Mark Gregory, Legal & General's group chief financial officer discusses this year's highlights, including Solvency II, the new dividend policy and his views on the company's future prospects.

Q Mark, what achievements were your personal highlights for 2015?

A 2015 has been another challenging but great year for Legal & General, with increased net cash generation, operating profit and return on equity. There have been many achievements. I would say that from a strategic perspective, writing our first US and European pensions risk transfer deals, LGIM becoming the world's 15th largest asset manager, with over $1.1 trillion of assets under management at year end and the progress on our urban regeneration schemes in Salford, Cardiff and Bracknell were significant steps forward. Additionally our auto-enrolment scheme wins, and the success of our newly acquired Home Finance business and Asian mandate wins in LGIM, were signs of positive momentum in our newer product offerings.

We retained our market-leading positions in LDI in the UK (over 40% market share), UK retail protection (25% market share to Q3 2015) and £77 billion assets under management on Cofunds means it's still the largest savings platform in the UK.

Mark Gregory, our group chief financial officer, on a visit to Salford, one of our urban regeneration schemes and the location for our MediaCity investment.

We started to transform the shape of our business, making us fitter for the future, with our strategy of bolt-on acquisitions and disposals.

But we aren't complacent; there are many further growth opportunities for the group and we can make more progress in improving the profitability of the Savings division.

Q You have announced a new dividend policy, how did the Board come to this decision?

A Our existing dividend policy was time-dated. We stated that we expected to reduce our net cash coverage of dividend towards returning two-thirds of our net cash to shareholders via dividends (i.e. 1.5 x in 2015), should our Solvency II surplus be no lower than Solvency I.

Now we are in the Solvency II regime, the Board has adopted a progressive dividend policy, reflecting the group's medium-term underlying business growth, including net cash generation and operating earnings.

Clarity on Solvency II means it's the right moment to announce our new policy. We view the primary method for rewarding our shareholders to be via the ordinary dividend and we think the new policy is a sustainable way of continuing to do that whilst retaining sufficient cash to invest in growth opportunities for the group.

Q Legal & General announced its new capital-lite strategy for UK bulk annuities at the time of the Interims. Could you tell us more about it?

A Our response to the potential global defined benefit liabilities estimated to be in excess of $9 trillion and the increased regulatory capital requirements for annuities under Solvency II, meant we accelerated the implementation of our capital-lite model for the pension risk transfer business. This means we take on less risk in respect of new business on our balance sheet, whilst seeking to optimise the return on capital we

Solvency II Capital Surplus

£5.5bn

169% coverage ratio

Figures are pre-accrual of proposed final dividend for 2015 on a pro-forma basis.

Solvency II

Solvency II is a risk-based capital regime designed to calculate the amount of capital needed for a worst 1-in-200 year event i.e. the impact on our business of scenarios like the Great Depression, the recent financial crisis or an epidemic like the Spanish Flu outbreak in 1919–1920.

In 2015, the PRA approved the usage of our internal model to calculate our Solvency II capital requirements for the regime which began on 1 January 2016.

Economic capital

Our corresponding economic capital surplus is £7.6bn with a coverage ratio of 230%.

Guide to symbols used in Financial review (pages 34 to 41)

Key performance indicator (KPI)

£ Key measure in the remuneration of executives

deploy in this market. For each new annuity contract we expect this to result in a higher proportion of profit emerging in the year of sale. However, we expect less total profit to emerge over the duration of the contract when compared to retaining all of the risk. We will use direct investments and selective derisking actions to optimise returns from the long-term predictable run-off of our £43.4 billion annuity back book.

Now we have clarity on Solvency II, it's the right moment to announce our new dividend policy"

Q Legal & General has been 'decluttering' non-core business units in the last year. What was behind that?

A We have been pursuing a focused and disciplined approach to executing the group's strategy. We have chosen to undertake the exit, closure or sale of a number of non-core or sub-scale businesses, such as closing our with-profits fund to new business and selling our Irish, Egyptian, Gulf, French and German businesses.

These operations were not going to be core to our group going forward and we felt that other owners may be more suitable, enabling us to reduce the management time required to oversee them.

Q You raised £600 million of sub-debt in October, why was this necessary?

A We have a long-term debt strategy which is designed to ensure we have an appropriate balance of debt and equity funding. The £600 million debt raised in 2015 was part of this long-term strategy.

Q In February 2016, you announced your intention to retire from the group in January 2017. Can you tell us about your decision?

A I've really enjoyed my time with Legal & General and the company is in great shape. By January 2017, I will have been here for 18 years and spent eight years on the Board so whilst a difficult decision, I have decided that next January is a good time for me to be retiring from the group.

Q And finally, what challenges do you face in the coming year?

A Well, the equity and bond markets are still proving to be volatile and that does give a reminder that there is still ongoing market uncertainty. But whilst no model can be completely immunised, we believe our strategy creates a high degree of resilience.

We've been very upfront about some of the challenges facing us: like the trend in maturing UK DB schemes moving out of equity index funds; legacy product run off; and the new Solvency II capital regime. However, we work hard at mitigating these exposures.

For example: we've been targeting the derisking trend by DB pension schemes being the only provider to offer the full range of pension derisking strategies; we are expanding our LGIM operations in the US; we're reducing our dependence on the UK market with pension derisking transactions in the US and Europe and have developed our new capital-lite model for UK business.

Our strategy is clear and focused. The challenge as always is to continue to execute it effectively. I'm proud of how well we respond to these challenges and have confidence in Legal & General going forward.