PHOENIX GROUP

## Phoenix Group Holdings: Q3 2015 Interim Management Statement 22 October 2015

**Phoenix Group Holdings announces that it is on track to meet both its 2015 cash generation target of £200 - £250 million and its long term cash generation target of £2.8 billion between 2014 and 2019**

### Highlights

- £137 million of cash generation[1] in the 9 months to 30 September 2015 (HY15: £110 million). A further £18 million has been generated during October, resulting in total cash generation of £155 million in the year to date.

- The Group is on track to meet its cash generation target for the full year of £200 - £250 million and reiterates its long term cash generation target of £2.8 billion between 2014 and 2019.

- Total holding company cash[2] of £809 million at 30 September 2015 (HY15: £916 million) with the 2015 interim dividend and pension scheme contributions paid during the third quarter.

- Investment grade credit rating achieved from Fitch Ratings in August, with the Group's two principal operating life companies being assigned an Insurer Financial Strength rating of "A".

- The Group continues to work with the Prudential Regulatory Authority ("PRA") as it reviews the Group's Internal Model application and expects to be notified of the outcome in early December, simultaneously with other firms.

- The Group expects to be well capitalised under the Solvency II regime, with the Group capital position under Solvency II[3] expected to be in excess of the current PLHL ICA[3] surplus, subject to regulatory approval. The Group is currently focused on optimising its balance sheet in preparation for Solvency II.

- Estimated PLHL ICA surplus and headroom of £0.6 billion and £0.5 billion respectively at 30 September 2015 (HY15: £0.7 billion and £0.6 billion). PLHL ICA will no longer be a regulatory measure from 1 January 2016.

- Estimated IGD[3] surplus and headroom of £1.4 billion and £0.6 billion respectively at 30 September 2015 (HY15: £1.6 billion and £0.8 billion). IGD will no longer be a regulatory measure from 1 January 2016.

### Clive Bannister, Group Chief Executive, commented:

"I am pleased to confirm that we are on track to meet our 2015 cash generation target range, notwithstanding recent market volatility. As the impact of reforms to the UK life industry become clearer, including the new Solvency II regime, I believe that attractive acquisition opportunities will become available. Our leading operational platform and recent investment grade credit rating position Phoenix to continue to generate value for both policyholders and shareholders from future consolidation in our market."

*Cash generation*

| Holding companies'[2] cash flows | 9 months to 30 September 2015 £m | 9 months to 30 September 2014 £m | Full Year 2014 £m |
|---|---|---|---|
| **Cash and cash equivalents at 1 January** | 988 | 995 | 995 |
| **Cash receipts** | | | |
| Cash receipts from Phoenix Life | 137 | 317 | 446 |
| Cash receipts from Ignis | - | 422 | 422 |
| Other cash receipts | - | 89 | 89 |
| **Total cash receipts** | **137** | **828** | **957** |
| Operating expenses | (17) | (19) | (29) |
| Pension scheme contributions | (52) | (84) | (88) |
| Debt interest | (60) | (63) | (80) |
| Debt repayment | (60) | (541) | (601) |
| Other non-recurring cash outflows | (7) | (39) | (46) |
| Shareholder dividends | (120) | (120) | (120) |
| **Total uses of cash** | **(316)** | **(866)** | **(964)** |
| **Cash and cash equivalents at end of period** | **809** | **957** | **988** |

**Cash receipts**

£137 million of cash was received by the holding companies in the 9 months to 30 September 2015. A further £18 million has been generated during October, resulting in total cash generation of £155 million in the year to date.

**Cash uses**

Pension scheme contributions of £52 million to 30 September 2015 include £40 million of contributions to the Pearl pension scheme made during the third quarter.

The debt interest payments reflect the lower debt principal balances over the period and the reduced margins on the Group's bank facility. Debt interest also includes the coupon on the Group's £300 million 5.75% unsecured senior bond which was paid in July.

Other non-recurring cash outflows include costs relating to the Tier 1 bond exchange, Group restructuring and corporate related projects.

Although the 2015 interim dividend payment date was 1 October, the cash was paid out of the Group on 29 September, and is therefore reflected in the holding company cash outflows for the nine months to 30 September 2015 (in line with 2014).

*Capital*

With the introduction of the Solvency II regime at the start of 2016, the Group is focused on optimising the capital position under Solvency II. The existing group capital measures, PLHL ICA and IGD, will no longer be regulatory measures from 1 January 2016.

**PLHL ICA**

The estimated PLHL ICA surplus reduced to £0.6 billion, with the headroom over the £150 million capital policy being £0.5 billion at 30 September 2015 (HY15: £0.7 billion and £0.6 billion respectively). The reduction was due to financing costs and market movements, including widening credit spreads and lower yields, as well as the impact of Solvency II management actions. The PLHL ICA position also includes the impact of the payment of the 2015 interim dividend.

**IGD**

The estimated IGD surplus and headroom reduced to £1.4 billion and £0.6 billion respectively as at 30 September 2015 (HY15: £1.6 billion and £0.8 billion). The reduction was due to financing costs over the quarter, including pension scheme contributions, as well as the impact of the payment of the 2015 interim dividend.

**Phoenix Life free surplus**

The estimated Phoenix Life free surplus, which represents excess capital over the life companies' minimum requirements and capital policies, was £294 million at 30 September 2015 (HY15: £315 million). The free surplus is calculated on a Solvency I basis and the reduction was primarily as a result of market movements and the impact of Solvency II management actions, partly offset by the natural run-off of the life company capital requirements.

**Solvency II**

The Group's activities in relation to Solvency II have continued to be focused primarily on the Group's Internal Model Application, as well as specific management actions to optimise the Group's balance sheet. The Group formally applied for regulatory approval of the Group's Internal Model, including the use of transitional measures, in June. We will continue to work with the PRA over the coming weeks as they review our application and expect to be notified of the outcome in early December, simultaneously with other firms.

Our cash generation targets incorporate assumptions about the impact of the Solvency II regime on the Group, including our expectation that the technical provisions and capital requirements of the Group's life companies will be higher under Solvency II than the existing Individual Capital Assessment regime. However, this impact will be partly offset by transitional measures and, furthermore, we expect an improved Group capital position resulting from the change in the methodology applied to the Group pension schemes.

There remain uncertainties with regards to the Solvency II capital regime, including the approval of the Group's matching adjustment application and the agreement of a capital management policy with the PRA. However, the Group continues to expect to be well capitalised under Solvency II, with the Group capital position under Solvency II as calculated at PLHL expected to be in excess of the current PLHL ICA surplus. However, this is subject to regulatory approvals and should not be seen as representing the views of the PRA.

### *Other regulatory and legislative changes*

The Financial Conduct Authority ("FCA") is expected to release the results of its thematic review of the fair treatment of long-standing customers in life insurance before the end of the year. The review will look at the level of servicing provided to policyholders whose policies are managed within closed life funds, which we believe is aligned to our strategy of continuing to look for areas of improvement in customer performance and service levels.

In light of the pension freedoms from the 2014 Budget, HM Treasury has been consulting on options to address any excessive early exit penalties and making the process for transferring pensions from one scheme to another quicker and smoother. Phoenix has responded to a request for information from the FCA which looks to understand the current level of exit fees and charges for administering transfers.

### *Customers*

The most important change impacting our customers this year has been the introduction of the new pension freedoms from 6 April 2015. As expected, the number of customer calls has now started to decrease following the initially high pension-related volumes immediately after 6 April. We have continued to make further improvements to our written and verbal retirement communications to help customer understanding of the alternative ways to access their savings. These improvements aim to increase customer engagement with their retirement journey.

We believe it will be 2016 before the full impact of the new pension freedoms becomes clear, but to date around 26,000 customers have requested full encashment of their pension savings, with an average pot size of £13,500. In addition to Phoenix Life promoting the availability of the Government's PensionWise service, customers are reminded of the value of guaranteed annuity rates within their products and encouraged to take financial advice before making important decisions on their pension savings. If customers need help to shop around or get advice we can refer them to our partners and, to date, around 2,500 customers have chosen to speak to either Just Retirement Solutions or 425 Financial Solutions.

One unintended consequence of the new pension freedoms may be an increase in fraudsters targeting our customers. We therefore continue to take action to identify possible incidences of pension fraud where possible, but clearly there is now an increased personal responsibility for our customers to ensure that they understand how their retirement funds are invested.

Despite all the changes implemented this year, Phoenix Life has maintained a high level of customer service. Within this context, complaints handling remains a key area of focus for us and one of the ways we demonstrate this is by monitoring the number of our decisions that are subsequently overturned by the Financial Ombudsman Service ("FOS"). The FOS overturn rate for the first half of 2015 was 18%, a 4% improvement on that achieved in the second half of 2014. This is the best ever performance recorded by Phoenix since FOS started publishing data in 2009.

### *Financial targets and outlook*

The Group is on track to meet its cash generation target for the full year of £200 - £250 million and reiterates its long term cash generation target of £2.8 billion between 2014 and 2019.

The Group believes there are a number of potential acquisition and consolidation opportunities in the UK closed life sector and continues to review options within the framework of its existing commitment to stakeholders. Having secured an investment grade credit rating earlier this year, the Group is well positioned to take advantage of the consolidation opportunities in its sector.

## Notes

1. Operating companies' cash generation is a measure of cash and cash equivalents, remitted by the Group's operating subsidiaries to the holding companies and is available to cover dividends, bank interest and other items.
2. The cash flow analysis is presented for the holding companies above the operating companies and includes Phoenix Group Holdings.
3. Any references to IGD, PLHL ICA, Solvency II or Group capital position relate to the relevant calculation for Phoenix Life Holdings Limited, the ultimate EEA insurance parent undertaking.
4. Financial targets are based on the assumption that the Solvency II regulations operate as we expect.

## Enquiries

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## Further information

- A conference call for analysts and investors will take place at 9.30am (BST) today.

  The dial in number is +44 20 3059 8125
  Please quote "Phoenix".

  Access to the audiocast, with the facility to ask questions, will also be available via our website www.thephoenixgroup.com. A replay will be made available on the website.

- Financial calendar

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|---|---|
| Full year 2015 results | 23 March 2016 |
| Q1 2016 IMS | 12 May 2016 |

- The financial information contained in this announcement has not been audited or reviewed by the Group's auditors.

### Forward looking statements

This announcement in relation to Phoenix Group Holdings and its subsidiaries (the 'Group') contains, and we may make other statements (verbal or otherwise) containing, forward-looking statements and other financial and/or statistical data about the Group's current plans, goals and expectations relating to future financial conditions, performance, results, strategy and/or objectives.

Statements containing the words: 'believes', 'intends', 'will', 'expects', 'plans', 'aims', 'seeks', 'targets', 'continues' and 'anticipates' or other words of similar meaning are forward-looking. Such forward-looking statements and other financial and/or statistical data involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group's control. For example, certain insurance risk disclosures are dependent on the Group's choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that the Group has estimated.

Other factors which could cause actual results to differ materially from those estimated by forward-looking statements include but are not limited to: domestic and global economic and business conditions; asset prices; market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally; the policies and actions of governmental and/or regulatory authorities, including, for example, new government initiatives related to the financial crisis and ultimate transition to the European Union's "Solvency II" Directive on the Group's capital maintenance requirements; the impact of inflation and deflation; market competition; changes in assumptions in pricing and reserving for insurance business (particularly with regard to mortality and morbidity trends, gender pricing and lapse rates); the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; risks associated with arrangements with third parties; inability of reinsurers to meet obligations or unavailability of reinsurance coverage; the impact of changes in capital, solvency or accounting standards, and tax and other legislation and regulations in the jurisdictions in which members of the Group operate.

As a result, the Group's actual future financial condition, performance and results may differ materially from the plans, goals and expectations set out in the forward-looking statements and other financial and/or statistical data within this announcement. The Group undertakes no obligation to update any of the forward-looking statements or data contained within this announcement or any other forward-looking statements or data it may make or publish. Nothing in this announcement should be construed as a profit forecast or estimate.