GIVING THE NEW GENERATION OF PENSION SAVERS A BETTER FUTURE

Every generation deserves a prosperous retirement.

We need imagination and innovation to meet the challenges of ageing.

We've developed innovative solutions in the face of change in the world of pensions. The number of UK defined benefit (DB) pension schemes continues to decline, with companies struggling to afford the costs of meeting their pension liabilities. We need to make sure that the shift to defined contribution (DC) schemes also gives younger generations the scope to build adequate levels of pension income. In the UK, the government's 'pension freedoms' mean people who've saved in DC schemes need to plan their retirement income carefully.

Investment management solutions

Our investment management business specialises in providing solutions to the challenges posed by ageing populations. This affects all global markets where populations are ageing, such as the US, parts of Asia and western Europe. The 'Globalisation of asset markets' section on pages 24–25 describes how we're expanding our investment management business internationally.

Our investment management business is the world's 15th largest (by 2014 asset values) with £746 billion assets under management. This is a diverse business, where in the UK we're continuing to attract institutional pensions' funds into both DB and DC schemes. We've almost doubled our DC assets under management since 2011, growing from £23.6 billion to £46.1 billion at the end of 2015.

One of our core strengths is managing index funds, where we have assets under management of £274 billion and are well placed to benefit from the growing global trend towards a greater use of index funds.

Our range of solutions for the maturing UK DB market is expanding and we expect demand for pooled and delegated solutions to grow rapidly as many pension schemes seek these solutions. Our liability driven investments (LDI) and multi-asset business is now our biggest segment with £338 billion of assets and £27.9 billion of net flows in 2015.

CASE STUDY

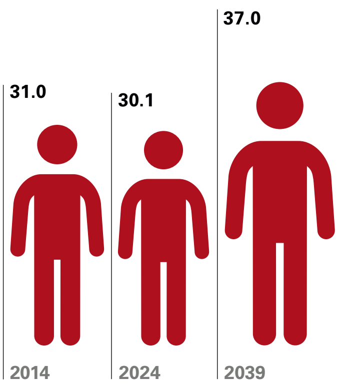
Ageing populations challenge governments across the globe.

Old age dependency ratios show the number of people above pension age for every 100 people of working age. Key influences are birth rates, longevity and migration. In Japan, with its rapidly ageing population and low birth rate, 2014 World Bank data showed there are 42 Japanese people aged over 64 supported by every 100 working age persons. Western Europe also has high ratios: 32 in Germany, 30 in France and 28 in Spain.

Ratios are lower in countries with higher birth rates: US (22) and Ireland (19).

Increasing dependency ratios matter because younger people, usually through taxation, have to support pensions, healthcare and elderly care for retired people. The challenge is to create an equitable balance between taxes paid by working people and state benefits. Encouraging people to save for their own retirements could lower the burden on the state. UK 2014 projections showed the planned state pension age increases could mean that the projected old age dependency ratio will be 34.2 in 2051, instead of 49.2.

Old age dependency ratio



Dependency ratios – number of people above state pension age supported by 100 working persons.

Source: 2014-based National Population projections published by the Office of National Statistics.

Freedom for DC scheme members

While LDI solutions help companies ensure that DB pensions are paid on time and in full, there's a growing need for people who have saved in DC schemes to plan their finances in retirement. In 2015, we developed two new plans to supplement our traditional individual annuity business, which has declined in volumes by 74% since 2013. Our new 'Fixed Term Retirement Plan' and our 'Cash Out Retirement Plan' give consumers increased choice about how to take the money they've saved in DC schemes. However, our experience has been that around 90% of people have taken their full savings in cash, with average payouts of £12,000.

> **We're getting older and need to save more, for a longer old age and the inevitable care costs"**

The average annual cost of elderly social care is estimated to be £29,250, increasing to £39,300 if nursing care is needed. People are forced to take difficult decisions whether to fund care costs from equity in the home or to hold back a large portion of pension capital for later years.

Turning the £1.4 trillion in housing equity into retirement income

It was estimated in 2014 that people over 65 in the UK, were sitting on £1.4 trillion in equity in their own homes. 3.3 million homeowners aged over 55 have been looking to 'rightsize' to smaller homes, freeing up 7.7 million spare bedrooms for younger people who are struggling to find affordable homes to buy or rent. Yet the UK is struggling to finance elderly care. Since 2010, cuts in council-funded adult social care have totalled £4.6bn, or 31% in real terms of net budgets.

We want to give elderly people the choice of moving to a smaller 'last time buyers' home which can be more suitable in later retirement or staying in their own home freeing up some of their equity to pay for domiciliary care. In 2015, our new Home Finance business completed £201 million in new mortgages for people who wanted to increase their retirement funds. The market is vibrant and it's possible that the total lifetime mortgage market could reach £5 billion a year by 2020. Our future strategy involves diversifying our distribution channels and aiming to continue to give increased value to consumers through competitive interest rates and reduced early repayment charges.

Innovation in corporate derisking

We're one of the few companies who can provide a complete suite of derisking services for DB schemes, comprising bulk annuities and longevity insurance as well as traditional fund management and LDI solutions. In 2015, the UK bulk annuity market saw a lower level of activity than 2014's record volumes. The new Solvency II capital regime led us to adopt a capital-lite approach to writing bulk annuities in the UK and we focused our attention on international markets, entering the US and European pension risk-transfer markets. In October 2015, we announced the first pension risk-transfer deal with the US subsidiary of Royal Philips for approximately $450 million, and in December we completed a €200 million reinsurance deal with ASR Nederland NV, a Dutch insurer. We extended our reputation for innovation in the UK, completing in December 2015 the UK's largest medically underwritten bulk annuity deal with a UK DB scheme. This buy-in deal covered around £230 million in pension liabilities, for selected scheme members.

Cutting the public sector pensions gap

The 2011 Hutton report highlighted the growing cost to the taxpayer of funding public sector pensions, which was estimated to be over £1 trillion. The recommendation to move to a DC basis is being steadily implemented by the state. However, expensive DB schemes still abound and we're well placed to help the public sector manage its DB liabilities and move employees into new schemes. In November 2015, we increased our pooled passive investment mandate for a group of seven local government pension schemes to £6.5 billion. We now manage £40.2 billion for 54 local government pension schemes.

SEE THE ONLINE FAST READ
www.legalandgeneralgroup.com/2015fastread

MANAGING THE RISKS

When we write pension derisking business and products to provide retirement income, we have to estimate how long people will live. We call this longevity risk. Longevity and credit, the risk of default by the issuers of bonds used to back our annuity liabilities, continue to be the most significant risks in our retirement business and the largest on our group balance sheet. As well as our capabilities to evaluate and price for longevity, we actively use reinsurance to manage aggregate exposures. Our credit experts in LGIM manage our bond portfolios.

Creating a modern, low-cost, high-pace business.

Launching our new Home Finance business in just nine months. Bernie Hickman, managing director, Legal & General Retirement.

In February 2015, we announced our acquisition of New Life Home Finance Limited for £5 million, a successful execution of our bolt-on acquisition strategy. We also entered into a funding agreement to be the sole funder of new lifetime mortgages, giving us an attractive source of direct investment assets to back our annuity liabilities.

In March 2015, we were already seeing £1 million a week in applications as we kicked off the task of rebuilding the IT platform, changing the branding of the new company in April 2015.

By June 2015, we had already finished the work to rebuild the IT infrastructure, managing to exceed our existing group standards and creating the group's first ever fully responsive website in November 2015 to support the direct marketing of lifetime mortgage products. By developing a modern platform, we were able to improve our service delivery performance time down from 82 days to 24 days from the receipt of the application to the issuing of the completed loan to the customer.

By September 2015, we were getting around £10 million in applications every week, already making use of group synergies with our in-house surveying team. We were also able to benefit from sharing the expertise of other parts of Legal & General Retirement, economists and housing experts working in our investment management business.

£1.4 trillion

in equity in over 65s housing in 2014 (English Longitudinal Study of Ageing (ELSA).