 9 months to an additional £195 million in the fourth quarter. Is that a tax issue? And secondly related to that, can you give us a feel for actions you are able to take going forward which will do similar things on the cash front?

Answer: Jonathan Moss
Okay, I will cover off the current position and then perhaps ask Jonathan to comment on the look forward. One of the things that we provided at the half year was an indication of the cash in excess of our capital policies, i.e. the amount of capital that we set for ourselves as being necessary to hold back in the life companies. And at the half year there was a clear excess. The reason we don't if you like take credit for management actions is that clearly cash is only useful to shareholders when it is moved outside of the operating companies and up to the Group. So if you like, although the underlying operating businesses are pregnant with the benefit of the management actions we have taken, we have not yet taken credit for that until such time as the cash moves up the Group. And that really is why we are sitting here today confident that we can deliver the top end of our target.

The actions that we have taken, they are partly tax related, they are partly related to improving the efficiency of our capital and again we have talked on previous occasions about how we get that efficiency as a result of the funds mergers that we undertake. So for example in Q1 this year we completed a rearrangement of our liabilities on the Pearl side of the Group between Pearl and National Provident Life, the old NPI, the benefit of that will be reflected later in the year as and when we take the cash out of Pearl. So there is a time lag if you like between when it is that we do these things, the recognition of the cash surplus within the life companies and then the third step of actually moving that cash from the life companies up the holding companies.

In terms of going forward?

Further Answer: Jonathan Yates
In terms of going forward, we haven't yet set targets for the management actions that we expect to deliver, but we are working on a series of initiatives which we do expect will bring forward cashflow, mostly around more efficient use of capital within the business. And we would expect to be able to give more information on that probably in Q1. Going forward beyond that of course, I mean we see this as being part and parcel of the business. This is what management is here to do, continually develop management actions which will improve the efficiency of the business and accelerate cashflow and create an enhancement to embedded value going forward.

Kevin Ryan
Great, thank you.

Question 3: Greig Paterson - KBW
Morning gentlemen. Just in terms of QIS5, will you actually be disclosing the results of that sometime next year? And if so sort of what quarter would we expect to get that information? The second one, I wonder if you could just give us an update on where your thinking is in terms of repaying the bank debt post the 10% repayment that is coming in the new year? And then a third one, I was wondering if you could give me an idea of the timing of your next sort of substantial management Roadshow? Are you going to do one now or in the new year or whenever?

Answer: Jonathan Moss
Thanks Greig. QIS5, I suspect that we will look to put forward some of the results of QIS5 probably along with our full year results and our expectation is that there will be a market move towards providing that information.

Repaying the bank debt, as we previously indicated, is the function of a negotiation or discussion with the banks that will take place over a period of time. And although those discussions are under way on an informal basis that needs to coalesce around a more formal basis of the banks putting together their steering committee and so forth. So there is nothing substantive really to add on that as we have always said, we think the main news on that is more likely to be a Q1 event next year.

In terms of management Roadshows, clearly we are always available and keen to talk to shareholders and everybody can liaise through Lorraine to gain that access. But I think that the next significant Roadshow is likely to be following the full year results in April next year.

Further question
Just one point, sorry. You were talking about people were trying to get an idea of what the QIS would look like. I didn't understand what you were saying. You said your QIS5 results are pretty consistent with the results you would have anticipated when you were considering your internal model. What does that actually mean?

Answer: Jonathan
What it means is, again as I think I said at the Half Year Results, we have our ICA calculation and in addition to that we have, we set capital policies to ensure that we can withstand the shock and still cover our ICA. We had always thought that the Solvency II results if sensibly calibrated would end up at a level which was not inconsistent with that and probably somewhere between ICA and the total of the capital policy. And that is broadly where we are with one or two pluses and minuses for the different life companies.

Further question
You were speaking about Solvency II, I was asking about QIS5?

Answer: Jonathan Moss
Yes and I am talking about where the QIS5 results have come out as well.

Further Question
So you are saying that the QIS5 results are producing a similar result to your ICA plus capital management policy at this point?

Answer:
Yes.

Greig Paterson
Thanks

Question 4: Oliver Steele – Deutsche Bank
Good morning. Two questions. First is just in terms of free surplus generation. I mean the IGD number I think we can agree is a bit of a nonsense number. But can you give us a sort of idea of the different sensitivities on the free surplus number in terms of what the effect would be of the falling interest rates in the third quarter versus rising equity markets? That is question one. And then question two is on sensitivities of future cashflows. Obviously markets are up. And actually credit spreads are slightly down this year. I am wondering therefore looking at the sensitivities you have shown in the past on your cashflows, whether we should be assuming there is some sort of potential positive swing of you know, in those future cashflows that we should be expecting?

Answer: Jonathan Moss
Okay, thanks Oliver. Yeah just to echo your comments that IGD is not a sensible basis for managing the business, and as you reflected in your note this morning, have certain peculiarities which emphasise that it is not a good measure. So we, as we have discussed before, managed the business very much on the basis of the economic capital, ICA plus capital policy with the intention of distributing the excess over that. We haven't sort of formally put any sensitivities out other than aggregate cashflow. I think it is fair to say however that the number that we produced for the half year of I think £538 million has gone north. But we are not giving any further guidance beyond that. The sensitivities we gave at the half year for the five year cashflow remain the most up-to-date guidance we have got on how cashflow changes as markets move.

Further question
Just coming back on that. I think you said sensitivities to a falling equity market, which was £32,000 million improvement in cashflow over five years from a 20% fall in equities. I mean equity markets must be up 15% since the half year. Can we apply the same sort of calculation in the opposite direction?

Answer: Jonathan Moss
I would not like to sort of give you an immediate off the top of my head answer. I would like to go away and think about that if I may. So perhaps we can take that one on board.

Question 5: Mikael Bergland – TPG Axon
Good morning. It is actually relating to Oliver's questions. Looking at the strong equity market moves since June and remember your earlier disclosed sensitivities on gross EEV, is it fair to assume that EEV may have increased in a fairly material way since the half year?

Answer: Jonathan Yates
Well again I don't think we can be over specific. We don't publish our quarterly EEV numbers. But clearly what we did do is illustrate sensitivities around market movements in terms of EEV. And the EEV to be clear, it is a lot more sort of binary in the sense that what market falls which drive the redemption in EEV do tend, the opposite tends to work the opposite way and it is a good prophecy, not exact but pretty close.

Further answer:
And sorry just to re-emphasise Jonathan did make the point that we did actually deliver the top end of our projected management actions on embedded value management actions and they exceeded our target by a very small amount basically.

Question 6: Trevor Moss – Berenberg
Good morning gents. Just a couple of very quick ones really. The first one relating to the contract you dealt with, Royal London, when you sold them the business a couple of years back when you acquired Resolution. I just wondered, then having lost the Santander business, whether there is any claw back under the original sales contract you had with them? That is the first one. The second one, just simply if you could give us an update on the performance of IGNIS year to date in terms of the number of funds where they have hit into the upper quartiles and also the success of some of the fund launches that they have had recently? Thanks.

Answer: Jonathan Moss
There are no outstanding provisions in our relationship with Royal London in relation to the recent deal they have with Santander so that is entirely an issue for them. In terms of Ignis performance. As I have indicated, broadly a billion pounds of net new money, much of which is in the liquidity funds as at the half year. Off the top of my head their performance is currently that 10 of the 13 main mandates for the life companies are performing ahead of benchmark. I haven't got with me the third party underperformance. So again I might ask Lorraine to liaise with you on that.

Trevor Moss
Okay that's fine. Thank you very much.

Question 7: Duncan Russell – JP Morgan
Hi, good morning. First one was just a general one on Solvency II and from your discussions with the FSA or the European bodies, whether you thought that there might be a QIS6, i.e. was your sense that QIS5 was going to be it or whether it might actually be extended? And the second question was, could you just remind us how much of the assets in the with profits fund are in equities please? Thank you.

Answer: Jonathan Moss
Thanks. I do not believe that we are expecting a QIS6. I don't know Jonathan whether you have any sort of different information on that?

Further Answer: Jonathan Yates
I certainly don't have any different information. I think it is very much down to what people see coming back from QIS5 at the moment and that is still unsure.

Okay in terms of the assets of the with profits fund, it does vary and we do have in excess of a dozen with profits funds. It tends to be the case that distressed with profits funds have very little equity exposure, so the old Phoenix and London, the old NPI which was National Provident Life, London Life, tend to be very largely corporate bond gilts and cash. The healthier with profits funds like Pearl and the old Britannic would be broadly 50% of the fund invested in growth assets which would typically be taken to be equities, properties, private equities and so forth. The thing about those with profits funds is that they are self supporting. They cover their own ICA, they cover their own capital policy and it is because they have got those significant amounts of working capital, that is what gives them the ability to be able to afford to take risk. So the one thing I would say about them is even though they have got equity exposure, they are very largely self contained and the shareholder capital exposure is very much as the lender of last resort rather than we would expect to see any requirement for shareholder support for pretty significant movement in the equity market.

Question 8: Greig Paterson - KBW
This is a clarification just on the Ignis cashflows. I wonder if you could just tell us what the, is that £1 billion net or gross? What is the net?

Answer: Jonathan Moss
That is gross sales less redemptions is a billion pounds and that is across all of their, both their active mandates and as I say their liquidity fund which is where the majority of the growth has been.

Further question
Is that third parties?

Answer: Jonathan Moss
The billion I am referring to is third party money yeah.

Further question
And then what is the excluding the £2.8bn, what is the in-house funds net position?

Answer: Jonathan Moss
Well obviously you have got the increase in the value of the assets offset by the run-off of the life funds as we pay claims.

Further question
Sure, what was the run-off in the life funds that is what I am trying to work out?

Answer: Jonathan Moss
I think it was broadly £4 billion-ish.

Further question
And then you have another £2.8 from Henderson?

Answer: Jonathan Moss
Well from another third party member which is not Henderson.

Further question
Right, so that is 4, including or excluding the £2.8bn?

Answer: Jonathan Moss
Sorry, that is all of claims paid.

Further question
Okay so net was 2.2 or whatever, no 1.2

Answer: Jonathan Moss
I can't do the maths in my head. Probably worthwhile following up with Lorraine on that.

Greig Paterson
Thank you.

<u>Question 9: Oliver Steele – Deutsche Bank</u>
Just to follow-up Greig's question, is that £4 billion year to date?

Answer: Jonathan Moss
Yes it is.

Oliver Steele
Okay, thank you.

Operator:
We have no further questions coming through. So I will hand you over to your host, Jonathan Moss to conclude or for any closing comments.

Jonathan Moss
Okay, well if there are no further questions, thank you everybody for joining the call. And look forward to talking to you in the coming days and weeks. Thank you very much.

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