Q1 2015 Sales and Revenue Call - Interim Management Statement

Company Participants

- David Paul Cooper
- Shayne Paul Deighton
- Simon George Thomas

Other Participants

- Andrew J. Sinclair
- Barrie J. Cornes
- Greig Paterson

MANAGEMENT DISCUSSION SECTION

Operator

Thank you for standing by and welcome to the Just Retirement Group's Q1 IMS Analyst Call. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session. I must advise you, the conference is being recorded today, Monday, the 10 of November, 2014.

I would now like to hand the conference over to your speaker today, Mr. Simon Thomas, Finance Director of Just Retirement. Please go ahead, sir.

Simon George Thomas {BIO 15219564 <GO>}

Thank you, operator. Thank you, operator. I'm Simon Thomas, CFO of Just Retirement, and I'd like to welcome you all to this conference call to discuss our IMS for the three months ended 30 of September, 2014. We really do appreciate your interest. And I'm joined on the line by Shayne Deighton, our Chief Actuary, and David Cooper, our Director of Marketing and Distribution.

I'll talk briefly about our first quarter's trading statement and then we'll have some time for your questions. Please do remember that we have a June year-end, so the first quarter of our 2014/2015 financial year, which is under discussion now, represents the third quarter of the calendar year.

So, first, we're today reporting a 42% fall in total sales, driven by a 48% fall in total annuity sales and a 23% fall in lifetime mortgages. Total annuity sales would have only been 26% lower if they had included the £75 million DB scheme we told you about a couple of weeks ago. This was signed in September and closed in October, making it a Q2 event. The 48% fall in total annuity volumes reflects the net effect of very different conditions experienced by our individual business compared to our DB de-risking business.

DB continued to grow strongly. Sales were up roughly sevenfold compared to the equivalent prior-year quarter to £24.8 million, obviously excluding the £75 million sale announced in October. If that scheme had been written a week earlier, then we would have written more DB business in Q1 than in the whole of the previous year.

We're are also pleased to be able to announce that we signed contracts on another large DB scheme for £76 million, which is due to complete later this week.

Base effects means DB growth rates will start to look more normal as the year progresses, but the business remains inherently lumpy and will continue to be volatile in shape. Trustees meet infrequently and the business is made up of a small number of relatively large transactions, so this lumpiness won't go away. But out of the total £1.8 trillion of DB scheme liabilities in the market, there are over £600 billion of pensions in payment for us to target.

Even if only a small percentage can benefit from our medical underwriting each year, this provides a strong growth potential. Many years of ALM work has reduced the volatility of the capital position of most DB schemes. This has improved the consistency of trustee demand, but not to the point that it will grow in a nice straight line.

The IUA picture is more challenging, as we continue to come to terms with the budget's aftermath. IUA sales were 59% lower than in the equivalent quarter of our previous financial year. They fell by 55%, if we compare them to the first calendar quarter of this year, which was the last to be unaffected by the budget. So it's difficult to portray this as anything other than a tough quarter for IUA volumes, albeit not as bad as the 90% drops some had predicted. We believe that for customers with less than £100,000 to work with, guaranteed lifetime income will continue to be a key part of their post-retirement financial planning, and our medical underwriting skills mean we can offer many of them a better income.

We managed mortgage volumes down by 23% in the quarter, against a tide of good market growth. Including the large DB sale which ended up being booked in Q2, the fall in lifetime mortgage sales was broadly in line with the drop in annuity sales. The mortgages continue to offer a great match to our liabilities, especially DB, which tends to bring longer duration cash flows.

As of today, trading conditions for IUAs have continued in the current quarter in line with our Q1 run rate. But, as we've flagged in several places, there is a risk of further volatility ahead of the new rules in April. So, even though DB volumes have exceeded our expectations so far, we are limiting ourselves to saying that we remain confident in achieving our overall full-year sales expectations, rather than talking prospects up. Obviously, we'll update you as the year progresses, but I think you can understand the huge uncertainties we face in the current sales environment.

Now, before we move on to Q&A, I want to pre-empt the inevitable questions about the new products we'll be launching once the rules change in April. In addition to the core retirement income proposition, we'll also offer a product allowing customers to leave some of their assets invested, whilst converting most of their retirement funds into a guaranteed income for life.

It's key to remember that our average case size is around £60,000, which often means our mass market customers really do need the additional income which a guaranteed income solution offers, rather than relying on the state pension. At this level, few financial advisors consider it prudent or economic to do the work required to put them into drawdown, given the relatively small sums involved by drawdown standards. Please don't forget this when you write about it.

For our individual customers, inheritance tax and often even income tax are simply not an issue once they retire, but enhancing the state pension with the best value guaranteed income solution they can get in order to pay their bills is. That's why we remain confident that our individual retirement income offering will remain relevant into the future. Our medical underwriting skills place us uniquely to provide value for money to secure income benefits. We'll update you further on the new products early next year.

Now, with that, I'd like to turn it over to questions.

Q&A

Operator

Thank you. The first question comes from the line of Andrew Sinclair from Merrill Lynch. Please ask your question.

Q - Andrew J. Sinclair {BIO 17749036 <GO>}

Morning, everyone. Just two questions if that's okay. Firstly, I just wonder if you could tell us a bit about the competitive environment at the moment for individual annuities and for bulks; and secondly, who you're coming up against in the bulk annuity market. And thirdly, again on bulks, just could you tell us anything about the margins in the bulk deals that have been done over the last few months, and if they're just similar to what we've seen elsewhere on your book previously? Thanks.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay, Andrew. Perhaps if I could pick up the – I'll ask David, actually, sorry, to talk about the competitive environment and who we're coming up against, and I'll cover the margin point, if that's okay. David?

A - David Paul Cooper {BIO 15900182 <GO>}

Hi, Andrew. Well, in two parts, in the individual underwritten annuity market, the competition is broadly the same as it has always been, even pre-budget. So we're coming up against the usual suspects in other specialist writers such as Partnership, MGM and LV. And then also we're still seeing the likes of Aviva and L&G reasonably competitive in the standard and lower end of the enhanced market.

On DB, we are seeing most of the DB writers in the markets – in the segments of the market that we're operating in. So we've come up against the likes of PIC, the likes of Aviva, L&G and Partnership.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay. And on...

Q - Andrew J. Sinclair {BIO 17749036 <GO>}

Sorry. Just to follow up on that. So, in there, any change on the price competitiveness in that market and individuals and on DB?

A - David Paul Cooper {BIO 15900182 <GO>}

Well, can Simon pick that up as part of the margin?

Q - Andrew J. Sinclair {BIO 17749036 <GO>}

Yeah. Sure. Sure.

A - Simon George Thomas {BIO 15219564 <GO>}

I was going to say on the margin side, I mean, clearly, to dwell on volumes rather than margins. But what I can say is that when we were talking back in September on the prelims, I indicated that the IUA margins were lower due to the competition in the marketplace that we'd seen. And I think I highlighted then that we thought that DB margins were slightly higher and slightly better than the IUA margins. That pattern actually has continued and so therefore I'm not really saying anything new in terms of the shape of margin that we've seen.

One thing I would flag is that in terms of our IUA market share, it's actually fallen, we think, in the quarter to June. So, that's relevant as well.

Q - Andrew J. Sinclair {BIO 17749036 <GO>}

That's good. Thank you very much.

A - Simon George Thomas {BIO 15219564 <GO>}

Thank you.

Operator

Thank you. The next question comes from the line of Greig Paterson from KBW. Please ask your question.

Q - Greig Paterson

Morning lads. Just on that guidance in terms of what – and I'm talking calendar quarters now, on the fourth quarter similar to the third quarter. Is that including taking account that December is a slow month, in other words, it's down actually in nominal terms, or are you saying that it's going to be flat in nominal terms?

The second question is, I wonder if you can just update us on lifetime mortgages, the structures that you potentially moving some of the stuff off balance sheet. And I thought it was quite surprising that you're still writing lifetime mortgages well ahead. That doesn't surprise me, but then your comment that economic capital remains unchanged, I thought if you're writing at that rate it puts some pressure on economic capital. I just want to chat about that.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay, Greig. Well, perhaps I'll ask David to talk about sort of the fourth quarter's progression and I'll come back and talk about the lifetime mortgages and the volume, and then perhaps we'll get Shayne to talk about the economic capital side. Get in all three, why not? So, David?

A - David Paul Cooper {BIO 15900182 <GO>}

Hi, Greig. Remember, our quarter to the quarter four that you're referring to doesn't tend to be depressed because of seasonality. We turn the business around sufficiently fast that our previous quarter fours have been broadly in line with quarter three. It's quarter one, in your terminology, where we see a seasonal drop, because of the lack of front-end activity from financial intermediaries over the Christmas period.

Q - Greig Paterson

All right, cool. So you're basically just saying that it's flat in nominal terms, quarter-on-quarter?

A - David Paul Cooper {BIO 15900182 <GO>}

Yes.

Q - Greig Paterson

All right, cool.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay. Greig, and on the lifetime mortgages, I think, again, we talked about this a few weeks ago, but clearly we have three levers to try and slow down and change the mix of the lifetime mortgages. The first is to write more annuities, which is clearly the favored route, as we capture most value that way. The second is to actually write fewer lifetime mortgages by becoming less competitive and putting the brake on, and as a by-product obviously increasing the yield on the asset. And then, thirdly, I think, as you mentioned, is to look to pass some mortgages onto a third party.

I think it's fair to say we're progressing on all three, and I think you can see the success that we've had in DB, particularly with the latest two announcements of the £75 million and the £76 million scheme has been helpful and that's obviously the one that we want to go for. But we do continue to talk to third parties if we feel the need to pass mortgages off the balance sheet. But I'd describe that really as a bit of a slow burner and, frankly, certainly my least preferred option.

Shayne, the economic capital?

A - Shayne Paul Deighton {BIO 17759794 <GO>}

Yeah. Good morning, Greg. You're absolutely right. Writing at more than the 25% we normally do has some impacts on economic capital. But I would say that the amount that we write in any one quarter, when you only consider the excess over 25%, isn't really enough to make a noticeable difference.

And what I'll add to that is the fact we are writing mortgages at the moment at very good margins. Plus the fact that to the extent we usually get with DB in addition to the IUAs means that we're able to make very good use of that additional yield from a capital point of view. So the position isn't, maybe, as bad in that respect as you're suggesting.

Q - Greig Paterson

Right. Just one point, you said market share, was that in calendar quarter two, because you said till June? Or what was your market share change in the third quarter, if you'd update us. And I know there's industry stats?

A - David Paul Cooper {BIO 15900182 <GO>}

Yeah. We haven't got industry stats for the quarter we're reporting on now. So, no, the comment was in relation to quarter two.

Q - Greig Paterson

Okay. Do you have any view on whether you're gaining shares or not, relative to your pricing, conversion rate, stuff like that?

A - David Paul Cooper {BIO 15900182 <GO>}

Probably no change to perhaps a little down, but that's a guess.

Q - Greig Paterson

All right. No problem. Thank you.

A - Simon George Thomas {BIO 15219564 <GO>}

Thanks, Greig.

Operator

Thank you. Next question comes from the line of Barrie Cornes from Panmure Gordon. Please ask your question.

Q - Barrie J. Cornes {BIO 2389115 <GO>}

Morning, everybody. It's Panmure Gordon. Just three questions if I may. First of all, I obviously appreciate you're managing down lifetime mortgage volumes, but do you see any increase in level of demand overall for LTMs as a result of the change in death taxes, in respect of pension pots?

Second question I had was just wonder when the new longevity savings product you mentioned, Simon, is going to come on stream? Is that going to be in April next year? And the last question I had was I just wondered if you had some color on the process for customers getting advice post April 2015 on their pots.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay, Barrie. Well, I'm going to hand over to David, I think, on those.

A - David Paul Cooper {BIO 15900182 <GO>}

I think, for those. Sorry. Yeah. Hi, Barrie.

Q - Barrie J. Cornes {BIO 2389115 <GO>}

All right.

A - David Paul Cooper {BIO 15900182 <GO>}

The lifetime mortgage markets, each has been growing (15:16) has been growing in successive quarters, I think, for the last seven quarters or eight quarters. So the demand is up regardless of what's actually happened in the budget, I mean, for all the well-rehearsed reasons about the income poor, asset rich.

I think you're correct that that could be another consequence of the budget changes, that we'll see greater demand for lifetime mortgages, but that's probably in the medium term. That won't be a rapid change after April.

Q - Barrie J. Cornes {BIO 2389115 <GO>}

Okay.

A - David Paul Cooper {BIO 15900182 <GO>}

In terms of the products, yes, we are still targeting April. And as Simon said, we hope to be able to share in more detail with you what we're doing in the New Year. And on the process, could you just ask that question again, the last piece?

Q - Barrie J. Cornes {BIO 2389115 <GO>}

Yeah. I just wondered about what the process is, what color you've got and visibility on how a customer will access advice and where the advice is coming from. Will it be a first port of call, then onto an IFA, or straight to an IFA? How's it going to be done?

A - David Paul Cooper {BIO 15900182 <GO>}

No. I think there'll be two routes, effectively. There will be people that seek out the guidance, which we've yet to see in its full glory, but those people will go through a guidance process, and probably then onto some form of advice. And then there will be a significant number of people that go straight to an advice business. I think what we will see is a broader offering of advice, which may well include simplified advice operating alongside or instead of full advice and possibly replacing non-advice, if that makes sense.

Q - Barrie J. Cornes {BIO 2389115 <GO>}

Yeah. Okay. Thank you.

Operator

Thank you. There are no further questions at this time. Please continue.

A - Simon George Thomas {BIO 15219564 <GO>}

Okay. If there are no further questions, I'd just like to thank you for your interest. And we look forward to speaking to you all again at the end of February for our interims. Thank you very much.

Operator

Thank you. That does conclude our conference for today. Thank you for participating. You may now disconnect.