Transcript

Legal and General Acquisition of £3bn UK Annuity Portfolio from Aegon

Monday, 23 May 2016

Mark Gregory: Thank you for joining us this afternoon. I know a lot of you had a busy day today, the Standard Life event, so thank you for joining us after that. So we are going to give a little bit more detail on the transaction we've announced today in respect of the Scottish equitable back book. I'm joined by Kerrigan Procter as well, and Kerrigan will take you through some of the wider dynamics going on in the annuity market as we speak and how we seek to take advantage of that.

Now, hopefully you should have access to a set of slides we just made available on our website so I will verbally refer to it, which slide I'm talking to. Clearly if you haven't got access, you need to find so very quickly because obviously that'll help to navigate the way through the presentation. At the end of that we'll obviously take questions in the normal way. If we can do, though, I'd like to keep it restricted to this transaction and annuities rather than getting onto generic questions. So for those people who'd like to ask other things, if we can keep today focused, I will be grateful. Thank you.

Right, so turning to slide 2 in the pack we've just sent out, this gives a little bit more detail on the actual transaction we've announced. So to get some precise numbers out there, to clear up any ambiguity, so the actual premium paid ultimately, which we agreed yesterday, was £2.93 billion. So when we talk about 3 billion, for those of you who like precision, the real number was £2.93 billion, the ultimate premium paid. These are all annuitants in payment, so this was business sold by Aegon, individual business sold by Aegon primarily between the years 2007 and 2010, all that point in time. So the average age of, on this book is between 70 and 71, so just a little bit more colour there in terms of the shape of the liabilities we've taken on.

As we made clear in our press release and RNS this morning, this is originally by way of form, by way of a reinsurance contract with Aegon, but we are both parties looking to do a part seven transfer into the Legal & General life fund in due course. But clearly that does need regulatory and court approval so we can't presuppose that, but that is definitely the long-term goal that we are, that both parties are moving towards. Clearly at that point it'll cease to be a reinsurance contract and we'll take over all the administration of the annuitants at that point in time.

In terms of the pricing of the deal, and clearly we're not going to give away exactly how we priced it from our perspective, but it's fair to say that all our discipline pricing remains intact. We, as you know, we have a required hurdle rate where we put capital at risk in the annuity market and this deal has certainly met those hurdle rates, so we're… but I'm not going to get drawn any more in terms of the exact dynamics and financials of the deal, simply to say that we have at least met our required hurdle rates where we put capital at risk.

We give obviously a little bit more colour today in terms of the actual Solvency II dynamics. A couple of things to say there; that the PRA have granted that we can use transitional relief for the risk margin that's set up as a result of this, taking this on board, so effectively it has something akin to kind of pre-Solvency II dynamics in that regard. The risk margin has been mitigated by the fact we are allowed to create a transitional in respect of this business.

As a result of that, the net surplus strain, and I do use the word surplus, so this is a combination of own funds going up as well as an increase in the solvency capital requirement, but the net of those two is an increase. It's, sorry, essentially a decrease in our surplus by £50 million, i.e. the SCR requirement for this deal is £50 million higher than the boost to own funds that it creates. And that calculation by grossing up both the numerator in our coverage ratio and our denominator means that it will result in an approximate reduction of three percentage points in our coverage ratio as a result.

In terms of kind of wider strategy, I'll let Kerrigan cover this off a little more, but we have been talking about back book consolidations as one of our nine sources of profits for quite some time and, without getting too excited, there is an almighty back book of individual new annuitants in the UK which we estimate to be about £100 billion, and that's not to say for a second that's all going to come to market, and… but nevertheless it does give some indication that there is a significant book out, books out there.

And it's fair to say I think most businesses now have taken a view on whether they want to be in this market or not going forward. I think Solvency II has created that need for people to clarify in their own minds whether that's a key part of their strategy going forwards or not. And clearly as well as this one today we'll point to the Lucida deal back in 2013, you know, £1.4 billion that we took on board there and, again, a very smooth integration which worked very well so, again, we are… we believe now establishing a track record in terms of these back book consolidations.

That's all I wanted to say on slide two, so moving then to slide three. Again, just a couple of other points to pull off of slide three. Just partly this is just to clarify some of the debates we had when we announced our prelims in March of this year. Just on, so the bar charts on the left-hand side here just showing the Solvency coverage ratio. If we calculated it using what we've called the peer method rather than the PRA method, and just to be absolutely clear what we've included there, all I've done is simply include the SCR and associate and equivalent own funds associated with our, with profit funds of around £650 million. I've simply deducted that from both sides of the equation. I reduced that from the own funds and taken out of the SCR as well.

What I've not done in our case is do the same thing for the circa £80 million of SCR and own funds associated with our in-house pension schemes. I've done it because actually my view is that the scheme is in deficit. I don't think it holds intellectual logic to adjust the coverage ratio accordingly. For those of you who want to have a good peer like-for-like with other people in our sector, it is £80 million is the SCR associated with our pension scheme so you can do the maths for yourself. But to be very clear, the 175 we're quoting here on a, on what we call a peer basis only allows for the adjustment for the £650 million or circa £650 million of own funds and SCR associated with our with profits fund.

I've covered off the point around the impact of this transaction on our pro forma balance sheet, so I think at that point I'll hand over to Kerrigan to talk more generally through what's going on in the market and L&Gs success in that space.

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Kerrigan Procter: Fantastic. Thank you, Mark. I think I'll just do a quick talk-through why LGR has been a growth business and just reiterate our confidence that LGR will continue to be a growth business. Just on slide five I've laid out some of the figures in the story that you're familiar with of course, but I thought it would be handy to put the figures all on one page. You can see the growth story in terms of op cash, or net cash, or op profit live on that page there, and I think a really positive story indeed. Just in terms of a little bit of detail in terms of the Q1 2016 figures on there, £410 million of bulk annuity business written. There was £550 million year to date in the press report once you add a couple of other deals, and individual annuity business you get to the £550 million year to date in total annuities.

Just moving on to slide six, we talk a lot about our nine sources for profit. I won't talk about these in any great length because that will take the time for the rest of the phone call, so I'll just quickly canter down the line there. And I think we tried to be helpful on the right-hand side by saying how we think of this business in terms of capital usage, so a quick run down the line. Back book for cash, you've seen the slides of our annuity portfolio and we've said for the first time we expect that to throw off of £10 billion of undiscounted cash over approximately the next 60 years.

It's a very long runoff, but further on and in the press release we talked about a field of £400 million per annum for the next five years of cash just from the back book. That's just prudence that's in there already. Clearly as we work hard on the assets and source the sorts of direct investments and self-manufactured assets that we like and have started to grow, then there's, I think there's further upside in that. The point there is we think that is very much like a Solvency I-like release rather than Solvency II because of this existence of transitional relief.

A further point, back book acquisitions. So we talked about the £2.93 billion Aegon deal today. I'm sure further questions on that so we'll come back to that later, but just to confirm that's like the rest of the back book. That's Solvency I-like release we think because of the transitional relief. I'll talk a bit in the future about UK capital like front book, but this is this £1.8 trillion of defined benefit liabilities in the UK and we're thoroughly and still enthused about that story.

I'll talk you a little bit about the US pension risk transfer market which at 2.5 trillion is a good $6 trillion. In terms of liabilities it's also a really interesting market to us. Longevity insurance is another market. It's been quiet recently, but we're still interested in that market and keen to participate, helping our clients transfer their pension risk who are in that market.

Lifetime mortgages, you can see there it's not only the 200 million written in 2015, the press release talked about the 150 million written year to date in lifetime mortgages. There's new loans in that market, so that continues to be an additional growth story for us. We have our global reinsurance hub, so L&G re, A-plus rated, Solvency II equivalent and now with registered reinsurer stated in the Netherlands and, again, we think that could be an interesting market for growth.

Individual annuities, clearly a market that shrunk a lot, but we see signs of industry consolidation actually leading to being a little bit more constructive about that market. Clearly it's not as big as some of the big bulk opportunities or back book opportunities but, again, it's a constructive story. Finish off with the secondary annuity market there; well, I guess we'll wait and see. We're reasonably positive about that market, but I'm sure more will be talked about that in the months and quarters to come so I won't say anything more about that here today.

I will touch upon, on slide seven, the UK pension risk transfer opportunity. I think it's always interesting – there's a little pie chart at the bottom which shows it's somewhat less than 10% of the UK defined benefit pension liabilities have transferred from pension schemes to the insurance sector, so there certainly is plenty of upside there and plenty of demand from our defined benefit clients to exit their largely legacy pension schemes. And certainly the messaging around challenges in the retail and steel sectors, shall we say, I'm sure will reinforce the wish of many people to pass on the risks of their defined benefit pension schemes.

I think there's something very similar going on in the US. As you know, we're now participating in the US market. Lots of interesting deals. The potential flight plan there is shown in figures. So $13.2 billion written in the market in 2015, and from what we're seeing it looks like a similar size pipeline or slightly bigger for 2016, so I think a really interesting market. The difference between the US market, many differences, many similarities, but one of the key differences is liabilities.

Pension benefits in the US, private sector pension benefits tend to be not inflation linked and so their valuation is sensitive to changes in nominal rates, unlike the UK where most benefits are inflation linked and valuation is sensitive to real rates. So as we see the potential for that US rate cycle shifting earlier than other markets, and certainly nominal rates shifting, then the affordability of pension plans to buy out we think will increase and so we're keen to be in that market in the long-term, but also I think there's some interest in the short-term as well in that market.

One of the questions we get asked a lot about is longevity reinsurance, so I just touch upon on that in slide nine. You saw some of these figures at the end of year results I think, so gross exposure of longevity risk on our back book ran about £48.7 billion and after reinsurance our net exposure of £37.1 billion, and that's… through doing that we've got established relationships with about a dozen reinsurers and live deals with a subset of those, but it gives us great access to the reinsurance market.

And I think more broadly, when we're answering our clients' needs of pension de-risking we have a lot of skills that we bring to that and I think behind us there's a deep global pool of capital, not just those existing reinsurers but more broadly I've seen a lot of interest in talking to other participants who want to enter the market as a reinsurer in one form or another, so I feel confident that there will be that deep global pool of capital to back those reinsurance relationships going forward.

I'm conscious I've been talking quite a long while now so I'll just finish off on slide ten and pop back to Mark for a few seconds and then open up to questions, but I just wanted to talk about our, what we think of as our USP's in the UK. We clearly have the most extensive UK client reach across the firm. There are 6,300 UK private sector schemes and 3,000 are already our clients. Also, we can uniquely offer clients full steps in pensionary de-risking. That could be a diversification of assets, so it could be LDI, it could be longevity reinsurance, it could be buy in or buy out, or combinations of any of those. We're the only company that can do all those things.

I think the other thing that's important in the market is integrated asset management. So when I think about this business, it is liability driven investment in its purest form and we are of course leaders in liability driven investment in the UK and very substantial of that in the US market. You need a global fixed income capability and you need a real assets and self-manufacturing capability, and you need to bring that together all at speed to deliver to the pace that clients want to work at.

Our longevity management, we've had 29 years in the bulk market. That's given us seasoned longevity data and longevity expertise, and we have 25 people dedicated to research and analysis in the longevity space. I'd say rather than just longevity risks, longevity management, because I think we're an attractive reinsurance counterparty. We think about our longevity expertise, diversified business, financial strength, balance sheet size, client reach and structuring skills then, and I'm sure you can see that lots of reinsurers are keen to work with us as a preferred counterparty.

In… the barriers to entry in the UK DB market are quite substantial. We have over those 29 years I think seen virtually every type of complex defined benefit pension there is and we could administer all of them, but no simple task there. And then finally I think through our brands and through our demonstration of deal execution at pace and meeting all the clients' needs in various deals, clients can have confidence in execution in working with us. So I think those are our USPs in the UK and we are rapidly trying to recreate those in the US, with which I hand over to Mark.

Mark Gregory: Great. Thanks, Kerrigan. So just to finish off then on slide 11, again just here to try and help you a bit, we're just thinking about the future dynamics of the financials of this business. So we have for today disclosed the first time the, if you like, the VIF, the value in force of our L&G retirement business which, based on year-end 15, 31 December 15, £5bn on a discounted basis and £10bn on an undiscounted basis. Not precise numbers, but close enough to give you a directional, and it is that undiscounted VIF which we would expect to flow through and be the operational cash going forward.

As we said in our press release and indeed as we said in our introductory comments, we're expecting that to be of the order of £400 million per year for the next five years. But, as Kerrigan said, that runs off over something like 60 years in total, although clearly it does run down a bit over that time. A couple of obvious points to add on top of that; that is based on the reasonably prudent assumptions based at year-end. We do think there's scope to augment that, particularly on the asset side through, you know, by sourcing more attractively priced direct investments, increasing our proportion of lifetime mortgages.

You know, we've just started that for the first time just over a year ago now. We've written £150 million so far in 2016 and have a target of £500 million for lifetime mortgages this year to add to the £200 million that we wrote last year. Further upside, I mean, we still have reasonably cautious assumptions around the long-term default provisions. Again, we would expect some of that to do better than that in terms of how we incentivise our fund managers so, again, we would hope on the credit side of the equation we could do better than the default allowances we allow for in our best estimates.

And clearly the last effect is as we augment with new business, you know, so the graph at the bottom here, so 27 onwards, for example, will benefit from the £3.5 billion of annuities we've written so far this year. So that VIF runoff there is purely based on the 31 December 15 position essentially which we've written profitable business. Thereafter that will augment the expected release in the year subsequent to any new business that we write. So, again, that should also be a source of augmentation to that VIF monetisation profile which showed at the bottom of page 11.

I think with that it's all the major points we wanted to get across in our presentational piece. At that point I'll open up the call to any questions that you may have. Thank you.

Operator: Ladies and gentlemen, if you would like to ask a question, please press star followed by one on your telephone keypad now. If you change your mind and wish to remove your question, please press star followed by two, and please ensure that when preparing to ask your question your phone is unmuted locally. Our first question comes from Gordon Aitken from RBC. Gordon, please go ahead.

Gordon Aitken: Hi, thank you. First… three quick questions, please. First on strain, there's a very low level of strain in this transaction 1.7%. Quite a bit lower than I understand is usual in large DB bulks. Why is it lower and is this something to do with a lack of competition at that very large end? Secondly on just the mechanics of how this works on the asset side, I mean, how do the assets come across? Is it cash? Is it an in-specie transfer? And what assets would you look to invest in?

And third, I mean, this back book has quite different characteristics to the £6bn book that was bought by Rothesay so it's quite a different book. This is open market. Why did you either win or choose to win this one, not the other? Is it something to do with the open market experience? Would this strain have been materially different on the other book? If you can comment on that? Thank you.

Mark Gregory: Right, I think that's… we'll probably both answer those. Actually, Kerrigan's sitting next to me. I'll let Kerrigan answer all three, but if he gets stuck I shall butt in.

Kerrigan Procter: Very good. Yes, Gordon, I think on the first point, yes, it is an attractive strain and I think an attractive premium. We worked for a long time with Aegon to make sure that we were both happy with the transaction and we're certainly happy with that premium that we charge. Just in terms of the asset side, these are mostly coming across from Aegon in-specie that, as you can imagine, they had a diversified book of mainly Sterling credit, mostly names that we were happy with. There's a little bit of, you know, transitioning but effectively instantly we had the credit spread risk that we wanted and the interest rate risk that we wanted.

Because these were individual annuities, there's essentially no inflation risk in them. So day one pretty much hedged and then it pretty much dropped into the back book and it's working on getting some upside through increased allocation to self-manufacturing assets, direct investment over the coming years, so a very familiar in-species asset book that's come across and leaves us with very, very little transition risk at all.

I think really important to talk about the different characteristics of this book and the longevity risk on this book. As Mark said, these were annuities sold in the open market that Aegon collected mainly in the years 2007 to 2010, so individual annuities in that market. Now, I think the important thing is that this clearly, this external open market option is clearly a market that we've been participating in strongly for many years and indeed were participating in during that period so we were able to compare the mortality, the experience, the characteristics of that book in huge detail against our own portfolio and really get to grips with the longevity risk thoroughly on that book of Aegon's.

And really you could only have done that if you were live and very active in the external market during that period, and so clearly if you think of the people who might have been interested in the book and the people who are able to do that, that pretty much narrows down to, well, I think just one participant basically. So we are very comfortable with that risk, but it would've been harder for people without that experience and back book to get comfortable with I think.

Gordon Aitken: Thank you.

Operator: Our next question comes from Jon Hocking from Morgan Stanley. Jon, please go ahead.

Jon Hocking: Afternoon. I have two questions, please. I wonder if you could elaborate a little bit on the hurdle rate for the deal. You said it's in line with sort of your usual hurdle rate. Yet, are you loading the 150% Solvency II capital against this AA capital? You know, how are you thinking, you know, philosophically about the capital loading? And then secondly, I realise this is the transaction where you benefit from the transitionals, but on a go-forward basis if you're going to do a chunky transaction in Solvency II, well, where are the PRA sitting at the moment in terms of longevity ratio? So they've made a lot of noise obviously about motivations in terms of risk margin, etc. Do you think there's an opportunity to do similarly large deals with longevity reinsurers that don't benefit from transitionals? Thank you.

Mark Gregory: Okay. Cheers, Jon. I'll pick up the first one on hurdle rate. I'll let Kerrigan comment on generally the use of longevity reinsurance and PRAs used on it. On the hurdle rate, Jon, I understand why you want to know. I think we have to take a view that is commercially sensitive from our side. As I've tried to reassure in the past, we do recognise this business is not without risk.

We are deploying shareholder capital to back this business; therefore we are very minded to achieve an appropriate return on that capital and I think I would say it's an attractive return from a shareholder's perspective and I'm not prepared to give it away, Jon, because that's the sort of thing which EBCs and other advisors in the market, if they knew what our pricing basis was they would use that against us.

So can I just reassure you that we recognise it is shareholder capital, we recognise that the business is not without risk and therefore we want to ensure we get an appropriate return for the risk we are taking. We do believe we can manage that risk very well and realise that into real profits but I'm not prepared to give away our precise hurdle rate that we're trying to achieve.

Jon Hocking: Okay, is the hurdle rate the same for annuities as other business you might write across the group?

Mark Gregory: Yes, so the actual risk capital we've set aside is actually, is adjusted for the actual risk of each we take on so essentially if we have riskier business that has a higher capital charge and vice versa so having got the right level of risk capital we're assigning then the hurdle rate for that risk capital remains the same but clearly the actual quantum of risk capital does vary based on the nature of the risk we're bringing onto our balance sheet.

Jon Hocking: Okay, thank you.

Kerrigan Procter: Jon, just on the other point, clearly I can't comment on private conversations with the PRA so I'll just give my broader thoughts on that. What we're looking at here is - when we use longevity reinsurance - we're talking about genuine risk reduction so I think no surprise is genuine risk reduction leads to reduced risk-based capital, ie, SCR, and reduced risk margins and I don't think there's any particular strong objection to that.

And then in terms of counterparties' risk, I think all parties, ourselves included and I'm sure you too, are keen to know that we have robust counterparty management in place so we think a lot about due diligence - really the three Ds - it's due diligence, diversification of counterparties and daily collateral and that's what we resolutely stick to and I think all participants and all stakeholders agree that that's a very sensible framework to work within.

So I don't think anybody's talking about anything surprising and left-field, it's genuine risk reduction and sensible counterparty management wins the day.

Jon Hocking: Okay, thank you.

Operator: Our next question comes from Greig Paterson from KBW. Greg, please go ahead.

Greig Paterson: Two questions; I mean, an investor asked me, they've done this deal, how much economic value's been created and, ie, what's the price? Now, you've dropped embedded value margin on this type of business going forward. I mean, how are we going to judge whether you've paid too much or too little or what the economic merits are of this? I'd like your thoughts in that regard.

Second question is, given the importance of the strong credit rating you have in your marketing message to trustees, and hence the appropriateness of, say, a AA S&P model, what would be the strain that you feel has resulted versus the 50 million on the solvency 1 BBB basis?

The third thing is one of your competitors told me recently that pricing and capacity by reinsurers to take on longevity risk has deteriorated for the primaries like yourselves recently and is that the reason why you have decided not to on-sell some of the risk like you decided to last year on this particular deal?

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Mark Gregory: Okay, thanks, Greig. I'll pick up the first one, say a few words about the second one and perhaps let Kerrigan again talk about why we haven't, at this stage at least, reinsured any of the longevity on this transaction.

On the embedded value created by this deal, we have clearly made several points there; one, we haven't disclosed it; secondly, your point around, that we clearly are proposing to drop EV reporting going forwards.

Obviously on that latter point, just to reassure you, we are working hard to think about, given the market, a value creation metric in a solvency two world and I'm working hard to try and have that in a robust state for the half year so we do recognise that some sense of value creation is still an important metric and certainly one we think about a lot internally so provided that work gets to a robust enough state by the time we do our interims on the 9th August - I would hope to be able to give you some indication of the extent to which the new business we've written during the quarter and the reporting period has created value in a solvency two world so that will have many consistencies with embedded value but clearly we'll factor in the cost of capital associated with solvency 2 rather than the S1 which underpinned our EV disclosure

So we will try and help you by way of value creation. On this particular deal...

Greig Paterson: Just wait one second. In effect you're not going to drop embedded value, you're going to embedded value ..

Mark Gregory: For new business... We're working very hard for new business to give you some sense of the new business value-add, which is - we won't be giving you a full EV balance sheet with all the other features so let's say...

Greig Paterson: How do we judge the merits of the assumption set if we don't have the detailed parameters?

Mark Gregory: As I say, Greig, we'll try and make sure it's as robust as possible and it's robust and we'll clearly make sure it's easy enough for you to interpret how we come at that number so if that means divulging some of the underlying assumptions we will do that as well. We're clearly looking very hard currently just to find a robust basis for doing that for external reporting purposes and that's certainly the ambition as we sit here today so I can't commit to it fully at this stage but we will certainly try and help you understand... We understand that is a question you want to have answered. We will try and help you answer it come the half year and beyond that.

In terms of the importance of our credit rating and the strain this creates to S&P and Moody models, etc, you know, clearly we haven't taken this deal precisely through yet but I would say in the overall scheme of things, you know, you've seen the strain it creates from an IFRS perspective and the solvency2 perspective. In the overall scheme of things, you know, for this transaction, this is not one that's going to create much of a delta between what we disclosed on our S2 impact and how that will be interpreted by the credit rating agencies. You know, clearly we are mindful of our credit rating and we know it is a source of some competitive advantage to us and, you know, we are cognisant of the impact it may have but so this deal has got quite attractive commercials so we would not expect this to have any material impact on the way that the main credit agencies actually think about our balance sheet.

Kerrigan Procter: And, Greig, just on the one on longevity risk, I think a couple of things. Firstly, as I said earlier, we got ourselves very comfortable with the longevity risk; number one.

Secondly and importantly, the existence of transitional relief removes some of the desire to remove that you see under pure solvency two business and really in the presence of those two things it looks and feels just like a further part of our back book. As you can see from the slides, we've reinsured roughly 25% of our back book. It drops into the back book and we'll pick and choose which parts of the back book that we want to reinsure in the future but certainly no huge desire to necessarily reinsure large parts of the back book further from the 25% reinsurance we've got.

So really the point is it sits in with the rest of the back book and we'll pick and choose which parts of that we want to reinsure in the future but no real incentive to reinsure that right now.

Greig Paterson: And pricing, I mean, do you recognise that point, that pricing has tightened a bit by the reinsurers, does that make sense?

Kerrigan Procter: Not obviously. We talked in the press release about a further £300 million ICI deal, 9% reinsurance on that, pricing absolutely fine so our evidence doesn't support that particularly.

Greig Paterson: So the £550; you've basically reinsured a good portion of that.

Kerrigan Procter: Yes. We have, particularly the £300 million ICI deal.

Mark Gregory: Not the individual stuff within that, Greig, just the bulk.

Greig Paterson: Yes, so I'm saying, of that £550, what sort of percentage must we think about as being reinsured? Of the £550 year to date that you mentioned

Kerrigan Procter: Well, I think the 300 million ICI deal does take it to 90% of that.

Greig Paterson: All right, thank you, cheers.

Operator: Our next question comes from Andy Hughes from Macquarie. Andy, please go ahead.

Andy Hughes: Hi, guys. I guess I'm looking at the Aegon press release, which seems to have a bit more information in it than yours and I just want to ask you a couple of questions So if I take the £275 m solvency two benefit and knock off your £50 m strain, does that give me the transitional, which is £225 m?

And I guess the second question is their IFRS loss is £215 mn on sales. Does that mean, assuming your IFRS basis is similar, you're going to record an IFRS gain of £215 mn on the other side?

Mark Gregory: Yes, a couple of things I would say to that, Andy. First of all, it's true that they have their own models and their own accounting and therefore you shouldn't assume just because it's the same risk and the same assets that it appears equal and opposite in our balance sheet.

Clearly we didn't give components on the solvency two numbers, components of the 50 million surplus impact. Clearly that is a combination of own funds going up as well as the FCR going up. Now, clearly we've got our own internal model to calculate our FCR; likewise, Aegon will have their own internal model and likewise we have our own adjustment portfolio approved by the regulator. Again, the MA treatment isn't uniform between different models.

In the overall scheme clearly, to an order of magnitude, the numbers are not a million miles apart but you shouldn't assume that just because they released £275mn of capital that means that we have, that then our site, the £275mn is the equivalent number in our case. But in the overall dynamics of the balance sheet, as I say, we, as Gordon said in his question earlier, the strain here net equates to about 1.7% of the total premium so we're very content, that being a good place to get the efficiency of our balance sheet to and probably something you wouldn't expect fully to achieve in every case going forwards.

In terms of their losses they announced on the transaction, again, you shouldn't expect that to all come through our balance sheet in the year of sales. Some of that will be prudential margin we set aside to be released in the future. Again our number is not exactly the same as the 215 but even if it were to be, that wouldn't all be released in year zero at the point of sale. We would set up, you know, sufficient prudential margins and then release that to operating cash as the experience comes through in line with our best estimate so that wouldn't be a year one profit release in our case. Though we will see a benefit in the new business service but not to the level of £215m .

Andy Hughes: Okay, I just want to check I understand the bit about transitionals so obviously they do it ex-transitionals so the £225 is just - obviously you said the strain is very low but the strain's very low because of the transitional benefit. I'm just wondering what the strain would be ex-transitionals. Is it fair to add the £225 back on for strain ex-transitionals?

Mark Gregory: Not... On your point, are transitions beneficial? Yes, they are. I'm not going to deny that's true but to say the missing bit in the middle is all transitional is incorrect as well. Clearly we haven't divulged any transitionals either now or in our balance sheet more generally so I'm loath to give that away but I would say, you know, clearly it's beneficial to this transaction in the fact that it comes with transitionals.

Andy Hughes: Okay, thank you.

Operator: As a final reminder, ladies and gentlemen, that's * followed by 1 to ask a question. Our next question comes from Colm Kelly from UBS. Colm, please go ahead.

Colm Kelly: Thank you for taking my questions, three questions please and following up from Andy's question; Aegon indicated capital generation uplift of about £30 million per annum - sorry a decline of £30 million per annum. Again, is there a similar impact in magnitude for yourselves? And also on the solvency surplus and ratio, can you indicate whether or not there'd be an impact following the parts having transferred, that's the first question.

Second question is around co-funds and whether there's any provision within this deal for the transfer of co-funds in the opposite direction, or is there any insight you can give us into that?

And the third question is on US bulks. I'm mindful that I think last year in the 2015 industry numbers there were around 300 separate contracts for, you know, under $100 million which, you know, is a supply chain you would have been operating in. Clearly, you know, it takes time to develop a business in that market but can you talk through some of the specific constraints that you're seeing in that market that haven't seen you pick up more of those contracts in 2015 please? Thank you.

Mark Gregory: Okay, thanks, Colm. I'll pick up your first two questions and let Kerrigan talk about the US bulk market. Sometimes I feel a bit like a cracked record here in terms of the kind of... Clearly Aegon have given the impact on their IFRS releases going forwards. Again, our numbers won't be exactly the same. Have we written business we expect to be profitable going forwards? Yes, we have so in that sense you can do your own analysis in terms of how you think it might play out. In our case we would have slightly different assumptions and therefore will release perhaps in a slightly different way from the way Aegon may have had it in their numbers but, as I say, just to reassure you, we have written this business to be profitable for us going forwards, therefore we would expect a benefit coming through op cash and indeed further down the P&L account going forwards.

In terms of any subsequent benefit of the part seven transfer when that comes through, I'm not sure we expect that to be anything at all from our perspective. I suspect that Aegon happen to hold some sort of counterparty risk against L&G so clearly in our case that isn't true so from our point of view there may be some very small second-order effects when it gets integrated into our wider long-term fund but it really second/third at all. I wouldn't expect a second benefit when the part seven transfer goes through from a pure solvency two perspective. There will be some cost benefits at that point. Some of the things we have to do as reinsurers will fall away but from a pure capital perspective there won't be a subsequent benefit when the part seven transfer materialises.

On the question about co-funds, obviously a very cheeky question, Colm, so as always I'm going to no-comment anything in that regard and pass on to question three.

Kerrigan Procter: Yes, just on US bulk fund, as you'll see, we closed our first smaller bulk deal, $65 million in the US. The way the US cycle works, as some of you on the call may understand well, is essentially fewer deals in the first half of the year and more of a flurry as you go into the third quarter and fourth quarter. We are actively participating in bidding for quite a few bulk schemes in the US, at the smaller end also. We have confidence in our longevity pricing, we have the asset management skills through LGIMA in Chicago of course and you may have seen that we've built our administration capability out of LGA in Maryland so we're up and running, ready to go, getting through safe, sustainable annuity, pricing competitively on these deals.

Now of course we go into that mindful that we don't want to win every single deal that we go in up front so we're testing the water, finding out where the pricing lies but really getting a good feel for where the market sits there and pretty encouraged by what we see.

Colm Kelly: Okay, thank you very much, I appreciate it, that's useful.

Andrew Sinclair: Hello, everyone, three quick questions if that's okay. Firstly, you previously talked, I think, about ten billion of bulk annuity transactions that you were currently quoting on. I just wondered where that number stands today and does that include the Aegon transactions, both the one that you've taken and the one that went through off-say and how much is outstanding?

Secondly just wondered if you could give just a general comment on what you've seen with individual and bulk annuity pricing since full year since the introduction of solvency two.

And thirdly, just wondered if you've got any comments on the potential recalibration of the risk margin. The PRA's commentary seemed to suggest that they'd like to see that recalibrated Just wondered if you had any commentary on what you've heard.

Mark Gregory: Okay, cheers, Andy. So I'll let Kerrigan talk to the first two and then I'll pick up on anything we can say about the risk margin recalibration.

Kerrigan Procter: Fantastic. Yes, so the ten billion pipeline that we just talked about - I mean, we think of pension risk transfer business in the round so whether that's bulk or buy-ins, buy-outs, longevity, UK, US, and really think of those things together.

Clearly when we made that comment before that we were mindful of the Aegon deal, what you see with this market is there's always a pipeline of large schemes looking to talk, sometimes those turn into deals this year and sometimes they turn into deals in the next couple of years and sometimes they go away in a few years.

So, you know, I think there's - the Aegon's a chunk out of the market but it's still a very substantial pipeline that we're - that the market is looking at, not exclusively with us but the market's looking at. So I think I feel confident in the sorts of figures that we're talking about in the slides of ten to 12 billion this year. That's certainly feasible, I think, in terms of the deals that are out there; somewhat depends on precise timing and conditions over the year but yes, it's a strong market, strong client desire.

I think in terms of individual and bulk pricing, then possibly a little tightening of pricing so maybe pension pricing up a little bit, deferred pricing up a little bit, probably deferred pricing up a little bit more than pension pricing but from the client's perspective and therefore their willingness to transact, I think that's been completely outweighed by the widening of credit spreads, for example, over the year compared to last year, somewhat offset by the level of rates but really when you think about it, the sort of pricing difference that we're talking about is tiny compared to the swings in the equity markets or interest rates or credit spreads so no significant reaction from clients to indicate a lack of desire to transaction.

And ICI we transacted with last year; we did the big deal in 2014; they were there, working with us, hitting their targets earlier this year.

Mark Gregory: Okay, just a couple of comments on the risk margin recalibration potential. I think it's fair to say there's been a lot of engagement with politicians and regulators around where the risk margin has been calibrated and the impact that it is having. I think generally there's acceptance that it's probably something that needs to be done in due course.

All I would kind of just caution is, even with some following winds, this is enshrined in primary legislation in Europe and therefore it's quite difficult to kind of see a quick fix. I do believe, in due, course, we may see a slightly better outcome than we have currently for the risk margin - we have some quite onerous, hard-wired calibrations factored into the legislation but I wouldn't hold your breath. I think that could well take, you know, Lord Hill's review of, you know, the capital markets review of 2018 to put that into a better place. We hope to find a solution to it before that but in all likelihood, just to kind of manage investors' expectations, I think probably it will take a couple of years for that to come to fruition and again I can't kind of speculate on exactly what shape that might take but I think there is an acceptance that perhaps it has been cut in the wrong place in terms of the calibration so we would hope that would be beneficial but exactly how much and by when I'm loath to give too much assurance on. But it is fair to say there is engagement going on in that regard as we speak.

Andrew Sinclair: Brilliant, thanks.

Mark Gregory: Cheers, Andy.

Legal and General Acquisition of £3bn UK Annuity Portfolio from Aegon

Monday, 23 May 2016

Operator: We do have a final question from Andrew Crean from Autonomous. Andrew, please go ahead.

Andrew Crean: Afternoon, all. I just wanted to ask a question as to how you see the market for bulk purchase annuities this year, whether it'll be second-half-orientated and particularly whether Brexit is something which is holding back some action, and whether your capacity to do deals has been constrained at all by this deal.

Mark Gregory: Both for Kerrigan, I think.

Kerrigan Procter: Yes, I didn't quite hear the last word.

Mark Gregory: Is our budget for this year in any way constrained by the crane transaction?

Kerrigan Procter: Okay.

Andrew Crean: Yes, exactly.

Kerrigan Procter: Yes, so is the market for bulks this year more of a second-half market? Well, certainly, I mean, you've seen our update for the year in terms of bulks. Certainly we had a flurry of deals, you know, in December last year, as you know, that were probably brought forward by people wanting to get in before solvency two came in.

That clearly made Q1 a little bit quiet. Q2 is reasonably quiet but we see strong demand so yes, we'd expect more to happen in H2.

The point around Brexit - I mean, the only point of that is if you're worried about transition risk around an EU referendum, which probably you should be a little bit worried about, volatility of interest rates and FX during that transition so that would need to be managed very tightly, as it was of course for the Aegon deal that we just did.

But it's very much a UK domestic DV run-off problem and you've got global capital and UK insurance capital on the other side so it's not a fundamental issue in the context of these deals, where a quarter is more like 25 years in three months; then just a few weeks to the referendum is no time at all and it won't, whichever result you get won't particularly upset that market.

And the final point in terms of capacity because of crane, well, I think it's back to Mark's point; we have capital, return on capital hurdle rates and if I bring up deals that look attractive enough on those rates then, you know, there's a positive desire to look at those deals.

Andrew Crean: Okay, thank you.

Kerrigan Procter: Cheers, Andrew.

Operator: We have no further questions.

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Monday, 23 May 2016

Mark Gregory: Okay, in that case thank you very much for your interest and no doubt you'll be in touch if you've got any other questions in to the IR team and we'll try and get back to you in due course but thanks for taking the time this afternoon, we appreciate it.

Kerrigan Procter: Thank you.