Legal & General

Legal & General 2023 Full Year Results, Q&A Transcript

António Simões (00:00):

We now have time for questions. So, I'd like to invite Jeff back on stage, and also Andrew, Laura, Michelle, and Bernie, to join me here on stage please.

So, I think the easiest way to do this is to start from the right and then make my way to the left. So, maybe if you can state your name and institution, and then if you could stick to the usual three questions, it would be great. Okay. You can group them into three and they can be nine at the end of the day, but yes.

Dominic O'Mahoney Exane BNP Paribas (00:33):

António, really excited to hear your more detailed thoughts in June. In the meantime, just firstly, a question on, I guess, the impact of bond yields on expected returns. So both in the PRT and I guess the individual annuities business, and in LGC, are you seeing the market adjust for the 300 bps improvement, or increase in, bond yields when they're thinking about what IRR the market solves for, market annuities?

And similarly in LGC, the target set in 2021, the 300 bps ago, I'm wondering whether we should expect the 10 to 12% yield on the alternative assets to be higher, I guess the same for the non alternatives?

Second question just on LGC, Laura, when you think about the binding constraints on your growth in allocation to the alternatives, is it the availability of investment opportunities or is it the availability of cash? Is it essentially demand or supply?

Third question. Just on the annuity in force book, going at gangbusters, brilliant volumes, CSM growth, what I observe is if you look at the OSG release from the in-force, you show us the outlook for the OSG release from the in-force, it actually seems to have gone ever slightly backwards. And in fact, actually I think it's 0.8 delivered in '23. The disclosure is showing 0.7 for next year, or sorry for 2024. Can you just walk me through what's going on there? Am I just missing a feature there? Where is the growth actually landing in that OSG? Thank you.

António Simões (02:17):

Great, thank you. Thank you Dominic. Maybe Jeff, I'll come to you on the third question and maybe you can also mention the impact of bond yields on expected returns and then Laura, I'll come to you on that, but also the second question on LGC. Jeff?

Jeff Davies (02:33):

Sure. Yeah, in reverse order if you like. The OSG, we've had lots of debate over this. It's trying to compare like with like, is what's difficult. What's really happened is we're earning more returns on free assets if you like, but the SCR, the capital requirement has fallen. And so more of the capital requirement is being covered by assets in the annuity business and less is being covered by assets from LGC if you like, where we get the higher return.

There's more cash and slightly lower return assets which are sitting in Andrew's business being allocated to that business. So again, slightly lower returns as well as a slightly lower SCR running off. So on a like-for-like basis, you'll have only have seen a smaller amount of capital running off, but actually there's two things happening, the total cap requirements go back into it with slightly lower return. We've still got the assets elsewhere, which is why the total OSG stays the same. But if you just look at the annuity business, it's almost more self-financing if you like and it's using less of the extra assets sitting around in the insurance business. And so it's really just how you compare those.

Interesting on yields. Yes, the PRT market to some extent is obviously, it's always driven by spreads, I mean rather than actual yields, and what you're looking for there. I mean at big picture level we compare to our cost of capital, cost of equity, cost of capital when we're looking at these returns and to the extent risk-free feeds into that, that's clearly reflected in what we're looking for. And so we are very happy with the returns we're making on the annuity business PRT business, I think we actually said at the half-year, we had slowed some of the investment in LGC, and Laura can pick this up, because we weren't seeing the returns commensurate with what we would expect. The market hadn't responded quickly enough and to some extent even some of the DI back in the annuity book as well. Laura?

António Simões (04:33):

And that's true for the market overall, right? So that has happened to us and to everybody else. Laura, on LGC?

Laura Mason (04:38):

No, just in terms of your two points then, Dom, in terms of the 300 basis points higher, Jeff's alluded to it, we did slow down investing because we were waiting for the market to reprice. And you're right, we should expect higher returns for the risk going forward.

I think in terms of your question on availability of cash versus investments, I mean we very deliberately positioned our strategy around sectors where we knew there was a huge demand for investment. So it plays very nicely really to our strategy where we are now starting moving from just investing our own balance sheet to bringing third party capital in conjunction with LGIM. The opportunities for our sectors, I'd say if anything, are continuing to grow from where we set out our strategy a number of years ago.

António Simões (05:26):

Thank you.

Abid Hussain Panmure Gordon (05:30):

Three questions if I can. The first one on LGIM, it's actually a two-part question, apologies. The cost-income ratio has been elevated for quite a while. Do you see a path for that coming down materially? And if so what is that path? And the second part is does it make sense for you to continue to push into active mandates given the general pressure on margins in that space?

So that's the first question. And then the second one is on GP investments. I saw that there's a write-down on the onto investment, is there any other investments in the amber or red bucket in terms of outlook or valuations? Any colour on that would be helpful.

And then just finally on longevity, I thought the general trend here was that life expectancies more recently have started to shorten. So just slightly confused with the negative variance in the US. If they are shortening, should we not also have seen a release, longevity release on the annuity book?

António Simões (06:41):

Yeah, thank you. Thank you Abid. I'll take the first, and a comment on the second. I'll ask you, Michelle, if you could add to LGIM and then, Jeff, I'll come to you on longevity.

So on LGIM, you know this because you know the industry, it was a challenging year for the industry, actually. Interestingly, we finished the year with a rally that we had towards December. We finished the year with AUM more stable, but overall we had AUM on average down 12% compared to 2022. So I know you asked the cost of income question, but there's a ratio. So starting with the revenues, that was a challenge. But you can actually see, and maybe this links to the second part here, one B of your question. You can see that taking out the outflows of DB, which we benefited on Andrew's business on the other side because a lot of what's left from LGIM became PRT.

You can see that excluding that, we had a 0.9 billion, so almost a billion of positive net flows that generated 24 million pounds of positive ANNR. So our strategy to go towards more higher margin products, it's working, there's more to do there. And then second, the cost control and Michelle can talk to this, in 2023, despite inflation we held costs broadly flat. So yes, our revenues came down and therefore our cost to income came up, if you see what I've just mentioned. Going forwards, today's about the full year results. On the 12th of June, I will talk about strategy, but it is a business that is a strong contributor to Legal and General and we want to build on it. I'll come to Michelle, but just onto was a first half...

So in the second half we didn't have any other similar write-downs. I said, I'll repeat exactly the same words. We are doing a full review of all of our businesses as you'd expect. There's a lot of strong businesses to build upon, but what will come back to you on the 12th of June is where are we growing? What are the growth opportunities? But also you'd expect me as a new CEO standing in front of you to do a full review of all of our businesses. So not anything else to say today in terms of 2023 results, but you can expect to hear more on the 12th of June. Michelle, do you want to add a bit more on asset management and then I'll come to Jeff for longevity.

Michelle Scrimgeour (09:03):

Thanks António. And we should recognise it's a challenging industry and, actually, when I look at cost income ratios across the board, we're in the pack, so elevated but in the pack. And as António has said, that is not about cost, it's about revenue. And actually the long-term strategy to diversify our business, to internationalise our business is beginning to pay back. We're confident that is the right strategy. And so active has an important part to play in that. What you'll continue to see from us, there is discipline and focus and execution and that will just be part and parcel of how we run the business day to day.

António Simões (09:44):

Jeff, over to you.

Jeff Davies (09:47):

You're right. As in we are seeing a slow-down in longevity. We are seeing adverse mortality. It was mostly the front end of '23. It was, if you're really geeky, by the end of '23, we were back at sort of 2019 levels of mortality, especially in the annuity portfolio. But we absolutely think that we will see that continue to trend down to all levels with flu, covid backlogs in general in the health services of US and UK. What you see in our numbers is you see we had a provision but we still had slightly more adverse experience in the US. We said it didn't improve quite as quickly, but it's significantly better than the previous year, towards the end of the year actually and the start of this. We're starting to see more positive results in the US, long may that continue for many reasons.

That pesky IFRS17 means the release on the longevity that we did put through gets put into the CSM and deferred over time. So you don't see so much coming through in the P and L, whereas you recognise the adverse mortality experience in the US straight away. So yeah, we put through, you saw it in my slide, the CSM increase as a result of the longevity increase. And so that is already coming through and we took again a prudent move to the next table. We believe that there will be adverse experience and poor mortality for a period of time before we return to normal levels.

António Simões (11:17):

Yeah, thank you. Go to your right, and then, yes.

Mandeep Jagpal RBC (11:22):

Three questions for me please. First one, on the S2 margin for UK PRT, looked like it came down from 8.9% last year to 7.4% this year. What were the drivers there and what is the outlook for this margin going forward? As it looked like the IRS margins were flatter. Second one is on funded re, utilised an increasing level of funded re, last year, how do you evaluate which deals to use funded re on and what level should we expect to be utilised going forward, especially with some of the large deals in the pipeline?

And finally, on LGIM outflows from UK DB were a key driver of overall net outflows. Aside from offering these clients PRT, are you looking at whether there are other asset management products that you could develop to keep these flows within the group?

António Simões (12:15):

Yeah, that’s all very good questions. So why don't I just do the key points first and then I think Andrew, I'll ask you to comment on the first and the second, maybe Jeff, you want to cover particularly the difference between the IFRS and solvency to a different evolution of the two margins. And then I know that we have some exciting plans, we have announced to market in terms of bridge, I think it's called, Michelle, so I'll come to you on that.

So in terms of funded re, I want to make a point on that. So as you know, we use funded reinsurance as a way to diversify risk and overall it's still a small proportion of our overall annuity book and we want to continue to do this in a controlled manner, but it is a logical tool for us to continue to use energy, so we did that in the Boots deal and more in 2023.

Do you want to cover maybe in order, maybe Jeff first, just the difference between the margins? I'll come to Andrew and then I'll come to Michelle.

Jeff Davies (13:20):

Sure, we'll do it that way. Yeah, so you're right. It's funny isn't it because it went down for solvency two but went up for us. It was broadly flat you said, but it went up.

And it's just the different bases around them, different use funded re and the different asset mix as in one has more prudence in one basis, one doesn't in another basis. The way we look at it is these are broadly in line with where we'd expect them to be, long-term average. They vary depend on the mix of business with duration that you've got in there, the sort of assets you put to work. So we are absolutely in line with what we'd expect our returns to be. And you say what's the outlook for them? Andrew will talk at some point, I'm sure, about the big demand in the market, but we will only do the business if it's hitting the returns that we want it to. And so you expect a certain level of returns from us in line with these metrics. We continue to do that. We continue to focus on low strain levels. Good VNB metrics. Good IFRS, CSM being added each time. And so we're very comfortable with where these are. I mean it's any half period or even a year, it's very difficult, the movements between them, because there's so much that goes on behind them.

António Simões (14:34):

And Mandeep, thank you for the question, because we did debate that a lot actually, the two numbers. But I think the point that Jeff is making is very important. The discipline, and this is important for me as a new CEO to say, our discipline in pricing is the same that it was six months ago and 12 months ago. So we are, Andrew should talk to what is a very healthy pipeline of PRT, but we're being disciplined from a pricing perspective. And what you see in the second half is good pricing in those two metrics. Good profitability. Andrew.

Andrew Kail (15:03):

Yep. You're right. You've seen this year a high level of funded reinsurance in the book than we've used before. We think about that very carefully. It's part of our strategy compared to our own assets, our own returns, making sure, as Jeff said, we get the right return on our capital, and funded reinsurance has been important for us to deliver the results we've delivered this year.

We look at it at a portfolio level, at an individual deal level, too, so depending on the size of the deal. And as you say, the larger the transaction, then maybe the more likely we'll be to use funded reinsurance. But it's something we think about very carefully, and certainly the controls, the processes, and how we think about that is something we evaluate across the business.

António Simões (15:39):

Yeah. And the final question was on DB. Just to mention this statistic again, over the last three years, 88% of everything we did on the PRT side came from Belgium. So not all of those schemes were just dealing with Belgium. Of course they had other clients. I would love for us to be the single asset manager working with them, but there is a huge overlap. Actually last year that overlap was even higher. It was close to 100%. And Michelle, maybe you want to talk about Bridge, which we launched-

Michelle Scrimgeour (16:11):

Yeah. And maybe just to develop that a little bit, important to say that it's not a surprise what clients are doing. An entirely rational response to what's going on with rates. And the way that LGIM works with clients over many, many years is to get them into a position that at some point they could go to transfer, pension risk transfer. And so that works very well. So what you're seeing from clients is an entirely rational response to reshaping. And it's important to know that some of these outflows are actually reshaping our portfolios, so it's, how do they take what they have today and get themselves in a better position given where rates are? And that is something we pay a lot of attention to.

What António is referring to here is, that works better for some of our larger clients. There are a number of, a bulk of medium size and smaller clients who can't necessarily access that, and we are looking at ways in which we can work with them to bring them to a similar outcome. And actually I think it's really exciting. But part of what we also do, the LDI and solutions book is a big part of what we do. There is also, how do we think about alternatives for many of those clients, depending on where they are and how well-funded they are? But that's when the whole organisation comes together. So actually, I'd say it's an entirely rational response. It's something we think about very, very carefully and work closely with our clients on.

António Simões (17:41):

Thank you. Thank you, Michelle. Thank you, Mandeep, Andrew. Behind you, yeah.

Andrew Crean Autonomous (17:49):

Could you tell us, on the treasury hold co assets, how much do you want to hold at hold co? Secondly, could you talk a bit more about development of private assets? You've got an awful lot of PE competitors who are looking for liabilities. You have the liabilities, but do you need to build your capability in private assets? And then thirdly, you talked, António, about a simpler business model or a simpler way of communicating. And I just wonder, there's an awful lot of noise now in IFR 17 as to whether you switch the emphasis and communicate to us through Solvency II metrics.

António Simões (18:32):

Well, thank you for the suggestion on the last one but Andrew, to your point, I think maybe a reflection. And I'll ask Jeff to answer hold co, and maybe both Michelle and Laura to say a word about private assets. But just on your point, I have been meeting shareholders but also potential investors. And in this side of the Atlantic is mostly shareholders. On the other side was mostly potential investors. And I think there's something about, that comment for me is about simplifying the investment narrative, the investment case.

I think we need to talk about our strategy first. And I was very deliberate about saying, "A clear strategy," and in a simpler investment case. And your point about metrics, I'm sure we'll take that on board. So without commenting on that, Jeff. So treasury hold co, and can you answer that? And then I'll come to Michelle and to Laura.

Jeff Davies (19:23):

Sure. Yeah. The simple answer is, as much as we need, but I don't mean that in that the way we absolutely run the business is we remit from, especially the insurance business, from LGAS, what is required to the business. Treasury only has a mandate to sit on cash, so we don't want to be sitting on cash, whereas we can plan the liquidity requirements for the insurance business and invest in higher yielding assets as required rather than move them out and just sit on them a group.

So what we do over our plan period, over each year is we remit. We see how much LGIM makes, how much it's passing up, a couple of other avenues, and then we basically move the rest out of the insurance business. So we have what we need at hold co cash. Should we change our view of how much we need over a 12, 18 month period, we will remit more up and therefore sit on that for a while before we spend it. So it's not that there's any issue in liquidity or access to cash. It's a case of, it makes sense for us to hold a sensible amount there that we need over a period of time subject to the next dividend that we're going to then bring out of the insurance business.

So you've seen the levels. It usually is about the same level, 1.2, 1.5, 1.7 billion, depending on the timing of dividends that we've passed up will be what you'll see if you look back over the years in what we've been holding there. And then the rest of the cash and liquidity sits in the insurance business.

António Simões (20:44):

Michelle, do you want to start with the real assets within LGIM? And then if we could, Laura, talk about LGC, please.

Michelle Scrimgeour (20:51):

Yeah. And Laura and I work very closely together and I think it's important that, as we are going out to clients, that that is how the market sees what we do. On the investment management side, we have a strong position in real estate equity. We have a very strong position in private credit. Of course we are managing assets on behalf of the firm's own balance sheet and on behalf of the annuity book. We are externalising that, and part of that is by adding capability. We brought in a team in the US to bid out US real estate equity.

It's also about how we take what we've originated already out to clients, some of the partnerships that we have already. A really good example of that is with a fund that we have launched with NTR. It's an investee company of LGC. We've raised 400 million euros so far in a clean power fund and we expect that to continue to grow. That's one example of what we're doing to bring LGC's capabilities to LGIM third-party clients.

Laura Mason (21:55):

And the only thing I would add is just in terms of, I suppose one of our secret sauces in winning PRT business has been having the understanding of liabilities that we do and the ability to originate assets that work extremely well for a PRT. So in terms of the duration, the spreads, the inflation linkages, which I do think we have quite an advantage over some of the newer players. But the short answer to your question is yes, we need to keep evolving that to keep ahead.

António Simões (22:25):

Yeah. And Andrew, in my 9 trillion number I gave earlier, giving quite a lot of big numbers, we see in the global asset management industry, private assets to continue to be a big growth. And implied in your question was, do we need to do it ourselves or do we do it through others? We believe we should be doing it ourselves. And we'll come back also on the 12th of June in terms of, what role does that play from a strategy going forward? Thank you. If we finished that section I'm going to move on.

Farooq Hanif JPMorgan (23:03):

I think in the presentation, António, that you gave on flavours around the CMD, you're talking about your existing franchises. And I think you're being quite careful about that, but it's normal for the markets to worry when somebody new comes in, that you might look to build inorganically. So what can you say about that transformational or bolt-on? Do you think, for example you mentioned private assets, would that be something to look at?

Secondly, maybe a slightly stupid question, do you think you have lots of surplus capital? There are lots of ways of looking at that. You've reduced your interest rate sensitivity so I would say yes, you do. But what about rating agencies? What about leverage, cash? How would you answer that question, basically? And maybe a very last question: given all the PRA noise on funded re, are you very happy that you're doing all of the stress tests and doing all of the modelling around that already that the PRA's going to ask for anyway? Thank you.

António Simões (24:14):

Thank you for the very good questions. Maybe on that, the easier answer, starting from the last one is, as I said, we use it in a considered and controlled manner and it is a small part of our overall books. So we will continue to work with the PRA, and so we're reasonably comfortable there. Just on the other two. In terms of M&A, I think there's a sequence to this, which is, we set out our refreshed strategy to you on the 12th of June, which I don't believe in M&A for the sake of M&A. We need to be very clear about, how do we build on a very strong set of businesses? And so would bolt-on acquisitions be a part of that? Potentially. But I have a healthy scepticism about M&A in general. So I think we really need... we have a great business to build on.

A lot of the opportunities in front of us are organic opportunities, as I mentioned in my other slide earlier. None of that necessarily implied M&A. But we may need, at some point, to literally bolt on capabilities that we don't have. So I would be open-minded about that. In terms of Solvency II, I think we need to, overall capital position, we need to step back, which is, well, first we've just paid a 5% dividend and the board is committed to paying a 5% dividend for 2024. And what we will do in June again is to outline, what is our strategy and what is our capital allocation and capital distribution policy? Which actually is in line with what we said at a half year. We compare the returns of growth opportunities with the alternative, which is to return capital to shareholders either through dividends or share buybacks. So that is our position.

You're right that, within that, we then look at both capital and liquidity and other aspects, but I don't think there's much more I would like to say on that unless you feel strongly that there's something you want to add.

Jeff Davies (26:12):

No, except I would just slight word of caution. I know it's very exciting that we're down to only... we've lowered the sensitivities. We do think they've got a tiny bit. We were a bit longer at the year-end, and so where it's 10% or 11%, it might be 13% in our medium term, is where we'd possibly look at. Maybe not. It's a great position to be in, as you say. We've removed a lot of sensitivity from the balance sheet.

António Simões (26:38):

Agreed. I think the number today is good news in that sense, from a sensitivity perspective. It gives us strategic optionality. We need to come back clearly on the 12th of June. What is that capital return framework? Which, by the way, was also one of the comments we have from Fahad, so I can just take that one off. Can we expect a capital return framework on the 12th of June? I'm reading this from the online questions. So Andy? And I'll come back to you.

Andy Sinclair Bank of America (27:02):

My first question I always ask is, LGC's cash generation, can you give us that figure and how that compares to operating profits, and the sources of that cash? The second question was just on the Solvency UK reforms coming through. From what we've seen so far, what's actually changed in practise for Legal & General? Has anything really changed other than getting a few extra percentage points to the Solvency II ratio? And the third question was just on property revaluations. Real estate, what have you seen over the past year? How have you revalued the portfolio over the past year? Thank you.

António Simões (27:46):

Jeff, can you-

Jeff Davies (27:47):

Sure, yeah, I can do all of those. Yeah, the LGC cash, I knew it would come. Yeah, it's a good healthy number in excess of the operating profit. We're looking at 600 plus. And so as we've said, it will vary period-on-period, and we choose to reinvest a lot of that back into the business. So that's a good healthy number which, again, gives us optionality over time. What do we decide to do with that? When do we choose to invest it? When do we choose to slow investment around that?

Yes, Solvency II reforms. Well, of course the only part that's really been enacted so far is the risk margin, so that's really all that we've seen. We're still working very, very closely. Mr. Steadman's still here and working with Brian in his new role, working with the PRA and with the industry around what it means. We've got people in Andrew's team really challenging what that can mean for, what are the right asset classes to go in? I think there are a couple of asset classes we're potentially looking at that could benefit from the highly-predictable, but as yet there's no real economics were put in through. But clearly we like the removal of what was called the Triple B cliff, the risk of downgrade to sub-investment grade is good around risk management. It's a good thing for the industry. It removes some of those cliff-edge risks that would be there around selling in extreme events, et cetera. So that's very positive in the way that we look at things.

But we'll continue to work with the PRA, and when the next version comes out we'll be able to put numbers on it ourselves and think about, what does that really mean? And we'll start to see that coming through in assets. Property revaluations, as ever there's no one single number, but you saw our investment variance quite a bit in the annuity portfolio is the residual value notes, as we've called them. The residual bits of property that we have on the very long leases. So for example, 80% of our offices are to the government, HMRC. They have 22 year leases, but some of that is a vacant possession value of the bit of property that we don't put to back the annuities. If those are...

... property that we don't put to back the annuities. Those have come down about 10% or so, just because you just reflect higher rates and higher return assumptions, that gives you a couple of hundred million in there. It's just market to market. That then is cash flows for twenty-something years. So, this is about, what is that property worth in 20 years? Do we really expect to have it on our balance sheet at that point, et cetera.

So, that's really what happened. A lot of the assets in Laura's world, some been more resilient because the specialised commercial real estate, we've definitely seen that. Some of it has been catch-up because private assets takes a bit longer to come through.

Larissa Van Deventer Barclays (30:48):

Three questions, one on bulks, one on LGR and then on one on LGC, please.

In the past we have seen bulk annuity volumes heavily weighted towards the second half of the year. With the current momentum and volumes, do we expect that to be the same, and can we reasonably assume that L&G will continue to chase those aggressively until we have the new capital plan?

On LGR, if we consider the CSM runoff, if you look at the accreted interest and the new business and you take off what was recognised in earnings, it was broadly flat, and then the positive growth came from assumption changes. How should we think about the drivers of growth for the LGR CSM going forward?

And lastly on LGC, tough half year for housing, shall we expect it to remain housing-dominant and... Well, if/and how do you see the release of component parts of that portfolio evolving over time?

António Simões (31:51):

Great. Thank you, Larissa. And thank you for being patient earlier. I know you had the microphone and we took it away from you.

So first was the second half, first half, second half from a PRT perspective, then. Retail will come to Bernie. And then Laura, in terms of LGC.

Just on, maybe Andrew and/or Jeff may want to comment, but we do see this profile skewed towards the second half. It's true this year as well. But as, Andrew, you mentioned earlier, we have a healthy pipeline of PRT into 2024. As you know, we're the record market as well, not just as Legal & General, and we expect the projections are the same for 2024. Do you want to add anything on that, Andrew?

Andrew Kail (32:36):

Yeah, maybe just a few comments on the general pipeline, Larissa. I think in the industry there's always the sort of deep intake of breath and people relax for Christmas and you start to get in the new year. I mean if you just look at, generally, and everyone in the room will see the estimates like I do, of the size of the pipeline. The most interesting stat I heard in the last few weeks, is one of the employee benefit consultancies saying there's some 250 billion of schemes now in the UK that are at buyout funding.

So, if you think about the level of potential demand, that would be five years of transactions if you go on 23 volumes in a much higher multiple of previous years. So, I think it's fair to say, at current levels of funding, there's the ability for the trustees to look, with their advisers, for buyouts. It is very high and we would expect that the 24 volumes will be at or around the 23 level. So, 50 billion or so of transactions, potentially even higher.

A few things to remember. One is it is definitely seasonal, and that we are seeing now at the current time, probably 15 transactions that are being shown to us over a billion. Those big transactions are likely to, not many of those will complete in the first half, which is even if they're live now, they'll take some time to complete. It's why you'll get the weighting.

Then when it comes to the very large schemes, how they transact and when they transact makes a big difference to the market. And so if the very large schemes don't quite get over the line by the 31 December, they'll go into next year, or they split the transaction to multiple parts and therefore the very big scheme becomes a number of smaller schemes. So, I think it's still second-half weighted, but still very high levels of demand out there from trusting their advisers to ask us to quote on transactions, which obviously we are.

António Simões (34:17):

And just to manage expectations, and this is an important point, it is very lumpy. Maybe that's an obvious thing to say, but had we not done Boots right at the end of the year and let's say that Boots had ended up being in January, we would showing you a very different what we would probably be talking about, that number.

So, for 2024, expect the same thing, because some of the schemes are quite lumpy. So, in a way it may well be that I'm here in August talking to you about a great first half where some of those deals might end up being in the second half. So it's lumpier than, let's say Bernie's business, where we know what's happening in individual annuities or in protection because it's more of a retail business. So, just to state the obvious.

On the second question, maybe do you want to give a broader view on CSM? And we haven't talked about retail, but maybe you should-

Jeff Davies (35:06):

Sure, yeah.

António Simões (35:07):

... answer first, Jeff, and then Bernie.

Jeff Davies (35:09):

I think, Larissa, your question was more of the bigger picture that we had added how much CSM, how much did we run off, and then where's the growth coming? It was interesting, Andrew did a different number and said it was grown at 4%. So...

Jeff Davies (35:33):

Yeah, that's right.

Well, actually there's a general point on CSM runoff and Bernie can comment, because actually the biggest influence was retail protection probably last year, I would say. There's a general point that yeah, we are showing good growth without the longevity and I think it's important to see that even without... The profits of the businesses grow at a faster rate than the actual CSM.

As you get growth in the expected returns, you get some of the back-book optimization, the risk adjustment growth. And so we're aligned with sort of where we'd said before that we'd expect our profit, say on the annuity book to grow at 6, 7%, if you're writing 10 billion per annum from what you're adding. And actually we're seeing more of that come through in the higher rates as well, because you get slightly faster runoff, et cetera, and higher investment accretion around that. So I think it's useful to look at that rather than just the pure CSM growth. There's some other stuff.

António Simões (36:26):

Yeah. That's a good point. And on retail, Bernie?

Bernie Hickman (36:31):

... the CSM kind of runoff. So that's in there for you. But at the end of the day it is going to follow the performance of the business. And last year, yeah we've got three great protection businesses. Obviously US is doing really well and that's adding healthy amounts of CSM from a new business perspective.

Group protection is also well, but it's quite a short-term business, and retail protection was one that was impacted by higher interest rates, and the mortgage market was also very subdued last year. And so volumes were down. As we say, frequently we take a very disciplined approach to pricing as well. And so there was some poor quality business that we deliberately bought back from last year. We're happy for our competitors to take that on, and that will be coming through to their book going forward. So we are expecting an improvement in margins, and that will flow through to the CSM, going forward.

António Simões (37:30):

Thank you. Thank you, Bernie. And housing, LGC?

Laura Mason (37:33):

Yes, so you're right. Housing has been a tough year for housing, particularly private for sale. Having said that, I do think CALA has performed relatively well. I mean there's been a lot of analysis of the listed house builders, but to put that into perspective, sales rates for CALA are at a level that they were sort of pre-COVID, so a very good sales rate per site. Our average sales prices above or just tiny bit above where it was in 2022. So, relatively really good performance.

I think in terms of the second part of your question, in terms of this overall portfolio and the weightings, probably the best way to think about that, is three buckets. Yes, housing, CALA's part of that. We also have our affordable housing business, our rental businesses. The second bucket being around clean energy, climate transition and specialist commercial real estate. So, digital infrastructure, what we're doing in life sciences and with universities. And the third, alternative finance, which includes both Pemberton and venture capital.

So, some really good tailwinds in those other buckets, particularly private credit in Pemberton and climate transition and commercial real estate where it's going in terms of the need for digital infrastructure, the need for universities to have different types of accommodation, which we're working very closely in some of our partnerships with, in both Oxford and Manchester.

So, definitely the portfolio is becoming more diverse in terms of the different opportunities we have going forward.

António Simões (39:05):

Thank you. Thank you, Laura. Thank you, Larissa. I think Rhea had a hand up there. Yep.

Rhea Shah Deutsche Bank (39:12):

Three questions. So the first, just going back to LGC, during your capital market, so a couple of years ago, you mentioned the ambition for 500 to 600 million of operating profit for 2025. Are you still on track for that, even with housing maybe being a bit slower?

And then secondly around LGIM, I mean 40% of the AUM is now international. Do you intend to grow that a bit more? And if you do, would that more towards higher margin assets to grow the revenues?

And then thirdly, just around consumer duty, the back-book implementation will be happening in July. How does that affect you? And just more broadly, António, you mentioned that you have 12 million customers, how are you thinking about that from a wider consumer duty and support standpoint?

António Simões (40:12):

Thank you, Rhea. So Laura, if you can answer on LGC, and then I'll ask, briefly, let's make the answers shorter. From an LGIM perspective, we did say that not only it's 40%, but it's been growing 80% since 2018. So the international part of LGIM has been growing faster and you'd expect that to continue. From a strategic perspective we'll come back more on the 12th of June, so maybe there's no need, Michelle, to repeat that.

And on consumer duty, we have implemented, we are implementing, we have implemented consumer duty. Maybe Bernie can give us just a quick word on that, because it impacts most all of our businesses, but particularly retail. Laura, 500 to 600 million.

Laura Mason (40:58):

Yeah, I think we actually said that by the end of 2025, we'd have 6 to 700 million of operating profit in total in aggregate across LGC, as well as having 25 billion of third-party assets under management. And we are on track for hitting both those targets despite, as you say, some of the headwinds we've seen, particularly in the housing market over the recent year.

António Simões (41:23):

Thank you. And Bernie on customer duty.

Bernie Hickman (41:25):

Yeah. So look, there's been a huge amount of activity as you'd expect, you'll have seen from other companies as well. It has raised the bar and the board's been giving it a lot of focus and attention, as is quite appropriate.

I would say on the back book, we have done a number of transactions over the years, which meant we've sold three back books, personal investing in L&G and mature savings as well, so the GI business as well. So we don't have a lot of back books, customers and policies to look at, which is a good thing, that I think they're going to be even more challenging than the front book, given they go back over a long period of time. So, we're feeling quite happy about the transactions that have been done a few years ago from a consumer duty point of view.

But generally raising the bar across the board. New MI packs, new board reporting going on. So, a huge amount of activity from the team to make sure we're really focusing on delivering great customer outcomes over the long term, which will have a lot of positive commercial benefits as well. So, we're focusing on that, getting really... And understanding where our customers do and don't understand our policies and our policy literature, is an ongoing task that is really going to help our communication to our customers.

So, it's delivering a lot of good things as well as being obviously a lot of new activities to generate.

António Simões (42:55):

And just to add, it is a big focus of mine as the group CEO and of the board. So, just to reassure you on that.

Andrew Baker Citi(43:03):

I'll stick with the trend of three questions if that's okay.

First is on the BPA market. So, I appreciate your comments on the high demand. What about on the supply side? There's been some headlines around three potential new entrants in the UK this year. Do you expect that to have any impact on the competitive environment there?

And then the second one, I guess just a clarification of your thinking around the dividend, and specifically around this, the nuance around the longevity assumption changes and the negative drag from investment variances if you continue to have longevity assumption changes. I understand that IFRS profits isn't really the driver of your dividends, but that will reduce your dividend cover on that metric. Does the IFRS dividend cover come into your thinking, if at all, when you're thinking about that dividend going forward?

And then third one, just a quick one on the LGRI investment margin. It was down second half versus first half. Can you just talk through some of the moving pieces there and how we should think about this one going forward? Thank you.

António Simões (44:08):

Thank you, Andrew. Maybe I'll take the first one, actually not the other two, Jeff, I'll ask you to cover. So, the dividend cover point, and the LGRI investment margin.

On the supply and demand from a BPA perspective, first, I wouldn't comment on rumours of other players coming into the market, but there is quite a lot of interest in the market, which I take from a positive perspective, both public and private capital wanting to come into this space validates what is a key part of our own business model. And we've been doing this longer than anybody else. So, I see it from a strategic perspective as a good thing.

What we've seen so far is that supply demand is not changing the economics that we've seen in 2023. The market continues to be very competitive. It was already very competitive. And there are deals that we want to, from a pricing-

... and there are deals that we want to from a pricing discipline perspective. Yes, we will need to keep on watching the space. There's nothing that, now, standing here on the 6th of March, changes the dynamic of what we had in 2023, but it may well change and we need to keep close to that. Jeff, dividend cover?

PART 3 OF 4 ENDS [00:45:04]

Jeff Davies (45:22):

No, that's fine. Yeah. Broadly, you answered it yourself. Yes, we don't pay that much attention to it. We have plenty of distributable reserves, et cetera, and we talked about that on the transition to IFRS 17. We would look at, well, what's the underlying growth and profitability of the business? And clearly, we would take those sorts of impacts from the longevity releases out. That number will change of course as rates environment. So if rates come down a bit and we've locked in more business, then it could switch that way. It could be positive, if rates were ever half a percent again. Let's hope not.

And so, we therefore would take that out in our thinking because it's not a constraint on there and then look at some underlying. On the margin, I mean there's always second order impacts, but I think there was certainly more back book optimization probably in the first half than the second half. So you certainly can double that up if you like. Some of that was, as someone has said before, a lot of volume done in the second half. So the assets we're sourcing, we've put those to new business versus putting them against back book optimization. So that's broadly what's happened there.

António Simões (46:32):

Perfect. Thank you. Next question.

Nasib Ahmed UBS (46:36):

So, first question on basically the government's focusing a lot on DB solutions via public sector consolidators or super funds. How do you see L&G competing with that? Michelle, to your point, you're helping some of the smallest schemes. What solutions do you have? I think you've got APP and ISS. I hope I've got those acronyms right, are those helping in that space?

And then secondly, Jeff, you mentioned the sensitivity on interest rates is going up on the Solvency II basis, but I think in the IFRS disclosure in the footnote, you say January 2024, you put in more inflation and interest rate hedging. So does that come down again in 2024 on the Solvency II basis as well?

And then on the investment variance, I noticed in LGIM there's a cost provision for some of the partnerships. I think it's State Street and Charles River. Are there more to come or any more details on that provision itself? Thanks.

António Simões (47:28):

Thank you. Thank you, Nasib. So Jeff, why don't we start in reverse order. You answered those to the investment provision and actually there was a question online, which I can see here on, can you split... it was the bigger question about the 1.6 billion. So maybe you could try to mention the small one and the big one there and then come back with the interest rates hedging, and I'll talk about the government fund.

Jeff Davies (47:50):

Sure, yeah. Yeah, yeah. The cost provision, I mean it is just being prudent about the implementation of the operating model changes in LGIM, the outsourcing to State Street. As António said, we've started to go live on that. We've got more to go...

António Simões (48:06):

Yes. Phase one, done.

Jeff Davies (48:07):

And so, we all like to think we're brilliant at change but generally they're overrun. So we're being really prudent on that and just trying to make sure that we've made some provision for that. We're hoping Michelle beats it with her team and we release it in the future and we will watch this space.

Michelle Scrimgeour (48:23):

That is not the target.

Jeff Davies (48:26):

The rate sensitivity, yeah, all I was saying was we were slightly longer than we expected to be at the end of December, which is why the rates, the Solvency II sensitivity was just marginally lower. And so I didn't want you baking in the 10, 11%, because we think it will just go up a couple of percent.

The Solvency II and IFRS are now actually quite separate because we've been using the designation of assets and the IFRS 9, as we've said. And so we've managed to get quite close now to where we wanted. It's pretty neutral, if you look at that disclosure. I'm amazed you got that, impressive. Then there's a footnote that says in January we did a bit more because boots landed in December, we did a bit more in January. So the IFRS is 25 million for a hundred basis points down. It's slightly convex, so up we're still going to work on reducing that, but we are very happy where that's been.

And similarly, for the same reason we did some stuff on inflation because the boots had landed, it all takes time. So we thought it was more useful to give you updated IFRS sensitivities as well, but broadly less happening on the Solvency II. Just one or two basis points up we suspect when we've changed everything around. And did you want to...?

António Simões (49:36):

No, I'll do... Yes, do you want to just do that? Yes.

Jeff Davies (49:38):

Yeah, it was just a, what's the split? The one, but I think most people have got there. What's the split?

António Simões (49:42):

Just the overall investment variance of the split.

Jeff Davies (49:43):

The investment variance, the 1.5, 1.6. And obviously there's 500 million or so, which is one's a quirk. It's obvious too, longevity we've talked about. The buyout of our own pension scheme where we put that through is very much a one-off, no pension scheme ever again, governs very happy that there's no more pension scheme accounting.

And then in the remainder we've talked about the residual values. The only real, it says what's real assets, impairment real loss, it's only the modular and the onto. The couple of 100 million others are either provisions as we've talked about or absolutely just market to market unrealized. We're very long-term investors. We're hoping to get the upside as well as downside on those in the same way as we do on equity. So that was really the breakdown.

António Simões (50:32):

Yeah. Thank you. And your first question on government proposals and you put a bunch of stuff together. But, if you think of PPF and super funds, our view has been that PRT has served the market and society well and it protects the benefits of the individual's annuitants. And we have over many years funnelled some of those assets into the productive economy from a super funds' perspective and a PPF perspective, we see the solution for schemes that cannot be bought in. Yes, we can see that as a solution, but we don't see it necessarily. And we've been quite clear for the schemes that are well-funded and where we and other insurers could do a buy-in buyout, we see that as a gold standard and so does the government more generally.

So I think I would make a broader point, which is we do support all the initiatives around DB and DC assets being put to work from a productive assets' perspective. And as you know, we are a signatory to the mansion house compact and so we're very supportive of that and we're very engaged both on the DB and on the DC side. Thank you.

Thomas Bateman Berenberg (51:52):

I just want to go back to the capital return because capital return is a really important part of the sector's performance at the moment. And it just feels, despite the growth angle in the UK life sector, they're at risk of lagging behind the European peers a little bit. So I was just wondering how you think about that capital return, if you do benchmark it versus the peer group.

Secondly, I think you said before that 10 billion of UK PRT would drive six to 7% growth in operating profit or capital generation. Is this still relevant given the increased use of reinsurance, and also how does that change with high volume? So if you do 12, 13 billion, does that move the operating profit growth up?

And finally, there's been a lot of talk about US CRE exposure at the moment. I know that you are investing into the specialist CRE market, but if you could just have a quick, quick update on any potential risks for US CRE.

António Simões (52:53):

So I'll take the first one, and Jeff, can you take the other two?

So from a capital returns perspective, look, there's not much more I can say today. As I said, 5% dividend growth, we intend to do the same for 2024 and I'll be more clear about capital allocation and distribution on the 12th of June. To your point, do we benchmark? Yes, of course we benchmark ourselves against everybody else. We also have to go back to the principles of, we look at what are the returns of our growth opportunities versus the alternative of distributing that capital.

And that's different firm by firm. And if you look at large European insurers and others, they have fundamentally different business models than ours. So the answer can be different because we are different. But that's something I want to set out very clearly on the 12th of June with, here's a strategy, here's capital allocation and here's capital distribution. But yes, we look at competitors. Thank you.

Jeff Davies (53:47):

Do you want the other two?

António Simões (53:48):

Yes.

Jeff Davies (53:49):

Sure. Yes, so that's right. That's what I was quoting earlier, that 10 billion extra of annuities drives that off profit growth, six to 7%. We talked about that in the IFRS 17 teaching if you like, when we were first doing that, that that stands. We've been looking at that. Clearly, if we write more... So that's 10 billion net, obviously. You have to be retaining the value to be able to get that, but obviously individual annuities contributes to that as well, significantly.

So to the extent we write more the math's of, it's a bigger book, you get a bigger CSM, you get more expected margin unwind, it will grow faster, yes. And so to the extent you're writing more, you get more upside. Clearly, the profits are spread over the whole lifetime for annuities, but clearly that's part of the value proposition of writing this stuff. It makes greater returns on capital and it gives you a very large store of profits that unwinds into the future. And we give you the runoff for that.

A US CRE, and the simple answer is very, very little. But to give it a bit of colour, middle of last year in particular, I remember emailing back and forth with risk with the investment CIO if you like, of the US balance sheet, which is where it says there was virtually nothing in the UK balance sheet for this. And I think there were three assets on a watch list and they were all $10 million or less, and they were waiting for someone to resign a lease, that sort of thing. So it was basically immaterial for us as a group.

António Simões (55:22):

Thank you, Jeff.

William Hawkins KBW (55:23):

Just the one question. I'm sorry.

It's really simple. When you were giving your early look remarks, António, I don't think I heard you refer to technology explicitly. So I'm just wondering if you can give some early look thoughts about what you think about the technology platform that you've inherited, where you think you may be inheriting areas where legal in general already has a competitive advantage? And where that may be an area that you want to be thinking about for investment for the future?

António Simões (55:56):

Yeah, thank you William. Actually, that's a really good question. In my slide, the one where I spent a bit, the one that had more content where we talked about the trends. If you look on the left, I was quite deliberate about the four trends that I chose and clearly, a trend to more personal responsibility the DB to DC is important. I highlighted climate change, I highlighted the changing macro environment.

But the fourth one that I highlighted there, which I didn't speak to, you're right, is what's the impact of technology and AI specifically, but technology more broadly? Not just as an enabler of business, but as a catalyst for business change. So what have I seen? There are different parts of LNG are more or less strategically advantage or disadvantage from a technology perspective. What you can expect is on the 12th of June for us to also be more clear about the role that technology plays as a catalyst for business.

I've just come back from Maryland, Frederick, our US protection business. And that's a good example of a business that is compared to our competitors in the US, probably more advantaged from a technology perspective. You mentioned the results both Jeff and Bernie did that. That business has really been able to, one product, one channel, beat most of our other competitors because we're better from a technology perspective. That's a great example.

I wouldn't say that's universal across LNG. In many cases we're actually playing catch-up. Actually, what we're doing with State Street is an investment that we hadn't done before. And so that investment I wouldn't argue is cutting edge. It's really a catch-up in terms of technology. And so more about that on the 12th of June, but well spotted and it's an important trend. Thank you William.

Any other questions? Okay, we had one question online. I'll do a final thing. What is the outlook for cost in LGIM? You get to answer the last question. I think we sort of answered that, but since Fahad had asked it online, Michelle, outlook for cost in LGIM?

Michelle Scrimgeour (58:05):

Sure. And similar to what I said earlier on, it is absolutely the case that we are disciplined in cost management, that we are driving out efficiency, but that we are also continuing to invest, and that is really important. So we don't just focus on the cost line, we talked about revenue and that is really what we are focused on every single day.

António Simões (58:25):

Great. So I think, looking around, I think that's it for today. Thank you. Thank you for coming. Thank you for all your questions and I look forward to seeing you on the 12th of June at our capital markets' event. Thank you.