Old Mutual US Life Presentation – 7th July 2004
Transcription of Presentation by GUY BARKER

I want to give the picture of the business how it moved from when I was appointed in 2001, which was a vehicle with a very good sales message and franchise, because foreigners cannot sell to foreigners basically, so you need to be local to get the local market, and to turn it into something really worthwhile for the Old Mutual group, developing that front office success, and building a back office that will make it best of breed.

Slide 3 - Introduction
Development has been in two stages. Firstly through the Americom venture which was our learner venture, and then through the F&G venture. Expansion since, and I will talk about that, has been essentially organic, to consolidate and build strength of our new offering, and we have added the US Life Network. I am going to talk about the strategy we adopted in the States, and our current position along that strategy to optimise the US Life venture. I am going to talk about where we are in the market and the products. It is a very complicated market because fundamentally it is not a single market, it is a conglomerate of specialist markets, and you pick your niches very carefully. Then go into the finances. I am going to be backed up in Baltimore by my Chief Actuary, and one of the joint number twos on finance, John Fenn, who is in charge of the planning and reporting aspects of finance. I will talk about the outlook, which essentially is the culmination of our strategy, without giving numbers, and then take Q and A. I have two goals in this, one is to let you hear from the horse's mouth what we are doing, two is to let you know who the horse is, so that you know who the people are.

Slide 4 - OMUSL Senior Staff

This is my top team; there is an Executive Committee of seven, which runs the company. Some are technical specialists, a very able general counsel, those who know the US environment knows how important that is. And our head of HR, but they are all essentially company and business focused, as opposed to technology focused. Managing finances is John Varvaris, he and Michel Perreault, the Chief Actuary, are both from F&G, so they have stayed from the old team to the new team, particularly important to me because understanding the finances of the company and then migrating to an US/UK perspective has been key to both their efforts, getting the products right into the market has been very key to the success we have had in the past, and continue to have with Michel as Chief Actuary. I brought in Mike O' Brien from Natwest, from my Natwest life and Investment Services days. He was very well positioned to believe in outsourcing, and to take outsourcing across to an US model that works so he is a key member of our team. Essentially there was an outsourcing model that did not work there and I will talk about that a little later, we now have that working. John Clifford joined me, I included him in Jackson National in my days there, and he is the intellectual powerhouse who times our expansion of distribution, and runs our acorn areas for distribution, which will now be providing about a fifth of our business, and he works for Bruce Parker, our Chief Marketing Officer, brought in from Jefferson Pilot, a well-respected large company in the States, and is President of our Prime Retail Franchise which is Old Mutual Financial Network. That is the key team. I work a style that is to have the management understanding, and approving everything they do but essentially trust each other. We do not go into big consensuses, our operating officer is the operating officer, he makes the operating decisions, keeps the team informed, takes challenges and fundamentally gets on with the job, and the same applies for the CEOs. Some decisions I will take, acting entirely on a consensus basis, some I will take having taken soundings of my team and made difficult decisions from them. We accommodate well to that, it is a good style, it allows for fast reaction, it allows for open book management and it allows for real involvement by the team.

Slide 5 - Executive Summary

2001, clearly we buy the company we get the executive team, we say goodbye to a couple of people who did not want to stay under a new ownership, et cetera. We spot in the due diligence, we need to change the outsourcing relationship from CSC in 2002, we need very keen and very efficient administration and in the past F&G were the small guys. With Old Mutual behind us and with the strong CSC Old Mutual linkage in South Africa, we are renegotiating that deal to get something better out of it. Eventually both CSC and ourselves come to the conclusion there is not mileage in this, what we are wanting in cost efficiency terms is not possible, in a heavy infrastructure of general purpose organisations like CSC. We migrate to two firms, MAAS, Mid-American Agency Systems as a specialist underwriter, and that is yielding a lot of book savings that are not obvious, high quality specialist underwriting; and TAG – Transactions Application Group - for administration. Both Mid-west based, both large specialists, we are their largest client, but we do not dominate them, and really find this is our best agreed approach.

Moving to 2002, in high volumes in transition your outsource is not too interested and your new ones are just learning. Very smooth 2004, and in between. F&G have been noted for low quality administration, it is now noted for high quality administration, few queries. Not fussy administration where we do an awful lot and bend over backwards for the client, but what we do, we do smoothly.

The next part was migrating this from a one trick pony selling from a billion to a billion and a half, I am exaggerating it was not quite a one trick pony, but a two trick pony to a four, five trick distribution. We have five channels so that where the markets are not in favour of one channel, they are in favour of others. That is the soft distribution bouncing up and down. You will see later that we now run the business between 4 billion and 3 billion of single premium sales a year, that gives us enough smoothness to be able to steer the earnings steadily on the upper track to our target 12 percent, which has been well voiced, and without us needing to chase volume for volume's sake, we sell it to make money.

2003 is when, having established what we are doing and letting that start to motor nicely in the other two, we redirect ourselves to saying what do we do on the Home Office infrastructure, that is still work that is going on, but essentially is to take out, particularly to take in-house bits that the outsourcers should not be doing such as claims management but also leave with the outsourcers phone handling stuff that they should be doing without doing our own back up. So no belt and braces, we believe in belts or braces but they better both be strong. Diversification plans were approved and instituted in 2003 to build the solid base that I want, and you will see when we go through 2004's figures how well that paid off. I cannot talk beyond the first quarter, but that was a strong first quarter and a well diversified first quarter of this year. 2004 is all leading you to what I believe will be 2005 which is a best year for me, which is continuing the Home Office work, doing the final tidying up of the TPA migration, and doing some on the job redesigning of the front end, all minor stuff and doing what we are doing better, product changes.

Slide 6 - Who are we?

Often one will talk of Old Mutual in the US being F&G, we are moving away from the F&G brand, that is readily accepted so what an agents have thought in the past of as F&G becomes Old Mutual Financial Network. Old Mutual Financial Network is our retail on-shore organisation, it encompasses the F&G product range and distribution, and Americom, the initial seed company for agent distribution. And it is migrating probably over a three year path towards Old Mutual Financial Network. We needed to do it anyway, our licence rights in F&G were restricted to anything called F&G insurance, it could be of New York, or what have you, so we migrated that, but it is giving a strong message that we, like the other guys are here to stay. Contrast that with companies where there was no brand change and the market took that as a message it was a speculative investment. The market has the message that we are strategic investment in the States for the selling market.

Accompanying that is OMNIA, which is our US offshore life insurance. OM stands for Old Mutual as you will have guessed and OMNIA, it passed our focus group tests quite well. We are selling US type products to non-US clients, non-US extremely wealthy clients, because this is the private banking market of HSBC, City Corp, Chase, Wachovia, and we have the product range for them. Complimentary skills to what we do, and the rest of the US, it is a natural extension. It arose from another company, SAGE, which had an offshore operation but had undercapitalised, and did not have access to capital, so we picked it up at a song, and developed it.

Lifestar is our fairly low-key development to be a broker ourselves, other companies do that in a major way, we are doing it in a low-key way to pick up our orphan agents, those who have lost their agent connections, so we have can continue to get the business flow from them. It will build up over the years, it is achieving quite a lot of franchising advantage with other companies, it is not exclusively selling us, it is complimentary part of our portfolio.

Slide 7 - Background

Sales for 2003 were 3.1 billion, we are well beyond that, if you make it pro rata the first quarter of 2004, 3 to 4 billion was our range, what we had bought had been a billion a year until the final 10 to 15 month run-up to when we bought it, so this is a double scaling. We had a lot of investment and we are very pleased with it, from Old Mutual, that 1.8 billion includes about half a billion of transient investments, which is the capital fluctuations, which were positive at the end of the year, but in total of the amount invested in terms of initial capital, subsequent capital and reinvested GAAP earnings is 1.3 billion. It is a strong investment by Old Mutual Group, it is an investment that is now migrating from being a drawing-in capital phase, to being a pushing out earnings in forms of dividends phase, that takes a few years because the cycle of products is about five years but we are on the cusp of that growth, where our capital needs will cusp this year and thereafter turn the corner and I will talk a little bit about that later. So we have come from a sizeable company which was 600 million to 1.3 to 1.8 billion, depending how you count it and we have more than doubled the earnings during that case, as appears in another slide.

We are focused on 550 agent groups, this is not a 80/20 rule, this is 80 per cent of it comes from 20 of those MGAs, so that we keep our fingers in the pie of 550 managing groups, it is no overhead to us to speak of, but keeps our product, and we will find in our 20 top groups that there is about five that will bite each year and five that come in to support the market. Of the 103,000 agents that are licensed with us, the top 9,000 sell the top 80 per cent of our business. The next 20,000 sell some of our business, the next few tens of thousands are a mixture of those that are no longer active in business, and those that are watching us and are seasoning into a business with us. That turns over quite happily, it is a sign of confidence. We have just finished a culling exercise, and that has taken just below the 100 thousand, that is where you find the ones that are only there to look at the products but not to sell.

Contracts in force, three quarters of a million, we will be passing the billion mark at some time during 2005. Outsource as I said, all but a handful will be with TAG, and that handful is the offshore handful. Assets under management 13.3 billion we bought at 5 billion company, 13.3 at around 4 billion a year of sales, it will hit 20 billion, which is fairly much critical mass, all the critical mass for our outsource model. Of the British owned companies, clearly Jackson National in place for longer than us and for this first eight years of its existence is still doing very well. But we believe that we have a secure position in there.

Slide 8 - Profits Growth

Earnings growing, you can project by analysis, I have seen nothing in most analyses that I would argue with, it is a growth track, it is a capitalist of UK, US GAAP that our expense savings that we are doing tend to get spread over the next five years, so we have saved an awful lot of expenses which migrate into the balance sheet over five years, so we will see our earnings going up. It is a characteristic of the product shape that we sell in the US that the profit is deferred one year and then continue to grow quite strongly. So the 2004 gap profile will be determined very largely by what we did in 2003 and 2005 by this year. That is all emerging as you would expect from that graph. The big hop from 2001 to 2002, is the quick victories one always gets in a take over, the sensitive recapitalisation and the product effects from the last half of 2001, when it was very visible to the market that F&G now had an owner that was really interested in it, so we got the kicker in 2002.

Slide 9 - Distribution – New Business

We have changed distribution, a key message I want to get through is that what we bought was a company that sold annuities, read that as savings bonds, through independent agents run by MGA's and groups, and life insurance, same agency set-up, different agents. And it was very much dominated by interest rates, so if the markets were with you, you sold a lot, if the market was against you, you sold little, if it did not have a secure future, it essentially had a ceiling of a billion and a half, with a secure future the agent perception changes, and your ceiling rises, hence our success.

Slide 10 - Distribution – New Business

But it was a restricted number of tricks. We split that up with the acorns, one of the acorns is the offshore element, and the same sort of thing, the other acorn is corporate, where leverage in our portfolio is natural advantage and expedience to other insurers, that do not have the same market as us, or to the federal mortgage banks which is lovely option we will talk about later and that gives us greater sufficiency on the portfolio. We also have our own agency lifestyle which is selling some of the sales, and if you open your agency it can channel, force anybody to buy products but it can certainly make sure that we get the best shelf space, and you see that coming through with 3 per cent of our products. We have been able therefore to pull away from the institutional channels which has saved the banks where our portfolio was almost entirely dependent upon whether we could arbitrage a better yield to the bank customer than the bank could with own deposit base. That was possible because of the steepness of the yield curve, and the abilities of the insurers to invest into that yield curve and protect their portfolio by surrender charges. Well, the yield curve is so steep now, so that was very much a channel that would tend to fluctuate. Reduced dependency on that enormously. Migrated the single premium annuity portfolio to one that was based on structured settlements. I impaired lives to ones based on regular lives, which is -- technically of course, it is healthier, but it is healthier financially as well. And we have the deferred annuities with the MGA's majoring quite nicely, much bigger than it was, but a smaller proportion of the lists, because it is not spread and shared with the IMDs. Then they have taken us to, we have surpassed now the critical mass of our organisation. And that has taken a bit of time to come through, which is GAAP, but we have got a model that works, and outsourcing helps.

Slide 11 - Strategy

We have broadened distribution, so we do not have to tool up for distribution to go this way and that, which is dispensable for our sales organisation. It is going to the retail channels, got the offshore channels, got the Lifestar, take out 3 per cent of our sales. We are definitely embracing the outsourcing model, which takes us away from the flex other companies have of being too small in scale or been too large a scale where they are too unwieldy. We go to horses for courses, or best of breed, as it is called these days. It is low cost administration with quality that is good, basic, dependable. That is what we demand. We have a high quality underwriter and an underwriter of high quality does count, and he is on good costs and we are doing well on our synergies with Old Mutual Group. That is investment synergies, IT synergies and prohibitive synergies, the idea being there being a customer for technology investment. We have an active corporate channel, which is 11 per cent of our sales, some years it will be zero, it will never be more than 20, which is based on the stabilizing source of income put on from the banks. We use group reinsurance to stabilise the capital emergence too. We had something that was distinctly broken in terms of inefficient outsourcing. We also had something that was distinctly improvable in terms of working to not US industrial strength, but UK industrial strength, and that is where we strengthened the proposition enormously.

Slide 12 – Strategy

Investment management used to be a passive portfolio, it is now actively managed, Dwight, for basic portfolio investment in corporate bonds and Dwight run a portfolio of 30 billion plus, of which ours is the bottom third. It was the largest single client, but it is part of their portfolio, and they have immense expertise and they have been giving us a significant yield advantage over those to whom money is just another client. Analytic, which is the investment house in LA that specialises in quantum-type structures and has developed us a derivative portfolio in the index, that is a yield advantage to us, profit advantage to them, and works because we have had critical mass and Equity Index now since 1998 so we have enough money there not to have to go bespoke with every purchase. We rebalance the equity index balance sheet every week, not by increments, but the totality of the balance sheet, which is extremely precise and enabled by the sort of tools they and I actually have in place. We use Barrow-Hanley, essentially to help keep Dwight on their toes, but I do not think it is necessary. It is also a corporate bond house, operates a slightly different structure than Dwight, also run by Old Mutual in the US, and we use them on an our corporate sales portfolio, so it gives us an advantage - two people to look at what is best for each in what way.

Our profit taking is active, because of US GAAP, most companies will not take their portfolio actively, the effects on the bottom line have to always be explained away. We have been able to because of the smooth investment methodology that is in use in England, and that will continue through international accounting as we see it. You have a big advantage on the upside, because we can actually move the portfolios within the boundaries of prudence. This has major, major advantages on the down side, and we found that in both 2000 and 2002 and 2003, when other insurance groups were basically having to live with the Tycos and the Enrons, until they became Tycos and Enrons, as companies started to degrade and negative messages came up, people would not sell because of the hit they would get on their quarterly US earnings. We trade out of anything much more easily, and that is because we are based on value add, rather than the recognition problems of US companies.

Well, you probably have CEOs saying great things all the time and that was how Tyco came about, that was how Enron came about, they made these statements. We have got a UK style controlled environment, the head of internal audit in the US is entirely separate from myself, or from Scott Powers, the Head of Asset Management. He runs the show, he makes sure that he can intrude where he likes, that no bluffs survive in Old Mutual. It is independent. I have always had the practice anyway of having non-executives on my boards. The F&G Life Board the other statutory boards we have, I want somebody there who does not owe a thing in his career future to me, to tap me on the shoulder. I have had an implicit belief that management will always risk fooling itself, so you have to have outsiders in, so I have a spread of non-executives on each of the major boards. Bringing together all of the control figures under the Chief Actuary, in many companies will be the CFO, with us it is Chief Actuary, who is not only responsible for the long term wealth of the company, he is responsible to make sure that the risk management is acting, he is responsible for the internal audit threads linking in with the independent executive. So essentially you be an independent conscience. So I am keeping the Chief Actuary defence very much in charge of the controls and separate from the chief executive thread.

Slide 13 - CEO’s Strategic Summary Since Acquisition

Going back, where have we been, if I look at each of the areas that we have here, finances, 2002, we started cleaning it up. 2003 we start cleaning and polishing. We have a major exercise now to put a final push, which is to build separate threads for handling the UK style accounting expertise, so we have one more beef-up undergoing for our finances. But my aim is to finish 2005 as totally pure, consolidated and transformed. The whole process of modernisation has finished from being under-invested, through being good enough, through being really quite nice to being, if you are in Old Mutual Group and you are looking for something to applaud, that is the one. Operations, we are one year ahead, we spent 2002 negotiating, we spent 2002/2003 migrating. The end of 2004 our migrating is finished, I expect to spend the whole of 2005, bar an unexpected hiccup, essentially with our Chief Operating Officer finding a new challenge. We have industry best in terms of agent complaints, ie, there are some, but they are fewer than anybody else we know, and we have industry strength better than ever. Sales, it was do the best you can in your client market while we learn the market in 2002, and by golly it was a good year. 2003 was less orderly, because we know where the opportunities of this and that is where the risks occur in the future. 2004 is check the board is working, which it has, very strongly, and 2005 is to pure consolidate and transform.

Slide 14 - Challenges, Progress & Plans

On sales, we have weathered Equity Markets, we have weathered Interest Markets where the markets have favoured high yield curves, we have weathered markets that favoured low yield curves, and what we have seen is this company consistently twice as big as it was before, and potentially three times as big. Reaping the benefits, well that is going to take time. Some come through quickly, enforced items come through quickly. Others we have to allow in the DAC items, which to the new business expenses, the old ones to emerge over the next five years, and to be replaced by the new ones and you will see that coming through over five years with the clock starting in 2002, year end. So that is the migration process, which I intend to see through.

Slide 15 - Market

Now let us talk a bit about the market. I am going to be joined by Bruce Parker for the Q and A session, take any questions and I give you the key marketing message which is: Spread it and get it. The final part of that is feet on the street, which is getting the marketing out of Baltimore, and into the US generally as a whole. I have talked about brand development, it is going to be Old Mutual something, or OM something, Lifestar is an exception because it must sell other companies' products as well. I have talked about dispersion, now let us talk about product success.

Slide 16 - The Distribution Landscape and Our Positioning

Our Power Partner programme is our plan for keeping the top 20 agency groups, and their agents close to us, and developing their product as they want it to. How have we done by product, you can see the implication on the slide, the assortment of colours on the right shows the channel dispersion. There are far fewer colours on the left where there where fewer for sale. I have separated out the Index products from the other fixed annuities also in that chart.

Slide 17 - Life Sales

Life sales, an important stabiliser of the profit flow, which is very profitable, an important stabilizer for capital use, because the dispersion of risk implicit in having a life as well as annuity is well rated by the rating agencies, and therefore helps us to maintain our capital. It is lower than it would otherwise be and our level of capital is 250 per cent of risk based capital, ie, which is five times the 50 per cent threshold for regulator jumping in, and two and a half times the level where the regulator asks a question about solidity. But that steady progression is quite important to our health because the stabilisation gives the capital enhancement it gives to earnings, and the profile it gives to earnings, because this is not a fluctuating stream. Agents loyal to your product and not chasing anything in yield terms, in chasing solid sales.

Slide 18 - Spread Based Products

But our core has been spread based products, we invest in corporate bonds, we take the charge as necessary for the product, and for profit and the long term capital, and then we design product to pass on the balance to the customer. That balance is through the steady growth of term products. Diversified channel takes that over a wider range of customers and wider range of interests.

The OMNIA customer is not interested in whether interest rates are high or low, he is interested in whether the product is sold in US dollars or not, and that does not negate this to his capital, so our steady interest growth, whether it is 1 per cent or 5 per cent suits him, but what matters is that we are selling dollar products that are not linked to the S&P Index, the equity market.

The corporate to corporate has quite different needs, he has the predominant money that he has charged from US government to finance people who invest in mortgage or mortgage back bonds. He places money with us depending on our underlying portfolio, irrespective of what we offer. So these funds only payment of interest rates, which is nice. Strong growth and immediate annuity interest rates is really based not so much on interest rates, it ought to be, but it is not, it is based on people's perceptions of the equity market, we do not want to gamble our life savings, in our retirement annuity equity, so those three channels are not dependent on the absolute level of interest rates, or even how high we are compared to our competitors and those three channels are strong alternatives to our spread based products.

Then in our spread based products the critical thing is to keep ahead of the second raters. You do not have to be a winner, there is plenty of business for many, but you have to show that you are first things first, paying attention to the customers, that comes into product design and the product design we do is developed by the marketing people and the pricing actuaries, it is tested by the Chief Actuary, it is subject to review by KPMG and others and essentially is a strong product. Requires us to be alive in terms of all the moving parts, expenses must not be too much, the capital must be efficient, the return to Old Mutual must be met and the investment performance must equal or exceed bench marks elsewhere in the industry. And then we have something that we mix up the features, and the commission to get the market. And we check it out each month and we report it to Old Mutual each month, we get kicked if we have a bad month, where we are below our target. It will happen, if you have a slide in the interest rate market, you may find for two or three months in a low, the market is against you and you plan your products around 3.8 per cent treasuries and it turns out to a 3.7 per cent market. Over the cycle you get as many times as you are planning around 3.8 per cent and the treasuries turned up and give 3.9 per cent. So the monthly fluctuations are there. Every month, we have to have an explanation and that is part of the control system.

Slide 19 - Equity Indexed Annuities

In 2004, companies that have cheap financing rates and low capital will still be chasing interest rates products. That is not very efficient for us, so we are choosing to go for the equity index market. It is a healthy market for us, but an expertise intensive market. Those who know what they are doing, that is Allianz, ourselves, American Equity, Midland National, have the market and they jostle the position between it, but fundamentally the key there is to have good basic product, a good understanding of the dynamics and a good partner to hedge risk against because you do not want to take the derivative risk yourselves. Some may have elected to go for the high commission versions. We are in the mid-range at the moment. A dynamic hedging programme helps; it is possible by us because we have a good partner in the group, Analytic, and it is possible by us and not by others because, except perhaps for the companies I mentioned, nobody else has the critical mass to do balance, to have the balance sheet hedging dynamically as we do. It has taken us to being number two in the market for the first quarter of this year. If you looked at last year's pattern you will remember that the first half year, our sales were a bit down from a 4 billion a year rate and that our profitability was a bit down because the tailing of interest rates did drop at that time. We did not have an equity index product as good as we wanted to. By the second half, we had the product and things were moving in our favour and we moved our way up to about fourth in the market. At one point, we were third. First quarter of this year, we were second. We will not come first; first is a long way away from us and involves splashing the market, a lot of volume capacity at the agent. That is Allianz's position. I am very happy with two, I am happy with three or four but I am confident about staying up in that level. That is our key market for this year.

Slide 20 - OMNIA Life Bermuda

OMNIA, I mentioned up there, what it is is taking that product range, putting in a variable annuity, making it available to private banking clients, has an average ticket size of US$250-400,000 depending on the bank from which the client is emerging. Our typical ticket size on the onshore product is about $40,000. They are priced similarly, the savings, the size, gives us a lot of extra margin. Corporate to corporate channel, we are using as ballast. FHLB is particularly interesting; it is one of the safest products on our portfolio in terms of options. Any annuity product, of course the client can make a decision to move it and we protect ourselves very thoroughly with market value adjustments and surrender charges. But there is no option that the FHLB has, it is obliged to offer its product by the terms of its charter from federal government which says that if an institution has a mortgage portfolio, whether it is direct mortgage which ours is not or in terms, collatoralising mortgages which ours does, then it has to offer them funds. Well, we can pick that up when we choose to. We chose to do this for two reasons, one because it is highly profitable as the flavour of the month which has been the case for part of this year. Two is because we liked the capacity. We have not picked up any for the last few months because it has not been necessary, the capacity has been there in other respects but it is a device to be sure that we have a well balanced portfolio, another device, season in or season out. It is free of client optionality, the optionality is all on our side, which is pleasant for us. The reason we take a profit margin is because it is essentially based around mortgage interest rates by their charter. Will it be there always? No, I do not expect so but I expect it will be there for good solid years to come. It takes two years to actually go through and finalise a deal with the due diligence, with the issuing bank. We are the only ones who have had the patience to do this with the relevant bank for us, which is the Federal Home Loan Bank for our size. Will it be there forever? Well, I do not want to do any plans around it but it has been there since 1929 so it appears to be well seasoned. Do I want the business to depend on it? No, but as the filler in the portfolio and the one we use repeatedly to keep our earnings smooth in value added terms and in due course in GAAP terms, it works very nicely and we are very pleased with that.

Slide 21 - Corporate-to-Corporate

We also do corporate deals to optimise our risk based capital. Remember that the agencies each have their own risk based capital models but by and large, they like you to have a balance of interest based risk, insurances and any other general businesses. If I can take reinsurance which is light on interest risk but heavy on insurance risk and doing a swap, we actually improve the risk profiles of both the companies and improve our risk based capital as a result. Does it distort the figures? No. Does it help them to the tune of 1 to 2 per cent which is 2-400 million or thereabouts? Yes and therefore we do that too. Do not be surprised if you see as a running theme; do be surprised if you see it as being a major theme because it is a tuning mechanism. I wanted to draw attention to it because it represents the depth of tuning that we like to do.

Slide 22 - Finance

And that takes me into finance. Highlights of finance are: bigger than we used to be, stable, and do not be silly about going for growth for growth's sake.

Slide 23 - Growth Earnings & Capital Needs

So we have had a history of control and diversified growth. I have talked about this already; we are not frightened of decreases in sales, I want them above 3 billion, the company fits quite nicely for that. I am not going to chase it for loss purposes, I want to keep my retail franchise clean, I want to keep access to capital from PLC clean and I will not do that if I go out buying business. So it does not suit me instinctively, quite apart from it does not suit US Life. That means we have a discipline of sales and the disciplines that Bruce Parker has brought to the company have worked very well. He has a broader base than the founding sales team, he has great credibility in the market, he has kept the relationship up well with the original MGA network and he has worked with John Clifford and others on broadening the base. So the discipline has been there, the success has been there. Quarter 1 has shown that; quarter 2, I cannot talk about yet.

Life insurance steady growth is part of the picture. Market opportunities, product design is key to our main channel, do not fall behind everyone else. It is not rocket science, it is a matter of identifying what you can do well, compared with everybody else, checking you have the tools in the kit which we are broad enough to do and going for it, and making sure you have a bunch of people who understand the market or who listen to those who do and actually translate it into product. You will see in the growth history, statutory losses. Statutory losses occur when you are good, the statutory account is a solvency account. If you looked at economic reserves, they are less than you would need on a statutory basis. When you are growing, you need to build up those statutory accounts. I will come in a moment or two to the pattern that is beginning to emerge on statutory. Behind that we have capital and capital statements. Underlying that we have GAAP profits, long been recognized, statutory accounts are inappropriate as showing the health of the company in emerging profits or of the dividends in the Old Mutual case. So everyone is encouraged to use GAAP in the US and we transferred it to UK for our purposes. That is a good indicator. I mention that because I was a little worried to see a long analysis about a year ago that based itself entirely on the statutory, which are very easy to reach but very difficult to read, and should be read in conjunction with GAAP accounts. History and the business plan horizon indicate capital contributions are decreasing and I have a slide of that towards the end.

Slide 24 - Summary Financial Statements – GAAP Balance Sheet – OMUSL

Here is the GAAP balance sheet, there is a lot more detail on that than you are used to. This is all publishable information, you have it in your packs. The key messages are steady process, steady growth and it is growing. And that is really the picture of where the company is and it will continue. Here is the statutory one which I put up to indicate the fact that you compare this 9.7 figure, you say, "Hang on, statutory assets liabilities 9.7, GAAP 13.3". Well, we operate across F&G, Americom, Old Mutual Reinsurance in Ireland which takes about a quarter of the portfolio and this is only the F&G component. I do not have consolidated statutory accounts, they are not the norm in the US within the group because everybody's statutory is on a different basis.

Slide 25 - Summary Financial Statements – Consolidated F&G Life STAT Balance Sheet

This is the US statutory account but it is showing nothing that would cause a US analyst concern. It is going steady, it is going nicely, it has the interest maintenance reserves to stop the companies spending in their statutory profit line any receipts it has from sales or income that is high interest related to reserves, and to spread out effects. So it is a fairly vanilla statutory account.

Slide 26 - Summary Financial Statements – GAAP Operating Earnings OMUSL

Here is the GAAP earnings, again more detail than you are used to. I would just like to draw your attention to amortisation of the DAC which is steady in our full year post and will continue to grow slightly but will steady off as we continue at our plateau of 3 to 4 billion. Change in investment market value, which is of course dependent on outside conditions and a strong and healthy return there. Here we are taking out the largest amount of change in investment market value, which is the LTIR. I have included the operating earnings of F&G because it shows the shape that I am aiming for.

Slide 27 - Summary Financial Statements – Consolidated F&G Life STAT Operating Earnings

You will see for the first year in 2003, excluding the realised capital effects, which is market fluctuation related and could go either way of the cycle, the net operating state is now zero at 2003. You can extrapolate it to 2004, so the message from that is as far as stretching to capital needs, F&G is now in the right point in its cycle of movement from a small company to a medium company to have taken those down to neutrality. But the essential message is capital turning the corner.

So I now have slides on particular aspects: capital, investments and expenses.

Slide 28 - Capital

Capital is important, concern is Old Mutual going to pump money, money, money? No, we have designed this company to move swiftly from plateau A, a billion to a billion and a half, to plateau B, 3 to 4 billion sales. As you go through that cycle of the plateau, after five years, your mature company is at a new level. And in that cycle, then you need capital in the early stages and you do not need capital in the later stages. If you reach maturity or towards it, you have the choice of whether to aim for a new plateau or to start repaying dividends as cash. We are managing to about 250 per cent and that has been consistent since we bought the company. There is a drift to push it higher, rating agencies drifts. They take a more cautious view of the market. The key agency, A M Best, has maintained our rating throughout this period; we do not have indication they tend to do anything else. That is critical to our sales. So we are looking at that as our capitalisation ratio. On that basis, this is going to be 100 million capital, give or take a small amount. Last year was 109 million. Message being, including funding the statutory, the statutory contribution included funding the risk based capital needs of the portfolio, we have now cusped our capital need and we will see it go down. On this volume, we should be self-sustaining by 2007. All our financing or statutory effects and all our capital behind reduces. It could change. Changing to another plateau of sales, which would be a conscious decision by PLC and ourselves. If we jump down to one and a half billion a year coming in, oh, boy, we do see capital being the least. You also see the value has no longer been built up. If you went the other way and tried to jump us to a 6~billion company, which the market might allow, you would have the opposite effect, you would have vast capital needs. We have chosen the plateau of 3 to 4 billion, we are consistent on that and we have achieved capital neutrality, within the US on the statutory accounts and we are targeting that neutrality including the risk in '07. It is a much more disciplined approach than I have known in other companies.

Slide 29 - Investments

Investment portfolio, I brought this up to show diversification, with mortgage in there, which with hindsight I wish I had broken up. High yield part of the portfolio is always receiving attention. Our investment guidelines are not to go above 10 per cent, we are currently on 8 per cent. It is interesting at the moment that the US corporate bond market has taken such a benign view of future defaults and the spread between high yield and regular corporate bonds are now very thin. We are not buying at this stage any more high yield bonds because there is not enough advantage on it to pay for the capital loans in the risk based capital formula, which charges heavily for usage of high yield. We like high yield, it is generally useful; we would be happy to go up to 10 per cent if circumstances warranted, they do not at the moment. You will not expect to see that figure rise if today's economic views continue.

Slide 30 - Expenses Levels

The last matter I want to talk to you about: expenses. We bought an under-invested but very healthy sales company with problems with its bottom line, such problems as there were only through expense management. We have been benchmarking where we are related to our peers, companies owned by UK companies, other brokerage peers and various categories. We look pretty good on that, not good enough, but where I intend to be is in this sort of range between 2003 and 2002. 2002 we had the 4 billion volume, and the low expense ratio that we have there showed how well we were tooled up for 4 billion of volumes. 2003, it was 3 billion volumes and our expense ratio was not as good as it had been the previous year. I want to work on that because I want to make anything that we have with 3 billion onwards, and my team is reminding me on this, to be a source of expense profit so we balance at 3 billion rather than at 4.

Outlook, I said, was the last section; I have no slides on this. Our outlook is that we believe we have a very solid sales base, nicely spread, nicely risk diversified for being a 3 to 4 billion a year company. A bad year is 3 billion and a good year is 4 billion. I do not want to go charging ahead in large volumes beyond that because I am building up a nice progression from the old profit characteristics to the new profit characteristics, from the old expense characteristics to the new and from the old capital characteristics to the new. Something ought to be done with the franchise at some stage, but let that be a conscious decision, this is not going to be a company that is going to drift. So the outlook, I think, for US Life is that we will have fluctuations, we will continue to push through efficiencies in the structure, we view ourselves as having a critical mass and some intrinsic stability in the organisation, it may not have been there in the past. We certainly view ourselves as being a much more material and effective company than what we bought and that was pretty good, very good on sales. So the outlook is very, very exciting, more of the same and I want to consolidate around that.

Now, I have the team in Baltimore, we are going to try to switch to seeing them during Q and A, by video conference.

Question and Answer Session (see separate file)

MR BARKER: Can I introduce from left to right, John Fenn, Accountant, Michel Perreault, Actuary and Bruce Parker. John is in the high thinking end of the accounts in direct report to John Varvaris, the CFO; Michel is the Chief Actuary and Bruce Parker is the Chief Marketing Officer, President and Chief Executive of Old Mutual Financial Network, the sales organisation. Do you have any questions?