S1 2018 Earnings Call

Company Participants

- Andrew Croft, Chief Executive Officer
- Craig Gentle, Chief Financial Officer and Director
- David Lamb, Managing Director and Executive Director
- Ian Gascoigne, Managing Director and Executive Director

Other Participants

- Andrew Crean, Analyst
- Ashik Musaddi, Analyst
- Barrie Cornes, Analyst
- Benjamin Bathurst, Analyst
- Blair Stewart, Analyst
- Edward Houghton, Analyst
- Gordon Aitken, Analyst
- Haley Tam, Analyst
- Oliver Steel, Analyst

Presentation

Andrew Croft {BIO 5711239 <GO>}

Right. So morning, everyone, and welcome. Now back in February, at the time of our full year results, I shared my thoughts on why we've been consistently successful to date and the reasons why I was confident that we'll be as successful in the future as we have been in the past.

Now just to recap, the size of the market is large and growing, with a considerable savings gap that needs to be bridged. The need and demand for trusted face-to-face advice has never been greater, whilst at the same time, the number of qualified advisers in the U.K. is insufficient, creating an advice gap, the perfect environment for client-focused advice business like St. James's Place. This environment means that we remain confident we can achieve our medium-term growth objectives, although inevitably, as we have experienced historically, we will have quarters where we exceed our medium-term objectives and quarters where we may not. Such events do not impact our medium-term view.

In February, I went on to say that what makes St. James's Place an attractive proposition for clients is, first and foremost, our partnership, the best and most experienced advisers in the industry spreads throughout the U.K., and now, with offices in Hong Kong, Singapore and Shanghai. With our focus on developing long-term relationships that span both clients and adviser generations, our partners can provide a level of tailored and expert advice and service that clients truly value, advice that is ongoing and relationship-based, not transaction-driven. At the same time, clients have the security of dealing with a St. James's Place partner, knowing that supervision and support of a FTSE 100 company stands behind everything that they do. Without doubt, the strong relationships our partners have with their clients, coupled with the ongoing advice and service, are major contributors to our excellent and improving retention of existing funds.

Consequently, we continue to see stronger growth in net flows than gross flows, with the net flow, of course, being the more important measure. Now given the importance of the partnership to our ongoing success, in addition to Craig covering the results, Ian Gascoigne will provide an update on the partnership, our growth engine. I will then wrap up at the end before opening up to the usual Q&A.

Before handing over to Craig, a few words on the other announcement this morning. As you have seen, David Lamb has informed the board of his intention to retire in early 2019. David joined the company in February 1992, a few weeks after we opened for business, and was appointed to the board in 2007. On his retirement, David will have completed 27 years of service to the company, and the last 12 as a main board director. He has made an enormous contribution to the success of St. James's Place, spanning many areas of the business over the years. But David was particularly instrumental in the development and operation of our investment management approach. I'm therefore delighted that once David has retired, he has agreed to continue to chair our investment committee.

I'm also very pleased to announce that Rob Gardner will be joining St. James's Place in January 2019. Rob will take over from David on the Executive Board and lead our investment proposition going forward, working closely, of course, with David during a handover period. Rob is 39 years of age and is Co-Founder of Redington, one of the U.K.'s most respected investment and pension consultancy businesses. Having worked closely with us for the last 6 years, Rob comes not only with a wealth of business, pensions and asset management experience, but also extensive knowledge of our business as well as knowing many of our partners and people. Rob is an important and significant new hire for St. James's Place. I'm delighted he has agreed to join. And we very much look forward to working with him over the coming years.

I'll now hand you over to Craig to run through our financials.

Craig Gentle {BIO 20095126 <GO>}

Thanks, Andy, and good morning, everyone. My presentation of our half year results is going to take a familiar course. Ian is going to cover developments in the partnership, so I'll provide a very brief update on the way in which our adviser numbers have continued to grow during the first 6 months. I'll then comment on both our growth in gross and net flows, followed by a commentary on the cash result for the first half. I'll then cover EEV, IFRS and capital. Finally, I'll comment on the interim dividend that we announced this morning.

The number of advisers has grown from 3,661 to 3,810 at the 30th of June, which is an increase of 4%. We continue to attract high-quality people from all over the financial advisory sector. And our Academy continues to play an increasingly valuable contribution to our growth, with 95 having graduated between January and June. And as mentioned, the advice gap that we have in the U.K. and our growth strategy of not only attracting the best existing talent in the industry but also providing an environment for new talent to flourish is turning this gap to our advantage.

During the first half, our gross inflows grew by 15% and amounted to GBP 7.9 billion. Importantly, net inflows grew by 21% and amounted to GBP 5.2 billion. This growth, together with global market performance that was challenging in the first quarter but stronger in the second, has resulted in funds under management of GBP 96.6 billion at the 30th of June.

Our growth in the second quarter for gross and net flows is 10% and 13% respectively, a little lower than the growth we reported in the first quarter. But it is important to remember that in the second quarter of 2017, we grew by 29%. The reality of this is that individual quarterly growth percentages will fluctuate, but we remain confident in our medium-term growth target. All in all, then, a very strong half year on top of what was a record year in 2017.

I'll now turn to the cash result, which is the most important performance indicator for our business, as it reflects the way in which cash emerges from both existing and new business. In the past 2 comparative years, there have been a number of changes to the pattern of cash emergence, following our unit liability reassessment at the end of 2016. But I'm pleased to say that we're now in a steady state, and therefore, the pattern in 2018 is the same for 2017, which should make modeling and comparisons more straightforward.

The increases in net income from funds under management of 12% to GBP 332.5 million and margin arising from new business of 18% to GBP 70 million are therefore directly attributable to the profile of funds under management during the half, together with flows out of gestation and the increase of 15% in new business year-on-year. There's been no change to the blended margin of 77 basis points.

It's worth emphasizing that we now have GBP 33 billion of funds under management within the gestation period. And whilst these are yet to contribute to the cash result, they will do so in time. These are funds that have already been secured and which we expect will exhibit the same consistently high levels of persistency that we experienced as a group. Each of the cohorts will start to contribute to cash emergence 6 years after being written. And as a guide, once the entire balance matures, it'll contribute an extra GBP 0.25 billion of net income to the underlying cash result without any further attributable cost. This will, of course, be supportive for future dividend growth.

Expenses are being in lined with our expectations, but there are 2 preoperating cash items that merit comment. Firstly, the FSCS appears, on the face of it, to have shown some improvement, but I'm afraid this isn't the case. What has actually happened is that the billing period for our 2018 accounts has been reduced from 12 months to 9 months, reflecting a decision by the FCA to move its compensation levy period in line with the same financial year. This is, therefore, a one-off timing difference that will only benefit 2018. The underlying reality is that although we are supportive of the importance of FSCS for clients of our industry, the costs associated with supporting it remain at a frustratingly high level.

Secondly, and briefly, tax relief from capital losses has run at a faster rate in the first half, and this is largely driven by market conditions, particularly in the first quarter. Operating cash has therefore increased by 18% to GBP 164.3 million. You will, however, recall that for the full year, we said we are going to move Academy costs to above the operating cash line. Investments in the Academy, which in the first half amounted to GBP 4.2 million, represents a significant current investment in future growth and cash generation. Past investments in the Academy is already contributing very strongly to our results. And so we now see this change as the best way to present future results, as a pro forma in the back of your packs which shows the operating cash result, including Academy above the line. And it, therefore, shows the comparatives you can expect to see in the future statements.

Our other areas of investment below operating cash continue to grow and develop in line with plan. As I mentioned back in February, the strategies for both Asia and DFM remain one of continued investment, but with growth in income from these businesses offsetting much of that additional cost of investment.

Our additional cash -- our underlying cash result, taking these investment activities into account, has increased by 20% to GBP 147.1 million, which results in an underlying basic cash EPS of 28p, which is 19% up from the last half year.

The first half has seen significant activity levels on back-office infrastructure, development and migration. In June, we successfully migrated our drawdown plans, which involved over 38,000 accounts and GBP 5.3 billion of funds under management. I'm pleased to say this migration went smoothly. We've also, this month, started to migrate part of our preretirement account pensions book using a phased approach by location. This is the start of a significant phase. And once again, I'm pleased to say that it's progressing well.

We now have GBP 40 billion of our funds under management on Bluedoor, and 70% of all new business written in the first half of 2018 was written on the new system. We continue to approach the systems migration with great care. And our #1 priority is to do it well and to do it safely. We continue to expect to have, substantially, all activity on migration complete by the end of 2019 at which point you'll see a substantial fall in the associated costs.

I'll now turn to the embedded value results, where EEV operating profit has increased by 23% to GBP 489.6 million. There are a number of factors that contribute to this increase, the most obvious one, being the growth in new business. We're also, however, benefiting from the longer-term contract boundary within the retirement account, which whilst leaving cost for the clients unchanged, allows for the full benefits of pension business pre and post retirement to be recognized in embedded value.

Investment return variances reflect market conditions, with a weak first quarter somewhat offset by a positive second. But taking all of this into account, our EEV net asset per share now stands at GBP 11.15. But as a reminder, our preretirement account book, currently in the course of migration onto Bluedoor, has a significant embedded value attached into it that is not recorded in our statement because of the way in which the contract is written. We have no plans to novate these contracts. But if we were to, modeling periods would be extended, and we would record somewhere in the region of GBP 400 million of additional embedded value, which would increase embedded value per share by around 75p.

I won't comment too much on IFRS, but the background is very much the same as it has been. And as usual, there's a reconciliation to the cash results in your packs. If you focus, however, on IFRS profit before shareholder tax, you see modest growth of 3.6% to GBP 82.5 million.

There's also little for me to say about capital since very little has changed since we presented our results for 2017. As I indicated then, our capital needs will grow broadly in line with growth of the business. It's worth reiterating, however, that our business model, which involves ensuring client assets are matched at all times, means that not only are clients' investments, where they're supported by the specific underlying assets that they've selected, but as a result of that, the shareholder is not exposed to the financial, and therefore, the capital risks that would otherwise be present.

Finally, I'll turn to the interim dividend that we announced this morning. And we've taken a very simple and consistent approach to the interim dividend, and the growth of 20% is a direct reflection of the increase in the underlying cash result. As we said back in February, we expect to distribute around 80% of our underlying cash result for the year, which we believe strikes a sustainable balance between providing returns to shareholders and continuing to grow the business.

So in summary, advisers are up by 4%. Gross inflows are up by 15%. Net inflows are up by 21%. Underlying cash is up by 20%. And there's an interim dividend reflecting this success, also up by 20%. All in all then, a very strong performance during the first half that we look forward to building on over the coming months.

I'm now going to hand over to Ian, who is going to speak a little bit more about developments in the partnership.

Ian Gascoigne {BIO 4439479 <GO>}

Thank you, Craig, and good morning, everyone. I'm delighted to be speaking today. Andy has asked me to say a few words about the partnership and to try and give a real flavor of what's happening under the bonnet of what Andy correctly refers to as our growth engine.

Those of you who followed us for some time will already be familiar with our growth model, a very simple model to understand, but quite complex and challenging to execute.

However, we have been extremely successful. We have grown by 9% compound across both metrics over the last 10 years. .

However, this only tells half the story, and Andy wanted me to bring some real-life case studies into the meeting this morning. And when he asked me to do this, I wanted to find something that was recent, relevant and representative. I looked through my diary and came up with my attendance in June at an office opening of a practice I've known for over 20 years. Now to counter any accusation that I have cherry-picked this business, it is based in the financial hotbed of Wrexham, one of the most deprived parts of the United Kingdom.

And the story starts in 2001, with the 2 banker assurers leaving NatWest and Lloyds Bank, respectively, to form 2 sole trader businesses with SJP. In 2006, they approached us to merge into 1 joint business. And at that time, I must confess, we were slightly reluctant. Obsessed with our gross partner numbers, such a merger would be a minus off the partnership total. And those 2 individuals were bringing in between about GBP 3.5 million and GBP 4 million of gross funds each on an annual basis. Solid citizens of the classic model.

Now since then, they have, with our help, been developing their business, just like hundreds of other partners at SJP. Now last month, as I said, I attended their office opening. They've moved into the old Wrexham brewery building. And just to prove the point, here's a picture of me at the event. So let's take a closer look at just how this business has developed. While here, we see Warren and Medwyn, joined by a new Co-Director, James. James is a 28-year-old graduate and joined SJP in 2013 and the practice in 2015. He bought into the business, utilizing access to loan capital, facilitated by SJP. And as such, he became a shareholder and Co-Director of the business, the first step in a sensible succession plan.

And the advisory team has grown significantly since the days of those 2 single partner businesses. Here, we see Tom, Gwyn, Ben and Howard, each with an interesting story to tell and representative of the interface between the partnership and SJP. Tom and Gwyn are the sons of the founders, university graduates and graduates of our own Next Generation Academy, as is Ben. Ben and Gwyn are both chartered advisers, having benefited from our own in-house workshops as we look to increase the professionalism and the qualifications of the partnership. And such is our commitment in this area. You may be interested to know that 40% of all chartered advisers in the United Kingdom who qualified in 2018 currently work for St. James's Place.

Howard is interesting for another reason, representing our ability to retain talent or the other end of careers. Having run his own practice, Howard wanted to work part time. So he sold his practice into Hadlow Edwards, allowing him to capitalize his business, but to continue to work part time with his key valued clients, something appreciated by them, and allowing Howard to focus on advising, with the practice providing the support and all the other mechanisms that are necessary.

To further advise us, Mandy and Jon complete the advisory team, with Jon specializing on the provision of mortgages. Now a team of 9 advisers in 2018 need specialist support, and this is provided by a fully qualified paraplanning team. And the whole business is supported by a further 9 PAs and secretaries. This whole operations team is managed and supervised by Dom Richmond, who is an experienced manager, who himself is also a chartered financial planner. The business utilizes its own website, hosted by SJP, which provides access to regular e-briefings to clients and updates on developments to our fund range, any changes to taxation, et cetera.

So when we talk about the development of small SMEs, this is what we mean. Warren and Medwyn, the senior directors in this business, are now responsible for total funds under management of GBP 400 million and are on track this year to attract gross inflows of GBP 60 million. And as you've seen, the 2 sons of the founders are in the business, ensuring stability and succession and reassurance for the 2,700 clients of the business.Now the business also provides strong support for our own charitable foundation. And the business supports 3 local charities in Wrexham, social responsibility and giving something back, being important components of our culture.

The business coexists with SJP, and here, we see how the practice is supported by us. We provide support across a range of areas, ranging from training and development, technology, technical support, marketing, risk management. Now am I confident about the business? Yes, I am. Is it unique within the partnership? No, it isn't. We currently have 637 multimember businesses on the very same journey as this one. So beneath our headline numbers, you will see the development of an increasing number of multimember practices co-investing, developing and building for the future.

Here, you can see how the development of this business has been taking place over the last 5 years or so. The dark-blue columns are the numbers of our high-performing single-partner practices. In 2012, you can see this stood at about 1,500. And on the top of the dark-blue column, you can see our small, medium and large businesses. In 2018, our single-partner businesses have grown, where the major growth is in the small, medium and large businesses. Such has been the growth, that now, over 50% of our capacity is in such business structures. 58% of the advisers within these businesses have been with us for less than 3 years, and we know that their productivity will increase dramatically over time as they mature and become more experienced.

Now I went to Wrexham for that example. But I could have just as easily selected almost any TAM in the United Kingdom. But it's a good representative of what we're seeing across the country: investment by partners and their own infrastructure and support; the development of the next generation of advisers; client retention through ordered succession; the ability for new advisers to buy in to existing businesses, facilitating that succession; younger, next-generation advisers accessing younger, next-generation clients; and businesses that are terribly future-orientated.

So that's enough of Wrexham. I now wish to move on to the Academy. I mentioned how the Academy had assisted the development of that business, and I thought it might be worth updating you on the increasing contribution it is making to our business. Our earlier Academy intakes were predominantly London-based. And it's here where the graduates are making a significant contribution to the new business. They have been with us a little bit longer. Here, we see the percentage of new business that our graduates are making to our London offices. That over 1/4 of our new business from one of our largest offices comes from Academy graduates is a strong testament to the success of the program. Nationally, across the business, the total Academy contribution is about 11% of new business. But that will increase as the graduates start to develop from our centers in Solihull, Manchester and Edinburgh. We currently have over 300 individuals across the 4 centers in training, with an average age of 37; and with a far more representative gender split, they also bring a great energy and diversity into our business.

However, that doesn't mean we're not continuing to grow our capacity through traditional recruitment. We've had a record number in the first half for recruitment. A record number of applications this year, such that our adviser numbers, as you've heard, are up 4%. And we continue to turn away applicants who do not meet our entry standards. And within those new joiner figures is our largest-ever recruit business, a firm with 10 advisers within it. And we're also beginning to attract the few significant joiners from stockbroking backgrounds. This is a new source of recruits for us. And they're beginning to see SJP as a suitable home for them to advise and service their clients. We're sifting through 41 applications in the first half of the year to join our Asia business, and we've already appointed some significant hires in Singapore and Hong Kong.

Now we try not to PR in the trade media every time a significant hire joins the partnership. We prefer to grow organically, modestly, but relentlessly. So I have thus given you a flavor of what's happening under the bonnet of the business: the organic growth of our partner businesses; the continued and growing contribution of the Academy; and of course, our commitment to attracting the very best professionals throughout the country.

We often say our business model is simple, not easy. It requires relentless focus and high levels of partner contact and a certain resilience. It is not easy to replicate because as well as the hard yards, it has to be underpinned with a strong culture and a set of values. It also needs a large number of high-quality employees who care about the partnership and their clients, which is something we're very lucky to have. You cannot replicate this model based on random acquisitions thrown together under the banner of industry consolidation. The demand for high-quality advice has never been higher. And I remain extremely confident, and I very much look forward to the partnership continuing to provide for their clients with the advice they need in a time of increased complexity and uncertainty. Thank you very much.

Andrew Croft {BIO 5711239 <GO>}

Thank you, Ian. And hopefully, that provides you with a good insight on how our partners are investing in their businesses, their infrastructure and their future.

Now corporately, SJP is also investing for the future across a number of initiatives. So let's hold have a look at these. Firstly, a key priority is to maintain and develop the support to our partner businesses, in particular, providing the tools to support their client relationships. Now here, we use technology far more than I believe is understood. Ian showed the partner website for Hadlow Edwards, which we design, we maintain and we host, and through which we can send out e-briefings and other communications direct to clients, but personalized from the partner business.

To support partners in their client relationships, we also have our client portal called the online Wealth Account, which enables clients to access up-to-date valuations of their investments as well as see detailed performance reporting. Performance reporting, which allows not only for all charges and fees specific to each individual client, but also taking into account the clients' own actual cash flows. We believe this is unique in the industry.

Clients can also, through their online Wealth Account, choose electronic or paper correspondence for business administered on the Bluedoor platform. They can receive notifications by e-mail or by text, and of course, make online payments. This online Wealth Account is also available to clients as an app for both iOS and Android phones.

We also provide digital tools to help partners run their business through their partner portal, which we call My Practice [ph]. This enables partners to see key information about their business, such as continuing professional development records, information about clients and the ability to identify, for example, which clients have not used their ISA allowance this year. All this is about making it easier for partners to do business at SJP and for clients to do business with their partner.

Partners also have access to our Portfolio app, which we have developed in-house. This app incorporates the clients' actual investment holdings, along with BlackRock's Aladdin system, featuring portfolio construction as well as (inaudible) modeling. This enables a partner to work with their clients to understand their investment experience, and if necessary, rebalance so that the client stays on track to achieve their overall objective.

Alongside this, a number of partners use a CRM system called CURO, which integrates with both SJP and third-party systems. CURO also integrates with Voyant, a cash flow planning tool, enabling partners to create bespoke, personal financial plans for their clients.

Another key system that we provide for our partners is called iBusiness, our partner back-office system. This is integrated with SJP's systems to produce illustrations as well as third-party tools to source, for instance, whole of market protection quotes. Partners are able to electronically submit business to both SJP's systems as well as many of our third-party providers. We will continue to invest to make SJP the place of choice for advisers and clients, a place where it's easy to do business by using relevant and appropriate technology.

And staying with the partnership. Ian touched on the Academy, an initiative where we are investing GBP 10 million in 2018 and have recently agreed to increase to spend in future years, an investment that will play an important and growing role in developing our next-generation of financial advisers. This will provide partner succession, support retention of long-term client relationships as well as build an inter-generational bridge to both manage and capture the significant inter-generational transfer of wealth in future decades.

Craig has also covered the progress of our Bluedoor program, a significant multiyear investment. Such major IT transformations can be tricky, as the experience of others over the years have shown. Hence, we are being cautious, going for bite-sized developments and migrations rather than attempt a one-off big bang. Whilst this caution means the project takes longer and costs more, it's safer, and therefore, it's the right approach. That said, whilst we have broken the back of the project and can see the end in sight, we still have much to do and we're not complacent. This is an important and necessary investment for us to ensure that we have the right processes and systems for the future. It will provide the capacity and capability for our future growth and supports the continued development of those client and partner portals I spoke about a little earlier.

Now as well as making it easier for partners to do business with us and investing in our administration capabilities, it is of equal importance we continue to invest in our investment management approach, thereby ensuring we always have sufficient investment capacity for our future growth. And we are doing exactly that. And I've just announced the launch of a new diversified asset fund that will be managed by KKR. This provides an exclusive opportunity for our clients to invest in the diversified portfolio of public and private market assets within a single investment fund, a strategy which has historically only been available to institutional investors.

We've also announced the appointment of Impax Asset Management to manage the renamed sustainable and responsible equity fund. With the addition of the diversified asset fund, together with the recent appointments of Impax, GMO, Wellington and Jennison, we now have an investment approach that spans 39 investment management firms from across the globe, with 36 exclusive strategies for U.K. retail investors.

In the first half of 2018, we also continued to enhance both the depth and breadth of the services we make available to our clients, adding, for example, new protection and medical insurers to our approved third-party providers as well as introducing a new foreign exchange and international payment service.

We also continue to invest in other areas. Our Asian operations are progressing well, and they have had a good first half. Gross inflows were up 51%, ahead of plan. Whilst net flows were up 47%, taking funds under management to over GBP 550 million, increasing by 32% during the 6 months. In addition, we have launched an international discretionary fund management service in Hong Kong, with a view to replicating this offering in Singapore and Shanghai in due course.

Rowan Dartington also continues to build scale, with funds under management now above GBP 2.3 billion, having almost doubled since the business was acquired in 2016. The number of investment executives continues to grow, up from 46 to 51 since the start of the year.

Of note, the client slide shows the growth in RD funds under management months-by-months, the yellow bars, together with the proportion of total funds that have been introduced by the partnership, represented by the black line, and which now stands at

25%. Hopefully, this gives you more information on how we are investing to support our future growth and how we are scaling our business to manage this growth.

So to summarize, the challenges individuals face in planning for and managing their wealth both before and after retirement as well as when considering the transfer of wealth to their next generation are considerable. Consequently, we continue to see a growing demand for trusted, face-to-face, client-focused financial advice and support. At the same time, it is a fact that there are not sufficient qualified individuals to meet this growing demand and an advice gap exists. Furthermore, we, and very importantly, our partner businesses, continue to invest in our respective infrastructure to ensure we are well-placed for future growth. The environment we are operating in, together with these investments, provides us with the confidence that we can continue to achieve our medium-term growth objectives. And supporting these objectives is a strong balance sheet, with the knowledge of a growing income from existing business. Both of these are supporting a growing return to shareholders, as shown by the 20% increase in the interim dividend.

So thank you for your attention. A summary of the key financials are shown on the current slide. Continued strong growth across all key financial metrics. And I will now ask Ian, Craig and David to join me for the usual Q&As. Thank you.

Questions And Answers

A - Andrew Croft {BIO 5711239 <GO>}

Got couple at the front here.

Q - Blair Stewart {BIO 4191309 <GO>}

Thanks very much. It's Blair Stewart from BoA. A couple of questions. Firstly, could you talk a little bit about the Bluedoor costs? The operational aspect seem to be on track. I just wonder if you can update on cost and the outlook. And by 2019, does that just drop away completely? Secondly, just interested if you can put any numbers around the productivity opportunity? I think you talked about a significant number of the advisers in the larger firms being inexperienced, with less than 3 years' experience. I wonder if you could just talk about that productivity opportunity. And finally, just on the -- some of the other investments you're talking about in there, Andy. With technology, it seems very interesting. Just wondered what you're spending there and where are that shown. Does that just come through in establishment costs or is it somewhere else?

A - Andrew Croft {BIO 5711239 <GO>}

Yes. So if I take the last one first. Look, we are spending all the time on IT. And that's just included in the establishment costs. So there is no separate line that we'll will be showing you in the future.

Q - Blair Stewart {BIO 4191309 <GO>}

(inaudible)

A - Andrew Croft {BIO 5711239 <GO>}

Above the line. Yes, it's above the line.

Q - Blair Stewart {BIO 4191309 <GO>}

Is that (inaudible)?

A - Andrew Croft {BIO 5711239 <GO>}

I wouldn't say as a -- particularly, as a proportion of total costs, no. It's going up every year. But our costs are going up every year as well. Another major area we invest in is cybersecurity, quite naturally. Craig, do you want to take the question on Bluedoor costs?

A - Craig Gentle {BIO 20095126 <GO>}

Yes. The guidance we gave back in February was that this year would see an annualized run rate equal to the run rate that we saw in the second half of last year, which I appreciate is a bit of a mouthful. But there was a change in intensity at the back-end of last year which continues into this. And that guidance largely holds. So I think if you look at the results -- in the cash result, it's probably running somewhere at around GBP 1 million ahead of where we might have expected. But as Andy referenced earlier, the important thing with this is to get it done well and to get it done right. We're not taking the cheapest approach to this. I mentioned the migration of pensions business. I think if you took a pure cost-based approach to that, you'd go for a big-bang approach. You'd do everything at once. Our experience, and I think the experience of others is that, that might not be the best approach. So we are taking this piecemeal because it gives us an opportunity to check, fix, check, fix all the way through. Having said all of that, I would say the guidance for this year, keeping it simple. If you were to look at somewhere in the region of double what we have for the first half, that would be, I think, a fairly accurate position.

A - Andrew Croft {BIO 5711239 <GO>}

Okay. Ian, do you want to take the productivity question?

A - Ian Gascoigne {BIO 4439479 <GO>}

Yes. I'm not sure I kind of got the actual numbers for you. But what we do know is that partners in their first 3 years are not as productive as partners who's have been with us 5 to 7 years. We also know that at 7 years, there are some partners who plateau and some partners who continue to grow. So I think we're very confident that we can look at the population of the people who joined this in the last 2 or 3 years, which is quite a substantial population. And we know they're going to grow their productivity year on year on year for the next 4 to 5 years.

Q - Blair Stewart {BIO 4191309 <GO>}

How many partners are less than 3 years?

A - Ian Gascoigne {BIO 4439479 <GO>}

How many partners have we got? How many advisers and partners less than 3 years -- Let me come back to you. I'll give the -- I'd rather give you the exact number -- of the number we've got in the first 3 years.

A - Andrew Croft {BIO 5711239 <GO>}

We have some questions from over the next --

Q - Oliver Steel {BIO 6068696 <GO>}

Oliver Steel from Deutsche Bank. You said that the quarterly performance was occasionally above and occasionally below the long-term target. And in the second quarter, gross sales were only up 10%. I don't quite get the explanation for that because I think in the first quarter of 2017, you grew gross sales by 32%. And then you did 21% in the first quarter of this year. Second quarter of last year, it was 29%, I think. And then it's suddenly 10%. And if we look at third and fourth quarters of last year, it was up about 27%. So clearly, something did happen, whether it was consumer confidence or something else, between the first and second quarters of this year. I'm just wondering what makes you so confident that, that can then bounce back in the third and fourth?

A - Andrew Croft {BIO 5711239 <GO>}

Okay. Well, I mean, I think as a long-term business, we're not focused on sort of discrete quarters quite, quite naturally, as there's quite a lot of difference between 2017 and '18. So for instance, in 2017, the ISA allowance went up 23% from 15,000 around somewhere to 20,000. It didn't go up this year, so you wouldn't have seen a repeat of that. If you look at -- and I know these all sound small things, but they all count. If you look at where Easter fell in 2018, then more tax [ph] year end business would have been done in the first quarter than in the second quarter compared to 2017. So we just look at the whole long-term, medium-term developments in the market and remain confident that over that period, we can continue to grow our medium-term growth objectives. Guys, I don't know whether anyone wants to add anything else at all? Obviously not. But yes.

A - Ian Gascoigne {BIO 4439479 <GO>}

Well, I mean as -- I could throw in the hurricane card here. And so that if we had gotten knocked-out in the first round, we would have had a stronger June. I don't see any evidence of a slowdown as well amongst partnership. The hot weather and the World Cup may have deflected ascension for a short period of time. But the trend is very positive. And I don't sense anything happening out there.

Q - Oliver Steel {BIO 6068696 <GO>}

Can I just follow-up on that? Because actually, again, if I look at the growth year-on-year, it's all in pensions. I think you're actually down in the other 2 product areas. Again, any explanation for that?

A - Andrew Croft {BIO 5711239 <GO>}

Well, it was -- sorry.

A - Ian Gascoigne {BIO 4439479 <GO>}

Partners are in the advice business, and they will go where people are wanting advice. And there is no doubt, in the last 12 months, there's been an explosion in consumers wanting to talk to their advisers about their pensions options. Now that doesn't necessarily mean it immediately leads to a pension business. But that is what we're experiencing, that people are wanting to talk about. And so it's no surprise that our pensions businesses are compared with other areas to me.

A - Andrew Croft {BIO 5711239 <GO>}

That's what I was going to say. Exactly the same. Also in (inaudible), again, are down. Supposedly, it's to increase this year as it was in previous years. So you wouldn't naturally see the growth you have done in the ISAs. Right behind you, Oliver. Actually, just pass it to Ed, it's easier.

Q - Edward Houghton {BIO 17612475 <GO>}

Just to pick up on Oli's question. It's Ed Houghton from Bernstein. To Oli's point, protections have been a significant proportion of net flows. Do you think those pension net flows might fall away as protections for higher allowances in prior years now also fall away? And you've had a boost, but does that fall away? And then relatedly, what proportion of those potential lost flows in pensions would you expect to see picked up in other product lines, ISAs, for example?

A - Andrew Croft {BIO 5711239 <GO>}

Sorry, could I just to say to the support team, we're picking up some noise at the back here. Someone talking. So I don't know whether that's something you can -- you're going to have a look at. Sorry, David, do you want to take that question?

A - David Lamb {BIO 15016583 <GO>}

Yes. I think it's -- what's interesting about the pension market is it's still unstable with change. And it's been in a sort of change, I think, as many years I've been here, which is, as you now know, 27 years. The current debate is about what's happening to lifestyle allowances and tax roofs and things like that. So my guess is that amount of uncertainty is not going to go away overnight. And therefore, pensions are not going to suddenly be a topic people won't want to talk about. Alongside that -- but one of things we haven't spoken about in terms of where partners spend their time, what Ian talked about, is inter-generational advice. And the whole rationale that people have looking it, how do we help our families and how do we look out for our wealth. That is a growing marketplace. So I think the marketplaces are moving and the demand for advice is very clear. What tax wrappers you end up investing in is a question of legislation, how legislation changes. So sometimes it's (inaudible). Now it's pensions that's being talked about. It could be ISAs. It could be yet another version of something that comes out in our government budget in November or in future governments. So the background is one of change. And change drives the demand for advice, and advice ends up being invested in different tax wrappers. So that isn't going to alter.

Q - Edward Houghton {BIO 17612475 <GO>}

Can I follow-up with one more as well? Again, I think this one's is for David. You announced the launch of this diversified assets fund with KKR. And that allows your clients to invest in public and private assets. I'm interested in how you've approached the potential liquidity requirements of your clients in respect of what are, potentially, relatively illiquid assets?

A - David Lamb {BIO 15016583 <GO>}

Absolutely. So we spent a long time, I think, designing the portfolio to enable us to balance these 2 things. How do you capture liquidity premium, recognizing though you've got to fund, which is essentially an open-ended fund. And that's not, traditionally, what happens in private assets markets. And the way you solved this is to have roughly 50-50 between private assets and liquid credit and other forms of quoted assets. So we can capture illiquidity for part of the portfolio, but maintain liquidity at the other part of the portfolio. That's a diversified approach. But it's also managed by single manager, and that helps us in terms of deciding, which parts of the illiquid market we're going to go into from one time into another, and which parts of the liquid market we will counterbalance that with. And ultimate -- the ultimate journey for us will be to launch a fully private assets fund. This is a very important step on that journey. I think it would be very well received, looking at the conversations we've had with people. But it's got to get [ph], again, that balance right. We spent a long time with KKR working on that balance.

Q - Andrew Crean {BIO 16513202 <GO>}

To the other side of the room.

Q - Haley Tam {BIO 4674831 <GO>}

It's Haley Tam from Citi. Could I ask a quick follow-up question on back-office infrastructure? Could you give us an idea of how much of the spend in the first half was actually the dual running cost? So we can maybe think about that being an ongoing cost for next year, but the rest maybe dropping out? And the second question, I'm sorry to come back to new business as well, but if we think about some of the longer-term drift trends, perhaps in the changes year-on-year, I noticed you didn't mention anything specific about transfers from DB to DC. I wonder if you have any comment there. And also, if there's any change in the competitive environment for your partners, perhaps, some other businesses emulating your business model.

A - Andrew Croft {BIO 5711239 <GO>}

Craig, you want to take the dual running costs first?

A - Craig Gentle {BIO 20095126 <GO>}

Yes. We haven't given an analysis of the figures. So we don't publish a dual running cost proportion. But I think the simple way to look at that figure within the cash result is that the whole lot falls away once migration is complete we turn the old systems off. So gradually, where we're able to identify clear, obvious dual running costs, we're building that into a figure that will disappear from the cash result.

Q - Haley Tam {BIO 4674831 <GO>}

So I say, when do you to complete? In the end of 2019? And how much longer (inaudible)?

A - Craig Gentle {BIO 20095126 <GO>}

Sorry, I can't quite hear you.

A - Andrew Croft {BIO 5711239 <GO>}

So at the end of 2019, does the dual running cost fall away?

A - Craig Gentle {BIO 20095126 <GO>}

Yes. Yes, the dual -- in any project, you're going to get some decommissioning. I think we referred to that at the previous results presentation. But yes, essentially, the dual running costs cease the moment we get everything on the new systems and we switch the old ones off. Because it's not just the systems, it's the surrounding bits of the system as well that create that dual running inefficiency when you're going through a migration.

A - Andrew Croft {BIO 5711239 <GO>}

And I'll just add that it -- obviously, we're showing it all separately. So it's not impacting the underlying cash result and therefore, not impacting the dividend sort of conversation. If I do the transfers, there's 2 parts to the transfer market. And I'm going to talk about the defined contribution market first. So more and more people don't have the benefit of defined-benefit pensions. They've bought being sort of accumulating funds in DC ports [ph]. They no longer need to take an annuity, and actually, in our marketplace, they probably didn't have to previously. And more and more individuals are going into income drawdown. We expect that market to continue to grow and all the statistics we've got from another external commentators would suggest that.

And we see that as a big market. People accumulating their various small pension ports and bring them into one, to go into income drawdown. The second part where we've seen more interest, and if you bear in mind, we're the sort of the largest advice brand in the U.K., it's not surprising, is a lot more interest in DB transfers. This is a very, very complex area. And for lots of people, it isn't appropriate. We are taking a continued cautious approach to this. So we see relatively low numbers in absolute terms. But each number tends to be a larger transfer. We haven't disclosed it. We're not planning to disclose it. But that market is still there. But we are just treating it with real caution.

A - Ian Gascoigne {BIO 4439479 <GO>}

Her question about competition.

A - Andrew Croft {BIO 5711239 <GO>}

I'm sorry, the competition. Thank you.

A - Ian Gascoigne {BIO 4439479 <GO>}

Yes, the -- I'm not -- I don't think our partners are experiencing any increase in competition for business at all. Compared with the kind of massive opportunity in terms of the baby-boomer generation, the advice gap, increased IHT, pensions complication, that far outweighs -- the opportunity far outweighs any experience of a new kid on the block or anything, which I'm not aware of. And I don't think any of our partners are saying to me that they've -- they're finding competitive pressures at all.

A - Andrew Croft {BIO 5711239 <GO>}

Okay. Should we try down that side? There we've got Gordon and Ben. Gordon goes first. And then over to Ben.

Q - Gordon Aitken {BIO 3846728 <GO>}

It's Gordon Aitken from RBC. Yes. Just a -- first question, follow-up on the pensions. Obviously, it's such a big part of gross sales now. But I mean, can you give a rough split of -- you talked about consolidation of ports [ph] and then DB to DC. And we've always said it's -- consolidation of ports is a big driver. But is that continually still the case? And the second question, on outflows, I mean, I guess, the 2 main buckets that you lose flows to are probably number one, deaths; and number two, bank of mom and dad. You talked a bit about both of those and what you're doing to reduce the impact. And maybe -- and back to mom and dad, is it becoming bigger threat?

A - Andrew Croft {BIO 5711239 <GO>}

I'll do the outflows first. So where we see outflows are people taking regular income withdrawals. I mean, that's exactly what we expect owing to income drawdown or in the investment bond arena. They're taking regular income. The other area we are seeing is actually as you say, through deaths, where we will see some money that leaves because people have reached the end of their investment time horizon. And I'm sure there are some to do with bank of mom and dad. But the other thing that we have is the ability for bank of mom and dad to borrow funds of their -- secured on their investments. And that certainly is quite a popular thing. I wouldn't say we are seeing any large outflows as a result of bank of mom and dad. In terms of pensions, and again, I might turn to David in a minute, but how much an individual can save in pensions on a regular basis these days isn't a huge sum of money. So the majority of the pensions business will be transfers, and predominantly, DC transfers. David, I don't know if you want to any to --

A - David Lamb {BIO 15016583 <GO>}

No. I'd just point out demographic move -- we talked about inter-generational wealth transfer. And there's a big demographic move in terms of people coming into that stage, where they're thinking about retirement, and I have some experience of at present. And what that means is we're seeing that still ongoing right now. So that's a very live marketplace, and it's not just -- it is a growing marketplace. So there's transfer market, DC, DB, and the ability to not have to take an annuity via the income and these -- and pension planning, let's say, IHT planning. So that's a large part of the conversation in the retirement marketplace in terms of planning terms. That cohort the demographic cohort is not yet mature. That's still coming. We are probably just beginning to see the first generation of nonfinal salary pension retirees in the U.K. So there's quite a lot of growth in this part of the market.

A - Andrew Croft {BIO 5711239 <GO>}

Gordon, do you want to pass the mic over to Ben.

Q - Benjamin Bathurst

Hi. Ben Bathurst from Soc Gen. First question is on the Academy. I think Andrew mentioned that you've agreed to increase the spend in that area. I just wondered if you could give some guidance on the quantum of that increase? I think that's new information today. And then secondly, on interest rates, I market expectations for the MPC to increase interest rates this week. At what level do you think the attraction of the high returns from cash might start to eat away demand for your investments?

A - Andrew Croft {BIO 5711239 <GO>}

Craig, do you want to do the Academy?

A - Craig Gentle {BIO 20095126 <GO>}

Yes. The Academy investment that we were referring to will -- it sort of starts now and continues. I would imagine, if we were to think of it in terms of somewhere between 10% and 15% for next year, subject to an update at the end of the year, I think that would be a reasonable amount to go for.

A - Andrew Croft {BIO 5711239 <GO>}

So not material amounts. David, you want to do the interest?

A - David Lamb {BIO 15016583 <GO>}

On the interest rate one, it's interesting. When we talk to clients about investing, we try to make it really clear that you need to keep some money to one side for emergency things that happens in your life that you don't expect. And that's the cash element. Whether you end up a 0.25% or 0.50% or 0.75%, that is not conversation about investment. When you're investing, you're investing for the longer term. And there, your expectations of return are much higher, albeit with different risks. So a move from 0.50% to 0.75% on base rate is not going to alter that conversation or alter the demand for investments.

A - Andrew Croft {BIO 5711239 <GO>}

A few more on -- down this side, if we may.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Ashik Musaddi from JPMorgan. Just a couple of question on investment performance. I mean, first half has been a bit volatile, first quarter more volatile than second quarter. Any thoughts on how your active investment managers have done relative to their peers? Any numbers on that would be very helpful. Secondly, I mean, given that year adding KKR, which is more of an alternate investment idea, how should we think about the fees that you are paying to them? Is it similar to what you have been doing with others, around 30, 35 basis points, or is it more on the higher side? Any thoughts on that. Should we be -- does that lead to any sort of margin contraction, overall? I know it would be very small because this is just one of the many 39 you have. But any implications for the forward-looking margins?

A - Andrew Croft {BIO 5711239 <GO>}

I'll let David take both of those. Good job he's not retired yet.

A - David Lamb {BIO 15016583 <GO>}

I'll take the second one first. So KKR, no impact on margin whatsoever because we have our standard charge and then the extra amount of fees are added on to that. And so the KKR on are filled in on top of our normal charge. So margin, no impact. In terms of Q1, Q2, it's really interesting this year. So first quarter, negative. Second quarter, much more positive for markets. If you look at our fund performance and look at those relative in terms of their peer groups and other competitor fund, this time last year, RBC's funds -- global equity funds are doing really well. U. K. [ph] funds are behind the curve. This time, this year, our U.K. are way ahead of the curve in terms of markets. And -- but our RBC funds are about 50-50. The interesting one to look at though is -- look at rolling 3-year, rolling 5-year client returns. It's been really stable over the last 4, 5 years now at 7% to 9%. And that's sort of a relatively tight band. That's still happening. And I think that's the important thing to focus on.

A - Andrew Croft {BIO 5711239 <GO>}

I'm conscious of time. So we'll take 2 more questions. Barrie and Andrew. Look, we're around afterwards for coffee. But I know some of you need to get away. Andrew?

Q - Andrew Crean {BIO 16513202 <GO>}

Andrew Crean, and Autonomous. Can I back to Bluedoor thing? And could you be clear, what is the likely spend in '19 over '18 and the dropoff in '20? That's what people have tried to ask for. And then second, if I (inaudible) question. I mean, you talked about growth in funds under management related to the number of partners and things like that. But do you any analysis of the amount of money that you manage for each customer and whether you can capture more of their assets? I suppose related to that, you were talking about the apps and stuff like that, which the clients can get access. Do they actually use them? Is there much engagement?

A - Andrew Croft {BIO 5711239 <GO>}

Who can answer the app question?

A - Ian Gascoigne {BIO 4439479 <GO>}

Yes, the partners, there's a range of partners, and there's a range of partner styles and their interactions with their clients. So some partners are very techy, use cash flow forecast and use all the technology and work with their clients in very in-depth, analytical, report-driven approach to financial planning. Other partners don't do any of that and are more talk about concepts and savings and having a relationship and I'll look after you, and it's a touchy-feely journey with the person. Both trying to help the client achieve their financial goals. So who uses what is very, very relative to the actual style of the specific adviser and the practice they're in. So some are very techy, some aren't. The important thing is that we facilitate all approaches and styles, and we have that available. The important thing is that we want to see technology supplementing the partner relationship, not replacing the partner relationship. That's the key of our approach.

A - David Lamb {BIO 15016583 <GO>}

And on the funds under management fees, what's interesting is that you see clients' funds under management where there's increase of the relationship duration. So in other words, if you look at average investment in the first 3 years and look at it again 3 or 4 years later, you will see an increase. Not just because of fund growth, but actually, as the relationship develops and mature, we end up having a deeper relationship with our clients and it increases over time.

A - Andrew Croft {BIO 5711239 <GO>}

Craig, do you want to just go the --

Q - Andrew Crean {BIO 16513202 <GO>}

You don't -- you can't measure that at all, can you?

A - David Lamb {BIO 15016583 <GO>}

We do measure some of those metrics. Yes, we do, without [ph] publishing them.

A - Andrew Croft {BIO 5711239 <GO>}

Craig, do you just want to clarify the Bluedoor one?

A - Craig Gentle {BIO 20095126 <GO>}

Yes. So the figure that I'm referring to that will fall away in the cash result for the first half of 2018 is GBP 15.2 million net. Just for the sake of really simplistic modeling, let's imagine that, that GBP 15 million were to turn into GBP 30 million to the end of the year. And this isn't guidance for next year yet, but let's imagine that, that also repeated itself in 2019 as we complete the migration of bonds. Then that same GBP 30 million would not reappear in 2020.

Q - Andrew Crean {BIO 16513202 <GO>}

Thanks.

A - Andrew Croft {BIO 5711239 <GO>}

Just pass it back to Barry. We call this is the last question. So I know there's a few the other hands, but we are around afterwards. Since they can't -- these people need to get away. Barry.

Q - Barrie Cornes {BIO 2389115 <GO>}

Thank you. Couple of questions. Barrie Cornes, Panmure. Andy, you mentioned the -- not everyone takes the DB to DC transfer, it's not appropriate for everyone. Can you just give us a flavor of what sort of percentage either don't get advice or don't take that switch, please?

A - Andrew Croft {BIO 5711239 <GO>}

Again, that's quite hard. So we have advice guidelines. So on a regular basis, our clients will be -- or clients will be having conversations with partners, where the partner says you should not even contemplate transferring a pension. We don't actually capture that information so I can't give you an accurate one. What I will say is every defined-benefit pension transfer we do has to be preapproved by an independent compliance team in Cirencester.

Q - Barrie Cornes {BIO 2389115 <GO>}

Okay. Thank you. Okay. And the other question I had was on the FSCS. I appreciate there's a timing issue this year around, but going back a few years, I think you talked about how high it was for specific reasons and hoped that it would come down. Any signs of that happening?

A - Andrew Croft {BIO 5711239 <GO>}

Craig, your word now?

A - Craig Gentle {BIO 20095126 <GO>}

I still hope it will come down. It's probably the main thing. I think that the construct of what it is FSCS is dealing with has probably changed and evolved over the last few years. What we saw a few years ago was some very big obvious cases that required attention and bailing out. It's still not uncommon to read of organizations that you never heard of that impose, actually, a pretty heavy demand on FSCS. So whilst I'd love to say there will be a beneficial impact of improvements in the way the world is working, I'm not sure I can point to anything like that. There are also some consultation papers out there that could reshuffle the way FSCS is charged. And I don't actually see there being a terrific amount of net threat or net benefit in that either. And I'm afraid, other than that, there's not much more I can say. But I like to be positive and hope that it stabilizes and come down.

Q - Barrie Cornes {BIO 2389115 <GO>}

Okay, thank you.

Q - Andrew Crean {BIO 16513202 <GO>}

Okay, thank you very much, everyone. I appreciate -- there were couple of hands we didn't get to. But we are here, as I say. If you want to come up and grab us. Thank you for coming today.

Operator

Ladies and gentlemen, this concludes today's call. You may now disconnect your lines. And have a lovely day.