Phoenix Group
Half Year Results Presentation
Friday 27 August 2010

Ron Sandler
Chairman

Right good morning and thank you all very much indeed for coming here this morning on this rather cold and grey day. It is my great pleasure to welcome you to the Interim Results of Phoenix. I am extremely pleased with the progress that the Group is making. And I think as you hear what we have got to say this morning you will understand why I say that. And when I look at what Jonathan and his team have achieved in the first half of 2010, there is indeed much to be pleased about. Firstly we have simplified the capital structure and this has enabled us to successfully achieve the premium listing in the early part of July. And we now await FTSE 250 inclusion which we expect in just a few weeks time.

Second we are tracking extremely well towards our financial targets in both cashflow and EV. And as you will see and as we have consistently said, the Group is highly cash generative. And third, the team has continued to deliver on all of its promises. Not just on the big headlines like the premium listing or some of the cashflow numbers, but on the myriad of operational improvements and organisational strengthening initiatives that underpin our plans.

The bottom line is we believe Phoenix represents an extraordinary investment opportunity. The cashflow provides the foundations. We are now well down the track of normalising our capital structure and we are beginning to focus on the restructuring of our banking arrangements and the lifting of the dividend cap.

And over the longer term we see tremendous consolidation opportunities in the closed life sector. And we have the scale and the operational platform to take advantage of these.

So I hope you will see why we are as enthusiastic and as optimistic as we are.

But enough from me. It is my great pleasure now to hand over to the two Jonathans to present the highlights of our Results. And after this we look forward to answering any questions that you may have.

Thank you very much.

Jonathan Moss
Chief Executive

Thanks Ron and good morning to everybody. Thank you for coming to our first half 2010 Results Presentation. And just to echo Ron's sentiments that we believe this is a good and strong set of results which supports the proposition that we brought to you in September last year following the Liberty transaction.

So just to reprise, one of the slides we have shown you. This is a relatively simple business model. It is all about extracting the cash from the underlying operating companies, putting that up to the Group Holding companies, deferring the costs, pension scheme costs, pension scheme costs, corporate costs and then the residual amount that is left over, that can either go to pay interest and

pay down bank debt or up the Group to pay dividends to shareholders. Clearly over time what we would like to see is an increasing amount of the available cash pushing up and taking the form of dividends to shareholders.

In terms of the underlying operating businesses, we have got management services and IGNIS which are essentially relatively simple P&L businesses. They receive fees from the life companies and in the case of Ignis from third parties. They have a cost base to the extent that they make a profit. That profit should be available to be passed up the Group. But the real core of the Group is clearly the life companies. Of the £335 million of cash we have delivered over the first half, £326 million of that has come from the life companies representing both the profit margins that are made, but also the release of the £5 billion of policy holder and shareholder capital that sits in those businesses and is paid back over time as the business runs off.

Strategically, we believe we can grow the business, that we can create further scale to support that underlying business proposition essentially to be the consolidator of choice. And in support of that we have a number of key strategic goals which then drive our priorities each of which I will say more about in a moment.

The key strategic goals essentially. Increase the value of the underlying business through managing the business better, making sure that we are managing it efficiently and where we can taking rewarded risk. Where we are not being rewarded taking that risk off the table. Maintaining a robust and scalable platform. Clearly we want to grow the business but we can't rely on that and therefore we want to run ourselves as efficiently as we can, particularly within the service company, given the runoff of the book. Efficient capital usage is all about again, managing risk well and accelerating the release of cashflow. Making sure that Ignis runs successfully, profitably, grows its third party franchise, meeting the needs of our customers and as I have indicated, ultimately leading the consolidation of the closed life sector.

Underpinning all of that, a desire to be very transparent in what we do. It is a simple business model. It should be possible for us to demonstrate what the value of the business is, how that is going to emerge, what our targets are and how we are doing against those targets.

So to move onto the priorities, this slide really is trying to capture the way in which we think about cash coming from the business. So our overall capital that we keep within each life company is based on the ICA or if you like, the economic capital assessment of the risks to which we are exposed. And then a buffer on top of that, i.e. our capital policies.

Now the capital policy is really a statement of our risk appetite. We want to be able to run our business unfettered so we want to be able to survive economic stresses and still be certain we are holding sufficient capital after that stress. And that is really how we set the capital policy. As I say over time the business runs off, therefore the capital requirements reduce because there is simply less risk in the business. And that generates free surplus which can then be passed up the Group. To the extent that we can either reduce the ICA or reduce the amounts of capital policy, clearly that will accelerate the cashflow that is being released.

So if we move over to the right hand side of the diagram, at the end of 2009, the amount of capital held within the life companies in excess of the capital policies was £408 million. During the course of the first half of 2010, that excess is transferred and you can see £326 million passed up to the holding companies through the first half of the year. At the end of half year 2010, that excess had grown to £534 million. We don't actually see all of that coming out during the second half, some of it is going to be retained to harmonise the capital policies that we have got across the Group. So we want to have a common standard, common level of resilience within each and every one of our life companies so that we are happy that they can withstand the sort of economic stresses that we want to be able to throw at them. So some of that £530 million will be retained, clearly some of it will come out in order to meet the targets that we set for ourselves.

We believe that we will deliver the remaining management action target that we have of 225 and that we will be at the top end of our business as usual target of cash release of £400-500 million. So that we are setting a target for the year as a whole of £725 million of cash release.

Cashflow acceleration and capital management is all about bringing forward the cashflows. The management actions that we undertake for the embedded value about increasing the quantum of cashflows that will emerge in the future.

Last year during the course of 2009 we set a target of £300 million of additional value. We delivered £155 million of that last year, £116 million during the first half of this year. So we have a relatively modest £29 million in order to meet that target and clearly we will be looking for other opportunities during the course of the second half.

The £116 million itself comprises three main items. Tax management, reviewing our tax provisions, taking advantage of our ability to put companies together and offset for taxable profits against taxable losses from different companies.

Secondly, from the sort of truing up process in relation to the project Libra, which was the Phoenix and London guaranteed annuities scheme where an initial estimate had been made of how much we would need to enhance asset shares. As it turns out, that was over-egged and we have been able to release some of that potential asset share enhancement back to shareholders.

And the third one is data integrity which again is at the heart of the business in the sense of, as we move onto new platforms operated by our outsourcers and clean up data, typically that will allow us to release prudent data provisions.

The impact of the £116 million of management actions, together with the unwind of the discount in embedded value meant that we delivered an MCEV operating profit of £216 million for the half year as compared to £269 million for the whole of 2009.

Turning to IGNIS, we have managed to increase assets under management, managed to offset the runoff of the life business by three things. One, obviously markets have been helpful. Secondly, a one off of bringing assets back that were managed by a third party manager on behalf of the life companies. But then perhaps most pleasingly, £800 million of net cash inflow into IGNIS from third parties.

Investment performance has been sort of fairly decent in very difficult markets and the overall impact of that has been that IGNIS has delivered a £22 million profit for the half year as compared to £16 million during the equivalent period last year.

All of which, as I say, goes to our intention to make sure that the transparent reporting of what it is that we are trying to achieve and how we are going against those targets. The £2.7 billion of cash over five years that we indicated to you earlier in the course of the year, remains our target. We have achieved £335 million of that during the half year. We have now broken that down into its component parts and Jonathan is going to talk more about that during the course of his Presentation.

As Ron mentioned, in order to sort of drive and deliver our financial targets, there is a plethora of projects which are undertaken within each of the business units and in terms of our progress against those, we completed the restructure of National Provident Life and moving some of its business up to Pearl during the first half of the year. And we are in the process of moving the business of Phoenix & London into Phoenix Life limited during the second half.

Site closure. As you know we have been going through a project to close down our Glasgow site, our Peterborough and move all of that work to a single site in Withal. The vast majority of the work from Peterborough has now moved to Withal and the accounting was done for the half year in Withal. It is really just the Actuarial Department that has yet to be moved.

Solvency II. We have completed our pre-application so we are on the road to adopting Solvency II. We are currently undertaking the actual calculations to determine what our results would be under QIS 5. We probably can't say too much more than that at the moment, but clearly we are anticipating that QIS 5 will give a significantly better outcome than was the case under QIS 4.

Ignis continues to strengthen its management team and its investment capability, having appointed a new CIO earlier in the year together with a new Chief Operating Officer. Similarly the work simplified the relationship between the life companies and Ignis to make that a more arms length, third party arrangement. £7 billion of assets have been moved into collectives from segregated mandates and we anticipate a further £10 billion being transferred in the second half.

As Ron said we have simplified the capital structure, that enabled the listing in London on 5 July and we are expecting that in turn will lead to our inclusion in the FTSE 250 by the end of September.

Discussions with the lenders, the small box second from the bottom on the right hand side is clearly a very significant priority for us for the second half in the desirability of lifting the dividend cap. So that is our principal priority for the second half of this year.

On that point I will hand over to Jonathan.

Jonathan Yates
Group Finance Officer

Thank you Jonathan and good morning everybody. I am delighted to be here to present what I hope you will agree are a very strong set of financial numbers for Phoenix. In particular strong recurring cash generation. £335 million of inflows to the UK holding companies in the first half of the year. Group NCV has shown impressive growth to £1962 million despite volatility in the equity market. So over 7% growth in the first half of the year.

We have maintained robust IGD capital surplus at £1.3 billion which represents coverage of 135% over our minimum requirement. IFRS operating profits remain strong and assets under management, as Jonathan said, grew to almost £69 billion. And also we have maintained our dividend at the equivalent of 50 Euro cents per share for the full year, on the basis that we are going to pay our dividend in two equal instalments. So we will be doing that whilst the dividend remains capped under the existing banking arrangements.

So turning to cashflows into the holding companies, these again were very strong. We are well on track to meet our recurring target of £4-5 million per annum and we expect to come in at the top end of this range. Total cash receipts of £335 million reflects the predictable nature of our recurring cashflows and it includes £30 million of cash accelerated through management actions. The remaining £195 million of our targeted management actions for 2010 are on track to be achieved in the second half of the year.

The vast majority of cash generated comes from our life companies as you can see and is driven by the emergence of surplus in particular in the release of capital. And later on I will come to explain or try and explain in more detail how and where this arises. We have paid down £49 million of interest on our senior debt facilities and £27 million on our Tier 1 bonds. We also prepaid £22 million of senior debt in the first six months.

In the second half of 2010 we will be commencing negotiations with the banks within our two facility agreements. I expect this to lead to additional prepayments of senior debt in the next 9 months.

The non recurring cash outflows shown here of £59 million reflect costs incurred in the first six months in relation to achieving our premium listing on the LSE which was effective on the 5 July. It also includes IT and other business transformation costs associated with policy administration transformation programme which is being implemented by us with our outsourcers. This is very much in line with previous guidance we have given you in this regard.

So moving on to MCEV. As I have said before, despite fairly lacklustre equity markets, MCEV has performed remarkably well and remarkably resilient over this period growing by £135 million or 7.4%. This included £116 million from management actions, the movement analysis we have shown here follows the CFO forum principles. Hence the operating earnings include £97 million of these management actions, primarily in respect of tax optimisation which we have achieved on fund mergers and resolution of legacy tax issues and the data clean-up work we have been doing alongside our outsourcing partners.

The economic variances include improvements in the property market and strong return on hedge funding investments, offset by equity market declines and negative returns on interest rates for swaps in the holding companies. We then had a further £90 million of finance costs and £45 million of actuarial costs related to the movement in solvency positions of the defined benefit pension schemes.

And finally I would just like to reiterate a point which I am sure you are all very much aware of, that our MCEV numbers do not include any value of future profits from Ignis or from the service companies.

So moving on to IGD surplus. As I said before, it remains robust at £1.3 billion, which represents 135% coverage of our Group capital requirements and well in excess of the target we set ourselves of 125%. As you are probably aware, Phoenix has a relatively complex Holding Company structure and the calculation of IGD surplus itself is quite complex. But we do actually have a further £200 million of regulatory value which does exist within [?] sub group which we are not currently able to count towards the IGD surplus.

Just to try and re-emphasise the point about just how robust the IGD surplus is, it is pretty insensitive to fairly extreme market movements and we will show here a few sensitivities to those market movements. In particular I will probably highlight the one that is the most extreme here, but on the combined stress scenario which comprises 25% equity fall, 20% property fall, 75 basis point increase in yields and credit spreads widening, this would only reduce our IGD surplus by £200 million. Interestingly the margin goes up given the way the calculation works.

So as I said before, we had very strong IFRS profits. Phoenix Life operating profit was £182 million which reflects the expected returns and non economic experience variances. It is somewhat behind what we delivered for half the full year 2009 result, but this benefited from favourable data clean up experience and longevity assumption changes as we harmonise those across the Group and those weren't repeated in the first half of the year.

We are also, as Jonathan said, delighted to report that against the set to trend and despite volatility in markets, Ignis delivered strong operating profit of £22 million. The corporate costs we show here include staff and other corporate expenses associated with the head office and so on and pension scheme charges.

So turning to profit after tax, we generated £207 million profit after tax in the first half of 2010. Positive investment variance contributed £128 million with a further £28 million on shareholder funds. Intangible assets recognised on the acquisition of Pearl have been amortised in line with the run off of the business and this resulted in the charge of 73. Nonrecurring items include the costs incurred in our premium listing on the London Stock Exchange and business transformation costs connected with our policy holder administration outsourcing programme.

The finance costs included £49 million of debt interest for the period together with £11 million of interest on the Tier II bonds we have in Phoenix Life. And finally, tax itself added £27 million due to the movement in the value of deferred tax assets.

So what I wanted to show here was very much that there is a clear link between the profits we generate and the cash that appears on our balance sheet. And we believe we are able to show a clear pattern from these IFRS profits to free cash. Profit generation capital releases increased the free surplus in our life companies from which we draw the distributions of cash to the UK holding companies. In the first half of 2010, we distributed £326 million of cash up to the UK holding companies, from the 408 of free surplus that was in the life companies at the end of 2009. 82 being held back in respect of the probably need to strengthen capital policies in particular in Pearl Assurance and London Life.

During the year the life companies generated an IFRS operating profit of £175 million and of the non operating items such as investment variances of £160 million. As the book runs off and actions taken to address capital inefficiencies, so the capital requirements decrease and the free surplus increases. And during the first half of 2010, the movement in capital requirements resulted in £160 million increase in free surplus as a result.

So at the end of June we had £534 million of free surplus in the life companies which is the capital held in excess of the capital policies at that time. The exact amount of cash which will be released from the life companies to the holding companies however in the second half of the year will be very much determined by the completion of the review of the capital policies within those life companies. As I said before principally that involves Pearl Assurance and London Life.

This next slide is very much what you might call work in progress. And I certainly don't intend talking through every single number here, but it very much reflects discussions we have had with many of you over the last months where you have been asking for greater disclosure and more information on what actually drives our IFRS profits. And this is very much as I have said before sort of work in progress. And we are making a start. And I would be delighted to sit down with you and talk about this in more details, probably on a one to one basis rather than in a large group.

Essentially what we are trying to do here is break our IFRS profits down between the different lines of business that exist within our life companies and show where the profit comes from and how it gets through into those results. And taking you back to that previous slide, how that then becomes cash on the balance sheet.

And we have done a similar analysis for Ignis as well. Ignis in this instance being a more simple and transparent business. What we have done here is we have broken it down between the different types of business that Ignis has and writes. And in particular the retail business, the institutional business. As you can see, very high margin business, but obviously the vast majority of the IFRS operating profit coming from the life funds. But it is clear to see equally that those life funds are paying for all of the infrastructure within Ignis and therefore when we do write new business in the retail and the institutional sector, it does contribute a very high margin straight to the bottom line which obviously serves to emphasise the point that Jonathan was making about the very good new business that Ignis has been able to generate within the first six months of the year. It shows just how valuable that business is.

And with that I would like to hand back to Jonathan.

Jonathan Moss

So in summary, we believe we have got a very strong Agenda for increasing shareholder value over the coming period. We would like to carry on establishing the Group within the London Market, getting into the Index, broadening our appeal, in order that there is greater liquidity in the shares.

In support of that really, simplifying and restructuring our banking arrangements with a view to lifting certain restrictions that we have in the way we operate, principally the dividend cap. Whilst doing all of that at the corporate level, obviously not losing sight of the real drivers ultimately of the cash that we can delivery which is the life companies, service companies and Ignis, consider the work we are doing on capital management and cash acceleration as well as embedded value management and value increase. And ultimately increasing the scale of that platform which we believe is an effective platform through MNA activity.

All of this we think positions us well for the future. As Jonathan has shown you, a simple link from profit and capital to cash. Strong performance, resilient performance from the business in relatively weak markets. We believe we have got a clear strategy and a focus on delivering that strategy and that over the course of the first half we have made significant progress in delivering our strategic goals.

At that point I would like to close and move to Q&A. Thank you.

Question and Answer Session

<u>Question 1 : Greig Paterson - KBW</u>
Good morning, Greig Paterson, KBW. Three questions, one is, a little confused. If you read CEIOPS commentary, higher risk capital margins specifications, QIS 5 would result in a reduction in life company surplus positions and you guys are saying it is the other way. I just wonder if you could elaborate what peculiarities exist at Phoenix, why it seems to buck the trend?

The second question is, I noted that your CFO has gone on to Paternoster's Board. Is that not a distraction or is there are reason? Are you planning to acquire a bulk annuity player and move into that space?

And the third question, and I ask this all the time, is obviously function of your history being [?] that blank cheque vehicle from the Caribbean, I wondered when you are going to do a book build that you mentioned before to restructure your shareholder base? If you can give us an idea on the timing of that, thank you.

Answer : Jonathan Moss
Thanks Greg. I will pick up two of those and leave the inevitable question to Jonathan. COP's, your point about risk margins is well made. I guess one would look at Solvency II and break it into a number of components. On the capital resources side the classification of assets as Tier 1, Tier 2, Tier 3 etc, which we don't feel we are going to be particularly affected by, the calculation of the best estimate liabilities, where clearly there has been a lot of focus within the industry about liquidity premiums and whether they would continue to be allowed. And clearly that looks

favourable. And then the third component is the actual capital requirements. And as you say those are made up principally of two parts, one of which is the actual market stresses and operational stresses that one applies to the business. The other is the risk margin or if you like the profit margin that you would pay to a third part to take the business off your hands. In terms of that first component of capital requirements being the capital required to be held against market stresses, and as I say we are working through the numbers so this is work in progress, but we do not believe that those stresses are any stronger. And in some cases they are weaker than our existing ICA stresses.

So it really all boils down to the risk margin and I guess one of the ways I would look at that is the extent to which the risk margin is equivalent to our capital policy and so I guess what I am saying is in aggregate I would expect we would be able to retain the Solvency II requirements within the total quantum of our ICA plus capital policy, which I think was a point that Simon made when we spoke to you with the year end results.

In terms of book build, I mean clearly one of the key points we have sought to emphasise throughout this Presentation is that this is a significantly cash generative business that is throwing off more than enough cash to allow us to meet our mandatory obligations to the banks and to others and therefore give us flexibility to do more than that in terms of repaying bank debt. Even without that the cash generative nature of the business means that we can afford the current level of gearing that we have got. Clearly we are anticipating that we will pre-pay some debt in conjunction with amending other terms. But we believe we can do that with the organic cash that we will generate. We do not see the need to go out and do a capital raise.

Further question
You are structuring .....[difficult to hear]

Further answer : Jonathan Moss
Well nor do we believe that it is necessary to undertake a book build or raise capital in order to restructure the shareholder base.

Further Answer: Ron
And I will just pick up if I may on the Paternoster points, since I am Chairman of both Paternoster and Phoenix. What we are looking at here is simply an accident of history. I was involved in conversations with Jonathan, wearing my Paternoster hat, Jonathan Yates that is, at the same time to join the Board of Paternoster, at the same time I was involved in conversations with Jonathan to join Phoenix as an operating executive. It is not uncommon as you know for executives to have a modest commitment outside their executive responsibilities. It is quite common place. There are pros and there are cons. I am satisfied, the Board of Paternoster are satisfied that Jonathan is well able to discharge both of those sets of duties without compromising one or the other and you should absolutely not read into it anything to do with an appetite on the part of Phoenix for bulk annuities. Thank you.

Question 2 : Jon Hocking – Morgan Stanley

Jon Hocking, Morgan Stanley. I have got three questions please. Can you comment a little bit on the debt repayments. You have paid £22 million back in the first half which seems a little bit churlish given the cash generation. Is that a function of not having got to a point with the banks yet where you can repay more? Second point on the debt. In terms of the terms in the banking covenants to repay 10% of the principal I think before you can get rid of the dividend cap, could you explain a little bit about your thinking about the timing there? Whether if you do make that 10% pre-payment you are going to have total flexibility on the dividend or whether restrictions will still remain?

And second question, sorry a bit long first question. Second question, on low yields, I see the aggregate impact on the IGD of yields falling seems pretty small. But you did mention the interest rates swaps I think in the holding companies. Are there any other impacts for low yields that we should be aware of? Is that IGD surplus actually a good indication of the overall Group exposure to low yields?

And then finally, I think there has been some commentary in the press about potential industrial action at Capita, which I believe is one of your outsourcing partners. Could you comment on what the impact could be there? What contingencies you have in place please?

Answer : Jonathan Moss

Okay, debt repayment. The £22 million is a formulaic amount dis-reflecting the terms of the arrangements that we have with the banks. And really I guess in terms of the way we had thought about our priorities and our objectives, we always saw that bringing the company to London and with it undertaking the necessary restructure of the equity side of the capital structure was the number one priority. So that was really what kept us occupied at a corporate level throughout the first half. As a result of that, we had no negotiation or discussion with the banks about restructuring the banking arrangements. We saw that very much as a second half and into 2011 activity and one that really would be facilitated by us having generated significant cash which we had always anticipated doing. So in a sense the £22 million is neither here nor there.

The 10%, I guess the 10% in many ways is a sort of entry point to the discussions in the sense it opens up the door for us and the banks to have a sensible negotiation. There aren't any defined parameters which say if it is 10% of the debt then the dividend cap gets lifted by X or Y. It is the sort of minimum ticket to entry to those discussions. Clearly we are hopeful that those discussions will go well and we anticipate getting a good outcome of it, but it is I think too early to sort of describe the parameters around where we will end up.

The point on yields, I don't know Jonathan whether you want to pick that up or do you want me to have a go?

Further Answer : Jonathan Yates

Well yeah. It is a good point. I think low yields generally are a difficult period for life insurance companies. But what is particularly difficult is when we start hitting very low inflation and inflation starts to go below zero and we get deflation. In those situations the guarantees within the business become increasingly onerous. And of course we are not unusual in that regard. You are

absolutely right that we have put hedges in place around our interest exposure and that helps to some degree, but of course that helps both as the yields rise and fall. But in terms of the business going forward, I think low yields make it difficult or make it more difficult for us than one would expect in a high yield environment. But as a life insurance company, as I say, I don't think we are unusual in that regard.

Further answer : Jonathan Moss
Generally we take, certainly in terms of the fixed interest securities that we buy, we would tend not to be looking to take significant rates risk. So clearly where we are not invested in fixed interest, it is not true, but to the extent we are invested in fixed interest we would seek to be broadly matched in terms of assets versus liabilities. Certainly very closely matched on the annuities side, less so on the with profit side, which does give us some resilience against rate movements in either direction. And we inevitably have to go through a process of rebalancing the asset portfolios periodically because you can't guarantee that the offs from the business would be as you would have anticipated them and so force. But we do regular reviews, that is part of our ALM process to do regular reviews of the position of the assets against the liabilities, as frequently as monthly for annuities, but perhaps half yearly for the other business.

Capita, we are aware of the industrial or proposed industrial action at Capita. We do not believe that we will suffer as a result of that. As originally indicated, it was going to be a relatively isolated occurrence which would not have had an impact on the majority of our book. And because it was in an isolated area, the indication from Capita was that they would be able to continue to provide a service to the relatively modest affected book.

Question 3 : James Pearce - UBS
Good morning, James Pearce from UBS. Just looking at your IGD cover of 135, it looks really low compared to the other quoted UK life companies. Could you say why you think it is adequate, particularly given that it doesn't include the debt? And moving on from that, the MNA feels like it is ahead of the game to be talking about MNA, given that you would be putting together a financially very geared under covered on IGD business with whatever the target was. I mean how confident are you that the FSA would be happy to see that happen given your current financial arrangements? Thank you.

Answer : Jonathan Moss
Thanks James. Let's start off with the IGD point. I think, as I described earlier, the real way of looking at these businesses and the way that the Solvency II will take us as well, is to look at them from an economic capital point of view. And that is the way in which we try to manage the business. All of our life companies are basically pillar 2 companies rather than P1. And having established the economic capital requirement which as you know is reviewed by the FSA, we then set a buffer. And we set the buffer in order to ensure that the company can withstand a severe economic stress. Now that is the normal course in which we operate the companies. It is also the basis on which the company was looked up in terms of coming onto the London Market in terms of demonstrating it had the necessary working capital. So we go through a process anyway and that process has now gone through significant external review both from our sponsors and also our advisers and their advisers. So we are very comfortable that we have a very strong degree of resilience in this business which means it can not only survive the first level of economic stress

which included sort of 20% falls in equities, 15% falls in properties, spreads flowing out and so forth. And that having been hit by that stress, we would still be covering our ICA requirements. So my view is that certainly on an economic capital basis, we are well capitalised. As I have indicated, the financial strength of Phoenix and London and of the ex-Pearl companies was less than that of Phoenix Life Limited, the biggest of our companies. And during the second half of this year will be looking to align that and move towards a common level of resilience. So the IGD calculation is a fairly formulaic calculation based on the old Peak 1 world as Jonathan indicated, it does not even include all of the capital that we hold within the Group because of the peculiarities of our structure.

And I guess the third point is that as a closed fund, there is no particular need for us to over capitalise the business and holding back unnecessary capital in order to manipulate the artificial figure that is the IGD. We and the Board look at and run the Company on the basis of its economic capital position.

The FSA looks at us I think in the same way. Clearly, one has to meet IGD. It is a minimum requirement. It is in the books. You would not want to fall foul of it, but equally I don't think one should drive ones business in order to maximise the IGD. I don't think you get sensible economic outcomes from doing that. The discussions we have with the FSA are on the basis of the Pillar 2 capital requirements and our capital policy. How happy are they with us? Would they agree a change of control? I suspect it depends very much on any deal we would be looking at from time to time. It is going to be a bespoke consideration depending on whether one is going with a small deal or large deal I suspect and the complexity of the business one is looking at.

Further answer : Ron

Can I just comment on behalf of the Board. I mean the Board looks very carefully at issues of capital efficiency and also looks equally carefully at issues of prudence. And we try and run this business on the basis that we are efficient in our use of capital but equally that we are operating to a very high standard of prudence. And we are confident of that and we obviously need to ensure that the outside world is equally confident of that. But we would expect that that would be the result of a proper assessment of what are the risks to which this business is exposed an is there enough capital within this business to support and deal with any of those risks should they materialise. And simple IGD comparisons versus other life companies, whereas they may have a role to play in the development of that external perspective. We would hope that the outside world and the commentators on this business would look carefully at the risk profile and would not simply look at our IGD coverage and compare it with AVIVA's and draw any conclusions from that because there was more to assessments of capital efficiency and prudence than that sort of computation James. I am sure you would agree.

Further answer : Jonathan Yates

The point has also been made about the amount of debt that we have and comparisons between the amount of leverage in this company compared to others. But the amount of debt is very much less about that and more about the extent to which we are able to service that debt. And what we have shown in Appendix 1 we have given, is a sensitivity of the cashflows which demonstrates the high resilience of the cashflows in order to maintain that debt service going forward. The issue that we face is that we have term debt. And of the objectives we have with our renegotiations with the banks which will be coming up in the next few months is to see the extent to which we can actually

extend that term to something that is more reasonable and aligned with the profile of our emergence of surplus and generation of capital.

Further answer : Ron

And we are most unambiguously not saying we are gearing up to do big acquisitions now. What we are saying is that the longer term future of this business is as a closed life fund consolidator and that therefore MNA plays a role in the future development of this Group. Right now we are on a journey towards the restructuring of our capital base and improving our access to capital markets, be they debt or equity markets. And as and when, and improving our operations and our management strength and our controls and all of the factors that need to be there. And in the fullness of time we expect to be a significant player in the consolidation of the closed life sector in this country, which we think is both a good thing socially and we also think is a good thing for our shareholders, but it will be done properly and prudently at the appropriate point in time and we are working our way towards that point. Because we talk about our longer term goals, that should not be interpreted as saying we are out there desperately turning over stones trying to do deals, because we are not.

Question 4 : Andy Hughes, Exane BNP

Andy Hughes, Exane BNP. Can I rephrase the question from earlier about low interest rates. Are we still seeing that people taking 25% tax free cash will have the guaranteed annuity option? And at what point do you expect to see people stop taking tax free cash into that and how is that reflected in your ICA sensitive and indeed your hedging requirements? Presumably you don't hedge the full guaranteed annuity option, you basically hedge on the basis that a proportion of people take tax free cash.

And the second question was really about Ignis. Completely agree with the point about operational leverage in the business. However as you point out, your funds are running down. And other people have made the point that they would rather like to acquire asset managers. And it doesn't generate huge amounts of cash, so do you have a valuation in mind for the business at which point you would be prepared to pay down some of the leverage in the Group? Thank you very much.

Answer : Jonathan Moss

To answer the straight question. I guess I would differentiate between the exposure that sits within the with profits funds that have given the guaranteed annuities and the willingness or otherwise of the non profit fund to carry on writing annuities on. Clearly we take on annuity business from the with profits funds at a price we believe is an appropriate price which generates an appropriate level of profit. We have an agreement between the non profit fund and the with profits fund as to the level of competiveness that we need to achieve, but we certainly don't set our prices on annuities to be out there on top of the market. We set them at a level we believe is sensible and gives us an adequate return on capital. Within the with profits funds, clearly they have to consider the exposures they have got including the exposures that they have got to guaranteed annuities. And as you say they would broadly match the anticipated costs of those guarantees by way of options and other.

Your question about what proportion of future guarantees are taken into account in those cashflows is a high proportion. I can't recall, I don't know whether you can, but what that proportion is, but it is certainly something that is thought about.

Answer : Jonathan Yates
As a general rule, even when people get stunningly good annuity options they almost invariably take the cash. People are conditioned to take cash. The expectation is it is going to be worthwhile and of course it is tax free. So it has got to be a hell of a margin to persuade people not to take it. And to believe that that long-term income is going to give them a better result. There aren't many people out there, apart from retired actuaries who can do that calculation.

Further answer
I am not even sure ......[laughter]

Further question
Just thinking about it, interest rates are very, very low now. Therefore the valuation is becoming increasingly compelling for people to stop taking actuary cash?

Answer: Jonathan Yates
Agreed, but in practice, it is a real difficult choice for them to make isn't it.

Further answer : Jonathan Moss
Okay onto the question of Ignis, as I say, we do get benefit from third party business that we write. Clearly the size of the margins that one gets on retail institutional business relative to the life business means that you don't need as much business. If you do look at the retail to life Co fees, the ratio is about 5 to 1, effectively saying that a billion of new retail business is sufficient to recover the margins lost by losing 5 billion of the insurance business. So that gearing is definitely there. We have no plans to sell Ignis. We see very much that there is value in the business and that there is an opportunity for us to see that value coming through by way of significant increases in profits, starting from a relatively low base through 2008 to 2009. I think it is broadly your job rather than mine to place a value on that asset. Having said which, I guess you could go back 6 or 9 months to when we published an embedded value, including both Ignis and the service company and from memory the value in that embedded value which represents the value of the future cashflows without a great deal of allowance for third party business, was about £400 million. But as I say that doesn't reflect any sort of franchise value and ability to write third party business.

<u>Question 5 : Greig Paterson</u>
This is a question for Ron. It is interesting that you have got a foot in Paternoster and a foot in Phoenix. The last, just in terms of the Solvency II debate etc. Last year Phoenix set its internal capital policies in excess of ICA's and last year Paternoster set its policies according to the press that is around about the time the FSA came along and said, well Solvency II is plus X,Y and Z, you guys thought you had X amount of capital. I wonder if there is any sort of read across to Phoenix seeing that they both set their policies before the regime and they both said they were at sufficient solvency and then the QIS 5 debate happened and Paternoster was struggling and now Phoenix is fine. I was just wondering if you could compare and contrast those two.

Answer : Ron
Greg, I think this is very much a Phoenix Results Presentation, I don't think this is a forum for exploring Paternoster Capital policies. So no I would rather not talk about Paternoster. But all I would say I suppose is that we look very carefully in Phoenix at what is an appropriate level of capitalisation for the business. Indeed I would make the same response I made to James a few moments ago. This is the subject of a considerable amount of work internally which of course is overseen very closely by the FSA and we are very confident when we set out capital policies. As was made very clear in the presentation earlier, we are reviewing some of the life company capital policies as we do repeatedly, that we do so on a prudent basis. We like to think of ourselves as a rather dull and safe business in many respects and we want to make sure our capital policies reflect that.

Operator
You have one question from the Internet from Navere Sadu, one quick question on Tier 1 bonds.

Question 7 : Narvir Sidhu - Carlson Capital
One quick question on the Tier 1 bonds - when will the company the pay the skipped-coupon? Guidance was by the end of the year - any clarity on that guidance? Thanks?

Answer : Jonathan Moss
The missed coupon for 2009 will be paid by the end of 2010.

Jonathan Moss
Okay, if there are no further questions, thank you very much everybody for coming along and see you on another occasion. Thank you very much.

End