Legal & General Annual Results 2020, 10th March 2021
Jeff Davies
Hello everyone, I hope you are keeping healthy and safe.

Today, I will be covering...
…our resilient 2020 financial performance across the Group, including our credit portfolio and balance sheet,
… and how each business has started to deliver against the ambitions we outlined at our capital markets event last November.

2020 was a challenging year for global markets and our customers, and Legal & General was not immune to this.

Although we view 2020 as a pause year, with metrics in line with 2019, our focused, diversified, and robust business model performed well, and has seen limited real economic impact, continuing to deliver strong returns for our shareholders.

This is demonstrated by an ROE of 17.3%, significantly in excess of our cost of capital.

Operating profit from continuing divisions was broadly flat at £2.4 billion, with growth in three of our five businesses.

The primary impact from COVID was on LGC and LGI which I will cover in more detail later.

Group costs were elevated reflecting the debt we raised, and approximately £27 million of exceptional COVID-related costs, for example, the deployment of hardware to facilitate remote working for our people and adapting our work places.

Additionally, in Group costs, as previously indicated, we continue to make measured investments in technology in order to augment cyber security and to upgrade the IT infrastructure, including preparation for IFRS 17.

We expect these costs to reduce to previous levels as these projects are delivered over the next couple of years.

In line with recent practice, we have moved to the next release of the actuarial tables for annuitant mortality.

Given the uncertainty over the 2020 data and the need to assess the long-term impacts of the pandemic, we have conservatively adopted CMI 18, resulting in a reserve release of £177 million.

Including these impacts, group operating profit was broadly in line with the prior year at £2.2 billion.

The negative investment variance of £430 million was largely due to the formulaic impact of discounting reserves at lower rates in LGI.

It is the primary driver of the step down in 2020 EPS, but has substantially reversed with the recent increase in rates in the UK and US, close to pre-pandemic levels…

Additionally, in the investment variance, there are reductions in asset valuations within LGC's investment portfolio, where we are long-term investors and can absorb short-term volatility without realising these mark to market losses.

These were partly offset by the £335million profit on disposal from the sale of our Mature Savings business.

Finally, the Group's Solvency II operational surplus generation from continuing operations was £1.5 billion, up 4% … and the coverage ratio for year-end was 177%, which has also increased significantly with rates since the year end.

Turning to our divisions…

In LGR, operating profit excluding mortality reserve releases was up 10% to £1.6 billion.

This performance was driven by the on-going predictable delivery of prudential margin releases from our growing back book, new business surplus generated from good volumes of both PRT and individual annuities, and positive variances arising from routine updates to our modelling assumptions.

The evident, heavier mortality experience largely offset the corresponding adverse impact in LGI.

In UK annuities, we maintained pricing discipline, achieving a Solvency II new business margin of 10.6%, reflecting longer duration transactions compared to the prior year, and good asset sourcing.

UK PRT business written during the year was especially capital efficient, resulting in a strain of less than 4%.

Individual annuity and lifetime mortgage volumes were down year on year as they were temporarily impacted by the spring lockdown measures.

To counter this, we accelerated technology innovation across our retail product offerings, helping our customers and colleagues adapt to the current environment.

In particular, our operational response saw individual annuity sales up 3% in the second half compared to the prior year, and an increased intermediary presence allowed us to grow market share to over 20%.

This has meant we have entered 2021 strongly and delivered good volumes despite the lockdown, though clearly uncertainty remains in the outlook.

LGRI had another strong year, writing £8.8 billion in global PRT across 61 transactions, at attractive margins across all deal sizes.

In the UK, we wrote £7.6 billion on a wide range of deals including a ninth buy-in with ICI… another example of where we are able to leverage one of our many long-standing client relationships.

2020 was a record year for our US PRT business, with premiums up 42% at $1.6 billion, representing a growing market share of 6%.

This included our largest fully retained US transaction at over $350 million.

Since entering the US market in 2015 we have now underwritten over $5 billion.

Our ambition is to write a further $10 billion of international PRT over the next five years.

With both a UK and a US PRT business we are uniquely positioned to offer transatlantic de-risking solutions.

During the year, we insured two such transactions, securing benefits for their UK and US pension plans at the same time.

Back in the UK, and despite COVID-19, 2020 was the second largest year on record, with approximately £30 billion of PRT transacting.

Our performance in 2020 reinforces our intention to write £40 to £50 billion of new UK PRT out to 2024.

We will remain disciplined in our pricing and deployment of capital, weighing the interests of all our stakeholders when making new business decisions.

LGR's diversified bond portfolio, which now stands at £80.4 billion, is defensively positioned and has not been materially impacted through 2020… a testament to our rigorous risk management practices in a challenging year.

We have maintained high credit quality with 2/3rds of our bond portfolio rated A or better, and 19% in sovereign-like assets.

We have minimal lower-rated, cyclical exposures, including those sectors directly impacted by COVID... for instance, travel, leisure and traditional retail combined represents less than 1%.

During the year we had just 0.9% of net downgrades to sub-investment grade, compared to around 1.8% for the index.

As is normal practice, we continue to analyse our BBB exposures, and where appropriate, have taken the opportunity to improve credit quality at attractive pricing levels.

These remain well diversified, and secure, with limited cyclical BBBs and BBB- exposure.

As further protection, we continue to hold a substantial credit default reserve of £3.5 billion, which remains unutilised.

Going forwards, we recognise the global economic impact of COVID is still developing, and we will continue to monitor and safeguard our portfolio.

LGR has a diversified direct investment portfolio with stable income from high quality counterparties, often secured, making it resilient to market stresses as we have seen over the last year.

The £24.7 billion DI portfolio experienced no defaults, and 99.9% of scheduled cash flows were paid.

Where not externally rated, assets are independently internally rated.

Every asset has been reviewed at least once since the start of the pandemic, and as with the traded credit portfolio, downgrades to sub-investment grade have been minimal.

As we show here in the chart on the left, the primary exposure in LGR's DI portfolio is counterparty risk to high quality institutions.

This constitutes around 70% of the portfolio... as shown by the light grey circle.

Many of LGR's DI assets are aligned to our ESG investment principles.

Our ability to invest in sectors such as clean energy, and to manufacture attractive, long-term assets to back annuities, such as build-to-rent and affordable housing, remains a key competitive advantage.

Moving on to LGIM...

Operating profit was up 3% to £404 million, reflecting increased revenues partly offset by continued investment in the business across data analytics, digitising customer experience, platform optimisation, and international expansion.

As we said in November, this investment is required to modernise, diversify and internationalise LGIM, so that we can deliver on our long-term growth ambitions.

Higher revenues were driven primarily by LGIM's AUM, supported by growth in higher margin areas like factor-based and thematic ETFs and Multi-Asset.

Internal revenues increased by 13% as LGIM continued to benefit from LGRI's growth in the global PRT market.

Total AUM reached £1.3 trillion, with international assets accounting for approximately 30% at £388 billion.

We remain a market leader in UK DC, where we now have 4 million workplace members and AUM of £113 billion.

Despite significant market volatility, total Retail AUM stands at £42 billion and we were top 4 in gross UK sales in 2020.

We continue to be a global leader in ESG.

At the end of 2020, LGIM managed approximately £207 billion in responsible investment strategies explicitly linked to ESG criteria, and we expect this to keep growing.

Our diversified asset base has been resilient during a period of significant market volatility, with AUM up 7% from the end of 2019.

We maintained positive external net flows of £20.4 billion…
… with strong growth in UK DC driven by 82 new scheme wins in the year,
… ongoing demand for LDI solutions from our UK DB clients
… and positive performances in our retail and ETF businesses.

However, this was partially offset by outflows in the US where we saw some DB pension clients rebalance their portfolios away from fixed income towards other asset classes based on pre-set allocation thresholds.

Despite this, we expect our US growth to resume as clients, particularly DB pension schemes, continue to focus on long term de-risking, notably multi-asset and LDI solutions.

Through the strategic actions we are taking, we are laying the foundation for the resilience and scalability critical for continued global growth.

We are building on our strong position in ESG, for example, leveraging our bespoke climate risk framework, Destination at Risk, to assess the climate risk of our own portfolios, and those of our clients.

…And following our successes in Germany and Italy, we will expand into other European markets, aiming to be a leading asset manager in Europe by 2025.

We are confident LGIM's strategy strongly positions the business to grow in line with our ambitions.

In LGC, operating profit decreased 24% to £275 million primarily due to a pause in traditional housebuilding activities during the first national lockdown.

CALA was the most materially impacted of our build to sell businesses, however, in line with the market, saw second half housing sales make a strong recovery, reflecting pent up demand for new homes.

This has continued into 2021, though again uncertainty remains.

Reductions in asset valuations resulted in lower profit before tax.

A significant part of this was driven by COVID impacts on two retail direct investments that we have previously highlighted, and a prudent approach in the valuation of realisable yields in some of our housing businesses.

We can be long term investors and so these reductions in market valuations do not constitute a realised loss.

During 2020, we continued to prudently deploy cash to support the growth of our existing businesses and access new opportunities.

Our diversified DI portfolio now stands at £3.1 billion, up 9%.

Over the plan period we expect to continue to build our diversified DI AUM up to approximately £5 billion, with a target blended portfolio return of 8% to 10%, and as Nigel covered, aim to increase third party capital to over £14 billion.

Now moving onto our protection division, LGI.

Operating profit was £189 million, reflecting higher claims experience due to COVID-19... particularly impacting our US Protection and UK group life businesses where we retain the majority of the mortality risk.

UK retail protection is heavily reinsured and saw little impact.

Additionally, we have set up a provision of £110 million for COVID-19 potential future claims that may arise in 2021.

This compares to the total of £76m claims we experienced in 2020.

Given the ongoing uncertainty and projections for impacts on the US population we believe this is a sensible and prudent approach.

Profit before tax was down largely due to the formulaic impact on reserves of falling interest rates as seen in previous periods, however, as mentioned earlier, this has now largely reversed with rates increasing.

Despite market competition and the temporary disruption from COVID, new business annual premium increased 10%, and total gross premiums were up 4%.

The business continues to grow at good levels of profitability with Solvency 2 new business value up 18% to £254 million, due to strong sales in Group Protection and improved margins as a result of an increased focus on value optimisation across the business.

This good performance has continued into 2021.

Moving onto our capital position.

Despite market volatility our balance sheet remains well capitalised with the Group's Solvency II surplus at £7.4 billion.

As at 5th March the coverage ratio was estimated at 192% following positive market movements.

The quality of our capital remains strong… 75% of our Own funds is tier 1, and we remain confident in the resilience and capacity of our balance sheet to withstand further shocks.

We have bridged the Solvency II surplus to help explain the movement during the year.

Operational surplus generation from the growing backbook was up 4% at £1.5 billion, demonstrating the predictable nature of our capital.

After allowing for efficient new business strain of just £0.3 billion, and dividends paid, net surplus generation was £0.2 billion, consistent with our five-year ambition.

Market movements were £1.4 billion, primarily made up of...

… £0.8 billion relating to interest rates, reflecting the non-economic impact of lower interest rates on the valuation of our balance sheet…

… and £0.4 billion reflecting the impact of credit spread dispersion that we described at the half year.

Finally, as previously disclosed, we took advantage of favourable market conditions to raise £0.5 billion of sub-debt and £0.5bn of restricted Tier 1 debt... providing additional buffers and optionality should there be further material market shocks.

We will of course remain disciplined in the deployment of our surplus capital to ensure we meet or exceed our target returns, and remain within our risk tolerances as market uncertainty continues.

To conclude, although 2020 has been a challenging period for all, we have delivered a resilient performance, with profits up in three out of five businesses, and we have made a good start against the Group's five-year ambitions.

Our synergistic business model positions us well to execute on new and existing opportunities.

Our rigorous approach to risk management has ensured the balance sheet is strong, well-capitalised and continues to generate predictable levels of cash and capital… and our credit portfolio is positioned defensively, performing well in challenging markets.

We have made a positive start in 2021 with good levels of new business, however, we remain vigilant and will monitor and manage the impact of COVID-19 across our businesses.

As the vaccination rollout continues, we intend to be a leader in the post-pandemic economic recovery.

As always, we will support our shareholders, customers and people while delivering Inclusive Capitalism through investments in infrastructure, clean energy, affordable housing, and providing products to support individuals' financial resilience.

Thank you.

Nigel Wilson - Closing Remarks
Thank you, Jeff.

Just a few closing thoughts from me…

First, we have talked already about the unique business synergies across and within L&G.

Our approach could be described as "joint and several" and each of our divisions has an important role to play delivering our five-year ambitions.

LGRI will increase UK PRT volumes in this period and double International PRT new business volumes.

LGIM will grow cumulative profits, at least in line with Group dividends.

Adding higher margin products in existing and new geographies.

LGC will significantly grow alternative assets AUM and add billions of third party capital.

LGI will use technology to sustain its UK market leadership and grow US new business.

It will also achieve double-digit growth in its fintech businesses.

And LGRR will capitalise on its expertise, reach, and leadership in all aspects of UK retirement financing.

Across the business, we will intensify our focus on climate... reducing the carbon-intensity of our balance sheet and shifting our housing businesses to operational net zero by 2030.

Addressing climate change is not just a risk management function, but also the greatest investment opportunity of our lifetimes.

Our business demonstrates continued evolution: we have our five scaled-up, “grown-up” core businesses.

Here you also see some constituents that are in the process of scaling-up... some 100% owned by L&G, others where we own in partnership with third-party capital already, where that enables faster growth, with Pemberton or Podpoint being two examples.

You also see the “start-ups”... again some where we are a 100% shareholder, some where we a minority investor.

There is a high level of optionality for growth.

COP being hosted in Glasgow later this year, is highly significant for us.

We have proved ourselves financially robust, operationally resilient, and we have never been more relevant.

Thank you, and I look forward to questions.