S1 2011 Earnings Call

Company Participants

- Andrew Moss, CEO
- Igal Mayer, CEO, Aviva Europe
- Patrick Regan, CFO
- Trevor Matthews, CEO, Aviva UK

Other Participants

- Andrew Crean, Analyst
- Andy Hughes, Analyst
- Greig Paterson, Analyst
- James Pearce, Analyst
- Jon Hocking, Analyst
- Marcus Barnard, Analyst
- Nick Holmes, Analyst
- Paul De'Ath, Analyst
- Raghu Hariharan, Analyst
- Toby Langley, Analyst
- Tony Silverman, Analyst
- Unidentified Participant, Analyst
- William Elderkin, Analyst

Presentation

Andrew Moss {BIO 3628034 <GO>}

Okay. Good morning, everybody. Welcome to Aviva. Thanks very much for making time to come and see us, to talk about our 2011 preliminary results.

Before I start, an introduction, actually. We have here Colin Sharman, our current Chairman. Actually, this will be Colin's last session in terms of results announcements. But with him John McFarlane as well, who takes over as our Chairman in June of this year. So great to have John with us.

Right. Now, what we want to do this morning is just talk about, I guess, three things. First of all, I want to give you an overview in terms of operational performance, and a strategic update as well, so talk about progress from a strategic perspective in 2011. I'm going to ask Pat, as normal, to take us through the financial results in some detail. And I know from some of the discussions already before there are two or three things in particular that you're interested in. I think we'll face straight into those things and give you some detail.

Then I'll come back and talk about prospects for 2012, which I think is actually a year of considerable change facing the industry, particularly here in the UK. So I think good to have an opportunity to talk about those things.

Now, worth stepping back and just saying what were our objectives for 2011, and I think they're just listed on this slide. As always, improving operating performance, and as part of that I think just continuing to sharpen focus in terms of capital allocation, making sure that we're allocating capital to those markets where we can grow and earn higher returns.

And from a strategic perspective, clearly we set out our stall in late 2010 that we were going to do some work to simplify the portfolio. And I think with Delta Lloyd, with the RAC, with our Central and Eastern European operations, we've made some good progress on that in 2011.

And as always, particularly in the volatile markets that we've been operating in again, maintaining balance sheet strength, maintaining capital strength has to be an overriding priority for, I think, all insurance operations, and of course that counts Aviva amongst them.

So that's what we were setting out to do. And if you look at the backdrop, particularly the second half of last year, you have to say it was quite tough. It was pretty volatile. This slide shows you what happened to sovereign yields in Europe, particularly in the second half of last year. Equity markets moving around, equity volatility going up very markedly in the second half as well, and corporate credit spreads as well playing their part in a pretty volatile environment.

And when Pat talks to you about the capital position in particular and just explaining the effects of that on the way that clearly it had a downward move on capital in the second half of 2011, much of that's come back already. And it's something we were staying very close to and taking particular action on and around all through that period.

So I think against that backdrop, the results that we're reporting today I believe are very creditable. The operating profit just above GBP2.5 billion and on a continuing basis up some 6%. The result of that focus on capital allocation, life internal rates of return going up by more than a full percentage point to 14.4%. Combined operating ratio continuing to track downwards. Very strong current year performance in our general insurance businesses.

And worth noting, actually, that if you look at the global insurance market, 2011 clearly in terms of catastrophes was a very, very serious year. So whether it be Australian floods, New Zealand quake, Thai floods, a number of other events, including of course the tragic events in Japan last March, all of those things affecting the global insurance market. We expect reinsurance rates to be higher as we renew our big cat program this year. But Aviva's particular focus on personal lines and the geographies within meant that with obviously a degree of luck we were not affected by any of those particular events.

Now, the next number, I think a particular important number, operating capital generation. We'd set some targets for that, which actually started out at GBP1.5 billion for the year, and we've come in at GBP2.1b. We upped guidance, if you remember, throughout last year on that number. But it is a strong number. And I think when you look at it, if you strip out the head office costs and debt costs as well, leaves you at about a net GBP1.5b, which broadly covers the dividend 2 times.

Now, that is a big change. It's doubled, that number, in the last two years. But that hasn't happened by accident. Very much because of actions that we've taken, making choices about business that we write, supported then by increasing profitability in the business as a whole.

And the balance sheet remained reasonably stable through the period, the IFRS net asset value there coming down a little bit to GBP4.35. Actually, as we stand here today, with markets doing what they've done in the first couple of months of the year, it's back at that GBP4.54 or just above level. And again, Pat will talk you through those movements in more detail.

Now, all of that has underpinned a decision on the dividend, to increase it by 2% for the year. And I think you can summarize our thoughts on the dividend by saying very, very pleased with the strong operating capital generation, which gives us confidence in terms of the dividend being absolutely sustainable, ready to grow, but at the same time in terms of the macro environment and the uncertainties we've seen in the course of the last six to nine months, a measured approach in terms of the final dividend.

Now, if we just disaggregate it a bit, talk about the Life business and then the General Insurance business and perhaps just look at some longer-term trends, I'm really pleased with those trends that you can see on these slides. The operating profit going up from GBP1.6 billion two years ago in the Life business up to GBP2.1b, and broadly based growth across our geographies.

And the net operating capital generation, here's where the big moves are. Choices that we've made about businesses that we've written in the course of the last couple of years, particularly pulling back on Italian with-profits business in the course of the last couple of years, really making a difference in terms of the amount of capital that we're investing in new business. And that is what is driving the IRR up, as you can see in the bottom right-hand graph.

A similar trend, actually, in the General Insurance business as well. So again, a broad-based increase in profitability, the combined operating ratio heading downwards below our target of 97%. And what is really pleasing about that is that we've been growing into that more profitable market, so sales going up strongly.

We've seen growth in European markets, we've seen growth in our Canadian business, and particularly in the UK market where we have actually quite aggressively grown into a stronger market in UK Motor. So another, I think it's 413,000 UK motor customers coming onto the books in 2010 -- '11, sorry, following about the same in 2010. So over 2 million motor customers now here in the UK.

Now, I mentioned the UK, and as always we start there when we start looking at the business. I think the two businesses in the UK have really had a very, very encouraging year, on the back of very strong brand recognition. I've already talked about all those new motor customers. You don't get that without competitive pricing here in the UK market.

And on the life side, driving up market share in individual annuities, certainly number one in that market now. And continually growing market share in protection. And that's on the back of the next line here, which is strong distribution reach, 9,000 IFAs, important. But a lot of that protection business coming through our banking relationships, with the likes of Barclays, RBS and Santander coming on-stream in 2011.

And great to see actually some external recognition of what's happening in our UK business, winning UK General Insurer of the Year again, first time for a couple of years. Really pleasing for the team to win that award. Best Pension Provider of the Year. For the second year running, UK Health Insurer of the Year. So it's always good to get that third party recognition, but actually it's when you look at the hard numbers I think that the story, if you like, tells itself.

The Life IFRS operating profits up to GBP920m. That's double what we were making in our UK Life business six years ago. So that upwards trend I think has been pretty continuous and obviously very encouraging. And it's really simply on the back of taking cost out of the business, making the business more competitive, making our pricing more competitive in the market, writing business in annuities and protection, which are higher-margin products, and it shows through in the bottom line.

And sales are up. The UK economy is challenged; we all know that. But in the areas that we want to write business, we are doing so. That's in annuities and protection, which I've already mentioned, but actually over a 60% growth in our Group Personal Pensions business as well, very important as we head towards the next year or two and also enrolment.

And the internal rate of return, here in the UK market some people say it's not a profitable market. We don't agree. If you can write business at 15% internal rates of return in the volume that we're writing, we think that makes for a pretty attractive business in a pretty attractive market.

In General Insurance, outside of the RAC, which of course is no longer part of the Group, an 11% increase in profitability, and net written premium up by 10%. So growing into those stronger areas of the market, such as personal motor. And a combined operating ratio staying flat at 96%, but just remember, please, that that's taking out the RAC, which used to help that combined operating ratio number to the tune of about 2percentage points here in the UK.

Let's turn to Europe. In the second half of last year, we spend an awful lot of time talking to third parties, investors, you, about what was going on in Europe and how it was affecting us. But I think what's really pleasing is that our big businesses in Europe in profit terms did actually very well in the year.

So France still our biggest contributor, nearly GBP500 million of profit. Very resilient life result. The bancassurance relationship with Credit du Nord growing in terms of profit. Margins looking good. And internal rates of return going up substantially, particularly as we change some of the guarantee structures in our AFER distribution relationship. And that was all backed up by a strong General Insurance result, helped year on year by the non-recurrence of some weather events in 2010.

Moving down, Spain, perhaps the most interesting example of what's going on in our businesses in Europe. We all know that Spain is going through a very difficult economic period and that is not going to change any time soon. At the same time, we have a business which is still relatively young. Reserves are growing. We're still selling a good amount of protection business, so we're seeing record profitability coming through the business.

Poland held up very well, our Pensions business constrained now by some government changes that were made a couple of years ago. So we've redirected the direct sales force very much towards protection business, and that's been very successful for us.

More challenged, without a doubt, particularly in terms of consumer demand, has been Ireland. Clearly the Irish economy is still in a difficult place. And to a lesser extent in terms of demand but obviously in terms of the macro effects of what's happening, the Italian business. Actually, what we've done is take some pretty decisive action in both places, first of all, in Italy, decreasing volumes of lower-margin with-profits business, and in Ireland actually taking more radical action, moving the Irish business under the umbrella of the UK business, so combining it with the UK to improve profitability.

And I'm pleased to say that the latest reaction we've got from IFAs and from brokers in Ireland around the increased product range and the depth of capability that we have coming out of the UK business, combined, frankly, with a lower cost of production which will flow through to pricing, is very, very positive. So that now, I think, moving absolutely in the right direction.

Then, just to prove that Europe is not homogenous, that there are different countries moving at different paces, Turkey in particular I think is a great example of that. Okay, low profits at the moment, but a young business which is beginning to turn upwards into profitability, a market where very underpenetrated, a very young population, so real growth characteristics and a very strong market position that we have there.

So the overall picture then on Europe I think is, yes, it's been tough, but actually the business has shown its resilience. Operating profits just up a touch, sales down a little bit because of the action that we've taken, primarily in Italy, but profitability of new business going up, above 14%. And actually quite a marked increase in General Insurance operating profits, helped, as I said, by the non-recurrence of some weather events in 2010.

If we move across the Atlantic, talk about Canada and the USA. Well record profits in both businesses. So Canada reporting GBP254 million of operating profitability, up some 14%, net written premium growth, the combined operating ratio coming down. I think an excellent performance, paying very strong dividends back here into the UK. So a good business, growing and doing well.

And the US business, which of course we've been managing for profitability over the course of the last couple of years, and with a strategic objective of making sure that it pays dividends back to the UK, well, it's absolutely doing that. Profits doubled in 2010 and they're up a good solid 13% again in 2011.

To do that, we've had to moderate annuity sales, get the balance right between value and volume, and I think the team have done a great job on that. And you can see that in the profitability of new business, with the IRR up above 14%.

Then turning to Asia Pacific, again, I think a very positive story. In fact, to be honest, I think one or two of our businesses in Asia Pacific have outperformed even our expectations in the course of the last 18 months or so. So across the region you can see sales continuing to trend upwards.

And IRRs, really over the last couple of years a step change as we've written more business, some different product mix to improve profitability of new business, but that business being spread over essentially a fixed cost base in the Asia Pacific region, leading to that marked increase in IRRs over the last two years.

And the profit signature of the business beginning to really change. These are young life businesses which we've invested in organically over the last six or seven years, and that costs you money upfront as you're investing, but as the profit starts to come through then clearly you see that different signature. So two years ago a loss of GBP30m, now a profit of GBP45 million on an underlying basis, with good growth characteristics going forward.

Now, lastly, in terms of a tour round the businesses, we should talk about fund management and Aviva Investors. And I would describe the profit outturn for the year, basically flat in the fund management activities, as a solid performance in what clearly was a difficult market.

You will have seen, a few weeks ago, we made some announcements about some changes at Aviva Investors. That's actually a microcosm of what we've been doing across the Group, so focusing on what we do well. So for example, we're still managing UK equities in London and European equities out of Paris. What we're not doing any more is managing, for example, European or emerging market equities out of London. That will see something like a 12% drop in the workforce at Aviva Investors. So that of course is geared towards improving profitability as we go forward.

But the main strategic objective that we've had in Aviva Investors over the last couple of years is to continue to grow third party sales. And that trend you can see on the right hand, whereas we were losing third party customers two years ago, actually a net GBP5.6 billion of inflows, gross GBP12b, something like that, in 2011. That's an encouraging trend. It's a record, actually, for Aviva Investors business, and clearly we want to see that continue.

So that's all 2011. I think it's worth just stepping back a little bit and looking at the change in the Group over the course of the last couple of years. So if you look at profitability of new business, up from 10% to 14% plus in the Life side. Combined operating ratio coming down, driven by current year earnings.

The operating capital generation, I mentioned it earlier, more than doubled in the last two years. And that's about improving profitability in the business, but it is also about choices we've made about what business we want to write.

More focus in the business. We were operating then in 30 countries; we're down to 21. So a significant change in the last couple of years. And that together with action we've taken to take out cost has driven the cost base down to around GBP4 billion on a run rate basis. It was GBP5.1 billion two years ago. It was actually GBP5.7 billion three years ago.

So these are significant changes. And headcount of course has played an important part of that. So we used to employ more than 57,000 people; we're down to the mid-30s of thousands, but still writing the same amount of business, broadly.

Capital is obviously a continuing issue for all insurance companies at the moment. Things are uncertain, with things like Solvency 2. I've no doubt we'll talk about it later. So driving up economic capital has been a priority for us. We did that leading up to the half-year. And having that strong buffer of nearly GBP7 billion of capital at the half-year served us well in what was a volatile second half.

And operating profitability, GBP2 billion two years ago, up to GBP2.5 billion today.

So I think all of that does demonstrate the change that we've seen in the Company, the very decisive action that we've taken to improve the overall profitability, capital strength and efficiency within the Company, making the Company fitter and stronger.

Okay. I'm going to stop there. I'm going to hand over to Pat, to take us through the numbers in a bit more detail, and then I'll come back in a moment.

Patrick Regan {BIO 15131018 <GO>}

Terrific. Thank you, Andrew. And good morning, everybody. Nice to see you all here again.

In terms of the framework Andrew referred to earlier, I'm obviously going to talk in a little bit more detail about the operating profit numbers, how we did the capital allocation and how we drove the increase in the operating capital generation, and then talk a bit more about balance sheet movements and capital levels towards the end.

Starting with the operating capital generation, as Andrew said, a 25% increase to GBP2.1 billion in 2011 on top of the 70% increase we saw in 2010. So overall, more than doubling over a two-year timeframe.

Just before I go through the component parts of that, just talking about what that's there to cover, GBP2.1 billion of net operating capital generation, about GBP100 million or so of corporate costs and GBP500 million or so of Group debt costs, pension, other bits and pieces. Those numbers are net of tax, as is OCG. So it gives you GBP600 million of deductions or around GBP1.5 billion to fund the dividend.

For those of you who think of things in terms of free cash flow yield, that's, what, about a 15%, 14%, 15% free cash flow yield compared to our 7% dividend yield or, as Andrew said, a bit over 2 times covered.

So how did we do that? Well we've talked a few times when we've been together about the block of profits coming from the in-force business. So if you rewind a few years, that was GBP1.6b, GBP1.7b; 2009, that was GBP1.9b. GBP2.1 billion growing to GBP2.3b. Why? Because we've got just shy of 30 million customers on long-term contracts. We're increasing our life in-force profitability, good retention levels, managing expenses, growing the in-force profitability in a reasonably predictable manner each year.

Non-life generation, you can't quite see it in the roundings here. That increase is a bit shy of GBP100m, again reflecting the work we're doing to grow, across the piece, the General Insurance profitability.

Non-life investment really as flagged last year. We had something of a one-time benefit last year in the reduction of the CRR for General Insurance, and that benefit has not completely gone away but muted somewhat in 2011.

So the last bit and probably the most significant bit of the story is the reduction in capital invested in Life new business, so a bit more on that. Remember, two years ago that figure was GBP1.5b, so a GBP600 million reduction over the last two years. Putting that into context, our sales this year, our Life new business sales of GBP28b, are actually pretty similar to the GBP28 billion of two years ago. What we're doing, though, is just writing that business in a less capital-intensive way, in a more profitable way for us.

As you can also see, by the way, average reserves have also gone up over that period, partly because a number of our businesses are actually still quite young businesses.

So again, how have we done that? Well it's a little bit from each of the businesses. Within the UK, we use about GBP200 million less capital now than we did two years ago, whilst growing that business about 10% a year. Why? Because all of our non-annuity business is written out of the reattributed estate and that's therefore incredibly cash-efficient for us.

In Europe, by making different decisions about product features, guarantee levels and net/net a lower amount of with-profit sales this year, while focusing on things like protection, we've reduced capital consumed by new business by about GBP100 million in Europe this year.

In US, we've talked about this lots, product feature changes, guarantee levels, a realign on pricing as we went through what was a continued and decreasing low interest rate environment, again has further reduced by another GBP100 million capital consumed in the US.

And whilst you can't see it on my chart here, Simon and the team have really been focusing on product profitability in Asia as well, and that shows up even more in the IRRs, and Asia coming in now at almost the Group average.

Moving on then to operating profit, 6% overall increment, and a few other movements, giving that 6% overall.

I'm going to talk in a little bit more detail in a moment on GI and Life, so picking up these other lines. Andrew's already talked to fund management. Other non-insurance costs, you've got our regional costs in there. The increase, though, is the non-repeat of a small pension credit that existed in 2010.

Corporate costs slightly declining, notwithstanding the fact that we continue to invest more in both risk management and capital management capabilities. Group debt cost marginally higher, reflecting the marginally higher average debt. And pension costs, on the other hand, coming down, reflecting the better position on the pension scheme surplus.

Just picking up Delta Lloyd at the bottom then, obviously that last year's number is 100% of their operating profit for the full year. This year is 100% till May and then 40% from that date onwards. As you may have seen from their results, their actual 100% operating profit went up slightly, and really that was the feature of them delivering -- actually over-delivering on their cost reduction program, particularly within the Life business.

So a little bit more detail. I'm going to pick up that Life result, growing from GBP1,988 million to GBP2,123 million and how -- and what drove that. Well very much the same as before, growing income at 5%, a little bit more than we're growing expenses at 3%.

Picking those apart a bit, new business income broadly flat at GBP1b. So what we see is a slight increase in the UK business, reflecting the growth there. And as you would expect, a slight decrease in our European businesses as we've been more selective of the business we're writing. Similarly, acquisition costs broadly flat, very much in line with that new business income.

Admin costs, again, as you remember, we measure these as a percentage of the in-force reserves, and as a percentage of the in-force reserves, marginally down. Nice story again in the UK, so that's 42 basis points overall for the Group. UK's now down to 30 basis points, so the cost of managing those in-force reserves. And a few years ago that would be well above 35 basis points. Europe now down in 2011 as well, now down to the Group average of 42 basis points.

Underwriting margin, again, we've talked about the feature, that comes from, what, six, seven, sometimes eight businesses producing more than GBP50 million each of underwriting profits. Again, that's very predictable underwriting profits emerging this year, with an increase in the expense margin within that.

So just a little more then on the investment return figure and what drove that 6% increase. Couple of features here. Growth in the unit-linked in-force reserves really coming through there. Couple of things there. We're writing more group personal pension business, as you may have seen, up 66% this year. And we also took the RBS joint venture assets fully onto our balance sheet.

On participating, two things. Last year we had the last of those special distribution incomes in the UK; it was GBP84 million last year. And that's offset by the continued growth of the in-force participating business, primarily within France, within Europe.

Spread margin, the average reserves there about half and half the UK and North America. In UK you've got about a 10% increase in average reserves. In North America you've got both an increase in in-force reserves and again an increase in that spread margin, something they've been really focused on for the last couple of years. And the combined effect of all of that driving that overall 18% increase in spread margin.

Moving on to General Insurance, investment return and underwriting result. On investment return, slightly declining yield, as you would expect. Average yield on the portfolio is around 4% at the moment, new money yield probably about 3.5%. Offsetting that is the growth of the business. We've seen UK's grown, Canada's grown, France has grown. So the reserves back in that business are now turned around and growing again, and hence the assets back in the business are growing, and that's offsetting the reducing yield environment.

The underwriting result growth is very much driven by the continued improvement in the current year result. You've seen our chart up here. Again, across the piece on that, very much in the UK, our 96% core very much driven by improvements in the current year, both on household and on motor. I'll talk more about motor in a minute. Similar story in Canada, very strong result on personal lines in Canada as well. And as Andrew mentioned, a strong French combined ratio result.

In terms of the overall prior year, if you look at the loss development tables, as I'm sure you will at your leisure later, overall a positive prior year position. We decided to take some small amounts of reserves, strengthening a couple of bits in the UK and a little bit in Italian Motor as well, but that's more than offset by the emergency of profit from that prior year. What we then decided to do was then rebook that in current year prudence [ph].

A little bit more than on UK Motor, a book that's grown from, what, about 1.2 million policy count two years up to over 2 million now. So how are we doing that? Well we introduced the Aviva risk index three years ago now. We use a mixture of questions we ask the customer and private data that gives us together a proprietary underwriting tool that we think differentiates our risk selection.

What that's meant over that period is we've decreased the proportion of higher-risk customer sales, the 1 to 3 customers, as we would categorize them, and then increased the proportion that's coming from the lower-risk customer sales. Typically, therefore, your slightly older drivers and away from the slightly younger drivers.

What that's meant over that same period is as the market much heralded increase in bodily injury frequency, over the same time period we've seen a decrease in bodily injury frequency flowing through the motor book and hence a decrease in our combined from 103 last year to mid-90s, about 96 now, with more of that to come through in 2012.

Okay. Now, switching to the below-the-line items, I'm going to do this in two bits, first those relating to Delta Lloyd. As you remember, last year Delta Lloyd benefited from the move in the Delta Lloyd curve to discount their liabilities. This year, as we saw at the half-year, that reversed. So that's the bit at the bottom there. Then a bit more detail on the bits pertaining to Aviva.

Integration and restructuring costs, within there you've got Solvency 2 costs, the completion of the Quantum Leap program, and a couple of bits of restructuring specifically designed to drive expense saves in the future, one in the European regional costs and one in Aviva Investors, as Andrew talked to you earlier.

On investment variances, a few things going on within there. Really, as you know, our investment variances are much more driven by bonds than they are equities. There's a small amount of equities, a little bit to do with our UniCredit holding within there. What we have seen is widening of about 60 basis points over the full year of corporate bonds, and that's affected the value of our bonds in both the UK, France in particular, then a little bit, a couple of hundred million, to do with widening of governance spreads in Spain and in Italy.

As you'll see in a moment, that corporate bond spread widening is largely offset in the NAV by the pension scheme impact. So they're almost equal and opposite impacts from an IFRS perspective.

Profit on disposals, obviously the RAC. Then within goodwill and amortization, run rate of about a couple of hundred million of amortization, with two additional items. One is we took about GBP100 million goodwill impairment in Ireland, reflecting the restructuring we're doing there and the ending of our relationship with AIB. And we also took the decision to write down our Delta Lloyd holding, remaining Delta Lloyd holding, from EUR17 a share down to its year-end share price value of EUR13.

Now, how does that translate into the NAV numbers? Well as I mentioned, on IFRS basis you see the -- whilst on one hand you have the impact of those investment variances driven by corporate spreads, that's almost equal and opposite impact offset by pension fund. So net/net, what you've got in there is profits flowing through, partially offset by the Delta Lloyd impact and then foreign exchange, in essence, the euro rate to sterling. Obviously, as a sterling reporter, that was a net negative for us versus obviously our European peers where that's a net positive.

Since year-end, as Andrew said, we've seen a reversal of those trends. Actually, corporate spreads largely offset by pension scheme and then some net positives on the euro and government spreads coming in.

In MCEV terms, just talking on the Fourth Quarter movements, really a couple of things going on there. Overall, our sensitivities reasonably well predicted the full-year movements, so corporate bond spreads widened about 60 basis points. So that gives you about GBP1 billion net of liquidity premium. Government bond spreads, again, a similar kind of number. Then the remaining movement is a combination of lower swap rates, a little bit on equities and a little bit on equity volatility.

In addition to that, you've got the Delta Lloyd movements, the Ireland write-down, as I mentioned. And within foreign exchange and other movements, there's about 10p -- a little over 10p of some modeling changes we put through to do with the US.

So when you're looking at the Fourth Quarter movements, government spreads widening gives you about a 20p impact, 10p to do with modeling changes and about 10p to do with those Delta Lloyd, Ireland, etc., moves.

EEV is obviously a much more stable number, ending the year about 6p.

As we've seen, obviously, on an MCEV business, real contraction on government yields since year-end, 7% for Italians at year-end, down to about GBP4.80 this morning. And similarly on corporate bond spreads, with a strong rebound in MCEV now to about GBP5.11, probably a little more than that as of today.

And similar story on IGD. In the Fourth Quarter movements in Fourth Quarter IGD, couple of things. As you know, as we planned to do, we retired our GBP700 million hybrid and then we reissued some new hybrids, so about a net GBP400 million movement. Then about GBP300 million from market movements, almost all of which was government bond spreads. Corporate spreads -- and the right index to look at for us is iBoxx, which is a little bit more of a wider index which is a bit more representative of our holdings -- broadly neutral, maybe marginally negative.

Since year-end, obviously a very sharp tightening of both government and corporates, plus some small management actions that we said we'd take, which we have taken, together growing the surplus back up to GBP3.3b. At today's date again, it would be a bit more than that.

Similar story on economic capital surplus. Obviously, similar movement to MCEV in the Fourth Quarter, with again that strong rebound to around 150%.

I think also worth noting a number of actions that we've taken and continue to take on the risk management front. We've expanded our equity hedging program. It's an out-of-the-money equity hedging program, but we've now expanded to a GBP3 billion notional. We continue to have in place that currency cap and collar at some GBP2 billion notional. We've put in place and expanded a credit hedging program that's about now a GBP4 billion notional.

So I've mentioned as I've gone through, we've made various product changes in terms of product features, guarantee levels. And obviously the strength of the operating capital generation continues to flow through as well.

That's it from me. I shall now hand back to Andrew.

Andrew Moss {BIO 3628034 <GO>}

Thank you, Pat. As I said, what I really want to do is just spend a few minutes talking about this year and what this year might hold. So I think really what we've got is a pretty fascinating year of change, I think, coming up for the UK industry and the European industry as a whole.

First of all, if you look at the external environment, clearly the Eurozone outlook is improved, but it's going to be a bumpy road, I think. It's going to take a while for the politicians to sort through some of the issues that Europe has got. It's clearly on a much better track than it was six months ago. So we're going to have to keep an eye to that downside risk.

And it's probably fair to say that low interest rates for longer, we would be thinking in that way. We probably have been, in fact, for the last year or two, in truth. But I think it's true in the US. I think it's true in the UK. I think it's going to be true in Europe as well.

But the one thing I think I'd point you to is that we've been operating really in that low interest rate environment for some time now, a number of years. So the results for 2011 actually already reflect some of the things that we can do, some of the ways we can change our business and manage our business in that environment. So a very good example is what we've done in France, where we've changed some of the guarantee structures, particularly in the fixed affair products that we sell.

So today's profitability, and Pat talked about, for example, the long-term investment return in the General Insurance business, yes, we expect yields to come off a bit. But with the business growing in absolute terms, we actually see potential growth in that investment income.

The regulatory outlook is uncertain. And by that I don't mean actually the change in the regulatory architecture here in the UK, which clearly is substantial but I don't think holds any particular fears for Aviva. But we all know that the Solvency 2 outlook at the moment is so uncertain that it's almost moving by the day, if you listen to everything that you're hearing out of Brussels at the moment.

So I think, on that, we have the benefit here in the UK of having managed an economic capital framework for a number of years. And so the volatility of that and the way that you manage that, I think we have some practice at. We've had an eye over the course of the last couple of years to what could be the less good outcomes on Solvency 2 already.

So for example, when we're writing annuity business here in the UK, whilst we're not pricing totally to a world, for example, if we didn't get matching premium where we'd be, because there would still be a change, no doubt, we have moved some way in that direction. So what is for us, we believe, a very profitable product, even at those changed rates, if you saw worst-case outcomes, would still be a profitable product. So we've had that in mind as we've been writing new business.

UK specific issue, RDR and auto-enrolment. We've been writing quite a lot of good commission-based business, actually, in the course of the last year or so, so we'll continue to do that in the period up through RDR. But actually, we're writing quite a lot of business on a fee base already.

And when you add to that in the annuity and the protection space, where our market position is particularly strong, which are not RDR affected products, we believe that we're in good shape headed into RDR. And I mentioned earlier the group personal pensions business and the increase in that, as we ready ourselves actually very aggressively for the auto-enrolment world.

And right round all of that, we've seen some pretty significant changes in customer behavior and the way in which we communicate with our customers over the course of the last couple of years. So consumer behavior in a digital world is something at the front end of our business that is affecting us in a very, very big way. And we passionately believe that those insurance companies who are going to make the changes required, and we believe we're one of them, are going to win in that new digital world.

So for example, I haven't got my iPhone in my pocket, just in case it was to go off during the presentation, but it is true, for example, that where we used to put a black box in a car and sell pay-as-you-drive insurance, we're absolutely sure that pay-as-you-drive insurance is going to come back and be a norm in this country and others within just a few years. The technology already exists on that iPhone to do that.

We have a certain number of apps on iPads, iPhones, to help people through their claims experiences here in the UK. Gets an awful lot of good customer feedback. We've got 10 pilots on digital and technology issues running in different parts of our business at the moment, to improve the way which we communicate with customers and make their lives easier.

So we're investing in that area. Yes. We're pulling our costs down overall. But investing in that part of our business we see as absolutely vital to our success at the moment.

We have three guys in our call center in Norwich whose job it is to monitor what people are tweeting about us. And we get back to them within an hour, and we tell them and help them with what they're complaining about. And it's amazing how quickly you can turn that negative experience on Twitter into them being positive back, saying you know what, this is amazing but Aviva got back to me, they fixed my problem, and you turn a negative into a positive. This is the nature of the world we're now operating in. And it isn't going to change; it's only going to accelerate.

So all of these changes I think are things that we have to be ready for. So I think we are well positioned, whether it's in terms of improved operational capital generation, where we've made a step change in the last couple of years, whether it's being competitive in our markets, digital is part of that.

But pricing will still be the key driver in most of our markets, so taking cost out of our business. We're operating now in our UK Life business with admin costs at about 30 basis points of what we write. That is more competitive than anybody else in the market. It drives pricing. It's why we're growing the business. It's just that simple.

It's a diversified business. Look at Europe, in the course of the last 12 months. Yes. There are some markets which are really challenged, but because we have a diverse portfolio we're still able to grow our profitability. And we're beating our short-term profitability targets. That's important to us. We know it's important to you.

And over and above that, when you're looking at the balance sheet, and this is something which -- we don't measure in Aviva Investors profitability, but where they make a huge contribution to the Group is that they are very, very good managers of credit. Yes. We see large mark-to-market swings in the value of assets in our balance sheet. The actual credit default across our business over the course of the last few years has been minimal and below average relative to our peers. So we think that's a great performance and it continues to underpin our performance as we go forward.

So what are our objectives for this year? Well I'm afraid they're unashamedly similar to the ones that we had in 2011. So it is improving operating performance again. We will continue to sharpen our focus in terms of capital allocation. There's a bit more to do on simplifying the portfolio, making our business less complex. So you will see further change in that, and in fact I think an acceleration of that in 2012. And meanwhile, we're going to keep our eye very firmly on the ball in terms of capital and maintaining balance sheet strength.

And in terms of targets, well, we are tightening things. We're just increasing the targets a little bit for 2012. A 13% target on the IRR, so up a percentage point. Combined operating ratio we're going to hold at 97%, aim to outperform, of course, against that. On net operating capital generation, we're upping it a little bit, so a range, GBP1.6 billion to GBP1.9b.

So keeping the range, we think that's important. Where there are profitable opportunities we can write Life new business and put capital to work, but we still want to maintain good cover on that metric against the dividend.

And the last thing was a 2012 target anyway, GBP400 million of cost and efficiency savings by the end of 2012. We're right on track to hit that. And actually that's a pretty demanding target because, you know what, we set that originally with Delta Lloyd in the numbers. And Pat mentioned that they've done well, but we're keeping the target without Delta Lloyd in the numbers now, so it's effectively a strengthening, a tightening of that target as well.

So we will continue to drive for efficiency across the Group, because we know that it's the key to our competitiveness in our key markets.

All right. I'm going to stop there. We're going to move to Q&A. I'm going to ask Pat to come back on the stage. I'm going to ask Igal to join me as well. And Trevor, of course, who's now been with us for a couple of months and hopefully will be able to answer any questions that you may have.

Questions And Answers

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Andy, why don't we start with you?

Q - Andy Hughes {BIO 15036395 <GO>}

Thanks very much. Andy Hughes from Exane BNP Paribas. I guess I should start with the massive elephant in the numbers, which is the GBP1.4 billion from Italy. Obviously the comment on page 77 that the pre-tax profits would be GBP1.7 billion -- GBP1.4 billion lower if you hadn't changed the basis for Italy for calculating the liabilities, can you just talk about that? Obviously Italian yields have come back quite a lot, but does that kind of effect on your bottom line give you a view of the Italian business going forward that -- and the way you might want to change it?

The second question I guess is on France. Obviously things are tough in France. We've seen a lot of outflows, particularly from the AFER contract during the Fourth Quarter. And I guess a bit stunned that actually, if I look at page 166 on the EV changes you're actually -- that wasn't my question, by the way. If you look at the outflows in the AFER contract, you actually seem to be saying you're seeing lower lapses in France, when everyone else is very worried about the French election and possible outflows and actually talking about the opposite going on. I'm just wondering what's going on with your French business.

And the third question was on North America. I see the spread margin's gone up a lot this year. I'm just wondering how sustainable that is going forward, because I'm just thinking about whether you've reduced the crediting rate. I can see the outflows in North America are now about 10% a year. If I look at your VIF to cash for North America, you've still got quite a lot of VIF in force after 20 years. And I noticed you made a lapse change in North

America as well, to reflect higher lapses. So is what's going on that you're sacrificing long-term value for short-term profitability in the US? Thank you.

A - Andrew Moss {BIO 3628034 <GO>}

Okay, Andy. Thanks for that. Can everybody hear me? Yes, okay. Okay. Well first of all, on the recoverability test, because I think that's what we're talking about in Italy, well, we've applied absolutely a standard approach for that market.

A - Patrick Regan {BIO 15131018 <GO>}

Yes. Thank you for your question, Andy. It's a liability adequacy test, as you know. So we applied the methodology actually we used to use on that and the methodology that all of the people in Italy are currently using, which is, one, are you earning enough from your assets to meet your liabilities, and we factor in a good default assumption within that. So that's what we did and other people did within that market, nothing more or less.

A - Andrew Moss {BIO 3628034 <GO>}

On AFER, I think the reality is we saw a little bit of outflow in 2011. The rates I think that we credited in the rates was 3.43%, wasn't it, Igal?

A - Igal Mayer {BIO 15440055 <GO>}

Yes.

A - Andrew Moss {BIO 3628034 <GO>}

Which we think is very competitive and I think puts us in a good position as we move forward.

A - Igal Mayer {BIO 15440055 <GO>}

Yes, I think this is working, so I'll just say a little bit more about France and AFER. Most of the movement you're seeing is balance sheet movement, if you look at the disclosure. The outflows number themselves are about GBP1b. That was driven, Andy, more by two things.

The rate we announced at the beginning of 2011, now, at the beginning of 2011 we made a decision to realign that portfolio. We announced a rate of 3.53%. I'll come back to the 3.43% in a minute. That was the first time AFER went from being a first quartile announcer of rate to basically middle of the pack. We were anticipating that we would see some lapses on that. That is in fact what happened.

In terms of the long-term prospects, if you look at the kinds of things that were happening, it wasn't people lapsing their policies; it was partial lapses. I do want to come back to the structural nature of the product in France. It is a long-term product. It encourages long-term savings. But we did see lower levels of deposits and some partial withdrawals.

This year, so this is what Andrew is referring to, middle of January we announced a rate, a bonus rate on 2011 of 3.43%. We're back to first quartile, and as predicted and expected we've seen volumes stabilize. Okay?

Now, let me talk about the overarching -- every time we have an election coming up in France, there's always an announcement, the taxes could be attacked, the taxes could be attacked, and the long-term benefit of this product, and it is absolutely cultural, people in France use this product and one of my guys refers to it as the Swiss army knife of savings. Why? Because it provides them protection, it provides them with deferred income growth and it provides them with essentially estate planning. It is a great product. People buy it in France. It is 1.3 trillion of total assets under investment. So it is a big, big industry.

Now, what happened with the opposition party? They made noises about taking the tax advantage away. There was a press release a week ago, Friday, basically saying they're not going to touch existing contracts, and on new contracts they will only penalize withdrawals if they happen in the first eight years. Frankly, that's good for our business because it encourages people putting the money in and leaving it in the product. So we're not worried.

A - Andrew Moss {BIO 3628034 <GO>}

We don't have 1.3 trillion of assets, obviously, Andy. That would be the elephant in the room if that was the --

A - Igal Mayer {BIO 15440055 <GO>}

That's the industry.

A - Andrew Moss {BIO 3628034 <GO>}

A bit of unnecessary detail on France. We also split the lapse assumption between unit-linked and with-profit, so that was another thing we did.

On the US, I think it's a challenge in terms of the crediting rates and the low interest rate environment. The team's done a terrific job at maintaining product profitability. You can see that in the IRRs. They're pushing the Life business more as opposed to annuities, and we've taken a reduced annuity volume as a result of that. So very much a focus on keeping the crediting ratings, we do that.

Candidly, Andy, in terms of the assumptions, the US MCEV stuff's a bit messy. We made a series of modeling changes. I referred to one on the slides earlier. And so all of it, whether it be the lapse stuff or more generally, it's more a reflection of us improving our modeling there than it is anything else.

Okay. Thank you. Greig.

Q - Greig Paterson

Yes. Greig Paterson, KBW. Three quick questions. One is can you just tell me at the year-end whether you -- in Italy whether you burned through the regulation 28 buffer at that point? That's question one.

The second one is, in terms of your proposals to sell some of the Asian businesses, I was wondering what sort of offers of interest you've had, what the demand is that you are receiving from people. And maybe you want to make a quick comment on Taiwan and issues around that.

Then, on the third point, is if you are generating GBP2.1 billion operating capital generation this year, and it doesn't look like there's too many funnies in there, why have you set a target well below that? Should we pencil in lower numbers or is that target not really meaningful?

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Why don't we start with that one? I think, as we said, we gave some guidance at the beginning of last year at GBP1.5b. We upped this at the half-year. And we've been, I'm pleased to say, able to outperform against that. But we do genuinely believe that just maximizing that number is not the be all and end all in our business.

Where we see opportunities to put capital to work profitably, and I'm talking about internal rates of return of 14%, for example, which we think is good business, then we want the flexibility to be able to do that. Equally, we also want to be able to give you, the market, our shareholders, confidence in the sustainability and the growth prospects in the dividend. So that's the balance that we're trying to strike on that.

On Asia, I said there's a little bit more to do in terms of simplifying the portfolio. I think you've taken that on into some thoughts about Asia in your mind, Greig. We've got some businesses which have performed extremely well in the course of the last 18 months or so. Singapore comes to mind.

So when we look through that lens of making $100 million IFRS operating profit within a reasonable timeframe, actually, even in the last 18 months our confidence in Singapore doing that has gone up markedly. So it's knocking on the door of getting into our first division, if you like.

There are one or two other markets which I think -- Taiwan you mentioned. We've been clear that Taiwan's not for us, as we go forward. We've been in negotiation with our partner there. We've been talking to the regulator there. It's quite a good example, actually, of how protracted such processes can be in our business. Regulators can act with real caution around these sorts of changes, and sometimes it takes you longer than you'd hope. So it doesn't mean that it isn't going to happen. I think it is, and probably in one or two other markets as well over time.

In terms of demand, I think the first thing to say is the businesses have generally been performing well, so bluntly they're more valuable than they were 18 months ago. And I think for the right assets in Asia there is demand. But it's quite interesting to observe some of the other processes that are going on at the moment. We know, for example, ING are looking to sell Asian assets. Well some of that portfolio is attractive and some of it probably isn't quite as attractive to people. So it really does depend on exactly what it is that you might be looking to move. In general, I think our businesses are more at the attractive end of the range.

Sorry, there was another question.

A - Patrick Regan {BIO 15131018 <GO>}

Regulamento 28. I've been itching to talk about Regulamento 28, so thank you, Greig. We were still benefiting from Regulamento 28 in the quarter. Pretty much, you see half of the spreads flowing through to IGD and half not. Since year-end it has been, as you know, both extended in time and in terms of applicability.

Q - Greig Paterson

(Inaudible).

A - Igal Mayer {BIO 15440055 <GO>}

We're not burning through it at all, Greig. And I think the other thing, I'd like to put a couple of other comments on Italy that'll help the context. We've actively been reducing with-profit business over the last couple of years. So in terms of -- we're not going to breach through it, because frankly that business is now within risk appetite and we've got the volumes where we want them to be. Where we've been focusing the sales in the last couple of years is protection. We've gone from nowhere in protection to being a top five player in Italian protection.

A - Andrew Moss {BIO 3628034 <GO>}

Good. Okay. Andrew?

Q - Andrew Crean {BIO 16513202 <GO>}

A couple of questions. Andrew Crean with Autonomous. Could you give us the figures around the economic capital at December, the total capital available and required rather than just the ratio? And how much liquidity premium and hybrid is in there?

Then, second question, on the free cash generation, how much of the Life free cash generation is experience variances and one-offs, assumption changes? And what do you predict for that for this year?

A - Andrew Moss {BIO 3628034 <GO>}

I think it's fair to say we haven't disclosed the first of those numbers, have we?

A - Patrick Regan {BIO 15131018 <GO>}

No, actually, whenever we used to disclose an absolute figure I'm sure you asked me for the ratio, so that's why we've put out the ratio today. Broadly, our required hasn't changed from previously. So as of now, our surplus will be in the GBP5.5 billion kind of number.

Q - Andrew Crean {BIO 16513202 <GO>}

(Inaudible)?

A - Patrick Regan {BIO 15131018 <GO>}

Yes.

Q - Andrew Crean {BIO 16513202 <GO>}

(Inaudible).

A - Patrick Regan {BIO 15131018 <GO>}

As of now, as of now. In terms of -- what was the second question? Oh, in terms of the OCG, yes. So the only item I'd point you to, actually, is we benefited to the extent of around GBP100 million from bringing the RBS joint venture assets 100% onto our balance sheet, so that benefited capital generation by about GBP100m. Other than that, there weren't any items that were one-off in nature I would point you to, Andrew.

Q - Andrew Crean {BIO 16513202 <GO>}

To be clear, you do include experience variances?

A - Patrick Regan {BIO 15131018 <GO>}

Yes we do.

Q - Andrew Crean {BIO 16513202 <GO>}

It was about GBP350m, I think.

A - Patrick Regan {BIO 15131018 <GO>}

We have some experience variances within the MCEV. Nothing -- we have some negative assumption changes within there as well. So -- as we have done previously.

A - Andrew Moss {BIO 3628034 <GO>}

Jon.

Q - Jon Hocking {BIO 2163183 <GO>}

Morning. Jon Hocking, Morgan Stanley. I've got three questions, please. On the credit hedging, can you talk on specifically which portfolios that covers? I'm assuming it doesn't cover the UK annuity portfolio, given the provision. When did that come into place and what would the IGD volatility have been during the year if that had been in place? That's the first question.

Second question, on UK commercialized, can you talk a little bit about how you see the market, what pricing activity you're seeing?

And thirdly, I wonder if Trevor could comment on what his priorities are for the UK.

A - Andrew Moss {BIO 3628034 <GO>}

Sure. Do you want to talk about the credit hedging first?

A - Patrick Regan {BIO 15131018 <GO>}

Yes, sure. So we've taken that as a macro hedge at Group, Jon. We haven't applied it portfolio by portfolio. And we've split that between the different indices, so we've done that a little bit under US and a little bit under European indices as well. It's out of the money protection, so it's difficult to give you a precise number. So it kicks in once there's a -- certainly a reasonably significant movement in corporate spreads from where we are today.

A - Andrew Moss {BIO 3628034 <GO>}

Thanks, Pat. Trevor, first of all, welcome.

A - Trevor Matthews {BIO 2001261 <GO>}

Thank you. Thank you very much.

A - Andrew Moss {BIO 3628034 <GO>}

And look, you may as well pick up the commercialized question in the generality of the other question.

A - Trevor Matthews {BIO 2001261 <GO>}

Yes, okay. Well thanks. Yes. Well I must say it's very good to be here. I'm very impressed with the UK business that I find I've inherited. Certainly my predecessors have done a great job. I think we've got some major advantages here in the UK market which I'm very keen to exploit even further. I think there's an opportunity to take this UK business to the next level.

If you look at some of those numbers that Andrew and Pat have been showing you, you can see we've got the scale and we've got the efficiencies. If you look across the two businesses, on the GI side we've got our expense ratio down from 11% to 10.3%. That's probably the lowest it's ever been. On the Life side, as Pat has said, we've got the maintenance expenses down from 31 to 30 basis points. That's I think probably market-leading, as Andrew said. We've also got the acquisition expenses. It's in the pack. As a percentage of the APE or the Annual Premium Equivalent, they've come down as well from 27% to 25%.

You put all that together, and that's why you get the 15.2% IRR on the new business last year and it's why you get the 96% core ratio. So we're in a very, very good position.

In terms of priorities for this year, well, we've got a big change agenda in the UK. But I tell you, we're well placed. I know from coming in from the outside, we are well placed, not only to tackle that change but to really drive it for our advantage. If you look here in the UK on the Life side, we've got the retail distribution review; we're well prepared for that. I know other competitors are scrambling around, trying to work out what to do and get all the basic things done. We've got that well under control and we're going to benefit. I'm very confident we're going to benefit from that.

There's a move now towards restricted advice in the UK market. And who do you want to have on your panel? Well Aviva's a good company to have on your panel, I tell you. And we're already seeing that. We're already signing up people for this restricted advice idea.

We've got automatic enrolment coming along later in the year, very [ph] complicated for small; and medium-size enterprises to cope with. So we've gone out there just last week and we've offered a solution which will help the small; and medium-size businesses who are battling with this to cope with the complexity. And again, with the big pensions business that we've built up over the last couple of years, we stand to benefit from that going forward.

On the General Insurance side, we've ridden this great motor insurance development over the last couple of years. You heard the numbers earlier. We've seen good rate rises there. Again, I'm very impressed with the sophistication of the technology that's involved in both sides of our business. The rating that Pat talked about is really world class. That's enabled us to grow where we want to grow that motor book and we'll continue to do that as we go further forward.

The commercial business that you asked about, yes, that's -- the commercial rating is not good. Commercial motor rates have gone up. Overall, in our -- if you take out the RAC business, our total premium's gone up on the general side by about 11% over the last 12 months. That's excluding RAC. And about 6% of that has been rate and about 5% of that has been volume. But we've seen good movement in commercial motor rates, but not in the rest of the commercial business. So that's a real priority for us and we're working hard on the rest of that commercial business.

But I know from coming in from outside, I know what it's like out there. It is a challenging market and Aviva is the one to beat. The big scale that we've got, the very successful brand, the very wide range of distribution. I've been out there, as you'd expect, in my early days talking to a whole range of distributors, many of whom I've known before, and a lot of them are very happy and very keen to see what we're doing and very keen to do more business with us. So we're well placed to really drive and be the real leader and shaper in this market going forward.

A - Andrew Moss {BIO 3628034 <GO>}

Thanks, Trevor. Toby?

Q - Toby Langley {BIO 15924432 <GO>}

Thanks very much. It's Toby Langley from Barclays. I've got three questions. The first is on goodwill. You've taken a hit today of about GBP300m, but you've still got some fairly chunky blocks of goodwill on the books still. Particularly you've got about GBP800 million in the US and GBP600 million relating to Spain. You mentioned in the presentation that the US is now paying up some reasonable dividends. Is that part of the equation when you're considering how you assess the feasibility of that goodwill or the validity of that goodwill going forwards? It's quite a long a first question, sorry.

And secondly, I wonder if you can bridge the gap between capital generation and then the dividend that you've declared today, because I think it would be useful for me to -- what number should I be thinking in my head? Should I be thinking two or should I be thinking five? I asked this question of Charles, but I'd appreciate your views here.

A - Andrew Moss {BIO 3628034 <GO>}

A better answer than you got earlier.

Q - Toby Langley {BIO 15924432 <GO>}

Then perhaps a question for the fund management business. There's a lot of scrambling around on the distribution side, but as I understand it there's quite a lot of scrambling around going on in the fund management industry as well. And I'm keen to know what views you have about the issuance of RDR qualifying shares for retail asset management units. And what kind of a level of AMC charge do you think you're going to have to come down to, and how does that compare to your incumbent base?

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Why don't we start with that one? It's a really interesting question, I think. And I think when you're talking about retail, for us you're talking about our UK Life business, primarily.

A - Trevor Matthews {BIO 2001261 <GO>}

Yes. That's right. You've seen some interesting trends across the industry in retail Life over the last couple of years. You've seen a reduction in the insurance bonds, of course, as people are looking at the tax basis of investing in bonds. We also sell a range of collectives which are more or less ready for RDR at the present time. It's hard to predict exactly where charges are going to be -- are going to land, but we believe there will be a continuing market there. And I think with the broad range -- we sell not just to Aviva Investors, of course; we give access to other fund managers as well.

So you're right, there's a period of change going through. But we've got a good platform, good distribution, and I think we will ride with those changes and I think we'll benefit from them.

Q - Toby Langley {BIO 15924432 <GO>}

Can you give us any sense of what -- presumably the direction is downwards, but are you able to quantify that yet?

A - Trevor Matthews {BIO 2001261 <GO>}

Well it's really interesting. If you look at what's happening in other markets, as you've gone through this sort of open-upness, of transparency, and you've seen total fund management charges come down. But in Australia, which I know well, they've tended to stabilize such that advisors are taking fund management charges of the order of 50 basis points off the platform and customers seem okay with that. Now, it's different, I know, but that's what we've seen in that market. So we'll see what happens here.

A - Andrew Moss {BIO 3628034 <GO>}

Impairment testing?

A - Patrick Regan {BIO 15131018 <GO>}

Sure. The primary thing in the US business really is improved profitability of the back book and the new business profitability. So that's really the big assumption that drives that recoverability test.

Similarly, in Spain, you could look at it either way. You could look at the profitability projections, the in-force profit and cash flow projections for the future, or you could even look at it from the contracts. Obviously there's lots of change within the cajas. Actually, we do look at it both ways, and either way it stacks up.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. The question about operating capital and dividend, a really, really important question, I think. And I don't know what Charles said to you but I'll do my best anyway, tell you how I'm thinking about it.

First of all, we do see the operating capital generation as underpinning the capability to pay the dividend. So concentrating on that and moving that up has been a really important priority for us over the last couple of years. And I think you've only got to look at the numbers to see there's a step change between now and two, three years ago. So I think the whole market should take real confidence from that. I think the dividend is rock solid and sustainable at these levels.

And of course our ambition is to grow it. But I think the Board, quite rightly, when it was looking at the volatility over the course of the last six, nine months and even some of the issues that still face Europe today, decided to just be measured on the final dividend. So it's a decision for 2011 and you shouldn't read more into it than that, Toby. That's -- I think what we've done is create an operating capital generation flow which gives us some real flexibility as we go forward. But we have to have regard to what's happening there in the external market.

Q - Toby Langley {BIO 15924432 <GO>}

Thanks.

A - Andrew Moss {BIO 3628034 <GO>}

Yes. Sorry, either of you two gentlemen. Do you want to do this first?

Q - William Elderkin {BIO 3349136 <GO>}

Thanks. It's William Elderkin from Soc. Gen. Just on that dividend point, at what point will you come back to the base of whether to abolish the scrip element, because that obviously gives you in cash terms an enormous coverage at present?

Then secondly, two operational questions. On the GI side, your return on capital I think this year was 13.9%. Assuming you hit this year's combined ratio target and that your investment yield earns towards your new money rate, where can that return on capital realistically end up?

Then finally, on I think it was slide 25 you give figures for your bond return on Life shareholder (inaudible) shareholder of assets. I think that actually went up in 2011. I just wondered how you achieved that.

A - Andrew Moss {BIO 3628034 <GO>}

Do you want to take two and three?

A - Patrick Regan {BIO 15131018 <GO>}

Yes. What flows through to the income on the bond side on the Life side is essentially the actual holdings that we earn. So it's not an assumed return; it's an actual return. There wasn't any great change in the profile. You can see if you trawl through the asset disclosures that the proportions at the different grades of AAA, AA, etc., is very similar to the year before.

In terms of the longer-term investment return in General Insurance, it's quite a slow-moving trend. As I say, you've got those two offsetting factors. The yield impact hasn't been particularly profound in this period and I wouldn't expect it to be particularly profound in the next period. So net/net, I don't think it's unachievable to achieve a similar like of return on equity.

A - Andrew Moss {BIO 3628034 <GO>}

Yes. Look, on the scrip, and just to be clear the dividend is 2 times covered on a full cash payout. So you're right in making the point you make in terms of the strength. I don't think we've changed our long-term thinking on that, which is we'd like to take the scrip away. So we're aiming towards that. We have to do that on the basis of a strong overall capital position and a strong operating capital position.

And with markets where they are at the moment, actually we're quite comfortable to leave the scrip where it is. And it's a really interesting discussion that we have with shareholders, because some people don't like it and 40% of people take up the scrip. So it is genuinely a balance in the argument, I think.

But actually, our long-term position and thinking hasn't changed on that, and we'd like to get to that position as soon as we sensibly can. But as always, I think the Board quite rightly and us as executive directors will be cautious around that.

Q - Raghu Hariharan {BIO 15133573 <GO>}

Morning. Raghu Hariharan from Citi. I just have three questions. The first one was on European flows. If you look at your flow data, I think it's on page 16 or 17, European flows -- sorry, European assets were down 7%, so they went from GBP105 billion to GBP98b. However, your IFRS reserves have gone up 8 -- average reserves have gone up 8%. So I'm just wondering what's gone on there. The flows clearly were negative. You had negative market movements. So if you can reconcile that and see what that means for earnings going forward.

The second one was really on UK annuity -- I guess new business strain in a way. This is benefiting from the GBP600 million of with-profits estate. I think it was in 2008, so that's GBP120 million for five years. So that's got a cash benefit. So I'm wondering when does that benefit run out and how should we look at cash generation?

And the last one is really around capital fungibility [ph]. You mentioned in the presentation about Canada and US up-streaming dividends. I was wondering what level of dividends did you get from Europe to HO this year and how do you see that going forward? Thank you.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Shall we start with European flows?

A - Igal Mayer {BIO 15440055 <GO>}

Yes. I think, Raghu, European flows, bottom line, take out FX and market movements and you're down to circa about GBP1 billion of negative flows. And that to me is the thing we've been talking about, essentially the step change in Italy reducing or pulling back on the with-profit business. We're now at a with-profit level that's fairly stable and we'll keep it there. So you won't see that negative impact. And when you look at the rest of the markets, largely steady or growing flows.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. European dividends, we've still got some good dividend payouts (multiple speakers).

A - Patrick Regan {BIO 15131018 <GO>}

Yes. Slightly more broadly, Canada's been an incredibly consistent dividend payer. The US, as you say, is now in a position where it's capital positive, not consumptive. The UK obviously has been a very consistent dividend payer. In Europe, France makes a lot of money; Poland's been an incredibly consistent dividend payer. Spain. It would have been a bit aggressive to take a dividend out of Italy last year, candidly, and similarly in Ireland. So I think across the portfolio we feel quite good about that, very good about that. Obviously, in a couple of places that's a little bit more difficult.

And we missed one of your questions, Raghu, didn't we?

Q - Raghu Hariharan {BIO 15133573 <GO>}

The UK with-profits estate benefit to annuity.

A - Patrick Regan {BIO 15131018 <GO>}

Yes. So the team's done a terrific job of managing the with-profit estate over time, reducing the volatility of that. I think our initial estimate was that will be available for five years of writing new business. It's probably a bit more than that, John, now, isn't it? So it's at least another five years into the future, I would say, Raghu, on that.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Good. Nick?

Q - Nick Holmes {BIO 3387435 <GO>}

Nick Holmes at Nomura. Two questions. First one is on the IGD and economic solvency coverage ratios. Wondered what sort of level you're targeting, and if there's anything you can do to reduce volatility.

And secondly, on Solvency 2, this is -- well, matching premium is the focus. The whole of Solvency 2 is getting delayed, but matching premium, I thought we were going to hear something last year on it, something definitive. Could you update us where we are and when at long last we might expect something?

A - Andrew Moss {BIO 3628034 <GO>}

Yes. It is a long haul, isn't it? I agree with you. First of all, on the IGD, at the levels we're at today we're in what we would describe as our green zone in terms of the way we look at it. So that's obviously a good place for us to be.

In terms of volatility, there's a couple of ways that you can manage the volatility in a UK reported IGD measure. You can talk to people in Canary Wharf and get them to change some of the European rules that are applied, or you can take some uneconomic hedging action which doesn't make much sense until you get down to lower levels. And essentially that's what we do. So when we're talking about the credit hedging and the equity hedging and some of the actions we've taken, it is out of the money. It is a way from that drop between, say, GBP4 billion to GBP2.5b. It starts to cut in more when you get to those lower levels.

So we are making a judgment about where we're prepared to spend money to protect the IGD. And it's not in that range from GBP3 billion to GBP4b, to be clear. But once you get to GBP2 billion or below, you'll find those hedges beginning to cut in and help us. And anyway, actually, the way it's reported, the volatility goes out of the numbers to quite a high degree anyway, particularly in relation to France.

So I think it isn't a linear progression, when markets move. And we've got quite a lot of experience clearly at managing it over the course of the last few years, when it has been volatile for sure, Nick.

On matching premium, you're absolutely right. My god, it's a long saga. And if you'd gone back six months ago, everything looked fairly comfortable on it. And the truth is it's been thrown back into the political mix in the course of the last couple of years -- sorry, couple of months in particular. I don't exactly know, to be frank, how that's going to work through.

I think what's been really encouraging this week is that the European industry -- I'm a member of the Pan European Insurance Forum. There was a meeting on Monday of this week which led to a letter being written to a number of MEPs who are particularly influential in this debate. We showed a completely united front in terms of the same way that we were presenting a united front last summer. That united front in reality was rent asunder in the two or three months leading up to last Monday.

So that united front is important. It's been reasserted. I think it is the basis on which to have the discussion with the European parliament and AOPA. And I fully expect over the course of the next three, four, five weeks that debate to rage pretty strongly.

I can't tell you with certainty what the outcomes are going to be. What I can tell you is that we've modeled the effects on whatever the outcomes are for our book. And of course, being practical about it, I think that whatever the outcomes are we expect there to be transition provisions which will allow things to be managed over time.

So I wish I could be more certain on it, but this is exactly where we are at the moment. Your heartfelt sentiment I completely agree with, that we need certainty. It's been nearly 10 years that the industry's been working on this, and it is still a weight round the industry's neck. So certainty is what we need.

James?

Q - James Pearce {BIO 16758460 <GO>}

Morning. James Pearce from UBS. A couple of things. First of all, I think you say that you've taken management action to improve the IGD in the First Quarter of this year. Can you tell me what you've done and what options are still there for you if you do need to strengthen that further?

Second, a bit like the OCG target, I think you're already ahead in 2011 of the target you've set for 2012. How should we look at that? And in particular, could you just say what you have in mind in Ireland? And does the 6%, I think, IRR in Ireland already reflect the cost saving action you've taken there?

And thirdly, can you talk a bit more about UK commercial motor, where I think the combined ratio deteriorated quite a bit in H2?

A - Andrew Moss {BIO 3628034 <GO>}

Yes. Why don't we start with UK commercial motor? Do you want to go there first, Trevor?

A - Trevor Matthews {BIO 2001261 <GO>}

Yes, sure. Yes. We're not happy with the performance in commercial motor. We're looking for rate increases where we can get them. There was more rate increase available in the first half than there was in the second half. So that's an area of attention for us at the present time.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. IGD and actions we've taken or actions we could take?

A - Patrick Regan {BIO 15131018 <GO>}

Yes. Nothing incredibly profound, James. We did a couple of -- we extended a little bit of existing reinsurance, as I say, not huge at all, and another similar type of item that both just helped on the CRRs. But they were reasonably modest actions. There are a number of similar or slightly larger actions you could choose to take, given the size of our in-force cash flows.

And I missed your -- Irish, that's right.

A - Andrew Moss {BIO 3628034 <GO>}

The Irish situation, James. No. The 6% IRRs don't take into account (multiple speakers).

A - Patrick Regan {BIO 15131018 <GO>}

No, obviously. It would be a bit sad if it did, wouldn't it?

A - Andrew Moss {BIO 3628034 <GO>}

One of the reasons that we wanted to take action, because it's so far away from the Group averages. So the action that we're taking in Ireland runs both across the Life book and the General Insurance book. And it's really building on strength. They're backing that business in many ways into the UK business, which as I said in my presentation, it's great to see now -- there was a difficult phase, to be frank, in Ireland, because we are talking about a number of people leaving the business, and we're still in consultation on that and that's a serious matter.

But equally, I think why are we doing it, to be competitive in the Irish market, provide our customers with good value products, which at the same time, because of the lower costs that will be associated with it, will work through into better profitability for us. So genuinely we believe that's the right thing to do. It's a win/win for customers and for us.

Q - Unidentified Participant

Two small questions. One, on the GBP400 million cost saving target, where are you now, run rate, and what was actually in the 2011 number?

Then the second thing is can you remind me about what happened with the AIB joint venture? Did it just naturally come to an end or -- because I thought you got compensation usually in these circumstances, maybe not in that case?

A - Andrew Moss {BIO 3628034 <GO>}

No. And we will, and we will. Do you want to tell the story on that, Igal?

A - Igal Mayer {BIO 15440055 <GO>}

Sure, yes. I think it was up for renegotiation, as these things normally are. We put our best foot forward in terms of what we felt was acceptable terms and conditions, and AIB at the end found a better deal. We decided to walk away from that. What you see in this year's accounts is the write-off of the goodwill associated with that. What is still outstanding is the resolution of the unwind of the JV. And you should anticipate proceeds coming our way from that, because we will essentially sell back one of the insurance companies to AIB.

A - Patrick Regan {BIO 15131018 <GO>}

And that should be modestly capital positive, shouldn't it?

A - Igal Mayer {BIO 15440055 <GO>}

Correct. It will be capital and cash positive.

A - Andrew Moss {BIO 3628034 <GO>}

On the cost savings, the nature of that was the two-year effort that we were making. So naturally, actually, a lot of that is not front-ended and in the 2011 numbers, Pat?

A - Patrick Regan {BIO 15131018 <GO>}

Yes. So the good examples of some of it, Delta Lloyd was part of it, they've delivered all of their part already. In the UK, remember we're saves and efficiency. There's some cost saves in the UK Life business flowing through. On UK GI, the cost ratio -- Trevor mentioned this earlier -- has come down, so essentially more volume for the same expense in there. So some good efforts in that. Igal and the team are very focused on some of the areas in Europe, and obviously we're bringing on-stream some savings within Aviva Investors as well.

A - Igal Mayer {BIO 15440055 <GO>}

And Canada is the other one.

A - Patrick Regan {BIO 15131018 <GO>}

And Canada. Sorry, and we've already achieved around GBP60 million in Canada.

A - Igal Mayer {BIO 15440055 <GO>}

Yes. Which is a couple of points.

Q - Unidentified Participant

Have you got a total figure, just to make it easy?

A - Patrick Regan {BIO 15131018 <GO>}

I didn't total that. No, you're right. But we're not too far off. We'll probably be a little under halfway there, I would say.

A - Andrew Moss {BIO 3628034 <GO>}

Yes. That's right. Tony.

Q - Tony Silverman {BIO 2162363 <GO>}

Yes. Tony Silverman, S&P Capital IQ. I've got two questions and a request, please. Firstly -- first question, I think on page 135, where it's got an asset breakdown, I think it shows quite a substantial shift from AA to A. In fact I think it's about 25% to 30% of the AA bonds moved to A. Is that -- are you happy to be holding that amount of A? Is that where you want to be? And isn't that quite a strong driver of the spread income, which is very important to the investment result in the Life segment?

The second question is just more generally. You mentioned yourself that the interest charge has gone up marginally. It's now GBP650m. If you include the preference dividends, I suppose you owe GBP700m. Is the debt associated with that amount of interest something you're happy with and what do you see as the future trajectory of that?

And the final thing was a request. I'd like to congratulate you on introducing undiscounted cash flow for the in-force, and will we see it for new business, please, next time round?

A - Patrick Regan {BIO 15131018 <GO>}

Okay. Yes, sure. We can do that happily. This is going to sound a little cheeky is my response, Tony, so apologies in advance. We're holders of long-term assets. We don't trade in and out a lot. We don't look to shift the portfolios. The main shift from AA to A was a result of the rating agency actions that impacted the portfolios.

Q - Tony Silverman {BIO 2162363 <GO>}

It's what's called migration.

A - Andrew Moss {BIO 3628034 <GO>}

I think to perhaps give a bit more color on that, one of the things Pat talked about was investing in greater risk management capability across the Group, which I think we've done very successfully, actually, in the last 18 months or so. The general review of credit in the portfolio has been a very, very marked feature in that.

So we do an awful lot of credit analysis ourselves now within the Group, much more than we did even two years ago, to be frank. And that's probably appropriate, given the world that we now live in. But I think it gives us quite a -- much higher degree of assurance, almost name by name, actually, in terms of some of the assets that we hold.

A - Patrick Regan {BIO 15131018 <GO>}

In terms of the debt levels leverage, I think we stood up just over a year ago now and talked about our ambitions on leverage. And I think those ambitions are still the same aim and in the medium term that's what we'll aim to do.

A - Andrew Moss {BIO 3628034 <GO>}

Yes, Marcus.

Q - Marcus Barnard {BIO 2103471 <GO>}

One quick question, please, a quick one. So that GBP3.3 billion IGD number at end of February, does that include the final divi and does that include the potential redemption of a hybrid in June?

A - Patrick Regan {BIO 15131018 <GO>}

No and no. And again, the number would be actually a little bit higher than that today, if we struck it at today's date.

Q - Marcus Barnard {BIO 2103471 <GO>}

Thank you.

A - Andrew Moss {BIO 3628034 <GO>}

Yes, gentleman over there.

Q - Paul De'Ath

Hello. Paul De'Ath from RBC. Just one question on the OCG. Given the huge difference between your operating profit and net result on an IFRS basis, can you give us a feeling of what the non-operational capital generation is, so the bottom line on the capital generation?

A - Patrick Regan {BIO 15131018 <GO>}

Well as I talked about on the MCEV stuff, we saw net of tax and net of MI investment variance movements, which obviously is the nature of an MCEV style of reporting. Within that, though, the actual realized amounts of losses on either the corporate bond portfolios, the government bond portfolios or the commercial mortgages were very small. So if you factored in, which I think is the appropriate thing to do, those numbers, you wouldn't get a great difference, to be honest.

On corporate bonds, we're running at about a 5 basis point record. It's a tiny bit higher than that on commercial mortgages but not much. So actually, if you look at it in that sense, you wouldn't get a very different number. And obviously, as we talked about, those unrealized movements have largely come back post year-end.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. Any more for any more? Yes, Greig.

Q - Greig Paterson

Just in the context of the UK economic environment, I wonder if you want to talk about that GBP10 billion SME mortgage book and just give us an update on that.

A - Andrew Moss {BIO 3628034 <GO>}

Yes. It's continued to perform generally, actually, very, very well. We have, as we expected, seen a little bit of loss coming through the book in 2011 and made provision for that. We still have very, very substantial provisions in the balance sheet which we haven't released to protect us against that.

But just to be clear, we do see it as one of the competitive advantages we have in pricing annuities in the UK, the yield that we earn on that book. And we have been adding to it at good margins in 2011. So we remain very positive on it. Trevor and I were up with the team in Norwich looking at that two or three weeks ago, actually, and getting the detailed story behind it.

And I think we have 30 years of experience in some of the individuals up here, who've managed through a number of cycles before. And in one or two cases they're having to restructure arrangements, but they're doing so very, very effectively. And we're right on it, I think. So very confident still about the levels of provisions and confident still to write new business, and the origination capability in that unit is a massive asset to us.

Andy?

Q - Andy Hughes {BIO 15036395 <GO>}

Follow-up question on the commercial mortgage -- the loan book. Obviously, as interest rates come, the fair value on the balance sheet is going up a lot. And when you look at the LTVs that obviously appear to be quite scary with an average of 103%, which is caused by obviously the value you put on those loans on your balance sheet. Under Solvency 2, will you be able to use the fair value treatment for certain? And if you're not, what would the actual difference be in terms of capital treatment between moving from fair value loans to straightforward amortized costs like a bank would do? Thank you.

A - Patrick Regan {BIO 15131018 <GO>}

Firstly, a little more broadly on the portfolio, Andy, you're quite right to say that the move in LTV, which has moved a little bit, not a lot, I think, is due to the discount rates increase in the fair value of the loans. The value of the properties actually is pretty rock solid, I think, John, isn't it. Interest cover stayed about 1.3 times. The provision is about GBP800 million portfolios. The amount that's non-securitized is just under 9, John. So you've got 9%, 10% provision against that book. So all of that I think is pretty good stats.

I think in terms of Solvency 2 outcomes, well, I guess nothing's certain in outcomes, particularly things backing annuity businesses. We do think we can use the fair value, yes.

A - Andrew Moss {BIO 3628034 <GO>}

Nick?

Q - Nick Holmes {BIO 3387435 <GO>}

Same subject, sorry. Did you say credit provision is now GBP800m?

A - Andrew Moss {BIO 3628034 <GO>}

GBP800 million against commercial mortgages, yes.

Q - Nick Holmes {BIO 3387435 <GO>}

Reduced from GBP1.1b?

A - Patrick Regan {BIO 15131018 <GO>}

No, no, sorry. It's total provisions GBP1.6b, so --

Q - Nick Holmes {BIO 3387435 <GO>}

This is GBP1.6b.

A - Patrick Regan {BIO 15131018 <GO>}

GBP1.6b, yes. Thank you for picking that up. So half corporate bonds, half commercial mortgages.

A - Andrew Moss {BIO 3628034 <GO>}

Okay. If there are no other questions -- sorry, Greig.

Q - Greig Paterson

I know it's an obvious one and I'm a bull on the stocks and I criticize other companies for it, so I just would like to know your answer. Just looking at the new disclosure in terms of flows on page 17, UK with-profits obviously in decline, it's got a bit outflow. And obviously the margins on there are pretty thick versus some of the new stuff putting on your book (multiple speakers) for others it appears to be the case. I'm wondering if the sustainability of the VIF going forward is in question because of model switch and that secular decline.

A - Andrew Moss {BIO 3628034 <GO>}

Do you want to comment on that in the UK, Trevor?

A - Trevor Matthews {BIO 2001261 <GO>}

Yes. We're putting business -- you're absolutely right, in common with many companies around the world, quite frankly, with-profits business is running off and other non-profit and other businesses is running up. We're very happy with the new business we're putting on. These sort of IRRs that you've seen today are very, very good, well competitive. So we're not fussed about that. It's a natural part of the process that we're going through here and we're very keen to write more profitable business.

A - Patrick Regan {BIO 15131018 <GO>}

I think it's fair to say that what we earn from our in-force reserves, the lowest amount is on the old with-profits. That's our lowest earning business. We earn a lot more in basis points from -- particularly from annuities, but generally. So in terms of what we're getting on new business versus old, the new stuff is much more profitable.

Q - Greig Paterson

Is that sufficient to make up for (inaudible) the outflows were twice the inflows. Is that the new business has got twice the margin?

A - Patrick Regan {BIO 15131018 <GO>}

Yes, I think -- on annuities, if you include underwriting margin, we're almost up to 200 basis points, John. And the old with-profits is, what, 10, 20. So yes, absolutely.

A - Andrew Moss {BIO 3628034 <GO>}

I think this has always been our issue around the reporting of flows. We're very happy to do it and we do it. But Aviva is an underwriting company and it makes a lot of money underwriting longevity risk in annuities and mortality on the protection side, and we make a lot of money writing general insurance business as well.

And I've said it before but I'll say it again, those are markets in which there are relatively few competitors and that means margins are higher. And we're very, very good at it. We have some very expert people in both the Life business, nearly 2,000 underwriters out there today writing business across the SME space in the UK alone. So that's where we make a lot of money. That's where we have competitive advantage. That's where we have real expertise which we're putting to work every day. So yes, you can look at the net flows, but you're only going to get half the story about this Company.

Okay. Let's stop there. Really good session. Thank you. Very good questions. We will always -- as always, Charles and the team will be willing to take other questions as we go along. Thanks very much for coming to see us this morning and we look forward to further discussions with you. Thank you.