Phoenix Group Holdings

Thursday, 29 Nov 2018

Capital Markets Day

Nicholas Lyons, Chairman

Well good morning ladies and gentlemen and a very warm welcome to Phoenix's Capital Markets Day which we have titled Cash, Resilience and Growth. It is terrific to see such a good turnout here at 10 Trinity Square.

My name is Nicholas Lyons and I'm delighted to be here with you today as the new chairman of Phoenix. We have a busy agenda and my introduction will therefore be brief. Our management team will provide you with a trading update on Phoenix's year-to-date performance and will also explain to you how Phoenix has changed as a result of the transformational acquisition of Standard Life Assurance Limited, which completed on 31 August 2018.

During my time with the Group I have been impressed with the team's singular focus on the delivery of our financial targets and strategy. I leave you in their capable hands and look forward to seeing you either over lunch today or over the coming weeks or months.

I'll pass over now to Jim McConville, Group Finance Director and our Group Director for Scotland. Jim.

Jim McConville, Group Finance Director and Group Director for Scotland

Thank you very much Nick and good morning everyone. I would like to start today with a brief update on our trading performance. We have today updated the market on our strong performance in 2018. The highlights are compelling.

We have delivered £1.3bn of cash generation in 2017 and 2018, exceeding the upper end of our target range. Our Group solvency position has improved with a surplus of £3.1bn at 30 September, with a 164% Shareholder Coverage Ratio. The increase in the period is in part driven by £400m of capital synergies delivered on the Standard Life business.

Our Assets under Administration have remained stable at £240bn over the period to Q3 from the pro forma Full Year 2017 position. This reflects strong business net inflows on our Open and Heritage businesses which has offset outflows on our Heritage books. And our funding outlook is positive with circa £1bn of financial resources available for inorganic growth.

We have a long track record of either meeting or exceeding our cash generation targets for many years. I am delighted to announce we have now completed our 2018 cash generation with a further £315m delivered in the second half of 2018. This takes cash generation to £1.3bn over 2017 and 2018, significantly ahead of the £1bn - £1.2bn target we set for this

two year period. We remain very much on track to deliver our five-year cash generation target to 2022 and in March next year we will update you on revised targets.

Rakesh will talk in more detail about our year-to-date performance in a few minutes.

Moving on now to the transition programme. On 31 August 2018 Phoenix completed the acquisition of Standard Life Assurance Limited or "SLAL" as it is known. This deal was transformational for Phoenix adding significant additional scale to our business and extending both the quantum and duration of our cash generation. It also changed Phoenix into a biped with both Heritage and Open business channels and our product range under the Standard Life brand that is market-leading across workplace, retail pensions and Wrap products.

At our 2018 Interim Results presentation in August we outlined our plans for the transition. Today we will update you on our progress post-completion and can confirm that we are on track to meet the Day 100 milestones we outlined to you back in the summer.

Our Full Year results presentation in early March 2019 will be our first as an enlarged group and at this date we will issue updated cash generation and synergy targets that reflect our transition strategy. We continue to expect to complete our transition of the combined business by the end of 2021 – this is within three years rather than the four we originally signalled on the announcement of the acquisition.

We have established a set of objectives for the programme. The programme is responsible for designing and implementing an end state operating model which retains the best of both organisations whilst delivering on cost and capital synergy benefits.

In February we set out our indicative expectations of synergy benefits which we are now confident we will meet or exceed. Our strategic partnership with Standard Life Aberdeen underpins the products we continue to underwrite and administer under the Standard Life brand. We will focus on embedding this partnership into the heart of our business.

It is also important that we continue to deliver services to Standard Life Aberdeen under the transitional service agreements and work towards exiting these agreements by the end of 2021.

We have identified five guiding principles to ensure that the end state operating model will meet the strategic priorities of the Group. First we want to preserve the existing business model by ensuring that the Group's proven capabilities in managing in-force business are maintained and enhanced.

We are no longer a purely closed business and therefore our operating model must also support the Group's expansion into capital light Open book management and cultivate the specific skills and capabilities required to grow and deliver value in the open market for life and savings products. The existing SLAL business has a wealth of talent and experience of open book management which we can build upon.

This slide shows the structure of the Group as of today. Two independent businesses in the form of Standard Life and Phoenix Life, with Phoenix Life a predominantly Heritage book and Standard Life a mix of Open and Heritage business. We calculate our Solvency II capital requirements through a combination of two separate regulatory approved Internal Models for our UK business and the Standard Formula for our international business.

This second slide shows our end state operating model. We will manage our business along geographical lines. Our UK operations will ultimately be within a single life company and the small European business will operate from Standard Life International which is domiciled in Ireland. We will calculate the Solvency II capital requirements of the whole Group using a single Internal Model.

Our UK business will be managed in two segments: Heritage and Open.

Our Heritage business will include products that are not actively marketed to customers, for example with-profits business, annuities and many of our legacy unit linked life and pension products.

Products which continue to be actively marketed to new and existing customers will fall into the capital light Open business segment and will include those products sold under the Standard Life and Sun Life brands.

These three separate business segments will be supported by a set of combined support functions. These support functions include Customer services, IT and back office support such as Finance, Actuarial, HR and Legal.

We have £240bn of assets under administration. We will apply Phoenix's proven model for adding value through the delivery of management actions across the whole of this in-force book, irrespective of the business segment. We have estimated this in-force business will deliver £12 billion of cash generation over the life of the book. And this cash generation will be increased by new business written across all three segments.

We are working to finalise our end state operating model which we will deliver in three phases. Phase 1 includes the enabling functions such as HR, Legal and Risk and will be completed by the end of 2019.

Phase 2 covers Finance and Actuarial and will be completed by the end of 2020. And this includes the harmonisation of the Group's capital frameworks and related Internal Models and systems.

And finally the most material element of our combined cost base – our Customer and Technology functions – where we will complete our work on the end state operating model by the end of 2021. In parallel we will explore opportunities in our European operations.

The transition programme is responsible for the delivery of capital synergies and a single Internal Model for the whole Group.

In February we set a £440m capital synergy target for the acquisition which we expected to deliver through a combination of hedging and strategic asset allocation. The actions we have taken to mitigate the shareholders' exposure to both equity and currency risk on the SLAL business have already realised capital synergies of £400m, ahead of our expectations.

Work is ongoing to identify the further management actions which will include applying our strategic asset allocation to the SLAL annuity book and ultimately delivering a Part VII transfer to a single UK Life company legal entity. We therefore expect to deliver more capital synergies than originally envisaged and will provide regular updates to the market on further management actions at each reporting period.

In addition, the programme will also bring together our two Internal Models. This has never been done before and the timeline we outline today targeting PRA approval by the end of 2020 remains indicative as we work through a number of key decisions and work with our regulators to assess do-ability.

The combined cost base of the Group is £600m per annum. Our work to date has identified a number of opportunities which provide us a high degree of confidence that we will meet or exceed our £50m per annum cost synergy target.

In Phase 1 we will harmonise our systems, processes and management teams across risk, HR, legal, procurement and internal audit. We will seek to harmonise the best of both in bringing our legacy organisations together and will deliver enabling functions which support the wider business across all three business segments.

In Phase 2 we will bring together the financial, actuarial and investment offices of the Group. This will include implementing a single ledger, a single Internal Model, a single actuarial modelling platform and a single set of financial processes and controls.

In Phase 3 we will deliver a best in class operating model which supports both our Heritage and Open businesses, maintains customer service levels and acts as a foundation for future acquisitions. To date, Phoenix has utilised an outsourced model for customer administration which has the advantage of delivering a variable cost base to a Heritage business in run off. SLAL undertake their customer administration and technology in-house, enabling them to respond quickly to an evolving customer proposition.

Our transition will deliver an operating model which preserves these key attributes and, inevitably, will have a combination of both outsourced and in house operations. Work is ongoing to define the detailed model and the changes will take some three years to implement. We remain committed to retaining Edinburgh as an operational headquarters.

To conclude we have delivered £1.3bn of cash in 2017 and 2018, exceeding the upper end of our target range for this period.

We have a clear vision for our end state operating model which will have three business segments: UK Heritage, UK Open and Europe. These business segments will be serviced by a single set of supporting functions.

The programme is on track and will deliver in three clearly defined phases by the end of 2021.

We have already completed sufficient work on the design of our end state operating model to have a high degree of confidence that we will meet or exceed the £50m per annum cost synergy target announced in February. Having already delivered £400m of capital synergies we are on track to exceed our original capital synergy targets and will continue to search for value accretive management actions.

We will shortly complete the planning stage of our transition programme and will update our cost and capital synergy targets and set new cash generation targets when we report our FY18 results in March.

Andy Moss, Chief Executive Phoenix Life and Group Director Heritage Business

Thank you Jim and good morning everyone. Phoenix are specialists in the safe and efficient management of Heritage business with a strong track record of delivery. Our UK Heritage business comprises products that are no longer actively marketed to customers and has £125bn of assets under administration.

The Heritage business has been built from two decades of consolidation. It comprises over 100 legacy brands including Britannic, Pearl, Scottish Mutual, AXA, Abbey Life and Sun Alliance. It has a broad range of life and pensions products which provide Phoenix with natural diversification.

Our strategy for our Heritage business is simple – to deliver value to shareholders and customers and to improve customer outcomes. Integral to this is ensuring that our cost base reduces more quickly than our policy run off.

Insurance can be seen as a complex business which is hard to understand. At Phoenix, we have simplified things by making cash generation our key metric of value delivery. By cash generation, we mean physical cash remitted to the Group from our Life companies out of free surplus.

We have a strong track record of delivering cash generation having met or exceeded all financial targets since we obtained our premium listing in 2010.

Organic cash generation emerges naturally from our Heritage business as it runs off and capital unwinds. At Phoenix we enhance this organic cash generation through the delivery of management actions which either increase the overall cash flows from the business or accelerate the timing of these cash flows.

Cash generated from management actions is lumpy and whilst over 50% of our cash generation in recent years have been attributable to management actions we expect this ratio to return to one third over the longer term.

The first layer of our management actions maximise the shareholder value from each product type. For with-profit funds where the shareholder shares in bonuses, including the estate distribution, management actions will target increasing the value of the estate and, or accelerating its distribution in a managed way.

For unit-linked business where the shareholder earns a margin, management actions seek to reduce costs through expense base management and mitigate the shareholders exposure to market risk through hedging.

Annuity business is a spread business so here management actions seek to increase asset returns and manage exposure to longevity risk through reinsurance.

Free surplus is calculated at an entity level and we therefore deliver a further layer of management actions at company level which either increase value or accelerate cash.

Cost efficiencies continue to be a key source of management actions which add value across both Heritage and Open books. We delivered £27m per annum cost savings on the acquired cost bases of AXA and Abbey and, as Jim outlined; we have a current target of £50m per annum savings for the transition of the Phoenix and SLAL businesses.

We also add significant value through our approach to investment management which includes asset liability matching, our move to more illiquid assets backing our annuity portfolio and our use of hedging.

On the risk capital side, Internal Model harmonisation, reinsurance and Part VII transfers all enable us to access diversification benefits and therefore increase free surplus. These actions have all been integral to delivering value on our recent acquisitions.

Not only do our management actions focus on delivering value to shareholders, they also look to deliver value to customers and improve customer outcomes. At Phoenix Life we recognise the importance of a sustainable outsourcer model for customer administration that delivers a digitally enhanced offering to customers and can adapt to change in a fast and cost efficient manner.

We have selected Diligenta to partner Phoenix for this journey and as a result will be transferring circa 2 million legacy-Phoenix policies to Diligenta by end 2021.

Following this transfer, Diligenta will administer circa 5.5 million Phoenix policies from a single administration platform. This will deliver an end to end digital journey and enhanced customer experience. It will also lead to a reduction in per policy administration cost across the legacy-Phoenix book.

The benefit of this management action was recognised in H1 this year with a £100m Solvency II benefit emerging, part of which was reinvested for the benefit of customers in charge capping.

As Jim explained earlier, we will apply a single approach to the management of our in-force book of business. Essentially this means that we will seek to deliver management actions across all of our in-force business. We are often asked when these will run out. With a 224% increase in our assets under administration, the simple answer is not for the foreseeable future.

We have traditionally sought to identify management actions across four main buckets: operational management, restructuring, risk management and effective partnerships. We will therefore continue to focus on the delivery of management actions across both our Heritage and Open books of business.

Turning now to the customer. As a Heritage business, we are passionate about improving customer outcomes on the books we administer. Abbey Life provides an excellent case study of the benefits we bring to customers when they join the Phoenix family. As you will be aware, Abbey was under FCA enforcement when we acquired it, and under review for its non-advised annuity sales practises.

On Day 1 we rolled out our oversight model and approach to product governance with the result being that all regulatory actions and concerns have now been addressed.

At Abbey we have improved value for customers by introducing charging caps, increased customer engagement through our gone-away tracing exercise and improved effectiveness by implementing a mandatory annuity shopping around service.

As a result, we are now certain that the indemnity provided by Deutsche Bank at the point of acquisition to cover the costs associated with these FCA reviews will be more than sufficient.

We will continue to put customers at the heart of what we do at Phoenix.

To summarise, Phoenix specialise in the safe and efficient management of Heritage business and we have a proven track record of delivering value.

The Heritage business generates organic cash flows which Phoenix enhance through the delivery of management actions. This gives us dependable cash generation in the short, medium and longer term.

Moving forwards we will continue to focus on delivering value to shareholders and customers and extend our programme of management actions across both our Heritage, Open and European businesses.

I'll now hand you over to Susan.

Susan McInnes, Chief Executive Standard Life Assurance Limited and Group Director, Open Business

Thank you Andy and good morning.

I wanted to take some time this morning to talk to you about our Open capital light business. This business is important to Phoenix as it brings both additional scale to our operations, but it also dampens the run-off of our Heritage books, extending our dividend paying capabilities.

As Jim mentioned, we define Open to be products that are actively marketed to new and to existing customers. In the main our Open book business refers to those products being sold as part of our strategic partnership with Standard Life Aberdeen, but it will also include those aimed at the over-50s market distributed by Sun Life.

We have just over £90bn of assets under administration in our Open business, predominantly held in three segments: workplace, retail pensions and Wrap products.

In terms of size almost half of our assets are in workplace, which has benefited from the recent growth following auto-enrolment.

In terms of revenue the picture is similar, with more than half of the revenue coming from workplace, and a small proportion, about 13%, coming from Wrap products.

It's important to note that these are all unitised products which have no guarantees and where the investment risk sits with the customer. Our Open business therefore comprises only capital light products.

In terms of strategy there's very much a shared vision with our Heritage book in that we aim to deliver value to shareholders and customers alike. Our strategic partnership, which leverages the skills of both organisations, is important in supporting that strategy.

Let me describe how this new element of the strategic partnership with Standard Life Aberdeen works. We refer to this as our Client Service and Proposition Agreement.

So, Standard Life Aberdeen is responsible for distribution, branding and marketing of the products. They do this through their existing networks of employee benefit consultants and independent advisors, and for some products using their successful investment platform.

Responsibility for the investment platform, which for some of our investment products such as Wrap SIPP and Onshore Bond also sits with Standard Life Aberdeen, given that that platform will also host their specific products such as mutual funds and direct investments.

Where a customer needs or wants advice it can be delivered by Standard Life Aberdeen's in-house advice arm.

Phoenix are responsible for providing the insurance product and the administration once the product is sold. This plays very much to our strengths given our existing expertise in product administration for our existing circa 5.5 million Phoenix Life customers.

The relationship is built to work seamlessly for customers with the full proposition from distribution through to administration being done under the Standard Life brand.

In terms of risk they remain unique to both organisations and linked to the activity performed.

I'd now like to take a couple of minutes to describe in a bit more detail what sits within the Open book. Firstly workplace. Standard Life has built a strong proposition to compete in the workplace auto-enrolment market, with 35,000 schemes across over 16,000 employers serving around 2 million customers.

Auto-enrolment for all employers is now complete, but the strength of the Standard Life proposition puts us in a strong position to react to market trends, such as scheme reviews and employers shifting from unbundled to bundled arrangements.

The brand continues to benefit from strong relationships with large employee benefit consultants and employers.

But even without the introduction of new schemes our expectation is that workplace will continue to grow. Over 280,000 customers join naturally each year through existing employer schemes, and the increase in auto-enrolment minimum contribution levels from 5% to 8% in 2019 is also expected to contribute an additional £400m assets under administration each year.

You will hear later from Rakesh that this new business has not been counted in our cash generation estimates, so any increase in premiums or new policies will be upside to cash generation.

Critical to success here is scheme retention. And with Standard Life Aberdeen we'll continue to invest in the overall proposition to ensure it remains competitive and differentiated from the competition. Similarly we believe employee engagement is key, not just to ensure that our customers save more for the future, but also to encourage them to stay with Standard Life in our retail product if and when they leave their workplace employer.

While mentioning retention it's important to emphasise we have seen no increase in lapse rates following the acquisition of this business by Phoenix. The charging position is simple here: the customer pays one product charge to us, from which we pay a proportion to Standard Life Aberdeen to cover investment management. There are no further charges.

The retail pensions book is in part built up by the strategic partnership with Standard Life Aberdeen where they sell retail pension products via independent advisors. We also see a steady flow of customers moving from workplace schemes to retail pensions when they

change employer. This helps us retain assets under administration within the Group, and it provides an easy way for customers to keep both their product in the accumulation stage of their life and to consolidate pension pots with other providers into one vehicle.

The products themselves have a strong digital and service offering which is critically important in this marketplace.

Retail pensions will continue to grow, and we think the product makes us well-placed to offer a solution for both that accumulation and decumulation fees, and keep our customers into the longer term.

Turning now to Wrap. Wrap has historically been one of the largest areas of growth for Standard Life. As mentioned previously, the platform itself remains with Standard Life Aberdeen, and it's very well positioned to continue to grow, given the functionality offered through the platform and the strong relationships with advisors.

In terms of how the relationship works with Standard Life Aberdeen, all product charges are collected by Phoenix, all platform revenue collected directly by Standard Life Aberdeen, and the customer pays any investment fees directly to Standard Life Aberdeen. Clearly this is a very competitive market, but the Wrap platform remains number one in the market based on both advised gross and net volumes, and is very well placed to grow in the future.

The last area I wanted to mention is our European business. This business contains both Open and Heritage products split across Germany and Ireland. They also manufacture an International Bond which is sold by Standard Life Aberdeen through the retail market and the investment platform. All other products are sold by the European units themselves.

Our European business distributes to the more affluent population via the broker distribution channel, and is supported by around 650 European based employees.

In terms of the Open book it's important to know that all the products currently being sold are capital light, unitised, fee based products. The German book does have a large with-profit book as part of the Heritage business, which has been closed to new business since 2015.

Across both Heritage and Open products the European business is self-sustaining. Our focus in 2018 has been about preparing the organisation for Brexit and we're well advanced in our plans to move the German and Irish branch businesses into Standard Life International, an Irish insurance entity. Clearly continuing to operate a seamless service to our customers post-Brexit is key.

Our European operations also give Phoenix optionality to grow inorganically through both Open and closed European life consolidation.

So, to finish: both our UK and European Open businesses comprise a range of modern, fee based products that are capital light in nature. We see growth in assets under administration across all areas of our Open business, which will dampen the run off of our Heritage business.

The strategic relationship with Standard Life Aberdeen plays to the strengths in both organisations and may give us opportunity to look for other ways to work together in the future to add value to both businesses.

Europe, while currently small in terms of value, gives us optionality for future consolidation should an opportunity present itself.

And I will now hand over to Simon.

Simon True, Group Corporate Development Director and Group Chief Actuary

Thank you very much Susan and good morning everyone.

Phoenix now has a range of growth opportunities. As Susan has explained our Open business in the UK and Europe is capital light, and therefore does not require us to allocate capital to support this business. However organic growth, vesting annuities and inorganic growth do require capital, and we have a disciplined approach to the deployment of capital which optimises value for our investors.

To do this we use a dynamic capital allocation framework to assess growth opportunities using a hurdle rate of return which is based on our weighted average cost of capital, plus a project specific risk premium.

We continue to apply three key criteria in assessing M&A opportunities and BPA. Namely any transaction must be value accretive, it must support our stable and sustainable dividend policy, and finally it must maintain our investment grade rating.

Whilst we now have a range of growth opportunities our key focus remains on growing the business through mergers and acquisitions. The three acquisitions which we have completed in the last three years have transformed the Group, bringing an additional £7.6bn of cash generation, establishing Phoenix as the largest life and pensions consolidator in Europe.

Scaling the consolidations sector brings competitive advantage, and I will illustrate that in a few moments. It is this scale, combined with Phoenix's strong regulatory relationships, flexibility in financing, which positions us strongly to execute value creating transactions in the future.

I'm going to take a few moments on this slide because it will actually go to serve to illustrate how we can generate value through mergers and acquisitions. The integration of the AXA acquisition is now complete and it serves as a key case study.

If I start on the left-hand side, you will remember that we paid £373m to acquire the AXA business in 2016. This was an attractive price for a sub-scale business, and it allowed AXA to deploy the proceeds in higher return businesses elsewhere in their Group.

From our perspective the purchase price represented 85% of the Solvency II Own Funds at the year-end 2015, which had a surplus over the Solvency capital requirements of £152m.

Since announcement of the transaction in May 2016 we have delivered a wide number of value accretive management actions which have supported the Group's cash generation.

Prior to completion we undertook hedging of the acquired business's exposure to equity and interest rate risk. We also took the opportunity to strengthen some elements of the Solvency II balance sheet based on our findings during the due diligence. Day one internal

reinsurance allows us to access some initial diversification benefits to reduce risk capital and to increase Own Funds.

The move to Phoenix's outsourcing model generated maintenance expense savings which were capitalised into Own Funds. Extending Phoenix's Internal Model to the acquired business generated a significant reduction in risk capital. And finally when we finalised the Part VII transfer of the business into Phoenix Life Limited this generated the final capital synergies and increased Own Funds.

Overall these management actions increased the Own Funds to £553m. Or saying it another way, we effectively bought at 85% of Own Funds which we turned into 125% after the completion of our management actions.

In addition the management actions reduced the solvency capital requirements attributable to the business from £289m on a standalone basis to £103m. And that enabled us to significantly accelerate the release of cash.

And all of this was evidenced by the £282m of cash distributed within six months of the acquisition and which was used to pay down our debt financing on the transaction.

Every M&A transaction is unique, but there is a commonality in Phoenix's approach. Our second acquisition in 2016 was Abbey Life, and again we bought it at a discount to Own Funds. We then sought to enhance these Own Funds through expense reductions and adoption of our strategic asset allocation.

We then undertook a number of further management actions, including internal reinsurance to access day one capital synergies, adoption of the Phoenix Internal Model, and finally a Part VII transfer of the business into Phoenix Life. All of these actions were only accessible to us due to our scale as a consolidation player.

And on Standard Life, as you have already heard, we will be adopting exactly the same approach. We will look to boost own funds to expense savings and our strategic asset allocation, and we will look to reduce risk capital through hedging, harmonisation of the Internal Models, internal reinsurance and ultimately through Part VII transfers of the business.

In June last year we set out our plans to extend our M&A capabilities to the bulk purchase annuity market. Since that time we have built a small dedicated team and established our presence in this rapidly growing market. We've been very clear in our approach to this. Our target for growth is proportionate. We are looking at around £500m to £1bn of volume per year. We are focused on cash generation, not volume. That means we can be selective in our choice of deals. And we have also been clear that we will fund this line of growth from our own resources.

In the first half of the year we announced our first transaction with the Marks & Spencer's pension scheme, but we have completed two further transactions in the second half of the year, bringing our year to date BPA volumes to £0.8bn.

We have invested around £100m of capital to facilitate these transactions. This investment increases our longer-term cash generation by around £300m.

The BPA market is undoubtedly growing; latest estimates are of a £20bn market this year with steady year-on-year growth thereafter. And Phoenix is well-positioned to benefit from this market growth and generate longer-term cash flows to support our dividend in the future.

Our ability to compete in the BPA market is heavily influenced by our asset sourcing capabilities. At our Interim Results in August we outlined the intention to increase our allocation of illiquid assets which back annuity liabilities to 40%. And to execute this strategy we have developed our asset sourcing capabilities through a combination of direct sourcing and third party mandates.

We have established direct sourcing relationships with over 60 issuers, banks, brokers, consultants and advisors, and these relationships have been extremely effective in building our portfolio of equity release mortgages and in securing bespoke bilateral transactions.

For asset classes such as commercial real estate and infrastructure debt we have put in place third party mandates which will leverage our chosen partners' expertise and market access.

Year to date we have originated £1.2bn of illiquid assets over 19 individual deals, and this has delivered over £100m of solvency benefit to the Group.

To summarise: Phoenix now has a range of growth opportunities, and we apply a clear set of criteria in assessing the relative attractiveness of these options. We will continue to participate in the BPA market on a selective and proportionate basis. This activity is supported by a strong asset sourcing capability which will ensure that we can price competitively and deliver appropriate risk adjusted returns for our investors.

However it's mergers and acquisitions which really turn the growth dial, and we have a strong record of delivering value to our shareholders on UK M&A, and it remains our core focus going forwards.

Thank you.

Rakesh Thakrar, Group Deputy Finance Director

Thank you Simon. At the start of today's presentation Jim provided you with a trading update across our key metrics. I am going to outline the drivers of our year-to-date performance and set out how we will report our business in the future.

As you have heard, Phoenix has changed, and as a result our reporting will evolve. Cash generation will remain our key reporting metric going forward. We will set new targets for the Combined Group when we announce our year-end results in March, but our approach to the setting of these targets will remain unchanged.

For our Solvency II reporting we will report the contribution of new business to own funds in each period, and the impact from writing new business. We will now report movements in assets under administration showing net flows for each business segment.

And finally our operating profit will be reported for each business segment separately. Our first update on operating profit will be made with our Full Year results, at which time we will extend our disclosure of operating profit drivers across our Open business lines.

I wanted to take a moment to confirm what is included and what is excluded from the cash generation guidance we have given. Currently we have given an estimate of £12bn of cash generation from the £240bn of in-force assets under administration, and this is of the Combined Group. This includes regular premiums on in-force policies and management actions in the first five years from 2018 to 2022.

However our cash generation guidance excludes the incremental premiums on in-force policies, new business arising on our UK and European Open businesses, management actions post-2022, and any inorganic growth from either BPA or M&A. We therefore feel confident that the actual cash generation will be higher than the guidance provided.

We are often asked about the shape of our cash generation. Prior to the Standard Life acquisition we were largely a Heritage business, and therefore in the absence of M&A or BPA we would expect our cash generation to decline as the Heritage business runs off. Our Open business changes this. Susan has explained how we expect our Open business to grow in the future. Assuming future growth at the levels experienced in 2018 year to date we expect the cash generated from our Open business to offset the run-off of cash generation from our Heritage business.

Management actions will increase or accelerate cash generation, and this will be delivered across both our Open and Heritage business segments.

As an Open business we will now report period movements in assets under administration. The Full Year 2017 opening position is the Combined Group assets under administration as previously reported in our acquisition related prospectuses. Movements in the period therefore include those of the acquired Standard Life business for the Full Year rather than just the post-completion period, and show that net inflows on the UK Open and European business have, together with positive market movements, fully offset the net outflows on the UK Heritage business.

This is an indicator of the transformational nature of the Standard Life acquisition to the Phoenix Group, which has previously only ever presented net outflows in assets under administration period-on-period, and supports the evolving cash generation profile on the previous slide.

The solvency position of the Group has also been significantly strengthened from the Combined Group Full Year 2017 figures presented in our acquisition prospectuses, increasing from a pro forma surplus of £2.5bn to a 30 September 2018 actual Group surplus of £3.1bn.

The increase in surplus translates to a 17% increase in the Shareholder Coverage Ratio in the nine-month period to 164%, and demonstrates the increased resilience of the Group.

Integral to this increase is the delivery of £0.4bn of Standard Life capital synergies that Jim explained earlier, which are in additional to the £0.4bn of management actions delivered in the period on the legacy Phoenix business.

We have also seen the benefit in our solvency position of issuing more capital qualifying debt instruments in the period than anticipated in our pro forma figures.

It is important to note that the new business capital strain of £0.1bn relates to the cost of writing BPA only. We have seen no capital strain in the period from organic new business,

with the strain of writing vesting annuities in our Heritage business being offset by the gain arising in our new business across the Standard Life range of Open products. New business has made £0.2bn contribution to own funds in the period.

In addition the adverse impact of the equity hedge implemented at announcement has been largely offset by the growth in own funds within Standard Life in the period.

To demonstrate our improved resilience, we have set out the sensitivity of our Group solvency position to various stress events. As you will be aware, Phoenix has a low appetite to market risks and uses hedging to mitigate the majority of its exposure to equity, currency and interest rate risk. This translates into the extremely low sensitivity to these risks we present today. You will see that all of the sensitivities tested here keep Phoenix well within its target Shareholder Coverage ratio range of 140% to 180%.

If the Group Shareholder Coverage ratio were to fall below this target range, we would consider appropriate rectification plans after allowing for surplus emerging and in-train management actions. And if the Group's Shareholder Coverage ratio were to go above this target range, we would consider future available options for the deployment of capital, which could include a potential return of capital to investors.

We see a similar resilience in our cash generation expectations from these risk events. This is driven by the direct relationship between surplus capital and cash generation. Phoenix's resilience to risk events remains a key differentiator of its business model and approach to risk management, and underpins the dependable nature of our cash generation in the short, medium and long term.

This slide is provided courtesy of Deutsche Bank who recently issued a report comparing the sensitivity of insurance firms to movements in key market risks. We have included our main UK life peers in this exhibit, which clearly demonstrates that Phoenix's resilience is very strong relative to its peers.

We are often asked whether Phoenix provides a shareholder value metric, and reiterate today our ongoing belief that Solvency II Shareholder Own Funds provides a good proxy to such a metric. As many of you will be aware, we already provide a bridge between the strict regulatory measure of Solvency II Own Funds, and a shareholder view of Own Funds, by removing the unrestricted own funds of our unsupported with profit funds and the PGL pension scheme. As at 30 September 2018, the Group had Shareholder Own Funds of £8bn. To move to a view of the unrestricted Tier 1 capital available to equity investors, we must then remove the face value of the debt instruments Phoenix has in issue across all three capital tiers.

However, Solvency II Own Funds does not attribute value in a number of areas where real shareholder value exists. These include contract boundaries where the value of in-force on the unit linked business is restricted under Solvency II and the shareholders' share of the with profits estate. Adjusting for these items quantifies a proxy to shareholder value for Phoenix at 30 September 2018 of £6bn, which equates to £8.32 per ordinary share. Additional shareholder value will of course be created as new business is written and management actions are delivered.

Moving now to leverage and funding capacity. Whilst Fitch only calculate and publish their formal calculation on our leverage ratio on a semi-annual basis, we have estimated our 30 September 2018 leverage ratio, calculated in accordance with their stated methodology, to

be 22%. This is below the target range associated with maintaining an investment grade rating of 25% to 30%.

Our under-leverage has been driven by the restricted Tier 1 bond issued in April, and unallocated surplus being recognised as equity in the Fitch calculation. Recalculating the ratio on an IFRS basis of debt over debt plus equity, would equate to an IFRS leverage ratio of 33%. We calculate our current capacity for funding in organic growth without a return to equity markets through a combination of our leverage and shareholder solvency coverage target ranges. The nature of the acquisition targets' balance sheet will also impact on our capacity. The current under-leverage against our Fitch target range and strong Solvency II Shareholder Coverage ratio, provides us with a funding capacity of circa £1bn as at 30 September 2018.

To conclude: Cash generation remains Phoenix's key reporting metric, and we will provide updated cash generation targets in March. Whilst current cash generation is predominantly driven from our Heritage business, we now expect growth in our Open business cash generation to offset Heritage business run-off. The growth of our Open book is evidenced by the stability of our assets under administration over 2018. Open new business written places no capital strain on the Group, and our solvency position is significantly strengthened with a surplus of £3.1bn at 30 September 2018.

We have set out today the resilience of our balance sheet and therefore our cash generation to sensitivities, and illustrated how this sets us apart from our peers. We are therefore extremely comfortable operating a target shareholder ratio range of 140% to 180%. Phoenix reports today a position of financial strength, and with our current leverage sitting below our target range we have significant funding capacity for further acquisitions.

Thank you. I'll hand you over to Clive.

Clive Bannister, Group Chief Executive

Thank you, Rakesh, and thank you to my team. What an extraordinary group of individuals. It falls on me to conclude the presentation today, and I start with a thank you to our new colleagues at Standard Life. We have found a community of truly hard working committed professionals who share with Phoenix a genuine love and knowledge of our business, insurance.

Today, with £240bn of assets under administration, and circa more than ten million policyholders and customers, Phoenix is the largest pension consolidator in Europe. Formerly we were "just" – and I put that in inverted commas – a UK Heritage business. We now have both Heritage and capital light Open business in the UK and in Continental Europe, in Ireland and in Germany, and therefore we have the ability to grow organically and by doing further transactions.

Whilst Phoenix has evolved, cash is still king. We will manage our in-force business in both our Open and Heritage books to deliver cash generation in the short, medium and long term. Since achieving our FTSE listing in 2010, we have met or exceeded all of the targets we have put in the public domain. We take enormous pride as management in that track record, and we are intent upon its maintenance. It matters to us as management, and it matters to you as our investors.

This slide advertises £12bn of future cash generation. However large this number is, it is an underestimate as it does not recognise first the benefit of management actions post 2022. Second, it makes no allowance for the new business under the strategic partnership we have with Standard Life Aberdeen. And finally, it adds no value from future BPA and future transactions. We hope to do much better than the £12bn advertised.

As Andy explained, we are specialists at delivering value from the businesses we already have on our own books. We are happy to cover the hard yards, to sweat balance sheets, and are industry leaders at delivering capital efficiencies. Our approach to risk management, together with our well diversified product range, as advertised by Andy and by Susan, delivers a range of resilience that sets us apart, as characterised by Rakesh, from our peers, and our size delivers manufacturing economies of scale in an industry that rewards scale. These attributes underpin our ability to deliver real value from management actions that supplement the organic cash generation as our Heritage businesses unwind. We have a track record that speaks for itself.

The Standard Life acquisition brings to Phoenix a new capital light Open business. This has been described. For a business that has always been in run-off, growth across each of our open lines of business represents a fundamental strengthening of our model, extending our dividend paying capability without having to do yet another transaction. However, this is not an open business as you've seen it before, or indeed elsewhere, as Rakesh has ably explained with Susan. Under the strategic partnership with Standard Life, Phoenix continues to underwrite and administer, and Standard Life Aberdeen continues to own the platforms and takes responsibility for sales, distribution and marketing. This model strengthens our persistency across the open book, thereby protecting shareholder value, and does not cost us additional capital, and each partner does what it does best.

Having completed our first planning cycle as a Combined Group, we understand how cash will emerge in the future. The headline is that the combined Heritage business gives longer term sustainability to our cash generation. Based on the assumption that our Open business continues to grow at the levels we have experienced year to date in 2018, it means that our Open business has offset our Heritage business run-off over the same period. This is extraordinary and represents a fundamental change for Phoenix, and provides the opportunity for real sustainability in our cash generation.

We have always, as Simon has described, exercised strong discipline when spending shareholder money. We have a clear capital allocation framework and acquisition criteria. Capital will only be put to work where it yields positive returns, value accretion. Deals must keep the Group within the target ratio range for Fitch leverage, and enhance our dividend paying capabilities.

Simon has talked today about the value accretive nature of M&A deals that we have done to date. Our recent transactions show that we have bought wisely, and have then added value through delivering cost and capital synergies.

At every presentation I have asked Jim to quantify the size of his war chest. I am stealing his thunder today by confirming that the strength of our balance sheet gives us the capacity to fund up to £1bn of inorganic growth opportunities without returning to the equity markets. Of course that is dependent on the type of deal we look at. Therefore, in the past few years our equity investors have done the heavy lifting. Going forward, our own balance sheet will bear more of that burden.

The drivers of consolidation are increasing. We believe that firms will divest themselves of their capital heavy business to consolidators such as Phoenix. The market is in flux and we continue to see a wealth of opportunities. We have three main gating items that define our readiness for doing more deals: access to funding; the support of our regulator; and the management bandwidth available for doing transactions. The team, led by Simon, is eager to get the next transaction across the line. Funding is not an issue, and as such I am confident that we have the management bandwidth to do another deal today should the opportunity arise.

To conclude. The fundamentals of Phoenix is the story: cash; resilience; and growth. The acquisition of SLAL was transformational for the Group, and Phoenix is changed forever and for better. We have now reached a critical mass in terms of scale, product range and management strengths. Organic growth through our capital light open business will offset the run-off of our Heritage business, and bring more sustainability to our cash flows over the longer term. Our approach to risk management delivers a resilience to these cash flows that sets us apart from our peers in these turbulent times. Well executed M&A and BPA on top of these resilient foundations present real growth opportunities to Phoenix in the future.

So, what does Phoenix represent? Phoenix equals cash, resilience and growth.

Thank you very much indeed. We're going to stop the formal part of the presentation. I'm going to invite my colleagues to come up here, and then we're going to go into Q&A for about the next half hour. So what I'd like you do is wait for a microphone to arrive, then give us your name, and then tell me which institution you represent. I'll answer all the easy questions, and all the difficult questions will go to the team. Thank you.

QUESTION AND ANSWER SESSION

Question 1

Oliver Steel, Deutsche Bank

Three questions. The charts which are showing that the new business is offsetting the run-off of the old, I'm just trying to think through that myself, because if your £240bn is running off at 5% to 7% per annum, then that's going to be £12bn plus of outflows from the old business. But annualising the net inflows you've taken in this year, it's going to add up to, what, £4bn or so. I accept there's a difference there because you've also got BPA business coming in, but can you just talk through the margins on the new fee based business, and indeed the margins on the old business, so that we can work it through ourselves, because I can't make the maths add up at the moment?

Second question is your debt targets. You're continuing to use the Fitch ratio which doesn't include the RT1, as you admit. Does that mean that you just go on increasing the RT1 every time you want a few hundred extra million of capacity, because effectively about £700m of your billion of your capacity has effectively been generated by moving your target?

The then third question I've got is Diligenta. You're moving to one outsourcer. What are the savings that you'd expect to generate from that?

Clive Bannister

Thank you. Three questions – all chunky – Jim can you deal with the debt target first and then Rakesh and Susan perhaps you'd talk about growth, and then margin, Susan? And then finally with Andy would you take care of Diligenta? I'm just putting up the debt slide there Jim.

Jim McConville

Thank you, Oliver, for your questions. We have a Fitch target ratio for our leverage of between 25% and 30%, and the definition that Fitch use is debt over debt plus equity and the unallocated surplus, and an RT1 instrument for that purpose is counted as equity. So as Oliver says, if we continue to just issue RT1 instruments we would see improvements in our leverage position as a result of that.

In terms of the debt capacity available to us, at the present time Phoenix has roughly about £1bn of RT1 capacity, and it has £1.5bn of Tier 2 and Tier 3 capacity available to it. So debt capacity is not an issue. Clearly we will seek to derive an optimal debt funding mix as we go forward, and clearly Tier 3 and Tier 2 debt is going to be cheaper than Tier 1 debt. So I don't think it's correct to assume that we would just automatically go and use the RT1 instruments as a way of manipulating the leverage ratio. The more important thing is managing the cost of that debt in an efficient manner.

Clive Bannister

Rakesh do you want to go through the growth, I'm going back to Page 45?

Rakesh Thakrar

Thank you, Oliver. I think you made a comment about the Heritage business running off at 5% to 7%. I think that's absolutely right. And what we would expect is that if we continue with the volumes that we've experienced in 2018 in relation to the Open business, and that the margins we're writing continue at the same rate, and that over time we are maintaining our expense base so that the unit cost effectively is reducing, we will expect that the open business will offset the Heritage business run-off.

I'll briefly hand over to Susan on margins.

Susan McInnes

Yes Oliver, I think you were asking whether we expect the margins to continue on the open book. I think, as Rakesh says, we expect particularly workplace margins to continue. We do expect that position to improve if we reduce the cost base for the open book.

Andy Moss

Diligenta. I think this is a great example of where we actually looked at both policyholder and shareholder value. So I think you probably heard me talk over the last couple of reporting periods about our increased investment in digital, and looking to move more to the digital journey for our customers. That is similar, which improves the service to our customers, but as you say Oliver, also gives us a cost saving.

So we recognised that £100m of cost saving at the half year. That was reinvested partly in product charge capping, so again it shows a good example of adding both policyholder value and shareholder value.

What we expect in terms of going forward as we move more towards Diligenta, then the costs of our change activity will reduce being on one platform. But in terms of the actual per annum savings, then effectively we'd make that into our numbers today.

Clive Bannister

I hate being left out, so just on the debt I am going to say, and I want to thank our Treasury Team, two and a half years' ago our average debt was four and a bit years, and it's now 6.9 years, so we've got two and a half years' greater maturity and we paid another 30 basis points. That's the trade-off that you get for length, but that's the way to finance long term business. So I think the debt management has been astute. We have no senior debt outstanding. When we first met eight years' ago it was all senior debt and no subordinated debt. A transformation.

Question 2

Greig Paterson, KBW

I'm going to stick in four quick questions quickly. SIPP regulatory risk, there's a lot of noise we're seeing in the press. I'm wondering if you want to talk about your exposure to that?

Clive Bannister

Sorry, it was very indistinct, I could not hear.

Greig Paterson

Sorry. SIPP regulatory risk, there's a lot of noise around SIPP and you've bought it and got a big exposure from Standard Life. Second thing is, I wonder if you can talk about CP13/18 and your exposure to that?

Third thing is in terms of debt constraints, I wonder if you can talk about the fixed charge cover, because that obviously restricted Tier 1 costs coming to that?

And the fourth thing is, just in terms of the opportunity for large M&A, outside the large UK listed books and the big mutual funds, could you talk if there's a capacity outside that to do deals?

Clive Bannister

So Simon would you take the first question? We'll answer them in sequence but CP13/18 its impact and where you see it going in the context of the size of ERM. And then Jim you'll deal with the debt if you'd be so kind. I'll deal with the other two issues.

Simon True

We did announce what our exposure was to CP13/18 as it was drafted in July, so in our results we said what we expected that hit to be on our back book, it was the order of £200m.

Since then the issue of that consultation paper, the PRA said it's not going to be enacted at the year-end this year. So we don't know when it's going to be enacted and in what form. We will continue to monitor it.

In terms of the attractiveness of equities/mortgages, they remain a very attractive asset class for us. They are a very good match for our annuity liabilities, and the spread on them is attractive to other alternative assets, obviously allowing for the risk capital that we hold. One thing just to bear in mind is that we have a relatively seasoned book, because we started our acquisitions on back books, so we actually have a relatively high average age, around 79 years old, and our loan to value ratio is around 33%.

So we're very comfortable with the quality of the book. We understand the potential impact of CP13/18, and of course it may be a more benign outcome, we will have to wait and see what the PRA say.

Jim McConville

Our fixed charge coverage in 2018 is four times, and it will improve as we go forward in future years given the projected cash generation.

Clive Bannister

Then there were two other questions. One was to do with M&A so I'll do that, that's the easy one, and I'll come back to the first of the four questions asked. The question was where's the M&A opportunities in traditional, closed or Heritage legacy business, and in the UK where might it exist outside the publicly quoted entities. So I can start with the big picture.

The big picture is a market that we define across Europe, which is in our case the UK, Ireland and Germany, as about £540bn. To that we would break it down with over £350/360bn being in the UK, £160bn being in Germany, so about half the size of the UK, and Ireland being one-eighth the size of Germany at about £20bn. So £20bn, £160bn, and around £340/360bn in the UK.

These markets are all at different levels of maturity, so they are apples and oranges, but what it does advertise is that across Continental Europe, including the UK, there is this continued bifurcation where the cost to capital supporting Heritage books, trapped capital, expensive capital, supporting stranded costs, and also suffering from increased regulatory oversight, is being repositioned by players across Europe.

Our priority remains the UK. That is where we have the most obvious scale and relevant transferable skill sets, and that is where we intend to focus. But as Susan said, our new businesses in Ireland and Germany bring with them strategic optionality to look at business prospects, consolidation prospects, in those territories.

So, the nuance of the question is well, what happens outside of that £340bn outside the quoted sector? We never speak about specific market opportunities, but I think we have seen a sea change this calendar year. We'd anticipated it three years ago, where publicly quoted entities, be it the Pru, Standard Life, or indeed, Swiss Re, have declared that they wish to restructure their businesses. So I don't think it's a fair question to say exclude the publicly quoted entities because we've seen them, if you want to take quota, with the de-merger and the restructuring that took place in Old Mutual.

So we look at the UK as a total market of around £340bn to £360bn, we're intrigued about the product spread, we can deal with any and all of those products, and it's the relevance of our platform which makes us a compelling counterparty.

So, can I go back? It was an excellent question, if I can say that. The first one, if I understood it is, you said there are increasing regulatory risks with the separation from…

Greig Paterson

SIPP product.

Clive Bannister

Ah, SIPP product. Ah fine, I thought it was separation from Standard Life. Forgive my hearing. And I was going, gosh!

Susan McInnes

Can I do that?

Clive Bannister

Ah, please. That's why I left it till last. That's another question. Susan.

Susan McInnes

Sorry for taking so long to understand your question there, sorry. So I think in terms of the SIPP market you're referring to, the influx in the SIPP market from defined benefit to defined contribution schemes, particularly into SIPP, I think there's a few things we'd say there. I think the first is that Phoenix's role in that, as we've described in the partnership arrangement, is administration. We're not involved in the sales process, so as part of the CSP it's Standard Life Aberdeen who are involved in sales. We do administration, and all of those sales that are coming to us are coming as advised sales through the independent advisers. So we think we're protected from that risk.

<u>Question 3</u>

Andrew Crean, Autonomous

Can I ask also three questions? Slide 12, I think you give the assets at £280bn. I was just wondering, could you split the £12bn of cash generation between those, because there's clearly very different margins? I was just saying on slide 12 you've got £240bn of assets there. Could you split the £12bn of cash flow between those three buckets, Europe, Open and Closed?

And following along the same line, on the new business, the Workplace, the Retail and the Wrap, could you give us the revenue margins in basis points that you actually receive, having paid away the asset margin to Standard Life?

And then thirdly, could you talk a little bit about size? I mean I know you throw around these very large figures about the potential market which you can consolidate, but your size in the UK means that there's got to be certain deals which simply are not worth getting out of bed

for and troubling the PRA with. So could you give us a sense of how many targets are actually realistically in your lens?

Clive Bannister

Certainly. Okay, so a three part question. I'm going to deal with the second one. We don't disclose our margins. It's competitively advantageous if we describe to people our slices of the pie, and so I mean, I take words from your mouth, Susan, but I think that's the answer to that question.

Susan McInnes

It is, yes.

Andrew Crean

Can we get some sense? Because I mean, Oliver was going for the same thing, if the margins on the new business are substantially different to the margins on the old then none of that is really coming out here, so if you could…

Clive Bannister

I thought there was a very clear statement, Andrew, by Rakesh, that said there was no net new capital charge that we had accredited and our Solvency II funds had gone up by £200m, if I heard that correctly.

Rakesh Thakrar

That's right, yes.

Clive Bannister

Okay, so this is net accreted to our business. And that's one part of the maths. I get the desire for understanding margin back into an IFRS world, but we're talking about a cash world. The second part is that it brings additional volume so that we put that through our manufacturing machine so that Andy has more buying power with our outsourcers. I don't know if you want to say anything about how we'll be describing the maths in March?

Rakesh Thakrar

On the £12bn, so we'll be giving further guidance on the cash generation in March in any case, but just so everyone's aware, so the £12bn, as most people know, £6.5bn of that was the old Phoenix entity and £5.5bn was the additional from the acquisition of Standard Life. And all I'd say in terms of Europe, that would probably be proportionate to its size in terms of its contribution to the £5.5bn. And just to reiterate that there is no new business within that £12bn, or no additional BPAs in that £12bn figure.

Clive Bannister

The final question was, was there a size of transaction that we wouldn't bother with. I think we said bother our regulator, because we had other fish to fry. There's only a certain number of deals that one can do. We did two transactions in '16 and then one transaction in this

year. So I think there's a frequency rather than a size. We've always said that size matters far less than the quality of the transaction, which is approached from a cash lens, and to what degree can we make it accretive. And therefore I think we will look across the whole spectrum in the UK by product and by size, but clearly, to move our needle now is, as Rakesh said, and Simon inferred and implied, we have to have deals which are of greater stature and size.

<u>Question 4</u>

Ashik Musaddi, JP Morgan

Just a few questions. First of all, on the capital synergies on Standard Life. I mean you have already done £400m out of £450m, but your Internal Model merger has yet to be done, Part VII transfer has yet to be done. I mean, so far you have just done hedging basically, and so can we get some sense about is like £450m just too low? Or I mean, I'm sure you won't give the number but any thoughts on the magnitude of how much you can do better than that one, the 450 versus 400 already done. So that's the first one.

The second one is can we just get some colour about your capital? I mean, clearly you're saying £1bn capacity on the funding structure; you're at 164% Solvency II ratio. Your target range is 140% to 180%. Your shares are pretty low, driven by Brexit I guess, so shall we think about a buyback? Is it the right time? Or do you think M&A opportunities will by far overweigh any concept of buyback? Any thoughts on that would be great.

And lastly, credit spread sensitivity. I mean, you have shown some sensitivity to credit threat. Can you just elaborate on that? What does that 150 basis point mean? I mean, is it on a step up by rating and then there is a note, about 10% default as well? Can you just give more elaboration on that? What does that sensitivity actually mean? Thank you.

Clive Bannister

Ashik, thank you very much indeed. I think, Jim, you've got the first two parts there, one of which is, and I'll put up your slide 14, have you under-egged it on capital synergies and what is to be expected? And then are we going to do a buyback? And then, Rakesh, if you'd be kind enough to talk about credit spreads.

Jim McConville

Okay, so Ashik, on hedging, the time we announced the Standard Life deal we said capital synergies would amount to £440m. That comprised of hedging and strategic asset allocation initiatives, and that was roughly split two thirds, one third. We have completed the hedging work on both equity and currency hedges that we've put in place, and that has delivered £400m of benefit, as I described earlier, so ahead of the initial expectations that we had.

So I did indicate that we would be looking at this target again, and I think you're correct to surmise that it will go up, because clearly we expect to do more in terms of the strategic asset allocation and other initiatives which we will report on in March.

In terms of the Internal Model harmonisation itself we have not assumed any positive or negative benefit from that harmonisation. Clearly that's a process we'll have to go through quite carefully with the PRA, and it would be wrong at this stage to assume either a benefit or an additional capital requirement for that.

I think your second question was related to share buybacks. As you would expect that is a subject that is considered from time to time by the management and the board of the Group, and the judgment of us at this stage is that there are better opportunities in terms of our growth from M&A, from BPA and elsewhere to deploy our capital than a buyback at the present time.

Clive Bannister

Do you want to talk just through the resilience and credit spreads?

Rakesh Thakrar

Yes, so I think, Ashik, you asked about the credit spread stress in a bit more detail. So I think what we've described here is an average of 150 basis points stress across all the different ratings. There is a step up, so the triple As obviously, the tripe As, the double As will be lower, but the triple Bs, double Bs will be a lot higher. Overall it's an average of 150 basis points. I think more importantly the fact that what's applied is a consistent 10% on defaults across the rating.

Ashik Musaddi

Sorry, what does that mean, 10% default? I mean, on your overall credit book you're expecting a 10% default?

Rakesh Thakrar

Assumed defaults of 10%, that's right.

Ashik Musaddi

10% increase in default or 10%...?

Rakesh Thakrar

That's 10% assumed increase in default, so not actual defaults, but assumed increase in defaults.

Ashik Musaddi

Okay, thank you.

Clive Bannister

A question here. I know we've been prejudiced towards the front row, we will work round.

<u>Question 5</u>

Dominic O'Mahony, Exane BNP Paribas

Good morning, Dominic O'Mahony, Exane BNP Paribas. Two questions from me if that's all right. You've told us lots of exciting things about the new business prospects, but you've also

been very careful to remind us that the core is UK closed books. I'm just thinking about the competitive dynamic for those closed books. On the one hand, if you think about the global consolidator landscape, there are a lot of new names or ambitious names that seem to have emerged over the last few years. Maybe most of that is focused on other markets, but there certainly seems to be capacity for chasing some of those opportunities, and at the same time you'd expect that some of the low hanging fruit has been pulled out since Solvency II.

So just thinking about the economics of future UK back book transactions, how confident are you that you can deliver those as attractively as you have done in the three previous transactions post Solvency II?

The second question is on Heritage unit linked. There have been press reports that the regulator's looking at exit fees. You've clearly got the pensions dashboard coming through. The value in that business relies on people sticking around and I wonder if that creates a risk to lapse. What confidence do you have that the value for money for example on the products means that actually people will stick around, despite some of those headwinds? Thank you.

Clive Bannister

Okay, so there were two questions there. Simon, would you take the first, which I think breaks into two parts, one of which is our confidence about flow and margin in the UK and the legacy space. And you mentioned some maths, but would you also talk about the BPA and the degree of competition, because we are a biped in that respect? And then perhaps, Susan, you would talk about persistency in the context of our unit linked business today and tomorrow?

Simon True

Okay, well I'll kick off on the initial question on competition for closed books. Yes, I think there is increased competition, a lot of people have seen the returns that might be available and feel that that's something they want to play in. Every time we go into an auction, and just bear in mind that in '16 we bought AXA and we bought Abbey Life in auction, so we were in competitive process there. You know, you can sometimes see upwards of 20 people taking the initial book. People want to have a look, they're very nosy.

What differentiates people in whether they can actually execute a course is ability to price competitively. We think that we deliver compelling pricing to people that want to get out and allow them to deploy their capital elsewhere. And to be compelling in our pricing we have to make assumptions about what we will do with the book. And as we explained earlier on, on the AXA transaction, we had in line a whole range of management actions which would deliver shareholder value to us, but also deliver a compelling proposition to the vendor, and I think that's quite unique.

On top of that you have high barriers to entry, so people will think that they can come in and do this, but to be an established base, to have a robust outsourcing option that we have, to be able to have engaged over a period of years with the PRA and FCA, to demonstrably treat policyholders well, to actually understand the regulator's concerns, and to have a PRA improved Internal Model are all very, very key to us in debt. And all of that said, we will lose transactions.

People will pay more, and we have walked away from a number of transactions in the last three years where someone else with a different imperative, a different strategic logic,

perhaps a different capital treatment, has been able to pay more than us, in which case we walk away from those transactions because you have seen to debt we have a dynamic capital allocation model and our Board are extremely focused on loss generating, value accretive, M&A, so we will walk away.

And that philosophy extends to the BPA market where it's more established, you have eight players in there, and at any point in time some will be more or less competitive than others. And what we do, and we're very patient in investing across the cycle, we wait until there is a sweet spot for us in terms of a particular transaction, it might have additional complexity, we might have sourced some particular assets that make us able to price it competitively and attractively, and we will just be disciplined and patient about how we deploy capital, whether that's M&A or BPA.

Clive Bannister

And you looked at 28 deals and you did three in the BPA space.

Simon True

We did. Now, at the end of the year Clive is going to pull me up and say it's 25 failures. So I have witnesses here, but it is all about making sure that you maintain that discipline and be able to say we can't get there and if there's a better buyer then good luck to them.

Clive Bannister

Susan, so we've been asked about persistency. One of where we are today and how we make sure it stays rock solid. And secondly, looking to the future. And it's a bit of conjecture there about where we may travel with our regulator.

Susan McInnes

Sure. So you make some good points about the regulator's interest in value for money and charges on legacy back books. I think a couple of stats for you. 85% of our legacy back book have no exit charges, and in terms of the book overall, about 80% of it have a charge of 1% or less. And I think Andy also talked to you in terms of Phoenix Heritage and about just how important customer outcomes are to us. And when we talked about the value generated from the move to a single outsourcer, much of that value was given to improving customer charges, hence the percentage that are 1% or less. So we do take that value for money point really seriously.

You also made a good point about the threat of the pensions dashboard. I think we have been a strong supporter of the pensions dashboard as a closed fund consolidator, and that's because we genuinely believe that giving customers all of the information on all of their pension pots in one place actually helps them leave their pot with their existing provider, it's not necessarily a threat that they'll consolidate into the one place. And we've been a very strong supporter from the beginning in that initiative.

<u>Question 6</u>

Gordon Aitkin, RBC

Three questions please. And I first can't let you go out of here without talking about Brexit. If we do have a no deal what's your expectations for the growth that you're looking at bulks, pensions, and what about future M&A?

The second point, and related, have any of the European owners of UK life books, and you say that's almost half of the £380bn which is out there, indicated that Brexit is potentially a line in the sand for them, i.e. do you expect more back books to be put on a block post March next year?

And finally on bulks, I mean how can you compete with the likes of Legals and Aviva without a very large illiquid asset regeneration engine? Thanks.

Clive Bannister

Gordon, thank you. Three good questions. I think it's appendix one if my memory serves me correctly. I'm just getting to it. So let's get the facts for our business in terms of Brexit, it wouldn't be a normal meeting unless the B word is used. So, our business is 95% UK based, a full 90% and then there's a 5% which is an offshore business out of Dublin, and then there's only 5% which is continental assets, that's based in Germany and the Republic of Ireland.

We are completely prepared, we took over the preparation which was done by Standard Life which, as you would imagine is good, so we're prepared for a no deal, a hard Brexit. How have we prepared for that? We're putting our international assets under our Irish business and we're doing a Part VII. So we are as protected as one can be, it's a small slice of our business and you can see from our credit exposures etc. we're comfortable and we've done the thinking.

So I think that answers the first question. The second question was have we heard from anyone? So if we think of the UK business, I said about £340bn, £360bn of closed life Heritage business, half of that is in the hands of existing UK insurance company, about 10% and 5% is in the hands of banks and the remaining 25%, 35% is in the hands of foreign insurers.

We have yet to hear from vendors or people who are thinking about things that it is Brexit that is the driver. The systemic drivers for why vendors will want to come and have a conversation with us or our competitors are, as I said a few minutes ago, it is the cost of tracked capital. Our friends in AXA, as Simon said, had a better use of that money where capital was facing this way and they wanted to take their dollars or in this case sterling, and use it in their GI business in the UK and then of course they're more a substantial international acquisition.

So it's trapped capital. Stranded costs are an enormous issue. People have books which are running off and they have old legacy systems which are enormously non-economic, going back to Andy and Susan's point about value for money, very hard to give value for money if the cost per policy of administration becomes higher as that runs off. It's a sort of manufacturing tontine effect, not just the economic tontine effect.

And then finally, there is increased regulatory scrutiny. Why would you carry on holding on to a business that could expose you to regulatory risk when you get no more economic real advantage. So to answer the second question, no we're not hearing Brexit being a casus

belli, or a cause to change and sell an asset; we're hearing the big three, as I've just described them.

Would you mind describing how we can be effective against the players in the bulk markets, Simon?

Simon True

Yes, it's a great question. We are coming from a long way back. Existing players like Legal & General, Rothesay, PIC, Aviva, have been in this market for longer than us, and they have been sourcing assets for longer than us. But we've invested quite heavily in developing our capabilities in that area. As I showed earlier on, we've generated £1.2bn of illiquid assets to date. And in exactly the same way as M&A and BPA more generally, it is all about the value creation, it's not a vanity project. The volume, it doesn't matter to us, it's the spread and the value creation. The risk adjusted spread is what we're absolutely focused on.

And you're not going to get that off the shelf, so we are having to build our relationship up, direct relationships, trying to extend our capability. We also have partnerships with an equity release mortgage flow, so we write healthy volumes of that per annum. And it's something that we spend a lot of time thinking about in terms of how can we do this better and how do we allocate it? Because it's very easy for us to take our eye off the ball, but our cash generation on our back book is also supported by generating appropriate asset strategy and making sure that we get the assets that generate the cap that support the cash generation on the Heritage and the open books as well.

So we're very disciplined and we try and generate value. We've generated £100m of Solvency II benefit this year and we're growing and we will continue to grow and we feel that we can be competitive and that's evidenced by the fact we have consummated three transactions this year.

Question 7

Stephen Haywood, HSBC

Thank you I just had one question for you. Now that your new business inflows and your BPAs, they are growing or at least stabilising your total AUM, are you considering changing the dividend policy from stable to something else? Thank you.

Clive Bannister

That's a nice, very clean question. A very short answer. No. Stable and sustainable. That is what you would expect of our business. We have raised our dividend up three times in three years upon doing transactions, and that is the best advert for this machine working. We thank our shareholders and reward them for the capital they put up to support our business.

The other point is right now we want to show that we can deploy, as Jim has said clearly, the billion pounds of financial resources rather than going back to the equity markets in deals. Of course it depends on the type of deal going forward. Thank you.

Question 8

Marcus Barnard, Numis

Thank you. Marcus Barnard from Numis. Just the three figures on page 39 that you've given us about the bulk annuity transactions, £100m of Day 1 capital and £300m of long term cash generation. If I look at those as an eighth and three eighths, are those the sort of ratios you would think are typical going forward for your bulk annuities? In particular, does that Day 1 capital allocation have any benefit from reinsurance of mortality? Can you say whether that's included or not? And also the £300m cash generation, I mean presumably you're expecting some sort of decent spread from illiquid assets included within that. I just wonder if you could comment on some of the assumptions behind those numbers. Thank you.

Clive Bannister

So, Simon, I think that's yours. I've put the slide up. I think you're asking about balance, you're being asked about reinsurance of longevity risk and where you see margins and so on.

Simon True

So in terms of the initial question about are we going to see these ratios going forwards, I'd like to see them better, I'd like to see less capital and more cash. We will continue to work on that. It's not a bad guide going forwards I think. It is related to your second question which is on the reinsurance of longevity. We are very prudent in our management of longevity. The longevity is one of our biggest risks in terms of our solvency capital requirements, and therefore on bulk purchase annuities we are reinsuring between 90% and 100% of the longevity risk. So this is very much an asset situation than obviously an administrative capability issue.

So what does the £300m sort of represent? Well, you're putting up £100m of risk capital that on your best estimate you're not going to require, and then the remainder is margins within the best estimate assumptions, and also the unwind effectively of the additional return that we're going to receive on the full £900m of allocated that we're not giving back effectively in the pricing. So it's a combination of all those elements and that's how that unwinds over time. And as you can imagine, the £100m capital requirements fully reflects our capital management policy, and it allows for effectively a transition to our strategic asset allocation, which we can't achieve on day one, as we typically receive just cash and gilts from the trustees.

<u>Question 9</u>

Alan Devlin, Barclays

A couple of questions. First of all on the M&A, you mentioned you've got your billion pounds of fire power and the shareholders have done the heavy lifting so far and now the balance you can do some of the heavy lifting. Should we assume that that's kind of the sweet spot for the next M&A deal up to a billion pounds or you can fund it yourselves or are you indifferent and it depends on the size of the deal and you'll come to the market if the deal's attractive and you have to?

And the second one on BPAs given that you've got about a £1.0bn of fire power what drives the appetite for the BPA volumes at £800m which only requires £1m of capital; is that I think into Gordon's question your ability to source direct investments; or, what do you see the size of the opportunity or what else? Thanks.

Clive Bannister

Alan, thank you very much indeed. So the first question is does that £1bn of company resources, Group resources indicate the target size for the potential next deal. So completely conceptual and the answer is no. I answered Andrew, size is not what drives the transaction, it is the lens of what cash can be generated; it's the quality of the value accretion and our opportunity to do a transaction. So there isn't a sweet spot size, the sweet spot is by what we can do with a potential transaction.

The second thing on BPA I think Simon has said, we are selective, we are proportionate and every transaction has to meet our acquisition criteria and we've gone through that. I don't think, and Simon you will correct me if there is anything you wish to change on that, and we're not about to go out and spend £1bn on BPA which is why we talked about the proportionate nature of this. Simon?

Simon True

The only thing I'd add, Clive, is that our preference is probably to invest across the cycle. If we had a £1bn to spend and you had the same BPAs you wouldn't necessarily do it all in one year. Quite apart from the operational bandwidth of my colleagues you'd probably want to invest across the cycle in the same way that our approach to sourcing illiquids will look to source those over the cycle.

Question 10

Simon Gergel, Allianz Global Investors

I've got two questions please. Firstly, you talked about balancing the run-off in the Heritage book with the growth in the Open side, is there anything exceptional about the rate of growth this year in the Open book either in terms of the margins and profitability of that growth, or in terms of the quantum? Or do you think it's reasonable to expect on the medium term you can continue to grow at that rate going forwards on the Open book?

And secondly, on the £3.5bn that you've got in alternative assets backing your BPA book how much of that has been sourced through the Standard Life Aberdeen relationship? And going forwards how important is that relationship to the sourcing of new assets?

Clive Bannister

Fine. Two part question. Susan, would you deal with the first one? It is early days. I have to pinch myself that we've actually been the owner of this business and I think we're on day 87. So let's put that in context but the question is about the flows and the margins going forward in this Open business.

Susan McInnes

So I think it's quite an easy answer. I think there's been nothing exceptional in 2018 to date in terms of either size or margin. And our expectation is that that should continue into the future.

Clive Bannister

And the second part of the question was about the source of alternates and the role that SLI have paid in that?

Simon True

So far we've sourced most of our illiquid assets ourselves, the £3.5bn. But that is because we weren't in a stronger strategic partnership. We are looking at ways to accelerate our sourcing, get access to better returns through our strategic partner. We also have two other strategic partners which we currently work with on commercial real estate debt and infrastructure debt. We will just look to strengthen our relationship going forwards and see if we can work together more efficiently going forward. As Clive says it's very early days.

Clive Bannister

And our source of ERM.

Simon True

ERM we've sourced by three back book transactions and we have a flow where we financed two other providers of equities mortgages; this provides something in the order of £300m per annum of equities mortgages. But we are the funder not the direct seller of the business.

<u>Question 11</u>

Martin Silverman, Private Investor

You've made clear how important and how interesting the Open book side of the business is to you and this is obviously relatively new business to you. I understand that SLA represents a very important channel for gauging this business but I seem to have understood that it's not the only channel. And given the responsibilities that have to be taken on board with the development of the business, given how important it is to you, could you just explain please who is going to be responsible for that part which is not to be channelled through SLA?

Clive Bannister

It's a very thoughtful question, Martin, thank you. This is an evolution of our business, it's not new we always had some small amounts of open business, I'm thinking about Sun Life, I'm looking at Andy there. It is an intelligent deployment. It's a complementary business and it's where we can intelligently deploy pre-existing skills. So we see the Open business as a short cut to getting more volume which we can then apply our management tools, management actions to a bigger in-force book. And our friends, the deal with Standard Life brought £91bn worth of in-force business which we can now practise on. It also brings additional volume to our manufacturing business. It elongates or extends our dividend payment capability and is clearly accretive.

So Open done the way that we do it which is leaving sales risks to somebody else, the platform providers, in this case Standard Life is an intelligent use of a separation of skills. And as I said we have not deployed any capital against that new business. So that's why we do it.

And then the second part of your question is who's going to do it going forward? And so Susan is the chief executive looking after our Open business working in tandem with Andy

who manages the Heritage business. So what I'm saying is we're almost indifferent to the source of the business. The enormous Heritage business, like a reservoir which we're harvesting – apology for the mixing of metaphors – but we're also getting this new source of business and we apply the same management tools to the Heritage, the in-force business, on both.

And if part of your question is what may happen in the future, because we're very clear about how we manage the business today, thus the team standing or sitting here this morning, Open with Susan and Heritage with Andy, and going forward, that is in the future, we would welcome the opportunity to have more Open business but only in the context of it supporting our core business which is Heritage. Thank you.

I think we're moving to the last two questions.

Question 12

Corinne Cunningham, Autonomous

I know you've said you've got plenty of debt capacity but of the £1bn resources that are in your war chest currently how do you perceive that as being split between surplus equity and available debt?

And then the second question is a broader one: you have a lot of debt outstanding now, your spreads are actually quite wide, would you consider getting a second credit rating to improve transparency and illumination perhaps on the debt side of your business?

Clive Bannister

Jim, I think both of those questions for you: one about what of the composition of the £1bn of Group resources. And the second one is would we consider doing other than Fitch, adding to Fitch in terms of a credit rating?

Jim McConville

So the £1bn number that is referred to assumes that we take our leverage up to the 30% top of the range that we've quoted. And it also assumes we make some use of our existing cash resources as we have some £400m of existing cash resources.

In terms of the ratings we have had the Fitch rating as a single rating for a number of years now. We do consider, from time to time, whether we should expand that to a second or a third rating but our judgement remains, at this time, that a single rating is sufficient.

Question 13

Blair Stewart, BAML

Thanks very much for a very clear set of presentations. Maybe just have another go at the question that's been asked earlier regarding the slide on the run-off of the Heritage versus the impact of the Open book in cash terms. I think you've indicated that in AUM terms you lose something between £12bn and £15bn of AUM a year. I don't think the level of inflows is as high as that, unless I'm mistaken. I think at industry level we all appreciate that the margins of new business today are lower than there were in the past. So maybe you can just

help us square it, what are we missing there, what's the missing piece of the jigsaw if possible?

And just maybe linked to that could you comment on the £300m of cash from the Annuity business in terms of how quickly that's recognised? Thank you.

Clive Bannister

Two questions there. Rakesh, I think I'm going to look to you. One goes back to the question about the nature of the flows and the margins accordingly. And then if you want to comment also on the annuities. I don't know whether that's BPAs or vesting but anyway when that converts into value.

Rakesh Thakrar

Okay. So taking the first question about the run-off of the Heritage so just a reminder what we expect. So as the Heritage books runs off and as we start to write this Open book of business we would see an offset coming from that. I think what's important to remember you know that's based on the volumes that we maintain, it's also based on the margins that we currently write, that's maintained. I think probably the more important of all of that is also the fact that we ensure that our unit cost goes down; so the incremental margin for every additional piece of new business as written gets higher and higher. And of course this will also have a cumulative effect.

Now also Susan mentioned the fact that in relation to workplace we get a significant amount of new members joining every year and we already have that capability already in place. So that will just also grow as well. So a combination of all those items will ensure that you get the offset.

And second question if it was related to BPAs I think Simon's going to take that one.

Simon True

So the BPA cash will emerge over a very long period because effectively we fund to the highest capital requirement. As we deliver management action, as Andy delivers management actions on the Heritage back book because effectively it will go straight into the Heritage back book, that will effectively become part of the cash generation. So you expect to see – it can be quite a strange profile you can end up with capital going up on day one and then coming down as we move into our strategic asset allocation. So that could happen relatively quickly, you can get a release over six months. And the residual may come out over a much longer period.

Clive Bannister

Thank you very much. Susan, did you say it was 280,000 new clients?

Susan McInnes

I did yes. In workplace? Yes.

Concluding comments: Clive Bannister

So we're going to end on time. I move to close this meeting. But first of all I start with some thank yous. I want to thank the Chairman for being here. His first day out. We're immensely proud to have you on board. Nicholas, thank you for being here.

Claire Hawkins, where's Claire? Can you stand up, Claire? Claire is in charge of investor relations. All of the difficult questions have to go in her questions. However inadequate we've been on the panel, she knows all the truth. So, Claire, thank you for organising today, it really matters to us.

I want to thank my colleagues. As I said right at the outset of my speech, what an extraordinary team and the success that we have has been because we play team and we make sure that that gets delivered.

So, we announced strong results today, or strong update. We wouldn't use that word, that adjective, strong, unless we believed in it and we think we have demonstrated clearly today and to the markets that the three attributes of this firm are cash, resilience and growth.

Thank you very much indeed. I think there's some food right next door. Thank you.