Transcript

Legal and General Half Year Results **Wednesday, 04 August 2021**

Nigel Wilson Thank you. And thank all of you for joining the call today. Thank you indeed for the speed at which several of you managed to get out supportive notes this morning. Jeff, myself and all of the team here at Legal and General are delighted with our results, a very strong performance in operating profit at a group level.

But we're also delighted with the performance of all of our divisions and even the subdivisions within the divisions. Not only did we perform well in the pandemic, and just from managing our staff, managing our customers and delivering a resilient performance last year which we labelled a pause year, it's great to see us returning to normality in a sense that we're driving forward in earnings per share and, of course, in ROE. Our ROE performance of 22% was outstanding really, when you consider that we're still operating under a pandemic.

We very much believe an investment led growth is the solution to both the UK and the US's economic growth over the long term, and we're playing an ever-increasing role in investing in real assets, creating real growth, real jobs and real wages growth here in the UK.

I guess our capability to scale up businesses is coming through in LGC for the first time materially, and I know one or two of you have been talking to Jeff about that this morning. We've been on that journey for a number of years. We've said this year that LGC would be a breakthrough year. And indeed, that's what we've delivered.

And it was terrific yesterday to sign the deal with the NatWest Group Pension Scheme, where they've become co-investors in our later life business. Why this is strategically important is if you look at our Build to Rent business, the partners there were PGGM, a very prestigious and incredibly well-run Dutch pension scheme.

And we've seen this sort of activity from European pension schemes, but particularly from US and Canadian. We're getting increasingly confident that we'll see the same thing happening here in the UK and that we will play an incredibly big role in getting these partners to help us scale up businesses not just here in the UK but, increasingly, internationally. We are pleased with our performance in the US, in Europe and in Asia, where we're seeing again this sort of scaling up impact that it's having on our results.

I guess our biggest challenge, and it's a shared challenge with all of you, it's a collective challenge really, is how do we get financial services rerated in the UK? We've seen it happen in the United States and we're not the only industry where there's a difference in rating between the US and the UK.

We're hoping, over time, as we continue to deliver outstanding results, that that gap will disappear and that we'll see wider recognition for the quality and the growth of our earnings, going forward. That's all I was going to say by way of introduction. We'd like now to move to questions. And the first question is from Louise Miles at Morgan Stanley. Louise.

Louise Miles So, the LGR new business margin was down versus the first half of 2020. How should we be thinking about the margin for the full year? Should it be similar to the first half or should we be looking at more of the 2020 or 2019 margin?

At LGI, you have about £30 million of that FY20 mortality provision left. Do you have any concerns that this is going to be sufficient, given the outlook for [unclear] debt in the second half? We're hearing that these might be a bit heightened versus previous years.

And then finally, I was having a look at your sensitivity analysis on your Solvency II stresses. On the credit migration stress, this seems to have moved a bit since FY20 compared to the other ones. Is there any particular reason for this or is it nothing to think about? Thanks.

Nigel Wilson I think, Jeff, those are all for you.

Jeff Davies Yes. Yes, thanks, Louise. Yes, LGR new business margin. We know we said we traded very well last year, especially in the first half, around trading credit when spreads were pretty volatile. That helped us with the margin, plus there was probably a bit less competition. Certainly, we were demanding more return on our capital for putting it to work in much more uncertain times.

The level is around, what, 8.4% for Solvency II new business margin, so it's definitely in a normal range for us. So I'd say we'd look to continue to deliver that sort of level of returns, which is really in line with what we've seen in 19 and what we've seen in the first half of this year.

And obviously, as you all know, it does vary a little, depending on the duration of what we write and the exact assets that we're applying at any point in time. And we continue to source very, very good assets and to manufacture those ourselves.

LGI. Yes, there's 30 million left and there was obviously a big impact in Q1 in particular in the US due to COVID. We've followed the same methodology in terms of projecting out the IHME, and we're within that and believe there's a little bit of prudence based on that. Clearly, there's a big range of uncertainty around that.

There is some sense, but with not a huge amount of data, that potentially, any penetration of adverse claims into the insurance market will be slightly less due to some of the socioeconomic impacts. So certainly, we are comfortable with that level of provision going into the second half. And as ever, of course, we don't make any allowance for any potential excess debt in the annuity portfolio, which acts as extra prudence for us.

And the credit migration. No, nothing really to worry about there. That's just the impact of the maths in terms of your starting point, in terms of rates and where spreads are. And that moves the sensitivity. But nothing has changed at all in the underlying portfolio there or the stresses.

Nigel Wilson Okay, thank you, Louise. Thanks for your questions. Next is Larissa.

Larissa Van Deventer Good morning, everybody. A couple of quick questions from our side, please. Two on bulk annuities and then one on LGC. Actually two on LGC, if you don't mind. On bulks, can you help us understand what is currently driving the dynamics and what gives you confidence that the 2H volumes should come through? Related to that basically, do you think there's a lag effect from a COVID shock last year, or are there other factors?

Then the two on LGC. How robust is the pipeline? In which areas are you seeing particularly attractive opportunity? Is it mainly a housing play or are there other areas that are coming through? And then secondly, can you give us some colour, please, on how much of the 250 million in earnings related to mark to market on the evaluation of the portfolio?

Nigel Wilson Yes, thanks for those questions. I'll take the first two and Jeff can take the third one. Just in terms of markets for PRT, we broadly expect the market to be about the same size this year as it was last year. So, there isn't really a macro COVID impact. We're seeing a stronger pipeline in H2, hence the reference in the release to the 2 billion that we've either closed already or are in exclusives for the second half of the year.

We will retain our financial discipline in the second half of the year, as we've always done in previous years. But we're very confident in the long-term size of the market opportunity in the UK, and indeed internationally, for the business. So the numbers that Jeff and I have used in numerous other presentations, the 40 to 50 billion over four to five years, are absolutely the same as they've been over the last few years.

In terms of LGC, it's across the board. We invested in a number of these businesses several years ago. And whether that's in the various housing businesses, the urban regeneration businesses, the energy businesses, the SME finance that's supported in Venture Capital but also in Pemberton, they're all doing incredibly well. They're all performing very strongly.

And we're very confident that they'll continue to perform strongly, even more so because of the third-party capital that we're bringing in at scale into these businesses, which I think is a good thing not just for us and for our shareholders, but actually for the UK economy and elsewhere, that big pension funds and big asset managers want to co-invest alongside us.

We've done a lot of the heavy lifting, built the management team, built the market opportunity and scaled up these businesses, and they're very attractive investment opportunities for other people. Jeff, do you want to take the third question?

Jeff Davies Yes, sure, on the mark to market for the 250. It depends on what you mean by mark to market. The direct investment, the alternatives, those are underpinned by either transactions we've seen or pending transactions we'll be talking about in the second half.

But in terms of the profit there, yes, there's 55 million from the traded portfolio. Clearly that is a pure mark to market and we can't predict what repeats on that, if you like, in the second half. And we wouldn't necessarily expect to see some of the VC continuing to move at the same rate in the second half as the first half, but we'd expect those to keep growing over time.

But Nigel covered it to some extent. The others are good quality operating businesses and underlying businesses with growth. So, CALA, Affordable Housing, Build to Rent, Pemberton. We'll continue to see revenue growth there and sales growth, and those are how we put valuations on that. CALA is real profit at the point we sell a house. That's the only time we get profits coming through. And so, in terms of the second half, we wouldn't double that 250 number, but there are strong underlying businesses we continue to see growing.

Nigel Wilson Yes. If you look at slide 28, you'll see that the traded portfolio delivered 87 million profit in 2020 and 55 in 2021, so that's not been the source of profit growth but it's the really high performance of the businesses. We now pass on to Andy Sinclair.

Andrew Sinclair Thanks, Nigel. Morning, everyone. And completely right, these are good results. The business is clearly in good shape. Three questions from me if that's okay. Firstly, it was on LGR. You talked about this assured payment policy as being your capital light PRT product. Just really wondered if you can tell us a little bit more about how the capital intensity and margins differ versus traditional PRT business.

Secondly, on LGI, I thought there were really good protection sales growth in H1 in both the UK and the US. Just really wondered if you can tell us a bit more about the outlook here. What sort of growth do you think is sustainable?

And third, on LGC, I suppose we're a little bit surprised to see that the LGC investment portfolio AUM seemed to only be around flat, year to date. Just wondered if this is due to investments maturing and being passed on to other parts of the business or what's going on. Just could you give us a little bit more colour here on how the alternatives and traded portfolios have moved, year to date? Thanks.

Nigel Wilson Jeff, do you want to take the first and the third question and I'll take the second?

Jeff Davies Yes, sure. Yes, the APP. As you say, it's capital light. It's really along the way on the journey and it doesn't pass on the longevity risk. It allows schemes to really partake in the direct investments that we put to work on our own LGR portfolio and gets them to buyout sooner.

So we had a good example of that where we'd done a transaction with AIB under APP. And we've now moved to full buyout on that. And so they really exposure to our credit expertise. They transfer that risk to us and we're able to deliver the returns to them that they lock in. And then they eventually move further down the track to that.

So it looks very attractive to us and allows the schemes to move earlier. Clearly, the returns meet all our hurdles. We don't price in any differential way. We put the capital to work and get the returns broadly in line with what we get on the rest of the business. We allow for it in that way.

LGC investment portfolio. Yes, there's nothing particularly going on there. We're expanding the portfolio. It grows. We had reduced the traded portfolio, as Nigel said, in terms of op profits. You could see less reliance on that so that had reduced. But otherwise, no, there was nothing.

And now we look to continue to grow the alternative investments. We give views on where we think that will be. We usually put to work a good few hundred million in any year, whether that's 200, 300, 400, 500 million. And we continue to do that. We continue to transfer from the traded portfolio. So there's nothing particularly going on there.

Nigel Wilson On LGI, thank you, Andy, for your kind words. Over the years, they've not always been so kind about LGI. But Bernie Hickman, Steve Griffiths and the rest of the team, both in the UK and the US, have done an outstanding job, particularly in paying claims sadly during the pandemic. But we did see strong growth in both the UK and the US and we expect it to continue in both the UK and the US.

We're becoming increasingly optimistic about the United States and the progress that we've been making there. And we're strengthening the management team, building out its capabilities as we speak. We think the US market will begin to follow the UK market in that there will be greater use of technology.

It's always been quite a long way behind the UK in terms of use of technology. And the fact that we're technology leaders here in the UK stands us in great stead in the United States. So I'm becoming increasingly confident about our capabilities in the United States to grow the business. Next question is from Colm.

Colm Kelly Thanks, Nigel. So just a first one on LGC. Obviously, strong results today and obviously a lot of emphasis on LGC in the presentation slides, so quite a strong expectation in terms of the future growth, going forward.

If we think about it from a cash flow perspective and particularly upstreaming cash to the group holding company, when we think about LGR, it's a very consistent track record of upstreaming relatively stable cash to the group. Can you just touch on LGC's remittance track record and what we should expect, going forward, in terms of upstreaming capacity there?

And then just secondly on the LGRI business, obviously Laura moving across to LGC. I didn't see anything announced in terms of a successor for the CEO position of LGRI. I'm just wondering if you can update on the process there if that's okay. Thanks.

Nigel Wilson Jeff, do you want to take the first one? I'll take the second one.

Jeff Davies Yes, sure. Hi, Colm. Yes, LGC cash flows. Yes, it's interesting. It's a combination. Clearly, when you revalue a VC portfolio, you don't get the realisation straight away but there's a lot of operating businesses that are real profits and real cash at that point in time. CALA, there's 70 million-plus PBT in the first half. Those are real houses, real completions, money in the door.

And so clearly, in the past few years, we've been investing in the business to grow those. And so we've been helping the portfolio mature and adding our liquid resources into that. But then as those mature, they start to throw off either realisations with third-party money, if it's like NatWest Pension Fund and other examples, or we sell them as they become mature anyway. Or, alternatively, if they're the maturing, yielding type equity, we're happy to move those across into the insurance company, which then moves the liquidity around the business.

So, there's a differing profile across the board. But we do see that as those businesses mature, we see them throwing up a lot more cash than obviously there's been historically, when we've been growing them, through the realisations, through third-party money, and simply businesses like CALA becoming mature operating businesses that pay dividends.

Nigel Wilson Yes. So in big picture terms, Colm, it's just like any normal, regular business, LGR and stuff like that. We've invested in assets. Those are operating assets, and we've helped manufacture those assets. But then they become cash flow producing on a go-forward basis. Similarly with Pemberton and other areas of the business.

On LGRI, yes, I'm pleased to report that actually, Kerrigan has now arrived in Asia. It's taken a while to get there. He's moved from quarantine in Thailand to quarantining in Hong Kong, so that's been a journey. It's been non-trivial, interviewing international candidates, to be fair, during the lockdown period and we've certainly been looking across the world for candidates for the LGRI position.

And as you said, although she's on holiday today but calling in, Laura has just recently taken the reins for LGC. But we're comfortable with where in terms of finding successors in LGRI. Next question is from [sound slip] from Credit Suisse.

Farooq Hanif Hi. It's Farooq Hanif from Credit Suisse. Thanks very much. Just turning again to the APP and ISS, the alternative LGR PRT solutions, can you talk about the pipeline? And do all of these inevitably end up in a buy-in and buyout when they mature?

Second question is you talked about the CMI 19 transition not having an immediate, explicit release, but there being a margin release. Will this be actually equivalent in size to what happened with the CMI 18 experience, for the purposes of our modelling?

And then lastly, on LGC, can you just talk about the profit implications of the third-party capital? So is it simply that you need that 14 billion to get to 5 billion alternative assets? Or is it that you will get realisations which improve cash? Or is there some other margin that you can make on that? Thanks.

Nigel Wilson If Jeff takes the first two and I'll take the third question.

Jeff Davies Sure, yes. Hi, Farooq. Yes, the APP ISS, yes, there's a good, strong pipeline on that. Trustees have lots of responsibilities. They want to understand when they're doing different things. There's been good precedents now in the markets around APP, both third-party or seeing it with our own scheme, etc.

And the ISS, we have a good number of conversations around those. It's interesting. Some of them, you have long conversations about these alternative structures. They suit them at the time along their journey. And then, suddenly, they have a windfall, the markets move, and actually say, do you know what, we can afford a buyout now so let's jump straight to that. And that has happened to us. But they're very useful tools to have along the way.

That almost then answers the second part of your question that yes, if we do our job properly and the schemes manage themselves, they would all eventually be running to buyout. We wouldn't expect people generally to be putting these in place to sit on them forever. And there may be exceptions to that, but they would be looking to buy out.

So we see this as really helpful on that whole de-risking journey. As we say many times, we're the only ones that start all the way at the beginning, in LGIM, and move all the way through, and so we continue to build on that. And about 50% of the cases were from LGIM this time.

Yes, the CMI 19, we were prudent in the way we implemented CMI 18. And we obviously already had the 19 table at the time. We know broadly where that sits. And so we see that being pretty neutral to implement, as neutral as you can be when you've got such a big book and you're dropping in some new tables.

But we have built some prudence in. We think we're conservative, given the uncertain outlook on data for 2020/2021. And so we do anticipate some of that prudence, some of those excess debts flowing through the P&L for the next couple of years, as we've said.

In terms of size, it's very hard to predict. But yes, we'd expect it to be probably in the high tens of millions, which is not dissimilar to the lower end of some of the longevity releases that we've had. We could get as high as 100 million flowing through.

But that will be through P&L as we release these over time, a combination of some of the experience coming through and the prudence released as 20 and 21 data, and what we believe about what's happening in terms of delayed hospital appointments, etc. and treatments come through. And we understand the market and the outlook on mortality a bit better.

Nigel Wilson Okay. On LGC, we have a variety of businesses, some of which are outlined in the pack, which will give you case studies. And as you'll have seen, we're having an investor day in October so we can go through everything in a lot more detail. So this is really just a sampler ahead of that.

But the model is really that we put up equity, we hire a management team for a particular sector. We then invest in the business. And Pemberton is a good example of that, NTR, build to rent, affordable housing, venture capital, data centres, later life living.

And we ultimately look to get fees from alternative asset management platform fees, is the expression that we use in-house, from these activities. So if you take something like Pemberton, of the funds that they have under management, somewhere between 5% and 10% are actually our funds. The rest are from their 120-plus LPs.

And we think this model works incredibly well for us and we can scale it up brilliantly well. And so we've just got to continue repeating that. And data centres is another area that we think we can scale up on a go-forward basis by bringing in further third-party capital.

As Jeff mentioned, we may realise some of that value on a go-forward basis. There's obviously market mutterings around Pod Point, which is one of our many, many, our 300 different investments that we have in starting-to-scale-up businesses. There's huge demand for electric vehicle charging.

We have another business called Onto, which is our electric vehicle leasing business. All of these are being scaled up. And it's demonstrating value, realising value and building revenue from third parties which are all part of the narrative and the economics, going forward. And next question is from Oliver.

Oliver Steel Morning. Excellent results. Well done. The first question is I'm assuming that the guidance you're giving for the full year is off last year's 2Q 1.8 figure. And if that is the case, then it looks as if you have to make somewhere close to 1.4 billion in the second half. And I'm just trying to work out where that is, because if you're only talking about this smoothed release from longevity reserves of maybe 100 million, it's quite hard, well, and particularly if you're seeing LGC being lower in the second half. Where's the delta to that 1.4 billion in the second half?

Second question is on LGIM. I can see an excellent ETF margin on new net inflows. But how does the revenue margin on new flows compare to the 7 BPS or so that you're getting across the book as a whole?

And then thirdly, on LGI, you talk about growth. I'm talking about the UK business. You talk about growth in sales every year and generally you have been growing that business. Virtually almost every year, we also see a decline in the release from operations. And I know that's something to do with caps. But I'm wondering, when do we see the release from operations actually growing in line with your group targets?

Nigel Wilson Jeff, do you want to take the first and the third? And I'll take the second question on LGIM.

Jeff Davies Sure, yes. Hi, Oliver. Thanks. Yes, in terms of the op profits, we certainly expect to see that across the metrics, with continuing operating profit on continuing divisions, the total op profit. We've always focused on excluding longevity releases. We would see those numbers coming through strongly overall.

And don't forget, of course, with the strong investment variance, that will flow through to EPS growth overall. And so we don't focus so much on that longevity release. It would probably be a bit premature to say where the number looks compared to that. But we're looking at the underlying businesses expecting to deliver profits in those and double-digit returns across the board there.

Oliver Steel Can I just interject? Can I quickly just…? But just to be clear, you are looking… The guidance you're giving would imply 2,450, 2,440 million of operating profit in 2021 as a whole. That's the right figure, isn't it?

Jeff Davies I think we just need to be careful on where we're putting the guidance around that. As I say, if you flow it through from the double-digit growth for the full year across both continuing and the op profits, certainly excluding longevity releases, and then we would look to show growth overall with the growth below that, you get good EPS growth as well then.

Oliver Steel I'm still confused, I'm having to say. You say in the statement that you're looking to double-digit growth in operating profits over the year as a whole. Is that from last year's 2,218? Or what does it actually mean?

Jeff Davies Yes, we're looking to deliver the growth. We'll deliver growth from the total number from last year, and we'll deliver good double-digit growth off op profit excluding the longevity release. It's a combination of those, to deliver both good growth on all of those metrics and then that delivers very strong EPS growth overall.

Nigel Wilson Yes, we're not trying to give an explicit, absolute number here. But the direction of travel that you're going through, Oliver, we would say yes, if you're looking for a one-word answer, to where we want to get to. And it's double-digit growth. Can I take the LGIM question? Yes.

The LGIM question, Michelle has articulated a very comprehensive strategy for modernise, diversify and internationalise. Part of that diversify is building out some higher yielding, higher margin products. And if you go through the detail of the results, you will see that there were very strong international flows across the business. We're doing incredibly well in the UK, Europe and indeed in Asia for the business right now. So we're very happy with that.

But we're making fantastic progress in things like our award-winning high yield debt team. Our fixed income team has just done an amazing job in the last few years. Our emerging market debt team, exactly the same. And ETFs, which we highlighted for the first time, having made a bolt-on acquisition a few years ago, is seeing tremendous growth in revenue. And these are all 20, 30, 40, 50 basis point types of products.

And therefore, as we build these out over the next few years, we should see an acceleration of revenue from these high yielding, high margin products. We do have to invest more. Part of that is regulatory driven. Part of it is from the fact that we are expanding into new product areas and internationalising the business.

But we'd hope, going forward, that the growth in revenue would be greater than the growth in costs, which is what we haven't achieved in the last few years in LGIM. But the current, well, not the current, the still rather new management team that Michelle has pulled together are really working incredibly diligently on these areas.

Jeff Davies And the LGI question, as you say, yes, the biggest impact there has been a tax impact. We sell mature savings effectively. All term business has been taxed on a profits basis as opposed to the good old-fashioned BLAGAB business. And that's been the main impact overall on that.

There are some other second-order impacts and there are some things we do between what's reported. We've optimised some of our US business, historic. New business financing. Some of that appeared in the UK and that's been moving around. But generally, the underlying biggest impact has been the tax by a long way. The other are small items.

So we see across the board. In some ways, it's better to look across the LGI at the top level. That's where we see the true picture coming through because of the way we use our different entities and that shows the growth. And that continues to be the way that we see it in the OSG of the underlying as well, which is a good sign for us. Obviously, we don't split that out to you guys, but we do see that coming through. So that continues to grow in line with that.

Nigel Wilson Okay. And next question is from Ashik at JP Morgan.

Ashik Musaddi Yes, thanks. And morning, Nigel, morning, Jeff. Just a few questions I have. Just to go back on Ollie's question, sorry for this, again on operating profit. If I understand correctly, what you are saying is operating profit will grow at double digit, but before last year's mortality releases, which the base is 2 billion basically. On that, it will grow double digits.

Now, what I'm trying to understand is if it grows double digits, then you are just recovering back the COVID impact from last year which was stated at 228 million. So are we talking about some underlying growth as well or are we just mixing the numbers? It's not 2.2 billion. We are talking about 2.4 billion which is on the headline profit number of last year. So that's one thing it would be good to get some colour about in terms of numbers.

The second thing is on LGC, sorry, clearly the first half profit was very strong, no doubt about it. But would you be able to give some colour as to which sort of, say, run rate profitability we should assume for annual, like a normal year, so let's say next year onward, etc.? Or, say, if you can give us some return hurdles for the alternative assets, like in this half, it was 10%, but normally your expectation is you generate 5%, 6%, 7%, something like that.

And the third question is the PRA's quiz is out on the UK Solvency. On the one hand, they are very optimistic on risk margin getting reduced, but on the other hand, they are putting a bit more default stress on the matching adjustments, especially for illiquid assets. So any early thoughts that you have on that will be very helpful. Thank you.

Nigel Wilson Okay. Jeff is going to take the first and the third question and I'll take the second.

Jeff Davies Yes. Hi, Ashik. Yes, we shouldn't be giving too much guidance directly on the numbers. But to spell it out, we see good, strong underlying operating profit growth of all of the businesses in a double-digit level. And so we continue to deliver that. Across the divisions, we will deliver that growth which is what we have done historically.

The longevity releases have always been considered one-off and excluded from those metrics. However, if we deliver that across the businesses, we would still see growth on the overall operating profit level. And when you combine that with what we're delivering below as well, we would consider that that will then deliver strong EPS growth, which is what we're intending to deliver.

So there's good, strong underlying growth of all of the divisions, which is what we historically delivered. There are one-offs around longevity releases which we're not taking through and not included in those numbers. But we would expect to see overall operating profit growth, despite that. And then that would translate into strong EPS

Nigel Wilson Yes. LGC, we've got 3.4 billion at the moment in these alternative asset platforms. We set a target return of 8% to 10% for those assets. We've said in the presentation that 3.4 billion will increase to 5 billion, in which case we would expect £400 to £500 million of LGC profit coming out in the next two to three years. And that's broadly the direction of travel that you can use for your models.

We're going to give you a lot more detail on how this all fits together in October and try and do a lot more work for you guys to make it even more transparent as to what we're doing. Clearly, this is a really important part of our growth driver but it's part of the three businesses working together, LGIM, LGR and LGC. And where one goes, all go really, because there's so many growth opportunities for all three of those businesses. Jeff, do you want to take the quiz?

Jeff Davies Yes, sure. On the quiz, it's a very large exercise. There's at least 18 types of scenarios. So difficult, I think, as an industry and commentor, to draw too much from that. And from discussions with PRA, they're very much looking on some specific areas where they want to have numbers, a wide, wide range so that they can find an answer somewhere in the middle, in simplistic terms.

And there are lots of other areas they're looking at which are more qualitative and to do with process and what assets are allowed, etc., all where they already have extensive data. So these are specific areas where they're looking for extra information in terms of, okay, in a range of scenarios, what could that mean, so that they can feed that in.

It's very hard to draw any more from that, but we get the same positive noises from them around risk margin and assets being allowed into matching adjustment portfolios. Just a lot of things they don't need to test at this stage, but there's a range of things where they do want to get some numbers back. So there isn't more conclusion than that at this stage.

Nigel Wilson Yes. I'd articulate the PRA approach as being balanced and measured. I don't think they want to have any forms of shock to the industry. And it certainly has been supportive of the initiatives that we've been having and discussions we've been having about investing in real assets in the real economy.

I have a degree of empathy with or sympathy for my colleagues because it looks a huge amount of work [unclear] to Tim Stedman, as I said, it's going to be an enormous amount of work between now and October. And it's just that the PRA want to do a very thorough exercise, but we expect the outcome to be balanced and measured and not to have a material impact on our business, going forward. I'll now hand over to Andrew Crean from Autonomous.

Andrew Crean Morning, all. Three questions or three areas. Firstly, would you give us the updated Solvency II coverage figure post the fallen yields in July? And can you talk to us about what the ceiling is in terms of when you'd look either at inorganic or capital returns? Is it 180% as it is for peers?

Secondly, on LGC, I think the alternative assets have grown at a CAGR of 29% over the last four and a half years. And to hit your 5 billion target, it's a CAGR of only 9%, going forward. Do you think that that's a bit too conservative?

And then thirdly, it's clear from your final slide of the presentation you're somewhat exercised about Legal and General's valuation. And I can understand why. Are you still happy to leave it to public markets to find the right level for Legal, or do you think you're moving to a situation where you may need to look at slightly more dramatic actions, whether it's selling off minorities or bringing in private capital?

Nigel Wilson Yes, if Jeff takes the first one, I'll take the second two.

Jeff Davies Yes. Hi, Andrew. Yes, in terms of the ratio, it is basically broadly unchanged. As you say, rates fell a bit, but obviously we have had surplus generation since then. So within the usual plus or minus a couple of percent, it's broadly unchanged. There hasn't really been much that's moved otherwise, apart from rates and surplus generation.

In terms of ceiling, yes, we don't, as you know, like to give the ranges around that. There's a whole host of reasons why a number may not be appropriate at a point in time. The big picture, we obviously continue to make ROEs of 20%-plus, so believe investing back in the business makes sense for us. And as you comment on the [unclear], maybe 9% we can do. I think I'll first see what Nigel says now.

But there's always ways to deploy the capital to make good returns. But equally, it does depend on why you've got to that level. It could be 190% just simply because rates had increased. Is that right and what's our view on downside from there, etc. So it very much depends why you've got to a level and how sustainable, you're your

Nigel Wilson On the second question…

Andrew Crean Could I ask quickly on that, could I just come in? Could I ask on that, would you be able to give us, in terms of the operating surplus generation or the surplus generation, a split between what's going on in the equity-owned funds and the SCR separately? It's quite helpful, that.

Jeff Davies Looking with a view to IFRS 17 and everything else and generally looking at S two disclosures, we are sitting down post holidays to consider what we might do around that.

Andrew Crean Brilliant. Thanks.

Nigel Wilson Okay. On the second point about alternative assets, Andrew, you sound like me. I think you should take that as a compliment around that. Yes, indeed, the maths say that we could grow faster, going forward. Really, this is our plan from last year and we've just repeated it here.

But certainly, the businesses have performed better than our expectations, to be honest about it, right across the board. I think there's a lot of third-party equity that can be brought in at that private level, which is really, in part, the answer to three. In a sense, it's much easier to get equity into later life living and get a fair valuation for that, or into many of our other businesses, Build to Rent or whatever, and feed from it than necessarily getting the recognition from the public markets.

And the point that we were making earlier on is that there's now a big delta between alternative assets or people with a broad approach to assets and the valuation of them, and there's a whole bunch of American firms that are beginning to look more like us, ironically, that have a much higher multiple than we do right now.

And we're on this journey from moving from being a traditional insurance company, and we've sold off a huge amount of our assets in the last ten years and repositioned ourselves to be a modern investment management company, of which insurance forms an incredibly important part.

We have a whole series of liabilities, pension liabilities, insurance liabilities, client liabilities, of which to create assets to manage against those liabilities. And they offer us enormous growth opportunities, not just here in the UK but increasingly internationally. And we're busy recruiting people and investing in activities that should continue to deliver the great returns that we've seen over the last ten years.

We think, at some point, the public markets will catch up with that. We're a little bit frustrated but not massively frustrated about it because we recognise that we have to deliver more, we have to give greater transparency, which is what we're going to do with LGC in October and what Jeff and the team are sitting down to do post the summer on Solvency II. Next question is from Greig at KBW.

Greig Paterson Morning, everybody. Three quick questions. Sorry, my normal question is I wonder if you'd just talk about, in the first half, what the downgrade experience had been in the triple B asset range back in LGR. And of course things have improved. What the outlook in the second half for downgrades is as a potential Solvency Ratio.

The second point is in the US, on your term light business, you are rolling out your UK, call it fintech-slash-digital expertise which seems to be making a difference. My question is you really have a very large market share. Is that a constraint on what you can grow or are you going to go to or do you have the capacity to go into, say, other mortality-type products, different distribution channels, whatever? And the sky is the limit there.

And the third question is just in terms of your own company's debt and leverage, are you planning to issue any further debt in the next 12 months? Thank you very much. Jeff?

Nigel Wilson Jeff can take the second and third. On downgrades, we haven't really had downgrades as you rightly pointed out, Greig. We're on an upgrade trend right now. And so we can't be totally confident that that trend is going to continue, given what's happening in the pandemic.

But the sectors where there have been problems, as we've articulated before, have not been problems and our cash coming into our assets has remained at the very high 99.89%. And we're confident that we'll continue to deliver at that sort of level. Do you want to take the other two questions, Jeff?

Jeff Davies Yes, sure. US term. That's right, yes, we've been effective in rolling that out. That obviously was very good timing with the pandemic and people looking to move away from paper transactions, etc. We're seeing delivery on that. And it was interesting, one of the points you made.

Yes, that in itself is changing the way distribution is done. There's a number of very strong tech-based… Well, they're not, they're past being start-ups now. They have significant sales volumes. And we're quite often either sole [unclear] or the main partner with a number of these that are growing the market.

And they're in themselves a different distribution to the traditional brokers. They're advertising to a completely different segment of the market and they want the straight-through processing that we're offering much faster turnaround times of putting business on the books. And that is definitely paying dividends for us. We're seeing increased volumes and continuing to grow.

You're right, being number one in the broker market would have a limit, but the broker market is completely changing and there are new entrants that are pushing us and expanding the market. And we believe we can push back further. So there's a long way to go on that before we would need to look at different products, etc.

Nigel Wilson Did Greig use the expression, the sky is the limit, there?

Jeff Davies Yes. And then…

Greig Paterson You know I don't believe that though.

Nigel Wilson You're taking it back now.

Greig Paterson Yes.

Nigel Wilson I feel better now.

Jeff Davies Debt, you'll have seen the slides which show the debt reducing over time. The constant growth of the balance sheet gives us lots of optionality around that. Obviously, yes, 180-plus solvency, very, very strong liquidity, we wouldn't need to do that. You never say never, but that wouldn't be our plans at the moment, I think it's safe to say, given the position that we're in.

Nigel Wilson Okay.

Greig Paterson So I think one of the questions [unclear] looked at the Fitch ratio and the various rating agencies' ratios. And it didn't look like there's a lot of headroom until you grow the denominator. I was just trying to understand within the current situation whether there is headroom.

Jeff Davies That was in my presentation, and I think I say it actually, the leverage is lower than it's been in the last three and a half years. Down now, I think post the 300 million, we're about 26 on the Moody's, 30-odd on the Fitch. And those reduce constantly as the balance sheet grows.

So there would be… We don't feel like we need to issue at this stage, but we definitely have headroom, should we want to do that. But we see it reducing over time and us then choosing opportune moments to optimise shareholder returns rather than anything else driving what we would do around that.

Nigel Wilson Yes, there's a great slide in the pack which I would encourage you all to read, on page 31, which shows how much the leverage has fallen over time and will continue to fall out to 2024, which is very helpful guidance, I think. Next question is from Ming at Panmure.

Ming Zhu Hi, good morning and thank you for taking my question. Just two questions, please. First is on the LGC. You've got a target of 14 billion third-party capital. Now, that is double where you are now. And could you just give colour in terms of how do you expect to achieve that? And how much of that would depend on for you to achieve your 8% to 10% per annum blended portfolio returns?

And my second question is on the solvency ratio. Your solvency ratio has been very strong on the reported base. But for example, last year, it's really the volatility and in between. What is really the minimum solvency ratio that will keep you comfortable, while keeping the regulator happy so that you can still pay out the dividends? Thank you.

Nigel Wilson I'm certainly going to let Jeff answer the second question. On the first one, the 8% to 10% returns is related to the money that we put into these investments. And as Andrew was saying, that's risen quickly over the last few years. It sits at 3.4 billion. We want to make that 5 billion. That's us as a principal investor.

As an agency, we've identified that we'll rapidly increase the fees and the assets from external, so that will bring us up to 20 billion or above. Andrew, I guess, has the same view that I have about the opportunities we have for doing that right now. So we've got two sources of profit, the revenue that we get from third parties but also the return on the assets that we invest as a principal ourselves. Jeff, do you want to take the second one?

Jeff Davies Yes, sure. A bit like not having a maximum, we don't have a minimum either. It was a pretty strong message last year. We were in the 170s, and in the low 170s at times, and we paid the dividend. We maintained that whilst modelling some very, very adverse credit scenarios and handing those to the regulator.

The board is putting a lot of scrutiny on that. We know what our adverse scenarios look like. We've talked about that many times. We build up from that minimum level to then give us the flexibility we require. And that moves around, depending on the subjective view of how big stresses can be, where are you at any point in time. And so it moves to some extent, which is why we don't set the absolute ranges. But we've never been anywhere near the levels where we would be having concerning conversations with the regulator or the board around the solvency.

Nigel Wilson Yes, thanks. In general, the LGAS solvency II ratio is about 20% lower than the group ratio. And so the regulator obviously sees a different number from the number that you're seeing when they look at the regulated businesses. We have one last question, last but not least, from Dominic at Exane BNP. Dominic. Have I missed one? One more. And then followed by Steve at HSBC.

[*Phone line connection was lost*]

Operator Thank you for your patience, everyone. We have reconnected the speakers. Please resume.

Nigel Wilson It's over to Steve now from HSBC. Steve?

Steven Haywood Oh, thank you. Thank you for squeezing me in. Three questions here. The first one was on your third-party capital. 6.8 billion now, obviously growing strongly in the first half from 5.2 billion at the beginning of the year. I really want to know what sort of revenue margin you're receiving in terms of the fees from this third-party capital stream so we can look at what it might be when it reaches the 14 billion mark in a few years' time as well.

Secondly, you've previously given some information about the pipeline of UK PRT. I wonder if you can talk about L&G's pipeline. I know you've mentioned the 2 billion pretty much done in July, but if you can give some more guidance on the rest of the year, that would be very useful.

And then finally from me, on the operating profit guidance, it is obviously based off of the 2 billion base level. But I was wondering if you can be a bit clearer on the percentage range you're looking at. Are you looking at 10% to 20%, 20% to 30%? We're not obviously talking about a 90% double-digit growth rate. But maybe I'm being a bit facetious on the last question. But thank you.

Nigel Wilson I'll take the first one if you can take the second and third, Jeff. On the first one, well, the fee range is between about 50 basis point to 150 basis points across the different asset classes. Clearly, the mix, we can't be certain as to what the mix is going to be, going forward. But there's a healthy pricing range for those assets. Jeff?

Jeff Davies Pipeline. Yes, it's very strong. It's not dissimilar to the numbers we've given in the past. It's of that order of up to 20 billion that we see. But obviously a number of those deals which we're now seeing, which is stronger than we probably thought at the start of the year, some of those will naturally flow into next year as well.

Given the 2 billion one in exclusives, we're in a strong place coming into the second half or post-holiday second half, if you like. They obviously executed very well in July. And so we are comfortable that we don't necessarily need to be hitting 8 to 10 billion with the good quality assets we've got to get to the metrics we anticipate for this year and hit the metrics we need.

And so we can look at what's the best business out there, what's the most advantageous to us to build on top of that price. So there's plenty out there, coming from a strong position. If the market is 20 to 25, we keep our market share and we get a good level of new business volume on the back of that.

Yes, the op profit, I don't think I'd be giving too much away to say we don't particularly anticipate doing 20% to 30% profit growth overall. You never know. But we're clearly talking, what we've done historically has always been 10%-plus, 14% in the first half. Those are the sorts of numbers we talk about when we say double-digit.

Nigel Wilson Okay. Thank you to everyone for participating in the call this morning. And I think there was a great variety of questions which, Jeff's and my point of view, it's really kept us on our toes during the presentation. We look forward to seeing everyone, hopefully in person, at the LGC Capital Markets Day in October.

We remain very confident about our capabilities to continue to deliver great returns for shareholders on a go-forward basis. And we're very happy with our portfolio of business. I think, as we've alluded to, I think you should expect some further announcements on us bringing third-party capital into various parts of LGC, continuing to make very good progress in terms of executing LGIM's strategy around diversify and internationalise.

But also, Jeff just talked about a very solid performance that we're going to see and continue to see from our PRT business. And our retirement solutions business has been going from strength to strength, as indeed has LGI, particularly in the United States. So it's taken us a long time to get the portfolio into the shape it is today. And you can see the outstanding results, that that portfolio is driven by tremendous people efforts right across our organisation. So look forward to seeing you in October.