S1 2020 Earnings Call

Company Participants

- Andy Briggs, Group Chief Executive Officer
- Andy Moss, Phoenix Life Chief Executive Officer and Group Director, Heritage Business
- Claire Hawkins, Head of Investor Relations
- Rakesh Thakrar, Deputy Group Finance Director
- Susan McInnes, Chief Executive Officer SLAL and Group Director, Open Business
- Unidentified Speaker

Other Participants

- Analyst

Presentation

Claire Hawkins {BIO 20555563 <GO>}

Good afternoon, and welcome to the Phoenix Group 2020 Interim Results Presentation.

My name is Claire Hawkins, and I'm the Corporate Affairs and Investor Relations Director here at Phoenix.

We're all adapting to new ways of working in a COVID-19 world. And we thank you for joining our virtual presentation.

My colleagues and I are joined today by our sell side covering analysts within the Zoom environment to better simulate a live Q&A session. Analysts will be asking you to raise your hands to ask questions later. For those of you joining us on the webcast, you will also be able to raise questions in the normal way.

But before we get to Q&A, let me hand you over to Andy Briggs, our Group CEO and Rakesh Thakrar, our Group CFO, who will take you through our interim results presentation.

Andy Briggs {BIO 4311809 <GO>}

Good afternoon everyone and welcome to the Phoenix Group half-year results.

It's been a busy and successful half year for Phoenix as we completed the ReAssure deal and became the U.K.'s largest long-term savings and retirement business. Our strategy remains clear, simple, and unchanged. We do three things, which in turn drive delivery of the wedge.

First, Heritage, where we are the market leader in providing a safe home for customers in product lines, which are no longer actively marketed. It delivers a steady flow of cash for shareholders, the bedrock of the wedge. It is also the major driver of one of our key growth areas within the wedge, management actions.

Second, we're the market leader in M&A, and successfully integrating those businesses. And third, we are building a thriving and growing Open business through our capital-light workplace and retail pensions businesses, and through BPA. Together, these are the key drivers of growth within the wedge. Our financial framework is also clear, simple, and unchanged. We run a broad range of savings and retirement businesses, all to deliver cash, resilience, and growth.

2020 has been dominated by COVID-19. It is a horrific virus that has severely impacted many families and many businesses. These difficult times have demonstrated the resilience of Phoenix's business model. Financially, we are very resilient. We paid our dividend as planned and reconfirmed our cash generation targets; more from Rakesh on this later.

Alongside this, we championed ordinary savers and pensioners, many of whom are our customers, by making the case strongly why dividends should be paid when they can be afforded. And we took no form of government support, and furloughed no staff.

What I'm most proud of is how our colleagues have pulled together to deliver for our customers. We got 99% of our people working from home within 10 days of lockdown; impressive. What's even more impressive is that throughout that period, we kept our phone lines open. Our call answer rates were over 93%, which is close to pre-COVID levels, and we maintained customer satisfaction above 90%.

Our people were determined to be there when our customers needed them most. We implemented a range of other customer initiatives, including waving the moratorium on COVID related claims and our SunLife business, helping customers, who originally took checks to get banks payments, and provided the dedicated contact line for frontline care workers. Alongside this, we have a strong focus on the health and wellbeing of our colleagues, and our contribution to our broader communities. As a result, both colleague pride and advocacy in Phoenix grew by 20 percentage points to 73%.

So, in a volatile COVID environment, how did we do in the first half against our financial framework of cash, resilience, and growth? Cash generation is up 51% to GBP433 million. We remain as resilient as ever with a GBP4.0 billion Solvency II surplus at a coverage ratio of 169%. And in particular, all the economic volatility in the first half only had a GBP0.2 billion impact on this GBP4.0 billion surplus.

In terms of growth, as ever, our focus is value, not volume, and is all about cash, so the long-term cash, we expect from new business. This was up 41% to GBP358 million, a strong set of first half results. As well as new business, M&A is another key growth driver for us as we completed on the ReAssure transaction two weeks ago. With ReAssure, we are now the U.K.'s largest long-term savings and retirement business.

ReAssure adds GBP76 billion to our assets under administration, taking the total to GBP324 billion. And it adds 3.9 million policies taking our total to circa 14 million. ReAssure also adds GBP7 billion to our total long-term cash generation, including GBP800 million of cost and capital synergies.

On a pro-forma basis, the first half cash generation is GBP1.1 billion, Solvency II surplus is GBP4.4 billion, and the shareholder capital coverage ratio at 150%. And all of this enables us to increase our cash generation target for this year to GBP1.5 billion to GBP1.6 billion, demonstrating what a highly cash-generative business the enlarged Phoenix Group is.

Our focus on cash, resilience and growth turns into dividends for you, our shareholders. With a GBP4 billion impound capital surplus on top of the GBP5.8 billion of capital requirements that we maintain above our best estimate liabilities, we are well capitalized. And with our resilience and liquidity, we will be paying our interim dividend of GBP234 million. With Phoenix, you get real visibility of cash generation with the gross cash coverage of the dividend this year expected to be 3.2 to 3.4 times.

Now the strength of our cash, resilience and growth is all down to the strength of our underlying businesses, and successful execution and delivery in those businesses. And it's this I am most pleased with in the first half of this year. Heritage is the engine of our GBP1.1 billion cash generation and is also key to resilience, where some excellent work was done around hedging and active credit management. We've also done a first class job for our customers here.

In terms of M&A and integration, again, a busy first half, and I'm delighted to be able to confirm we've already have banked GBP227 million of our GBP800 million synergy target from the ReAssure deal. What I am even more pleased about is how well Day 1 went and how great it is to have our new colleagues from ReAssure as a part of the Phoenix family. Alongside this, we are on track with the Standard Life tradition program.

And then in the Open business, long-term new business cash is up by 41% at GBP358 million in spite of the challenging markets. Key to this has been our investment in our proposition in both Open business and in BPA, alongside strong asset origination.

Finally, we made good progress building our people capability. Matt Cuhls and Mike Eakins have joined the ExCo from ReAssure, Mike in the exciting new role of Group CIO. Following Susan's retirement plans, Andy Curran is joining us to run the Open business and we're appointing some of our excellent internal talent around the key business units in our Open business, supplemented by hiring Tom Ground externally to run annuities and equity release. And then Sara Thompson has joined as Group HR Director, and Claire Hawkins were promoted to the ExCo, adding corporate affairs and brand to our investor relations remit as we increase our external presence.

I'll be back shortly to talk about the outlook, but first I'll hand over to Rakesh to talk through the numbers in more detail. Rakesh?

Rakesh Thakrar {BIO 20549114 <GO>}

Thank you, Andy, and good afternoon, everyone.

As Andy said, we have had a strong first half of the year despite the financial volatility driven by the pandemic. These financial highlights demonstrate that we continue to manage our in-force business to ensure resilience, which leads to predictable cash generation and we are also focused on growth through new business.

Turning first to cash; in the first six months of 2020, Phoenix's insurance entities remitted GBP433 million to Group. This is after the provision of GBP50 million of capital injected into our Irish domicile subsidiary to strengthen its capital position following the falling yields. Alongside that, the newly acquired ReAssure business also delivered strong cash generation, remitting a further GBP690 million.

As a reminder, our acquisition of ReAssure was made as if the transaction happened on 30th September 2019; and as such, the GBP690 million reflects cash generation since then including GBP290 million from the Old Mutual Wealth businesses acquired from Quilter. Together therefore, the combined group delivered GBP1.1 billion of pro-forma cash generation in the period.

Today, we have announced an update to our 2020 cash generation guidance, increasing the Phoenix-only target of GBP800 to GBP900 million to reflect the GBP690 million of cash generation delivered by ReAssure. Historically, ReAssure businesses remitted cash only once a year at the start of each year. So, we aren't reflecting any further ReAssure cash flows in our 2020 target at this stage.

Our new target range is therefore GBP1.5 to GBP1.6 billion and we are firmly on track to meet this. As a reminder, we expect the combined group to deliver GBP19 billion of cash generation over the long term with GBP5.9 billion of this emerging over the next four years. These cash generation targets reflect the business that is already incourse. They therefore exclude any new business written after 31, December 2019, whether this new business arises through BPA also the Standard Life brand in the Open business. They also exclude any future M&A and exclude management actions after 2023.

To demonstrate the resilience of our four year cash generation target, we have set out the sensitivity of this target to various stress events. These sensitivities are presented for the combined group and therefore include the ReAssure business. As you will be aware, Phoenix has a low appetite to market risks and uses hedges to mitigate the majority of the exposure to equity and interest rates.

We also have a lower exposure to credit risk than our peers due to the relative size of our shareholder business and maintain a high quality credit portfolio, which we actively manage. This translates into the low sensitivities to market risks we present today and demonstrates that we would be able to continue to pay our dividend under all these scenarios.

Before we move on to talk about resilience, I will walk you through our IFRS results. We delivered operating profit of GBP361 million in the first half of 2020, 11% higher than the prior year. This increase is driven by strong performance in our Heritage and UK Open business segments, which have seen higher new business profits for BPA and Sun Life respectively. The impact of demographic assumption changes and experience variances has been small with positive longevity experience variances on our annuity business having been offset by negative mortality experience variances on our protection business.

The net positive investment return variances and economic assumption changes primarily arise as a result of gains on the equity hedges held by the life bonds following equity market losses during the first half of the year, together with the impacts from falling fixed interest yields. These positive impacts have been partly offset by widening credit spreads. Finally, our non-operating items include GBP48 million of costs incurred on the SLAL transition program.

Maintaining Phoenix's capital resilience has been my key priority during this period of economic turbulence. Our primary focus continues to be the overall quantum of surplus. This is because cash generation is made from surplus capital rather than surplus ratios. Therefore, whilst we have a target range for our shareholder capital coverage ratio, all of our hedging actions are taken to protect the overall quantum of surplus.

As at 30th June 2020, the standalone Phoenix Group had an estimated Solvency II surplus of GBP4 billion and a shareholder capital coverage ratio of 169%. This position is stated after recognition of the 2020 interim dividend of GBP234 million and excludes GBP2.0 billion of unrecognized surplus in the unsupported with-profits funds and staff pension schemes.

Shareholder-own funds continues to be a good starting point for determining shareholder value, but does not include a number of areas, where value exists. These include contract boundaries, where the value of in-force on unit-linked business is restricted under Solvency II, and the shareholders share of our with-profit estates. Adjusting for these items provides a proxy for shareholder value at 30th June 2020 of GBP6.1 billion, which equates to GBP8.45 per ordinary share.

This value proxy is effectively ex-dividend. It places no value on future new business from vesting annuities, a BPA and open channels or management actions. It also excludes ReAssure. During the year, we saw the PGH group surplus increased from GBP3.1 billion to GBP4.0 billion. The main driver of this increase was the raising of GBP1.4 billion of private capital net of costs. This was largely undertaken to fund the acquisition of ReAssure, but we also took the opportunity to access the debt capital markets in May when they were particularly strong with the proceeds providing additional flexibility for the refinancing of existing Phoenix borrowings.

As I mentioned, my priority in the period has been to preserve the resilience of the Group's capital position. Whilst we are not immune to the economic volatility, our approach to risk management has provided significant protection to our financial strength as equities and rates fell and credit spreads widened. The GBP0.2 billion solvency strain resulting from economics reflects the impact of this volatility, post hedging, together with falls in property pricing and the impact of downgrades experienced year-to- date. This movement is broadly in line with our published sensitivities.

The pandemic has also resulted in us making some changes to our underlying assumptions. Particularly on the property assumptions that underpin our GBP3.1 billion equity release mortgage portfolio, where we have strengthened our assumptions on future inflation, prepayments, and dilapidations.

We have also strengthened our persistency assumptions of products with valuable guarantees in relation to late retirements. However, we have made no change to our longevity assumptions in the period and will complete our annual review of this assumption across the combined group in the second half of the year.

On 22nd July, we completed the acquisition of ReAssure. As Andy outlined in his introduction, this is a deal that reinforces our key attributes of cash, resilience, and growth. On a combined group basis, the pro-forma Solvency II surplus was GBP4.4 billion at 30th June 2020 with a shareholder capital coverage ratio of 150%. This ratio is well within our target range of 140% to 180%. The pro-forma includes an estimated Solvency II surplus of GBP1.7 billion for the ReAssure business on a standard formula basis and reflects GBP120 million of capital synergies from equity hedging actions completed by Day 1. Moving forwards, delivery of management actions and integration synergies will further strengthen this solvency position.

Here, we present the sensitivities of the combined group. The sensitivities reflect the equity and interest rate hedging and longevity and reinsurance currently in place within the ReAssure business and illustrate that our large group remains resilient to risk events.

We have modeled the impact of our usual range of scenarios on both of our Solvency II surplus and ratio and added a separate credit downgrade sensitivity in response to investor feedback. I must stress that these scenarios are being applied to a capital position, which already reflects the economic environment as at 30th June 2020, which saw 15 year swap rates sitting at 44 basis points, 5 to10 year swap margins at around 130 basis point and the FTSE100 at circa 6,200. The fact that the combined group remains within our target shareholder capital coverage ratio range of 140% to 180% under all scenarios applied to this already strain solvency position is evidence of our ongoing resilience.

Phoenix has a diversified, high credit quality shareholder asset portfolio. 98% of our GBP21.6 billion shareholder debt portfolio is investment grade with only 16% held in BBBs. We also have a low exposure to those sectors more at risk from the pandemic with only 1.6% exposure to the oil and gas sector and 2.2% exposure to airlines, hotel, leisure, and traditional retail.

As at 30th June, our portfolio of illiquid shareholder assets was GBP6.1 billion. The credit quality of this illiquid asset portfolio mirrors that of our debt portfolio with 98% investment grade. Our illiquid asset portfolio continues to be well diversified across five main asset categories. For this portfolio, we are particularly focused on where the scheduled cash flows are met as this is a key indicator of the resilience of the underlying investment. As at 30th June, 100% of scheduled cash flows had been paid. The largest category is equity release mortgages where we have an average loan to value of 34% and an average age of 77 years.

In our 30, June 2020 valuation of this asset class, we have applied a one-off 2.2% reduction to the quarterly house price index to reflect the lower volume of property transactions in May and June. Our GBP1.9 billion portfolio of private placement loans has an average credit rating of A minus and is diversified across 41 exposures with over 64% of the portfolio secured on a variety of assets. And over 85% of our commercial real estate portfolio has a loan to value lower than 50%.

We continue to manage this portfolio very closely, and our focus on maintaining a high credit quality is reflected in the experience during the first half of the year. We have worked extremely closely with Aberdeen Standard Investments during the period to actively manage the credit quality of our debt portfolio, and rotate out of assets at risk of downgrading where possible.

Integral to this active management was a block trade, which replaced GBP0.5 billion of sterling corporate credit by market value on the ASI hit list with U.S. dollar denominated corporate credit. 75% of this trade related to moving BBB sterling credit to single A U.S. Dollar credit. This trade avoided a GBP60 million solvency strain, which would have crystallized had the bonds downgraded and generated GBP30 million solvency benefit recognized within management actions.

It's also increased diversity by individual issuer, sector allocation, and geographic region. Despite this active management, we are still experiencing some downgrades during the period with GBP860 million or 6.5% of bonds in the matching adjustment portfolio being subject to a letter downgrade. However, only GBP16 million, or 0.1% of the bonds have downgraded to sub-investment grade and there have been no defaults.

The maintenance of the credit quality of our debt portfolio is evidenced by the lack of average rating migration that we have experienced over the first six months of 2020 with only the industrial and utilities sectors seeing a decrease in average rating over the period. ReAssure also has a well diversified credit portfolio and made significant progress during 2019 to improve the quality of this portfolio, trading out of UK BBB bonds and into U.S. Dollar single A credit.

It is pleasing to see this credit quality maintained year-to-date, reflecting the active approach to credit management taken by the ReAssure team, despite the downgrades experienced in these volatile markets. The downgrade experience across the ReAssure portfolio is similar to our own with GBP575 million or 5.5% of bonds in the matching adjustment portfolio subject to a letter rating downgrade and GBP22 million or 0.2% of bonds downgraded to sub-investment grade. There have also been no defaults.

Turning now to growth; Phoenix has three key growth options, M&A, BPA, and Open business. First let me deal with M&A and integration. With a combined synergy target of GBP2 billion across Standard Life and ReAssure, our market leading integration activities continue to be a real driver of shareholder value. As you are aware, the nature of the ReAssure business being acquired has enabled us to deliver significant synergies on Day 1.

(Technical Difficulty)

However, we were able to limit this strain to a three to four week delay in plans and we remain on track to deliver our synergy targets on time. We have talked before of the complexity associated with bringing together the Standard Life and Phoenix Internal Models. Submission of our pre-application in June was a significant milestone in this program and we are on track to make our final application by the end of the year.

Any capital benefits that emerge from this harmonization will therefore emerge in our half year 2021 results, although, we have not anticipated any such benefits in our capital synergy targets. Integration of the ReAssure business will follow Standard Life transition activity, as we continue to promote enterprise stability. No decision has been taken on the end state customer and IT operating model of the ReAssure business and we have therefore made no estimate of potential savings in our cost synergy target.

Phoenix does not include new business in its long-term cash generation guidance. New business, whether through BPA or through the sale of Open products is therefore incremental to cash generation and brings further sustainability to our dividend.

In the first half of 2020, Phoenix saw gross inflows on new business across its three business segments of GBP4.2 billion. We estimate that this new business will generate GBP358 million of incremental long-term cash generation, circa 1.5 times the 2020 interim dividend.

Phoenix's Open business is capital light and growing, despite the challenged of COVID-19. In first half of 2020, our Open business in the UK and Europe delivered gross inflows of GBP3.1 billion from new business and GBP122 million of incremental long-term cash generation. Workplace continues to be our engine for growth and gross inflows in line with first half 2019 demonstrate the resilience of this business. Our Open business has also benefited from reduced outflows compared to last year as both employers and customers delay in making financial decisions.

Overall, it was a tale of two quarters with strong performance across all product lines during Q1 falling back during Q2 as people began to deal with the uncertainties resulting from the pandemic. Looking forward, it is clear that the second half of 2020 will continue to be challenging.

As you heard from Andy, we have made significant progress in our workplace proposition and will continue to do so as we look forward to the launch of our ESG passive default fund later this year. We continue to promote the use of digital, building on the significant progress made in this space so far this year and will continue to build out our retirement service seeking to generate flows into our retail product lines. Our BPA business had a very successful start to the year, putting GBP90 million of surplus capital to work across three deals, which will generate incremental long-term cash generation of GBP236 million.

The largest of these deals was an GBP800 million buy-in with Liverpool Victoria pension scheme. This was a complex transaction that included the conversion of an existing longevity swap and illustrates our ability to undertake increasingly complex opportunities in the future. Our deal economics are also continuing to improve with the capital strain reduced from 9% in 2019 to 8% in 2020 and thereby reducing the average payback from six to seven years in 2019 to five years in 2020.

We have previously guided to allocating circa GBP100 million of surplus capital per annum to BPA. The success of the team in the first half of the year means that we have the opportunity to do more. Especially as the pipeline of opportunities continues to be strong. However, we will only allocate additional capital if deals present attractive economics. We will, therefore, continue to participate on a selective and proportionate basis in this marketplace seeking to deliver value and not volume.

Management actions also deliver growth. Our success in the BPA market is underpinned by strong illiquid asset origination. During the first six months of 2020, we originated GBP789 million of illiquid assets across a range of asset classes, a 47% increase on the same period in 2019.

We continue to prioritize credit quality in our portfolio and first half 2020 origination had an average credit rating of A plus. Just under half of this origination was into ESG investments including social housing, renewable energy, and sustainable development. With illiquid assets now comprising 27% of assets backing annuity liabilities, we continue to make good progress towards our target allocation of 40%.

Illiquid asset origination continues to be one of our key management actions, and together with the benefits arising from active management of our credit portfolio, increased our Solvency II surplus by GBP0.1 billion during the period. This increase comprises GBP0.2 billion increase in own funds, which is a direct increase in shareholder value.

Whilst our first half management actions have been focused on asset origination, we are on track to deliver a broad range of management actions in the second half of the year. These include the Part VII transfer of the L&G mature savings business to ReAssure, scheduled to complete during Q3, the transfer of circa 1.2 million legacy Phoenix policies to Diligenta, and the securitization of a further circa GBP600 million of our ERM portfolio. Together, these management actions will increase the Group's Solvency II surplus and improve the shareholder capital coverage ratio.

I will now hand you back over to Andy.

Andy Briggs {BIO 4311809 <GO>}

Thank you, Rakesh.

I will now focus on outlook, before we move to Q&A. We've already talked about resilience, and it's more of the same going forward. So, I will cover the outlook for cash and growth, starting with cash.

As Rakesh said, we expect our in-force business to deliver GBP5.9 billion of cash generation between now and the end of 2023. If we take off operating costs, interest and dividends, the excess is GBP2.6 billion. So, if we use GBP0.8 billion of that to reduce debt, where there are maturities and core dates that leaves a further GBP1.8 billion of surplus available for growth, which we will use for the highest value option at the time. This clearly shows that Phoenix is a highly cash-generative business. This means that the dividend is very safe, with a gross coverage ratio of 3.1 times, and that we can fund the range of growth options we now have.

If we then look longer term, we get a balance of our GBP19 billion of cash generation from existing business, so after the GBP5.9 billion to 2023, a further GBP 13.1 billion from 2024 onwards. After debt and interest that leaves an GBP8 billion excess, enough to cover the dividend for a further 16 years out to 2040. But we expect to do much better than this. We will add to our cash generation through new Open business, further BPA, additional M&A and management actions, which can be funded through the GBP1.8 billion of surplus cash generation merging over the next four years. This will enable us to enhance the sustainability of the dividend and will, over time, allow us to grow the dividend.

So, let's move on to look at the outlook for growth, aligning this to the wedge. As the U.K.'s largest long-term savings and retirement business, we need to understand the major drivers of change in UK savings and retirement. And we see three of them, as shown on the slide.

First, insurers are consolidating to release trapped capital and to deal with cost and efficiencies due to legacy systems and regulatory change. And I would argue that in a post COVID-19 world, where some companies are struggling with their balance sheets, their valuations, and struggling to pay dividends, the pace of consolidation will increase. The combined Phoenix and ReAssure Group is clearly the unrivaled market leader in both running Heritage businesses and in delivering M&A and integration. And it remains an important part of our strategy going forward.

The second driver is strong defined contribution pensions growth. There are two key elements to this. The first is auto enrollment, coupled with a shift from defined benefit to defined contributions. This has tripled contributions since 2012. At Phoenix, we are a top three player in workplace pensions through our Standard Life branded business. This is a market, where scale and cost efficiency are critical. And this is a good example of where the whole, across the Group, is more than the sum of the parts.

We have a market leading partnership with TCS, built originally around the Heritage business; and as a result of our scale, we are able to secure an excellent digital customer experience, and also a market leading cost efficiency as we migrate from the Standard Life mainframe platform to the TCS BaNCS platform.

The other driver of strong DC pensions growth is the aging population, and pension freedoms. As the U.K.'s largest long term savings and retirement business, with over GBP300 billion of assets and 14 million customers, we have more of these 50-plus year old customers than anyone else. And they need help and support to think about consolidating and journeying to and through retirement. This is a further benefit of having both Heritage and Open businesses together. And in terms of the impact of COVID-19 here, through previous recessions we've tended to see the savings rate increase and people have a greater focus on their finances.

The third key driver of change is that corporates are de-risking. I've often said that I'm yet to meet the finance director of a manufacturing business, who is pleased to have a large pension scheme attached. So, imagine if you were the finance director of that manufacturing business during COVID-19, and you're worried about socially distanced manufacturing, and how you retail in a very different world of COVID-19. And imagine that you then get the email from your pension scheme actuary, saying you need to worry about credit risk within your pension fund. You are going to, want more than ever, to de-risk and offload that pension scheme and focus on your manufacturing. So, again, I see COVID-19 accelerating this driver of change.

At Phoenix, we will continue to take a selective and proportionate approach to BPA. One of our key advantages here is that shareholder credit and annuities only make up about 10% of our UK balance sheet compared to a much higher proportion of most of our competitors. We can therefore afford to grow our annuity business in a selective and proportionate way and benefit from better diversification in doing so while keeping this through a similar low proportion of our total balance sheet.

In summary, I believe Phoenix is very well placed to benefit from the strategic drivers of change in UK savings and retirement, while maintaining the financial discipline that has served Phoenix so well in the past.

So, what are our priorities for the second half of this year to turn those strategic opportunities into reality? For Heritage, the priority is delivering the cash and the management actions, which are weighted to the second half of this year with continued strong focus on our customers. For M&A and integration, the agenda is clear.

On Open business, the BPA focus is asset origination and further improving the capital efficiency, where we have made some progress, but there's much more to be done. And then for our 14 million customers expanding our digital retirement service is another priority. In workplace, it's the launch of our ESG passive default fund.

I also want to emphasize the importance of sustainability. With our scale now, we are much more than just a financial engineering consolidator. We have a much broader core social purpose. And I see sustainability at the center of that. Championing sustainability in the way that we run our business as we invest one third of a trillion pounds on behalf of our 14 million customers.

And finally, our future calendar; the only point I'll draw out here is that we are planning at capital markets day on the 3rd of December. This will be very much as we usually do, a working session, where we will deep dive into each business area and give you more color on our plans. So, this isn't some big strategic review; it continues very much as evolution, not revolution.

And with that, we will move to questions.

Questions And Answers

Operator

(Question And Answer)

A - Claire Hawkins {BIO 20555563 <GO>}

Welcome back. Today's Q&A panel will be hosted by Andy, and he will be joined by Rakesh, Andy Moss, who is the CEO of our Heritage Business, Susan McInnes, who is the CEO of our Open business.

First, we will take questions from ourselves side analyst. (Operator Instructions)

Andy, over to you.

A - Andy Briggs {BIO 4311809 <GO>}

Thank you so much, Claire. And Operator, can we get our first question, please?

Operator

Thank you, Andy. Our first question is from Louise Miles. Louise, can you please unmute your device and go ahead and ask you a question?

Q - Analyst

Hi. Good afternoon, everyone. Hope you can hear me.

So, we noticed in the appendices, the back that your half -- the half year '20 pro forma Fitch ratio is 29%, and obviously this included the positive investment return variance that we saw at the half year, and that even shareholder equity and that -- we would expect that to unwind as we see markets improve. So, how can you help us to gain comfort that the Fitch ratio isn't going to go above 30%, which is a requirement to maintain that A rating form Fitch? That's my first question.

My second question is you kind of gave some commentary in the release that you had some favorable longevity experience, but that was then offset by the negative mortality and this is based around COVID. It'd be great if you can quantify this on either side and also should we be expecting any longevity releases in the second half of 2020?

And then my final question is regarding the phasing of cash generation from both the ReAssure-Phoenix and the SLA entities. So throughout the year, what -- how should we think about the phasing for the Phase 3 three entities in the first and the second half? Thank you.

A - Andy Briggs {BIO 4311809 <GO>}

Okay. Thanks very much, Louise. So I'll take the third of those and then I'll get Rakesh to answer the first and second.

So, in terms of that the phasing, we haven't tended to have a particular policy around phasing between first and second half for the Phoenix or the SLAL legal entities, but obviously, we have guided and increased our target cash generation to GBP1.5 billion to GBP1.6 billion.

A - Unidentified Speaker

I can do that. Should we do it now?

A - Andy Briggs {BIO 4311809 <GO>}

Sorry? Can you hear me okay?

A - Unidentified Speaker

Sorry, go ahead, Andy. Yes, please.

A - Andy Briggs {BIO 4311809 <GO>}

Sorry. I heard some background talking now. Apologies.

So, we've increased our target to GBP1.5 billion to GBP1.6 billion cash generation. We've had a pro forma of GBP1.1 in the first half. So, that gives you a sense of what we expect in the second half.

As far as the ReAssure legal entity is concerned, historically, ReAssure have always done their cash generation in the first half of the year, just once a year in the first half. And hence, that's why with the GBP690 million of cash generation there, we've added the GBP700 million additional cash generation to the sort of target for the year as a whole.

Rakesh, do you want to pick up the first and second questions, please?

A - Rakesh Thakrar {BIO 20549114 <GO>}

Yeah. Thank you, Andy. And hopefully you can hear me.

And then Louise, just to your first question about the Fitch leverage calculation. So, you're absolutely right. On Slide 37, you can see that half year '20 pro forma of the Fitch calculation, and it's at 29%.

Now, I mean, this is the pro forma clearly as at 30th June. And I see a number of areas, where this will reduce over time. So, first would be just normal operating profits as they emerge over time. Second is that the L&G Part VII, which is due in September will help across a number of our metrics. And one of them will also help is on the Fitch calculation for the ratio. So, I should -- I would expect that to reduce. Third is just ongoing delivery of our synergies, our cost synergies, which will improve both profits within the life companies and the Group and therefore allow us to reduce that leverage.

And as you would have seen in one of the Andy's slides, where we are expecting all of the things being equal the repayment of debt maturities and on their core date, subject to maintaining balance sheet resilience of GBP0.8 billion; altogether, that will reduce the leverage ratio. Now out of that GBP0.8 billion, half of that -- probably half of that -- just on half of that is actually due early next year.

In relation to your second question about the favorable longevity, mortality, experience; so, within our IFRS results, we have seen positive longevity being partially offset by mortality experience. I mean these numbers are quite small, about GBP20 million in longevity favorable variance offset by about GBP10 million on the mortality experience.

Now looking forward, clearly, it's too early to tell. CMI '19 table is out. And currently, as you'll be aware, Phoenix is on the CMI '18 table and ReAssure are on the CMI '17 tables. We need to look ahead, see what the experience is telling us and then make a review at the appropriate time, which would be the second half of this year.

Back to you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks, Rakesh. Operator, next question, please.

Operator

Thank you. Our next question is from Ming Zhu. Ming, please unmute your device and ask your question?

Q - Analyst

Hi. Good -- good afternoon, everyone; just three questions, please. My first question is, could you please provide some color on your interest rate hedging, and how does that work -- if we enter a negative interest rate environment?

And second question is on the wedge diagram, since you've completed the ReAssure deal, which your cash generation tend to be, that's quite a lot towards the early years. And could you just please provide some color in terms of your new business plan, and the timeline when you will actually start to move into the shape of the wedge sort of going upwards over all cash generation?

And my third question is could you talk about in terms of we still having quite a lot of uncertainties from COVID-19? When you commit to the dividend payment and the increase going forward at 3%, how confident are you in terms of -- have you looked at scenarios where you assumed further lockdown? Or L-shaped recession? Thank you.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks very much, Ming. So, let me take the second and third of those, and I'll ask Rakesh to cover the first.

So, in terms of COVID and dividend and so on and so forth, that's exactly what we do. We run a broad range of scenarios including some very severe scenarios. And then as a Board satisfy ourselves, that the dividend is affordable across those different scenarios. And the critical thing with Phoenix is that the we hedge off most of -- hedge out most of the equity risk, most of the interest rate risk. And then in terms of the kind of shareholder credit, we keep shareholder credit annuities to circa 10% of the balance sheet, and therefore it's a much lower proportion than others. And hence what you saw in the dislocation in the first half of this year, the total economic a variance from the strain of the first half of the year was only GBP0.2 billion in the context of a GBP4 billion surplus. So, obviously, we're very, very resilient indeed as a balance sheet given the way we run the business.

In terms of the wedge, the point I would make is that we need to split the cash generation, which we do sort of year-end. We need to split the cash generation between the kind of organic underlying and then the management actions. And the management actions is to be the higher bits of the wedge, and what we're focused on is what's going on in terms of the runoff of the organic cash generation. And how is the new business replacing that. But probably one of the best ways to think about this is that our total kind of outgoings each year ordinary outgoings, so if you take the cost of dividend, the cost of debt interest, and the Group cost, so what the cash generation needs to meet, the Group costs, so all the ongoing Group costs, it is circa GBP750 million a year roughly.

So, if you think that the long-term new business cash in the first half of GBP358 million, obviously if we can keep it going at that rate, we're not far off the GBP750 million already. And then we also have the opportunity to outperform what we had assumed in terms of management actions, which last year was about one third of GBP0.2 billion of additional cash generation beyond that which we just assumed. So, we have that available to us as well. And therefore, we remain as confident as ever, but we -- even including ReAssure, we can do more than enough with our Open business to offset that the runoff of the Heritage business.

Rakesh, do you want to pick up the interest rates hedging question from Me?

A - Rakesh Thakrar {BIO 20549114 <GO>}

Thank you, Andy. So, just to that first question on interest rates hedging, so currently our hedging strategy is to hedge the there pretty much the surplus position. So, we look to focus and protect the surplus of our capital position rather than hedging the ratio itself. Clearly, interest rates are currently low.

And as you probably remember, we discussed partly this at the Capital Markets Day, where we actually changed our interest rate hedging strategy. So, we did move from having swaps when we -- when interest rates were falling during the latter part of 2019, and we switched that to using swaptions, and the benefit that gives is that if those swaptions were in the money, clearly interest rates continue to fall and reduce. We're effectively offsetting our economic costs and getting all that upside, all that benefit from interest rates falling. So, that's what we look to do and that's what we are doing, especially in this low environment, a lot of our swaptions are in the money protecting our Solvency II balance sheet.

Over to you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks, Rakesh. Operator, next question, please.

Operator

Thank you. And our next call is from Andrew Sinclair. Andrew, can you please unmute your device and ask your question?

Q - Analyst

Hi. Afternoon everyone; three for me as usual if that's okay. Andy, just wondered if you could first talk a little bit about Tom Ground's recruitment from Aviva and what that signals for their bulk annuity? So could we see their GBP100 million per annum starting to increase as long as the economics remain attractive? And just sticking on the annuities, just wondered if you could comment on what it would take for that capital strain, which is reduced to 8% to go more towards the sort of 4% we've seen elsewhere.

Secondly, was just on the L&G transaction. Just really wondered if you could give us an update on guidance for what you're expecting from that transaction in terms of cash and solvency.

And thirdly, I was just there've been some headlines in the industry press about some disagreements between yourselves and an SLA about some of the agreements that are taking place between the two firms. Just wondered if you could give us any color on that. Thanks.

A - Andy Briggs {BIO 4311809 <GO>}

Sure. Okay. I'll start off on the last one of those. I'll get Rakesh to talk about the L&G expectations. I'll talk about BPA, but I'll also get Susan McInnes to give a bit more color more broadly on SLA in a moment as well.

So, the position there is basically nothing to worry about, Andy. So, what we have a transitional services agreement in place as you do in all of these types of transaction, quite a complex involved transitional services agreement, and there are some areas, which is very common in this type of situation, where we're not quite fully aligned yet around costs and the services within that transitional services agreements. And very common, both parties working collaboratively to work it through, but obviously having issued a prospectus, we have to cover every single possible eventuality and putting in perspectives together as we did earlier this year. And hence, it was included in there. But it is very much the sort of short-term transitional services agreement that doesn't impact on the investment management side, the client service proposition agreement, where we work together or they're kind of shareholder in the Group. But I'll get Susan to comment at a moment -- in a moment just on a broader relationship in strategically with SLA.

In terms of the annuity side, so we will continue to take a selective and proportionate approach to BPA. So, what you saw in the first half is our capital strain got down to 8%. So, we spent about GBP90 million of capital writing GPB1.1 billion. And you would have seen in L&G's results yesterday, for example, that they quoted a new business strain of 4% on their annuity business.

So, what we're keen to do is to improve our capital efficiency. We've got quite a lot further to go. We've made some good progress already, but a lot further to go. Some of the capital were using goes further for us. And then we would consider of allocating a bit more than GBP100 million a year, not massively more, but we would consider allocating it a bit more. But very much taking a selective and proportionate approach.

And I mean specifically in terms of hiring Tom, we've got some fantastic people throughout the Phoenix Group, really impressed with the talent, the capability of people, but I'm also very ambitious about where we can go as a Group going forward. And so, we got strong capability in BPA already through Justin Grainger in the team we're adding to that with Tom. I mean, Tom ran the annuity next release business for me at Aviva. And I think when he joined, Aviva was doing about GBP600 million a year. Last year, I think it was more like GBP4 billion, but that was probably on even lower than a 4% strain in doing so.

But the key point to make is that we'll keep selective and proportionate on BPA business and we don't want total shareholder credit and annuities to be materially more than circa 10% of the balance sheet, because we keep that strong focus on cash generation and resilience alongside the growth.

So, Rakesh, do you want to comment on the L&G trend transaction? And then pass to Susan to comment more broadly on the SLA relationship?

A - Rakesh Thakrar {BIO 20549114 <GO>}

Thank you, Andy.

So, on the LNG transaction itself, so just generally on the process, so that is all progressing and that the court dates are set for later this month and subject to getting all the approvals we expect the effective date will be early September.

Now in terms of financials, I'll start with solvency. First I'll move on to cash. So, first on solvency, we are expecting that this will deliver a reduction in our SCR of about GBP0.1 billion, which broadly equates to about 2% on our shareholder ratio. So, in terms of cash, clearly, we've increased our guidance from the GBP690 million that ReAssure remitted to their Group company during the course of this first half.

And as a consequence, they only usually increase -- they only remit their cash once a year, and that's been the usual process going forwards. Now, we've increased our cash generation guidance for this year as a consequence of what's been already paid up. We will look later this year if anything is possible. We know we're not ruling it out, but certainly, if it's not going to be this year. It will be next year in terms of the cash generation.

So, now over to Susan.

A - Susan McInnes {BIO 19698729 <GO>}

Thanks, Rakesh. So -- hi, Andrew.

Let me just pick up the point about the relationship on the ground. So, Andy mentioned the client services and proposition agreement, which is the agreement that governs the relationship between ourselves at Phoenix and SME. And it manages the services that flow between the two organizations, and that is working very strongly on the ground.

The purpose of that relationship is in part to see how we maximize our offering for our customer base, and we're really pleased to see that we've had some good successes between us this year. We have managed to expand the Open products. Rakesh mentioned the Active Money Personal Pension or AMPP product, which has now been expanded to our Heritage base, and that allows those customers to benefit from drawdown retirement within the Phoenix family.

And secondly, we're working with this all on how we weave the SLA advice proposition into overall retirement proposition to make sure that all of our customers can benefit from information guidance and advice at the point of retirement. So, the relationship is working very well on the ground, and we're seeing more opportunities to jointly collaborate, which is strong.

Hope that answers your question, Andrew.

Q - Analyst

Very helpful. Thank you, all, and (inaudible) Andy.

A - Andy Briggs {BIO 4311809 <GO>}

My Scottish (inaudible). Sorry, Andrew, I realize that I didn't answer part of your questions. So, just adding to what Susan said there, our Open business net fund flows were up 50% in the first half. So, GBP1.2 billion against GBP0.8 billion in the prior year, which again is further evidence of how that's working well.

In terms of how we get the capital strain lower, basically two key drivers of that. But the first is the work we're already doing on this harmonized internal model. So, it's basically, historically Phoenix had been a particular player or focus on annuities and therefore the kind of annuity-related elements of our internal model comes of the risk diversification and credit elements of the model, what work, particularly the kind of latest versions of those. And as we work through this harmonized internal model, we will be upgrading and moving to much more modern ways of modeling and handling those aspects and that will be a key driver of improving the capital efficiency of the annuity business.

And then the other driver is the work we're doing around illiquid assets, and that's a key reason why as we combine with ReAssure, we've appointed Mike Eakins into the combine group CIO role across the Group as a whole. It really to increase our focus on the quality and scale of our illiquid asset origination. Again we've been making great progress in doing that; it's an area we want to do more in. So, those would be the two key drivers.

Operator, next question, please.

Operator

Thank you, Andy. There are no raised hands currently. (Operator Instructions). And I would like to hand back to Claire for typed questions in the meantime.

A - Claire Hawkins {BIO 20555563 <GO>}

Thank you very much. So, I actually have a question, which has come to me from Gordon Aitken at RBC. Gordon asks, you're now the clear leader in the back book consolidation. You were the number one and ReAssure, the number two. Where does your competition come from now? Is it an existing insurer? Or is it from that field? And a linked question, if it isn't or if there is an insurer at the moment, who writes bulks, what are the barriers to entry to stop them from taking on with profits and unit-linked businesses as well.

Andy, over to you.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks, Claire.

So, the -- I mean, let me just talk slightly more broadly on M&A first and now specifically about competition. So, our game plan here is to integrate the head offices of Phoenix and ReAssure by the end of this year. And therefore although we were obviously not about to announce a deal any day soon, but we are in a position now that if we were to announce the deal, it wouldn't complete until into next year, and because we would have integrated the ReAssure and Phoenix head offices together by the end of this year, we're basically a position, where we'd be able to do so if the deal was sufficiently attractive.

We need to leave it sort of set on the side in what I call the parking lot, because we've already got a full agenda or activity on the SLAL transition and the ReAssure integration and within ReAssure, the LNG, and the Old Mutual Wealth integration activity to go on as well. So, we'd have to leave it on the -- in the parking lot before we could bring it into kind of conveyor belt of what we're do around Integrations and transitions. But we'd have the capacity to do that, because we would have find the group head office. So, the answer is we are in a position, where we could do M&A.

Having said that, we're not spending morning, noon, and night pounding the streets looking for the next M&A deal. We've got a lot on the go already. We're in a very fortunate position. We've got so many highly value-creating initiatives that we -- are in our hands already that we can drive forward without relying on any external parties. And I think that's a good position to be in. But we could consider M&A and would do so if it was a particularly attractive deal, it remains a core central part of our strategy going forward.

In terms of where the competition is coming from, it's kind of probably not particularly helpful if I spent a lot of time speculating around that, but there is increased private equity interest in this space.

What I'd say there is that -- I think that the smaller sized deals than that -- I think that there's sort of credible competition in that space, but I think if you look at, our last two deals have been circa GBP3 billion each, it's harder to see private equity raising that sort of -- doing that sort of size and scale of deal. And I think also, you need to be mindful, if you look at the (inaudible) Part VII judgment, I think the strength and credibility of the counterparty is clearly very important as a FTSE 60 organization, I think, Phoenix, we're clearly a very strong counterparty to anyone that's looking to do anything.

I mean, I think in terms of BPA players, potentially moving into the space, I mean not impossible. But the whole exercise we go through when we do a big integration, and I'll maybe get Andy Moss to just comment a bit more on what we typically do as we do a big integration. But the harmonizing internal models, that the migration on to the new IT platforms and everything through the operating model, there's -- there's a lot there.

Andy, maybe give a bit of color of what's involved in successfully integrating the businesses.

A - Andy Moss {BIO 19123183 <GO>}

Yeah, thanks, Andy. Very happy to do that.

Yeah, I mean, I think we've talked before about the market that we tend to look at integrations probably in three phases, and they got an increasing complexity as we go through those phases. So, first of all, Phase 1, where we really are looking at the Group functions, looking to take out duplication of acquired companies, where we've taken on companies, and certainly that's the case in terms of our sort of Day 1 delivery of some of the ReAssure synergies, where we've been able to make Day 1 savings from an integration of the boards and integrations of our ExCo And then we move on to the functions like legal and an internal audit, which is largely a people-driven integration. Albeit, obviously rolling out the risk management framework is always going to be very key as part of that, so that's sort of Phase 1.

Phase 2 gets increasingly complex, because then we're really looking at sort of finance risk and investment systems. So, really there is an awful lot of heavy lifting to be done to move to one standard set systems to look at bringing in us onto a common internal model. And obviously, with style that's been incredibly complex given we bringing two big internal models together. So, there's an awful lot of heavy lifting as part of that work, but that tends to obviously then achieve a good amount of synergies in terms of bringing those functions together.

And then Phase 3, which is what we've been doing with SLAL and moved on to with the announcement of our extended partnership with TCS is really thinking about the whole customer service operation, and all of our IT system is around the support for that. So, again, that gets in terms of increasing complexity in the time that it takes to do that, where we're acquiring those sorts of operations, there's an awful lot of complexity and an awful lot of heavy lifting to be done around that. So, we tend to think it a bit in those three phases, and as I say each one gets an increasing complexity.

Back to you Andy, hopefully that helped.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks Andy. And probably one additional point, Gordon, I probably should have made is that, when you look at an M&A opportunity in the U.K., because of the scale of our existing business, we are far better placed to be able to drive the higher levels of cost and capital synergies than a new entrant into the space, where they wouldn't have the existing business, against which to get those costs and capital synergies. So, we ought to be able to generate more value, and that is the key focus for us. We have the three key criteria in M&A. It needs to be value accretive, it needs to support cash generation and our dividend sustainability in the longer term, and it needs to maintain our investment-grade credit rating.

Claire, other questions from the web?

Operator

Andy, sorry to cut you in. We have three more raised hands for you. So, can I start the first one? Oliver Steele for you. Oliver, can you please unmute and go ahead and ask your question?

Q - Analyst

Yes. Hi, Andy and Rakesh. Three questions; first is the sensitivity to downgrades is quite high, credit downgrade is quite high. And I don't really understand why it is quite so high, because you've only got whatever it is 16% of your portfolio in BBB. And as I said, your sensitivity appears higher than other companies', which have greater exposure.

The second question is on the solvency ratio. So, 150% pro forma solvency ratio and that's the first question. I pointed out you've got relatively high Fixed leverage debt within that. Are you happy at 150%, I mean your target range is 140% to 180%. If you do want to get back up towards, say, the middle of that target range, what's the glide path to getting there?

And then the third question is really just a sort of technical understanding issue, which is you've got GBP1.8 billion a central cash at the moment. Can the year end -- are we adding on the whole of the first half ReAssure contribution to that or what happens to that -- effectively by the year end, we'll be taking GBP1.5 billion plus the -- sorry, the GBP1.8 billion plus the GBP1.5 billion gross cash generation, less central costs and less debt -- less dividend.

A - Andy Briggs {BIO 4311809 <GO>}

Okay. Let me -- so, I'll do the math of the third one, and then I'll make a brief comment on the first two, but hand to Rakesh for those, Oliver, and good to catch up with you again.

So, the GBP1.8 billion includes the GBP433 million cash generation we had in first half. We then paid out GBP1.2 billion to Swiss Re just after the 30th of June as part of the acquisition of ReAssure, but then obviously -- since then, we've had the GBP700 million of cash. So, start GBP1.8 billion, take off GBP1.2 billion, add back the GBP690 million of ReAssure, and then any further cash generation in the second half of the year so that the balance up from the GBP1.1 billion pro forma in the first half, up to the GBP1.5 billion to GBP1.6 billion target will add on in the second half of the year obviously with any outgoing debt interest, the interim dividend, group costs coming off in the second half of the year.

Just on the first question, and again, I'll get Rakesh to comment in more detail in a second, but what you're seeing with our sensitivity is that, that's the impact of the downgrade. What I understand, I'm not particularly close to it. What I understand others do is their sensitivity will then assume that they sell that BB bond for example, and by a BBB with the proceeds. And hence, there's a management action that recovers back a lot of it. Now clearly, in practice, we could do that, our sensitivity doesn't allow for that. It just tells you what would happen if we got that downgrade without any management action to recover it. And obviously, it doesn't allow anything for us that the what we have been systematically doing in the first half of this year to sell out of BBB and moving, for example, U.S. single A.

But Rakesh, do you want to give a bit more color around that and around the Solvency II ratio by glide part?

A - Rakesh Thakrar {BIO 20549114 <GO>}

Yes, thank you, Andy.

So, let me start to with the credit downgrade. And as Andy said, I think one of the key points here is that we've allowed no management action in our credit downgrade sensitivity to recover that position, so it doesn't allow any, as Andy pointed out, any retrading of any sub investment grade debt coming back to investment grade or anything like that. And let me just briefly just mention this is a combined sensitivity so include both -- includes our enlarged group, so it's a Phoenix and ReAssure and an overall it's got a total BBB average of around 21% to 22% across the total.

Now what this sensitivity is trying to show is a combination of a full letter downgrade across a 20% of our portfolio, so taking a slice of our portfolio down 20% of it across all rating and then having it fall led to downgrade. So clearly, there is a effectively a cliff edge of those which are currently BBB.

And at the same time, it's moving the credit spread to the next letter. So, if there is a downgrade that goes from A to BBB, then you do also get the credit spread movement happening as well. So, it's a combination of those two plus the fact that we've got no management actions, which is why you're seeing the sensitivity of GBP0.5 billion. Now, in the context of GBP4.4 billion surplus, this is a reduction of GBP0.5 billion. So, given our size and the fact that we're actively managing that credit portfolio, I think we're pretty comfortable with that.

On the second point, Oliver, I think your question was around our solvency ratio and then our Fitch -- linked to our Fitch leverage. Now, I mean, I mentioned earlier about the actions that we currently have under way. And this is how I see that the glide path happening. So, clearly the L&G Part VII is on train, and that will improve both the surplus and the ratio. We've just started on our journey on the capital synergies with in ReAssure and clearly our target, we're only GBP120 million after that GBP400-odd million.

We're also looking to as you would have heard from my presentation in terms of the internal model harmonization, we've assumed no benefit of this, but the clearly, put simplistically what we currently have is a standard life internal model and a Phoenix internal model, and effectively added the two together and taken no diversification between them. So, that's got no credit for it currently in terms of our targets, but there is potential there.

There's also future Part VII, and then there's a list of management actions, which I also mentioned earlier, which will improve that position. So, we've got the ERM securitization. That is GBP600 million of it, which is currently sitting outside of the M&A fund, which will help improve our position and there's a number of other actions including additional credit trade, where we look to move again from the BBB portfolios that we currently have, and look for U.S. Dollar single A credit. So, there are a number of actions that we've already got planned and are underway to improve that position.

And so, back to you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks Rakesh. I mean probably just quickly add another quick two points, but first of all, because we have such resilient cash generation, and we have the hedging on the balance sheet, I think we take a lot of come from the reliability of that cash generation in terms of thinking about the leverage ratio.

Secondly, what I'd say, Oliver, is obviously where we're different most other organizations when you kind of do these comparators in that we have an active program of M&A. It's a core part of our strategy. And typically as we do deals, we would tend to move towards the higher end of our leverage ratio and move potentially down -- lower down the Solvency II capital ratio range, because these deals are so highly cash generative so quickly, and therefore it makes sense to kind of push towards the ends of those ranges, do all the actions that generate lots and lots of cash and improve capital efficiency and so on and so forth, and hence, that enables you to delever on the one hand and increase the solvency ratio on the other hand. So, it's kind of -- and because of the resilience and reliability of the cash generation as you can see today, up 51%, and increasing our target for the year as a whole, that's what gives us the confidence that to operate in that way.

Operator, next question, please.

Operator

Thank you, Andy. Our next caller is Ben Cohen. Ben, could you please unmute, go ahead and ask your question?

Q - Analyst

Hi guys. Thanks very much for taking my questions if you can hear me. The first thing I wanted to ask was you had to put some capital into the Irish business, and I just wonder the degree to which macro weakness and low interest rates might be changing your views to your long-term intentions towards the Irish and German businesses.

Second question was, what do you see in terms of the downside scenario or open book flows if the economy weakens materially from here, how much do you see that business being impacted? Thank you.

A - Andy Briggs {BIO 4311809 <GO>}

Okay. So, I'll kick off with the with our strategic view on the Irish business and I'll ask Rakesh to comment on the capital side, but first, I'll do with the kind of downside scenario in terms of the Open business.

So I mean, much as I said earlier, what we've tended to see in past recessions in terms of the kind of DC pension side and consumer behavior is the savings rate goes up and people engage more with their finances. And so, I think we would expect to see and we already have seen both minor in the scheme of things, but we have seen some of the regular monthly flows into our workplace pensions book, they have come off a little bit, where staff have been furloughed and their contributions go down to the minimum level and we probably would expect to see some more of that as if there is a spike in unemployments as the year progresses.

But in the scheme of the numbers, it's relatively small in terms of the moving parts. And as people have to engage more with their finances, the opportunity to get people to consolidate more assets together and start thinking about their journey to and through retirement, I think, represents a big opportunity. And obviously, we have more of those customers and more of those assets at the moment than anyone else, and therefore ought to be best placed to be the first place the customers to turn to.

I think if I look at it from the perspective of the BPA business, I mean I would be optimistic in terms of the outlook for BPA. Most commentators are talking about the market being GBP20 billion to GBP25 billion mid-year, which we would -- that will be consistent with our view, our perspective. As much as I said earlier in my prepared words, I think if you're a finance director of a manufacturing business, your desire to offload this is greater than ever. It spreads wider it becomes a bit more affordable. Generally for the company to offload the pension fund and lots and lots of pension funds have been on a journey of derisking over time. And therefore, are far closer to the point at which they can afford to do a buyout, so we would be optimistic about the outlook of the market there.

In terms of the European businesses and so, I'll get Rakesh to comment specifically on the kind of capital side, but from a strategic perspective, I mean Europe is a very small part of that total group. I think it is interesting strategic optionality, to think about potentially one day taking the core capability for M&A and integration that we have in the UK, and taking it into other markets. But having said that, I'd say, COVID will accelerate consolidation in the UK market and so most of our focus at this stage would be on M&A and in a UK context.

Rakesh, do you want to just comment on the capital position in terms of the European businesses?

A - Rakesh Thakrar {BIO 20549114 <GO>}

Thank you, Andy. And then there's -- it's a good question. So, on our Irish business, so as you're aware, it's -- we did the Part VII early last year in preparation for Brexit. A lot of the overseas business is sitting in that company, but it's significant proportion of it is then reinsured back into the UK to SLAL.

And this company, the Irish domicile company -- is on a standard formula basis. And as a result, given it's on a standard formula basis and the rest of the Group is on an internal model is that the Company does need to hold effectively counterparty risk. And with interest rates falling, that exposure albeit it's internal is meaning that it has to hold additional SCR, and therefore risk margin on this business. Now -- and this is as a consequence of a fact that interest rates continue to fall.

Now, we are working as part of our second phase of our internal model harmonization plan is to then bring the Irish company standard formula. If not all of it, at least certain risks into the our internal model, which will then allow us to better reflect the risks of that company and reduce that SCR requirement.

Back to you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks, Rakesh. And then, Operator, we have -- I think there's another hand raised, yeah?

Operator

Thank you. Yes, we have one more raised hand. It's Andrew Baker. Andrew, can you please unmute your device and go ahead and ask your question?

Q - Analyst

Hi. Thanks for taking my question. So, just one for me, it's on the ReAssure integration targets. So, I don't believe that these include any Phase 3 benefits from bringing together the customer and IT propositions. I think the original plan was to adjust these beginning in '22. But do you think you'll be in a position to communicate the size of these potential synergies prior to that date?

A - Andy Briggs {BIO 4311809 <GO>}

Okay. Thanks, Andrew, for the question. So I'll take that.

So, basically there are substantial benefits in these -- on the Standard Life transition in moving from the old Standard Life Legacy Mainframe platform across to the TCS BaNCS platform so that there's substantial benefits from doing that, not only related to the Heritage business within the and the Standard Life Insurance book, but also as I sort of touched on earlier, as we move our workplace pensions business crossing to that TCS BaNCS platform, we'll have a market-leading cost efficiency and a really strong digital customer interaction, and that's critical to winning in that workplace business. So, you got a real synergistic benefits of the strength of our Heritage business and relationships are crossing to the Open business and the workplace business.

So, that's our clarity, and that program has got about another couple of years to run. It's a big program of work that we're doing there progressing well, but a big program of work nonetheless. So, the earliest that we could kind of get to thinking about is their merits in combining together the ReAssure ALPHA platform and the TCS BaNCS platform would only be as we kind of got into 2022 so as you just mentioned.

But I have to say, from my perspective, the longest lead time in M&A much as Andy Moss said a moment ago, the toughest part of M&A is the customer operations and IT side. I mean ALPHA, we've got a very good strong platform. So, from my perspective, Plan A is that we can increase the pace at which we can do M&A by having two good platforms, ALPHA and TCS BaNCS, and that for me would be Plan A.

If Plan A doesn't come to pass, there aren't the -- will be disciplined on M&A's, it's core past the strategy, but we will be disciplined if the right opportunities don't come along at the right price. Then there would be significant additional synergies available to us by combining them one way or the other in terms of ALPHA and the TCS BaNCS platform, there'll be significant additional synergies there. Equally, we tend to focus here at Phoenix on under-promise and over-deliver. And therefore, that there's the potential that we could deliver more than GBP40 million per annum cost synergies, and the GBP450 million cattle synergies even without the customer operations in IT. And the first time we would consider updating on that would be with our March results in March '21.

Does that answer your question?

Q - Analyst

That's great. Thank you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Thank you. Operator, anymore hands raised before I go back to Claire?

Operator

It's clear. No more raised hands for you, Andy.

A - Andy Briggs {BIO 4311809 <GO>}

Okay. Claire, any other questions on the web?

A - Claire Hawkins {BIO 20555563 <GO>}

Thank you, Andy. Yes, we do. I'm going to ask you the final three questions from the website now. So, the first is are you presently looking at purchasing any other life and pensions consolidators?

The second is what is your take on super funds?

And the third question is, so you mentioned the possibility of increasing the dividend in time. When do you expect that might happen? Those are the four questions from the web cast.

Over to you Andy. Thank you.

A - Andy Briggs {BIO 4311809 <GO>}

Thanks, Claire. Sorry, you asked your questions much more quickly than the analysts. So, I think I've written them down, but tell me if I haven't.

So, are we looking at buying any other life and pensions consolidators? I mean -- I wouldn't comment on any specific deals anyway, but what I said a moment ago is that we could do M&A now core part of our strategy, it remains a core part of our strategy, but we're not pounding the streets desperately looking for the next deal, because we got a lot of a go already.

View on pension super funds? So, I mean if I'm honest, I'm probably quite concerned about this and the reason I'm concerned is that at the moment, at the customer who's a person we need to worry about and focus on most in all aspects of our businesses, in my view, the customer either has a covenant from an employer or they get a kind of a one in 200 year capital regime of an insurance company, if a big -- bulk purchase annuity is done. And so to have something in the middle that doesn't have either of those, I think it's really quite worrying from a customer perspective. And I know Andrew maybe and others have given their similar comments to that effect.

Having said that from the perspective of Phoenix and our participation in the BPA market, the way that the rules are being proposed or talked about around super funds, any company that was anywhere near being able to do a pop buyout wouldn't be able to go into a super fund, it would only really be targets in those schemes that were much less well-funded. So, I don't see it as a competitive threat to what we're doing in the BPA space at all. I don't change my view of the outlook of not purchasing the annuity market, but I am slightly concerned about it from a consumer perspective.

And then the final question in terms of dividend. I mean our dividend policy is unchanged. It remains that we have a stable and sustainable dividend. Our first focus with the dividend is the cash generation over the longer term that gives us confidence that we continue paying the dividend. What we covered earlier today was that if you just look at the cash generation from our existing business, there's enough there to cover the dividend for 20 years to 2040. And that's before you make any allowance for things like the GBP358 million of long-term new business cash that we generated in the first half of this year. Or any management actions above the level we've assumed up to 2023. There's no management actions from 2024 onwards in that analysis, no allowance for future M&A either. And hence, where we're very confident around our dividend position.

The way we will think about this in due course is just think about it in terms of the wedge. There's a level of organic underlying capital generation from the in-force business; it goes down a bit each year. We've historically said 5% to 7%. So, what we need to do is get to a place, where our new business is doing more than enough to offset that 5% to 7% runoff of the in-force business. And we kind of -- last year, overall, we kind of pretty much did it. This year, we've got the ReAssure business added on, but our new business is growing, but that will be the the trigger point at which we would be able to consider, and it will be my aspiration in time to be able to think about increasing the dividend without M&A. Obviously, M&A remains an important part of the strategy, but that would be my aspiration in due course.

But again just to reiterate as we do all of that, as we write our new business as we look at our business cash for resilience growth remains the financial framework. So, as we write new workplace scheme, we put the hedging in place to keep that was resilience and that overall financial framework remains as solid and secure through all of that.

So, any final questions either hands raised, or Claire, on the web?

Operator

Sorry, Andy; there are no raise hands at the moment.

A - Claire Hawkins {BIO 20555563 <GO>}

And no further questions on the webcast.

A - Andy Briggs {BIO 4311809 <GO>}

Okay. Well, thanks very much everyone for joining us. I'm particularly conscious that it's is a very busy day and a busy week for you all, so I appreciate you taking the time to join us today; and needless to say, if you have any follow-up questions at all, don't hesitate to contact Claire, and to myself of Rakesh, we're more than happy to pick up any follow-up questions you have.

Thanks so much indeed. Thank you.