PHOENIX GROUP

Phoenix Group plc 2011 Half Year Results

Thursday 25th August 2011

Clive Bannister: Chief Executive

Good morning, ladies and gentlemen and welcome to the Phoenix Group Interim Results presentation. Today we report strong progress on a number of fronts. Phoenix is well advanced on its journey to build an extraordinary business. It's a business that rests on the platform of financial stability that has a unique infrastructure and a set of distinctive capabilities. My colleagues and I are completely focused on bringing these to bear in the way in which we manage our assets and the way in which we manage risk in order to deliver value, both to shareholders and policyholders, particularly in today's volatile markets.

I'm joined on the podium by Jonathan Yates, our Group Finance Director, who will run through the maths and address risk management and Phoenix's balance sheet resilience to the volatile conditions in which we find ourselves. In addition we are joined by Mike Merrick and Chris Samuel, the CEOs of Phoenix Life and IGNIS respectively. They are here to answer questions about their businesses. Our Chairman, Ron Sandler, is in the audience, along with many senior members of the executive team and we are all at your disposal to answer questions at the end.

The Phoenix Group is on a journey. Three years ago the Group was in private equity ownership and undertaking the acquisition of Resolution mark one. Two years ago we undertook a restructuring and recapitalisation of the business and last year we moved forward with the premium listing, strong cash generation, fund restructuring, the integration of Resolution Asset Management and Axial into the creation of IGNIS. And this year we've started and we set clear and challenging financial targets. They were to strengthen our cash flow, to deliver enhancements to our MCEV, to reduce our gearing towards a permanently lower core level for the longer term and we have made good progress against all of these targets in the first half of 2011.

We have also continued to deliver operational improvements and we are proposing an interim dividend of 21 pence per share as previously indicated. The journey has been successful in the first half and we are confident that we can continue this success for the remainder of 2011.

Cash is the single most important measure for our business and the most relevant metric for our investors. We set a target range of £750 million to £850 million for the full year of 2011 and I am delighted to report that we have delivered £496 million in the first half. This includes a very substantial £197 million of cash acceleration from management actions, of which £170 million was for restructuring activities. We remain confident of delivering cash for the full year within the £750 million and £850 million target range. Current market volatility means that I'm not able to make a prediction as to where within that range we will fall, but I expect to be able to provide more detailed guidance at the time of our third quarter interim management statement on 8th November, later this year. Jonathan will also provide you with more colour as to how we have managed to structure our affairs so as to be able to remain as confident as we are. This is a testament to the work of many people in the Group who

ensure that we have clearly defined risk appetites and the business is operated within those parameters.

MCEV is the second key metric against which we measure our performance. We set an objective for the year which was to deliver £100 million of MCEV enhancing actions, and again I'm happy to report that we have delivered a full £69 million in the first half of 2011, £30 million of which comes from fund restructuring and £39 million from operational management actions. Our MCEV stands now at over £2.2 billion and this means that on a per share basis that it has risen from £12.27 per share at the end of December to £12.77 at the end of June. And this excludes the value of IGNIS future profits which is a VIF figure which is a further £2.35 per share, giving a total of just over £15 per share. Again, without making any precise predictions we are confident that we will hit the full year target of £100 million in the full year.

Turning to gearing, we set a 2011 target which was to bring gearing down below 50%. I'm pleased again to be able to report that we have already achieved that target and that our gearing as of 30th June stood at 48%. This is down a full ten percentage points since 2009 and I would hope that the level of our gearing will continue to fall over the course of this year.

As you will be well aware the Group has just over two and a half billion pounds of bank debt in two different silos and one of our key objectives is to restructure our debt so as to extend the maturity profile and to improve the flexibility of our covenants. Discussions with our banks continue in a very cordial spirit. But as I have said before we will only enter into any new arrangements on terms that are attractive to all of our stakeholders. In the meantime we reiterate that Phoenix remains entirely comfortable regarding its ability to service all of its debts. We will of course update the markets when there is any new news to announce.

The Phoenix Group is a business and not just a balance sheet and both of our operating businesses, Phoenix Life and IGNIS, have made good progress in the first half. This includes the completed fund merger of Phoenix and London Assurance and Phoenix Life, and this is of course the real bread and butter of our business, allowing us to reduce risk, add value and release cash. We also completed the restructuring of London Life and we were able to enhance the value of the distributable estate to our customers by £100 million, and this is thanks to the increased standardisation of our approach to with-profits management across a number of funds. This is what we call the Phoenix Way.

In the first six months of 2011 we wrote £375 million of new annuities on behalf of our vesting pensions customers, making us one of the UK's largest providers. We are writing this business, these new annuities, into our non-profit funds which improves our risk management by removing long tail longevity risk from the with-profit funds and it is a business that is highly profitable for our shareholders. In addition, Mike and his team have now converted over two million in force policies onto a modern policy administration platform and this is key to our strategy for cost control as closed life funds contract over time.

We have of course continued to invest in IGNIS, both in recruiting investment and operational talent and investing in the infrastructure. We are confident that IGNIS will be able to consistently add value for both policyholders, shareholders and of course external clients and investors. IGNIS was also able to gather £800 million of net new money in the first half and IGNIS launched two new funds in the period playing to the established strengths that already exist in the business and I would expect Chris and his team to have more launches over time. I'm happy that we have made strong progress towards the delivery of our financial targets and that there is continued development of our business platforms in such a period of turbulence.

Now I'd like to hand over to Jonathan to take you through the financial details behind those headlines. Jonathan.

Jonathan Yates: Chief Finance Director

Well, thank you, Clive and good morning. As Clive has highlighted these represent a solid set of financial results for the period. In particular, cash generation is well on the way towards our full year target at nearly £500 million. Group operating profit was in line with expectations at £136 million and MCEV grew by almost £100 million, including £69 million of management actions against our full year target for management actions of £100 million.

This delivered a very satisfactory annualised return on MCEV of 12% when one considers that short term risk free rates are now below 1%. It's also interesting to compare this return with our current share price which is around 40% of MCEV, ignoring IGNIS future profits. IGD Surplus is up from the full year 2010 and the excess over our capital policy grew to £300 million. Gearing fell to below 50% on the back of organic cash generation and the strong growth in MCEV.

As we've said many times before, Phoenix is characterised by the strength and reliability of its cash flow generation. We started the year with £486 million in the holding companies and this grew over the first six months of the year by £234 million to £720 million. This represents a very significant liquidity buffer given current market conditions which will enable us to carry on meeting our obligations into the medium term, in particular to keep on servicing bank debt and paying dividends.

The key drivers of this growth were strong cash flow from the life companies of almost £500 million and one off expenses were reduced significantly as IT and business transformation projects are now nearing completion. We also made a voluntary repayment of bank debt principal of £21 million and subject to market conditions and the availability of IGD headroom we'd expect to carry on making prepayments into the future.

The free surplus within the life companies started the year some £464 million in excess of what are already strong capital policies. This enabled us to make payments to the holding companies totalling £481 million. At the half year valuation free surplus in excess of capital policies was £468 million, including £197 million of cash generated through management actions. In spite of recent market turbulence which will have had an adverse impact on free surplus we remain confident that we will be able to meet our target for the year of £750 million to £850 million of cash flow generation.

So turning to IFRS operating profits we delivered an operating profit of £136 million at the Group which was in line with our expectations. IGNIS profits were down marginally which largely reflected higher costs within the business as we've taken on new managers to provide the talent we need to deliver the sustained out performance. Nonrecurring items benefitted from a one off recovery of historic costs under the management services agreements between the life companies and the service companies and a significant tax credit of £39 million due to resolution of certain legacy tax issues left us with a profit after tax of £108 million.

As I mentioned earlier MCEV grew by a very satisfactory £99 million after paying dividends to shareholders of £36 million and meeting finance costs on our debt of £75 million. Management actions of £69 million were delivered in the first half of the year leaving us on track to meet our target of £100 million for the full year. Clearly these are unsettled times and it's pretty certain that if we were to have recalculated our MCEV today it would have revealed a less benign picture on the economic variances. We've included a comprehensive

set of sensitivities in the appendix to this presentation that will give you an indication as to the impact of market movements on MCEV, both positive and negative. I'll also come on shortly to give you what I hope will be a clearer picture of our exposure to some of the issues currently affecting global markets.

So moving on to solvency. Our IGD Excess Capital representing the solvency capital within the Group available to meet adverse experience remained very strong at £2.9 billion. IGD Surplus in excess of our capital policy increased to £300 million. This was helped by some restructuring that we undertook to recapture internal reinsurance that had an adverse treatment under IGD. This is illustrative of the management actions that we have at our disposal to help to manage the IGD Surplus going forward and ensure that this isn't a constraint on our ability to make debt repayments from the holding company cash in excess of the liquidity buffers.

Assets under management fell by £1.1 billion. This was largely due to the assets managed directly by Hexam following the restructuring of the joint venture arrangements with them. Aside from that the natural runoff of the life company assets was in the main offset by a combination of new business and investment income and capital gains. It's particularly pleasing to see new third party assets at £800 million.

So as I mentioned just now when we were looking at the embedded value slide these are clearly unsettled times and a lot has happened in the few weeks since the financial results were struck at the half year. This time it's important to consider the exposure that we have as a business to bonds generally but in particular to the sovereign debt of certain eurozone countries, such as Portugal, Ireland, Italy, Greece and Spain.

On this slide we've broken the life companies' investments into the usual broad categories that we have seen, so gilts, bonds, equities and so on. But then we split this across the different types of fund according to who bears the investment risk. The key numbers to focus on here are the total shareholder non-profit and supported with-profits funds which is where the shareholder takes 100% of the investment risk. In the non supported or strong with-profit funds the shareholder broadly has a 10% interest in future profits and in the unit link funds the shareholder is exposed to movements in the annual management charge going forward and so broadly a second order impact from the market movements.

Our exposures to different asset classes are set having regard for the mandates that we put in place between the life companies and IGNIS. These reflect our agreed risk appetite and are monitored continuously by IGNIS and the life companies CIO as market develops. As you'd expect given our business mix our largest asset class by far is bonds at £20 billion, or 72% of our total assets, and of this 38% is in British Government securities.

On this slide we've set out by key areas of geographical exposure the different classes of debt security that we hold, covering sovereign debt, corporate bonds issued by financial institutions, corporate bonds issued by other than financial institutions and asset backed securities. As you can see the shareholder exposure to peripheral eurozone sovereign debt, namely Portugal, Ireland, Italy, Greece and Spain, is certainly not zero, but at less than 1% it's also not a material percentage of the total sovereign debt exposure. Of this, over 99% relates to Italy and Spain. All of these numbers are fully marked to market and reflected in the IFRS and MCEV numbers there that you've just seen.

So moving on to solvency and the impact on solvency, maintaining a strong solvency position throughout in difficult markets is absolutely crucial for our business as I'm sure you're very well aware. Our resilience here is very marked and reflects the sterling work done by Mike Merrick and his team at Phoenix Life over the last two years to de-risk the

business in line with our agreed risk appetite, but also of course the market's expectations. IGD Surplus and IGD Excess Capital are both very insensitive to market movements. In particular we're resilient to a breach of our IGD Capital policy, even where credit spreads to widen by as much as 300 basis points across the board for May and June our equities fall by probably around 75%. We also set cash generation targets for this year of £750 million to £850 million for 2011 and £3.2 billion for the six year to 2016. And as Clive said earlier on we remain on track to meet these targets and again are resilient to widening credit spreads and equity falls.

Overall, I hope you'll conclude that Phoenix is anything but complacent about the management of its risks and more over is well placed to deal with the turbulence and uncertainty which we're experiencing and ensure that we meet our key targets of policyholder security and shareholder value preservation.

And with that I'll hand you back to Clive. Thank you.

Clive Bannister

I am heartened to be in a position where our key metrics are resilient to market movement, not immune, but resilient particularly in these feeble times. It gives me confidence in the Phoenix business model and I believe this confidence can be shared by all our policyholders and shareholders.

To recap and conclude; we are on track to achieve all of our 2011 financial targets. Our approach enables us to be confident that with £496 million of cash already delivered that we are well on track to deliver the cash within our £750 million and £850 million target range. In addition, I'd like to take this opportunity to reconfirm our confidence in our declared £3.2 billion target of cash flows between now and 2016 in line with our previous forecasts.

Having already hit our full year objective of bringing gearing down below 50% we wanted to do better and we possess the cash resources to so do. But with so much uncertainty in the markets it would not be prudent to make a year-end prediction for gearing at this stage.

Finally, we have identified management actions that make us confident that we will deliver the balance of our £100 million target for MCEV enhancement.

To conclude, Phoenix continues on its journey and is in good shape. We have a unique shareholder driven simple business model. We have a proven management team and an effective set of operating platforms. We have a clear strategy and are absolutely focused on the delivery of our financial targets going forward.

For 2011 we have set out our stall to strengthen cash flows, enhance our MCEV and of course reduce gearing. Of course markets today look very different from the way in which they looked on June 30th both in terms of absolute valuations and volatility. But the fact that I can stand here with the confidence that we have in our ability to deliver our full year targets is a consequence of the quality of the thinking and the implementation in risk and asset management that has been effected by the Phoenix and IGNIS teams.

Just looking back this has produced £720 million of cash in the holding companies, generating £2 billion of cash flows and over £500 million of MCEV enhancements in the last two and a half years, so we're doing what we have done before. And although we face difficult economic conditions and market volatility this is a business that is well placed to ride out the storm. Our resilience and experience and our clear strategy gives us good reason to be quietly confidence in our prospects for the rest of 2011 and beyond.

Well ladies and gentlemen that brings to the end the formal presentation, thank you very much for your engagement. What I'd like to now do is move onto questions and answers. Happy to answer any questions that you have. Would you please wait for the microphone to be brought to you, if you could give us your name and the institution and then we will answer the question. I think we will wait until the end of the session to answer questions that may be on the phone or the internet.

Question 1

Greig Paterson - KBW

Three questions. This 12.27 EV per share. Could you just give that on a fully diluted basis, I assume that's not on a fully diluted basis?

Answer: Clive Bannister

I'm sorry, Greig, could you just start that question once again, you had three questions.

Greig Paterson

Yeah. Sorry you quoted a 12.27 EV per share. I might be wrong but I don't think that's on a fully diluted basis. I wonder if you could just give us the fully diluted number. The second one is the IGD sensitivities I see you've done a very good job at stabilising it across all the parameters, but what interests me is what happens if those stresses are two or three times the level. I'm trying to figure out where the non linearity is when market move about 40% or 50% which is not a non distinct possibility and also you know bond deals move quite dramatically more than that potentially can. So I'm trying to figure out where the stress points are or the non linear points are.

And the third point is I notice you've done two restructuring of IGNIS JVs and given that the IGNIS JVs have obviously been pulling in a lot of money I assume the management of the JVs seem to be in a sort of superior negotiating position when they renegotiate them. I just wonder what comfort you can give us that the economics are square in terms of when you change the percentage ownership. And also there's still some other JV... there's still another JV I think that's 50:50 and whether they'll be some value attrition during that. I assume they'll be some negotiation there as well?

Answer: Clive Bannister

Greig, well thank you very much, your first question was about our MCEV per share. I don't know whether I said it incorrectly but it is £12.77. At the end of the full year it was £12.27, it's now £12.77 and that does not include the VIF for IGNIS which we attach a value to of £2.35. So that is the maths that we have put forward in this presentation. And that is visible on slide 6.

Further question

((Inaudiable) if I'm not mistaken could you just give us what that number is now?

Answer: Jonathan Yates

I'm not sure we ever did actually I think we've only ever quoted it based on the shares in issue which is where we are today. But we obviously can show the number of shares that

could be in issue following exercises and various warrants and all the rest of it, and shares that were awarded under the settlement mechanism that took place last year when we took out the contingent shares.

Clive Bannister

So we can come back to you with that.

Answer: Jonathan Yates

I think all of that information is actually in the accounts. I think there's enough information in there to be able to do that calculation.

Clive Bannister

The second question you asked was to do with IGD and its sensitivity and I'm going to hand that over to Jonathan.

Answer: Jonathan Yates

Clearly the IGD is very insensitive and these numbers demonstrate that it's insensitive to a sort of relatively... in terms of the excess over capital policy to a relatively extreme degree. And there are two things driving that; one is the fact that as the surplus goes down the capital policy itself goes down with market movements. Our particular exposures are in respect of the with-profit funds. We actually hold capital in respect of with-profit funds through our capital policy, and as those funds effectively decline in size with the market then the amount of capital we hold will go down. So there is some offset there. There is an extreme position in which you could find clearly that the actual strong with-profit funds are no longer strong and in that case then clearly we're going to end up with solvency pressures. But those are the absolute extremes. And as I said before we're not going to be breaching our capital policies until equities have fallen by 75% or credit spreads have widened by well in excess of 300 basis points across the board. So we regard that as remote from today. The idea that triple A bonds would go to a 300 basis point spread is almost unthinkable.

Clive Bannister

And that advertises the resilience in the business that we take pride in. Your third question, Greig, was to deal with a repositioning of our business with our subsidiaries and our investments in IGNIS. And I have to say we take this as a positive move, which is an improvement in the relationship and a stabilisation which benefits both parties. But I'm going to ask Chris to answer your question specifically. Chris.

Answer: Chris Samuel: Chief Executive, Ignis Asset Management

Maybe just as background for those that aren't familiar with it, we've done a number of these joint ventures back in 2005, 2006, there's nothing new about the strategy of saying we were unlikely to do more of these, and that when they got to a time when we thought they were best served by becoming more independent, that's the structure that we would put in place. So we set up one in early 2010 called Castle Hill in a more independent structure, we moved Hexam to that structure in the middle of last year, and we've just announced doing the same thing with Argonaut.

The economics we hope will overall be beneficial to us obviously. We take our return in a different way we don't get a share in revenue, we get a share of profits. And we hope that as more independent businesses, the business will grow more quickly. Importantly we have an opportunity to generate capital value out of them, which wasn't available to us before. And thirdly we're very focused on strengthening the in-house teams, and we believe that's easier to do when you don't have all of our infrastructure supporting some teams in JVs that would be competing with them. So those are three ways of attracting value.

You mentioned Cartesian, which is for the moment a smaller business and not ready for that step. But at some point in the future if the partners in that business think it's the right thing to do if we agree with them we would certainly be open to such a move.

<u>Question 2</u>

James Pearce – UBS

On the IFRS earnings, the fall in non-profit profit, if you see what I mean, you mentioned negative variances compared to favourable ones last year can you explain what the 15 in negative variance was in more detail?

You say that recurring margins are down 11, that leaves another 12 million decline which is unexplained. Could you talk about what that is? And what is really the base level in non-profit profit?

On the embedded value group costs, which went up a fair bit, can you explain what the sustainable or ongoing group costs are and why the increase?

Clive Bannister

James, thank you. Two questions on IFRS profits, the decline and reasons behind, and then looking at the cost situation. Jonathan?

Jonathan Yates

First Mike, and then I'll return for the IFRS.

Answer: Mike Merrick: Chief Executive, Phoenix Life

Thanks, Jonathan. I think the key reason for the fall in profits between first half year 2010 and 2011 is, as you say, the good things that were done in 2010. In June in the Phoenix Life presentation we talked about the work that we do in terms of resolving legacy issues, a lot of those positives in 2010 came from such issues, and we hadn't seen the recurrence of those positives at the same kind of level in 2011.

The biggest component of the minus 15 that you referred to was at the result of resolving a legacy issue they're not always positive, and this unfortunately was a negative as a result of reallocating some historic revenue between our funds.

Answer: Jonathan Yates

In terms of the cost then clearly our costs have gone up over the last year, in fact the last couple of years. A major part of that is because we're now running as a listed group and we're having to obviously set up a head office that is capable of functioning as a listed group.

And being listed itself comes with certain costs, and also incurring sort of one-off project costs, although those are now largely coming to an end. In terms of what the sustainable level going forward will be, it will be something of the order around £60 million per annum.

Question 3

Ed Hawkes – Sun Capital Partners

Perhaps you could talk about your confidence levels around your cash generation targets that you spoke about on slide 22, the £3.2 billion, particularly in light of the gearing level of the business?

Answer: Clive Bannister

Ed, thank you very much indeed. We find ourselves in very interesting times, and we are very glad to be able to reconfirm two targets in effect one of which is the £750 million to £850 million cash flow for the full year – I have confidence about that. But we also think we want to backstop it in everybody's mind that the larger target, stretching out into the future till 2016, and we reconfirm our ambition and our abilities to deliver that £3.2 billion of capital.

The second clause in your question said well, what does that mean in context of our debt? Our debt at the moment is standing at about £2.6 billion, as I referred to earlier. We've seen organically our leverage and our gearing come down. We set a full-year target which was below 50%, we're already there at 48%. All things being equal, with the mandatory payments we have in front of us, that number would come down to 46% for the full year. And I think this emphasises that in the context of our cash flows it is not the quantum of a debt that causes any issue, it is our desire in the fullness of time and appropriately to return that debt against the maturities of those cash flows, and thereby deal with some of the issues that related to covenants that constrain us, particularly in the area of dividends. So, this is a comfortable and good position to be in.

Question 4

Oliver Steel – Deutsche Bank

Perhaps I can just follow up on that question, because I think it's actually probably the most important question today. Jonathan has talked about the sensitivity of your £3.2 billion of cash flows over the next six years, and if I look through the sensitivity there clearly is downward sensitivity related to equity markets, property markets, and I assume interest rates as well. So can you explain in a little bit more detail why you're so confident in that £3.2 billion still being achieved? And how much more of a market fall, if that were to happen, you can bear without sort of moving away from that £3.2 billion target.

Answer: Clive Bannister

Oliver, thank you very much for that question. Several parts to that, let me deal with one, and I'll ask Jonathan to repeat what he said about equity market movements and also spreads.

So the first point is there are clearly bumpy times, but we are very conscious of our responsibilities about making forecasts both about this year and also stretching out into the future. Our confidence resides around our ability to do a variety of management actions, and those are the things that we've done in the past, but also going forward, which allow us to accelerate cash. And in our appendix we show you what those future cash flows look like

coming out over time. And that range of management actions underpins that confidence. We will be in a better position to update on 8th November. And as I also said there is considerable resilience, but not immunity.

So that's how I would answer the broad position. And the £496 million generated year to date sets us up in a very good position. That adds up to our delta in terms of holding company cash of £234 million, giving us a total amount of holding cash of £720 million, which is the highest it's been.

So that's answering it in the round, management actions substantially. And you may want to comment about the market movements and the resilience in that context.

Answer: Jonathan Yates

Obviously this is an area that we have looked at and look at constantly, and we are doing re-projections of our future cash flow going forward at all times.

When we gave our target of £3.2 billion for the six years, and £750 million to £850 million for this year, we also included management action target of £300 million, purely in respect of this year. So, in other words, the projections going forward, the six-year plan, didn't have any management actions in it beyond what we'd already factored in for this year. Of course management actions are something that we are working at all the time in terms of looking what further benefits we can get out, and over what period we can actually get those benefits. That gives us and what we've been able to identify since gives us the confidence that we are resilient to market movements at the sort of level that I was indicating before. So in terms of if you look at single stresses, we could meet our £3.2 billion target, which is a six-year target as I say, with some fairly significant stresses around equities and spread widening, very significant stresses.

Having said that, that doesn't necessarily mean that the cash flow emerges in a nice sort of steady pattern, what it means is that it probably becomes more back-ended in nature, but not dramatically so. And I think that's what gives us a large degree of confidence of being able to say we're going to meet this year's target for cash flow.

So the business is resilient, we're making it more resilient as time goes on. Management actions are a key part of our business. In fact it's probably worth making a comment around management actions. When other companies talk about management actions generally what they're talking about is actions that they could take in the event of an extreme stress hitting the business, to prevent further damage. So for example what they're doing is they're showing the management actions that would limit the extent of ICA that they would require under Pillar 2.

Our management actions aren't like that. I mean we have management actions like that, but our management actions in the main is completing the merger of Pearl and Resolution, to some degree. And those two businesses still operate in separate silos. The more we start to address the mergers of those businesses, the way we start to bring them together in terms of consistent styles of management, consistent capital policies, capital treatments, we get better diversification of risk from merging the eight or so life companies that are actually within those companies, the more we're able to release value. Clearing up legacy tax issues for example is for us a management action. Doing the work that we did earlier this year on restructuring the corporate loan portfolio was a management action. Not something that we'd do in a stress position, but something we do because it makes sense for the business. And those are the things that we are constantly looking at and which we have a long agenda of

items that we're going to working on going forward. Obviously our confidence is higher around the ones which we intend to do sooner, but going forward the list is still a long list.

Question 5

Trevor Moss, Berenberg Bank

A few questions, I'm afraid. Could you split those £15 million of negative variances across the different non-profit lines please? And then if we were to then do that to indicate whether those run rate numbers that we would see having done so would be broadly speaking where we should expect the run rate to be.

Secondly, on the other investments line, where there's a decent spread of shareholder exposure, you've broken down the split of what other investments are in total, including policyholders, could you break down the shareholder exposures to other investments and tell us what's actually in there please.

Thirdly, if you're moving gearing into the 40 percents do you think that gives you optionality in the corporate bond market, or are you very much focused on renegotiating the bank facilities, which appears to be what you were saying, but I would have thought into the forties you have optionality in the corporate bond market.

And finally, I think for Chris, I see that in terms of IGNIS net flows and gross flows the net flow negatives came from UK retail and UK institutional and the net flow positives were in International. Is that, do you think, a consequence of fund performance, or is that a consequence of marketing efforts? And if you could talk a little bit more around what those marketing efforts are, particularly you seem to be focusing quite a lot of time and attention on the international business at the moment. Thanks.

Answer: Clive Bannister

Trevor, thank you very much indeed. There are four questions there. Chris, can I ask you to take the last one first, which is just to talk about the net flows. Whilst Chris is thinking about that the three other questions were first of all the £15 million negative variance first, Jonathan.

Answer: Jonathan Yates

This is something we're looking at at the moment in terms of coming up with an analysis, and what I suggest is that we come back to you on that and put something out which explains that in a bit more detail and gives a bit more granularity around how that is split up. But it is something that we are focused on.

In terms of the other investments, can I just be clear, you were talking about the other line on slide 19, was that...?

Trevor Moss, Berenberg Bank

Yes, I think so. You've got about three point something billion in total and 1.8 in the shareholder exposure. Then you break that down to get to your 3.3, I think it was, by some derivative instruments and billion of other, and various things. If you could break down what's actually in the shareholder exposure.

Answer: Jonathan Yates

Which one are you one? Slide 18, sorry.

Trevor Moss, Berenberg Bank

Yes, sorry, slide 18, okay. So you've got 1385 of total shareholder exposure to other investments and 3.3 in total. You break down the 3.3, and it's a whole variety of things that I don't know what they really are. But 1385, if you could break down, which is perhaps more interesting for shareholders. Thank you.

Answer: Jonathan Yates

Yes. If we could come back to you then with an analysis of that. I mean there is a sort of a footnote in there which tries to sort of explain it, but it's a whole series of smaller things.

Trevor Moss, Berenberg Bank

I just seem to remember from olden days there was quite a few slightly strange investments that were made by the previous private equity owners of this business, and I'm not sure where they reside, and whether they are still there even, so on and so forth.

Answer: Jonathan Yates

There are a range of hedge funds and things of that nature which have been progressively sold down over the last few years as part of the derisking that we've done. I've got to say our main reason for selling them is because of the capital treatment that they attract, but actually their performance over the last few years has actually been exceptionally strong, and it's been a big driver of profitability. But we can give you a better, more granular breakdown of that number. And then the...

Clive Bannister

Gearing. And whether we were getting too traded.

Answer: Jonathan Yates

It's a very good question and it's something that we've been approaching to discuss many times by various banks. And the response is that it actually, the amount we could raise would be relatively small compared to our existing bank debt. We would go out as, effectively, to non-investment grade credit at the moment. There are no real buyers of non-investment grade life assurance bonds. There's no real expertise in that market. And I think our feeling was that it probably wasn't a market that we should be looking to tap. And our focus is probably much longer term on tapping the investment grade corporate bond market, that makes a lot more sense, through sub debt.

Further question: Trevor Moss

Where do you think you would need to get to from a... I guess it might be primarily from a gearing perspective, to move into an investment grade category? Any thoughts on that?

Answer: Jonathan Yates

Well, that's one for the rating agencies, but I think typically the expectation would be S&P's gearing ratio is around 40% using their gearing calculation, which is subtly different to ours.

Clive Bannister

And the final question, Chris, it was about flow of funds.

Answer: Chris Samuel

Yes, Trevor, I think you were looking just for a bit of insight into our distribution efforts and page 33, I think, was the page you were looking at. So we have a team focused on the UK retail market, that's been a significant area of focus, not least because we obviously had, through the joint ventures, a range of product to sell there, and that focus will absolutely continue. We've been seeking to beef up our institutional efforts and you can see some reference to that. And that LDI mandate that's actually from one of the pension schemes we've excluded from the number on page 33, but it's an important win. And then the international really breaks down into two bits, a team we employ ourselves focused on Europe, and that's a fairly typical model of one to two people in the principal markets, and also third party marketeers that we use both in the Far East and the US. And I think you also asked about what drove sales. I mean at the end of the day it is heavily influenced by investment performance and so what we've won is concentrated around liquidity and property, where performance has been exceptionally strong versus the competition. But clearly at the more institutional end of the spectrum the quality of the team, the investment process, is also extremely important.

Answer: Clive Bannister

The other point I would say, Chris, is we've reinforced the team to lead our sales effort. Claude Chene is joining us shortly and that's a very significant addition to our bench strength because getting third party sales and third party business into IGNIS is a very high priority for us.

Question 6

Duncan Russell, JP Morgan

Could you just talk a bit about interest rates, and in particular if you look at the MCEV sensitivities, lower interest rates appears to be good. I'm guessing that's a quirk with the calculation. In your view, if interest rates remain where they are today, how hedged are you, how protected are you, would you like to see interest rates going up, what would be the optimal environment for you, as a group?

And then secondly could you talk about the regulatory environment, Solvency II, any updates on that? Are regulators more nervous in the current market environment, does that have any impacts on IGD etc?

Clive Bannister

Okay, so I think Jonathan hits the first question on the hedging, and Solvency II, Mike.

Answer: Jonathan Yates

In terms of interest rates, interest rates have a multiple of impacts on our business, so the first thing is if interest rates go down obviously the cost of our debt goes down, at least it would do were it not for the fact that we've actually largely hedged out the interest rate risk in our debts, but we haven't hedged it out completely. The extent to which we haven't hedged it out completely is broadly offset, though, against the amount of cash that we're carrying at the Group holding companies. As you can see we actually carry a significant amount of cash there, so that effectively hedges out the unhedged debt exposure.

Within the life companies clearly falling interest rates can mean a number of things. In terms of short term cash-type holdings, then obviously it means we're earning a lesser amount on those holdings going forward. To the extent that interest rates fall in terms of a shift in the yield curve down, in terms of our liabilities we'd be largely matched, we aim to match our liabilities very carefully so you wouldn't expect there to be a huge impact from that. Where you do see an impact, and this comes out in terms of the MCEV, are sensitivities that you were referring to, I think. Obviously if risk-free rates do come down we tend to see a very significant benefit, because you're just discounting those assets at a lower rate, and therefore the MCEV itself goes up, which is why you see such a positive movement. But I think the answer is it's a mixed picture in many different parts, but broadly overall positive, to see falling interest rates.

Answer: Mike Merrick

Sorry, Andrew, could I ask you to repeat the question please?

Duncan Russell, JP Morgan

Just on the regulatory environment in general, with the market volatility which you've talked about. How is that influencing Solvency II? And secondly, how is it influencing the FSA and your own capital policy, the headroom you required, and are the regulators becoming more conservative in this environment?

Answer: Mike Merrick

I can't really speak for the regulators, but I think from a Solvency II perspective there are still many key critical areas of the Solvency II that remain to be determined. I don't know but I would imagine the current environment will have some influence on the outcome of those key decisions. But we believe that the strength of our existing ICA and the capital policy that we operate on top of our Pillar 2 calculations puts us in a good place to address the requirements of Solvency II as they emerge. But we certainly haven't seen any explicit questioning of the adequacy and the strength of our current Pillar 2 capital assessment and our capital policy.

<u>Question 7</u>

Toby Langley, Barclays Capital

Apologies if I'm going over old ground, but on the dividend, following up on some comments around your approach to the bank debt situation, with specific regard to the dividend, what kind of message are you trying to deliver here, or what policy are you trying to project? Because my sense is that we should be just looking at the 42p full year dividend for the foreseeable future. Is that the right way to read what you're telling us today?

And then a lot of your peers, some of which produce a lot less cash than you do, have removed the scrip dividend and I'd just be interested in your views on whether you see that as something feasible, or why you still see it as attractive to retain a scrip?

Answer: Clive Bannister

Okay, well two parts to the question Toby, thank you very much. We reconfirmed the 21 pence per share. We are constrained under bank covenants at £58 million this year and £72 million for our dividend payout rate. We are – you asked about the future policy – dividends will be decided in the light of those covenants, but also, as always, in the state of the business and how it finds itself, and that we work within those. Part of our desire to compete successfully discussions with our bank is so we can re-term the debt and one of the concomitant consequences, happy consequences, would then be a change in those covenant restrictions. So those would be the comments I would make on the dividend.

And with regards to the script, the script is a function of history. It is a consequence of contractual arrangements with certain shareholders that were entered into when we did the premium listing. Those obligations fall away and expire with this interim dividend and then it will be up to the board, and the board intends to review that policy going forward with regard to a scrip option.

Another question? James.

<u>Question 8</u>

James Pearce, UBS

A supplementary one on the debt. If you renegotiate the bank debt and it costs you, for example, 100 basis points more, does that get offset by lower hedging costs and by how much.

And secondly, what's plan B on the bank debt, given that I think you'll probably run out of money in 2016 if you don't renegotiate because of the phasing of your cash flows. You seem very nonchalant about the renegotiation, you must have something else in mind if the banks play tough, so could you just outline where you would go in that situation?

Answer: Clive Bannister

Fine, so that's a two-part question. I'll answer the second part and then I'm going to go and ask Jonathan to answer about the consequences of what it would cost if our debt rises. So let me answer the first point.

We have very good relationships with our bank, so it's not nonchalant. This is a challenge for us but it's almost a positive, inasmuch as it's not the quantum of debt that concerns us, it's the nature of the terming. To repay all of our debt and get to zero leverage would not be in the interests of our shareholders at all, and the debt today is currently very well priced at about 195 basis points, and we talk about that in appendix nine. And therefore we don't set ourselves a finite period by which to solve this issue, because we want to do it in the round, thinking about all our stakeholders, cognisant as we are about the market volatility and we take a considerable pride and delight, it's a high class problem to have the volume of cash that we have in the holding company at £720 million. So you refer to a plan B, our plan A absolutely is to work with our bank, our consortia of banks, of which there are 14 in two silos, and to reach a re-terming of that debt which serves multiple stakeholders at the right time in

the right place, particularly for our shareholders. We don't feel under pressure to do it tomorrow, as you correctly point out this is something that has to be solved by 2016. So that's how I would answer your question.

Jonathan, you may want to talk about the cost of our debt and whether that gets offset.

Answer: Jonathan Yates

Very simply, we pay LIBOR plus a margin on our debt. LIBOR is around 75% hedged under the existing arrangements. If we were to refinance and the margin were to increase by 100 basis points we would remain 75% hedged on LIBOR but we would be paying 100 basis points more on the margin.

Clive Bannister

Another question? I'm looking at Lucie. Are there any questions on the internet or on the telephone? Okay, can we have a question please off the internet or telephone? Would the questioner please given name and institution. Thank you very much.

Question 9

Magash Chetty, Pramerica Investment Management

Can you please provide some colour regarding your £3.2 billion cash generation target to sensitivities in equity and credit markets?

Answer: Clive Bannister

We've covered that ground before, but I'm going to ask Jonathan to in effect repeat and go through what he has said before in terms of our confidence level, both for this year and going out to 3.2 billion, and the sensitivities which you have alluded to beforehand.

Answer: Jonathan Yates

Thank you, Clive. As I said before we remain confident about our ability to be able to deliver £3.2 billion, which is a six year target. In terms of the stresses that we've applied to that, in terms of things like equity stresses and credit spreads, it would need very considerable widening spreads, or falls in equity markets, to leave us in any danger of not meeting that target. Part of the reason for that is that we're constantly working at coming up with new management actions that we can put in place and have a long list of these that we're confident would actually enable us to deliver that target into the longer term. The profile of the emergence of that £3.2 billion may be changed slightly, but actually the end result would be no less certain.

Concluding comments – Clive Bannister

Lucie, is that it? That's the questions done?

I want to end today, unless there are any further questions from the floor? Thank you very much indeed, very good questions, positive for the firm as we started, this is a strong, robust set of results and our confidence in terms of cash generation, adding to MCEV and bringing gearing down organically over the rest of this year makes us look with good confidence out into the future. Thank you very much indeed.