Q2 2015 Earnings Call

Company Participants

- Andy D. Briggs, Chief Executive Officer-Aviva UK & Ireland Life, Chairman-Global Life & Executive Director
- David McMillan, Chairman-Global Health Insurance & Chief Executive Officer-Aviva Europe
- Jason Windsor, Chief Capital & Investments Officer
- John Lister, Group Chief Risk Officer
- Mark Andrew Wilson, Group Chief Executive Officer & Executive Director
- Maurice Tulloch, Chairman-Global General Insurance & Chief Executive Officer-Aviva UK & Ireland General Insurance
- Thomas D. Stoddard, Group Chief Financial Officer & Executive Director

Other Participants

- Abid Hussain, Analyst
- Alan G. Devlin, Analyst
- Andrew J. Crean, Analyst
- Andy Hughes, Analyst
- Ashik Musaddi, Analyst
- Barrie Cornes, Analyst
- Blair T. Stewart, Analyst
- Fahad U. Changazi, Analyst
- Gordon Aitken, Analyst
- James A. Shuck, Analyst
- Ming Zhu, Analyst
- Oliver G. Steel, Analyst

MANAGEMENT DISCUSSION SECTION

Mark Andrew Wilson {BIO 7102576 <GO>}

Well, good morning, everyone. And to those of you in the room and there's quite a few online as well, welcome. Thank you for making it to our offices on a very busy day, albeit one without the tubes again.

Now, you've got the slide packs in front of you, and you'll notice there is a pullout in the slide pack. And that I think explains the Aviva story. It comes from the Annual Report, and that summarizes very succinctly the overall Aviva strategy. And I think it's important to keep that in mind. Now, what you should note is the consistency in our story. So, to be clear, it's cash flow and growth, and cash flow – in that order and cash flow remains our primary focus and will continue to remain our focus.

But before we get into the key messages for today, I wanted just to step back and remind you of our recent issues and the progress against those issues. And you know we always focus on our issues. But I think it's easy to forget where we were less than three years ago. So, at the beginning of 2013, everywhere we looked, there seemed to be challenges. Cash remittances were low, capital was weak, leverage was high, employee morale was poor, and shareholders had lost patience simply seeing us as too risky a proposition with our balance sheet. Now, we had control issues at Aviva Investors. We had commercial mortgage losses. Add to that a relationship with the regulators around the world that was strained and a management team that, amongst other things, lacked coherence.

It's all good stuff if you enjoy turnarounds. But we also had a core business that was strong, we had a brand that is hard to beat and we had technical expertise throughout the company that certainly surprised me on the upside. And most of all, we had a strategic competitive advantage for a digital era being a composite insurer with a very large customer base, albeit entirely untapped.

So, back in 2013, we had quite a to-do list to tick off. But I think that's exactly what we've done. We've improved the balance sheet. We've simplified the group and we are now moving to a new phase of Aviva's development, namely transforming and growing our business. So, we've moved from that fixed phase on the balance sheet. But it's fair to say I'm not really known for my patience and this result is by no means enough.

So today, I want to cover three main topics. And it's you that have told me what you want to hear today. So, I'm going to cover those. That's the results. It's the Friends Life integration. And it's Solvency II. Now, I have separate slides on integration and Solvency II and, therefore, I will focus on the results on the left-hand side of the slide initially.

So, here are the headlines. The numbers, I think, are evidence of the progress we have made. First half operating profit is up 9% to £1.17 billion. Now, there's a lot of moving parts here and I'd forewarned you of that. The key point here is that we have £86 million of underlying profit growth, which together with the Friends Life more than offsets the significant headwinds from a much stronger sterling. Of course, we had disposals in the year and lower management actions in our UK Life business. In Life the value of new business is up for the group at 25%. This is now 10 successive quarters of value of new business growth. And I think it's easy to forget that.

And as an aside, I would encourage you all to compare this 25% growth rate with that of insurers operating in the UK or indeed a little further east of here or much further east of here, as I think you will find that this growth in VNB stacks up extraordinarily well against either our local or global peer group.

Our general insurance business has had a highly satisfactory half with growth in premiums and profit, and I'll come back to that a bit later. And I know dividend is important and today we are increasing the interim dividend by 15% to £0.0675 per share, which should give you some confidence in our cash flow outlook.

But our results have not all been good, however, and I'm less than impressed with some of the areas of performance. So, outside of the significant Friends integration expense savings, and we've made some good savings there, we've made some progress on expenses but it's not as much as I would have liked. And some of our European results, even taking into account currency, and I guess we need to do that, but some of those results were not up to the highest standards they've been in the last couple of years. So, there is still much more to do.

I'll cover the Friends Life integration shortly, but the key takeaway on the Friends Life integration is that we are ahead of schedule with run rate savings of £63 million achieved in just three months. So, now, a successful integration, I believe, is all about delivery and speed and, so far, we appear to have both.

On Solvency II, we'll cover that in more depth and I have a slide on that, so we'll go into some depth on that.

Tom will take you through some more of the detail on the numbers. But also, wanted to focus on the second part of our investment thesis, which is growth. And by growth, you know what I mean. I mean future cash flows. Now, as you know, I measure this growth by value of new business in Life Insurance, by underwriting profit in GI, and net funds flow in asset management.

The 25% growth in VNB was fueled by the result in the UK that, okay, I admit was well ahead of expectations. And I guess that's despite the doom and gloom of many commentators following the annuity changes. Now, why have we been able to achieve that? Well, we have a diverse product range that gives us inbuilt resilience to market changes in any market. If you look at, for example, the so-called mature market in Italy, that was up 66%; Asia was up 18% and Ireland was up 17%. Now, France and Poland were flat, while Spain and Turkey suffered modest declines, albeit for reasons we can understand and address.

It's important to note, I think, different markets will grow at different times. And our results once again prove that we are not overly dependent on a single product or a single market for growth. Insurance is about diversity and diversification, and this is the key to the risk profile and it's the key to growth. And in my view, our diversity lowers our risk profile and gives us consistent growth.

Our general insurance performance has been I guess ahead of expectation and, it would appear, ahead of peers in the half. And underwriting profit was up 45% to £223 million. Today, we are also announcing - you might have seen a separate press release, we're announcing a seven-year distribution agreement with TSB, and we are pretty excited to bring our GI offering to TSB's 4.7 million customers. They're a fine organization, and I think this can be a fine partnership.

And finally, Aviva Investors. I've consistently said, and I said it at the last results, that the turnaround at AI will take longer than the turnaround of the insurance businesses, and this is evident in the still very small contribution to profit from asset management directly. Now, it needs to move to double-digit percentage of earnings, and that is the target. And we are saying that today, and Euan and his team have that in their target.

Progress has been made at Aviva Investors. And I'm actually – I was going to say happy, I'm never happy. But I'm reasonably comfortable with the progress that they've made. Now, asset management, to be successful there, as you know, we need some hero products, and since the launch of AIMS, Aviva Investors Multi-Strategy, their performance has been strong, with the Target Return Fund, that's the first one, that's up 8%. Now, that is ahead of its peer group. The AIMS fund range has also got £1.7 billion of funds in it. So that's some pretty good fund flows, and that's a good start, but obviously it's not yet sufficient.

On the rest of fund flows with asset management though, our IFA platform continues to grow ahead of the market with £1.5 billion of net inflows in the first half. That makes that platform about £7 billion funds under management. And it contributed a meaningful £25 million of VNB for the half-year. Now, just for a little bit of context and comparison, this is more than double the VNB of DBS in the same period, and that's about the same as it was last year as well.

So, moving to the Friends Life integration, and I know there's a lot of focus on this and rightly so. So, how is it going? Now, this is a major exercise. And we've said we have moved at pace to secure at least £225 million of synergies through integration. Now, within the first three months, we have made our property rationalization announcement. And just to recap, we'll be reducing our presence in Salisbury, Exeter, Dorking, Salford Quays, York, Norwich and London. Now, as a result of these building closures over the next two years, our UK property footprint will be reduced by 33%. That's a reduction of some 900,000 square feet.

What else on the integration? We have transferred £22 billion of funds managed internally by Friends into Aviva Investors. And we have served notice on AXA for an additional £24 billion, which we'd expect to be transferred by the end of the year. And obviously, there will be further significant transfers that will follow next year. So, that's nicely on track.

Those of you that follow Friends Life will also know that there was a recurring theme of below-the-line spend. That's not too dissimilar to our own below-the-line spend a few years ago. I would call these costs the recurring/non-recurrings. And I repeat what I said then: I don't care whether the costs are reported above the line or below the line; it's all cash and it all counts. So, we're addressing these costs as well in addition to the £225 million recurring cost savings.

There was a lot of speculation when we did the deal and a lot of the commentators suggested that the scale of the integration would prove a distraction for our Life business. And I would accept that this is a big undertaking of the integration. And while I point out it is still very early days, I think these results suggest that the team has definitely retained its focus. The sales results and what they've done in that business I think has been first class.

And now on to Solvency II and move to the next slide. Let me be clear upfront, we are comfortable now with our capital levels under Solvency II. So, I'll give you a few facts. We submitted our internal model for approval to the PRA in June and we are confident that will be approved in December. As you know, in December, they will on a single day announce those who are internal model or standard formula. We are in constant dialogue with the regulator at all levels on this topic, and each week the envelope of uncertainty gets smaller. That's good.

We've been preparing for a transition, as you know, for a number of years and I think we probably started this process a little bit earlier than most people. And we have spent a lot of money and, I must confess, this has taken an enormous amount of management time and I'd really like that time back. On costs, it's going to cost us, or has cost us, in the region of £400 million of costs, and this figure does not impress me one little bit. The capital intensive businesses like the U.S., South Korea and Eurovita have been sold as, for us, they simply did not work under this regime.

Now, in preparation for Solvency II, we've also changed our business mix to the one you see today. So, the business mix you see today is much more aligned with Solvency II and it works.

Now, you'll hear from Tom that we've also strengthened our calibration on our economic capital model to get it more in line with how we believe Solvency II will land at the end of the year.

Now, the issues such as transitionals, and there's a lot of talk about transitionals, I think they have been clarified without any ambiguity in what I thought was a very helpful speech from the PRA's Sam Woods a couple of weeks ago. And I can say I think I'm very comfortable with our level of transitionals; they're right in the sweet spot.

A diversified company – and it's important to note this, a diversified company such as Aviva should not hold overly prudent capital buffers; that would be capital inefficient and dilutive. So, we will set the top end of our target range with that in mind.

And we're also focused on what happens after Solvency II implementation at the beginning of next year. In other words, how we're going to extract the synergies and generate capital which flows through to shareholder value. Now, obviously, over the next couple of years, we expect significant capital synergies out of the Friends transaction, and this will further improve our ratios.

So, finally, on to something very much forward-looking, that's on to digital and our true customer composite. Here we're trying to do something that no one else in the UK can do. It is game changing both for Aviva and the industry. Now, this is a screenshot from our new MyAviva experience that is currently in beta testing. You'll see a range of products that we offer from pensions, ISAs, car, travel, home, health, but this range might be different for each customer.

So, imagine a scenario where you have a pension with us, and when you check your balance, you get pre-underwritten, pre-approved product with three clicks, with a discount. Now, have a read on the FCA's new paper on Smarter Consumer Communications. They single out MyAviva as a good example of effective communication. They've even posted a video of the MyAviva app on the website. And so, the regulators are also working with us.

But I know actions very much speak louder than words, particularly to this audience. And our average products holding per customer is inadequate at 1.7 products per customer. Our initial target here is three products per customer, and it needs to be higher. Now you can do the maths on what it means for us.

And digital is not just limited to our UK business. We're doing initiatives all around the world. For example, we've just signed an agreement between the governments of Singapore, the UK, and Aviva to take digital into the Asian region. That was witnessed by the PM last week. And the Singapore government has been very active in making Singapore a digital hub and help us lead the way in that insurance revolution.

Now, on that future-looking digital note, I want to hand over now to Tom, and he'll take you through some of the detail of the operating numbers, then I will come back and we can have some Q&A.

Thomas D. Stoddard {BIO 15071280 <GO>}

Thank you, Mark. And before I dive into the numbers, I wanted to make a few introductory comments. From my perspective, the combination with Friends is delivering the expected benefits but ahead of schedule. We've had immediate benefit to cash and capital at closing. We're off to a strong start on realizing cost synergies. And we continue to expect significant capital synergies, which we will pursue over 2016 and 2017.

We still need to keep living the work, however, in order to see how far it can take us. I'm sure you recognize that today we're reporting less than a full quarter of combined results, so it's still early days.

Our remarks will take us quickly through results, and I'll conclude by talking through our capital position, Solvency II and dividend policy, which we're reaffirming. I'd expect us to refresh our longer term financial targets at yearend, although the direction of travel should be self-evident today. Dividends should grow faster than operating EPS over the next couple of years as we move toward a 2:1 cover ratio. Thereafter, once we get the full balance sheet benefits of the Friends deal working for us, it should be EPS growth that drives Aviva forward.

So now turning to the numbers. In terms of first half operating profit, we're getting good contribution from Friends Life, but this is just the start. The £63 million of annualized run rate synergies already achieved will flow through in future periods and have only just begun to benefit our current results. I'm expecting much more in the future.

In the meantime, there's a lot to say about these numbers, so I want to point out the negatives on the left part of this slide related to timing and transaction impacts which have reduced our profit after tax and then move on to what is actually happening in the business units, which has been good.

So, as one would expect, immediately following the issue of shares in a stock-for-stock merger, this should be the low point, with operating EPS down 9% apples-to-apples. But as we achieve more cost synergies by the end of 2017, we continue to expect the operating EPS impact to the deal to recover to neutral and ultimately become accretive once we apply the benefit of capital synergies.

Okay. Looking a little more closely at the business results themselves on the right hand of the slide, we've had good underlying growth in earnings at Aviva, up £86 million before the addition of earnings from Friends. Operating profit is up about £100 million overall as the contribution from Friends more than offsets reductions from foreign exchange, businesses we no longer own and fewer one-off good guys this year relative to last year.

As you may recall, in the first half of 2014, UK Life benefited from £100 million of expense reserve releases. In 2015, the back book has not yet been a big contributor. All in all, operating profit is up 9% over last year with growth balanced between Life and GI. Fund management is down as we sold River Road last year and as we spent more to develop the new AIMS product line, and I'll come back to that in a moment.

Putting that aside, I'm pleased to see the underlying businesses performing well during a period when the organization has been undergoing a lot of change.

The Friends Life acquisition has set a very positive impact on IFRS book value per share with NAV up 12% to £3.80, but less so on an MCEV basis. Pension movements, foreign exchange and integration costs have also hindered further growth in NAV during the period.

And consistent with my after, after, after theme, I need to point out that the amortization of AVIF from the acquisition will limit the growth in IFRS NAV per share over time, which of course will follow total EPS.

Now, in UK Life, VNB performance has been very strong, up 31% before Friends and 43% with Friends. But for me, the key point to make is how well-diversified and how well-balanced VNB is now. Annuities still matter, but protection, pensions and platform business contribute about half of our VNB in the UK and we continue to be the market leader in equity release. Premiums are up and our VNB margin has improved to 3.6%. Andy and team are doing well.

Excluding Friends UK, operating expenses have been cut 9% to £239 million. It's a much better business today, but there's obviously still more work to be done both on expense efficiency and capital efficiency.

And finally, we're moving UK Life to a more regular bi-annual cash remittance schedule better aligned with the Aviva shareholder dividend.

And moving on to UK GI now. Last year, in the first half, our net premiums written in UK GI were down 6% but Maurice and the team have delivered growth for the first time in recent memory together with our best combined operating ratio in eight years. At a COR of 93.2%, it's clear we are maintaining underwriting discipline while winning new customers.

Weather has been relatively benign this year, but we've also adjusted the business mix and had less favorable prior-year development in personal lines.

Our expense ratio in the business has improved to 9.1%. And recall that, as always, investment income and operating profit are affected by the lower balance in the internal loan, but underwriting profit is stable as the better COR works through the volume of earned premium. All in all, a promising start to the year.

Over in Canada, our other big GI market, we delivered an attractive COR at 91.9% for the half-year, resulting in a big improvement in underwriting profits. Favorable prior-year development, especially in personal motor as well as relatively better weather, aided this result. Home has been affected by a few large losses.

Of course, it's difficult to sustain a COR in the low 90%s, but I'm pleased to see Canada bounce back from its COR of 96.8% last year. This is usually one of our best returning businesses, and return on average capital employed in the first half of 2015 came in at 19.7%, a very good result. This business has the potential to grow faster, and with Aviva's increased financial flexibility overall, I would expect us to manage Canada more for a balanced mix of cash now and higher cash in the future as opposed to being almost exclusively focused on current cash and 100% remittance ratio.

With the exception of Italy, our financial results in Europe have not shown as much progress as we would like, largely because of economic conditions. Nevertheless, David McMillan is quick to remind me that we're still doing better than many of our competitors there, with VNB up 7% in constant currency. Low interest rates have been a negative generally, and in particular affected VNB for us in France and Spain.

In Italy, we're seeing more follow-through from our past restructuring efforts with reduced guarantees on with-profits products enabling us to enjoy better margins and volumes resulting in VNB up 66%.

On the GI side in Europe, net written premiums were up 4% to £802 million on a constant currency basis, excluding Turkey GI which we divested at the end of last year. And the

COR was stable at 94.3%. Note that overall operating profit and cash remittances from Europe have also been reduced by the FX impact of a stronger sterling, but operating profit was up 6% on a comparable basis.

Now moving on to Asia. We're breaking this region out in a new slide this time in order to emphasize a few points. Asia remains important to our future despite the fact that we did not chase the DBS renewal to levels we considered uneconomic. In Singapore, we have a broad range of products and remain a leader in selling through financial advisors. And by the way, DBS accounted for just £12 million of VNB in the first half, which we'll miss, but we're looking forward and have high expectations for growth from our joint ventures in Asia, and in particular in China and Indonesia.

In addition, we've looked at Friends Provident International, FPI, and currently believe it is more closely suited to operate alongside our Asian businesses led by Chris Wei. There have already been opportunities to leverage systems, IT, and the rest of the business, the early results of which you saw in the FPI cost reduction in Mark's deck. Altogether, Asia contributed 14% of our VNB in the first half, and we expect to grow this proportion over time.

So, on to the topic of operating expenses. As you can see from this slide, we're reporting mixed results in terms of expenses. Now, before the impact of Friends, it's good to see that our UK, European and Canadian insurance businesses have continued to deliver operating expense improvements. But Friends add to our overall expense base in UK Life, Aviva Investors, Asia and the corporate center. The acquisition also brings with it significant integration and restructuring costs, as well as additional Solvency II compliance costs.

So, you can see that the £109 million of Friends restructuring costs largely reflects three things: transaction expenses from the deal, property exit costs and break fees on moving assets to Aviva Investors.

And you'll note that at Aviva Investors and in Asia, we've increased our spending to support growth initiatives. We're also investing here in the UK, in digital and true customer composite propositions. So, while our expenses ultimately may increase as Aviva grows, our preference is to generate efficiencies and keep reallocating expense and capital budgets to favor our businesses generating the best economic returns. That means continued vigilance on expenses and productivity measures with an emphasis on improving expense ratios in each segment.

So, that's it for the half-year operating results. Our balance sheet position should not be a surprise. We have more capital surplus and more liquidity as a result of the Friends combination. Debt leverage remains within our target range.

In May, we got out ahead of some of the market volatility this year and raised approximately £1 billion of hybrid debt to pre-finance this year's redemptions and also pay off £200 million of expensive senior debt early.

Now, it's a bit premature to say anything definitive today, but we have some other actions in progress to free up underutilized capital and improve our risk profile still further, so keep watching.

Now, given all the interest recently in Solvency II, I thought you'd like to hear an update on our economic capital sensitivities and how we're transitioning to Solvency II. As you should see from this slide, our economic capital cover ratio is stable at 176%, and we've intentionally kept it in that range for several periods. Our overall capital surplus is higher following the acquisition, now just shy of £11 billion, and we've picked up £300 million of capital synergies at closing just from diversifying Friends across the Aviva Group capital base. We expect more capital synergies from merging legal entities with UK Life through Part VII transfers through 2017. And we also expect additional capital benefits from a variety of Solvency II optimization projects we have ongoing such as work we're doing on equity release.

You should also note from this slide that we've continued to strengthen our modeling, as we did last year, in terms of calibrations, correlations and other assumptions. One clearly positive comment I can make about Solvency II is that the multiple layers of internal and external review are naturally leading to more inherent conservatism. Between that and the actions we've taken to improve our balance sheet, the result is a stronger and more resilient capital base. Our economic capital surplus cover ratio would otherwise have increased this year and last, but we're taking steps to align it more closely with where we expect our Solvency II model to lead. We are very comfortable with our economic capital and we don't want there to be a big difference between our regulatory Solvency II capital and the models we use to run the business.

So, this next slide shows some of the key sensitivities of our economic capital surplus to economic variances. We are well matched on interest rates but more sensitive to property, including commercial mortgages and spreads. While this slide does not illustrate our Solvency II capital, I can say that the sensitivities are broadly similar, and that gives us confidence.

Going forward, we expect to receive further comment on our Solvency II model application this fall prior to receiving approval expected near the end of the year. And the model will always be subject to improvement, of course, as we use it in the business. And as I've said before, we've been managing Aviva based on our understanding of the application of Solvency II to our business. This includes today's declaration of an interim dividend of £0.0675 per share, an increase of 15% on last year's interim dividend, following 21% growth of the total dividend for 2014.

I want to finish by returning to the benefits of improved financial flexibility. As this slide shows, our capital, liquidity and leverage are in a much better position now, and the reduction in the internal loan remains on track. We're better positioned to deliver cash flow plus growth. So, based on what we know today, we're reaffirming our dividend policy of moving to a 2:1 operating EPS cover ratio over the medium term.

And while I'm at it, let me reiterate that I still expect the Friends transaction to be broadly neutral to EPS once we realize the full run rate synergies by the end of 2017 and accretive to EPS once we apply the benefits of capital synergies and active capital management.

And I'll conclude by saying that capital management remains a very big part of our future at Aviva, and we have at least three themes to consider: first, the perspective capital synergies to be realized in UK Life from the Friends transaction; second, management actions to re-optimize our business by reducing solvency capital requirements under the new regime; and third, opportunities to rebalance the group and redeploy or reallocate capital to higher returning, faster growing businesses. All upsides, from my perspective. And as always, we've got a lot more to do.

So, back to you, Mark.

Well, thank you, Tom. So that's our half-year result. Just while we have that slide up there, Tom showed what I think is a key slide on the balance sheet metrics. Historically, many of you and many investors have told me that we were difficult to invest in with our balance sheet. It's probably easy to see why when you look at that slide. But I believe that this slide shows that we have ticked this issue off. For example, our economic capital surplus is £10.8 billion. That's triple the level that was reported at the start of 2012, that's even with assumptions strengthening over that time. And elsewhere, the key indicators are up as well.

Now, growth is probably a bit of the surprise today. Growth is continuing to emerge across both the developed and the emerging markets, and particularly led by the UK today, as you can see.

Other key messages for this morning is that the Friends Life integration is ahead of schedule. And on Solvency II, I repeat that we are comfortable with our capital position within the overall target range. And of course we shouldn't forget that the dividend is up 15%, which should give you further confidence.

And on that note, let's open up for Q&A. I might take a seat and let's open up for Q&A.

Q&A

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Mr. Devlin?

Q - Alan G. Devlin {BIO 5936254 <GO>}

Thank you then. Alan Devlin of Barclays. A couple of questions. First of all, you mentioned the material capital synergies expected in 2016 and 2017. Given your comments on Solvency II and also your comments that you don't want to be over-capitalized, what can we expect you to do with those capital synergies when they come through?

Second of all, the management actions were lower in the first half given you were focusing on Solvency II, internal model and Friends. In the second half, can we expect those management actions to pick up because you're giving them more management time to focus on them?

And then just finally, on Aviva France, can you make any comments on the lawsuit which rears its ugly ahead from time to time? Thanks.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Sure. I'll take some of those and Tom will take some. Just on the capital synergies, so you saw we took £300 million. There's obviously a much greater number than that to come out over the next two years in 2016 and 2017. I guess at that stage we will have choices of what to do with it. Do you want to – what do you want to do with it, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Well, we've got a lot of possibilities in terms of what we do with the excess capital we generate. Again, we're trying to drive the company forward. So, if we can invest and achieve good returns, we'll do that. So, that may be investing in the business or taking on more risk as we grow stronger. But if we can't find opportunities to deploy capital for the returns we're looking for, we'll in turn distribute that back to our shareholders.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

You could do anything. But I think it's a little bit premature to give any guidance on it. But we don't want to hold overly prudent buffers obviously.

On the management actions, I think you articulated it probably better than I could. There's still a lot of management actions to come out for a number of years, and being consistent, saying these won't be linear and they'll be lumpy. In the first half we did have other things to focus on. There's more to come, but I wouldn't give any promises for this year. I mean, I don't know when they're going to come out, except they're still significant. We know that. And they should be regular over time.

On Aviva France, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

I'm sorry. Was there a question on Aviva France?

Q - Alan G. Devlin {BIO 5936254 <GO>}

Just on the lawsuit.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Oh, just on the lawsuit, yeah. Well, we've got nothing new to say on the lawsuit. There's no new developments there for us. We're adequately reserved and it's an immaterial issue for us.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah?

Q - Gordon Aitken {BIO 3846728 <GO>}

Thanks. This is Gordon Aitken from RBC. Three questions, please. First, the margin in the UK pensions and platform businesses has picked up dramatically. Just wondering if you can tell us what's going on there.

Second, I think it was a year ago you told us that you were - one of your new targets was that you were going to say to every business every year you're going to cut their cost/income ratio. And you said you wouldn't tolerate anything less. Just if you can - I see the currency effect, but explain what's gone on with the increase in expense ratio this year.

And just finally, some numbers, What's the remittance percentage, and the the £800,000s of after, after, after, where are we on the first six months? Thanks.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. Maybe if I can start with the cost/income ratio, and that's still is the expectation. I'd say with - there's a couple of exceptions to that. I think digital, obviously, is - we're going to be investing in that, and we're going to invest quite heavily in that and continue to do so. It's got over £1 billion of revenue in digital, but we've got to invest in that and that's fine. What do we look at doing there is reallocate. So, we're actually reallocating expenses from one part of the business to another.

And the other exception to that, at the moment we took the decision on Aviva Investors that we needed to build out some of the distribution capability. For example, we signed the deal with Virtus and we had to - I guess, we had to pre-fund that distribution ability as that's coming - just coming online now. So, there's some things there.

As I said, I think some of the areas have done really well on expenses, as Tom mentioned, and some weren't. And we're addressing that in the second half, if I can say that. The year isn't finished yet.

The pensions, Andy, do you want to talk about the pensions? I mean, the interesting thing with pensions, the platform has changed the way we're doing business, and that's had some good VNB. And also, I should point out that all the media noise we had around the pension freedoms and whether we can do them, as of last week, we can do them. It was only a matter of time, and it wasn't us being obstructive. It's just the government didn't give us a whole lot of notice on making those changes and it took a bit of time.

Do you want to...?

A - Andy D. Briggs {BIO 4311809 <GO>}

Yes. I mean, it's a classic of we have strong propositions in the market, so we're growing strongly, at the same time as cutting costs and getting the benefits of the operating leverage from that. So, our net fund flows on the IFA platform were £1.5 billion. Our net fund flows on the corporate pensions market is about £1 billion, and that's on a kind of Friends and Aviva for the whole of the six months, but it's about £1 billion there. And then we've taken significant cost out. And the combined effect of all of that is we've pretty much doubled the VNB on the pension and platform business. So, if you grow and cut costs at the same time, the profit impact is pretty pleasing.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

And so the last point was on the £800,000s. Just thoughts on that, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Yeah. So, just on remittances generally, we're not setting any new targets today on where we're trying to drive. I comment that in UK Life there's a timing issue here just given the time that we've closed the transaction. We've decided to intentionally delay the UK Life dividend into the second half of the year and we'll get on to a more regular bi-annual remittance schedule out of UK Life. But that hasn't changed at all the expectation in terms of the cash flow we're expecting out of the UK Life business overall. So, no change in targets. We're feeling good about our liquidity and our cash flow.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

We did that just because we could, because it made sense to align it with the rest of the group. And obviously, our liquidity position at the center is pretty robust at the moment, so we've just aligned it all together.

Q - Gordon Aitken {BIO 3846728 <GO>}

But the target is still 80%?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Oh, in terms of remittance ratios? Yeah. Again, that remittance ratio is tied to OCG which we're not focusing on quite as much now. We're much more focused on just the absolute level of cash remittances. As we move into a Solvency II world next year, we'll be looking at sort of other measures in terms of the capital generation coming out of the businesses.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah, just behind you.

Q - Fahad U. Changazi {BIO 15216120 <GO>}

Good morning. Fahad Changazi from Nomura. Just to manage expectations on synergies, could you give us an idea of the trajectory of the synergies? For example, how much low-hanging fruit is done, £63 million, versus the run rate?

Second question, again, to manage expectations for Solvency II, when you do eventually come out with your range at full year results, will that be looking ahead to integrating Friends Life in terms of the internal model only, or will that range change or be static?

And just an operational question on France. I appreciate the VNB's weight is because of interest rate. But could you just again talk about the competitive environment? Générale and AXA seem to be doing well. And you'd previously said that Solvency II will open up opportunities for you.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah. Okay. Can I take your other questions in reverse order? I think our competitive position generally under Solvency II improves. I think you're going to find we had been operating closer to Solvency II probably than anyone, I think. And you can probably see that from comment through on the market. And one of the reasons we've benefited in Italy is because some of the high-guaranteed products that people have stopped selling, so all of a sudden the products that we have started selling look a whole lot better, and I think that's generally the case.

France is a combination of a few things in interest – and I'll pass over to David – the interest rates have impacted us. I mean, also we've had I think about probably six or seven or eight strong quarters there and I think they just took a breath as well. Do you want to comment?

A - David McMillan {BIO 17298829 <GO>}

Yeah. Just echoing what Mark said, France is very much a mixed story. As Mark said, we've had VNB growth of 25% last year and 30% the year before. If you look within the different books in France, our protection book is ahead 25% year-on-year. And it's actually ahead 25% across the whole of Europe, and protection is now 50% of European VNB. The hit we've taken in France is largely in the with-profits book where we've seen the impact of the falling bond yields in 10-year French govies. That of course recovers in the third quarter. So, the bond yield in the second quarter was half what it is in the third quarter. So, that's the principal impact.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Talking about the synergies, and the synergies are, as you know, in a number of places, I don't think – I saw a couple of comments, is it low-hanging fruit. You've got to pick all the fruit off the tree, and the question is when do you do it? We have ladders, by the way. So, we've announced some of the strategies, like the property, but you don't get the benefits from that yet. We've brought over the Friends money into Aviva Investors; you haven't actually seen the cost reductions of that yet because we needed to keep those resources for when we bring the AXA people over and then you don't need to increase costs in that there.

So, I think it's a little bit early to tell, and I'm not trying to be evasive. But the £63 million in three months is probably – is certainly ahead of expectations just for timing. And you'll see some more significant progress by the end of the year. But other than that, I can't really give you much guidance because we've got to – I'd rather do and show than say what we're going to do.

The team is – we have dedicated teams on this. We have Nick Amin. He's not known for subtlety but he is known for his results. And Andy and his team are all over this, but it's quite a broad project.

So, and the last one was on Solvency II on Friends on the standard model.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Sure. On Solvency II for Friends, we have them on the standard formula basis next year. Our intent would be to try to move them onto the Aviva internal model around the end of the year next year. When we do that, we should pick up some pretty significant capital benefits by doing that. But none of that is baked into our numbers right now.

Q - Fahad U. Changazi {BIO 15216120 <GO>}

And just in terms of the range you will give, presumably the range will hold when we get – it will be a higher ratio which potentially breaks through the range or will the range change?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Well, I think our intent is to have a range that's based on appropriate risk. And so we wouldn't change the range just because we've got more capital. I think that the real question then is what do we do with the capital as we had the question earlier.

Q - Fahad U. Changazi {BIO 15216120 <GO>}

Yeah. Thanks.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah?

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. Andy Hughes from Macquarie. A few questions if I could. First of all, on economic capital, I wasn't too sure how Part VII transfers changed economic capital. But is that basically moving from standard to internal model on Aviva?

And I guess the other question was, if this is closer to Solvency II, are there any transitionals in here? And what impact does that have on the numbers we can see if you do introduce transitional allowances?

On the annuity portfolio, one of your competitors changed their strategy to be more Solvency II compliant to reduce the capital allocated to annuities. Is that something you're thinking about doing as well?

And I guess the side question on digital in Singapore. I guess it sounds interesting, but the pushback probably I get on this is that if you look at the price comparison website for protection in Singapore, there's a huge difference in price between you guys and AXA at the low end of the price range and the ones with distribution who are charging significantly more, and it doesn't seem to have influenced customer behavior in any way, i.e., people are still buying protection from Pru and AIA. Do you think that's going to change? What is the catalyst for that to change? Thank you.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Andy, that's a whole lot of questions.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Take the first three or...?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

If I can just maybe start just a comment on transitionals and you can take the other ones, and I'll take the bond one.

Transitionals, I think I'll be surprised if any of you now are too concerned about transitionals given the comments from Sam Woods. I think it was extraordinarily unambiguous. Transitionals is good capital. Though it was meant to be tier 1 capital, it's good capital that counts. The question you should be asking, and no one seems to be asking, is what's your liability profile, how quickly does that fall off versus how quickly do the transitionals fall off. And in the UK, I think we asked originally for about 13 years. I mean, that was public knowledge. And we got 16 years because everyone has to be the same and the other countries asked for different amounts because their liability profile was longer.

But it is good capital. Dividends are paid after the benefit of transitionals. And our transitionals, we are very comfortable. It's right in our sweet spot and where we think it should be. Yeah, there's still a bit of ups and downs and we'll see how it ends out, but it's - we're in the sweet spot and I think our percentage of transitionals will stack up pretty well.

Q - Andy Hughes {BIO 15036395 <GO>}

[Question Inaudible] (45:12-45:19)

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Well, effectively, under Solvency II, think of it like the risk margin matches the transitionals broadly. So, it sort of nets off. So it's not going to go up from that with transitionals, if that's what you're asking. So it's sort of apples and jumbo jets. So the margin that we're working to would include transitionals, of course, and everyone's got different...

Q - Andy Hughes {BIO 15036395 <GO>}

Right.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Okay. So, I'll address the two questions, the one on the Part VIIs and the other is on longevity reinsurance.

So, on the Part VII transfers, to be precise, we get two sources of capital benefits. We get one on bringing Friends into our internal model. So, that will be one place where we'll pick up some diversification benefits, in particular at the Life company level. And then secondly with the Part VII transfers, we'll be able to align risk appetite in the businesses. Now, we'd - maybe we ought to do that sooner, but certainly by the time we get the Part VII transfers done, we'll be able to align risk appetite. And again, because Aviva's a broader, more diversified company, we've been running with a different risk appetite than Friends had standalone.

And then coming to longevity reinsurance, that's something that we've looked at historically. We've retained most of our longevity risk. It's something that we could have used this year to reduce transitionals but we didn't see a lot of benefit to us for doing that. It's something we may consider in the future in 2016 and forward once we've fully applied Solvency II.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

So, we didn't see any need for it, and there's downside to doing that as well, as you well know.

And your last point was on Singapore. I think it remains to be seen whether we can be successful there. What I can say is, so the agreement we signed - and I had the head of the MAS here looking at our Digital Garage and London and Shoreditch. And he saw that and went back and decided - wanted to help us get him one in Singapore and be the hub there.

They announced - when we signed that deal, they also announced this. So, the MAS announced they had put a specific team on making the regulation appropriate for digital and they're trying to be helpful, not harmful.

There is a little consumerist agenda there, like there is in many places around the world, and I think they would see that the commissions paid in Singapore and the commissions paid in bancassurance are too high and unsustainable. And I think the amounts paid, yeah, they are high and I think you're going to see - I will make a prediction. I think you will see a digital revolution in Singapore, and obviously we want to be at the front of that and that agreement we signed helps us be at the front of that. But we'll wait and see.

I think it's happening everywhere now. I think it is easier here for us in the UK, for sure, because we already have the customer base. We have 16 million customers in the UK and we have one in four pensions, and pensions is the key to this. You have the pensions, you can handle the other products offered. And so far, although it's only in beta testing on small numbers, so far the results are extraordinarily. So we'll wait and see.

Yeah?

Q - James A. Shuck {BIO 3680082 <GO>}

Thanks. It's James Shuck from UBS. I had three questions, please. The first one is – I'll try and get as much of an answer as I can out of it. But I mean, you talk about cash flow plus growth, but we can't actually measure you properly on cash flow at the moment because you're transitioning to Solvency II and, by your own admission, you're moving away from OCG as a measure because it's largely irrelevant. So, I mean, at what stage and how are you thinking about how you're going to disclose on that? And if we actually think about what your OCGs are versus the Solvency II compliant cash generation, is it materially different? I mean, I know it's very early days, but given it's such a strong part of your investment case, then I think it's important that we get some insight into where those are going.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. I mean, that's a well put question. And I think I can add some clarity and help with that. So, the end result of cash flows, so think of OCG was like an interim step anyway, and as you point out, it's a bit irrelevant for anyone under Solvency II. The key and most simple, most obvious measure is you look at the earnings and then look at remittances up to group. So, the real end of cash flow is the remittances we get into the group's center. So, it's the liquidity and cash flow we get here.

And then the final result of that is measuring what is the cover on the dividend. And we've said we're moving to 2 times. So you look at – at the end of the day, it's earnings through to dividend is the ultimate calculation, and OCG was an interim step in between that. So, I would measure earnings on the company, or individual company, the remittance ratio of the earnings to that and then the dividend payout, because that's the ultimate thing what you're aiming for, so that's the way I measure it.

Do you want to add that?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Yeah. I'd add some additional remarks. I think if you think about where Aviva's come from, we've been in sort of a transition. So, we've had decent profitability but our cash flow and liquidity was not that strong. So, we've been managing cash flow and trying to optimize that as best we can. Now we're in a position where we're much stronger financially and so we're going to want to retain and invest more in our businesses. So, I'll take Canada as an example. We've been taking about 100% cash out of that business relative to net income each year. But that business is generating great returns for us. So, the optimal thing for us to do is to take less cash out of that business and continue to grow it at high returns.

So, that means as we move forward, we're going to be again coming back to a capital generation metric as really the fundamental way to think about the business. But we're still currently in a position of transitioning to that. And so, cash and cash remittances continue to be an important metric. And we're using the 2:1 dividend cover ratio as a way to show where we're trying to go so that you've got a sense that dividends are going to move faster than earnings over this time period. And then as we get out and fully realize the benefit of the Friends transaction, we'll be more into a position where we're looking at capital generation earnings over the long term.

Q - James A. Shuck {BIO 3680082 <GO>}

Okay. My second question, there's a bit of corporate activity going around at the moment and I just wanted to understand your appetite for acquisitions. I mean, it may not necessarily be large ones, but if you get something opportunistic coming up either in the UK or indeed in other markets, then do you have your hands full at the moment, or is that something that you would entertain?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. And you weren't specific on that, so thank you, because, obviously under takeover rules I wouldn't say anything on that.

But what I can say is this. We have a very full agenda. All our time is taken. We're very focused on integrating Friends Life and getting that done, if that provides some help.

Now, I'd also caveat that with - and I was consistent last time as well - we will consider modest bolt-ons. We've done a little bit in Poland recently. I'd like to do more in Poland if we can; frankly, we've got trapped capital there that earns about 2.5% and I'd like that to earn something more. So, we would do stuff like that and we'll do modest bolt-ons, but we're very focused on what we're doing, if that gives you a bit of clarity.

The other I should say also - I don't know whether you'd call this M&A, but it's relatively modest. But with the changes in India and the contract we have in India, it's a pretty obvious choice to move our shareholding up in India to 49%. It's fairly modest money. And we're currently in discussions with our partner there to do so.

So, I'm talking modest things here is what we're looking at, if that helps you.

Q - James A. Shuck {BIO 3680082 <GO>}

So a few hundred million but not in the billions.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Oh, no, it's - India is...

Q - James A. Shuck {BIO 3680082 <GO>}

No, not India. Just in general.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Just generally, that's the right context.

Q - James A. Shuck {BIO 3680082 <GO>}

Yeah. Okay. And then...

A - Mark Andrew Wilson {BIO 7102576 <GO>}

India is tens, not hundreds, by the way, just to be clear and sure.

Q - James A. Shuck {BIO 3680082 <GO>}

This is my final point. Could you just comment a little bit about UK non-life competitive environment? It's obviously been a very tough environment, particularly on the commercial lines side of things. Again, corporate activity potentially going on. And maybe the outlook is looking a bit better.

And then if you could quickly comment on the personal lines motor combined ratio at H1 which was 101%.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

You're sitting beside the right person. Maurice?

A - Maurice Tulloch {BIO 17683736 <GO>}

Yeah. Morning. Thanks, James. Listen, the UK is a competitive market. Let me start with motor and then I'll talk about some of the other lines quickly.

So, our motor results, you're right to say they've gone from 95% to 101%. If you actually break them down, there's two factors. So, firstly, this year we've had £6 million unfavorable versus £11 million favorable last year, and that's about 3.5 points of that 6 point shift. And the other factor is we actually took the opportunity to add 106,000 customers in our digital direct business.

So, if we look at the overall outlook for UK motor, headwinds and tailwinds, this is always going to be a competitive market but actually they're coming more in balance. And we've seen the government step up and announce the work that they're going to look at the claims management companies. And we've also seen after two years of rate decreases, finally the market is starting to bottom out, and whether you look at AA or the ABI or you look at Towers Watson, they're all sort of signaling sort of 3% to 5%. We're also seeing that and we're seeing some actual slight increase.

So, the outlook in UK motor is improved, but just to put a little bit of conservatism on there, it's always going to be in a competitive market. And we use our pricing advantages and our scale advantages and our indemnity management and fraud and also continue to get more efficient on cost.

If we look at the other lines in general insurance in the UK, home is pretty stable. Certainly it's benefited this year from benign weather. That's been about 5 point improvement on our home results. Rates are down about 1% to 2% in the first six months and have stabled. We like the home business, and certainly our new deal with TSB gives us access to 4.7 million customers. And the commercial lines are stable, results are strong for us, and it's an area of business that we're looking to grow on the commercial side and just rebalance our mix a little bit.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. He's got the mic.

Q - Barrie Cornes {BIO 2389115 <GO>}

Good morning. It's Barrie Cornes at Panmure. I think James just asked most of my questions. But a couple I have got left is, the GI COR, obviously you were just talking, Maurice, about the weather benefit. I just wonder if 95% give or take would be a reasonable long-term sustainable combined for the GI.

And the other question was just on the Part VII transfer. Roughly what sort of timescale have you got before you achieve the Part VII transfer, please?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. The first one, I'm going to answer that we're not going to give any forecasts or targets on that. And Maurice is good, but as yet he can't control the weather. So, he's not going to give a target on that. But do you want to talk about Part VII?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Yeah. Sure. Part VIIs, I would expect, John, 2017 is the right timeframe...? John wants more time. I want it to go faster. So I think 2017 is the right time to think about.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

I want it to go faster as well, just an aside, John.

A - John Lister {BIO 15438517 <GO>}

Thanks, Barrie.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah. Barrie, do you want to just pass the mic across? You can pass it across here.

Q - Abid Hussain {BIO 20229932 <GO>}

Morning. It's Abid Hussain from SocGen. Just two questions if I can. Firstly, how do you intend to maintain the 25% of VNB growth? Perhaps if you can give us some indication on timing of the reallocation of capital to the growth businesses.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah.

Q - Abid Hussain {BIO 20229932 <GO>}

And then secondly, your average policies per customer, you've showed a target of three. I'm just wondering how do you protect yourself against potential mis-selling and is the FCA comfortable with yourselves setting these sorts of targets?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. Good question. Firstly, if we maintain 25% growth, you guys need to - we're going to have a whole lot higher multiple. That would put us probably in the top-most stock in the insurance world I would think if we can maintain it anywhere near there.

But what we do have is you are seeing growth, and particularly in the mature markets as well. And all of you know I have a different view to the rest of the market. I don't look at regions. I look at markets and our position in that market. I think it's total nonsense to look at a region. You're seeing a slowdown in China at the moment; that's impacting some of the countries, but it's impacting them in different ways. But I can't give any forecasts on growth, but we have had 10 successive quarters and we're going to get some more I think. And with all the actions we've got on, we've got a huge amount to do in all our businesses.

So, I did say 12 months ago that growth would come. I accept that the growth in this half has been higher than probably everyone was expecting, but that's the result of a couple of years of doing the right stuff.

Now, your point on the - growing the products per customer and the FCA is an important one. My model here, and I'm in active dialog with the FCA personally and saying that, like we're doing with MAS, we want to work with them, and we are taking our models to them and getting their input on the way through, because what we're doing has never been done before. There's no one that's ever been doing that.

Now, in the UK, packaging can sometimes be a dirty word, and after - what packaging in the UK means is PPI where you hide charges. What we are talking about is what we showed you on the screen where everything is totally transparent and you get discounts the more you buy and things like that. And the customer makes those choices. And what we are trying to build is a model where we can take the customers through it and that the FCA agrees with. And so far, when they're using us as the example of good customer communications, I think that's a good start. But I can assure you we're not complacent, and it's something that the board - and we have our Chairman here as well - the board is very focused on and we're very focused on. But it is something that's never been done before. This is game-changing the insurance industry and you can only do it if you are a composite like us.

Yeah. Andrew, down the back. Sorry, and then could you pass...

Q - Andrew J. Crean {BIO 16513202 <GO>}

It's Andrew Crean at Autonomous. Can I explore three areas? Firstly, remittances. Are there any other areas where there's trapped capital other than Poland? And on the bi-annual move on the UK Life dividends, what's the implication of that in terms of UK Life dividends for the second half?

Secondly, when you were talking about there is a high watermark on where you want your economic capital coverage as a composite company who needs to be efficient, can you give us some idea as to where that might be set under Solvency II?

And finally, I think you've got touching faith in my mathematics, but could you help me a bit with going from 1.7 to three policies per customer, what that might, in broad scope, mean in terms of both GI premiums and Life premiums?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. Poland, it's fair to – on some businesses, we wouldn't have tested whether we can pay capital yet, so, for example, China. Some of the Asian businesses, which I think I'd probably know better than most, it can take a long time and you've got to negotiate that out. Are there any others of the actual dividend-paying ones or cash-paying ones that we've looked at? I don't think there is, is there?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

No. I think we've actually done a good job. I mean, if you think about the restructuring we've done in Italy, we've done a lot to sort of unpick the internal capital structure...

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Italy was there, yeah.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

And improve it. So, our ability to move capital around has improved and will continue to get better.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

So, that – I have to think about it, but I don't think there's any other that we've got any chunky amounts of trapped capital. The treasurer is shaking his head. So, there's none others. But that's what's taken a lot of structural work. It wasn't just Italy. It was Ireland. It was France. There was a whole lot of places that structurally were too difficult to get the capital up. So, now it's more a decision on when it's right to bring it up and what sort of payout ratio do we want on those.

The bi-annual move, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Bi-annual move, the implication is that effectively we've postponed some of the UK Life dividend into the second half. So, we'll expect to get that in the second half. And so, overall, our remittance plan remains on schedule. So it's really just a timing issue.

Q - Andrew J. Crean {BIO 16513202 <GO>}

(01:01:35)

A - Thomas D. Stoddard {BIO 15071280 <GO>}

We're not actually disclosing what that number is ahead of time.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

I mean, I definitely wouldn't read any – what can I say, I wouldn't read anything negative into that postponement. We just took the opportunity because we could and just to align that because they've been sort of out of step for a long time.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Yeah. And I'd say, if you look at the past progression, we've been increasing the remittances from UK Life over a period of time, and so we continue to work on that.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

But that's not guidance. And your last one, doing the maths. Now, I had this discussion with Mr. Simpson last night, and he said you'll have to give more detail to allow people to do the maths. So, I guess, unfortunately, you've proved him right.

I'll give you a bit of guidance without helping you model, because I'm not going to help your models. But I'll give you a bit of guidance. What we're moving to is a scenario where historically with price, every insurer in the world that I'm aware of is priced product line by product line. So, you ask a whole lot of questions on car, motor, health, pet, whatever, house and you ask all those questions and you underwrite on a product-by-product line basis.

We realized that the key to this is actually underwriting on a customer basis, right? So, we are actually – and we have a project that's getting well advanced on how you underwrite on a customer basis and how you only ask the same question once.

Now, that's game-changing because when you do that, you can also then price on a customer basis, which is hard. And I'm not saying that we've overcome all the issues yet, because we haven't. We have a dedicated team of some very smart people working on it. And the intention is to get to price on a customer basis. Now, when you do that, you look at the return per pound of capital, you get that return, and you're looking to maximize that return per customer.

So, what that means is you get – so what that does mean is you get a much bigger share of the wallet and you grow it. And if you grow up from 1.7 to three, obviously your VNB is up a lot higher as well.

The other factors in there is the more products you get, the better your discontinuances get. And obviously, discontinuances is really sensitive on the profit and the margin. You reduce your costs as well which is also sensitive in the profit and margin.

So, we haven't worked out the margins across – well, we've got a fair idea, but we haven't finalized the margins across the customer, and this is going to take years to achieve. But the significance to what we can do from a growth perspective, particularly in this market here – and we're starting – we're putting the resources initially, we're focusing here just because the size of the prize is so huge.

Now, if you look at the best in the world, Wells Fargo, they have 6.2 products per customer. I'm not suggesting we're going to get to that, but our initial target is three. And we'll see how we go. We will provide as we go – and we'll provide more and more detail on that. And at the moment, we're doing an enormous amount of work.

Yeah?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Do you want to talk about Solvency II ranges?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Oh, solvency ranges, yeah...

A - Thomas D. Stoddard {BIO 15071280 <GO>}

So, on the Solvency II range, we're not disclosing a specific range today in advance of getting model approval, so that'll be something that would follow. Conceptually, the way we're thinking about it is that the Solvency capital requirement is a 1 in 200 risk. And so, we're then looking at a buffer above that and looking at the probability sort of within a range of what we'd take into that SCR. So, based on that, our risk committee, our board, et cetera had sort of adopted a range that we're comfortable operating with. And that's what we're in right now.

But as Mark was saying earlier, at some point, you get to a point where you don't need that buffer; it's imprudent to hold a buffer above a certain level and you need to do other things with that capital, either taking on more risk or investing or returning it to shareholders.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah. I mean, today, we've probably gone further than most, I expect, in telling you a bit about Solvency II. We've gone as much as we can before we can get the Solvency II model approval. But we're comfortable.

Oliver? Colin, you want to pass the mic back?

Q - Oliver G. Steel {BIO 6068696 <GO>}

Oliver Steel at Deutsche Bank. Three questions. So two little ones just first of all. On the targets or guidances that you've set today, so first for Aviva Investors getting to more than 10% of the total profit and then the products per customer, when do you want to be assessed on these in terms of timing?

Secondly, the property sensitivity in your economic solvency looked quite high, and I see it includes the commercial mortgages. So, I'm just wondering firstly what assumptions you're making within that and, secondly, does that worry you unduly?

Thirdly, slightly bigger question. Your P/E looks quite low, so implicitly the market is putting a high cost of capital on you. You're leaving your options open on what you do with any capital releases. But obviously, and this is short-term capital at work, or short-term capitalism at work I guess, investors will value a return of capital rather more highly than you might in terms of sort of investing in the business or making bolt-on acquisitions. So, I'm just thinking about the hurdle returns you want to set for investing the capital internally or into bolt-ons and what sort of timing you think you should be generating those returns over.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. So can't stop the third one. Yeah, the P/Es are low, aren't they, especially with the sort of growth rates we're showing at the moment. And we are well aware of what the investors value and in terms of the focus. I'm also aware, though, that we have to keep growing the cash flow to the shareholders. And it's like having a sugarcane machine; if you don't put the cane on the top, you're not going to get the sugar out the bottom. And that's a balance that we have to pick. And so if you did bolt-ons, they have to have pretty quick payback periods. I'm not a big fan of big strategic bolt-ons if they don't work out financially; it just doesn't make any sense to me, and I think we've proved that.

But I accept we're leaving ourselves some room, but bolt-on acquisitions do not change - just to be absolutely clear, bolt-ons do not change the target of getting to the 2:1 ratio. One of the reasons we chose that is because it gives us a pretty fair amount of wiggle room within we can invest other stuff as well.

The key thing we should be focusing on as well when you're talking about bolt-ons is we are looking closely at each business. In some businesses we're saying, well, actually, no, I want X hundred million capital out of you because we want to put that somewhere else, whether that's normal organic growth or whether it's bolt-ons or whatever. And the key thing here, I think the market focuses way too much on the generation of capital and where we've put it rather than reallocation of capital.

Just to be totally crystal clear, I would - and nothing planned, just to be clear, but I would sell a business line or a business if it wasn't meeting the targets and put that somewhere else, because that's how we work.

And so, I wouldn't think of it in the linear way of just the capital you generate out of the business in profits to put somewhere else. Think the way I'm thinking and Tom's thinking, which is reallocation of capital. It's one of Jason's key roles in the business is working out how we do that effectively, and we, in fact, spent a couple of days with the board just talking about this. So, that's the way I'd focus on that.

The property, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

So, the question was about the exposure to commercial property and the sensitivity there. And yes, it's something we do look at quite a lot. If you look at what we've been doing over last year, this year, we have been divesting from commercial mortgage and some of the legacy portfolios that we have. And so, that's something that we'll continue to think about over time. I would like to see that sensitivity less. We continue to have appetite for commercial mortgages, but we do have some legacy exposures that we would like to manage down.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah. And we have been. I mean, with some of the poor quality properties, we have been making some fairly significant divestments.

The other one on the Aviva Investors one and the products per customer, I'm not going to put a timeframe on it, partly just because I don't know yet. On Aviva Investors, there's a few moving parts in it. Obviously, the Friends Life money coming across makes quite a big difference because you can do that with some fairly modest cost increases.

The other two key things to focus on is the AIMS fund flows because that's high-margin product and it's good. And we have increased expenses a bit because we have some pretty big distribution agreements that were signed. So, we have increased that. I guess we've pre-funded that a bit as well. And they're well aware of what's expected, but I'm not going to give any further guidance on that today.

Blair?

Q - Blair T. Stewart {BIO 4191309 <GO>}

Thanks. It's Blair Stewart from BofA/Merrill. I've just got a couple left and they're not particularly interesting. The general insurance combined ratio, if you add back the weather and the reserve release impacts, the combined ratio deteriorated on a year-on-year basis by about 1.5 points I think. Just wonder what's going on there because the pricing environment looks to be reasonably good. Is it just the change of business mix or something like that?

The Friends Life contribution in the first half of the year was £174 million to the operating number. It's a bit more than I would have expected. Is there anything strange in there? Is there anything we need to take out that wouldn't be kind of "operating operating," if you like?

And thirdly, Tom, I think you alluded to looking again at the 2 times cover target after Friends Life has been integrated. Is that a pickup rate on that or is the 2 times something that we should think about for the long term? Thanks.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Maurice, do you want to start on (01:11:46)?

A - Maurice Tulloch {BIO 17683736 <GO>}

Sure. Morning, Blair. You're right, there's really two factors that adjust underlying. So the first one is the weather here in the UK. That's about a 3 point factor. So, yeah, if you go to underlying, you'd back that out. What I would say, and it's actually important, is we actually price and we use weather on a 15-year average and we actually price our business lines to a 95% COR or better. So listen, we can't control the weather but certainly we've benefited, and you're right, the opposite is in adjusting it out for the underlying.

And the other big factor if you look at the underlying is the Canadian motor. So, in the Canadian motor, we released 6 points. There was a new motor product that came in, and the big factor being prejudgment interest rate. If you look at what we released in terms of favorable, that was actually quite a bit less than our two peers released, and you adjust the two of those and, yeah, it does move up slightly. But once again, also in that business, we price to a 95% or better long term, which is about a 17% return on capital.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Tom?

Q - Blair T. Stewart {BIO 4191309 <GO>}

So I was wondering why it deteriorated year-on-year.

A - Maurice Tulloch {BIO 17683736 <GO>}

Pardon me?

Q - Blair T. Stewart {BIO 4191309 <GO>}

The question was why the underlying combined ratio deteriorated on a year-on-year basis. I think the underlying was about 97%. What was the reason for the underlying deterioration?

A - Maurice Tulloch {BIO 17683736 <GO>}

Yeah, it was 97.4% this year versus 95.5% last year, and the big movement is in favorable development. So, we're 2 points, 3 points favorable this year versus only being 0.7 points last year, and we've operated in a pretty tight range over the last 10 years. That's the answer. And with the weather being more benign. Those two factors.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

I think I can also just – there's one other factor as well on the motor side which you saw that deteriorate. We did increase the direct side of that motor book. And as you know, in the first year, you make a loss obviously. So that's one factor.

A - Thomas D. Stoddard {BIO 15071280 <GO>}

And again, also recall that pricing environment was pretty tough, and so there's sort of a delayed timeframe here as that earns through the book.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Okay. A couple of questions on Friends. So, you're right, Friends contributed about £174 million to operating profit. I think one of the adjustments you need to make as you think about any acquisition, one of the things we do in purchase accounting is we need to take the target and eliminate the AVIF and the DAC that's on their books. And so, the amortization of DAC would have been running through as an expense in the Friends Life operating profit. And so, we've now adjusted that and replaced it with AVIF, as you always would in an acquisition, and the AVIF is excluded from operating profit. So, that's one impact you have to look at.

I'd comment, though, that our dividend policy, the real cash impact is tied to operating profit. So, although that's sort of a non-cash accounting adjustment, it's actually still driving the cash dividend that we'll be paying over time so shareholders can get the benefit of that positive adjustment.

And one other comment I'd make in terms of comparing last year versus this year as well is that if you look at the back book contributions to operating profit in the first half, last year we had about £139 million of good guys, £100 million in UK from expense reserve releases and then some from Poland. This year, we only had about £50 million of contribution. If you look at the whole year last year for 2014 and took the two companies together, there were about £500 million of back book effects that helped profit. So, so far this year, we haven't seen as much of that as we would have last year.

And then your point about – or question about the dividend cover ratio, I don't have a new dividend policy to announce today, and so I'd say that we're continuing with the 2:1 dividend cover ratio over time. I do think, though, that as we get better in looking at Solvency II capital generation, we'll probably want to refine that and end up replacing it with something that's a little bit more tightly aligned with cash.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

There's a question at the front.

Q - Ming Zhu {BIO 17001429 <GO>}

Ming Zhu, Canaccord. Just two questions, please. First is on the UK Life. I think when Friends Life was standalone, you had retention ratios of between 30% to 40% from the back book. And just two-and-a-half months into the acquisition, so where are you now and how much more to go?

And the second question sort of a tie back to Oliver's - Aviva Investors. And you've spent quite a bit of money on this half-year in terms of building a new team and new products launching. And how much more to go on expense, because I'm trying to work backwards in terms of your target of group contribution from Aviva Investors, because after the acquisition of Friends Life, you gave a guidance of about £40 million contribution a year, I think, from the insource and funds. So I'm trying to sort of - in terms of the timing...

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Yeah. Okay. Yeah, the first one?

A - Andy D. Briggs {BIO 4311809 <GO>}

Absolutely. So on the first question, in the old world where basically people saved to retirement and then bought annuities, it was quite relevant to look at the proportion of people that did that with you. In the new world of pension freedoms, basically there's a whole host of different things people will do. They'll carry on saving into their pension as well as starting to draw some income out. They'll take their tax-free cash but carry on, invest it in a pension. So, we now can offer the full range of pension freedoms across all our customers, so as of releases we did last weekend. So we now have that full range for all of our customers, be they Aviva, heritage, Friends.

We're not measuring specific retention rates, because the world has moved on. But the point I'd draw out, as we said before, is if you look at our VNB, on individual annuities, it's down 11%. Annuities overall is up because of the bulks contribution. But individual annuity is only down 11%. But then on the pension and platform side, our VNB has virtually doubled. So, basically, we're doing a good job of offering a broad range of options to our customers, and that's driving our growth in UK Life.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

On the Aviva Investors and the Friends Life integration, of the £225 million, the figure, I think I'm right in saying, was £45 million in savings from the fund managers. You haven't really seen any of that come through yet. The reason being, you've transferred over the Friends Life but we've kept those people because we're going to be taking on a lot more assets from AXA and other players.

You'll get the AXA £24 billion this year. And I think we've said publically, that was at a figure of above 12 basis points?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Above 14 basis points.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

14 basis points. So, above 14 basis points. That's all we've ever said publically. And then there's more as well next year. And we said it was around about £70 million we would bring in is what we've said. And you would expect next year we'd get some more chunky amounts in, if that's helpful.

Yeah? And then I'll come over to this side.

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. Andy Hughes at Macquarie. A follow-up question on the apples and jumbo jets, which I never think about either. So, I think the answer to my previous question was that there was not much impact from including transitionals and the economic capital ratio. And I guess it begs the question, if that's the case, why would you use transitionals?

And the second question was basically following up on the bit about the re-risking of the Friends Life asset portfolio. Couldn't you do that today by reinsuring the assets across ahead of the Part VII transfer and making the asset switch today?

And the third question is on the pensions VIF. Are you still assuming people terminate at 75 or are you assuming they've gone beyond that, and is that going to have a positive impact? Thank you.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. So, firstly, why transitionals. I think the answer is very simple: because the transitionals basically takes account of the risk margin. And I didn't say we didn't have any. Of course we've got some, but I'm very comfortable with where it is. And the fact is the transitionals for us fall off slower than the liabilities fall off. Does that make sense? So, the transitionals will fall off slower than liabilities fall off. So, it's good.

Q - Andy Hughes {BIO 15036395 <GO>}

I guess I'm just trying to get to what the capital ratio might look like under Solvency. That's the kind of - what I'm trying to...

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Well, the capital ratio under Solvency II, of course, doesn't include the transitionals. Anything else is nonsensical. But I'm not going to give you the capital ratio because for obvious reasons...

Q - Andy Hughes {BIO 15036395 <GO>}

All right. So, I guess, my point is it would be higher than what you're reporting today if you include transitionals?

A - Mark Andrew Wilson {BIO 7102576 <GO>}

No, because there's no risk margin in what you're reporting to...

Q - Andy Hughes {BIO 15036395 <GO>}

Oh, okay.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Right? So, the way to think about it is we've tried to get our calibrations of Solvency II in the ballpark of where our calibrations are now. That's the sort of thing we've tried to do. But of course, that includes transitionals because that takes account of your risk margin. And that's what it was done for. That's the whole reason it was done. And I think Sam Woods tried to be as unambiguous as he could possibly be. I think his words were so let me be clear, a dividend is paid after the benefit of the transitionals. I don't think he could be any more unambiguous if he tried. So, we'll see.

On the other two, Tom?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

Yeah. On the re-risking or the aligning, I think you could think of this as analogous to trapped capital. So, effectively, it's being managed and it's sort of stuck in that subsidiary, so I can't get my hands on it as cash to redeploy it elsewhere. But we will once we can align the risk appetite. Yes, it's there and so that's a good thing, and so you could theoretically take more risk anticipating that you would be able to get your hands on that, but can't actually get to it now. And so, that's why we need to do the work.

Was there another one or was that...

Q - Andy Hughes {BIO 15036395 <GO>}

On pensions, 75 termination, is that helping the VIF...

A - Mark Andrew Wilson {BIO 7102576 <GO>}

No...

Q - Andy Hughes {BIO 15036395 <GO>}

And you're still assuming everyone terminates at 75? And what's the impact if you turn that on to go on for (01:21:25)?

A - Thomas D. Stoddard {BIO 15071280 <GO>}

I'm looking at John Lister and Andy Briggs for this.

A - Andy D. Briggs {BIO 4311809 <GO>}

We've not changed any assumptions around that. And obviously, if people stay invested for longer, we'll see the benefits. And that's what's happening. Basically, people with the smallest pots are tending to cash them in. That's happening across the market as a whole. The effect of that is pretty negligible in terms of the size and scale of our pensions book. Others are basically deferring retirement. Given our size and scale with, again, that £80 billion of unit-linked pensions assets, we'll just keep taking the annual management charge for further years on that. So, yeah, but we haven't adjusted any of our VIF or assumptions for that at this stage.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Andy, the other thing that – I guess it was the unknown result from RDR, is that the people – cashing them in because there's no incentive for brokers to twist it. Our retention's been better, but we haven't taken that to anything yet. But it's interesting, isn't it?

Ashik, you had a question?

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. I just want to get your thoughts on this pension consultation, this change in the tax regime. I mean, what are your thoughts into that? What are you suggesting to the Chancellor on that would be good, and how does that impact your outlook on the pensions business? So, that's one.

Secondly, you mentioned that expected outlook on capital is much better, i.e., you will free up some of the capital which you want to deploy in somewhere else. And clearly, there is a whole lot of bulk annuity market is there, which the market is expecting will be in hundreds of billions over the next five years. So, would you try to go all guns blazing into that market for any reason, or do you think that you will still be skeptical with that market even with a whole lot of new capital-light models around, so – and there's a huge amount of expected longevity reinsurance market as well which we have been seeing over the last one, two years. So, what's your thought on that outlook? Thank you.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Okay. Those are some fairly big questions. The pension consultation we welcome. And I think it is time for review and we are and will be intimately involved in it. Our views are clear. But I'll talk about them here just briefly.

Firstly, any pension must be workplace-based. In the developed world, if it's not workplace-based, it doesn't work. And I think probably most people would agree with that. Now, given we have one in four pensions in the UK and we are the number one workplace pension provider, I think that's helpful. In fact, it's very helpful.

On the way it is treated for tax, it's actually we have taken the Friends position on this because we thought it was compelling, and that's that there should be a flat rate of tax of 33% because at the upper end of the market, one, it would save the government money

- I think they'll want to do that. Secondly, at the upper end of the market, they will save anyway for 33%; they'll save for tax relief in anyway. And at the lower end of the market, it's going to encourage more saving, and that's where it needs to happen from a society perspective. And so, take Aviva out of it, we would do well as well out of it and our market is mass market. But for society, I think it would be a really good outcome. So, those are the two things that we are pushing that I think would be very helpful.

On bulk annuities, you'll recall we sat here last year and I took a different position, I think, to most other groups in the UK and I said the bulk annuities didn't work as well under Solvency II. And I also said that the margins would get tighter. And what I said there, and it still holds, is we will come in and out of that market and be selective and more opportunistic on the bulks. We are a big bulk writer. In fact, the bulk annuities writing went up in this last half a reasonable amount. But annuities are more balanced as our overall book.

So, what are you going to see? Solvency II, there is no doubt that bulk annuity - because you don't get - at the moment you get the transitionals; by the end of the year, you don't. Into next year, the rates will increase. There is no other possible outcome. Or the margins are going to get hammered. Take your pick. And it's one of those two things. And we remain that and we'll keep on coming in and out of it.

And bulks, like all of our other product lines, are a part of our offering. But just to put it in perspective, the VNB from our protection business is now bigger than our total annuities, okay? So, what you have seen is quite a dramatic change that we've been doing for two years but you've only really seeing it come through the results - it's one of the reasons you're seeing our results up, you're seeing that come through. It's more effective in Solvency II, it's got a better cash flow payback, it's got higher VNB and lower capital requirements. So, it ticks all those boxes. And for the first time I don't know in how many years - Jason, you might be able to help me, but...

A - Jason Windsor {BIO 17967688 <GO>}

Probably 10 years.

A - Mark Andrew Wilson {BIO 7102576 <GO>}

Probably 10 years - you've seen our protection higher than annuities. And I like that mix of business.

And I'm being told I'm well over time, so I'm going to have to - I'm going to close it. The guys will be around and I'll be around for a bit as well if people want further questions. But thank you, everyone. And as always, I'll look forward to reading what you have to say.