PHOENIX GROUP

Proposed acquisition of Standard Life Assurance by Phoenix Group and Strategic Partnership with Standard Life Aberdeen plc

Friday 23 February 2018

Clive Bannister, Group Chief Executive

Good morning everybody and thank you very much for being here on this historic and important day for Phoenix. Welcome to our presentation on this transformational acquisition of Standard Life Assurance and the entry into a new strategic partnership with Standard Life Aberdeen.

This is an exceptional transaction. Strategically it's 100% on message. It is value accretive. It enhances our scale, nearly doubles the size of our business. It brings new business opportunities by way of Europe and new business generation, and it's reinforced by a fabulous strategic partnership with Standard Life Aberdeen.

Jim, Andy and I are going to take you through key highlights of the transaction from a Phoenix perspective, because many of you will have heard from Standard Life already today, and we will then answer any questions that you may have.

The proposed transaction is the acquisition of Standard Life Assurance. Standard Life Aberdeen will retain their UK wealth platforms. Standard Life Assurance comprises Standard Life Aberdeen's UK and European life and pension businesses with assets of £166bn. The total acquisition price is £2.93bn, the equivalent of 84% of Own Funds.

In addition, I'm delighted to announce a new long-term strategic partnership with Standard Life Aberdeen covering investment management and a new client and services proposition agreement for workplace pensions, retail and SIPP products. This strategic partnership is underpinned by Standard Life Aberdeen taking a shareholding in us of just under 20% in the enlarged Phoenix Group.

The strategic rationale for the proposed transaction is simple. It allows both of us to focus on what we do best. Phoenix will become the pre-eminent closed life consolidator in Europe and Standard Life Aberdeen will focus on its world class investment management business.

The strategic partnership covers two key areas. First, Standard Life Aberdeen will, as it does today, manage the majority of Phoenix's assets. Long-term investment management agreements will cement this strengthened relationship.

Second, Phoenix will underwrite workplace pensions and SIPP products that Standard Life Aberdeen will continue to market and distribute under its own brand. This provides the

Group with an opportunity to access future asset growth. Standard Life will also have the ability to offer products and services to our 5.6 million policyholders, where appropriate.

The acquisition of Standard Life Assurance results in a bigger, but more importantly, a better Phoenix. The transaction will deliver an additional £5.5bn of cash generation in future, a doubling of Phoenix's existing cashflows. The Solvency II surplus will increase to £2.5bn and the enlarged Group will include £240bn of assets owned by over ten million policyholders.

The consideration of £2.9bn represents 84% of Own Funds. This is an attractive price and compares favourably with our prior acquisitions of AXA and Abbey Life in 2016. This consideration is made up of £1,971m of cash and shareholdings in the enlarged Group of just under 20%. This shareholding is valued at £959m, based on yesterday's share price and the size of the proposed rights issue.

The cash consideration will be financed with a mixture of new equity and debt. £950m will be financed from the proceeds of a fully underwritten Rights Issue. In addition, we have underwritten debt funding of £1.5bn, plus our own cash resources that will comfortably cover the remaining requirement.

The financing mix is in line with our acquisition criteria of maintaining an investment grade rating with the Fitch leverage metric expected to remain within our target range of 25% to 30%.

As part of the strategic partnership we will welcome two Standard Life Aberdeen directors to the Phoenix Group Board, bringing their additional skill sets and experience. We welcome this.

Our intention to bring the Group onshore is undiminished, although the timing will be delayed until after completion of this acquisition. With regards to life company governance we will align the Standard Life Assurance Life Board with the existing Phoenix Life Boards.

Phoenix has long seen potential in European consolidation. The acquisition provides an existing European base in both Germany and Ireland. The European Closed Life market is still nascent but offers an additional avenue to create value in the future. We believe that there remains a market opportunity of around £380bn of assets in the UK Closed Life market, up from our previous estimate of £300bn. Germany and Ireland will add an additional £160bn of assets to an overall total amounting to £540bn.

Our disciplined approach to M&A means that any acquisition needs to meet our four criteria. This transaction ticks all of the boxes. This is a UK Closed Life acquisition. It provides a step change in scale of our current Closed Life business, but not by type or by process, it's scale with a capital "S" but it's more of the same, and it's what you pay us to do.

It is accretive. We expect to generate total cashflows of £5.5bn from the in-force book that we are acquiring. Our experience of generating cost and capital synergies from our recent acquisitions also gives us confidence in our ability to create £720m of value from the combination of our businesses.

We can raise our dividend, and we will increase the dividend from the time of the final 2018 dividend and the equivalent increase would be 3%. Of equal, if not greater importance, is the long-term nature of the cashflows which enhance the sustainability of our dividend, and Jim will say more about this shortly.

Finally, the acquisition maintains our balance sheet strength with a Solvency II surplus increasing to £2.5bn but shareholder capital ratio will remain strong at 147% and the Fitch leverage metric will be maintained within the target range, as I said a moment ago.

I will now pass you across to Jim.

Jim McConville, Group Finance Director

Thank you very much, Clive, and good morning to everyone. Before I talk about the proposed acquisition let me spend a few minutes on our 2017 results. These will be announced to the market on 15th March but we have today provided a short trading update.

We've had a successful 2017 with strong financial performance. We have generated £653m of cash from Phoenix Life and we expect to be at the top end of the range of our £1bn to £1.2bn target for 2017 and 2018.

The integrations of AXA and Abbey Life have delivered benefits ahead of the plans we announced at the time of the acquisitions. We have already generated over £500m of cash from these two acquisitions, and the expected annual cost synergies of £27m are £10m higher than originally expected.

2017 saw the completion of our strategy to reduce our reliance on short term bank debt and replace it with subordinated debt with maturities better matched to our cash generation. We issued £835m of Tier 2 and Tier 3 subordinated debt in 2017 and now no longer have any bank debt, with an undrawn £900m revolving credit facility. We also achieved an upgrade in our Fitch credit rating last July.

This slide summarises the key metrics that we've been tracking with regards to the integration of AXA and Abbey Life. Since the completion of the acquisitions in late 2016 we have delivered £282m of cash from AXA and £236m from Abbey Life. The AXA business is now on the Phoenix Internal Model and the policies have been moved to Phoenix Life Ltd, by way of a Part VII transfer.

The Abbey Life business was reinsured into Phoenix Life Ltd at the end of 2017, supporting the release of cash from the business. The application to move the Abbey Life business on to the Phoenix Internal Model was made during the fourth quarter of 2017 and we hope to hear the results of that application relatively soon.

We have therefore broadly completed the integration, over delivering against expectations, and we are now ready for the new acquisition. The experience of our project teams and the lessons learned from these transactions put us in a very strong position to deliver value from the integration of Standard Life Assurance.

Now moving to the transaction. Overall we expect the combined Group will deliver a total of £11.8bn of cash. Our Solvency II position remains strong following the transaction, with a surplus of £2.5bn and a shareholder capital coverage ratio of 147%. This is well within our risk appetite and could be further strengthened through additional hybrid issues. The assets of the combined Group of £240bn is around three times that of our largest closed fund competitor.

Given our strong performance in 2017 we have set a new cashflow target of £2.5bn for the existing Phoenix business from 2018 to 2022. We have a long track record of always meeting or exceeding public targets, and we remain committed to continuing this record. In total we expect £5.5bn of cashflows from the acquisition, an uplift of 87%. These cashflows relate to the existing in-force book and do not include any potential future value from underwriting new workplace pensions or SIPP products.

With regards to future cash generation from the proposed acquisition it is expected that cash generation will be muted in the first couple of years, however there is a significant increase in cashflows in later years, more than doubling expected Phoenix cash generation after 2022. And we will of course update our cashflow targets following the completion of the transaction.

We have already demonstrated the Group's ability to deliver complex separations and integrations through the AXA and Abbey Life acquisitions. These are now very close to completion and therefore the Group will now be fully focused on the integration of the newly acquired business.

The management and support functions for the life companies will be the initial integration challenge where we will be bringing together the strongest skills from each organisation. From a customer and IT perspective the initial focus will be maintaining the existing high service levels. Over time we will examine options to move towards Phoenix's outsource model. These actions will contribute towards an expected cost saving of £50m per year.

From a capital efficiency perspective we see opportunities from hedging certain market risks as well as applying the Group's strategic asset allocation to the annuity portfolio. The combined post tax value of cost and capital synergies is expected to be £720m, including post tax integration costs of around £135m.

We have set out on this slide the sources and uses of cash, including the impact of the proposed transaction. The chart illustrates that the expected cash generation will build holding company cash over time. This can be redeployed on further closed life transactions, or in the bulk annuity market. The analysis assumes that the dividend has increased from the time of the 2018 final dividend.

Given the Group's investment grade rating and the longer term cashflows that are expected from the acquisition we have also assumed in the analysis that any maturing debt will be refinanced.

This slide follows on from the previous one showing the position from 2023. There is significant expected cashflow over the longer term, with the acquisition adding £4.5bn to Phoenix's existing expectations of £3.8bn from 2023. This provides additional durability to the dividend. In addition, we have not assumed any value from new business generated through the strategic partnership which would add to the in-force cashflows shown here.

One of our key criteria for an acquisition is that the level of dividend per share should be at least sustained. As a result of the acquisition the dividend will be increased from the time of the final 2018 dividend, resulting in a new annualised dividend cost of £338m. Based on last night's share price this is the equivalent to a 3% increase in dividend per share. This increase takes into account the cash generation profile of the acquired business and signals our confidence in the transaction. Thereafter, Phoenix will maintain its stable and sustainable dividend policy.

With regards to the Group's Solvency II surplus the transaction will increase the surplus by £0.7bn from £1.8bn to £2.5bn post acquisition. This results in a shareholder coverage ratio of 147%. This ratio does not include any of the expected capital synergies. In addition we have the option to raise further hybrid debt post completion whilst maintaining the Group's leverage within our target range. Both businesses are currently on their own Internal Models and the future strategy will be to have a single harmonised Internal Model for the enlarged Group.

One of the key parts of the new strategic partnership with Standard Life Aberdeen is the new client service and proposition agreement for workplace pensions and retail SIPP products. Standard Life Aberdeen will continue to distribute their own workplace pensions proposition under their own brand, as well as provide investment management services with Phoenix pricing and underwriting the products. In addition, Phoenix will also continue to act as a provider of self-invested personal pensions and drawdown products to Standard Life Aberdeen’s retail customer base.

Phoenix will pay fees to Aberdeen Standard Investments for investment management services. The agreement aligns the interests of the two organisations, whilst ensuring that the new partnership leverages their respective competitive strengths. Therefore the client service and proposition agreement provides Phoenix the opportunity to access assets in the future which will partly offset the run off of legacy products.

There will be minimal capital strain in the near-term, as these are capital light products, and there is significant potential over the long-term to add additional value to the existing in-force cashflows.

I will now pass you to Clive to wrap up.

Clive Bannister

Jim, thank you very much. We are now seeing the active recontouring of the UK life industry, a phenomena that we have advertised for a number of years, its time has come.

The Phoenix sponsored Meaning for Life report anticipated this reshaping with a bifurcation of the industry into those businesses willing to commit capital to underwrite risk and others looking to deliver capital-light, fee generating products. Today’s transaction maps to this industry shift. Both businesses are deploying their skill sets in a strategic partnership for the benefit of both existing and future clients.

Phoenix remains entirely focused on its strategy of delivering value from closed books. We continue to seek selective transactions in the bulk annuity market and, in that context, I'm delighted to be able to announce that we are currently in exclusive discussions with our first external pension buy-in transaction.

The new client service and proposition agreement with Standard Life Aberdeen offers the opportunity to generate future assets and cashflows on a white label basis, as Jim has just described.

We will also continue to write annuities for our own policyholders as well as the over 50s protection products through Sun Life Direct. These are complementary products providing a natural longevity hedge for the Group as a whole. This transaction reinforces our leading market position in the traditional closed life space, brings Europe to the mix and adds growth via our new partner in workplace pensions and SIPP products. Phoenix is firing on all cylinders.

Here is the expected timeline and timetable over the next few months. We will publish the circular and prospectus around the middle of April, with the shareholder vote the following month. The acquisition is subject to normal regulatory approvals and we hope to complete the transaction in the third quarter of the year.

To conclude; this is an exceptional transaction, a game-changer for Phoenix, strategically logical for both partners and financially compelling. This transaction will create the preeminent closed life consolidator in Europe with expected future cashflows of £11.8bn.

Phoenix will now focus on the efficient integration of the businesses and the realisation of expected future synergies of £720m in value.

The transaction also offers future value through the strategic partnership with Standard Life Aberdeen as well as the potential for European Closed Life fund consolidation.

Our recent experience and track record gives me great confidence that Phoenix will once again deliver value for shareholders and policyholders.

Those of you who know me well know that I like history, as a pundit once said 'Nothing is as powerful as an idea whose time has come' this transaction is an idea whose time has come.

So what I'd like to move on to is now Q&A. Jim and I will be delighted to answer any questions, the easy ones for me, the hard ones for Jim and the really exceptionally difficult ones for Andy who's got away without speaking. So, as always, wait for a microphone to come to you. If you would give us your name and the institution you represent and then we will fire away.

Q&A session

Question 1

Andy Sinclair, B of A Merrill Lynch

Three questions if I may. Firstly the £.5.5bn cash generation target for the Standard Life block is that pre or post management actions, particularly if we can split that into 2018 to 22 and 2023 plus blocks?

Secondly, German-backed books can be quite different risk profiles to UK-backed books, could you tell us which particular parts of the German life business would or would not interest you?

And, thirdly, I just wondered if you could explain to me a little bit more about how this workplace pensions relationship works? Do you pay a distribution fee to SLA as well as anything in terms of asset management mandates and is there any change of terms if the charge cap was to be reduced? Thanks.

Clive Bannister

Okay fine so there are three questions there, Jim will you take the first one about the nature of cashflows within the 18 – 22 and 23 afterwards? Andy, will you go through our arrangement on the partnership and then I'll deal with Germany.

Jim McConville

Okay. First of all in the cash generation the £5.5bn splits £1bn over the first five years to 2022 and the £4.5bn comes thereafter. We have included within the £5.5bn the impact of the synergy benefits that I spoke of earlier but, importantly, in the £4.5bn there is no assumption for management actions.

So in the normal course we would expect to continue delivering management actions into the future but as we have always done with the longer term numbers we have put into the marketplace we have excluded these management actions.

Clive Bannister

The partnership arrangements, it’s page 21 I think.

Andy Moss, Chief Executive

Yes, I will talk a little bit about the workplace pensions. So very simply I think as Jim says Phoenix will underwrite and price the workplace pensions. Aberdeen Standard Investments will distribute workplace pensions as they do now. The arrangements from a financial perspective are that Phoenix will collect the fee from the customers and will pay investment management fees away as part of that and then that margin obviously is there for Phoenix to cover both its costs and any future contributions to overall marginal costs going forward.

The default provider in terms of the investment fund will be ASI and that will absolutely continue and we anticipate working in really close partnership, and I think this is a really good example of how the partnership will work, to set basically a business plan for both sides every year such that we’re fully aware of what we’re targeting to do next year. And that will also pick up things around pricing parameters as well, should we have any future changes to the caps on the fees.

Andy Sinclair

Would it still be possible for a scheme to choose say a Blackrock fund and if that's the case do you actually pay anything to SLA?

Andy Moss

So yes obviously the EBCs and the employer selects the fund; Standard Life will be in control of the distribution so obviously there will be other ASI funds available as well as the default fund, but yes in theory that is absolutely possible for them to choose other funds, as is the case now.

Clive Bannister

Andrew, you had a third part of your question which was about Germany, so I want to get things in perspective here. None of the maths that you have seen today includes either the new business optionality in the UK, which has been described by Jim and by Andy and there isn’t a dollar of value in terms of new business attached to our European components of the acquisition.

Two European assets, one is in Ireland and one is in Germany, you've asked about the German one, we’re all very careful about a place called Germany and the nature of the guarantees embedded in some of their products. This is a business which in total is 5% of our future £240bn, so the words “tail and dog” have to be thought about. It has about

480,000 policies, 250 employees. It was effectively closed to new business of the guaranteed type in 2015 and the fee rates were lowered in 2000 down to guarantees which were around 1.25%.

So we thought very hard about it. We've understood the nature of possible liabilities contained therein and it's all factored in the value that we have offered to the vendor. So what I said is this creates optionality for us, it's not there today but the European consolidation is going to take place. We think Germany is an attractive market. You may remember that a year ago Jim and I said we wanted to do another deal in the UK; we'd look at Europe at the end of 2018. When we looked at Europe our preference comes through as Germany and we'd only go to Germany if two things happened – that we could find a German partner with a pre-existing asset. We know that the way we deliver capital synergies and cost synergies is by having a pre-existing asset. What is so exciting about this transaction is it gives us two chips on the European table, one in Germany and one in Ireland.

Question 2

Angel Kansagra, HSBC

Three questions please. The first one is on the operational integration, what's your expectation round, like can you compare this to your AXA and Abbey Life experience to date, so one was quickly integrated, the other is taking some time?

And the other one was on the cashflow expected from the new business, so do you have a number in mind, how much AUM the new business will bring in every year and what will be the profile of the cash, back-end loaded, front-end loaded and so on?

And the third one is on the Own Funds that come with the SLA acquisition, what's the structure of the Own Funds like, is it tier one, tier two and so on? Thank you.

Clive Bannister

Thank you very much for those questions, there are three, one about operational experiences and how much this future prospect will track what we have learned and that is Jim, those comments about AXA and Abbey Life, and I'll ask Andy to talk about that in a moment. The cashflows from the new business and as we've said we've put no value. The scale of those flows at the moment are £2bn in the workplace pensions and £4bn if you take SIPP and drawdown products, and then you can put your own growth metrics and put a timeline against it.

And then the final one is about our Own Funds. Jim do you want to talk about the Own Funds for a second?

Jim McConville

The Own Funds we are acquiring are very substantially tier one own funds with the majority being value in force.

Clive Bannister

So I'll just say something about the headlines of the integration. The majority of the £720m of value that we think we'll generate from synergies comes from capital synergies. That is what we do as a Closed Life business and that comes from looking at our strategic asset allocation and looking at the equity in the VIF and how we will treat that going forward. That is the majority that I have identified today, the majority of the synergies coming forward.

On the cost and operational synergies they will come from both of our businesses, or all of the businesses in the UK to come and no one integration is identical. The inclusion of Abbey Life it was 46 employees, to give you an idea. It was more of a financial transaction, whereas AXA was much more complicated involving locations, human beings and computers.

But I tread on your territory Andy, would you describe our approach and the Phoenix way?

Andy Moss

So if we just quickly go back to AXA and Abbey I think as Jim said in his presentation both of those integrations are now largely complete. Both of them actually took about 15 months to do, so AXA we acquired in the previous October and it's pretty much complete now and Abbey we are very close to completion by the end of Q1. So actually they both took a similar amount of time despite the different complexities.

I think in respect of this we fully recognise the scale and complexity of this business and also the different nature of the business, particularly with the open business as well. So this will take substantially longer, between two and four years to fully integrate.

Question 3

Andy Hughes, Macquarie

The first one is the capital synergies, so when I see the £250m coming off to get to the 2.5 it looks like it's just the cash coming off basically in your numbers, so you're not assuming any increased diversification for the new group which is a bit of a surprise. And so I thought the capital synergies looked a bit mean because I could see you hedging a bit of the unit-linked VIF and adding a bit in for additional annuity asset allocation. But I think they made £150m last year pre-tax from the annuity business, most of which was from reallocating the assets, so is there a lot of upside in the synergies from the capital side? If you could let me know.

And the second question is, are you going to lose some of the assets as a result of the transaction? So Standard Life consistently told us over the years that they have a five star service and that's very important to the corporate customers that they have. Can you remind me how many star service Phoenix has? I guess it's not been a focus of the Group but do you think this could cause some of the assets to walk out the door? Thank you.

Clive Bannister

So Jim while I try and deal with the customer, I'm going to share that with Andy, and then Jim you'll talk about the nature of whether you've under baked or undercooked the capital synergies. You have a group chief actuary looking at you very hard when you say whatever you're going to say.

Jim McConville

Yes indeed.

Clive Bannister

So Andy I categorically reject part of your statement which suggests that we don't care about customers, you didn’t say that but we have put in, and we started in 2014, and identified how we serve policyholders. It matters; it matters first of all because it’s the right thing to do. It matters because it’s economically very sensible to us if you have a big unit-linked book and what we’re about to buy has 70% unit-linked and 20% with profits and 10% annuities. So if you don't maintain that persistency you have a lapse challenge. And so service really matters. And we have always looked to the set of metrics which include estate distribution, helping people with their small pots and their fees. We've looked at FOS overturn rates which are industry leading and below industry standards on complaints. So we feel that we would take enormous care of our future policyholders, the 4.8 million who are coming with this acquisition as we do our current policyholders.

And in that context there are specialist skills which exist in Standard Life Assurance which we must protect because we have a vested interest in the smooth transition of their business from their current environment into our family and we will do everything to protect. Do you want to just talk about what we do on the client side?

Andy Moss

Yeah, well first of all I absolutely reiterate that customers are enormously important; we spend an awful lot of time thinking about our customers. It might be worthwhile ringing out the actual example. So AXA is highly IFA intermediated and obviously we’ve learnt an awful lot from that and also our service to IFAs has not dipped during that time period and also our lapse rates have not seen a big spike.

We are absolutely conscious of that risk and I think the key thing is we’ll actually use the skills which are already there to make sure that we continue to provide that high level of service. It will absolutely be a focus for us. And in terms of the metrics we’ll talk in a couple of weeks about our metrics for the year and I think what you'll find is that we do maintain very high levels of service and different customer metrics.

Jim McConville

Okay finally on the synergies. Andy, as you rightly point out the capital synergies are the majority of the synergies we have identified to date. They come from a variety of actions that we have identified.

First of all on hedging as you know from previous presentations our policy is to hedge our Solvency II surplus position because that very much protects our cash generation. And we will be taking a similar approach here and therefore we’ve identified a number of opportunities to hedge, particularly the equity element within the transaction and the risk that comes from the fee structures that are driven by equity levels.

Secondly, probably next most important, is strategic asset allocation within the annuity fund where we see opportunities to move towards Phoenix’s approach to strategic asset allocation that will provide us with an uplift in benefit.

And then there are a number of things we’ve identified, and it’s early days, but if we think smartly about how we combine the businesses together from our diversification of risk perspective we will see further opportunities that will give rise to capital benefits.

What we haven’t baked into the numbers is any benefit coming from the integration of the Internal Models themselves because it’s frankly just too early to come to that view. So we do see opportunities but we haven’t stopped looking for further opportunities.

Question 4

Ben Cohen, Investec

I had two questions. The first question was just on the increase in the dividend: could you maybe just give a bit more colour as to why a 3% increase was the right increase to go for, maybe in the context I think of with the Abbey Life deal or one of the deals you had a bigger step up in the dividend and this is obviously a much bigger deal?

The second question was just on IFRS earnings, if you could give some indication in terms of the impact of what you're doing to the outlook for IFRS earnings? I presume there's a huge amortisation charge to be going through but maybe you could also reference the underlying IFRS earnings of the business that you're buying? Is what Standard Life has produced today a good guide to be starting with? Thank you.

Clive Bannister

Ben, thank you for those two questions. Jim, you've been accused of being niggardly on the dividends so you will defend that. And then you're being asked to read across from their IFRS and where it may end up in our books.

Jim McConville

Okay. Just on the dividend first of all as you know, just to reiterate, I'm sure many of you do know, our policy is to have a stable and sustainable dividend. It is not a progressive dividend policy. But we have said that on a major event, and by that we mean transactions, we would take the opportunity to review the level of the dividend. And indeed in both the AXA and Abbey deals we took the opportunity to increase the dividend each time by some 5%.

In this case we're increasing the dividend from £197m to £338m, as I said, an equivalent of 3%. And basically what we consider when we're looking at the dividend levels is really the equation of an increase and the elongation of the sustainability of the dividend. And you can see from the cash numbers that I spoke of, there is substantial cash generation coming off the acquired business in the later years which supports the elongation story. We therefore came to the conclusion, and it's art not science, there's no perfect answer here, that a 3% increase was the appropriate answer. And I think if you do the numbers, that leaves us very substantially within the FTSE top 50 as a level of dividend player. So that is the dividend question.

On IFRS we've not disclosed any IFRS numbers in this presentation. Clearly we have our results announcement coming up in a few weeks' time where we will cover the Phoenix position and you'll get a view on IFRS there. You'll be aware of the operating profit we made last year which was very healthy, and we had good results in our half year, and we've continued to make good progress in the second half of this year.

I think if you look in the Standard Life presentation this morning you will find the total profit before tax that has been made for the business that has been sold, and that is in excess of £350m. My understanding there includes investment variances which are positive and some one-offs, but at a future time we will give you a view on the IFRS for the acquired business.

Question 5

Marcus Barnard, Numis

I've got two questions. Firstly, the £50m of cost savings you've identified in your cost savings chart, can you tell me is that within the existing costs of Standard Life as it will be kept? Or is there any assumption within that that you'll move some of the costs within Standard Life onto some of your existing outsourcing contracts? I'm just interested in whether we can see additional scope on top of that £50m for outsourcing of costs.

And secondly a question I asked Standard Life this morning is: the annuity book took a provision for poor advice at point of sale. I think when you bought the Abbey Life business you were very clear about indemnities and guarantees from the vendor in respect of further payments there. I think Standard Life said they've increased the provision on that, but I wondered if you could comment if you have a similar set of indemnities and guarantees in place. Thank you.

Clive Bannister

Marcus, thank you for that two-part question. I'll deal with the second part first, and then Jim, perhaps you'd talk about the cost and the synergies.

We are well aware of annuities and, as you can imagine, are working our way through, as we do at the moment with the Abbey Life and the enforcement action which is there. So we thought very hard in the processes leading up to this announcement in terms of due diligence. We have sought and have received appropriate protection from the vendor so we feel comfortable that we have bottomed that out, as much as one ever can in a world where there are known unknowns. But we know what we're doing and we feel comfortable.

Jim McConville

On cost synergies, if you take the combined cost base of the two organisations it comes to just over £600m, and if you then reverse out the cost of the European operations it's slightly in excess of £500m. So in the context of our declared annual saving of £50m it's slightly less than 10% of the combined cost base that we declared.

Clearly these are early days, but we do see the synergy opportunities coming from a combination of things, thinking about how we combine these businesses in a smart fashion. That includes putting our Life Co managements together and the Life Co Boards together. We will see savings in support functions, supporting both operations. And in due course we expect to see savings from our customer and IT functions as we move towards an outsourced model – but that is some time in the future.

I will point to our experience in AXA and Abbey Life where once we got into the business and understood it better we identified more opportunities, which you've seen come through in the trading update we gave.

Question 6

Jon Hocking, Morgan Stanley

I've got three questions please. Firstly, it's probably a stupid question, but on the consideration is the sterling billion number fixed, or if your share price goes up over the course of the process does the consideration of Standard Life actually go up?

Second question, on the synergy number, I can see you've capitalised them over ten years, could you please give us the discount rate you've used? And is it inconsequential in any event because the PV number really relates to the cost synergies, and actually the capital synergies are upfront? So is there any degree of understatement from the present value of the synergies?

And then finally, I know you don't give the embedded value numbers anymore, but looking at the Own Funds that you've acquired, conceptually if we look at things like contract boundaries for the types of contracts you're acquiring, what are the conceptual blocks of value that might not be properly recognised in that Own Funds versus the sort of embedded value calculation? Thank you.

Clive Bannister

Three relatively complex questions; we may pick some of them up in greater detail at the end of this. The consideration is £2.93bn and that stays on the wire and that stays as it is.

Jim, do you want to talk about again whether – we have two parts on the synergies; we don't talk about our discount rate – but whether we've understated the capital synergies? And the third question talks about our definition, the definition of Own Funds and the contractual perimeters.

Jim McConville

On the third one we will pick that up with you later, Jon. There's a man in the audience who knows the answer and I'll point you to him. So sorry to duck that slightly technical question.

But on the synergies I'll go back to what I said earlier. Quite simply the capital synergies we will see getting to them fairly quickly in terms of certainly some of the initial opportunities, particularly on the hedging. And on the cost synergies, as Andy said earlier, they will take some two to four years to emerge and come through.

But overall in terms of synergies, as I've said, our experience in the past has been we have identified more opportunities as we've gone on. And as you know our business is about identifying opportunities delivered through management actions. And that becomes a recurring theme and I would expect that to flow out in this opportunity as well.

Question 7

Andrew Crean, Autonomous

Two questions. Firstly, could you actually give us the new business profit now for the vesting annuities, the AXA or Sun Life business and the new opportunities coming here?

And then secondly, if you take the £5.5bn what is the discount rate which brings you back to the current price? So a sense of what is the long-term profile and the £4.5bn beyond the first five years.

Clive Bannister

Jim, you've got the new business profit and where we are with that. And then the second one goes back to the discount rate and the treatment of the £5.5bn.

Jim McConville

Yes, on the new business profits, Andrew, certainly for the existing Phoenix business as we've explained before, we need to be careful it's the tail not wagging the dog here, new business profits in the scheme of Phoenix are relatively small, in single-figure millions for the AXA business and the vesting annuities number each year, we write £500m of vesting annuities, and therefore it's not going to change the dial significantly.

We've not disclosed new business profits for this new arrangement. As Clive said, if you take 2017 as the example, on a net basis the new business flows were £6bn. We're satisfied with the arrangement that we have with the client service agreement that that new business opportunity will be profitable for us. But we've not disclosed any figures at this time.

And on the discount rate, I know you'd love us to give you an IRR that you could back solve, but I don't think that serves us well into the future in future transactions and therefore we're not disclosing that at this stage.

Andrew Crean

The profile of the £4.5bn?

Jim McConville

The profile is not that dissimilar from the existing Phoenix book, so it goes out quite a number of years. You have 70% of the book unit-linked, 20% is with profits, and 10% is annuities.

Question 8

Gordon Aitken, RBC

I think you've a good deal and you're acquiring an excellent business at a good price. I've got a question though on how the cash emerges.

You've said that the future cash generation £5.5bn, and you're going to get £1bn out of that in the first five years, so that's about 18%. Now, back in March 2009 when Standard Life reported its results then, I was obviously bottom of the bear market, embedded value was pretty important, share prices were pretty depressed, so I asked the guys in group finance to show me and do a slide of cashflows which emerged from the VIF back then. So we put a slide in the presentation, we did it several times, to see that 47% of the VIF appeared in the first five years. Now, I know that that was a decade ago, but I can't imagine the book has changed that much; so how does that 47% become 18%?

Clive Bannister

You are forearmed with some information that we do not possess, so I can't step it back in time or comment on another company's financial profile.

The maths is the maths as we choose to put in the public domain today, which is the emergence of £1bn of cashflow in the first five years between 2018 and 2022, and thereafter the £4.5bn. It may change when we get to know more about this business, but that is what we feel comfortable saying today.

Jim, would you say anything else?

Jim McConville

Well, I was a very young CFO ten years ago. Yeah, it partly reflects the profile of the business. It partly reflects the fact that with Brexit there are additional costs arising with the subsidiarisation of the German and Irish companies which tend to dampen the cashflow over that initial period. But thereafter it steps back up, as you point out.

Question 9

Trevor Moss, Berenberg

I think the first one might be quite a simple question for Jim actually, which is: you've got to pay Standard Life £2bn odd, and you're talking about raising debt of £1,500m and Rights Issue of £1bn, so that's £2.5bn. Where's the other £500m gone?

Second one, the commercial value of the product manufacturing and service on the new business or on the pensions business effectively of Standard Life, was that part of your consideration when you thought about the valuation overall of what you're paying for, or is this a kind of add-on for you? I know that Andy has sort of partly answered this question already, but how should we be thinking about the value we should be ascribing to that, I guess?

Maybe the third is not actually a question, but perhaps the movement in the VIF, per Gordon's question previously, might be related to the fact that we've had auto-enrolment coming in which will have changed the VIF profile, and pensions freedoms that has extended the duration of pensions business. I wondered what you might think about that.

Clive Bannister

Trevor, thank you very much. Jim, the first question was how are we going to pay for it.

Jim McConville

The simple way to think about the funding for this acquisition is there are three components to it and it's a third, a third, a third. So a third comes from Standard Life's 19.99% stake which, based on last night's share price is £959m. The second comes from the Rights Issue that we hope to announce, £950m. And the balance, just over £1bn, comes from a combination of debt and our own resources. And we've advertised in the past in these meetings the own resources we believe we have.

We have arranged a facility of £1.5bn as part of the underwriting for this deal, as you point out Trevor. It's because I like my cash, quite simply. No, it's to make sure we have sufficient liquidity over the period – it's as simple as that. But the funds which will go out represent the £2.9bn, and it's £1bn from our debt and own funds.

Trevor Moss

Sorry, you're intending to refinance the £1,500 for a lower number? Where's the missing amount?

Jim McConville

Yes, the debt that we take on will be refinanced into the hybrid capital markets in due course.

Trevor Moss

So you're not raising an extra £500m here?

Jim McConville

Not necessarily, no.

Trevor Moss

Not necessarily but possibly?

Jim McConville

Yes.

Trevor Moss

Okay.

Clive Bannister

Jim, what is our Tier 2 subordinated debt trading at now?

Jim McConville

It is trading below 4% at the present time.

Clive Bannister

For ten-year money?

Jim McConville

For ten-year money.

Clive Bannister

Okay. I think can we take, with Simon True, our Group Chief Actuary, whether our movement in VIF may have happened, going back to Gordon's earlier question, perhaps it's affected or not affected by auto-enrolment, let's take that after this session.

And then you asked about in our consideration and what we thought we were paying. An enterprise has many contributory parts, and we have decided, I think appropriately, to look at optionality with regards to Europe and new business because it's not there today. So we were looking at cashflows on an unrestricted Own Funds restricted basis of what will emerge and therefore what we could afford sensibly and appropriately for our shareholders.

But Andy, do you want me to give confidence on how it works with Sun Life Direct where we are in effect the white label underwriter, the provider of capital and the policy administrator, and we have our friends Sun Life Direct going out and managing channel, customers and brands, and that's exactly the relationship that we anticipate, but much scaled up, much larger with our friends at Standard Life Aberdeen?

Andy Moss

I'd just reiterate the point that Jim made earlier that still in the overall scheme of things this is a small contribution towards our overall profits each year.

So with Sun Life we have set that up very much as a distribution unit and it will act very, very similar to the relationship that we have going forward with Standard Life. They are standalone in terms of the way that they market and the way that they distribute; and then obviously the business comes into us from an underwriting perspective and a pricing perspective.

The arrangement will be exactly the same, albeit more complex and obviously a much bigger scale.

Question 10

Oliver Steel, Deutsche Bank

Three questions; I'm sure they'll be fairly simple. I'm sort of surprised at the profile of the £4.5bn, coming back to Andrew's question, because you last took on serious new business 15/16 years ago, whereas Standard Life has been taking on new business until really quite recently. So surely their profile is longer dated than yours? And it is important because we're trying to work out an NPV of that £5.5bn.

Secondly, what's included in the 147% solvency ratio, so how much of the planned synergies are captured within that? And also how much of the debt that you are or aren't planning to issue is included in that?

And finally, do your central costs change materially as a result of this deal?

Clive Bannister

Jim, I think they fall into your bucket. It is interesting from my perspective when we talk about cashflows. AXA delivered a sugar rush, and we targeted £250m release out of an enterprise we'd paid £375m for, and actually we have delivered £282m, and that was at the shape of that profile.

If we look at Abbey Life, a much longer profile. First five years was £100m a year, and thereafter £1.1bn, coming to an enterprise value or cashflows of £1.6bn against which we paid £935m.

So by shape of cashflows we are looking at a much more Abbey Life type deal, and for us that is inherently immensely attractive.

And Jim has talked about the elongation and extension of our dividend paying capability, that runway has gone out longer because the £4.5bn comes in the years after 2023.

So that's a layman's description: everything is different. You'll now have to talk more about that profile and then talk about the component parts of solvency and talk about our central costs.

Jim McConville

Let me deal first of all with our central costs. Central costs representing the Phoenix Group head office are relatively small, roughly £30m per annum. I can imagine some of my colleagues will be coming with pleas that we're now a much bigger business and therefore it should be a slightly higher number. I look forward to these conversations.

Clive Bannister

Very short arms and very deep pockets, I'll just tell you that.

Jim McConville

On the capital numbers, page 20 gives you the pro-forma capital position for the two businesses. That is the pro-forma position based on the December 2017 results and takes no account of the synergies that I discussed during the presentation, either the capital synergies or the cost synergies. So you can expect that as they come through they will result in an improvement in our solvency position.

What they do assume is that as we are buying this business debt free it assumes there is £600m of the funding as hybrid capital debt, and that has already been underwritten, so that we do know that that debt is definitely there.

We still have the capacity to go out and do further hybrid raisings, which again would increase that 147% further.

There's not much more I can add to the £4.5bn. We've not given you a profile of that at this stage. Clearly as we go forward with the business we will provide more colour into the shape of these profiles.

Question 11

Alan Devlin, Barclays

A couple of questions on annuities. This obviously comes with a big annuity book. Does this transaction add any capabilities which will help you accelerate your annuity strategy discussed at your investor day last year?

And secondly, given that it's going to double the size of company, does it also change your appetite for annuities going forward? I was wondering if there are any details you can give on the exclusive deal you've talked about this morning for the first time as well on size or anything to add.

Clive Bannister

Exclusive in what respect, Alan?

Alan Devlin

The exclusive annuity transaction you disclosed.

Clive Bannister

Let's put this in proportion: it's 10%, so what we're buying is 10% annuity, and 20% with profits and 70% unit-linked, going back to an earlier issue about persistency and lapse management. So we don't think this changes the profile of our book today. Our annuities are 70% reinsured. We're entirely comfortable with the longevity risk. As you know our business has three big enterprise risks against it: longevity, long low-term interest rates, and of course credit spreads blowing out.

We haven't yet tested all, and we haven't put in the domain public domain that we understand the stresses, and we think the shape of our business and our exposure to those three risks remains about the same. So I don't think this changes our appetite or changes our risk in the context of annuities.

Then your second question is does it change our appetite to the BPA market. Well, you'll remember in June of last year Simon True stood up and he explained that there is a spectrum of what we called annuities, and it's closed life business by any other name. So at the far end we have our vesting annuities, we did a very substantial pension buy in, and we are looking at the bulk purchase annuity market.

We've been very clear that we're not going to drink from a fire hydrant; we're going to drink from a cup. We're going to do business which is selective, we choose it; it has to be proportionate to the other things that we do; and it has to be funded out of our own, Jim's treasure chest, the money that he has at the Holdco cash, so we're not going to come back to shareholders for that. So we are keen to pursue that strategy, and therefore we are delighted to be able to say that we are in exclusive discussions.

Regrettably I can't say any more at this stage. We may be in a position to say more when we announce our full-year results on March 15th. But we just wanted to say, and there was a slide that I gave, that we look at the business optionality and we now have more strings to our bow, and BPA remains an important string.

Question 12

Andy Hughes, Macquarie

Just a couple of quick questions. The first one was, the £600m cost base for Standard Life you talked about before the transaction, does that include the Standard Life DB staff pension scheme? Because presumably that stays with Standard Life, and presumably if that was in there that would be a big cost saving on its own?

And the second one is, the £2.5bn you're showing on the slides there assumes £600m of senior debt. Could you just quickly get… Does that include the capital synergies you're expecting in the future? Because if I add the capital surpluses from before it looks like it's only taking off £250m, which is the cash resources. Whereas in theory if you're raising a load of senior debt to fund the difference between the £1.5bn and the £600m it should be £900m lower. So where does the £900m difference come from please?

Jim McConville

Just on the £2.5bn which you're referring to, the capital surplus I believe on page 20, that does not include the benefit of the capital synergies that I spoke of. So as these capital synergies are realised we would expect that surplus to increase by an equivalent amount.

And on your first question in relation to the staff pension scheme, that is not included as part of this transaction. The pension scheme remains with Standard Life.

Andy Hughes

That wasn't in your £600m that you started with, it's not one of your cost synergies?

Andy Moss

Just to be clear, the £600m is the combined cost base.

Andy Hughes

Oh, the combined cost base, sorry.

And just coming back on the £2.5bn, because I obviously don't understand this, you've got a slide here that shows £1.8bn surplus at Phoenix, and then another number for Standard Life next to it, so could you just give us a bridge from the £1.8bn plus the other number to get to the £2.5bn?

Jim McConville

The number next to it in the blue bar is not the Standard Life position. That is the pro-forma position for the combined business.

Clive Bannister

That's the 147% SCR coverage ratio on another slide.

Andy Hughes

Yes, the two-way. So if you back one, you've got £1.8bn plus £1bn gets to £2.5bn, but you seem to be raising a load of senior debt to pay to Standard Life and you're using £250m cash resources. So this just seems to show the £250m cash resources being used.

Clive Bannister

Hybrid.

Andy Hughes

The hybrid is £600m, but there's still a gap of £900m that I can't…

Jim McConville

We'll pick it up offline, Andy. There isn't a gap in there.

Clive Bannister

Final question today.

Question 13

Marcus Barnard

Just quickly, the 19.9% shareholding that they take in here, are there any lock-ups on that? Are they free to sell it? Are they distributing it to their own shareholders? They seemed to imply this morning they'd be a long-term shareholder and they were prepared to support future fundraisings. I just wondered if you had any thoughts on that.

Clive Bannister

Yes I do. I'm just trying to find the slide that I didn't show. I started talking and I didn't show this slide; I should have started with it.

One year lock-up is the technical answer to that question. And we expect them to be very good long-term loyal shareholders, because that's what they say and we're dealing with a world-class counterparty.

At a dinner that our Chairman had with Gerry Grimstone earlier in this process, Gerry and Martin and Keith were very clear that they see us as another channel through which they can, as an organisation, gather assets. And so they are enthusiastic about supporting us as we go out and do other sober and sensible transactions, because we will bring assets in. They are our first preferred choice as an asset manager, and we look forward to the closed business which we then risk underwrite and then administer.

So what a good way to end this presentation. I said right at the beginning that this was an important and historic day. This is a strategically logical transaction which we believe is financially compelling. It gives us, it's strategically bang on message, it is accretive, it brings really credible scale to what we do. Two forms of business optionality in terms of Europe and new business. And it's embedded in a high-class quality, durable strategic relationship, a strategic partnership reinforced by a 19.9% investment by them and us. We're delighted.

Thank you very much indeed.