Market release

Challenger Limited

09 February 2021

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CHALLENGER ANNOUNCES HALF YEAR RESULTS

- Strong growth and diversification providing business momentum
  - Life book growth 4.7% in 1H21
  - Funds Management net inflows $6.4 billion in 1H21
  - Group assets under management up 13% to $96 billion in 1H21
  - Bank acquisition to drive medium-term growth
- Performance in line with expectations
  - Normalised net profit before tax (NPBT) $196 million reflects progressive deployment of excess liquidity
  - On-track for full year normalised NPBT guidance
  - Statutory net profit after tax $223 million with positive investment experience
- Strongly capitalised
  - Challenger Life Company Limited excess capital above top end of target range
  - Dividend 9.5 cents per share fully franked

Challenger Limited (ASX: CGF) today announced its results for the first half of the 2021 financial year, with very strong growth in its Funds Management business and growing momentum in its Life business demonstrating the benefits of its strategy of diversification.

Managing Director and Chief Executive Officer Richard Howes said the outcomes were in line with expectations and Challenger was on-track to deliver a full year normalised profit before tax within its guidance range of between $390 million and $440 million.

Mr Howes said: “Our strategy of diversifying revenue is working with strong book growth in our Life business and industry leading organic flows in Funds Management.

“We remain strongly capitalised with prudent portfolio settings which are appropriate given our growing customer franchise. The investment portfolio is in good shape, with no significant credit defaults and stable property valuations during the half year. We are gradually deploying our excess cash and liquidity to enhance future returns.

“The Board has declared a dividend of 9.5 cents per share reflecting confidence in our future business performance and in the strength of our capital position.

“Our Funds Management business is the fourth largest and fastest growing active manager in the country. Fidante net inflows near tripled to $5.8 billion in the half, supported by very strong institutional flows and retail flows, which were up 32% compared to the previous corresponding period.

“We continue to be the number one provider of secure retirement income streams in Australia and have benefited from our strategy of diversifying into institutional and overseas markets.

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"We have reported record long-term annuity sales[1] during the half, which underpin future book growth. We have also seen stabilisation in the adviser market and deepened our relationships with independent financial advisers.

"Our recently announced acquisition[2] of a bank will provide us with an opportunity to extend our customer and product reach. It allows us to play a greater role in supporting customer retirement incomes, and attracting new customers more directly, including pre-retirees.

"The highly strategic acquisition reflects our confidence in the broader role that guaranteed products will play in retirement, the growth that we will enjoy as a result, and our willingness to invest to capture this growth over the medium term.

"The federal government's Retirement Income Review, released in December 2020, highlights the importance of finding better solutions for retirement. The focus on retirement solutions reinforces the importance of the role that we play in the sector.

"Challenger enters the second half of the 2021 financial year in good shape, having withstood industry and COVID-19 related disruption of recent years. Our strong performance in funds management, building momentum in annuities, and new opportunities in banking mean Challenger is well placed to achieve our vision of providing customers with financial security for retirement.

Group financial performance

Driven by strong growth in both Life and Funds Management, Group assets under management increased by 13% to $96 billion over the half.

The financial performance for the last half reflected steps taken to move to more defensive investment portfolio settings in the early stages of the COVID-19 pandemic, including holding higher levels of liquidity which will be gradually deployed over the year.

As a result, normalised NPBT[7] was down 14% to $196 million, compared to the second half of the 2020 financial year.

Normalised net profit after tax (NPAT)[7] was down 10% to $137 million, compared to the second half of the 2020 financial year. Statutory net profit after tax was $223 million, including positive investment experience[3] of $87 million, which represented the partial reversal of investment experience losses incurred last year.

Reflecting the confidence in future business performance and strong capital position, the Board declared an interim 2021 dividend of 9.5 cents per share, fully franked.

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[1] Long-term annuities represent Lifetime and MS Primary annuities.
[2] The acquisition is subject to regulatory approval by both APRA and the Federal Treasurer and is expected to settle in late March 2021 once approval has been obtained.
[3] All investment experience numbers quoted after-tax.

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Challenger Life

Challenger Life earnings before interest and tax (EBIT) was $193 million. Total Life sales were $3.4 billion, up 10% compared to the prior corresponding period, including record long-term annuity sales. The strong sales result reflected Challenger's strategy of diversifying revenue streams and provides a solid basis for future earnings in the Life book.

Domestic annuity sales were up 11%, with the strongest growth in lifetime annuities. Domestic sales benefited from new institutional client opportunities, a stabilisation in the adviser market and greater penetration among independent financial advisers.

The contribution from annuity sales in Japan (MS Primary) rose 15% and represented approximately one-quarter of total first half annuity sales.

Notwithstanding elevated maturities during the period, the Life book grew 4.7%[4] in the half reflecting the significant growth in sales.

Challenger Life maintained a strong capital position and had $1.5 billion of excess regulatory capital, unchanged for the half. The PCA ratio[5] of 1.63 times was around the top end of the target range of 1.3 to 1.6 times the minimum amount set by the Australian Prudential Regulation Authority.

Challenger expects to deploy around $1 billion of cash and liquids in the second half which is expected to support earnings growth and intends to maintain a PCA ratio around the top end of the target range.

Funds Management

Funds Management had a very strong half. Net flows for the half year were $6.4bn, reflecting strong contributions from both retail and institutional clients, and benefiting from a diverse range of boutiques. Fidante Partners' leading distribution capability was recognised by Zenith Investment Partners, winning their 2020 Distributor of the Year.

Net flows were also supported by ongoing superior investment performance, with 88% of Fidante Partners funds under management (FUM) outperforming benchmark over five years[6].

First half Funds Management EBIT increased by 18% on the previous half, benefiting from an increase in FUM based management fees and disciplined expense control. Average FUM in the first half was $85.9 billion, up 7% for the half.

Closing FUM was $91.2 billion and is 6% higher than average FUM, providing strong business momentum heading into the second half.

Outlook

Challenger expects normalised net profit before tax in FY21 in the range of $390 million to $440 million. Earnings are expected to be weighted to the second half reflecting the gradual deployment of Life's excess cash and liquid investments over the year.

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[4] Book growth percentage represents net flows for the period divided by opening book value for the financial year.
[5] The PCA ratio represents the total Challenger Life Company Limited Tier 1 and Tier 2 regulatory capital base divided by the Prescribed Capital Amount.
[6] As at 31 December 2020. Percentage of Fidante Partners Australian boutiques meeting or exceeding performance benchmark.

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Investor Presentation Webcast

Challenger's Managing Director and Chief Executive Officer Richard Howes and Chief Financial Officer Andrew Tobin will give an investor presentation on the results at 9:30am (Sydney time) on 9 February 2021). The presentation will be streamed live via webcast which can be accessed at www.challenger.com.au.

Disclaimer

The forward-looking statements, estimates and projections contained in this release are not representations as to future performance and nothing in this release should be relied upon as guarantees or representations of future performance.

This release has been authorised by Challenger's Continuous Disclosure Committee.

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Key metrics[7]

	1H21	2H20	1H20	Change 1H21-2H20	Change 1H21-1H20
Total assets under management ($bn)	96.1	85.2	86.3	13%	11%
Annuity sales ($bn)	2.2	1.2	2.0	87%	12%
Total Life sales ($bn)	3.4	2.0	3.1	71%	10%
Life net flows ($bn)	0.7	(0.6)	0.9	n/a	(23%)
Funds Management net flows ($bn)	6.4	0.7	1.9	large	large
Normalised NPBT ($m)	196	228	279	(14%)	(30%)
Normalised NPAT ($m)	137	152	191	(10%)	(29%)
Statutory NPAT ($m)	223	(636)	220	n./a	1%
Normalised basic EPS (cps)	20.4	25.0	31.5	(18%)	(35%)
Statutory basic EPS (cps)	33.2	(104.4)	36.3	n.a	(9%)
CLC excess regulatory capital ($bn)	1.5	1.6	1.4	(4%)	8%
Normalised ROE pre-tax (%)	11.5	14.0	15.2	(250 bps)	(370 bps)
Normalised ROE post-tax (%)	8.0	9.4	10.4	(140 bps)	(240 bps)
Statutory ROE post-tax (%)	13.0	(39.2)	12.0	n/a	100 bps
Normalised cost to income ratio (%)	39.0	38.1	33.5	90 bps	550 bps
Interim dividend (cps)	9.5	-	17.5	9.5 cps	(8.0 cps)

[7] The normalised profit figures are non-statutory amounts and in Challenger's view better reflect the underlying operating performance of the business. The normalised profit figures exclude investment experience and significant items. Investment experience includes both assets and policy liability experience and net new business strain. Asset and liability experience is calculated as the difference between actual investment gains/losses (both realised and unrealised) and normalised capital growth in relation to assets, plus any economic and actuarial assumption changes in relation to policy liabilities for the period. New business strain results from using the risk-free rate plus an illiquidity premium to value term and lifetime annuities. New business strain is a non-cash item and subsequently reverses over the future period of the contract. The normalised profit also excludes any significant items which represent non-recurring income and expense items for the period. The normalised profit framework and reconciliation to statutory profit have been discussed in Section 8 of the Operating and Financial Review in the 2021 Interim Financial Report. The normalised profit is not audited but is subject to a review performed by Ernst & Young.

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About Challenger

Challenger Limited (Challenger) is an investment management firm focusing on providing customers with financial security for retirement.

Challenger operates two core investment businesses, a fiduciary Funds Management division and an APRA-regulated Life division. Challenger Life Company Limited (Challenger Life) is Australia's largest provider of annuities.

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