

Challenger Capital Notes

Newsletter February 2021



Peter Polson
Chair

\$96.1_{bn}

Group assets under management

Value of assets managed by Challenger up 13% for the half year

\$196_m

Normalised NPBT¹

On-track for FY21 profit guidance of between \$390m to \$440m

\$223_m

Statutory NPAT¹

Includes partial reversal of unrealised pandemic related investment losses

+4.7%

Life book growth

Benefiting from diversification strategy

+\$6.4_{bn}

Funds Management net flows

Fastest growing Australian Active Fund Manager²

\$1.5_{bn}

Excess capital above APRA requirement

Strongly capitalised and above capital targets

Dear Noteholder,

On behalf of the Board and management team, I'm pleased to provide you with an update on Challenger's performance over the first half of the 2021 financial year.

Having withstood industry and COVID-19 related disruption over recent years, this result shows our strategy to diversify revenue is working.

Demonstrating strong growth in both Life and Funds Management, Group Assets Under Management increased 13% to \$96 billion over the half.

As Australia's number one provider of annuities, we believe in the importance of guaranteed income in retirement. The federal government's Retirement Income Review, released in December 2020, highlighted the importance of better retirement solutions, reinforcing the important role we play in providing customers with financial security for retirement.

Our Funds Management business is the fastest growing² and fourth largest³ active fund manager in the country and attracted \$6.4 billion of new funds during the half.

In December, we announced the acquisition of MyLife MyFinance, an Australian-based customer savings and loans bank that will allow us to enter Australia's term deposit market. This acquisition will increase the role Challenger plays supporting customer retirement incomes, extend our customer reach and accelerate our medium-term growth.

Financial performance

Challenger's financial performance in the first half of the 2021 financial year reflects steps taken last financial year to move to more defensive investment portfolio settings in the early stages of the COVID-19 pandemic. These actions included increasing levels of cash and liquidity which, as previously flagged, we expect to progressively deploy over the remainder of the 2021 financial year to enhance earnings.

Normalised net profit before tax (NPBT)¹ reflects the changes made to Life's investment portfolio and was down 14% to \$196 million, compared to the second half of the 2020 financial year.

Statutory net profit after tax was \$223 million, up significantly on the second half of last year, and includes the partial reversal of pandemic related investment losses recognised last year.

Life sales continue to benefit from our diversification strategy and increased by 10% on the prior comparative period to \$3.4 billion. Sales in all key product categories increased, driving a ~5% increase in the size of Life's guaranteed income business over the half.

Funds Management earnings benefited from a stable margin and increase in funds under management, aided by both strong inflows and more positive investment markets.

Reflecting the strength of our distribution capability, Fidante Partners won Distributor of the Year at the annual Zenith Fund awards.

¹ Normalised profit framework and a reconciliation to statutory net profit after tax is disclosed in Section 8 of the Operating and Financial Review in the Challenger 2021 Interim Financial Report.

² Measured as listed Australian fund manager net flows over the past 12 months divided by FUM 12 months ago. Data based on most recent ASX disclosures.

³ FUM for Australian Fund Managers – Rainmaker Roundup, September 2020.

Challenger Life strongly capitalised

Challenger Life remains strongly capitalised and is maintaining appropriate investment portfolio settings. The investment portfolio remains in good shape with no significant credit defaults and stable property valuation outcomes during the half year.

Challenger Life has \$1.5 billion of excess regulatory capital, which is well above both APRA's minimum requirement and our own internal capital targets.

Reflecting confidence in both the business performance and capital position, the Board has recommenced paying dividends after pausing during the early stages of the pandemic. The Board declared a 9.5 cent fully franked interim dividend.

Launch of Challenger Capital Notes 3 (ASX: CGFPC) and replacement of Challenger Capital Notes (ASX: CGFPA)

In October 2020, Challenger announced a new Challenger Capital Notes Offer (Challenger Capital Notes 3) with the proceeds to be used to repurchase Challenger Capital Notes.

Challenger completed the Challenger Capital Notes 3 Offer, which raised \$385 million. The proceeds were used to partially repurchase Challenger Capital Notes.

Whilst it was Challenger's intention to fully repurchase all Challenger Capital Notes, \$47 million remains on issue as noteholders were not required to participate in the repurchase offer.

Challenger Capital Notes will continue to trade on ASX until Wednesday 25 May 2022, at which point Challenger must convert any outstanding Challenger Capital Notes into Challenger ordinary shares in accordance with the Challenger Capital Notes Terms, subject to the mandatory conversion conditions under the Challenger Capital Notes Terms. Challenger will consider its options to reduce the remaining size of Challenger Capital Notes before the mandatory conversion date.

Franking of Capital Notes distributions

The Challenger Board seeks to frank shareholder dividends to the maximum extent possible, as it is an effective use of franking credits. Challenger Capital Notes distributions are required to be franked at the same level as Challenger dividends.

Challenger's 2021 interim dividend has been fully franked and as a result, all Capital Notes distributions up until 30 June 2021 will also be fully franked, including the February 2021 quarterly distributions period.

Outlook

Challenger expects normalised net profit before tax in the 2021 financial year to be in the range of between \$390 million to \$440 million. The gradual and prudent deployment of Life's excess liquidity will mean earnings are expected to be weighted to the second half.

Our strong performance in Funds Management, building annuity sales momentum and new opportunities in our banking operations mean Challenger is well placed to achieve our vision of providing customers with financial security for retirement.

Thank you for your ongoing support and commitment to Challenger.



Peter Polson
Independent Chair
Challenger Limited

Additional information section

Manage your holding

For administrative matters in respect of your Challenger Capital Notes, please contact Computershare Investor Services.

T: 1800 780 782

› computershare.com.au

Challenger Capital Notes distribution history

Distribution payment date	Cash distribution	Total return p.a.
25 November 2020	\$0.62	3.50%
25 August 2020	\$0.62	4.26%
25 May 2020	\$0.73	4.28%
25 February 2020	\$0.76	4.36%

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Challenger Capital Notes 2 distribution history

Distribution payment date	Cash distribution	Total return p.a.
23 November 2020	\$0.79	4.51%
24 August 2020	\$0.81	4.50%
22 May 2020	\$0.89	5.28%
24 February 2020	\$0.95	5.29%