Phoenix

Full year 2021 results transcript

2021 review

Andy Briggs, Group Chief Executive Officer

Good morning, everybody and welcome to Phoenix Group's 2021 Full Year Results Presentation. I am delighted to be back presenting in person, and it is great to see you all here. Thank you for coming.

It's clearly been an extraordinary two years since I started, firstly with the pandemic, and now with the tragic war in Ukraine. And our thoughts, of course, go out to all of those affected.

Before we take you through our results, we wanted to share the new visual identity of Phoenix Group, which has been designed to embody our purpose, and better reflects the growing, sustainable business we now are.

Under our new Group brand strategy, Phoenix Group will be our master brand, and employer brand and endorse our powerful consumer brands, of Standard Life, SunLife, Phoenix Life and ReAssure, who will be part of Phoenix Group. A powerhouse of brands that together, will support us in delivering our purpose and our strategy.

Visual identity is important, but what a brand stands for is really critical. I passionately believe that the best businesses have a core social purpose, which is why ours is, helping people secure a life of possibilities. Helping a broad range of people in the UK, to journey to and through retirement, and enjoy a better later life.

As a purpose-led organisation, we are committed to delivering better outcomes, for all of our stakeholders. It is only by having the best people, who are focused on our purpose, that we can deliver better outcomes for our customers and wider society, and in turn, produce stronger returns for all of our investors. The virtuous circle you see on this slide.

So how have we delivered for investors in 2021, against our financial framework of cash, resilience and growth? 2021 has been an outstanding year for Phoenix and extends our excellent track record of financial results.

We delivered record cash generation, once again exceeding our target range for the year. Our balance sheet remains strong, with our Shareholder Capital Coverage Ratio at the top-end of our 140% to 180% target range. And we have generated record new business long-term cash generation, up 55% for the year.

I am delighted that 2021 was the year that we have proven the wedge, the hypothesis first set back in 2018. In fact, we have more than proven the wedge, with £1.2bn of new business long-term cash generation from our Open business, exceeding the £800m per annum, needed to offset the Heritage run-off.

And the investment we are making into our Open business means that we are now confident of delivering ongoing organic growth, which will more than offset the Heritage run-off, year after year.

In addition, we have unique, market-leading capabilities, and a proven track record of generating further value, both by delivering management actions, and by executing more M&A. Phoenix is now a growing, sustainable business.

As a result of our strong outperformance in 2021, and having met our two conditions for dividend growth, the Board has recommended Phoenix Group's first ever organic dividend increase of 3%. This increase reflects both the growth in our business, and our strong delivery of management actions during 2021.

Our new, increased level of ongoing dividend is just as sustainable as it was before. As you can see on the chart, our dividend track record is strong, and we have significantly outperformed the wider FTSE 100, over the past seven years. However, until now, our historical dividend increases have only come from M&A. What is really exciting, is that we now have two sources of potential dividend increases, both organic growth, and inorganic growth.

We have therefore evolved our dividend policy to reflect this, and Rakesh will cover this later.

Organic growth is a huge step for Phoenix, and significantly enhances our investment case. But what remains unique about Phoenix, is both the dependability and resilience of our cash.

We are confident that the cash from today's in-force business, without any new business, or any M&A, can pay our current, increased dividend, over the very long term. There are very few stocks, in any sector, that can say that.

And unlike any other insurer, our cash is also extremely resilient, due to our hedging approach. As you can see here, in any market conditions over the last 5 years, our Solvency II economic variances have been negligible. This is clearly a huge advantage, and differentiator, in times of significant market uncertainty, such as we have today.

And we continue to grow. Both through our Open business, and through further M&A. And as our business grows, so will our dividend, while fully maintaining its sustainability, and resilience.

Putting all this together, I am sure you will agree, is a unique, and highly attractive combination.

So that's the numbers. What have we been focused on to deliver them? We have five strategic priorities that structure how we deliver our purpose and strategy, across Heritage, Open and M&A. These are the key programmes and initiatives that will build distinctive capabilities, to win in our chosen markets.

Let me talk through our progress, during the year, against each of these strategic priorities.

Optimising our in-force business is the bedrock of Phoenix. It is a market leading capability that we have built up over many years, and we have undertaken a range of actions during the year. In particular, I am delighted that we have delivered a record level of management actions in 2021, at £1.5bn, which included £550m, from our internal model harmonisation programme.

And the investment in our asset management capability is delivering tangible results, with £3bn of new illiquid asset origination, at a strong average illiquidity premium of 70 basis points.

Enhancing our operating model and culture is our second strategic priority. Again, this is a distinctive capability that sets Phoenix apart from others.

During 2021 we have, once again, demonstrated how good we are at realising significant cost and capital synergies from our integrations, with substantial further synergies in the year.

Across our two integrations, we have now delivered over £2.5bn of synergies, having exceeded our target on Standard Life, and delivered 89% of our target for ReAssure, in just 18 months.

These are huge numbers, and demonstrate the significant value we create through M&A.

This is underpinned by our unique capability of delivering multiple integrations concurrently, as we delivered both the migration of Old Mutual Wealth customers, onto our ALPHA platform, and the ongoing migration of Phoenix customers from Capita to TCS.

Turning to our people and culture on the right of the slide. A clear area of focus for me, during 2021, has been investing in the development of our fantastic internal talent, to support our ambitions. As well as strengthening our teams through the hiring of market-leading external talent, to bring new skills to the Group.

I am also pleased that our focus on increasing female representation is beginning to develop momentum, with the number of females in our top 100 leadership positions increasing from 21 to 31.

Finally, it is always important to see our efforts reflected in an improved colleague engagement score. In particular, our colleagues tell us that our strong sustainability agenda is of real importance to them.

Our third strategic priority is to grow our business, to support both new and existing customers. We are investing in people, processes and technology, to build a market leading Open business. I am determined that our Open business growth strategy is balanced, over time, between BPA, and our capital-light, asset based businesses, such as Workplace.

And having acquired the Standard Life brand last year, we are leveraging this trusted brand, to accelerate our growth.

The investment into our Retirement Solutions business delivered a strong year in BPA, with £5.6bn of premiums written, whilst reducing our capital strain. But to be clear, we are not growing in BPA at the expense of our resilience, with a balanced portfolio, and low credit risk sensitivity, remaining our long-term ambition here.

I was also delighted that we saw clear momentum building in our Workplace business, with 41 new schemes won during the year. This demonstrates the strong proposition we now have and is evidenced by us being awarded Master Trust Offering of the Year, by Pensions Age, for the second year in a row.

While these new schemes wins are small in terms of assets, it is an important milestone, with advisers giving us the opportunity to prove ourselves on these smaller schemes, before we hopefully begin winning the larger schemes in time.

And finally, we have maintained yet again, yet again, our high customer satisfaction scores, exceeding our targets for the year.

Our fourth strategic priority is to innovate, to provide our customers with better financial futures. The UK faces a significant retirement savings gap, which we are committed to helping close. To do this, we will provide people with the right guidance and products, at the right time, to support the right decisions.

Key successes in the year include the development in our digital capabilities, which supported a 16% increase in customer logins across our Standard Life digital platforms. As well as the development of a roadmap to transition 1.5m customers, and over £15bn of assets, into a sustainable default fund, which is now in train, enabled by the strengths of our core strategic asset management partner, Aberdeen.

I am also really excited by the 2022 programme of work from our new think tank, Phoenix Insights. We will use research to lead fresh debate, prompt a national conversation, and inspire the action needed to make better longer lives a reality, for all of us.

Be sure to keep an eye out for the launch of our Longer Lives Index, on 30th March, which explores the UK's preparedness for longer lives.

And our fifth priority, is to invest in a sustainable future. As the UK's largest long-term savings and retirement business, we are responsible for managing over £310bn of assets, on behalf of our 13m customers.

Our customers and shareholders trust us to keep their money safe, and provide them with strong long-term financial returns, while using our scale to play our part in delivering a sustainable future.

That is why we are integrating ESG across our business, investing responsibly, and progressing towards our commitment, of being net zero by 2050.

A clear demonstration of the impact our scale affords us, is the £1.3bn that we invested into sustainable assets during 2021. For example, we invested over £500m into affordable housing, which helped support some of society's most vulnerable people.

And invested over £200m into projects with a positive environmental impact, such as the provision of renewable electricity, to nearly half a million homes.

So, in summary, 2021 was a pivotal year for Phoenix, as we have now proven the wedge, and are confident of proving it going forward.

The Board has recommended our first ever organic dividend increase of 3%, which remains just as sustainable over the long term

Strong progress has been made against our five strategic priorities, as we deliver on our purpose and strategy.

We offer an attractive dividend that is funded by our in-force business over the very long term. It is uniquely resilient. And both our organic and inorganic growth can now support future dividend increases.

And with that, I will hand over to Rakesh.

2021 financial results

Rakesh Thakrar, Group Chief Financial Officer

Thank you, Andy, and good morning everybody, it is great to see you all here.

As Andy said, Phoenix has delivered a strong financial performance in 2021. We delivered record cash generation of just over £1.7bn in the period, maintained our strong Solvency balance sheet, and achieved a 55% year on year increase in incremental new business long-term cash generation of £1.2bn.

And having met our two conditions for organic dividend growth, the Board has recommended our first ever organic increase of 3% in our final dividend, equating to a total dividend of 48.9 pence per share.

As you can see from this slide, our record financial results reinforce our consistent track record of delivering cash, resilience and growth. For example, our cash generation has more than doubled over five years, while our dividend has increased by 8%.

Meanwhile our Solvency II surplus has nearly tripled over five years, and our shareholder ratio has increased by 16 percentage points.

And in terms of growth, our assets under administration have more than quadrupled, and our incremental new business long-term cash generation has grown to nearly £1.2bn, in just four years and from a standing start.

Turning first to cash. With strong cash generation of £1.7bn, we have once again, exceeded the top-end of our target range of £1.5bn to £1.6bn for the year.

This exceptional level of cash generation reflects the synergies generated by the integration of the Standard Life and ReAssure acquisitions.

We are also today setting new one-year and three-year targets, with the latter becoming a rolling target that we will update every year going forward. For 2022, we have set a target range of £1.3bn to £1.4bn of cash generation.

This is lower than 2021 due to a reduced level of integration capital synergies going forward, having over delivered on both integrations already.

Our three-year cash generation target is £4.0bn, and guidance over the life of the business is now £17bn.

As ever, I do just want to remind you that Phoenix's cash generation guidance is conservatively based on our in-force business only.

It excludes the benefit of any future new business or M&A, and also excludes management actions from 2025 onwards.

Looking over the period from 2022 to 2024, this slide sets out the Hold Co uses of cash generation. This includes operating costs, debt interest, and our increased dividend. It also reflects debt maturities and call dates, which includes a £450m repayment due in July this year.

The slide highlights the significant amount of surplus cash that will be generated over this period. We expect £1.7bn to be available for both organic growth through BPA, and inorganic growth through M&A.

Group long-term free cash was £13.2bn at the end of 2021, broadly flat on the prior year. Importantly, our recurring sources of cash exceeded our recurring uses by around £300m in the year.

We have made a significant investment into our growth ambitions during the year, with the incremental costs we expect to incur to support our growth ambitions capitalised into long-term free cash, with a total £200m impact.

We have also recognised a £200m adverse impact from the industry-wide transition from LIBOR to SONIA.

After the servicing of debt until maturity, there is £11.8bn of cash available to shareholders.

With our future increased dividend cost of around £0.5bn per annum, this level of Group cash from our in-force business supports our dividend over the very long term.

Our Solvency II capital position remains strong, with a resilient surplus of £5.3bn, which includes the deduction of our 2021 final dividend, while our Shareholder Capital Coverage Ratio has increased to 180%.

We operate a target shareholder ratio range of 140% to 180%. Our ratio is at the top-end of that range, which means we can invest in both organic and inorganic growth opportunities, to drive future returns.

Our Solvency II surplus has remained resilient through the year, and the additional value we generated through management actions provided us with the capacity to invest into growth. This includes our allocation of £0.4bn of capital to BPA in 2021.

We also continued to invest into our people, processes and technology, which underpin our future growth ambitions, with these costs now reflected in the Solvency balance sheet within our expense assumptions.

While the surplus remained stable year-on-year, our ratio has increased by 16 percentage points, primarily due to the strong over-delivery of management actions.

We have a particularly low appetite to equity, interest rate, inflation and currency risks, which we see as unrewarded and therefore hedge to protect our Solvency II surplus.

This translates into the low sensitivities presented here, under our new harmonised internal model. We also manage our longevity risk through reinsurance, retaining around half of the risk across our current in-force book, and reinsuring most of the risk on new business.

We see credit risk as rewarded and so actively manage our portfolios to ensure they remain high quality and diversified.

The key sensitivity we focus on here is a full letter downgrade of 20% of our credit portfolio, which is currently £0.4bn, and small in the context of our £5.3bn Solvency II surplus.

It is also worth noting that the credit sensitivities we disclose here are prudent, as they assume no management actions are taken to rebalance our portfolio, which is different to how many of our peers disclose.

We will continue to manage our credit risk sensitivity as we grow in BPA, through operating a balanced portfolio and with active risk management.

As a consequence of our hedging approach, we are far more resilient to the major market risks than our UK peers, as this slide clearly demonstrates. This low sensitivity is especially important during times of market volatility, such as we have at present, and remains a key differentiator for us.

This resilience allows us to operate with a 140% to 180% target range for our Shareholder Capital Coverage Ratio.

We manage over £310bn of assets on behalf of our customers and shareholders. And we have invested significantly into our asset management capability, which oversees this key responsibility.

We currently partner with ten global asset managers to manage our portfolio, which provides us with access to a wide range of new assets to support our growth aspirations, with the expertise of our core strategic partner, Aberdeen, a major advantage to us here.

In order to manage our credit risk, Phoenix maintains a diversified £40bn shareholder credit portfolio, split between liquid and illiquid credit. Our £12bn illiquid credit portfolio comprises 29% of annuity backing assets, and we continue to target increasing our allocation of illiquid credit assets to around 40% over the medium term.

The proactive management of our shareholder credit assets has enabled us to uphold the high credit quality of this portfolio, where we manage our sector exposures to minimise our risk.

Integral to this is ensuring we operate within our conservative risk appetite for our BBB exposure being below 20%. At the end of 2021 we were at 17%, while our exposure to BBB- remains very low at only 3%, and we have had no defaults during the year.

Also, given the current situation, I just wanted to flag that we no longer have any shareholder credit exposure to Russia or Ukraine, nor any exposure to sanctioned banks.

Long dated, or illiquid assets provide excellent cash flow matching for our £42bn annuity book and are a key enabler of reducing the capital strain on our BPA business too.

Reflecting the ongoing investment into our capability and team, during the year we increased our illiquid asset origination by 48% to £3bn, with an average credit rating of single A.

The strength of the team we are building is demonstrated in the strong average illiquidity premium we achieved this year. We were able to rotate out of liquid credit assets, into illiquid credit, at the same credit rating, for a yield pick-up of around 70 basis points.

We have also increased our investment in sustainable assets to £1.3bn, which is now based on a rigorous definition of sustainable assets developed with Sustainalytics

Importantly, our illiquid origination strategy is designed to diversify our risk. We do this through using the best asset managers in each asset class and geography, as well as by limiting our credit concentration risk.

Our ability to deliver value accretive management actions is a key differentiator for Phoenix. I am therefore delighted that we have delivered record management actions of £1.5bn during the year.

This included a strong performance of around £700m from business as usual activity, including illiquid asset origination and asset risk management actions.

In addition, our internal model harmonisation success provided a significant contribution, at around £550m, the majority of which was a reduction in SCR.

With most of our capital synergies now realised, these will be lower in the future, until the next M&A transaction.

Going forward, there continues to be further BAU actions for us to realise.

We continued to make great progress across both integration programmes in 2021, with £824m of further synergies in the year. A big contributor was of course the internal model harmonisation, which delivered up-front capital synergies of around £550m from Standard Life, exceeding our previous expectation of around £400m.

It also supports future capital optimisation actions and underpins our future M&A ambitions. We have now delivered over £2.5bn of synergies from Standard Life and ReAssure, with nearly £2bn of this realised through capital synergies.

We have also taken the strategic decision to re-phase our Standard Life customer & IT migration programme, with the legacy policy migrations now expected to complete by 2025.

We are looking to accelerate some exciting new capability development on TCS BaNCS, to support our future Workplace growth.

Moving now to growth. We have reported a 55% increase in new business long-term cash generation to £1.2bn. The biggest contributor was Retirement Solutions, where a strong year in BPA delivered £950m of long-term cash generation, an 82% increase on 2020.

Elsewhere, it was great to see our Asset-based businesses deliver increased long-term cash generation year-on-year, after adjusting for the disposal of the platform businesses to Aberdeen in 2021.

We remain focused on only allocating capital to the highest return growth opportunities for our shareholders. The investment we have made into developing our BPA and asset management capabilities has supported us in writing £5.6bn of premiums during the year.

Our capital strain has reduced from 9% last year to 6.5%. This is fantastic progress towards our target for 5% over the longer-term.

Having completed two significant transactions of £1.7bn and £1.8bn, it is clear we have become an established BPA market player.

We also continued to maintain our discipline in a competitive market, as evidenced by the double digit IRR we achieved on our transactions in 2021.

As we enter 2022, we are confident in the outlook.

Due to the surplus cash generated by our in-force business, we are now able to invest around £300m of capital into BPA annually. We are expecting a larger market in 2022, at £30bn to £40bn, but do expect the market volumes to be more weighted to the second half based on our pipeline.

However, I am delighted to report that we have already won 2 external transactions this year, covering £600m of liabilities, and expect these to complete in the second quarter. And we also expect to buy-in the remaining Pearl Pension Scheme liabilities of around £750m in the second half.

So that is a total of nearly £1.4bn already in-train during the first quarter, which is a great start to the year.

We will of course continue to retain our pricing discipline through our focus on value over volume, and while individual deals will vary, we expect to see broadly similar transaction economics in 2022 as we did in 2021.

Turning to our IFRS results. We delivered strong operating profit of £1.2bn in 2021, 3% higher than the prior year. Operating profit in our Heritage business increased year on year primarily reflecting a full year of profits from ReAssure.

Our Open business operating profit reduced slightly year on year, due to a £100m lower longevity benefit in 2021 and a strengthening of expense assumptions to reflect our investment into our growth capabilities. This was partly offset by stronger new business profit from BPAs.

The sizeable swing in investment return variances and economic assumption changes reflects the impact of our hedging strategy from rising rates and equities.

We hedge the Solvency position to deliver dependable cash and dividend resilience and to protect against market uncertainty and accept that this will cause volatility in our IFRS balance sheet.

Having proven the wedge and recommended our first ever organic dividend increase for 2021, the Board has chosen to announce a new dividend policy, to better reflect the growing, sustainable business that Phoenix now is.

We have therefore replaced our previous stable and sustainable dividend policy with a new policy that sets out our clear intention to pay a dividend that is sustainable and grows over time.

It is important to emphasise that the Board will, above all else, prioritise the sustainability of our dividend over the long term. But we can now grow both organically through our Open business and inorganically through M&A.

The Board will therefore assess annually whether business growth can sustainably fund a dividend increase.

We see this new dividend policy as a critical evolution in Phoenix's investment case.

So, to conclude, we delivered record financial results in 2021, across our financial framework of cash, resilience and growth.

And we have a clear set of targets for 2022. This includes our one-year target of £1.3bn to £1.4bn of cash generation in 2022 and £4bn over the three years to 2024. And we will retain our resilient balance sheet, by operating within our target ratio ranges for Solvency and leverage.

In terms of growth, we are now confident of proving the wedge going forward, through generating in excess of £800m of new business long-term cash generation annually, and we also remain focused on completing value accretive M&A.

And with that, I will now hand you back to Andy for the outlook.

Outlook

Andy Briggs, Group Chief Executive Officer

Thank you, Rakesh. There are four major trends in the UK long-term savings and retirement market. And these offer Phoenix multiple growth opportunities.

The Heritage M&A market is huge at around £480bn. And with the BPA market estimated at over £2tr of uninsured defined benefit liabilities, many would say the current £40bn per annum of flows, will be exceeded in the future.

While the Workplace and individual retirement solutions markets, each with an estimated £40bn of annual market flows, represent significant capital-light growth opportunities for us, over time.

We have a clear and differentiated strategy, which creates shareholder value, through leveraging all four of these major market trends.

Heritage is the bedrock of our business, which delivers high levels of predictable cash, that covers our dividend into the very long term. And it also generates surplus cash, that we can re-invest into both our Open business, to support organic growth, and into M&A, to support inorganic growth. Both of which can support future dividend increases.

We are very focused on optimising every pound of shareholder capital, through a rigorous capital allocation framework, that ensures we only invest in those growth opportunities that drive real value.

Heritage and M&A are unique, market-leading capabilities for Phoenix, and create significant value. While the investment we are making into our Open business, will develop market leading capabilities here too.

But what is particularly attractive about Phoenix, is how the whole is greater than the sum of the parts.

By reinvesting surplus cash into Open and M&A, we are effectively generating further in-force business. And as we apply our distinctive Heritage capabilities of optimising our in-force business, and enhancing our operating model, to this further in-force business, we will have material competitive advantage, and hence will generate significant shareholder value.

Let me give some specific examples. For our Open business, the Heritage book enables significant capital efficiencies, particularly in our Retirement Solutions business, so BPAs.

This is because we can diversify the different risks, across the two portfolios, which reduces the capital we have to hold under Solvency II . Others, without a Heritage business, cannot do this.

Another example is that our strategic partnership with TCS, driven by the scale of our Heritage business, provides us with a market leading, cost per policy, administration platform, that will give us a meaningful cost advantage for our asset based businesses.

And our scale in Heritage means our Open business has access to around 13m customers, where we can meet a broader range of their needs over time. Including helping them consolidate their pensions, and journey to and through retirement, with us.

Now to be clear, we are not fully leveraging these advantages for our Open business today. We need to invest to fully do that. But if you think about the progress we are making, and the structural competitive advantage we will have in time, I think this is really exciting. Because this is the same logic as when we do M&A.

We have demonstrated how we leverage these core Heritage capabilities, to the further in-force business we acquire inorganically. Our Heritage business enables us to generate significant cost and capital synergies, that underpin our track record of shareholder value creation in M&A.

So let me talk further on M&A. M&A has always been a key part of Phoenix's DNA, and very much remains a core part of our growth strategy. Like my predecessor, I'm very fond of cups of tea with my fellow insurance CEOs. Indeed rarely a week goes by when I don't partake. And when I meet with these CEOs, the message from most of them is very much one of when, not if.

This is because, over time, the attraction of the steady cashflows is overtaken, by the cost challenges of legacy IT, and the burden of regulatory change. In addition, insurers across the market are looking to simplify their strategies and seeking to unlock trapped capital for reinvestment. We therefore have a clear M&A strategy that responds to these drivers.
We are, unquestionably the market leader in Heritage M&A, and have a proven track record of delivering significant shareholder value, through cost and capital synergies.

Phoenix is also a trusted counterparty for vendors and is well known as a safe home for customers, so we are one of the first names on the call list, for any potential disposals.

In terms of the market opportunity, we believe that the £480bn UK Heritage market can be broadly split into two parts. The first is a small number of large portfolios, that might come to market over time. While the likelihood and potential timings remain uncertain, we will be keen and enthusiastic if they do.

The second category comprises a larger number of small-to-mid sized portfolios, which have an estimated consideration of up to £1bn. These could be funded from our own resources, and therefore would be strongly accretive for our investors.

The feedback from CEOs here is when not if, so there is likely to be a series of these opportunities, over time. And we stand ready to do our next deal, enabled by our scalable platforms, and our £1.3bn of available firepower.

2022 will therefore be another exciting year for Phoenix, as we execute against our five strategic priorities.

Our key focus areas for the year are outlined on this slide. I am not going to go through these individually, but as you can see, we are prioritising, and investing in, the areas that build our competitive advantage, to enable us to differentiate ourselves in the market.

In summary, we have a clear and differentiated strategy, which leverages the major market trends, where the whole is greater than the sum of the parts.

This supports us in continuing to deliver cash, resilience and growth. With the cash from our in-force business funding our attractive dividend over the very long term.

While our business is uniquely resilient, owing to our strong capital position, which is hedged against the major market risks. Particularly important in uncertain times.

And we will be growing both organically, and inorganically. Phoenix is a growing, sustainable business

And with that, we will move to questions. So, we will start with questions from the audience in the room. If you can raise your hand if you have a question - not straight away, in a moment, and we will direct one of our roaming microphones to you. It's good to see there's plenty of interest though.

If you can please stare by introducing yourself and the institution you represent. For anyone dialled into the conference call, please let the operator know you have a question. And for anyone watching on the webcast, please use the Q&A facility and we will come to your questions after we've answered those in the room and those on the call.

So I'm going to ask Rakesh to re-join me on the stage, and also Andy Curran the CEO of our Heritage, Open business, almost a change of role there Andy, and Mike Eakins, our Group CIO will also join us on the stage.

Q&A

Andy Briggs, Group Chief Executive Officer
Rakesh Thakrar, Group Chief Financial Officer
Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe
Mike Eakins, Chief Investment Officer

Andy Briggs, Group Chief Executive Officer

So somehow or other Andy Sinclair managed to snaffle the microphone first. That's probably just to remind me of the Scotland-England rugby score earlier this year, but we'll see, Andy, fire away.

Andrew Sinclair, Bank of America

Yeah, just wish we could back it up with a few more results. My usual three please. Firstly, just on M&A, I just wondered, firstly could you have a look at the £480bn AUM figure and give me an idea of what that means in terms of Own Funds for the market opportunity for M&A? And you said 'when not if', for those smaller deals coming to market, but the smaller ones are probably ones where we don't normally get as much vision - as much insight over, can you just give us an idea of what are the triggers to bring those sorts of deals to market? So that's the first one on M&A.

Secondly, just on the dividend, great to see the first organic increase coming through, but to me, as I say, M&A is still so important for Phoenix. Where do you think more of the growth will come through in the dividend in the next few years, do you think that will still be M&A, or do you think organic is the core part of the dividend increase?

And then thirdly was just on annuities, you said economics pretty much the same for 2022 as 2021. Just really given your increased capabilities, what is the next leg that takes us down to the 5% strain from where we were in 2021?

Andy Briggs, Group Chief Executive Officer

Okay, thank you Andy. So I will take the first couple of those and then ask Andy to take the third one.

So in terms of M&A, you asked of the £480bn, what's the Own Funds. So I guess what I'd point you to is if you think about the ReAssure deal, that was about £3.5bn of Own Funds for £80bn of assets. So that's probably not a bad guide to thinking about what's the level of Own Funds within that market if you like.

And then in terms of the larger number of smaller deals, so as we said on the slide, we see there is about £225bn of assets there, so put another way that's going to be a little over £10bn of Own Funds. But there is a series of books, and we think you know up to about £1bn.

And what is particularly attractive is all the M&A we've done historically we've raised equity and therefore you need to service that equity. If we can do M&A from our own cash resources, then clearly, it's going to be particularly accretive and attractive from a shareholder perspective.

And so as I go around and have my cups of tea and I was on the receiving end of those from Clive for many years, so it's quite nice to be the other side of the table doing that. I mean as I say, what I get you know consistently from the significant majority of those CEOs, is we do quite like the reliable cashflows that come off this closed book business, but every single year it goes down a bit and you've got to reduce your costs every year to keep in line. And that becomes a challenge, particularly when you have legacy IT and particularly when there's costs of regulatory change. So what they all say is there comes a point where, you know, we will - it's a when not and if, we will sell this.

In terms of dividend going forward from here, so I would think about it that we have a model where Heritage generates very high levels of predictable resilient cash and that covers our current dividend into the very long term, very resilient and reliable, that is very attractive, but it's generating excess cash. And what we do is, we quite rigorously think about is, how can we generate the best return on each pound of excess shareholder cash.

So that will very over time, we're very confident of the ability to deploy into BPA on an ongoing basis. We are confident that M&A will happen over time, but what we can't predict is the exact timing.

And I would view it that Phoenix Group is now a three legged stool, so actually our strategy is quite a lot more focused than most of our competitors. We do the three things, Heritage, Open and M&A, the excess cash from Heritage we'll redeploy based on where we can get the most attractive returns. We absolutely believe M&A will be a core part of that going forwards. We are keen, eager, ready to do the next deal and think we'll drive substantial value as we do so.

Andy, do you want to pick up on the BPA side?

Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe

Sure, good morning, everyone. Thank you, Andy for the question. I guess the first thing I would say is we will always think about the BPA market across value not volume. So that would be the first thing I would say. The second thing I would say is I am pleased with the momentum which we've delivered last year.

So what's the outlook where we continue to focus? I guess probably four areas where I would draw your attention to. Number one, so broaden and deepen our quality of relationships with the reinsurers, that's the first thing. The second thing is working with Mike's team on the illiquid asset origination, so that's obviously an important part of the equation. We will continue thirdly to optimise our capital efficiency, using our internal model and over and into 2023 we'd expect to have a major model change which we would expect to be approved next year. And of course, without question, and given you're sitting next door to Tom Ground, the quality of BPA team itself is, in my opinion, market leading. So we're delighted with that.

So they would be the three or four major areas where we think we can drive ultimately towards that capital - down towards a capital strain of around the 5% mark.

Andrew Sinclair, Bank of America

Just coming back on the M&A market, Andy you were saying that the cost pressure is really one of the triggers, does that mean a higher inflation world should potentially accelerate the M&A market?

Andy Briggs, Group Chief Executive Officer

Yeah, I would say generally in more challenged economic environments - but then you've got a whole host of drivers haven't you, because balance sheets you know have economic impacts on them generally, capital is tighter generally, inflation will be more of a challenge, exactly as we you say. So I agree.

And what we can't do is we can't predict the exact timing, but what I can say is we are really confident that there will be, you know, a series of the smaller deals over time and I think there is a decent chance of bigger deals as well for the reasons you know well. So it remains a core part of the strategy and we're confident as we sit here year by year going forwards, we will be talking about organic growth consistently and we will also consistently be taking about inorganic growth.

Andrew?

Andrew Crean, Autonomous

Three questions, just coming back on the M&A side, it's been over two years since you announced your last deal. That money could be deployed to increase the earnings per share and the dividend per share immediately through a buyback, what are the changes of you doing a deal this year? I know you say, when not if, but the market can be quite intemperate.

Secondly, just to clarify on the organic dividend growth, I assume that if you generated long term capital generation of £800m, the dividend would remain flat from an organic point of view. Could you tell us for every £100m over the £800m what does that mean in points dividend growth?

And then thirdly, you were talking about taking advantage of maturing Heritage customers to bring them into retirement products. Could you tell us at the moment what proportion of your Heritage clients who are reaching 65 are actually buying products from you?

Andy Briggs, Group Chief Executive Officer
Sure, so I'm going to take the start of the first one of those and then pass to Rakesh to cover the dividend aspects and the share buyback question. I'll then ask Andy to talk to the last of those.

So you're right, you know, we completed our last M&A deal just over 18 months ago. I would say though that the £2.5bn synergies that we've delivered from the Standard Life and ReAssure deals over the last couple of years, we've not really been sat twiddling our thumbs, we've been driving lots of value within the business.

I mean we can't predict when these things will happen. I would say there is a good chance of an M&A deal this year, because I talk to the different CEOs out there and the sense I get is that there is a good chance of a deal this year, but we can't be sure. What we can be sure of is we are ready, eager and keen to go when the opportunity presents itself. You know we will create higher levels of synergies than anyone else, we are the most reliable and trusted counterparty, you know regulatory relationships, the ability to look after customers well, look after colleagues well, so I think we're exceedingly well placed as and when things come along.

Rakesh Thakrar, Group Chief Financial Officer
Yeah, so on the share buyback, clearly this is something that the Board is updated on on a regular basis, but at the moment we have a clear financial framework that looks at cash, leverage and capital and we aim to operate within our ranges. So for leverage between 25% to 30%, on a Fitch basis and for capital 140% to 180% on a Solvency II Shareholder Capital Coverage Ratio basis. So on a Fitch basis we're currently at 28%, so in the middle, on the ratio we're at 180%, so we're at the top end.

But clearly then the next step is, you know, what are the opportunities for reinvestment of that capacity into other value accretive returns. Andy has already spoken about the M&A aspect of it, but clearly you know the progress we are making on our Open business and the fantastic work that we've done on the BPA of achieving £950m of long-term cash generation, you know, we've talked about it today that I'm looking to spend around £300m on BPA annually, value over volume.

But also, I highlighted the fact that we've got a £450m maturity as well on our Tier 3 in July of this year.

So in summary, you know, we keep a constant watch to make sure we drive the best return for our investors, but certainly, you know, where we are today, we see a lot of opportunity for organic growth and also inorganic growth.

Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe
On the third part of your question, it's very difficult to say in aggregate because each individual product type has very different characteristics. So, what we've been building through the Open division is working really hard with how do we think about engagement and how do we think about propositions?

We've had significant improvement across engagement, digital engagement in particular, has made a big difference from our retention perspective, and we're working through, this year in particular, new and wider propositions to engage our customers for longer.

All of that is on the bedrock of an extremely good level of customer service. I think it was covered in the previous session which was just explaining that all of our customer metrics are above the 90% mark. So, from that perspective, it's really encouraging, and also the Standard Life brand and the clarity around where that sits has made a massive difference to us.

So, to give you just a number on that, so we have around about a 250,000 members of pension schemes now engaging with us digitally. That's a massive increase on the previous year. And, as we continue to build out what we think will be innovative solutions with that engagement layer, we'll be in a very strong position going forward.

The other thing just to say about scale, there are around about 30m adults in the UK who are between the age of 50 and 65, and we would guess that we have round about 4m of them as policyholders. So, that is a massive scale opportunity for us and it's up to me, I guess, along with the team, to make sure that we find a way of engaging with those people and making sure that we deliver products which will help them as they move to and through retirement.

Andy Briggs, Group Chief Executive Officer
So no pressure there. But in fairness, we have done a bit of sequencing here, a degree of sequencing. So, we focused on BPA first and foremost, and you can see the benefits of that, then on Workplace, and I think the 41 new schemes having won virtually none in the preceding years, you know, albeit they're only small initially, that's how advisors will always test us out, is great progress.

And then the, you know, what we call the Customer Savings & Investment side, if you sort of, thinking about the slide I did on outlook with the four market trends, M&A we've always been after and focused on, then it's BPA and then Workplace and then the kind of, consolidation and rollover into retirement income. So, there is a logical sequence we've been investing there.

Okay. Shall we move along the row here, yeah?

Dominic O'Mahony, Exane BNP Paribas
Thank you. Love the new brand. Three questions, if that's all right. The first is just on the cash flow guidance. Your £4bn for the '22 to '24 period implies roughly flat cash flow given the £1.3bn to £1.4bn in '22. I'm just trying to square that with the synergies. And, on a capital basis, you delivered £800m of synergies in '21. My understanding is that synergies usually flow into cash thereafter, not immediately, and, in fact, I think only £400m of the cash in 2021 was synergies. That implies quite a large, sort of, availability of synergies from a capital perspective. Would it be fair to assume you're expecting that to come through into cash over several years rather than in an, sort of, early wave? Is that the right way to, sort of, read it? I promise my other questions aren't quite as complicated.

The second question is a really simple one. The war chest number, the £1.3bn, can you just remind us how that's calculated, and is debt leverage the binding constraint on that?

Thirdly, on M&A, could you give us a sense of your philosophy about the sustainability of the dividend increase? So, the point here is a simple one which is acquisition of a run-off book naturally has a run-off profile. A sustainable dividend is flat. Those two things create an interesting intersection where you can imagine a higher dividend policy being sustainable for 10 years and a lower dividend being sustainable for 20 years and thereafter, so what's your philosophy on what sustainable looks like in terms of a dividend increase from M&A? Thank you.

Andy Briggs, Group Chief Executive Officer
Rakesh, I think they're all three for you, aren't they? [Laughter]

Rakesh Thakrar, Group Chief Financial Officer
Thank you.

Andy Briggs, Group Chief Executive Officer
Mike's getting it easy here, by the way! [Laughter]

Rakesh Thakrar, Group Chief Financial Officer
All right. Let me start with the first one on the guidance and the synergies point. So, clearly, you know, we had a fantastic year, on the synergies, you know, and delivering £2.5bn of synergies across the acquisition of Standard Life and ReAssure.

So, what we particularly got this year was the benefit of the internal model harmonisation, and, as I pointed out in Half Year last year, and then what we've ended up with, you know, we delivered £550m of synergy from that particular initiative. Now, a lot of that is from the benefit of having Group diversification.

So, if you imagine what we were doing was effectively bringing together Standard Life and the legacy Phoenix businesses onto one internal model and, therefore, at a Group level, we can take that benefit from capital because it's under one internal model, I can take that diversification benefit.

So, that will then turn into cash when do the Part VII essentially because that diversification will then sit in the individual entities and, therefore, when we look to bring those companies together which are scheduled, as you would have seen in one of the slides, for 2023, the second half of 2023, that will then turn a lot of that into the cash. And that's already within the numbers that we've quoted. So, hopefully, that gives you some colour on that.

On the second one and how the £1.3bn was calculated, well, that's calculated at a point in time. So, it's based on the 31 December balance sheet. It looks at the leverage ratio and it looks at the cash position. And you were right, at that point in time, you know, it is the leverage ratio that is then restricting getting us to 30%.

So, what we do is take the cash number, look at how much cash we would take to get to 30% leverage, and that is essentially what that figure represents. And that will fluctuate over time as cash is generated from the operating companies. We've got £2.6bn of surplus sitting there. So, you know, that will move but, as it currently stands at 31 December, that's what that £1.3bn represents.

And the third point on sustainability and M&A and what that means for how we think about the sustainability of the dividend, I think it really depends on each transaction, on what that transaction is and how the cash, you know, evolves over time. And that'll be different for each one.

But certainly what's paramount for me and for the Board is that sustainability is maintained; you know, that has to be key. And then, you know, if we're then able to grow the total amount of cash through the acquisitions, then we can see whether that dividend increase can fund that sustainably. And how long a period? I mean, it'll depend on each transaction. I don't want to put a figure on it, but it's got to keep the resilience that we have today on our dividend. That's paramount.

Andy Briggs, Group Chief Executive Officer
Shall we pass along to Farooq?

Farooq Hanif, J.P. Morgan
Hi, everybody. Three questions as well, please, and one on investment you'll be happy to know.

So, a big problem that I see is the availability of illiquids when you've got Solvency II reform, you know, everybody want's sustainable assets. So, how do you see that challenge for yourselves? Do you think you're small enough now that it doesn't matter to get to your 40% or would you be considering going overseas? Would you consider putting your own equity in to originate?

Second question on the new business strain, so, if you go down to 5% will you get the same cash multiple? So, what's the interplay between those two? And surely, you know, it's more important to keep the 2.6 multiple than it is to go down to 5%. So, you know, are you going to be willing to look at that on a value basis going forward?

And then the last question, just more of a numbers one, on the £1.2bn of new business, what's the phasing on that? Shall we assume 6%? I mean, what's the realisation of that into cash generation? Thanks.

Andy Briggs, Group Chief Executive Officer
Okay. I'm going to ask Mike to take the first, Andy the second and Rakesh the third, I think.

Mike Eakins, Chief Investment Officer
So, on the illiquid origination, Farooq, it is a challenging market, it is competitive. Our response to that has been to really increase our capabilities internally. So, you would have seen, over the course of the last 18 months, we've made some material hires, and that's really helped us focus on our strategy in illiquids which is focusing on quality over quantity.

And so, if we look at 2021 in terms of that £3bn number that we originated for illiquids, we actually only transacted on 10% of the deals that were shown to us.

The second area where we believe we've got a real competitive advantage is that we can partner with any asset manager anywhere in the world to get the best illiquid asset origination, both from a return perspective but also from a sustainability perspective. And that latter point in terms of geographical diversification is a key area of focus for us.

So, even over the course of this year in the recent market volatility, we've actually been able to rotate significant quantums of our liquid credit portfolio out of sterling into non-sterling assets, cross-currency swap back to sterling. And that really does give us that diversification and increases the bandwidth of assets that we can originate.

Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe
Yeah, Farooq, on the strain question and the multiple question, clearly, the capital deployment will depend across a broad range of considerations which Andy and Rakesh and others will consider. So, we would take that in the round as and when we can see it. As I said, we would always think about this as a value over volume plain. The multiples of cash are a function of the capital deployed, so we just think about it in that respect. It's pretty simple.

Andy Briggs, Group Chief Executive Officer
Rakesh?

Rakesh Thakrar, Group Chief Financial Officer
Thanks, and maybe just from a CFO perspective, on what Andy Curran just said, absolutely agree with him, it's value over volume, but I won't necessarily think about the interaction because, if you imagine we achieved in 2020, we were at 9% strain and 2.3 cash multiple, and this year we've done 6.5% strain and 2.6 cash multiple. So, a lot of depends, as Andy exactly rightly said, it depends on each deal, the dynamics of each deal, and ultimately, it's the value over volume.

On that final point, you know, we've got, you know, £1.2bn. Most of that, as you know, £950m of that is from the BPAs and, therefore, I would expect most of that to be running off in line with our overall run-off of the £800m, so around, what, 6%, 7%, 8%.

Andy Briggs, Group Chief Executive Officer
So, shall we start with Louise and come back in, yeah?

Louise Miles, Morgan Stanley
Perfect. Hi. Good morning, everyone. I'll just take two questions, please. The first one is on your expense base. So, you know, you've hired quite a lot of people and you want to invest more in your Open business capabilities. It looks like, on the IFRS operating profit, you know, expenses might have been a little bit higher this year. I'm just wondering, you know, are you finished with the hiring and the investment here? And, if not, how much more should we expect in terms of the expense base going up going forwards, particularly given, you know, inflation is high, hiring people is getting more and more expensive? So, that's my first question.

And the second one is on the dividend increases. You've got rid of the two conditions that you used to have. I'm just trying to understand the rationale for that. I suppose, you know, having a simplistic dividend policy is a lot easier to communicate, so that might just be the reason.

Obviously, on condition two, I think sources of cash had to exceed uses of cash and, given you're now saying you've got £300m of cash that's going to be invested in BPAs versus the £150m to £200m before, I guess there was more reliance on the overrun of management actions. So, if you could just give us a bit of colour there. And does this now mean that you'd increase the dividend even if your uses of cash were bigger than sources of cash? Thanks. Hopefully that makes sense.

Andy Briggs, Group Chief Executive Officer
Yeah, yeah, very good. Do you want to take the first of those and I'll take the second?

Rakesh Thakrar, Group Chief Financial Officer
Yeah, absolutely. So, looking at, you know the investment we're making in our growth capabilities, I think you would see some of the benefits in that in this year's results, you know, with £1.2bn of new business cash generation, you know, originating £3bn of illiquid assets, you know, £1.5bn of management actions of which £0.7bn is BAU. So, we can see the benefit of that investment coming through.

You know, we have now, you know, set the strategy. So, as I sit here today, I'm not expecting any further increases in that. But that said, you know, to the extent there are opportunities to drive value accretive returns for investors, you know, I will consider that in that time.

Andy Briggs, Group Chief Executive Officer
Okay, and then in terms of the dividend, I mean, so the first point to be clear on is that the Board is really determined that the dividend is sustainable into the very long term, and we prioritise that sustainability.

We are confident, as an Executive team, as a Board, that we will deliver both organic growth and inorganic growth going forwards, but what the Board is going to do is, rather than have specified set conditions, they're going to form a judgement once a year and, you know, it'll be additive between what's happened organically and what's happened inorganically, add the kind of two together and make a decision each March on the dividend going forward. But using a broader range of judgement in the same way most companies would rather than have specified set out conditions. So, that's how we're thinking about it.

As I say, a key point, sustainability into the very long term but confidence within the business that we will deliver growth, both organically and inorganically.

Come along the line.

Mandeep Jagpal, RBC Capital Markets
Morning. Three questions from me, please. In this year's results, there was another material longevity release, so how is Phoenix thinking about the long-term impact of COVID when making its assumptions in 2022?

And then, on the Open business, the long-term cash generation is currently heavily weighted towards BPA versus Workplace. How should we expect the proportion to change and how quickly?

And then as a follow-up on that on organic dividend growth, does the split between BPA and Workplace affect the ability to grow the dividend organically given the cash profile of these two products is quite different?

Andy Briggs, Group Chief Executive Officer

Okay. So, I'll get Rakesh to take the first and third of those and Andy to comment on the second. I would just like to quickly say it's great to have you here. We're sorry Gordon isn't here but it's fantastic we still get a longevity release question from RBC because it wouldn't be the same without it [laughter]. So, do you want to do that one first?

Rakesh Thakrar, Group Chief Financial Officer

All right. Let me start with the longevity question. So, yes, we did get a release this year, but it was nothing to do with COVID-related.

So, although the new table came out this year, CMI20 where we effectively calibrate our own cause of death model to the CMI20 tables, what we did was exclude the 2020 data. You can't set an assumption. And this was based on, you know, our view of it and also a lot of medical experts' view on it. You just can't use it. So, we have not used that at all. The benefit, essentially, arises from, you know, just further refinement of the methodology, but nothing to do with anything to do with the pandemic or anything like that.

Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe

Yeah, on the balance between BPA as the major driver of long-term cash in the Open business, it's very clear that what we want to do is make that a much more balanced picture. As you quite rightly point out, that will take a bit of time. Each product has a slightly different financial footprint.

My focus last year was particularly on getting Retirement Solutions where we really needed it to be. This year, the focus will be around that capital-light market. I must say, I'm encouraged with that as well. I think Andy quoted 41 new scheme wins in the whole of last year. The year before it was only one, just one. This year's it's already 16, and we see our pipeline growing almost by the day, which is also encouraging.

We are also continuing to develop our engagement, our digital capability across many of our product lines, which will make a big difference. So, for example, over a third of our pension customers are now self-serving.

So, from my perspective, it's very, very clear. The instruction is to balance that long-term cash generation from the non-BPA part of our portfolio into the capital-light portfolio. My own sense of this, having been in the industry for a very, very long time, I can feel there is definitely a momentum building and one of the things we'll continue to invest in, which we've not see the benefit of, it's so far, is how we approach the retail IFA market. We will focus on that as they move quite a bit of money.

Andy Briggs, Group Chief Executive Officer

And just so you don't think I'm a totally unreasonable boss, if there's £950m of BPA, we've spent £350m of capital getting that, so it's, sort of, a net of £600m if you like. That's the way to, sort of, calibrate thinking about being balanced, yeah.

Rakesh Thakrar, Group Chief Financial Officer

Yeah, so, then, you know, I think that then follows on to the organic dividend growth question, and just to reiterate, you know, clearly, the sustainability of the dividend is paramount. And then, after that, we will look at the organic dividend growth.

I think your specific question was around, you know, if we were investing £300m on BPA, does that constrain the dividend growth? I think the answer to that is no because, one, we've thought about, you know, our plans over the next few years, and, you know, £300m is the appropriate figure for us taking into account the balance that Andy that was just talking about, that we are looking for the asset-based businesses to actually improve. And the momentum we're building in that is really pleasing, you know, from perspective.

And third, we're already shown the target of getting that strain down, long-term strain down to 5% as well which improves the returns, improves the payback and, therefore, ability to reinvest that as well. So, those were the, you know, three main reasons why we're comfortable that it shouldn't impact the organic dividend growth, recognising sustainability is key.

Andy Briggs, Group Chief Executive Officer
So, one to your right. Yeah, go for it.

Nasib Ahmed, UBS
Hi. Thanks for taking my questions. So, just two from me. So, coming back again on the M&A, UK Heritage universe of £480bn, I'm assuming that includes some mutuals as well, and, given some issues recently with acquiring mutuals, does that increase the risk of that £480bn? And what would, kind of, differentiate you as opposed to, sort of, a private equity firm acquiring a mutual? Would it be easier for you guys to do it?

And then, secondly, on just the Life Company Surplus, there was about minus £900m of assumption changes and other. Can you just shed more light on that and the rationale for not, sort of, remitting up the Ark Life proceeds from there? Thanks.

Andy Briggs, Group Chief Executive Officer
Okay. So, I'll let Rakesh take the second of those in a moment. In terms of the M&A side and the £480bn of UK Heritage assets, it is a very small proportion of that that is mutuals, but I would say, you know, one of the real attractions of Phoenix is that we are a very trusted counterparty for any vendor.

So, you know, if you see things going on in the market where there are challenges, you know, working through it with regulators, with media, with customers, then, for me, it just further strengthens why you'd turn to Phoenix because we've got a long track record of doing these things really well. Customers are enhanced significantly by our ability to migrate them to more modern technology. We give customers better outcomes as a result of that. We look after colleagues well. We always take a best of both from a colleague perspective, and we've got a long track record of successfully doing this for regulators. So, you know, to be honest, as I see different things going on in the market, I just think it further enhances our credentials as a counterparty.

Do you want to pick up on the LifeCo surplus, Rakesh?

Rakesh Thakrar, Group Chief Financial Officer
Yeah. So, I think there are two parts to that. Let me answer the Ark Life part first.

So, when we sold Ark Life, it is a subsidiary of ReAssure, and therefore the proceeds of that went into ReAssure, and we're expecting that will be released in the future. It's currently sitting there as a surplus.

On the second part, I think your question was around assumptions and other items within the Life Company Free Surplus. I think that broadly, in five or six categories, one is the fact that we've already talked about the investment in our growth capabilities is within that number.

We also got the impact of LIBOR to SONIA, which is effectively, you know, if I just give you some colour on that, it's about 15bps reduction to what the previous Solvency II regime was. So, just it means we got effectively - we've got a lower discount rate, so that's in there. You've also got the impact of the tax change, the corporation tax change where it was announcing going from 19% to 25% by 2023. That's included in that number. You've also got the impact on Life Company Surplus of the second order coming through the capital management policy as well. So, when that changes, you know, that will come through. And, finally, that's partially offset by longevity. So, that bucket is in here. It's slightly more, you know, put into those two areas, but those are broadly the categories.

Nasib Ahmed, UBS
Thanks.

Andy Briggs, Group Chief Executive Officer
Okay. Shall we go to Charlie next?

Charlie Beeching, Keefe, Bruyette & Woods
Morning. Two questions from me, please, both on M&A. Firstly, you've talked about the prospects for business as usual run-off book M&A, but do you think there are any gaps in your capabilities within your Open business that you might look to address via potential bolt-ons?

And then, secondly, you've been quite positive recently on the potential for smaller deals, so should we thinking that the next transaction will be more likely to fall within the under £1bn bucket or perhaps a larger deal?

Andy Briggs, Group Chief Executive Officer
Okay. So, on the first of those, Charlie, I think it's possible that we might accelerate the pace of growth of our Open business and capability by doing a small capability-based acquisition there. I think it would be small and I don't think it's essential. You can see the pace at which Andy and Tom and the guys are going already. So, they're doing a great job of building organically, but I wouldn't rule out, not particularly likely, but I wouldn't rule out, you know, considering a small capability-based acquisition there.

In terms of the, you know, is a larger or smaller deal more likely? I mean, I guess, given that there are a much larger number of the smaller deals and a much smaller number of the larger books, I guess smaller is probably a bit more likely. But from our perspective, you know, we will happily look at either, and think we have got the bandwidth, the capability, the wherewithal to consider either.

We'll go to the gentleman who had the microphone earlier and lost it.

Andrew Baker, Citi
Hi. Thanks.

Andy Briggs, Group Chief Executive Officer
Sorry, Andrew. It's dark at the back there. I couldn't see you. Apologies.

Andrew Baker, Citi
Yeah. My learning is I should have sat further forward today, I think. So, yeah, just one left from me, actually. What impact do you expect from Solvency II reforms? And I guess, if that pushes you above the 180%, because obviously you're quite close to that now, does that change anything that you've talked about today in terms of where you'd like to deploy or what you would do with any excess there? Thank you.

Andy Briggs, Group Chief Executive Officer

Yeah, sure. So, what I would say is we are very supportive of John Glen, the City Minister's recent speech. You know, we think insurance is one of the real strengths of the UK economy, the UK generally, and having the UK insurance sector to be able to be competitive on a global stage we think is really important and valuable.

What we're doing is we're working very hard with the Treasury with the PRA, as the UK's largest life and pensions business. We're working very hard with them in support of the work that's going on to try and, you know, bring this to fruition. I don't want to speculate yet what it might mean because, until we see detailed rules, we don't know what it might mean.

What we've historically always said is that, you know, if we were outside of our 140% to 180% range, we would consider a range of options for deployment of that capital, but we would do that on a very objective basis. What are the returns we can get if we deploy organically? What are the returns we can get if we deploy inorganically? What are the returns we can get if we return capital? And so the Board would consider that at any point in time on a very rigorous, objective basis. We really do take this sense of managing every pound of shareholder capital, you know, rigorously and allocating it carefully. We take that very, very seriously indeed.

Larissa, you're sat just in front of the screen. I can see you [laughs].

Larissa van Deventer, Barclays

Backlit. Two questions, please. The first on cash. You've been generating a lot and you have a strong pipeline, as you've mentioned. Do you have a target cash range? Is there a point at which you would consider deploying by way of special or buyback rather than keeping it for future dividends and M&A?

And the second question is on the bulk annuity markets. You mentioned that you expect stronger volumes in the second half of this year. Could you comment on your views on the longer term pipeline for the bulk annuity industry, please?

Andy Briggs, Group Chief Executive Officer

Sure. So, I'll ask Rakesh to take the first of those and Andy the second.

Rakesh Thakrar, Group Chief Financial Officer

So, on that first one, you know, really, in terms of any special dividend or buyback, I think it comes back to the framework and see what is the, you know, effectively, when you look at the three in the round, which is cash, leverage and capital, what is the surplus? Do we have surplus across all three? Do we have headroom across all three? And, at that point, we would consider potential options, as Andy just pointed out in the previous question, about how we allocate that capital to make sure we maximise the return for investors. So really, Larissa, it's focused on that framework of cash, leverage and capital.

Andy Briggs, Group Chief Executive Officer

Andy?

Andy Curran, Chief Executive Officer, Savings & Retirement, UK & Europe

Sure. Our outlook for BPA, wouldn't be surprised if it's £30bn to £40bn market. For almost as far as I can see, as Andy mentioned, you know, there was £2tn of liabilities there to be insured, so I see the market having longevity.

From our perspective, I guess, depending on how you view the market, I think we probably, on the basis of our performance last year, are probably second or third by market share, which is a significant growth. So, from my perspective, I think we're seen as a major and compelling player in that space, and I don't see that changing.

As for the near-term outlook, I think we mentioned that we've gone exclusive on £600m of trades. We already have and are quoting on something in the region of £8.5bn already. So, from my perspective, this market, from the short, medium and longer term, will be a really strong market for us going forward.

Andy Briggs, Group Chief Executive Officer

And I think it's fair to say we would expect the significant majority of that £2tn of assets to end up in the hands of insurers over time. So, this isn't a market that's going to stop any time soon. It will run for many, many years into the future.

Okay. Where next? The young lady down here.

Rhea Shah, Deutsche Bank

Thank you. Just two questions for me. So, going back to the Ark Life question, you said that the proceeds should be remitted in the future. Is there a timeline for that?

And then the second question is around management actions going forward. So, obviously, your management actions going forward will be lower because of less integration synergies, but to what extent is it due to the allocation of illiquids between new business and in-force? Has that changed in 2021? And what would you think about that going forwards as well?

Andy Briggs, Group Chief Executive Officer

Okay. I'll ask Rakesh to take the first and the second, but, Mike, you might want to just quickly comment on how we're building capability in Asset Management which, ultimately, will lead to further management actions. You know, if you could give us a broader sense of that as well, but, Rakesh, do you want to pick up first?

Rakesh Thakrar, Group Chief Financial Officer

So, starting on the Ark Life one, so, as I said, we didn't distribute it this year or in 2021. I expect it's not in 2022, but it's within our target range of £4bn. So, over the next three years it'll be out. I suspect it'll be a lot sooner than that.

On the management actions point, so, you know, we delivered £1.5bn of which £0.7bn of that was what we called BAU actions, you know, our ongoing actions, and, of that, we continue to have, you know, a strong pipeline of actions, including illiquids, asset risk management, balance sheet, you know, methodology alignment, etc., still ongoing.

In terms of the allocations, you know, historically, you know, certainly, we make sure that we get the balance right, and what we saw in 2021 was an allocation of broadly two-thirds/one-third to the back book, yeah.

So, going forward, you know, we want to get to an overall illiquid target range of 40%, and we may think about whether that may need to increase in the future, but certainly I would see a broad split of illiquids allocated between back book and new business.

Andy Briggs, Group Chief Executive Officer

And Mike?

Mike Eakins, Chief Investment Officer

Absolutely. So, just on the 2021 illiquids origination, we were really pleased with how 2021 progressed; £3bn of illiquids, an average range of single A, we've got 70 basis points of illiquidity premium. And we were able to do that because we had the right building capability. We're building capability in terms of origination professionals who are engaging directly with the market and our asset management partners, but also it goes to this point on quality over quantity.

We also increased our capabilities in terms of our credit ratings and risk team. We've now got a dedicated Chief Credit Officer in the from Michela Bariletti who we brought on last year, and Michela's building out her team to really make sure we do focus on those quality assets.

And then the final thing I'd say is we work extremely closely with Tom Ground and the BPA team in terms of that BPA pricing and making sure that we've got the right pipeline of assets to fill the liabilities that Tom and the team bring in.

Andy Briggs, Group Chief Executive Officer
Thanks, Mike. So, are we done in the room? Any more in the room? So, Andrew, we have questions from the conference call?

Telephone Operator
The first question comes from the line of Steven Haywood from HSBC. Please go ahead.

Steven Haywood, HSBC
Thank you. Good morning, and apologies that I couldn't be there in person. I have, sort of, two questions left really. In terms of the capital strain margin on BPA, you're heading towards a 5% level, but what could the potential Solvency II reforms lower this margin to in the future?

And then, secondly, you mentioned earlier that you can partner with any asset manager globally, have you thought, or would you consider partnering with other insurers for illiquids and for sustainable investing, i.e., to take advantage of greater scale or greater capabilities? Thank you.

Andy Briggs, Group Chief Executive Officer
Thanks, Steven. And sorry you're not with us. I understand your daughter has COVID, so I hope she's doing okay. I actually had a bout of it myself over the last couple of weeks but I'm fine now I'm pleased to say, but I hope she's okay.

Just on the first one, look, we're not going to speculate on what the Solvency II review may or may not do to capital requirements and new business strain and so on and so forth. It's too early to speculate until we see detailed rules.

Mike, do you want to pick up on the second question?

Mike Eakins, Chief Investment Officer
Sure. In terms of the partnering with other insurers for illiquid asset origination, the short answer to that is yes, we absolutely have done that will continue to do that, and we see that's most meaningful in our commitments to carbon net zero. We fundamentally believe that, as a single institution, we can't do this in isolation; it has to be industry moving together.

So, Steven, we do partner with other insurance companies, and we will continue to partner with other insurance companies, particularly as we're seeking to develop the market, and a key area of focus there is around sustainability.

Steven Haywood, HSBC
Excellent. Thank you very much.

Andy Briggs, Group Chief Executive Officer
Thanks, Steven. Any others from the conference call, Andrew? So, Vicki, any from the webcast? Can we get Vicki's microphone, please?

Moderator
Hello. A couple of anonymous ones first. The first one – How can we expect your solvency position to evolve over 2022?

And abrdn recently sold down some of their strategic stake, do you expect them to sell any more? And also what about MS&AD's intentions?

Andy Briggs, Group Chief Executive Officer
Okay. So, I'll take the second. And look, I mean, although, you know, having 17% of our stock come onto the market over the last 9 months, and 11% of that this year, you know, has led to a bit of volatility, I mean, overall, I think this is really good for us. You know, a year ago, we had only 58% of our stock in free float. That's now at 75%, so 30% higher. And I think having MS&AD and abrdn as core strategic shareholders is great for us.

So, from abrdn's perspective, they basically get the strategic asset management partnership and a seat on the Board by having 10%. They didn't get anything more than that by having 14%. And so, from their perspective, the strategic asset management partnership is really important to them, and what Stephen says to me, absolutely critical for them, works well from both parties' perspective. And I think, if you look at Stephen's results, he was very clear that they're committed at the 10% level.

MS&AD are holding for a different reason to abrdn. They have a conscious strategy of looking to diversify their earnings away from Japanese general insurance by taking strategic stakes in overseas insurers. They put the investment they currently have in us into ReAssure originally. That rolled over into Phoenix. And, when I talk to them, they're absolutely delighted to have this rock solid, reliable, 7% to 8% dividend yield that's covered into the very long term and is now growing. They're very happy with that and there's nothing I have picked from them that suggests that they aren't, you know, absolutely committed and very happy at that level.

So, from my perspective, you know, all is done in terms of strategic shareholders. We're going forward with a solid base from here onwards, which I think is good and attractive, with a high level of free float.

Rakesh, do you want to take up the Solvency evolving question?

Rakesh Thakrar, Group Chief Financial Officer
Yeah, absolutely, Andy. So, you know, looking into 2022 - and some of this I mentioned in my script as well, in the presentation – so, clearly, you know, we'll have the usual suspects. You know, we'll get benefits from organic surplus generation and management actions coming through. You know, although they'll be lower, we'll certainly have the BAU actions going forward and then we'll have the normal outflows of, you know, funding the interest and dividend and corporate expenses.

But I also highlighted that, you know, we do have a maturity of the £450m of Tier 3 debt in July of this year, and we also, you know, are looking to invest around £300m in BPA. So, that would hopefully give you some idea on how that position will evolve.

Moderator
Okay.

Andy Briggs, Group Chief Executive Officer
Anymore, Vicki?

Moderator
Yes. So, we've got two questions from Ming Zhu. Question one – could you please provide more colour on the reduction of proxy to shareholder value? Surplus emerging looks low. Shouldn't proxy to shareholder value grow over time?

The second question – given the rising interest rate outlook, would you review your interest rate hedging strategy over time?

Andy Briggs, Group Chief Executive Officer
I think they're both for you, Rakesh.

Rakesh Thakrar, Group Chief Financial Officer
So, taking the first one, you know, the proxy shareholder value now, you know, there's been a number of one-offs which, again, I alluded to in the presentation. We've had the impact of LIBOR to SONIA, so that's coming through. As I said, that's a reduction in the discount rate.

Second, we also saw the impact of the change in the corporation tax rate. So, again, for from going to 19% to 25%, we effectively have to recognise that in our proxy shareholder value today for those future tax rises because it's been enacted.

We also, you know, saw the impact of a couple of a supported with-profit funds that, because of the internal model harmonisation, became strong because of the more granular analysis we could do on its capital requirements and, therefore, that is no longer in the Own Funds, or the SCR is no longer in that calculation. And that's another reason for that value reducing.

Now, there was no impact on any cash numbers because we were always expecting, at some point, that those two funds will become strong again, but it's just been accelerated because of the delivery of the internal model harmonisation and the increased strength of those funds.

Second, on what to do in the rise of interest rates, I think that what would I say, what's critical to Phoenix's investment case is the resilience of its dividend and the cash generation that's coming from the operating companies.

You would have seen one of Andy's slides that showed us only having £0.1bn variance on economics broadly over the last 4 or 5 years where you'd seen the interest rates going up and down. We want to ensure our dividend is rock solid. To ensure our dividend's rock solid, the cash coming out of the operating companies needs to be resilient, and that is our focus.

So, at this stage, there is no intention to review that interest rate strategy.

Andy Briggs, Group Chief Executive Officer
Okay. No more questions? No more in the room? No more on the webcast? Fantastic. Well, look, thanks, everyone, very much indeed for coming along today. It's so exciting; my first results in person, and I've been with the company two years, so that's exciting.

The Executive Team will be around, a number of others here in the front row as well, for a while afterwards. Also, we have our Chairman here, Nick Lyons, and our Interim Chair who will take over, Alastair Barbour, as well. So, do stay around if you want to ask us any further questions but otherwise thank you very much for coming and catch up soon. Thank you.

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