Transcript

Legal & General Preliminary Results 2019

4 March 2020

Nigel: Good morning, everyone. Welcome to our full year 2019 results presentation and of course to our wonderful new surroundings. Today is about how Legal & General is delivering inclusive capitalism, great commercial and economic results but also benefits for society more broadly. The two go hand-in-hand for us.

We worked this out almost a decade ago and this is a programme of action for us on both fronts; inclusive and capitalism. By way of housekeeping, please switch off mobile phones. There are no planned fire drills. And the usual disclaimers apply to forward-looking statements.

2019 was another consistent year of strong performance for Legal & General; record-breaking in several key areas. Operating profit from divisions excluding mortality release and excluding discontinued businesses was up 17% at 2.5 billion. Solvency II operational surplus generation was up 9% at 1.6 billion. EPS was up 16% at 28.66p and ROE was 20.4%.

Book value per share was up 9% at 156p and the recommended full year dividend is 17.57p. That's up 7%. Jeff will take you through the financial numbers in detail. As an overview, all of our divisions performed well in 2019. These results are another step on a consistent journey. For almost a decade we have delivered annual double-digit growth in operating profit from divisions, EPS and DPS.

Our growth in book value per share has accelerated, reflecting the quality of our earnings plus ROE rising from 14.9% to 20.4%. 2019 was another year of consistent growth for all five businesses. Since 2015 all have delivered growth in operating profits.

LGRI delivered compound annual growth of 21%, LGIM 4%, LGC 12%, Insurance 2% and Retirement Solutions at the highest rate at 25%, overall 13%. In 2015 we set ourselves an ambitious goal for 10% compound growth in EPS for the five-year period from 2015 to 2020. We have achieved that goal with 58% growth in four years, so we'll be setting out our ambitions for the next stage of our development later in the year.

Our focus is twofold; firstly on large, often international markets where we have a small market share and can outpace market growth like at investment management, and secondly growth markets where we have leading market share and can grow by retaining market leadership and expanding internationally like PRT.

That strategy is working for us. We've also entered a number of new adjacent markets successfully and at scale, for example affordable housing and salary finance. Meanwhile in 2019 we continued to sharpen our business focus by completing the sale of the general insurance division for £255 million. We expect to complete the £650 million sale of the mature savings business in the first half of this year.

New business in 2019 was similarly strong, building on sustained compound growth across all of our divisions; 47%, 23%, 35%, 5%, 31% and 48% as shown on the slide. We have no laggards. In pension risk transfer LGRI delivered 11.4 billion including significant international success. We are a global leader in this market and our pipeline is strong.

LGIM's external net flows of 86 billion is more than twice the equivalent in 2018. LGC's direct investment of 2.9 billion is another step forward. LGC is unique; as well as contributing to its own operating profits it is a crucial part of our strategy to rate alternative assets for the broader group and to deliver outstanding economic and social outcomes in housing, in energy and in future cities.

Insurance GWP rose to 2.7 billion. Again we are a market leader. Competitive products, strong distribution and fintech sit at the heart of LGI which includes our intermediate mortgage business, which facilitated 78 billion of transactions in 2019.

Retail retirement in LGRR delivered 970 million of individual annuity premium and in a more competitive market 965 million of lifetime mortgage advances. I'd like to thank all of our divisional CEOs; Laura Mason, Chris Knight, Kerrigan Procter, Bernie Hickman, Claire Singleton, who is delivering the sale of mature savings, and Michelle Scrimgeour, as well as all of their colleagues and indeed many of our advisors for another stellar year and to wish Michelle a speedy recovery from her ski injury. She is listening in today and has every reason to be proud of her business' performance.

Our colleagues make Legal & General the success that it is today and they operate within a collaborative and mutually reinforcing structure. LGC, LGR and LGIM work closely together to create assets which deliver shareholder returns. We structure and/or self-manufacture assets to support PRT business and to provide AUM to LGIM and to LGC.

This model, which is built around positive and constructive collaboration, creates new asset classes and provides co-investment opportunities for our external institutional clients and this combination of investing as a principal and as an agent is supported by the Solvency II capital advantages and technological leadership provided by LGI.

Working collaboratively across our divisions has diversified risk and it is these structural and capital synergies which result in our 20% ROE. These synergies remain unique in our sector and our industry. I would now like to hand over to Jeff to take you through the numbers.

Jeff: Thank you, Nigel, and good morning, everyone. This morning I'm going to cover our 2019 financials on both group and divisional bases, the management of our credit portfolio, the ongoing investment in LGIM and lastly our capital position and surplus generation.

Looking to our group financial metrics, 2019 was a strong year for Legal & General, continuing to deliver value to our shareholders. Operating profit from continuing divisions was up 17% at £2.5 billion with growth in all five businesses, demonstrating the quality of our diversified business model and the value of our focused, long-term strategy.

This growth rate is excluding a mortality release from LGR's annuity book. We've been able to make sizeable mortality releases for the past three years because our long-term assumptions about mortality were prudent against emerging longevity trends. In the second half of 2019 and in light of the more recent mortality trends we conservatively adopted an adjusted version of the CMI 2017 table resulting in a reserve release of £155 million.

As usual we maintain our cautious and staged approach to the trends we are seeing and we will investigate a move to the next actuarial table, CMI18, in light of 2019 population experience and the relevance to our book of lives. We'll provide an update on our analysis later in the year.

Going forward all comparisons I make to prior year metrics will exclude these mortality releases unless otherwise stated. As I mentioned at our half-year results we're making measured investments into our business in order to improve efficiency, drive growth and comply with the evolving regulatory framework. For that reason you'll notice investment project spend is up £60 million.

The additional expenditure primarily relates to augmenting cybersecurity, upgrading the IT infrastructure and preparation for IFRS17. We expect this to reduce as these complete and move to BAU. Despite positive performance in equities and other asset classes over the course of the year the overall result was a negative investment variance.

In particular LGI was again impacted by falling UK and US government bond yields, as we've seen in previous periods. However we were still able to maintain profit before tax and EPS growth of 15% and 16% respectively and Nigel has already covered the synergies that lead to a 20.4% ROE.

Finally the group's Solvency II operational surplus generation was 1.6 billion, up 9% from last year and the coverage ratio for year end was 184%. I'll cover our capital position in more detail later.

Turning to our divisions, LGR's momentum has continued in 2019 with operating profit growing by 27% to 1.4 billion. This success was driven by the ongoing delivery of prudential margin releases from our growing back book, further helped by positive variances arising from routine updates to our mortality assumptions.

Both our retirement businesses delivered solid growth. Our institutional business grew operating profit by 34% to £1.1 billion,. For the second year in a row the UK PRT market had record new business volumes, topping £40 billion in 2019. LGRI took roughly a quarter of total market volumes as we maintained pricing discipline, achieving a Solvency II new business margin of 7.9% and capital strain of just 4%.

Our retail business delivered operating profit of £298 million, up 5% with annuity new business continuing to grow. As I said, LGRI had a fantastic year, writing more than £11 billion, a 21% increase. In the UK we wrote £10.3 billion on a wide range of deals including one of the largest pension buy-outs for Rolls- Royce, an LGIM client since 1989.

We are a trusted partner for pension schemes across their derisking journey and in 2019 we helped a number of plans meet their end goals including the culmination of a seven-year derisking journey for Hitachi. We also completed one of the first transfers from fiduciary management to pension buy-out for a client. We are unique in having both these capabilities in our business, meaning we are well-placed to help fiduciary management clients move to buy-outs over time.

The UK PRT market opportunity remains vast and we are continuing our development of capital-light PRT products. For example in 2019 we wrote our first assured payment policy which provides asset yield, interest rate and inflation risk protection to pension plans paving a more secure path to buy-out over a planned time frame.

Many of these transactions benefited from LGIM's long-standing client relationships. Over the past three years 51% of UK PRT deals have been from LGIM clients. There are also significant international PRT opportunities and in 2019 we entered the Canadian market with a transaction through our partnership with Brookfield of over CDN$200 million.

In the US we wrote more than $1 billion for the first time as we started writing larger mandates. In retail retirement we've delivered 24% operating profit growth annually since 2016. Our individual annuity sales increased 22% over the year, benefiting from our improved enhanced annuity proposition and increased broker presence.

We added a fourth introducer arrangement in November with Prudential which is expected to increase sales by 15% in 2020. Lifetime mortgage advances were down to £965 million as we maintained pricing and underwriting discipline in a competitive market.

Despite stronger competition we were still able to achieve a 25% market share driven by our wide range of products and strong customer-focused brand. Our LGR asset portfolio which is a source of long-term captive AUM for LGIM has now grown to £76 billion with 28% of the portfolio in direct investments including lifetime mortgages.

We have maintained high credit quality with two-thirds of our bond portfolio rated A or better and 17% in sovereign-like assets. The portfolio is well-diversified by geography and sector. Only 22% of our bond portfolio is in UK-listed corporate credit with many of these holdings being multinational companies with significant diversified overseas earnings.

Our exposure to overseas issuers makes up nearly half of our portfolio and we hedge our currency exposures to deliver matching sterling asset cashflows. We are thoughtful in our exposures to various sectors. As I have mentioned before, we have reduced our holdings in pro-cyclical sectors like banking where our exposure is less than 5%.

We have also avoided sectors which we believe are at risk of significant disruption, for instance traditional retail and automotive, which together constitutes less than 2% of our portfolio. LGIM manages the portfolio to avoid downgrades and defaults and has been extremely successful at this, realising less than £25 million of default losses in traded credit since 2007 whilst maintaining overall portfolio credit quality.

As further protection we continue to hold a substantial credit default reserve of £3.2 billion. LGR also has a diversified and high-quality direct investment portfolio with stable income from high-quality counterparties, often additionally collateralised or secured. 15% of the assets are rated AAA and approximately half of these are quasi-sovereigns like HMRC and the Secretary of State.

We added £4.3 billion of new alternatives assets over 2019 and have had particular success financing internally generated new asset classes in build-to-rent and affordable housing, leveraging the experience and skills of LGC Homes and LGIM Real Assets.

Again - and I know I stress this a lot - it's important to remember that our primary exposure in LGR's DI portfolio is to the counterparties, not to the properties. We recognise the influence our annuity investment decisions can have and therefore we've been thoughtful about how to integrate sustainable principles into our asset strategy.

We have made explicit commitments on overall carbon intensity in our TCFD publication. Across the group we have sought investment opportunities to develop and commercialise decarbonisation technologies. LGR alone has made more than £1 billion of direct investments into renewable energy such as solar and offshore wind.

We invest in assets like social housing and renewable energy because our pensions are for the long term and require long-term sustainable assets to back them.

Now moving on to LGIM, operating profit was up 4% to £423 million reflecting increased revenues from flows and positive markets. As previously guided this was offset by continued investment in the business resulting in a cost/income ratio of 54%, which has increased marginally from last year.

LGIM achieved record external net flows of £86 billion, representing 9.4% of open and AUM. Of this international net flows were £59 billion and included a £37 billion Japanese passive inflow reported in the first half. This mandate leveraged our proactive ESG approach and provides LGIM Asia business with a platform for future growth.

We also continued to see strong demand from a broad range of European customers with flows of £11.6 billion reflecting the continued focus we've placed on the region. Total AUM increased 18% to £1.2 trillion with international assets accounting for 30% at £370 billion.

UK DC had another strong performance with AUM up 33% to £94 billion, maintaining its market-leading position. This includes 8.9 billion in our master trust, one of the largest and fastest-growing in the UK, reflecting its continued appeal to DC plans who outsource their governance, investment and administration to LGIM.

Total retail AUM reached £39 billion. LGIM was ranked second on both gross and net UK retail sales in 2019 as we continued to experience high demand for our multi-asset and indexed products. As part of our ongoing change programme we continue to invest in the business to achieve the resilience and scalability fundamental to LGIM's future success and to generate operational leverage.

Areas we are investing in include digital client portals, technology-enabled investment platforms and international expansion leading to efficiency and lower unit costs as we grow. Going forward LGIM-related project expenditure, currently reflected in group expenses, will be allocated to the LGIM results. Rebasing the 2019 financials would have resulted in a £29 million transfer of expenses, increasing LGIM's cost/income ratio from 54 to 56% so £394 million is the base 2019 figure to start projecting from.

To help you, in 2020 we expect the equivalent transfer from group to be around £20 million of additional expenses. This allows better transparency and accountability of spend for management and aligns with the general practice in the rest of the group and, just to emphasise, there is no impact on the overall group results.

In LGC operating profit increased 13% to £363 million. Within this the direct investment portfolio delivered operating profit of £217 million, up 15%, with affordable housing delivering a profit in its first year of operation and existing assets performing well.

Our diversified direct investment portfolio now stands at £2.9 billion of 22% as we added 0.5 billion of new investments during the year across housing, future cities and SME finance. Profit before tax was up more significantly at £454 million driven by the relatively performance of the internationally diversified portfolio of equities.

Now moving on to our protection division, LGI, operating profit was up 2% to £314 million with the UK and US businesses collectively delivering stable growth and margins in highly competitive markets. The decrease in UK reported profits was largely due to a change in intra-group reinsurance of the US business, as previously flagged.

Consequently operating profit in the US was up £29 million to 91 million, primarily due to the same reinsurance change and a reserve release following improvements to the recently adopted IFRS methodology. This was partially offset by adverse mortality in line with experience across the broader US life sector.

Total gross premiums were up 6% to £2.7 billion. The business continues to grow at good levels of profitability with Solvency II new business value up 5% to £216 million. Looking forward we expect continued stable earnings and premium growth in our leading UK and US businesses as we invest in technology, enhance our product offerings and strengthen our distribution relationships.

Moving on to our capital position, at the end of 2019 the group's Solvency II surplus stood at £7.3 billion and our coverage ratio was 184%. Despite recent market volatility our balance sheet remains well-capitalised and resilient. As at the end of February the coverage ratio was estimated at 174%.

We have consistently demonstrated a rigorous approach to risk and capital management. Since 2016 it is worth noting we have maintained solvency while paying a progressive dividend, investing in new PRT and navigating market volatility. We have bridged the Solvency II surplus to help explain the movement during the year.

As we've said, operational surplus generation from the back book was 1.6 billion. There were a number of well-understood movements as well during the year. Among them the non-economic impact of lower interest rates on the valuation of our balance sheet was largely offset by positive equity market returns and other market movements and the mortality release, model refinements and management actions led to positive operating variances.

Net surplus generation was £1 billion even allowing for record new annuity volumes. We will of course remain disciplined in the deployment of our surplus capital to ensure we meet or exceed our return targets and remain within our risk tolerances.

So to conclude, we achieved record PRT volumes and asset management flows in 2019 with all our businesses producing a good financial performance and double-digit growth in key group metrics. Notwithstanding volatile markets we have a strong and robust balance sheet and this remains the case.

OSG and earnings continue to grow attractively as we execute, giving us optionality to invest in new business. The synergies between our businesses are a unique source of competitive advantage and we have again achieved a return on equity of around 20%. Thank you. I'll now hand back to Nigel.

Nigel: Thank you, Jeff. Turning now to our outlook, we will remain focused on delivering inclusive capitalism, economic impact, commercial success and the socially useful outcomes which give us long-term sustainability. These are not new themes for us. For example Sacha and his team have been long-term pioneers of stewardship, active engagements and ESG investment.

Our thinking is now becoming mainstream. Equally we have led in creating real asset investment outside London, a process now known in government as levelling up. We've invested in 15 cities to date including Edinburgh, Newcastle, Leeds, Salford, Manchester, Bristol, Cardiff with many more to follow and more than any other institution we've responded commercially to the ageing demographic.

Having led the process of change in many areas - and we are delighted others are following - we will accelerate our pace of change. Our six macro growth drivers are more relevant today than they have ever been. Markets are coming to us. The ageing demographic almost everywhere illustrates the scale of market opportunities. If retirees globally were a country it would be the third-largest economy in the world behind the US and China.

PRT and individual decumulation markets will continue to grow and in the US we are growing our capacity to execute larger PRT transactions. Across the markets where we operate there are more than five trillion of DB liabilities. LGIM has just 1.7% of global market share for AUM.

In 2018 total global AUM was $74 trillion and is forecast to grow to 101 trillion by 2023. The UK DC total market AUM is expected to more than double to 955 billion by 2028. The switch to DC is key to UK welfare reform and we have built quality products and a trusted workplace brand with more than 90 billion of AUM.

The next step will be to enable better investment outcomes for millions of ordinary pension savers including modest allocations to new asset classes such as infrastructure, build-to-rent housing and venture capital. Decades of underinvesting in the real economy need correcting and we are in a strong position in UK in housing and urban regeneration, infrastructure and climate change.

CALA Homes now have revenues of over £1 billion; that's four times the size when we first invested and we're growing fast across other housing tenures; affordable housing, later life living and build-to-rent. Westminster may have only just discovered the north but we're already the people who know how to invest there and in the midlands and in the west and in Wales and indeed in Scotland so we are perfectly positioned to leverage the expected expansion of public capital spending.

Technology will continue to drive market evolution and we continue to make strides with digital and with data, for example in protection but also the retail products like Salary Finance, intermediated mortgages and surveying.

We've added climate change as a growth driver. Climate change will simply be the defining financial challenge of our generation with huge investment, capex, ESG and stewardship opportunities as well as risk management challenges for the whole sector. I will return to this topic with a later slide but as Mark Carney has made clear, there will be both financial winners and losers. We intend to be the winners.

This slide illustrates the strong growth and growing scale of PRT markets in the UK and the US - £40 billion and £30 billion markets in 2019 respectively - but equally the fact that in both cases 90% of the DB markets remain on corporate balance sheets.

Market leadership in global PRT requires several characteristics which Legal & General already possesses: actuarial and longevity expertise, asset management skill, the capacity to source attractive, regulatory-compliant real assets like our £4 billion investment in the world's leading university in Oxford and the ability to execute and administer large schemes.

We also have the ability to work with the schemes on a derisking journey through LDI and potentially innovative capital-light solutions towards full buy-out as our recent AIB transaction illustrated. This is solving the issue that consolidators are trying to address.

This slide is a new disclosure enabling you to see the strongest growth areas by product, by geography and by channel as we diversify LGIM's expansion and lean into globalising asset markets and growth. Compound growth in the high 20 and 30% ranges in multi-assets, the US, Europe, UK DC and through international channels illustrates the increasing breadth and depth of our coverage and our ability to win mandates.

LGIM is more diversified than is generally recognised. Index at only 404 billion is a third of our AUM. LDI is an obvious step, as Jeff highlighted, on the path to buy-out and indeed the majority of our PRT business comes from existing clients; 60%-plus by number and 90%-plus by volume in 2019.

Multi-asset funds are aligned to grow with the expected growth of DC and more than 90% of our AUM is external. We have 100 billion of internal funds, mostly annuities or nearly 80 billion excluding mature savings which is shortly to be sold. That's only 7% of total AUM.

Kerrigan has updated you on LGC's growth at recent results presentations. The division continues to make strong progress, now with 2.9 billion in diversified direct investments and it's on track to achieve five billion in the next three to five years.

We are building a number of alternative asset businesses across three broad asset classes: future cities, housing and SME financing. In housing for example we have a diverse range of businesses which provide solutions by life stage, by affordability and by tenure. These include affordable homes, later life living and build-to-rent.

Our alternative asset businesses are at various stages of profit maturity as shown on the slide and therefore have significant future growth potential. We're also building them to attract LGR funding and third-party capital. This year, as we said earlier, we are formally adding climate, specifically the challenge of addressing climate change, to our strategic growth drivers.

This is where our combination of profit and purpose can combine to the greatest effect and where we can mobilise the skill and enthusiasm of our best people to produce inspiring results. As you will see when we publish our TCFD report next week we start from a strong base and are making real progress.

Among the scale players LGIM is rated as a leader in ESG investing. We haven't just discovered this. We were pioneers in the field, in the E and the S and the G, and we're further strengthening our analytical and product capability but also where we invest our own assets as a principal we are using the investment capability of LGC to back new technologies; for example in photovoltaics, electric vehicle charging and upstream energy management.

We'll also set new market-leading carbon standards for the housebuilding industry, for our housing businesses. Transitioning power generation from hydrocarbons to renewables like on or offshore wind involves a transition from opex models to capex models. The cost is up-front and the investment is long-term. This is highly suitable for debt capital market financing and where the technology is established and the economics proven, as in wind, highly suitable for LGR's annuity portfolio.

We have already 1.3 billion of renewable energy assets in the portfolio but all of us, institutions and individuals, have to step up. What the finance sector has done collectively so far has not slowed the pace of global warming. We all fall a long way short.

The stakes are high for the planet but also for business and the financial sector. Addressing climate change is therefore the next consistent step in the delivery of inclusive capitalism. Our track record since 2011 is very strong. From 2011 to 2015 we delivered 10% annual growth in EPS. Then we set out our ambition for replicating that growth from 2015 to 2020.

We have achieved the current goal in four years, not five. Our growth in operating profit, ROE, EPS and DPS and book value has been achieved through a period of serial changes and challenges. We've had Solvency II, pension freedom, low-for- longer rates, Brexit and various political instability but despite concerns around each of these at the time none of them have dented our ability to deliver good business or eroded customers' trust in our brand.

Legal & General has shown itself to be not just a highly resilient business but one that is quick to adapt, to change and to evolve. The latest challenge is now coronavirus. So far there's been no direct effect on our business. Our exposure to the most exposed sectors is very small and our balance sheet, as Jeff has explained, is strong.

We have ridden through previous challenges precisely because of the consistent relevance and application of our strategic macro drivers of growth and the capacity of our people to execute that strategy effectively. This remains the case today.

Despite the effect of the virus on markets we are now emerging into a period of greater political stability in the UK and the government's economic and policy direction as well as markets and public sentiment are increasingly aligned to the inclusive capitalism programme we have been pursuing for almost a decade.

Having done five years' work in four years we do not intend to spend the next year resting on our laurels or coasting. In the autumn we will set our our ambition for the next phase of our development for you. Headlines will include how we intend to build on our global leadership in pension derisking for corporate clients and retirement income revision for retail customers, how we accelerate the deployment of patient capital to improve the built environment, investing in our cities and infrastructure, how we grow, diversif and modernise to become a world-class global asset manager and how we deploy data and digital technology across our whole insurance and investment infrastructure.

In summary, how we build on our established strengths to become more international, more technology-focused and most importantly how we will rise to the challenge of the era; financial transition to low carbon and delivering inclusive capitalism. Jeff and I are now very happy to take questions and as usual our senior management team is here to pick up the really difficult ones.

I'm going to start from the front this time, Andy.

Andy Sinclair: Thanks. It's Andy Sinclair from BofA Securities; three from me as usual if that's okay. Firstly on LGIM, you've given some pretty constant outlook on the flows pipeline for the US for 2020. I just wanted you to give us a bit more colour on what you're seeing in the pipeline, what's in the mix and what that could do for the cost/income ratio as well.

Secondly I realise you've given a Solvency II number as at 28th February but I just wonder if you could confirm after recent market movements in the last few days that you're still above 170 and give some more colour.

Thirdly was on the annuity book; you've talked in the past about that book becoming self-sustaining in that 80 to 100 billion range. You're now at 76 so getting close. I wonder if you could give some colour on the uplift to cash and organic capital generation as you get towards that level.

Nigel: Okay, I'll take the first one and Jeff'll take the second and third ones. I'm not going to try and steal Michelle's thunder, to be fair. She'd love to be in here today but sadly she had a very serious skiing accident so she's not with us to answer that question.

We try to use a couple of slides to give you the direction of travel that we're going in. Clearly we're delighted with the success that we've had in Japan, breaking into China and we continue to have great success in the United States. I think the new asset classes that we've been entering into, the real assets, are going to help LGIM and will help drive more revenue and more profits going forward.

We're very happy with multi-assets and the way that's aligned with the DC business. Clearly LGR is a great driver as well for LGIM; the bigger it gets the higher-quality and the longer the returns, longer the revenue streams that LGIM receives so we're very happy with that.

I think the cost/income ratio has risen, as you pointed out, for two reasons. I think underlying costs have risen in the business and they've been a little bit ahead of where we've expected and Michelle will address that when she presents. As Jeff mentions, we've still been investing in the business to create this global business and expect that investment to continue over the next two to three years. Jeff, do you want to take two and three?

Jeff: Yes. It really is the hot seat. That's why I sat over there. Solvency II now; even with the most recent movements you're talking a one, 2% movement so we're well over 170. We continue to monitor it. There are many offsetting impacts - equity, rates, spreads, inflation - so they all are in the mix around that. It's never as simple, as you all know, as just following our sensitivities but yes, we're comfortable with that, we're in a strong position and we monitor it regularly.

Yes, annuity self-sustaining; I have talked about this quite a bit. That definitely stands but was borne out by our planning. When you're at certainly 90, 100 billion portfolio then that business covers the strain for sensible levels of volume in line with our ambition of 40 to 50 billion and also covers its contribution to the dividend.

So that is something we're aiming at with that 40 to 50 billion and we'll give more detail of that probably in the capital markets day so we'll share more on what it looks like, some of the dynamics, etc.

Andrew Green: It's Andrew Green. Can I ask three questions, one slightly indelicate? Firstly LGIM; when are you going to reaffirm the eight to 10% growth target which was mentioned a couple of years ago?

Following up on that question, Jeff, or the last question, when you talk about covering the strain and its contribution to the dividend what are you talking about in your business strain, is that at 100% or something like 150% and what is the contribution to the dividend?

Then thirdly the indelicate one; your base mortality improvement was about a 1% improvement. With coronavirus are you doing any scenario testing or can you give us any scenario testing for potentially what that could do? Because certainly the death rate of the older ages is a lot more than at the younger ages.

Nigel: I'll say a little bit on the last question and... I think, to be fair to Michelle, she's not here today and I think she's got a very long and worthy presentation which you're all going to get at some point when she's back to work where she will go through the whole strategy for LGIM.

On the whole issue it is quite interesting from a social point of view that we've been talking a lot about people dying earlier than expected and in our cities and towns across the UK typically in the poorest areas people die at 58 and in the richer areas about 85 and we've had very little social concern or much debate about that in the last 20, 30 years.

But coronavirus has resulted in us getting hugely interested in this particular topic and we've agreed an enormous and, I think, the largest private-sector partnership with Edinburgh University to do a huge amount of research on this very important topic, as to why people are dying much quicker than we all expected. Indeed all of my brilliant actuaries that sit in this room got that one wrong.

I'll let Jeff answer the really technical questions that you asked as well, Andrew.

Jeff: Yes, the self-sustaining point; that is not at the 4% level; that is holding a sensible solvency ratio and so that's what we factor in there; that is fully financing itself and equally on the dividend it's our own current projections on the contribution, what it has been historically, what that business has been contributing via LGAS and our views on how we want that to grow over time.

Obviously there's a whole load of variables; what level of strain, what mix of business, what volumes and that's why we will need to give a bit more colour in a future presentation.

Oliver Steel: Oliver Steel, Deutsche Bank. The slide, Jeff, you showed, the solvency ratio over the last four years holding pretty steady or actually, I think, even moving up slightly over that period; that has benefited in the last few years from a number of disposals, quite a lot of management actions and, I suppose, linked to the question that has been asked already about the self-sustainability of the annuity book, you're talking hear about 40 to 50 billion over five years, which would actually imply slowing growth in the annuity book.

So I'm just wondering, should we then assume slowing growth in that respect or do you have levers to pull that can enable you to go faster than that 40 to 50 billion? That's question one. Sorry, they're long.

Nigel: I might get Laura to talk about the growth of the annuity book and Jeff can pick up on the technical points that you raised.

Laura: We certainly see the pipeline in the UK and US meaning that we can have a very safe target of 45 to 50 billion. I will let Jeff comment on what other levers we have to pull to go above that level but the market certainly is there in our two core markets. Our pipeline in the Canadian market is also growing, which we haven't factored into that 45 to 50.

Nigel: She's doing a me; the 50 went from 45 to 50 without anybody batting an eyelid. I've been doing that for years with the board but sadly we've got a chairman now who notices those things and says, that wasn't quite what you said at the last meeting, Nigel. Jeff.

Jeff: Yes, as I've said many times we always have a wide range of management actions. We certainly have levers to pull. They take many, many different forms whether they're the model refinements, etc, that we see but more substantially partnerships, temporary capital provision from people who are very happy to give a third-party capital reassurance arrangement.

We have some quite innovative reinsurance structures that give us temporary financing at pretty low cost of capital so there's always no shortage of parties wanting to talk to us and no shortage of brains to put together those structures so we're comfortable we can allow those different volumes.

Oliver Steel: Can I ask my second question?

Nigel: You've not got three, have you?

Oliver Steel: No, I'm going to cut it down to two. The second question is, you've said again that interest rates are economically not that important even though they affect your solvency ratio. Given that the share price panics every time bond yields fall can you talk us through what impact lower bond yields really have in practice? If it's not the Solvency II ratio that matters for you what does matter?

Nigel: I think people have always been concerned about defaults and for many, many years that was the discussion here; what're the defaults going to be, what's going to arise in the economy? Now we've had many years of no defaults and, as Jeff said, we've only had 25 million since 2007 and the provision's now 3.2 billion. That's sort of disappeared from everyone's economic understanding but it hasn't changed the sentiment or perception.

When rates or credit spreads move around our share price seems to move disproportionately and I suspect that's not through buying and selling by people; that's much more by algorithms and I think we all have to get used to the algorithmic trading world in which we live now. When you go to your own rooms there're very few people compared to what there were ten or 12 years ago.

So I think that perception hopefully over time will diminish and to a certain extent no matter what we've said about it and what empirical evidence we've produced to it.

The second important thing about our business model which people forget is we encourage people not to own DD assets. We have a system in which in effect LGIM trades out of assets if they think they're going to go down to DD because we don't want to lose that reputation that we've got for outstanding credit management.

So we hold a lot of very good-quality BBB assets but very, very few DD assets and to get to be held as a DD asset you've got to have a pretty good prospect of getting upgraded again. Tesco would be a very good example of that when they got downgraded to DD we held on to quite a large part of our Tesco holdings because we had a lot of confidence in the management that they could get the credit rating back up.

Simon can go into - because he's been involved with this for many years - the details of how we've set that up and managed it, I think, very successfully over the last ten years. Kerrigan was around ten years ago as well when we were thinking through what was the best way to avoid to jump to default types of situations. Do you want to pick up the economic stuff, Jeff, if there's anything else?

Jeff: Yes, it's more reiterating; the rate itself doesn't do anything. It's discount in a very, very, very long liability; you get some risk margin impact; the SCR simply gets bigger. We have the same pound sterling the day after as we had the day before to pay the claims. The ratio, as you know, is reasonably sensitive therefore but actually the total surplus doesn't change that much in the grand scheme of things.

Jeff: No, because they've run off an IFRS model. It doesn't have much impact to that. It's much slower over time so we don't really see that. It's the same as the non-economic effect; it's simply the accounting on the term life business where you see that coming through in the investment variance. We don't lose any money economically, we don't pay anything out of the door when those rates go down.

John Hopkin: Thank you. Morning. John Hocking for Morgan Stanley. Three questions, please. On LGI, Jeff, you mentioned you've had this sort of investment variance because of rates. I wonder if you could give us an update given what's happened to the US curve recently. Given what you've just said I'm presuming that's a linear impact rather than anything which is geared.

The second question; on your Solvency II sensitivities we've still got curiosity for the sector where the annuity companies have got a positive solvency impact when spreads widen. We've had about a 25bps move, I suppose, in credit spreads; your sensitivity of 100bps. What would we actually have to see in spread-widening before you'd actually see a negative impact on solvency?

Then finally the EOPA risk margin changes which came out a day or so ago which look like tapering the risk margin for long durations; have you had a chance to look at that? If something does change the risk margin is that just a wash for the transitionals or is there any economic benefit to you? Thank you.

Nigel: I'm going to ask Simon or Tim to take the third question and Jeff can take the first two questions.

[Asides]

Tim Stedman: Yes, the risk margin change we would expect to wash through the transitional. The impact is helpful but probably not quite as much as we would have hoped. I'm not sure it's necessarily going to change the economics for the annuity business and reinsurance will still be a preferred option.

Jeff: Yes, it's relatively small as set out. First on the IV, yes, it's reasonably linear, especially on Bernie's business, possibly even slightly dampened from linear in the US because they hold some assets to back it whereas Bernie doesn't have any at all.

The S2 spread; yes, we show the sensitivity. You'd have to go well beyond that. I'd say there isn't a simple answer because it depends; the dispersion between A, BBB, BB and what we've already seen or assumed for downgrades at that point so it would be wrong to try and give an answer to that. Tim can talk you through some of the dynamics if you like because we look at it constantly; how do those sensitivities hold up?

Or we present them to try and give the clearest picture we can within a sensible range of movement. Obviously if we ever get beyond that we'll update the market if we thought it wasn't appropriate to use them.

Abid Hussein: Morning. It's Abid Hussein from Credit Suisse. Just two questions please if I can. Firstly on assumption changes can you talk to the 390 million valuation change that's coming through the LGR operating profit numbers? I think part of it is the move to the CMI17 tables but there's a larger part due to the move in base tables and I want to understand, to what extent can we assume that's repeatable going forwards if you can help us in terms of thinking around there please.

Then related to that the second question is on the mortality reserve release outlook. Previously you got 200 million. It's a little bit weaker, I guess, in light of the latest CMI19 projections. Are you giving any more guidance going forward?

Nigel: Jeff, do you want to have a go at it?

Jeff: Sure, yes. You're right; the experience of the assumption changes in LGR is a combination of the 155 we talk about so it's close to 200 million for the base table change. That is almost entirely mechanical. We've said before, we set our base table assumptions based on a rolling five-year average. We don't like to put too much weight on the most recent experience.

Clearly we were bringing in 2018 when we did that calculation and therefore dropping off 2013 and you all know that there was heavier mortality in 2018 so therefore that flows through. That's why it's characterised as a sort of business as usual. We did the same the previous year; it was less of a move. It depends what you see.

You can already tell 2019 and 2014 were quite similar so you won't see so much. We'll see what happens in 2020 and how that compares to 2015 so it's very much a rolling average with judgement obviously of how is it appropriate, what are we seeing in our own book of lives, how do we think things are changing but it's that base assumption set in a reasonably mechanical way which is why it falls there.

The one with more judgement is the trend because none if us know what's going to happen in the future and so we're not going to guide yet on the number. There's a lot of work being done on that. We definitely benefit from being a year behind so we have now seen what 2019 does again mechanically to that table.

It's a small change; I think it's about a month's extension to the life expectancy so we're in a strong position of being able to look at 18 and 19 and by the time we set our bases have a pretty good view on what's happened in 20 as well and therefore be able to reflect all of that and certainly therefore make sure we're never overshooting without doing something wrong. We're able to see almost three years of tables into the future from where we are so we'll give an update around the half year when we'll have developed our thinking and we'll have some idea as well what's playing out in 2020.

Greg Patterson: Hello. Greg Patterson, KBW. Three quick questions; one is, you mentioned you invested in structuring and we've got this example of this assured payment policy. Obviously when you bring in third parties to help with the financing you give away a portion of profits. I was wondering how as we increasingly bring in third-party financiers the PV new business premium margin would progress over time.

Second question; we noted that the lifetime mortgages have come quite dramatic - the sales of them have slowed; increased competition. That is a unique duration. I was wondering why we haven't really seen any impact from the margin in annuities also on the PV new business premium given that we've seen a reduction in lifetime mortgages.

Third, I wonder if you could upgrade on the downgrade situation; have you had any downgrades this year, what's the prospect for downgrades in 2020? Because obviously that's the key issue with your Solvency II ratio.

Nigel: Okay. Laura, do you want to answer the first, Chris the second and I'll do the third.

Laura: The APP policy, Greg, is actually an insurance policy covering, as Jeff said, all market risk of a particular part of a pension scheme. So in that particular example we haven't brought any other third-party financing in. It's quite a neat way, as Nigel said, of finding one of our solutions to the dilemma that the consolidators are trying to address so that there's a go-to capital-light solution for us where we didn't pass any of the financing or profits to anybody else.

Jeff: Yes, on the third party build-to-rent would be another example where PGGM are our partner in the development phase, who've got a lot of expertise through all their continental efforts in build-to-rent. We will be using LGR to provide the debt financing for that increasingly on a go-forward basis and LGIM also have an investment product open to lots of different institutions to invest in build-to-rent, many of whom don't want to be involved in the development phase but actually do want to hold on to the assets over the longer term.

We view that as a big asset opportunity. The equity for that; initial equity provided by LGC and PGGM; long-term equity provided by LGIM's clients and a proportion of the long-term financing is provided by LGR.

Jeff mentioned in his presentation; that's kind of how it works; affordable housing is very similar and I suspect later life living is going to go down the same route where we create these new asset classes through a combination of third-party equity, our own equity funded from both the annuity businesses and a mixture of LGC, LGR and LGIM. These are the sweet spots for us to invest in. Do you want to talk a little bit on lifetime mortgages, Chris?

Nigel: I think, as we've mentioned, lots of other third parties want to provide capital in different forms to this market and we've got lots of innovative solutions. I think we all agree, the size of the market is so big relative to our balance sheet we have to come up with innovative solutions that solve the problems for clients but also solve the issue for our balance sheet. The number of solutions and the innovation that our team has shown in developing those solutions has been incredibly high and I think each time we sit up and present Laura'll have yet another interesting structure for us to talk about.

Chris: Thanks. On lifetime mortgages, we could see from about Q2 onwards last year it was a soft market and for us volume is not the be-all and end-all, as the chairman reminds me on a monthly basis. We can also see from the market that we're achieving structurally higher margins than our competitors and that in itself of course feeds into annuity pricing and margins so that would have been supportive in the round on margins.

I think while other people are dipping into and out of the market our focus is building a long-term, sustainable business that balances in the right way between risk and margin and customer value. That's our focus.

Nigel: Any downgrades? No. The only interesting thing, I think, that's happened is in the BBB market in the United States where we've seen two trends. One is that self-help by a lot of the players including GE, AT&T and that's proving to result in some upgrades in the United States. The downgrade has been Kraft Heinz who, as you know, didn't execute on their plan and fell behind in terms of their plan but downgraded and their share price reacted very negatively to that, which we thought actually in the round was quite a positive outcome for us as a firm and we've had no other major events.

Johnny Vo: It's Johnny Vo from Goldman Sachs. Just a couple of questions. I guess the trend in your asset portfolio's been pretty clear; there's been a great proportion of internally rated bonds, which has obviously supported the business, but also there's a notable increase in BBB so could you just talk about the general trends? It's gone from 30% to 33 so if you could just talk about the trends there and certainly if there's a dislocation of the market should we see a change between the internal-rated sort of bonds to more liquid credit within your portfolio? That's the first question.

The second question is in terms of the MA. I think at the half year you had an MA spread of around 121bps. It's 110. Is that just driven by spreads in the market or was that a portfolio shift? Second thing; could you tell me what the MA spread is currently if you have that available?

The final thing is just in regard to treasury assets; it's declined by about 500 million. I guess Legal & General Finance has that liquidity position. Has some money been injected in some businesses or investments elsewhere if you can talk about that? Thank you.

Nigel: Yes, the third one Kerrigan will talk a little bit about, what we've actually used the money for. Most of the money is actually being given to Kerrigan for a number of start-up businesses. He can talk about that. Jeff, do you want to take the second one and I'll answer the first one?

Jeff: Yes, you're right; spreads came in and therefore the matching adjustment went down. Spreads have gone out since then so it'll be a bit higher. I don't have the exact number. I suspect Tim doesn't even have the exact number but you can know that it basically moves in the same way. The deduction doesn't change the fundamental spread so an average bond portfolio; add it on to the 110. Nothing much will have changed since the year end otherwise.

Nigel: Yes, the long-term trend in the amount of BBB that we have is about the same. Some of the BBB is actually assets under construction which are going to become AA assets. A lot of the government stuff is actually assets that we're constructing for them which'll get rated BBB. That's the only delta really from portfolio changes.

Johnny Vo: Thank you.

Nigel: Sorry, Kerrigan, I forgot.

Kerrigan: Yes, just on the treasury assets, the overall cash position for the group really, 2.5, two billion-ish cash; we've got plenty of cash there. We're always looking for interesting investment opportunities at the right time to invest so many pluses and minuses in that figure but the net 500 million or so invested across our portfolios of data centres, pod point at the start of the year and then later in the year things like the affordable homes business and later living really are interesting areas in which to put money in the ground and then things came out...

Nigel: Do you want to say a little bit more about the affordable home business and how excited we are about the prospects?

Kerrigan: Yes. A really, really interesting business for affordable homes that, I think, really brings to life a lot of what we're doing on inclusive capitalism. It's a very simple model of plenty of pension money looking for a home and plenty of affordable homes needing to be built. They pay CPI-linked rent, which is fantastic to back pension risk transfer deals so with that simple model we've set up over the course of the year this ability to use pension money now invested in this business to create these affordable homes and create a great commercial outcome for people here and also a great social outcome in terms of more affordable homes.

Nigel: It's about - what? - 1,000 homes this year.

Kerrigan: Yes, 1,000 homes this year, rapidly growing to 3,000 homes, 750 million pretty much in the pipeline in terms of those homes and we think we can scale this up commercially pretty quickly so we're very excited.

Nigel: Yes, and we think these are points of differentiation between us and the competition.

Colm Kelly: Thanks. Colm Kelly, UBS. Just on the LGAS solvency ratio I wonder if you'd mind giving an update on even a broad range around that given it's a high proportion of the cashflow. Then secondly on the subsidiary dividend from LGAS, it's fallen 10% year on year now. It remains at a healthy level and clearly these things are not linear so I'm just wondering what the decision-making behind that was. Do you remain confident in the ability to grow the remittance from LGAS in line with the strong growth in your two new business volumes? Thank you.

Nigel: Yes, there isn't really a target for the internal dividends on a year-to-year basis and we're basically using it to pay the external dividend. At one point a few years ago we used to dividend a lot more up of it and we have done that less. We are to a certain extent investing some of that in some of the areas that LGAS uses and the LGAS balance sheet is about 20% less, the solvency ratio, than the group balance sheet. It seems to hover at about that level; it might go up or down a couple of percent either way.

Ash: Yes, this is Ashik Musaddi from JP Morgan. Just one question; your five-year charts are pretty interesting but it also shows a clear trend that there is the straight line of growth in annuities and related business like LGC, which I would say is capital-backing annuities.

But if we think about asset management, LGI, it is not growing as fast as that so if I fast-forward five years I think your annuities business will be 80% of the group. How do you think about diversification benefit that is captured in Solvency II if you keep moving one business much faster than others? Do you think that you'll be losing diversification benefit, is it already captured in the past five years, how it has moved or are the diversification benefits still accounted at the same level which they were two or three years back?

Nigel: Yes.

Ash: Thank you.

Nigel: I think I'm going to let Bernie give you a little prequel of his presentation later in the year on what we're going to do to accelerate the growth of LGI because you're right; we get a very good diversification benefit of it. It would be very beneficial to us if Bernie could grow a little bit quicker and here's how he's going to do it.

Bernie: Here's how our one-to-ones go.

Nigel: That's an upbeat one.

Bernie: Yes. I'm in the privileged position of being able to focus on growth; also in a great position of being really strong in several markets it it is mathematically harder when you're at 24% market share to be delivering the growth. The good news is we've got great positions in the US protection business where we've got a business at scale but with plenty of growth potential. Their market share is three, 4% and so it's got plenty of room to grow there.

I spend a lot of my time focused on how we get that US business growing faster and the great news there; we've got lots of technology developments just going into the market now, being really well-received and we're really hopeful for that to lead to even faster growth from our US business.

The other trend and theme is technology investment in fintech and so investments like in salary finance; it's really closely aligned with what we do as a business. It's got a great social purpose, re [?] financial world being via employers and it's been going well and we've got great hopes for that going forward. So that's a business we can help to grow and really is great synergies in the workplace, both within the LGIM workplace, our own group protection benefits business as well.

So yes, we've got plenty of growth to look at. I have to say, we benefit enormously in LGI from a fantastic diversification benefit from annuities and it is a truly synergistic capital position. We're trying to grow as fast as we can but with all the usual caveats around ensuring we're optimising things and doing it in a really balanced way.

Nigel: Yes. There are a couple of comments I should have on that and I think the first one is each of the businesses have these adjacencies - Kerrigan mentioned the likes of pod point which exist there. Chris has got some care business which people don't know very much about. Bernie's got salary finance and a whole bunch of other things. When we come to November we'll talk a lot more about those sorts of things which will help accelerate the growth.

We all, I think, share the feeling that our US businesses, all three of our US businesses could grow a lot quicker. We've been very measured in our expansion; get the right people, get the right systems, get the right technology, build a brand and that's been really successful for us.

I wouldn't quite agree with the point you made about LGC's fortunes being totally tied to LGR. I think there's a lot of great things that LGC is doing outside of LGR. Yes, there's a big synergy with LGR but there're a lot of very exciting things that you'll hear more about and in fact there'll be a lot of releases about that during the course of this year. Two more questions. I think there're three hands up - two.

Dominic: Thanks. Dominic O'Mahony, Exane BNP Paribas. I'm afraid I've got a few more questions on bulks if that's all right. The first is in terms of the result in 19, it looks as if new business margins on an IFRS basis were slightly higher than expectations and maybe strain was slightly higher. I think that's consistent with insuring younger populations; tell me if I'm wrong. Is that a trend we're going to see? Presumably younger populations' value creation per pound of premium over the lifetime is higher.

Second question; you've very helpfully given some targets for growth in that business; 40 to 50 billion over the next few years. You also showed us that you actually think the UK market will grow in 2020. If you maintain your share of that then actually that suggests quite a large decline in 2021 and beyond. Are you hiding your light under a bushel, as people say in this business? Thank you.

Nigel: I've never knowingly hidden my light under a bushel... and I'm not dull but worthy either, which is the other headline that I seem to get associated with, courtesy of Mr Godfrey. Do you want to take the first question there, Laura?

Laura: Yes. Thank you, Dom. I think it's easy to read too much into the slight change in both the IFRS margin and the strain. I think on balance we definitely did one large deal last year with slightly shorter lives but we also did some longer-duration deals as well so probably in balance there wasn't a huge change from 2018.

There was very slightly less inflation, which we talked about this time last year. I think we do aim to keep relatively steady on both those two metrics and write business that means that we keep relatively steady on both of them and therefore work through reinsurance and other things to make that happen.

It's a hugely exciting market for us. We have a really good, strong, steady pipeline. We've mentioned we have been able to write larger deals in the US last year as our balance sheet size has grown and we are starting in Canada. It wasn't actually on the slide but that is a CDN$1 trillion market and only, I think, 5% of that market has gone to insurers so far and it is increasing in terms of the overall levels that are going to insurers.

We have, as was clear on the slide, a partnership with Brookfield where currently we're reinsuring and a good, strong pipeline with them for the start of this year.

Nigel: Thank you. Last question.

Andrew Baker: Hi. Andrew Baker, Citi. Just two questions, please; first on the risk margin. Previously the PRA has expressed the concern about the amount of longevity that's being offshored. With the potential change to the risk margin it doesn't sound as if you're changing your view on whether you would use reinsurance. Is there a potential risk that the PRA will change their view on how much they are comfortable with across the industry? That's first.

Then second one on mature savings; there's obviously been a delay to that close. Is that specific to the part seven transfer and what's going on there, please? Thanks.

Nigel: On the risk margin we have a meeting with Sam Woods on Monday so I'll ask him that question myself and see what he has to say about it. It's one we've been asking for a long period of time. As you rightly point out, there's a trade-off between how they adjust it and the amount of longevity that's taken in the UK. Our preference would be for us to take more longevity in the UK. We've always said that but unless they move the terms and they move them slightly independently of what EOPA is suggesting that's unlikely to happen. I don't know whether there's anything you want to add.

Jeff: No. That's right. I think that last point is the most relevant; this is very much an EOPA consultation that's put out which may not involve trade-offs against other items within there. It's not necessarily where the PRA's thinking is on this margin and not reflective of the discussions we have around that. They have the drivers that you talk about and who knows what flexibility there may or not be in the post-Brexit world.

Nigel: Thank you. We'll all be around for a bit afterwards to answer any further questions that anybody has. I'd just like to say a big thank you for all of your support, all of your very detailed questions which amazingly you've managed to conjure up in the few hours since the release came out. We thank you for your enthusiasm for all of that. We'll be seeing you at least twice during the year when we do the half year results and our capital markets day in November.

A big thank you to all my colleagues here for answering the questions today but for delivering a stellar set of results in 2019. Let's hope we can do something similar in 2020. Thank you.