Y 2019 Earnings Call

Company Participants

- Clare Bousfield, Chief Financial Officer, Board of Directors & Executive Committee
- John Foley, Chief Executive, Board of Directors & Executive Committee
- Spencer Horgan, Director of Investor Relations

Other Participants

- Analyst
- Andrew Baker
- Andrew Crean
- Andrew Sinclair
- Ashik Musaddi
- Greig Patterson
- Jon Hocking
- Marcus Barnard
- Oliver Steel

Presentation

Spencer Horgan {BIO 4241901 <GO>}

All right. Let's get going. Good morning, everybody. Welcome to our 2019 Results Presentation. Great to see so many of you here in the room. Welcome also to those on the webcast. Obviously, you all seen -- you all have seen our announcement this morning, so all we want to do is just have John and Clare go through some of the key messages from the results today. Then we'll have plenty of time say your questions and we will do that both in the room and for those of you watching on the webcast, you can also submit your questions over the internet.

So, without further ado, John if you're ready?

John Foley {BIO 4239156 <GO>}

Yes. Thank you, Spencer. So, good morning, everybody. Welcome to our -- [ph] the financial results as a newly independent company. I'd like to start by saying that this is a positive set of results against the backdrop of challenging markets in 2019, and markets that have become more challenging over the past few weeks as the world responds to COVID-19. Unlike others, we have restricted travel to business critical activities, so thank you to everybody in the room for joining. It's a much bigger turnout than we expected. Thank you.

And to say that 2019 was a busy year for us would be something of an understatement. I am very proud of what we achieved and I want to take this opportunity to thank once more my team for their dedication and commitment. I hope this morning provides you with a good overview of what we've done this year, as we continue to advance and execute our business strategy, delivered positive financial performance and strong capital generation and prepared ourselves to pursue future growth opportunities.

So here below the line on this slide are the milestones to our demerger and listing on the London Stock Exchange on October 21. Above the line are some of the operational and capability changes we made to our business over the year. You can see that we have continued to innovate in our business, while simultaneously executing and successful demerger and making progress on transformation.

In this slide is 2019 in key numbers. The value of our business mix and the quality of our diverse earnings comes through clearly. Assets under management and administration are up 9% over the year to GBP352 billion mainly on strong investment returns. Adjusted operating profits are over GBP1.1 billion very much in line with our expectations. Over the year, we generated capital of GBP1.5 billion helped by market levels as the impact of management actions is lower than in previous years.

Looking out over the next three years, we have assess ourselves to target of GBP2.2 billion for capital generation by the end of 2022, and recent falls in market levels make this more of a stretch. Nonetheless, I'm confident we can hit the GBP2.2 billion, and trust me, I am very focused on this. And from a capital perspective, we finished the year in a strong position with a shareholder -- solvency ratio of 176%.

Now, against the challenging backdrop for the industry, we had modest net outflows across our savings and asset management business of GBP1.3 billion. This represents less than 1% of assets under management and administration. Institutional asset management was flat over the year, returning to positive flows in the second half, almost entirely compensating for the slowdown in the first half.

In retail asset management, net outflows were GBP7.4 billion. These were largely offset by net inflows of GBP6.2 billion into our retail savings business, which includes PruFund. This proves the value of having a diversified business model and a balance sheet to support smooth investment returns, particularly at times of market volatility.

Now performance is key in any asset management business, encouragingly performance in our wholesale range of funds picked up in the second half of the year with 59% of products delivering above medium returns over three years. There's no doubt that parts of the active asset management industry are challenged at the moment. Partly because of the growing popularity of passives, but also to changes to the distribution landscape, but we're not sitting idle.

What I want to do in the rest of my presentation is to give you an idea of how we are tackling these challenges. Demand for active management is strong and rising, where it delivers a specific outcome for customers and clients. It's why we are focused on innovation in savings and investments solutions. Here profit margins are resilient and barriers to replication are high. To grow our business in active high value investment solutions, we are doing the following: we're building out our investment capability particularly in private assets, expanding our range of customer propositions and extending distribution both in the UK and internationally. We're overhauling our cost structure through transformation and creating an operational platform that is international and scalable, again, through transformation.

Through these actions we can continue to deliver attractive and sustainable total returns to shareholders, while retaining our capital strength. But how we implement our strategy is as important as the strategy itself. It's why in this slide, I wanted to remind you of our corporate values, of care and that is treating others with respect and taking time to understand; and integrity, always doing the right thing. And always doing the right thing for the customer is at the heart of our ESG strategy and I will cover that in a moment.

So, what progress have we made on delivering our strategy in 2019? Here is a reminder of our plans for customer and distribution. In short, how we are giving more clients in more markets, access to more of our investment capabilities; and two points I want to highlight here. First, we are in advanced talks with a number of European partners about the distribution of our PruFund like proposition to bring the benefits of smooth returns to a wider group of saver's. As we said back in September, we expect to see initial flows in the second half of the year. I cannot go into details about these discussions for reasons of confidentiality, but we will update you when we can.

Second, we continue to deepen our partnerships with institutional clients through more local support in our chosen markets. It's one of the reasons why during the year, we had more than 100 institutional mandate wins in the UK and Europe. All of this is in line with our strategy of making our full set of investment capabilities available to more customers and clients in more markets, in a wider range of formats.

An investment management in 2019, our priority has been to build out our international investment capabilities. In private assets, we are putting more resources into local asset origination in regions, which are important to our clients. It's helped us to commit just under $1 billion in new investments across the Asia and the U.S. in 2019.

On the public asset side, we're also investing in local capabilities including the higher [ph] last year of a team of fund managers and researchers, specializing in Asia-Pacific equities. Both initiatives increased our capability in areas where profit margins are resilient and where client demand is growing. Both underpinned our drive to investments solutions.

Now, some of you may recall that when I first took on the job as Chief Executive of Prudential's UK and Europe business, I did sell on condition of a sizable investment in operational transformation. Here we show how we have laid the foundations for the digital experience for our customers and improved systems for our colleagues, whilst restructuring our cost base. A milestone for the business in 2019 has been the migration of the most complex customer administration system in our -- [ph] Heritage business to the banks platform of Diligenta part of the Tata Consultancy Services Group.

This successful transfer of 450,000 life and pension policies demonstrates our ability to drive efficiencies through our operations, while improving customer outcomes at the same time. And transformation isn't just about modernizing old stuff, it's also about creating the right platform to scale our business safely and at pace. It's fundamental to our ambitions for a pru like -- PruFund like proposition across Europe.

I've already touched on the key numbers for 2019, and Clare will go into more detail in her presentation.

Still there are a few additional figures I want to mention. Thanks to our strong capital generation results, our own funds have grown, improving our solvency position to 176% and lowering our leverage ratio to 31%. On transformation, we remain on track to hit our target annual cost savings of GBP145 million by full year 2022. And when it comes to dividends, we are confirming a payout the GBP310 million that's 11.92 pence per share to be paid in May. And there will be a one-off the merger related dividend of GBP100 million or 3.85 pence per share.

Now what I've covered -- now that I've covered the numbers. I want to go back to our values of care and integrity. That I mentioned earlier, that underpin our all of our activity including our approach to ESG. For more than 170 years, we have been responsible stewards of our customers' savings. First as Prudential Assurance company and second, since 1931, as M&G Investments. Throughout that time, the challenges remain the same, to balance saver's requirements for long-term strong financial returns against the wider needs of society and the economy.

Today, impact on the environment is an increasingly important factor in how we deploy our customers' capital. As a major financial institution we have a part to play in finding a solution to climate risk. That's why as a newly independent company, we are embedding ESG considerations across our entire business. Both as a good corporate citizen and as an international asset manager,

On the left hand side, you can see the -- our ESG commitments as an asset manager. As ever our approach is to priority -- prioritize engagement over exclusion. However, we will consider this investment from companies who failed to engage. When it comes to climate risk our ambition on carbon is for our book of assets under management to be net-zero by 2050.

In terms of new propositions, we will expand our current range of impact strategies, actively seeking out companies which want to fix our planet one investment at a time. As an international business in 22 locations we want to be carbon net-zero by 2030. We also want to be a more inclusive and diverse employer and have set clear targets for better representation among the leadership on gender and ethnic background by 2025.

Now, before I hand over to Clare, I want to end by setting out our business priorities for 2020. Now pretty much all of them, our continuation of our work last year, improvement in the customer experience, extension of distribution in the UK and internationally build out of the investment capability, reaping the benefits of transformation and sound capital management.

Now, I'll hand you over to Clare, who will take you through the financials in more detail.

Clare Bousfield {BIO 16746072 <GO>}

Thank you, John, and good morning, everyone. Our results demonstrate the strength and resilience of our business and are in line with the expectations that we shared with you last September. The environment has been challenging, especially across the asset management industry. Being an asset manager and an asset owner enables us to produce good earnings even in tough market conditions. I'm going to draw out some of the key points on the underlying numbers before John sums up and we will then take your questions.

Our overall assets under management are 9% higher than last year-end, mainly driven by the performance of the market. On flows overall, we've shown our resilience. While the picture on retail asset management has remained challenging, our institutional business showed a positive trend in the second half and PruFund has continued to produce strong positive flows. Taking each intern, retail asset management remained in net outflow at GBP7.4 billion, primarily impacted by weak consumer confidence.

As we've previously acknowledged, we're very proud of our overall investment performance, which has been strong particularly over the medium-term. However, there are a few funds, where performance is weaker than we would have liked, particularly in the value orientated strategies. We are addressing areas of weak performance through independent deep-dive exercises supplementing the analysis done by the fund managers.

As John has commented before our role as management is to actively manage the active managers. Despite these headwinds our retail assets under management closed the year just slightly lower at GBP75 billion. Institutional asset management showed broadly neutral net flows for the full-year and a positive GBP700 million for the second half.

Over the course of the year, our institutional assets under management grew by 9%, GBP77 billion. PruFund remained a highly popular proposition in the UK market despite some pressure caused by the falling DB to DC transfers across the industry. Net flows into the PruFund amounted to 15% of the opening net asset. This included sales from the smooth element of our new PruFolio range, which allows customers to combine the PruFund proposition together with active and passive mutual funds, leveraging both our asset allocation and stock selection capabilities. These flows combined with another year of strong investment performance drove PruFund asset up 25% to almost GBP54 billion.

Lastly as you're aware, the -- the High Court has denied our request to transfer the annuity policies we reinsured in early 2019 to Rothesay Life. It's a new experience for all of us, because such a process has never been done before and respect to the Part VII transfer. We expect a hearing on our appeal in the second half of 2020. Because of the uncertainty on both timing and outcome, we're required to bring the GBP11 billion back into assets under management, previously it was reported as health sale and therefore excluded from our assets under management. Growth in the assets under management before this effect was 6%.

I'm now going to move on to adjusted operating profit, which was over GBP1.1 billion for 2019. In 2018, we released GBP441 million on longevity and had GBP166 million insurance recovery in respect to TRASP. In 2019, we've released GBP126 million from longevity and we'll find GBP24 million by the FCA on TRASP. When comparing 2019 to 2018 these impacts all from the heritage book were the most material on the adjusted operating profit.

Our savings and asset management business delivered a slightly higher result of GBP474 million for 2019. Asset management was lower with profits was stable and the other result improved from a loss of GBP59 million last year to a profit of GBP38 million this year. This was due to a one-off negative of 56 million in 2018 related to our international insurance operations with the remainder of the improvement explained by higher investment returns. Corporate Centre expensive increased as expected due firstly to the interest costs on the debt, which we inherited from Pru plc in October; and secondly to the build-out of our capabilities to become an independently listed entity.

I'm now going to cover the key profit drivers starting with asset management. Whilst overall assets under management were higher at year-end 2019 compared to 2018, it's the average level for the assets under management across the period, which is most relevant for the revenue. This was 4% lower because the drop in markets in 2018 only occurred towards the year end. This together with the moderate degree of ongoing margin pressure in the retail book resulted in 7% lower fee revenue. Cost was slightly higher year-on-year by GBP12 million or just under 2%. GBP3 million related to the increased FSCS fees.

In both years, we also had positive one-offs. In 2018, approximately GBP18 million from accrual leases and in 2019 around GBP30 million from changes to the staff pension schemes and other items. Importantly, we've been changing the nature of the costs with lowering the back office cost in favor of building investment management capabilities for future growth. You've heard John mentioned some of the initiatives that we've started. Asset net result, primarily at the lower fee income, the cost income ratio increased by 4 percentage points year-on-year to 63%. A number which continues to compare favorably to our peers.

The savings business has continued to perform well, driven by PruFund. PruFund showed strong growth sales again in 2019 of GBP10.2 billion, although below the prior year level of GBP12 billion. As I mentioned earlier, we expect DB transfers to reduce given the limited number of advisers who have the experience and permissions to write this business and potential changes in advisor charges proposed by the FCA. These transfers accounted for less than one-fifth of our PruFund sales in 2019. Growth outflows have also increased as expected as the book matures. This is important because we only recognize the cash transfers and the profits to shareholders when customers take their money out. Shareholder transfers grew by 9%, broadly in line with the level of withdrawals. In terms of adjusted operating profit, these increased transfers were offset by a lower hedge result, which I'll explain shortly.

So the traditional with-profits book, I commented back in September that even though the book is closed to new customers, we expect shareholder transfers to remain broadly stable for the next few years, assuming normal market conditions. And that's exactly what we've seen in 2019, are just over GBP250 million. As with PruFund, the hedge result is more negative than last year driven by the increase in equity markets. In our July presentation last year, I explain the cash flow hedging of shareholder transfers which we've been doing across the traditional and PruFund books.

What you're seeing in the operating result is the gain or loss on the hedging; we put in place for the shareholder transfer in 2019. The more negative result reflects the strength of equity market, since the hedges were initiated. We have included some further detail in the appendix to give you a better feel for how the numbers will move in the coming years as these hedges mature based off different equity market scenarios.

At the end of 2019 rather than putting in a new tranche of these cash flow hedges, we switched to a structure focused on the protection of dividends up from the life company in the event of a market shock [ph]. Since it's not a hedge of the IFRS earnings, but on solvency II, the impact of this new hedge will be excluded from operating profit.

This slide shows our shareholder annuity and other businesses. Results remain strong. As expected, the particularly large positive effects from longevity in TRASP last year did not repeat. The return on excess assets fell mainly as a result of lower releases from our credit default reserves and lower investment income. As we highlighted in September, part of this was related to us returning a significant amount of capital out of the insurance entity up to the parent ahead of demerger; and so some of that investment income has just simply shifted up the group structure.

Longevity of GBP126 million reflects the adoption of CMI17, which we executed in the first half of the year. In 2020, we will be reverting to our usual practice of reviewing the assumptions at the year-end and of course, it's too soon to give any guidance on what that might look like. In the TRASP line, we had GBP166 million recovery from our insurers last year. The small loss you see this year is in relation to the FCA fine that was announced in September.

Finally, other items contributed GBP137 million from close to zero last year. The main contributors are mismatched gains of GBP55 million and a one-off benefit of GBP29 million from changes to the staff pension schemes and some other minor items.

I'm now going to move on to capital generation, we had a very strong year. Total capital generation from continuing businesses came to GBP1.5 billion, including GBP538 million of positive impacts from the market. And it also did not include a full-year of interest and head office costs, which we will of course have going forwards. After pre-demerger dividends and related adjustments the overall increase in our surplus capital was GBP0.5 billion.

Pre-tax operating capital generation was GBP1.3 billion of which just over GBP800 million was underlying capital generation. The remainder of operating capital generation is less recurring in nature. The decline of GBP79 million in the underlying capital generation is primarily due to the corporate centre, where we started to incur debt interest and head office expenses and the latter part of the year around the demerger.

We have enhanced the methodology for allocating capital generation between the PruFund and the traditional with profits business to be based on underlying asset shares, which is resulted in a higher PruFund number, with a corresponding reduction in the traditional with-profits within Heritage. The other operating capital generation incorporates a number of elements. Asset trading and hedging contributed GBP251 million including GBP80 million from the new with-profit hedge program.

As reported in the first half results, the impact of longevity was just over GBP100 million, a number of other smaller items including for example experience variances and other operating assumption changes generated GBP95 million. The decline from the prior year was mainly driven by the TRASP insurance recovery. The capital generated resulted in an increased solvency ratio of 176% before dividends, up from the pro-forma of 170% last year end. The Solvency II debt leverage ratio fell from a pro-forma 34% at the first half as we disclosed in September to 31% driven by the gross in own funds. We estimate that the negative market movements up until last Friday have had a negative impact of around 10 points, since the beginning of the year, in line with the sensitivities that we've published.

The with-profit fund is an enormously important part of the group, something no one else can replicate. And we continue to explore ways in which we can leverage it as part of our ongoing development of our broader proposition and drive our long-term returns to our customers and investors.

Capitalization of the fund has continued to strengthen the solvency ratio of 267% up from 231% last year. It's also becoming increasingly resilient. The older style guaranteed products are running off and being replaced by PruFund customers, the vast majority of who select the non-guaranteed option. As a result, the sensitivity to equity markets is very low. If equity markets were to drop by 20%, the fund solvency position would reduce by around 1 percentage point.

This strength in resilience is why, as we announced last month, we will be making a distribution of excess surplus to policyholders of GBP1 billion. And being a 90-10 [ph] fund shareholders will receive one-ninth of this amount from the fund. Coming through to earnings when the customer takes their returns of cash, we expect this effect to be of the order of GBP10 million per annum over the next few years. The impact on the shareholders solvency position is negligible, since the positive economic impact is offset by the TMTP.

Finally, on the balance sheet. The parent company's initial liquidity position. This slide show the most significant transactions which founded the parent company's liquidity position including those related to the demerger. First of all, we had payments up from our subsidiaries of GBP1.7 million -- GBP1.7 billion, including GBP1.2 billion exceptional return of capital up from the insurance business as I reference, when talking about the Heritage result. The next two transactions are the debt for equity swap from Prudential Plc. We've received GBP3.2 billion in consideration for the debt we inherited and then paid a demerger dividend of GBP3 billion. Finally, you'll see the normal dividends we paid to Prudential Plc last year and some minor other movements including head office and interest costs.

So we ended the year with a cash and liquid asset balance of GBP1.3 billion, well ahead of the minimum we aim to hold according to our financial management framework, which is to cover one year's expected out go.

And I want to build on the update John gave on transformation, where we've completed the second year of our five year program. We're making good progress, having implemented key outsourcing arrangements, commenced legacy system migration work and upgraded customer facing platforms. These are just some of the initiatives all of which are improving customer outcomes, our control environment and the efficiency of our business. These -- the efficiencies, we are delivering are not short-term tactical cost savings. They are driven by fundamental deep rooted changes to the way that we run the business.

We remain on track to deliver around GBP145 million of shareholder cost savings by 2022. We are slightly behind where we wanted to be on timings because in 2019, we took the active decision to prioritize demerger activity in some areas. Finance is a good example of that, but we know what needs to be done to reach the target and we remain committed to our 2022 timetable.

Our priorities from here will include further decommissioning of legacy IT infrastructure increasing the scalability of our operations in our growth areas and driving out cost. With much of the groundwork done the level of resources we need, will inevitably decline. That's why we're announcing today a voluntary redundancy programme, which aims to reduce headcount related costs by around 10% this year. This runs across all areas of the business and on all levels of seniority.

In terms of 2020, its early days and there's obviously uncertainties, but you'll see here some indications of what we expect. The headlines are for savings and asset management will be fully focused on delivering our medium-term gross initiatives. We remain positive on the outlook for institutional business and we're working to improve flows in retail asset management, recognizing the need to refocus on focus on the UK, which has been under invested in historically.

We have a number of initiatives including developing our investment solutions expertise, continuing to expand our sub-advisory capability and capitalizing on our strong and broad propositions. We expect PruFund will continue to be a highly appealing proposition in the UK market. And we started to see strong traction for PruFolio. There is further uncertainty on DB to DC transfers given the FCAs review of contingent charging.

In Europe, we are on track to realize the ambition of exporting PruFund. The duration of the current COVID-19 outbreak and the associated market volatility will obviously be a factor in terms of how it flows develops across the group, especially in retail asset management. We expect fee margins in the institutional business to remain resilient, but for some fee pressure to remain in the retail asset management. This is why it's absolutely imperative that we are sharply focused on costs in 2020.

Shareholder transfers from the with-profits business should continue to grow as the book matures. In Heritage, we expect broadly similar transfers from the With-Profits book. For shareholder annuities and other, we will see some compression on the return on the excess assets following the dividends up in 2019, although there will be an offset in the Corporate Centre, which will now earn interest on that money.

This year, we will return to our normal practice of reviewing longevity assumptions at the end of the year. For Corporate Centre, we continue to expect 80 million to 100 million of overheads, mitigated by the interest earned on the liquidity now at the parent company. Coupons on the debt will be around GBP190 million, as previously guided. We will also have an accounting effect of the amortization of the fair value premium under IFRS, which will net off against this.

To wrap up all of the management team are highly energized post-demerger. We've continued to deliver on improvements in customer outcomes, reducing operational risk and creating an efficient and scalable business. We're absolutely focused on cost and ensuring that we deliver the transformation on time. Financially, 2020 will also be an important year because the clock starts on our 3-year target of GBP2.2 billion of capital generation by 2022.

Our 2019 numbers demonstrated once again the potential of the business and where -- and we remain focused on the necessarily growth initiatives and the balance sheet optimization measures to meet our goal. In short, we're aiming to deliver to our investors' good long-term growth prospects with a healthy dividend yield.

Thank you, and I'll pass back to John for some closing remarks. And then we'll be ready to take your questions.

John Foley {BIO 4239156 <GO>}

Okay. Thank you, Clare. So I just wanted to end by reminding you of the growth opportunity we see in markets and why M&G is well placed for that opportunity.

Savings gap to continue to open up across the developed world, a society's age and states restrict to retirement provision. In the UK alone the savings gap is currently estimated at $1 trillion by the World Economic Forum and it's growing. Face with longer lives and negative real returns on cash, people want the financial partner who can deliver reliable savings and investments solutions. M&G is well placed to become the partner of choice. We have the right mix of investment capabilities, a unique offering with profits and the client insights of an asset owner.

Our plan is to grow our offering in solutions at pace, leveraging our client relationships in 28 markets, and our two well respected brands. Now, with independence, we also have an energized leadership team determined to grow this business and that growth coupled with sound capital management will drive attractive and sustainable total returns for shareholders.

Thanks again to all of you for making the time to be with us today at our first set of annual results. We'll now, I think ready to take your questions. We have the leadership team in the front row, if the -- questions get a bit too tricky and you can spot them because they're all wearing the uniform. I didn't know we had a uniform.

Spencer Horgan {BIO 4241901 <GO>}

Great. Thank you, John. Thank you, Clare. So we will take questions both in the room and if we get some over the webcast -- over webcast as well. So use your rules, please if you want to ask a question, raise your hand as you already have. Two at a time, please, if we could. And don't forget the microphones -- sorry -- three questions. Yes. Microphones are in the -- in front of you -- I sound like an airline stewardess, don't I. But if you press the button on the microphone to switch it on. And we'll start with Andy.

Questions And Answers

A - Spencer Horgan {BIO 4241901 <GO>}

(Question And Answer)

Q - Andrew Sinclair {BIO 4672001 <GO>}

Thanks. It's Andy Sinclair from Bank of America Securities. Two for me, I guess, if that's okay. So firstly, just on the HoldCo cash figure, the GBP1.3 billion. It looks to me about twice what you've guided for what you need at the HoldCo You've ruled out buying back debts, special capital return and M&A. Does that mean we should feel that more bullish on the regular dividend or is there something else we're messing on that cash? First question.

And secondly, just on institutional asset management, you've talked about quite a lot of mandate wins in 2019. Just wondered if you could tell us a bit of color on paper fighting for mandates that have been won but not yet funded and what that means for 2020? Thanks.

A - Clare Bousfield {BIO 16746072 <GO>}

So on the first question. The level of HoldCo cash, yes, is a bit higher than we'd originally guided in terms of numbers. But overall, we're pretty comfortable in terms of that being sufficient buffer in order to manage the business. So, from a dividend perspective, I think we've guided in terms of where we believe the future is. You've got to recognize as well that the markets right now are certainly pummeling in terms of interest rates and the overall capital position. So we're comfortable with the strength and the resilience, both in terms of the level of capital and the liquidity. But obviously, we need to have that strength in terms of just just being able to survive some of the market conditions.

A - John Foley {BIO 4239156 <GO>}

And on the institutional business. The last time I looked at the pipeline is around GBP4 billion, not surprising we've put a number of people in various locations around the world actually to start to source assets. I mean, it's getting trickier in private assets, so we have people on the ground in Asia and in the U.S. now, as of yesterday. It's actually source assets for that those propositions. So, it's a big business for us and it's one that we're working hard to keep the momentum going behind it.

Q - Andrew Sinclair {BIO 4672001 <GO>}

Sorry, just to be clear, GBP4 billion of mandates that were one in 2019 all were funded?

A - John Foley {BIO 4239156 <GO>}

That the pipeline is GBP4 billion and the actual we've laid 100 mandate wins in 2019. And the pipeline is -- it's about GBP4 billion. I haven't got the exact number.

Q - Andrew Sinclair {BIO 4672001 <GO>}

Sure. And case a for those 100 there were one in 2019? Are some of them effectively still to receive the funds in 2020 or is that all received in 2019?

A - Spencer Horgan {BIO 4241901 <GO>}

Ashik?

A - John Foley {BIO 4239156 <GO>}

They will -- some of them will be funded in 2020, yeah.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes. Thank you. This is Ashik Musaddi from JP Morgan. Just a couple of questions. First of all first of all on your cash flows, I mean, you have a GBP2.2 billion cash flow guidance, but any visibility you have for this year 2020? Now, the reason I'm asking is, given that we are already 2.5 months in, you would have reasonable plans about longevity, say, the tables which you said you will review in the later this year, but you would have plans about asset rerisking in case you're considering longevity reinsurance. You would have visible plans around that given the close life nature of the annuities book. So any thoughts on that as to how we should think about cash flow's one-off nature specially for this year?

The second on asset management cost. I mean, revenues is it is what it is, but in terms of cost you put an extra emphasis that that is definitely a focus, especially in these markets. Are you managing that on a basis point way or are you managing on an absolute cost basis, like GBP642 million? Is that GBP642 million going up, going down, how should we think about that? Especially given where markets are. Thank you. Or how much flexibility you have on that GBP642 million? Thank you.

A - Clare Bousfield {BIO 16746072 <GO>}

Okay. So on the cash flow and the GBP2.2 billion, we obviously -- we're looking to manage that over a 3-year period. It's an all inclusive number. And we recognized during that three-year period that markets will move up and down during that period. So right now you would say there's -- we've already got quite a challenge in terms of where current markets are.

Yes, we have got a line of sight in terms of actually looking at our longevity in terms of the basic assumptions. CMI18 is what we'll be looking at in 2020, but we'll obviously have line of sight also to the 29 CMI table as well in terms of that. It's a calibrated table so it does depend a lot on your underlying experience in terms of where you're at. And then the other elements that we are also looking at as we put some equity hedging on, as I mentioned in the speech during 2019, and we also put some further interest rate hedging on in terms of what we're doing.

Right now the market side of it is where our focus is. What we want to make sure is, with any of that -- with the target that we've got that we're managing this business for the long-term and that we're not making short-term decisions just to drive capital in the short-term. Asset training will continue, that's been something that we've done consistently. And you can see from the numbers that we've shown in terms of the amount of asset trading, that does depend on the market conditions. But right now, we would expect to make something similar. But obviously, if there are market opportunities, we'll take -- we'll take advantage of it. So absolutely, we have ongoing plans but it's about how do you manage it over the long-term rather than necessarily just purely focused on the short-term.

In terms of asset management costs. So, as I talked about the transformation program, is about -- fundamentally about customer outcomes, it's about the control environment, but it's also about the efficiency of the business. And the efficiency of the business is also about how do you structure those costs. So, which costs are variable, which ones are fixed, how do you use technology and automation in order to improve what we're doing. And clearly with some of the ambitions that we have around growth particularly on some of the asset management and private asset capability, what we're working through at the moment is how do we build that scalable growth? And that is our focus as opposed to purely the cost-to-income ratio or any absolute level of cost level.

Because again, that's a -- the retail asset management business, particularly in the mutual funds, is cyclical by nature. So what do you want to make sure of as you've got a cost base that is that is actually sustainable and efficient in the future. So that's where the focus is. In terms of that cost-to-income ratio and where we would expect it to go in 2020, obviously, over the long-term we're expecting it to come down. But what we want to make sure of is, during 2020 we're investing in the right things in order to get to that cost base to where we want it to be.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Thank you.

A - Spencer Horgan {BIO 4241901 <GO>}

Oliver?

Q - Oliver Steel {BIO 6068696 <GO>}

Oliver Steel, Dutch Bank. In your presentations, previously you've talked about business growth and investment expenditure. And I think that was sort of up to GBP200 million by 2022 or 2023 against the GBP145 million that you were saving on the transformation program. How much of that -- how much the costs in 2019 include that business growth and investment expenditure? And I don't think you've ever really talked about the sort of returns that you expect on effect on that and when you expect those returns to come through, so perhaps you can give a bit more detail on that today?

And then the second question, if it's not too long. It's back to Ashik's question about the capital generation guidance. Frankly, I can't see why you're totally -- while you're targeting a total capital generation figure. Because it's clearly being moved by markets. But implicitly you've lost GBP600 million of the solvency so far this year. So are you saying that the GBP2.2 billion can be made up? That you can make up that GBP600 million organically or through exceptionals over the course of the next 3-years?

A - Clare Bousfield {BIO 16746072 <GO>}

So going to the first question, Oliver, on the growth in terms of, yes, what we did included. So obviously, for -- there are certain elements of our business where the growth actually requires us to have more people in order to be able to deliver it. So if you think about private assets as a good example, you can't use technology and automation to get you that growth. So that's what was included in that GBP200 million. And remember, it's over a 5-year period, so effectively it's the ongoing cost to be able to support that growth.

And as I said, the -- we have invested during 2019 in the front office in the business in terms of the growth, particularly on the institutional business in terms of actually building private asset capability, whether it's putting people in Asia or in the U.S. in terms of building that out. And we'll continue to do that in terms of the approach. The numbers in that chart were all built off where we see the future in terms of the revenue, so what we were basically assuming is that there is an element of incremental cost that aligns with the revenue. And clearly some of the pressures that we're currently facing from a retail asset management perspective we're very conscious around balancing the cost initiatives versus it has being prepared for the growth in terms of the future.

In terms of capital generation, the total -- we always set the target to be total, because basically we wanted to be totally aligned with our shareholders. And over a 3-year period the expectation is that market should -- you should be able to even out some of that volatility. And if you think about it, we basically made GBP500 -- just over GBP500 million of positive market returns at the end of 2019. And as you say, the beginning of this year has pretty much reversed that position. So there's an example of where you would expect for it to be over the period. It just didn't feel right as to basically have a 3-year target that wasn't based off the total returns, so that's how we look at it.

And just going back to the first question and terms of how do we assess returns on the business? So we look at it very much on a cash generation basis, and we look at it using IRRs to effectively say its a very simple approach in terms in terms of how we decide where are we going to spend our money and what are the things that we want to grow the business from.

A - Spencer Horgan {BIO 4241901 <GO>}

Joel?

Q - Analyst

Well, it's Joel (inaudible). I've got two questions, please. On the capital front, your solvency ratio is optically low, but obviously the profit fund is very strong. Just wondering how much you think of this is actually really economic and how much of it is just the risk margin, giving it a low optical number? And in the statement this morning, John, make the comment that it's within your risk appetite. What levers do you have to pull to get the ratio back up, if it becomes an issue? So can I accept there's not really an economic issue, but it's headline is -- you're screening very low versus rest of the industry?

And then secondly, some of your peers go to some sort of early trending indications, some post election terms of flows et cetera. I guess you've got a bit of an each way bet on in terms of having improve on that works well enough in a risk off environment and the rest of business which is recovered. Can you talk a little bit about what the early experience was in January and February in terms of the retail flows? Thank you.

A - Clare Bousfield {BIO 16746072 <GO>}

So, on the solvency ratio, Joel, on the -- so we're -- we basically match the annuity liabilities and the assets on a Solvency II basis. So if you look at, for example, interest rates in terms of the impact of it, we don't get much impact in terms of just what's happening with assets and liabilities. That obviously creates a little bit of a mismatch on the IFRS, which you saw come through the results in terms of where you're at.

The place where we get the interest rate impact is basically from the capital. So this -- the SCR is where -- because effectively you're getting that. We put some hedging in place in the middle of August to effectively dampen some of that. But that is a non-economic hedge in terms of actually -- in terms of that exposure. So -- but that's -- that is one of the key areas that's causes the volatility in the solvency ratio.

We're pretty happy with the resilience, so if you look at the sensitivities, we're pretty resilient in terms of these markets and we're comfortable where we sit right now. We're above risk appetite in terms of -- but clearly, some of the tools that we can leverage is effectively putting some more hedging on around that interest rate. We also use -- we also put additional hedging around the equity side of it. We're all, obviously, looking for asset optimization in terms of risk and reward and using the private asset capability that we have across the business.

Reinsurance and longevity is also options that we have. Although from that perspective you've always got to think about the value that you give up versus the risks that you're actually mitigating, particularly where you see upside and the longevity in the longer term. But yes, we have a lot of levers that we can pull in terms of actually from a solvency perspective. But each one of them needs to be weighed up against what benefit you're actually getting.

In terms of flows. So it's interesting, I guess, from a flow perspective, because the election happened in December, even had Christmas. And then basically we pretty much got hit with the coronavirus, kind of slipped the sentiment in the markets in the early part of January. So it has been pretty difficult to actually see where -- any kind of movement in it. January is always a relatively slow months on the retail savings side of things, but with market volatility we're starting to see some advisers actually wanting to come into the product in a heavier way than they previously been in. Which shows that customers are thinking about, right, given these volatile markets this is a great proposition.

So is -- it's an interesting proposition, particularly the guaranteed option, but also the non-guaranteed option in terms of getting customers more certainty in terms of outcomes. Because it effectively takes out the kind of top slices of the volatility in the markets. And that's what we've actually -- that's exactly what we've seen over the last couple of weeks is, the fund has performed very well. So it's takes -- but it is it's early -- is still early days. And because of the amount of uncertainty in the markets it's really quite difficult to call right now.

A - John Foley {BIO 4239156 <GO>}

But you're right in terms of PruFund and the mutual fund business and institutional business. I mean, you will continue to see solutions business being attractive, both from us and from a client perspective, because it's outcome orientated. PruFund, both in terms of the down market and up market, it's still a very strong proposition. And then mutual funds is a volatile business, that accounts for about 20% of our book today. And whilst we -- that's a very important part of what we do and we -- as Clare said in her presentation, we are going to some lengths to actually make sure that we start to deliver consistently the right returns for the clients on those funds. The actual jump that we've got on the market is around the PruFund proposition and the passives and the institutional flows, there's no question of that. And that's what makes us fee we're quite resilient to these choppy markets.

Q - Jon Hocking {BIO 2163183 <GO>}

I'm going to take Greg in the room for next question, and I'll take a couple on the internet. And then we'll come back in the room.

A - Spencer Horgan {BIO 4241901 <GO>}

Greig?

Q - Greig Patterson

Hi. Greig Paterson, KBW. Two questions, one is, could you just -- on the GBP26 billion annuity fund, that's not their office part. Can you just give me the percentage of that to the reinsured while longevity swaps at this point? And the second thing is, in terms of this with profit hedging program you made a comment in the presentation that you renewed it. Is my understanding correct that the old program remains unchanged to run-off in the operating profit and the new program comes in below line? And if that's the case, does that mean we can expect more volatile IFRS operating profits going forward in aggregate?

A - Clare Bousfield {BIO 16746072 <GO>}

So the simple answer to your second question is, yes. What we've done is the old program effectively hedged kind of the 5-year -- the transfer 5-years ahead, and that will run-off over the next 5-years. The new program effectively focuses on the capital, the Solvency II capital generation, rather than the absolute Solvency II ratio. And that will potentially create a bit more volatility in the underlying IFRS numbers. But I wouldn't expect it to be significant, Greg. On the annuity fund, we'll have to get you the exact number. It's around 40% to 50% in terms of how much is reinsured.

Q - Greig Patterson

(Inaudible)

A - Clare Bousfield {BIO 16746072 <GO>}

Well, you could clearly increase it, even right up to a 100%. But this is a risk reward in terms of how much of that kind of future value do you want to give away.

Q - Greig Patterson

So on the internet, we have one question which is -- there's a potential gap between the cash flow generation target and the dividend commitment. So, what are the management priorities for the use of that surplus capital? And related to that question, how the share buybacks fit into the capital framework given the current share price?

A - Clare Bousfield {BIO 16746072 <GO>}

So I guess, in terms of the gap that -- because of the total capital generation its basically covering the full impact, including all the market movements. Then what we have done is built in an element of recognition that gap needs to be there in order to be able to support the company and the resilience of the balance sheet. So, right now if we have excess capital then what we will do is we will look to return it to shareholders, we've got no interest in return --in basically retaining excess capital for the business. But certainly, for volatile market conditions that we're in at the moment, absolutely it's the right thing to do to have a resilient balance sheet.

A - Spencer Horgan {BIO 4241901 <GO>}

Andrew?

Q - Andrew Baker {BIO 3694545 <GO>}

Sorry. Hi. Andrew Baker, City. Two questions, please. First, for 2019 I think you said less than 20% of PruFund flows were from DC transfers. Are you able to give that number for 2018? And then you're expecting this to still be a headwind then in 2020, so that 20% coming down I guess. And then secondly on Solvency II sensitivity to 20% downgrade -- credit downgrade scenario is only 6 points. Is there any management action assumed in that sensitivity? And if so, are you able to give a little bit line of sight into what that is? Thank you.

A - Clare Bousfield {BIO 16746072 <GO>}

So, I don't know the 2018 number off the top of my head in terms of the percentage of DB transfers, but it has come down reasonably significantly between 2018 and 2019. So we do expect there to be some headwinds around DB transfers because of the FCAs consultation around contingent charging. But the one thing I would say is there is an element of resilience in the in the adviser market and also the quality of our proposition is very strong. So we -- right now we don't know what the outcome will be on that consultation, but it does look like it could potentially have a reasonably significant impact in terms of just how the advisers operate.

Yes. And then obviously we've got the initiatives around launching PruFund in Europe, which is a big focus right now in terms of -- and there's a lot of interest in terms of that opportunity. So for our broader perspective, we're very comfortable in terms of the ongoing flows on PruFund. And on downgrade, I don't believe that there is any management actions included in that 20% credits downgrade, but I'm looking at Spencer to double check that.

A - Spencer Horgan {BIO 4241901 <GO>}

We will double check it, but I think that's right. Yes.

Q - Andrew Crean {BIO 16513202 <GO>}

Hi. It's Andrew Crean, Autonomous. Can I ask two questions? First one on costs -- asset management costs. I think you're also kind of talking to continue to -- investmemt continuing to grow the cost base. Should we grow it from the GBP652 million you've reported or about GBP687 million included after taking back the one-off DB rating that you had? And then secondly in terms of gain on the retail asset management flow situation. As I understand it, quite a lot of the flows and the growth over time has come from expanding into European business. I just wonder how that performed the European flows into retail asset management in 2019 and how it's doing under coronavirus?

A - Clare Bousfield {BIO 16746072 <GO>}

So on the cost for asset management, I'm not guiding that, I'm saying that I think they're going to increase over time, they will come down over time. I guess there's a couple of things. One is, what we want to make sure of is that structurally we fix the underlying operating model so that we've got scalable growth in the future. The actual investment that will be needed or has -- we've already started on is included within the transformation cost beneath. So this is more around making sure that the period as we go through the transition through 2020, is just managing that you're not going to see a sudden drop in 2020 is really what I'm trying to acknowledge. You're absolutely right --

Q - Andrew Crean {BIO 16513202 <GO>}

Is the basics GBP687 million or GBP652 million?

A - Clare Bousfield {BIO 16746072 <GO>}

So you're absolutely right, the pension -- you've got to adjust for the pension credit, because that was effectively a one-off gain in 2019, that won't repeat in 2020.

A - John Foley {BIO 4239156 <GO>}

So in terms of the retail asset management business UK versus Europe, it's pretty pretty evenly spread across the whole of the market. The problem really comes in as much with the virus as you alluded. We've got the office in Milan is closed, as you would expect. We've got a mature book, so what we are finding is a big asset manager with a mature book is that it matures every -- part of it matures every year. So it's a question of keeping the flows coming in, that's going to be tricky in certain parts of Europe as we have entered this lock down.

And that's why, I mean, candidly, we're replacing that to a certain extent by the PruFund proposition, which will be structured quite differently to the UK proposition. And that will, as I say, we've been talking to a number of parties in Europe and we're close to signing an MoU with two, and we're hopeful for that as a solution to the issues across Europe. So that's the current picture. But with this virus, I'm not going to make any predictions, it would be a brave man who'd do that.

A - Spencer Horgan {BIO 4241901 <GO>}

Ashik, follow up.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Sorry. Just to follow-up again on asset management cost. Where would that GBP100 million additional transformation plan you have will fit in? I mean, are we talking about an absolute benefit or like will that be able to offset any potential investment you are doing in asset management cost? Or you think that additional investment could actually outgo this GBP100 million savings so it could be like a GBP150 million, GBP200 million something like that, your additional investment? Thank you.

A - Clare Bousfield {BIO 16746072 <GO>}

So bear in mind that the -- so we are about a third of the way through in terms of actually what we're delivering in terms of cost savings. But the cost -- the way that the cost program is done and the transformation program is across the broader business, which picks up both with profit and the shareholder element of it. So not all of the GBP100 million -- additional GBP100 million would flow through to asset management, because there will be an element that flows through to the shareholder component on the insurance business as part of that.

In terms of what we're looking to do, the program is all part part of the transformation program in terms of actually the investment that we've made in order to improve the underlying processes. Some of that cost has already been incurred in order to get to start the process, and that will continue to be incurred through 2020 and 2021 in terms of the outcomes.

A - Spencer Horgan {BIO 4241901 <GO>}

I'm going to take one more from the internet. So what is latest position on the suspended property fund?

A - John Foley {BIO 4239156 <GO>}

So while it remains in suspension, you know we closed that fund or we gated that fund for the benefit of customers. The team are making very good progress in terms of generating cash, so that when we do eventually open the fund we can meet any redemptions that have been storing up. And the team have been quite successful in rebalancing the funds to make sure make sure that we're not in a fire-sale situation. So we'll keep it gated until such time that we are confident about opening it, and how we would respond to redemption. So I'm not going to make any predictions around that at this point.

A - Spencer Horgan {BIO 4241901 <GO>}

Andy?

Q - Analyst

Just wanted check, just one final one for me, which was PruFund. I just wanted to check, have any of the versions of PruFund had a negative adjustment to the unit price over the last few weeks of pricing in market volatility?

A - Clare Bousfield {BIO 16746072 <GO>}

As far as I'm aware, no, they haven't.

A - John Foley {BIO 4239156 <GO>}

There's an optimist.

A - Spencer Horgan {BIO 4241901 <GO>}

Oliver?

Q - Oliver Steel {BIO 6068696 <GO>}

You talked about identifying levers for balance sheet optimization. What sort of things are you looking at?

A - Clare Bousfield {BIO 16746072 <GO>}

So that includes hedging that we do around interest rate, equities, looking at the risk and reward on the asset portfolio in terms of the use of a liquids and private assets, and how do we maximize that. Also, obviously, longevity and any of the other provisions that we have in terms of the balance sheet, potentially reinsurance in terms of although as I've tried to balance that in terms of making sure there's a value piece of that in terms of where we go. So those are a number of the different levers that we have in terms of how we manage the balance sheet.

A - Spencer Horgan {BIO 4241901 <GO>}

Yep, Marcus.

Q - Marcus Barnard {BIO 2103471 <GO>}

Yes. Marcus Banner. Just one question. Your capital generation target by 2020, presumably that doesn't include include any benefit from acquisitions, but how would you adjust that figure if you did make any acquisitions?

A - Clare Bousfield {BIO 16746072 <GO>}

So, the capital generation was set to be total capital generation. So to a certain extent, I think, it would depend on the size of any acquisition. So clearly, if we did something very significant, which I'm not suggesting by the way by making this comment that that's what we're looking at, then I think there will be a different conversation. For small acquisitions we would expect that to be included -- including both the cost of it and then also the benefits that you would get from the acquisition.

Q - Marcus Barnard {BIO 2103471 <GO>}

Sorry, did I say acquisition, I actually meant disposals. I'm thinking that --

A - Clare Bousfield {BIO 16746072 <GO>}

Same answer to the question.

A - Spencer Horgan {BIO 4241901 <GO>}

Another one from internet is, Tom Howarth from Barclays, actually two questions. The first one is, the 2019 restructuring costs were GBP190 million with GBP62 million transformation. What's the remainder in particularly, what run rate should we expect? And then also, how significant are Italian flows given that that's one of our larger markets?

A - Clare Bousfield {BIO 16746072 <GO>}

You want to take the Italian flows?

A - John Foley {BIO 4239156 <GO>}

You want me to do that first?

A - Clare Bousfield {BIO 16746072 <GO>}

Okay.

A - John Foley {BIO 4239156 <GO>}

So on the Italian flows, I mean, we are clearly not seeing much activity there either way, because of the lockdown in the virus -- because of the virus. It's probably still too early to determine what is actually happening, what will actually happen. My guess is we will be in outflow in Italy as a consequence of this, it's almost inevitable. And that might run into other markets as well. But it won't surprise you to know that one of the institutions that we are talking to about PruFund or the version of PruFund is an Italian institution.

A - Clare Bousfield {BIO 16746072 <GO>}

So, on the difference between the restructuring costs and the transformation cost of GBP62 million, there are a number of other costs related with the separation from Pru Plc. So whether it's the IT infrastructure that we have based in the U.S., the re-branding that we've had to do in terms of the move away from using the Prudential rate and some of the elements around Prudential. There -- so that -- that's the difference between those two amounts. They're not -- it's not recurring amounts, it's one-off amount that we're not expecting to have any future cost.

A - Spencer Horgan {BIO 4241901 <GO>}

Anymore in the room, Greig?

Q - Greig Patterson

Just -- I'm just trying to understand the magnitude of one element to the management actions, you had a benefit this year from asset optimization. I wonder how many -- if you could tell us what -- how much assets that actually are involved, so we have some kind of feel for you do x amount, we get y amount?

A - Clare Bousfield {BIO 16746072 <GO>}

Of the top of my head, I don't know the nominal value of the actual assets that were traded. But effectively what you're doing here is you are looking at the use of illiquid and private assets first to effectively increase the yield of the bonds for something that is an equivalent risk profile, if not lower risk profile. So that's effectively what we're doing.

The illiquid -- so what's the constraint or I guess the way that we look at this is, what proportion of the annuity PruFolio do we feel comfortable are invested in private and illiquid assets. And there's still a reasonable margin above what we're currently in, that would take us up to, I guess, our risk appetite level in terms of what we're looking to do. But that conceptually is what we're doing, Greig, in terms of optimizing the portfolio. Because if there are illiquid liabilities, so they're ideally match by illiquid assets. But clearly, you want to make sure, you've got sufficient liquidity should you need it in the event for -- either from a market or a customer perspective.

Q - Analyst

(inaudible)

A - John Foley {BIO 4239156 <GO>}

Yeah. But price moves in the market, you've got price moves versus cost of assets. Its -- you won't be able to calibrate that and then project what that would mean overtime for the whole book. I mean, that's just not possible given the way markets move, especially over the last couple of weeks.

A - Clare Bousfield {BIO 16746072 <GO>}

And that's always one of the considerations is making -- is you got to find the right market conditions to purchase the right asset is critical in terms of actually what you're doing.

Q - Analyst

(inaudible)

A - John Foley {BIO 4239156 <GO>}

It comes and goes, I mean, that's why we had a team of people doing this some days, some weeks, some months it looks positive, others it doesn't. I mean that's in the moving market. If you can't optimize at the drop of a hat, you need certain conditions and one of them is a friendly market shall we say.

A - Spencer Horgan {BIO 4241901 <GO>}

Thank you, Greig. Are we all done in the room? Good. So, I can see there's a couple of questions left on the internet, but actually I think we've covered them. So the IR team is just going to get in touch with you to make sure your questions are properly answered. Other than that, thank you all for participating. It's been a pleasure to have you here. If you have any further questions, obviously, the IR team is available. And otherwise, we look forward to seeing you next time. Thank you.

A - Clare Bousfield {BIO 16746072 <GO>}

Thank you.