partnership
seeing retirement differently

Partnership Group plc

Wednesday 13th May 2015

Q1 2015 Trading Update

Steve Groves – Chief Executive Officer

Good morning everybody and thank you for attending Partnership's Q1 call.

I'm Steve Groves, the Chief Exec of Partnership. I'm joined here today by David Richardson, our CFO, and Katherine Jones, our Director of IR. We'll be happy to answer your questions in a few minutes, but first I'd like to take you through the highlights of our first quarter announcement, which we released this morning.

So we've announced Q1 sales of £99m and that comprises of £54m of individual annuity sales. As expected, sales were down around 13% on Q4 2014, reflecting the increased level of deferrals in the run-up to the 6th April.

In addition, we generated £24m of medically underwritten DB sales, £20m of sales from care annuities and £1m of protection sales.

Taking each of our three key markets in turn:

In the UK Retail market, in the short term, Q2 sales are likely to remain subdued as they will be driven, to a large extent, by the quote levels in Q1.

However, since the 6th April, we have seen a step up in adviser and consumer activity with advisers seeking quotes for new customers, and also revisiting clients who had previously chosen to defer their retirement income decision.

It's too early to say definitively, but historically, an improvement in these key lead indicators has flowed through to increases in individual annuity sales. So as I look ahead to the second half of the year, I'm continuing to anticipate a gradual return to growth as we start to see these increased activity levels flowing through to sales.

Longer term, I believe the outlook for the market is also positive, supported by ageing demographics and structural growth in the Defined Contribution market.

In the Defined Benefit space, we have a strong DB pipeline comprising high quality deals across all major EBCs. Our analysis shows that in 2014, over 10% of DB deals for schemes with liabilities less than £100m were medically underwritten, and that compares to 3% in 2013. This demonstrates the significant increase in traction of the medically underwritten proposition with EBCs and trustees.

Based on our current pipeline and market activity, I remain confident in achieving our target of at least £200m of medically underwritten bulk annuity sales in 2015.

In the United States, our discussions with potential partners regarding the launch of our Immediate Needs Care Annuity are progressing well and we will, of course, provide a further update in due course.

Operationally, we have made good progress. On the cost front, although current subdued levels of sales mean we still have a mismatch between revenues and cost, the action taken on costs in 2014 have been embedded and we are now on track to deliver our 2015 targeted cost base of £75m.

We have refreshed our existing annuity product, offering to provide new flexibility, such as providing Benefit Based Quotes, which allow customers to identify the level of annual income they would like to guarantee for life and receive a quote for the cost of securing that income through an annuity using part of their savings.

partnership
seeing retirement differently

The next step will be the launch of our new retirement account which is planned for the second half. This new proposition will use an award-winning third party wrap platform to provide customers with one product which offers an individually underwritten guaranteed income for life using part of their pension savings and allows flexibility on the residual funds.

We have received further industry recognition for our customer-focused proposition with our Enhanced Lifetime Mortgage being awarded a 5 Star Rating by Moneyfacts for the third consecutive year at the Enhanced Lifetime Mortgage Awards.

Finally on Solvency II, we are now seven and a half months away from implementation. Our Solvency II programme is well progressed and designed to ensure we are ready to meet the new regulations when they are implemented on 1st January 2016. We currently expect to use the Standard Formula approach, initially, for our most material risks. Along with the rest of the industry, we have work planned in order to be ready for Go Live, but our current interpretation of the draft regulations indicates that we will continue to be well capitalised under the Solvency II regime.

In conclusion, it's early days post the pension changes. I expect further clarity on customer behaviour and the outlook for the individual annuity market to emerge over the coming months and will look forward to providing an update at our interim results.

Looking ahead, we remain focused on levering our unique Intellectual Property to carefully select risks and write profitable new business in the UK Retail, Defined Benefit and US Care markets.

Thank you for your attention ladies and gentlemen. I'd now like to move on to the question and answer session.

Question and Answer session

Question 1

Andrew Sinclair – Bank of America Merrill Lynch

Thanks and good morning everyone. Three quick questions please.

Firstly, there have been a few new entrants in the Lifetime Mortgage space recently and I just wondered how much impact this has had on Partnership's ability to source equity release investments?

Secondly, just on the Benefit Based Quotes, has there been a material difference in take-up of those using the Benefit Based Quotes versus those using a traditional approach, and is there any difference in pricing?

And thirdly, just on the Retirement Account, I just wonder if you could give us any idea on the sales expectations for this product? Thanks.

Steve Groves

I guess starting with the Lifetime Mortgages, we have seen a combination of factors in that market, and so we have seen some new entrants. At the same time, I think the vast majority of the market has always been funded by annuity providers, certainly in recent history, and funding from annuity providers has been reduced. Overall, we haven't seen any significant change in the dynamics of that market. I guess you'd characterise it

as there are probably more providers, but each of them in total has slightly less capacity than they had prior, leading to a similar dynamic to prior to the changes.

In terms of the Benefit Based Quotes, we've seen a reasonable proportion of the quotes activity we're doing now is involving that Benefit Based approach. I think in reality that comes down to how we saw this market developing, which is we think that IFAs will look to secure a guaranteed minimum income that people can live on using the annuity product, and will then look to invest the balance of any pension flexibly. Clearly, if what you're doing is targeting a guaranteed minimum income, then Benefit Based Quotes become quite an important tool in doing that. So we have seen a significant proportion of quotes since 6th April involving Benefit Based Quotes. It's too early to say in terms of whether the conversion on those is any different to the normal but we wouldn't expect there to be a difference.

In terms of pricing, no, we price using the same pricing disciplines we apply for all of our other business, and therefore there's not a difference in that pricing.

I think you asked a question on the retirement account. I think it's too early at this stage to give you any meaningful guidance on what the sales of that product will be. We're a month since the changes and it's a relatively new proposition to take into the market, particularly a medically underwritten one. I guess it's worth saying, though, we clearly wouldn't be developing or launching the product if we didn't believe that over time there's a material opportunity there.

Question 2

Gordon Aitken – RBC

Morning, thanks; three quick questions please.

Several of the UK companies last week said that they would be using transitionals and will you be applying for a transitional deduction to your technical provisions? That's the first question.

The second one on bulks. You're only writing business which covers your capital requirement. If you just give us an indication, what percentage of schemes which are looking for risk reduction are priced such that the capital requirement is covered? I'm just wondering how much of this business you have to turn away because it doesn't meet your criteria.

And the third question is on Lifetime Mortgages. I think what we expect, and the knowledge does seem to be, that matching adjustment approval will be there for Lifetime Mortgages. My understanding is that these mortgages may have to be put through a SPV just to make the cash flows fixed. And can you just give an indication, how much yield could be lost there, and if that is the case, what could it do to your in-force? Thanks.

David Richardson – Chief Financial Officer

Thanks for your questions, Gordon.

Starting with the Solvency II ones, I'll take both of those together. Where we are at the moment is we haven't reached a conclusion yet on how and exactly whether we will apply transitional measures. The way the rules work is you have a choice to apply transitional measures to some of your business, all of your business, or, in fact, none of your business, if that's what gives you the best outcome, and we're still working through those various options and have each of those open to us. We've got a good open dialogue with the PRA on interpreting their requirements on matching adjustment and then stepping through the implications of each of

those. But as Steve mentioned in his opening comments, based on our current interpretation of the regulations, it's our expectation we'll remain well capitalised, regardless of which route we go down.

With respect to equity release particularly in how it gets treated under the matching adjustment, as you rightly say, without modification it does not meet the matching adjustment requirement in the view of the PRA. Therefore, we have two options available there. We can include that asset in the business, which would have transitional measures applied to it, in which case there's no day one loss in yield pick-up. Or else we can go down the SPV route or other transformation route where you make sure the cash flows do meet the matching adjustment. Again, that falls into this general optimisation path that we're going down at the moment where we're looking at those different combinations in conjunction with the Regulator and their expectations and working out which gives the optimum outcome.

In terms of reaching a conclusion on that, matching adjustment permissions need to be in to the Regulator by the 30th June, and so we'll be able to give you greater clarity at the time of the interim results in August.

On the bulk pricing question, it's an interesting one, as you rightly point out, pension schemes don't need to hold risk capital, so the fact that our pricing discipline means we aim to cover the capital requirement on the business as we write it, on the face of it as you say it kind of presents a pricing challenge. However, what we've found is that by taking our IP and using a high data approach to pricing these DB opportunities, we've managed to put attractive pricing in front of trustees and that's translated into actually a fairly high proportion of transactions completing. Not necessarily all with us and, as you'll see, Just Retirement, who compete with us in this segment, they also closed a number of opportunities, but we're finding that this market segment is developing very well and those trustees who decided to take a look at this option have, by and large, been pleasantly surprised by the pricing they get.

<u>Question 3</u>

Barrie Cornes – Panmure Gordon

Good morning all. Just a couple of questions from me. First of all in terms of bulks, obviously slightly lower than I was shooting for in Q1 and compared to Q4 last year. I just wondered, Steve, whether there was anything I should be reading into that. I appreciate obviously you're talking about £200m for the full year; was there anything specific to Q1 which meant it was slightly below expectations?

And secondly, in terms of the Tories getting back in, and maybe Ros Altmann becoming Pensions Minister, I just wondered if there's any likely change on the individual annuity front that you can see, maybe a change to 25% tax free allowance perhaps, and what the impact of that would be?

Steve Groves

I guess taking those two questions in turn, Barrie. I wouldn't read very much into the Q1 bulk position. We've always said that it's a lumpy market and we remain very confident, based on what we've got in the pipeline, on the £200m that we've guided towards. So, I think it's just a feature of the particular schemes that completed in the period, and it doesn't change our assessment of where we are or that opportunity.

Interesting question on Ros Altmann. I think overall we would welcome Ros' appointment. I think Ros is a consumer champion; she is somebody who has campaigned for what is good for the consumers for a long time. And by and large we think for the subgroup of customers that we are targeting there is a widespread

acceptance that what we do is pretty good for them. So, I think that would be an opening comment that we welcome having a consumer champion in the Pensions Minister role.

I think there are certain areas you can look to if you look at Ros' history where she's certainly called for things before. She's been an outspoken supporter of a second-hand annuity market previously. She has also been an outspoken supporter of early access to pensions to a limited degree for people, in terms of making younger people feel more engaged with pensions by giving them very limited early access on certain life events, like buying a house and having children etc. So, I wouldn't be surprised if you saw ideas like that coming back again.

I've never seen her come out and speak on capping tax free cash. I've seen other Conservatives float that idea in discussion, but I've never seen Ros do it. That doesn't mean it won't happen. But if I were looking at the things Ros has really called for in the past I'd say it's probably a positive for the development of a second-hand annuity market, and I wouldn't be at all surprised to see some discussion on early access to pensions in the near term.

Question 4

Oliver Steel – Deutsche Bank

Morning. Two questions. The first, perhaps slightly light question, is, why haven't you launched the retirement account sooner?

And then more specifically on that retirement account, why would IFAs want to give you the drawdown element of that money? I can see why they might want to buy an annuity or recommend their client to buy an annuity through you; but what's the charging structure that encourages them to give you the drawdown element of that money?

Steve Groves

I guess taking your first question, why haven't we launched sooner: we felt there was a huge amount of change going through the market, that it was very important to put the focus on updating the current product and communicating, particularly to the advisory community, what those changes were and how they could be used.

We felt that putting two product launches very close together actually runs the risk that you fail to effectively communicate either of them. So, it's a very deliberate and very planned decision; and I think will reflect how we expect product development from all of the life companies to emerge over the coming 12 months. The market has gone through a phenomenal amount of change, and we need to make sure that the pace at which we change product and we change proposition is something that the advisory community are comfortable and able to safely manage with their clients.

So, a very deliberate decision to do it in that way. And I guess to the extent I'm giving you any forward looking steer, I think that is how we will continue to develop as this market emerges.

In terms of why would a customer place the business with us: well clearly I'm not going to prelaunch the conditions of the product right now; but we see that in the retirement account space there are two or three key

determinants of why someone will buy a retirement account product. The first one will be the cost of the guaranteed income, because the cheaper they can secure the level of guaranteed income that their client wants, the more they have available to invest and to put into the investment type solution. So, clearly the first big USP will be that the cost of guaranteed income for somebody with medical conditions using Partnership's unique intellectual property will be lower for a specific group of customers.

Then you say, having secured that guaranteed income in the cheapest possible way and left myself the most possible to invest with the client, I think you're right, Partnership's investment solution needs to stack up and to have USPs that are attractive relative to the wider drawdown market. And in the proposition that we're developing we're very confident that we've achieved that.

Oliver Steel

Okay, I don't think I'm going to get any more out of you on that front.

Actually just as a follow up question on a completely different matter: the £54m of individual annuities that you sold in the first quarter, given that this logically should have been the lowest possibly quarter of any quarter in recent past and indeed going forwards coming up to the rule changes, is there any reason why we shouldn't see that as the absolute minimum for quarters going forwards, barring the current quarter?

Steve Groves

I think when you look at what we've said, and we've said it for a long time, we expected client activity, and particularly deferral, to be a big impact in Q1. Completions in Q2 are driven from quote activity substantially in Q1. And then I think what we're guiding people to is that we are expecting a return to growth from that point. So, I guess the only answer to your question is that we think quarters one and quarters two are significantly affected by the worst of the deferral, and then the market will return to growth.

And I guess the other thing we've been seeing today quite clearly is we are seeing the lead activity that suggests that is the case. So, all being equal yes, we would expect quarters one and quarters two to be the low points, and you'll see a return to growth from there.

Question 5

Jon Hocking – Morgan Stanley

Hi morning everybody. I've got three questions please. Just to clarify what David said about the matching adjustment, I'm not sure if I heard clearly; did you say you are going to apply formally for matching adjustment on 30th June? And by implication were you saying that you'd pretty much know the outcome when you applied, giving the discussions ongoing with the PRA? So, are we going to get a full clarity on Solvency II at the interims?

Second question, on pricing of new business how are you thinking about that given the uncertainty of where the equity release book will be in terms of the transitionals or the SPV etc.?

And then finally on the UK care business, I was just wondering whether anything had changed there post-election, whether you thought there was going to be an acceleration of that market?

Steve Groves

I guess I'll take the UK care question and then hand over to David for the other two.

I don't think there will be a significant change in the near term on the UK care market. I think if you look at the drivers behind the previous, reforms they were substantially driven by Liberal Democrat coalition members. And therefore I would be surprised if we saw rapid progress on many of the wider reforms. That means I think two things: one is the uncertainty about what are the changes that are coming in some ways will start to fall away because there will be less vocal conversation about the changes that are coming. The second is I think it means that you can rule out a step change caused by a change in legislation that builds an insurance solution into the customer piece. So, I think you head back to the world we were probably in before, which is you will see progressive growth as the population ages.

I think the overhang of a potential threat from significant new policy has probably reduced. But I also think that we're back to the position we probably were ten years ago where there is a limited amount of clarity on what the government's long-term position on long-term care will be.

So, I see it as facilitating, if you like, orderly growth; but probably reducing the likelihood of a legislative step change one way or another.

David Richardson

The way the process is going to work on the matching adjustment submissions to the regulator is that by 30th June we, along with any other companies which intend to use matching adjustment, need to make their submission for the matching adjustment by that date. So, that includes what assets you think are eligible for matching adjustment; what the corresponding liabilities are; and why you believe they meet the matching adjustment requirements taken together.

Now, the process we're going through at the PRA at the moment is clarifying the feedback that they gave us and the industry more generally at the end of March, and working out what is the, as I said, optimal mix of submissions that you can make to the PRA, balanced between matching adjustment and, if you choose to do so, transitionals.

So, by 30th June we will have our, as it were, preferred choice or preferred path identified. We then submit it to the PRA. They have in theory up to six months to formally approve your matching adjustment submission or not. We would not expect that to just disappear into a black hole for six months; but rather to enter a period of ongoing dialogue. So, what that means is, I would love to be in a position where I can give you full clarity at the time of our interims in August; however, based on experience to date I would still just caution it's likely to be a journey with the PRA rather than you get clarity on that date. But certainly we should have a clear idea on our preferred approach, and also an update on where we think the regulator's thinking is heading.

On your pricing on new business, I think it probably follows from what I've just said there. Because there are still a number of moving parts, and because in aggregate we expect to remain well-capitalised on a Solvency II basis, at this point in time there is no clear steer that would impact our pricing at this stage. We are developing

the tools so that we can price on a Solvency II basis; but at this state we're not going to implement those until we've got greater clarity.

Steve Groves

Thank you for your time this morning everybody and goodbye.