Investor Teach In

Friday 24th June 2011

Jonathan Yates: Group Finance Director

Good afternoon everybody. Thank you very much indeed for joining us here on HMS Belfast this afternoon. I did read somewhere recently that Belfast isn't actually floating it's sort of sitting on the bottom – a bit like our share price really.

Our CEO Clive Bannister, Lorraine and I spend a lot of time talking to all of you about the financial side of our business, but we rarely get the opportunity to take a closer look at the operational side of our life insurance run off business Phoenix Life.

Phoenix is the largest consolidator of closed life funds in the UK, and our business model is quite simply the profitable run off of closed fund life assurance businesses. But to achieve this objective in the most efficient and therefore the most profitable way possible it's essential that we define a single business model for the run off of life assurance, that not only encompasses the run off of (recording breaks) but which also provides a template for future acquisitions which will come to the Phoenix Group.

This is what you'll have heard us said or refer to previously as the Phoenix Way. And whilst we can't claim to have reached the end point of this particular journey, and now we're managing the perfect life assurance company, we are clear about the direction of travel and we are making very good progress. And that's exactly what we're here to talk about today. So I'm joined this afternoon by my colleagues from Phoenix Life who will be talking to us about some of the operational detail that underpins what it is that makes Phoenix Life the centre of operational excellence within the Phoenix Group.

So, first of all we'll hear from Mike Merrick, who's the Chief Executive of Phoenix Life, who will give us an overview of the business before he hands on to Andy Moss, our Finance Director, who will take us through the financials, and then we'll hear from Pete Mayes, our Chief Actuary, and last and by all means least we'll hear from Tony Kassimiotis who'll be talking to us about outsourcing and operations. We'll then finish off with Q&A, and if you have any questions at all obviously we'd be delighted to try and answer those as best we can.

So, with that I'll hand over to Mike. Thank you.

Mike Merrick: Chief Executive Phoenix Life

Good afternoon. Thanks Jonathan. I think I'd like to start by saying it's really good to be here on number one court this afternoon. Jonathan and Clive obviously appear on Centre Court for the regular results announcements but it's good to be out on the show courts and, as you might expect, Serena is on number two court and she's still fed up about it.

So, our aim today is to give you a much greater insight into Phoenix Life and how we, as the management, add value for shareholders and for policyholders.

First of all I'd like to start with a few facts and figures. So Phoenix Life consists of seven life companies, it's got 13 with profit funds, and we have six non profit funds, and over 6 million policyholders, and 580 full-time employees, principally based in our Phoenix Life head office just outside Birmingham.

So, some figures; we've got £57 billion of assets within Phoenix Life compared to the Group total of £67.5. There is a slight apples and pears comparison there, but I think you get the message. £388 million of IFRS operating profit, compared to the Group total of £373. £3.6 billion of MCEV out of a Group total of £2.1 billion the big difference there being the Group's debt. And £708 million of operating cash generation out of a group total of £734 million. So, I think on any metric you care to use Phoenix Life represents a substantial part of the overall Group.

I think it's also helpful to paint a picture of our overall operating model. We operate a significantly outsourced model. So we have outsourced all of our customer services, all of our customer administration, our IT, investment administration services, and some other finance processing functions. What we have kept in-house are the key financial and actuarial management and reporting functions, as well as those functions necessary to oversee the functions that are outsourced plus central functions of HR, risk and internal audit.

This slide is a summary of the corporate structure. The entities inside the dotted line represent Phoenix Life. So Phoenix Life does not include Opal Re, Ignis and other parts of the group above but what it does include are seven life companies, three of which are sister life companies and the other four are subsidiaries of those other life companies, and two service companies.

The next picture shows the value of the assets. And what we've done is split the value of the assets just to give you an idea of some of the dimensions of Phoenix Life. So, we've split it by bank silo and we've also split it by product. What I would highlight there is a very significant annuity business, a large portion of unit linked business, alongside the two significant with profits businesses that we've split into two; and we've split those along the lines of those with profits businesses that are more than capable of standing on their own two feet, handling their own risks, and those which have an element of shareholder support and Pete Mayes will talk to you later about the key characteristics of each of these product lines.

So who is Phoenix Life? This is the management team, and this management team focused on Phoenix Life and four of them are presenting to you today. The total relevant experience of this management team is 183 years. I make it that's an average of more than 20 years each. And that experience has been gained with 20 different organisations, some which are now part of the Group and some which are elsewhere in the industry.

Andy Moss will talk to you shortly about what we focus on from a financial perspective. I just want to cover some of the other key metrics that we use within Phoenix Life. First of all estate distribution; we look to maximise our estate distribution to increase our payouts to our customers. Obviously that increases value for our customers. There is also shareholder share in that surplus. And we are currently distributing £898 million of estate amongst our policyholders, so we distribute that over the lifetime of the run off of those with profit funds, shared fairly across all those policyholders.

Second key metric we look at focuses on reducing complaint volumes, alongside reducing the time it takes us to solve legacy issues. Why do we do this? We're looking to improve, customer service and to improve the efficiency of our operations. And the current key metrics are we receive 1.16 complaints per 1,000 policies, that's very much in line with the industry; and in terms of the lapse time to fix legacy issues we reduced that by 10% last year and we're looking to do the same this year.

In terms of people; maintaining the expertise that we have to manage the business that we've got is very important to us. And we look at that in two dimensions; we look at the key staff and we look at overall staff. Why are we doing that? Obviously we're looking at more of a contribution from our employees to achieve our objectives. Our current turnover for key staff is 3% per annum, and overall turnover is 7% per annum both of those are well below industry benchmarks. And we also look at employee engagement and we participate in a survey which helps us measure that. And our engagement score is currently 74%, again ahead of the financial services benchmark of 69%.

Risk management is absolutely central to what Phoenix Life does. In terms of economic risk we are regularly monitoring emerging economic conditions. The key tool that we have to managing market risk is the regular re-balancing of our asset/liability positions. This ensures that we take actions as necessary to protect both cash and profits.

In terms of insurance risk again, we monitor the experience of our own portfolios, but we also measure the emerging industry data to ensure that our assumptions remain up to date and again take the necessary action to protect cash and profits. The primary device, the primary control that we have is in respect of our annuity business. We are currently writing at around £800 million per annum of new annuities. And the primary control that we have is the price that we set in respect of our longevity risk within those annuities.

In terms of operational risk we complete a monthly control risk self-assessment process, so assessing the effectiveness of all of our controls on a regular basis to ensure that our risks are controlled properly. Two key things that we do on operational risk is we do an in-depth regular review of how our products are performing and the services that we are delivering to make sure that we are delivering on the commitments that we gave to our policyholders. A key feature of this is it helps us avoid and manage future regulatory risk.

Secondly, it is very important to us to ensure that our outsourcers, to whom we have transferred risk, actually deliver on those risk transfer mechanisms and we make sure that they work. So throughout this on operational risk what we're looking to do is to take appropriate actions to reduce the use of capital for this unrewarded risk.

Finally as regards regulatory risk we look to identify and address the regulatory risks directly and through industry lobbying. So, we've got a constant eye out on the emerging feedback that we get from the ombudsman in terms of our complaint handling, looking for any emerging trends that can be managed. We've responded to the FSA consultation papers such as CP11/05, and also been part of the industry lobbying. And finally the Solvency II.

I thought I should say a little more about Solvency II. Right now it looks like the implementation date will change from 1 January 2013 probably to 1 January 2014. However this is not certain. The FSA are currently clear that they are working to a date of 1 January 2013 and are expecting firms to do likewise and indeed that is what we are doing. We are on track to deliver to that timescale, and we certainly don't need any deferral of the implementation.

In terms of the internal model we are applying for a partial internal model, but that is partly as a consequence of taking a phased approach linked to our programme to re-engineer our underlying actuarial systems. The ultimate aim is for a full model and actually a deferred timetable may be helpful in this regard.

As far as QIS5 is concerned we thought QIS5 was a useful exercise. And our position is that our current capital policies cover the QIS5 requirements but we have to note many elements are still subject to considerable uncertainty.

To illustrate to you the journey that Phoenix Life is on this is a simplified structured chart of just the life companies. And this one is backdated to shortly after the acquisition of Resolution. So you'll see on there it actually had ten life companies, several of those life companies had one with profit fund, one non profit fund and one shareholder fund. If I move forward to today's picture this is the structure we now have seven life companies. The consolidation that's happened has placed the historic with profit funds alongside each other in Phoenix Life Limited but the shareholder funds and the non profit funds have been combined.

Shortly this will move to a six life company structure as PPL, the company in the bottom left-hand corner, which was set up for tax reasons in 2007, those tax reasons no longer exist and we are recapturing the business that we reinsured from Phoenix Life Limited to PPL, and placing the business effectively back into Phoenix Life Limited. This has an additional benefit from a Solvency II perspective where intra-group reinsurances is not treated very favourably; so it will remove a potential Solvency II inefficiency. So, you can see the restructuring activity that we are doing is starting to look ahead and embrace Solvency II.

So this restructuring work has reduced complexity and, as Andy Moss will illustrate later, has added value and released cash. However there is still plenty more to be done.

This slide illustrates the basic business model for a closed fund. I believe it's a simple model. The Value in Force, the VIF, turns into cash over time, and capital is released as the risk profile reduces, as the business runs off. This run off process is continuous and inevitable, unless risks crystallise along the way. What we can do as management is increase the value of the VIF and/or accelerate the release of capital. That business model can then be further enhanced through acquisitions. So VIF and cashflows can be replenished, value creation from acquisitions can happen via the discount to the embedded value of the acquisition, plus tax and capital synergies. And then there's potential to add further by deploying what we call the Phoenix Way.

I have a bit more about what deploying the Phoenix Way means. The Phoenix Way is the solution to the challenge, so challenge of increasing value for shareholders and policyholders, adding value and turning that value into cash, generating cashflow for shareholders, and ultimately leading to higher payouts for customers. That's our challenge. The operating environment that we have I'm sure, as you're well aware, we have a myriad of reporting bases and methodologies of MCEV, IFRS, Pillar I, Pillar II etc, and we have a book of business with very varied legacy heritage created by different and disparate management teams in the past. Add to this we've got an ever changing regulatory landscape, of which Solvency II is not the least part, and we also have the option and the ability to add value through partnership with Ignis. And throughout all of this it is underpinned by the need for a flexible cost base with Phoenix Life which can respond to increasing and decreasing policy volumes.

So the Phoenix Way is the methodology for delivering this change within an operating environment. It is all about simplifying and clearly setting out how we manage closed funds.

And the four boxes you see there are the four categories in which we place all of that activity. And this flows through all the way through the 580 people in Birmingham so they know where they fit in in implementing the Phoenix Way.

To demonstrate the Phoenix Way you will hear more detail on specific case studies that we'll talk about later. But in terms of operational management it is about addressing historic legacy issues, providing permanent solutions for those issues, such as legacy tax challenges. It's about standardising how we do things, for example, dealing with and providing for outstanding claims and managing our cost base.

In terms of outsourcing – Tony Kassimiotis will talk about this later – but it's about simplifying and consolidating our arrangements, transforming the model and improving outcomes for customers.

In terms of restructuring I've talked about fund mergers, and Andy will talk about it further. But we also have executed a number of liability management initiatives. So, there was one initiative to effectively trade with policyholders and remove guaranteed annuity options which significantly reduced risk for shareholders. And we'll be looking to transfer annuity business so the right risk is taken in the right place. And you saw earlier this year the potential benefits of asset restructuring that Pete will talk about later.

And finally in terms of risk management, it's all about taking risk in the right places. An example of that is in 2010 we've completely reviewed the hedge fund exposures we've got, reallocated those exposures, reduced capital requirements and given more opportunities for customers – a genuine win/win for policyholders and shareholders. And the focus in risk management is on standardised controls to reduce operational risk, as I spoke to earlier.

So our focus in terms of 2011 for the Phoenix Way, in terms of operational management it's the continued development of the Actuarial Systems Transformation project that we will talk about later, continuing to find permanent solutions for legacy issues, and those issues still remain; we want to establish a standard way, a Phoenix Way of managing with profits business, which takes the best practice across all of our with profit funds to give benefits for policyholders and shareholders and we'll be managing our costs and running and reporting the business as usual.

In terms of restructuring: we have restructured the corporate bond portfolio that was reported earlier this year, we are doing further fund mergers, and we will be ensuring that our corporate structure is fit for purpose under Solvency II.

In terms of outsourcing a key focus is on improving our customer experience in 2011, but there will be further policy migrations to transform platforms at our outsourcers that we will be supporting. We will also be making further improvements to incident management – which is the legacy issues I talked about earlier – and to complaint handling and further developing and deepening the relationship with Ignis.

And the focus in terms of risk management is on improving and strengthening the management of market risk, continuous improvements to asset liability matching, and delivery of the Solvency II project plan.

And through all of is it will enable us to improve customer outcomes and deliver on our shareholder targets.

So with that I will hand you over to Andy Moss who will talk more about the financials.

Andy Moss: Phoenix Life Finance Director

Thank you. Good afternoon all. I'm Andy Moss. I should say before we start I'm no relation to any of the other eminent Moss's that work within this industry. What my aim is over the next 15 minutes or so is to give an overview on the things that we focus on from a financial perspective, and also to pull out some case studies as to how we can add value to this business, both in the past with some examples, but also how they're applicable to the future as well.

So, first of all, as Mike said earlier, we have a number of key metrics on which we measure ourselves as a management team and, as you would expect, the financial metrics are key to that. The five financial measures that we've set out here are obviously a subset of those Group measures which you will have heard about at Group presentations in the past. These receive a significant amount of management focus within Phoenix Life on a monthly, quarterly and an annual basis.

So, if we just quickly run through them. Cash; so obviously we're looking to generate cash for onwards distribution up to the Group. Embedded value; obviously we have a lot of embedded value within Phoenix Life, as I'll demonstrate later on. What we're looking to do is to take management actions to enhance that embedded value. Capital strength; we obviously want to comply with our regulatory requirements and ensure that we maintain capital buffers to withstand future shocks. We also focus on operating profits, looking at our IFRS targets. And finally within the service companies we also focus on controlling our costs and again, I'll talk a little bit about that later.

The good news is that as we stand here today we are on track, as a business, to hit our key financial targets in 2011. And obviously you'll hear more about that in our half-year results.

So a few comments about how we generate cash. On the left-hand side of this slide we're showing the basic generation of cash. So we get surpluses coming through from the distribution of with profit shareholder bonuses, emergence of our non profit fund surpluses, and also returns on shareholder funds that we hold. In addition to that, as Mike touched upon earlier, we run off our capital and we're able to manage that capital by looking at our risk profile. There are obviously some sensitivities on an annual basis in respect of those, which can go up as well as down. Obviously the economic conditions can impact it, our experience on some of our key assumptions can impact in, and our overall tax position can also impact it. All of that leads to us distributing surplus cash. So basically we hold regulatory capital, a capital buffer to withstand a range of adverse events, and then basically any excess capital available above that buffer is available for distribution.

This is a slide that you've seen in aggregate previously in Group presentations. What this is here to do is basically to show the significant amount of embedded value within Phoenix Life. And in particular you can see the amount of embedded value that now sits within Phoenix Life Limited, which has been the subject, as Mike mentioned earlier, of a number of funds' mergers. Over time that VIF will turn into cash.

Again, just reiterating some of the year-end presentation, the numbers you see in there are as per the year-end presentation. That was our regulatory excess capital at the end of 2010, and the free surplus also at the end of 2010. A couple of points to point out on this slide: at that point in time PALAL was a separate company we have taken action in the first quarter of this year to funds merge that particular company into Phoenix Life Limited, and that cash is now available for distribution. As you'll see within London Life there is a very small amount of surplus within London Life which is currently restricted and what we'll be looking to do and expect to do over the next couple of years is to take action to enable us to be able to get

access to that surplus. You will have seen from the first quarter's announcement that some of this surplus has now been distributed, and obviously we'll give you further updates on the distribution of surplus at the half-year presentation.

IFRS operating profits, just to run through this in a little bit of detail. On the left-hand side again we have got the surplus of our profits that I referred to earlier. As you can see within that the with profits cost of bonus is relatively stable. It will fluctuate depending on the amount of business that matures in any particular year and any spikes in surrenders. So, within a certain range that amount will fluctuate up and down. The with profit supported funds, unit linked, annuities and protection, which Pete will talk a little bit about a little bit later on, will fluctuate basically because we're looking at new business contribution, the margins on which will vary in individual years, again the expected margins emergence as the business runs off, our experience variances within insurance, and then finally we obviously look at all of our assumptions on an annual basis, and assumption changes come through our operating profit.

Within shareholder funds this represents the long-term return on our shareholder funds looking at a rate looking forward. The return on these funds is dependant obviously on the size of the shareholder funds and again can fluctuate depending on how much surplus we hold within those shareholder funds.

So when you see our operating profit there are a number of one-offs on an annual basis within that. But if you were looking forward over the next two to three years we expect that the range of our underlying operating profits is in the range of £275 to £325 million.

If we move on to costs our operating model works in the way that the service companies provide services through to the life companies. Thus all the costs are charged with a guaranteed amount as a per policy charge through to the life companies. Thus any better management of these costs gives risk to profit or losses within the service companies. If you look at the breakout of our BAU costs there you can see that a large proportion of it is around outsourcers, which Tony will go into in a little bit more detail during his section. The key point I would like to make as part of that though is that those outsourcer costs are directly linked to our policy run off thus the costs will fall in line with the income which the service companies are generating, and it also gives us flexibility when we take on other books of business for those costs to go up directly in line with the income we are generating.

In respect to the retained costs these are more of a semi variable nature however over the last two to three years we've had a significant track record of reducing retained costs, either by synergies as we acquire other businesses and we move all of our business on to one site, or by making ongoing operational improvement, as Mike referred to a number of areas where we've simplified the business and streamlined the business, thus enabling us to realise some ongoing operational improvements. So whilst those reductions tend to be more of a lumpy nature, we are managing those costs very well.

As you might expect, and probably in line with the rest of the industry, we are incurring a significant amount of project costs at the moment. Our project costs during 2010 were in the order of £70 million, and we have seen this big spike of project costs during 2010 and into 2011 as we carry on with our outsourcer transformation programmes, as we address Solvency II, and as also do quite a lot of work around our actuarial systems, which again Mike referred to earlier.

Another significant element of our costs is investment management expenses. Mike talked about our relationship and partnership with Ignis. And in 2010 we did a significant amount of work with Ignis to look at the fee structures which the life companies were paying over to

Ignis. We did a lot of benchmarking externally to ensure that the deal that the life funds were getting was commercially attractive and we also looked to align our interests, both ours, Ignis' and our policyholders' with looking at moving more of our fees towards a performance fee basis. As you can see that, over £20 million of our fees in 2010 related to performance, thus directly giving benefit to the policyholders and shareholders within the life companies, at the same time as obviously aligning the interest in terms of the way that Ignis are managing our money.

So turning to a couple of case studies to finish. Under operational management Mike talked about resolving legacy issues. One of our acquired businesses, for which the administration had previously been outsourced, when we acquired this business we identified a number of weaknesses in controls over the completion of accounting for premiums and claims. This had led to significant unmatched items on the balance sheet. And whilst we refer there to an overall number of £2.3 billion, just to reassure you that is a gross number adding all the pluses and minuses together. So what we had on the balance sheet was a number of outstanding claims with unmatched cash.

We set up a project in late 2007 to address these issues. Our first objective was obviously to clear that suspense account balance down to an acceptable and manageable level. Secondly, we wanted to improve the controls as we move forward. All of this activity needed to take into account any potential customer detriment and also to ensure that there are no further errors in any of that accounting. The core project ran through 2008 and 2009, and during that time period we cleared the majority of that £2.3 billion, £2.2 billion of that was cleared. There was no significant customer detriment identified. And this activity led to a significant release of capital, some £117 million, and a significant increase in EV of some £75 million. And that was basically due to correcting overstated liabilities, largely around outstanding claims which had built up over a large number of years. Controls now operate to ensure that those things are managed on an ongoing basis. And again Mike referred earlier about the Phoenix Way these controls are now standard across all of our outsourcers.

What I would point out in respect of this, this is not unusual. For books that we buy you quite often see that they've been through a period where there has not perhaps been as much focus on it as there would be in a new business environment. So we very often find there are things we can do around the balance sheet that's giving us some repeatable techniques we can use in terms of future acquisitions. This is also an advantage of our closed business model because we focus on some of the back book issues.

In terms of funds merger, we acquired the life insurance businesses of Abbey National, which is obviously now part Santander, in 2007. The plan at the time was to transfer this into PLL via a funds merger which was effective from 1 January 2009. Funds mergers require quite a lot of focus and quite a lot of activities to get us to the final funds merged position. In particular we obviously have to go through a legal process, we have to go through significant regulatory discussions, there is obviously independent scrutiny to ensure that policyholders are not disadvantaged, we also have to get tax clearances, and obviously we have to communicate with our policyholders. We've now done a number of these, and we have improved our processes and again these are things that we can do into the future. In the bottom you can see the value that funds mergers can add an MCEV benefit of £33 million, capital synergies of some £225 million, and an IFRS impact of some £90 million.

So in summary we are on track to meet our 2011 financial targets. We do have resilient and reliable cashflows. Our cost base is well controlled, particularly reflecting a significant variable element within that and a reducing project cost base as well. We have a strong capital position. And we still have significant embedded value within the business.

Thank you. I'll hand over to Pete Mayes, our Chief Actuary.

Peter Mayes: Chief Actuary

Good afternoon. Today I'm going to talk to you about the major product lines within Phoenix Life, those being with profits, annuities, unit links and protection. In particular I'll talk to you about the types of actions that we do take and can take as management to try and prove value to both our policyholders and our shareholders, but in particular I'll try and focus on each shareholder value.

So starting with with profits funds, this is a slide that Mike showed you earlier but what I've done on this slide is I've split the with profits funds, colour coded them into those which are standalone and those which I've called supported. So the blue coloured ones are all with profits funds that are standalone, they can meet their liabilities and the regulatory capital requirements from assets that have accumulated from within the with profits fund. The maroon type coloured ones are the funds that are supported. They've needed capital injections to meet liabilities and need capital from outside of the with profits funds to meet their capital requirements.

So let's have a look at the standalone funds. As you can see it's a significant amount of funds in the management from the standalone funds, we have just over £23 billion of assets under management, we have £17 billion of with profits asset shares and there's a VIF, a value in there to shareholders of £612 million. That value represents the present rate today of the shareholder 10% of future bonus payments.

So what can we do to try and improve returns to our policyholders and returns to shareholders? Firstly we can consider a trend to accelerate the estate distribution. This doesn't increase the size of the cake, but does accelerate cash flow to shareholders and can also mean that those policies that mature in the very near term in the future, policyholders get more share of the estate.

Acceleration of estate distribution will generally be achieved with more certainty of runoff and therefore generally through improved risk management. And the actions we can take are for example pension policies that rest in those funds, rather than writing annuities within those funds we can actually transfer those annuities into a shareholder fund. That can be in the interests of policyholders by taking out risk and therefore allowing estate distribution, and clearly can also be a source of value to the shareholder provided it can be done on acceptable terms to both parties.

Another example would be taking out any of what we've called, dare I say it, over prudence in reserves. An example of that may be for example we know that many old whole of life policies will not claim, therefore prudently recognising that today will speed up the emergence of surplus and again allow us to accelerate estate distributions to both policyholders and shareholder.

In addition to speeding up estate distribution we can also of course try and increase the size of the cake. So for example we can try and split the with profits funds into different blocks of business, so that certain blocks of business can have a more risky investment strategy if that's what they can bear, something I've called here 'hypothecation'. And by taking that risky investment strategy we hope to increase the expected returns and therefore increase bonus payments above policyholders and shareholder. In addition of course we can drive returns through the investment manager.

So what are we doing and what will we continue to do over the longer term? We'll continue to try and drive through cost efficiencies by harmonising the legacy practices and methods

across the with profits funds. We'll continue to focus on distributing estate more quickly to the benefit of policyholders and shareholders. We'll remove unrewarded risks, for example, trying to reduce operational risk capital so that again we can accelerate estate distribution. And finally, in the longer term we may even be able to try and simplify the overall proposition that current policyholders have.

So turning to supported with profits funds, so these funds constitute about half the size of the standalone business. We have assets under management of nearly £12 billion, we've asset shares of just over £7 billion and the difference there between the assets under management and the asset shares clearly can't be a stake because I've said it's supported, that really is representing the substantial costs of guarantees and options embedded in the policies. And we have a VIF here of just £34 million. That VIF is representing again the 10% shareholder portion of future bonus payments which as you can imagine will be very low, the expected repayments of any capital that's been injected into the funds, less the cost of capital support from outside the with profits funds.

The focus of management here is very much about increasing the repayment of shareholder capital while managing the risk of needing to inject more. The focus therefore is very much around risk management through hypothecation of investment, policy to lines of business and hedging market risks effectively and efficiently. Opportunities to invest in low risk liquid assets to help back any liquid liabilities would be attractive if you can earn the necessary liquidity premium. And lots of standalone funds again transferring in force in future vesting annuity business outside of the fund is again potentially attractive to policyholders and the shareholder.

The longer term aims that we continue to focus on are essentially just a subset for the standalone funds, so cost efficiency, taking out unrewarded risks and again can we simplify into something easier and better for the policyholders.

Moving on to annuities. Annuity is an attractive and growing business line within Phoenix. We have one with £6 billion of assets under management, that excludes almost three and a half billion of assets that sit within Opal Re which we talked about earlier which is part of the Group outside of Phoenix Life. It also excludes £2.2 billion of annuities that currently sit within with profits funds. As Mike mentioned earlier we write around £800 million per annum of new annuity business; that represents generally 100% of vesting guaranteed annuity rate policies. We also write the majority of non guaranteed annuity rates vesting business within Phoenix Life.

The margin we expect to earn and we aim to earn on this business is around 8% of the premium, that is just the margin within Phoenix Life, so it excludes any extra margins we can make within the service companies and within Ignis Asset Management. And we have a VIF of the enforced business of £415 million. As I said, at present Phoenix writes annuity business solely for internal vestings, Phoenix clearly has the advantage of being a low cost provider to internal investment policies which generates value to the shareholder whilst still being competitive to policyholders. In addition to our new vesting annuities as I mentioned earlier, transferring annuities that have already vested and remain within with profits funds can be another source of value in our annuity business. In addition of course we will try and generate additional value through our investment policy, in particular by looking for value added from liquidity premiums from assets.

Longer term objectives include improving the retirement proposition, for example consolidation of pension funds, improving pricing bases, for example more underwriting factors. And what I've called here 'further development of liability management', for example exploration of longevity swaps and trying to reduce the number of suspended accounts that we have within the business.

Looking at the last two business lines together, unit linked and protection, unit linked is a substantial part of our business, it has £12 billion of assets under management and a VIF of £447 million. Protection and everything else we could think of has assets under management of under £800 million and a VIF of £360 million.

For both of these business lines really the aim of management is to make that as cost efficient as we can, to maximise customer retention so we can earn the margins, and obviously particularly for unit link businesses, obviously drive through investment performance. In the longer term we do have affinity relationships, we would look to broaden and deepen those affinity relationships in terms of using our customer base as well as we can.

I have talked about the direct benefits of each of the business lines, there are many indirect benefits from actually bringing all those business lines together so that the whole is greater than the sum of the parts. So, for example, I've already talked about writing profitable vesting annuities so, for example, from our unit link business pension policies that vest we potentially write the majority of the vesting annuities on those. Clearly all those business lines bring additional assets under management for Ignis. There are often tax synergies that arise. Clearly by adding policies into the book we get greater service company efficiency and as we've also talked about today, there are often fund merger and diversification benefits we can gain by putting policy and fund lines together.

Finally, I want to talk about one example of asset investment policy which generated significant shareholder value. Pearl Assurance, London Life and National Provident have significantly achieved books which they have reinsured with Opal Re, the internal reinsurer of the Group. However, when we perform our Pillar 2, our ICA calculations, we look through to the underlying collateral that those firms have access to should Opel Re not be there. The collateral consisted of a significant block of leveraged sub investment grade loans from which we did not recognise any liquidity premium in terms of our liability assessments but which we were also having to put against risk capital for the Phoenix interest being wiped out. By buying out the leverage from the arrangement enabled us to take credit for the liquidity premium to back the liabilities and it also allowed us to reassess the capital requirements to one of default risk rather than one of market volatility. The net result was a much simpler structure in terms of collateral arrangements and in an improvement in the MCEV and the Pillar 2 capital of over £130 million, a substantial benefit to our shareholders.

So, on that note I'll hand you over to Tony.

Tony Kassimiotis: Managing Director

Good afternoon everyone, I'm Tony Kassimiotis and I'm MD of Operations for Phoenix Life. I was going to say that I was delighted to be here but given what Jonathan said last and least I'm not particularly sure and I'm still reeling from that particular statement.

I'd like to talk to you today about our operating model, clearly you've heard from Mike, Andy and Peter about the financial management aspects of that business. We've heard about cost base, we've heard about funds restructuring. What I'd like to do is specifically talk about the operating model and with particular focus on our outsource management model. And in doing so I'm going to focus on a couple of key aspects, the transformation journey that we've been on with our outsourcers and a case study that we've already heard today around our actuarial systems transformation.

So, this diagram depicts the operating model that we operate within Phoenix Life. It's a three tier model and as you can see we start with the life companies which have a whole series of

different systems, different applications, different processes that have been built up over a number of years when those life companies operated on an individual basis. And clearly it's important for those life companies to transfer the risk of the policy run-off and to help give effect to that within the Phoenix Life business we have created one service company. We call it 'one' service company, we can call it the Phoenix Way, but essentially it's talking about consolidating the operational management of those life companies into a streamlined, efficient and cost effective way of doing so. And within that, that 'one' service company has taken on operational risk from the life companies. And if we just left if there that would clearly not be sufficient and would create a bit of a challenge for our operational business.

So what we have done and the focus of my presentation is really to talk about how we have taken that operational risk, the challenges that the 'one' service company has and we've outsourced a significant portion to our outsource partners. And in doing so we believe as a result of working with external partners to help bring us capability and transformational expertise that we will and have improved our customer service to our policyholders, clearly driving one way of delivering service to our policyholders. Our outsourcing agreements are transformational in nature, i.e. they transform the business that we gave the outsourcers to a different state, a much more streamlined and much more effective state.

We have also future proofed the technology investment that would otherwise need to have been made, and I'll explain a little bit about that as we get to some of the remaining slides. The net result of our operating model we believe is that it allows us to first and foremost manage the business today effectively and at a price point that we believe is in line with the runoff and clearly and importantly it creates a platform for future acquisitions.

Outsourcing is something that I've already mentioned a couple of times and in some of the other speeches you've already heard that outsourcing is a significant part of our operating model. So I thought it would be helpful just to paint a bit of context about how many outsourcers we have and what kind of business they do for us. So as you can see from this slide and some of the numbers that you will have seen from Andy's presentation we spend full year, 2010, £144 million on our outsource arrangements. And we have five outsourcers in place, in fact we outsource to all the life and pensions outsourcing firms within the UK marketplace.

If we're starting with a clean sheet of paper it's inevitable it would be fair to say that we would not seek to build a model that has five outsourcers in place, so obviously what we have in front of us is the outworking of an acquisition model. However, I will say that we do have two primary benefits that we derive from these outsourcers. Number one, we have most of the policies under administration between two key outsourcers, so as you can see from both the Diligenta and the Capita agreement we have more than six and a half million policyholders managed within that arrangement. So from that standpoint 95% of our policyholders are managed within two outsource agreements and they are longstanding agreements with significant commercial risk being transferred to the outsource partners and with strong obligations on the outsource partners to build systems and capability, not only for today but into the future.

I think the other point is, given we have such a diverse level of outsourcing agreements if I was presenting this slide a year ago you would have seen another outsourcer on here and that would have been the Unisys operation. And over the last six to nine months we've worked very strongly with our existing partners to consolidate that Unisys operation into one of our existing arrangements. So the number we have and the scale of our operations affords us optionality and affords us the opportunity to make flexible decisions based on our operating model.

Outsourcing as you can see derives a number of benefits for us. Number one, it allows us to convert a significant part of the fixed cost base of our business to a fully variable cost base business. And within that fully variable cost base business there are all the constituent components, investment in IT, the regulatory change, other small discretionary changes, all within the cost per policy that we have already locked in on a fixed term basis and a variable basis to our outsourcers.

I've spoken about the investment strategy and the fact that our outsourcing agreements allow us to reduce the investment that otherwise would have needed to be the case, and significantly, as I've mentioned a couple of times, we have operational risk transfer within those outsource agreements.

I thought it would be important to delve into a little bit about the project spend. You will see that from the Phoenix Life management expenses we spend £298 million in total which Andy has spoken about, a significant or a component of that spend is £7 million on our project spend and the most important element of this slide is that whilst we have spent the last three or four years transforming the operation you'll see that post 2011 our transformation programmes have largely concluded and the project costs declined rapidly from then on. We have taken hard steps historically, we have transformed those operations and working with our partners, our transformation programmes are largely complete, and therefore we believe the net result are the platforms that result which allows us to take on future business.

So how have we gone? So let's look at what we have achieved so far. Andy also spoke about the £144 million, so just to lift the covers a little bit on the £144 million you'll see from the top right hand slide that the £144 million which is our 2010 year spend has reduced from 2006 from the rate of £202 million all the way down to £144 million. And this cost reduction has been done on a variable cost basis, so these results have resulted from our outsource transformation programmes and as a result of the contractual agreements we have in place.

Projecting forward we therefore believe the £144 million with a level of certainty will decline all the way to 2014 to £91 million. And what I've done, just to give you a little bit of coverage there, I've worked back from 2006, so the top line that you see which has £194 million in 2010 started off at £202 million, and essentially that line takes up our increase less a £10 million benefit on a year to year basis. And what I'm trying to compare for you is had we not deployed the operating model that we have in place today and had we not taken such drastic measures in 2006, 2007, we would have been living with a cost base which would have been more in line with a top line rather than the run-off line that we enjoy today.

Last but not least I thought I'd just give you a bit of a sense of a case study around our actuarial systems transformation. I've spoken a little bit about the customer services and IT transformation programmes within our outsourcers, we've spoken a lot about systems rationalisation and transformation and the journey we've been on has taught us a lot about how we can transfer operational risk to our outsource partners through strong contractual measures. So the case study that we've got here in front of us talks about the fact that through the acquisition strategy we've built up a number of actuarial models within our actuarial management functions, and those actuarial models have been lifted and shifted into the Wythall base facility and we have rationalised those operational models and we have got synergies and benefits from those and staff reductions.

But that is our phase one process. Our phase two process which Mike and Andy have already spoken about is the remaining elements of our actuarial systems transformation programme. And what we have embarked upon is a long term agreement with Millimans to build all our various actuarial models onto one platform which Millimans calls MG ALFA. So that MG ALFA platform in combination with our outsource partners allows us to deliver reduced operational risk, improved MI and one acquisition ready platform.

So with that I'd like to hand over to Mike to wrap up and close I think.

Mike Merrick: Chief Executive

Thank you, Tony. So in summary, I hope you get the clear message that risk management is absolutely central and critical to what we do. I hope we've demonstrated that underlying Phoenix Life is a very simple business model. Tony's talked about our successful outsourcing strategy. And I think the message from Pete was within Phoenix there are a number of value streams, but there are significant synergy benefits between those value streams.

I think we've demonstrated that we have a very experienced and focused management team and that we're focused on the delivery of value for shareholders and policyholders, at the same time as building a simpler and sustainable long term business. So thank you very much for that and I think we'll open it up for questions.

Question and Answer Session

Jonathan Yates

I'd like to say thank you to my colleagues, thank you very much, and we'd be delighted to try and answer any questions you've got. I'm here to handle your questions but to actually pass them on to somebody else who's far more qualified to answer them. So does anybody have any questions? Oliver.

<u>Question 1</u>

Oliver Steele - Deutsche Bank

Yes, two questions and first on one of those last slides put up by Tony in terms of the cost reductions that you're targeting, indicating, guiding us towards over the next few years how much of that is in your group-wide projections already, and in the embedded value sort of numbers that you've given us? So that's question one.

The second question is in terms of the project costs, no sorry, not the project costs, the outsourcing costs… Actually sorry, I've just realised that was the outsourcing costs, so we'll leave that as one question.

Jonathan Yates

It sounds like perhaps a question for Andy rather than for Tony, but…

Answer: Andy Moss

Okay, so I'll pick up your first question. In terms of the way we measure EV, so the published EV, going back to my earlier slide, is that for the service companies we don't have any forward projections of obviously the future profits, what we have is today's net assets within there, so to the extent that we make future profits within the service companies then there is no reflection within the EV. In terms of the life companies, as I said basically the per policy costs are within the life companies so all of those are reflected in today's current EV, so effectively you have a per policy cost which is guaranteed to the life companies and that will run down obviously in line with the book.

Further question

So those policy cost reductions are, they're guaranteed already by the outsourcing?

Answer: Andy Moss

So there's two elements to this, it's basically where we're looking for a flow through of expenses, so within the life companies we pay to the service company a per policy cost, so within the life companies we're obviously taking credit for the rundown of those per policy costs in line with the book. Within the service company they have an arrangement obviously with outsourcers so there's two elements to the per policy costs within the service company, one is the amount we pay to the outsourcers, the second amount is the retained costs. So to the extent that we run those costs down faster than the income there is no credit currently taken for that, and that's obviously our aim to do that.

Further question

I still need to follow this one up. You've given us an indication of what you think the costs will be.

Andy Moss

Yes.

Further question

How much of those costs are included in the embedded value and how much are effectively outside the embedded value? And again in terms of the cash flow projections which you've given us for the Group how much is in those cash flow projections now and how much isn't?

Answer: Andy Moss

Okay, is there a different way of answering that. So in terms of the service company we do not reflect any of the future profits of the service company within the embedded value.

Further question

Greig Patterson, KBW

(inaudible question)

Answer: Andy Moss

So obviously our internal management accounts will assume we are making some profits in the service company going forward and none of those are reflected in the embedded value as we publish it today.

Further question

(inaudible start) just to get the question answered, is that if you run off according to those profiles will the service company produce profits?

Answer: Andy Moss

It will produce profits, yes.

Further question

And how big would they be in terms of present value from sort of some kind of normal discount rate?

Answer: Andy Moss

Well, we haven't actually done those…

Answer: Jonathan Yates

We haven't done those calculations. I mean to be clear, the service companies, if you look at them today, I mean as Tony explained, we've got a whole series of costs in there, we've got the sort of the basic costs of policy administration and then we've got the sort of the project costs that are sitting on top of that. So there's a degree to which we're actually having to fund those projects, so the underlying costs are sort of mixed in to some degree with the project costs, as we go forward the project costs will strip out and we'll be left with a lower run rate. That lower run rate is what's designed to be reflected in the management service agreements that exist in the long term between the life companies and the service companies. So we're not looking to make significant profits from those agreements going forward.

Having said that, one of the things that we do look to do is to reduce our costs over time through creating more efficiencies as we go forward, but also from buying other books of business and merging them in where we get genuine scale benefits. And I think as Tony sort of outlined we've actually got a solid base on which to build.

So it's not the sort of the absolute categorical answer in terms of X pounds per annum profits within the service companies that we don't include within the embedded value, but we do not wish to guide in terms of what those profits might be going forward, given the level of uncertainty that exists around them, other than to say that actually we believe that the allowances that exist within the management services agreements, the agreements with the life companies, are sufficient to provide for all our costs going forward.

<u>Question 2</u>

Kevin Ryan – Investec

Thanks. It's Kevin Ryan, Investec. A couple of questions. On the outsourcers, you've got three outsourcers who do about just over 5%, 5.1% of the book. Is that a significant cost and is there any scope for getting rid of those? That's question one.

And the other question is, coming back to sort of slide 32 talking about with profits standalone stuff your longer term objectives are harmonisation of practices, could you give us a feel for the sort of real timescale of harmonising things? Presumably this is an ongoing thing? And what we can expect in terms of benefits to shareholders coming out of that?

Jonathan Yates

Perhaps Tony could take the…

Kevin Ryan

And presumably it's a step process. I'm just trying to get a feel for timescale and quantum.

Jonathan Yates

Thanks, Kevin. Perhaps Tony could take the first question and then maybe Mike, if you'd like to deal with the second?

Answer: Tony Kassimiotis

Okay. In terms of our outsourcing agreement, so if you look at the three outsourcers they have about 5%. Some of those arrangements were put in place some time ago so in answer to your question about are they significant in cost, the answer to that is no in comparison to the other two. In relation to the question about are there opportunities to rationalise those, when those agreements come to a natural end we will seek opportunities to create more efficiencies and synergies from our other bigger and larger agreements if it makes sense to do so. So there is opportunity to do that at the time that it unfolds.

Answer: Mike Merrick

In terms of harmonisation of the with-profits processes that's, currently under development, that'll be largely established in 2011. What we do then have to do is having established the way in which we think it's optimal to run a with profit fund each with profit fund has to be benchmarked against that optimal way. And there may be some constraints within with profit funds as to how they've been historically managed or commitments that have been made to policyholders which will prevent some of the aspects being implemented. So I think we would expect full implementation as far as is possible by the end of 2012. As far as benefits for shareholders go I think it's important to say the primary benefit falls to the funds themselves and these are the strong standalone funds and the shareholders would get a 10% benefit of those benefits. It's really a second order benefit for shareholders.

<u>Question 3</u>

Barrie Cornes – Panmure Gordon

It's Barrie Cornes from Panmure Gordon. A couple of questions if I may? First of all in terms of annuities I wonder if you could give us a flavour as to the percentage of potential vesting annuities you actually retain. And of those ones that you retain if there's any variance in terms of the rate you offer in respect of enhanced or impaired lives if you actually ask the question. And the other question I had for you is in terms of numbers of complaints that you receive, I just wondered what the run-off profile of those complaints looks like and what the uphold rates with the ombudsman are please?

Jonathan Yates

Perhaps Pete could answer the first one and Mike deal with the second one?

Answer: Peter Mayes

Yes, in terms of the percentage retained, as I mentioned we effectively retain 100% of vesting policies that are on guaranteed annuity rates. Of the other, on the non guaranteed annuity rates, I think it's around 70% retained on that. You went on I think to ask about impaired annuity, so that isn't something we currently offer, but it is something that we would be looking to… we are considering.

Further question

So you don't refer them to somebody else and take a turn on the referral or anything like that?

Answer: Peter Mayes

Not at the current time.

Answer: Mike Merrick

In terms of complaints a minimum hurdle for us is obviously the complaints reduce in line with the policy volumes and I think we are looking to achieve and drive better than that. As I said, we are currently around the industry benchmark in terms of the volume of complaints but we think we can do better than that.

In terms of ombudsman referrals, again our uphold rate is very much in line with the industry, so we're not an outlier in any way.

Further question

Just give me a ballpark figure as to roughly how many complaints you've got or how it's trending.

Answer: Mike Merrick

I can't do that. We'll have to get you that information.

Barrie Cornes

Okay, thank you.

Question 4

Marcus Barnard: Oriel Securities

Can I just ask about how likely you think acquisitions are? I mean it's something you often talk about, you know, is this sort of a long term aspirational idea that you'd like to do them or do you think it's more a sort of short term realistic proposition?

Answer: Jonathan Yates

Well, perhaps I could pick that one up. I mean specifically we're here today to talk about more the operational side and our capacity to be able to take on acquisitions. And I think one of the things that Mike and the team have sort of demonstrated is that what we believe we have is an incredible model for taking on acquisitions and creating the scale benefits.

In terms of what you would get from those acquisitions and managing them in a way which is consistent and the fact that you're managing to a consistent model means the chances of actually developing, getting better profits than other people might do is that much greater.

In terms of the potential for doing deals then that's something we've dealt with in previous discussions that we've had but we see that as being something not for the immediate future but for the slightly more long term future.

Further question

So, if I may, in terms of how you run that department that looks at acquisitions or would handle the sort of process, how do you fund that? Do you fund that on a sort of aspirational long term basis i.e. not very much, or is it quite well funded?

Answer: Jonathan Yates

Well, put it this way, they're quite busy. There's no shortage of corporate actions for them to work on other than now getting involved in direct transactions, there's plenty of things to be done. And when we do get involved in a transaction specifically we bring in a very wide range of people which involves all the people sitting here today. So all the business gets involved in the due diligence process and planning for integration as part of the actual pricing and the deal process itself. It's not a sort of a virtual or a sort of a separate, segregated team that sits here in London that does acquisitions, it's very much a sort of a company-wide activity.

Further question

So in other words, if you saw a change in circumstances like your share price went up a lot we could potentially see an increase in acquisition activity quite quickly if conditions were right?

Answer: Jonathan Yates

I think that's probably not entirely unreasonable.

Question 5

Greig Patterson, KBW

Yeah, I'm just trying to get a feel, this is a question that's been puzzling me for a while, the burn through risk of all these with profit funds and I've got a series of questions around this issue, I wonder if somebody just wants to write them out and fire off as answers. The first one, and I'm not too concerned about GAOs because you do some hedging there but I'm looking at maturity and death guarantees in the with profit fund, the optionality in that. And I wonder if you can give us just a size of the TVOG liability. I think we can work it out from here but just as a starting point.

And if you can give us the size the sort of nominal risk, I suppose that's the asset share I suppose the answer is there as well. I'm trying to get a feel for the degree of "in the moneyness" of these guarantees when you do your modelling. I mean when you're TVOG is it all time value or is there an element of implicit value there as well? I'm just trying... if you can give us a feel for "in the moneyness" of those risks.

And then if you can talk about how you're hedging them, what sort of Greeks you're hedging etc so we can get a handle of where you specifically are exposed to those and what sort of market parameters?

And finally when you're modelling and you're making these hedging assumptions I'd like to get a feel for what sort of managing assumptions, sort of mitigating factors that you're assuming in the modelling and the hedging process, so we can get a feel for how tight or loose they are.

Jonathan Yates

You can do that Pete.

Peter Mayes

It might take the rest of the time.

Further question

Put it another way I don't know if you can talk about it in layman's terms you've got a big put option sitting on your balance sheet and I'm just trying to get a feel for how big it is, how near it is to being in the money and what attempts you've made to hedge it because I've tried it to look at that in a lot of detail and I find it a very difficult exercise to do. So I wonder if you can give us just a flavour of risk are we going to have a major burn through if the equity market drops 40% or interest rates the long end of the curve goes down to 1% this type of thing.

Answer: Peter Mayes

I'll certainly try my best. So in terms of the standalone funds clearly those funds are meeting their ICA requirements from within the fund. Clearly to the extent that we have guarantees and options the realistic value is what you'll see in FSA Returns, and clearly the ICA will capture the additional costs of various economic scenarios. The supported funds it's almost moved out from being an option to an absolute certainty so the asset shares as I showed you on that slide were substantially below the assets within those funds, and that actually guarantees almost a certainty. So for those funds you will see very little equity hedge fund property risk. You will see the majority of the guarantees and options being hedged out. And the numbers I quoted, the EV numbers I quoted, do allow for any burn through risk in those numbers. So that's a very, very brief... Is that too brief or do you want a bit more?

Further Question

I'm trying to ascertain where the strike is versus the nominal on the standalone funds are they well out of the money on the supported funds when you say they're hedged what do you mean by that? Hedging the delta, the vols, it's a black box we need some clarity on that that's what I'm...

Peter Mayes

OK, so on the supported funds they are in the money, quite considerably. On the standalone funds you will see a range of strikes and we do obviously disclose some information; it's going to be a range of strikes varying by product line, varying by term, varying by funds. But just to be clear on this the cost of those guarantees, the cost of those options are allowed for in the balance sheet and the capital requirements are allowed for in the ICA. In terms of risks we do hedge out the majority of the risks. We typically will aim to hedge out delta risk, for example, and we typically aim to hedge out interest rate risk. So as Mike was saying earlier we do have quite an active risk management programme that I think you would expect so that we do try and optimise our capital efficiency, and do try and aim to release cashflow up the Group.

Further question

When you do the delta is there an assumption that management's able, within your stochastic modelling process, is there an assumption that management should be able to reduce the high risk assets as equity markets start dropping? Or do you just assume unchanged asset allocations as no management you know I've heard of hedged delta where I'll name an insurance company called Standard Life I remember when they listed and I looked at, you know, I assumed that there was no management action I looked at applied vols it was 1% on their equities. So in other words they were just basically assuming away the problem with management action. I was wondering to what extent when you say you hedged are your models buffered by an assumption of the ability to just cut bonuses to zero instantaneously, sell equities instantaneously I was just trying to get a feel for how you come to your delta neutral hedge assumption?

Peter Mayes

We don't try and just assume everything will be mitigated magically by management actions. So to assume reasonable stresses will happen in terms of what we will then apply our delta hedging to.

Mike Merrick

I think as a broad guide we do tend to assume that we can, as we have done, management bonus rates actively. But investment strategy would tend to be assumed to be fairly static. But that's a broad guide rather than necessarily true in every case.

Further question

And just in aggregate know there's different strikes and I know that some of the pots it's not top down bottom up doesn't... but if someone woke you up in the middle of the night and put a gun at your head and said, "How far is the non supported funds out of the money as a percentage?" So what is the asset share's percentage of the strike? What would be your rough... is it 10, is it 5, is it 15, is it 20?

Jonathan Yates

It varies, I think it was actually shown on the slide in aggregate wasn't it? Actually I think we should move on now. Have we got a question at the back?

<u>Question 6</u>

Toby Langley - Barclays Capital

I've got a few questions I think primarily for Andy. The first one's on the suspense accounts quite an interesting concept to consider. Presumably given that this has been sanctioned by the FSA and/or the auditors this is a number that was to the credit from a net perspective on the balance sheets and hence that's why you were able to run with it. But could you clarify what the net position was? And if you had to put your finger on a similar number that still exists in your book today what would it be?

Secondly, on page 28 you've given a suggestion as to where capital synergies have been sourced and you've given a number of £225 million as to the total capital synergy benefit. Could you give us some flavour as to how that £225 million will be split across those different sources or the actions I think as they're labelled?

And then finally on the annuity pipeline within the book, the £800 million should we be thinking of that as going up, going down are we at the beginning of a hump or are we coming off a hump, that would be interested to know what that looks like as well?

Answer: Andy Moss

Okay if we pick up the first one around the suspense accounts first of all. The net position I can't remember the exact number it was in the region of about £280 million and I think as I said earlier on there were a large number of offsetting debits and credits within the balance sheet, and clearly we were adopting a reasonably prudent position hence why we obviously achieved benefits from that.

I think in terms of the balance sheet there are further opportunities, I would hesitate to put a number on it, there are certain things we are looking at it's going to be nowhere near in that order, certainly in terms of the things we have acquired we've largely done those amounts of work to date.

Okay. So in terms of the second question around the funds merger. Sorry could you just repeat the second question?

Toby Langley

Yes. I'm just trying to get some sense of you've got a total capital synergy benefit of £225m and then the bucket's you know how... has all that come from regulatory benefit, you know how much has come from tax? I don't know if these are the right way to think about these different actions?

Answer: Mike Merrick

I don't think it is really. They're all the activities you need to achieve one outcome and then that one outcome enables you to generate the tax benefits... not tax benefits sorry capital benefits.

Further question

Okay. And actually following up on that question actually could you remind us what was the capital base on which those capital synergies were earned? So what was the before and after capital base i.e. what was the percentage synergy benefit?

Andy Moss

No we don't know.

We can get you that.

Mike Merrick

You asked about the £800 million as well?

Toby Langley

Yeah the pipeline what that looked like.

Mike Merrick

We do expect it to be fairly flat for quite some time.

Peter Mayes

It's not going to suddenly fall off we see that as staying reasonably constant for the next short to medium term I'd say.

Question 7

Roddie Wallis, Brown Vanneck Partners

I think on slide 17 in your liability management you spoke about negotiating with policyholders to remove guarantees on products I think maybe annuities. I was wondering if you could give a bit more colour there on how that works.

Answer: Mike Merrick

We didn't actually negotiate with policyholders I'm sure you won't be surprised to know. We developed a scheme of arrangement and essentially the proposal there was that we undertook to increase the asset shares for policyholders in exchange for removing the guaranteed annuity benefits. The scheme was constructed to be broadly EV neutral otherwise we would not have got the approval of the courts and the regulators. There was an independent expert who reviewed the whole process and advised the court and policyholders voted as to whether they wanted to go for the scheme or not. And the key thing which enabled it to happen was we did allow policyholders, individual policyholders to opt out of the scheme. Very few did but we did allow that to happen. I think it was a block of 40,000 policyholders where this was implemented.

Roddie Wallis, Brown Vanneck Partners

Thanks.

Question 8

Ashik Musaddi, JP Morgan Cazenove

A couple of questions. One if you could give us some sense on the supported with profit fund. Are they supported by the shareholder fund, the other with-profit fund in the same business, or from the non-profit fund capital?

Second question would be your shareholder fund in the with-profit fund does that include that 10% of the estate in that fund? Thank you.

Peter Mayes

Second question yes. First one, I think it's from both non-profit and shareholder funds.

Mike Merrick

It's certainly not other with-profit funds.

Further question

So it's basically from the shareholder fund and the non-profit fund.

Mike Merrick

Yes. It tends to work in the first instance it's from the non-profit fund but it can be from the shareholder fund.

Further question

Can we get some sense of the capital requirement from that fund basically from the unsupported fund that is being... sorry from the supported fund that is being supported by the shareholder or the non profit fund?

Mike Merrick

I think I'd suggest you might look at it the other way round which is we show you the excess capital for each of our entities, that's the excess capital after providing for those supported funds and their capital requirements.

Ashik Musaddi, JP Morgan Cazenove

Thank you.

<u>Question 9</u>

Lance Burbidge - Redburn Partners

A couple of questions about the outsourcing agreements; you said they were generally 10 to 15 year agreements is that from now or is that from when you originally signed them and, if so, when did you sign them?

And in terms of longer term in acquisitions do you have a commitment from those outsourcers to take on new acquisitions at the same rate?

Answer: Tony Kassimiotis

So the 10 to 15 years is from the time the agreements were struck so largely that's around 2006/2007. Those agreements are perpetual in nature so we protect ourselves in terms of longer term so we can put those services back to the same outsourcer on a continuous basis at our request... at customer request rather than the outsourcers potentially walking away.

And your second question was?

Lance Burbidge

Will they take on new acquisitions?

Tony Kassimiotis

Yes so those agreements are built in with an ability for new business to be added to those agreements and that's already been pre-negotiated when those original deals were put in place at the start of the agreements.

Question 10

Greig Patterson, KBW

In terms of that £2.2 billion of annuity sitting in the with-profits fund if you transferred up does it also have to be EV neutral to pass muster with the independent actuary has to come and vet that?

And the other one this is historical question in terms of longevity risk and I think I've actually asked this question privately but I've forgotten the answer. Swiss Re used to have some reinsurance, quite substantial, with either NPI or London Life one of them, is that still around and, if so, would there be an opportunity to renegotiate or I'm just trying to find to what extent you have already passed on some of your longevity risk?

Answer: Mike Merrick

There are a number of longevity risk reinsurance treaties within the Group. I'm not really aware of them being with Swiss Re but there is a material amount of longevity reinsurance.

And in terms of the question of what terms could the £2.2 billion leave the fund the key is that it's fair and there are many ways in demonstrating that it's fair. We currently demonstrate how with profit policies or guaranteed annuity policies the vest transfers to the non profit fund and that's on the basis of the kind of profit margin that Pete was talking earlier. So it's a process that we need to go through it's a block transaction and there will be independent experts involved in the process, but I don't think it's far from certain that it would have to be EV neutral I think there's a definite opportunity.

Further question

So it would be like sort of 8% minus the commission that you have to kick back to the fund?

Mike Merrick

Yes. Somewhere in the middle.

Further question

I mean traditionally commissions are sort of 150...

Mike Merrick

Yes 1% and 2% that sort of thing.

Further question

Now has that been included in the synergies you've already told us about or is this part the £225 or whatever or can I sort of add that?

Mike Merrick

It's part of the means of delivering the targets we've already talked about.

Further question

So it could or couldn't be. You've got a pipeline of things of which obviously in excess of the 225 and one might...

Jonathan Yates

I think the easiest way to put that is we've set goals for embedded value growth through management actions. This, should we choose to do it and should we reach agreement, would be one of those management actions.

Further question

And when you quote annuity liabilities are those net or if you're reinsuring the longevity and you're still left with the spread risk how do you adjust... are we looking at gross numbers liabilities here or are they net adjusted for... I'm just trying to understand?

Peter Mayes

The ones I've quoted, the £5.9 billion I've quoted there that's gross liabilities.

Further question

You're not on hock for the full longevity on it? Those reinsurance contracts.

Peter Mayes

Correct.

Further question

All right so it's spread on the... could you venture a percentage?

Jonathan Yates

The reinsurance isn't substantial though is it? The longevity reinsurance that exists within the funds is quite minimal by comparison with the total number we've just quoted.

Mike Merrick

It's relatively small yes.

Jonathan Yates

And don't forget we've got another £3.5 billion in the Group that sits within Opal Re so the total amount of annuities is significantly greater than the number that Pete described which is only the Phoenix Life annuities.

Further question

(In auditable)

Jonathan Yates

No it's all retained within Opal Re but it just wasn't included in the total number that Pete indicated. It is actually mentioned on the slide.

Mike Merrick

Just a point of detail the reinsurance that we do, reinsures the spread risk as well as longevity risk.

Further question

So it's not swaps?

Mike Merrick

No that's it.

<u>Question 11</u>

Ashik Musaddi, JP Morgan Cazenove

Just one more question on the PALAL. You mentioned that this has been transferred on 1 January 2011 so the free surplus generated from this transfer is that included in your £700 to £800 million cashflow target for this year or that part is not included? If you could give some colour on that.

Andy Moss

Yes it is.

Ashik Musaddi, JP Morgan Cazenove

Thank you.

Jonathan Yates

Okay. Are there any more questions? Thank you very much indeed everybody for coming along today we really very much appreciate you coming along to hear about Phoenix Life. As Mike described earlier and as the team have explained we believe we do have a phenomenally strong platform on which to run this business, but not only run it but to grow it going forward. And it gives us all the scale benefits that we would seek to have. And as I said earlier and as Mike and the team explained having a consistent, simple model for

running the business is essential if you are going to drive out those scale benefits and create value from acquisitions.

I also appreciate this is really just scratching the surface of something which is a phenomenally large and complex business and we would be delighted to try and take this forward and answer more questions that might occur to you in future. And we'd be delighted if you could come back to us and ask us any questions at any time. But in the meantime, thank you very much indeed for coming along today, we appreciate it.

Thank you.