

Analyst Pack FY15

30 June 2015

**Challenger Limited** provides  
Australians with financial security  
for retirement.

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## Important Note

Information presented in the FY15 Analyst Pack is presented on an operational basis (rather than statutory) to reflect a management view of the business. Challenger Limited (ACN 106 842 371) also provides statutory reporting as prescribed under the Corporations Act 2001. The audited full year financial report is available from Challenger's website at [www.challenger.com.au](http://www.challenger.com.au).

The analyst pack is not audited. The statutory net profit after tax as disclosed in the consolidated profit and loss (see page 2) has been prepared in accordance with Australian Accounting Standards and the Corporations Act 2001. Challenger's external auditors, Ernst & Young, have audited the statutory net profit after tax as disclosed in the consolidated profit and loss. Normalised net profit after tax, as disclosed in the consolidated profit and loss (see page 2) has been prepared in accordance with a normalised profit framework. The normalised profit framework has been disclosed in section 4.3 of the Directors' Report in the Challenger Limited 2015 Annual Report. The normalised profit after tax has been subject to a review performed by Ernst & Young.

Any forward looking statements included in this document are by nature subject to significant uncertainties, risks and contingencies, many of which are outside the control of, and are unknown to, Challenger, so that actual results or events may vary from those forward looking statements, and the assumptions on which they are based.

Past performance is not an indicator of future performance.

While Challenger has sought to ensure that information is accurate by undertaking a review process, it makes no representation or warranty as to the accuracy or completeness of any information or statement in this document. In particular, information and statements in this document do not constitute investment advice or a recommendation on any matter, and should not be relied upon.

## Key Performance Indicators

	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
<b>Earnings</b>									
Normalised NPAT (\$m)	334.0	328.7	308.5	179.1	154.9	165.2	163.5	159.8	148.7
Statutory NPAT (\$m)	299.0	340.6	416.8	168.9	130.1	174.3	166.3	194.8	222.0
Normalised EBIT (\$m)	438.4	387.9	364.8	232.0	206.4	195.1	192.8	187.0	177.8
Underlying operating cash flow (\$m)	287.9	321.0	321.5	194.3	93.6	177.6	143.4	170.4	151.1
Normalised cost to income ratio	33.8%	34.6%	34.4%	33.3%	34.4%	35.2%	34.0%	33.9%	35.0%
Normalised effective tax rate	23.1%	14.4%	14.4%	22.1%	24.3%	14.5%	14.2%	13.6%	15.1%
Normalised effective tax rate excluding TOFA <sup>1</sup>	23.1%	22.2%	22.7%	22.1%	24.3%	22.3%	22.1%	21.8%	23.7%
<b>Earnings per share (cents)</b>									
Basic – normalised	61.2	64.0	58.6	32.4	28.8	32.2	31.8	30.7	28.0
Basic – normalised excluding TOFA <sup>1</sup>	61.2	58.1	52.9	32.4	28.8	29.3	28.9	27.8	25.2
Basic – statutory	54.8	66.3	79.2	30.5	24.2	34.0	32.3	37.4	41.8
Diluted – normalised	57.2	60.6	58.0	30.0	27.0	30.4	30.3	30.2	27.8
Diluted – normalised excluding TOFA <sup>1</sup>	57.2	55.1	52.3	30.0	27.0	27.6	27.5	27.4	25.0
Diluted – statutory	51.4	62.8	78.3	28.3	22.8	32.1	30.8	36.8	41.5
<b>Return on equity (%)</b>									
Normalised Return on Equity (RoE) – pre-tax	18.0%	18.8%	19.6%	18.6%	17.4%	18.6%	18.9%	19.7%	19.6%
Normalised Return on Equity (RoE) – post-tax	13.9%	16.1%	16.8%	14.5%	13.2%	15.9%	16.2%	17.0%	16.6%
Statutory Return on Equity (RoE) – post-tax	12.4%	16.7%	22.7%	13.7%	11.1%	16.8%	16.5%	20.7%	24.9%
<b>Capital management</b>									
Net assets – average <sup>2</sup> (\$m)	2,410	2,044	1,836	2,494	2,331	2,090	2,000	1,899	1,772
Net assets – closing (\$m)	2,543	2,153	1,947	2,543	2,443	2,153	2,052	1,947	1,827
Net assets per basic share (\$)	4.60	4.22	3.78	4.60	4.42	4.22	3.99	3.78	3.47
Net tangible assets (\$m)	1,994	1,607	1,426	1,994	1,896	1,607	1,530	1,426	1,308
Net tangible assets per basic share (\$)	3.60	3.15	2.77	3.60	3.43	3.15	2.98	2.77	2.48
Dividend (cps)	30.0	26.0	20.0	15.5	14.5	13.5	12.5	10.5	9.5
Dividend franking (%)	85.5	20.8	–	100.0	70.0	40.0	–	–	–
Normalised dividend payout ratio	49.0%	40.6%	34.1%	47.8%	50.4%	41.9%	39.3%	34.2%	33.9%
Share buy back (\$m)	–	–	50.0	–	–	–	–	29.6	20.4
<b>Sales and net flows</b>									
Life sales (\$m)									
Retail	2,753.1	2,798.8	2,179.2	1,178.3	1,574.8	1,341.8	1,457.0	1,123.9	1,055.3
Institutional	944.0	581.6	951.8	395.1	548.9	291.5	290.1	30.6	921.2
Total Life sales	3,697.1	3,380.4	3,131.0	1,573.4	2,123.7	1,633.3	1,747.1	1,154.5	1,976.5
Life retail net flows <sup>3</sup> (\$m)	738.2	887.1	598.1	177.4	560.8	347.2	539.9	385.3	212.8
Life retail annuity book (\$m)	8,692.6	7,824.3	7,123.3	8,692.6	8,573.1	7,824.3	7,617.2	7,123.3	6,819.6
Life retail net book growth <sup>3</sup>	9.4%	12.5%	9.1%	2.2%	7.2%	4.6%	7.6%	5.6%	3.2%
Funds Management – net flows (\$m)	7,738.9	2,147.4	6,978.6	972.7	6,766.2	1,033.6	1,113.8	4,754.4	2,224.2
<b>Assets under management (\$m)</b>									
Life	12,795	11,087	10,787	12,795	12,393	11,087	10,889	10,787	10,170
Funds Management	57,902	47,126	41,103	57,902	55,212	47,126	44,986	41,103	35,335
Cross holding elimination	(10,908)	(7,488)	(7,120)	(10,908)	(10,436)	(7,488)	(7,061)	(7,120)	(7,221)
Total assets under management	59,789	50,725	44,770	59,789	57,169	50,725	48,814	44,770	38,284
<b>Other</b>									
Headcount – closing FTEs	560	539	487	560	563	539	498	487	482
Weighted average number of basic shares on issue (m)	545.7	513.8	526.1	553.2	538.2	513.1	514.5	520.8	531.4
Number of basic shares on issue (m)	553.4	510.6	515.6	553.4	552.9	510.6	514.1	515.6	526.4
Share price closing (\$)	6.72	7.44	4.01	6.72	6.53	7.44	6.20	4.01	3.54

1 Normalised tax includes the effect of a private binding tax ruling received from the ATO in February 2012 in relation to the application of Taxation of Financial Arrangements (TOFA). The TOFA private tax ruling reduces normalised tax by \$30m p.a. in FY13 to FY14.

2 Net assets – average calculated on a monthly basis.

3 2H14 and FY14 excludes \$284m maturity of the High Yield Fund annuity.

## Consolidated profit and loss

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
Cash earnings	463.4	425.7	416.2	240.1	223.3	214.4	211.3	209.7	206.5
Normalised capital growth	80.4	55.6	36.0	45.9	34.5	29.7	25.9	17.4	18.6
<b>Normalised Cash Operating Earnings (COE)</b>	<b>543.8</b>	<b>481.3</b>	<b>452.2</b>	<b>286.0</b>	<b>257.8</b>	<b>244.1</b>	<b>237.2</b>	<b>227.1</b>	<b>225.1</b>
Net fee income	117.5	110.2	99.4	61.4	56.1	56.4	53.8	54.2	45.2
Other income	1.3	1.8	4.9	0.6	0.7	0.6	1.2	1.7	3.2
<b>Total net income</b>	<b>662.6</b>	<b>593.3</b>	<b>556.5</b>	<b>348.0</b>	<b>314.6</b>	<b>301.1</b>	<b>292.2</b>	<b>283.0</b>	<b>273.5</b>
Personnel expenses	(154.8)	(144.4)	(130.3)	(78.3)	(76.5)	(74.8)	(69.6)	(64.9)	(65.4)
Other expenses	(69.4)	(61.0)	(61.4)	(37.7)	(31.7)	(31.2)	(29.8)	(31.1)	(30.3)
<b>Total expenses</b>	<b>(224.2)</b>	<b>(205.4)</b>	<b>(191.7)</b>	<b>(116.0)</b>	<b>(108.2)</b>	<b>(106.0)</b>	<b>(99.4)</b>	<b>(96.0)</b>	<b>(95.7)</b>
<b>Normalised EBIT</b>	<b>438.4</b>	<b>387.9</b>	<b>364.8</b>	<b>232.0</b>	<b>206.4</b>	<b>195.1</b>	<b>192.8</b>	<b>187.0</b>	<b>177.8</b>
Interest and borrowing costs	(3.8)	(4.1)	(4.6)	(2.1)	(1.7)	(1.9)	(2.2)	(1.9)	(2.7)
<b>Normalised profit before tax</b>	<b>434.6</b>	<b>383.8</b>	<b>360.2</b>	<b>229.9</b>	<b>204.7</b>	<b>193.2</b>	<b>190.6</b>	<b>185.1</b>	<b>175.1</b>
Normalised tax <sup>1</sup>	(100.6)	(55.1)	(51.7)	(50.8)	(49.8)	(28.0)	(27.1)	(25.3)	(26.4)
<b>Normalised profit after tax</b>	<b>334.0</b>	<b>328.7</b>	<b>308.5</b>	<b>179.1</b>	<b>154.9</b>	<b>165.2</b>	<b>163.5</b>	<b>159.8</b>	<b>148.7</b>
Investment experience after tax	(35.0)	11.9	99.8	(10.2)	(24.8)	9.1	2.8	26.5	73.3
Significant items after tax <sup>2</sup>	–	–	8.5	–	–	–	–	8.5	–
<b>Statutory net profit after tax</b>	<b>299.0</b>	<b>340.6</b>	<b>416.8</b>	<b>168.9</b>	<b>130.1</b>	<b>174.3</b>	<b>166.3</b>	<b>194.8</b>	<b>222.0</b>
<b>Performance analysis</b>									
Normalised earnings per share – basic (cents)	61.2	64.0	58.6	32.4	28.8	32.2	31.8	30.7	28.0
Shares for basic EPS calculation	545.7	513.8	526.1	553.2	538.2	513.1	514.5	520.8	531.4
Normalised cost to income ratio	33.8%	34.6%	34.4%	33.3%	34.4%	35.2%	34.0%	33.9%	35.0%
Normalised effective tax rate	23.1%	14.4%	14.4%	22.1%	24.3%	14.5%	14.2%	13.6%	15.1%
Normalised effective tax rate excluding TOFA <sup>1</sup>	23.1%	22.2%	22.7%	22.1%	24.3%	22.3%	22.1%	21.8%	23.7%
<b>Total net income analysis</b>									
Cash earnings (Life)	69.9%	71.7%	74.7%	69.0%	71.0%	71.2%	72.3%	74.1%	75.5%
Normalised capital growth (Life)	12.1%	9.4%	6.5%	13.2%	11.0%	9.9%	8.9%	6.1%	6.8%
Net fee income (Funds Management)	17.7%	18.6%	17.9%	17.6%	17.8%	18.7%	18.4%	19.2%	16.5%
Other income (Corporate)	0.2%	0.3%	0.9%	0.2%	0.2%	0.2%	0.4%	0.6%	1.2%
<b>Normalised EBIT by division</b>									
Life	456.7	404.2	381.9	240.9	215.8	203.6	200.6	191.8	190.1
Funds Management	44.1	43.3	34.1	23.3	20.8	22.6	20.7	21.2	12.9
Corporate	(62.4)	(59.6)	(51.2)	(32.2)	(30.2)	(31.1)	(28.5)	(26.0)	(25.2)
<b>Normalised EBIT</b>	<b>438.4</b>	<b>387.9</b>	<b>364.8</b>	<b>232.0</b>	<b>206.4</b>	<b>195.1</b>	<b>192.8</b>	<b>187.0</b>	<b>177.8</b>

1 Normalised tax includes the effect of a private binding tax ruling received from the ATO in February 2012 in relation to the application of Taxation of Financial Arrangements (TOFA). The TOFA private tax ruling reduces normalised tax by \$30m p.a. in FY13 to FY14.

2 2H13 and FY13 significant items after tax primarily represents the gain on sale of Challenger's equity investment in Homeloans Limited.

## Consolidated profit and loss

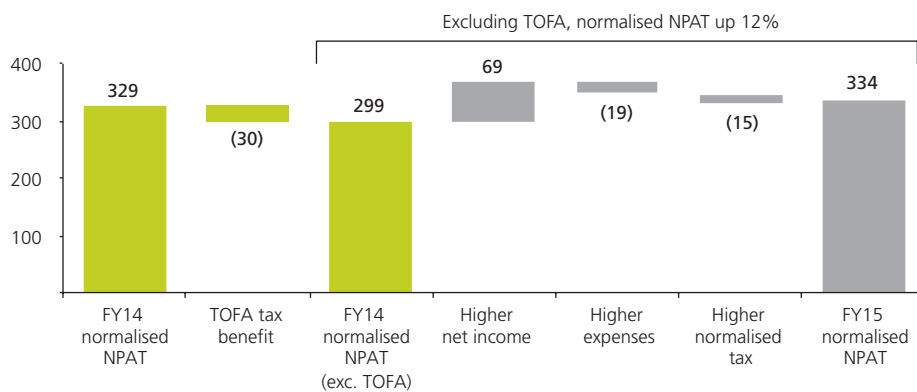
### Normalised net profit after tax

Normalised net profit after tax was \$334m in FY15, up 2% from \$329m in FY14. The increase in normalised net profit after tax reflects a 13% (\$50m) increase in EBIT, partially offset by higher normalised tax (up \$45m). EBIT increased as a result of AUM growth, driving a \$69m (12%) increase in net income, partially offset by a \$19m (9%) increase in expenses.

The increase in normalised tax (up \$45m) is predominately due to the conclusion of the Taxation of Financial Arrangements (TOFA) transitional deduction, which ended on 30 June 2014. As a result of TOFA, FY14 normalised tax was reduced by \$30m, with no corresponding TOFA benefit recognised in FY15 (refer to page 4 for additional detail).

Excluding the impact of TOFA, normalised net profit after tax increased by 12% (\$35m).

### Change in normalised net profit after tax (\$m)

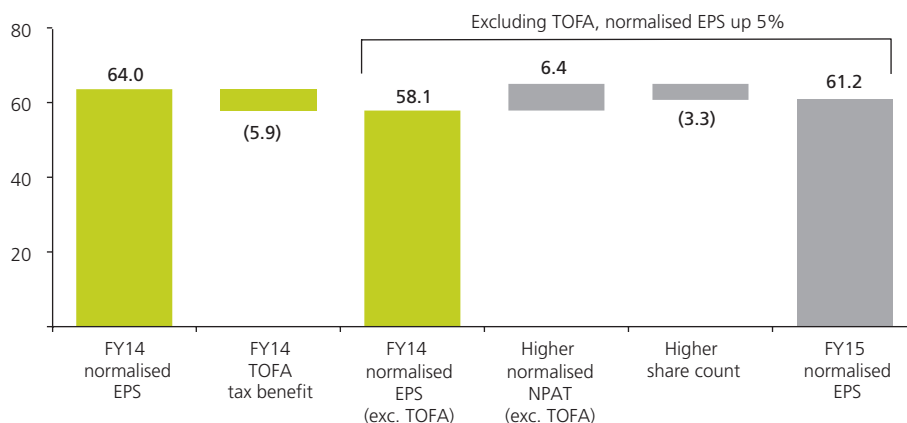


### Normalised EPS

Normalised EPS decreased by 4% from 64.0 cps in FY14 to 61.2 cps in FY15. The decrease in normalised EPS reflects higher normalised net profit after tax (up \$5m), offset by a higher weighted average number of shares on issue following the capital initiatives undertaken in 1H15 (refer to page 11 for additional detail).

Normalised net profit after tax and normalised EPS were both impacted by the transitional TOFA tax deductions that concluded on 30 June 2014. Excluding TOFA, normalised EPS increased by 5% from 58.1 cps in FY14 to 61.2 cps in FY15.

### Change in normalised EPS (cps)



## Total net income

Total net income increased by \$69m (12%) in FY15 due to:

- higher Life Cash Operating Earnings (up \$62m or 13%) as a result of higher Life average AUM (up 13%) with a stable Life COE margin (4.5%); and
- higher Funds Management net fee income (up \$7m or 7%) as a result of higher average FUM (up 24%).

## Expenses

FY15 total expenses were \$224m, up \$19m (9%) on FY14. The increase in expenses relates to higher personnel costs (up \$10m) as a result of an increase in employee numbers and higher other expenses (up \$9m).

Personnel costs increased due to higher employee numbers, which increased by 4% to 560 people in FY15. Employees have been added across distribution, fixed income asset origination and IT in order to support Challenger's growth ambitions.

Other costs increased as a result of including Accurium (acquired in February 2014) for a full year (\$2m impact) and one off expenses of \$3m in relation to the Kapstream sale and Fidante Partners European expansion (including Dexion Capital acquisition costs).

Challenger's business remains one of Australia's most efficient financial services companies and is highly scalable. In FY15 the cost to income ratio fell by 80 bps to a new low of 33.8%.

Challenger's business is growing strongly with some of the benefits of scale being reinvested back into the business in order to capture future growth opportunities.

Challenger targets a normalised cost to income ratio of between 32% to 36% and is well within this range.

## Normalised EBIT

FY15 normalised EBIT was \$438m, increasing by \$50m (13%) from \$388m in FY14. EBIT increased across both Life (up \$52m or 13%) and Funds Management (up \$1m or 2%), and was partially offset by lower Corporate EBIT (down \$3m or 5%).

The increase in Life normalised EBIT reflects growth in average assets under management, which increased by 13% in FY15 with a stable Life COE margin. The Life COE margin has been stable at 4.5% for the last three financial years. Refer to page 16 for more detail.

The increase in Funds Management EBIT reflects growth in average FUM (up 24%), partially offset by a lower net income margin due to a change in FUM mix. The change in FUM mix includes the formation of Whitehelm Capital on 1 July 2014 and consolidation of Asset Backed Security (ABS) fixed income teams. Refer to page 21 for more detail.

Corporate EBIT decreased by \$3m due to lower net income and higher personnel expenses. Refer to page 24 for more detail.

## Normalised tax

Normalised tax was \$101m in FY15 with an effective tax rate of 23%. The effective tax rate increased from 14% in FY14 as a result of the conclusion of the TOFA transitional deduction on 30 June 2014. Excluding TOFA, the normalised effective tax rate in FY14 was 22%.

In February 2012 the Australian Taxation Office issued a private tax ruling in relation to the application of Taxation of Financial Arrangements (TOFA). The TOFA private tax ruling reduced normalised tax by approximately \$30m for each of the three financial years FY12 to FY14. FY14 normalised tax was reduced by \$30m for TOFA, with no corresponding TOFA tax deduction recognised in FY15.

Challenger's medium term normalised effective tax rate is expected to be between 23% to 25%, reflecting Challenger's current earnings mix.

## Investment experience

Challenger Life is required by Australian accounting standards to value assets and liabilities supporting the Life business at fair value. This gives rise to fluctuating valuation movements on assets and liabilities being recognised in the profit and loss. Challenger is generally a long-term holder of assets, due to them being held to match the term of life contract liabilities. As a result, Challenger takes a long-term view of the expected capital growth of the portfolio rather than focusing on short-term movements.

Investment experience represents the difference between actual investment gains/losses (both realised and unrealised) and expected gains/losses based on Challenger's long-term expected returns. Refer to page 34 for details on Challenger's assumed long-term expected returns by asset class. Investment experience also includes the impact of changes in economic variables and valuation assumptions on Life's liabilities (refer to page 35 for more detail).

Investment experience relates to the Life business and pre-tax investment experience is disclosed as part of Life's financial results (refer to page 14).

FY15 after tax investment experience was a loss of \$35m, comprising a loss of \$28m on Life's assets and a loss of \$7m from changes to economic variables and assumptions on Life's annuity liabilities.

The loss on Life's assets primarily relate to losses on the fixed income portfolio from expansion in domestic and offshore credit spreads, partially offset by strong property valuation gains net of property transaction costs.

### Statutory net profit after tax

Statutory net profit after tax includes post-tax investment experience. Statutory net profit after tax was \$299m in FY15, down from \$341m in FY14. The reduction in statutory net profit after tax reflects higher normalised net profit after tax (up \$5m) offset by lower investment experience (down \$47m).

### FY16 guidance

#### Life COE

Life COE guidance for FY16 is a range of \$585m to \$595m (FY15 actual \$544m). FY16 Life COE guidance reflects growth in Life's annuity book, and a lower normalised growth assumption for equities.

Commencing from 1 July 2015 (FY16), Life's assumed equities normalised growth assumption has been reduced from 6.0% per annum to 4.5% per annum to reflect lower expected returns. This includes both lower global economic growth expectations (i.e. lower equities risk premia) and the nature of Challenger's equities portfolio, which consists of both listed and unlisted equities.

The lower equities normalised growth assumption has the impact of reducing Life's FY16 COE guidance by approximately \$13m (based on Life's closing FY15 equity investments of \$0.9bn).

On a like-for-like basis, the mid point of the FY16 Life COE guidance range is 11% higher than FY15.

#### Retail annuity net book growth

Challenger has provided retail annuity net book growth guidance in recent years. With the revised ASX disclosure regime it is increasingly more challenging to provide guidance. This is further impacted with a number of new product and distribution initiatives commencing in early FY16, including the Colonial annuities on platform initiative and the launch of the CarePlus product. As a result, Challenger will not provide FY16 retail net book growth guidance, but will continue to provide the market with quarterly updates throughout FY16.

### Dividend policy

Challenger has historically targeted a combined dividend and buy back payout ratio of approximately 50% of normalised profit after tax over the medium term.

With the increase in dividend franking levels, in August 2014 the Challenger Limited Board increased the targeted dividend payout ratio to a range of 45% to 50% of normalised net profit after tax.

Challenger aims to frank its dividends to the maximum extent possible and expects future dividends to be fully franked. However, the actual dividend payout ratio and franking levels will depend on prevailing market conditions and capital allocation priorities.

## Management balance sheet

\$m	FY15	1H15	FY14	1H14	FY13	1H13
<b>Group balance sheet<sup>1</sup></b>						
<b>Assets</b>						
<b>Life investment assets</b>						
Fixed income and cash (net)	8,513.7	8,541.1	7,955.7	7,983.2	8,219.2	7,974.2
Property (net)	2,883.7	2,716.4	2,167.8	1,952.0	1,761.1	1,540.9
Equity and other investments	882.8	632.4	400.7	433.1	318.5	227.7
Infrastructure (net)	514.4	503.0	563.2	520.9	488.4	426.9
<b>Life investment assets</b>	<b>12,794.6</b>	<b>12,392.9</b>	<b>11,087.4</b>	<b>10,889.2</b>	<b>10,787.2</b>	<b>10,169.7</b>
Cash and cash equivalents	98.6	126.0	141.2	154.8	177.1	135.5
Receivables	175.7	217.4	181.9	281.8	446.3	381.6
Derivative assets	255.0	356.6	326.3	245.2	336.9	438.9
Other investment assets	—	—	—	3.5	5.4	7.5
Investment in associates	43.4	39.4	39.4	36.4	40.0	49.8
Other assets	27.3	42.6	27.9	46.3	35.2	42.1
Fixed assets	8.4	10.9	12.4	12.3	14.5	16.0
Goodwill and intangibles	549.4	547.2	545.8	522.1	521.1	519.6
Less Group/Life eliminations <sup>2</sup>	(136.5)	(154.9)	(182.2)	(202.3)	(223.1)	(254.9)
<b>Total assets</b>	<b>13,815.9</b>	<b>13,578.1</b>	<b>12,180.1</b>	<b>11,989.3</b>	<b>12,140.6</b>	<b>11,505.8</b>
<b>Liabilities</b>						
Payables	180.1	191.0	190.7	191.7	165.4	275.1
Tax liabilities	155.3	150.4	165.7	161.2	133.9	100.5
Derivative liabilities	370.6	344.5	222.1	327.2	393.9	123.9
Subordinated debt	567.0	560.7	525.9	509.5	510.1	472.3
Challenger Capital Notes	336.8	336.2	—	—	—	—
Other interest bearing liabilities	1.4	4.0	3.2	103.8	88.2	79.9
Provisions	23.8	20.5	22.5	26.1	27.0	30.2
Life retail annuity book	8,693.0	8,573.1	7,824.3	7,617.2	7,123.3	6,819.6
Guaranteed index return liabilities	944.7	954.8	1,072.4	1,000.3	1,751.4	1,777.0
<b>Total liabilities</b>	<b>11,272.7</b>	<b>11,135.2</b>	<b>10,026.8</b>	<b>9,937.0</b>	<b>10,193.2</b>	<b>9,678.5</b>
<b>Group net assets</b>	<b>2,543.2</b>	<b>2,442.9</b>	<b>2,153.3</b>	<b>2,052.3</b>	<b>1,947.4</b>	<b>1,827.3</b>
<b>Equity</b>						
Contributed equity	1,527.2	1,524.3	1,237.5	1,263.2	1,271.9	1,313.5
Reserves	23.7	13.8	69.8	52.1	49.8	33.0
Retained earnings	992.3	904.8	846.0	737.0	625.7	480.8
<b>Total equity</b>	<b>2,543.2</b>	<b>2,442.9</b>	<b>2,153.3</b>	<b>2,052.3</b>	<b>1,947.4</b>	<b>1,827.3</b>

<sup>1</sup> Excludes consolidation of Special Purpose Vehicles (SPV's) and non-controlling interests.

<sup>2</sup> Group/Life eliminations represent the fair value of SPV residual income notes (i.e. NIM) held by Challenger Life Company Ltd.



## Management balance sheet

\$m	FY15	1H15	FY14	1H14	FY13	1H13
<b>Life balance sheet</b>						
<b>Assets</b>						
<b>Life investment assets</b>						
Cash and equivalents	728.4	1,307.3	1,243.7	1,331.5	1,292.7	441.3
Asset backed securities	4,238.7	4,082.1	3,477.2	3,425.4	3,397.3	3,593.4
Corporate credit	3,444.7	3,024.3	3,146.1	3,075.3	3,366.8	3,692.1
Other	101.9	127.4	88.7	151.0	162.4	247.4
<b>Fixed income and cash (net)</b>	<b>8,513.7</b>	<b>8,541.1</b>	<b>7,955.7</b>	<b>7,983.2</b>	<b>8,219.2</b>	<b>7,974.2</b>
Australian – Office	1,359.0	1,138.2	805.5	657.6	656.8	643.9
Australian – Retail	818.0	721.6	480.3	437.4	260.0	131.4
Australian – Industrial	96.7	162.8	165.1	134.6	130.6	123.7
Japanese	225.1	204.3	203.4	233.9	241.4	235.3
REITS and other	384.9	489.5	513.5	488.5	472.3	406.6
<b>Property (net)</b>	<b>2,883.7</b>	<b>2,716.4</b>	<b>2,167.8</b>	<b>1,952.0</b>	<b>1,761.1</b>	<b>1,540.9</b>
Equity and other investments	882.8	632.4	400.7	433.1	318.5	227.7
Infrastructure (net)	514.4	503.0	563.2	520.9	488.4	426.9
<b>Life investment assets</b>	<b>12,794.6</b>	<b>12,392.9</b>	<b>11,087.4</b>	<b>10,889.2</b>	<b>10,787.2</b>	<b>10,169.7</b>
Other assets (including intangibles)	456.4	601.4	659.1	490.4	612.4	847.9
<b>Total assets</b>	<b>13,251.0</b>	<b>12,994.3</b>	<b>11,746.5</b>	<b>11,379.6</b>	<b>11,399.6</b>	<b>11,017.6</b>
<b>Liabilities</b>						
Life retail annuity book	8,693.0	8,573.1	7,824.3	7,617.2	7,123.3	6,819.6
Guaranteed index return liabilities	944.7	954.8	1,072.4	1,000.3	1,751.4	1,777.0
Subordinated debt	567.0	560.7	525.9	509.5	510.1	472.3
Challenger Capital Notes	345.0	345.0	–	–	–	–
Other liabilities	292.3	199.8	144.8	301.2	149.5	183.7
<b>Total liabilities</b>	<b>10,842.0</b>	<b>10,633.4</b>	<b>9,567.4</b>	<b>9,428.2</b>	<b>9,534.3</b>	<b>9,252.6</b>
<b>Net assets</b>	<b>2,409.0</b>	<b>2,360.9</b>	<b>2,179.1</b>	<b>1,951.4</b>	<b>1,865.3</b>	<b>1,765.0</b>

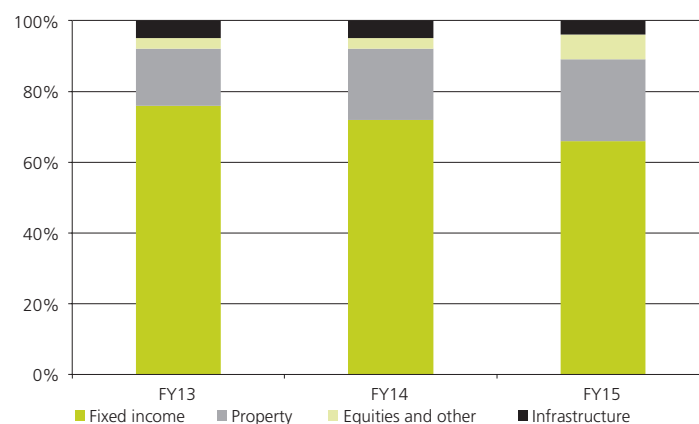
## Life investment portfolio overview

Life's asset allocation reflects both the relative value of different asset classes and the tenor of annuity sales as Life runs a cash flow matched portfolio.

Life's investment assets at 30 June 2015 comprised:

- Fixed income and cash 66%;
- Property 23%;
- Equities and other investments 7%; and
- Infrastructure 4%.

## Life investment portfolio overview



## Fixed income and cash

Fixed income and cash of \$8.5bn (net of debt) represents 66% of Life's total investment assets, down from 72% in FY14.

Challenger manages credit risk by maintaining a high quality investment portfolio and applying a rigorous investment process. The fixed income portfolio is diversified across different industries, rating bands, asset classes and geographies. The fixed income portfolio comprises over 1,100 different securities with 76% of the fixed income portfolio investment grade (i.e. BBB or higher).

A total of 71% of the fixed income portfolio is externally rated (Standard & Poor's, Fitch or Moody's) and 29% is based on internal ratings calibrated to the Standard & Poor's or Moody's ratings framework.

The fixed income and cash portfolio is Australian focused, with domestic cash, domestic asset backed securities and domestic corporate credit accounting for 67% of the portfolio. Life does not have any exposure to European sovereign debt.

Approximately 30% of Life's fixed income portfolio represents fixed income investments that have been originated by Challenger. Direct fixed income origination includes senior secured loans, asset backed securities, commercial real estate lending and specialised finance. Life's direct origination capability has been in place for over ten years and provides opportunities to capture relative value including illiquidity premiums as Life is a hold-to-maturity investor.

FY15 credit default losses on the fixed income portfolio were ~26 bps, which is well below the normalised growth assumption of a 35 bps loss each year. Over the past five years average credit default losses were ~11 bps per annum.

### Fixed income portfolio by credit rating

Security rating	Total \$m	Investment grade	Non-investment grade	Duration
Cash and equivalents	728	9%		n/a
AAA	1,422	17%		2 years
AA	804	9%		4 years
A	1,562	18%		3 years
BBB	1,975	23%		4 years
BB	1,121		13%	4 years
B	575		7%	3 years
Unrated	327		4%	5 years
<b>Total</b>	<b>8,514</b>	<b>76%</b>	<b>24%</b>	<b>3 years</b>

## Property

Property of \$2.9bn (net of debt) represents 23% of Life's investment assets, up from 20% in FY14. The increase in property reflects a lengthening in tenor of Life's annuity sales, including both longer tenor term and lifetime sales.

Life's property portfolio increased by \$0.7bn (net of debt) during FY15 as a result of domestic commercial office and retail shopping centre acquisitions, partially offset by property disposals as part of Life's ongoing property portfolio remix.

Life is currently undertaking a property portfolio remix to ensure the portfolio delivers the required cash flows to match Life's annuity liabilities and remains a high quality and diversified portfolio. As part of the property portfolio remix, a number of properties have been sold at or above book value. The property remix is expected to be ongoing into FY16.

Full details of property acquisitions and disposals in FY15 are listed in the following tables.

FY15 property acquisitions	\$m	Detail
Exchanged and settled in FY15		
53 Albert Street, Brisbane	222	Retail 2%; Office 98%
Barracks Shopping Centre, Brisbane	153	Retail 47%; Office 53%
Golden Grove Shopping Centre, Adelaide	139	Retail 100%
35 Clarence Street, Sydney	145	Retail 8%; Office 92%
565 Bourke Street, Melbourne	86	Retail 4%; Office 96%
<b>Total</b>	<b>745</b>	Retail 31%; Office 69%
Exchanged in 2H15 to settle in 1H16 (not included in FY15 property AUM) <sup>1</sup>		
215 Adelaide Street, Brisbane	238	Retail 16%; Office 84%
North Rocks Shopping Centre, Sydney	135	Retail 100%
Channel Court, Kingston	80	Retail 100%
<b>Total</b>	<b>453</b>	Retail 57%; Office 43%

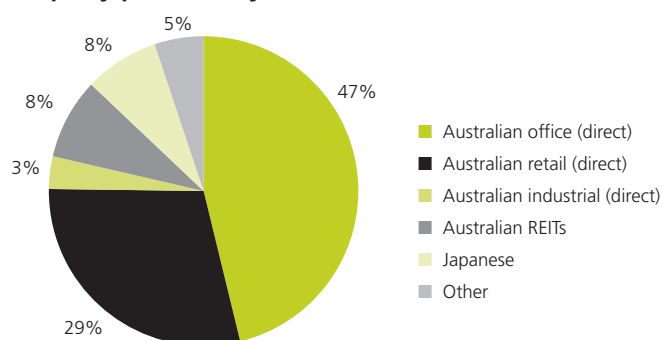
FY15 property disposals	\$m	Detail
Exchanged and settled in FY15		
CSIRO, Sydney	170	Sold 7% premium to book
Taylor's Institute, Sydney	40	Sold at book value
<b>Total</b>	<b>210</b>	
Exchanged in 2H15 to settle in 1H16 (included in FY15 property AUM)		
The Forum Cisco, Sydney	112	Sold 1% premium to book
Innaloo, Perth	48	Option at premium to book
<b>Total</b>	<b>160</b>	

1. Properties exchanged in 2H15 with deposits paid and balance payable on settlement.

Property acquisitions incur stamp duty and acquisition costs. Under Australian accounting standards, property acquisition and transaction costs are required to initially be capitalised. When the property is subsequently revalued, there is generally no value ascribed to the acquisition costs which may result in a reduction in the property valuation and a corresponding negative investment experience impact. In 2H15, all properties acquired in 1H15 were subject to either an independent valuation or a directors' valuation, with \$32m of transaction costs including stamp duty offset against property valuation gains.

2H15 property acquisition costs, including stamp duty of \$22m, will be offset against property revaluations in 1H16.

### Property portfolio by sector



Life's property portfolio principally comprises directly held properties and investments in Australian REITs. The Australian property portfolio is diversified across office and retail properties, with a small (3%) exposure to industrial properties.

Australian properties have a weighted average lease expiry of 4.8 years and an occupancy rate of 98%. A total of 81% of the Australian direct property portfolio has either fixed or CPI-linked rental increases, giving rise to cash flows that increase over time.

Rental income is diversified across sectors and tenants, with 55% (by forecasted 2016 gross rental income) of Australian tenants classified as investment grade (i.e. rated BBB or higher).

The Australian Government is a major tenant, leasing a range of commercial office buildings and is expected to account for 34% of 2016 gross rental income.

Property includes a net \$225m exposure to Japanese property (8% of the property portfolio), consisting of suburban shopping centres, focused on non-discretionary retailing. The weighted average lease expiry of the Japanese portfolio is 9.1 years.

Challenger Life has a policy that all properties are independently valued each year with approximately 50% valued in June and 50% valued in December. Internal valuations are also undertaken for properties not independently valued each June and December. An independent valuation is subsequently undertaken if the internal valuation shows a significant variance to the most recent independent valuation.

In FY15 independent valuations were undertaken for all properties within the portfolio. The weighted average capitalisation rate of the Australian direct property portfolio was 7.4% at 30 June 2015.

### Equity and other investments

Equity and other investments of \$0.9bn represent 7% of Life's total investment assets and include domestic and international listed and unlisted equity investments. Equity investments provide diversification across the investment portfolio.

### Infrastructure

Infrastructure of \$0.5bn (net of debt) represents 4% of Life's investment assets.

Challenger Life seeks infrastructure assets that generate reliable and consistent cash flows, which are preferably inflation linked, giving rise to sustainable income growth over time. Infrastructure investments comprise directly held infrastructure assets and indirectly held listed and unlisted investments. Approximately 75% of the infrastructure portfolio is held in unlisted investments.

The infrastructure portfolio is diversified across a number of geographic regions and sectors. Approximately two thirds of the portfolio is invested in logistics, utility and patronage assets, predominately in Australia, UK and Europe.

## Capital management

## Challenger Life Company (CLC) regulatory capital

\$m	FY15	1H15	FY14	1H14	FY13	1H13	
<b>CLC's excess capital under LAGIC</b>							
Common Equity Tier 1 (CET1) regulatory capital	1,907.6	1,886.7	1,783.1	1,719.0	1,563.5	1,465.8	
Additional Tier 1	345.0	345.0	–	–	–	–	
Tier 2 regulatory capital – subordinated debt <sup>1</sup>	474.0	504.7	476.8	486.8	488.8	477.3	
<b>CLC total regulatory capital base</b>	<b>2,726.6</b>	<b>2,736.4</b>	<b>2,259.9</b>	<b>2,205.8</b>	<b>2,052.3</b>	<b>1,943.1</b>	
<b>CLC prescribed capital amount (PCA)</b>							
Asset risk charge	1,773.6	1,718.0	1,530.5	1,517.0	1,452.4	1,324.1	
Insurance risk charge	120.5	143.5	83.9	68.5	31.6	26.8	
Operational risk charge	22.6	23.9	22.8	20.6	18.5	17.5	
Aggregation benefit	(91.9)	(108.5)	(64.7)	(53.2)	(24.8)	(21.2)	
<b>CLC Prescribed capital amount – excluding transition relief</b>							
Transition relief	1,824.8 (107.6)	1,776.9 (215.2)	1,572.5 (215.2)	1,552.9 (322.8)	1,477.7 (322.8)	1,347.2 (322.8)	
<b>CLC prescribed capital amount</b>	<b>1,717.2</b>	<b>1,561.7</b>	<b>1,357.3</b>	<b>1,230.1</b>	<b>1,154.9</b>	<b>1,024.4</b>	
<b>CLC excess over prescribed capital amount</b>	<b>1,009.4</b>	<b>1,174.7</b>	<b>902.6</b>	<b>975.7</b>	<b>897.4</b>	<b>918.7</b>	
<b>PCA ratio (times)</b>	<b>1.59</b>	<b>1.75</b>	<b>1.66</b>	<b>1.79</b>	<b>1.78</b>	<b>1.90</b>	
<b>Tier 1 ratio (times)</b>	<b>1.31</b>	<b>1.43</b>	<b>1.31</b>	<b>1.40</b>	<b>1.35</b>	<b>1.43</b>	
<b>CET1 ratio (times)</b>	<b>1.11</b>	<b>1.21</b>	<b>1.31</b>	<b>1.40</b>	<b>1.35</b>	<b>1.43</b>	
<b>Tier 2 regulatory capital – subordinated debt<sup>1</sup></b>							
<b>First call date after 1 Jan 2013</b>	<b>Maturity date</b>	<b>FY15</b>	<b>1H15</b>	<b>FY14</b>	<b>1H14</b>	<b>FY13</b>	<b>1H13</b>
7 Jun 2013	7 Dec 2016	63.5	88.3	77.6	107.2	103.2	109.4
7 Dec 2016	7 Dec 2026	33.9	31.0	27.5	28.3	28.0	24.2
7 Nov 2017	7 Nov 2037	376.6	385.4	371.7	351.3	357.6	343.7
		<b>474.0</b>	<b>504.7</b>	<b>476.8</b>	<b>486.8</b>	<b>488.8</b>	<b>477.3</b>

## Group cash, CLC debt facilities and Group net assets

\$m	FY15	1H15	FY14	1H14	FY13	1H13
<b>Group cash</b>	<b>98.6</b>	<b>126.0</b>	<b>141.2</b>	<b>154.8</b>	<b>177.1</b>	<b>135.5</b>
<b>CLC debt facilities</b>						
Controlled property debt	566.1	679.2	721.4	823.1	845.6	857.9
Subordinated debt	567.0	560.7	525.9	509.5	510.1	472.3
Repurchase agreements	1,267.3	1,163.3	978.3	729.2	448.9	235.7
Infrastructure debt	206.0	205.0	206.1	206.1	206.1	206.1
Other finance	1.4	3.3	3.2	103.8	88.2	79.9
<b>Total CLC debt facilities</b>	<b>2,607.8</b>	<b>2,611.5</b>	<b>2,434.9</b>	<b>2,371.7</b>	<b>2,098.9</b>	<b>1,851.9</b>
<b>Change in Group net assets</b>						
<b>\$m</b>	<b>2H15</b>	<b>1H15</b>	<b>2H14</b>	<b>1H14</b>	<b>2H13</b>	<b>1H13</b>
<b>Opening net assets</b>	<b>2,442.9</b>	<b>2,153.3</b>	<b>2,052.3</b>	<b>1,947.4</b>	<b>1,827.3</b>	<b>1,692.2</b>
Statutory net profit after tax	168.9	130.1	174.3	166.3	194.8	222.0
Dividends paid	(81.4)	(71.3)	(65.3)	(55.0)	(49.9)	(55.7)
Share buy-back	–	–	–	–	(29.6)	(20.4)
New share issue	–	287.2	–	–	–	–
Reserve movements	9.9	(56.0)	17.7	2.3	16.8	(31.7)
CPP Trust movements	2.9	(0.4)	(25.7)	(8.7)	(12.0)	20.9
<b>Closing net assets</b>	<b>2,543.2</b>	<b>2,442.9</b>	<b>2,153.3</b>	<b>2,052.3</b>	<b>1,947.4</b>	<b>1,827.3</b>

<sup>1</sup> FY15 subordinated debt (\$474m) differs to the management balance sheet (\$567m) due to inadmissible sub-debt (\$95m) less accrued interest.

## Capital management

### Challenger Life Company Limited (CLC) regulatory capital base

CLC holds capital in order to ensure that under a range of adverse scenarios it can continue to meet its regulatory and contractual obligations to customers. CLC is regulated by the Australian Prudential Regulation Authority (APRA) and is required to hold a minimum level of regulatory capital.

CLC's regulatory capital base and prescribed capital amount have been calculated based on regulatory capital standards. APRA issued new capital standards in October 2012 (LAGIC standards) which became effective from 1 January 2013. CLC's regulatory capital disclosures have been prepared based on LAGIC capital standards.

### CLC excess regulatory capital

CLC's excess capital above APRA's prescribed capital amount at 30 June 2015 (FY15) was \$1.0bn, up \$0.1bn for the year. The increase in excess regulatory capital was due to:

- an increase in the regulatory capital base (up \$0.5bn) as a result of retained earnings and capital initiatives completed in 1H15;
- an increase in the prescribed capital amount (up \$0.3bn) as a result of growth in Life's investment assets and an increase in capital intensity.

Life's investment assets increased by \$1.7bn for the year, and the 30 June 2015 prescribed capital amount includes properties purchased at 30 June 2015, but are yet to settle.

The capital intensity increased following a change in investment asset mix, with property accounting from 23% of assets at 30 June 2015, up from 20% in 2014. Equities and infrastructure also increased. Property, equities and infrastructure investment assets require a higher prescribed capital amount than fixed income investments.

- LAGIC transition resulting in a \$0.1bn increase in the prescribe capital amount on 1 January 2015. Two-thirds of the LAGIC transition balance has now amortised, with the remaining \$108m amortising on 1 January 2016.

During FY15 both CLC's regulatory capital base and the prescribed capital amount were impacted by a change in the tax indemnity agreement between CLC and the Challenger group, however there was no impact on CLC's excess over the prescribed capital amount.

The Challenger group has historically indemnified CLC for all tax related liabilities, which resulted in CLC carrying a tax indemnity asset on balance sheet. This asset was included in the Common Equity Tier 1 (CET1) regulatory capital base of CLC under the LAGIC capital standards. In 2014 APRA changed the regulatory treatment of this asset resulting in a reduction of both CET1 capital and the Prescribed Capital

Amount (PCA) with no change to CLC's excess over the PCA. This change was amortised over an agreed transition period with APRA and is now complete.

CLC's PCA ratios at 30 June 2015 were as follows (including LAGIC transition):

- CLC excess capital to PCA ratio of 1.6 times (APRA minimum 1.0 times);
- Common Equity Tier 1 (CET1) to PCA ratio of 1.1 times (APRA minimum 0.6 times);
- Additional Tier 1 Equity to PCA ratio of 0.2 times; and
- Tier 2 Equity to PCA ratio of 0.3 times.

Excluding the LAGIC transition balance, CLC's excess capital to PCA ratio was 1.5 times (APRA minimum 1.0 times) at 30 June 2015 reflecting the mid-point CLC's target range of 1.4 to 1.6 times.

CLC maintains a target level of capital representing APRA's prescribed capital amount plus a target surplus. The target surplus is a level of excess capital that CLC seeks to carry over and above APRA's minimum requirement.

CLC's target surplus is set to ensure that it provides a buffer against adverse market conditions and to ensure sufficient capital is maintained to cover insurance risk. CLC uses internal capital models to determine its target surplus, which are risk-based and are responsive to changes in CLC's asset allocation and market conditions.

While CLC does not target a specific PCA ratio, CLC's internal capital models generate a PCA ratio based upon asset allocation and economic circumstances which is currently in the range of 1.4 to 1.6 times. This range may change over time.

APRA requires CET1 capital to be at least 60% of the PCA and total Tier 1 capital to be at least 80% of the PCA.

Following the introduction of LAGIC standards, CLC's regulatory capital requirements increased by \$323m. APRA provided a three-year transition period to meet the new requirements, which will conclude on 1 January 2016.

Since the introduction of the LAGIC capital framework, CLC has increased AUM by \$2.6bn (26%). During this same period, CLC has increased its regulatory capital base by \$0.8bn (up 40%). This has resulted in CLC improving its PCA ratio, excluding the APRA transition amount, from the lower end of its target range to the mid-point of the target range.

### 1H15 capital initiatives

Challenger Life is growing strongly and expects to materially increase the size of its retail annuity business. Challenger Life's market opportunity and growth profile are set out on page 19. In order to support Challenger's growth profile, the following the capital initiatives were completed in 1H15:

- \$250m institutional equity placement undertaken on 20 August 2014 with 33.2m shares issued. The placement price of \$7.53 per share represented a 1.1% discount to the 10 day volume weighted average price (adjusted for the FY14 final dividend);
- \$40m Share Purchase Plan (SPP) undertaken to provide eligible retail Australian and New Zealand investors the opportunity to participate. The SPP was completed in October 2014 with an issue price of \$7.10 per share and 5.7m new Challenger shares issued; and
- \$345m raised via Challenger Capital Notes, which are subordinated unsecured convertible notes issued by Challenger Limited. Challenger Capital Notes are quoted and tradable on the ASX (code 'CGFPA') and pay franked distributions on a quarterly basis at a margin of 3.40% p.a. over the Australian 90 day Bank Bill Rate. Distributions can be paid to note holders as a combination of cash and franking credits.

The proceeds from Challenger Capital Notes (\$345m) have been injected to CLC as Additional Tier 1 Equity. The majority

of the proceeds (\$150m) from the institutional equity placement and SPP have been injected into CLC as Common Equity Tier 1 capital, with the remainder (\$140m) retained at Group.

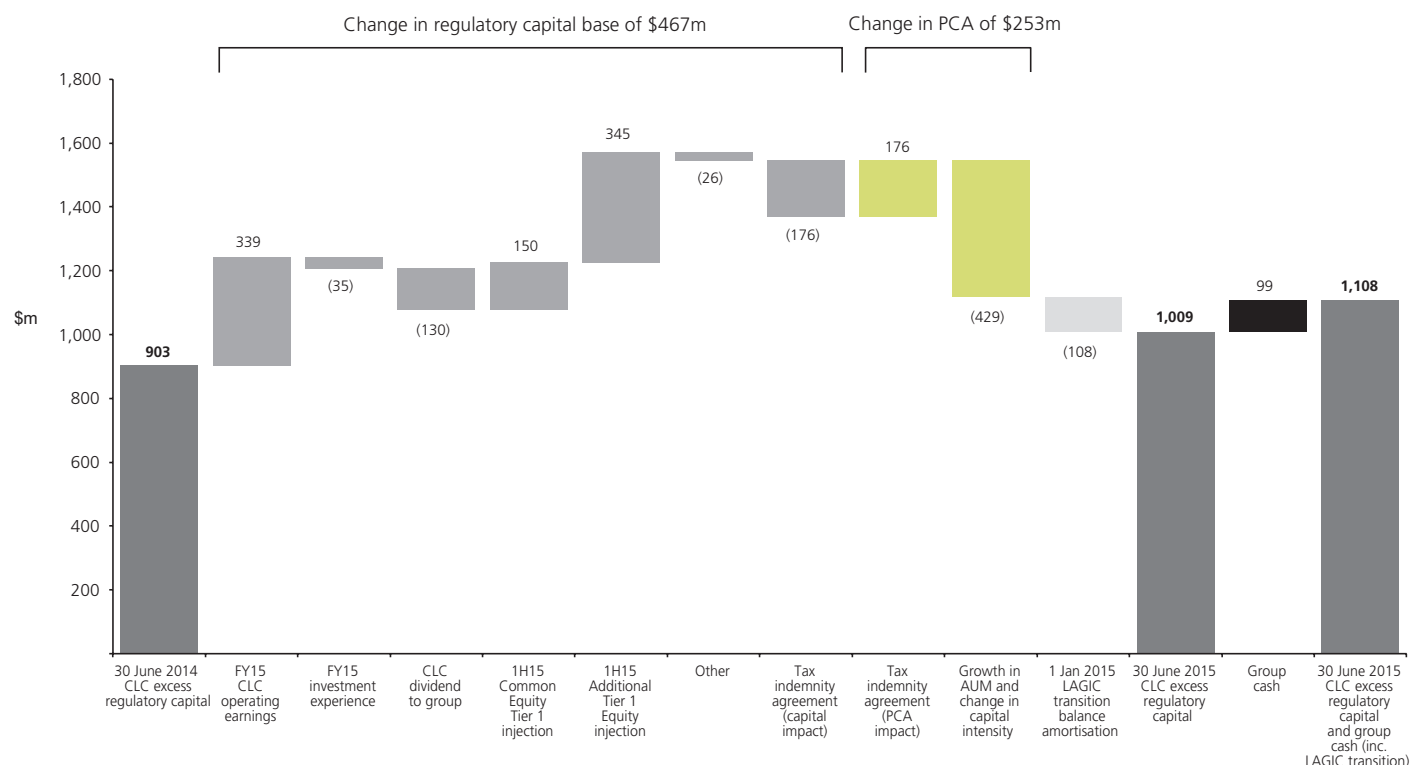
## Subordinated debt

CLC's total regulatory capital base includes \$474m of admissible subordinated debt. Subordinated debt issued prior to 1 January 2013 (implementation date of new LAGIC capital standards) will continue to be fully eligible as Tier 2 regulatory capital under LAGIC until each tranche's first call date<sup>1</sup> after 1 January 2013, and will then amortise over four years.

CLC's subordinated debt includes \$159m which had a call date on 7 June 2013. As a result, under APRA's transition arrangements, only \$63m (i.e. 40% of the total amount) is included as Tier 2 regulatory capital on 30 June 2015.

The largest tranche of CLC's existing subordinated debt is a \$377m tranche with a call date in November 2017. As such, this tranche will continue to be fully eligible as Tier 2 regulatory capital until its call date in November 2017 and will continue to be partially eligible until November 2021.

## Change in CLC Excess Regulatory Capital and Group Cash



<sup>1</sup> For tranches already past their call date, under LAGIC the first coupon date is considered the first call date.



## Group cash

In addition to CLC's excess regulatory capital, Challenger maintains cash at a Group level, which can be utilised to meet regulatory requirements.

Group cash at 30 June 2015 was \$99m, down \$42m for the year. The movement in Group cash predominately relates to operating cash flows, 1H15 capital initiatives (net of capital injected into CLC) and dividends paid to shareholders.

Challenger has an undrawn Group banking facility of \$350m, which is maintained to provide additional financial flexibility. The banking facility was undrawn throughout FY15.

## APRA's Level 3 (conglomerate) proposals

APRA is currently developing a supervisory framework for Level 3 (conglomerate) groups, which was due to be effective from 1 January 2015. Level 3 are groups of companies that perform material activities across more than one APRA-regulated industry and in one or more non-APRA-regulated industries. Draft Level 3 capital standards have been issued by APRA. However, APRA is yet to confirm the implementation date. Based on the draft Level 3 standards issued by APRA, Challenger does not expect any material impact on its regulatory capital base.

In August 2014, APRA deferred a decision on its Level 3 final capital standards and implementation until the Government responds to the recommendations of the Financial System Inquiry.

## CLC debt facilities

CLC debt facilities includes debt which is non-recourse to the Challenger Group and is secured against assets held in investment vehicles by CLC, including direct properties and infrastructure investments. CLC debt facilities increased by \$0.2bn during the year, with higher repurchase agreements partially offset by lower controlled property debt.

## Change in Group net assets

FY15 Group net assets were \$2,543m, up from \$2,153m a year ago. The increase in Group net assets is due to the capital initiatives completed in 1H15 (refer to page 11 for more detail), the full year statutory net profit after tax (including investment experience), partially offset by dividends to shareholders and reserve movements.

## Dividends and share buy back

### Final 2015 dividend

A final 2015 dividend of 15.5 cents per share (100% franked) has been declared, up 15% on the final 2014 dividend. The payout ratio for the final 2015 dividend was 48% and is within Challenger's dividend payout ratio guidance of between 45% and 50% of normalised net profit after tax.

The final 2015 dividend dates are as follows:

- Ex-date: 31 August 2015;
- Record date: 2 September 2015; and
- Payment date: 30 September 2015.

### Total FY15 dividend

Total dividends declared for FY15 were 30.0 cps (86% franked), up 15% on FY14. The increase in total FY15 dividends reflects a higher dividend payout ratio, which increased from 41% in FY14 to 49% in FY15.

As part of the capital management plan review in August 2014, which included consideration of the recommencement of dividend franking, the Challenger Limited Board increased the dividend payout ratio guidance to a range of 45% to 50% (up from 35% to 45%) of normalised profit after tax. Challenger's FY15 dividend of 30.0 cps (payout ratio of 49%) was at the upper end of the dividend payout guidance range.

### Dividend franking

Challenger seeks to frank its dividend to the maximum extent possible and expects future dividends to be fully franked. However, the actual dividend payout ratio and franking levels will depend on prevailing market conditions and capital allocation priorities.

Challenger's franking account balance at 30 June 2015 was \$57m, up from \$24m at 30 June 2014.

### Dividend reinvestment plan

With the return to full dividend franking, the Challenger Limited Board has established a Dividend Reinvestment Plan (DRP). The DRP provides an effective way for shareholders to reinvest their dividends and increase their holding without incurring any transaction costs.

The DRP will commence for the final 2015 dividend, which will be paid on 30 September 2015. For the final 2015 dividend, the Board has determined that new shares will be issued to fulfil DRP requirements, however the shares will not be issued at a discount to the prevailing Challenger share price. Under the DRP terms, shares will be issued to DRP participants as determined by a ten day Challenger share price VWAP.

## Credit ratings

In December 2014, Standard & Poor's (S&P) affirmed both CLC's and Challenger Limited's ratings.

Ratings were confirmed as:

- CLC: 'A' with a stable outlook; and
- Challenger Limited: 'BBB+' with a stable outlook.

The S&P ratings reflect the financial strength of Challenger Limited and CLC. In particular they demonstrate Challenger's strong business profile, earnings and capital position.

## Life financial results

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
Investment yield – policyholders' funds	765.8	740.2	761.3	390.2	375.6	365.7	374.5	375.2	386.1
Interest expense	(413.8)	(397.0)	(398.9)	(209.1)	(204.7)	(197.4)	(199.6)	(195.9)	(203.0)
Distribution expense	(25.5)	(30.2)	(25.0)	(11.5)	(14.0)	(15.0)	(15.2)	(12.2)	(12.8)
Other income <sup>1</sup>	19.8	10.7	–	10.8	9.0	9.9	0.8	–	–
<b>Product cash margin</b>	<b>346.3</b>	<b>323.7</b>	<b>337.4</b>	<b>180.4</b>	<b>165.9</b>	<b>163.2</b>	<b>160.5</b>	<b>167.1</b>	<b>170.3</b>
Investment yield – shareholders' funds	117.1	102.0	78.8	59.7	57.4	51.2	50.8	42.6	36.2
<b>Cash earnings</b>	<b>463.4</b>	<b>425.7</b>	<b>416.2</b>	<b>240.1</b>	<b>223.3</b>	<b>214.4</b>	<b>211.3</b>	<b>209.7</b>	<b>206.5</b>
Normalised capital growth	80.4	55.6	36.0	45.9	34.5	29.7	25.9	17.4	18.6
<b>Normalised Cash Operating Earnings (COE)</b>	<b>543.8</b>	<b>481.3</b>	<b>452.2</b>	<b>286.0</b>	<b>257.8</b>	<b>244.1</b>	<b>237.2</b>	<b>227.1</b>	<b>225.1</b>
Personnel expenses	(51.0)	(45.6)	(39.1)	(25.6)	(25.4)	(24.3)	(21.3)	(19.6)	(19.5)
Other expenses	(36.1)	(31.5)	(31.2)	(19.5)	(16.6)	(16.2)	(15.3)	(15.7)	(15.5)
<b>Total expenses</b>	<b>(87.1)</b>	<b>(77.1)</b>	<b>(70.3)</b>	<b>(45.1)</b>	<b>(42.0)</b>	<b>(40.5)</b>	<b>(36.6)</b>	<b>(35.3)</b>	<b>(35.0)</b>
<b>Normalised EBIT</b>	<b>456.7</b>	<b>404.2</b>	<b>381.9</b>	<b>240.9</b>	<b>215.8</b>	<b>203.6</b>	<b>200.6</b>	<b>191.8</b>	<b>190.1</b>
Investment experience	(50.0)	18.2	138.1	(14.6)	(35.4)	14.1	4.1	37.8	100.3
<b>Net profit after investment experience before tax</b>	<b>406.7</b>	<b>422.4</b>	<b>520.0</b>	<b>226.3</b>	<b>180.4</b>	<b>217.7</b>	<b>204.7</b>	<b>229.6</b>	<b>290.4</b>
<b>Reconciliation of investment experience to capital growth</b>									
Investment experience	(50.0)	18.2	138.1	(14.6)	(35.4)	14.1	4.1	37.8	100.3
Normalised capital growth	80.4	55.6	36.0	45.9	34.5	29.7	25.9	17.4	18.6
<b>Capital growth</b>	<b>30.4</b>	<b>73.8</b>	<b>174.1</b>	<b>31.3</b>	<b>(0.9)</b>	<b>43.8</b>	<b>30.0</b>	<b>55.2</b>	<b>118.9</b>
<b>Performance analysis</b>									
Cost to income ratio <sup>2</sup>	16.0%	16.0%	15.5%	15.8%	16.3%	16.6%	15.4%	15.5%	15.5%
Net assets – average <sup>3</sup>	2,294	2,022	1,763	2,385	2,270	2,065	1,908	1,815	1,707
Normalised RoE (pre-tax)	19.9%	20.0%	21.7%	20.4%	18.9%	19.9%	20.9%	21.4%	22.1%

1 Other income includes Accurium revenue and Life Risk revenue (premiums net of claims).

2 Cost to income calculated as total expenses divided by Normalised Cash Operating Earnings.

3 Net assets – average calculated based on period opening and closing balances.



## Life financial results (continued)

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
<b>Sales</b>									
Fixed Term sales	2,273.2	2,185.7	1,922.3	1,017.6	1,255.6	998.9	1,186.8	967.6	954.7
Lifetime sales	479.9	613.1	256.9	160.7	319.2	342.9	270.2	156.3	100.6
<b>Life retail sales</b>	<b>2,753.1</b>	<b>2,798.8</b>	<b>2,179.2</b>	<b>1,178.3</b>	<b>1,574.8</b>	<b>1,341.8</b>	<b>1,457.0</b>	<b>1,123.9</b>	<b>1,055.3</b>
Maturities and repayments <sup>1</sup>	(2,014.9)	(1,911.7)	(1,581.1)	(1,000.9)	(1,014.0)	(994.6)	(917.1)	(738.6)	(842.5)
<b>Life net retail flows<sup>1</sup></b>	<b>738.2</b>	<b>887.1</b>	<b>598.1</b>	<b>177.4</b>	<b>560.8</b>	<b>347.2</b>	<b>539.9</b>	<b>385.3</b>	<b>212.8</b>
Life retail annuity book	8,692.6	7,824.3	7,123.3	8,692.6	8,573.1	7,824.3	7,617.2	7,123.3	6,819.6
<b>Retail annuity net book growth<sup>1</sup></b>	<b>9.4%</b>	<b>12.5%</b>	<b>9.1%</b>	<b>2.2%</b>	<b>7.2%</b>	<b>4.9%</b>	<b>7.6%</b>	<b>5.9%</b>	<b>3.2%</b>
Institutional sales	944.0	581.6	951.8	395.1	548.9	291.5	290.1	30.6	921.2
Maturities and repayments	(1,031.3)	(1,292.6)	(993.1)	(360.0)	(671.3)	(250.5)	(1,042.1)	(39.4)	(953.7)
<b>Life net institutional flows</b>	<b>(87.3)</b>	<b>(711.0)</b>	<b>(41.3)</b>	<b>35.1</b>	<b>(122.4)</b>	<b>41.0</b>	<b>(752.0)</b>	<b>(8.8)</b>	<b>(32.5)</b>
<b>Assets</b>									
<b>Closing investment assets</b>	<b>12,795</b>	<b>11,087</b>	<b>10,787</b>	<b>12,795</b>	<b>12,393</b>	<b>11,087</b>	<b>10,889</b>	<b>10,787</b>	<b>10,170</b>
Fixed income and cash <sup>2</sup>	8,394	7,935	7,890	8,575	8,234	7,911	7,964	8,102	7,690
Property	2,640	1,953	1,563	2,906	2,385	2,036	1,870	1,606	1,517
Equity and other investments	626	394	219	742	511	423	371	246	194
Infrastructure	516	518	489	518	512	533	504	438	531
<b>Average investment assets<sup>3</sup></b>	<b>12,176</b>	<b>10,800</b>	<b>10,161</b>	<b>12,741</b>	<b>11,642</b>	<b>10,903</b>	<b>10,709</b>	<b>10,392</b>	<b>9,932</b>
<b>Liabilities</b>									
<b>Closing liabilities – annuities, GIR, capital notes and sub debt</b>	<b>10,550</b>	<b>9,425</b>	<b>9,385</b>	<b>10,550</b>	<b>10,436</b>	<b>9,425</b>	<b>9,127</b>	<b>9,385</b>	<b>9,069</b>
Average liabilities – annuities and GIR	9,397	8,675	8,563	9,706	9,107	8,617	8,623	8,667	8,463
Average liabilities – capital notes	239	–	–	345	148	–	–	–	–
Average liabilities – sub debt	563	518	478	582	543	525	509	491	465
<b>Average liabilities<sup>3</sup></b>	<b>10,199</b>	<b>9,193</b>	<b>9,041</b>	<b>10,633</b>	<b>9,798</b>	<b>9,142</b>	<b>9,132</b>	<b>9,158</b>	<b>8,928</b>
<b>Margins<sup>4</sup></b>									
Investment yield – policyholders' funds	6.3%	6.9%	7.5%	6.2%	6.4%	6.8%	7.0%	7.3%	7.7%
Interest expenses	(3.4%)	(3.7%)	(3.9%)	(3.3%)	(3.5%)	(3.7%)	(3.7%)	(3.8%)	(4.1%)
Distribution expense	(0.2%)	(0.3%)	(0.2%)	(0.2%)	(0.3%)	(0.3%)	(0.3%)	(0.2%)	(0.2%)
Other income	0.2%	0.1%	–	0.2%	0.2%	0.2%	–	–	–
<b>Product cash margin</b>	<b>2.9%</b>	<b>3.0%</b>	<b>3.3%</b>	<b>2.9%</b>	<b>2.8%</b>	<b>3.0%</b>	<b>3.0%</b>	<b>3.2%</b>	<b>3.4%</b>
Investment yield – shareholders' funds	0.9%	1.0%	0.8%	0.9%	1.0%	1.0%	0.9%	0.8%	0.7%
<b>Cash earnings</b>	<b>3.8%</b>	<b>4.0%</b>	<b>4.1%</b>	<b>3.8%</b>	<b>3.8%</b>	<b>4.0%</b>	<b>3.9%</b>	<b>4.1%</b>	<b>4.1%</b>
Normalised capital growth	0.7%	0.5%	0.4%	0.7%	0.6%	0.5%	0.5%	0.3%	0.4%
<b>Normalised Cash Operating Earnings (COE)</b>	<b>4.5%</b>	<b>4.5%</b>	<b>4.5%</b>	<b>4.5%</b>	<b>4.4%</b>	<b>4.5%</b>	<b>4.4%</b>	<b>4.4%</b>	<b>4.5%</b>

1 2H14 and FY14 maturities and repayments, Life net retail flows and retail annuity net book growth excludes maturity of the High Yield Fund annuity (\$284m).

2 Includes NIM (FY15: \$156m, FY14: \$202m, FY13: \$258m).

3 Average investment assets and average liabilities are calculated on a monthly basis.

4 Ratio of Normalised Cash Operating Earnings components divided by average investment assets.

## Life financial results

CLC is Australia's leading provider of annuities and guaranteed retirement income products. Products appeal to investors seeking the security and certainty of guaranteed cash flows with protection against market, inflation and longevity risks. Products are distributed via financial advisers, both independent and part of the major hubs. Being an independent product manufacturer, CLC's products are included on all major hubs.

CLC has won the Association of Financial Advisers/Plan for Life 'Annuity Provider of the Year' for the past seven years and in 2014 also won the 'Long Term Income Stream' and 'Annuity & Income Stream Innovation' awards.

The Life business includes Accurium (previously Bendzulla Actuarial), Australia's leading provider of Self Managed Superannuation Fund (SMSF) actuarial certificates. Challenger acquired Accurium in February 2014 (refer to page 18 for additional detail).

CLC is diversifying its capital and earnings base by participating in wholesale reinsurance longevity and mortality transactions (Life Risk). Life is experienced in managing, pricing and reinsuring longevity risk and this is a natural business extension. Refer to page 18 for additional details on Life Risk transactions.

CLC is an APRA regulated entity and its financial strength is rated by Standard & Poor's with an 'A' rating and stable outlook. CLC is strongly capitalised with significant excess capital above APRA's minimum requirements. CLC's regulatory capital base and excess capital above prescribed capital amount are disclosed on page 10.

### Normalised EBIT and RoE

FY15 normalised EBIT increased by \$53m (13%) to \$457m due to an increase in normalised cash operating earnings (up \$63m), partly offset by higher expenses (up \$10m).

FY15 Life RoE (pre-tax) was 19.9% and was down 0.1% for the year. Life RoE decreased as a result of the capital initiatives undertaken between August and October 2014. A total of \$150m of equity was injected into CLC (refer to page 11 for more details) in 1H15. This new capital has progressively been deployed, which is increasing Life's RoE. Life's 2H15 RoE was 20.4%, and was 150 basis points higher than 1H15, reflecting deployment of the 1H15 capital initiatives.

Challenger is committed to its 18% (pre-tax) RoE target and expects to continue to meet this target over the medium term.

### Normalised Cash Operating Earnings (COE) and COE margin

FY15 normalised COE increased by 13% to \$544m. The increase in normalised COE is a result of higher average

AUM (up 13%), and a stable Life COE margin of 4.5%. Life's COE margin has been stable at 4.5% for the past three years.

FY15 normalised COE includes other income of \$20m, which increased from \$11m in FY14. Other income includes Accurium revenue of \$10m (FY14 \$4m – reflecting only four months of revenue following the acquisition in February 2014) and Life Risk (wholesale reinsurance longevity and mortality transactions) of \$10m (FY14 \$7m). Life Risk net income represents premiums net of expected claims.

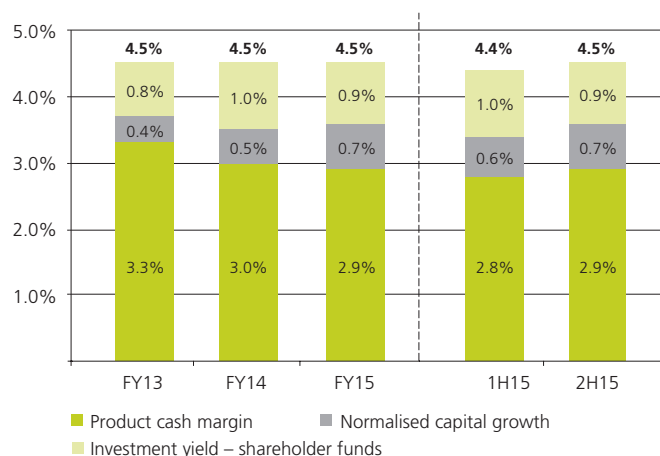
The FY15 COE margin was 4.5%, and is unchanged from FY14 and includes the following:

- Product cash margin of 2.9% was down 0.1% from FY14. The product cash margin reduced as a result of lower asset returns, partially offset by lower annuity funding rates. Product cash margin includes Accurium and Life Risk of 0.2% (FY14 0.1%).
- Return on shareholder funds of 0.9% was down 0.1% from FY14. Return on shareholder funds reduced as a result of lower investment returns, partly offset by higher shareholder capital. Shareholder capital is not hedged for interest rate movements.
- Normalised capital growth of 0.7% was up 0.2% from FY14. The increase reflects a higher proportion of Life's investment portfolio invested in property and equities. Property as a portion of average investment assets was 22% in FY15, up from 18% in FY14.

2H15 Life COE margin was 4.5% and increased by 0.1% on 1H15. The increase in Life COE margin in 2H15 was due to;

- higher product margin (up 0.1%);
- lower shareholder return (down 0.1%);
- higher normalised capital growth (up 0.1%).

### Life COE Margin Composition



## Expenses

FY15 total expenses were \$87m, up \$10m (13%) on FY14. The increase in expenses includes a full year of Accurium expenses (\$2m impact) following its acquisition in February 2014. Life expenses also increased as a result of adding employees in order to build out Life's asset origination capability and to support distribution initiatives, including annuities on platform.

## Investment experience

Investment experience represents the difference between actual investment gains/losses (both realised and unrealised) and expected gains/losses based on Challenger's long-term expected returns. Refer to page 34 for details on Challenger's assumed long-term expected returns by asset class. Investment experience also includes any impact of changes in economic variables and assumptions on Life's liabilities (refer to page 35 for more detail).

FY15 investment experience was a loss of \$50m (pre-tax), comprising a \$40m loss on Life's investment assets and a \$10m loss from changes in economic variables and assumptions impacting Life's annuity liabilities.

The FY15 loss on Life's investment assets (-\$40m) was primarily due to losses on the fixed income portfolio (-\$66m) as a result of expansion in domestic and offshore credit spreads, partially offset by strong property valuation gains net of property transaction costs (+\$33m).

Investment experience includes a loss of \$10m in relation to changes in economic variables and assumptions impacting Life's annuity liabilities. This mainly relates to the fair value adjustment applied to Life's new business. This arises as the actual funding cost of new business is higher than the risk free discount rate required to be used to value policy liabilities. This difference is recognised as a loss at the time of sale, and reverses over the term of the policy.

### FY15 investment experience (pre-tax)

Asset class (\$m)	Actual capital growth	Normalised capital growth	Investment experience
Fixed income	(95)	(29)	(66)
Property	85	52	33
Infrastructure	17	21	(4)
Equity and other	33	36	(3)
<b>Asset investment experience</b>	<b>40</b>	<b>80</b>	<b>(40)</b>
Annuity valuation experience	(10)	–	(10)
<b>Total</b>	<b>30</b>	<b>80</b>	<b>(50)</b>

## Sales and AUM

FY15 Life retail annuity sales were \$2.8bn, down \$46m on FY14. Retail annuity sales were impacted by the discontinuance of the Care Annuity product in November 2014. Excluding Care Annuity, retail annuity sales increased by 5% in FY15.

Retail annuity sales continue to benefit from favourable macroeconomic trends, including an ageing population and retirees taking a more conservative approach to retirement investing. These favourable macroeconomic trends are being leveraged by Challenger's product innovation and extensive distribution footprint, including annuities on platform initiatives.

Lifetime annuity sales (Liquid Lifetime and Care Annuity) were \$480m in FY15, down from \$613m in FY14. Lifetime annuity sales represent 17% of total FY15 retail annuity sales, down from 22% in FY14. The reduction in lifetime annuity sales predominantly reflects the discontinuance of the Care Annuity.

Care Annuity sales in FY15 were \$100m, down from \$279m in FY14. The Care Annuity was discontinued in November 2014 following the Department of Social Services decision to redefine how the Care Annuity would be treated for social security purposes. In order to reduce uncertainty for customers, Challenger discontinued the Care Annuity. The aged care market remains an attractive market and in August 2015 Challenger launched a replacement Care product (CarePlus). The social security treatment of CarePlus has been confirmed by the Department of Social Services.

Retail annuity sales continue to benefit from strong reinvestment rates for term annuities with a residual capital value. The reinvestment rate for term annuities with a residual capital value of 50% or more was ~70% in FY15, down slightly on the long term average (~80%) due to Challenger's active decision not to roll over short term annuities in the last quarter of FY15. Term annuity reinvestment sales were \$560m in FY15, or 25% of total retail term annuity sales.

FY15 retail annuity net flows (i.e. annuity sales less capital repayments) were \$738m, down from \$887m in FY14. Based on the closing FY14 Life retail annuity book (\$7,824m), retail annuity net book growth in FY15 was 9.4%, down from 12.5% in FY14.

Excluding Care Annuity (both sales and capital repayments), FY15 net book growth was 9.3%, up on 8.9% in FY14.

FY15 institutional sales represent Challenger's Guaranteed Index Return (GIR) product. FY15 sales were \$944m and mainly represent the reinvestment of GIR maturities.

Life's FY15 investment assets (AUM) was \$12.8bn, up 15% (\$1.7bn) for the year. The increase in investment assets is due to Life earnings (net of dividends to Group), retail annuity net flows, and capital injected into CLC following the capital initiatives completed in 1H15 (refer to page 11 for additional detail).

For additional Life sales and AUM commentary, refer to the Assets Under Management and sales disclosure commencing on page 28.

## Capital management

Refer to page 11 for details on CLC's regulatory capital base and excess capital above prescribed capital amount.

## Accurium acquisition

In February 2014 Challenger completed the acquisition of Bendzulla Actuarial for \$25m and the business was rebranded Accurium and repositioned as a SMSF retirement specialist in 1H15.

Accurium is Australia's leading provider of Self Managed Superannuation Fund (SMSF) actuarial certificates. An actuarial certificate is required by a SMSF when one (or more) members are in the retirement phase of superannuation and one (or more) are in the savings phase of superannuation. Accurium has approximately 60% of the SMSF actuarial certificate market share.

The Accurium acquisition was a strategic investment for Challenger. Accurium's vision is to become Australia's SMSF retirement specialist and leverage existing relationships with SMSF practitioners to increase the level of engagement and education for SMSF retirement solutions.

In FY15 Accurium launched a SMSF Retirement Healthcheck in order to help build an understanding of the sustainability of retirement spending and build an understanding of retirement issues, including life expectancy, market performance and inflation.

From 1 July 2016 accountants will no longer be able to provide SMSF financial advice unless they hold an Australian Financial Services Licence (either restricted or full). The SMSF Retirement Healthcheck is being piloted to incorporate these licensing reforms, and used by SMSF practitioners to generate referrals for financial advisers.

Life's FY15 financial results include Accurium, with revenue of \$10m in FY15 reported as other income and included in Life's COE framework. Life's total expenses includes \$5m in relation to Accurium.

## Life Risk

Challenger's lifetime annuity sales represent 17% of total retail annuity sales for FY15. Lifetime annuities provide guaranteed payments to customers for life. Through selling lifetime annuities, CLC is assuming longevity risk, which is the risk annuitant customers live longer, in aggregate, than expected. This is in contrast to mortality risk, which is the risk that people die earlier than expected and is a natural hedge to longevity risk.

CLC is diversifying its capital and earnings base by participating in wholesale reinsurance longevity and mortality transactions (Life Risk).

Under APRA capital standards an aggregation benefit rewards diversification of risk across asset and life insurance risks. Based on Life's current business mix, the aggregation benefit reduces the insurance risk charge by approximately 80%. As a result, longevity risk provides CLC with earnings diversification in a highly RoE accretive way. For additional details on CLC's regulatory capital requirements and prescribed capital amount across insurance and asset risks, refer to the capital management disclosures on pages 10 to 13.

CLC has participated in a number of Life Risk Wholesale reinsurance transactions, providing exposure to UK/European longevity and mortality, North American mortality, and Australian mortality and morbidity. All transactions have been executed via reinsurance and swap transactions, and do not assume asset risk.

FY15 Life COE includes \$10m as a result of Life Risk transactions and represents premiums net of expected claims (FY14 \$7m contribution). As at 30 June 2015, the present value of future profits arising from Life Risk transactions was \$181m (FY14 \$105m), representing the present value of expected future cash inflows (premiums) and cash outflows (claims). The Life Risk portfolio has an average duration of 15 years.

Undertaking wholesale longevity and mortality transactions is a natural business extension for Life. Life is participating in established markets, has specialised expertise and is taking a disciplined approach to the Life Risk opportunity.

## Outlook

The Australian retirement incomes market is expected to grow strongly over the next 20 years as Australia's Baby Boomers (born 1946 to 1964) move from retirement 'saving' to retirement 'spending'. Over this period, the number of Australians over 65, which is Life's target demographic, is expected to increase by 75%.

Challenger Life is well positioned to benefit from changes in retiree risk preferences, including focus on longevity risk by retirees and their advisers. Annuities address many of the financial concerns retirees face in retirement.

Demand for annuity products is being amplified through Challenger's market-leading distribution, product innovation and strong retirement incomes brand recognition.

Challenger is investing in technology to allow its annuities to easily integrate with account-based pensions as there is a growing acceptance that annuities are part of the optimal retirement income solution. Integrating annuities with account-based pensions support income layering and enable guaranteed incomes to be combined with other products to build more comprehensive retirement income solutions.

In FY15 Challenger formed a strategic partnership with Colonial First State, adding Challenger to the Colonial platforms from August 2015, resulting in annuity platform access to half of Australia's financial adviser firms.

In the industry fund sector, Challenger backed term and lifetime annuities have been integrated with VicSuper account-based pensions to create Australia's first comprehensive income product for retirement. Challenger has also formed a strategic alliance with the Link Group/AAS that will see Challenger's annuities available to their industry fund clients, who service the needs of 10 million super fund members.

The Australian Federal Government commissioned the Financial System Inquiry (FSI) to provide a 'blueprint' for Australia's financial system over the next decade. The FSI report (released December 2014) recommended the retirement phase of superannuation would benefit greatly from pre-selected retirement products for members. These products would provide regular and stable income streams with longevity protection. Annuities were recognised as providing stable incomes and providing longevity protection, and could be part of pre-selected retirement products offered by all superannuation funds.

The FSI also recommended the impediments to longevity product development be removed. This would clear the way for Challenger to develop and issue Deferred Lifetime Annuities, expanding Life's product offering. Deferred Lifetime Annuities are expected to be popular as they provide protection against the risk of running out of money late in life.

The Federal Government is expected to respond to the FSI recommendations in 2015. Challenger expects the Government to support the recommendation for more comprehensive retirement income products and to remove impediments to longevity product development.

The Australian retirement incomes market is undergoing significant change as retirees move from public to private pensions. The focus is shifting to the retirement phase of superannuation and there is considerable media and public policy discussion on the need for more private provision of longevity risk and product innovation. With this increased focus on the retirement phase, models adopting income layering are emerging, and superannuation funds are partnering with life companies to build more comprehensive retirement solutions.

As Australia's leading retirement income specialist, Challenger is uniquely positioned to benefit from growth in Australia's retirement incomes market. Challenger is developing alliances across both the retail and industry superannuation segments and when coupled with relationships Accurium holds in the SMSF sector, Challenger has access to one third of Australia's superannuation industry.

## Funds Management financial results

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
<b>Fidante Partners</b>									
Fidante Partners income <sup>1</sup>	35.6	33.7	31.8	16.9	18.7	18.7	15.0	17.9	13.9
Equity accounted profits <sup>2</sup>	26.7	31.2	16.1	13.3	13.4	15.1	16.1	11.2	4.9
<b>Net income</b>	<b>62.3</b>	<b>64.9</b>	<b>47.9</b>	<b>30.2</b>	<b>32.1</b>	<b>33.8</b>	<b>31.1</b>	<b>29.1</b>	<b>18.8</b>
<b>Challenger Investment Partners</b>									
Net management fees	33.2	39.5	41.0	16.0	17.2	20.4	19.1	19.4	21.6
Performance and transaction fees	22.0	5.8	10.5	15.2	6.8	2.2	3.6	5.7	4.8
<b>Net income</b>	<b>55.2</b>	<b>45.3</b>	<b>51.5</b>	<b>31.2</b>	<b>24.0</b>	<b>22.6</b>	<b>22.7</b>	<b>25.1</b>	<b>26.4</b>
<b>Total net fee income</b>	<b>117.5</b>	<b>110.2</b>	<b>99.4</b>	<b>61.4</b>	<b>56.1</b>	<b>56.4</b>	<b>53.8</b>	<b>54.2</b>	<b>45.2</b>
Personnel expenses	(50.2)	(47.8)	(45.8)	(25.4)	(24.8)	(24.4)	(23.4)	(23.0)	(22.8)
Other expenses	(23.2)	(19.1)	(19.5)	(12.7)	(10.5)	(9.4)	(9.7)	(10.0)	(9.5)
<b>Total expenses</b>	<b>(73.4)</b>	<b>(66.9)</b>	<b>(65.3)</b>	<b>(38.1)</b>	<b>(35.3)</b>	<b>(33.8)</b>	<b>(33.1)</b>	<b>(33.0)</b>	<b>(32.3)</b>
<b>EBIT</b>	<b>44.1</b>	<b>43.3</b>	<b>34.1</b>	<b>23.3</b>	<b>20.8</b>	<b>22.6</b>	<b>20.7</b>	<b>21.2</b>	<b>12.9</b>
<b>Performance analysis</b>									
Fidante Partners – income margin (bps) <sup>3</sup>	15	20	20	14	16	20	20	21	18
Challenger Investment Partners – income margin (bps) <sup>3</sup>	43	40	45	47	39	41	40	44	45
Cost to income ratio	62.5%	60.7%	65.7%	62.1%	62.9%	59.9%	61.5%	60.9%	71.5%
Net assets – average <sup>4</sup>	124.3	132.2	129.2	121.7	127.1	134.3	131.0	127.4	130.5
RoE (pre-tax)	35.5%	32.8%	26.4%	38.6%	32.5%	33.9%	31.3%	33.6%	19.6%
Fidante Partners	44,667.0	35,879.4	29,757.0	44,667.0	42,502.5	35,879.4	33,670.8	29,757.0	23,984.3
Challenger Investment Partners	13,235.4	11,247.1	11,346.4	13,235.4	12,709.4	11,247.1	11,315.0	11,346.4	11,351.0
<b>Closing FUM – total</b>	<b>57,902.4</b>	<b>47,126.5</b>	<b>41,103.4</b>	<b>57,902.4</b>	<b>55,211.9</b>	<b>47,126.5</b>	<b>44,985.8</b>	<b>41,103.4</b>	<b>35,335.3</b>
Fidante Partners	42,432.9	33,164.3	24,330.1	44,381.9	40,493.9	34,850.7	31,550.2	27,359.9	21,250.9
Challenger Investment Partners	12,712.8	11,273.8	11,556.6	13,358.2	12,066.9	11,153.7	11,399.8	11,456.2	11,627.7
<b>Average FUM – total<sup>5</sup></b>	<b>55,145.7</b>	<b>44,438.1</b>	<b>35,886.7</b>	<b>57,740.1</b>	<b>52,560.8</b>	<b>46,004.4</b>	<b>42,950.0</b>	<b>38,816.1</b>	<b>32,878.6</b>
<b>FUM and net flows analysis</b>									
Fidante Partners	6,104.4	2,411.7	7,544.7	678.3	5,426.1	1,148.1	1,263.6	4,801.9	2,742.8
Challenger Investment Partners	1,634.5	(264.3)	(566.1)	294.4	1,340.1	(114.5)	(149.8)	(47.5)	(518.6)
Net flows	7,738.9	2,147.4	6,978.6	972.7	6,766.2	1,033.6	1,113.8	4,754.4	2,224.2
Distributions	(261.7)	(234.9)	(315.4)	(97.2)	(164.5)	(105.9)	(129.0)	(245.4)	(70.0)
Market linked movement	3,298.7	4,110.6	3,423.1	1,815.0	1,483.7	1,213.0	2,897.6	1,259.1	2,164.0
<b>Total FUM movement</b>	<b>10,775.9</b>	<b>6,023.1</b>	<b>10,086.3</b>	<b>2,690.5</b>	<b>8,085.4</b>	<b>2,140.7</b>	<b>3,882.4</b>	<b>5,768.1</b>	<b>4,318.2</b>

1 Fidante Partners income includes distribution and administration fees.

2 Equity accounted profits represent Challenger's share of boutiques' pre-tax earnings.

3 Income margin represents net income divided by average FUM.

4 Net assets – average calculated on a monthly basis.

5 Average FUM calculated on a monthly basis.



## Funds Management financial results

Challenger's Funds Management business is Australia's seventh<sup>1</sup> largest investment manager and one of the fastest growing. Over the last three years Funds Under Management (FUM) has increased by approximately 90%. The business is benefiting from a clear business strategy, which is focused on investor alignment.

Fidante Partners' multi-boutique platform comprises separately branded, investment management businesses. The model aligns the interests of investors, boutique investment managers and Fidante Partners.

The Fidante Partners model is delivering superior investment performance, with 95% of all funds and mandates outperforming their benchmark since inception.

Challenger Investment Partners manage fixed income and property under Challenger's brand for the Life Company and third party institutional investors. On 1 July 2014 (beginning of FY15), Challenger Investment Partners' infrastructure business merged with Access Capital Advisers to form Whitehelm Capital and create Fidante Partners' first infrastructure boutique fund manager.

### EBIT and RoE

Funds Management EBIT was \$44m and increased by \$1m (2%) in FY15. Higher total net fee income (up \$7m) was offset by higher expenses (up \$6m), including costs associated with investing for business growth.

FY15 Funds Management RoE was 35.5%, and increased by 270 basis points for the year. RoE benefited from higher EBIT and lower average net assets.

### Total net fee income

FY15 total net fee income increased by \$7m (7%) due to higher Challenger Investment Partners net income (up \$10m) offset by lower Fidante Partners net fee income (down \$3m).

Fidante Partners net fee income includes distribution fees, administration fees and a share in the equity accounted profits of boutique investment managers. Fidante Partners' net income also includes Fidante Partners share of performance fees earned by boutique investment managers.

FY15 Fidante Partners net income was \$62m, down 4% (\$3m) on FY14. Distribution and administration fees increased by \$2m, however were offset by lower equity accounted profits (down \$5m) due to lower performance fees earned by boutique investment managers. Fidante Partners net income of \$62m includes \$9m in relation to performance fees, down from \$19m in FY14.

Fidante Partners income margin (net income to average FUM) was 15 bps, down 5 bps from FY14. The reduction in net

income margin is due to lower performance fees (-4 bps) and a change in FUM mix (-1 bp).

FY15 Fidante Partners performance fees were impacted by market volatility. Performance fees on funds are not earned during periods of negative investment performance, despite superior relative performance.

Challenger Investment Partners net income increased by \$10m (22%) in FY15, with higher performance and transaction fees (up \$16m) offset by lower net management fees (down \$6m).

Performance and transaction fees benefited from fixed income and property fees.

Net management fees fell as a result of a change in FUM mix, including the merger of Challenger Investment Partners infrastructure business to form Whitehelm Capital, the consolidation of Challenger's ABS (Asset Backed Securities) fixed income teams into Challenger Investment Partners, and the wind up of the Challenger Howard Mortgage Fund.

Challenger Investment Partners FY15 income margin (net income to average FUM) was 43 bps, up 3 bps for the year. The income margin benefited from higher performance and transaction fees (+12 bps), partially offset by the change in FUM mix (-9 bps).

### Expenses

FY15 total expenses were \$73m, representing an increase of \$6m (10%) on FY14.

The increase in expenses is mainly due to expenses associated with the sale of Kapstream, Fidante Partners' European expansion and the acquisition of Dexion Capital (\$3m). Personnel expenses increased by \$2m primarily as a result of the transfer of the ABS fixed income team to Challenger Investment Partners.

The FY15 cost to income ratio was 62.5%, up from 60.7% in FY14, with higher net fee income offset by higher expenses.

### FUM

Total Funds Under Management (FUM) at 30 June 2015 was \$57.9bn, up 23% for the year.

### Fidante Partners FUM and net flows

Fidante Partners FY15 FUM was \$44.7bn, up \$8.8bn (24%) for the year. FUM growth was driven by strong net flows and positive investment markets.

Fidante Partners net flows were \$6.1bn, up from \$2.4bn in FY14. FY15 net flows include the formation of Whitehelm Capital (\$3.9bn) and strong organic net flows across a range of boutique investment managers (\$2.2bn).

<sup>1</sup> Consolidated FUM for Australian fund managers – Rainmaker Roundup March 2015.

On 1 July 2014 Whitehelm Capital was formed by merging Challenger Investment Partners' infrastructure business with Access Capital Advisers, resulting in \$3.9bn of infrastructure net flows. Whitehelm Capital is Fidante Partners' first infrastructure boutique and manages approximately \$4bn of FUM focused on core infrastructure assets such as regulated utilities and airports.

Fidante Partners organic net flows were \$2.2bn in FY15 and include a \$0.5bn outflow in respect of Five Oceans, which closed in late FY14. Organic net flows were positive across both equities and fixed income, with a \$0.4bn outflow in alternatives.

Approximately 52% of Fidante Partners FY15 FUM is invested in fixed income, 39% in equity products and 9% in alternatives (e.g. infrastructure) products.

### **Challenger Investment Partners FUM and net flows**

Challenger Investment Partners FY15 FUM was \$13.2bn, which was up \$2.0bn (18%) for the year. The increase in FUM was driven by net inflows of \$1.6bn, up from a net outflow of \$0.3bn in FY14.

Challenger Investment Partners FY15 net inflows include \$0.9bn in relation to:

- Life's ABS fixed income team transferred to Challenger Investment Partners on 1 July 2014 resulting in a net inflow of \$1.8bn; partially offset by
- the merger of Challenger Investment Partners infrastructure business with Access Capital Advisers to form Whitehelm Capital on 1 July 2014 resulting in a net outflow of \$0.9bn.

Challenger Investment Partners FY15 organic net inflows were \$0.7bn, with positive fixed income inflows of \$1.1bn partially offset by property net outflows of \$0.4bn.

Approximately 70% of Challenger Investment Partners FY15 FUM is invested in fixed income and approximately 30% of FUM is invested in property.

For additional Challenger Investment Partners FUM and net flow commentary, refer to the Funds Under Management and net flow disclosures on page 26.

### **Sale of Kapstream and new distribution agreements**

In early July 2015, Fidante Partners sold its 25% equity interest in global fixed income boutique investment manager, Kapstream to US-based Janus Capital Group Inc. (Janus) for \$45 million. Fidante Partners also entered into new distribution and administration agreements with both Kapstream and Janus.

Challenger will recognise a \$40m pre-tax profit on sale in FY16 as a significant item.

The Kapstream sale provides opportunities to further develop Kapstream and Fidante Partners' businesses and provides opportunities for long-term strategic collaboration between Fidante Partners and Janus.

Kapstream FUM at 30 June 2015 was \$9.2bn and comprised retail FUM of \$3.8bn and institutional FUM of \$5.4bn. Following the sale of Kapstream, Fidante Partners will continue to receive administration and distribution fees on retail FUM (\$3.8bn), however will not receive distribution fees on institutional FUM (\$5.4bn). As a result, on 1 July 2015, Fidante Partners FUM will reduce by \$5.4bn. Despite the reduction in FUM, Fidante Partners earnings over the short and medium term are not expected to be negatively impacted following new distribution agreements.

### **Dexion Capital acquisition**

In July 2015 Fidante Partners acquired 100% of Dexion Capital Holdings Limited, a European alternative investments group comprising interests in three specialist fund managers, as well as an investments distribution business. Dexion Capital employs approximately 40 staff, predominately based in London.

The acquisition substantially expands Fidante Partners' presence in Europe where it already holds interests in UK-based alternative asset managers Whitehelm Capital (global infrastructure) and WyeTree Asset Management (asset-backed securities). The acquisition also provides Fidante Partners with established distribution channels to UK and European alternative focused investors.

The acquisition completed in July 2015 for an agreed fixed payment of £19.6m (A\$41m) to Dexion Capital's shareholders. The final acquisition price is dependent on profitability over a period of up to six years, under earn-out arrangements with key Dexion Capital executives.

The acquisition is immediately earnings accretive and expected to meet Challenger's 18% pre-tax return on equity target in FY16.

Following the acquisition, Fidante Partners FUM is expected to increase by \$0.6bn, representing the FUM managed by the three Dexion Capital boutique investment managers and Dexion Absolute, a white-labelled specialist alternatives fund. Dexion earns distribution and administration fees on this FUM and has economic interests in the Boutique managers.

Dexion Capital also earns income from its UK-listed funds business, with distribution fees earned either upfront or over time. The UK-listed funds business has raised over US\$18bn since 2002. Fidante Partners FUM will not be adjusted to include the FUM raised by the UK-listed funds business.



The Dexion acquisition is expected to meet Challenger's 18% return on equity (pre-tax) target in FY16. This equates to approximately \$7m in Funds Management earnings for FY16. Dexion's cost to income ratio is in the range of 65% to 75%.

## Outlook

The Australian funds management market remains an attractive market underpinned by mandated superannuation contributions. Contributions increased to 9.5% of gross salaries on 1 July 2014 and are scheduled to increase to 12% by 2025. The mandated nature of Australia's superannuation system is expected to significantly grow the size of Australia's superannuation assets from \$2 trillion to \$7 trillion<sup>1</sup> over the next 20 years.

Fidante Partners continues to identify new investment manager talent. The platform has a variety of managers across Australian equities, international equities, fixed income and alternatives. Fidante Partners is adding capacity to existing managers and is expanding its platform in Europe.

The acquisition of Dexion Capital substantially expands Fidante Partners' presence in Europe where it already holds interests in two alternative boutique investment managers. This acquisition represents a significant step-up in European presence and is an important part of Fidante Partners international distribution and product expansion. Dexion's funds management operations provide a scalable platform to expand Fidante Partners successful multi-boutique model into the European market, whilst opening up global distribution opportunities for existing boutique investment managers.

Challenger Investment Partners continues to build out its client base and product offering. There are opportunities to add new mandates from domestic and international institutions, superannuation funds and sovereign wealth funds, in order to grow its third party fiduciary business.

Challenger's Funds Management business is well positioned to benefit from growth in Australia's superannuation system. The Funds Management platform has multiple brands and strategies with scalable platforms in Australia and Europe. Coupled with Challenger's distribution capability, institutional strength, administration platform and strong boutique investment manager performance, the Funds Management business is well positioned to continue to increase returns to shareholders.

<sup>1</sup> Deloitte – Dynamics of the Australian superannuation system: the next 20 years 2013 – 2033 – September 2013.

## Corporate financial results

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
<b>Other income</b>	<b>1.3</b>	<b>1.8</b>	<b>4.9</b>	<b>0.6</b>	<b>0.7</b>	<b>0.6</b>	<b>1.2</b>	<b>1.7</b>	<b>3.2</b>
Personnel expenses	(36.8)	(34.3)	(34.6)	(18.5)	(18.3)	(17.7)	(16.6)	(17.0)	(17.6)
Other expenses	(10.1)	(10.4)	(10.7)	(5.5)	(4.6)	(5.6)	(4.8)	(5.4)	(5.3)
<b>Total expenses (excluding LTI)</b>	<b>(46.9)</b>	<b>(44.7)</b>	<b>(45.3)</b>	<b>(24.0)</b>	<b>(22.9)</b>	<b>(23.3)</b>	<b>(21.4)</b>	<b>(22.4)</b>	<b>(22.9)</b>
Long term incentives (LTI) <sup>1</sup>	(16.8)	(16.7)	(10.8)	(8.8)	(8.0)	(8.4)	(8.3)	(5.3)	(5.5)
<b>Total expenses</b>	<b>(63.7)</b>	<b>(61.4)</b>	<b>(56.1)</b>	<b>(32.8)</b>	<b>(30.9)</b>	<b>(31.7)</b>	<b>(29.7)</b>	<b>(27.7)</b>	<b>(28.4)</b>
<b>Normalised EBIT</b>	<b>(62.4)</b>	<b>(59.6)</b>	<b>(51.2)</b>	<b>(32.2)</b>	<b>(30.2)</b>	<b>(31.1)</b>	<b>(28.5)</b>	<b>(26.0)</b>	<b>(25.2)</b>
Interest and borrowing costs	(3.8)	(4.1)	(4.6)	(2.1)	(1.7)	(1.9)	(2.2)	(1.9)	(2.7)
<b>Normalised profit/(loss) before tax</b>	<b>(66.2)</b>	<b>(63.7)</b>	<b>(55.8)</b>	<b>(34.3)</b>	<b>(31.9)</b>	<b>(33.0)</b>	<b>(30.7)</b>	<b>(27.9)</b>	<b>(27.9)</b>

## Corporate financial results

The Corporate division comprises central functions such as group executives, finance, treasury, legal, human resources, risk management and strategy.

Corporate also includes interest received on Group cash balances and any interest and borrowing costs associated with Group debt facilities.

### Normalised profit/(loss) before tax

FY15 Corporate normalised profit before tax was a loss of \$66m, up from a loss of \$64m in FY14. The increase in Corporate normalised loss was due to lower other income (down \$1m) and higher total expenses (up \$2m).

### Other income

Other income includes interest received on Group cash balances. In FY15 net income decreased by \$1m as a result of a lower average cash balance on which interest income is earned.

## Total expenses

FY15 total expenses were \$64m, up \$2m on FY14. The increase in expenses is due to higher personnel costs as a result of an increase in employee numbers. Employee numbers increased in order to support Challenger's growth ambitions, including new distribution initiatives.

Long term incentive costs relate to the non-cash amortisation of equity grants and were unchanged from FY14.

## Interest and borrowing costs

FY15 interest and borrowing costs were \$4m and were unchanged from FY14. The Group debt facility was undrawn during FY15, with interest and borrowing costs reflecting debt facility fees. The Group maintains a banking facility in order to provide additional financial flexibility.

<sup>1</sup> Corporate financial results include all of the Group's long term incentives provided under the Challenger Performance Plan. Short term incentives under the Employee Incentive Plan are accounted for within each operating division's personnel expenses.

## Consolidated operating cash flows

\$m	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
Receipts from customers	543.0	508.5	456.8	288.8	254.2	259.5	249.0	224.9	231.9
Dividends received	77.1	61.2	44.2	43.1	34.0	34.3	26.9	22.5	21.7
Interest received	585.9	549.3	542.7	316.3	269.6	279.1	270.2	272.8	269.9
Interest paid	(438.7)	(406.5)	(373.3)	(225.3)	(213.4)	(203.1)	(203.4)	(187.5)	(185.8)
Payments to suppliers and employees	(413.7)	(377.3)	(344.2)	(206.6)	(207.1)	(180.2)	(197.1)	(159.0)	(185.2)
Income tax paid	(65.7)	(14.2)	(4.7)	(22.0)	(43.7)	(12.0)	(2.2)	(3.3)	(1.4)
<b>Underlying operating cash flow</b>	<b>287.9</b>	<b>321.0</b>	<b>321.5</b>	<b>194.3</b>	<b>93.6</b>	<b>177.6</b>	<b>143.4</b>	<b>170.4</b>	<b>151.1</b>
Adjust for:									
Net retail annuity policy capital receipts	738.2	603.4	598.1	177.4	560.8	63.5	539.9	385.3	212.8
Net institutional capital (payments)/ receipts	(186.7)	(745.1)	(150.0)	(16.7)	(170.0)	25.3	(770.4)	(40.0)	(110.0)
Other <sup>1</sup>	(23.5)	(31.9)	19.6	(7.7)	(15.8)	(5.5)	(26.4)	12.5	7.1
<b>Operating cash flow per financial report</b>	<b>815.9</b>	<b>147.4</b>	<b>789.2</b>	<b>347.3</b>	<b>468.6</b>	<b>260.9</b>	<b>(113.5)</b>	<b>528.2</b>	<b>261.0</b>

## Consolidated operating cash flows

Underlying operating cash flows excludes cash flows that are capital in nature such as annuity sales and annuity capital payments.

FY15 underlying operating cash flow was \$288m, down from \$321m in FY14. The reduction was primarily due to higher tax payments, reflecting Challenger moving to monthly tax instalments in FY15 and the payment of the final FY14 tax instalment.

## Net retail annuity policy capital receipts

Net retail annuity policy capital receipts in FY15 were \$738m and comprise:

- retail annuity sales of \$2,753m; less
- retail annuity capital payments of \$2,015m.

Retail annuity capital payments are capital payments to annuitants and exclude interest payments.

Retail annuity net book growth can be calculated as retail annuity net flows (\$738m) divided by the opening period Life retail annuity book (\$7,824m for FY15 – refer to page 6). FY15 retail annuity net book growth was 9.4%.

## Net institutional capital payments

FY15 net institutional capital payments of \$187m comprise:

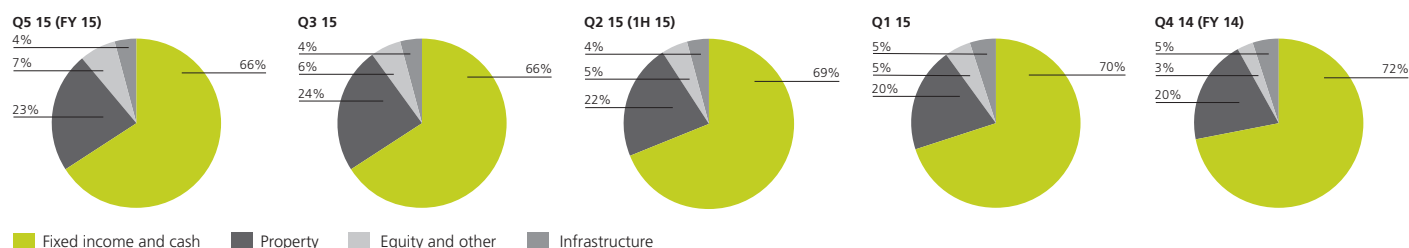
- Institutional capital payments \$1,131m; less
- Institutional sales of \$944m.

<sup>1</sup> Other includes net SPV operating cash flow and adjustments for classification differences between statutory operating cash flow and normalised cash operating earnings.

## Assets and Funds Under Management, net flows and sales

\$m	Q4 15	Q3 15	Q2 15	Q1 15	Q4 14
<b>Total Assets and Funds Under Management</b>	<b>59,789</b>	<b>60,430</b>	<b>57,169</b>	<b>54,189</b>	<b>50,725</b>
<b>Represented by:</b>					
<b>Funds Management</b>					
<b>Fidante Partners<sup>1</sup></b>					
Equities	17,323	18,011	16,626	15,960	16,541
Fixed income	23,085	22,952	21,795	20,699	19,338
Alternatives	4,259	4,178	4,082	3,893	–
<b>Total Fidante Partners</b>	<b>44,667</b>	<b>45,141</b>	<b>42,503</b>	<b>40,552</b>	<b>35,879</b>
<b>Challenger Investment Partners</b>					
Fixed income	9,231	8,985	8,624	8,461	6,036
Infrastructure	–	–	–	–	922
Property	4,004	4,609	4,085	3,565	3,418
Challenger Diversified Property Group (ASX:CDI) (gross assets)	–	–	–	–	871
<b>Total Challenger Investment Partners</b>	<b>13,235</b>	<b>13,594</b>	<b>12,709</b>	<b>12,026</b>	<b>11,247</b>
<b>Total funds under management</b>	<b>57,902</b>	<b>58,735</b>	<b>55,212</b>	<b>52,578</b>	<b>47,126</b>
Average Fidante Partners	42,433	43,936	41,567	39,435	35,634
Average Challenger Investment Partners	12,713	13,191	12,339	11,784	11,066
<b>Average total funds under management<sup>2</sup></b>	<b>55,146</b>	<b>57,127</b>	<b>53,906</b>	<b>51,219</b>	<b>46,700</b>
<b>Life</b>					
Fixed income and cash <sup>3</sup>	8,514	8,514	8,541	8,120	7,955
Property <sup>3</sup>	2,884	3,046	2,717	2,320	2,168
Equity and other	883	736	632	551	401
Infrastructure <sup>3</sup>	514	527	503	536	563
<b>Total Life investment assets</b>	<b>12,795</b>	<b>12,823</b>	<b>12,393</b>	<b>11,527</b>	<b>11,087</b>
<b>Average Life investment assets<sup>2</sup></b>	<b>12,176</b>	<b>12,647</b>	<b>12,001</b>	<b>11,254</b>	<b>10,872</b>

## Life asset allocation



1 Fidante Partners comprise a number of co-owned, separately branded active boutique investment managers from which Fidante receives distribution and administration fees. Fidante Partners also shares in the profits from these businesses through its equity ownership.

2 Average total funds under management and Life investments calculated on a monthly basis.

3 Fixed income, property and infrastructure are reported net of debt.

## Assets and Funds Under Management, net flows and sales (continued)

Analysis of flows	Q4 15	Q3 15	Q2 15	Q1 15	Q4 14
<b>Funds Management net flows</b>					
Equities	473	(170)	220	(551)	(210)
Fixed income	240	520	653	1,251	841
Alternatives	(120)	(265)	4	3,849	–
<b>Total Fidante Partners</b>	<b>593</b>	<b>85</b>	<b>877</b>	<b>4,549</b>	<b>631</b>
Challenger Investment Partners	(314)	609	609	731	149
<b>Funds Management net flows</b>	<b>279</b>	<b>694</b>	<b>1,486</b>	<b>5,280</b>	<b>780</b>
<b>Life sales</b>					
Fixed Term	652	365	727	529	664
Lifetime (including Care)	81	80	158	161	200
<b>Total retail annuity sales</b>	<b>733</b>	<b>445</b>	<b>885</b>	<b>690</b>	<b>864</b>
Institutional sales	–	395	451	98	273
<b>Total Life sales</b>	<b>733</b>	<b>840</b>	<b>1,336</b>	<b>788</b>	<b>1,137</b>
<b>Reconciliation of Total Group Assets and Funds Under Management</b>					
Funds Management (FUM)	57,902	58,735	55,212	52,578	47,126
Life investment assets	12,795	12,823	12,393	11,527	11,087
Adjustments to remove double counting of cross holdings:					
Life Company investment in CDI	–	–	–	–	(585)
Life Company investment in fixed income, property and infrastructure	(10,908)	(11,128)	(10,436)	(9,916)	(6,903)
<b>Total Assets and Funds Under Management</b>	<b>59,789</b>	<b>60,430</b>	<b>57,169</b>	<b>54,189</b>	<b>50,725</b>

## Total Assets and Funds Under Management

FY15 total Group Assets and Funds Under Management was \$59.8bn, up 18% for the year.

### Funds Management

FY15 Funds Management FUM was \$57.9bn, up 23% for the year.

Funds Management net flows were \$7.7bn with Fidante Partners achieving net inflows of \$6.1bn and Challenger Investment Partners net inflows of \$1.6bn.

#### Fidante Partners

Fidante Partners net inflows are supported by strong investment performance across its boutique investment managers. Since inception of each boutique, 95% of all funds and mandates have outperformed their benchmark. Over three years, 96% of funds and mandates have outperformed their benchmarks. Over 1 year, 60% of funds and mandates have outperformed their benchmarks.

Fidante Partners FY15 net inflows were \$6.1bn, up from \$2.4bn in FY14. FY15 Fidante Partners net inflows include \$3.9bn following the formation of Whitehelm Capital on 1 July 2014.

Fidante Partners organic net inflows were \$2.2bn in FY15 and include a \$0.5bn outflow in respect of the closure of Five Oceans, a boutique investment manager. Organic net inflows were positive across both equities and fixed income. There was a net outflow of \$0.4bn in alternatives.

At 30 June 2015 approximately 52% of Fidante Partners FUM was invested in fixed income, 39% in equity and 9% in alternatives (e.g. infrastructure) products.

#### Challenger Investment Partners

Challenger Investment Partners net inflows were \$1.6bn in FY15, up from a net outflow of \$0.3bn in FY14.

Challenger Investment Partners FY15 net inflows include \$0.9bn in relation to:

- Life's ABS fixed income team transferred to Challenger Investment Partners on 1 July 2014 resulting in a net inflow of \$1.8bn; partially offset by
- the merger of Challenger Investment Partners infrastructure business with Access Capital Advisers to form Whitehelm Capital on 1 July 2014, resulting in a net outflow of \$0.9bn.

Challenger Investment Partners FY15 organic net inflows were \$0.7bn, with fixed income inflows of \$1.1bn partially offset by property net outflows of \$0.4bn.

At 30 June 2015, approximately 70% of Challenger Investment Partners FUM was invested in fixed income and approximately 30% invested in property.

### Life AUM and sales

FY15 Life AUM was \$12.8bn, up 15% for the year.

FY15 Life retail annuity sales were \$2.8bn, down \$46m on FY14. Retail annuity sales were impacted by the Care Annuity product discontinued in November 2014. Excluding the Care Annuity, retail annuity sales increased by 5% in FY15.

Lifetime annuity sales (i.e. Liquid Lifetime and Care Annuity) were \$480m in FY15, down from \$613m in FY14. Lifetime annuity sales represent 17% of total FY15 retail annuity sales, down from 22% in FY14. The reduction in lifetime annuity sales were impacted by the discontinuance of the Care Annuity.

Care Annuity sales in FY15 were \$100m, down from \$279m in FY14. The Care Annuity was discontinued in November 2014 following the Department of Social Services decision to redefine how the Care Annuity would be treated for social security purposes. In order to reduce uncertainty for customers, Challenger discontinued the Care Annuity.

The aged care market remains an attractive market and in August 2015 Challenger launched a replacement aged care product (CarePlus). The social security treatment of CarePlus has been confirmed by the Department of Social Services.

Retail annuity sales continue to benefit from strong reinvestment rates for term annuities with a residual capital value. The reinvestment rate for term annuities with a residual capital value of 50% or more was ~70% in FY15, down slightly on the long term average (~80%) due to Challenger's active decision not to roll over short term annuities in the last quarter of FY15. Term annuity reinvestment sales were \$560m in FY15, or 25% of total retail term annuity sales.

FY15 retail annuity net flows (i.e. annuity sales less capital repayments) were \$738m, down from \$887m in FY14. Based on the closing FY14 Life retail annuity book (\$7,824m), retail annuity net book growth in FY15 was 9.4%, down from 12.5% in FY14.

Excluding Care Annuity (both sales and capital repayments), FY15 net book growth was 9.3%, and up from 8.9% in FY14.

FY15 average tenor for new business sales was 6.4 years, and was unchanged from FY14. Average tenor of new business sales has increased significantly over the past five years, increasing from 3.5 years to 6.4 years. A lengthening of tenor assists future net book growth, enables investment in longer-dated assets, which earn higher illiquidity premiums, and is more efficient in terms of distribution and administration.

FY15 institutional sales were \$944m, mainly representing the reinvestment of maturities in Challenger's Guaranteed Index Return (GIR) product, with GIR maturities invested for a longer tenor.

## Profit and equity sensitivities

\$m	Change in variable	Profit/(loss) after tax FY15	Change in equity FY15	Profit/(loss) after tax FY14	Change in equity FY14	Profit/(loss) after tax FY13	Change in equity FY13
<b>Interest rate</b>							
Non-SPV	+100bps	7.1	7.1	5.0	5.0	5.5	5.5
	-100bps	(7.1)	(7.1)	(5.0)	(5.0)	(5.5)	(5.5)
SPV	+100bps	(2.0)	(2.0)	(2.6)	(2.6)	(3.6)	(3.6)
	-100bps	2.0	2.0	2.6	2.6	3.6	3.6
Total	+100bps	5.1	5.1	2.4	2.4	1.9	1.9
	-100bps	(5.1)	(5.1)	(2.4)	(2.4)	(1.9)	(1.9)
<b>Infrastructure and equity</b>							
Infrastructure investments	+10%	20.3	20.3	25.2	25.2	21.2	21.2
	-10%	(20.3)	(20.3)	(25.2)	(25.2)	(21.2)	(21.2)
Equity investments	+10%	50.9	50.9	20.6	20.6	16.1	16.1
	-10%	(50.9)	(50.9)	(20.6)	(20.6)	(16.1)	(16.1)
Total	+10%	71.2	71.2	45.8	45.8	37.3	37.3
	-10%	(71.2)	(71.2)	(45.8)	(45.8)	(37.3)	(37.3)
<b>Property</b>							
Direct Property	+1%	21.2	21.2	16.5	16.5	13.3	13.3
	-1%	(21.2)	(21.2)	(16.5)	(16.5)	(13.3)	(13.3)
Australian listed property securities	+10%	12.4	12.4	11.1	11.1	10.3	10.3
	-10%	(12.4)	(12.4)	(11.1)	(11.1)	(10.3)	(10.3)
Other property securities	+10%	8.4	8.4	21.8	21.8	21.1	21.1
	-10%	(8.4)	(8.4)	(21.8)	(21.8)	(21.1)	(21.1)
Total		42.0	42.0	49.4	49.4	44.7	44.7
		(42.0)	(42.0)	(49.4)	(49.4)	(44.7)	(44.7)
<b>Credit</b>							
Fixed Income assets	+50bps	(80.5)	(80.5)	(78.9)	(78.9)	(91.9)	(91.9)
	-50bps	80.5	80.5	78.9	78.9	91.9	91.9
<b>Currency</b>							
British Pound	+10%	0.3	0.3	0.7	0.7	(1.0)	(1.0)
	-10%	(0.3)	(0.3)	(0.7)	(0.7)	1.0	1.0
US Dollar	+10%	1.9	1.9	(0.1)	(0.1)	(0.2)	(0.2)
	-10%	(1.9)	(1.9)	0.1	0.1	0.2	0.2
Euro	+10%	(0.3)	(0.3)	(0.4)	(0.4)	(2.0)	(2.0)
	-10%	0.3	0.3	0.4	0.4	2.0	2.0
Japanese Yen	+10%	-	0.3	-	-	-	-
	-10%	-	(0.3)	-	-	-	-
Other	+10%	(0.2)	(0.2)	1.7	1.7	-	-
	-10%	0.2	0.2	(1.7)	(1.7)	-	-
<b>Longevity, mortality and morbidity<sup>1</sup></b>							
Life insurance contract liabilities	+50%	(37.7)	(37.7)	(25.6)	(25.6)	(13.7)	(13.7)
	-50%	37.7	37.7	25.6	25.6	13.7	13.7

<sup>1</sup> Longevity, mortality and morbidity life insurance contract liabilities sensitivity is net of any reinsurance with third parties.



## Profit and equity sensitivities

Profit and equity sensitivities set out the expected impact from changes in a range of economic and investment market variables on Challenger's earnings. These sensitivities represent the after-tax impact, assuming a tax rate of 30%.

The sensitivities are not forward looking and make no allowance for events occurring after 30 June 2015.

If using these sensitivities as forward looking, an allowance for changes post 30 June 2015, such as sales and asset growth, should be made.

These sensitivities assess the risk of changes in economic and investment markets on the valuation of assets, which in turn impact earnings. The earnings impact is included in investment experience and does not take into consideration the impact of any under or over performance of normalised growth assumptions for each asset category. Refer to page 34 for normalised growth assumptions.

These sensitivities do not include the indirect impact on fees for the Funds Management business.

## Interest rate sensitivities

Interest rate risk is the risk to earnings from movements in interest rates, including changes in absolute levels, shape of the yield curve, margin between different yield curves, and volatility of interest rates.

The sensitivities assume the change in variable occurs on 30 June 2015, and are based on assets and liabilities held at that date. It is Challenger's policy to minimise the impact of movements in interest rates via the use of interest rate swaps. Interest rate sensitivities are disclosed as either SPV (special purpose vehicle) or non-SPV.

SPV interest rate sensitivities relate to securitisation trusts that hold residual income stream notes (NIM) acquired by Challenger Life Company in FY09. For the SPV, changes in the BBSW benchmark over the RBA's target cash rate, results in a change in the cost of funding and impacts earnings. SPV interest rate risk is mitigated through the use of hedges.

In determining the interest rate sensitivities, it is assumed that changes in interest rates occur at balance date and there are concurrent movements in interest rates and parallel moves in the yield curve. All material underlying exposures and related interest rate hedges are included in the interest rate sensitivities.

## Infrastructure and equity sensitivities

Infrastructure and equity risk sensitivities represent the impact of changes in investment markets on asset valuations on balance date.

## Property sensitivities

Direct property sensitivities relate to Challenger's direct property portfolio.

The direct property sensitivities represent the impact from a change in property valuations on balance date and are based on Life's gross direct property investments of \$3,450m (net investments of \$2,884m plus debt of \$566m). The sensitivities do not include the impact on Funds Management fees. The property securities sensitivities relate to listed and unlisted property securities, such as real estate investment trusts.

Property sensitivities do not include the impact of property acquisition costs (e.g. stamp duty). Under Australian accounting standards, property acquisition and transaction costs are required to initially be capitalised. When the property is subsequently revalued, there is generally no value ascribed to the acquisition and transaction costs which may result in a reduction in the property valuation, with a corresponding negative investment experience impact.

## Credit sensitivities

Credit risk sensitivities set out the expected impact from movements in fixed income credit spreads. Challenger is exposed to movements in credit spreads above the interbank swap curve on its fixed income portfolio. The sensitivities apply to fixed income investments held at 30 June 2015.

## Currency sensitivities

Currency sensitivities set out the expected impact from changes in currency. It is Challenger's policy to hedge the exposure of all balance sheet items for movements in foreign exchange rates. Currency exposure arises primarily as a result of offshore investments. In order to mitigate foreign currency risk, Challenger has entered into foreign currency derivatives.

## Longevity, mortality and morbidity sensitivities

Challenger is exposed to longevity, mortality and morbidity risks on its life insurance liabilities and wholesale reinsurance transactions. Longevity risk is the risk of living longer than expected. Mortality risk is the risk that mortality on the underlying portfolio exceeds expectations. Morbidity risk is the risk that claims arising from sickness and accident in the underlying portfolio exceed expectations. There is a natural hedge between longevity and mortality risk. Challenger Life Company is required under APRA prudential standards to maintain regulatory capital in relation to the longevity, mortality and morbidity risks it carries.



Challenger manages some of its longevity risk exposure by using reinsurance for closed lifetime annuity portfolios (e.g. AXA) as well as regularly reviewing the portfolio and longevity experience to ensure longevity assumptions remain appropriate. Mortality and morbidity risks are managed by regularly reviewing the portfolio and other experience.

Mortality and morbidity rates are based on industry standards which are adjusted for Challenger's own recent experience, and includes an allowance for future rates of mortality improvement. Challenger assumes that future mortality rates for individual lifetime annuities will improve by between 1% and 4% per annum (depending on different age cohorts). This has the impact of increasing the life expectancy of a male aged 65 from 22 years (per the base mortality rates) to 27 years.

The mortality sensitivities set out the expected impact of an improvement in mortality. This is in addition to the mortality improvements Challenger already assumes. A 50% increase in mortality improvement rates would increase the life expectancy of a male aged 65 from 27 years (above) to 31 years.

## Issued share capital

Number of shares (m)	FY15	FY14	FY13	2H15	1H15	2H14	1H14	2H13	1H13
Basic share count	553.4	510.6	515.6	553.4	552.9	510.6	514.1	515.6	526.4
CPP 'treasury' shares	16.3	20.3	15.3	16.3	16.8	20.3	16.8	15.3	12.3
<b>Total issued shares</b>	<b>569.7</b>	<b>530.9</b>	<b>530.9</b>	<b>569.7</b>	<b>569.7</b>	<b>530.9</b>	<b>530.9</b>	<b>530.9</b>	<b>538.7</b>
<b>Movement in basic share count</b>									
Opening	510.6	515.6	529.0	552.9	510.6	514.1	515.6	526.4	529.0
CPP deferred share purchase	(4.6)	(3.0)	(6.6)	–	(4.6)	–	(3.0)	(3.0)	(3.6)
Net treasury shares (acquired)/released	8.6	(2.0)	7.0	0.5	8.1	(3.5)	1.5	–	7.0
On market buyback during the period	–	–	(13.8)	–	–	–	–	(7.8)	(6.0)
New share issues	38.8	–	–	–	38.8	–	–	–	–
Closing	553.4	510.6	515.6	553.4	552.9	510.6	514.1	515.6	526.4
<b>Movement in CPP 'treasury' shares</b>									
Opening	20.3	15.3	15.7	16.8	20.3	16.8	15.3	12.3	15.7
Shares vested to participants	(14.1)	(3.7)	(7.0)	(0.5)	(13.6)	(0.4)	(3.3)	–	(7.0)
CPP deferred share purchase	4.6	3.0	6.6	–	4.6	–	3.0	3.0	3.6
Shares bought into CPP Trust	5.5	5.7	–	–	5.5	3.9	1.8	–	–
Closing	16.3	20.3	15.3	16.3	16.8	20.3	16.8	15.3	12.3
<b>Share capital for EPS calculations</b>									
<b>Weighted average number of shares (m)</b>	<b>FY15</b>	<b>FY14</b>	<b>FY13</b>	<b>2H15</b>	<b>1H15</b>	<b>2H14</b>	<b>1H14</b>	<b>2H13</b>	<b>1H13</b>
<b>Basic EPS shares</b>									
Total issued shares	562.8	530.9	538.8	569.7	556.0	530.9	530.9	533.5	544.0
Less CPP 'treasury' shares	(17.1)	(17.1)	(12.7)	(16.5)	(17.8)	(17.8)	(16.4)	(12.7)	(12.6)
Shares for basic EPS calculation	545.7	513.8	526.1	553.2	538.2	513.1	514.5	520.8	531.4
<b>Diluted EPS shares</b>									
Shares for basic EPS calculation	545.7	513.8	526.1	553.2	538.2	513.1	514.5	520.8	531.4
Add dilutive impact of equity awards schemes	20.7	28.2	6.1	18.6	23.0	30.4	25.8	8.6	3.6
Add dilutive impact of capital notes	37.1	–	–	51.2	25.4	–	–	–	–
Shares for dilutive EPS calculation	603.5	542.0	532.2	623.0	586.6	543.5	540.3	529.4	535.0
<b>Summary of Share Rights</b>									
<b>Number (m)</b>	<b>FY15</b>	<b>FY14</b>	<b>FY13</b>	<b>2H15</b>	<b>1H15</b>	<b>2H14</b>	<b>1H14</b>	<b>2H13</b>	<b>1H13</b>
<b>Hurdled Performance Share Rights</b>									
Opening	26.6	21.8	14.4	17.6	26.6	27.0	21.8	22.2	14.4
New grants	2.6	6.6	8.4	0.2	2.4	–	6.6	0.2	8.2
Vesting/forfeiture	(11.9)	(1.8)	(1.0)	(0.5)	(11.4)	(0.4)	(1.4)	(0.6)	(0.4)
Closing	17.3	26.6	21.8	17.3	17.6	26.6	27.0	21.8	22.2
<b>Deferred Performance Share Rights</b>									
Opening	3.8	3.3	3.2	3.6	3.8	3.8	3.3	3.3	3.2
New grants	2.3	2.5	2.7	–	2.3	–	2.5	0.1	2.6
Vesting/forfeiture	(2.6)	(2.0)	(2.6)	(0.1)	(2.5)	–	(2.0)	(0.1)	(2.5)
Closing	3.5	3.8	3.3	3.5	3.6	3.8	3.8	3.3	3.3

## Issued share capital

### Issued share capital and diluted share count

The number of Challenger Limited shares listed on the Australian Securities Exchange (ASX) at 30 June 2015 was 570m shares, up from 531m shares at 30 June 2014. The increase in shares listed reflects:

- 33.2m shares issued following the \$250m institutional equity placement undertaken in August 2014; and
- 5.7m shares issued following the \$40m Share Purchase Plan (SPP) for retail investors completed in October 2014.

Refer to page 11 for additional detail on capital initiatives undertaken during in FY15.

The basic and diluted share counts used to determine Challenger's normalised and statutory EPS is based on requirements set out in Australian accounting standards. Under Australian accounting standards:

- the basic share count is reduced for treasury shares;
- the dilutive share count includes unvested equity awards made to employees under the Challenger Performance Plan Trust; and
- the dilutive share count considers convertible instruments (e.g. Challenger Capital Notes – refer to page 11 for more detail), with inclusion in the dilutive share count determined by a probability of vesting test.

### Treasury shares

The Challenger Performance Plan (CPP) Trust was established to purchase shares to satisfy Challenger's employee equity obligations arising from hurdled and non-hurdled equity awards issued under employee remuneration structures. Shares are acquired by the CPP Trust to mitigate shareholder dilution and to provide a mechanism to hedge the cash cost of acquiring shares in the future to satisfy vested equity awards.

The CPP Trust typically acquires physical shares on market or via forward share purchase agreements entered into by Challenger. The use of forward share purchase agreements was implemented in FY13 to increase capital efficiency. Shares held by the CPP Trust are classified as treasury shares.

It is expected that should equity awards vest in the future, the CPP Trust will satisfy equity requirements via a combination of treasury shares and settlement of forward purchase agreements. As such, it is not anticipated that new Challenger shares will be issued to meet future vesting obligations of equity awards.

## Unvested equity awards

### Hurdled Performance Share Rights (HPSRs)

Challenger's approach to executive remuneration includes providing Long Term Incentive (LTI) awards to ensure alignment between key employees and shareholders. LTI awards are delivered as Hurdled Performance Share Rights (HPSRs), which vest over a five year period and are subject to meeting TSR performance hurdles before vesting.

### Deferred Performance Share Rights (DPSRs)

A portion of Short Term Incentive (STI) awards are deferred and vest over a three year period. The deferred STI is delivered as Deferred Performance Share Rights (DPSRs) and vesting is subject to continued employment.

### Challenger Capital Notes

In October 2014, Challenger issued Challenger Capital Notes to the value of \$345m, which are subordinated, unsecured convertible notes issued by Challenger Limited (refer to page 12 for more detail).

Under Australian accounting standards convertible debt is considered dilutive whenever the interest per ordinary share obtainable on conversion is less than the basic earnings per share. As such, for Challenger Capital Notes a test is required to be undertaken each reporting period to determine if they are included in the dilutive share count.

At 30 June 2015, Challenger Capital Notes have been considered under Australian accounting standards to be dilutive and have been included in Challenger's 30 June 2015 dilutive share count.

Challenger Capital Notes are convertible to ordinary shares at any time before May 2022 on the occurrence of certain events, and mandatorily convertible to ordinary shares thereafter, in both cases subject to meeting certain conditions. However, Challenger also retains the option to redeem or resell Challenger Capital Notes and has an outright option to redeem or resell on 25 May 2020 (both subject to certain conditions being met). If Challenger exercises its option to redeem or resell, there will be no conversion of Challenger Capital Notes to Challenger ordinary shares and subsequent dilution to existing shareholders.

## Normalised growth framework

### Life normalised cash operating earnings

Normalised cash operating earnings is Challenger's preferred profitability measure for the Life business, as it aims to reflect the underlying performance trends of the Life business.

The Life normalised cash operating earnings framework was introduced in June 2008 and has been applied consistently

since. The framework removes the impact of market and economic variables, which are generally non-cash and are a result of external market factors. The normalised profit framework is subject to a review performed by Ernst & Young each half year.

Life normalised cash operating earnings includes cash earnings plus normalised capital growth, but excludes investment experience (refer below).

<b>Cash earnings</b>	<p>Cash earnings represents investment yield, less interest expenses and distribution expenses.</p> <p><b>Investment yield</b> Represents the investment return on assets held to match annuities and the return on shareholder investment assets. Investment yield includes net rental income, dividends received, infrastructure distributions, accrued interest on fixed income and cash, and discounts/premiums on fixed income assets amortised on a straight line basis.</p> <p><b>Interest expense</b> Represents interest accrued at contracted rates to annuitants and Life subordinated debt holders and other debt holders.</p> <p><b>Distribution expenses</b> Represents payments made for the acquisition and management of Life products, including annuities and commissions to third party mortgage brokers on term funded residential mortgage assets (NIM).</p> <p><b>Other income</b> Other income includes revenue from Accurium and profits on Life Risk wholesale longevity and mortality transactions (refer to page 18).</p>
<b>Normalised capital growth</b>	<p>Normalised capital growth represents the expected capital growth for each asset class through the investment cycle and is based on Challenger's long term expected investment returns for each asset class.</p> <p>Normalised capital growth can be determined by multiplying the normalised capital growth assumption (see below) by each asset class average balance for the period (net of debt).</p> <p>Normalised capital growth assumptions for FY15 are as follows:</p> <ul style="list-style-type: none"> <li>• Fixed income and cash – negative 0.35% representing an allowance for credit defaults;</li> <li>• Property – 2.00%;</li> <li>• Infrastructure – 4.00%; and</li> <li>• Equity and alternative asset classes – 6.00% (reducing to 4.50% in FY16).</li> </ul> <p>Normalised capital growth assumptions have been set with reference to long term market growth rates and are reviewed regularly to ensure consistency with prevailing medium to long term market conditions.</p> <p>Commencing from 1 July 2015 (FY16), the assumed equities normalised growth assumption has been reduced from 6.0% per annum to 4.5% per annum to reflect lower expected returns. This includes both lower global economic growth expectations (i.e. lower equities risk premia) and the nature of Challenger's equities portfolios, which consists of both listed and unlisted equities.</p> <p>The lower equities normalised growth assumption has the impact of reducing Life's FY16 COE guidance by approximately \$13m (based on Life's closing FY15 equity investments of \$0.9bn).</p>

## Normalised profit framework


<b>Investment experience</b>	<p>Challenger Life is required by accounting standards to value all assets and liabilities supporting the Life business at fair value. This gives rise to fluctuating valuation movements on assets and liabilities being recognised in the profit and loss, particularly during periods of market volatility. As Challenger is generally a long-term holder of assets, due to them being held to match the term of life liabilities, Challenger takes a long-term view of the expected capital growth of the portfolio rather than focusing on short-term movements.</p> <p>Investment experience is a mechanism employed to remove the volatility arising from asset and liability valuation movements from Life business earnings so as to more accurately reflect the underlying performance of the Life business.</p> <p>The asset and liability valuation movements are reported as investment experience. These movements are generally non-cash, and by separating them from the Life business result, Life's reported earnings more closely represent the cash earnings of the business.</p> <p><b>Impact from economic variables</b></p> <p>Investment experience also includes the impact of changes in macroeconomic variables on the valuation of Life's assets and liabilities. Economic and actuarial assumption changes include changes to bond yields and inflation factors, expense assumptions, losses on new business and other factors applied in the valuation of life contract liabilities.</p> <p>Investment experience is calculated as the difference between actual investment gains/losses (both realised and unrealised) and the normalised capital growth plus any economic and actuarial assumption changes for the period.</p>
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## Glossary of terms

Terms	Definitions
Additional Tier 1 regulatory capital	High quality capital that provides a permanent and unrestricted commitment and is freely available to absorb losses.
Cash earnings (Life)	Investment yield and other income less interest and distribution expenses.
CET1 ratio	Common Equity Tier 1 regulatory capital divided by prescribed capital amount.
Common equity tier 1 regulatory capital	The highest quality capital comprising items such as paid-up ordinary shares and retained earnings. Common equity tier 1 capital is subject to certain regulatory adjustments including in respect of intangibles and adjusting policy liabilities.
Earnings per share	Net profit after tax divided by weighted average number of shares in the period.
Equity accounted profits (FM)	Challenger's share of Fidante Partners boutique investment manager pre-tax profits.
Distribution expenses (Life)	Payments made for the acquisition and management of annuities and other Life products.
Fidante Partners income (FM)	Distribution and administration fees from boutique investment managers.
Funds under management (FUM)	Total value of listed and unlisted funds/mandates managed by the Funds Management business.
Group cash	Cash available to Group excluding cash held by Challenger Life Company Ltd.
Interest and borrowing costs (Corporate)	Interest and borrowing costs associated with group debt and group debt facilities.
Interest expenses (Life)	Interest accrued and paid to annuitants, subordinated debt note holders and other debt providers.
Investment experience (Life)	The difference between actual investment gains/losses (both unrealised and realised) and the normalised capital growth plus any economic and actuarial assumption changes for the period.
Investment yield (Life)	Net rental income, dividends received and accrued interest and discounts/premiums on fixed income securities amortised on a straight line basis.
Investment yield – shareholder funds (Life)	Represents the return on shareholder capital held by the Life business.
Life investment assets	Total value of investment assets that are managed by the Life business.
Life net book growth	Life net retail annuity policy capital receipts over the period divided by the opening Life retail annuity book.
Life net retail annuity policy receipts	Life retail annuity sales less retail annuity capital payments.
Net assets – average (Group)	Average net assets over the period (excluding non-controlling interests) calculated on a monthly basis.
Net fee income (FM)	Fidante Partners income, equity accounted profits (FM) and Challenger Investment Partners net management fees and performance and transaction fees.
Net management fees (FM)	Management fees for managing investments.
Net tangible assets	Consolidated net assets less goodwill and intangibles.
Net Interest Margin (NIM)	Net interest margin on term funded prime mortgages and included as part of Life's investment assets.
Normalised capital growth	Long term expected capital growth based on long term return assumptions calculated as long term capital growth assumption multiplied by average investment assets.
Normalised Cash Operating Earnings (NCOE) (Life)	Cash earnings plus normalised capital growth.

## Glossary of terms

Terms	Definitions
Normalised cost to income ratio	Total expenses divided by total net income.
Normalised dividend payout ratio	Dividend per share divided by normalised earnings per share (basic).
Normalised EBIT (Life)	Normalised cash operating earnings less total Life expenses.
Normalised EBIT (FM)	Net income less total FM expenses.
Normalised effective tax rate	Normalised tax divided by normalised profit before tax.
Normalised Return on Equity (RoE) – pre-tax	Normalised Life EBIT, FM EBIT or Normalised NPBT (Group) divided by average net assets.
Normalised Return on Equity (RoE) – post-tax	Group's normalised NPAT divided by average net assets.
Other expenses	Non-employee expenses, including external professional services, occupancy costs, marketing and advertising, travel, technology and communications costs.
Other income (Corporate)	Includes equity accounted profits of associates and interest received on Group cash balances.
Other income (Life)	Relates to Accurium revenue and Life Risk. Refer to page 14 for more detail.
Performance and transaction fees (FM)	Fees earned for outperforming benchmarks and fees earned for the origination, disposal and restructuring of assets.
Personnel expenses	Includes fixed and short term variable incentive components of remuneration structures. The amortisation of long term incentive plans is reported separately within the Corporate results.
PCA ratio	The ratio of the total CLC tier 1 and tier 2 regulatory capital base divided by the prescribed capital amount.
Prescribed capital amount (PCA)	Amount of capital that a life company must hold which is intended to be sufficient to withstand a 1 in 200 year shock and still meet adjusted policy liabilities and other liabilities. For further details refer to APRA's LPS110 Capital Adequacy.
Product cash margin (Life)	Represents the return on assets backing annuities and other income, less interest and distribution expenses.
Significant items	Non-recurring or abnormal income or expense items.
Statutory Return on Equity (RoE) – post-tax	Statutory NPAT divided by average net assets.
Tier 1 regulatory capital	Tier 1 regulatory capital comprises common equity tier 1 regulatory capital and additional tier 1 regulatory capital.
Tier 2 regulatory capital	Tier 2 Capital is capital that contributes to the overall strength of a life company and its capacity to absorb losses but does not satisfy all the criteria to be included as Tier 1 regulatory capital.
Total expenses	Personnel expenses plus other expenses.
Total net income	Normalised Cash Operating Earnings (Life) plus net fee income (FM) plus other income (Corporate).



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