S2 2013 Earnings Call

Company Participants

- John Pollock, CEO LGAS
- Kerrigan Procter, Managing Director, Annuities
- Mark Gregory, Group CFO
- Mark Zinkula, CEO LGIM
- Nigel Wilson, Group Chief Executive
- Paul Stanworth, Head of Group Treasury and Investments
- Unidentified Speaker, Unknown

Other Participants

- Alan Devlin, Analyst
- Andrew Crean, Analyst
- Andy Hughes, Analyst
- Gordon Aitken, Analyst
- Jon Hocking, Analyst
- Oliver Steel, Analyst
- Unidentified Participant, Analyst

Presentation

Nigel Wilson {BIO 1535703 <GO>}

Good morning, everyone. And thank you for joining us. The usual etiquette about mobile phone applies and also the standard disclaimer about forward-looking statements.

Legal & General's Executive Team share collective responsibility and accountability for our performance. So this morning I will introduce the results. Mark Gregory, our new CFO, will take you through them in detail. And John Pollock and Mark Zinkula will overview the performance and strategic direction for their businesses. And I will finish off with outlook. Other key members of our team are also in the room and will also be available to answer questions.

You will hear from the full Executive Team. This reflects the new management and business structure we are putting in place. We are creating a Legal & General that has five profit centers. But is one brand, one set of values, one set of shared goals. I see our simple structure as important in delivering growth and value.

First, in combining Protection and Savings under John Pollock's leadership, we are merging together two very big businesses. This presents a substantial challenge for John and his management team. They will however deliver cost synergies. There are also revenue synergies from reducing silos and driving up cross-sell by presenting our retail, direct and corporate customers with a better multi-product offering. Our cross-selling is too low. And despite our very strong performance on costs, they're still too high.

Combining Retail Investments and LGIM under Mark Zinkula's leadership and his team enables us to leverage LGIM's institutional excellence in the retail space. We need to improve our Unit Trust business and move it significantly from its current 11th place in the market. Our performance in the DC market has lagged. And to date we've had minimal presence in the Private Wealth business.

Bringing Annuities under Kerrigan Procter, that's closer to L&G Capital and closer to LGIM, similarly makes huge sense for a business with increasingly sophisticated wholesale international dimension. We've recognized the need to grow annuity net inflows, including individuals. And we have been successful. But there is much more still to do.

Consolidating L&G Capital and Direct Investments under Paul Stanworth enables us to deliver high returns by coordinating our global asset and liability management and by disciplined deployment of capital into Direct Investments. We have to deliver greater risk-adjusted returns from executing this strategy.

And Jimmy Atkins in L&G Americas made good progress in growing cash and profits and getting LGA from its number 11 position to number three in its markets. But our business in the US is single product and through a single channel and there are many opportunities to scale this business.

This is another very strong set of results. The direction of travel at Legal & General is consistent. The pace is accelerating. Good growth with strong financials. Operating cash up 14%. Net cash 23%. Operating profit up 10%. EPS 13%. DPS 22%. ROE up to 16.8%.

And as I've said before, Legal & General is a simple business in a complex world. We're selling the right products at the right prices through a variety of distribution channels. We execute efficiently and we have an efficient model which enables us to deliver rising dividends to our shareholders. However, we're not complacent. We are still very much work in progress. There are many challenges and there are huge opportunities so there's still much to do.

This slide marks our strategic progress. Everybody sleepwalked into the financial crisis. Policymakers successfully contained the recession through monetary method on [ph] and it worked. Post the financial crisis, Legal & General's response was to focus on cash, de-risk our balance sheet and industrialize our processes. This enabled us to show exceptional resilience during a very poor economic climate. However, this has resulted in us being in great financial shape as economies improve and presents us with many growth opportunities.

The cash focus was successful and we will retain that focus and that discipline. And this has been a really solid six months of execution by my colleagues. There is strong evidence that in the last year we're moving from thought leadership to doing leadership. For example, three M&A deals in three months and in three of the growth sectors that we identified. CALA Homes in the Direct investment space, Lucida in Retirement Solutions and core funds in Digital Platforms, all well executed. And I'm confident there is more to come from Wadham and his team.

Our first international bulk annuity deal was completed in the half. We're also innovative as we executed a GBP3.2 billion longevity contract. More of both to follow.

There was continued progress in the international expansion of LGIM. We have now won 47 customer mandates from US clients, with many more to follow. And the launch of Passive in the United States and Asia will both be positive.

The five macro drivers that propel our business have not changed. This is not a surprise as they are long-term trends. They are being increasingly recognized as such, not just by us. But we were early identifiers and we are increasingly leaning in to the trends where we see them playing more strongly to our strengths. For example, aging populations and retirement solutions. Our Annuities business, both retail and institutional, is now reaping the benefit of the baby boomers with DC pensions.

Workplace savings is very strongly positioned in a sector which has the potential to copy the success of Australia. We are developing powerful direct-to-employer D2E propositions. And LDI, very much part of the pension de-risking retirement solutions package, delivered a 73% increase in gross flows into LGIM.

In digital, the core funds purchased gives us the largest market share in the UK and platforms business, over 20%, a sector expected to double to around GBP500 billion by 2017.

In welfare reform and protection, risk sharing is providing a growing role for Legal & General. It is economically vital and increasingly politically acceptable. It is already established in pensions. It's happening now in protection, where we are the number-one provider in the UK. And ultimately it will happen in the funding of long-term care, where we are working closely with the government following the Dilnot Review.

Homogenous asset markets and the internationalization of LGIM, index, real income and solutions business are all predicted to grow. These are businesses that LGIM increasingly specializes in and where we have demonstrated we have the international capability to grow.

Bank retrenchment and direct investment, in Europe, according to Commissioner Barnier's recent green paper, 85% of financing is provided by banks. But banks today are receiving or will receive aid close to 37% of EU GDP. That's a very different model from the United States. No wonder the Commission wants to do more to channel savings towards long-term investment. Everyone now recognizes that institutions like L&G are core to this strategy.

And in Direct Investments it means that Legal & General Capital is able to execute to deliver enhanced returns for the annuity book and for shareholders. An additional 50 basis points on the GBP4.5 billion of shareholder funds equates to GBP22.5m. An additional 20 basis points on a GBP33 billion annuity book is GBP66m. Opportunities include infrastructure, direct investment, bilateral lending. Again, we have to execute well.

We have GBP4 billion invested in infrastructure and direct investments already. We've already invested in social housing, student accommodation, transport, distribution and solar energy. We intend, as opportunities arise, to bring more of our overseas bond investments back to invest in more tangible assets here in the UK, including helping to develop a UK private placement market.

We also have no burning [ph] platforms. Even the persistent regulatory brake on growth caused by the uncertainty around Solvency II is showing signs of being taken off. We believe that at last a settlement that will work is within reach. The UK Treasury and the PRA are fully engaged and making good progress. The direction and speed of travel is better than at any stage so far.

So with five clear profit centers, LGIM, LGAS, LGA, Annuities and L&G Capital, which includes Direct Investments, we are well positioned, able to accelerate growth in line with the five macro trends and deliver value to our shareholders. We have the right strategy and we have to continue to demonstrate the ability to execute well and execute consistently.

I'd now like to hand over to Mark Gregory to take you through the results in more detail.

Mark Gregory {BIO 15486337 <GO>}

Good. Thanks, Nigel. Good morning, everyone. I have to say, these are a great set of results for me to start with as CFO. We talked previously about the importance of both sustainability and growth. And these results illustrate the further progress we're making. Growth has been broad-based, right across the business, both in terms of trading and in cash and earnings generation. Our cash generation is high-quality. The vast majority of it flows up to Group level and is available as a source of dividends to our shareholders.

So let me take you through the financials, starting with the business performance. We delivered further growth in our businesses, building a stock which is the single biggest driver of profitability, not just this year but in the future. Growth highlights included GBP7.5 billion of LGIM net inflows coming from international clients. And the UK business also delivered net positive inflows.

Total annuity sales, at GBP1.4b, were up 142% year on year. Savings assets under administration are GBP111 billion versus GBP70 billion at the full year following the Cofunds acquisition.

Gross written premiums for UK Protection were up 3% to GBP689m. And GI premiums were up 10% to GBP183m.

Sales of US Protection were up 6% to $70 million APE, which combined with our retention levels, meant that gross written premiums for the US Protection were up 10%, at $503m.

A strong six months also saw net and operational cash up 23% and 14% respectively, operating profit up 10% at GBP571m. And EPS of 7.82p, up 13%.

Finally, the balance sheet remains strong, with an IGD surplus of GBP4.1 billion and the annualized return on equity strengthened further to 16.8%.

The key message here is that while we've had strong growth over the last two years, which is illustrated on this graph with the compound annual growth rate shown, actually what's been delivered in the first half of this year accelerates that rate of growth across all these key metrics, operating cash, net cash, Group operating profit and total sales growth. I think equally importantly this is exactly what we said we were trying to achieve. We said we'd move the strategy on from being a cash story to cash and growth. And now you have seen that cash plus growth story becoming a reality. In time, we expect the third leg, selective acquisitions, to also make a meaningful contribution to our financials.

The strongest growth in all of our financial metrics has been the increase in net cash generation, up 23% to GBP0.5b. What this slide does is explain to you the net cash generation -- how that net cash generation has been delivered. So we see a strong improvement from the contribution from LGIM, up 9% to GBP106m. Even stronger contribution in terms of growth from Annuities, which saw GBP17 million of new business surplus augmenting the 7% increase in operational cash.

In Housing and Protection we saw a 54% increase in net cash to GBP126m, driven by our increased scale in retail protection, lower new business strain and an outstanding result from our General Insurance business. And Savings and our US Protection business also made meaningful additional contributions to net cash generation.

Overall, what we're seeing are the benefits of scale and greater efficiency and our multiple sources of cash generation.

Here you see the link between operational and net cash generation, feeding through to profit before and after tax. And how this in turn is funding the dividend growth that we announced today. So very clear and transparent visibility between the operational cash growth and profits and dividends, just as our strategy is designed to do.

Moving on then to the individual divisions. And starting with LGIM, our global asset manager. Here you see further strong progress from LGIM, with revenue up 12% and the cost-to-income ratio remaining a market-leading 45% in the first half of this year, resulting in operating profit up 13% to GBP135m. Zink will cover LGIM in more detail a little later.

Onto Annuities, where we're talking about what we consider to be the leading annuity provider in the UK. And again, more superb progress. Net cash generation up 20%, benefiting from larger scale as well as writing new business this year, this half year, which generated an IFRS surplus of GBP17m [ph] on the back of the GBP1.4 billion of new annuity premiums.

New business embedded value margins are at 8.4%. This was an outstanding six months for our annuity business. We saw record sales of individual annuities, up 44% to GBP754m. And we are the beneficiaries from open market options; 79% of those individual annuity sales were sourced externally rather than from our own internal pension book. We're also growing our enhanced annuities, where premiums doubled in the period.

Bulk annuity sales of GBP670 million were up tenfold as we wrote 45 policies, including our first one from outside the UK. We also completed the largest longevity insurance contract in the UK to date at over GBP3 billion for BAE Systems.

This slide underlines many of the advantages we have in annuities. We have been at this business for over 30 years and therefore have a huge amount of data and, equally importantly, we have the experts to analyze that data. So we have a deep understanding of the nature of longevity risk and its likely future development. In addition, we have the key benefit of having LGIM as an integrated fund manager, with its proven strength in active fixed income and LDI to develop and deliver the asset strategy which is so key to this business.

Annuities is a growth business, with rich opportunities in BPAs, longevity deals, international transactions, buying back books as well as driving up individual annuities as more DC pension savers reach retirement. We've already written GBP0.5 billion in July and the Lucida deal brings a further GBP1.4b.

The task for Kerrigan and his team is one of execution, to push up net flows and grow the stock of business from the figures shown in the first half of 2013.

Moving on to Housing and Protection, we saw operating profits up 12% to GBP168m. Within this, net cash was up 54% as we benefited from increased scale and a GBP10 million reduction in new business strain due to the removal of retail protection from the old I minus E tax regime. This was partially offset by new business margins down from the super levels that we saw in 2012, which resulted from the volume spike in Q4 ahead of the introduction of gender-neutral pricing.

Having said that, we have seen a strong bounce back in volumes in Q2, where sales were up 6% year on year. So we are now seeing a return to normal levels. We would therefore expect the margins being achieved on new business sales in the second half of the year to increase compared to the first half, although not back to the same levels we saw in 2012.

GI had a very strong result. It benefited from very benign weather conditions and also from greater efficiencies leading to an excellent combined operating ratio of 81% for the first half of this year.

In the US, sales were up 6%. We're now the third largest writer of term assurance in the United States. We have over 1 million policies in force. This business has good growth dynamics, writing new business with a 10% margin in the first half of this year and producing operating profit of $81m. As a reminder, we recognize net cash in L&G America as a full-year dividend which is received in the first half and which was up 10% to $66m.

So good momentum in all of our protection businesses.

Moving on to Savings. Many of you were with me in May when we outlined our strategy for transforming our Savings business into an asset-gatherer. In the first half of this year you will see some of those aspects coming to fruition, with net inflows of GBP2.3 billion into our growth businesses. We're also seeing a spike in maturities with the 25th anniversary of the 1988 endowment peak. But overall, we saw net inflows in the first half of this year of GBP100m. And we have total closing assets under administration, including Cofunds, of GBP111b, up from GBP70b.

There's been good growth in the business, with operational cash generation up 8% to GBP95m. The business has been written more efficiently, with new business strain down to 1.8% of new business premiums. Remember, that was 5.5% back in 2008. So we're now roughly three times more capital efficient at writing new business than we were back then. And the absolute value of the new business strain came down in the first half despite writing much higher volumes of workplace pensions.

Operating profits in savings were GBP62m, with 14% increase in net cash, offset primarily by reduction in tax synergies in our life fund impacting our insured savings business.

We have a very strong balance sheet and are generating a healthy return on equity. We're keen to make sure this remains the case and hence we have a strategy and a discipline around the deployment of capital. We will maintain the same disciplined approach to capital deployment via selective acquisitions.

We continue to see many opportunities to grow our business organically and will continue to deploy the capital in a way that generates healthy returns on risk-based capital. And continuing all that L&G has stood for in the last few years, we're always looking at ways of making the business ever more capital efficient, through expense efficiencies and through making sure that our balance sheet is being appropriately rewarded for the risks we choose to run and where we have competitive advantage.

And finally, today we've announced a very strong growth in the interim dividend, up to 2.4p from 1.96p at the interim stage last year. We are committed to rewarding shareholders for the success the business is having. We recognize it is shareholders' capital we are deploying. Therefore, we aim to give a healthy return on that capital.

As Nigel says, we are beginning to see progress in the journey towards greater clarity on Solvency II. Assuming this progress continues, then we hope to be able to provide greater clarity in due course on how we intend to progress the dividend. In the meantime, we can see how our dividend is benefiting from the continued business momentum, which in turn is delivering greater cash generation.

So in summary, we've delivered a very strong trading performance, with sound growth across all businesses, growth in the stock of our [ph] businesses which is driving profitability, hence growth in operational cash, growth in net cash generation, growth in operating profit and perhaps most importantly of all for shareholders, growth in the interim dividend. And we're positive on the prospects for the business going forwards.

I'll now hand over to John.

John Pollock {BIO 6037447 <GO>}

Thanks, Mark. Good morning, everyone. I'm delighted to be here talking to you about LGAS. Merging Savings and Protection brings together two innovative market-leading businesses, each with very strong track record. Collectively LGAS brings competitive advantages, new opportunities and synergies.

Over 10 years we have grown Protection gross premiums by GBP1 billion to GBP1.3 billion and driven strong profit growth. And over the last four years, Mark and his team have successfully turned the Savings business around. With deep and strong foundations, it can grow into a scalable, efficient, asset gatherer. Mark told you in May of his aspiration to deliver annual average compound growth in total savings assets of 10% to 2017. I will be really disappointed if we can't achieve that goal.

LGAS businesses are central to three of the growth drivers Nigel outlined. Shifting risk from the state to the individual creates a need and an opportunity, particularly in the retirement and protection markets. Our recent deadline-to-the-breadline report showed that people have on average just 18 days between an unforeseen event occurring and their savings running out. It's not enough. It creates a clear imperative for society and an opportunity for trusted providers such as LGAS.

In H1 we saw some of these themes coming through. We're strong in retirement solutions. Substantial net inflows of GBP0.7 billion for workplace now gives us over GBP7 billion assets on our workplace platform, virtually double the 2011 level. In H1, our SIPP platform, Suffolk Life, gained material net inflows of GBP300m. And that platform is approaching GBP6b.

We remain the leading retail protection business in the UK and we successfully navigated gender-neutral pricing. Average retail protection APE over the last three quarters was GBP36m, in line with the previous three quarters. But with volumes rising back above equivalent 2012 levels in the last quarter and lower lapses, the GWP continues to grow.

Auto enrollment is working well for us, with over 90% of our new joiners staying in the schemes. We need to focus on profitability here. But there is a clear synergy gain with Group Life, where volumes are up 44% against 2012 as employers add benefits like death in service and group income protection to their new pension schemes.

LGAS brings together the UK's leading digital platforms in both protection and savings. Cofunds attracted net inflows of GBP3.5 billion and is the UK's largest platform, with GBP54 billion of assets. Our protection platform is the most automated in the UK. 80% of our customers are fully underwritten online when they apply.

The continuous focus on automation since 2000 has brought down unit cost in Protection by almost 60%. Still online, our Group Protection Quote and Buy portal has already been used by 1,300 employers.

Enhancing our digital capability is a clear, key strategic priority. Platforms are more efficient and better for customers. Cofunds is at scale and we can build bigger, more efficient, more automated processes to outperform in attractive, growing markets and earn revenue at multiple points in the value chain.

Cofunds has the leading market share of around 20% and is well placed to take full advantage of market growth. Only 8% of the investable asset pool in the UK is on platforms. So headroom remains. Fundscape's forecast is for the market to double over the next four to five years.

We have already started the Cofunds integration. The new L&G management team has delivered over GBP3 million of annualized cost savings so far and we are comfortably on track to deliver the GBP11 million per annum savings by 2015 that we identified at the time we did the acquisition.

We already have broad-based scale and distribution through our unique mortgage network, our IFA presence, to our unrivaled bank and building society footprint, employees of our large workplace businesses and our emerging direct channel where we are already the largest provider of household insurance online. Cofunds gives us further opportunities to join up propositions for different customer groups, both corporate and individual. And also to continue to access these customers in the manner of their choosing, despite the rapidly changing and more digital distribution environment that we see today.

LGAS is already a high-scale, low-capital, cash-generative business and it can leverage further profitable growth from our strength in key growth markets. Housing and protection provides a strong engine for cash and profit. We will maintain and build on the leadership in Protection and broad channels of distribution, including the L&G network, which now accounts for one in seven mortgages sold in the UK.

In Savings, we are on track to achieve the same virtuous circle that has worked so well in Protection. Industrial scale and highly automated, efficient processes driving customer value, in turn driving further scale economies. We know the mature savings market and assets will gradually decline. But it's my goal to retain customers and drive up the contribution from our growth businesses, reducing costs as the legacy assets run off to ensure that profits from the mature businesses can be distributed or selectively reinvested for growth.

Merging two large businesses will create significant synergies, both revenue and cost. We are already identifying these and I will update you later in the year.

In summary, we have the track record, the brand, the financial strength, the propositions and the distribution reach to deliver further profitable growth in the protection and savings market. We have the skills and commitment to deliver the benefits of our combined business for customers and our shareholders alike and to be a force for good in society.

Thanks a lot. I'll now hand over to Zink for LGIM.

Mark Zinkula {BIO 16142450 <GO>}

Thank you, John. I'd like to start by discussing our key metrics, which show the ongoing development of our asset management business with strong profit and cash delivery. Our operating profit of GBP135 million increased 13% during the first half of the year. This reflects growth in revenue as a result of AUM growth and efficient cost/income ratio of 45%.

We've maintained a low cost/income ratio while continuing to invest in the business, in particular in infrastructure and resources to enable further geographic and product expansion. We've had exceptional new business growth once again experienced across all of our core businesses of index, LDI and fixed income.

Highlights during the first half include net inflows of GBP7.5 billion from international clients and GBP5.7 billion in LDI gross inflows as our expertise from retirement solutions continues to attract growing interest from pension clients. We're now the largest manager of LDI in the UK, with over GBP70 billion in assets and over GBP140 billion of derivatives under management. We expect these trends to persist as we continue to execute on our strategy.

A key part of our strategy is the ongoing expansion of our international business. And this slide shows the evolution over the past several years. Our AUM has grown from GBP15 billion in 2008 to GBP52 billion today. Since the beginning of the year we've received inflows from clients in each of our targeted regions. We continue to grow our footprint in the Gulf and Europe, adding new clients while also expanding existing relationships by offering an innovative range of passive capabilities as well as select active capabilities.

In Europe, gross inflows of GBP4.7 billion illustrate the success of our strategy of targeting the largest investment pools in the region. And we're in the process of further expanding our product range. We've also just received regulatory approval in Hong Kong to allow us to actively market our capabilities in Asia. And our team in the US continues to deliver excellent performance across its range of strategies.

AUM has increased to GBP22 billion with our active fixed income and LDI proposition attracting growing interest from clients and consultants. In the first six months we added eight external clients and now have 47 direct external clients, including several of the largest plans in the country. The vast majority of our assets are managed on behalf of pension plans and we're well positioned to provide a wide range of solutions for defined benefit and defined contribution plans.

We continue to experience significant inflows into our LDI and fixed income strategies as pension plans de-risk. Much of our success over the last few years has been with large clients. And we're in the process of rolling out a digital solution to help smaller clients de-risk. As the defined benefit market matures, we're increasing our focus on growing our DC business.

A good example of the recent progress is the recent announcement by NEST that they have awarded us two property mandates, its first direct investment in the property asset class.

We've also made several key hires in our asset allocation team and are expanding our range of multi-asset products by leveraging our core areas of expertise as we expect growing demand for these types of products over the next several years. And we're repositioning our Active Equity team to move away from strategies that aren't consistent with our brand or that directly compete with our index business and instead focus on funds designed to meet client objectives in the DC and other target markets. We'll be in a position to share more information on our plans in this area in the near future.

Finally, we continue to make progress in maximizing the expanding synergies between LGIM and other parts of the Group. We've just begun the process of integrating our Unit Trust business into LGIM. This will allow us to have a more joined-up approach to product development, have a more efficient and streamlined business model and be better positioned to deliver LGIM's strengths as an institutional-grade investor to the retail market.

We're working closely with our workplace savings platform and benefiting from a growing allocation of our expanding range of funds for the DC market. And our already close relationship with the Annuity division continues to develop, both in regards to client engagement as well as expanding their investment strategy into direct investment opportunities. During the first half of the year we successfully invested over GBP500 million in property and infrastructure investments and are taking steps to increase our activity in these asset classes going forward.

And I'll hand it back over to Nigel.

Nigel Wilson {BIO 1535703 <GO>}

Thank you, Mark, John and Mark. Legal & General has a clear, strong and evolving story. And I'm very fortunate that we have such strength, not only amongst my executive colleagues. But also increasingly throughout our organization. The changes we have made are an important step in our continued evolution. And I'll round off the formal part of this presentation with three observations that I feel are important to our outlook.

First, you've seen how we are driven much more by macro trends than by short-term economic changes. This is part of the explanation for our resilience in the period since 2009. And it will remain the case that our business model will benefit from demographic, technology and social changes. But we can't ignore the broader economy. Our LGIM economists see global growth gradually strengthening through H2 and into 2014.

Last year we spoke at this meeting about the triangle of austerity, fiscal, regulatory and banking austerity. And the opportunities they created for Legal & General. The opportunity now exists to turn the triangle of austerity into a triangle of prosperity as we invest in vital infrastructure, shift away from state welfare to direct provision by individuals or through employers. Also we expect EU and UK financial regulators to catch up with their colleagues in the US; that is regulation that reflects economic reality and that facilitates growth and investment.

My second point is about internationalization. L&G is spreading its wings. In the US we are now the number-three provider of life cover. LGIMA [ph] is rapidly acquiring mandates and showing leadership in the LDI space. And we are only just launching index products in the United States and in Asia.

We have mandates from sovereign wealth funds in Asia and in the Gulf. In BPA and longevity we are starting to move outside the UK. Our new structure will enable us to get more synergy benefits for our French and Dutch businesses, both in product developments and in capital management.

We are restructuring our MENA joint ventures in the Gulf region and looking for ways to build on the presence which the IndiaFirst JV has established.

My third and final point is that our structure will make us a leaner, more customer-focused company with five clear profit centers. What we are creating at Legal & General we believe is unique in the sector. Its DNA includes our 176-year life office heritage with its traditional financial strength, strategic discipline, customer service and social responsibility. But Legal & General also has versatility, the ability to provide a wide range of protection, savings, investments and annuity solutions to our millions of individual and thousands of corporate and institutional customers. We've put the customer at the heart of what we do. And we're also becoming a destination for talent.

The model we are creating is rooted in the life sector. But it's scalable through savings and investment management, with additional value add through institutional trades and direct investment. It is highly attuned to what is happening in our economic policy and our regulatory environment. And it goes beyond the traditional scope and scale of a UK life office.

So I'm excited by our prospects. The second half of the year, as Mark talked -- Mark, John and Mark talked about, started very well. We are strongly positioned in the short, medium and long term. And we have an excellent management team who can deliver and execute on our strategy.

I would now like to hand the floor open to questions. Could you just name who you are and the company you represent? Who's got the mic?

Questions And Answers

Q - Andy Hughes {BIO 15036395 <GO>}

Sorry. Andy Hughes, Exane BNP Paribas. Three questions, if I could. The first one is on the Protection business. Obviously, the thing it seems to me is that you may be getting peak levels of net cash this year from UK Protection as a result of the tax changes. So you're benefiting from the reduced new business strain as a result of the higher tax rate that's applying. But when I look at the future cash flows they're going to be significantly lower, as implied by the lower new business margin you're earning, which is significantly lower than it was last year. So is it right to say this year is peak cash for the UK Protection business?

Second question is on annuities. Obviously you've written a lot of enhanced annuities this year relative to last year. But you're still in line or below market share on enhanced annuities. Has the non-enhanced part of the world, which you've been specialized in, in the past, have you looked back at that and said maybe the mortality experience of those is going to be impacted by the presence of the enhanced annuity market, i.e. we're getting longer life expectancy than we expected coming through that market?

And the third question is on the savings net flows. Obviously you showed big inflows and outflows of savings. But there's no way to scale the actual fees you're earning on the inflows and outflows. So I'm assuming that the inflows are significantly lower fee income than the outflows. And could you tell me what's going on? Are you reducing expenses at the same rate as the net fee income is being reduced? Thank you.

A - Nigel Wilson {BIO 1535703 <GO>}

Thank you for positive questions there, Andy. We'll take them all in turn. I think the general point is that I think we've all, including ourselves, tended to underestimate the operational and net cash generation of our businesses. I know that we've done it in our own internal modeling for a number of years. And some of you have pointed out the need for us to be more ambitious in areas like the annuity market. We've held back whilst we've been building our infrastructure and our people capabilities so that when we execute we get to execute very well.

I'll let Mark, John and Kerrigan have a go at the respective three questions.

A - Mark Gregory {BIO 15486337 <GO>}

Just on the question around the impact of our net cash generation going forwards for retail protection, we've quite clearly highlighted in the note we have had this benefit of the removal of retail [ph] protection from the I-E regime, which came into effect January 1 this year. There is a neat little note in your pack which quantifies what that benefit is.

Just very, very simply, we used to get tax relief on deferred -- on acquisition costs on a -- spread across seven years. We now essentially get them all in one go. So what you're seeing is a permanent increase in the tax benefit we get from that. But we will see a lower -- sorry, a lower release of margins over the subsequent seven years. We can get back to the number we first thought of. But actually there's a pull-forward acceleration of cash profit. So that's what's going on there.

In terms of the impact of margins, you're quite right, Andy, the margins on -- say on protection do flow through quite quickly into our IFRS profits and cash numbers; therefore, that is a key number for us. As I stated it in my speech, we are expecting margins the second half of this year to go back from where they were in the first half, although not back to the level we saw last year, which really was exceptional levels based on some very peaky volumes ahead of the impact of gender-neutral pricing. So we are expecting margins to go back to perhaps the more normal levels we've seen in prior years.

A - Nigel Wilson {BIO 1535703 <GO>}

John, do you want to comment about H2 margins versus H1 margins and margins going forward in the protection business? Kerrigan can make a few comments on the annuity business.

A - John Pollock {BIO 6037447 <GO>}

Yes. I guess I would say I was slightly offended by that, Andy, given our track record of -- in protection. The scale of the protection business and growing the GWP is far more material in the long-term cash generation of the business than the minor changes that happen around tax or regulatory regime. I'm still very, very confident that we've got a lot of opportunity to grow the protection business going forward. And the synergies that I talked about in LGAS give us the opportunity to sell more of it at a highly automated way, retain longer lower lapses, should result in benefits coming through.

Your other question. So margins for H2 I would expect to be better than we had reported at the first half and we continue to see our competitive position leading the market.

As far as the other question on savings, if you like, as both Nigel and I alluded to in the presentation, we're very keen to exercise the cost synergies that we see in bringing LGAS together. That's an important and ongoing factor for savings profitability. And as I said in my speech, I will be coming, once we've had a chance -- Andrea is leading the project for me, once we've had a chance to have a really good look at it, we'll come back and give you a much fuller update on what those synergies will mean for our expenses and therefore the implied margins.

A - Kerrigan Procter {BIO 15093363 <GO>}

Thank you, Andy. So your second question was on enhanced annuities and the risk of anti-selection in that market. So as you kindly pointed out, we've more than doubled our volume since H1 2012 in the enhanced annuity market. It's a really exciting market for us. As we deploy our capability increasingly into that market we can see great prospects, if the price is right of course.

And your question about whether we've been aware of anti-selection in that market and the risk of healthier lives only going for standard annuities, yes, categorically we have. Over the last five years, as the enhanced market has grown in the open market option then we've been continually adjusting our standard rates to allow for the increasing number of healthy lives that will be in that category. So, as you know, around about 65% of 65 year olds have a medical condition. If I add to that that it takes 40 years to save for a pension, 20 years for a pension to be in payment and only half an hour to go online and fill in your medical conditions, yes, of course we assume that if you come through the standard market you're going to be healthy and we price for that.

A - Nigel Wilson {BIO 1535703 <GO>}

Thank you. Do we just have one mic? Yes?

Q - Jon Hocking {BIO 2163183 <GO>}

It's Jon Hocking, Morgan Stanley. I've got three questions, please. Could you talk a little bit about the risk appetite you've got for the asset mix backing shareholders' funds? You seem to be talking about doing slightly more ambitious things with the investment return on that. I wondered if you could talk about the risk controls you've got around that and what the target allocation might be. That's the first question.

Second question, was Mark hinting about a rebasing of the dividend when you get some clarity on Solvency II and what further color can you add around that?

And then finally, on the asset management business, you talked about unit trusts and active equities. I just wondered if you could give a little more color about what you're doing in the active equities space. Is this retail, institutional? Is it UK? Is it international? And how we might thing about that going forward. Thank you.

A - Nigel Wilson {BIO 1535703 <GO>}

Thanks, Jon. On -- I'll ask Paul and Mark Zinkula to pick up those questions in a second. I think there are a couple of points of clarification first, is that on the whole, synergies between putting the two businesses together, John's going to hold a conference call probably in late September or October. Andrea's been -- October and -- I've been told by Andrea it's October, one single look. That -- and really give you much greater clarity around all of that. There's a lot of work been carried out already. But we want to give a very clear presentation around that which will give you some color on the projections going forward in that business.

On the dividends, again, Mark made the point very clearly that at the full year end he's going to give a complete comprehensive outline of the dividend policy going forward. I think to be fair to Mark, he's been Finance Director for I think all of five weeks now. And I know they've been five very long and hard weeks. But we wanted a bit to highlight, to signal that we're going to continue with our very progressive dividend policies today. But we'll give greater clarity on that at the year end.

You're right to talk about the shareholder funds. As I mentioned, I think there's a more -- a better risk-adjusted return that we can get out of shareholder funds. And maybe Paul can talk about the things that he's doing in the direct investment piece first. And then, Mark, can you talk about the more ambitious plans that we have for improving our lagging DC performance and how you're going to re-energize the active business going forward. And including the private wealth options that we've got for further growth?

So, Paul?

A - Paul Stanworth {BIO 15495409 <GO>}

Yes. Thanks very much. As far as the shareholder funds are concerned, our aim is to manage the risk in the shareholder funds so that we can maintain a certain level of solvency and earnings stability. And currently the portfolio itself has got a very, very tradable portfolio. And what we're looking to do is to increase the amount of direct investments that go into that portfolio, largely because that surplus is really attached to a solvency margin that itself is part of the annuity business. And we can see better risk-adjusted returns by taking asset exposures which traditionally insurers perhaps didn't take but increasingly we will take, mainly because the banks have crowded us out of the market over the last couple of decades.

And we've made some inroads with that with CALA. And CALA itself as an example gives us a number of synergies in terms -- for instance, developing our land banks which shareholder funds have and also developing the synergies in terms of financial support to that company. And that's an example. And we hope to have more of those in the shareholder funds to utilize the investments there. The important thing that we're looking for is investments to meet our target rate of return. But those that also can support a social purpose agenda and also the synergies that we can get out of those investments themselves.

A further example is sale and leasebacks which we put into the annuity funds. And those themselves have created synergies to allow LGIM to be able to create products that it can sell to its existing client base, who themselves are looking to go into direct investments themselves.

So the shareholder funds and annuity funds are both there to create synergies and to increase risk-adjusted returns. But also to support the organic growth of the Group itself.

Q - Jon Hocking {BIO 2163183 <GO>}

Sorry, can I ask a follow-up on that? So to what extent are you going to end up with a similar asset mix in shareholders' funds as the assets backing annuity liabilities? And if so, does that not -- is that not sensible given the fact you want to have your shareholder funds uncorrelated from the risk in the annuity fund?

A - Paul Stanworth {BIO 15495409 <GO>}

Yes. I think the target portfolio we're looking at for shareholder funds is going to have a different term profile to the annuity funds. The key thing to recognize is that we have a very, very liquid portfolio currently against a very illiquid balance sheet and that illiquidity has benefited the banking sector to date. We would be looking for investments which could have slightly different correlations to the annuity book. We're not looking to match the interest rate sensitivity or to create a cross section of the annuity fund in the shareholder funds. But to use the shareholder funds to take advantage of direct-investment opportunities that suit the -- a shorter-term requirement than the shareholder funds have.

A - Nigel Wilson {BIO 1535703 <GO>}

I think again, we may at some point hold an investor breakfast and go through in a lot more detail some of the -- part of the detail is covered in the Report and Accounts. We give quite a lot of detail on it. But I think there's an appetite probably for some of the people in the room for an even deeper exploration of actually what assets that we're investing in the two different parts of the business. To pick up your last point, it's a very relevant point, Jon, we don't want them perfectly correlated. And indeed that's part of the job of the team, is to make sure they're not correlated.

Mark, you want to pick up the --?

A - Mark Zinkula {BIO 16142450 <GO>}

Yes, certainly. Active Equities. So we have had an active Equities business for a number of years. We haven't talked a lot about it because it hasn't been that successful. It has primarily focused on the retail market. And we're repositioning the business right now to move away from strategies that are index-plus oriented so we're not competing directly with our passive business and other strategies that just aren't really consistent with the LGIM brand.

So we've had a variety of hedge funds that were launched in the past and we've closed down all of those over the past couple of years. So we are refocusing those resources to be -- I won't [ph] say now. But we're going through a process that's involving a lot of individuals on the team. So we're being careful what we state now and we'll share more once we get through that process. But ultimately have a set of strategies and investment process where there's clearly an active component that can't really be replicated in a passive format that would also be very complementary for the product set we are developing, particularly for the DC space and then could also be sold in the private wealth space and in the institutional space. So in addition to retail.

So ultimately, having a team that's probably going to be -- probably end up being slightly smaller, more focused and more focused on those types of strategies conceptually. And we'll provide more details once we work through the process that we're going through internally.

A - Nigel Wilson {BIO 1535703 <GO>}

And again, being a destination of talent. Lance Phillips joined us from Standard Life and has made a very positive and significant start to the business here.

And next questions, please.

Q - Unidentified Participant

My first question actually dovetails --

A - Nigel Wilson {BIO 1535703 <GO>}

How many have you got first, Greig?

Q - Unidentified Participant

Yes, I was going to do three questions. But it dovetails -- it's actually two because you didn't answer the dividend question. But what I was interested in knowing, I do appreciate the Solvency II regime is heading to a more favorable outcome. But isn't it fair to say that your writing agency model is also a key constraint? And would that prevent you from -- under that regime, would you have surplus capital? I'm just trying to understand -- Solvency IV's away. But then the rating agency model is the constraint.

The two other questions is one is from the city. I wonder if you can just give us an idea on the strain that we will expect on that in the second half or release -- sorry, release and the EV margin on that.

And the third question is I was just puzzling, you had 15,000 deaths. I was wondering what percentage have linked underwriting data, enhanced and impaired underwriting data, because isn't it fair to say that most of those 15,000 deaths aren't very useful in the enhanced and impaired space? I was just trying to understand what percentage is actually linked to decent underwriting data.

A - Nigel Wilson {BIO 1535703 <GO>}

The last question has no interest in partnership, presumably. I didn't quite get the dividend question in there. But I'll maybe talk a little bit about --

Q - Unidentified Participant

Is the writing agency a constraint (multiple speakers)?

A - Nigel Wilson {BIO 1535703 <GO>}

No. It's never been an issue for us before, Greig. I know it's a new question for us. But it's not one that we feel as though -- we did get upgraded recently, as you're aware, in

America on the rating agency side. But the Solvency II regime is heading to some sort of solution. I think everybody in the room probably expects that to be a much more positive solution than where we were three or four years ago. Our ICA capital surplus is bigger than our IGD capital surplus. So we're not being presumptuous. But we assume we'll be in a very strong capital position and continue to be in a very strong capital position going forward.

But you can't be certain until the -- all the Is and Ts are dotted and crossed. So we are being watchful of that. And one of the things that we've done in the last few years is create this huge headroom and buffer in case there's any macro shocks that we're not expecting or any regulatory shocks. We haven't seen any of them.

The technical question, the question on strain is -- do you want to --?

A - Mark Gregory {BIO 15486337 <GO>}

Just quickly, we didn't give precise details in terms of the actual how it's going to play through in the IFRS accounts. But we did reiterate when we announced the completion of the deal yesterday that given prospective releases on capital and reserves we are going to be -- we will have paid just over 50% of the embedded value for the transaction. So I think (inaudible) we are expecting there to be a surplus in the second half of this year on annuities.

A - Nigel Wilson {BIO 1535703 <GO>}

And I don't know whether -- it's -- I don't know whether you can answer that question, Kerrigan. But I'll give it to you anyway.

A - Kerrigan Procter {BIO 15093363 <GO>}

Well, I guess I'll pick up on the point on data. Just characterizing what we have in longevity, we have fantastic capability in what are called big data, informed by experts. So the big data capability is really statisticians and programmers in-house to really crunch and analyze that data, informed by medical longevity and actuarial experts internally. And then externally that's complemented by our university links. So particularly UCL. And then that's overseen by an expert panel of longevity science advisors, chaired by Dame Karen Dunnell. So that's a very formidable beast. If you feed that formidable beast with data and point it in the right direction you get very robust results indeed.

In terms of the specific data question that you have there, 15,000 deaths per annum, though that gives us a great understanding of ultimate mortality, unless we deploy that formidable beast on the broader sets of data that we can get that include medical data and cause-of-death information then I think we've got a very strong capability indeed to build our capability in the enhanced market.

A - Nigel Wilson {BIO 1535703 <GO>}

John, is there anything you -- given that you are one of our mortality and longevity gurus around here, anything you would like to add to that?

A - John Pollock {BIO 6037447 <GO>}

Well, I think, Kerrigan, for a new boy, did a -- that was a pretty good answer, to be honest. No, I don't think there is much to say. Our data capability is, we believe, more substantial than anybody else's in the market. And as Kerrigan alluded to, our -- the science that we have undertaken to go around selecting or applying to our selected pricing is based on that big data. Others claim all sorts of impressive statistics. If we just look at the facts, we have 30 million annuitant years worth of data and are very, very solid in our pricing.

Remember, enhancement, we started it in the scale market with postcode pricing. So any increase to an annuitant beyond standard rating is an enhanced annuity. It's not the narrow definition that's currently being bandied around. And we were very confident at that time in our capability to price that on the back of our data.

So no, Kerrigan gave a comprehensive answer. Well done. Well done.

A - Nigel Wilson {BIO 1535703 <GO>}

If I can move around the room a bit. I've been very focused in one area for the moment.

Q - Oliver Steel {BIO 6068696 <GO>}

Oliver Steel, Deutsche Bank. I find the questions I really want to ask you're refusing to answer. So I'm going to try again, first to John in terms of the synergies within LGAS. Okay. So you're not going to give us some numbers. But I wonder if you can just talk in a little bit more detail about where the synergies are, at least in terms of revenues. And perhaps give us a little bit more of a hint as to where they are in terms of costs.

Secondly, on the dividend issue and Solvency II. And it's linked to my third question, which is you have, as you say, more of a surplus under ICA than under IGD. You're looking to spend, I think you said at the start of the year, between GBP0.5 billion and GBP1 billion on acquisitions. But actually the acquisitions you've made so far I suspect are barely covering the level of excess cash generation you're making year to date. So I'm just wondering -- let's pin that down to two questions. Is any dividend re-basement likely to include capital as well as reducing the cover?

Secondly, on the acquisition front, are you actually able to find sufficient acquisitions to cope with the capital and cash generation you've got?

A - Nigel Wilson {BIO 1535703 <GO>}

John, do you want to talk about the synergies? Mark, do you want to pick on the dividend? And I'll pick up the acquisition.

A - John Pollock {BIO 6037447 <GO>}

Yes. It is fairly early days to give any detailed thing. So we're not ducking the question, Oliver. The kind of synergies -- we did talk a little bit about a very obvious one in workplace savings, where as we're seeing schemes transition to the new form of workplace savings so we are picking up quite substantial opportunities in our Group protection business. So we have seen Group Life -- you saw 44% increase in Group Life. We've also got opportunities there for the workplace rehabilitation stuff that we've been driving. Now, bringing the two businesses together creates a single capability for proposition development with employers. So that's just a narrow single example.

All of our digital work that we are doing, clearly customers engage with us digitally. What we had been doing was driving more product-specific digital solutions that we are now bringing together in a single coherent form and that it is our intention to underpin that with the Cofunds technology and build out from there into a customer-centric set of services that allow people to -- I prefer the term cross buy rather than cross sell. So we are enabling capability and we can deliver that through. Now, all of those things will emerge and we will talk about them increasingly as we go forward.

In terms of cost synergies, it's obvious. You bring two businesses together, supporting functions, all of the capabilities that we had built, to have two big divisions. We can find synergies there. And also, as I alluded to in my speech, all of the things that have been driving the need for cost reduction, we can bring single solutions, single digital, single IT capabilities that drive lower needs for specific solutions being developed on a product-by-product way.

So Andrea's got a whole program or work. And we will bring to you -- we will give much more specific targets, goals and aims when we talk to you in October.

A - Nigel Wilson {BIO 1535703 <GO>}

Mark, do you want -- we'll have our third go at the dividend.

A - Mark Gregory {BIO 15486337 <GO>}

Yes. Just (inaudible) questions around how we think about stock, how we think about flow and acquisitions and dividends and the way it all plays out. I think fundamentally I do see dividend as being a fundamental link to the flow and I do see M&A primarily linked to the capital stock and the use of that. So clearly those things are not permanent forever. But in terms of the way I think about the underlying exam question that's the way I come at it. As Nigel says, we will try and offer greater clarity at year end. We are seeing more close [ph]s on Solvency II. But all I would say, we have had false dawns in the past where we take two strides forward and three strides back again. So we'll -- but we think this time around there might well be some greater clarity beginning to emerge.

In terms of your point around -- and I'm not spending to eat your capital stock up. Clearly, the capital surplus on an IGD basis was flat year on year at GBP4.1b. And within that you're seeing GBP0.5 million of net cash production and that being spent, GBP140 million on the dividend, GBP135 million buying Cofunds, about $100 million providing temporary capital for our XXX reserves in America. So in some ways we are spending some of the capital stock. But as you say, it's pretty stable at this point in time.

A - Nigel Wilson {BIO 1535703 <GO>}

I think the -- just to give you a bit of -- one particular data point, when David Prosser was Chief Executive the cross selling in this Company was 1.11. After 15 successful years we've driven it up to 1.12.

A - Unidentified Speaker

(inaudible).

A - Nigel Wilson {BIO 1535703 <GO>}

1.13. Okay, 1.13. We've outperformed by a huge amount. But there's a very large potential. And I think one of the things that the team has done is really act as a team increasingly. And there's a great deal of cooperation across the Group. And it's a metric. Whether you call it cross buying or cross selling, it's a metric that we're increasingly going to measure across the Group and incentivize because incentives drive behavior. And the behavior at the moment is incredibly positive across the Group and we'll capitalize on that. And we're seeing customers who want us to do that. And one of the great successes of Mark's business on LDI is we've done a lot of cross selling to customers in that space.

On acquisitions, you seem to be implying that Wadham's not pulling his finger out enough. He's only done three deals in three months. And he's here today when he could have been out there doing some further work. So if you want to give him a hard time afterwards I'll -- that'd be good to do.

But we are seeing a much better deal flow across the world at the moment and more opportunities. But we're being very selective. And we've already said that we're not buying SWIP, we're not buying the Co-Op. There's lots of things that we get rumored to be buying in the newspapers that we're not buying. We're very much trying to stay very disciplined to the five growth themes and stick very consistently to them across our business.

Q - Gordon Aitken {BIO 3846728 <GO>}

Thanks. Gordon Aitken from RBC. I'm going to follow on on this dividend point. But you've made the comment and -- about the dividend and Solvency II. And to make that comment you must feel there's an expectation that your dividend guidance is going to change one way or the other. So are you implying you're holding onto additional capital? And in your answer to this, can you include comments on the corporate bond for provision which still exists? Now, I reckon cash cover is 1.8 times, IFRS cover is probably 1.7 times. It's still higher cover than some of the big corporate pension writers in the UK. So what is the right level of dividend cover in your view?

A - Nigel Wilson {BIO 1535703 <GO>}

I think it's a personal view and not yet a Board view. I think the Board have said to Mark, can you come back after you've been Finance Director for a few months and articulate? I think I've always had a view that we could pay out more in dividends. We've had a very progressive dividend policy for a number of years now. If you look at your own forecasts and analysis of our dividends they've been much behind what we've actually paid out, in part because our operation cash and net cash has been much better than we thought.

We've said we're going to unwind cover. The specifics on that, we're not going to give them today. It's very unfair on Mark. He's only been here a few weeks doing that job. We will absolutely give it in March. We're expecting Solvency II to not end in tears.

I think Carl Dowthwaite's here and John Godfrey, have done an outstanding job on articulating the industry position, along with the treasury and the PRA. I'm very happy with the direction of travel that it's going on. We don't know that for certain because there has been, behind the scenes, all sorts of changes in Solvency II, as we think before we've been heading for a solution.

As we get clarity -- you're just going to have to wait until March. Your own models. And yours in particular, has proven to be reasonably accurate at this moment. So you should pat yourself on the back and say you did a very good job of getting it right and trusting us that to the extent that we can deliver accelerating dividend growth, we will do.

Andrew?

Q - Andrew Crean {BIO 16513202 <GO>}

Andrew Crean, Autnomous Could I ask three questions? Firstly, could you expand a little bit on your conference on Solvency II? Because as I understood it EIOPA came out, they granted the matching premium method. But it was so restrictive that I thought a lot of the UK companies were unhappy with it. I know we're undergoing discussions at the moment. Are you just indicating that those discussions and EIOPA's response to those discussions is helpful?

Secondly, on LGIM, the switchback in risk-free rates from May, could you just give us a bit of comment if that were to persist and continue and we were in a changing higher-rate environment how you'd see that for your business?

And a couple of detailed questions. What was the weather in the first half relative what you'd normally expect for GI?

And secondly, what -- this change around in the shareholder funds portfolio yield, what are you expecting the portfolio yield to increase to?

A - Nigel Wilson {BIO 1535703 <GO>}

Yes. Well, I'll give my weather guru, Mr. Pollock, some time to prepare the weather question. And afterwards, if you've got some very technical questions, Carl is here, sitting in the front row. He can go through in a lot of detail.

But your overall governing thought was really EIOPA gave a position, a very technical position. It's then thrown open to discussion and debate. And the key point I think that we're seeing is that the regulation is reflecting economic reality and then the drive for growth. We always felt the original Solvency II solutions were designed for a different era, if you like, to prevent a financial collapse of the system. And I think people are looking at us and companies like us to perform a much wider role in terms of the State Welfare Reform and economic growth in particular. So we do expect the matching premium and various other adjustments to be made away from the original EIOPA proposals, which I always think were a technical solution rather than the ultimate commercial solution. But Carl can go through some of the more technical details around that afterwards.

Mark, do you want to comment on LGIM? John, if you pick up the one about the weather. And Paul, you might have another go at direct investments.

A - Mark Zinkula {BIO 16142450 <GO>}

If rates continue to trend up I think you have to look at the nature of our client base. So the vast majority of our clients are invested. And whose behalf we're investing in fixed income securities, are pension plans that are liability passed to the other side, if you will. So, as rates increase that would cause more plans to accelerate de-risking strategies, especially if the equity markets stay at reasonably elevated levels. That will help the funded status situation. So that would increase demand, actually increase demand for fixed income and other investments. So we wouldn't expect there to be a lot of outflows as a result. [ph]

In the retail space, where you have a much smaller percentage of holdings, there tends to be a backwards contraction [ph] oftentimes with asset market movements. The flipside though is that obviously it would put downward pressure on AUM and reduce our fees accordingly. So there's a natural offset, if you will. It should generate more business. But the AUM would obviously go down as rates go up.

A - Nigel Wilson {BIO 1535703 <GO>}

John, do you want to talk about the weather?

A - John Pollock {BIO 6037447 <GO>}

Yes. Like all of the risk businesses, we tend to have a real -- one of these big data models. So we look really, really carefully at long-term trends, averages and deviation from that, look at the incidents and impact of flood, freeze. And I can say with absolute confidence, from studying the weather in the first half, this year versus everything else was better.

Q - Andrew Crean {BIO 16513202 <GO>}

It's not such a silly question actually.

A - Mark Gregory {BIO 15486337 <GO>}

No, it's not. We're probably somewhere slightly -- maybe just a touch. I would rest in the low teens on core, something of that order, better than normal run of events. So we do have a normalized expectation of weather. And clearly, 81 core, we were massively inside that normal. Now, we'd say at this point of the year we're probably low teens better than the norm. Sorry for having a laugh at your expense.

A - Nigel Wilson {BIO 1535703 <GO>}

Paul, is there anything you want to add on direct investments that we can help?

A - Paul Stanworth {BIO 15495409 <GO>}

Yes. What I would say on the direct investment side is that the shareholder funds, as I mentioned, are in very liquid assets at the moment and because of the general state of the market the returns are low. If we were able to select a third of the shareholder funds to increase the portfolio returns by just 1% then we would have another GBP20 million coming through in shareholder funds. Yes, just if you take roughly a third of the GBP4.5b.

The way that we're going to approach it is that we're not going to approach it by setting volume targets. And the reason is that we're looking for incremental value with the direct investments. Our concern around volume targets is that you may -- we may compromise the quality of the assets that are coming into the portfolio. And we've created a discipline around an independent valuation of the risks that we hold in all our direct investments because it's an underwritten model and not a trading model. And we're keen to make sure that we're selling scope to put our assets into that portfolio but not setting targets so that we're rushing into investments that we don't think are incrementally a good value in the long term.

A - Nigel Wilson {BIO 1535703 <GO>}

Thank you. I think we -- one last question around. Why don't you ask the last question and I'll sum up?

Q - Alan Devlin {BIO 5936254 <GO>}

Thanks. Alan Devlin from Barclays. Just a question on your LGIM pipeline. I think you've had GBP8 billion of flows in the first half, which is more than you did in the whole of last year. And what the pipeline is looking, certainly given your comments on higher interest rates leading to people more likely to de-risk pension funds on the LDI side.

And then the same question on the bulk annuities as well, higher interest rates leading people to de-risk. I think you said you had GBP500 million of premium already in the -- in July.

And then the third question on auto-enrollment, if you could comment how close in auto-enrollment you are in workplace pensions to breaking even. And if you included all the cross-sell opportunities as well from auto-enrollment through the Group business or LGIM, the default fund side or selling annuities eventually, what's the economics of that business like in total for L&G? Thanks.

A - Nigel Wilson {BIO 1535703 <GO>}

Yes. Which order are you going to take them in then? I lost the hand signals there.

A - Mark Gregory {BIO 15486337 <GO>}

I'll do the workplace one.

A - Nigel Wilson {BIO 1535703 <GO>}

Yes. If you do LGIM sales.

A - Mark Gregory {BIO 15486337 <GO>}

(multiple speakers) do the LGIM sales one and you do the annuities one, Kerrigan.

A - Mark Zinkula {BIO 16142450 <GO>}

In regards to the pipeline. So, yes, we did have a fantastic first half of the year, we had a good Fourth Quarter of last year. So (inaudible) excellent. However, as I recall, last year, August, we laid an egg. It was quiet. So I don't want to jinx us. But the pipeline continues to be strong.

We're definitely continuing to gain traction, gain momentum in the US business. Performance is absolutely excellent and the pipeline remains strong there. As you saw, we're starting to get more traction now in expanding our index business beyond the UK. As Nigel has pointed out, I think at least twice, that our DC asset growth, we need to see more acceleration there. We're taking several steps to do that.

So I do feel reasonably confident that we continue to have strong gross inflows. However, we're also seeing, the last few months, more elevated outflows as well. So those plans of de-risking, that causes -- it puts more pressure on us to retain those assets since not all the plans will de-risk with us even though we've taken a lot of steps. I think we have a very good plan in place to retain those assets, either with LGIM or ultimately into Kerrigan's business and still retain the assets within LGIM within that sense. But ultimately, as rates go up that does put more pressure potentially on outflows as well.

A - Nigel Wilson {BIO 1535703 <GO>}

Mark, do you just want talk about auto-enrollment?

A - Mark Gregory {BIO 15486337 <GO>}

Yes. Your point, Alan, about the growth and breakeven on workplace. And we've got GBP7.3 billion now on our workplace pensions platforms. That's GBP0.7 billion of net inflows in the first half of this year. So we are getting there. But I think, as I said in the past, we are going to need probably we think low early double-digit billion on the platform to get to that breakeven. But we're not seeing it as being -- it's just not a point in time of getting to breakeven.

Clearly, it's been a long-term value creation opportunity. It's not just about -- clearly we want to get to breakeven. That's obvious in first principals. But we do see it as being a source of potential long-term value.

On your wider question around is there downstream value? I've said we don't price for it on that basis and we absolutely -- we price -- underwrite all the schemes based on actual dynamics purely in terms of what it means as a workplace scheme in isolation. But you're right to say actually a lot of the assets do get managed by LGIM. I think it's up around 90% of the assets we've acquired in (inaudible) have gone into the LGIM funds. And subsequently, down the track, we would expect quite a lot of those to annuitize with Kerrigan's annuity products. But we don't price on that basis.

I have to say I haven't actually worked out what the downstream value might look at to see where that would get us to the mythical breakeven point. But it certainly would be helpful, Alan. It can't be unhelpful because clearly there's value downstream which we're not currently allowing for in our accounting.

A - Nigel Wilson {BIO 1535703 <GO>}

I think in general it's really about execution. The pipelines are all pretty full. And it was notable the other day in the US we had a great success because Mr. Zinkula went along to the pitch and did such a fantastic job that the client decided to buy there and then. So we're lending a bit of a hand to it. The annuities pipeline is very full here in the UK, both for standard deals. But also for longevity and insurance. And we're increasingly looking at Holland, the Netherlands -- sorry, Holland, Ireland, Canada and the United States, where we've been doing research for about 18 months, two years to see whether there's opportunity. We saw very measured response to those areas.

Just in summary, there's a great quote at the back on new business from Dave Realson [ph], who's very kind to let us use that quote. But also a very nice photograph of himself. Because it's all about execution. And we really see the chance to move Legal & General forward is really about how well we execute. The opportunities are all there. The regulatory economic environment is improving and we've identified five growth areas, which at the moment the macro trends are resulting in winning strategies. We've just got to continue to execute very well. We definitely see ourselves as test match cricketers rather than 2020 guys. It is about ones and twos and building a big score gradually.

And just really I'd like to thank Kate. Kate's been doing IR for some time and sadly she's been poached away by Andrea to form part of her team in driving together the savings and protection businesses with John. And I hope she makes such a significant positive contribution in that area. And we'll be announcing some changes to that in due course.

But thank you again for all of your support. Legal & General is very much still a work in progress. We're not being complacent about the performance we've had in the last few years. There's a lot still to go for and we're pretty determined to execute the plans that we have, the very ambitious plans that we have for growing the business. So thank you.