Standard Life

2012 Half Year Results

Tuesday, 14 August 2012

David Nish – Group Chief Executive

Well good morning everyone and welcome to our Half Year Results. Jakub and I were just chatting about one of the admin things for today. Because of what was happening with the Olympics, we have also co-ordinated with a web link. So I apologise, half way through the questioning I will just stop for a wee second and just check whether there is anything coming over live and then I will do it again at the end. So that is the only change regards admin.

Obviously joined as usual by Jackie, Keith and Paul and we look forward to taking your questions later. Our usual safe harbour and I assume everyone has turned their mobiles off.

I think it was reflected that this might be the last time you will see this slide. I know some of our slides can get quite repetitive after a wee while. But very much if I do look at the Half Year Results, Standard Life is performing well. Markets have given us a lot of challenges over the last couple of years, but I think one of the things we have consistently demonstrated is the robustness of the business, particularly when you look at the capital strength and the balance sheet. And very much when you look at what the team has delivered, both in terms of a large programme of transformation for the Group, but also investing. And I think it is very important that we have invested for future growth, particularly when we look at the market changes that are coming up.

In terms of the results that Jackie will cover in more detail, we have obviously stepped up the operating and financial performance of the Group. And that very much supports the delivery of our progressive dividend policy which is very important to us. And as we look ahead, very much our goal is to continue driving an ongoing improvement in operating and financial performance. And I think we are very well placed to take advantage of the changes in the markets that we are going to see progressively over the coming months.

So with that I will hand over to Jackie to look in more detail at the financial results.

Jackie Hunt – Chief Financial Officer

Thanks David and good morning everyone. So as David has said I will turn now and go through the financial results and start really with some of the highlights.

So we have increased Group operating profit by 15% to £302 million and the UK has performed particularly strongly, due both to improved revenue growth and also cost reduction. This has been offset in part by lower profits in our Canadian business and that is due to the low yield environment and also the timing of management actions. Assets under administration have increased to £204 billion and third party assets under management are now more than £74 billion. Net flows in our long-term savings business are down from 2011 but they are still at a robust level reflecting the more subdued consumer sentiment, ongoing economic uncertainty and also the expected increase in commission based competition ahead of the Retail Distribution Review. Third party investment management net flows were impacted by the £1.8 billion outflow that we had already flagged in our Q1 results. And excluding this our first half of 2012 net flows in third party which is £0.4 billion.

Our EEV operating profit before tax increased by 61% to £604 million primarily driven by increased new business contribution, EEV profits from our global investment management business and also back book management actions. EEV operating profit and capital generation has increased by 53% to £295 million reflecting the increase in gross cash and capital generation and also lower new business strain. We have declared today an interim dividend of 4.9p that is a 6.5% increase from last year's interim dividend. And this is a sign of our confidence that the implementation of our strategies is continuing to drive an ongoing improvement in financial performance.

So let me run through the drivers of our increase in operating profit in more detail and as usual there are four component parts. Firstly you can see that we increased profits on our fee business by £49 million. Within this, fee based revenue has increased by £9 million while total costs actually reduced in absolute terms by £40 million. And that is the function of the scalability of our business, particularly our UK operations.

Now we indicated at our Prelims that we were confident of delivering the full £100 million efficiency saving by the Half Year, that was the existing target and we have now done so and you can see the benefits of that coming through in the results.

Last year we said we would no longer show our investment expenditure separately and this has now been absorbed within our acquisition and maintenance expenses. We have given information in our Half Year Report showing the trend in investment costs within operating profit and they have decreased by £24 million. However as well as driving down the investment costs, we have also achieved a significant reduction in operating costs more generally. Unlike 2011 when operating investment spend was weighted towards the first half of the year, we expect the operating investment costs in 2012 to be broadly even across the first and second halves of the year. We would expect the full year 2012 outturn for total investment expenditure, and that includes capitalised costs and also investments into our joint ventures, to be less than the £180 million we had indicated in March.

The second driver of the operating profit in the result was the impact of the £27 million reduction in spread or risk margin. Within this the UK showed improvement of £4 million due to growth in annuity sales, but that was outweighed by £31 million reduction in Canada. And I will come back to each of these movements in more detail as we go through each of the businesses. The third driver was our capital management result which improved by £10 million and that arose from higher investment returns on shareholder funds and also the improved funding position of our UK pension scheme.

And finally, you can see the contribution from our life insurance joint ventures in India and China improved by £8 million. This represents good progress over the last year and again I will give more detail on this shortly.

In terms of the split of Group Operating profit by our businesses, you can see that all of our businesses continue to make a significant contribution to the Group's operating profit and whilst each business has made progress, and I will touch on those in more detail, there are clearly different opportunities and challenges. I will go through each of those in a second.

So if we turn now to look at the UK in more detail. UK operating profit is up 62%. We have seen improvements in every item of our operating profit analysis. So we have increased income, particularly from fee based business, and that reflects higher assets under administration and a stable revenue margin of 73 basis points. We have reduced costs both in absolute amounts and in terms of unit costs and I will come back to that. And we have also increased capital management profits.

So I will go through the drivers of the UK results in more detail. Now we have included in today's presentation further detail on the contribution split between new and old style retail propositions, corporate and spread or risk business. And this is really along the lines of the disclosures we presented to those of you who attended our UK Analyst and Investor Day last October and it is something that we are providing as a result of requests from many of you. We have seen positive contributions from across our business, our new style retail and corporate propositions show significant growth in both profit contribution and in assets under administration. While the contribution from our older style retail fee propositions and our spread or risk business continues to be strong.

I am particularly pleased that retail new saw significant progress from breakeven at this point last year to report a £25 million contribution in this period. And remember that this contribution allows for all of the direct costs of ongoing development of the propositions and acquiring new business. We have seen strong net inflows into higher margin investment solutions such as MyFolio and Standard Life Wealth and these figures, just by way of a reminder do not include the additional margin that is captured in Standard Life Investments. Our Corporate Business on the right hand side of that graph now has assets under administration of £23 billion and it made a contribution of £40 million, up 60%. And that demonstrates the scalability of the business, showing the potential for future operational leverage. We have capitalised on the success of the MyFolio funds and the Retail markets by launching a range of investment solutions for employers to maximise our revenue.

Older style retail propositions continue to make a significant contribution to Group profitability reflecting the value of our backbook. The Half Year 2012 contribution of £90 million was similar to the £93 million at the Half Year of 2011. Assets under administration were broadly stable reflecting increments and market movements. And finally our UK spread or risk margin business contributed £50 million. The increase in spread or risk operating profit came from a higher new business return. And this new business increase was driven by 36% growth in sales. That was partly offset by a lower margin per premium mainly as a result of the impact of reserving changes that took place at the back end of last year.

Standard Life Investments increased its operating profits to £68 million. The headline increase is £1 million period on period but if you allow for the impact of both the proceeds from the transfer of the UK money market funds in 2011 and then also from including our share of the profit of HDFC asset management on a before tax basis, there is an adjusted increase of £5 million or over 8%. As flagged previously, we saw one large low margin outflow of £1.8 billion and that was due to a change in the client's investment strategy. Despite this upflow, third party assets under management grew £2.5 billion to £74 billion over the period with a greater proportion of flows going into higher margin business and that includes our global absolute return strategy funds as well as fixed income and some other areas. This mix effect saw third party fee business revenue basis points increase from 37 bps to 39 bps.

While our maintenance expenses increased in absolute terms to support growth, maintenance costs as a proportion of average total assets under management were maintained at 17 basis points and our EBIT margin as a result increased from 33% to 35%.

Reported within Standard Life Investments, our Indian asset management joint venture, HDFC Asset Management, in which we have a 40% ownership share, continued to grow and it remains the largest mutual fund company in India. Its assets grew to £10.7 billion at the end of the period and that is despite a weakening of the rupee. Our share of profits in this business was £10 million before tax in the first half of the year.

Operating profit in Canada fell to £72 million. Fee based revenue and expenses were broadly stable, however there was a £31 million fall in the spread or risk margin. The low interest rate environment reduced the assumed return on spread or risk assets, resulting in an £11 million reduction compared to the first half of 2011. The first half of 2011 also benefitted from a £31 million profit attributable to management actions taken to enhance yields. And while we continue to focus on actions of this nature, they do tend to be very lumpy. In March we said that whilst the components of our spread or risk margin may vary from year to year, we believe that the overall level of spread or risk margin achieved in 2011 was a reasonable indicator of the underlying run rate of the business and we are not changing that guidance, although obviously there will be some volatility from year to year. The split of the total risk margin is shown in more detail in one of the slides within the appendix and we can obviously run through that in the Q&A. And I should note that as a result of the low interest rate environment and as part of the continued management of capital around the Group, we are holding about £120 million of additional capital in our Canadian business.

Our International Business includes our four wholly owned businesses and our two joint venture investments. We recently announced that we would transfer the Irish and German domestic businesses to a UK and Europe function under Paul Matthews. While Nathan Parnaby will focus on developing our Asian and emerging markets business. We will move to reporting on this basis over the coming months.

Overall the wholly owned businesses reported an operating profit of £20 million, that is a growth of 12% in constant currency. Total expenses fell by £6 million which included benefits from operational cost savings and also some currency movements. The joint ventures contributed a combined operating profit of £8 million from break even at the same point last year with both our Chinese and our Indian businesses improving. We have increased market share across our joint venture businesses, HDFC Life saw sales increase by 25% in constant currency to £233 million on a PVNBP basis, while in China sales remained broadly stable despite a slowdown in the market. India is moving towards capital self sufficiency with capital injections over the next few years being largely geared towards China where we continue to expand our distribution capability.

If I turn now to the scalability of our business model and the benefits of our focus on efficiency, you are now familiar with these graphs and I am pleased with the continuing trends. The unit acquisition costs improved by a further 23 basis points across the Group and 25 basis points in the UK. In absolute terms, acquisition costs across the Group reduced from £175 million to £144 million and that was driven largely by improvements and efficiency and cost reductions in the UK.

Similarly maintenance expenses were slightly down at £380 million across the Group despite higher levels of assets. This equates to 3 basis point reduction and the improvement was largely driven by the UK with lower absolute maintenance expenses, despite continued asset growth, again demonstrating the scalability of our business.

Cash generation is clearly important as it underpins our ability to invest in the business and to pay dividends. We show this by disclosing gross operating capital and cash generation which increased from £312 million to £402 million before investment in new business. This strong growth reflects higher contributions from covered business in the UK and Canada as well as increased EEV profits from Standard Life Investments and the improved funding position of the UK pension scheme. We applied £107 million of the gross capital in cash generation to writing new business and that new business generated an IRR of 16% and a payback period of six years. As a result our EEV operating capital and cash generation grew by 53% to £295 million. Whilst this has been boosted by back book activities our core capital and cash generation has grown mainly due to increases from our non life businesses including Standard Life Investments and lower costs of writing new business.

We use embedded value as a key measure of value. The 61% increase in EVOP to £604 million was mainly driven by £230 million of back book profits reflecting asset strategy changes and modelling improvements which benefited the UK and the Canadian results. The results also include the 7% increase in new business contribution to £178 million. Non operating items amounting to a positive £140 million after tax and this included the impact of favourable investment returns and the benefit of reduced UK corporation tax rates. Adverse FX rates were the main driver of the £35 million loss from other and non trading. We also paid our 2011 final dividend which amounted to £216 million which was paid in cash following the removal of the scrip dividend option. So overall despite the continuing challenging market conditions we are pleased that our embedded value has reached £7.8 billion with EEV per share rising 14p to 331p.

We continue to have a strong balance sheet. Our IGD surplus at the 30 June was £3 billion and it remains largely insensitive to market movements. As usual we have included sensitivities in the appendix to this Presentation and the Results Announcement. We also have no shareholder exposure to European periphery sovereign debt and minimal exposure to bank debt. We remain supporters of Solvency 2, however we and the industry generally need more certainty and more clarity on the rules and on the timeline. Nevertheless our programme remains on schedule to implement as at 1 January 2014. Our leverage remains at around 25%, similar to full year following the repayment of the lower Tier 2 instruments in the second half of last year and we view this leverage position as conservative.

We have continued to grow our dividends and we have declared an interim dividend of 4.9p, that is an increase of 6.5% on last year's interim dividend. This is supported by a strong capital and cash generation. We have maintained our progressive dividend policy since listing and we remain very focused on delivering against that policy.

So in summary, we have increased assets despite difficult market conditions, we have continued to grow our fee based revenue and we have reduced maintenance and acquisition expenses in both absolute terms and on a bps basis. This has led to

15% increase in our operating profit and an improved operating RoE of 15.9%. And all of that has supported our progressive dividend policy which has allowed us to declare an increase of 6.5% in the interim dividend.

So with that I will hand back to David.

David Nish

Thanks Jackie. Very much we continue to operate our simple business model that drives profit and cash. Underlying that as we look ahead, very much I do believe we have got strong market opportunities that will support future growth. All of our businesses are well positioned to take advantage of these opportunities and I think what for me really comes through Jackie's bit of the Presentation is that we are pulling all levers to create performance improvement and value across the whole of the Group.

If we look at the drivers of future growth, very much they remain the same. And despite the tough economic conditions, the strong customer need remains and today may even be greater. UK pensions reform and auto enrolment are being implemented. We will launch our RDR service in mid-October. The Canadian Federal Government is driving pensions reform. And the globalising of our investment solutions has good momentum especially in the US. So overall our confidence in the opportunity for Standard Life have strengthened as we get to that point of delivery.

I think these results also reinforce that we have a breadth of propositions across the value chain and this gives us wider access to both revenues and margin. We have got a leading position in each part of the value chain and progress has been made in all areas of the Group. However there is more to be achieved. We have the capability to capture assets through several channels, whether that is corporate, institutional, direct or intermediary. We obviously administer assets, we manage assets. And an opportunity exists obviously to drive assets into Standard Life Investments and that is a strong feature of how we are developing our business. Our propositions give us multiple sources of revenue and margin. And I am very pleased that this year that we have made further progress in connecting the different elements of this value chain which drives flows, and also increases revenues and profits.

So maybe to spend a wee bit more time just in looking ahead at where we see the opportunities for further profitable growth and beginning within the UK. We are ready for RDR. We have been competing on the strength of our propositions and customer service for a long time. RDR will open up the whole of the Retail and Corporate markets of Standard Life. We have unbundled our platform charges and are introducing fully RDR compliant adviser pricing from mid-October, giving our advisers extra time to ensure smooth transition into the new world. The phased implementation of auto enrolment begins in less than two months. We have the potential of 400,000 additional members into our existing schemes with more than 500 of our biggest employers transitioning in 2013. Auto enrolment is also resulting in many employers revisiting their overall pension and benefit provision leading to higher levels of enquiries from employers in our target market. We are also well positioned to benefit through our leading corporate proposition, recently launching our master trust and range of investment solutions for employers which include MyFolio, and Passive Plus Funds.

In Canada we have a new management team and further changes have been announced over the last couple of weeks. And Charles Guay will now be driving a programme of transformation through that business. With our strong group savings franchise, well positioned to benefit from the shift from DB to DC and PRPP, Canada's equivalent to auto enrolment being rolled out.

As Jackie has mentioned, our newly created Asia and emerging markets business under Nathan will bring us stronger focus on the fast growing Asian markets and leveraging our expertise in offshore savings. Our life joint ventures continue to improve their performance. HDFC Life is making a good contribution to operating profit, its capital self sufficient and has a number two position in the private market in India.

And finally, Standard Life Investments. SLI continues to innovate, expanding its capability and geographic reach while securing higher margin business for both Standard Life Investments and across the Group through investment solutions. Distribution agreements with the likes of John Hancock in the US have helped to drive net inflows from outside the UK to over £1 billion in the first half of this year. The growing global reputation of Standard Life Investments presents further opportunities for growth. And very much I believe these all support why Standard Life Group is very well positioned for future growth.

So in summary, we continue to drive higher assets, more valuable asset mix and drive unit and absolute costs down. Our operating profit in the first six months has nearly doubled over the last three years. We have delivered consistent growth in dividends backed by our strong capital position. Of course there will be market challenges ahead, but we are well placed to deal with those. We also have significant opportunities to grow and very much we are committed to continue to drive further operating improvement in both our financial performance and returns, which very much will support our progressive dividend policy.

So with that I would like to thank you and we would be very happy to take your questions.

Question and Answer Session

Question 1 : Ashik Musaddi, JP Morgan Cazenove

Thank you. Ashik Musaddi from JP Morgan. Just three questions. First on the UK Retail new business. The current margin, the £25 million contribution implies a margin of 20 basis points on full year. Now this compares with the revenue margin which you gave, 68 basis points, last time you only gave some details on that. So can you update on those revenue margins so we can just see how the cost is moving here?

Second on Canada. The earnings are going down. Obviously due to low interest rate. Can you guide us how should we think of it going forward on the Canadian spread earnings?

And third, can you just give us some outlook on the Group pension? You mentioned last time that the second half Group pensions will be strong so some outlook on that? Thank you.

David Nish

Jackie do you want to take the first two and Paul do you want to take the third as regards Group Pension outlook?

Answer : Jackie Hunt
So in terms of the UK Retail new business, the overall sort of trend if you look sort of Half One 2011, Half Two 2011 and then First Half of 2012, at the revenue basis points, the sorts of numbers we have given you in the past around the sort of mid-60s, somewhere between 68,67,65. That is sort of an underlying trend. So we are not seeing much movement on the revenue basis points. It is pretty stable quarter to quarter and half to half. It is the costs that are driving that improvement in the contribution and we have seen this come down the most. Historic numbers I have got sort of the first half of 2011 you were talking about low 70s basis point direct cost. That is now coming down to around the 50s. So it has been a very significant leveraging up of the scalability of this proposition that is driving a lot of the improvement that is coming through that.

In terms of the Canadian spread earnings, you know if you look at Half 2012 versus Half 2011 you will see there is about a £31 million sort of movement between those two. Of that about £11 million is as a result of lower yields. And as long as these yields continue, you know I would expect that if the Canadian Government bond is seen as a safe haven asset in the way it has been because of Eurozone uncertainty, I would expect to see lower yields. So you can almost literally double that up. You would expect to see about £22 million down on the yield side. The Canadian result is impacted by management actions and we have been very clear in the past that we do aim to maximise the return we can get on our assets. And last half, so Half 2011 there was a significant gain as a result of those management actions. And the difference between that gain in the first half of 2011 and the gain in this half is around £20 million. Now the nature of these things are, they are lumpy. So about £20 million I would say of the lower performance is as a result of the actions that we may or may not be able to take, depending on what assets are available in the Canadian market. And I appreciate that that is difficult to model. We are very focused I should say on driving you know better yield for the assets, but within our credit appetites, but it will be lumpy and whether we will deliver something in the second half of the year or not I think remains to be seen.

Answer : Paul
As far as the corporate pensions outlook, perhaps break it into two sections, so you have got the second half 2012 and then you have got 2013 I will perhaps comment on. So we have already had commitments of around 500 of the 35,000 employers we look after that we will auto enrol their employees in 2013. We will do two major PLCs, FTSE companies in 2012. But generally the 500 of the first set of companies we are dealing with at the moment will also enrol in 2013. Of the next few years as a result of those companies alone, we are counting, expected figures of up to 220,000 employees potentially to come over in the next couple of years. What I would say is at the moment you are seeing some quite I don't know whether it is rational or irrational behaviour of commission of 'Buy now while stocks last'. And you are also seeing a number of employers deferring making a decision on which they would typically have done this year to next year in order to make sure they get the auto enrolment sorted at the same time they do the restructuring of their company pension plans. So it is difficult to say what the second half of the year's numbers will be. We know roughly what will roll over of the schemes we have been discussing at the first half of the year, but there will be I suspect continually some companies buying some market up over the next six months so I think you should expect that.

<u>Question 2 : Greig Paterson, KBW</u>

Yes good morning Greig Paterson, KBW. Three quick questions. One is obviously the acquisition cost basis points was affected by lower product development costs in the first half. I was wondering what those were and what the expectation will be for the second half, just to give some colour around your comment that you are not going to be spending 180, how much is in that particular line? And what is the expectation going forward?

The second thing is, there was £112 million uplift EEV variance for Canada because of your change in modelling in your segregated fund business. I was wondering if you could be more specific? Were there lapses better than expected or whatever? Or was it one of those non market consistent adjustments that just create value?

And the third point I suppose on the same theme is there is a £120 million delta on a TVOG where you have I assume derisked your assets. Is that, does that create value? In other words you shall just carry on doing that until you know you have no risky assets? I want to know what your attitude is around that or is it just one of those non market consistent adjustments that creates value by just jigging the accounts?

David Nish

Great, thanks Greig. I think they are all for Jackie.

Answer : Jackie Hunt

So if I start and if I talk about the overall investment for growth programme and our expectations and I will come back to your direct question about the acquisition cost element of that. So last year you will remember we spent about £196 million in total on investments for growth. We have indicated that we thought that would come down to about £180 odd million in the course of this year. In practice our run rate is a little bit lower than that and that is largely as a result of some of the sourcing initiatives we have put in place. So our day rate for a lot of these change programmes is actually quite significantly down year-on-year. So sustainable reduction in terms of the amount of change we can deliver for the same element of cost.

So our outlook at the moment without being too precise because obviously it does depend on a very synthetic cut-off from 31 December, you know I would be saying maybe £165-odd million is probably what we will see at the total investment for growth, sort of level. £165 maybe £170 million. What you see coming through into the operating profit number excludes obviously capital that we have put into our JVs and it also excludes any capitalised costs which we capitalise in terms of the standards. So if you look at the amount of operating profit that was reflected in the first half of the year's results it was £56 million attributable to this particular item. So we spent first half a total of £84 million in capitalised costs and the JV injections and £56 million of that went through the operating profit number. Of that around £20-odd million went through acquisition costs.

Now if you look at outlook as we go forward, we would say the £56 million, £60 million, somewhere around that in operating profit is in line with what we spent in the second half of last year. So you will recall last year a lot of the investment for growth expenditure was geared towards the first half of the year, second half was around £60 million, I can't remember the precise number. We have seen the same run rate again first half of this year and we would expect in operating profit at a similar sort of run rate next year. But the shape of that programme is changing. So less into the UK, a bit more into some of our international operations.

And then the last question, no sorry the Canadian funds question, this is just more granular modelling. What we do at the half year is we adjust our embedded value for economic assumption changes. We generally don't look at non economic. We do all our experience analysis in the third quarter of the year. It is a long-term business, so looking at it more frequently than that we think is sort of a false degree of precision. So we do that in the third quarter. This was just a better look, given the yield environment particularly in Canada, the Actuarial Team is just looking in more detail at the cashflows and modelling things on a more granular basis and I would see it as that and nothing more.

The TVOG improvement is fundamentally different. So the £100-odd million of improvement you talked about in terms of the reduction in burn through, you will see the UK and some of the disclosures of the back burn through is reduced from about £250 million to about £140-odd million I think for the six month period. And that is a result of changes to the asset strategy to protect against downside risk. And those changes took two forms. The first was that we did extend some of the equity hedging that we had in place to protect against particularly volatility we saw at the start of this year. And the other is also the are entering into further interest rate swaptions, interest rate protection, particularly against very low German yields and again you know it is something I think we flagged at each of the calls to date. I think this point about you know, is it economic, absolutely I think you would have to say in terms of the amount of robustness, the resilience, the reduction of risk in the business has had a significant benefit. You can see that in the burn through number. Clearly what we are aiming to do in that with-profit fund is to give a good return to our customers who remain in it. So we wouldn't seek to continue indefinitely because you know they are looking for some sort of return on assets. So for us it is a balance between the return we generate and as a consequence what our with-profit policy holders can earn out of those assets. And then also managing the fund in a way that is prudent, that maintains it strength and its stability so that it can afford to deal with some of the more volatile market conditions.

<u>Question 3 : Gordon Aitken, RBC</u>

Gordon Aitken from Royal Bank of Canada. Three quick questions. There is no mention of Lifelens in the release. Can we have an update please and how many schemes have you executed on there?

Then second, when you launched the investment programme you talked about a spend, we talked of IRRs of 15%, paybacks of 5 years. Just how do you plan to demonstrate that you have achieved that? And can you give an update on the current progress towards that?

And finally on acquisition costs and maintenance costs, these have obviously come down dramatically over the last few years. You have said there is scope for further improvement. I mean ultimately, where can these get to?

David Nish
Paul do you want to kick off about Lifelens?

Answer : Paul
Yes Lifelens we, I think we are on target to write about 24 Lifelens schemes this year. So I think we have said a number of times now is when we fully integrate a proposition, we can only take so many on per annum. So we are probably on target for round about 24 which was bang on plan for this year.

Answer : David Nish
I think very much just picking up on one of the key words there Gordon, about integrating the proposition, very much we are seeing now, what becomes the pension offering of Standard Life going ahead.

Answer : Jackie Hunt
So Gordon your questions about the investment programme, how we are going to demonstrate the 15%, 5 year. Clearly we would point to the bottom line. I think we have been very clear that as a management team what we seek to focus on is IFRS operating profits, the other measures are important, but that is where we are putting a lot of our energy and our focus. And so you will be able to judge us on whether effectively in 3,5,10 years time we have generated a good return on equity across the business as a whole.

In terms of the current portfolio, as it stands at the moment we are talking about a return in excess of 16% in a payback period of about 3.8 years. So it is meeting the hurdle rates. I am very comfortable with that portfolio.

In terms of the acquisition and maintenance costs. You know I think if you look at the trends across the business, I mean we would say overall the acquisition costs are more leveragable by their nature because they tend to be pretty fixed headcounts. So we have got distribution teams in each of our businesses, very simply if somebody goes out and sells £300 million of business or sells a billion pounds worth of business, the costs tend not to expand because we don't pay commission and there is only a bit of variable pay associated with that. So acquisition costs you should always expect that sort of trajectory and the ability to leverage that to be sharper on that than it is on the maintenance side, where maintenance costs where as you know as you add more assets sometimes you do need to add to the processing capabilities or the people. We see further to run in this frankly. And quite a bit further to run. It does differ by business. So the UK business is a large business, it is clearly at scale. You have seen it perform most strongly in each of the operations. You will see a much stronger focus on the unit cost and the ability to leverage it there. On other areas like Standard Life Investments, we are seeking to grow globally so you have seen some of the investment into global growth, new teams, new infrastructure, so you will see a little bit less leverage there.

David Nish
Andy and then could I just check after Andy has had his questions, whether we have got anything from the web.

Question 4 : Andy Hughes, Exane BNP Paribas
Hi, Andy Hughes, Exane BNP Paribas. First question is about solvency 2 and capital of the Group. Perhaps you could share some numbers on economic capital, excluding the equivalence for Canada? And maybe comment a bit about Canada and particularly with low interest rates what the IRRs on Canada would look like if you weren't to get Solvency 2 equivalence and how you would think about that scenario of not getting equivalence for Canada? I know that is not the base case that people are looking at at the moment. And how long you basically retain the capital for, you know the possible risks from Solvency 2 in Canada and maybe update on where the internal model is going in the UK?

And then a quick question if I could on the fee revenue in the UK. I noticed in Q1 it was 72 basis points and then for the half year it was 73, so it sort of went up in Q2. I mean is that a function of markets, is it basically equity markets falling and with profit funds relatively stable that is driving that fee revenue up? Thank you.

Answer : Jackie Hunt
If we talk a little bit about Solvency 2 and economic capital, you know clearly we have managed our business at the back of economic capital and our internal model for yearsm certainly as long as I have been here. I have been somewhat I guess loath to publish economic capital models because my belief has always been that that is what Solvency 2 was trying to deliver. And so you know our view has always been rather than confusing the message, we have IGD, you know, we start publishing economic capital and Solvency 2 is still coming, we end up with this question as to which is the capital number we should focus on. In practice as Solvency 2 diverges from an economic basis and I think this whole debate about outstanding elements will be resolved hopefully one way or the other and we will see whether it is economic or not. And also as it is looks like it is increasingly being kicked into the long grass I think we will come back and look whether it is right to go with some sort of economic capital disclosures more generally. But at the moment we have chosen not to do that and I think as long as we are going with Solvency 2 on the current timeline I think that is the right approach to take. I think you will end up with something that is neither a regulatory measure nor compliance.

In terms of the Canadian equivalence elements you know clearly we have been quite vocal in saying that equivalence is an important for our Canadian Business. It is important because it is firstly a spread base business and so Solvency 2 tends to impact on it more than it does the rest of our model. The rest of our model is very Solvency 2 friendly, very Solvency 2 compliant. From our perspective this is about a level playing field and competitiveness as much as anything else. So competing in a Canadian market at the moment what we aim to do when I talk about management actions and the assets sort of profile that we use to back our liabilities, they are focused on the Canadian regime. It is quite difficult to optimise both the Canadian regime and Solvency 2. The mood music around equivalence is positive. I think everybody is saying it is going to happen, European insurers won't be made less competitive as a consequence. We plan on both bases and there are a number of things that we can do, whether that is asset strategy changes, whether that is potential reinsurance, whether that is looking at parts of the book that are particularly long tail in nature and where we may choose to do something else around them. So we work on all of those and again when I talk about management actions, that is forefront of my mind.

I think you asked then about the internal model in the UK. You know we are going through the process so you know there is now a two stage FSA process. We have had a number of you know long dialogues with the FSA. I think it is going to one of their panels quite shortly. I think we are on track. We are going to do the original. I get confused on the submission versus the application language. But we are due to go in and sort of third quarter of this year on the first round. And then I think first quarter of next year. And so far I think we are where we want to be, we are in a good spot.

And then fee revenue in the UK. You know the basis points in those revenue yields I think there is always a risk that we read too much into very small movements. And some of it is just where AUA happened to end at the end of any particular period. So I wouldn't read a whole lot into the 73 versus 72. I think the key takeaway is that from a pricing level, the prices are relatively stable that we see across our portfolio as a whole. So pricing has not been driven either particularly upwards or particularly downwards.

David Nish
There are no questions from the web. Oliver and then go to Andrew, then James and then at the back. And there is a bonus question if someone asks something of Keith!

Question 5 : Oliver Steele, Deutsche Bank
Oliver Steele from Deutsche Bank. You made that point too late for me I am afraid. Two questions. The first is on acquisitions costs I am afraid again. Because obviously this is where you beat expectations. You have said the £24 million of the reduction I think in the acquisition cost element came from lower investment spend. So I am really just wondering what drove the rest of the reduction because there is

quite a difference between an absolute reduction in costs and the word you have used in the past which is scalability. Can you give us some sort of breakdown on what the remaining acquisition costs look like split between say staff costs and non staff costs so that we can get a sense of what is fixed and not fixed?

And again you seem to be talking about the idea that acquisition costs can come down further in absolute terms, and I am just wondering what sort of parameters are around that? If inflows come in as you expect are you still expecting acquisition costs to come lower in absolute terms? That is rather a long first question.

The second question is, you use the term on your leverage that you regard it as conservative. Is that happily conservative or are you trying to hint that it is too conservative?

Answer : David Nish
I think we just say it is conservative.

Answer : Jackie Hunt
So maybe if we deal with that one first. We are very comfortable with the balance sheet as it stands at the moment. Clearly there is a lot of external uncertainty, there is a lot of volatility. Having a conservative and a strong and robust balance sheet is a good place to be and I would hold with that. I have said in the past that we have operated with leverage levels of the 30s. And we were comfortable at that level you know, comfortable in terms of what that means from a rating perspective. So when the time is right we may well look to do something, but I am comfortable as we stand today, the kind of shape of that leverage.

In terms of acquisition costs, so maybe if we step back a little bit and we say if you look at the overall UK picture, because I think this is where it is most coming through, we have had this underlying improvement from £87 million operating profit to £141 million. Now I will talk about the absolute amounts, I appreciate each of you were kind of missing on certain elements of this. But if I talk absolute drivers, you know the first thing is that we should note that revenue of that period, period on period, is about £20 million up. So I think the UK while a lot of the beat was on the cost side, I don't want to lose the message that actually the revenues in the UK are pretty strong. There were more sort of muted elsewhere, but we have seen good revenue growth in the UK. So about £20 million of that £54 million delta came out of revenue growth.

Acquisition expenses were down £23 million, maintenance expenses broadly flat, about £2 million different and capital management return was up about £9 million. So your drivers £20 million revenue, acquisition expense reduction £23 million, maintenance expense reduction £2 million and capital management up £9 million.

So if we talk then about the acquisition expenses, I think the key point to make is that not all of that was a result of the lower level of investment for growth. So if you look at the first half of 2011 we spend £22 million in acquisition expenses that were investment for growth and went into operating profit. That fell to about £9 million in the same period this year. So you have seen roughly you know £12-odd million, £12-13-odd million reduction in just acquisition on the UK. The rest of that £23 million was actually underlying efficiency improvement.

And so if you talk about the outlook, we are confident that that efficiency improvement we continue to drive at the same sort of level and potentially increasingly as we grow these assets as we go forward, I think we feel that we understand the levers, we are pulling those levers, it is starting to bear fruit and there is more to come.

If you look at the delta on acquisition just period on period, clearly it can't drop as fast because we haven't spent as much this year. So don't double it up is my rough way of saying.

Question 6 : Andrew Crean, Autonomous

Andrew Crean from Autonomous. Three questions. On Canada you put in £135 million more capital. Is this part of a rebuilding of the capital base of Canada? Can you go into that in a bit more detail?

Secondly, can you talk a bit about tax rates in the first half, how much is one off? And what is your long-term expectation for tax rates in the individual areas, so we can plug that in?

And then coming back to Oliver's question on acquisition costs. You have always maintained that the idea was to keep costs flat and drive more revenue through. But here acquisition costs have actually fallen, even excluding the investment spend element to that. That was certainly a surprise to me. Is that something you see continuing?

Answer : David Nish

I think, why don't I start maybe with some comments. Particularly if I connect it back to what we have been doing over the last 2-3 years and without using a simplistic analogy about peeling an onion, it is one of these things, when you begin to drive transformation into a business, you see a view of it that is there and particularly since we had been investing round about things like platforms, the type of trough positions. We have simplified the propositions over the last three years as well. And although these are individual items, there is a point at which they begin to come together and you get a different view of the next layer of the onion. And I think what you are beginning now to see is that they organisation in terms of its processes etc is maybe giving us a different view of then how we take it forward and how the market relates to propositions etc. So that is why over time we can begin to have, you could see a subtly different view as where we can drive the efficiencies through. As Jackie was saying earlier when we really started driving off two years ago, it was very much about we are going to improve the overall operating returns of this business and it would come through a combination of driving revenues and driving costs. We are now beginning to see that at a more granular level.

So if you look at some of the things, we have simplified the propositions. We have probably got a lot more digital in terms of how we do it, so the scale of some of the propositions. You know if Paul talked a wee bit about the types of IFAs and the scales of their book relative to where we started on before. You know IFAs have given multiples of the revenues that they had that a few years ago they were working with. So you have got quite a different economic dynamic that is there. And that is why we can never obviously reduce this down to zero to one person or Paul would be selling everything in the UK. Now maybe that is where, you might want to drive the things, but I don't think that is probably the right thing. But it does mean that it will shallow out, but the scalability factor and that is back to maybe the point that was half of Oliver's question, we are building in scalability that can keep costs under control, but leverage up the business.

Answer: Jackie Hunt

So as we talked a bit about, in answer to your questions, capital that we are holding in Canada now is £124 million, I think you quoted a slightly different number, but £124 million is the additional capital as a consequence. We aim to hold a buffer on top of regulatory capital in each of our businesses and then once we hit that sort of buffer, anything surplus is kind of pulled up through the corporate structure to top end of the PLC. I think it is worth being very clear that we are significantly in excess of the regulatory capital requirements in Canada and all this is really reflecting is that we are holding more to get back towards our internal buffers in the Canadian business more generally. We see this as temporary. If you look at the Canadian yield environment, as I mentioned in some of my earlier comments, Canada is being seen as a safe haven currency. That has had a knock on impact onto Canadian yields. And so we do think that is going to normalise over time as things get resolved. So I wouldn't kind of expect, it is not a rebuilding of the capital base in any way. It is just making sure we are comfortable and we can manage that business easily.

In terms of the tax rates, this period has not been a great indication of underlying tax rate, I absolutely appreciate that. As Andrew picks up, we have had a tax credit in the first half of the year. That is really as a result of the release of some tax provisions that we were holding, we finalised a number of assessments on prior years and on current years with HMRC. The tax teams have been busy and so you have seen the release of some of those provisions, that is one of the nature. In the long-term, so medium term, probably 2-3 years time we would expect to be moving towards an effective tax rate of around 20%. In practice the percentage of the RCF contributes to profit will bring that a little bit down over the next couple of years. And the RCF is as you recall, as a result of the scheme of demutualisation, is actually the emergence is tax free, so that element becomes tax free and that pulls the ETR down.

<u>Question 7: James Pearce, UBS</u>

Morning, James Pearce from UBS, A couple of questions. You have disclosed you are still making IRRs of 8% on new business in UK personal pensions and Canada. On the UK side of that, is that including the current run rate of costs or do you need to take further action to get the IRR up and if so, what will you do?

And a similar question in Canada about how you get that to acceptable profitability?

And then on SLI, since you ask, it looks like profits are flat, net inflows are sharply down, how confident is Keith on restoring momentum to profitability of SLI?

Answer : David Nish
Good question for Keith, James!

Answer : Jackie Hunt
So perhaps if I take the first question around IRRs. It is worth saying that obviously we look at all our non economic assumptions at the back end of the year and as a result of our experience variances, particularly around cost reductions, are largely fed through into the EEV numbers as a result of that. So we may see some movement. Clearly we haven't pre-empted on any of those, some of the cost savings that we have seen through the business more generally.

On Canada there is a particular driver. We had implemented and we had started selling probably I don't know, 8-9 months ago GLWB products in Canada. We stopped selling that product in about February of this year I think. It was always intended only to be an infill product, so we had capped the volumes. We had said, the only reason we will sell GLWB is to make it available on the platforms so it wasn't a reason for us to be excluded. What we were finding is that with yields falling so far, GLWB was becoming non economic. Again you know our view is that this is a temporary measure, but it is clearly that that is driving through into those particularly low Canadian IRRs. And I think we have taken the action we need to deal with that.

Answer: Keith Skeoch
I am always suspicious when somebody tells me about all the factors that generate an underlying number. But I don't think we had any loss of underlying momentum in the first half of the year. We had one large mandate, £1.8 billion that we knew a year ago was going to come off our book of business. It was relatively low cost. If you remove that then net flows onto our third party book were £2.4 billion. The way in which people value asset managers, they look at that annualise the starting assets. That was 7% which I think in terms of the flows I have seen so far from competitors in the first half of the year, puts us in the number two position. So we continue to see very strong inflows on an underlying basis onto our book of business, both on the institutional side and if you look at today's Pridham Report on the Wholesale side, we were number one in terms of net flows first half in institutional and number two in terms of net Retail flows. From everything I can see, we have a pipeline because we have business that we have won, but we don't know when it is going to transition. The second half of the year looks pretty much as robust as the first half. So I think

that the momentum that has been in place for some time will continue and our profitability, because a lot of the stuff that is coming onto our books is at a higher revenue yield, has a positive mix, again has continued to improve. So we think we can maintain a pretty high level of profitability despite looking to invest for that overseas expansion.

David Nish
I know you have a question at the back, but can I just check if there is anything in the weblink. Okay, so maybe at the back and then Andrew's hand is up and that looks. So Andy you want to come again. So back, Andrew, Andy.

Question 8 : Marcus Barnard, Oriel Securities
Marcus Barnard, from Oriel Securities. Can I just go back to the tax charge following on from Andrew's question. I take the point about £30 million of prior year releases. But even so, £8 million or £3 million of tax on an operating profit of £300 million still seems very low. Or the £39 million credit on a £223 million PBT. What other factors are at work there apart from the recourse cashflow and the changes or is that it? I am trying to explain it really.

Answer : Jackie Hunt
Maybe the easiest place, page 50 of the document. I appreciate you haven't got it in front of you. But we can talk through a little bit. If you actually compare income tax UK sort of six months on six months, it is up a bit, so it was about £76 million last year, it is £93 million this year. The drivers are genuinely the kind of tax credits that you see coming through there and then the fact that the recourse cashflow is just a larger percentage relative half on half. There are no other sort of key elements that I would pull through there. You know the rest if you look period on period it is pretty flat, but again if you want to take it off line we have got David Clayton our Financial Reporting Director here as well, and he can pick it up with you.

Question 9 : Andrew Crean, Autonomous Research
Yes a couple of things. Do you give the fee revenues for old retail, new retail and corporate? I know you have given the profits. When you did your seminar or Investor Day last year, I think you gave revenues more than profits.

Answer : Jackie Hunt
We did. Let me just have a quick look. We haven't filed it anywhere in the document. We have provided, those are profits, you are looking for basis points. So it is not in the documents anywhere. In terms of message. So I talked a bit about retail new, it is pretty flat around sort of mid-60s. On corporates again there is not a whole lot of movement, sort of it is low 70s, that sort of range. It would have been similar to the numbers we were disclosing at that sort of period. So revenue basis points pretty flat. There is a bit of volatility period to period, but nothing significant. And fee retail old revenue basis points around the low 80s and again there is no underlying trend on those numbers.

Further Question

And the other thing was, on the spread revenues on Canada, at one point you said that 2011 was a good base and then at another point you said you weren't sure whether the improvements in spread would come through in the second half. So I wasn't quite sure whether you are trying to say that the second half you will get some impacts from widening spreads?

Answer : Jackie Hunt

So what we are saying is in the long run if you look at the spread business over a period of time without volatility, I think the guidance we gave around that sort of level was absolutely, it holds true, we haven't changed our view at all. We do see this low yield environment as being you know particularly extreme and we don't believe it is going to remain forever. The question is, how long? As long it is here you should expect the yields to be depressed as you saw in the first half of this year. So your £11 million impact I would roughly be doubling depending on your view of whether the Canadian yields are going to remain at this level or not. The bit that is lumpy in nature is the management action. And we are focused on it. But we have got nothing to announce at this stage. If you look at what we did last year, we entered in the first half of the year, the year into a bond that was financing a particular healthcare provider, it met our credit criteria, it was the right sort of thing and it gave us yield to pick up. The second half of the year we sold some property because we found that the market was overheated. So we can't really give you any more guidance other than to say we continue to focus on those sorts of things to see whether there is anything we can do to support that Canadian result and to get the yield pickup that we want.

Question 10 : Andy Hughes, Exane BNP Paribas

Hi, thanks very much, Andy Hughes, Exane BNP Paribas, three questions if I could. For Paul first. On the sort of 1st January, obviously IFAs will be re-registering assets off existing funds supermarkets onto their existing preferred wrap providers and hopefully you are one of those. Have you got any indication of how big that is going to be in terms of inflows?

And the second question I guess was on, I think you mentioned that existing pension from existing companies on the Group side were looking to move assets around, I was just wondering if you had got any idea about how much or an indication of when that might be coming and if there is any and indeed how big it will be?

And the third question was a numbers question on the sterling fund thing. I know you won the court case and I think that was about £70 million and I can't remember whether it was originally an operating charge. So when that comes back, is it in the numbers today and does it come back as an operating profit or is it a below the line item? Thanks.

Answer : David Nish

Why don't we start with that one. When the charge was taken it was an operating hit back a number of years ago. And obviously we are now focused on the appeal process. There is nothing recognised in the accounts from effectively the result last year. It is fully provided against because there is uncertainty that is there.

Answer : Jackie Hunt
Can I just add one thing to that. So from operating profits perspective, absolutely right, there is no net impact. Because we have the cash that was lodged with us by the insurers, the assets are in there and we have made a provision on the other side. So it is in the balance sheet, it is not in the profit numbers.

Answer : Paul
So RDR, the first question, is 139 days and counting before commission is outlawed. I don't have any figures actually on re-registration of assets from supermarkets to wraps, but we would expect, once an IFA has to start charging for his time, or her time, there are two things that will happen. They will have to reduce the costs of their business. So they will look at a couple of things, they will outsource their investment mandates. I think we are seeing something like £25 million a week coming into MyFolio, £15 million a week coming into Standard Life Wealth. I think that is £3 billion in the last 20 months. That will only accelerate from January 2013. One reason because the IFAs will not be qualified under the new regulations to give that investment advice. Two, the cost of running the investment selection process and the research and governance and due diligence will be too high for the consumer to pay, so they will outsource to people like ourselves. The third thing is, I think what you are saying is, to run the service they require they need a wrap platform to run all the portfolios and planning and the cost of doing that at the moment is subsidised by commission. So I think it is right to assume that more will come across. I don't have any specific figures Andy on that one. What I would say though is some of the business going elsewhere over the next 18 months will be re-directed so it is not just the back book of assets, it will be new business.

Was the second question the corporate side?

Andy Hughes
The existing restructuring of corporate pension schemes as they do their move over to auto enrolment?

Answer : Paul
Yes so typically, we go through a five stage process with the company. Secure the company. Two is to work with them on their back book as to when that is working across. The third is to get the investment solutions mandate over to us rather than to a third party. The fourth is then try and get the flex in and the fifth is to develop the relationship with employees so we get more upscale, but also when they leave we can move it across to direct.

Andrew was trying to ask me this sort of question earlier I think. So to give you a figure on how much back book stuff can come across, I can't. All I can say is that for the last two years what we have been saying is that more companies have been setting up a money purchase plan and putting their new staff into that money purchase plan. We expect over the next 2-3 years, in line with auto enrolment, companies will close their existing final salary schemes to their existing employees. And the contributions from that which are quite meaty, typically 25-30-35% of annual income, will then be switched into money purchase plan. And therefore the schemes that we have got, we would expect to see some reasonable growth over the next three years. But I can't give you any flows other than to say that you should expect that process over the next 2-3 years to happen. We have 35,000 companies, 50% of the FTSE 350, we have relationships with, we are in a very good place, a better place than anybody else would be my view.

David Nish
One final question, Greig.

<u>Question 11 : Greig Paterson, KBW</u>
It will be a number then. Slide 10, right hand side. Corporate. You have the contribution from corporate at £40 million in the first half. I was wondering if you could split that into old style corporate pensions and new style corporate pensions? Because you persistently refuse to split those two out. I assume one is loss making and the other one is profit. Could you give us the split please?

Answer : Jackie Hunt
No we don't. I mean when we look at our business and we talk about it at the A&I Day. We manage our business, fee, retail new, fee, retail old. Because they are fundamentally different products, the spread and risk and then the corporate as a whole. We don't see a difference between old corporate schemes and new corporate schemes. It is a continuing evolution. We continue to accept new increments, new providers into each of those corporate schemes and I certainly wouldn't assume that one is loss making and one is profit making.

Further answer : Paul
Well a couple of things, back to my five stage process. The problem you have is when you secure the scheme sometimes you are just charging an administration fee. The second, when you take the back book, you might charge a different rate for that back book. And the third thing is that when you deal with investment solutions and we can have some old schemes that are now using MyFolio or GARS which is typically 30-40 bps richer proposition, so it is quite difficult. Because you would then be saying, at what stage are the companies on the five basis'? Are they doing it as administrator? Have they got their back book with us or are they just a new book? Have they got investment solutions or not? It is quite difficult to do that. You would be breaking every single scheme down.

David Nish
Good okay. So thank you for your time. We will be mingling around. Unfortunately I think Jackie and I have to go off to a media event in about five minutes. But the rest

of the team are here, there are quite a few of the members in the front row. Okay, thank you.

End of Presentation