2021 Annual Report

Providing our customers with financial security for a better retirement

challenger.com.au

Challenger Limited ACN 106 842 371

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Key dates

22 September 2021
Final dividend payment date

28 October 2021
2021 Annual General Meeting

17 February 2022
Half year financial results

22 March 2022
Interim dividend payment date

16 August 2022
Full year financial results

21 September 2022
Final dividend payment date

27 October 2022
2022 Annual General Meeting

Full listing of key dates available at:

> **challenger.com.au/shareholder/shareholder-information/key-dates**

Dates may be subject to change. Any change in dates will be advised to the Australian Securities Exchange.

About this Annual Report

The 2021 Annual Report, including the financial report for the year ended 30 June 2021, can be downloaded from Challenger's online Shareholder Centre at:

> **challenger.com.au/shareholder**

2021 Annual Review

The 2021 Annual Review is intended to provide you with useful information about your company in an easy-to-read document. Included in the Annual Review is an operational and financial performance update, reports from the Chair and the Chief Executive Officer, and information on the environmental, social and governance matters that affect your company.
The Annual Review can be viewed online at:

> **challenger.com.au/annualreview2021**

2021 Corporate Governance Statement

The 2021 Corporate Governance Statement can be viewed online at:

> **challenger.com.au/corporategovernance2021**

2021 Sustainability Report

The 2021 Sustainability Report can be viewed online at:

> **challenger.com.au/sustainabilityreport2021**

2021 Annual General Meeting

Location
To be determined and subject to COVID-19 pandemic requirements.

Date
28 October 2021

Time
9.30am (Sydney time)

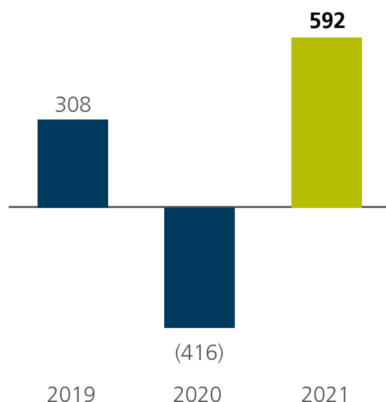
Full details of the meeting will be included in your Notice of Annual General Meeting, which will be sent to shareholders in September 2021.

Board nominations
The closing date for receipt of nominations for the Challenger Limited Board is 25 August 2021.

Group performance highlights

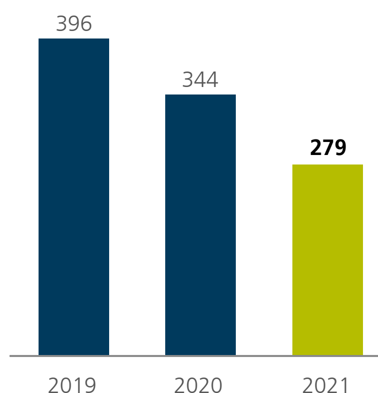
Statutory net profit/(loss) after tax ($m)

Normalised net profit after tax and investment gains on Life's investment portfolio



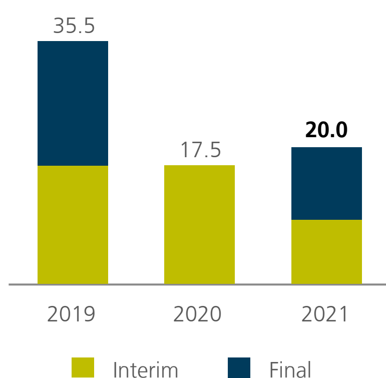
Normalised net profit after tax ($m)

Reflects more defensive portfolio settings and higher levels of capital



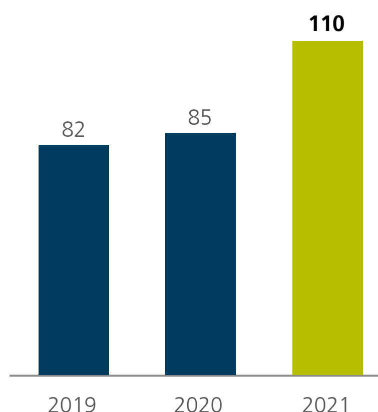
Dividend (cps)

20.0 cps fully franked
48% of normalised earnings paid



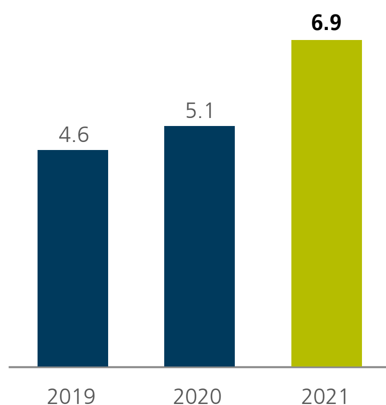
Group assets under management ($bn)

Strong growth across both Life and Funds Management



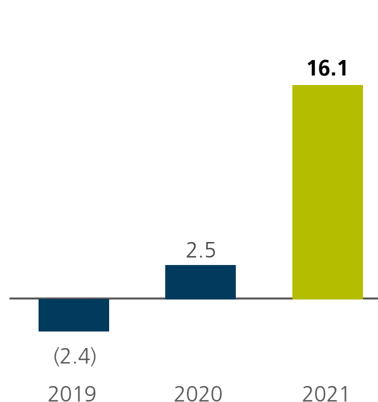
Life sales ($bn)

Sales up 35% on 2020
Strong contribution from institutional sales



Funds Management net flows ($bn)

Diversified client base and product offering
Record net flows and FUM growth



Operating and financial review

1 About Challenger

Challenger Limited (Challenger, CGF, the Group or the Company) was founded in 1985 and is Australia's largest annuity provider[1] as well as one of its largest[2] active fund managers.

Challenger is listed on the Australian Securities Exchange (ASX) and has offices in Australia, London, Singapore and Tokyo. At 30 June 2021, Challenger employed 738 people on a full-time equivalent (FTE) basis.

Challenger is regulated by the Australian Prudential Regulation Authority (APRA), the Australian banking, superannuation and insurance regulator. Challenger's activities are also subject to supervision by other regulatory agencies both in Australia and the other offshore markets in which it operates.

Challenger's assets under management (AUM) were $110.0 billion, increasing by 29.1% for the year ended 30 June 2021 (30 June 2020: $85.2 billion).

Normalised net profit before tax (NPBT) for the year was $395.8 million, decreasing by $110.7 million or 21.9% (30 June 2020: $506.5 million). Sections 2 and 8 contain a description of Challenger's operating segments and its normalised cash operating earnings (NCOE) framework.

Normalised net profit after tax (NPAT) was $278.5 million, decreasing by $65.2 million or 19.0% for the year (30 June 2020: $343.7 million).

Statutory net profit after tax was $592.3 million, which includes investment experience, being the valuation movements on assets and liabilities supporting the Life business, and increased by $1,008.3 million for the year (30 June 2020: loss of $416.0 million).

Challenger's total equity as at 30 June 2021 was $3.8 billion (30 June 2020: $3.2 billion).

2 Operating segments and principal activities

Challenger's purpose is to provide customers with financial security for a better retirement. To fulfil this purpose, Challenger leverages capabilities across its two operating segments, Life and Funds Management. These core operating segments are supported by shared support functions which are responsible for providing centralised regulatory, compliance, financial reporting, legal, risk management and human resources.

Life — the Life operating segment focuses on the retirement spending phase of superannuation, providing products that help customers convert retirement savings into safe and secure income in retirement. The Life segment includes Challenger Life Company Limited (CLC), an APRA-regulated life insurance company and is Australia's leading provider of annuities and guaranteed retirement income products.

As Australia's leading provider of annuities, Life is expected to benefit from the long-term growth in Australia's superannuation system and regulatory reforms designed to enhance the retirement phase.

The purpose of the superannuation system is to provide income in retirement to substitute or supplement the Government-funded age pension. With the transition from Government-funded age pensions to private pensions, retirees are seeking retirement income products that convert savings into regular and secure income, helping to provide financial security in retirement.

Life has been recognised as a retirement income product innovator and has won the Association of Financial Advisers 'Annuity Provider of the Year' for the last 13 years, and is the dominant retirement income brand in Australia.

Life is also focused on building institutional partnerships in the profit-for-member sector of the superannuation system, which is growing strongly. As their members transition to retirement, profit-for-member funds are increasing their focus on providing more comprehensive retirement solutions. As the retirement system develops, the profit-for-member sector provides a significant growth opportunity.

Life has an annuity relationship with Mitsui Sumitomo Primary Life Insurance Company Limited (MS Primary), a leading provider of Australian dollar and US dollar annuities in Japan. MS Primary is part of MS&AD Insurance Group Holdings Inc. (the MS&AD Group).

The retirement incomes which Life pays are backed by a high-quality investment portfolio, predominantly invested in fixed income and commercial property investments. These long-term investments generate regular and predictable investment income streams which are used to fund retirement income payments to Life's customers.

Funds Management — the Funds Management segment focuses on accumulating wealth for retirement. As people work and save for retirement, Funds Management supports them building their retirement savings by providing investment strategies that seek to deliver superior investment returns.

Funds Management is Australia's third largest active fund manager[2] and is diversified globally with operations in Europe, Japan and Singapore.

The Funds Management operating segment comprises two business divisions: Fidante Partners and CIP Asset Management (CIPAM).

Fidante Partners invests in minority equity interests in individually branded boutique investment management firms. Fidante Partners provides distribution, administration and business support services to the boutique investment managers and shares in the profits of these businesses through equity ownership.

Fidante Partners' business model has allowed it to attract and build successful active equity, active fixed income and alternative investment managers, which deliver strong investment performance.

CIPAM principally originates and manages fixed income and commercial real estate, along with providing investment solutions for leading global and Australian institutions, including CLC.

[1] Plan for Life – March 2021 – based on annuities under administration.
[2] Consolidated FUM for Australian Fund Managers – Rainmaker Roundup, March 2021.

2 Operating segments and principal activities (continued)

Principal activities – there have been no significant changes in the nature of these principal activities or the state of affairs of the Company during the year.

In December 2020, Challenger announced the acquisition of MyLifeMyFinance Limited (MyLife MyFinance, the Bank), an Australian-based customer digital bank, for $35.0 million. The acquisition price is subject to a completion adjustment and is based on a net asset value of $18.0 million. The acquisition received formal approval from the Treasurer of the Commonwealth of Australia on 29 July 2021 and was completed on 30 July 2021. The acquisition is highly strategic and provides Challenger the opportunity to significantly expand its secure retirement income offering, including entering Australia's term deposit market. In the 2022 financial year, the Bank will represent a third operating segment of the Group.

3 Challenger’s purpose and strategic priorities

Challenger’s purpose is to provide customers with financial security for a better retirement.

In June 2021, Challenger announced a refreshed corporate strategy that builds on the foundations of the core strategic pillars that have been in place for many years.

The refreshed strategy will make Challenger stronger and more relevant for the future as the Company seeks to further expand offerings for retirees, including more direct acquisition of customers.

Providing customers with financial security for a better retirement remains Challenger’s purpose, which will be served by providing both guaranteed income products such as lifetime annuities and term deposits, as well as non-guaranteed funds management products that help people save for retirement.

Challenger has also introduced explicit vision statements for each key stakeholder group: customers, shareholders, employees, and the community, to help clarify Challenger’s objectives and long-term ambitions.

Challenger has four strategic priorities to ensure that it achieves its purpose of providing customers with financial security for a better retirement.

The four strategic priorities are to:

- broaden customer access across multiple channels;
- expand the range of financial products and services for a better retirement;
- leverage the combined capabilities of the Group; and
- strengthen resilience and sustainability of Challenger.

4 Risk management

The management of risk is fundamental to Challenger’s business and to building long-term shareholder value. The Board’s Risk Appetite Statement outlines the level of risk that is acceptable and is combined with an effective risk management framework which monitors, mitigates and manages the risks to which Challenger is exposed.

The Board recognises the broad range of risks that Challenger faces as a participant in the financial services industry. These include:

- funding and liquidity risk;
- investment and pricing risk;
- counterparty risk;
- strategic, business and reputation risk;
- operational risk;
- climate change risk;
- conduct risk; and
- licence and regulatory risk.

An integral part of risk management for Challenger is the maintenance of a strong risk culture amongst its employees. Challenger’s expectations of its employees are encapsulated in the ‘Challenger I ACT’ values of:

- Act with integrity;
- Aim high;
- Collaborate; and
- Think customer.

All employees are assessed against the Challenger I ACT values as part of the annual performance review process, and this outcome contributes to their overall performance rating and individual remuneration outcomes.

5 Challenger's 2021 strategic progress

2021 strategic progress

Progress in 2021 against our strategic priorities is set out below:

Increase the use of secure retirement income streams

Challenger is focused on growing the allocation of Australian retirement savings to secure and stable incomes.

2021 progress

Strategy to diversify sales delivering – Life sales up 35% to $6.9 billion

Challenger is building more resilient sales by diversifying across a range of retail and institutional products and clients.

In 2021, sales increased across all key Life product categories, including domestic retail annuities (up 19%), institutional annuities and Index Plus (up 53%) and Japanese annuities (up 6%).

Total Life sales increased by 35% and are benefiting from Challenger's diversification strategy, which includes:

- increasing focus on institutional sales;
- working with a wider range of independent financial advice networks following structural change in the domestic financial advice market; and
- expansion of the annuity relationship with MS Primary in Japan and expanding the relationship to include the reinsurance of US dollar-denominated annuities.

Stabilisation of structural change to Australian financial advice market

Life has traditionally relied upon third-party financial advisers, both independent and part of major advice hubs, to distribute its products. The Australian wealth management and financial adviser markets have been significantly disrupted following public hearings and completion of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Royal Commission) in 2019.

These industry changes impacted Challenger's annuity sales, particularly term annuity sales, which had been well supported by advisers aligned to the wealth management operations of major banks.

With adviser movement from major banks to Independent Financial Adviser (IFA) networks and advisers exiting the industry stabilising over the last 12 months, the scope for further impact on Challenger's domestic retail term sales has reduced.

The contribution to Challenger term annuity sales by major banks has stabilised and accounted for approximately 9% of 2021 domestic fixed term annuity sales, which was consistent with the contribution in 2020 (approximately 12%).

Sales disruption from COVID-19 pandemic

Since March 2020, the COVID-19 pandemic has impacted the ability of financial advisers to meet new clients, and their focus has been on servicing their existing client base, rather than on-boarding new clients. New clients on-boarded at the point of retirement represent an opportunity to recommend annuities, particularly lifetime and aged care-focused annuities. Despite this, retail lifetime annuity sales increased by 6% in 2021.

The COVID-19 pandemic has also delayed retirees entering aged care. Despite this, CarePlus sales were up 11% on 2021.

Extending customer reach and entering Australia's term deposit market

In December 2020, Challenger announced the acquisition of MyLifeMyFinance Limited (MyLife MyFinance), an Australian-based customer digital bank, for $35 million[1]. The acquisition received formal approval from the Treasurer of the Commonwealth of Australia and was completed in July 2021.

The acquisition is highly strategic and provides Challenger the opportunity to expand its secure retirement income offering, including entering Australia's term deposit market.

Adding an Authorised Deposit-Taking Institution capability to sit alongside the Life and Funds Management businesses will both broaden Challenger's product and distribution reach and help fulfil Challenger's vision to provide customers with financial security for a better retirement.

[1] Acquisition price subject to completion adjustments and based on a net asset value of $18 million.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Increase the use of secure retirement income streams (continued)

Extending customer reach and entering Australia's term deposit market (continued)

Term deposits are Government guaranteed[2] and a familiar product amongst both retirees and those approaching retirement, and they form a significant portion of their wealth allocation.

The acquisition also provides Challenger the opportunity to attract and engage with customers at an earlier age as they approach and enter the retirement phase, increasing Challenger's brand recognition in early age demographics.

Lead the retirement incomes market and be the partner of choice

Challenger's strategy includes being the partner of choice for superannuation fund advisers, wealth managers and investment platforms in providing retirement income solutions. Challenger has deep expertise in retirement income, including knowledge of the regulatory landscape and significant experience and track record in managing the financial risks that retirees face. Challenger is the market leader in annuities with 80%[3] market share.

2021 progress

Annuity provider of the year

Life is a market leader in Australian retirement incomes and won the Association of Financial Advisers Overall Annuity Provider of the Year and Long Term Income Stream of the Year. Life was also the winner of Plan For Life's Overall Longevity Cover Excellence Award for 2020, which recognises Australian life insurance companies and fund managers who design products to assist retirees in meeting the challenges of rising longevity.

Building institutional partnerships

Challenger is focused on providing institutional investors with targeted solutions that help address their strategic and fiduciary objectives. Challenger does this by offering innovative strategies catering to the needs of superannuation funds, insurance companies and multi-managers.

Challenger's institutional offering provides institutional clients with access to Challenger Life's capabilities, including:

- investment and structuring skills;
- asset and liability management; and
- intellectual property and thought leadership, especially around retirement income.

Challenger's institutional approach is solutions led and an enabler providing components to client solutions, helping them build more comprehensive retirement solutions.

Challenger Life's institutional business (annuities and other institutional products) continues to grow strongly and increased by 81% in 2021, and has increased by 32% Compound Annual Growth Rate (CAGR) over the past four years.

Sales are benefiting from an expansion in the institutional product offering, including introducing institutional term annuities, and an increase in the institutional client base. The number of institutional clients has more than doubled over the past five years, and covers profit-for-member funds, insurance companies and multi-managers.

With the low interest rate environment, Challenger's institutional clients are focused on diversifying their investment returns. Significant growth in institutional term annuity sales was achieved in 2021, which accounted for 36% of annuity sales, up from 19% in 2020.

Total institutional sales (annuities and other institutional products) was $4.0 billion in 2021, representing 58% of total Life sales.

The focus on more comprehensive solutions, including using guaranteed income products by profit-for-member funds, represents a significant growth opportunity for Challenger.

Superannuation fund clients are increasing their focus on providing retirement income solutions for their members and are engaging with Challenger on the support it can provide to help them build more comprehensive retirement solutions for their members. The Retirement Income Covenant is also increasing superannuation funds' focus on providing their members with products that provide longevity risk protection.

[2] The Financial Claims Scheme provides protection to depositors of up to $250,000 per account holder per authorised deposit-taking institution (ADI).

[3] Plan For Life – March 2021 – based on annuities under administration at 30 March 2021.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Lead the retirement incomes market and be the partner of choice (continued)

Enhanced customer digital engagement through Challenger Investor Online

Challenger is committed to providing a high-quality service and experience for its customers.

In 2021, Challenger's online customer portal was enhanced to provide an improved customer experience and increased security.

The enhancements also drive efficiencies by transitioning customers from paper processes to digital engagement, and provide a range of new features, including online self-service. The enhancements also increased security, including introducing two-factor authentication.

Leading adviser ratings

Despite structural changes in the Australian financial advice market and new competitors entering the retirement incomes market, Challenger has remained the dominant retirement income brand.

Among Australian financial advisers, Challenger continues to be the most recognised retirement income provider, with 90%[4] of financial advisers rating Challenger as a leader in retirement income. Challenger's retirement income leadership position, which supports new distribution and product relationships, is 35 percentage points above its nearest competitor.

Excellent customer experience

Challenger has a reputation for excellent customer experience demonstrated by Challenger's Net Promoter Score of 35%[5], up from 22% in 2020. Overall client satisfaction was 91%, with 67% of customers very satisfied and 24% somewhat satisfied. Customer satisfaction scores were broadly consistent across all product types and distribution channels (advised vs non-advised).

When surveying customer experience with Challenger compared to other financial institutions, 60% rated it better and 38% rated it the same as other companies[5].

The Customer Satisfaction and Advocacy research[5] also shows 90% of customers agree that Challenger products provide them with confidence in retirement and 87% agree that Challenger is a trustworthy company.

Retirement Essentials Age Pension Concierge Service pilot

Challenger trialled a Retirement Essentials Age Pension Concierge Service, aimed at helping to simplify the process of applying for the age pension. Retirement Essentials is a specialist provider of age pension eligibility and entitlements tools, which were made available to advisers to help cut Centrelink red tape and improve the client experience.

The objective for Challenger was to drive increased adviser engagement and sales of lifetime annuities through its retirement income leadership position. The pilot resulted in an increase in lifetime sales and engagement with advisers focused on retirement issues, including accessing the age pension for clients.

Enhanced online origination process

Challenger has enhanced its online origination process to improve the digital experience for its customers. A range of manual and paper-based processes have been replaced with editable PDFs, digital signatures and other automated processes. The enhanced online origination process led to:

- 69% improvement in turnaround time from quote to application;
- 100% improvement in the take-up of online ID and verification; and
- 25% reduction in rework on eSignature applications.

Adviser referral program

Changes in the advice landscape continue to impact customers, who are looking for a closer relationship with Challenger as a retirement expert. Customers want information about changes that impact retirees and are concerned about how to find a new adviser. Challenger has implemented an Adviser Referral program, referring new and existing customers who do not have a financial adviser, to an external panel of advisers who have experience in retirement planning and income advice. This program has assisted customers with a referral to an accredited Financial Planner.

[4] Marketing Pulse Adviser Study, December 2020.
[5] Fifth Quadrant, February 2021.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Provide customers with excellent funds management solutions

Challenger is focused on providing excellent funds management solutions in order to help people build their wealth and savings for retirement.

2021 progress

Distributor of the year

In 2021, Funds Management is one of the fastest growing[6] Australian active investment managers, attracting net inflows of $16 billion, representing 20% of opening period FUM.

FUM growth is benefiting from a diverse range of boutique managers covering key asset classes and high-quality retail and institutional sales teams. In 2021, FUM increased in all but one of Fidante Partners' boutiques. Four boutiques finished 2021 with FUM exceeding $10 billion, up from one boutique in 2020.

Fidante Partners' distribution capability continues to be externally recognised and in 2021 won Distributor of the Year at the annual Zenith Investment Partners (Zenith) Fund Awards. Zenith recognised Fidante Partners' sales teams and broad distribution footprint.

Top ranking wholesale trust for inflows

Fidante ranked as the top Australian active manager for retail net flows in 2021 with the highest net flows among 117 active managers[6]. Fidante Partners also ranked number one for retail flows in both fixed income and equities.

The Ardea Real Outcome Fund achieved the highest inflows of any wholesale investment trust in the entire Australian market for the second consecutive year[7] and is the fastest growing Active Exchange Traded Fund (ETF) in Australia[8]. The Ardea Real Outcome Fund also received its highest conviction rating in retail with Lonsec upgrading it to Highly Recommended.

Adding new boutiques and investment strategies

Fidante Partners continues to expand its product offering by developing new investment strategies for existing managers, adding new boutiques and forming partnerships with best-in-class investment managers.

New products for existing managers

Ardea Investment Management launched the Ardea Global Alpha Fund, a relative value fixed income fund investing in a global portfolio of high-quality government bonds and related derivatives. The fund is an Undertakings for the Collective Investment in Transferable Securities (UCITS) compliant version of the Ardea Real Outcome Fund which is one of the fastest growing fixed income strategies in Australia and provides a platform for offshore investors to access a strategy that has been very popular with Australian investors. The fund will be distributed across the United Kingdom and select European markets and will be among a number of products available for Southeast Asian distribution.

In November 2020, Ares Australia Management launched its second product - the Ares Diversified Credit Fund (ADCF), which offers investors direct access to global private credit markets not readily accessible by Australian wholesale investors. In May 2021, the Ares Global Credit Income Fund received a recommended rating from Zenith Investment Partners.

Alphinity Investment Management launched a new Global Sustainable Equity Fund. The fund aims to invest in quality global companies that are supporting a transition to a more sustainable future and are also identified as undervalued and within an earnings upgrade cycle. A Sustainable Advisory Compliance Committee, including two recognised independent ESG experts, will provide specialist insights and ensure the Fund remains 'true to label' and aligned with the fund's Charter.

New boutiques

Fidante Partners has an active program of seeking and screening potential new boutique managers. In 2021, Fidante Partners announced the launch of a new emerging market boutique manager, Ox Capital Management.

Ox Capital Management brings together a team of highly experienced portfolio managers and analysts with extensive experience investing in Asia and other dynamic emerging markets. Ox Capital Management will launch a long-only and a long-short emerging market equity fund in 2022.

[6] Plan For Life Wholesale Trust Data, September 2020, December 2020 and March 2021.
[7] Plan For Life Wholesale Trust Data, September 2020.
[8] ASX Investment Products monthly update July-June 2021, inflows/outflows.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Provide customers with excellent funds management solutions (continued)

New partnerships

In April 2021, Fidante Partners and global specialist asset manager Impax Asset Management Limited entered into a new partnership agreement, with Fidante Partners becoming Impax's exclusive distribution partner in Australia and New Zealand. Impax Asset Management Group is a global leader dedicated to investing in the transition to a more sustainable global economy.

Fidante Partners' European business partnered with Proterra Investment Partners, a leading private equity fund manager focused on the food and agribusiness sectors, providing European investors with access to Asia's food sector. Proterra Asia's Food Strategy invests across the entire food value chain in Asia, with a particular focus on the fast-growing and high return-oriented branded food sector.

Funds Management also entered into a distribution partnership agreement with the number one Japanese investment trust manager, Nomura Asset Management. Fidante Partners has been selected to distribute the Nomura Global Dynamic Bond Fund and Nomura Global Multi-Theme Equity Fund products in Australia and New Zealand on behalf of Nomura Asset Management.

CIP Asset Management fixed income product expansion

Challenger is Australia's largest fixed income manager, with Fidante Partners managing $41 billion and CIP Asset Management (CIPAM) fixed income franchise managing over $16 billion across multiple strategies, comprising both public and private credit investments.

CIPAM was formed over 20 years ago, with the business evolving from providing investment management for Challenger Life to managing money for institutional clients. Over the past four years, the business has expanded its offering to a wider group of investors, which include retail and high net worth clients. In 2020, it rebranded to CIP Asset Management as it increased its focus on retail investors.

Following this rebrand, CIPAM launched a retail version of the CIP Asset Management Credit Income Fund in October 2020, which is a floating rate, multi-sector credit strategy investing in public and private debt markets. The Fund aims to provide high net worth investors with capital stability and income on a regular basis accompanied by lower levels of volatility than traditional fixed income strategies. The fund also received its first retail research ratings, a Recommend rating from both Zenith Investment Partners and Lonsec.

In December 2020, CIPAM launched its third income-oriented fund and attracted external seeding. The CIPAM Private Lending Opportunities Fund is a higher returning fund open to institutional investors, focusing on floating rate investments in mezzanine private lending opportunities, primarily within Australia and New Zealand.

In May 2021, CIPAM launched a new wholesale share class of its flagship Multi Sector Private Lending Fund, providing the opportunity for wholesale/sophisticated individual investors to access the offering. The fund was launched in February 2020 and is a multi-sector credit strategy investing in Australian and New Zealand private securitised, corporate and real estate lending.

In addition to a range of institutional client mandates, CIPAM now has three income focused credit funds that provide investors with a range of return and risk options, ranging from cash plus three percent (credit income fund) per annum, cash plus five percent (multi asset fund) per annum and cash plus eight percent (private lending opportunities fund) per annum.

Diversifying globally

Funds Management continues to see significant growth opportunities in Australia and recognises the opportunity to diversify globally. Distribution efforts over the past few years are now showing great momentum and are expected to support future net flows.

Funds Management has been selectively expanding offshore and is focusing on markets where it has the right product, there is the right market structure and where it can build the right sales capability. After selectively expanding into the European and Japanese markets through our presence in London and Tokyo, Challenger opened an office in Singapore in May 2021. The Singapore office will provide a distribution hub to access investors across Asia.

In Europe, Fidante Partners 2021 sales remained robust despite the disruption from the pandemic on European sales activity. A range of investment strategies have been successful and are attracting new customers. More recently, Fidante Partners won its first major multi-geography (Australia and UK) mandate win of over A$1 billion, which will be funded in 2022.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Provide customers with excellent funds management solutions (continued)

In Japan, CIPAM won its first mandate to manage Japanese real estate for a third-party client, investing in a diverse portfolio of real estate assets across Japan.

Maintaining superior investment performance

Funds Management has a long track record of achieving superior investment performance, which has helped attract strong net flows over many years.

Long-term investment performance for Fidante Partners Australian boutiques remains very strong with 92% of FUM outperforming benchmark over three years and 96% over five years[9]. Since fund inception, 84% of Fidante Partners' funds have achieved either first or second quartile investment performance[10].

Award-winning investment strategies

Fidante Partners' investment managers continue to be externally recognised. During 2021, the following funds won investment manager awards:

- Greencape Capital – Zenith Fund Awards - Australian Equities - Large Cap (2020);
- Alphinity's Sustainable Share Fund – Money magazine Best of the Best Awards - Best Australian Share ESG Fund (2021);
- Eiger Australian Small Companies Fund – Money Management 2021 FMOTY Awards – Emerging Manager;
- Greencape Broadcap Fund – Financial Standard Investment Leadership Awards – Australian Equities Active Core (2021);
- Ardea Investment Management – Zenith Fund Awards - Global and Diversified Fixed Interest (2020); and
- Alphinity Sustainable Share Fund, Greencape Broadcap Fund, Greencape High Conviction Fund – Canstar 2021 Managed Fund Star Ratings and Awards Australian Shares Large Cap (funds that invest in domestic stocks which are in the top 70% of the stock market by value).

In addition to these investment manager awards, Fidante Partners was awarded the Zenith Distributor of the Year award 2020. This award recognises the quality of investment managers as well as the operating and distribution platform which supports them.

Highly rated retail investment products

Fidante Partners' investment managers and funds are highly rated by external asset consultants:

- 35% of ratings are the top rating (e.g. 'Highly Recommended' or 'Gold') compared to an average of approximately 12% across the Australian funds management industry; and
- 80% of ratings are a 'buy' rating compared to an average of approximately 73% across the Australian funds management industry.

The quality and performance of Fidante Partners' investment managers and funds continue to receive strong independent validation. At 30 June 2021, Zenith rated 20 out of the 24 ratings awarded to Fidante Partners' funds as either Recommended or Highly Recommended.

In addition to the retention of a number of ratings, there were a number funds that received rating upgrades from primary research houses. These included two 'Highly Recommended' (from 'Recommended') by Lonsec, one 'Highly Recommended' (from 'Recommended') by Zenith and one to Bronze by Morningstar[11]. There were also eight first time ratings, of which six were 'buys' across ActiveX, Alphinity, Ares Australia Management, CIPAM and Whitehelm managers.

Embedding ESG across the Funds Management platform

Principles for Responsible Investment (UNPRI) is a United Nations-supported international network of investors working together to implement its six aspirational principles. Its goal is to understand the implications of sustainability for investors and support signatories to facilitate incorporating these issues into their investment decision-making and ownership practices.

[9] As at 30 June 2021. Percentage of Fidante Partners Australian boutiques meeting or exceeding performance benchmark.

[10] Mercer as at June 2021.

[11] Ardea Real Outcome Fund and Lennox Microcap Fund both upgraded to Highly Recommended by Lonsec and Lennox Small Companies Fund upgraded to Bronze by Morningstar.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Provide customers with excellent funds management solutions (continued)

Embedding ESG across Funds Management's platform (continued)

Reflecting Challenger's commitment to sustainable investing, Funds Management established a Responsible Investment Committee during the year. In the Principles for Responsible Investment Assessment Report 2020, Challenger received an "A" rating.

In 2021, Challenger continued to develop its ESG practices and supported Fidante Partners to embed ESG practices within their boutique fund managers. All boutiques have developed their own standalone ESG policies and are now signatories to the UNPRI.

Within Fidante Partners' boutiques, Alphinity launched a Global Sustainable Share Fund, and Whitehelm Listed Core Infrastructure Fund rebranded as Low Carbon Infrastructure Fund to better represent their ESG approach.

Maintain leading operational and people practices

Challenger believes maintaining a highly engaged, diverse and agile workforce committed to sustainable business practices with a strong risk and compliance culture is essential for providing customers and shareholders with superior outcomes.

2021 progress

High employee engagement and strong risk culture

Employee engagement measures the strength of the relationship between an organisation and its employees. Challenger believes having a highly engaged team that is inspired by its business purpose and its values will lead to superior customer and shareholder outcomes.

Challenger's employee engagement survey conducted by Willis Towers Watson in April 2021 showed that despite the COVID-19 pandemic and shift to work from home, Challenger has maintained high employee engagement achieving an overall sustainable engagement score of 85%. This was 1% higher than Challenger's 2019 result and in line with the global high performing norm.

Challenger has a strong risk culture, which was reflected in a risk culture score of 86% in the latest employee engagement score. The score was four points above the Global High Performing Norm, and 10% higher than the Australian National Norm. The consistently high risk culture result confirms risk culture is embedded right across the business.

Diversity and inclusion

Challenger believes that a diverse and inclusive workplace delivers better outcomes for employees, the business and the community.

Challenger continued to make progress implementing its Diversity and Inclusion strategy and achieved a Diversity and Inclusion score of 94% in the annual employee engagement survey. This was 11 points above the Australian National Norm and 12 points above the Global High Performing Norm. In addition:

- 98% of employees believe gender-based harassment and sexual harassment is not tolerated;
- 95% of employees believe we have a working environment that is accepting of differences in personal identity; and
- 94% of employees have the flexibility they need to manage their work and other commitments.

During 2021, Challenger continued to be recognised as an employer of choice for women, and was included in:

- Workplace Gender Equality Agency (WGEA) Employer of Choice for Gender Equality;
- Equileap Global Top 100 employer for gender equality; and
- The Bloomberg Global Gender Equality Index.

Challenger also joined the Pride in Diversity network – a leading not-for-profit support program providing inclusion strategies for LGBTQI+ persons, and submitted responses to the Australian Workplace Equality Index's annual questionnaire on how supported LGBTQI+ persons feel at work.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Maintain leading operational and people practices (continued)

Refreshing approach to sustainability

Challenger evolved its sustainability strategy in 2021 to reflect Challenger's most material social, environmental and governance opportunities and align it to its purpose.

With focus on responsible investment across stakeholder groups increasing, Challenger's updated sustainability strategy reflects a strengthened focus on responsible investing.

Challenger's sustainability strategy focuses on:

- Financially resilient customers and communities;
- Constructive public policy settings;
- Doing things right; and
- Responsible investment.

To support the implementation of Challenger's sustainability strategy, a group-wide ESG steering committee has been established. The committee includes representatives from across the business that meet regularly to assess and progress ESG related initiatives. The committee also provide updates and recommendations to the Challenger Board.

Health and wellbeing of our people during the COVID-19 pandemic

Looking after the health of employees during the COVID-19 pandemic is a key business priority. Prior to the COVID-19 pandemic, Challenger had strong flexible work foundations. During the pandemic this was accelerated with almost 100% of employees moving to remote work. Business continuity has been maintained throughout the pandemic.

Challenger recognises that the way employees work has changed forever, and organisations need to adapt to leverage the benefits. Challenger is promoting and supporting a hybrid work model that supports employee engagement and delivers on Challenger's organisational strategy. Challenger is supporting leaders and employees to introduce new ways of working that balance the needs of the team, organisation and individuals, providing an opportunity to build an even more diverse and inclusive workplace.

To support hybrid work, Challenger has adopted cloud-based collaboration tools and rolled out new laptops to employees. A Future of Work Group has been formed to work with employees to constantly evolve Challenger's work practices.

Community partnership with the Council on the Ageing NSW (COTA)

Challenger's partnership with COTA was established in 2019 to deliver a program of research, advice and practical support to address the underemployment of people over 50. The program aims to encourage people to talk about ways to tackle perceptions and misconceptions around older workers. This includes giving employers the tools to attract and retain older employees.

Enabling people to work for as long as they wish provides a range of benefits for individuals and the economy and aligns strongly with Challenger's purpose of helping provide financial security for a better retirement.

In 2021, working alongside both COTA and Newgate Research, Challenger published its first piece of research on understanding the needs of older workers and how businesses can enhance their workplaces for older Australians.

Based on insights of this research, a program and toolkit are being designed, covering:

- Education and advice for hiring managers;
- Support for auditing existing programs and policies, and building new ones to promote age diversity;
- Advice on fostering connections between age diverse groups at work; and
- Developing training programs to deliver equal access to upskilling and training opportunities.

Launched a mental health and wellbeing strategy

Challenger is committed to maintaining a positive and inclusive workplace culture where everyone feels safe and encouraged to talk about mental health and reach out for support when needed. In these unprecedented times, providing a supportive and caring environment has never been more important. Guiding Challenger's approach are three core areas:

- Improving understanding of mental health and combating stigma;
- Promoting positive health and wellbeing; and
- Increasing awareness and support for impacted employees.

5 Challenger's 2021 strategic progress (continued)

2021 strategic progress (continued)

Maintain leading operational and people practices (continued)

Commitment to effective climate change management

Challenger recognises climate change is one of the biggest challenges facing society now and for future generations. It is a shared global challenge that requires input from governments, businesses and individuals.

Challenger is committed to supporting progress in transitioning to a low carbon economy. This year, Challenger published its first climate change statement outlining its overall approach to climate change and how it considers climate-related risks and opportunities. This includes working with internal and external stakeholders to find ways to reduce risk and create a more resilient economy.

Challenger's strong governance supports the resilience of its business, with the Board having oversight of climate-related risks and opportunities. A newly established ESG Steering Committee that provides quarterly reporting to the Group Risk Committee, will enhance this process in 2022.

Became a signatory to the Investors Against Slavery and Trafficking initiative

Investors Against Slavery and Trafficking (IAST) Asia-Pacific is an investor-led initiative engaging with companies to pursue real action to combat modern slavery, human trafficking and labour exploitation. Challenger understands the importance of industry collaboration and supports the IAST Asia-Pacific initiative. Challenger has joined other signatories to add focus to this important issue. As a signatory to this initiative, Challenger is included on a letter sent to all S&P/ASX100 companies setting out investor expectations on how these issues are considered in their practices.

Fidante UK joined Pensions for Purpose

Fidante UK joined the Pensions for Purpose initiative in the United Kingdom (UK). This is a collaborative initiative of impact managers, pension funds, social enterprises and others involved or interested in impact investment. Its aim is to promote understanding of impact investing in companies, organisations and funds that have the commercial purpose of solving social or environmental problems.

Fidante UK joined this initiative to demonstrate their commitment to ESG and interest in impact investing. Fidante UK, together with Fidante Partners UK-based boutique managers, plan to launch a thought leadership series on ESG investing across various asset classes and showcase this on the Pensions for Purpose platform.

6 Market overview and outlook

Challenger's purpose is to provide customers with financial security for a better retirement. To fulfil this purpose, Challenger will leverage capabilities across its Life, Funds Management, and recently acquired Bank businesses.

Challenger's Life and Funds Management businesses are expected to benefit from the long-term growth in Australia's superannuation system.

Australia's superannuation system commenced in 1992 and is the fifth largest pension system globally and one of the fastest growing, with assets increasing by 11% per annum over the past 20 years[1].

Critical features driving the growth of Australia's superannuation system include government-mandated and increasing contributions, tax incentives to encourage retirement savings and an efficient and competitive institutional model.

Australia's superannuation system is forecast to grow from approximately $3 trillion today[2] to almost $7 trillion[3] over the next 15 years.

Growth in the retirement phase of the system is supported by ageing demographics and the Government's focus on enhancing this component of superannuation.

Life outlook

Life focuses on the retirement spending phase of superannuation, providing products that help customers convert retirement savings into safe and secure income in retirement.

As Australia's superannuation system grows, the retirement phase of superannuation is expected to increase significantly. As Australia's leading provider of annuities[4], Challenger Life is expected to benefit from this growth. The number of Australians over the age of 65, which is Life's target market, is expected to increase by 50% over the next 20 years[5]. Reflecting these demographic changes, and growth in the superannuation system, the annual transfer from the retirement savings phase of superannuation to the retirement phase was estimated to be approximately $70 billion[6] in 2020.

[1] Thinking Ahead Institute - Global Pension Assets Study 2021.
[2] APRA, as at March 2021.
[3] Rice Warner Superannuation Market Projections Report 2020.
[4] Plan For Life – March 2021 – based on annuities under administration.
[5] 2020 – 2040 comparison based on Australian Bureau of Statistics, Population Projections Series B, cat no. 3222.0.
[6] Based on Taxation Statistics 2018-19 from Australian Taxation Office.

6 Market overview and outlook (continued)

Life outlook (continued)

The purpose of the superannuation system is to provide income in retirement to substitute or supplement the Government-funded age pension. With the transition from Government-funded age pensions to private pensions, retirees are seeking retirement income products that convert savings into regular and secure income, helping to provide financial security in retirement.

The Australian Government is progressing a range of retirement income regulatory reforms designed to enhance the retirement phase and better align it with the overall objective of the superannuation system.

These reforms provide an opportunity to increase the proportion of savings invested in products that deliver stable, regular and reliable retirement income.

Annuities currently represent only a small part of the retirement phase, with lifetime annuities representing less than 2% of the annual transfer to the retirement phase.

As Australia's leading provider of annuities, Challenger Life is expected to continue to benefit from the long-term growth in Australia's superannuation system and regulatory reforms designed to enhance the retirement phase.

Challenger has been recognised as a retirement income product innovator and has won the Association of Financial Advisers 'Annuity Provider of the Year' for the last 13 years and remains the dominant retirement income brand in Australia.

An important distribution channel for Life's products is third-party financial advisers. Life's products are included on all major advice hubs' Approved Product Lists (APLs) and are available on the leading administration platforms.

Challenger is also focused on building institutional partnerships with large super funds. As their members transition to retirement, major super funds are increasing their focus on providing more comprehensive retirement solutions to their members. As the retirement system develops, the profit-for-member sector provides a significant growth opportunity for Challenger.

In Japan, Life has an annuity relationship with Mitsui Sumitomo Primary Life Insurance Company Limited (MS Primary) to provide Australian dollar and US dollar annuities. MS Primary is a leading provider of annuity products in Japan and is part of the MS&AD Insurance Group Holdings Inc. (the MS&AD Group).

Under a reinsurance arrangement with MS Primary, which commenced in July 2019, MS Primary provides Challenger an annual amount of reinsurance, across both Australian and US dollar annuities, of at least ¥50 billion (equivalent to approximately A$600 million[7]) per year[8]. This is subject to review in the event of a material adverse change for either MS Primary or Challenger Life.

At 30 June 2021, MS&AD held approximately 15% of Challenger Limited issued share capital and a representative from the MS&AD Group and an Alternate Director have been appointed Non-Executive Directors of Challenger Limited.

The retirement incomes Life pays are backed by a high-quality investment portfolio, predominantly invested in fixed income and commercial property investments.

These long-term investments generate regular and predictable investment income which is used to fund retirement income paid to Life's customers.

Funds Management outlook

Funds Management focuses on building savings for retirement. As people work and save for retirement, the business supports them to build their wealth and savings by providing investment strategies that seek to deliver superior investment returns.

Funds Management is one of Australia's fastest growing[9] and third largest active fund manager[10] and is diversifying globally with operations in Europe, Japan and Singapore.

Growth in funds under management can be attributed to the strength of Challenger's retail and institutional distribution teams, a market-leading business model focused on alignment with clients and high quality managers with strong long-term investment performance.

Funds Management comprises Fidante Partners and CIP Asset Management.

The Fidante Partners' business model involves taking minority equity interests in separately branded boutique funds management firms, with Challenger providing distribution, administration and business support, leaving investment managers to focus entirely on managing investment portfolios.

Fidante Partners' business model has allowed it to attract and build successful active equity, active fixed income and alternative investment managers, while maintaining strong investment performance. Over the last three years, long term performance for Fidante Partners' Australian boutiques remains strong with 92% of funds and mandates outperforming their respective benchmarks.

Fidante Partners is focused on broadening its product offering, which includes partnering with best-in-class managers, expanding the product offering of existing managers and accessing new distribution channels.

Funds Management has extensive client relationships, for example 45 of Australia's top 50 superannuation funds are clients of Fidante Partners.

CIP Asset Management principally originates and manages fixed income and commercial real estate, along with providing investment solutions for leading global and Australian institutions, including Challenger Life.

CIP Asset Management is transitioning from being an internally focused to an externally focused manager, and Challenger is committed to growing the business and building on CIP Asset Management's breadth of investment expertise.

Funds Management is well positioned to benefit from ongoing growth in both Australia's superannuation system and global pension markets.

[7] Based on the exchange rate as at 30 June 2021.
[8] Challenger Life entered into a new agreement with MS Primary to commence reinsurance, across both Australian and US dollar annuities, of at least ¥50 billion per year for a minimum of five years. Challenger will provide a guaranteed interest rate and assume the investment risk in relation to those policies issued by MS Primary and reinsured by Challenger.
[9] Plan For Life Wholesale Trust Data, September 2020, December 2020 and March 2021.
[10] Consolidated FUM for Australian Fund Managers – Rainmaker Roundup March 2021.

6 Market overview and outlook (continued)

Bank acquisition

Challenger is diversifying its product offering and extending its customer reach.

In December 2020, Challenger announced the acquisition of MyLifeMyFinance Limited (MyLife MyFinance), an Australian-based customer digital bank, for $35 million[11].

The acquisition received formal approval from the Treasurer of the Commonwealth of Australia and was completed in July 2021.

MyLife MyFinance is an Australian-based authorised deposit-taking institution (ADI) and digital bank, offering a range of simple savings and lending products. MyLife MyFinance has an ADI licence with an existing term deposit offering.

The acquisition is highly strategic and provides Challenger the opportunity to significantly expand its secure retirement income offering, including entering Australia's term deposit market.

Adding an Authorised Deposit-taking Institution (ADI) capability to sit alongside the existing Life and Funds Management operations will broaden both Challenger's product and distribution reach and help fulfil its purpose: to provide customers with financial security for a better retirement.

The Bank provides Challenger the opportunity to attract and engage with customers at an earlier age, as they approach and enter the retirement phase, increasing Challenger's brand recognition in early age demographics.

Initially, Challenger will offer government guaranteed retail term deposits, which are familiar banking products and represent a significant portion of both retiree and pre-retiree wealth.

The Bank will provide Challenger with access to a wider range of customers through multiple distribution channels, including new intermediated channels such as the broker term deposit market, and will accelerate Challenger's direct-to-customer capability. To ensure speed to market, term deposits will initially be marketed under the MyLife MyFinance brand and will transition to the Challenger brand during 2022.

The asset and lending strategy for the Bank will centre on broadening the lending capability and embedding a strong risk management approach in order to deliver the Group's return on equity target once the business scales.

The acquisition price and capital requirements, including regulatory capital to support its initial growth, was funded by a $100 million distribution from Challenger Life Company Limited (CLC) paid during the March 2021 quarter.

Integration is well progressed, with integration costs expected to be between $5 million and $8 million incurred over 2021 and 2022, which will be reported as a significant item.

COVID-19 pandemic

The COVID-19 pandemic has presented significant challenges to global economies and investment markets.

Looking after the health of our people during this time has been a key business priority for Challenger, which transitioned almost all its employees to working from home arrangements from mid-March 2020 and again in July 2021. Challenger continues to comply with national and state public health orders.

Challenger has also been supporting its customers and business partners throughout the pandemic, including advisers, superannuation fund clients and commercial property tenants.

Investment market conditions have been significantly disrupted by the COVID-19 pandemic, initially resulting in a market sell-off and increased market volatility. Following the pandemic related market sell-off in March 2020, Challenger Life actively repositioned its investment portfolio to more defensive settings, which will be maintained.

As a result of this repositioning, Life was holding over $3 billion of cash and liquid investments at the start of 2021. Excess cash and liquids instruments have been progressively redeployed over the course of the year predominantly into higher yielding fixed income investments.

Challenger has enhanced its capital settings to more closely align with its brand and purpose of providing financial security for a better retirement. From 2022, Challenger is extending its target capital ratios and intends to operate toward the top of its target range providing increased flexibility for investment market volatility and reducing the risk of realising negative investment experience during significant market shocks.

Risks

The above outlook for the Life and Funds Management businesses is subject to the following key business risks:

- investment market volatility;
- ongoing impact of COVID-19 pandemic on the global economy and the ability of individuals, businesses, and governments to operate;
- general uncertainty around the global economy and its impact on markets in which Challenger operates and invests;
- regulatory and political changes impacting financial services markets participants;
- demand for and competition with Challenger products, including annuities and managed funds; and
- operational risk.

Other risks to which Challenger's businesses are exposed are summarised in Section 5 Risk management and in the Corporate Governance Statement.

[11] Acquisition price subject to completion adjustments.

7 Key performance indicators (KPIs)

7.1 Profitability and growth

KPIs for the year ended 30 June 2021 (with the year to 30 June 2020 being the prior comparative period (pcp), unless otherwise stated) include:

	2021	2020	Change %
Profitability			
Statutory profit/(loss) attributable to equity holders ($m)	592.3	(416.0)	large
Normalised NPBT ($m)	395.8	506.5	(21.9)
Normalised NPAT ($m)	278.5	343.7	(19.0)
Statutory EPS (cents)	88.2	(68.4)	large
Normalised EPS (cents)	41.5	56.5	(26.5)
Total dividend (cents)	20.0	17.5	14.3
Total dividend franking	100%	100%	—
Normalised cost: Income ratio	41.2%	35.7%	(5.5)
Statutory RoE after tax	16.8%	(12.1%)	28.9
Normalised RoE pre-tax	11.2%	14.8%	(3.6)
Normalised RoE after tax	7.9%	10.0%	(2.1)
Sales, Flows, AUM			
Total Life sales ($m)	6,928.1	5,151.4	34.5
Total Life net flows ($m)	2,163.8	315.8	large
Total Life net book growth (%)	14.4%	2.1%	12.3
Total FM net flows ($bn)	16.1	2.5	large
Total AUM ($bn)	110.0	85.2	29.1

The recovery of market conditions, since the World Health Organization declared the outbreak of COVID-19 a pandemic in March 2020, resulted in Challenger recognising significant investment experience gains in the year ended 30 June 2021.

Challenger's statutory profit attributable to equity holders for the year ended 30 June 2021 was substantially higher than the statutory loss reported in the previous year. The material increase was driven by large positive net fair value changes on Challenger Life Company Limited's (CLC's) assets and liabilities as a result of the investment market recovery.

Normalised NPAT decreased by 19.0%, and normalised EPS decreased by 26.5% compared to 2020, reflecting lower earnings in Life as a result of the sharp decline in credit spreads over the year which were not fully reflected in customer pricing. This was partially offset by higher earnings in the Funds Management business.

Investment experience profit after tax was $318.6 million compared to a $750.3 million loss in the pcp.

A final dividend of 10.5 cents was announced, franked at 100%, taking the total dividend for 2021 to 20.0 cents franked at 100% for 2021, which is 2.5 cents higher than the prior year.

Challenger's normalised cost to income ratio of 41.2% is higher than the ratio in 2020 (35.7%). Lower normalised cash operating earnings (NCOE) for Life was the main driver of the higher normalised cost to income ratio for the year. Operating costs were lower than the previous period despite reflecting the adoption of the International Financial Reporting Standards Interpretations Committee (IFRIC) agenda decisions which have resulted in a reclassification of deployment costs associated with Software-as-a-Service (SaaS) arrangement from intangible assets to recognition as an expense in the Statement of comprehensive income.

The normalised pre-tax return on equity (RoE) was 11.2% in 2021 compared to 14.8% in the prior year due to the reduced NCOE combined with higher average capital levels. The RoE outcome was below the target of the Reserve Bank of Australia (RBA) cash rate plus 14%. In June 2021, consistent with Challenger's deliberately higher capital levels, the group revised its pre-tax return on equity target to the RBA cash rate plus 12%.

Statutory RoE after tax of 16.8% has increased substantially compared to the prior year (2020: negative 12.1%) as a result of the materially higher statutory NPAT primarily as a result of the positive net fair value movements on CLC's assets and liabilities. These movements were experienced as a result of the recovery in investment market values following the volatility caused by COVID-19. Normalised RoE after tax decreased from 10.0% in the prior period to 7.9%, primarily reflecting lower normalised NPAT.

7.2 Capital management

Challenger's capital position is managed at both the Group and the prudentially-regulated CLC level, with the objective of maintaining the financial stability of the Group and CLC while ensuring that shareholders earn an appropriate risk-adjusted return.

On 22 June 2020, Challenger announced an underwritten institutional placement of equity in the amount of $270.0 million together with a non-underwritten share purchase plan (SPP) for retail shareholders which was targeting to raise up to $30 million. The institutional placement of $270 million was completed on 23 June 2020 and injected directly into CLC on 26 June 2020. The SPP was completed on 24 July 2020, raising $35 million. The majority of the SPP proceeds ($30 million) were also subsequently injected into CLC on 31 July 2020 and form part of the capital base for CLC for the current period.

7 Key performance indicators (KPIs) (continued)

7.2 Capital management (continued)

The decision to raise additional capital was taken to further protect CLC's capital position in the wake of COVID-19 while at the same time being used to further enhance returns once deployed.

On 25 November 2020, Challenger completed its third capital notes issue, Challenger Capital Notes 3, raising $385 million through the issue of 3.850 million notes for $100 each. On the same date, Challenger confirmed the repurchase and redemption of approximately 2.975 million Challenger Capital Notes 1 with a face value of $100 each. The net proceeds of these transactions provided incremental Additional Tier 1 regulatory capital for CLC.

On 25 May 2021, Challenger completed the off-market repurchase of 197,308 Challenger Capital Notes 1 that were offered by eligible holders of Challenger Capital Notes 1 under the repurchase invitation announced by Challenger on 27 April 2021. Challenger accepted all valid offers by participating holders of Challenger Capital Notes 1 for a repurchase price of $102 per Challenger Capital Note 1. Following the completion of the repurchase, approximately $27.7 million of Challenger Capital Notes 1 remain on issue.

The following table highlights the key capital metrics for CLC and the Group:

Capital	2021	2020	Change
Net assets attributable to equity holders ($m)	3,825.8	3,249.6	576.2
CLC excess capital over PCA ($m)	1,650.0	1,584.7	65.3
Group cash ($m)[1]	223.0	146.1	76.9
CLC excess capital over PCA + Group cash ($m)	1,873.0	1,730.8	142.2
CLC PCA ratio (times)	1.63	1.81	(0.18)
CLC CET1 ratio (times)	1.14	1.20	(0.06)

[1] Pcp included $50.0 million of the Group corporate debt facility drawn.

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 its customers. CLC is regulated by APRA and is required to hold a minimum level of regulatory capital. CLC has ongoing and open engagement with APRA.

CLC maintains a level of capital representing the Prescribed Capital Amount (PCA) 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 in order to provide a buffer against adverse market conditions, having regard to CLC's credit rating.

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. To underpin Challenger's growth strategy, the group has revised its target capital range to 1.3 times to 1.7 times the APRA PCA, extending the upper end of the range (previously 1.6 times) and outlined an intention to operate at around 1.6 times. This range may change over time and is dependent on a number of factors. CLC's PCA ratio was 1.63 times as at 30 June 2021.

In addition to CLC's excess regulatory capital, Challenger maintains cash at a Group level which can be used to meet regulatory capital requirements. Challenger further maintains a Group corporate debt facility of $400 million in order to provide additional financial flexibility.

The facility was fully drawn in March 2020 in response to the investment market volatility caused by COVID-19 and had $50 million outstanding at 30 June 2020. This was fully repaid during the period, $25 million on each of 22 March 2021 and 22 June 2021. The amount drawn at the end of the period was nil.

Dividends and dividend reinvestment plan

Dividends	2021	2020	Change
Interim dividend (cents)[1]	9.5	17.5	(8.0)
Final dividend (cents)[2]	10.5	—	10.5
Total dividend (cents)	20.0	17.5	2.5
Interim dividend franking	100%	100%	—
Final dividend franking	100%	—%	—

[1] Interim dividend declared on 9 February 2021 and paid on 23 March 2021 in respect of the half year ended 31 December 2020.
[2] Final dividend declared on 9 August 2021 and payable on 22 September 2021 in respect of the half year ended 30 June 2021.

The Board targets a dividend payout ratio range of 45% to 50% of normalised earnings per share. The dividend payout ratio for the year ended 30 June 2021 was 48.2% (30 June 2020: 31.0%) and therefore within this range.

The final dividend of 10.5 cents will be fully franked. The Company seeks to frank its dividends to the maximum extent possible and expects future dividends over the medium term to be also fully franked. However, the actual dividend payout ratio and franking will depend on prevailing market conditions and capital allocation priorities at the time.

The Company recommenced operating its Dividend Reinvestment Plan (DRP) during the year. The participation rate for the 2021 interim dividend was 4.5%, and 441,762 ordinary shares were issued to satisfy DRP requirements on 23 March 2021.

The DRP will continue in operation for the 2021 final dividend, and the Board has determined that new shares will be issued to fulfil DRP requirements in respect of the final dividend. The new shares will not be issued at a discount to the prevailing Challenger share price.

No shares were bought back during the year.

7 Key performance indicators (KPIs) (continued)

7.3 Credit ratings

Challenger Limited and CLC are rated by Standard & Poor's (S&P). In November 2020, S&P reaffirmed both CLC and Challenger Limited's credit ratings but revised the outlook from positive to stable as a result of the uncertainty caused by COVID-19.

Ratings were confirmed as:

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

8 Normalised profit and investment experience

Normalised framework (Non-IFRS)

CLC and its consolidated entities are required by AASB 1038 ***Life Insurance Contracts*** to value all assets and liabilities at fair value where permitted by other accounting standards.

This gives rise to fluctuating valuation movements on assets and liabilities being recognised in the profit and loss in CLC and on consolidation in Challenger Limited. CLC is generally a long-term holder of assets, due to holding assets 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 CLC's medium to long-term expected returns together with the new business strain[1] that results from writing new annuities. Investment experience also includes any impact from changes in economic and other actuarial assumptions.

A reconciliation between statutory revenue and the management view of revenue and net income is included in the financial report as part of Note 3 Segment information.

This note also includes a reconciliation of statutory NPAT and normalised NPAT (the management view of post-tax profit). The application of the normalised profit framework has been reviewed by Challenger's independent auditor to ensure that the reported results are consistently applied in accordance with the methodology described in Note 3 Segment information in the financial report.

Management analysis – normalised results

	2021 $m	2020 $m	Change $m	Change %
Net income[1]	682.1	797.4	(115.3)	(14.5)
Comprising:				
– Life normalised COE	512.8	638.9	(126.1)	(19.7)
– FM net income	169.3	158.1	11.2	7.1
– Corporate and other income	—	0.4	(0.4)	(large)
Operating expenses[1]	(281.3)	(284.4)	3.1	1.1
Normalised EBIT	**400.8**	**513.0**	**(112.2)**	**(21.9)**
Comprising:				
– Life normalised EBIT	398.9	524.7	(125.8)	(24.0)
– FM normalised EBIT	71.0	57.7	13.3	23.1
– Corporate and other normalised EBIT	(69.1)	(69.4)	0.3	0.4
Interest and borrowing costs	(5.0)	(6.5)	1.5	23.1
Normalised NPBT	**395.8**	**506.5**	**(110.7)**	**(21.9)**
Tax on normalised profit	(117.3)	(162.8)	45.5	27.9
Normalised NPAT	**278.5**	**343.7**	**(65.2)**	**(19.0)**
Investment experience after tax	318.6	(750.3)	1,068.9	large
Significant items after tax	(4.8)	(9.4)	4.6	48.9
Statutory net profit/(loss) after tax attributable to equity holders	**592.3**	**(416.0)**	**1,008.3**	**large**

[1] 'Net income' and 'Operating expenses' are internal classifications and are defined in Note 3 Segment information in the financial report. These differ from the statutory revenue and expenses classifications, as certain costs (including distribution expenses, property expenses, management fees, special purpose vehicle expenses and finance costs) are netted off against gross revenues. These classifications have been made in the Directors' report and in Note 3 Segment information to reflect how management measures business performance. While the allocation of amounts to the above items and investment experience differ to the statutory view, both approaches result in the same total net profit after tax attributable to equity holders.

[1] New business strain is a non-cash accounting adjustment recognised when annuity rates on new business are higher than the risk-free rate used to fair value annuities. The new business strain unwinds over the annuity contract.

8 Normalised profit and investment experience (continued)

Management analysis – normalised results (continued)

Life normalised cash operating earnings (COE) and earnings before interest and tax (EBIT) decreased as a result of lower investment yield generated on the portfolio and a lower contribution from normalised capital growth, due to both a composition change in Life investment assets as well as a reduction in normalised capital growth factors when compared to the prior year.

Life's average assets under management (AUM) increased by 2.6% as a result of the net book growth in annuities and external unit holders' liabilities accompanied by favourable valuation movements on investment assets.

Funds Management net income increased (up $11.2 million) due to increased equity accounted profits and distribution fee revenue. Funds Management average FUM increased by 15.0% as a result of mark-to-market gains on investments and exceptionally strong net inflows over the year.

Operating expenses decreased by $3.1 million (or 1.1%) for the year despite reflecting the adoption of the IFRIC agenda decisions which have resulted in a reclassification of deployment costs associated with SaaS arrangement from intangible assets to recognition as an expense in the Statement of comprehensive income.

Challenger's full-time equivalent employee numbers increased by 3 (or 0.4%) to 738.

The normalised effective tax rate was lower than the prior year due to the availability of foreign tax offsets and no deferred tax asset impairments being recognised in the period.

Significant items were negative $4.8 million (after tax) in the period and represent costs associated with the acquisition of MyLife MyFinance as well as the write-down in the carrying value of one Funds Management boutique.

Management analysis – investment experience

	2021 $m	2020 $m
Actual capital growth[1]		
Cash and fixed income	331.5	(528.8)
Equity and infrastructure	76.6	—
Property (net of debt)	120.6	(155.3)
Alternatives	47.5	—
Infrastructure	—	(114.9)
Equity and other investments	—	(269.3)
Total actual capital growth	**576.2**	**(1,068.3)**
Normalised capital growth[2]		
Cash and fixed income	(52.0)	(46.4)
Equity and infrastructure	20.0	—
Property (net of debt)	66.1	66.6
Alternatives	—	—
Infrastructure	—	28.0
Equity and other investments	—	72.0
Total normalised capital growth	**34.1**	**120.2**
Investment experience		
Cash and fixed income	383.5	(482.4)
Equity and infrastructure	56.6	—
Property (net of debt)	54.5	(221.9)
Alternatives	47.5	—
Infrastructure	—	(142.9)
Equity and other investments	—	(341.3)
Policy liability experience[3]	(76.1)	86.1
Asset and policy liability experience	**466.0**	**(1,102.4)**
New business strain[4]	(10.9)	31.9
Investment experience before tax	**455.1**	**(1,070.5)**
Tax (expense)/benefit	(136.5)	320.2
Investment experience after tax	**318.6**	**(750.3)**

1 Actual capital growth represents net realised and unrealised capital gains or losses and includes the attribution of interest rate, inflation and foreign exchange derivatives that are used to hedge exposures.

2 Normalised capital growth is determined by multiplying the normalised capital growth rate for each asset class by the average investment assets for the period. The normalised capital growth rates represent Challenger's expectations for each asset class over the investment cycle. The annual normalised growth rate is +4.0% for equity and infrastructure, +2.0% for property, 0.0% for alternatives, and -0.35% for cash and fixed income in order to allow for credit defaults. The rates have been set with reference to medium to long-term market growth rates and are reviewed to ensure consistency with prevailing market experience.The asset classes' composition changed from 1 July 2020. The annual normalised growth rates for the pcp were as follows, and reflect the composition of the portfolio at that time: +3.5% for equity and other investments, +4.0% for infrastructure, +2.0% for property, and -0.35% for cash and fixed income.

3 Policy liability experience represents the impact of changes in macroeconomic variables, including bond yields and inflation factors, expense assumptions and other factors applied in the valuation of life contract liabilities.

4 New business strain is a non-cash accounting adjustment recognised when annuity rates on new business are higher than the discount rate, being a risk-free rate plus an illiquidity premium used to fair value annuities. The new business strain unwinds over the annuity contract.

8 Normalised profit and investment experience (continued)

Management analysis — investment experience (continued)

Investment experience after tax relates to changes in the fair value of Life's assets and liabilities. Investment experience is a mechanism employed to remove the volatility arising from asset and liability valuation movements and new business strain from Life business earnings so as to more accurately reflect the underlying performance of the Life business.

Pre-tax investment experience in 2021 comprised an asset and policyholder liability experience gain of $466.0 million and a loss of $10.9 million from Life's new business strain. These gains are largely unrealised and were primarily due to the improvement of fixed income and equity markets during the year.

9 Life segment results

Life focuses on the retirement spending phase of superannuation, providing products that help customers convert retirement savings into safe and secure income in retirement. The Life segment includes Challenger Life Company Limited (CLC), an APRA-regulated life insurance company and is Australia's leading provider of annuities and guaranteed retirement income products.

CLC is regulated by APRA, and its financial strength is rated by Standard & Poor's, with an 'A' credit rating and a stable outlook. CLC is strongly capitalised, with significant excess capital above APRA's minimum regulatory requirements.

Life normalised results	2021 $m	2020 $m	Change $m	Change %
Normalised COE	512.8	638.9	(126.1)	(19.7)
– Cash earnings	478.7	518.7	(40.0)	(7.7)
– Normalised capital growth	34.1	120.2	(86.1)	(71.6)
Operating expenses	(113.9)	(114.2)	0.3	0.3
Normalised EBIT	**398.9**	**524.7**	**(125.8)**	**(24.0)**

Life normalised EBIT decreased by $125.8 million (down 24.0%) due to lower normalised COE (down $126.1 million or 19.7%), which was partially offset by operating expenses decreasing $0.3 million (or 0.3%). The lower normalised COE was the result of lower asset yields and contribution from normalised capital growth. The lower yields were mainly attributable to earnings on the Cash and fixed income portfolio, impacted by higher levels of cash and liquid assets held in the portfolio, and lower distributions in the Equity and infrastructure and Alternative portfolios. CLC held $3.0 billion of cash and liquid assets at the start of the period given the COVID-19 related market volatility, and the majority of this was gradually deployed into higher yielding assets, mainly investment-grade and sub-investment grade fixed income assets, over the course of 2021. The cash and liquid assets balance has reduced to $1.4 billion at 30 June 2021. The lower contribution from normalised capital growth of $34.1 million is due to both a composition change in Life investment assets, as well as a decline in normalised capital growth across Equity, Infrastructure and Other investments, as well as a net reduction in the normalised capital growth factor for Alternatives.

Life generated a normalised RoE (pre-tax) of 12.4%, down by 4.2 percentage points from the prior year as a result of lower normalised EBIT.

Total Life sales increased from the prior period (up 34.5%), with increased Lifetime sales (up 38.8%), increased fixed-term sales (up 47.1%) and other Life sales (up 16.7%). Lifetime sales increased by 38.8% due to new institutional relationships and rebuilding of momentum across the retail advised channel.

CLC participates in the Japanese foreign currency annuity market via a reinsurance agreement with MS Primary, a Japanese life insurance company and subsidiary of MS&AD Insurance Group Holdings, Inc. The reinsurance agreement with MS Primary provides CLC with an annual amount of reinsurance across both Australian and US dollar annuities of at least ¥50.0 billion (approximately A$600.0 million based on the exchange rate at 30 June 2021)[1] each year for a minimum of five years commencing from 1 July 2019. The MS Primary reinsured sales comprised 17.3% of Life's total annuity sales in the period, which is a decrease on the pcp (23.8%).

Life sales	2021 $m	2020 $m	Change $m	Change %
Fixed-term annuities	3,990.4	2,712.8	1,277.6	47.1
Lifetime annuities	575.6	414.6	161.0	38.8
Total Life annuity sales	4,566.0	3,127.4	1,438.6	46.0
Other Life sales	2,362.1	2,024.0	338.1	16.7
Total Life sales	**6,928.1**	**5,151.4**	**1,776.7**	**34.5**
Annuity net flows	1,079.8	(251.1)	1,330.9	large
Other Life net flows	1,084.0	566.9	517.1	91.2

Annuity net flows (new annuity sales less capital repayments) increased to $1,079.8 million, driven by higher annuity sales. Based on the opening Life annuity book for the 2021 financial year ($12,581.2 million), annuity net book growth for the period was 8.6%, up from (2.0)% in the prior period.

Other Life sales represents Challenger's Index Plus products and increased as a result of new client sales during the period.

Other Life net flows for the period were $1,084.0 million, increasing by $517.1 million compared to positive $566.9 million in the prior period. Total Life net flows were $2,163.8 million, representing, total Life net book growth of 14.4% (30 June 2020: $315.8 million or 2.1% book growth).

[1] This is subject to review in the event of a material adverse change for either MS Primary or Challenger.

10 Funds Management segment results

The Funds Management (FM) operating segment focuses on accumulating wealth for retirement. As people work and save for retirement, the business supports them building their wealth and savings by providing investment strategies that seek to deliver superior investment returns.

Funds Management is Australia's third largest active fund manager[1] and has diversified distribution capability in Europe, Japan and Singapore.

The Funds Management segment comprises two business divisions, Fidante Partners and CIP Asset Management (CIPAM).

Fidante Partners' multi-boutique platform comprises a number of separately branded funds management businesses. The model seeks to align the interests of investors, boutique investment managers and Fidante Partners.

CIPAM develops and manages fixed income and commercial property assets for CLC and third-party institutional investors.

FM normalised results	2021 $m	2020 $m	Change $m	Change %
Net income	169.3	158.1	11.2	7.1
– Fidante Partners	107.5	96.3	11.2	11.6
– CIPAM	61.8	61.8	—	—
Operating expenses	(98.3)	(100.4)	2.1	2.1
Normalised EBIT	**71.0**	**57.7**	**13.3**	**23.1**

Funds Management normalised EBIT increased by 23.1% for the year, with increased net income primarily from the Fidante Partners business.

Fidante Partners' net income includes distribution fees, transaction fees, administration fees and a share in the equity accounted profits for the boutique fund managers in which it has an equity interest.

Fidante Partners' net income improved for the period primarily as a result of higher equity accounted profits, performance fees and distribution fees (up $11.2 million).

CIPAM's net income remained stable with a mix shift to more recurring management fees and lower one-off transaction fees.

Funds Management's normalised RoE (pre-tax) for the year was 27.7%, up by 3.4 percentage points from the prior year.

FM FUM and flows	2021 $bn	2020 $bn	Change $bn	Change %
Total FUM	105.8	81.4	24.4	30.0
– Fidante Partners	84.9	62.3	22.6	36.3
– CIPAM	20.9	19.1	1.8	9.4
Net flows	16.1	2.5	13.6	large
– Fidante Partners	14.3	3.8	10.5	large
– CIPAM	1.8	(1.3)	3.1	large

Fidante Partners' FUM increased by $22.6 billion (or 36.3%) compared to the prior year.

During the period, Fidante Partners' net inflows were $14.3 billion compared to a net inflows of $3.8 billion in the prior year.

11 Corporate and other segment results

The Corporate and other segment comprises central functions such as the Group executive, finance, treasury, legal, tax, human resources, risk management and strategy.

The financial results also include interest received on Group cash balances and any interest and borrowing costs associated with Group debt facilities.

Corporate and other normalised results	2021 $m	2020 $m	Change $m	Change %
Net income	—	0.4	(0.4)	(large)
Operating expenses	(69.1)	(69.8)	0.7	1.0
Normalised EBIT	**(69.1)**	**(69.4)**	**0.3**	**0.4**
Interest and borrowing costs	(5.0)	(6.5)	1.5	23.1
Normalised loss before tax	**(74.1)**	**(75.9)**	**1.8**	**2.4**

Normalised EBIT for the Corporate and other segment was up $0.3 million as a result of lower operating expenses.

12 Guidance for the 2022 financial year

Challenger's 2022 normalised net profit before tax guidance is a range of between $430 million and $480 million. The mid-point of the guidance range ($455 million) represents Challenger's best estimate and would result in Challenger achieving its Normalised RoE (pre tax) target.

Consistent with Challenger's growth strategy to maintain higher capital levels, the Group has revised its go-forward normalised pre-tax return on equity target from the Reserve Bank of Australia (RBA) cash rate plus a margin of 14% to the cash rate plus a margin of 12%.

Subject to regulatory requirements and market conditions, Challenger continues to target a dividend payout ratio in the range of between 45% to 50% of normalised profit after tax and aims to frank dividends to the maximum extent possible.

[1] Consolidated FUM for Australian Fund Managers – Rainmaker Roundup, March 2021.

Five-year history

	2021	2020	2019	2018	2017
Earnings ($m)					
Normalised cash operating earnings	512.8	638.9	670.1	669.6	631.4
Net fee income	169.3	158.1	149.9	151.2	134.0
Other income	—	0.4	1.0	1.0	0.8
Total net income	**682.1**	**797.4**	**821.0**	**821.8**	**766.2**
Personnel expenses	(179.9)	(174.0)	(185.3)	(187.8)	(179.3)
Other expenses	(101.4)	(110.4)	(82.1)	(80.6)	(76.6)
Total expenses	**(281.3)**	**(284.4)**	**(267.4)**	**(268.4)**	**(255.9)**
Normalised EBIT	400.8	513.0	553.6	553.4	510.3
Interest and borrowing costs	(5.0)	(6.5)	(5.3)	(6.1)	(5.3)
Normalised profit before tax	**395.8**	**506.5**	**548.3**	**547.3**	**505.0**
Normalised tax	(117.3)	(162.8)	(152.2)	(141.2)	(120.1)
Normalised profit after tax	**278.5**	**343.7**	**396.1**	**406.1**	**384.9**
Investment experience after tax	318.6	(750.3)	(88.3)	(76.0)	12.7
Significant items after tax	(4.8)	(9.4)	—	(7.6)	—
Profit attributable to equity holders	**592.3**	**(416.0)**	**307.8**	**322.5**	**397.6**
Normalised cost to income ratio (%)	41.2%	35.7%	32.6%	32.7%	33.4%
Normalised effective tax rate (%)	29.6%	32.1%	27.8%	25.8%	23.8%
Statutory effective tax rate (%)	28.7%	28.9%	29.2%	22.7%	23.3%
Earnings per share (EPS) (cents)					
Basic EPS – normalised profit	41.5	56.5	65.5	68.1	68.5
Basic EPS – statutory profit	88.2	(68.4)	50.9	54.0	70.7
Diluted EPS – normalised profit	33.8	46.9	56.0	64.2	65.8
Diluted EPS – statutory profit	68.0	(68.4)	44.8	52.2	67.8
Capital management (%)					
Normalised return on equity – pre-tax	11.2%	14.8%	15.8%	16.5%	18.3%
Normalised return on equity – post-tax	7.9%	10.0%	11.4%	12.2%	14.0%
Statutory return on equity – post-tax	16.8%	(12.1%)	8.9%	9.7%	14.4%
Statement of financial position ($m)					
Total assets	29,917.9	28,461.6	27,457.5	25,300.5	23,026.7
Total liabilities	26,092.1	25,212.0	23,834.7	21,814.7	20,125.4
Net assets[1]	3,825.8	3,249.6	3,622.8	3,485.8	2,901.3
Net assets[2]	3,825.8	3,249.6	3,600.3	3,485.4	2,888.1
Net assets[2] – average[3]	3,518.9	3,424.4	3,462.1	3,323.3	2,753.8
Net tangible assets[4]	3,202.0	2,619.2	3,019.1	2,892.5	2,299.7
Net assets per basic share ($)	5.69	4.90	5.94	5.79	5.14
Net tangible assets per basic share ($)	4.76	3.95	4.98	4.81	4.09

[1] Including minority interests.
[2] Excluding minority interests.
[3] Calculated on a monthly basis.
[4] Excludes right-of-use lease asset, goodwill and other intangible assets.

Five-year history (continued)

	2021	2020	2019	2018	2017
Underlying operating cash flow ($m)	**194.7**	**194.7**	**236.9**	**197.4**	**299.9**
Dividends per share (cents)					
Dividend – interim	9.5	17.5	17.5	17.5	17.0
Dividend – final	10.5	—	18.0	18.0	17.5
Total dividend	**20.0**	**17.5**	**35.5**	**35.5**	**34.5**
Dividend payout ratio – normalised profit (%)	48.2%	31.0%	54.2%	52.1%	50.4%
Dividend payout ratio – statutory profit (%)	22.1%	n/a	69.7%	65.7%	48.8%
Sales and annuity book net flows ($m)					
Annuity sales	4,566.0	3,127.4	3,543.1	4,000.7	4,011.2
Other Life sales	2,362.1	2,024.0	1,006.9	1,554.9	941.2
Total Life sales	**6,928.1**	**5,151.4**	**4,550.0**	**5,555.6**	**4,952.4**
Life annuity net flows	1,079.8	(251.1)	685.8	1,392.7	900.4
Life annuity book	13,669.9	12,581.2	12,870.2	11,728.3	10,322.2
Life annuity net book growth (%)	8.6%	(2.0%)	5.8%	13.5%	9.4%
Total Life flows	2,163.8	315.8	474.8	1,796.3	1,312.9
Total Life book	17,302.1	14,997.0	14,836.4	13,863.3	12,010.0
Total Life net book growth (%)	14.4%	2.1%	3.4%	15.0%	12.1%
Funds Management – net flows	16,111.5	2,540.9	(2,438.4)	5,301.2	6,220.6
Assets under management ($m)					
Life	21,563	18,303	19,010	18,085	15,677
Funds Management	105,824	81,435	79,029	77,984	66,906
Elimination of cross-holdings[1]	(17,427)	(14,501)	(16,269)	(14,926)	(12,595)
Total assets under management	**109,960**	**85,237**	**81,770**	**81,143**	**69,988**
Other					
Headcount – closing full-time employees	738	735	687	676	655
Weighted average number of ASX-listed basic shares on issue (m)	671.6	608.3	605.0	596.7	562.2
Number of shares on issue – closing (m)	676.0	667.5	611.6	610.9	572.0
Share price – closing ($)	5.41	4.41	6.64	11.83	13.34
Market capitalisation at 30 June ($m)[2]	3,657.2	2,943.7	4,061.0	7,226.9	7,630.5

1 Life assets managed by Funds Management.
2 Calculated as share price multiplied by ordinary share capital.

Directors' report

The Directors of Challenger Limited (the Company) submit their report, together with the financial report of the Company and its controlled entities (the Group or Challenger), for the year ended 30 June 2021.

The information appearing on pages 1 to 22 forms part of the Directors' report for the financial year ended 30 June 2021 and is to be read in conjunction with the following information.

1 Directors

The names and details of the Directors of the Company holding office during the financial year ended 30 June 2021 and as at the date of this report are listed below. Directors were in office for the entire period, unless otherwise stated.

Peter L Polson
(appointed 6 November 2003)

Independent Chair.

Chair of Nomination Committee.

Member of the Group Audit Committee, Group Risk Committee, and the Group Remuneration Committee.

Experience and qualifications:
Bachelor of Commerce (Witwatersrand University, Johannesburg, South Africa), Master of Business Leadership (University of South Africa, Pretoria, South Africa), Management Development Program (Harvard Graduate School of Education, Boston, United States).

Mr Polson's experience spans international and domestic markets in banking, insurance and funds management. Mr Polson previously held the positions of Group Executive, Investment and Insurance Services at Commonwealth Bank and Chief Executive of Colonial First State Limited.

Directorships of other listed companies:
Chair of IDP Education Limited (appointed 21 March 2007).

Richard J Howes
(appointed 2 January 2019)

Managing Director and Chief Executive Officer.

Experience and qualifications:
Bachelor of Commerce (Hons) and Bachelor of Economics (University of Queensland).

Mr Howes has previously held a number of senior executive roles at Challenger since joining in 2003, including Chief Executive of Distribution, Product and Marketing, Chief Executive of Challenger's Life business and Chief Investment Officer.

Mr Howes has over 25 years financial services experience. Prior to joining Challenger, he held senior roles at Zurich Capital Markets, Macquarie Bank and Bankers Trust where his primary responsibility was providing risk management solutions to major companies and institutions globally.

Directorships of other listed companies:
Nil.

John M Green
(appointed 6 December 2017)

Independent Non-Executive Director.

Member of the Group Audit Committee, Group Risk Committee, Group Remuneration Committee and the Nomination Committee. Chair of MyLifeMyFinance Limited, appointed 30 July 2021.

Experience and qualifications:
Bachelor of Law and Bachelor of Jurisprudence (University of New South Wales), Fellow of the Australian Institute of Company Directors and Life Member and Senior Fellow of FINSIA.

Mr Green was previously an executive director at Macquarie Group and has also been a partner at two major law firms. He is Deputy Chair of QBE Insurance Group Limited, director of Cyber Security Cooperative Research Centre and also a novelist and co-founder of book publisher Pantera Press.

Directorships of other listed companies:
Non-executive director of QBE Insurance Group Limited (appointed 1 March 2010, appointed Deputy Chair on 1 January 2015).

Steven Gregg
(appointed 8 October 2012)

Independent Non-Executive Director.

Member of the Group Audit Committee, Group Risk Committee, Group Remuneration Committee and the Nomination Committee.

Experience and qualifications:
Bachelor of Commerce (University of New South Wales).

Mr Gregg has held a number of executive roles in management consulting and investment banking. His more recent senior executive roles included Partner and Senior Adviser at McKinsey & Company and Global Head of Investment Banking at ABN AMRO. His experience has spanned both domestic and international arenas, because of his work in both the US and the UK.

Directorships of other listed companies:
Non-executive director of Tabcorp Holdings Limited (appointed 18 July 2012, appointed Chair on 1 January 2021) and Ampol Limited (formerly Caltex Australia Limited) (appointed 9 October 2015; appointed Chair on 18 August 2017).

Masahiko Kobayashi
(appointed 26 August 2019)

Non-Executive Director.

Experience and qualifications:
Master of Business Administration (Questrom School of Business, Boston University, Boston, United States), Bachelor of Law (Kyoto University, Kyoto, Japan) and is a Certified Internal Auditor.

Mr Kobayashi has over 30 years expertise in general and life insurance and is currently Director and Senior Executive Officer (Corporate Planning and Enterprise Risk Management) of MS Primary, a subsidiary of MS&AD Insurance Group Holdings Inc. Prior to joining MS Primary, he held a number of executive and director roles within the MS&AD Group, including in Singapore and the United Kingdom.

Directorships of other listed companies:
Nil.

1 Directors (continued)

Heather Smith
(appointed 20 January 2021)

Independent Non-Executive Director.

Member of the Group Audit Committee, Group Risk Committee and the Nomination Committee.

Experience and qualifications:
Bachelor of Economics (Hons 1) (University of Queensland), PhD in Economics (Australian National University).

Dr Smith has over 20 years experience in government, including as Secretary of the Australian Department of Industry, Innovation and Science, Secretary of the Department of Communications and the Arts, and Deputy Secretary of the Department of Prime Minister and Cabinet. She holds the position of Professor at ANU National Security College and is deputy chair of the United States Studies Centre. She is a recipient of the Public Service Medal.

Directorships of other listed companies:
Nil.

JoAnne M Stephenson
(appointed 8 October 2012)

Independent Non-Executive Director.

Chair of the Group Remuneration Committee.

Member of the Group Audit Committee, Group Risk Committee and the Nomination Committee.

Experience and qualifications:
Bachelor of Commerce and Bachelor of Laws (Honours) (University of Queensland), member of Chartered Accountants Australia and New Zealand and member of the Australian Institute of Company Directors.

Ms Stephenson has extensive experience in financial services both in Australia and in the United Kingdom. Ms Stephenson was previously a partner with KPMG and has significant experience in internal audit, risk management and consulting.

Directorships of other listed companies:
Non-executive director of Asaleo Care Limited (appointed 30 May 2014 and ceased on 1 July 2021), Japara Healthcare Ltd (appointed 1 September 2015) and Myer Holdings Limited (appointed 28 November 2016).

Duncan G West
(appointed 10 September 2018)

Independent Non-Executive Director.

Chair of the Group Audit Committee.

Member of the Group Risk Committee and the Nomination Committee.

Experience and qualifications:
Bachelor of Science in Economics (University of Hull, Hull, United Kingdom), Fellow of the Chartered Insurance Institute, member of the Australian Institute of Company Directors and a Senior Associate of the Australian and New Zealand Institute of Insurance and Finance.

Mr West has over 30 years experience in financial services in the UK and Australia. He has held a series of senior executive positions including as CEO of Vero Insurance and CGU Insurance, and as EGM of Insurance at MLC.

Directorships of other listed companies:
Non-executive Director of Genworth Mortgage Insurance Australia Limited (appointed 1 September 2018).

Melanie V R Willis
(appointed 6 December 2017)

Independent Non-Executive Director.

Chair of the Group Risk Committee.

Member of the Group Audit Committee and the Nomination Committee.

Experience and qualifications:
Bachelor of Economics (University of Western Australia), Master of Law, Tax (University of Melbourne) and a Fellow of the Australian Institute of Company Directors.

Ms Willis has significant senior executive experience in corporate finance, strategy and innovation and funds management. Ms Willis previously held the position of Chief Executive Officer of NRMA Investments and senior executive roles at Deutsche Bank and Bankers Trust. She is also a Non-Executive Director of PayPal Australia Pty Limited and QBE Australia Pacific Limited.

Directorships of other listed companies:
Non-executive director of Southern Cross Media Group Limited (appointed 26 May 2016) and Property Exchange Australia Ltd (PEXA) (appointed 11 June 2021).

Hiroyuki Iioka
(appointed 13 December 2019)

Non-Executive Director (alternate for Masahiko Kobayashi).

Experience and qualifications:
Master of Business Administration (Duke University, Durham, United States) and Bachelor of Economics (Kobe University, Kobe, Japan).

Mr Iioka is currently Senior General Manager (Business Development Department) at MS&AD Insurance Group Holdings, Inc. (MS&AD) in Japan.

Directorships of other listed companies:
Non-executive director of Phoenix Group Holdings PLC, listed on the London Stock Exchange (appointed 23 July 2020).

2 Company Secretary

Linda Matthews (Bachelor of Laws) is the Head of Company Secretariat. She is a qualified as a solicitor and was appointed as Company Secretary on 1 January 2021. Ms Matthews' responsibilities at Challenger involve the oversight of all company secretarial functions. Ms Matthews joined Challenger in 2013 as a Senior Legal Counsel in the Challenger Corporate and Investments Legal team from commercial law firm Norton Rose Fulbright, where she was a senior associate in the Banking and Finance practice. Ms Matthews has over 18 years experience as a solicitor and is admitted to practise in New South Wales and New York. Ms Matthews is an affiliated member of the Governance Institute of Australia.

3 Corporate governance summary

3.1 Roles and responsibilities of Board and management

The role of the Board and delegations

The Board is accountable to shareholders for the activities and performance of Challenger by overseeing the creation of sustainable shareholder value within an appropriate risk framework and having regard for stakeholder interests and community expectations.

The Board is responsible for setting Challenger's corporate strategy and strategic priorities. Challenger's purpose is to provide our customers with financial security for a better retirement. This is a long-term purpose and the Board sets strategic priorities each year to work towards fulfilling this purpose.

Directors are actively involved in setting, approving and regularly monitoring Challenger's strategic priorities and holding management accountable for progress.

This process includes one annual Board strategy offsite, regular Board reporting and meetings, and discussion and review with management. Similarly, the Board ensures that rigorous governance processes operate effectively to guide decision-making across the business.

The Board's responsibilities are set out in the Board Charter, which is available at:

> challenger.com.au/about-us

The Board's role and responsibilities include:

- establishing, promoting and maintaining the strategic direction of Challenger;
- approving business plans, budgets and financial policies;
- considering management recommendations on strategic business matters;
- establishing, promoting and maintaining proper processes and controls to maintain the integrity of accounting and financial records and reporting;
- fairly and responsibly rewarding executives, having regard to the performance of the executives, Challenger's risk management framework and culture, the interests of shareholders, market conditions and Challenger's overall performance;
- adopting and overseeing of implementation of corporate governance practices;
- overseeing the establishment, promotion and maintenance of effective risk management policies and processes;
- determining and adopting Challenger's dividend policy;
- reviewing Board composition and performance;
- appointing, evaluating and remunerating the Chief Executive Officer (CEO) and approving the appointment of the Chief Financial Officer (CFO), Chief Risk Officer (CRO), General Counsel and Company Secretary; and
- determining the CEO's delegated authority.

The Board has established committees to assist in carrying out its responsibilities and to consider certain issues and functions in detail. The Board committees are discussed on page 26.

Management responsibility

The Board has delegated to the CEO the authority and powers necessary to implement the strategies approved by the Board and to manage the business affairs of Challenger within the policies and delegation limits specified by the Board from time to time. The CEO may delegate authority to management, but remains accountable for all authorities delegated to management.

3.2 Directors' skills matrix

The Board has determined that its current members have an appropriate collective mix of skills, experience and expertise to:

- exercise independent judgement;
- have a proper understanding of, and competence to deal with, current and emerging issues of the business;
- encourage enhanced Challenger performance; and
- effectively review and challenge the performance of management.

The Board's competencies are assessed annually and the results of the most recent assessment are shown in the table on page 26.

The Board skills matrix shows that Board members have a high level of competency across the areas of expertise relevant to Challenger's business.

3 Corporate governance summary (continued)

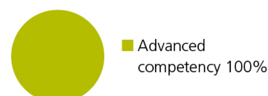
3.2 Directors' skills matrix (continued)

Leadership & Strategy

Leadership, effective communication and influencing skills. Strategic thinking capability and transactional expertise.

Corporate Governance

Public company corporate governance literacy.



Financial Acumen

Financial reporting literacy including exposure to Accounting Standards.

Risk & Compliance

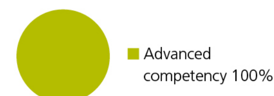
Financial services and fiduciary regulatory awareness. Relevant compliance and risk experience including legal and tax risk management.

Sectoral Exposure

Exposure to funds management and life insurance sectors, and market experience in jurisdictions in which Challenger operates.

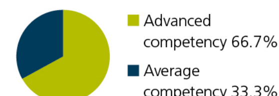
Investment & Credit Expertise

Credit risk management and investment expertise including asset class literacy and exposure (eg: property, fixed income, equities, etc).



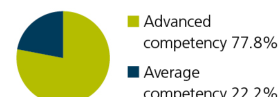
Customer

Experience in distribution, marketing and fostering key institutional customer relationships.



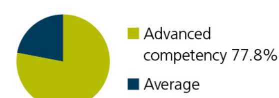
Public Policy

Experience in relevant public policy areas and key Government and regulator relationships.



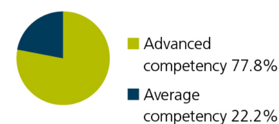
IT and Digital

Understanding of IT strategy, the application of technology in large organisations, and innovation.



People & Remuneration

Experience in building capable and highly engaged teams and understanding of current remuneration regulation, structuring and sectoral conditions.



3.3 Board committees

To assist it in undertaking its duties, the Board has established the following standing committees:

- Group Risk Committee;
- Group Audit Committee;
- Group Remuneration Committee; and
- Nomination Committee.

Each committee has its own charter, copies of which are available at:

> **challenger.com.au**

The charters specify the composition, responsibilities, duties, reporting obligations, meeting arrangements, authority and resources available to the committees and the provisions for review of the charter.

Details of Directors' membership of each committee and those eligible members' attendance at meetings throughout the period from 1 July 2020 to 30 June 2021 are set out below.

Directors' meetings

	Board		Group Risk Committee		Group Audit Committee		Group Remuneration Committee		Nomination Committee	
Director	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended
P Polson	11	11	4	4	4	4	5	5	3	3
R Howes[1]	11	11	—	—	—	—	—	—	—	—
J M Green	11	10	4	3	4	3	5	4	3	3
S Gregg	11	10	4	4	4	4	5	5	3	3
M Kobayashi	11	11	—	—	—	—	—	—	3	3
H Smith[2]	5	5	2	2	2	2	—	—	1	1
J Stephenson	11	11	4	4	4	4	5	5	3	3
D West	11	11	4	4	4	4	—	—	3	3
M Willis	11	11	4	4	4	4	—	—	3	3

1 The Managing Director and CEO attends the Group Risk Committee, the Group Audit Committee, the Group Remuneration Committee and the Nomination Committee meetings at the invitation of these committees.

2 Ms Smith was appointed a Director, and joined the Group Risk Committee, the Group Audit Committee, the Group Remuneration Committee and the Nomination Committee on 20 January 2021.

There are no management representatives appointed as members of any Board Committee.

3 Corporate governance summary (continued)

3.4 Risk management framework

Challenger's Board is responsible, in conjunction with senior management, for the management of risks associated with the business and implementing structures and policies to adequately monitor and manage these risks.

The Board has established the Group Risk Committee (GRC) and the Group Audit Committee (GAC) to assist in discharging its risk management responsibilities. In particular, these committees assist the Board in setting the appropriate risk appetite and for ensuring that there is an effective risk management framework that is able to manage, monitor and control the various risks to which the business is exposed.

The Executive Risk Management Committee (ERMC) is an executive committee chaired by the Chief Risk Officer which assists the GRC, GAC and Board in discharging their risk management obligations by implementing the Board-approved risk management framework. On a day-to-day basis, the Risk division, which is separate from the operating segments of the business, has the responsibility for monitoring the implementation of the risk framework, including the monitoring, reporting and analysis of the various risks faced by the business, and providing effective challenge to activities and decisions that may materially affect Challenger's risk profile.

Challenger has a robust risk management framework which supports its operating segments, and its risk appetite distinguishes risks from which Challenger will seek to make an economic return from those which it seeks to minimise and which it does not consider will provide a return. The management of these risks is fundamental to Challenger's business, customers and to building long-term shareholder value. Challenger is also prudentially supervised by APRA, which prescribes certain prudential standards that must be met by Challenger and its life insurance subsidiary, CLC. APRA also supervises authorised deposit-taking institutions (ADI) and accordingly will supervise prudential standards relevant to MyLifeMyFinance Limited, the bank which Challenger agreed to purchase in December 2020.

In addition to having a separate risk management function, Challenger recognises that a requirement for an effective risk management framework is for there to be a strong risk culture throughout the organisation, where risk is everybody's business. The foundation of this risk culture is a set of values, the Challenger IACT values. All employees are assessed against the Challenger IACT values as part of the annual performance review process, and this outcome contributes to the overall performance rating and remuneration outcomes. In addition to this, Challenger regularly assesses its risk culture with a combination of external reviews and internal staff surveys to ensure that the management of risk and day-to-day compliance remains entrenched within the way in which Challenger operates. Challenger's risk appetite statement provides that, subject to earning acceptable economic returns, it can retain exposure to credit risk, property risk, equity risk and life insurance risk.

- credit risk – is the risk of loss due to a counterparty failing to discharge its contractual obligations when they fall due, a change in credit rating, movements in credit spreads, or movements in the basis between different valuation discount curves;
- property risk – is the potential impact of movements in the market value of property investments on Challenger's income and includes leasing and tenant default risk which may impact the cash flows from these investments;
- equity risk – is the potential impact of movements in the market value of listed equity investments, unlisted equity investments and investments in absolute return strategies. Absolute return strategies are generally uncorrelated to listed equity market returns. Challenger holds equities as part of its investment portfolio in order to provide diversification across the investment portfolio; and
- life insurance risk – represents both longevity risk and mortality risk. Through selling lifetime annuities and assuming wholesale reinsurance agreements, CLC takes longevity risk, which is the risk that customers live longer, in aggregate, than expected. This is in contrast to mortality risk, which is the risk that people die earlier than expected. CLC is exposed to mortality risk on its wholesale mortality reinsurance business.

Challenger seeks to minimise the risks for which it does not consider an appropriate return can be generated. These risks include:

- foreign exchange risk – is the risk of a change in asset values as a result of movements in foreign exchange rates;
- interest rate risk – is the risk of fluctuations in Challenger's earnings arising from movements in interest rates;
- inflation risk – is the risk of fluctuations in Challenger's earnings from movements in inflation rates;
- operational risk – is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events; and
- regulatory and compliance risk – is the risk of legal or regulatory sanctions or loss as a result of Challenger's failure to comply with laws, regulations or regulatory policy applying to its business.

Further details on Challenger's approach to risk management are included in both the 2021 Sustainability Report and Section 5 of this report.

4 Remuneration report

Letter from the Chairs of the Board and Remuneration Committee

Dear Shareholders

Following the significant disruptions of recent years, Challenger finished 2021 in strong shape, with a high level of capital, record assets under management, more diversified distribution and a clear strategy for growth.

This year we have taken significant steps to respond to shareholder concerns about remuneration outcomes last year, with changes to our framework and communications, and differentiated outcomes for executives that reflect the performance of our different businesses.

Our response to shareholder concerns in relation to the 2020 remuneration report

At our 2020 Annual General Meeting, we incurred a 'first strike' with 28.25% of votes cast against the adoption of the 2020 remuneration report. The Board takes this outcome very seriously and recognises that decisions we made last year about how we reward our executives were not in line with the expectations of all of our shareholders.

We have taken significant action during 2021, which has focused on three key aspects:

- working closely with shareholders to ensure that their concerns are well understood;
- reviewing the executive reward framework to ensure it remains 'fit for purpose' in the current environment; and
- ensuring 2021 reward decisions appropriately reflect performance and are communicated clearly.

Primarily, shareholders were disappointed that we awarded short term incentives (STIs) in a year where Challenger incurred a large statutory loss and shareholders experienced a decline in share price and reduced dividend income. Shareholders also told us that there was insufficient transparency around discretion applied to reduce STI outcomes.

Other concerns included the role of normalised earnings in determining STI outcomes, specific features of our long term incentives (LTIs) and Non-Executive Director fees. We have responded to these concerns in a range of ways set out on page 30 of this report.

2021 reward outcomes

Shareholder concerns have been front of mind in making reward decisions during 2021. Supported by the framework changes outlined below, key reward decisions for 2021 include:

- the CEO's STI outcome is 56% of target (37% of maximum);
- STI outcomes for other Key Management Personnel (KMP) range between 56% and 98% of target opportunity (37% and 65% of maximum) with the degree of differentiation reflective of the relative performance of the Life and Funds Management businesses;
- in determining these STI outcomes, the Board used its discretionary modifier to apply a 30% downward adjustment to further reflect the extent of the impact caused by the events of 2020 and the flow-on impact into 2021; and
- no LTIs will vest in September 2021 for the third consecutive year demonstrating strong alignment of executives' realised reward with shareholder outcomes.

We have also continued to take advantage of opportunities to rebase remuneration arrangements. In 2021 this has included the appointment of a new Chief Financial Officer and the expansion of Ms Murphy's role on appointment as Chief Executive, Life, both with significantly lower target and maximum total reward than their predecessors. Across all KMP roles, STI targets have been set materially below historic outcomes.

The Board notes that following a period of lower employee movement in our sector, there is now strong demand for financial services executives and it is important to ensure our framework continues to support us to attract and retain top talent.

A more transparent reward framework

We have reflected on concerns raised by shareholders in relation to our approach to STIs last year. The Board exercised significant discretion in 2019 and 2020 to reduce STIs and acknowledges that communication of the link between reward and performance in these circumstances can be improved.

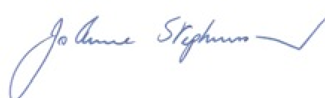
We have made two changes to the reward framework that are designed to work together to address these concerns. Firstly, we have introduced STI targets for executives to provide clarity on what the Board considers to be an appropriate STI outcome for individual and business performance in line with expectations, thereby supporting a clearer link between pay and performance. Secondly, we have introduced an STI modifier which makes explicit the rationale for, and magnitude of, discretionary adjustments made by the Board.

Importantly, we have included additional disclosures to provide greater transparency on performance outcomes and to clearly communicate the Board's decision-making processes and use of discretion in determining reward outcomes.

Looking forward

Continuing to engage with you as our shareholders will be a key priority for 2022 and beyond. This will be particularly important as we expect to make further changes to our reward framework when APRA finalises its new prudential standard on remuneration.

Yours sincerely



Peter Polson
Board Chair

JoAnne Stephenson
Remuneration Committee Chair

4 Remuneration report (continued)

4.1 Contents

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4.2 Key Management Personnel

Challenger's executive Key Management Personnel (KMP) for 2021 are detailed in the table below:

Name	Role	Term as KMP in 2021
Current KMP		
Richard Howes	Managing Director & Chief Executive Officer	Full year
Rachel Grimes[1]	Chief Financial Officer	From 3 May 2021
Nick Hamilton	Chief Executive, Funds Management	Full year
Angela Murphy[2]	Chief Executive, Life	Full year
Chris Plater[3]	Chief Executive, Operations & Technology	Full year
Former KMP		
Anton Kapel[4]	Acting Chief Executive & Chief Investment Officer, Life	From 7 December 2020 until 9 March 2021
Andrew Tobin[5]	Chief Financial Officer	Until 31 March 2021

1 Ms Grimes was appointed to the role of Chief Financial Officer on 3 May 2021 and was designated as KMP from the date of appointment.
2 Ms Murphy was appointed to the role of Chief Executive, Life on 10 March 2021. Prior to this, Ms Murphy held the role of Chief Executive, Distribution, Product & Marketing. Ms Murphy was designated as KMP for the full year.
3 Mr Plater was appointed to the role of Chief Executive, Operations & Technology on 7 December 2020. Prior to this, Mr Plater held the role of Chief Executive & Chief Investment Officer, Life. Mr Plater was designated as KMP for the full year.
4 Mr Kapel was appointed to the role of Acting Chief Executive & Chief Investment Officer, Life from 7 December 2020 until 9 March 2021. Mr Kapel was designated as KMP for the duration of the interim appointment.
5 Mr Tobin ceased employment on 31 March 2021 and was designated as KMP until this date.

Challenger's Non-Executive Directors for 2021 are detailed in the table below:

Name	Term as Non-Executive Director in 2021
Peter Polson (Chair)	Full year
John M Green	Full year
Steven Gregg	Full year
Masahiko Kobayashi[1]	Full year
Heather Smith	Appointed 20 January 2021
JoAnne Stephenson	Full year
Duncan West	Full year
Melanie Willis	Full year

1 Hiroyuki Iioka is an alternate director to Masahiko Kobayashi.

The term KMP is used throughout the Remuneration Report to refer to executive KMP only.

4 Remuneration report (continued)

4.3 Our response to shareholder concerns in relation to the 2020 remuneration report

The Board takes shareholder concerns very seriously and has taken significant action during 2021, with a focus on:

1. Shareholder engagement	2. Reward framework changes	3. 2021 reward decisions
Engagement increased Concerns well understood Consultation on proposed changes	Introduction of STI targets Introduction of an STI modifier Enhanced governance and disclosures	Linked to performance Appropriately differentiated Clearly communicated

Our understanding of shareholder concerns and how we have sought to address these concerns is summarised below. Further detail on reward framework changes and a summary of 2021 reward outcomes are provided on the following pages.

What we heard	What we changed and why
STI outcomes were not aligned to performance Shareholders' primary concern was that payment of STIs to KMP for 2020 was not appropriate given the large statutory loss and the shareholder experience.	• Introduced STI target opportunities to support a clearer link between performance and reward by providing clarity on what the Board considers to be an appropriate STI outcome for individual and business performance in line with our high expectations. • Enhanced the disclosures of performance and STI outcomes, including an assessment against each sub-measure in the CEO's balanced scorecard and a new table showing KMP STI outcomes as a percentage of target and maximum. • Determined 2021 STI outcomes for KMP which are linked to overall group performance and appropriately differentiated to reflect business unit and individual performance.
Use of discretion in determining STI outcomes was not clear There was insufficient transparency in relation to the rationale for, and the magnitude of, the Board's exercise of discretion to reduce STI outcomes.	• Introduced an STI modifier to make explicit the range of factors considered by the Board in applying discretion to performance and reward outcomes. This retains discretion as an important governance tool while enhancing transparency around the magnitude of, and the rationale for, adjustments. • The modifier works together with the STI targets to support clear differentiation of reward outcomes to reflect variation in business unit and individual performance while demonstrating the shared accountability for group performance and material matters with a group-wide impact.
STIs are too closely linked to normalised profit Shareholders questioned the role of normalised profit in determining both STI outcomes for the KMP and the size of the group variable reward pool.	• Clarified that normalised profit is one of a range of performance measures rather than the sole or predominant measure in determining STIs and the variable reward pool via: – enhanced disclosures in the CEO's scorecard which clarify the range of financial measures included in assessing performance and performance against each of them; – introduced an STI modifier (as noted above) which makes the factors driving discretionary adjustments, which may include financial measures, more explicit; and – enhanced disclosures relating to the variable reward pool to clarify that the pool is built on a 'bottom-up' basis with a range of 'top-down' lenses applied, of which the target funding range of 10% to 15% of normalised profit is one. • The Board is committed to continuing to review the appropriateness of key financial measures and their role in determining reward outcomes.
Overall quantum of KMP remuneration is too high Shareholders considered total awarded remuneration to be high, primarily driven by the quantum of LTI awards.	• Set new STI targets which represent a reduction versus historic outcomes. For example, the CEO's target is set 33% below the actual 2018 outcome for his predecessor. • Reduced the maximum STI opportunity (from 200% to 150% of fixed pay) and the quantum of LTI awards (from 225% to 125% of fixed pay) for control and support function roles[1] under the new framework. • Re-based remuneration arrangements with the appointment of Ms Grimes as Chief Financial Officer (total reward opportunity is 26% lower than her predecessor) and Ms Murphy as Chief Executive, Life (10% lower than her predecessor).
Single LTI hurdle and cumulative five-year test Shareholders questioned the appropriateness of the absolute TSR as a single measure and the cumulative five-year test.	• Committed to undertaking a comprehensive review, including extensive consultation with shareholders, once APRA's new standard[2] is finalised. • Determined to retain the current LTI structure at this time having reflected deeply on: – the inherent challenges with shareholder return measures (both absolute and relative), particularly during periods of market volatility; – adding a second financial measure, noting this would not align with upcoming regulatory requirements to have a material weighting to non-financial measures and that multiple changes to measures may lead to inconsistent vesting outcomes; and – the appropriateness of the five-year cumulative test, noting that the test is applied against a higher hurdle and therefore differs from traditional 're-tests'.
Non-Executive Director fees Non-Executive Director fees are considered high versus market with particular concern expressed in relation to the Chair's fees.	• Engaged KPMG to conduct an independent review of Non-Executive Director fees which will be finalised in 2022 once changes to committee and sub-Board structures as a result of the acquisition of MyLife MyFinance are confirmed. • The Board notes that the retirement of the current Chair will provide a natural opportunity to review and, if appropriate, reset the Chair fees.

[1] Grandfathering arrangements apply for the Chief Executive, Operations & Technology.
[2] APRA's new prudential standard CPS511 ***Remuneration***.

4 Remuneration report (continued)

4.3 Our response to shareholder concerns in relation to the 2020 remuneration report (continued)

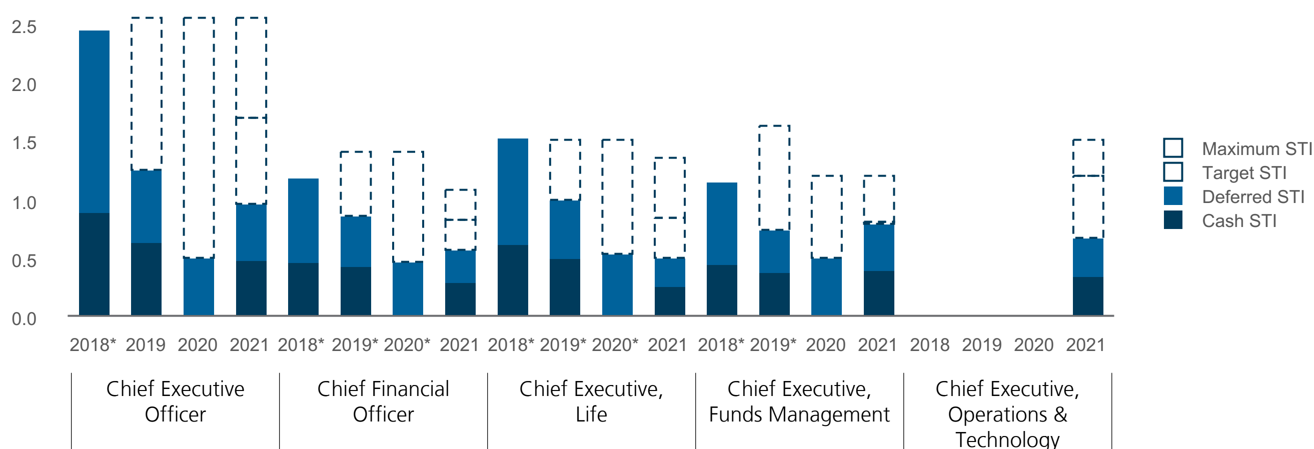
Summary of 2021 reward outcomes

Shareholder concerns have also been front of mind in making reward decisions during 2021, including annual reward outcomes and remuneration arrangements for new appointments during the year. These are summarised in the table below.

STI outcomes for KMP	• STI outcomes are significantly down again on historic outcomes. The CEO's 2021 STI is 56% of target (37% of maximum) and STIs for other KMP range between 56% and 98% of target (37% and 65% of maximum). • These outcomes reflect a 30% discretionary adjustment (via the new STI modifier) which the Board determined to apply to reflect the extent of the impact of the events of 2020 and the flow-on impact into 2021.
Annual fixed remuneration increases for KMP	• No annual increases were applied for KMP for financial year 2021. • The only annual increase to fixed remuneration planned for financial year 2022 is for the Chief Executive, Funds Management, to reflect the additional size and complexity of this role and to recognise the importance of retaining Mr Hamilton, noting fixed pay will still be 17% lower than his predecessor.
Remuneration arrangements for new appointments	• Ms Murphy's fixed remuneration was increased on her appointment as Chief Executive, Life in March 2021. Her fixed remuneration is 10% lower than her predecessor, noting the size and complexity of the role has significantly increased. • In addition, the rebasing of remuneration arrangements as incumbents have been replaced has continued, with Ms Grimes' total maximum remuneration opportunity on appointment as Chief Financial Officer being 26% lower than her predecessor.
No vesting of LTIs for third consecutive year	• LTIs will not vest in September 2021 for the third consecutive year, demonstrating the strong alignment between executives' realised reward and shareholder outcomes.

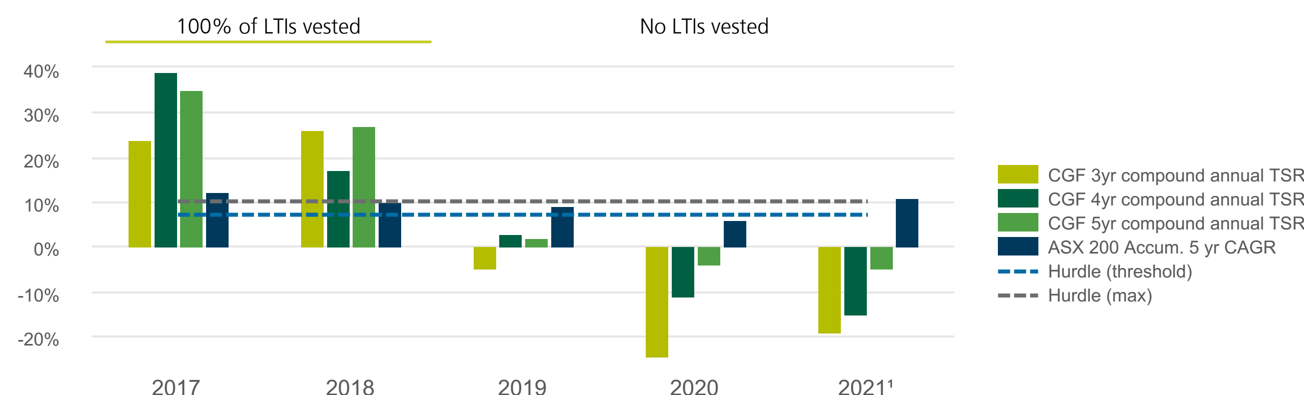
Short term incentive outcomes

The chart below sets out 2021 STI outcomes ($m) together with target and maximum opportunities (on an annualised basis) by role. Outcomes are in respect of the incumbent as at 30 June each year (prior incumbents are denoted with an asterisk).



Long term incentive vesting outcomes

The chart below illustrates Challenger's compound annual TSR performance over time versus the S&P/ASX 200 Accumulation Index five year compound annual growth rate (CAGR).



[1] Indicative outcomes based on Challenger's share price as at 30 June 2021.

4 Remuneration report (continued)

4.3 Our response to shareholder concerns in relation to the 2020 remuneration report (continued)

Further detail on reward framework changes

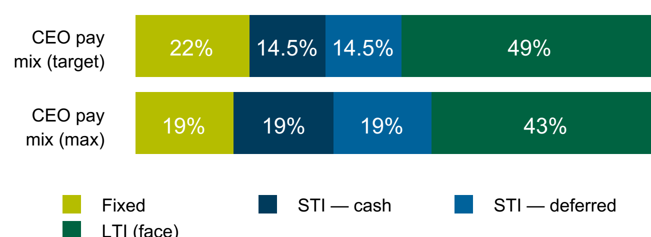
Pay mix framework and short term incentive targets

A pay mix framework, including STI targets, has been introduced to provide greater transparency and consistency in setting executive remuneration packages. The framework, which includes STI targets and LTI as a percentage of fixed pay, is set out below.

	STI target (% of fixed)	STI max (% of fixed)	LTI face value (% of fixed)
CEO & business lines	133%	200%	225%
Control & support functions	100%	150%	125%

Maximum STI opportunity is 150% of target which retains the maximum opportunity of 200% of fixed pay (which was introduced in 2019) for the CEO and business lines and results in a reduction in maximum opportunity for control and support functions.

For completeness, the chart below illustrates the pay components as a percentage of total reward for the CEO at both target and maximum.



Pay mix is differentiated between business lines and control functions with a lower weighting to variable reward for control functions. This aligns with regulator and shareholder expectations and promotes the independence of control functions. A significant portion continues to be delivered as LTI to provide alignment with shareholders.

The new STI targets:

- provide a reference point reflecting what the Board considers to be an appropriate STI outcome for individual and business performance in line with expectations. This builds on the maximum STI opportunity which has applied since 2019;
- set a consistent ratio of target to maximum reward (maximum is 150% of target) providing appropriate leverage to differentiate for outperformance; and
- support a clearer link between performance and reward outcomes and facilitates comparisons against internal and external benchmarks.

The application of this framework aligns with the rebasing of executive remuneration packages over time. The STI targets are lower than historic outcomes for prior incumbents and, as noted above, the maximum STI opportunity is reduced for control function roles.

The STI outcomes chart on the previous page illustrates how the new STI targets are positioned versus historic outcomes, noting that 2018 is considered a more typical performance year than 2019 or 2020.

STI targets have been set in line with the framework for the majority of roles. However, arrangements for Mr Plater have been 'grandfathered' by applying the business line pay mix and setting the STI target above 133% of fixed pay (maximum STI opportunity and LTI are per the framework). The Board considers this approach to be appropriate given:

- Mr Plater's STI opportunity in his former role as Chief Executive & Chief Investment Officer, Life;
- the criticality of the Chief Executive, Operations & Technology role in delivering on strategic priorities; and
- the importance of retaining Mr Plater as key talent and developing leadership capability.

The pay mix for the newly appointed Chief Financial Officer is slightly outside the framework with an STI target of 112.5% of fixed pay. These arrangements will be transitioned over time.

Short term incentive modifier

The other significant change is the introduction of a modifier to make explicit the factors considered by the Board in applying discretion in determining STI outcomes.

The modifier provides greater transparency in the Board's decision-making processes by quantifying the magnitude of discretionary adjustments. In applying the modifier, the Board considers a broad range of factors, including the quality of financial results, risk and conduct matters with a group-wide impact and any other matter which the Board considers is not fully reflected in scorecard outcomes.

STI outcomes for KMP (excluding the CEO) are calculated by applying the modifier to pre-adjustment STI outcomes, as recommended to the Board by the CEO and as illustrated below. Pre-adjustment STI outcomes reflect performance outcomes which are informed by individual, business unit and group performance and an assessment of behaviours against the Challenger values.

Pre-adjustment STI outcome (0-150% of target)	x	Modifier (0-100%)	=	Final STI outcome (0-150% of target)

The modifier can vary between zero and 100% thereby acting as a gateway and a downwards adjustment mechanism. The modifier cannot adjust STI outcomes upwards as individual behaviours (including risk behaviours) already act as a modifier in determining individual performance outcomes.

A consistent modifier generally applies for all KMP to reflect shared accountability for group performance and other significant factors, for example, where a risk or conduct matter has a group-wide impact.

Enhancements to disclosures

Performance disclosures have been enhanced to provide greater transparency via an assessment against each sub-measure in the scorecard.

The Board has elected not to disclose specific targets as it deems this information to be commercially sensitive due to KPIs being linked directly to Challenger's strategic priorities. The Board will review this practice on an ongoing basis and consider input from stakeholders regarding changing this practice in the future.

4 Remuneration report (continued)

4.4 Remuneration strategy and structure

Our vision and strategic priorities for 2021

Challenger IACT values: Act with Integrity, Aim High, Collaborate, Think Customer

Remuneration strategy — guiding principles

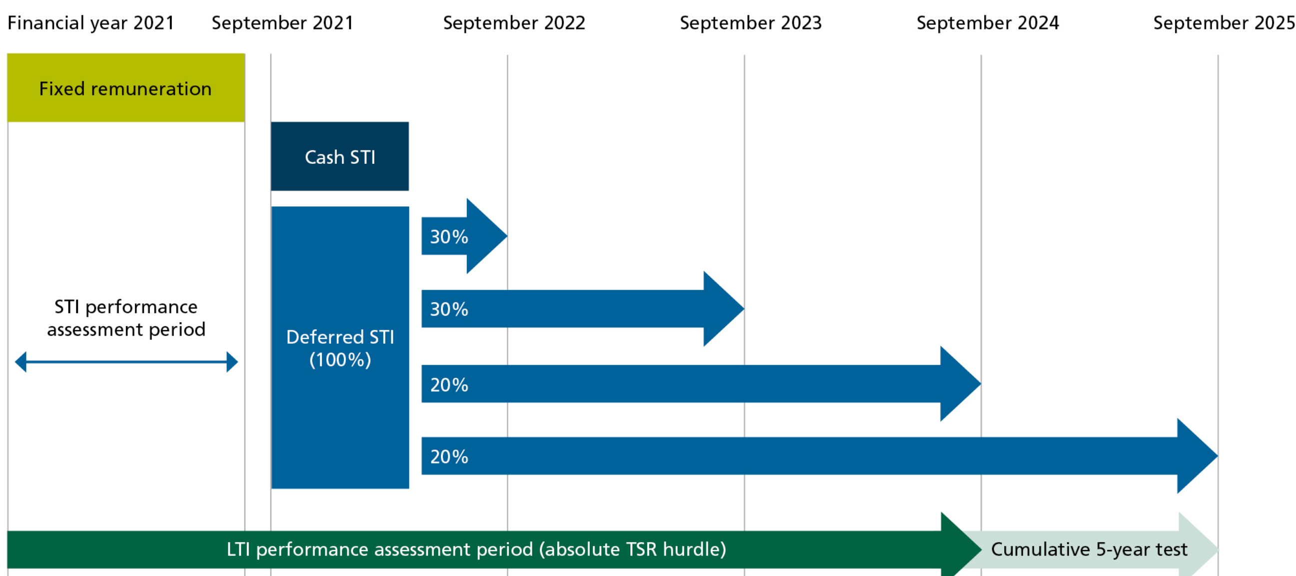
Market-competitive	Performance-based and equitable	Aligned with shareholders	Underpinned by sound risk management

Remuneration structure for KMP

Fixed remuneration	Variable remuneration — Short term incentives	Variable remuneration — Long term incentives
Base salary, salary-sacrificed benefits and applicable fringe benefits tax. Employer superannuation contributions. Positioned around the market median using appropriate benchmarks, reflecting size and complexity of role, responsibilities, experience and skills.	Maximum opportunity of 200% of fixed remuneration (150% for control and support functions). Annual 'at risk' remuneration, rewarding Challenger performance and individual performance and behaviours. 50% is deferred into equity vesting over four years, subject to forfeiture provisions.	225% of fixed remuneration at face value (125% for control and support functions). Longer-term 'at risk' remuneration. Awarded as hurdled share rights vesting up to five years. Awards are subject to a cumulative absolute TSR hurdle tested after four or five years and subject to forfeiture provisions.

Delivery of remuneration for 2021

Reward is realised over an extended period supporting a focus on strong risk management and long-term performance. Significant weighting to variable remuneration means a large proportion of executive reward is at risk and issued in equity with long deferral, ensuring strong alignment with shareholders.



4 Remuneration report (continued)

4.5 Short term incentives

Structure of short term incentives

STIs provide annual 'at risk' remuneration which rewards Challenger and individual performance and behaviours. A significant portion is deferred into equity to provide strong alignment with shareholder interests and support retention. STI terms are set out in the table below.

The introduction of STI target opportunities for 2021 provides greater transparency on reward opportunity and enables Challenger to demonstrate more clearly the link between performance and reward outcomes. In addition, the new STI modifier makes explicit the range of factors considered by the Board in making discretionary adjustments to STI outcomes. The operation of the new STI targets and the modifier in determining 2021 STI outcomes for KMP is detailed on page 32.

Performance period	Annual in line with Challenger's financial year.
Award determination	STIs are determined with reference to the performance of Challenger, and individual performance and behaviours. Individual performance is assessed based on: • a balanced scorecard comprising financial, people and culture, customer and strategic KPIs and application of, and adherence to, the risk management framework; and • behaviour in line with the Challenger values which is a gate-opener and a modifier. The Board may apply the new STI modifier to adjust STI outcomes to reflect a broad range of factors.
STI opportunity	Target STI opportunity is 133% of fixed remuneration for the CEO and business line roles and 100% of fixed remuneration for control function roles. Maximum STI opportunity is 150% of target STI.
Delivery	Ordinarily, 50% of the STI award is delivered as cash and 50% is deferred into equity. For 2020, there was no cash STI for KMP as 100% was deferred into equity. Deferred STI awards are delivered as Restricted Shares. Prior to 2021, deferred STI awards were delivered as Deferred Performance Share Rights (DPSRs) which represent the right to receive a fully-paid ordinary Challenger share for nil consideration subject to continued employment at the time of vesting.
Allocation methodology	Face value with the number of Restricted Shares or DPSRs granted based on the five-day VWAP of shares prior to grant date.
Vesting period	Deferred STI awards vest over a four-year period in accordance with the schedule below: **At the end of year** — **% of grant vesting** 1 — 30% 2 — 30% 3 — 20% 4 — 20% Awards made prior to September 2019 vested in two equal tranches after one and two years.
Vesting conditions	Vesting is subject to continued service.
Termination treatment	Termination for cause will result in forfeiture of all unvested equity awards. Awards issued from 1 July 2019 onwards are subject to specific good leaver conditions specified at the time of grant, which apply unless the Board exercises its discretion to do otherwise. Where the 'good leaver' treatment applies, unvested equity remains 'on foot' i.e. it will vest on the original vesting date. Board discretion applies in relation to unvested awards issued prior to 30 June 2019.
Forfeiture (malus)	The Board has the ability to adjust unvested equity (including to zero) in a range of circumstances, including to protect financial soundness or respond to unexpected or unintended consequences that were significant and unforeseen by the Board (such as material risk management breaches, unexpected financial losses, reputational damage or regulatory non-compliance).

Summary of 2021 financial performance

This section provides performance information including five-year trends and key financial and operational outcomes for the year. Further commentary on performance is provided in the CEO's balanced scorecard on the following page.

For the year ended	30 June 2017	30 June 2018	30 June 2019	30 June 2020	30 June 2021
Normalised NPAT[1] ($m)	384.9	384.9	396.1	343.7	278.5
Normalised EPS (cents)	68.5	68.1	65.5	56.5	41.5
Closing share price ($)	13.34	11.83	6.64	4.41	5.41
Dividends per share (cents)	34.5	35.5	35.5	17.5	20.0

[1] Normalised NPAT excludes asset or liability valuation movements that are above or below expected long-term trends and significant items that may positively or negatively impact financial results. Refer to the Operating and financial review section for further information.

4 Remuneration report (continued)

4.5 Short term incentives (continued)

2021 balanced scorecard outcome for the CEO

KPIs are aligned to Challenger's vision and strategy and underpinned by strong risk management practices that inform how we deliver on our commitments to customers and shareholders. The CEO's 2021 balanced scorecard is provided below.

Measures	Performance
Financial (40%)	**Partially met**
Profitability Not met Met Exceeded	**Group normalised NPBT:** $395.8 million, within guidance range ($390.0m to $440.0m) **Statutory profit after tax:** $592.3 million, up $1.0 billion on 2020 with full reversal of unrealised pandemic market losses **Normalised ROE:** 11.2%, below the through-the-cycle ROE target as expected due to holding significant cash balance through the pandemic
Capital Not met Met Exceeded	**Capital position:** strong at 1.63 times APRA's prescribed capital amount (PCA) and above the top end of 1.3 to 1.6 times target range which applied during the year
AUM Not met Met Exceeded	**Group AUM:** up 29.1% to $110.0 billion, significantly above target **Life sales:** $6.9 billion up 34.5%, with growth in all key segments and significantly above target **Life book growth:** 14.4%, significantly above target **Funds Management net flows:** $16.1 billion, one of the fastest growing Australian active managers, industry leading and significantly above target. Fidante ranked top active manager for retail net flows[1] **Funds Management FUM:** $105.8 billion, up 30.0% and significantly above target. Four boutique fund managers' FUM exceeded $10m (one in 2020)
People & culture (30%)	**Met**
Risk culture Not met Met Exceeded	**Risk culture:** strong at 86%[2], which is 4% above Global High Performance Norm (GHPN) and 10% above Australian National Norm. Risk focus supported by internal and external auditors **Responsible investment:** 'A' rating Principles for Responsible Investment Assessment Report 2020
Employee engagement Not met Met Exceeded	**Sustainable engagement:** high at 85%[2], which is up 1% on 2019 and in line with the GHPN **Flexible hybrid working:** model established for employees with focus on technology upgrades and support for mental health
Diversity Not met Met Exceeded	**Gender equality:** recognised as Employer of Choice by Workplace Gender Equality Agency, included in 2021 Bloomberg Gender-Equality Index and Equileap Global Top 100 employer for gender equality. Female representation at 44% overall (target: 45%) with 41% in management (target: 40%) and 37.5% on the executive team, being the highest ever level
Customer (20%)	**Met**
Customer satisfaction & support Not met Met Exceeded	**Customer satisfaction:** high satisfaction rating (91%) maintained, Net Promoter Score up 13 percentage points to 35%[3], 60% rate Challenger as better than other financial companies and 87% rate Challenger as trustworthy **Awards:** winner of 'Long Term Income Stream' and 'Overall Annuity Provider' categories at 2021 Association of Financial Advisers Life Company of the Year Awards, Fidante named distributor of the year at 2020 Zenith Fund Awards **Process improvements:** online origination process delivered, improving average application turnaround time by 69%
Expand products & distribution channels Not met Met Exceeded	**Fidante Partners partnerships & products:** new partnerships with Impax Asset Management, Proterra Investment Partners and Nomura; new boutique Ox Capital Management; new products from Ares Australia Management, Alphinity and Ardea **Life institutional channel:** significant growth with AUM increasing 50% through enhanced product offering and new profit-for-member fund relationships **Funds Management global diversification:** significant offshore mandates won and new Singapore office **CIP Asset Management expansion:** three new retail-focused credit funds and won Japanese real estate mandate
Strategic (10%)	**Met**
Progress growth strategy Not met Met Exceeded	**Digital bank acquisition:** extends customer and product reach and accelerates strategy to enter term deposit market and build more direct customer relationships. **Corporate strategy:** refreshed to drive future growth following acquisition of the Bank and updated sustainability strategy with increased focus on responsible investing
Overall outcome	**Partially met**

1 Top performing fund manager among 117 active managers - Plan for Life Wholesale Trust Data, September 2020
2 Willis Towers Watson employee engagement survey April 2021.
3 Fifth Quadrant, February 2021.

4 Remuneration report (continued)

4.5 Short term incentives (continued)

2021 short term incentive outcomes

2021 STI outcome for the CEO (as a % of target): 56%

The Board determined a pre-adjustment STI outcome of 80% of target which reflects the overall performance outcome of 'partially met' as set out in the balanced scorecard above together with an assessment of Mr Howes' behaviours as strongly in line with the Challenger values and risk management outcomes. The Board has applied a modifier of 70% to the pre-adjustment outcome (as discussed in further detail below) to reflect the extent of the impact of the events of 2020 and the flow-on impact into 2021. After application of the modifier the final STI outcome is 56% of target (37% of maximum).

2021 modifier

The Board recognises that the balanced scorecard outcome does not always capture the full range of factors that are relevant to making reward decisions and that the ability to make discretionary adjustments is an important governance mechanism.

The new modifier makes explicit these discretionary considerations and enables the Board to clearly communicate the magnitude of, and the rationale for, adjustments to STI outcomes.

STI outcomes for other KMP are calculated by applying the modifier to pre-adjustment STI outcomes as recommended to the Board by the CEO as illustrated below.

Pre-adjustment STI outcomes, expressed as a percentage of target STI, reflect individual performance outcomes which are assessed based on:

- a balanced scorecard comprising financial, people and culture, customer and strategic KPIs and application of, and adherence to, the risk management framework; and
- behaviours in line with the Challenger values which is a gate-opener and a modifier.

2021 STI modifier: 70%

The Board has determined to apply a modifier to 2021 STI outcomes for KMP.

The Chief Risk Officer has confirmed that no risk or conduct matters have been identified which would warrant the application of the modifier.

However, the Board considers it appropriate to adjust outcomes to recognise the extent of the impact caused by the events of 2020 and the flow-on impact into 2021.

Pre-adjustment STI outcome (0-150% of target) x Modifier (0-100%) = Final STI outcome (0-150% of target)

2021 short term incentive outcomes for KMP

The table below sets out the 2021 STI outcomes for current KMP as a percentage of target and maximum, including the impact of the modifier. STI targets do not apply to former KMP; however, a discretionary adjustment has been applied to what would otherwise have been awarded.

STI outcomes for KMP range between 56% and 98% of target (37% and 65% of maximum). While aggregate outcomes are up on 2020, they are still materially down versus historical outcomes as illustrated in the chart in section 4.3.

	2021 STI outcomes		
	Pre-adjustment	Final	
	% of target	% of target	% of max
R Howes	80%	56%	37%
R Grimes	100%	70%	51%
N Hamilton	140%	98%	65%
A Murphy	80%	56%	37%
C Plater	80%	56%	45%
Average	**96%**	**67%**	**47%**

There is significant variability in outcomes to differentiate for business unit and individual performance. Most notably, the outperformance of the Funds Management business is reflected in the STI outcome for Mr Hamilton.

In addition, accountability for the performance of the Life business is reflected in the outcomes for both:

- Ms Murphy given both her current expanded role as Chief Executive, Life and her previous role as Chief Executive, Distribution, Product & Marketing; and
- Mr Plater who was Chief Executive & Chief Investment Officer, Life for the first five months of the year before taking on the role of Chief Executive, Operations & Technology.

4 Remuneration report (continued)

4.6 Long term incentives

Long term incentive structure

LTIs are awarded annually to support a continued focus on long-term performance and strong shareholder alignment. The meaningful weighting ensures a significant proportion of total reward is 'at risk' and directly linked to shareholder outcomes.

LTI terms are set out in the table below.

The Board considers that TSR is an effective measure of shareholder outcomes and that an absolute rather than a relative TSR performance measure is appropriate because:

- there are no other listed companies in the Australian market with a retirement income business that are directly comparable to Challenger;
- a broader index is not considered an appropriate peer group as there is risk of misalignment between remuneration and shareholder value creation; and
- if the absolute TSR threshold performance target is set at a level above average market returns over the long term, vesting will be directly linked to the delivery of superior returns to shareholders.

As part of its annual review, the Board determined to retain the thresholds of 7% to 10% (compounded annually) for 2021 on the basis they continue to be challenging in a low growth and low interest rate environment and represent a relatively strong return for shareholders. Over four years, 7% annual compound return represents total shareholder return of 31%, and 10% represents total shareholder return of 46%.

Where the hurdle is not satisfied at four years, a higher test is applied in year five (requiring total shareholder returns above 40% for any vesting to occur and total shareholder returns above 61% for full vesting to occur).

As a higher hurdle applies in year five, Challenger's approach differs from traditional 're-tests' and reflects our commitment to driving focus on long-term performance and strong risk management. Any unvested awards lapse after five years.

The Board continues to consider the appropriateness of introducing a second LTI performance measure and intends to undertake a comprehensive review of LTIs in light of impending regulatory change.

Quantum for KMP	225% of fixed remuneration for CEO and business lines and 125% for control and support functions.
Delivery	Hurdled Performance Share Rights (HPSRs) which represent the right to receive a fully-paid ordinary Challenger share for nil consideration subject to satisfaction of an employment condition and a performance hurdle.
Allocation methodology	Face value with the number of HPSRs granted based on the five-day VWAP of shares prior to grant date. HPSRs for the CEO are granted following the shareholder vote at the Annual General Meeting using the same allocation price as other KMP.
Vesting period and conditions	LTI awards vest after four or five years subject to satisfaction of an employment condition and Challenger satisfying the absolute TSR performance hurdle. Awards are tested after four years with any unvested HPSRs subject to a final cumulative test after five years. Awards made prior to September 2019 will continue to be tested after three or four years and subject to a final cumulative test after five years. Two-thirds of an award is eligible to commence vesting after three years and the final third after four years.
Performance hurdle	Vesting is subject to an absolute TSR performance hurdle set out in the table below: **Absolute TSR hurdle** — **% of HPSRs that vest** Less than 7% p.a. — 0% 7% to 10% p.a. — Straight-line vesting between 50% and 100% 10% p.a. and above — 100% The start and end price for absolute TSR performance testing is calculated using a 90-day VWAP leading up to the relevant performance start or end date. A 90-day VWAP eliminates the potential for short-term price volatility to impact vesting outcomes.
Termination treatment	Termination for cause will result in forfeiture of all unvested equity awards. Awards issued from 1 July 2019 onwards are subject to specific 'good leaver' conditions specified at the time of grant, which apply unless the Board exercises its discretion to do otherwise. Where the 'good leaver' treatment applies, unvested equity remains 'on foot', i.e. it will vest on the original vesting date, subject to satisfaction of the performance hurdle. Board discretion applies in relation to unvested awards issued prior to 30 June 2019.
Forfeiture (malus)	As detailed in the STI table in section 4.5 above.

Long term incentive vesting outcomes

No LTIs will vest in September 2021 for the third consecutive year. In September 2020, LTIs awarded in 2015, 2016 and 2017 were tested with annual compound TSR results of -4%, -11% and -25% respectively. As illustrated in the chart on page 31, the non-vesting of LTIs reflects strong alignment of executives' realised reward with shareholder outcomes.

4 Remuneration report (continued)

4.7 2021 awarded Key Management Personnel remuneration

Awarded remuneration represents the value of remuneration that has been awarded for the financial year, as determined by the Board, and includes fixed remuneration, STIs (cash and deferred) and LTIs. The actual value realised will depend on future performance outcomes, and LTIs will only deliver value to executives in the future if shareholder return hurdles are achieved. This ensures strong alignment with shareholder interests.

Awarded remuneration for KMP has been decreasing over time. This is driven by reductions to STI outcomes, reflecting the impact of challenging conditions on performance over the last three years, and the rebasing of remuneration arrangements as incumbents have been replaced, in line with broader market trends.

			Short term incentive					Long term incentive	
KMP	Year	Fixed[1] $	Total STI $	% of max	Cash STI $	Deferred STI[2] $	Other[3] $	Face value[2] $	Fair value[2] $
Current KMP									
R Howes	**2021**	**1,275,000**	**950,000**	**37%**	**475,000**	**475,000**	**23,902**	**2,868,750**	**1,270,856**
	2020	1,275,000	500,000	20%	—	500,000	25,709	2,868,750	1,199,138
R Grimes[4]	**2021**	**120,834**	**92,000**	**51%**	**46,000**	**46,000**	**—**	**1,208,333**	**600,118**
	2020	—	—	—	—	—	—	—	—
N Hamilton[5]	**2021**	**600,000**	**784,000**	**65%**	**392,000**	**392,000**	**6,944**	**1,518,750**	**672,806**
	2020	464,286	367,560	40%	—	367,560	3,696	1,044,643	436,661
A Murphy	**2021**	**610,699**	**465,000**	**37%**	**232,500**	**232,500**	**7,674**	**1,687,500**	**783,776**
	2020	583,298	400,000	34%	—	400,000	5,959	1,350,000	564,300
C Plater	**2021**	**750,000**	**672,000**	**45%**	**336,000**	**336,000**	**20,293**	**1,687,500**	**747,563**
	2020	750,000	525,000	35%	—	525,000	20,519	1,687,500	705,375
Former KMP									
A Kapel[6]	**2021**	**154,865**	**39,286**	**13%**	**32,738**	**6,548**	**385**	**118,241**	**52,381**
	2020	—	—	—	—	—	—	—	—
I Saines[7]	**2021**	**—**	**—**		**—**	**—**	**—**	**—**	**—**
	2020	192,262	—	—	—	—	—	—	—
A Tobin[8]	**2021**	**525,000**	**385,000**	**37%**	**192,500**	**192,500**	**—**	**—**	**—**
	2020	700,000	470,000	34%	—	470,000	17,079	1,575,000	658,350
Total	**2021**	**4,036,398**	**3,387,286**		**1,706,738**	**1,680,548**	**59,198**	**9,089,074**	**4,127,500**
	2020	3,964,846	2,262,560		—	2,262,560	72,962	8,525,893	3,563,824

1 Includes base salary and superannuation.
2 To be formally granted in September 2021 and allocated based on the five-day volume weighted average price (VWAP) prior to the grant date. Mr Howes' LTI will be granted following shareholder approval, which will be sought at Challenger's 2021 Annual General Meeting and allocated based on the same five-day VWAP as other KMP. The fair value is independently calculated and is also used to determine the accounting value which is amortised over future vesting periods. The fair value of 2021 LTIs has been estimated at 44.3% of face value based on the average fair value relative to face value of awards over the past three years. The fair value of 2020 LTIs was estimated at 41.8% of face value. Includes additional awards granted in May 2021 to Ms Grimes on appointment as Chief Financial Officer and Ms Murphy on appointment as Chief Executive, Life.
3 Values represent estimated distributions from the CPP Trust.
4 Ms Grimes became a KMP on 3 May 2021. The 2021 disclosure is pro-rata for the period in which she was KMP.
5 Mr Hamilton transferred to a KMP role on 23 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
6 Mr Kapel held a KMP role from 7 December 2020 to 9 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.
7 Mr Saines ceased to be a KMP on 22 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
8 Mr Tobin ceased to be a KMP on 31 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.

4 Remuneration report (continued)

4.8 Remuneration governance

Challenger's remuneration governance structures, outlined in the table below, provide strong oversight of remuneration practices and policies. Detailed information concerning the scope of the Board and the Remuneration Committee's responsibilities can be found under the corporate governance section of Challenger's website.

Remuneration governance arrangements promote compliance with the provisions of the ASX Listing Rules, the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations, the ***Corporations Act 2001*** and, in respect of CLC and Challenger Retirement and Investment Services Limited, the principles contained in the Australian Prudential Regulation Authority standards CPS 510 and SPS 510 respectively.

Board	• The Board is responsible for ensuring effective remuneration governance and related risk management practices. • Board approves remuneration principles and structures and ensures that they are competitive and equitable and that they support the long-term interests of Challenger. • The Board receives recommendations from the Remuneration Committee and approves these remuneration recommendations, where appropriate.
Remuneration Committee	• Board convenes a Remuneration Committee comprising at least three Independent Directors to assist the Board in discharging its responsibilities. • The Remuneration Committee meets at least five times during the year, with additional meetings scheduled as required. For the year ended 30 June 2021, five meetings were held. • The Remuneration Committee determines and recommends to the Board various principles and policies (including remuneration, recruitment, retention, termination and diversity), Managing Director & CEO and KMP remuneration, incentives, superannuation and life insurance arrangements, and the Directors' remuneration framework.
Independent remuneration advisers	• The Board, independent of management, appoints an adviser to the Remuneration Committee. • In 2021, the Board continued its engagement of KPMG. This engagement is based on a defined set of protocols. The Board is satisfied with KPMG's remuneration structure and quantum-related advice and that such advice is free from undue influence. • During 2021, KPMG attended all the Remuneration Committee meetings and provided advice with respect to KMP remuneration arrangements, updates on regulatory developments, tax advice and a review of sales incentive plans. No 'remuneration recommendations', as defined by the ***Corporations Act 2001,*** were provided by KPMG. • Mercer was retained in 2021 to independently value DPSRs and HPSRs and test HPSR vesting outcomes.

Remuneration benchmarking

Challenger's remuneration strategy is supported by a strong focus on benchmarking remuneration against the external market to roles with comparable financial services, banking, insurance and capital markets skills.

Annually, the Board approves the peer groups to be used when benchmarking KMP remuneration, and in 2021 approved the following peer groups:

1. **Financial Industry Remuneration Group survey:** This peer group supports consideration of roles with comparable financial services, banking, insurance and capital markets skills to Challenger's KMP.
2. **Financial services publicly disclosed data:** Data is comprised of publicly disclosed KMP remuneration data for select financial services companies. This peer group supports consideration of roles with comparable skills to Challenger's KMP.

During 2021, the Board considered remuneration benchmark data as an input when introducing STI targets, setting remuneration arrangements for new appointments and determining 2021 remuneration outcomes for KMP. The Board is confident that awarded remuneration reflects performance and is positioned and structured at a market-competitive level reflective of the markets in which Challenger competes for talent, and the specialist nature of the skills and experience of Challenger KMP.

Variable remuneration governance

The Board approves a pool for total variable remuneration (cash STI and share-based) annually.

The group pool is built on a bottom-up basis with individual allocations informed by internal and external market remuneration levels and individual contribution. Divisional pools for business lines are adjusted by the CEO to reflect contribution to group financial results with pools for control and support functions informed by the quality and integrity of support provided. Divisional pools may also be adjusted for other factors, including risk management outcomes.

A number of top-down lenses are applied in determining the group pool which is an aggregation of individual and divisional pools. Historically, the Board has used a range of 10-15% of normalised net profit before variable reward and tax (NNPBVRT) as one of these lenses.

While this continues to act as a guide, the Board considers a range of factors in assessing the appropriateness of the pool, including:

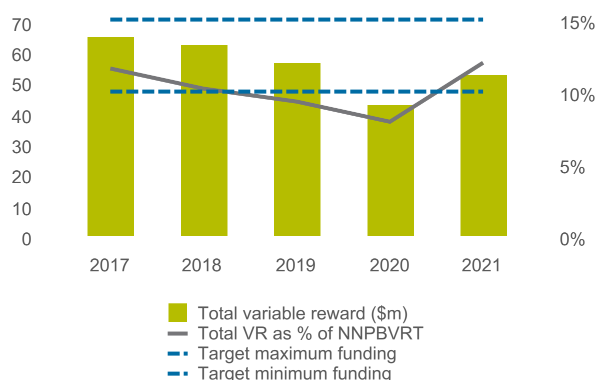
- overall business results against plan (financial and non-financial performance measures);
- progress against short and long term strategic objectives;
- external remuneration levels and movements;
- the retention of key talent;
- the cost and amount of capital employed;
- factors beyond management's control; and
- the management of risk, including adjustments for any risk and conduct matters with a group-wide impact.

4 Remuneration report (continued)

4.8 Remuneration governance (continued)

Variable remuneration governance (continued)

The Board approved a variable remuneration pool for 2021 which is within the target funding range (12%) and materially down on historic levels (excluding 2020). The Board considers that the pool reflects a reasonable and equitable distribution between shareholders and employees and provides a clear line of sight to, and a strong relationship between, performance and remuneration outcomes.



Minimum shareholding guidelines

The Board reviews KMP and Non-Executive Director minimum shareholding guidelines annually in order to ensure alignment with shareholders and market practice. The 2021 review determined that no changes were required to the guidelines at this time. Challenger's minimum shareholding guidelines do not count unvested deferred equity towards minimum holdings; however, for completeness the shareholding disclosures in Section 4.10 Key Management Personnel remuneration arrangements also show unvested deferred STIs.

Minimum shareholding requirements are detailed in the following table:

Group	Requirement	Implied value[1]
Non-Executive Directors (NEDs)	One times base fees	Chair: $525,500 NEDs: $179,000
Managing Director & CEO	Two times fixed remuneration	$2,550,000
Other KMP	One times fixed remuneration	$600,000 to $750,000

[1] Based on fees and remuneration as at 30 June 2021.

A five-year transitional period in which to acquire the required shareholding applies for Non-Executive Directors and KMP. The Board retains discretion to allow Non-Executive Directors and KMP to vary from this guideline. Where fees are paid to the employer of the Non-Executive Director, the guidelines do not apply.

The shareholdings of Non-Executive Directors and KMP at 30 June 2021 are set out in Sections 4.10 Key Management Personnel remuneration arrangements and 4.11 Non-Executive Director disclosures.

Employee share trading policy

Employees, including Directors and KMP, must comply with Challenger's employee share trading policy and are required to obtain pre-approval from the Company if they wish to trade in Challenger shares.

Employees are prohibited from trading during specified periods, including prior to the release of Challenger's financial results.

Employees are prohibited from hedging their unvested equity awards, as this would not be consistent with Challenger's remuneration strategy or appropriate governance outcomes and is contrary to the intention of equity-based remuneration arrangements. Any breach of this requirement would be regarded as serious misconduct and may result in dismissal.

Challenger prohibits KMP and employees from taking out margin loans on Challenger shares, with any exceptions to this rule requiring Board approval. There have been no requests for exceptions to this policy for the year ended 30 June 2021 (no requests in 2020).

Employee share ownership

The Board believes that greater employee share ownership increases alignment with shareholders.

The Tax Exempt Share Plan provides permanent Australian employees a means to acquire Challenger shares at no cost, and to participate in the future growth and performance of Challenger. Eligible employees are offered $1,000 worth of fully-paid Challenger ordinary shares on an annual basis, subject to a three-year minimum holding period.

As at 30 June 2021, 82% of permanent employees hold unvested Challenger equity (77% in 2020), which constitutes 2% of Challenger's issued capital (2% in 2020).

Challenger Performance Plan (CPP) Trust

The CPP Trust is an employee share trust established to satisfy Challenger's employee equity obligations arising from Restricted Shares, DPSRs and HPSRs.

Challenger shares held by the CPP Trust generate dividend income. The CPP Trust does not receive dividends from forward share purchase agreements.

The Trustee of the CPP Trust has absolute discretion to determine whether any net income earned from shares held by the CPP Trust is distributed to beneficiaries. Any undistributed income at the end of the year is taxed at the maximum marginal tax rate (which exceeds the company tax rate) and carries no franking credits.

In 2021, a distribution was paid in respect of DPSRs that vested in September 2020 only (equal to Challenger's dividend per share less tax paid in the Trust).

Any income distributed to KMP from the CPP Trust is considered by the Remuneration Committee and the Board when considering remuneration recommendations. CPP Trust distributions paid or payable to KMP are disclosed within the remuneration tables.

4 Remuneration report (continued)

4.9 Risk and reward

The Board seeks to align remuneration with effective risk management, the generation of appropriate risk-based returns and Challenger's risk appetite.

The Board has agreed a risk management framework which sets out the Board's tolerance to risk exposures and the management of risk. Challenger's risk profile is continuously monitored and managed against its risk appetite and any divergence is resolved within Challenger through a series of escalations and delegated authorities culminating with the Board. All business activities are carried out in accordance with this risk management framework, regardless of potential remuneration outcomes.

During the year, the Risk Committee provides reports to the Remuneration Committee and the Board summarising risk management and risk outcomes, including any breaches of the risk management framework or other compliance policies. In addition, the Consequence Management Committee, which comprises representatives from Risk and Human Resources, reports to the Remuneration Committee six-monthly on matters referred to it. The Remuneration Committee and the Board consider these reports when finalising remuneration pools and individual allocations.

All employees are required to comply with Challenger's policies and other risk management and regulatory requirements as they apply to their role and business area. Breaches of compliance with these policies and other requirements are taken seriously and may result in a range of potential consequences including disciplinary action and termination of employment.

All employees are assessed against the Challenger values, which includes risk behaviours, as part of the annual performance review process. The values rating contributes to the overall performance rating and remuneration outcomes. Satisfactory assessment of behaviours against the Challenger values is treated as a gate-opener for variable reward and behaviours can either increase or decrease reward outcomes.

During 2021, a range of activities have been undertaken to embed the Conduct Risk and Consequence Management framework which was approved by the Board in 2020. This has focused on raising awareness of risk management and regulatory requirements, transparency in relation to potential consequences for conduct matters, updating policies to improve clarity, and enhancing reporting and monitoring capabilities.

The Remuneration Committee and the Board consider potential risk implications of performance targets when setting performance measures for variable reward plans.

The Board also places significant focus on risk culture and monitors and assesses Challenger's risk culture. In 2021, this included:

- risk culture questions included within the YourVoice employee engagement survey;
- risk culture pulse check surveys sent to employees through the year;
- as part of its internal audit program, KPMG provided an assessment of risk culture arising from interviews and control findings;
- Ernst & Young undertook an analysis of verbatim responses to risk culture surveys to provide greater insights; and
- a range of key risk indicator metrics are monitored and assessed throughout the year.

Variable reward forfeiture provisions

Under the terms of the CPP, DPSRs, Restricted Shares and HPSRs may be reduced or forfeited should the Board determine that a KMP or employee:

- has committed an act of dishonesty;
- is ineligible to hold their office for the purposes of Part 2D.6 Disqualification from managing corporations of the *Corporations Act 2001*; or
- is found to have acted in a manner that the Board considers to be gross misconduct or is dismissed with cause.

In addition, the Board may resolve that an award of DPSRs, Restricted Shares or HPSRs should be reduced or forfeited in order to:

- protect financial soundness;
- respond to unexpected or unintended consequences that were significant and unforeseen by the Board (such as material risk management breaches, unexpected financial losses, reputational damage or regulatory non-compliance); and
- respond to any examples of misconduct, risk events, acts or omissions or breaches of law or regulation.

Prior to any awards vesting, the Chief Risk Officer confirms whether there are any matters that should be considered by the Board, including any ongoing investigations into potential matters.

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements

This audited remuneration report describes Challenger's KMP and Non-Executive Director remuneration arrangements as required by the *Corporations Act 2001*.

Statutory remuneration

Statutory remuneration represents the accounting expense of remuneration in the financial year. It includes fixed remuneration, cash STI awards, the fair value amortisation expense of deferred share awards granted, distributions from the CPP Trust, long service leave entitlements and insurance.

		Short-term employee benefits			Long-term employee benefits		
		Salary[1]	Super-annuation	Cash STIs	Other[2]	Share-based payments[3]	Total
KMP	Year	$	$	$	$	$	$
R Howes	**2021**	**1,256,237**	**21,694**	**475,000**	**60,861**	**1,759,563**	**3,573,355**
	2020	1,256,195	21,003	—	46,552	1,750,168	3,073,918
R Grimes[4]	**2021**	**117,301**	**3,616**	**46,000**	**115**	**8,546**	**175,578**
	2020	—	—	—	—	—	—
N Hamilton[5]	**2021**	**581,172**	**21,694**	**392,000**	**32,030**	**668,516**	**1,695,412**
	2020	449,799	16,252	—	13,793	325,659	805,503
A Kapel[6]	**2021**	**150,357**	**5,682**	**32,738**	**3,241**	**42,266**	**234,284**
	2020	—	—	—	—	—	—
A Murphy	**2021**	**593,377**	**21,694**	**232,500**	**52,214**	**616,699**	**1,516,484**
	2020	565,863	21,003	—	20,083	435,196	1,042,145
C Plater	**2021**	**730,844**	**21,694**	**336,000**	**52,862**	**1,183,429**	**2,324,829**
	2020	730,970	21,003	—	32,571	1,332,901	2,117,445
I Saines[7]	**2021**	**—**	**—**	**—**	**—**	**—**	**—**
	2020	187,511	4,751	—	2,278	263,185	457,725
A Tobin[8]	**2021**	**515,968**	**16,271**	**192,500**	**6,784**	**742,645**	**1,474,168**
	2020	688,605	21,003	—	28,296	1,141,362	1,879,266
Total	**2021**	**3,945,256**	**112,345**	**1,706,738**	**208,107**	**5,021,664**	**10,994,110**
	2020	3,878,943	105,015	—	143,573	5,248,471	9,376,002

1 Includes the cost of death, total permanent disability and salary continuance insurances.
2 Values represent distributions paid or payable from the CPP Trust and long service leave accruals.
3 Calculated on the basis outlined in Note 28 Employee entitlements and reflects the fair value of the benefit derived at the date at which they were granted. Fair value is determined using an option pricing model and is undertaken by an independent third party. The HPSRs included in share-based payments are subject to market-based performance conditions; consequently, no adjustment to the fair valuation following grant date is permitted to be made for the likelihood of performance conditions not being met. As a result, the value of the share-based payments included in the table may not necessarily have vested during the financial year.
4 Ms Grimes became a KMP on 3 May 2021. The 2021 disclosure is pro-rata for the period in which she was KMP.
5 Mr Hamilton transferred to a KMP role on 23 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
6 Mr Kapel held a KMP role from 7 December 2020 to 9 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.
7 Mr Saines ceased to be a KMP on 22 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
8 Mr Tobin ceased to be a KMP on 31 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements (continued)

Split of statutory remuneration components

The splits of KMP statutory remuneration are set out below:

KMP	Year	Fixed remuneration	Cash STI	Share-based payments	Other	Total
R Howes	**2021**	**36%**	**13%**	**49%**	**2%**	**100%**
	2020	41%	—	57%	2%	100%
R Grimes[1]	**2021**	**69%**	**26%**	**5%**	**—%**	**100%**
	2020	—	—	—	—	—
N Hamilton[2]	**2021**	**35%**	**23%**	**40%**	**2%**	**100%**
	2020	58%	—	40%	2%	100%
A Kapel[3]	**2021**	**66%**	**14%**	**18%**	**2%**	**100%**
	2020	—%	—	—%	—%	—%
A Murphy	**2021**	**40%**	**15%**	**41%**	**4%**	**100%**
	2020	56%	—	42%	2%	100%
C Plater	**2021**	**32%**	**14%**	**52%**	**2%**	**100%**
	2020	35%	—	63%	2%	100%
I Saines[4]	**2021**	**—%**	**—%**	**—%**	**—%**	**—%**
	2020	42%	—	57%	1%	100%
A Tobin[5]	**2021**	**36%**	**13%**	**50%**	**1%**	**100%**
	2020	37%	—	61%	2%	100%

1 Ms Grimes became a KMP on 3 May 2021. The 2021 disclosure is pro-rata for the period in which she was KMP.
2 Mr Hamilton transferred to a KMP role on 23 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
3 Mr Kapel transferred to a KMP role from 7 December 2020 to 9 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.
4 Mr Saines ceased to be a KMP on 22 September 2019. The 2020 disclosure is pro-rata for the period in which he was KMP.
5 Mr Tobin ceased to be a KMP on 31 March 2021. The 2021 disclosure is pro-rata for the period in which he was KMP.

Share Rights granted

Deferred Performance Share Rights

The number of DPSRs granted is determined based on the five-day volume weighted average price (VWAP) of shares prior to grant date. This is the face value allocation price that determines the number of DPSRs granted.

DPSRs granted to KMP during the year ended 30 June 2021 are detailed below:

					Vesting			
					Tranche 1 1 September 2021	Tranche2 1 September 2022	Tranche 3 1 September 2023	Tranche 4 1 September 2024
KMP	Awarded DPSR value from 2020 $	Face value allocation price $	Total number of DPSRs granted	Date of grant	Number[1]	Number[1]	Number[1]	Number[1]
R Howes	500,000	4.0100	124,544	7/9/20	37,363	37,363	24,909	24,909
N Hamilton	475,000	4.0100	118,316	7/9/20	35,495	35,495	23,663	23,663
A Murphy	400,000	4.0100	99,634	7/9/20	29,890	29,890	19,927	19,927
C Plater	525,000	4.0100	130,770	7/9/20	39,231	39,231	26,154	26,154
A Tobin	470,000	4.0100	117,070	7/9/20	35,121	35,121	23,414	23,414

1 The number of DPSRs granted is determined by dividing the dollar value of the award by the allocation price which is determined based on the VWAP in the five days prior to grant. The fair value of each tranche was $3.84 for Tranche 1, $3.67 for Tranche 2, $3.50 for Tranche 3 and $3.35 for Tranche 4. The fair value is independently calculated and is used to determine the accounting value which is amortised over future vesting periods. The fair value differs to the face value allocation price as the DPSRs do not carry a dividend entitlement and reflect the deferred nature of the award.

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements (continued)

Hurdled Performance Share Rights

The table below includes the awarded face value of the granted HPSRs as well as the fair value which takes into account the likelihood of vesting and is in line with accounting standards.

HPSRs granted to KMP during the year ended 30 June 2021 are detailed below:

				Vesting Tranche 1 1 September 2024			
KMP	Awarded HPSR face value	Grant date	Face value allocation price $	Total number of HPSRs granted[1]	TSR start price[2] $	Fair value at grant date[3]	Awarded HPSR fair value
R Howes	2,868,750	2/11/20	4.0100	714,579	4.4968	2.58	1,843,614
R Grimes	301,736	10/5/21	4.0100	75,246	4.4968	2.64	198,649
N Hamilton	1,350,000	7/9/20	4.0100	336,272	4.4968	1.87	628,829
A Murphy	1,350,000	7/9/20	4.0100	336,272	4.4968	1.87	628,829
A Murphy	168,556	10/5/21	4.0100	42,034	4.4968	2.64	110,970
C Plater	1,687,500	7/9/20	4.0100	420,340	4.4968	1.87	786,036
A Tobin	1,575,000	7/9/20	4.0100	392,318	4.4968	1.87	733,635

1 The number of HPSRs granted is determined by dividing the dollar value of the award by the face value allocation price. This is the VWAP in the five days prior to grant date.

2 The TSR start price for all awards granted during the year ended 30 June 2021 is the VWAP in the 90 calendar days prior to 7 September 2020.

3 The fair value is independently calculated and is also used to determine the accounting value which is amortised over future vesting periods. The fair value differs to the face value and the TSR start price as the HPSR vesting events are subject to achieving future TSR hurdles, do not carry a dividend entitlement and reflects the deferred nature of the award.

Share Rights vested

The following tables show the short and long-term incentives that vested during the year ended 30 June 2021.

Deferred Performance Share Rights

DPSRs which vested to KMP during the year ended 30 June 2021 are detailed below:

KMP	Date of grant	Number	Face value at grant $	Vesting date	Vested value $
R Howes	11/9/17	33,022	404,988	1/9/20	132,148
	11/9/18	34,360	356,241	1/9/20	137,503
	9/9/19	28,266	187,494	1/9/20	113,116
N Hamilton	11/9/17	4,280	52,491	1/9/20	17,128
	11/9/18	7,836	81,243	1/9/20	31,358
	9/9/19	5,653	37,497	1/9/20	22,622
A Murphy	11/9/17	3,669	44,997	1/9/20	14,683
	11/9/18	6,631	68,750	1/9/20	26,536
	9/9/19	11,872	78,749	1/9/20	47,510
C Plater	11/9/17	24,461	299,995	1/9/20	97,889
	11/9/18	29,538	306,247	1/9/20	118,206
	9/9/19	22,342	148,199	1/9/20	89,409
A Tobin	11/9/17	22,015	269,996	1/9/20	88,100
	11/9/18	22,304	231,246	1/9/20	89,257
	9/9/19	19,221	127,497	1/9/20	76,919

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements (continued)

Hurdled Performance Share Rights

No HPSR awards vested to KMP during the year ended 30 June 2021 as the minimum absolute TSR performance hurdles were not achieved. It should also be noted that no HPSRs will vest in September 2021.

	Grant details			Vesting details				
KMP	Grant date	Number	Fair value at grant[1] $	Vesting date	Number vested	Number forfeited[2]	Compound annual TSR outcome	Number yet to vest or lapse
R Howes	13/9/15	101,233	287,502	1/9/20	—	(101,233)	(4)%	—
	12/9/16	226,577	937,494	1/9/20	—	—	(11)%	226,577
	11/9/17	161,227	944,996	1/9/20	—	—	(25)%	161,227
N Hamilton	12/9/16	18,125	74,995	1/9/20	—	—	(11)%	18,125
	11/9/17	20,899	122,495	1/9/20	—	—	(25)%	20,899
A Murphy	13/9/15	26,409	75,002	1/9/20	—	(26,409)	(4)%	—
	12/9/16	63,441	262,496	1/9/20	—	—	(11)%	63,441
	11/9/17	17,914	104,998	1/9/20	—	—	(25)%	17,914
C Plater	13/9/15	39,613	112,501	1/9/20	—	(39,613)	(4)%	—
	12/9/16	163,136	674,998	1/9/20	—	—	(11)%	163,136
	11/9/17	119,427	699,994	1/9/20	—	—	(25)%	119,427
A Tobin[3]	13/9/15	70,422	199,998	1/9/20	—	(70,422)	(4)%	—
	12/9/16	145,009	599,995	1/9/20	—	—	(11)%	145,009
	11/9/17	107,485	629,998	1/9/20	—	—	(25)%	107,485

1 The fair value is independently calculated and has been determined by the Board as the best estimate of the awarded financial value at the grant date.
2 HPSRs awarded in 2015 lapsed during the year as a result of the higher hurdle test applied in year 5.
3 HPSR awards subsequently forfeited on termination.

Share Rights held

Performance Share Rights held

Details of KMP DPSRs and HPSRs held as at 30 June 2021 are set out below:

KMP	Instrument	Number held at 1 July 2020	Number granted as remuneration	Number forfeited	Number vested	Number held at 30 June 2021
R Howes	DPSRs	195,601	124,544	—	(95,648)	224,497
	HPSRs	1,111,353	714,579	(101,233)	—	1,724,699
R Grimes	DPSRs	—	—	—	—	—
	HPSRs	—	75,246	—	—	75,246
N Hamilton	DPSRs	38,191	118,316	—	(17,769)	138,738
	HPSRs	282,935	336,272	—	—	619,207
A Murphy	DPSRs	54,212	99,634	—	(22,172)	131,674
	HPSRs	335,519	378,306	(26,409)	—	687,416
C Plater	DPSRs	157,406	130,770	—	(76,341)	211,835
	HPSRs	738,138	420,340	(39,613)	—	1,118,865
A Tobin	DPSRs	132,260	117,070	—	(63,540)	185,790
	HPSRs	693,644	392,318	(937,807)	—	148,155

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements (continued)

Key Management Personnel and their affiliates' shareholdings in Challenger Limited

Details of KMP and their affiliates' shareholdings in Challenger Limited as at 30 June 2021 are detailed below, along with the number of unvested DPSRs. The CEO and other KMP are required to have a minimum shareholding equal to two times, and one times, their fixed remuneration respectively. From the date of appointment, KMP have a five-year transition period to reach the minimum shareholding. Mr Howes held substantially more than the minimum requirement as at 30 June 2021. Mr Plater achieved the minimum requirement during the period and all other current KMP remain within their transition period.

							Shareholding as a multiple of fixed remuneration[1]	
KMP	Year	Opening balance	Number of vested DPSRs and HPSRs	Number of shares acquired	Closing balance of shares	Number of unvested DPSRs	Fully-owned shares	Shares and DPSRs
R Howes	**2021**	**561,478**	**95,648**	**250,000**	**907,126**	**224,497**	**3.8**	**4.8**
	2020	461,592	99,886	—	561,478	195,601	1.9	2.6
R Grimes[2]	**2021**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
	2020	—	—	—	—	—	—	—
N Hamilton[3]	**2021**	**—**	**17,769**	**—**	**17,769**	**138,738**	**0.2**	**1.4**
	2020	—	—	—	—	38,191	—	0.3
A Murphy[4]	**2021**	**24,896**	**22,172**	**—**	**47,068**	**131,674**	**0.4**	**1.4**
	2020	—	24,896	—	24,896	54,212	0.2	0.6
C Plater	**2021**	**136,331**	**76,341**	**—**	**212,672**	**211,835**	**1.5**	**3.1**
	2020	54,845	81,486	—	136,331	157,406	0.8	1.7
A Tobin[5]	**2021**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
	2020	364,765	63,384	—	428,149	132,260	2.7	3.5
Total	**2021**	**722,705**	**211,930**	**250,000**	**1,184,635**	**706,744**		
	2020	881,202	269,652	—	1,150,854	577,670		

1 Shareholding multiple based on 30 June 2021 closing share price of $5.41 (30 June 2020: $4.41).
2 Ms Grimes transferred to a KMP role on 3 May 2021 and has a five year transition period in which to acquire the required shareholding.
3 Mr Hamilton transferred to a KMP role on 23 September 2019 and has a five year transition period in which to acquire the required shareholding.
4 Ms Murphy transferred to a KMP role on 12 December 2018 and has a five year transition period in which to acquire the required shareholding.
5 Mr Tobin ceased to be a KMP on 31 March 2021.

4 Remuneration report (continued)

4.10 Key Management Personnel remuneration arrangements (continued)

Richard Howes – Managing Director & CEO

Mr Howes was appointed Managing Director & CEO effective 2 January 2019. All equity awards for the Managing Director & CEO are satisfied by the purchase of shares on market. The following table summarises the notice periods and payments which apply to Mr Howes upon termination.

	Notice period	Payment in lieu of notice	Eligibility for STI	Treatment of unvested performance rights
Bad leaver termination[1]	Employee initiated: 6 months Employer initiated (Poor performance): 12 months	The Board may elect to make a payment of salary package in lieu of notice	No	Lapse
	Employer initiated (Misconduct): None	None		
Good leaver termination[2]	Employee initiated: 6 months Employee initiated (Material change): 1 month Employer initiated: 12 months[3]	The Board may elect to make a payment of salary package in lieu of notice	Eligible for a pro-rata STI payable at the usual payment date	Continued vesting[4]

1 Bad leaver termination will occur where employment is terminated by Challenger for poor performance, misconduct or resignation without the prior approval of the Board.
2 Good leaver termination will occur if employment ends in any circumstances that do not constitute a bad leaver termination.
3 Material change means where there is a substantial diminution of Mr Howes' duties, status, responsibilities and/or authority arising without his agreement.
4 Unvested performance rights will remain on foot subject to the specified time based vesting conditions and/or performance hurdles and to the rules of the CPP.

Key Management Personnel (excluding Managing Director & CEO) employment agreements and notice periods

KMP do not have fixed terms of employment. The notice period for Challenger and the KMP is 26 weeks unless terminated for cause.

Upon termination, if the KMP is considered a good leaver (such as cessation of employment due to redundancy), they will be entitled to a pro-rata STI award. Board discretion applies in relation to unvested awards issued under the CPP prior to 30 June 2019. Awards issued under the CPP from 1 July 2019 onwards are subject to specific good leaver conditions specified at the time of grant, which apply unless the Board exercises its discretion to do otherwise.

Loans and other transactions

There were no loans made to Directors or key executives as at 30 June 2021 (30 June 2020: nil). From time to time, Directors of the Company or their Director-related entities may purchase products from the Company. These purchases are on the same arm's length terms and conditions as those offered to other employees or customers.

4 Remuneration report (continued)

4.11 Non-Executive Director disclosures

Fee pool

The maximum aggregate amount of annual fees is approved by shareholders in accordance with the requirements of the *Corporations Act 2001.*

The current fee pool of $2,500,000 was approved by shareholders in 2016.

Fee framework and review

Challenger aims to attract and retain suitably skilled and experienced Non-Executive Directors to serve on the Board and to reward them appropriately for their time and expertise.

Non-Executive Directors are remunerated by way of fees paid in recognition of membership of the Board and its committees.

Additional fees are paid to the Chair of the Board and sub-committee members to reflect added responsibilities.

The Board is committed to periodically reviewing the fee framework in order to ensure that fees remain appropriate against the external market and support the attraction and retention of high quality Non-Executive Directors.

On recommendation from the Remuneration Committee, the Board approves the fee structure within the bounds of the overall maximum fee pool.

The fee structure is benchmarked annually to align with the market and to attract, retain and appropriately reward quality independent directors. Board and committee fees remain unchanged for the year ended 30 June 2021, noting the temporary reduction outlined below.

The following table summarises the fees applicable to membership and chairmanship of the Board and its sub-committees, inclusive of services provided at a subsidiary board level, for the year ended 30 June 2021. All amounts are inclusive of superannuation, where applicable.

Reduction to Board fees

In response to the impact of the COVID-19 pandemic on Challenger's performance, the Board determined to reduce its base fees by 20% for a period of six months, commencing 1 June 2020.

Board/Committee	2021 fee structure Chair fee[2] $	2021 fee structure Member fee $	2020 fee structure Chair fee[2] $	2020 fee structure Member fee $
Board[1]	525,500	179,000	525,500	179,000
Group Risk[3]	47,000	14,000	47,000	14,000
Group Audit[4]	47,000	14,000	47,000	14,000
Remuneration	47,000	23,500	47,000	23,500

1 Board fees include Nomination Committee fees.
2 The Board Chair fees reported in the table are inclusive of committee fees paid to the Board Chair.
3 The fee for the Chair of the Group Risk Committee includes membership of the Group Audit Committee.
4 The fee for the Chair of the Group Audit Committee includes membership of the Group Risk Committee.

The fee framework includes services provided at a subsidiary board level.

4 Remuneration report (continued)

4.11 Non-Executive Director disclosures (continued)

Non-Executive Director fees for the year ended 30 June 2021

The following table summarises Non-Executive Director fees for the year ended 30 June 2021.

Non-Executive Director	Year	Director fees $	Superannuation $	Total $
P Polson	**2021**	**475,933**	**—**	**475,933**
	2020	495,739	21,003	516,742
J M Green	**2021**	**196,880**	**18,704**	**215,584**
	2020	207,778	19,739	227,517
S Gregg	**2021**	**218,647**	**20,751**	**239,398**
	2020	245,514	21,003	266,517
M Kobayashi[1]	**2021**	**—**	**—**	**—**
	2020	—	—	—
H Smith[2]	**2021**	**84,768**	**8,053**	**92,821**
	2020	—	—	—
J Stephenson	**2021**	**232,848**	**21,235**	**254,083**
	2020	245,014	21,003	266,017
D West[3]	**2021**	**205,956**	**—**	**205,956**
	2020	204,017	—	204,017
M Willis	**2021**	**206,469**	**19,615**	**226,084**
	2020	217,367	20,650	238,017
L Zwier[4]	**2021**	**—**	**—**	**—**
	2020	44,750	—	44,750
Total	**2021**	**1,621,501**	**88,358**	**1,709,859**
	2020	1,660,179	103,398	1,763,577

1 Mr Kobayashi as a shareholder representative, does not receive fees. Similarly his alternate Director, Mr Iioka, does not receive fees.
2 Ms Smith was appointed as Director on 20 January 2021. The 2021 remuneration reflects fees on a pro-rata basis.
3 Mr West provides a service through a company; fees exclude GST.
4 Mr Zwier retired from the Board on 31 October 2019. The 2020 remuneration reflects fees earned on a pro-rata basis.

Superannuation

Non-Executive Directors receive superannuation contributions where required by Superannuation Guarantee legislation.

Equity participation

Non-Executive Directors do not receive equity as part of their remuneration and do not participate in any incentive arrangements.

4 Remuneration report (continued)

4.11 Non-Executive Director disclosures (continued)

Non-Executive Director shareholdings in Challenger Limited at 30 June 2021

Details of the Non-Executive Directors' and their affiliates' shareholdings in Challenger Limited are set out below:

Non-Executive Director	Year	Shares held at the beginning of the year	Movements	Shares held at the end of the year
P Polson	**2021**	**122,000**	**6,944**	**128,944**
	2020	122,000	—	122,000
J M Green[1]	**2021**	**10,000**	**6,944**	**16,944**
	2020	10,000	—	10,000
S Gregg[2]	**2021**	**14,000**	**—**	**14,000**
	2020	14,000	—	14,000
M Kobayashi[3]	**2021**	**—**	**—**	**—**
	2020	—	—	—
H Smith[1,4]	**2021**	**—**	**10,000**	**10,000**
	2020	—	—	—
J Stephenson[2]	**2021**	**17,000**	**4,629**	**21,629**
	2020	15,000	2,000	17,000
D West[1]	**2021**	**18,957**	**6,944**	**25,901**
	2020	18,957	—	18,957
M Willis	**2021**	**149,892**	**6,944**	**156,836**
	2020	149,892	—	149,892
L Zwier[5]	**2021**	**—**	**—**	**—**
	2020	7,360	(7,360)	—
Total	**2021**	**331,849**	**42,405**	**374,254**
	2020	337,209	(5,360)	331,849

1 Mr Green, Mr West and Ms Smith are within the five-year transitional period in which to acquire the required shareholding.
2 Due to significant share price movement during 2021, Mr Gregg and Ms Stephenson's shareholdings as at 30 June 2021 did not satisfy the minimum shareholding requirements.
3 Mr Kobayashi is exempt from the minimum shareholding requirements. His alternate director, Mr Iioka, is exempt also.
4 Ms Smith joined the Board on 20 January 2021.
5 Mr Zwier retired from the Board on 31 October 2019, so his holding disclosure is removed under 'movements'.

Total remuneration of KMP and Non-Executive Directors[1]

KMP and Non-Executive Directors	Short-term benefits $	Post-employment benefits $	Share-based payments $	Other benefits $	Total $
Non-Executive Directors					
2021	**1,621,501**	**88,358**	**—**	**—**	**1,709,859**
2020	1,660,179	103,398	—	—	1,763,577
KMP					
2021	**5,651,994**	**112,345**	**5,021,664**	**208,107**	**10,994,110**
2020	3,878,943	105,015	5,248,471	143,573	9,376,002
All KMP and Non-Executive Directors					
2021	**7,273,495**	**200,703**	**5,021,664**	**208,107**	**12,703,969**
2020	5,539,122	208,413	5,248,471	143,573	11,139,579

1 No termination payments were made to KMPs or NEDs during the period.

4 Remuneration report (continued)

4.12 Summary of key terms and abbreviations used in the remuneration report

Key term	Description
Awarded remuneration	Represents the value of remuneration that has been awarded for the financial year. This includes fixed remuneration, STI (cash and deferred) and LTI.
Board	The Board of Directors of Challenger Limited is the main body responsible for the implementation of effective remuneration governance and related risk management practices at Challenger.
CPP	*Challenger Performance Plan.* Deferred equity awards are issued under the CPP.
CPP Trust	*Challenger Performance Plan Trust.* The CPP Trust was established in 2006 for the purpose of acquiring, holding and transferring shares to employees upon the vesting of their equity awards.
DPSR	*Deferred Performance Share Right.* Prior to 1 July 2021, deferred STI awards were delivered as DPSRs under the CPP. DPSRs represent the right to receive a fully-paid ordinary Challenger share for zero consideration subject to continued employment at the time of vesting. DPSRs do not provide an entitlement to vote or a right to dividends; however, employees with unvested DPSRs may receive a distribution of income from the CPP Trust. The Board has discretion to amend or withdraw DPSRs at any point.
Face value	The number of DPSRs, Restricted Shares and/or HPSRs granted to KMP is determined based on the face value of the shares using a five-day volume weighted average price (VWAP) prior to the grant date.
Fair value	The number of HPSRs awarded to KMP prior to 1 July 2019 was calculated by reference to the fair value. The fair value for HPSRs is calculated on the basis outlined in Note 28 Employee entitlements and reflects the fair value of the benefit derived at the date at which they were granted. An independent third party determines the fair value using an option pricing model and discounted cash flow methodology, as appropriate.
HPSR	*Hurdled Performance Share Right.* LTI awards are delivered as HPSRs under the CPP. HPSRs represent the right to receive a fully-paid ordinary Challenger share for zero consideration subject to satisfying an employment condition and Challenger satisfying the absolute TSR performance hurdle. HPSRs do not provide an entitlement to vote or a right to dividends. The Board has discretion to amend or withdraw HPSRs at any point.
KMP	*Key Management Personnel.* Persons having authority and responsibility for planning, directing and controlling the activities of an entity, directly or indirectly, including any Director (whether executive or otherwise) as defined in AASB 124 *Related Party Disclosures.*
LTI	*Long term incentive.* LTIs are awarded annually to KMP to support a continued focus on long-term performance outcomes. Executives will only realise value from LTIs if total shareholder returns exceed the hurdles set, ensuring a direct link between executive reward and shareholder outcomes.
Normalised NPAT	*Normalised net profit after tax.* Excludes asset or liability valuation movements that are above or below expected long-term trends and significant items that may positively or negatively impact financial results. Refer to the Operating and financial review section for further information.
Normalised RoE (pre-tax)	*Normalised return on equity (pre-tax).* Normalised profit before tax divided by average net assets.
Normalised NPBVRT	*Normalised net profit before variable reward and tax.* Excludes any asset or liability valuation movements that are above or below expected long-term trends and any significant items that may positively or negatively impact the financial results, and excludes STI expense, employee share award expense and tax.
Remuneration Committee	The Board convenes a Remuneration Committee comprising Independent Non-Executive Directors and which is a delegated committee of the Board to assist the Board in discharging its responsibilities.
Restricted Share	Deferred STI awards are delivered as Restricted Shares under the CPP. A Restricted Share is a beneficial interest in a fully-paid ordinary Challenger share acquired for zero consideration. Restricted Shares are subject to disposal restrictions and vest subject to satisfaction of an employment condition. Restricted Shares provide an entitlement to vote and a right to dividends.
Statutory remuneration	Represents the accounting expense of remuneration for the financial year. This includes fixed remuneration, cash STI awards, the fair value amortisation expense of share-based awards granted up to balance sheet date, distributions from the CPP Trust, long service leave entitlements and insurance.
STI	*Short term incentive.* STIs are used to reward KMP and employees for significant contributions to Challenger's results over the course of the financial year. Individual STI awards are allocated on the basis of annual contribution and with reference to STI targets and market benchmarks. The Board has discretion to amend or withdraw the STI at any point. STIs may be awarded in the form of cash and/or equity.
TSR	*Total shareholder return.* TSR represents the change in share price plus dividends received over a given timeframe. Challenger uses absolute TSR as the measure of performance for HPSRs.
Variable remuneration	Consists of cash STI and share-based awards. Share-based awards comprise Restricted Shares (DPSRs prior to 1 July 2021) and HPSRs.
VWAP	*Volume weighted average price.* Ratio of the value of shares traded to total volume traded over a time horizon. A five-day VWAP is used to calculate the number of DPSRs per dollar of deferred STIs. A five-day VWAP is used to calculate the number of HPSRs per dollar of LTIs. A 90-day VWAP is also used for absolute TSR performance testing (start and end price) for HPSR awards.

5 Indemnification and insurance of Directors and officers

In accordance with its Constitution, and where permitted under relevant legislation or regulation, the Company indemnifies the Directors and officers against all liabilities to another person that may arise from their position as Directors or officers of the Company and its subsidiaries, except where the liability arises out of conduct that is fraudulent, dishonest, criminal, malicious or a reckless act, error or omission.

In accordance with the provisions of the ***Corporations Act 2001***, the Company has insured the Directors and officers against liabilities incurred in their role as Directors and officers of the Company. The terms of the insurance policy, including the premium, are subject to confidentiality clauses and therefore the Company is prohibited from disclosing the nature of the liabilities covered and the premium paid.

6 Indemnification of auditor

To the extent permitted by law, the Company has agreed to indemnify its auditor, Ernst & Young, as part of the terms of its audit engagement agreement. The primary purpose of the indemnity is to indemnify Ernst & Young for any loss that it may suffer as a result of a false representation given by Challenger management where a claim is made against Ernst & Young by a third party.

There is a caveat if Ernst & Young's loss results from its own negligence or wrongful or wilful acts or omissions. No payment has been made to indemnify Ernst & Young during or since the end of the financial year.

7 Environmental regulation and performance

Some members of the Group act as a trustee or responsible entity for a number of trusts that own assets both in Australia and overseas. Some of these assets are subject to environmental regulations under Commonwealth, state and offshore legislation. The Directors are satisfied that adequate systems are in place for the management of the Group's environmental responsibilities and compliance with various legislative, regulatory and licence requirements. Further, the Directors are not aware of any breaches of these requirements, and to the best of their knowledge all activities have been undertaken in compliance with environmental requirements.

8 Significant events after the balance date

On 23 December 2020, Challenger agreed to acquire 100% of MyLifeMyFinance Limited, an Australian-based customer digital bank, for $35.0 million. The acquisition price is subject to a completion adjustment and is based on a net asset value of $18.0 million. Provisional Goodwill on acquiring the business is estimated to be approximately $17.0 million and may be subsequently adjusted in accordance with the requirements of AASB 3 ***Business Combinations***. The acquisition received formal approval from the Treasurer of the Commonwealth of Australia on 29 July 2021 and was completed on 30 July 2021. The acquisition is highly strategic and provides Challenger the opportunity to significantly expand its secure retirement income offering, including entering Australia's term deposit market. In the 2022 financial year, the Bank will represent a third operating segment of the Group.

At the date of this financial report, no other matter or circumstance has arisen that has, or may significantly affect, the Group's operations, the results of those operations or the Group's state of affairs in future financial years which has not already been reflected in this report.

9 Rounding

The amounts contained in this report and the financial report have been rounded to the nearest $100,000, unless otherwise stated, under the option available to the Group under Australian Securities and Investments Commission (ASIC) Corporations Instrument 2016/191.

10 Non-audit services

The Group Audit Committee has reviewed details of the amounts paid or payable for non-audit services provided to Challenger during the year ended 30 June 2021 by the Company's auditor, Ernst & Young.

The Directors are satisfied that the provision of those non-audit services by the auditor is compatible with the general standard of independence for auditors imposed by the ***Corporations Act 2001*** and did not compromise the auditor independence requirements of the ***Corporations Act 2001*** for the following reasons:

- All non-audit services were approved in accordance with the Auditor Independence Policy which outlines the approval process that must occur for all non-audit services and which involves the Challenger CEO, CFO or delegate, depending on size and circumstances; and
- No non-audit services were carried out that were specifically excluded by the Auditor Independence Policy.

For details of fees for non-audit services paid to the auditors, refer to Note 29 Remuneration of auditor of the financial report.

11 Authorisation

Signed in accordance with a resolution of the Directors of Challenger Limited:

P Polson
Independent Chair

9 August 2021

R Howes
Managing Director & Chief Executive Officer

9 August 2021

12 Auditor's independence declaration

The Directors received the following declaration from the auditor of Challenger Limited:

Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Auditor's independence declaration to the Directors of Challenger Limited

As lead auditor for the audit of the financial report of Challenger Limited for the financial year ended 30 June 2021, I declare to the best of my knowledge and belief, there have been:

a. no contraventions of the auditor independence requirements of the ***Corporations Act 2001*** in relation to the audit; and
b. no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Challenger Limited and the entities it controlled during the financial year.

Ernst & Young

T Johnson
Partner

Sydney

9 August 2021

A member firm of Ernst & Young Global Limited

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Sustainability

Sustainability is embedded across Challenger. Through a refreshed strategy, Challenger aims to create value for customers, shareholders, employees and the community.

The sustainability strategy supports Challenger's purpose to provide financial security for a better retirement through:

- responsible business practices that focus on customers, employees, shareholders and the environment;
- acting on issues affecting the ability of retirees to achieve financial security;
- helping customers and communities to be strong and financially resilient; and
- investing responsibly by incorporating environmental, social and governance (ESG) considerations when making investment decisions.

Challenger's 2021 Sustainability Report outlines the Group's approach to sustainability and is available from the company website:

> **challenger.com.au/about-us**

This report covers Challenger's key initiatives and achievements and the Group's approach to addressing Challenger's most material matters. It also demonstrates the Company's contribution to the UN Sustainable Development Goals (SDGs).

Material matters

Trust and confidence

Operating ethically, with strong governance practices and high levels of trust is critical to Challenger's ability to deliver to customers, shareholders, employees and the broader community. Challenger recognises the importance of maintaining a strong culture and high levels of conduct; providing open and transparent disclosures; and responsibly managing risks.

Better customer outcomes

Challenger is committed to providing better customer outcomes that lead to improved satisfaction and support our customers to achieve financial security for a better retirement. Challenger does this by investing in research to understand more about the Group's customers; designing products that meet customer needs; and continuing to provide a trusted brand.

Economic, market and regulatory conditions

As an investment management company, Challenger is impacted by market volatility and uncertainty as well as the low interest rate trend. The need for diversification and ensuring access to appropriate assets remains an important focus for Challenger's business and stakeholders.

Investing responsibly

There has been growing pressure for companies to consider ESG issues when setting investment strategies. These considerations will help make Challenger more resilient. Changing stakeholder expectations highlight the importance of responsible lending and investment practices that support good ESG outcomes.

Climate risk

The physical and transition risks related to climate change will have financial impacts on Challenger if not considered.

The physical risks will have an impact on Challenger's real assets, considering their ability to withstand extreme weather events. Transition risks will be felt more widely through investment portfolios, with market, legal and reputation risks occurring across many industries.

Product and technology innovation

Dynamic market conditions require innovation to ensure Challenger is keeping up with the pace of change. Ensuring the Company has appropriate digital tools and technology in place is key to this. In addition, partnerships and collaboration with stakeholders will allow Challenger to develop products and services that continue to meet the changing needs of customers.

Privacy and security

The global pandemic accelerated the growing trend to move business operations online. The speed of change has increased the risk of exposure to cyber threats and fraud. As Challenger increases digital customer interaction, there is an increased focus on ensuring the privacy and security of both customer and business data.

Great place to work

Challenger seeks to provide an engaged and enabled workforce that embraces diverse thinking and has positive labour practices. The Company recognises that maintaining a great culture and capabilities is critical to success, supporting Challenger's ability to deliver the business strategy. Providing the tools and technology to enable employees are essential elements of an engaged workplace.

Community connection and resilience

As a retirement income provider, Challenger plays a key role in contributing to fiscally responsible solutions to funding the ageing population. Using internal expertise, Challenger supports the industry in understanding how to effectively plan for retirement to improve financial security. Investing strategically in the community to address a social issue further enhances Challenger's contribution to this. Through giving and volunteering programs, and plans for future community activities, Challenger aims to connect with and support the communities in which the Company operates.

Providing a great workplace

Challenger's strategy provides a clear, coherent, unifying statement of who it is, where it is going and how it will get there. A key component of this strategy is an employee vision to bring together a diverse group of top talent, inspired by the Company's purpose, with strong culture and capabilities to deliver shared success.

While COVID-19 has proven disruptive for many businesses, a big priority for Challenger has been, and continues to be, focusing on the wellbeing of employees. Throughout the pandemic Challenger achieved this in a variety of ways, including communicating regularly and keeping employees up to date with the Company's approach; setting up a new working from home hub on the intranet; and holding online discussion forums with leaders.

The results of a pulse survey in March 2021 showed that many employees have enjoyed the benefits of remote working, something Challenger is committed to offering on an ongoing basis.

At the same time, the survey revealed that nearly everyone (96%) wanted to mix this with the personal connection and collaboration time that being in the office offers.

To deliver this, Challenger is rolling out a team-based approach to hybrid work, where teams work together with their leaders to agree more formally on their work patterns, taking into account the needs of the team, Challenger and individuals.

Sustainability (continued)

Making diversity count

Challenger knows that ensuring business success relies on a workforce with diverse thinking and experience. As such, Challenger actively looks to recruit and retain employees from a range of backgrounds.

To make this a reality, Challenger continues to make progress on implementing the Company's Diversity and Inclusion strategy. Key focus areas for this are to: build a truly inclusive and diverse workforce; advance gender equality; and create meaningful employment opportunities for people over 50.

This year Challenger advanced a number of initiatives through four diversity and inclusion networks, focused on gender, age, LGBTQI+ and cultural diversity. This included rolling out a series of diversity videos challenging misconceptions and biases; joining the Pride in Diversity network – Australia's leading not for profit support program providing inclusion strategies for LGBTQI+ persons; and submitting Challenger's responses to the Australian Workplace Equality Index's annual questionnaire on how supported LGBTQI+ persons feel at work.

While COVID-19 meant employees couldn't come together to celebrate key diversity milestones such as Mardi Gras, Lunar New Year, Diwali and Ramadan this year, Challenger continued to promote employee involvement in these events outside of work through the company intranet and other internal channels.

Risk is everybody's business

The management of risk is fundamental to Challenger's business, supporting better outcomes to our customers and building long-term shareholder value. At Challenger, risk is everybody's business.

The Board's Risk Appetite Statement outlines the level of risk that is acceptable to the business to achieve its strategic objectives. This is combined with its risk management framework, which monitors, mitigates and manages the risks to which Challenger is exposed.

The Board recognises the broad range of risks Challenger faces as a participant in the financial services industry, including funding and liquidity risk; investment and pricing risk; counterparty risk; strategic, business and reputation risk; operational risk; licence and regulatory risk; climate change risk; and conduct risk. The Board also maintains a focus on contemporary and emerging risks, monitoring key risks to Challenger's strategy.

The Leadership team is accountable for managing identified risks within their divisions and is required to manage risk as part of business objectives with risk management integrated across business processes.

There are clear accountabilities for risk management for all Challenger employees and these are measured through Challenger's annual performance management process.

Challenger's risk management framework also incorporates key ESG issues. The Company's range of policies and practices carefully consider ESG risks and opportunities when making business decisions.

More detailed information about Challenger's risk management approach is provided in the 2021 Sustainability Report.

Investing in the community

Challenger's partnership with Council on the Ageing (COTA) NSW was established in 2019 to deliver a program of research, advice and practical support to address the underemployment of people over 50.

This year, working alongside both COTA NSW and Newgate Research, Challenger published research on understanding the needs of older workers and how businesses can enhance their workplaces.

Based on the insights of this research, a program and toolkit are being designed, covering:

- education and advice for hiring managers;
- support for auditing existing programs and policies, and building new ones to promote age diversity;
- advice on fostering connections between age diverse groups at work; and
- developing training programs to deliver equal access to upskilling and training opportunities.

Challenger introduced a new payroll giving platform this year, allowing employees to donate to the charities that are most important to them. Challenger matches employee donations up to $500 for each employee every year. Employees also have one paid day of leave for volunteering every year and are given opportunities to support personal charities throughout the year.

Managing Challenger's impact on the environment

Challenger is committed to supporting progress in transitioning to a low-carbon economy. This includes working with internal and external stakeholders to find ways to reduce risk and create a more resilient economy.

Challenger's strong governance supports the resilience of the business, with the Board having oversight of climate-related risks and opportunities. A newly established ESG Steering Committee which provides quarterly reporting to the Group Risk Committee, will enhance this process for 2022.

Each year, Challenger calculates the impact from direct operations, including scope 1, 2 and 3 emissions. To ensure accuracy and transparency, an external consultant supported this work, which was audited by a third party. These emissions are offset using high-quality credits which support projects that improve the environment in Australia and around the world.

Challenger's full commitment to sustainability is outlined in the 2021 Sustainability Report, which can be viewed at:

> challenger.com.au/sustainabilityreport2021

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This financial report covers Challenger Limited (the Company) and its controlled entities (the Group or Challenger).

Statement of comprehensive income

For the year ended 30 June	Note	2021 $m	2020 $m
Revenue	1	2,785.7	1,132.8
Expenses	2	(1,662.4)	(1,538.9)
Finance costs	15	(327.9)	(213.8)
Share of profits of associates	23	35.2	29.3
Profit/(loss) before income tax		**830.6**	**(590.6)**
Income tax (expense)/benefit	4	(238.3)	169.5
Profit/(loss) for the year after income tax		**592.3**	**(421.1)**
Profit/(loss) attributable to shareholders of Challenger Limited		592.3	(416.0)
Profit/(loss) attributable to non-controlling interests		—	(5.1)
Profit/(loss) for the year after income tax		**592.3**	**(421.1)**
Other comprehensive income			
Items that may be reclassified to profit and loss, net of tax			
Translation of foreign entities	14	(49.7)	1.6
Hedge of net investment in foreign entities	14	46.8	0.5
Cash flow hedges – SPV[1]	14	(0.5)	—
Other comprehensive income for the year		(3.4)	2.1
Total comprehensive income for the year after tax		**588.9**	**(419.0)**
Comprehensive income attributable to shareholders of Challenger Limited		588.9	(413.9)
Comprehensive income attributable to non-controlling interests		—	(5.1)
Total comprehensive income for the year after tax		**588.9**	**(419.0)**
Earnings per share attributable to ordinary shareholders of Challenger Limited		**Cents**	**Cents**
Basic	17	88.2	(68.4)
Diluted	17	68.0	(68.4)

[1] SPV = Special Purpose Vehicles.

The statement of comprehensive income should be read in conjunction with the accompanying notes.

Statement of financial position

As at 30 June	Note	2021 $m	2020 $m
Assets			
Cash and cash equivalents	11	928.6	603.9
Cash and cash equivalents – SPV	7	60.8	58.0
Receivables		830.4	594.1
Derivative assets	10	738.3	1,112.5
Financial assets – fair value through profit and loss	5	22,174.7	20,834.0
Investment and development property - held for sale	6	396.0	—
Investment and development property	6	3,389.7	3,685.9
Mortgage assets – SPV	7	570.3	706.6
Finance leases		26.8	31.7
Property, plant and equipment		28.2	25.9
Investment in associates	23	83.2	63.0
Other assets		63.1	65.8
Right-of-use lease assets	26	34.7	32.4
Deferred tax assets	4	4.0	49.8
Goodwill	25	579.9	579.9
Other intangible assets	25	9.2	18.1
Total assets of shareholders of Challenger Limited and non-controlling interests		**29,917.9**	**28,461.6**
Liabilities			
Payables		1,744.1	1,640.9
Current tax liability	4	48.1	1.0
Derivative liabilities	10	507.6	725.4
Interest bearing financial liabilities	13	5,950.2	7,278.2
Interest bearing financial liabilities – SPV	7	373.3	460.7
External unit holders' liabilities	9	3,632.2	2,415.8
Provisions		35.7	35.5
Lease liabilities	26	70.3	67.6
Deferred tax liabilities	4	60.7	5.7
Life contract liabilities	8	13,669.9	12,581.2
Total liabilities of shareholders of Challenger Limited and non-controlling interests		**26,092.1**	**25,212.0**
Net assets of shareholders of Challenger Limited and non-controlling interests		**3,825.8**	**3,249.6**
Equity			
Contributed equity	12	2,425.5	2,377.6
Reserves	14	(50.9)	(50.9)
Retained earnings	14	1,451.2	922.9
Total equity of shareholders of Challenger Limited		**3,825.8**	**3,249.6**

The Statement of financial position should be read in conjunction with the accompanying notes.

Statement of changes in equity

For the year ended 30 June 2020	Note	Attributable to shareholders of Challenger Limited Contributed equity $m	Share-based payment reserve $m	Cash flow hedge reserve –SPV $m	Foreign currency translation reserve $m	Adjusted controlling interest reserve $m	Retained earnings $m	Total shareholder equity $m	Non-controlling interests $m	Total equity $m
Balance at 1 July 2019		**2,093.7**	**(57.7)**	**0.1**	**(2.6)**	**7.8**	**1,559.0**	**3,600.3**	**22.5**	**3,622.8**
Transition of new leasing standard net of tax		—	—	—	—	—	(3.7)	(3.7)	—	(3.7)
Restated balance at 1 July 2019		**2,093.7**	**(57.7)**	**0.1**	**(2.6)**	**7.8**	**1,555.3**	**3,596.6**	**22.5**	**3,619.1**
Loss for the year	14	—	—	—	—	—	(416.0)	(416.0)	(5.1)	(421.1)
Other comprehensive income for the year		—	—	—	2.1	—	—	2.1	—	2.1
Total comprehensive income for the year		**—**	**—**	**—**	**2.1**	**—**	**(416.0)**	**(413.9)**	**(5.1)**	**(419.0)**
Other equity movements										
Ordinary shares issued	12	269.4	—	—	—	—	—	269.4	—	269.4
Treasury shares purchased	12	(8.8)	—	—	—	—	—	(8.8)	—	(8.8)
Treasury shares vested	12	14.5	—	—	—	—	—	14.5	—	14.5
Settled forward purchases of Treasury shares	12	8.8	—	—	—	—	—	8.8	—	8.8
Share-based payment expense net of tax less releases	14	—	1.5	—	—	—	—	1.5	—	1.5
Dividends paid	16	—	—	—	—	—	(216.4)	(216.4)	—	(216.4)
Other movements		—	—	—	—	(2.1)	—	(2.1)	(17.4)	(19.5)
Balance at 30 June 2020 and 1 July 2020		**2,377.6**	**(56.2)**	**0.1**	**(0.5)**	**5.7**	**922.9**	**3,249.6**	**—**	**3,249.6**
For the year ended 30 June 2021										
Profit for the year	14	—	—	—	—	—	592.3	592.3	—	592.3
Other comprehensive income for the year		—	—	(0.5)	(2.9)	—	—	(3.4)	—	(3.4)
Total comprehensive income for the year		**—**	**—**	**(0.5)**	**(2.9)**	**—**	**592.3**	**588.9**	**—**	**588.9**
Other equity movements										
Ordinary shares issued	12	37.7	—	—	—	—	—	37.7	—	37.7
Treasury shares purchased	12	—	—	—	—	—	—	—	—	—
Treasury shares vested	12	10.2	—	—	—	—	—	10.2	—	10.2
Settled forward purchases of Treasury shares	12	—	—	—	—	—	—	—	—	—
Share-based payment expense net of tax less releases	14	—	3.4	—	—	—	—	3.4	—	3.4
Dividends paid	16	—	—	—	—	—	(64.0)	(64.0)	—	(64.0)
Other movements		—	—	—	—	—	—	—	—	—
Balance at 30 June 2021		**2,425.5**	**(52.8)**	**(0.4)**	**(3.4)**	**5.7**	**1,451.2**	**3,825.8**	**—**	**3,825.8**

The Statement of changes in equity should be read in conjunction with the accompanying notes.

Statement of cash flows

For the year ended 30 June	Note	2021 $m	2020 $m
Operating activities			
Receipts from customers		645.1	630.0
Annuity and premium receipts	8	4,802.9	3,162.9
Annuity and claim payments	8	(3,787.9)	(3,747.0)
Receipts from external unit holders		2,346.8	2,024.0
Payments to external unit holders		(1,397.9)	(1,670.9)
Payments to vendors and employees		(589.2)	(593.3)
Dividends received		65.0	66.0
Interest received		638.8	733.6
Interest paid		(56.1)	(104.6)
Income tax paid		(90.9)	(15.8)
Net cash inflows from operating activities	11	**2,576.6**	**484.9**
Investing activities			
Payments on net purchases of investments		(936.1)	(1,623.4)
Payments for purchase of controlled entities		—	(10.2)
Net mortgage loan repayments		105.3	164.7
Payments for net purchases of property, plant and equipment		(12.9)	(9.3)
Payments for purchase of associate interest		(21.3)	—
Net cash outflows from investing activities		**(865.0)**	**(1,478.2)**
Financing activities			
Proceeds from issue of ordinary shares		35.0	275.3
Costs associated with issue of ordinary shares		(0.2)	(5.9)
Net (repayments)/proceeds from borrowings – interest bearing financial liabilities	13	(1,409.7)	823.7
Payments for lease liabilities		(6.9)	(5.1)
Proceeds from/(payments) for Treasury shares		0.7	(8.3)
Net dividends paid		(64.0)	(216.4)
Proceeds from the issue of Challenger Capital Notes 3	13	385.0	—
Costs associated with the issue of Challenger Capital Notes 3	13	(6.7)	—
Repayment of Challenger Capital Notes 1	13	(317.3)	—
Net cash (outflows)/inflows from financing activities		**(1,384.1)**	**863.3**
Net increase/(decrease) in cash and cash equivalents		**327.5**	**(130.0)**
Cash and cash equivalents at the beginning of the year		661.9	791.9
Cash and cash equivalents at the end of the year		**989.4**	**661.9**

The Statement of cash flows should be read in conjunction with the accompanying notes.

Section 1: Basis of preparation and overarching significant accounting policies

Challenger Limited (the Company or the parent entity) is a company limited by shares, incorporated and domiciled in Australia, whose shares are publicly traded on the Australian Securities Exchange (ASX).

The financial report for Challenger Limited and its controlled entities (the Group or Challenger) for the year ended 30 June 2021 was authorised for issue in accordance with a resolution of the Directors of the Company on 9 August 2021.

(i) Basis of preparation and statement of compliance

This is a general purpose financial report that has been prepared in accordance, and complies, with the requirements of the *Corporations Act 2001*, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board (AASB) and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). Challenger Limited is a for-profit entity for the purposes of preparing financial statements.

Unless otherwise stated, amounts in this financial report are presented in Australian dollars and have been prepared on an historical cost basis. The assets and liabilities disclosed in the Statement of financial position are grouped by nature and listed in an order that reflects their relative liquidity. In the disclosure, the current/non-current split is between items expected to be settled within 12 months (current) and those expected to be settled in greater than 12 months (non-current).

(ii) Significant accounting judgements, estimates and assumptions

The carrying values of amounts recognised on the Statement of financial position are often based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the recognised amounts within the next annual reporting period are disclosed individually within each of the relevant notes to the financial statements. The impact of COVID-19 has been considered in relation to the disclosures made in these financial statements.

Coronavirus (COVID-19) impact

Background

COVID-19, a respiratory illness caused by a new virus, was declared a worldwide pandemic by the World Health Organization in March 2020. COVID-19, as well as measures to slow the spread of the virus, have since had a significant impact on global economies and equity and debt markets. The Group has considered the impact of COVID-19 and associated market volatility in preparing its financial statements. The impact of COVID-19 has resulted in the application of further judgement in the areas in which significant judgement already occurs. Given the dynamic and evolving nature of COVID-19, limited recent experience of the economic and financial impacts of such a pandemic, changes to the estimates and outcomes that have been applied in the measurement of the Group's assets and liabilities may arise in the future.

Processes applied

As a consequence of COVID-19 and in preparing these consolidated financial statements, management:

- re-evaluated whether there were any additional areas of judgement or estimation uncertainty;
- reviewed external market communications to identify other COVID-19-related impacts;
- reviewed public forecasts and experience from previous downturns and conducted several internal processes to ensure consistency in the application of the expected impact of COVID-19 across all asset classes;
- assessed the carrying values of its assets and liabilities and determined any impact that may occur as a result of market inputs and variables impacted by COVID-19;
- ran multiple stress-testing scenarios, which are an integral component of the Group's risk management framework and a key input to the capital adequacy assessment process, to assess the potential impacts of the COVID-19 pandemic on its portfolio, which assists in the organisation's prudent risk management; and
- considered the impact of COVID-19 on the Group's financial statement disclosures.

As a result of applying these processes, the Group has made additional disclosures in respect of the impact of COVID-19 on accounting judgements and estimates for the following:

- Basis of preparation and overarching significant accounting policies; (xi) Receivables;
- Note 6 Investment and development property;
- Note 7 Special Purpose Vehicles;
- Note 19 Fair values of financial assets and liabilities; and
- Note 25 Goodwill and other intangible assets.

(iii) New and revised accounting standards and policies

Except for the matter referred to below, the accounting policies and methods of computation are the same as those adopted in the annual report for the prior comparative period.

Changes to significant accounting policy

Software-as-a-Service (SaaS)

The International Financial Reporting Standards Interpretations Committee (IFRIC) issued a final decision in April 2021 which impacts SaaS arrangements. The decision discusses whether configuration or customisation expenditure relating to SaaS arrangements can be recognised as an intangible asset and if not, the time period over which the expenditure should be expensed in the Statement of comprehensive income.

(iii) New and revised accounting standards and policies (continued)

The Group's accounting policy has historically been to capitalise all costs related to the configuration and deployment of SaaS arrangements as intangible assets in the Statement of financial position. The adoption of the above decision by IFRIC has resulted in the recognition of an expense of $7.5 million in the Statement of comprehensive income in the current period. Refer to Note 25 Goodwill and other intangible assets for more detail.

New accounting standards and amendments that are effective in the current financial year

There have been no new or revised accounting standards or interpretations that are effective from the year beginning on or after 1 July 2020 which materially impact the financial results. Where applicable, comparative figures have been updated to reflect any changes in the current period.

Accounting standards and interpretations issued but not yet effective

AASB 17 *Insurance Contracts*

AASB 17 ***Insurance Contracts*** replaces AASB 4 ***Insurance Contracts***, AASB 1038 ***Life Insurance Contracts*** and AASB 1023 ***General Insurance Contracts,*** and is effective for Challenger from 1 July 2023. The Group is not expected to early adopt the standard. AASB 17 ***Insurance Contracts*** establishes globally consistent principles for the recognition, measurement, presentation and disclosure of life insurance contracts issued. Life investment contracts are currently measured under the financial instruments standard and will continue to be recognised under this standard.

AASB 17 introduces changes to the profit emergence profiles of life insurance contracts but does not affect the underlying economics or cash flows of the contracts. The impacts on capital requirements and income tax are unknown, pending regulatory responses from APRA and the Australian Taxation Office (ATO) respectively.

The main changes anticipated for the Group under AASB 17 are set out below:

- Insurance contract portfolios will be disaggregated to more granular levels and will be required to be evaluated by risk type, issue year and profitability.
- Although conceptually similar, the Contractual Service Margin (CSM) recognises profit on a different basis to the current Margin on Services (MoS) approach and therefore the profit signature is likely to change for portfolios with positive profit margins.
- A new risk adjustment for non-financial risk will be introduced which reflects the compensation that the Group requires for bearing the uncertainty in relation to the amount and timing of cash flows. The confidence level used to determine the risk adjustment will need to be disclosed.
- Additional disclosures will be more extensive, requiring increased granularity and more analysis of movements.

The Group has conducted a business impact assessment and has identified the following focus areas:

- Measurement model – the Group will adopt the General Model approach, also referred to as the Building Block Approach (BBA). In principle, the General Model approach is similar to the current MoS methodology as prescribed under AASB 1038. The General Model approach is a more detailed methodology that will require enhanced data capture and storing for additional modelling and processes.
- Contracts affected – the Group expects that all contracts classified as insurance contracts under AASB 1038 will meet the definition of insurance contracts under AASB 17.
- Separating components – the Group has assessed the requirement to unbundle features and components under AASB 17 and expects that no change will be required given no contracts are currently unbundled under AASB 1038.
- Under AASB 17, assumptions are to be reviewed on an annual basis at a minimum with some items requiring more frequent review.
- Level of aggregation – AASB 17 requires insurance contracts that are subject to similar risks and managed together, be allocated to a portfolio. AASB 17 requires that each portfolio be divided into a minimum of:
  1. a group that is onerous (loss-making) at initial recognition;
  2. a group that at initial recognition has no significant possibility of becoming onerous subsequently; and
  3. a group of any remaining contracts in the portfolio. The Group has conducted a high-level review of historical data to ascertain the feasibility of meeting the level of aggregation required by AASB 17. In addition, the Group will be formalising a policy for defining portfolios and contract groups. Due to the nature of the insurance products that Challenger offers its customers, the Group expects that most of the portfolios will be designated as onerous. If a portfolio is designated as onerous, a CSM calculation will not be required. Alternatively, the tracking of the loss component will be required under AASB 17.
- Risk adjustment – the Group expects the risk adjustment methodology to align with the cost of capital approach.
- Disclosure - AASB 17 introduces a new way of viewing life insurance revenue and expenses and accompanying financial disclosures. Under AASB 17, insurance contract revenue will be allocated to each period in a proportion to the reduction in liability over the remaining coverage period. The Group has assessed the capability of the Group's general ledger system and confirms that no issues are anticipated for configuring the system to meet the new financial reporting and disclosure requirements under AASB 17.
- Insurance contracts will need to be restated at 1 July 2023 (being the date of initial application). The first full year financial statements presented under AASB 17 will be for the year ended 30 June 2024 with comparatives required for 30 June 2023. The first half year financial statements will be for the period ended 31 December 2023, with comparatives required for 31 December 2022. The Group notes that the full retrospective approach may be impracticable in some cases, especially for older cohorts where assumptions cannot be determined without hindsight.

While the standard is expected to impact the Group's comprehensive income, it is not yet practicable to determine the quantum.

Existing standards and interpretations not yet effective

Other amendments to existing standards or interpretations that are not yet effective are not expected to result in a material impact to the Group's financial statements.

(iv) Comparatives

Where necessary, comparative figures have been reclassified to conform to any changes in presentation made in this financial report.

(v) Rounding of amounts

Unless otherwise stated, amounts contained in this report and the financial report have been rounded to the nearest $100,000 under the option available to the Group under ASIC Corporations Instrument 2016/191.

(vi) Foreign currency

Both the presentation currency and the functional currency of the Company and its controlled Australian entities are Australian dollars. A number of foreign controlled entities have a functional currency other than Australian dollars.

Transactions in foreign currency are translated into the functional currency at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into Australian dollars at the foreign exchange rate at the Statement of financial position date.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the transaction.

Non-monetary items measured at fair value in a foreign currency are translated to the functional currency using the exchange rates at the date when the fair value was determined. Derivatives are used to hedge the foreign exchange risk relating to certain transactions. Refer to Note 10 Derivative financial instruments.

Foreign controlled entities

On consolidation, the assets and liabilities of foreign subsidiaries whose functional currency differs from the presentation currency are translated into Australian dollars at the rate of exchange at the Statement of financial position date. Exchange differences arising on the retranslation are taken directly to the foreign currency translation reserve in equity.

The change in fair value of derivative financial instruments designated as a hedge of the net investment in a foreign controlled entity is also recognised in the foreign currency translation reserve.

On disposal of a foreign controlled entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the Statement of comprehensive income.

(vii) Finance leases

Where Challenger acts as a lessor, leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership. Contracts to lease assets and hire purchase agreements are classified as finance leases for accounting purposes if they transfer substantially all the risks and rewards of ownership of the asset to the customer or an unrelated third party. Assets held under a finance lease are recognised at the beginning of the lease term at an amount equal to the net investment in the lease which comprises the gross investment in the lease discounted at the interest rate implicit in the lease.

The collectability of lease receivables is assessed on an ongoing basis and a provision for expected credit loss is made using inputs such as historical rates of arrears and the current delinquency position of the portfolio. Bad debts are written off as incurred.

(viii) Property, plant and equipment

Items of property, plant and equipment are stated at cost, or deemed cost, less accumulated depreciation and impairment losses. Depreciation is calculated on a straight line basis to realise the net cost of each class of these assets over its expected useful life. Estimates of remaining useful lives are made on a regular basis for all assets, with annual reassessments for major items. The expected useful life of property, plant and equipment is three to five years.

The carrying values of property, plant and equipment and infrastructure fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Impairment losses are recognised in the Statement of comprehensive income.

Any impairment losses recognised in prior periods are reversed through the Statement of comprehensive income if there has been a change in the estimated useful life used to determine the asset's recoverable amount since the last impairment loss was recognised.

The increased carrying amount of an asset attributable to a reversal of an impairment loss would not exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.

(ix) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation. A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for. When the Group expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognised as a separate asset only when the reimbursement is virtually certain. The expense relating to any provision is presented in the Statement of comprehensive income net of any reimbursement.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the obligation at the Statement of financial position date. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the time value of money and the risks specific to the liability. The increase in the provision resulting from the passage of time is recognised in finance costs.

(x) Goods and services tax (GST)

Revenue, expenses and assets are recognised net of the applicable amount of GST, except where the amount of the GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of the acquisition of the asset or as part of the expense.

Receivables and payables are stated with the applicable amount of GST included. The net amount of GST recoverable from, or payable to, the ATO is included as an asset or liability in the Statement of financial position.

Cash flows are included in the Statement of cash flows on a gross (GST-inclusive) basis. The GST components of cash flows arising from investing and financing activities that are recoverable from, or payable to, the ATO are classified as operating cash flows.

(xi) Receivables

Receivables are recognised at amortised cost using the effective interest method, less any allowance for expected credit losses. The entity has applied a simplified approach to measuring expected credit losses, which uses a lifetime expected loss allowance. To measure the expected credit losses, receivables have been grouped based on days overdue. The modelling methodology applied in estimating expected credit losses in these financial statements is consistent with that applied in the financial statements for the year ended 30 June 2020.

The impact of COVID-19 on the global economy and how governments, businesses and consumers respond is uncertain. This uncertainty is reflected in the Group's assessment of expected credit losses from its receivables portfolio which are subject to a number of management judgements and estimates.

The judgements and associated assumptions have been made within the context of the impact of COVID-19, and reflect historical experience and other factors that are considered to be relevant, including expectations of future events that are believed to be reasonable under the circumstances. In relation to COVID-19, judgements and assumptions include the extent and duration of the pandemic, the impacts of actions of governments and other authorities, and the responses of businesses and consumers in different industries, along with the associated impact on the global economy. Accordingly, the Group's expected credit losses estimates are inherently uncertain and, as a result, actual results may differ from these estimates.

(xii) Payables

Payables represent unsecured non-derivative, non-interest bearing financial liabilities in respect of goods and services provided to the Group prior to the end of the financial year. They include accruals, trade and other creditors and are recognised at amortised cost, which approximates fair value.

Section 2: Key numbers

This section presents the results and performance of the Group for the year and provides additional information about those line items on the Statement of comprehensive income that the Directors consider most relevant in the context of understanding the financial components of the Group's operations.

Note 1 Revenue

	30 June 2021 $m	30 June 2020 $m
Investment revenue		
Fixed income securities and cash		
Interest revenue[1]	662.7	774.2
Net realised and unrealised gains/(losses) on fixed income securities	42.8	(90.5)
Investment property and property securities		
Property rental revenue	291.1	283.9
Dividend and distribution revenue	5.6	2.0
Net realised and unrealised gains/(losses) on investment property and property securities	114.6	(112.1)
Equity and infrastructure investments		
Dividend and distribution revenue	22.1	37.9
Net realised and unrealised gains/(losses) on equity investments	124.8	(12.7)
Net realised and unrealised losses on infrastructure investments	(13.0)	(96.7)
Other		
Net realised and unrealised losses on foreign exchange translation and hedges	(78.6)	(51.6)
Net realised and unrealised gains/(losses) on interest rate derivatives	384.2	(99.8)
Net realised and unrealised losses on equity swap derivatives	(16.1)	(202.2)
Net realised and unrealised gains/(losses) on credit default swap derivatives	23.6	(199.7)
Fee revenue		
Management and performance fee revenue	190.7	183.3
Transaction fee revenue	22.8	41.2
Other revenue		
Life insurance contract premiums and related revenue	1,600.6	1,192.7
Change in life insurance contract liabilities	(622.0)	(502.1)
Change in life investment contract liabilities	29.8	(15.4)
Change in reinsurance contract liabilities	—	0.4
Total revenue	**2,785.7**	**1,132.8**

[1] Interest revenue earned for items measured at amortised cost using the effective interest method $29.7 million (30 June 2020: $41.0 million) and interest revenue earned for items measured at fair value through profit and loss $633.0 million (30 June 2020: $733.2 million).

Accounting policy

Revenue is recognised at an amount that reflects the consideration to which the Group expects to be entitled in exchange for providing services to a customer. Revenues and expenses are recognised on an accrual basis. The following specific policies are applied:

- Interest revenue is recognised as it accrues using an effective interest rate method, taking into account the effective yield of the financial asset. The effective interest rate is the rate that discounts estimated future cash flows through the expected life of a financial instrument, or where appropriate, a shorter period.
- Interest revenue on finance leases is recognised on a basis that reflects a constant periodic return on the net investment in the finance lease.
- Gains or losses arising from changes in the fair value of financial instruments classified as fair value through profit and loss are recognised as revenue in the Statement of comprehensive income when the change in value is recognised in the Statement of financial position.
- Property rental revenue is accounted for on a straight line basis over the lease term. Contingent rental income is recognised as income in the period in which it is earned.
- Lease incentives granted are recognised as part of the total rental income. Operating lease rental income is recognised on a straight line basis over the life of the contract.

Note 1 Revenue (continued)

Accounting policy (continued)

- Dividend revenue from listed equity shares and listed property securities is recognised as income on the date the share is quoted ex-dividend. Dividend revenue from unlisted equity shares and unlisted property securities is recognised when the dividend is declared.
- Management fees are invoiced quarterly based on a percentage of the funds under management (FUM). The fees relate specifically to the services provided in that quarter, and are distinct from services provided in other quarters.
- Performance fees are based on returns in excess of a specified benchmark market return, over the contract period. Performance fees are typically received at the end of the performance period specified in the contract. The Company recognises revenue from performance fees over the contract period, but only to the extent that it is highly probable that a significant reversal of revenue will not occur in subsequent periods.
- Transaction fee revenue is accrued when the transaction is executed.
- Life insurance contract premiums are recognised as revenue when risk is transferred to the Group.
- Changes in life insurance and investment contract liabilities arising from discount rates, inflation rates and other assumptions are recognised as revenue, with other movements being included in Note 2 Expenses.

Refer to Note 8 Life contract liabilities for more details on the accounting policy of life contract liabilities.

Note 2 Expenses

	30 June 2021 $m	30 June 2020 $m
Life insurance contract claims and expenses	852.4	749.6
Cost of life insurance contract liabilities	104.1	99.2
Cost of life investment contract liabilities	125.6	121.9
Investment property related expenses[1]	91.2	85.1
Management fee expense	140.3	163.1
Distribution expenses	56.4	47.6
Employee expenses	158.8	146.4
Employee share-based payments and superannuation	21.3	23.6
Occupancy expense – operating lease	4.2	6.0
Depreciation of right-of-use lease asset	6.0	4.7
Depreciation and amortisation expense	9.3	10.6
Technology and communications	29.5	26.7
Professional fees	37.3	20.0
Other expenses	26.0	34.4
Total expenses	**1,662.4**	**1,538.9**

[1] Investment property related expenses relate to rental income generating investment properties.

Accounting policy

Expenses are recognised on an accrual basis. The following specific policies are applied:

- Investment property expenditure, including rates, taxes, insurance and other costs associated with the upkeep of a building, are brought to account on an accrual basis. Repair costs are expensed when incurred. Rental expenses incurred under an investment property operating lease are recognised on a straight line basis over the term of the lease. Other amounts that improve the condition of the investment are capitalised into the carrying value of the asset.
- Life insurance contract claims and expenses are recognised when the liability to the policyholder under the contract has been established.
- Cost of life insurance and life investment contract liabilities recognised as an expense consists of the interest expense on the liability and any loss on the initial recognition of new business less the release of liability in respect of expenses incurred in the current period. The interest expense on the liability represents the unwind of the discount on the opening liability over the period, whereas the impacts of changes in the discount rate applied for the current valuation are included in the change in life contract liabilities disclosed in Note 1 Revenue.

Refer to Note 8 Life contract liabilities for more details on the accounting policy of life contract liabilities.

Note 3 Segment information

The reporting segments[1] of the Group have been identified as follows:

	Life		Funds Management		Total reporting segments		Corporate and other[2]		Total	
For the year ended 30 June	**2021 $m**	**2020 $m**	**2021 $m**	**2020 $m**	**2021 $m**	**2020 $m**	**2021 $m**	**2020 $m**	**2021 $m**	**2020 $m**
Net income	512.8	638.9	169.3	158.1	682.1	797.0	—	0.4	682.1	797.4
Operating expenses	(113.9)	(114.2)	(98.3)	(100.4)	(212.2)	(214.6)	(69.1)	(69.8)	(281.3)	(284.4)
Normalised EBIT	**398.9**	**524.7**	**71.0**	**57.7**	**469.9**	**582.4**	**(69.1)**	**(69.4)**	**400.8**	**513.0**
Interest and borrowing costs	—	—	—	—	—	—	(5.0)	(6.5)	(5.0)	(6.5)
Normalised net profit/(loss) before tax	**398.9**	**524.7**	**71.0**	**57.7**	**469.9**	**582.4**	**(74.1)**	**(75.9)**	**395.8**	**506.5**
Tax on normalised profit									(117.3)	(162.8)
Normalised net profit after tax									**278.5**	**343.7**
Investment experience after tax									318.6	(750.3)
Significant items after tax									(4.8)	(9.4)
Profit/(loss) attributable to the shareholders of Challenger Ltd									**592.3**	**(416.0)**
Other statutory segment information										
Revenue from external customers[3]	1,918.1	148.4	204.9	210.2	2,123.0	358.6	—	—	2,123.0	358.6
Interest revenue	662.2	772.6	—	—	662.2	772.6	0.5	1.6	662.7	774.2
Interest expense	(291.2)	(172.8)	(1.3)	(0.5)	(292.5)	(173.3)	(35.4)	(40.5)	(327.9)	(213.8)
Intersegment revenue	(44.8)	(43.6)	44.8	43.6	—	—	—	—	—	—
Depreciation and amortisation	(4.6)	(3.4)	(3.5)	(2.3)	(8.1)	(5.7)	(1.2)	(4.9)	(9.3)	(10.6)
As at 30 June										
Segment assets	22,337.1	19,481.7	300.6	291.7	22,637.7	19,773.4	7,280.2	8,688.2	29,917.9	28,461.6
Segment liabilities	(18,790.0)	(16,543.3)	(28.4)	(36.0)	(18,818.4)	(16,579.3)	(7,273.7)	(8,632.7)	(26,092.1)	(25,212.0)
Net assets attributable to shareholders	**3,547.1**	**2,938.4**	**272.2**	**255.7**	**3,819.3**	**3,194.1**	**6.5**	**55.5**	**3,825.8**	**3,249.6**

1 Refer below for definitions of the terms used in the management view of segments.
2 Corporate and other includes corporate companies, corporate SPV, non-controlling interests and Group eliminations.
3 Funds Management revenue from external customers is predominantly management fees.

Definitions

Operating segments

The following segments are identified on the basis of internal reporting to Key Management Personnel, including the Chief Executive Officer (the chief operating decision maker) of the Group, and comprise component parts of the Group that are regularly reviewed by senior management in order to allocate resources and assess performance:

Life

The Life segment principally includes the annuity and life insurance business carried out by CLC and Accurium Pty Limited (provision of self-managed superannuation fund actuarial certificates). CLC offers fixed rate retirement and superannuation products that are designed for Australian investors who are seeking a low-risk, fixed term or lifetime investment and reliable income. CLC also offers fixed term and lifetime investments to investors in Japan through its reinsurance arrangement with MS Primary. CLC invests in assets providing long-term income streams for customers.

Note 3 Segment information (continued)

Definitions (continued)

Funds Management

Funds Management earns fees from its Fidante Partners and CIPAM operations, providing an end-to-end funds management business. Funds Management has equity investments in a number of the Fidante Partners boutique fund managers and, through the CIPAM business, offers a range of managed investments across fixed income and property.

Corporate and other

The Corporate and other segment, which is not considered an operating segment of the Group, is used to reconcile the total segment results back to the consolidated results and consists of other income and costs that fall outside the day-to-day operations of the reportable segments. These include the costs of the Group CEO and CFO, shared services across the Group, long-term incentive costs, Directors' fees, corporate borrowings and associated borrowing costs and shareholder registry services. To reconcile to Group results, the Corporate and other segment also includes eliminations and non-core activities of the Group.

Transactions between segments

All transactions and transfers between segments are generally determined on an arm's length basis and are included within the relevant categories of income and expense. These transactions eliminate on consolidation.

Normalised vs. statutory results

Net income and operating expenses differ from revenue and expenses as disclosed in the Statement of comprehensive income as certain direct costs (including distribution expenses, property expenses and management fees) included in expenses are netted off against revenues in deriving the management view of net income above. Net income consists of the following sub-categories of management views of revenue:

- normalised cash operating earnings (Life segment);
- net income (Funds Management segment); and
- other income (Corporate and other segment).

In addition, the revenues, expenses and finance costs from Special Purpose Vehicles (SPVs) are separately disclosed in the statutory view but are netted off in net income.

Revenue also includes investment gains and losses which are excluded from the management view as they form part of investment experience (refer below).

Normalised cash operating earnings

This is calculated as cash earnings plus normalised capital growth (refer below). Cash earnings represent the sum of investment yield (being the management view of revenue from investment assets, such as net rental income, dividends and interest), interest expense, distribution expenses and fees.

Normalised EBIT

Normalised earnings before interest and tax (EBIT) comprises net income less operating expenses, as defined above. It excludes investment experience, corporate interest and borrowing costs, tax and any significant items (refer below).

Tax on normalised profit

This represents the consolidated statutory tax expense or benefit for the period, less tax attributable to non-controlling interests, investment experience and significant items.

Investment experience after tax

The Group is required by accounting standards to value applicable assets and liabilities supporting the life insurance business at fair value. This can give rise to fluctuating valuation movements being recognised in the Statement of comprehensive income, particularly during periods of market volatility.

As the Group is generally a long-term holder of assets, due to assets being held to match the term of life contract liabilities, the Group takes a long-term view of the expected capital growth of the portfolio rather than focusing on short-term volatility. Investment experience is a mechanism employed to isolate the volatility arising from asset and liability valuation within the results so as to more accurately reflect the underlying performance of the Group.

Investment experience is calculated as the difference between the actual investment gains/losses (both realised and unrealised) and the normalised capital growth (refer below) plus life contract valuation changes and new business strain. Investment experience after tax is investment experience net of tax at the prevailing income tax rate.

Normalised capital growth

This is determined by multiplying the normalised capital growth rate for each asset class by the average investment assets for the period. The normalised growth rates represent the Group's medium to long-term capital growth expectations for each asset class over the investment cycle.

The annual normalised growth rates are +4.0% for equity and infrastructure, +2.0% for property, 0.0% for alternatives and -0.35% for cash and fixed income. The asset classes and normalised growth rates changed from 1 July 2020. The rates have been set with reference to the composition of the asset classes and medium to long-term market growth rates, and are reviewed to ensure consistency with prevailing market conditions. The rates for the prior period were as follows, and reflect the composition of the portfolio at that time: +3.5% for equity and other investments, +4.0% for infrastructure, +2.0% for property, and -0.35% for cash and fixed income.

Life contract valuation experience

Life contract valuation experience represents the impact of changes in macroeconomic variables including bond yields and inflation factors, illiquidity premium, expense assumptions and other factors applied in the valuation of life contract liabilities. It also includes the attribution of the corresponding interest rate, foreign exchange and inflation derivatives used for hedging.

Note 3 Segment information (continued)

Definitions (continued)

New business strain

New business strain is a non-cash valuation adjustment recognised when annuity rates on new business are higher than the risk-free rate used to fair value life contracts. Maintenance expense allowances over the expected future term of the new business are also included in the life contract valuation. New business strain reported in the period represents the valuation loss on new sales generated in the current period net of the reversal of new business strain of prior period sales.

Significant items after tax

The Group presents additional non-IFRS financial information to the market to provide meaningful insights into the financial condition of the business. Due consideration has been given to ensure that disclosure of Challenger's normalised profit framework is explained, reconciled and calculated consistently period-on-period. Within this framework, Challenger defines significant items as non-recurring or abnormal income or expense items.

Major customers

No individual customer amounted to greater than 10% of the Group's segment as defined above.

Geographical areas

The Group operates predominantly in Australia, hence no geographical split is provided to the chief operating decision maker. Reinsurance of annuities issued by MS Primary accounted for $901.6 million of the Group's life insurance premium income in 2021 out of total life insurance premium income of $1,363.7 million (2020: $742.6 million out of a total of $1,157.1 million) and comprised 15.2% of total policy liabilities outstanding as at 30 June 2021 (2020: 13.7%); while the underlying annuitant resides in Japan, the reinsurance service provided by CLC is considered to be Australian business and is therefore not recognised as a geographically separate segment.

	30 June 2021 $m	30 June 2020 $m
Reconciliation of management to statutory view of after-tax profit/(loss)		
Operating segments normalised net profit before tax	469.9	582.4
Corporate and other normalised net loss before tax	(74.1)	(75.9)
Normalised net profit before tax (management view of pre-tax profit)	**395.8**	**506.5**
Tax on normalised profit	(117.3)	(162.8)
Normalised net profit after tax	**278.5**	**343.7**
Investment experience after tax	318.6	(750.3)
Significant items after tax	(4.8)	(9.4)
Profit/(loss) attributable to the shareholders of Challenger Limited	**592.3**	**(416.0)**
Loss attributable to non-controlling interests excluded from management view	—	(5.1)
Statutory view of profit/(loss) after tax	**592.3**	**(421.1)**
Reconciliation of management view of revenue to statutory revenue		
Operating segments	682.1	797.0
Corporate and other	—	0.4
Net income (management view of revenue)	**682.1**	**797.4**
Expenses and finance costs offset against revenue		
SPV expenses and finance costs offset against SPV income	3.3	11.1
Distribution expenses offset against related income	56.4	47.6
Change in life contract liabilities and reinsurance contracts recognised in expenses	1,082.1	970.7
Property related expenses offset against property income	91.2	85.1
Interest and loan amortisation costs	289.0	160.3
Management fee expenses	140.3	163.1
Adjustment for non-controlling interests and other items	(13.8)	(32.0)
Difference between management view of investment experience and statutory recognition		
Actual capital growth	576.2	(1,068.3)
Normalised capital growth	(34.1)	(120.2)
Life contract valuation experience	(76.1)	86.1
New business strain	(10.9)	31.9
Statutory revenue (refer Note 1 Revenue)	**2,785.7**	**1,132.8**

Note 4 Income tax

Reconciliation of income tax (expense)/benefit	30 June 2021 $m	30 June 2020 $m
Profit/(loss) before income tax	830.6	(590.6)
Prima facie income tax based on the Australian company tax rate of 30%	(249.2)	177.2
Tax effect of amounts not assessable/deductible in calculating taxable income:		
– Challenger Capital Notes distributions	(7.9)	(8.3)
– non-assessable and non-deductible items	8.4	(5.3)
– tax rate differentials	10.6	5.9
– tax adjustment in respect of non-controlling interests	—	(1.5)
– other items	(0.2)	1.5
Income tax (expense)/benefit	**(238.3)**	**169.5**
Underlying effective tax rate[1]	**28.7%**	**28.9%**

[1] The calculation of the underlying effective tax rate excludes the non-controlling interests' profit of nil (30 June 2020: loss $5.1 million).

Analysis of income tax (expense)/benefit	30 June 2021 $m	30 June 2020 $m
Current income tax expense for the year	(140.0)	(28.6)
Current income tax benefit prior year adjustment	1.9	3.9
Deferred income tax (expense)/benefit	(101.6)	198.3
Deferred income tax benefit/(expense) prior year adjustment	1.4	(4.1)
Income tax (expense)/benefit	**(238.3)**	**169.5**
Income tax benefit on translation of foreign entities	17.4	5.0
Income tax expense on hedge of net investment in foreign operations	(20.1)	(0.2)
Income tax (expense)/benefit from other comprehensive income	**(2.7)**	**4.8**

	Statement of financial position		Statement of comprehensive income	
Analysis of deferred tax	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m
Deferred tax assets				
Accruals and provisions	49.3	49.4	(0.1)	10.2
Employee entitlements	5.5	5.1	0.4	1.2
Losses	6.1	92.1	(86.0)	80.9
Other	19.0	16.6	0.7	3.6
Total deferred tax assets	**79.9**	**163.2**	**(85.0)**	**95.9**
Set off of deferred tax assets	**(75.9)**	**(113.4)**		
Net deferred tax assets recognised in Statement of financial position	**4.0**	**49.8**		
Deferred tax liabilities				
Unrealised foreign exchange movements	(7.7)	(1.9)	(3.5)	12.3
Unrealised net gains on investments	(124.1)	(114.6)	(9.5)	68.4
Other	(4.8)	(2.6)	(2.2)	17.6
Total deferred tax liabilities	**(136.6)**	**(119.1)**	**(15.2)**	**98.3**
Set off of deferred tax liabilities	**75.9**	**113.4**		
Net deferred tax liabilities recognised in Statement of financial position	**(60.7)**	**(5.7)**		
Deferred income tax (expense)/benefit recognised in Statement of comprehensive income			**(100.2)**	**194.2**

Note 4 Income tax (continued)

Tax Transparency Code Disclosures

Australia and overseas tax (expense)/benefit	30 June 2021 $m	30 June 2020 $m	Change $m
Total Australia	(228.5)	176.6	(405.1)
Total overseas	(9.8)	(7.1)	(2.7)
Income tax (expense)/benefit	**(238.3)**	**169.5**	**(407.8)**

Analysis of current tax liability	30 June 2021 $m	30 June 2020 $m
Opening balance	1.0	(2.7)
Current income tax expense for the year	140.0	28.6
Current income tax prior year adjustment	(1.9)	(3.9)
Tax in equity	(0.4)	(1.8)
Income tax paid	(90.9)	(15.8)
Other	0.3	(3.4)
Closing balance	**48.1**	**1.0**

Unrecognised deferred tax balances	30 June 2021 $m	30 June 2020 $m
Non-tax consolidated group revenue losses – tax effected	7.6	7.4
Tax consolidated group capital losses – tax effected	56.4	56.2

Accounting policy

Income tax expense

Income tax expense for the year comprises current and deferred tax. Income tax is recognised in the Statement of comprehensive income except to the extent that it relates to items recognised directly in equity.

Current tax assets and liabilities

Current tax assets and liabilities for the current and prior periods are the amounts expected to be recovered from or paid to the taxation authorities based on the respective period's taxable income. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted as at the Statement of financial position date. Current tax assets and liabilities have been offset where there is a legally enforceable right to set off.

Deferred income tax assets and liabilities

Deferred income tax is provided on temporary differences at the Statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax assets and liabilities are recognised for deductible or taxable temporary differences and are measured at the tax rates that are expected to apply to the year the asset is realised or the liability is settled, based on the tax rates (and tax laws) that have been enacted or substantially enacted as at the Statement of financial position date. Deferred income tax assets and liabilities have been offset where they relate to income tax levied by the same taxation authority on either the same taxable entity or different taxable entities within the same taxable group who have a legal right and an intention to settle on a net basis. Deferred tax assets are recognised for the carryforward of unused tax losses to the extent that it is probable that future taxable profit will be available against which the unused tax losses can be utilised.

Tax consolidation

Challenger Limited and its 100% owned Australian resident subsidiaries formed a tax consolidated group with effect from 1 July 2002 and are therefore taxed as a single entity from that date. Challenger Limited is the head entity of the tax consolidated group.

Tax effect accounting by members of the tax group

Members of the tax consolidated group have applied tax funding principles under which Challenger Limited and each of the members of the tax consolidated group agree to pay or receive tax equivalent amounts to or from the head entity, based on the current tax liability or current tax asset of the member. Such amounts are reflected in the amounts receivable from or payable to each member and the head entity. The group allocation approach is applied in determining the appropriate amount of current tax liability or current tax asset to allocate to members of the tax consolidated group.

Key estimates and assumptions

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Section 3: Operating assets and liabilities

This section discloses information relating to the assets and liabilities underlying the Group's financial performance and the key sources of funding for those assets. It further presents the derivative financial instruments employed to hedge the Group's financial risk exposures, and consolidated information relating to the cash flows of the Group.

Note 5 Financial assets – fair value through profit and loss

	30 June 2021 $m	30 June 2020 $m
Domestic sovereign bonds and semi-government bonds	6,054.8	8,610.3
Floating rate notes and corporate bonds	6,576.3	4,915.6
Residential mortgage and asset-backed securities	7,653.6	5,809.2
Non-SPV mortgage assets	112.2	139.8
Fixed income securities	**20,396.9**	**19,474.9**
Shares in listed and unlisted corporations	143.1	97.8
Unit trusts, managed funds and other	1,201.3	804.9
Equity securities	**1,344.4**	**902.7**
Units in listed and unlisted infrastructure trusts	48.8	55.9
Other infrastructure investments	296.6	324.2
Infrastructure investments	**345.4**	**380.1**
Indirect property investments in listed and unlisted trusts	88.0	76.3
Property securities	**88.0**	**76.3**
Total financial assets – fair value through profit and loss	**22,174.7**	**20,834.0**
Current	11,911.1	8,339.2
Non-current	10,263.6	12,494.8
	22,174.7	**20,834.0**

Accounting policy

The Group categorises its financial assets as financial assets – fair value through profit and loss (being initially designated as such). Assets designated as fair value through profit and loss consist of fixed income, equity, infrastructure, and property securities. They are carried at fair value with unrealised gains and losses being recognised through the Statement of comprehensive income.

Purchases and sales of financial assets are recognised on the date on which the Group commits to purchase or sell the asset and when all risks and rewards of ownership have been substantially transferred. Financial assets are then derecognised when the right to receive cash flows from the asset has expired.

The fair value of financial assets that are actively traded in organised financial markets isre determined by reference to quoted market bid prices at the close of business on the Statement of financial position date. Assets backing life contract liabilities of the statutory fund are required to be designated at fair value through profit and loss in accordance with AASB 1038 ***Life Insurance Contracts*** when permitted by other Australian Accounting Standards.

Key estimates and assumptions

Unlisted investment valuations

Investments held at fair value through profit and loss for which there is no active market or external valuation available are valued making as much use of available and supportable market data as possible and keeping judgemental inputs to a minimum, either by:

- reference to the current market value of another instrument that is substantially the same;
- using recent arm's length market transactions;
- option pricing models refined to reflect the issuer's specific circumstances;
- discounted cash flow analysis; or
- other methods consistent with market best practice.

Refer to Note 18 Financial risk management for further disclosure.

Note 6 Investment and development property

	30 June 2021 $m	30 June 2020 $m
Investment property held for sale[1]	388.0	—
Investment property in use	3,389.7	3,679.7
Investment property under development	—	6.2
Development property held for sale[2,3]	8.0	—
Total investment and development property[4]	**3,785.7**	**3,685.9**

1 Investment property held for sale: County Court (30 June 2020: Nil).
2 Development property held for sale: Maitland (30 June 2020: Nil).
3 Development property held for sale is recognised at fair value.
4 Investment and development property held for sale is considered current. All other investment property is considered non-current.

	Investment property held for sale		Investment property in use		Investment property under development		Development property held for sale	
Reconciliation of carrying amounts	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m
Balance at the beginning of the year	—	166.5	3,679.7	3,384.3	6.2	178.4	—	—
Movements for the year								
– acquisitions[1]	—	—	—	105.1	—	—	—	—
– disposals	—	(155.9)	—	—	—	—	—	—
– net transfers to/(from) investment property held for sale	326.0	(10.7)	(326.0)	10.7	—	—	—	—
– transfers to/(from) investment property under development	—	—	—	173.7	(6.2)	(173.7)	6.2	—
– capital expenditure	0.7	0.1	50.3	72.8	—	0.2	0.1	—
– net revaluation gain/(loss)	61.3	—	75.8	(78.4)	—	1.3	1.7	—
– foreign exchange gain	—	—	(90.1)	11.5	—	—	—	—
Balance at the end of the year	**388.0**	**—**	**3,389.7**	**3,679.7**	**—**	**6.2**	**8.0**	**—**

1 Investment property acquisitions: Nil (30 June 2020: Acquisition of remaining 50% of Lennox, NSW $33.5m, Aeon Matsusaka XD, Japan $14.7m, Kotesashi Towers, Japan $25.2m and Yorktown Toride, Japan $31.7m).

Accounting policy

Investment and development property

Investment and development property is initially recognised at cost, including transaction costs. Subsequent to initial recognition, investment and development property is recognised at fair value.

Investment and development property is classified as held for sale if its carrying value will be recovered principally through a sale transaction rather than through continuing use. This condition is met only when management is committed to the sale, and the sale is highly probable to occur in the next 12 months. Investment and development property held for sale is carried at fair value, being the latest valuation available, or agreed sale price.

Gains or losses arising from changes in the fair values of investment properties are included in the Statement of comprehensive income in the period in which they arise.

Investment and development properties are derecognised when they have either been disposed of or when the investment property is permanently withdrawn from use and no future benefit is expected from its disposal. Any gain or loss on the retirement or disposal of an investment and development property is recognised in the Statement of comprehensive income in the year of retirement or disposal.

Where properties are debt financed, that finance is provided either by secured mortgages or by funding that contains a number of negative undertakings (including undertakings not to create or allow encumbrances, and undertakings not to incur financial indebtedness which ranks in priority to existing debt).

Note 6 Investment and development property (continued)

Accounting policy (continued)

Investment property under development

When redevelopment of an existing investment property commences, it continues to be classified and measured as investment property when the asset is being redeveloped for continued future use as an investment property.

Investment property under construction is held at cost until an estimate of the fair value can be reliably determined.

Impact of COVID-19

Across all sectors, particularly retail, some tenants have sought rent relief due to the impact the COVID-19 pandemic has had on their ability to meet rental obligations. Rent relief is granted after considering various factors and individual tenant circumstances. Rent amounts will fall into the following categories: (i) current rent due and payable now; (ii) deferred rent, payable at a later date; or (iii) waived rent, not payable.

If relief is given for current and deferred rent, income will continue to be recognised on a straight line basis over the term of the lease. The resulting rent receivable assets recognised in the Statement of financial position as at 30 June 2021 have been assessed for impairment.

The methodology adopted for determining whether these rent receivable assets should be impaired is aligned to the requirements of AASB 9 *Financial Instruments.*

When an agreement is made between the landlord and tenant to waive rent:

- rent waived relating to future occupancy is spread over the remaining lease term and recognised on a straight line basis;
- rent waived relating to past occupancy is expensed immediately, except to the extent of a pre-existing provision for expected credit losses relating to unpaid rent.

Key estimates and assumptions

Independent valuations for all investment properties are conducted at least annually by suitably qualified valuers, and the Directors make reference to these independent valuations when determining fair value. For the year ended 30 June 2021, all investment properties were valued by external valuers.

Each independent valuer is appointed in line with the valuation policy, which requires that valuers are authorised to practise under the law of the relevant jurisdiction where the valuation takes place and have at least five years of continuous experience in the valuation of property of a similar type to the property being valued and on the basis that they are engaged for no longer than two consecutive years on an individual property.

The valuer must have no pecuniary interest that could conflict with the valuation of the property, must be suitably indemnified, and must comply with the Australian Property Institute (API) Code of Ethics and Rules of Professional Conduct (or foreign equivalent).

Fair value for the purposes of the valuation is market value as defined by the International Assets Valuation Standards Committee. In determining market value, valuers examine available market evidence and apply this analysis to both the traditional market capitalisation approach and the discounted cash flow approach (using market-determined risk-adjusted discount rates).

Valuers are required to provide valuation methodology and calculations for fair value including reference to annual net market income, comparable capitalisation rates, and property-specific adjustments. The values of investment property do not reflect anticipated enhancement from future capital expenditure.

Impact of COVID-19

As at 30 June 2021 the real estate markets to which the Group's investment properties belong were still being impacted by significant uncertainty caused by the COVID-19 pandemic. This has continued to create valuation uncertainty for the year ended 30 June 2021.

The valuation uncertainty has affected key inputs, assumptions and processes used in the valuation of the Group's investment properties, being:

- estimating and forecasting the net income that a property can produce; and
- converting that income to value by applying investment rates of return which are derived from analysis of recent market transactions.

Income uncertainty

The impact of COVID-19 on the income-earning potential of the Group's properties remains uncertain. The Group leases commercial space to a range of businesses from where they conduct their operations. Restrictions imposed by Government to combat COVID-19 has, in a majority of cases, impacted the ability for these businesses to operate effectively from their premises, or has affected their ability to operate in the usual manner prior to the onset of COVID-19.

In response to this and the Government's Code of Conduct for commercial tenancies, the Group is currently finalising the cost-sharing program introduced by the Code of Conduct for each tenant that has been affected. This involves the Group either deferring or waiving rent owed by the tenant depending on the individual circumstances. The legislative period for this relief has now ended across all states and there remains a small portion of rent relief negotiations in progress which are yet to be finalised. Since 30 June 2021, the NSW and Victorian Governments have reintroduced restrictions to combat several COVID-19 outbreaks within each state. These restrictions will impact the operations of businesses across all sectors in which the Group has property exposure. To assist businesses through these restrictions, the Government has announced business relief packages for those that are hardest hit. The Group will continue to monitor the Government's position on these business support packages and work with those tenants that have been severely impacted.

Rent receivable balances in respect of current and deferred rent recognised in the Statement of financial position for the reporting period, have been assessed for impairment. An approach has been adopted which applies a lifetime expected credit loss and assesses all possible default events over the expected life of the receivables balance.

Note 6 Investment and development property (continued)

Key estimates and assumptions (continued)

An appropriate loss rate has then been determined after considering the following factors:

- the asset sector in which the affected rent receivable is recognised. Each sector is affected differently by COVID-19 and this needs to be reflected in any loss assumption;
- the ranking of tenants by most to least affected by COVID-19 impacts; and
- the ageing of rent receivables.

After taking these factors into consideration and the cost-sharing program undertaken with tenants, an impairment of $2.7 million was recognised in the Statement of comprehensive income as at 30 June 2021 (30 June 2020: $2.2 million) which includes an impairment for current and deferred rent, as well as waived rent impaired immediately. This assessment was conducted based on reasonable and supporting information readily available, and considering current and expected future economic conditions.

Valuation uncertainty

Valuation uncertainty has also arisen from a lack of transactional evidence from which to gauge current market pricing with strong conviction.

Due to uncertainty relating to the impact of COVID-19, transaction volumes were low through the first half of the year ended 30 June 2021. Although activity has begun to improve, at this point in time, the repercussions of the pandemic on the property market remains uncertain and market pricing cannot be known with certainty until such time as the market stabilises.

In response to this valuation uncertainty, the Group determined that all directly held investment properties would be independently valued by external valuers at 30 June 2021. The Group's independent valuers have accounted for this income and investment uncertainty by adjusting valuation inputs and estimates to acknowledge the potential impact of COVID-19 on investment property values. In addition to having regard to the available sales evidence to determine capitalisation and discount rates, they have also, where appropriate, adopted lower growth rates in the short to medium term, increased vacancy rates and letting up allowances and lower market rental levels. Notwithstanding the end of the legislated period for rent relief, valuers have continued to make deductions for the estimated cost of rent relief to tenants for occupancy disruption resulting from the COVID-19 pandemic.

Analysis of investment property as at 30 June	Acquisition date[1]	Total cost[2] $m	Carrying value 2021 $m	Cap rate 2021[3] %	Last external valuation date	Carrying value 2020 $m	Cap rate 2020[3] %
Investment property in use and held for sale							
Australia							
6 Chan Street (formerly DIBP Building), ACT	01-Dec-01	127.5	261.0	4.88	30-Jun-21	202.0	5.50
14 Childers Street, ACT	01-Dec-17	98.8	85.5	6.50	30-Jun-21	91.0	6.50
21 O'Sullivan Circuit, NT	27-Jan-16	47.8	31.4	7.75	30-Jun-21	32.1	8.50
31 O'Sullivan Circuit, NT	27-Jan-16	29.4	28.5	7.25	30-Jun-21	23.5	8.50
35 Clarence Street, NSW	15-Jan-15	154.0	229.0	5.13	30-Jun-21	235.0	5.00
45 Benjamin Way (formerly ABS Building), ACT	01-Jan-00	150.2	251.0	5.38	30-Jun-21	223.0	5.75
82 Northbourne Avenue, ACT	01-Jun-17	62.3	51.8	5.75	30-Jun-21	53.3	6.00
215 Adelaide Street, QLD	31-Jul-15	256.7	225.0	6.00	30-Jun-21	230.5	6.13
565 Bourke Street, VIC	28-Jan-15	109.1	148.0	5.00	30-Jun-21	147.5	5.00
839 Collins Street, VIC	22-Dec-16	212.0	246.5	4.75	30-Jun-21	238.5	4.75
Bunbury Forum, WA	03-Oct-13	158.2	78.1	7.25	30-Jun-21	82.0	7.50
Channel Court, TAS	21-Aug-15	87.8	80.0	7.25	30-Jun-21	76.0	7.75
Cosgrave Industrial Park, Enfield, NSW	31-Dec-08	91.4	139.4	4.50	30-Jun-21	131.9	5.00
County Court, VIC	30-Jun-00	219.1	388.0	n/a	30-Jun-21	326.0	n/a
Discovery House, ACT	28-Apr-98	104.6	164.0	5.13	30-Jun-21	152.5	5.63
Executive Building, TAS	30-Mar-01	35.1	49.0	5.75	30-Jun-21	46.5	7.00
Gateway, NT	01-Jul-15	124.1	102.9	6.34	30-Jun-21	105.1	6.34
Golden Grove, SA	31-Jul-14	159.9	148.0	6.25	30-Jun-21	147.0	6.25
Karratha, WA	28-Jun-13	57.1	45.4	7.50	30-Jun-21	44.3	7.50
Kings Langley, NSW	29-Jul-01	16.6	24.7	5.75	30-Jun-21	23.0	6.25
Lennox, NSW	27-Jul-13	64.2	65.0	6.75	30-Jun-21	61.0	6.75
North Rocks, NSW	18-Sep-15	187.0	179.0	6.00	30-Jun-21	171.1	6.25
Total Australia		**2,552.9**	**3,021.2**			**2,842.8**	

1 Acquisition date represents the date of initial acquisition or consolidation of the investment vehicle holding the asset.
2 Total cost represents the original acquisition cost plus additions less full and partial disposals since acquisition date.
3 The capitalisation rate is the rate at which net market income is capitalised to determine the value of the property. The rate is determined with regard to market evidence.

Note 6 Investment and development property (continued)

Analysis of investment property as at 30 June (continued)	Acquisition date[1]	Total cost[2] $m	Carrying value 2021 $m	Cap rate 2021[3] %	Last external valuation date	Carrying value 2020 $m	Cap rate 2020[3] %
Europe							
Avenue de Savigny, Aulnay sous Bois	31-Dec-08	20.3	9.8	7.00	30-Jun-21	10.1	7.33
Japan							
Aeon Kushiro	31-Jan-10	30.5	34.2	5.40	30-Jun-21	38.5	5.40
Aeon Matsusaka XD	26-Sep-19	14.7	13.7	5.60	30-Jun-21	14.5	5.80
Carino Chitosedai	31-Jan-10	118.4	127.2	4.50	30-Jun-21	138.6	4.50
Carino Tokiwadai	31-Jan-10	77.6	75.5	4.60	30-Jun-21	85.9	4.70
DeoDeo Kure	31-Jan-10	32.2	31.2	5.50	30-Jun-21	35.3	5.60
Fitta Natalie Hatsukaichi	28-Aug-15	11.7	13.4	5.90	30-Jun-21	14.8	6.00
Izumiya Hakubaicho	31-Jan-10	69.6	71.4	4.80	30-Jun-21	78.0	5.00
Kansai Super Saigo	31-Jan-10	13.3	13.2	5.50	30-Jun-21	14.7	5.30
Kojima Nishiarai	31-Jan-10	12.2	14.6	4.10	30-Jun-21	16.4	4.40
Kotesashi Towers	28-Nov-19	25.2	21.5	5.07	30-Jun-21	24.3	5.10
Life Asakusa	31-Jan-10	27.9	35.1	4.20	30-Jun-21	38.6	4.30
Life Higashi Nakano	31-Jan-10	32.9	36.7	4.30	30-Jun-21	40.7	4.40
Life Nagata	31-Jan-10	25.2	27.7	4.90	30-Jun-21	30.3	4.20
MaxValu Tarumi	28-Aug-15	17.0	18.2	5.70	30-Jun-21	20.6	5.60
Seiyu Miyagino	31-Jan-10	9.8	10.6	5.20	30-Jun-21	12.0	5.20
TR Mall Ryugasaki	30-Mar-18	86.7	90.5	5.50	30-Jun-21	98.7	5.60
Valor Takinomizu	31-Jan-10	27.4	23.5	5.80	30-Jun-21	26.5	5.50
Valor Toda	31-Jan-10	42.5	41.7	5.20	30-Jun-21	46.3	5.10
Yaoko Sakato Chiyoda	31-Jan-10	19.8	20.9	4.70	30-Jun-21	22.8	4.90
Yorktown Toride	05-Mar-20	31.9	25.9	5.10	30-Jun-21	29.3	5.30
Total international		**746.8**	**756.5**			**836.9**	
Total investment property in use and held for sale[4]		**3,299.7**	**3,777.7**			**3,679.7**	
Investment property under development and development property held for sale							
Maitland, NSW	6-Dec-06	5.7	8.0	n/a	30-Jun-21	6.2	n/a
Total investment property under development and development property held for sale		**5.7**	**8.0**			**6.2**	

1 Acquisition date represents the date of initial acquisition or consolidation of the investment vehicle holding the asset.
2 Total cost represents the original acquisition cost plus additions less full and partial disposals since acquisition date.
3 The capitalisation rate is the rate at which net market income is capitalised to determine the value of the property. The rate is determined with regard to market evidence.
4 At 30 June 2021, the investment property portfolio occupancy rate for Australia was 90.3% (30 June 2020: 90.7%) with a weighted average lease expiry of 5.1 years (30 June 2020: 5.5 years), Europe 100.0% (30 June 2020: 100.0%) with a weighted average lease expiry of 0.1 years (30 June 2020: 0.1 years) and Japan 99.5% (30 June 2020: 99.5%) with a weighted average lease expiry of 9.4 years (30 June 2020: 9.7 years).

Note 7 Special Purpose Vehicles

Consolidated	30 June 2021 $m	30 June 2020 $m
Cash and cash equivalents	60.8	58.0
Mortgage assets[1]	570.3	706.6
Derivative assets	—	0.4
Total assets	**631.1**	**765.0**
Payables	257.7	303.9
Derivative liabilities	0.5	0.3
Interest bearing financial liabilities[2]	373.3	460.7
Total liabilities	**631.5**	**764.9**
Net assets	**(0.4)**	**0.1**
Cash flow hedge reserve	(0.4)	0.1
Total equity attributable to residual income unit holders	**(0.4)**	**0.1**

1 $138.9 million (30 June 2020: $137.7 million) of the Mortgage assets balance is considered current.
2 $90.9 million (30 June 2020: $89.8 million) of the Interest bearing financial liabilities balance is considered current.

Accounting policy

The Group manages and services Special Purpose Vehicle (SPV) trusts that hold residential mortgage-backed assets and issue securitised financial liabilities. The trusts are entities that fund pools of residential mortgage-backed loans via the issuance of residential mortgage-backed securities (RMBS). All borrowings of these SPVs are limited in recourse to the assets of the SPV.

As the Group retains the beneficial interest to the residual income of these trusts, it is deemed to control them and, as a result, they are consolidated. However, the significant risks and rewards (most notably credit risk) lie with the RMBS holders.

The assets and liabilities of the SPV have been separately disclosed in the financial report as this presentation is considered to provide a more transparent view of the Group's financial position. Transactions between the SPV and other entities within the Group are eliminated on consolidation.

SPV cash and cash equivalents are financial assets and comprise cash at bank and in hand plus short-term deposits with an original maturity of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents are initially recognised at fair value and subsequently carried at amortised cost.

SPV mortgage assets are non-derivative financial loan assets with fixed or determinable payments that are not quoted in an active market. They are recognised net of any credit loss provision.

The Group uses derivative financial instruments to hedge the risks associated with SPV interest rate and foreign currency fluctuations. All these derivative financial instruments are stated at fair value. Gains or losses arising from fair value changes on derivatives that do not qualify for hedge accounting are recognised in the Statement of comprehensive income.

SPV payables represent unsecured non-derivative, non-interest bearing financial liabilities in respect of services provided to the trusts prior to the end of the financial year. They include accruals and other creditors and are recognised at amortised cost.

SPV interest bearing financial liabilities are initially recognised at fair value calculated net of directly attributable transaction costs, and subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the Statement of comprehensive income over the period of the contract using the effective interest rate method.

Key estimates and assumptions

The Group continues to apply the historical provisioning methodology which is considered to be materially consistent with the provision estimated under the Expected Credit Loss (ECL) impairment model. In estimating ECL for individual mortgage loans, the Group makes judgements and assumptions in relation to expected repayments, the realisable value of the secured property, the prospects of the customer, the value of any mortgage insurance and the likely cost and duration of the work-out process. Judgements and assumptions in respect of these matters have been updated to reflect the potential impact of COVID-19. The Group has also considered historical probabilities of default, the relative age of the mortgage loan portfolio and the loan to valuation ratios applicable to the mortgage loans and has determined that the current provision estimated by the ECL impairment model is adequate and no further overlay for the impact of COVID-19 is required.

Analysis of SPV mortgage assets impairment provision	30 June 2021 $m	30 June 2020 $m
Balance at the beginning of the year	11.5	10.2
Increase in provisions	0.5	0.9
Utilisation of provision against incurred losses and adjustments to estimates	(0.2)	0.4
Balance at the end of the year	**11.8**	**11.5**

Note 8 Life contract liabilities

Fair value of life contract liabilities	30 June 2021 $m	30 June 2020 $m
Life investment contract liabilities – at fair value	6,230.4	5,867.8
Life insurance contract liabilities – at margin on services value	7,440.5	6,714.4
Reinsurance contract liabilities – at margin on services value	(1.0)	(1.0)
Total life contract liabilities	**13,669.9**	**12,581.2**

Movement in life contract liabilities	Life investment contract liabilities		Life insurance contract liabilities		Outward reinsurance contract liabilities		Total life contract liabilities	
	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m
Balance at the beginning of the year	5,867.8	6,757.7	6,714.4	6,113.1	(1.0)	(0.6)	12,581.2	12,870.2
Deposits and premium receipts	3,202.3	1,970.2	1,600.6	1,192.7	—	—	4,802.9	3,162.9
Payments and withdrawals	(2,935.5)	(2,997.4)	(852.4)	(749.6)	—	—	(3,787.9)	(3,747.0)
Revenue per Note 1	(29.8)	15.4	(978.6)	(690.6)	—	(0.4)	(1,008.4)	(675.6)
Expense per Note 2	125.6	121.9	956.5	848.8	—	—	1,082.1	970.7
Balance at the end of the year	**6,230.4**	**5,867.8**	**7,440.5**	**6,714.4**	**(1.0)**	**(1.0)**	**13,669.9**	**12,581.2**

Analysis of life insurance and reinsurance contract liability and expenses	30 June 2021 $m	30 June 2020 $m
Best estimate liability		
Value of future life insurance contract benefits	6,928.6	6,435.1
Value of future expenses	196.6	171.3
Value of future acquisition expenses	175.1	166.9
Value of future premiums	(902.1)	(889.3)
Total best estimate liability	**6,398.2**	**5,884.0**
Value of future profit margins	1,041.3	829.4
Net life insurance and reinsurance contract liability	**7,439.5**	**6,713.4**
Life insurance and reinsurance contract operating expenses		
Maintenance expenses	61.6	54.9
Total life insurance and reinsurance contract operating expenses	**61.6**	**54.9**
Analysis of life contract profit		
Profit margin release on life insurance contracts	23.5	27.8
Loss recognition in respect of life insurance contracts[1]	(50.6)	(43.5)
Loss recognition in respect of life investment contracts	(88.7)	(54.2)
Difference in actual and assumed experience in respect of life insurance contracts	267.8	(74.5)
Difference in actual and assumed experience in respect of life investment contracts	278.5	(68.6)
Profit/(loss) arising from difference between actual and assumed experience	**430.5**	**(213.0)**
Investment earnings on assets in excess of life contract liabilities	197.3	(123.6)
Life contract profit/(loss) after tax	**627.8**	**(336.6)**

[1] Under margin on services (MoS), any profits expected over the life of a contract are recognised over the life of the contract; however, if on the liability valuation basis the contract is expected to be loss making, the capitalised value of these future losses is recognised at the point of sale. Retail insurance contracts are in loss recognition because the liability valuation basis uses a risk-free discount rate but the rates offered to customers are higher.

Note 8 Life contract liabilities (continued)

Accounting policy

The operations of the Group include the selling and administration of life contracts through Challenger Life Company Limited (CLC). These contracts are governed under the ***Life Insurance Act 1995*** (the Life Act) and are classified as either life insurance contracts or life investment contracts. Life insurance and life investment contract liabilities are collectively referred to as life contract liabilities or policy liabilities.

Life investment contract liabilities

Life investment contracts are contracts regulated under the Life Act but which do not meet the definition of life insurance contracts under AASB 1038 ***Life Insurance Contracts*** and similar contracts issued by entities operating outside of Australia.

For fixed term policies, the liability is based on the fair value of the income payments and associated expenses, being the net present value of the payments and expenses using an appropriate discount rate curve as determined by the Appointed Actuary.

Life insurance contract liabilities

Life insurance contracts are contracts regulated under the Life Act that involve the acceptance of significant insurance risk. Insurance risk is defined as significant if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance (i.e. have no discernible effect on the economics of the transaction).

The financial reporting methodology used to determine the value of life insurance contract liabilities is referred to as margin on services (MoS). Under MoS, the excess of premiums received over payments to customers and expenses (the margin) is recognised over the life of the contract in a manner that reflects the pattern of risk accepted from the policyholder (the service) unless future margins are negative, in which case the future losses are recognised in the Statement of comprehensive income immediately. The planned release of this margin is recognised in the Statement of comprehensive income as part of the movement in life insurance contract liabilities.

Life insurance contract liabilities are usually determined using a projection method, whereby estimates of policy cash flows (premiums, payments and expenses) are projected into the future. The liability is calculated as the net present value of these projected cash flows using a risk-free discount rate curve.

The key areas of judgement in the determination of the actuarial assumptions are the duration of claims/policy payments, mortality, surrenders, acquisition and maintenance expense levels, and economic assumptions for discount and inflation rates.

Life insurance premium revenue

Life insurance premiums are recognised as revenue when risk is transferred to the Group.

Life insurance claims expense

Life insurance claims expense is recognised in expenses when the liability to the policyholder under the contract has been established.

Inwards reinsurance

The Group has maintained inwards reinsurance arrangements during the period that meet the definition of a life insurance contract. The MoS methodology requires the present value of future cash flows arising from reinsurance contracts to be included in the calculation of life insurance contract liabilities.

Valuation

The MoS valuation, calculated in accordance with APRA Prudential Standards and AASB 1038 ***Life Insurance Contracts*** results in the systematic release of planned margins over the life of the policy via a 'profit carrier'. The Group maintains life insurance contracts, including individual lifetime annuities, wholesale mortality, wholesale morbidity, longevity reinsurance and wholesale lifetime annuities. Annuity payments are used as the profit carrier for lifetime annuities and premium receipts, or best estimate claim payments are used as the profit carrier for wholesale mortality, wholesale morbidity and longevity reinsurance.

Key assumptions applied in the valuation of life contract liabilities

Tax rates

The bases of taxation (including deductibility of expenses) are assumed to continue in accordance with legislation current at the reporting date.

Discount rates

Under APRA Prudential Standards and AASB 1038 ***Life Insurance Contracts***, life insurance contract liabilities are calculated by discounting expected future cash flows at a risk-free rate, set at the Commonwealth Government Bond curve plus an illiquidity premium where applicable or for foreign-denominated liabilities, a curve derived from the yields of highly liquid AAA-rated sovereign risk securities in the currency of the policy liabilities plus an illiquidity premium where applicable. The illiquidity premium is determined by reference to observable market rates including Australian sovereign debt, corporate, securitised and collateralised debt publicly placed in the domestic market, and market swap rates.

Life investment contract liabilities are calculated under the fair value through profit and loss provisions of AASB 9 ***Financial Instruments***. The discount rates are determined based on the current observable, objective rates that relate to the nature, structure and term of the future liability cash flows.

For both insurance and investment contracts the approach is the same as adopted at 2020. Discount rates applied for Australian liabilities were between 0.3% - 2.8% per annum (30 June 2020: 0.9% - 2.4%).

Note 8 Life contract liabilities (continued)

Valuation (continued)

Key assumptions applied in the valuation of life contract liabilities (continued)

Expenses

Forecasted expenses for the next year are allocated between acquisition, maintenance and investment based on the nature of the expense. Forecasted maintenance expenses then are converted to a per-contract unit cost or percentage of account balance, depending on the nature of the expense.

Inflation

Inflation estimates are based on long-term expectations and reviewed at least annually for changes in the market environment based on a comparison of real and nominal yields of instruments of equivalent term and credit risk. The current assumption for Australia is 2.0% per annum for short-term inflation and 2.3% per annum for long-term inflation (30 June 2020: -0.2% short-term, 1.8% long-term).

Surrenders

For life investment contracts, no surrenders or voluntary discontinuances are assumed. For Australian life insurance contracts where a surrender value is payable on withdrawal, a rate of surrenders is assumed in line with Challenger's own experience on these products, currently between 0.0% - 2.1% per annum (30 June 2020: 0.0% - 2.1%). For inwards reinsurance of Japanese business a rate of surrenders is assumed in line with local experience in relation to similar contracts, currently 3.5% per annum (30 June 2020: 3.5%). Where policyholders have the option to commute a life insurance contract, the value of this option is included within the life contract liabilities. We also assume surrender rates based on past experience for this business which vary by product types and duration in-force for the contract.

Mortality

Base mortality rates for individual lifetime annuities are determined as a multiple of annuitant experience based on LML08 and LFL08 tables, adjusted for Challenger's own recent experience. LML08 and LFL08 are mortality tables developed by the Continuous Mortality Investigation (CMI) based on United Kingdom annuitant lives experience from 2007–2010. The tables refer to male and female lives respectively. Rates are adjusted for expected future mortality improvements based on observed and expected improvements. For the age ranges and cash flow projection periods that contribute the majority of CLC's exposure, rates of future mortality improvement applied are between 0.3% - 2.5% per annum (30 June 2020: 0.3% - 2.5%).

Base mortality rates for wholesale mortality and longevity reinsurance are determined as a multiple of pensioner mortality rates (based on the self-administered pension schemes or SAPS3 tables mortality investigation developed by the Institute and Faculty of Actuaries (UK) using United Kingdom data collected between 2009–2016). Rates are adjusted for expected future mortality improvements based on observed and expected improvements.

For the age ranges and cash flow projection periods that contribute the majority of CLC's exposure, rates of future mortality improvement applied are between 0.2% - 2.3% per annum (30 June 2020: 0.6% - 2.1%). Base mortality rates for the inwards reinsurance of Japanese business are determined as a multiple of Japanese population mortality rates.

Mortality assumptions have been reviewed but not adjusted in light of the COVID-19 pandemic.

Impact of changes in assumptions on life insurance contracts

Under MoS, changes in actuarial assumptions are recognised by adjusting the value of future profit margins in life insurance contract liabilities. Changes in future profit margins are released over future periods unless that product group is in an expected net loss position (loss recognition), in which case changes in assumptions are recognised in the Statement of comprehensive income in the period in which they occur. The valuation impact of changes to discount rate assumptions as a result of market and economic conditions, such as changes in benchmark market yields, are recognised in the Statement of comprehensive income in the period in which the changes occur.

Restrictions on assets

Financial assets held in the Group can only be used within the restrictions imposed under the ***Life Insurance Act 1995*** (the Life Act). The main restrictions are that the assets in a statutory fund can only be used to meet the liabilities and expenses of that statutory fund, to acquire investments to further the business of the statutory fund or as distributions when capital adequacy requirements are met.

Statutory fund information

The life contract operations of CLC are conducted within four separate statutory funds. Both the shareholders' and policyholders' interests in these statutory funds are reported in aggregate in the financial report of the Group. Fund 1 is a non-investment-linked fund and Fund 3 is investment-linked. Both of these are closed to new business. Funds 2 and 4 are the principal operating funds of the Group. Fund 2 contains non-investment-linked contracts, including the Group's term annuity business, lifetime annuity policies and the related outwards reinsurance, plus the wholesale mortality, wholesale morbidity and longevity inwards reinsurance. Fund 4 contains inwards reinsurance of annuity business written in Japan.

Life contract liabilities for Statutory Funds 1, 2, 3 and 4 are:

Life contract liabilities	30 June 2021 $m	30 June 2020 $m
Statutory Fund 1	1.5	1.5
Statutory Fund 2	11,582.4	10,854.4
Statutory Fund 3	3.0	2.6
Statutory Fund 4	2,083.0	1,722.7
Total life contract liabilities	**13,669.9**	**12,581.2**

Note 8 Life contract liabilities (continued)

Current/non-current split for total life contracts

There is a fixed settlement date for the majority of life contract liabilities. Approximately $3,099.3 million on a discounted basis (30 June 2020: $2,596.5 million) of life contract liabilities have a contractual maturity within 12 months of the reporting date. Based on assumptions applied for the 30 June 2021 valuation of life contract liabilities, $3,685.7 million of principal payments on fixed term and lifetime business are expected in the year to 30 June 2022 (expected in the year to 30 June 2021: $3,327.7 million).

Life insurance risk

The Group is exposed to longevity risk on its individual lifetime annuities (both direct and reinsured) and wholesale longevity reinsurance. Longevity risk is the risk that policyholders may live longer than expectations. The Group is exposed to mortality risk on the wholesale mortality reinsurance and reinsurance of fixed term business written in Japan. This is the risk that death rates in the reference portfolios exceed expectations. The Group is also exposed to morbidity risk on the wholesale morbidity reinsurance. That is the risk that morbidity rates in the reference portfolios exceed expectation.

The Group manages the longevity risk by regular reviews of the portfolio to confirm continued survivorship of policyholders receiving income plus regular review of longevity experience to ensure that longevity assumptions remain appropriate.

In addition, the Group maintains a reinsurance arrangement to manage longevity risk in respect of part of the closed book of individual lifetime annuities.

The Group manages the mortality and morbidity risk by regular reviews of the portfolio to ensure that mortality and morbidity assumptions remain appropriate. The Company's insurance risk policy is approved by the Board and sets out the relevant risk limits for insurance exposures, to ensure the insurance risk portfolio is appropriately diversified and contains no significant concentrations of insurance risk.

Insurance risk sensitivity analysis

The following table discloses the sensitivity of life insurance contract liabilities, profit after income tax and equity to changes in the key assumptions relating to insurance risk, both gross and net of reinsurance:

	Increase in life insurance contract liabilities				Loss after tax and equity impact			
	Gross		Net		Gross		Net	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020	30 June 2021	30 June 2020	30 June 2021	30 June 2020
Insurance risk sensitivity analysis	$m	$m	$m	$m	$m	$m	$m	$m
50% increase in the rate of mortality improvement	43.3	35.4	42.7	34.8	(30.3)	(24.8)	(29.9)	(24.4)
10% increase in maintenance expenses	18.3	16.3	18.3	16.3	(12.8)	(11.4)	(12.8)	(11.4)

Liquidity risk for insurance contracts

The following table summarises the undiscounted maturity profile of the Group's life insurance contract liabilities. The analysis is based on undiscounted estimated cash outflows, including interest and principal payments. The undiscounted maturity profile of life investment contracts is disclosed in Note 18 Financial risk management.

Undiscounted life insurance contract liabilities	1 year or less $m	1-3 years $m	3-5 years $m	>5 years $m	Total $m
2021	**863.9**	**1,465.8**	**1,158.7**	**4,817.7**	**8,306.1**
2020	775.4	1,272.1	1,014.4	4,574.9	7,636.8

Actuarial information

Mr A Kapel FIAA, as the Appointed Actuary of CLC, is satisfied as to the accuracy of the data used in the valuations of life contract liabilities in the financial report and the tables in this note.

The life contract liabilities have been determined at the reporting date in accordance with the Life Act, APRA Prudential Standards, AASB 1038 ***Life Insurance Contracts***, and AASB 9 ***Financial Instruments***.

Note 9 External unit holders' liabilities

	30 June 2021 $m	30 June 2020 $m
Current	3,090.1	1,587.3
Non-current	542.1	828.5
Total liabilities to external unit holders	**3,632.2**	**2,415.8**

Accounting policy

The Group controls a number of guaranteed index return trusts that contain contributed funds in respect of fixed term wholesale mandates. The fixed term and guaranteed nature of the mandates effectively places the balance of the risks related to the performance of the trusts with the Group. As a result, the Group is deemed to control these trusts. The contributed funds for these trusts are classed as external unit holders' liabilities on the Statement of financial position and represent the funds owing to third parties on these mandates. The liability is recognised at fair value.

Note 10 Derivative financial instruments

	30 June 2021			30 June 2020		
Analysis of derivative financial instruments	**Notional value $m**	**Net fair value assets $m**	**Net fair value liabilities $m**	**Notional value $m**	**Net fair value assets $m**	**Net fair value liabilities $m**
Non-SPV						
Interest rate swaps						
Less than one year	5,086.2	8.8	(2.7)	7,511.9	7.1	(5.2)
One to three years	9,083.3	47.0	(47.4)	8,962.4	34.7	(38.3)
Three to five years	11,294.6	80.6	(79.6)	8,739.3	100.7	(72.0)
Greater than five years	42,527.3	315.1	(437.9)	37,974.2	539.0	(693.0)
Total interest rate swaps	**67,991.4**	**451.5**	**(567.6)**	**63,187.8**	**681.5**	**(808.5)**
Collateral securities[1]	**—**	**—**	**216.7**	**—**	**—**	**259.0**
Inflation-linked swaps						
Less than one year	300.0	—	(2.3)	211.0	7.6	(1.4)
One to three years	243.0	2.5	—	243.0	10.1	—
Three to five years	387.0	10.0	(4.6)	72.0	3.0	(7.8)
Greater than five years	1,092.0	60.3	(28.0)	1,407.0	164.0	(43.0)
Total inflation-linked swaps	**2,022.0**	**72.8**	**(34.9)**	**1,933.0**	**184.7**	**(52.2)**
Futures contracts						
Less than one year	16,168.8	—	(1.0)	18,101.9	—	(0.6)
Total futures contracts	**16,168.8**	**—**	**(1.0)**	**18,101.9**	**—**	**(0.6)**
Forward currency contracts						
Less than one year	2,850.1	32.0	(22.5)	2,947.5	63.2	(46.9)
Total forward currency contracts	**2,850.1**	**32.0**	**(22.5)**	**2,947.5**	**63.2**	**(46.9)**
Cross-currency swaps						
Less than one year	1,397.7	17.8	(17.9)	1,268.7	29.2	(44.0)
One to three years	3,187.4	29.9	(40.5)	2,332.3	69.8	(15.3)
Three to five years	2,482.5	11.6	(29.2)	1,332.1	36.6	(10.5)
Greater than five years	765.0	7.5	(9.8)	825.4	25.3	(5.5)
Total cross-currency swaps	**7,832.6**	**66.8**	**(97.4)**	**5,758.5**	**160.9**	**(75.3)**
Equity swaps						
Less than one year	1,475.0	16.4	—	596.6	20.0	—
One to three years	308.9	2.1	(0.4)	—	—	—
Total equity swaps	**1,783.9**	**18.5**	**(0.4)**	**596.6**	**20.0**	**—**

Note 10 Derivative financial instruments (continued)

Analysis of derivative financial instruments (continued)	30 June 2021 Notional value $m	30 June 2021 Net fair value assets $m	30 June 2021 Net fair value liabilities $m	30 June 2020 Notional value $m	30 June 2020 Net fair value assets $m	30 June 2020 Net fair value liabilities $m
Credit default swaps						
Less than one year	63.4	0.3	—	—	—	—
One to three years	—	—	—	67.9	1.2	(0.6)
Three to five years	1,218.8	96.4	—	—	—	—
Total credit default swaps	**1,282.2**	**96.7**	**—**	**67.9**	**1.2**	**(0.6)**
Options						
Less than one year	—	—	—	2.5	0.6	—
Total options	**—**	**—**	**—**	**2.5**	**0.6**	**—**
Total non-SPV	**99,931.0**	**738.3**	**(507.1)**	**92,595.7**	**1,112.1**	**(725.1)**
SPV						
Interest rate swaps – SPV						
Less than one year	7.2	—	(0.1)	5.1	—	(0.1)
One to three years	0.7	—	—	7.6	—	(0.1)
Three to five years	0.6	—	—	0.5	—	—
Total interest rate swaps – SPV	**8.5**	**—**	**(0.1)**	**13.2**	**—**	**(0.2)**
Cross-currency swaps – SPV						
Greater than five years	212.1	—	(0.4)	261.0	0.4	(0.1)
Total cross-currency swaps – SPV	**212.1**	**—**	**(0.4)**	**261.0**	**0.4**	**(0.1)**
Total – SPV	**220.6**	**—**	**(0.5)**	**274.2**	**0.4**	**(0.3)**
Total derivative financial instruments[2]	**100,151.6**	**738.3**	**(507.6)**	**92,869.9**	**1,112.5**	**(725.4)**

1 Collateral securities relates to centrally cleared interest rate swaps.
2 The Group's derivative financial instruments are subject to enforceable netting arrangements under International Swaps and Derivatives Association (ISDA) Master Agreements with derivative counterparties, allowing for net settlement as a single arrangement of multiple instruments with a counterparty in the event of default or other specified circumstances. If applied to the derivative portfolio, the derivative assets would decrease by 284.9 million (30 June 2020: $474.1 million) and the derivative liabilities would decrease by $284.9 million (30 June 2020: $474.1 million).

Accounting policy

The Group uses derivative financial instruments predominantly to hedge its risks associated with interest rate and foreign currency fluctuations and to gain exposure to different markets. All derivative financial instruments are stated at fair value. Gains or losses arising from fair value changes on derivatives that do not qualify for hedge accounting are recognised in the Statement of comprehensive income. For the purpose of hedge accounting, hedges are classified as:

- cash flow hedges when they hedge the exposure to variability in cash flows that is attributable either to a particular risk associated with a recognised asset or liability or to a forecast transaction; or
- hedges of net investments in foreign operations when they hedge the exposure to changes in the value of the assets and liabilities of foreign-controlled entities when they are translated from their functional currency to the presentation currency.

At the inception of a hedge relationship to which the Group wishes to apply hedge accounting, the Group formally designates and documents the hedge relationship and the risk management objectives and strategies for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of the instrument in offsetting the exposure to changes in the hedged item.

Such hedges are expected to be highly effective in achieving offsetting changes in fair values, cash flows or foreign exchange differences and are assessed on an ongoing basis to determine that they actually have been effective over the period that they were designated.

Cash flow hedges

Cash flow hedges are hedges of the Group's exposure to variability in cash flows attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecast transaction, that could affect the Statement of comprehensive income. The effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised in the Statement of comprehensive income.

Amounts recognised in equity are transferred to the Statement of comprehensive income when the hedged transaction affects profit or loss, such as when hedged income or expenses are recognised or when a forecast sale or purchase occurs. When the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

Note 10 Derivative financial instruments (continued)

Accounting policy (continued)

Cash flow hedges (continued)

If the forecast transaction is no longer expected to occur, amounts previously recognised in equity are transferred to the Statement of comprehensive income.

If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction occurs.

Hedges of net investments in foreign operations

The gain or loss on the effective portion of the hedging instrument is recognised directly in equity and the gain or loss on the ineffective portion is recognised immediately in the Statement of comprehensive income. The cumulative gain or loss previously recognised in equity is recognised in the Statement of comprehensive income on disposal or partial disposal of the foreign operation.

Derivatives designated as hedges of net investment in foreign currency operations

The Group hedges its exposure to accounting gains and losses arising from translation of foreign-controlled entities from their functional currency into the Group's presentation currency on consolidation. At 30 June 2021, a post-tax gain of $46.8 million (30 June 2020: post-tax gain of $0.5 million) was recognised in Other comprehensive income (OCI) for the hedging of exposure to the net investment in foreign currency operations.

Derivatives designated as cash flow hedges

The Group applies hedge accounting when it can demonstrate that all, or a portion of, the value movements of a derivative financial instrument effectively hedges the variability in cash flows attributable to a specific risk associated with a recognised asset or liability or probable future transaction. As described in Note 18 Financial risk management, SPVs enter into interest rate swap agreements to hedge the interest rate risk between variable rate loans, which generally reprice with changes in official interest rates, and issued RMBS that reprice with changes in the 30-day and 90-day bank bill swap rates. Cross-currency swaps are also used to hedge currency movements on foreign denominated RMBS. The SPVs apply hedge accounting to both types of transactions, with the fair value change on the effective portion of the derivative being recognised in OCI.

For the year ended 30 June 2021, a post-tax loss of $0.5 million (30 June 2020: post-tax result of nil) was recognised in OCI for cash flow hedges with no Statement of comprehensive income impact in relation to any ineffective portions during either the current or prior comparative period.

Note 11 Notes to Statement of cash flows

Reconciliation of profit to operating cash flow	30 June 2021 $m	30 June 2020 $m
Profit/(loss) for the year	**592.3**	**(421.1)**
Adjusted for		
Net realised and unrealised losses/(gains) on investment assets	(582.3)	866.6
Share of associates' net profit	(35.2)	(29.3)
Change in life contract liabilities[1]	73.7	295.1
Depreciation and amortisation expense	15.3	15.3
Impairment in intangible assets, associates and other investments	12.3	12.8
Share-based payments	11.5	14.2
Dividends from associates	33.7	22.4
Change in operating assets and liabilities		
Decrease in receivables	72.1	7.9
Decrease/(increase) in other assets	1.7	(9.2)
Increase in payables	2.0	27.0
Increase in provisions	0.2	16.3
Increase/(decrease) in life contract liabilities	1,015.0	(584.1)
Increase in external unit holders' liabilities	1,216.4	449.6
Increase/(decrease) in net tax liabilities	147.9	(198.6)
Net cash flows from operating activities	**2,576.6**	**484.9**

1 Changes relate to movements through the Statement of comprehensive income.

Reconciliation of cash	30 June 2021 $m	30 June 2020 $m
Cash at bank and on hand	928.6	603.9
Cash at bank and on hand – SPV	60.8	58.0
Total cash and cash equivalents[1]	**989.4**	**661.9**

1 All cash and cash equivalents are considered current.

Accounting policy

Cash and cash equivalents are financial assets and comprise cash at bank and on hand plus short-term deposits with an original maturity of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Cash and cash equivalents are recognised and carried at fair value. For the purposes of the Statement of cash flows, cash and cash equivalents are stated net of bank overdrafts.

Section 4: Capital structure and financing costs

This section outlines how the Group manages its capital structure and related financing costs, as well as capital adequacy and reserves. It also provides details on the dividends and earnings per share of the Company.

Note 12 Contributed equity

	30 June 2021		30 June 2020	
	No. of shares m	Value of shares $m	No. of shares m	Value of shares $m
Analysis of contributed equity				
Ordinary shares issued and fully paid	676.0	2,462.4	667.5	2,424.7
CPP Trust shares treated as Treasury shares	(1.4)	(14.6)	(2.4)	(24.8)
CPP deferred share purchases treated as Treasury shares	(2.0)	(22.3)	(2.0)	(22.3)
Total contributed equity	**672.6**	**2,425.5**	**663.1**	**2,377.6**
Movements in contributed equity				
Ordinary shares				
Balance at the beginning of the year	667.5	2,424.7	611.6	2,155.3
Equity placement	8.1	34.8	55.2	264.1
Issued under dividend reinvestment plan	0.4	2.9	0.7	5.3
Balance at the end of the year	**676.0**	**2,462.4**	**667.5**	**2,424.7**
CPP Trust				
Balance at the beginning of the year	2.4	24.8	3.0	30.5
Shares purchased (including settled forwards)	—	—	0.8	8.8
Vested shares released to employees	(1.0)	(10.2)	(1.4)	(14.5)
Balance at the end of the year	**1.4**	**14.6**	**2.4**	**24.8**
CPP deferred share purchases				
Balance at the beginning of the year	2.0	22.3	2.8	31.1
Settled forward purchases	—	—	(0.8)	(8.8)
Balance at the end of the year	**2.0**	**22.3**	**2.0**	**22.3**

Accounting policy

Ordinary shares are classified as equity and have no par value. Issued capital in respect of ordinary shares is recognised as the fair value of the consideration received by the parent entity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Treasury shares are ordinary shares in the Company held by the Challenger Performance Plan (CPP) Trust or under CPP deferred share purchase agreements in respect of equity incentive plan awards to employees. Refer to Note 28 Employee entitlements for further details.

Terms and conditions of contributed equity

Ordinary shares

A holder of an ordinary share is entitled to receive dividends and to one vote on a show of hands and on a poll.

Challenger Performance Plan (CPP) Trust

The CPP Trust is a controlled entity and holds shares in the Company. As a result, the CPP Trust's shareholding in the Company is disclosed as Treasury shares and deducted from equity. Dividends paid from the Company to the CPP Trust are eliminated on consolidation.

CPP deferred share purchases

The shares purchased under forward agreements are treated as Treasury shares from the date of the agreement. Shares are transferred to the CPP Trust on the future settlement date.

Note 12 Contributed equity (continued)

Capital management

A company is generally limited in the risk-taking activities that it can engage in by the amount of capital it holds, with capital acting as a buffer against risk, ensuring that there are sufficient resources to enable the company to continue normal business in the event of an unexpected loss.

The prudentially-regulated Challenger Life Company Limited (CLC) manages capital via an Internal Capital Adequacy Assessment Process (ICAAP). Under the prudential standards, a life company must have in place an ICAAP, documented in an ICAAP Summary Statement. CLC complied with these requirements at all times during the year.

The objective of the ICAAP is to ensure that CLC maintains adequate capital in respect of the risks to which it is exposed so that it can fulfil its obligations to policy owners (in particular the duty to give priority to the interests of owners and prospective owners of policies referable to a fund). The ICAAP also enables CLC to invest both strategically and tactically in opportunities that deliver a return on equity above the cost of capital for shareholders.

There were no material changes to the Group's capital management process during the period. All of the Group regulated entities have at all times during the current and prior financial year complied with the externally imposed capital requirements to which they are subject.

Share Purchase Plan (SPP)

During the period, the Company conducted a non-underwritten share purchase plan (SPP) raising $35.0 million with 8.1 million shares issued to retail shareholders at a price of $4.32 per share. Total issue costs (net of tax) were $0.2 million, resulting in net proceeds of $34.8 million. Of the proceeds from the SPP, $30.0 million was injected into CLC as Common Equity Tier 1 capital.

Credit ratings

Standard & Poor's long-term credit ratings for the Company and CLC at the Statement of financial position date are 'BBB+' (stable) and 'A' (stable) respectively (30 June 2020: 'BBB+' (stable) and 'A' (stable) respectively). There were no changes to either the Company's or CLC's ratings during the period.

Dividends

The Group has historically targeted a dividend payout ratio of between 45% - 50% of normalised profit after tax over the medium term, subject to prevailing market conditions and alternate uses of capital.

The dividend payout ratio for the year ended 30 June 2021 was 48.2% of normalised profit after tax (30 June 2020: 31.0%). The increase is due to the resumption of dividends in 2021, following the Board's decision not to declare and pay a final dividend for the year ended 30 June 2020 given the significant investment experience losses incurred in the second half and in order to continue to protect the Group's strong capital position given the uncertainty caused by COVID-19.

Dividend Reinvestment Plan (DRP)

As a result of the uncertain economic conditions caused by COVID-19, and to maintain a strong capital position of the Life business, no final dividend was declared for 2020. With no final dividend having been paid, the DRP was not in operation in respect of the final 2020 dividend.

The Group resumed the DRP for the interim 2021 dividend, and on 23 March 2021 issued 441,762 ordinary shares to satisfy the plan. The DRP issue price per share for the interim 2021 dividend was $6.5302 and represented the volume weighted average share price over the 10 trading days from 26 February 2021 to 11 March 2021. The interim DRP participation rate was 4.5% of all issued shares, resulting in proceeds of $2.9 million.

Note 12 Contributed equity (continued)

Capital management (continued)

Prescribed capital amount (PCA)

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 its customers. CLC is regulated by APRA and is required to hold a minimum level of regulatory capital. CLC's regulatory capital base and PCA have been calculated based on the prudential standards issued by APRA. CLC's internal capital models result in a target PCA ratio range under current circumstances of 1.3 to 1.7 times. This range can change over time and is dependent on numerous factors. The PCA ratio at 30 June 2021 was 1.63 times (30 June 2020: 1.81 times), within this range of 1.3 to 1.7 times. The CET1 ratio was 1.14 times at 30 June 2021 down from 1.20 times at 30 June 2020.

CLC's target surplus

CLC maintains a target level of capital representing APRA's PCA plus a target surplus. The target surplus is a management guide to the level of excess capital that CLC seeks to hold over and above APRA's minimum requirements. CLC's target surplus is set to ensure that it provides a buffer against adverse market conditions and having regard to CLC's credit rating. 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.

Details of the CLC capital adequacy multiple are below:

CLC capital	30 June 2021 $m	30 June 2020 $m
CLC's excess capital under prudential standards		
Common Equity Tier 1 regulatory capital	2,971.2	2,337.0
Additional Tier 1 regulatory capital	872.7	805.0
Tier 2 regulatory capital – subordinated debt[1]	405.4	396.7
CLC total regulatory capital base	**4,249.3**	**3,538.7**
CLC's prescribed capital amount		
Asset risk charge[2]	2,481.8	1,842.8
Insurance risk charge	227.0	199.5
Operational risk charge	57.9	56.5
Aggregation benefit	(167.4)	(144.8)
CLC prescribed capital amount	**2,599.3**	**1,954.0**
CLC excess over prescribed capital amount	**1,650.0**	**1,584.7**
Capital adequacy ratio (times)	**1.63**	**1.81**
Common Equity Tier 1 ratio (times)	**1.14**	**1.20**

[1] Differs from $404.5 million (30 June 2020: $395.7 million) disclosed in Note 13 Interest bearing financial liabilities due to $0.9 million (30 June 2020: $1.0 million) of accrued interest.

[2] Asset risk charge includes the combined stress scenario adjustment and default stress.

Note 13 Interest bearing financial liabilities

	30 June 2020		Cash flows	Non-cash movements			30 June 2021	
	Facility $m	Opening balance $m	proceeds/ (repayments) $m	Foreign exchange $m	Fair value changes $m	Other $m	Closing balance $m	Facility $m
Bank loans								
Corporate[1]	400.0	50.0	(50.0)	—	—	—	—	400.0
Controlled property trusts[2,4]	453.8	453.8	(17.5)	(45.9)	0.5	1.4	392.3	394.9
Controlled infrastructure trusts[4]	185.8	185.8	(6.5)	—	—	—	179.3	179.3
Repurchase agreements	5,393.4	5,393.4	(1,282.3)	—	—	—	4,111.1	4,111.1
Total bank loans	**6,433.0**	**6,083.0**	**(1,356.3)**	**(45.9)**	**0.5**	**1.4**	**4,682.7**	**5,085.3**
Non-bank loans								
Subordinated debt	400.0	395.7	—	—	8.8	—	404.5	400.0
Challenger Capital Notes 1[4]	345.0	345.0	(317.3)	—	—	—	27.7	27.7
Challenger Capital Notes 2[4]	460.0	454.5	—	—	—	1.8	456.3	460.0
Challenger Capital Notes 3[4]	—	—	385.0	—	—	(6.0)	379.0	385.0
Total non-bank loans	**1,205.0**	**1,195.2**	**67.7**	**—**	**8.8**	**(4.2)**	**1,267.5**	**1,272.7**
Total interest bearing financial liabilities	**7,638.0**	**7,278.2**	**(1,288.6)[3]**	**(45.9)**	**9.3**	**(2.8)**	**5,950.2**	**6,358.0**
Current		5,468.9					4,310.0	
Non-current		1,809.3					1,640.2	
		7,278.2					**5,950.2**	

1 In March 2020, the Group elected to fully draw its $400.0 million banking facility in order to provide additional financial flexibility during the COVID-19 crisis. $350.0 million of this drawing was repaid in June 2020. The remaining $50.0 million was repaid during the year ending 30 June 2021.
2 Total facility limit consists of non-redraw loan facilities limits totalling $394.9 million (30 June 2020: $453.8 million).
3 Differs to Statement of cash flows due to $121.1 million (30 June 2020: $134.8 million) repayments relating to SPV. Net cash proceeds comprise $385.0 million (30 June 2020: $1,344.9 million) proceeds from borrowings and $1,673.6 million (30 June 2020: $521.2 million) repayments of borrowings.
4 Held at amortised cost except for the controlled property trust loan in respect of County Court. The fair value of these are: Challenger Capital Notes 1 $27.8 million (30 June 2020: $340.9 million), Challenger Capital Notes 2 $480.8 million (30 June 2020: $457.7 million), and Challenger Capital Notes 3 $407.9 million (30 June 2020: nil); controlled property trusts $396.3 million (30 June 2020: $474.9 million); controlled infrastructure trusts $182.3 million (30 June 2020: $189.8 million).

	30 June 2019		Cash flows	Non-cash movements			30 June 2020	
	Facility $m	Opening balance $m	proceeds/ (repayments) $m	Foreign exchange $m	Fair value changes $m	Other $m	Closing balance $m	Facility $m
Bank loans								
Corporate[1]	400.0	—	50.0	—	—	—	50.0	400.0
Controlled property trusts[2,4]	459.8	459.8	(17.7)	6.8	2.2	2.7	453.8	453.8
Controlled infrastructure trusts[4]	192.0	192.0	(6.2)	—	—	—	185.8	185.8
Repurchase agreements	4,448.5	4,448.5	944.9	—	—	—	5,393.4	5,393.4
Total bank loans	**5,500.3**	**5,100.3**	**971.0**	**6.8**	**2.2**	**2.7**	**6,083.0**	**6,433.0**
Non-bank loans								
Subordinated debt	400.0	403.8	—	—	(8.1)	—	395.7	400.0
Challenger Capital Notes 1[4]	345.0	343.6	—	—	—	1.4	345.0	345.0
Challenger Capital Notes 2[4]	460.0	452.7	—	—	—	1.8	454.5	460.0
Other finance	12.7	12.7	(12.5)	—	(0.2)	—	—	—
Total non-bank loans	**1,217.7**	**1,212.8**	**(12.5)**	**—**	**(8.3)**	**3.2**	**1,195.2**	**1,205.0**
Total interest bearing financial liabilities	**6,718.0**	**6,313.1**	**958.5[3]**	**6.8**	**(6.1)**	**5.9**	**7,278.2**	**7,638.0**
Current		4,473.2					5,468.9	
Non-current		1,839.9					1,809.3	
		6,313.1					**7,278.2**	

1 In March 2020, the Group elected to fully draw its $400.0 million banking facility in order to provide additional financial flexibility during the COVID-19 crisis. $350.0 million of this drawing was repaid in June 2020.
2 Total facility limit consists of non-redraw loan facilities limits totalling $453.8 million (30 June 2019: $459.8 million).
3 Differs to Statement of cash flows due to $134.8 million (30 June 2019: $189.0 million) repayments relating to SPV. Net cash proceeds comprise $1,344.9 million (30 June 2019: $632.8 million) proceeds from borrowings and $521.2 million (30 June 2019: $315.4 million) repayments of borrowings.
4 Held at amortised cost except for the controlled property trust loan in respect of County Court. The fair value of these are: Challenger Capital Notes 1 and 2 $340.9 million and $457.7 million (30 June 2019: $350.3 million and $485.7 million) respectively; controlled property trusts $474.9 million (30 June 2019: $458.0 million); controlled infrastructure trusts $189.8 million (30 June 2019: $192.5 million).

Note 13 Interest bearing financial liabilities (continued)

Accounting policy

All borrowings and subordinated debt are financial liabilities and are initially recognised at fair value. For borrowings and subordinated debt that are subsequently measured at fair value through profit or loss, directly attributable transaction costs are expensed with movements on fair value recognised in the Statement of comprehensive income.

Borrowings and subordinated debt, other than those held by CLC's statutory funds or their controlled entities, are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the Statement of comprehensive income over the period of the contract using the effective interest rate method.

Repurchase agreements are all short-term in nature, and are therefore valued at amortised cost which approximates fair value.

Details of liabilities

Bank loans

Bank loans	Type	Maturity	Rate type	Ranking/security
Corporate	Facility	Tranche 1: $150m expiring on 30 June 2022 Tranche 2: $250m expiring on 30 June 2024	Floating	Security by guarantees between members of the Group
Controlled property trusts[1]	Loan	June 2022 to October 2024	Variable	First ranking mortgages over Japanese investment properties: $378.5 million (30 June 2020: $426.6 million) First ranking mortgage over County Court, VIC: $13.7 million (30 June 2020: $27.0 million)
Controlled infrastructure trusts[2]	Facility	June 2022	Variable	First ranking mortgages over infrastructure assets

1 Controlled properties trusts consists of multiple loans with maturity dates from June 2022 to October 2024. At 30 June 2021 $378.5 million (30 June 2020: $426.6 million) of these loans are held at amortised cost. The fair value of these liabilities at 30 June 2021 was $396.3 million (30 June 2020: $474.9 million).

2 These loans are held at amortised cost. The fair value of these liabilities at 30 June 2021 was $182.3 million (30 June 2020: $189.8 million).

Repurchase agreements

CLC has entered into repurchase agreements with certain counterparties whereby fixed income securities are sold for cash while simultaneously agreeing to repurchase the fixed income security at a fixed price and fixed date in the future. These agreements finance bonds held for hedging purposes and are interest bearing, with interest factored into the price at which the bonds are repurchased and paid on repurchase. All agreements as at 30 June 2021 are current and all mature by August 2021. They will continue to be rolled into new agreements in the future.

CLC uses Australian Government and Semi-Government Bonds with repurchase agreements, interest rate swaps and bond futures to hedge movements in interest rates on its asset portfolio, annuity policy liabilities, Guaranteed Index Return mandates and the Challenger Index Plus Fund.

Non-bank loans

Subordinated debt

CLC issued subordinated notes of $400.0 million on 24 November 2017 with a call date on 24 November 2022. Holders of the subordinated notes have the option to convert their holding into ordinary shares of Challenger Limited on 24 November 2024 if CLC has not exercised its call option on 24 November 2022. If holders do not elect to convert the subordinated notes to ordinary shares of Challenger Limited, the subordinated notes will be fully eligible as Tier 2 regulatory capital of CLC until 24 November 2038.

Challenger Capital Notes – 1, 2 and 3 (Notes 1, Notes 2 and Notes 3)

On 25 November 2020, the Company completed its third capital notes issue, Challenger Capital Notes 3 (Notes 3), raising $385 million of new debt funding in order to replace its 2014 capital notes issue (Notes 1).

Under the reinvestment offer, $237.5 million of Notes 1 holders elected to reinvest into the new Notes 3, and under the repurchase invitation, $60 million of Notes 1 were repurchased by the Company. Following the completion of the issue, $47.5 million of Notes 1 remained on issue. On 27 April 2021, the Group offered eligible holders of the residual Notes 1 the option to have their holding repurchased by Challenger at a price of $102.0 per unit (face value $100.0 per unit). Repurchase applications were received for $19.7 million leaving $27.7 million of Note 1 holdings outstanding. These outstanding notes will mandatorily convert to ordinary Challenger shares on or before May 2022. In the interim, these Note 1 holdings will continue to receive quarterly distribution payments up until their conversion.

Note 13 Interest bearing financial liabilities (continued)

Details of liabilities

Challenger Capital Notes – 1, 2 and 3 (Notes 1, Notes 2 and Notes 3) (continued)

Notes 3 have similar structural characteristics to Challenger Capital Notes 1 and 2, including:

- quarterly, floating, discretionary, non-cumulative distributions based on a margin over 3 month BBSW;
- optional exchange whereby notes may be redeemed or resold for cash or converted to ordinary shares in the Company, at the Company's option, on the relevant Optional Exchange Date (or on an earlier date in certain circumstances), subject to APRA's prior written approval; and
- mandatory conversion to ordinary shares in the Company on the relevant Mandatory Conversion Date, subject to certain conditions being satisfied. If the conditions to mandatory conversion are not met on the relevant Mandatory Conversion Date, conversion will be deferred to a later date when the conditions are retested.

Like Notes 1 and 2, the costs associated with the issue of Notes 3 have been capitalised against the relevant liability and will be expensed to the Statement of comprehensive income over the life of Notes 3. The Notes 3 issue does not constitute regulatory capital of the Company. The proceeds from the issue of Notes 3 were used to fund a subscription for notes issued by CLC. The issue of notes by CLC was approved by APRA and constitutes Additional Tier 1 capital of CLC.

	Notes 1	Notes 2	Notes 3
Issue date	9 October 2014	7 April 2017	25 November 2020
Issue amount	$345.0 million	$460.0 million	$385.0 million
Outstanding amount	$27.7 million	$460.0 million	$385.0 million
Optional Exchange Date	25 May 2020	22 May 2023	22 May 2026
Mandatory Conversion	25 May 2022	22 May 2025	22 May 2028

Key estimates and assumptions

Subordinated debt valuation

Subordinated debt is recognised at fair value and is valued by reference to the ask price observable in the market at balance date.

The change recognised in the Statement of comprehensive income in respect of valuation changes for the year ended 30 June 2021 was a loss of $8.8 million (30 June 2020: gain of $8.1 million).

Note 14 Reserves and retained earnings

	30 June 2021 $m	30 June 2020 $m
Share-based payments reserve		
Balance at the beginning of the year	(56.2)	(57.7)
Share-based payments for the period	11.5	14.2
Releases from share-based payments reserve	(10.2)	(14.5)
Tax in equity	2.1	1.8
Balance at the end of the year	**(52.8)**	**(56.2)**
Cash flow hedge reserve – SPV[1]		
Balance at the beginning of the year	0.1	0.1
Loss on cash flow hedges	(0.5)	—
Balance at the end of the year	**(0.4)**	**0.1**
Foreign currency translation reserve[1]		
Balance at the beginning of the year	(0.5)	(2.6)
(Loss)/gain on translation of foreign entities[2]	(49.7)	1.6
Gain on hedge of net investment in foreign entities[2]	46.8	0.5
Balance at the end of the year	**(3.4)**	**(0.5)**
Adjusted controlling interests reserve[1]		
Balance at the beginning of the year	5.7	7.8
Change in holdings in controlled entities	—	(2.1)
Balance at the end of the year	**5.7**	**5.7**
Total reserves	**(50.9)**	**(50.9)**
Retained earnings		
Balance at the beginning of the year	922.9	1,559.0
AASB 16 adjustment	—	(3.7)
Profit/(loss) attributable to equity holders	592.3	(416.0)
Dividends paid	(64.0)	(216.4)
Total retained earnings	**1,451.2**	**922.9**

1 These items may eventually be recycled to the profit and loss section of the Statement of comprehensive income.
2 Net of tax.

Accounting policy

Share-based payments reserve

An expense is recognised over the vesting period of share-based payments granted to employees. This expense is based on the valuation of the equity benefits conferred at the grant date. When an instrument is granted, and an expense incurred, there is a corresponding increase in the share-based payments reserve directly in equity.

The total of this reserve is net of any gain or loss realised on the disposal of forfeited shares held within the schemes. On vesting of the award they are subsequently recognised as an increase in equity and a reduction in share-based payment reserve at an average acquisition price, which may be higher or lower than the initial recognised valuation price.

Foreign currency translation reserve

This reserve is used to record foreign exchange differences arising from the translation of the foreign subsidiaries. It also includes the effective portion of fair value changes on foreign exchange derivative contracts designated as hedges of a net investment in a foreign entity.

Adjusted controlling interests reserve

This reserve relates to changes arising from movements in the ownership interests in entities already controlled by the Group. The difference between the fair value of the consideration paid/received for the change in holding and the change in the Group's share of the net assets of the entity is recorded in this reserve.

Cash flow hedge reserve – SPV

This comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions.

Note 15 Finance costs

	30 June 2021 $m	30 June 2020 $m
Interest expense	283.7	155.5
Interest expense – lease liabilities	3.0	2.9
Interest expense – SPV	3.3	11.1
Interest expense – property trusts	5.3	6.1
Interest expense – Challenger Capital Notes 1, 2 and 3	28.4	31.1
Other finance costs	4.2	7.1
Total finance costs	**327.9**	**213.8**

Accounting policy

Finance costs represent interest incurred on interest bearing financial liabilities (primarily external unit holders' liabilities distributions, repurchase agreements, the securitised residential mortgage-backed securities (RMBS) issued by the consolidated Special Purpose Vehicles (SPV), subordinated debt, bank loans and other borrowings) and are recognised as an expense in the period in which they are incurred.

Finance costs that are directly attributable to the acquisition, construction or production of qualifying property assets (being assets that take a substantial period of time to develop for their intended use or sale) are capitalised as part of the cost of that asset. Revenue earned on the investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

To the extent that the Group allocates general borrowed funds for the purpose of obtaining a qualifying property asset, the borrowing costs eligible for capitalisation are determined by applying a capitalisation rate to the expenditure on that asset.

Note 16 Dividends paid and proposed

	30 June 2021 $m	30 June 2020 $m
Dividends declared and paid during the year		
Final 30 June 2020 100% franked dividend: nil (30 June 2019: 18.0 cents 100% franked dividend)	—	109.7
Interim 30 June 2021 100% franked dividend: 9.5 cents (30 June 2020: 17.5 cents 100% franked dividend)	64.0	106.7
Total dividends paid	**64.0**	**216.4**
Dividend proposed (not recognised as a liability at 30 June)		
Final 30 June 2021 dividend: 100% franked dividend: 10.5 cents (30 June 2020: nil)	70.8	—

Refer to Note 12 Contributed equity for details of the dividend policy.

Dividend franking credits

Franking credits available to shareholders are $118.8 million (30 June 2020: $12.4 million), based on a tax rate of 30%. The amount is calculated from the balance of the franking account as at the end of the reporting period, adjusted for franking credits that will arise after the end of the reporting period from the settlement of current liabilities for income tax and franking debits in respect of interest on Challenger Capital Notes 1, 2 and 3. The impact of the proposed dividend will be to reduce the balance of the franking account by $30.3 million. All dividends are franked at a tax rate of 30%.

Note 17 Earnings per share

	30 June 2021 cents	30 June 2020 cents
Basic earnings per share	88.2	(68.4)
Diluted earnings per share	68.0	(68.4)
	$m	**$m**
Profit/(loss) attributable to ordinary shareholders	592.3	(416.0)
Add back interest expense on Challenger Capital Notes 1, 2 and 3	26.1	—
Add back interest expense net of tax on CLC Subordinated Notes	6.0	—
Total earnings used in the calculation of diluted earnings per share	**624.4**	**(416.0)**
Number of shares	**Number**	**Number**
Weighted average of ordinary shares issued	675,201,946	612,872,293
Weighted average of Treasury shares	(3,550,972)	(4,540,931)
Weighted average ordinary shares for basic earnings per share	**671,650,974**	**608,331,362**
Adjusted for potential ordinary shares:		
Weighted average effect of Challenger Performance Plan	8,744,057	—
Weighted average effect of Challenger Capital Notes 1, 2 and 3	178,254,426	—
Weighted average effect of CLC Subordinated Notes	59,070,235	—
Weighted average ordinary shares for diluted earnings per share	**917,719,692**	**608,331,362**

Accounting policy

Basic earnings per share is calculated by dividing the total profit for the year attributable to equity holders of the Company by the weighted average number of ordinary shares outstanding during the financial year. The number of ordinary shares outstanding is net of Treasury shares held by the Challenger Performance Plan (CPP) Trust or under CPP deferred share purchase agreements in respect of equity incentive plan awards to employees.

During the year, the Company conducted a non-underwritten share purchase plan (SPP) raising $35.0 million with 8.1 million shares issued to retail shareholders at a price of $4.32 per share.

The weighted average number of Treasury shares for the period was 3,550,972 (2020: 4,540,931).

Note 17 Earnings per share (continued)

Accounting policy (continued)

Accounting treatment of Capital Notes and subordinated debt

Challenger Capital Notes 1, 2 and 3 and subordinated debt are an effective source of funding for Challenger.

Each of the Capital Notes 1, 2, 3 and subordinated debt have convertibility features which would result in these instruments converting to ordinary shares under certain circumstances, including APRA determining CLC to be non-viable.

With the exception of Challenger Notes 1, it is Challenger's current intention to refinance each of these instruments at their respective call dates, or prior to the Mandatory Conversion Date, and therefore conversion to ordinary shares is unlikely.

However, under AASB 133 ***Earnings per Share***, convertible debt is considered dilutive whenever the interest per potential ordinary share for each of these instruments is less than Challenger's basic EPS for the period. As such, a test is required at each reporting period to determine if they are included in the dilutive share count.

Diluted earnings per share is calculated by dividing the total adjusted profit attributable to equity holders of the Company by the weighted average number of ordinary shares outstanding during the year adjusted for the effects of dilutive shares that may be converted under the terms of Challenger Capital Notes 1, 2 and 3 (Notes), CLC Subordinated Notes and shares granted under the Challenger Performance Plan (CPP).

The dilutive share count for Challenger's convertible debt (Challenger Capital Notes 1, 2 and 3 and subordinated debt) is based on the following formula:

$$\frac{\text{Face value of debt}}{\text{Conversion factor x Challenger's 20-day VWAP}^{1}\text{ share price}}$$

The conversion factor on all Challenger's convertible debt is 99% of the weighted average Challenger share price over the last 20 days of trading (subject to a minimum VWAP floor) in each reporting period.

An assessment of the dilutive impact of convertible securities is usually done by reference to the determination as to whether the interest received would be more or less than the EPS and whether it would be rational for a holder to receive coupon from the convertible security or dividends from holding the shares. In the prior year, as the company was in a loss position the dilutive EPS is capped at the basic EPS. This is because the dilutive impact of issuing more shares means that the loss incurred is spread over a higher number of shares which results in a lower loss per share. In these circumstances, the dilutive EPS cannot be lower than the basic EPS. As a result, the potential shares that might be considered dilutive by virtue of their conversion to equity, are considered non-dilutive in a loss position and are therefore not included in the calculation. In the prior year this results in no adjustment for potential dilution from the conversion of securities to ordinary shares.

The profit attributable to ordinary shareholders is adjusted by $32.1 million interest on the Notes and CLC Subordinated Notes (30 June 2020: no adjustment) for the diluted calculation when the Notes and CLC Subordinated Notes are considered dilutive.

There have been no other transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of authorisation of these financial statements.

[1] Volume-weighted average share price

Section 5: Risk management

This section outlines how financial risk is managed within the Group and provides additional information about how the overall risk management program seeks to minimise potentially adverse financial effects associated with key financial risks. This section also provides disclosures on the fair values of assets and liabilities of the Group, the valuation techniques used in determining the fair value of those assets and liabilities, and the sensitivities of assets categorised as Level 3 instruments to reasonably possible changes in valuation assumptions.

Note 18 Financial risk management

Governance and risk management framework

The Group's activities expose it to a variety of financial risks, such as market risk (including currency risk, interest rate risk, inflation risk, equity price risk and credit spread risk), credit default risk and liquidity risk. The management of these risks is fundamental to the Group's business and to building shareholder value. The Board is responsible, in conjunction with senior management, for understanding the risks associated with the activities of the Group and implementing structures and policies to adequately monitor and manage those risks.

The Board has established the Group Risk Committee (GRC) and the Group Audit Committee (GAC) to assist in the discharge of certain responsibilities. In particular, the GRC assists the Board in setting the risk appetite and ensuring the Group has an effective risk management framework incorporating management, operational and financial controls.

The Executive Risk Management Committee (ERMC) is an executive committee, chaired by the Chief Risk Officer (CRO), which assists the GRC, GAC and Board in the discharge of their risk management obligations by implementing the Board-approved risk management framework.

The Group's Risk division has day-to-day responsibility for monitoring the implementation of the framework with oversight, analysis, monitoring and reporting of risks. The CRO provides regular reporting to the GRC and the Board.

The Group's principal financial instruments consist of cash and cash equivalents, receivables, financial assets at fair value through profit and loss, payables, life insurance contract liabilities, life investment contract liabilities, derivatives and other interest bearing financial liabilities.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial instruments, are disclosed in Section 1: Basis of preparation and overarching significant accounting policies and included in the relevant notes to the financial statements.

Market risk

Market risk is the risk that the fair value and/or future cash flows from a financial instrument will fluctuate as a result of changes in market factors. Market risk comprises (among others) of interest rate risk (due to fluctuations in market interest rates), price risk (due to fluctuations in the fair value of equities and other alternatives or credit spreads) and currency risk (due to fluctuations in foreign currency exchange rates).

Interest rate risk

Interest rate risk is the risk of fluctuations in the Group's earnings and equity arising from movements in market interest rates, including changes in the absolute levels of interest rates, the shape of the yield curve, the margin between the different yield curves and the volatility of interest rates.

It is the Group's policy to minimise the impact of interest rate movements on debt servicing capacity, Group profitability, business requirements and company valuation. The amount of drawn net recourse corporate interest bearing liabilities, and their duration, is determined with reference to the annual budget and the most current forecasts. The Group's strategy is to have no interest rate hedges with a duration of greater than five years and targets average hedge duration of three years.

CLC's market risk policy is approved by the CLC Board and sets out the relevant risk limits for interest rate exposure. It is CLC's policy to minimise the impact of interest rate movements on its projected future cash flows. The management of the risks associated with life investment and life insurance contracts, including interest rate risk, is subject to the prudential requirements of the Life Act and APRA. This includes satisfying capital adequacy requirements, which in turn include consideration of how the interest rate sensitivity of assets and liabilities are matched.

For the SPV entities, the impact of a rising/falling bank bill swap rate (BBSW) results in an increase/decrease in the cost of funding and therefore on the profit of the trusts. This interest rate risk is mitigated by actively adjusting the interest rates charged to borrowers if a sustained adverse differential to the benchmark is evidenced. SPV entities are also exposed to the risks arising from borrowers fixing the rates on their mortgage. This interest rate risk is managed by using cash flow hedges to swap the fixed rate to a floating rate exposure at an amount equal to the notional value of the mortgages being fixed.

Note 18 Financial risk management (continued)

Interest rate risk (continued)

Interest rate sensitivity

The Group's sensitivity to movements in interest rates in relation to the value of financial assets and liabilities is shown in the table below. It is assumed that the change happens at the Statement of financial position date and that there are concurrent movements in interest rates and parallel moves in the yield curve. All material underlying exposures and related hedges are included in the analysis which includes investment properties with leases, where the future income stream is duration-hedged for interest rate movements. The impact on profit and equity is post-tax at a rate of 30%. The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period. As shown below, 100 basis points (1%) movements in interest rates would have minimal impact on the Group's financial position:

	Change in variable	Profit/(loss) 30 June 2021 $m	Change in equity 30 June 2021 $m	Profit/(loss) 30 June 2020 $m	Change in equity 30 June 2020 $m
Non-SPV	+100bps	1.7	1.7	0.8	0.8
	-100bps	(1.7)	(1.7)	(0.8)	(0.8)
SPV	+100bps	(0.2)	(0.2)	(0.3)	(0.3)
	-100bps	0.2	0.2	0.3	0.3
Total	**+100bps**	**1.5**	**1.5**	**0.5**	**0.5**
	-100bps	**(1.5)**	**(1.5)**	**(0.5)**	**(0.5)**

Price risk

Price risk is the risk that the fair value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments. The Group is exposed to equity price risk on its holdings in equity securities, which include a range of investments in absolute return strategies where returns are considered to be generally uncorrelated to listed equity market returns, and credit spread risk on its fixed income securities. The Group is required to fair value all equities and fixed income securities held to back life contract liabilities.

Equity risks will arise as a natural result of CLC's Asset Allocation Plan. Equity prices can be driven by a range of risk factors specific to an individual exposure including broad macroeconomic and instrument specific factors that may be uncorrelated with broader equity markets. The Group's primary tools for managing investment price risks are CLC's Internal Capital Adequacy Assessment Process (ICAAP) and the Asset Allocation Plan.

Equity price risk sensitivity

The potential impact of movements in the market value of listed and unlisted equities on the Group's Statement of comprehensive income and Statement of financial position is shown in the sensitivity analysis. This sensitivity analysis has been performed to assess the direct risk of holding equity instruments; therefore, any potential indirect impact on fees from the Group's funds management business has been excluded.

The impact on profit and equity is post-tax at a rate of 30%. The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period. As shown below, a 10% movement in equity prices would have a material impact on the consolidated Group's financial position. It is assumed that the relevant change occurs as at the Statement of financial position date.

Equities and other alternatives	Change in variable	Profit/(loss) 30 June 2021 $m	Change in equity 30 June 2021 $m	Profit/(loss) 30 June 2020 $m	Change in equity 30 June 2020 $m
Property securities	+10%	6.2	6.2	5.3	5.3
	-10%	(6.2)	(6.2)	(5.3)	(5.3)
Infrastructure investments	+10%	7.8	7.8	3.9	3.9
	-10%	(7.8)	(7.8)	(3.9)	(3.9)
Other equities and alternative assets	+10%	108.8	108.8	55.5	55.5
	-10%	(108.8)	(108.8)	(55.5)	(55.5)
Total assets	**+10%**	**122.8**	**122.8**	**64.7**	**64.7**
	-10%	**(122.8)**	**(122.8)**	**(64.7)**	**(64.7)**

Note 18 Financial risk management (continued)

Price risk (continued)

Credit spread risk sensitivity

The Group is exposed to price movements resulting from credit spread fluctuations through its fixed income securities (net of subordinated debt) and policy liabilities. As at 30 June 2021, a 50 basis point increase/decrease in credit spreads would result in a post-tax (at 30%) unrealised loss/gain in the Statement of comprehensive income and equity of $146.9 million in respect of fixed income securities partially offset by an unrealised gain/loss of $81.8 million million in respect of policy liabilities (30 June 2020: $102.9 million fixed income securities, $77.8 million policy liabilities).

Currency risk

It is the Group's policy to minimise the exposure of all Statement of financial position items to movements in foreign exchange rates other than instruments considered to be Tier 2 capital under regulatory standards. Currency exposure arises primarily as a result of investments in the Eurozone, Japan, the United Kingdom and the United States, so currency risk therefore arises from fluctuations in the value of the euro, Japanese yen, British pound and US dollar against the Australian dollar. In order to protect against foreign currency exchange rate movements, the Group has entered into foreign currency derivatives.

In addition, the Group has exposure to foreign exchange risk upon consolidation of its foreign currency denominated controlled entities and materially mitigates this by designating foreign currency derivatives as hedges of net investments in foreign entities in equity to match its foreign currency translation reserve exposure. Effectiveness is monitored on a regular basis to ensure that the hedge remains effective and any ineffective portion of the hedge is recognised directly in the Statement of comprehensive income.

The SPV entities hedge exposure to foreign currency risk arising from issuing mortgage-backed securities in foreign currencies. The currencies impacted are primarily the British pound, euro and US dollar. All derivatives in the SPV entities are designated as cash flow hedges. These hedges are effective and there is no material impact on the profit and loss. The following table details the Group's net exposure to foreign currency as at the reporting date in Australian dollar equivalent amounts:

	GBP $m	USD $m	Euro $m	JPY $m	Other $m
30 June 2021					
Financial assets	765.7	1,999.1	1,164.7	387.2	574.6
Financial liabilities	(3.2)	(1,190.4)	(4.4)	0.1	—
Foreign currency contracts and cross currency swaps	(762.2)	(802.7)	(1,161.3)	(376.7)	(576.0)
Net exposure in Australian dollars	**0.3**	**6.0**	**(1.0)**	**10.6**	**(1.4)**
30 June 2020					
Financial assets	560.3	1,940.2	899.7	420.3	514.3
Financial liabilities	(4.7)	(648.8)	(1.7)	(0.8)	—
Foreign currency contracts and cross currency swaps	(550.8)	(1,260.3)	(895.4)	(405.5)	(513.6)
Net exposure in Australian dollars	**4.8**	**31.1**	**2.6**	**14.0**	**0.7**

The analysis in the currency risk table shows the impact on the Statement of comprehensive income and equity of a movement in the Group's major foreign currency exposure exchange rates against the Australian dollar using the net exposure at the balance date. All underlying exposures and related hedges are included in the analysis.

A sensitivity of 10% has continued to have been applied as it still reflects a reasonable measurement given the current level of exchange rates and the volatility observed during the conditions created by the COVID-19 crisis. The impact on profit and equity is post-tax at a rate of 30%.

The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period. As shown in the table on the following page, a 10% movement in foreign currency exchange rates would have minimal impact on the Group's financial position.

Note 18 Financial risk management (continued)

Currency risk (continued)

	Movement in variable against $	Profit/(loss) 30 June 2021 $m	Change in equity 30 June 2021 $m	Profit/(loss) 30 June 2020 $m	Change in equity 30 June 2020 $m
British Pound (GBP)	+10%	—	—	0.4	0.4
	-10%	—	—	(0.4)	(0.4)
US Dollar (USD)	+10%	0.4	0.4	2.2	2.2
	-10%	(0.4)	(0.4)	(2.2)	(2.2)
Euro (EUR)	+10%	—	—	0.2	0.2
	-10%	—	—	(0.2)	(0.2)
Japanese Yen (JPY)	+10%	0.2	0.8	—	1.0
	-10%	(0.2)	(0.8)	—	(1.0)
Other	+10%	(0.1)	(0.1)	—	—
	-10%	0.1	0.1	—	—
Total	**+10%**	**0.5**	**1.1**	**2.8**	**3.8**
	-10%	**(0.5)**	**(1.1)**	**(2.8)**	**(3.8)**

Credit default risk

The Group makes use of external ratings agencies (Standard & Poor's, Fitch, Moody's or other reputable credit rating agencies) to determine credit ratings. Where a counterparty or debt obligation is rated by multiple external rating agencies, the Group will use Standard & Poor's ratings where available. All credit exposures with an external rating are also rated internally and cross-referenced to the external rating, if applicable. Where external credit ratings are not available, internal credit ratings are assigned by appropriately qualified and experienced credit personnel who operate separately from the risk originators.

Each business unit is responsible for managing credit risks that arise with oversight from a centralised credit risk management team.

COVID-19 has led to a number of external and internal ratings downgrades and loan restructures and amendments.

Credit exposure by credit rating

The table below provides information regarding the maximum credit risk exposure of the Group in respect of the major classes of financial assets by equivalent credit rating. The maximum credit exposure is deemed to be the carrying value of the asset not including any collateral or other credit protection in place. The analysis classifies the assets according to internal or external credit ratings. Assets rated investment grade are those rated by Standard & Poor's at BBB– or above, with non-investment grade therefore being below BBB–.

	Investment grade				Non-inv.		
	AAA $m	AA $m	A $m	BBB $m	grade $m	Other $m	Total $m
30 June 2021							
Cash and cash equivalents	928.6	—	—	—	—	—	928.6
Cash and cash equivalents – SPV	60.8	—	—	—	—	—	60.8
Receivables	15.4	106.0	127.3	24.0	3.7	554.0	830.4
Mortgage assets – SPV	270.3	59.5	175.6	63.9	—	1.0	570.3
Fixed income securities	9,162.3	3,559.8	1,984.7	3,023.4	2,427.1	239.6	20,396.9
Derivative assets	—	590.2	51.6	96.5	—	—	738.3
Financial leases	—	—	5.8	9.7	11.3	—	26.8
Total assets with credit exposures	**10,437.4**	**4,315.5**	**2,345.0**	**3,217.5**	**2,442.1**	**794.6**	**23,552.1**
30 June 2020							
Cash and cash equivalents	603.9	—	—	—	—	—	603.9
Cash and cash equivalents – SPV	58.0	—	—	—	—	—	58.0
Receivables	27.7	41.7	58.2	21.6	5.9	439.0	594.1
Mortgage assets – SPV	348.5	68.3	125.4	164.4	—	—	706.6
Fixed income securities	11,308.4	1,189.9	2,113.0	2,474.7	2,114.5	274.4	19,474.9
Derivative assets	—	1,033.4	78.4	0.1	0.6	—	1,112.5
Financial leases	—	—	11.4	7.3	13.0	—	31.7
Total assets with credit exposures	**12,346.5**	**2,333.3**	**2,386.4**	**2,668.1**	**2,134.0**	**713.4**	**22,581.7**

Note 18 Financial risk management (continued)

Credit default risk (continued)

Mortgage assets – SPV

Mortgage assets – SPV are funded via securitised residential mortgage-backed securities (RMBS). As a result, the Group is not exposed to significant credit risk on these assets as this is borne by the RMBS holder.

Collateral held over assets

In the event of a default against any of the mortgages in any SPV, the trustee has the legal right to take possession of the secured property and sell it as a recovery action against settlement of the outstanding account mortgage balance. At all times of possession, the risks and rewards associated with ownership of the property are held by the trustee on behalf of the RMBS holder.

Concentration risk

The credit risk framework includes an assessment of the counterparty credit risk in each business unit and at a total Group level. The Group has no significant concentrations of credit risk at the Statement of financial position date.

Ageing of amortised cost financial assets

The table below gives information regarding the carrying value of the Group's financial assets measured at amortised cost. The analysis splits these assets by those that are not past due and those that are past due (including an ageing analysis at the Statement of financial position date):

		Past due				
Amortised cost financial assets	**Not past due $m**	**0-1 months $m**	**1-3 months $m**	**3-6 months $m**	**6+ months $m**	**Total $m**
30 June 2021						
Receivables	825.1	0.8	0.4	0.3	3.8	830.4
Mortgage assets – SPV	487.3	23.8	14.4	36.4	8.4	570.3
Finance leases	26.8	—	—	—	—	26.8
Total amortised cost financial assets	**1,339.2**	**24.6**	**14.8**	**36.7**	**12.2**	**1,427.5**
30 June 2020						
Receivables	587.8	—	4.5	1.8	—	594.1
Mortgage assets – SPV	598.2	26.1	26.7	51.2	4.4	706.6
Finance leases	31.7	—	—	—	—	31.7
Total amortised cost financial assets	**1,217.7**	**26.1**	**31.2**	**53.0**	**4.4**	**1,332.4**

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in raising funds to meet cash commitments associated with financial instruments. This may result from the inability to sell financial assets at their fair values; a counterparty failing on repayment of a contractual obligation; the inability to generate cash inflows as anticipated; or an unexpected increase in cash outflows.

The Group aims to ensure that it has sufficient liquidity to meet its obligations on a short, medium and long-term basis. In setting the level of sufficient liquidity, the Group considers new business activities in addition to current contracted obligations. It considers: minimum cash requirements; collateral and margin call buffers; APRA and Australian Financial Services Licence (AFSL) requirements; cash flow forecasts; associated reporting requirements; other liquidity risks; and contingency plans.

The basis of the approach to liquidity management is to target sufficient liquidity to meet all cash requirements of the Group over an ensuing 12 month period which ensures that the regulatory guidelines set out in ASIC Regulatory Guide 166 ***Licensing: Financial requirements*** for holders of an AFSL are met.

The Life liquidity management policy is approved by the CLC Board and sets out liquidity targets and mandated actions depending on actual liquidity levels relative to those targets. Detailed forecast cash positions are reported regularly to the Financial Risk Committee (FRC). The FRC and the Investment Committee (IC) replaced the CLC Asset Liability Committee (ALCo) from 1 July 2019. The IC is a committee of investment professionals from within CLC and represents the first line. The FRC is a committee of professionals mainly from the Risk division that is separate from the investment team of CLC. The FRC represents the second line for CLC. At the reporting date, all requirements of the CLC Board-approved liquidity management policy were satisfied.

Maturity profile of undiscounted financial liabilities

The table on the following page summarises the maturity profile of the Group's undiscounted financial liabilities. This is based on contractual undiscounted repayment obligations. Totals differ to the amounts in the Statement of financial position by the amount of time value of money discounting reflected in the Statement of financial position values.

Note 18 Financial risk management (continued)

Maturing profile of undiscounted financial liabilities	1 year or less $m	1-3 years $m	3-5 years $m	>5 years $m	Total $m
30 June 2021					
Payables	1,710.7	5.1	27.4	—	1,743.2
Payables – SPV	0.9	—	—	—	0.9
Interest bearing financial liabilities	4,386.9	969.1	735.4	0.7	6,092.1
Interest bearing financial liabilities – SPV	166.6	214.0	120.1	133.4	634.1
External unit holders' liabilities	3,090.1	542.1	—	—	3,632.2
Life investment contract liabilities	3,356.7	2,948.9	459.6	372.2	7,137.4
Life insurance contract liabilities[1]	863.9	1,465.8	1,158.7	4,817.7	8,306.1
Derivative liabilities	130.1	58.3	96.4	222.8	507.6
Total undiscounted financial liabilities[1]	**13,705.9**	**6,203.3**	**2,597.6**	**5,546.8**	**28,053.6**
30 June 2020					
Payables	1,555.5	—	—	27.9	1,583.4
Payables – SPV	2.0	10.2	45.3	—	57.5
Interest bearing financial liabilities	5,458.0	1,336.0	453.2	168.8	7,416.0
Interest bearing financial liabilities – SPV	139.9	260.6	147.1	170.2	717.8
External unit holders' liabilities	1,587.3	828.5	—	—	2,415.8
Life investment contract liabilities	2,966.4	2,325.5	542.5	427.0	6,261.4
Life insurance contract liabilities[1]	775.4	1,272.1	1,014.4	4,574.9	7,636.8
Derivative liabilities	97.1	48.7	80.7	498.9	725.4
Total undiscounted financial liabilities[1]	**12,581.6**	**6,081.6**	**2,283.2**	**5,867.7**	**26,814.1**

[1] Disclosure of life insurance contract liabilities is not required under AASB 7 ***Financial Risk Management,*** for reference purposes they have been included. Refer to Note 8 Life contract liabilities for further details.

Note 19 Fair values of financial assets and liabilities

Fair value determination and classification

Fair value reflects the price that would be received on sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The majority of the Group's financial instruments are held in the life insurance statutory funds of CLC and, as a result, are required by AASB 1038 ***Life Insurance Contracts*** to be designated at fair value through profit and loss where this is permitted under AASB 9 ***Financial Instruments.***

Financial instruments measured at fair value are categorised under a three level hierarchy, reflecting the availability of observable market inputs when estimating the fair value. If different levels of inputs are used to measure a financial instrument's fair value, the classification within the hierarchy is based on the lowest level that is significant to the fair value measurement. The three levels are set out below.

Level 1 Unadjusted quoted prices in active markets are the valuation inputs for identical assets or liabilities (i.e. listed securities).

Level 2 Valuation inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) are used.

Level 3 There are valuation inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The unobservable inputs into the valuation of the Group's Level 3 assets and liabilities are determined based on the best information available, including the Group's own assessment of the assumptions that market participants would use in pricing the asset or liability. Examples of unobservable inputs are estimates about the timing and amount of cash flows, discount rates, earnings multiples and internal credit ratings.

Valuation techniques

The majority of the Group's listed and unlisted fixed income securities, over-the-counter derivative financial instruments and interest bearing liabilities including the subordinated debt issuance are classified as Level 2. This recognises the availability of a quoted price but not from an active market as defined by the accounting standard.

Note 19 Fair values of financial assets and liabilities (continued)

Valuation techniques (continued)

Fixed income securities where market observable inputs are not available are classified as Level 3. The Group's derivative financial instruments are traded over-the-counter so, while they are not exchange traded, there is a market observable price. Most of the fixed income securities and all of the government/semi-government securities have market observable prices.

Externally rated unlisted fixed income securities are valued by applying market observable credit spreads on similar assets with an equivalent credit rating and are classified as Level 2. Internally-rated fixed income securities are classified as Level 3 as the determination of an equivalent credit rating is a significant non-observable input.

Equity, infrastructure and property securities that are exchange traded are generally classified as Level 1. Where quoted prices are available, but are not from an active market, they are classified as Level 2. If market observable inputs are not available, they are classified as Level 3. Valuations can make use of cash flow forecasts discounted using the applicable yield curve, earnings-multiple valuations or, for managed funds, the net assets of the trust per the most recent financial report.

External unit holders' liabilities are valued at the face value of the amounts payable, being an approximation of fair value, and classified as Level 2. The portion of life investment contract liabilities classified as Level 2 represents products or product options for which the liability is determined based on an account balance, rather than a discounted cash flow as applied to the rest of the portfolio.

Cash and cash equivalents are carried at amortised cost. To determine a fair value where the asset is liquid or maturing within three months, the fair value is approximate to the carrying amounts. This assumption is applied to liquid assets and the short-term elements of all other financial assets and financial liabilities.

The mortgage SPVs have total equity attributable to residual income unitholders (RIU) at amortised cost of ($0.4) million (2020: $0.1 million). The fair value of this RIU holders' asset is $31.3 million (2020: $41.0 million) and would be classified as Level 3 in the fair value hierarchy.

Challenger Capital Notes 1, 2 and 3 have carrying values (inclusive of unamortised issue costs) of $27.7 million, $456.3 million and $379.0 million respectively. The fair value of these notes is $27.8 million, $480.8 million and $407.9 million respectively and they are classified as Level 1 in the fair value hierarchy.

Valuation process

For financial instruments and investment properties categorised within Level 3 of the fair value hierarchy, the valuation process applied in valuing such instruments is governed by the CLC Practice Note on Investment Asset and Financial Liability Valuation. The Practice Note outlines the Valuation Committee's responsibilities in the valuation of investment assets and financial liabilities for the purposes of financial reporting. All significant Level 3 financial instruments are referred to the Valuation Committee which generally meets monthly, or more frequently if required.

All financial instruments and investment properties carried at fair value are measured on a recurring basis. Refer Note 5 Financial assets – fair value through profit and loss and Note 6 Investment and development property for further details on the valuation process applied to unlisted financial instruments and investment properties.

The table on the following page summarises the financial instruments and investment properties measured at fair value at each level of the fair value hierarchy as at the Statement of financial position date.

Note 19 Fair values of financial assets and liabilities (continued)

Valuation process (continued)

	Level 1 $m	Level 2 $m	Level 3 $m	Total $m
30 June 2021				
Derivative assets	—	738.3	—	738.3
Fixed income securities[1]	—	18,522.1	1,874.8	20,396.9
Equity and other alternatives	1.2	1,188.2	155.0	1,344.4
Infrastructure investments[1]	—	—	345.4	345.4
Property securities	—	—	88.0	88.0
Investment and development property[2]	—	396.0	3,389.7	3,785.7
Total assets	**1.2**	**20,844.6**	**5,852.9**	**26,698.7**
Derivative liabilities	0.8	506.8	—	507.6
Interest bearing financial liabilities	916.5	418.2	—	1,334.7
External unit holders' liabilities	—	3,632.2	—	3,632.2
Life investment contract liabilities	—	47.2	6,183.2	6,230.4
Total liabilities	**917.3**	**4,604.4**	**6,183.2**	**11,704.9**
30 June 2020				
Derivative assets	—	1,111.9	0.6	1,112.5
Fixed income securities	—	17,566.5	1,908.4	19,474.9
Equity and other alternatives	0.5	627.8	274.4	902.7
Infrastructure investments[1]	—	9.8	370.3	380.1
Property securities	—	—	76.3	76.3
Investment and development property[2]	—	—	3,685.9	3,685.9
Total assets	**0.5**	**19,316.0**	**6,315.9**	**25,632.4**
Derivative liabilities	—	725.4	—	725.4
Interest bearing financial liabilities	798.6	422.7	—	1,221.3
External unit holders' liabilities	—	2,415.8	—	2,415.8
Life investment contract liabilities	—	49.9	5,817.9	5,867.8
Total liabilities	**798.6**	**3,613.8**	**5,817.9**	**10,230.3**

1 The Group has exposures to structured entities (entities designed so that voting or similar rights are not the dominant factor in determining who controls the entity; for example, when any voting rights relate purely to administrative tasks) via investments in asset-backed finance vehicles (where it may act as a lender or purchaser of notes and/or residual income units) and securitisations (such as mortgages, finance leases and other types of collateralised vehicles). The Company assesses, at inception and at each reporting date, whether a structured entity should be consolidated based on the accounting policy. The maximum exposure to loss is limited to the reported fair value of the underlying securities plus any guaranteed undrawn commitments to the counterparties. At 30 June 2021 the carrying value of asset-backed financing assets was $76.7 million (30 June 2020: $91.1 million) with $56.4 million undrawn commitments (30 June 2020: $32.0 million) and securitisations was $4,517.9 million (30 June 2020: $5,386.5 million) plus $20.4 million undrawn commitments (30 June 2020: $107.2 million).

2 Refer Note 6 Investment and development property for valuation techniques and key unobservable inputs.

Level 3 reconciliation

The following table shows a reconciliation of the movement in the fair value of financial instruments categorised within Level 3 of the fair value hierarchy during the year:

	30 June 2021		30 June 2020	
	Assets $m	Liabilities $m	Assets $m	Liabilities $m
Balance at the beginning of the year	6,315.9	5,817.9	6,420.7	6,712.2
Fair value movements	(54.7)	95.2	(187.5)	135.7
Acquisitions	1,688.0	3,208.7	2,764.2	1,992.4
Maturities and disposals	(1,688.5)	(2,938.6)	(2,666.0)	(3,022.4)
Transfers to other categories[1,2]	(407.8)	—	(15.5)	—
Balance at the end of the year	**5,852.9**	**6,183.2**	**6,315.9**	**5,817.9**
Unrealised losses included in the Statement of comprehensive income for assets and liabilities held at the Statement of financial position date	(54.7)	(95.2)	(187.5)	(135.7)

1 The Group transfers between levels of the fair value hierarchy when there is a change in the observability of the pricing inputs or a change to valuation methodology.

2 Transfers to/from other categories are due to changes in the market observability of inputs used in the valuation of financial instruments. There were no transfers between Level 1 and Level 2 during the reporting period. There were no transfers into Level 3 (30 June 2020: $2.5 million) and there were $407.8 million (30 June 2020: $18.0 million) of transfers out of Level 3 and into Level 2 during the reporting period.

Note 19 Fair values of financial assets and liabilities (continued)

Level 3 sensitivities

The following table shows the sensitivity of Level 3 financial instruments to a reasonably possible change in alternative assumptions in respect of the non-observable inputs into the fair value calculation:

	Level 3 value[1] $m	Positive impact $m	Negative impact $m	Valuation technique	Reasonably possible change in non-observable input[2,3]
30 June 2021					
Fixed income securities	1,874.8	13.5	(54.0)	Discounted cash flow	Primarily credit spreads
Equity and other alternatives	155.0	12.0	(13.0)	Discounted cash flow, external financial report	Mortality rate, 5% change in valuation
Infrastructure investments	345.4	4.3	(4.2)	Discounted cash flow, external financial report	Primarily discount rate on cash flow models
Property securities[4]	88.0	4.4	(4.4)	External financial report	5% change in valuation
Investment contract liabilities	(6,183.2)	2.4	(2.4)	Discounted cash flow	Primarily expense assumptions
Investment and development property	3,389.7	152.3	(124.9)	Market capitalisation, Discounted cash flow	Primarily capitalisation rate
Total Level 3	**(330.3)**				
30 June 2020					
Derivative assets	0.6	—	—	Discounted cash flow	Primarily credit spreads
Fixed income securities	1,908.4	23.1	(74.9)	Discounted cash flow	Primarily credit spreads
Equity and other alternatives	274.4	18.8	(20.1)	Discounted cash flow, external financial report	Mortality rate, 5% change in valuation
Infrastructure investments	370.3	4.4	(4.3)	Discounted cash flow, external financial report	Primarily discount rate on cash flow models
Property securities[4]	76.3	3.8	(3.8)	External financial report	5% change in valuation
Investment contract liabilities	(5,817.9)	2.3	(2.3)	Discounted cash flow	Primarily expense assumptions
Investment and development property	3,685.9	165.3	(116.9)	Market capitalisation, Discounted cash flow	Primarily capitalisation rate
Total Level 3	**498.0**				

1 The fair value of the asset or liability would increase/decrease if the credit spread or discount rate decreases/increases or if expense assumptions and the other inputs increase/decrease.
2 Specific asset valuations will vary from asset to asset as each individual industry profile will determine appropriate valuation inputs to be utilised.
3 The effect of a change to reflect a reasonably possible alternative assumption was calculated by moving the credit band by one tier, adjusting the discount rates by between 50bps – 100bps, adjusting property capitalisation rates by 25bps (Australia) or 10bps (Japan), adjusting credit spreads by 50bps, changing the valuation of the unlisted schemes by 5% and adjusting the expense assumption allocation splits by 10%.
4 The effect of a change to reflect a reasonably possible alternative assumption was calculated by moving the capitalisation rate by 25bps (Australia) / 10bps (Japan).

The COVID-19 pandemic has had a significant impact on the economy and continues to drive uncertainty across the commercial property market. Independent valuers have noted these uncertainties in respect of the assumptions applied in the course of performing the independent valuation assessments for the direct property portfolio as at the reporting date. As a result of this uncertainty, a further sensitivity analysis has been undertaken to assess the impact on fair value when the significant non-observable input (capitalisation rates) experience a more material movement. Under this additional sensitivity scenario, the capitalisation rate is moved by 50bps (Australia) / 20bps (Japan), resulting in a positive impact of $309.6 million and a negative impact of $247.7 million across the direct property portfolio.

Fixed income also forms a material part of the Level 3 asset class held by the Group. This portfolio primarily consists of internally rated securities where the valuation is derived from applying the market observable comparable spread. The key non-observable inputs in these valuations are the internally derived credit ratings which are based upon credit assessments undertaken by the Risk division. The COVID-19 pandemic has impacted many businesses across various industries and the long-term effects are difficult to assess and not all industries and businesses have been impacted equally. An assessment of the current impact of COVID-19 on the performance of the Level 3 component of the fixed income portfolio has been undertaken and that performance has not changed sufficiently to warrant any additional sensitivity being included.

Note 20 Collateral arrangements

Accounting policy

CLC receives collateral, where it is considered necessary, when entering into certain financial arrangements. The amount of collateral required is subject to management's credit evaluation of the counterparty which is performed on a case-by-case basis. As at 30 June 2021 $264.5 million (30 June 2020: $471.8 million) cash received from third parties as collateral is recorded in payables and $74.6 million (30 June 2020: $221.4 million) of collateral assets received from counterparties was repledged by the Company to third parties.

Except in the event of default, collateral received can be called back by the counterparty in accordance with the financial arrangement. CLC is required to pledge collateral, as part of the standard terms of transactions, when entering into certain financial arrangements. Cash paid to third parties as collateral is recorded in receivables. Other financial assets transferred as collateral are not derecognised from the Statement of financial position as the risks and rewards of ownership remain with CLC. At the balance sheet date the fair value of cash and financial assets pledged are as follows:

Collateral pledged as security	30 June 2021 $m	30 June 2020 $m
Cash	269.9	97.8
Other financial assets[1]	6,675.5	7,730.9
Total collateral pledged	**6,945.4**	**7,828.7**

1 Includes assets sold under repurchase agreements. Please refer Note 13 Interest bearing financial liabilities for more information.

Section 6: Group structure

This section provides details and disclosures relating to the parent entity of the Group, controlled entities, investments in associates and any acquisitions and/or disposals of businesses in the year. Disclosure for related parties is also provided in this section.

Note 21 Parent entity

Company	30 June 2021 $m	30 June 2020 $m
Statement of comprehensive income for the year ended		
Dividends and interest from controlled entities	244.3	232.5
Finance costs	(28.5)	(31.1)
Profit before income tax	215.8	201.4
Income tax benefit	0.6	1.7
Total comprehensive income for the year	**216.4**	**203.1**
Statement of financial position as at		
Assets		
Cash and cash equivalents	2.9	3.0
Receivables	1,594.5	1,439.0
Financial asset – fixed income securities[1]	872.7	805.0
Deferred tax assets	1.3	84.1
Investment in controlled entities	2,416.4	2,373.8
Total assets	**4,887.8**	**4,704.9**
Liabilities		
Payables	544.1	661.6
Current tax liabilities	45.0	—
Interest bearing financial liabilities	863.3	799.8
Total liabilities	1,452.4	1,461.4
Net assets	**3,435.4**	**3,243.5**
Equity		
Contributed equity	2,462.4	2,424.7
Share-based payments reserve	(109.0)	(111.0)
Retained earnings	1,082.0	929.8
Total equity	**3,435.4**	**3,243.5**

[1] Financial asset – fixed income securities relates to the subscription by the Company of notes issued by CLC that qualify as Additional Tier 1 capital of CLC.

Refer Note 27 Contingent liabilities, contingent assets and credit commitments for details of any contingent liabilities applicable to the parent entity.

Note 22 Controlled entities

The table below presents the hierarchical structure of Challenger Limited showing its controlled entities that form the main composition of the Group as at 30 June 2021:

Entity name	Principal activity
Challenger Limited	
Challenger Group Holdings Limited	Corporate
Challenger Group Services Pty Limited	Corporate
Challenger Treasury Limited	Corporate
Challenger Japan Holdings Pty Limited	Corporate
Challenger Funds Management Holdings Pty Limited	Funds Management
Fidante Partners Holdings Pty Limited	Funds Management
Fidante Partners Holdings Europe Limited (incorporated in the UK)	Funds Management
Challenger Investment Partners Limited	Funds Management
Challenger Life Company Holdings Limited	Life
Challenger Life Company Limited	Life

Challenger's percentage holding of the above entities is 100% and all are incorporated in Australia unless otherwise stated.

Accounting policy

Controlled entities are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. The acquisition method of accounting is applied on acquisition or initial consolidation. This method ascribes fair values to the identifiable assets and liabilities acquired. The difference between the net fair value acquired and the fair value of the consideration paid (including the fair value of any pre-existing investment in the entity) is recognised as either goodwill on the Statement of financial position or a discount on acquisition through the Statement of comprehensive income.

Principles of consolidation

The financial statements consolidate the financial information of controlled entities. An entity is controlled when the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Statement of financial position date and the accounting policies of controlled entities are consistent with those of the Company. The Company assesses, at inception and at each reporting date, whether an entity should be consolidated based on the accounting policy.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, are eliminated in full. Non-controlling interests represent the share in the net assets of subsidiaries attributable to equity interests not owned directly or indirectly by the Group.

Note 23 Investment in associates

Name of company	Principal activity	Country of domicile	30 June 2021 %[1]	30 June 2020 %[1]	30 June 2021 $m	30 June 2020 $m
Alphinity Investment Management Pty Ltd	Funds Management	Australia	30	30	1.9	2.0
Ardea Investment Management Pty Ltd[2]	Funds Management	Australia	30	30	25.6	3.3
Ares Australia Management Pty Ltd	Funds Management	Australia	35	35	0.4	0.2
Avenir Capital Pty Ltd	Funds Management	Australia	40	40	—	3.3
Bentham Asset Management Pty Ltd	Funds Management	Australia	49	49	1.1	0.7
Eiger Capital Pty Ltd	Funds Management	Australia	40	40	1.0	0.8
Greencape Capital Pty Ltd	Funds Management	Australia	47	48	38.1	39.8
Lennox Capital Partners Pty Ltd	Funds Management	Australia	40	40	3.3	2.0
Merlon Capital Partners Pty Ltd	Funds Management	Australia	30	30	2.3	2.0
Novaport Capital Pty Ltd	Funds Management	Australia	49	49	0.3	0.3
Resonance Asset Management Limited[3]	Funds Management	UK	—	—	0.7	0.7
Ox Capital Management Pty Ltd	Funds Management	Australia	40	—	—	—
Wavestone Capital Pty Ltd	Funds Management	Australia	33	33	2.5	2.2
Whitehelm Capital Pty Ltd	Funds Management	Australia	30	30	5.9	5.6
Wyetree Asset Management Pty Ltd	Funds Management	UK	49	49	0.1	0.1
Total investment in associates[4]					**83.2**	**63.0**

1 Represents voting rights percentages.
2 During the year ending 30 June 2021 Challenger's economic interest increased to 49.9%. Voting rights remained unchanged.
3 Challenger is deemed to have significant influence.
4 Investment in associates is all considered non-current.

	30 June 2021 $m	30 June 2020 $m
Movements in carrying amount of investment in associates		
Opening balance	63.0	58.1
Acquisition of investment in associates	21.3	—
Share of associates' net profit	35.2	29.3
Dividends and net capital redemptions	(32.6)	(21.9)
Reclassification to investment in controlled entities	—	(0.6)
Impairment of investment in associates	(3.7)	(1.9)
Carrying amount at the end of the year	**83.2**	**63.0**
Share of associates' profit or loss		
Profit after tax for the year	**35.2**	**29.3**
Share of the associates' Statement of financial position		
Current assets	45.7	38.0
Non-current assets	4.8	4.6
Total assets	**50.5**	**42.6**
Current liabilities	21.7	21.8
Non-current liabilities	3.0	1.4
Total liabilities	**24.7**	**23.2**
Net assets	**25.8**	**19.4**

Accounting policy

Associates are entities over which the Group has significant influence of the entities' financial and operating policies but not control. Investments in associates, other than those backing life contracts, are accounted for under the equity method whereby investments are carried at cost adjusted for post-acquisition changes in the Group's share of the net assets of the entity.

Associates' financial reports are used to apply the equity method and both the financial year end date and accounting policies of associate entities are consistent with those of the Group.

The consolidated Statement of comprehensive income reflects the share of the results of operations of associates.

Note 23 Investment in associates (continued)

Accounting policy (continued)

Where there has been a change recognised directly in the associate's equity, the Group recognises its share of any changes in the Statement of changes in equity.

Key estimates and assumptions

An assessment is performed at each Statement of financial position date to determine whether there is any indication of impairment and whether it is necessary to recognise any impairment loss against the carrying value of the net investment in associates.

The Group determines the dates of obtaining or losing significant influence of another entity based on an assessment of all pertinent facts and circumstances that affect the ability to significantly influence the financial and operating policies of that entity.

Note 24 Related parties

Key Management Personnel

The Directors and key executives of Challenger Limited during the reporting period were as follows:

Directors	
Peter Polson	Independent Chair
Richard Howes	Managing Director and Chief Executive Officer
John M Green	Independent Non-Executive Director
Steven Gregg	Independent Non-Executive Director
Masahiko Kobayashi[1]	Non-Independent Non-Executive Director
Heather Smith (appointed 20 January 2021)	Independent Non-Executive Director
JoAnne Stephenson	Independent Non-Executive Director
Duncan West	Independent Non-Executive Director
Melanie Willis	Independent Non-Executive Director

[1] Hiroyuki Iioka is an Alternate Director to Masahiko Kobayashi.

Key executives	
Current KMP	
Richard Howes	Managing Director and Chief Executive Officer
Rachel Grimes[1]	Chief Financial Officer
Nick Hamilton	Chief Executive, Funds Management
Angela Murphy	Chief Executive, Life
Chris Plater	Chief Executive, Operations & Technology
Former KMP	
Anton Kapel[2]	Acting Chief Executive & Chief Investment Officer, Life
Andrew Tobin[3]	Chief Financial Officer

[1] Rachel Grimes commenced being a key executive on 3 May 2021.
[2] Anton Kapel commenced being a key executive on 7 December 2020 and ceased being a key executive on 9 March 2021.
[3] Andrew Tobin ceased being a key executive on 31 March 2021.

Controlled entities and associates

Unless an exception applies under relevant legislation, transactions between commonly-controlled entities within the Group (except where otherwise disclosed) are conducted on an arm's length basis under normal commercial terms and conditions. The Group's interests in controlled entities are disclosed in Note 22 Controlled entities.

Other related parties

During the year, there were transactions between the Group and Challenger-sponsored managed funds for the provision of investment management, transaction advisory and other professional services.

Note 24 Related parties (continued)

Other related parties (continued)

Transactions were also entered into between the Group and associated entities (refer to Note 23 Investment in associates) for the provision of distribution and administration services.

The Group earned fee income during the year of $54.5 million (2020: $47.4 million) from transactions entered into with non-controlled funds and associates. Transactions are conducted on an arm's length basis under normal commercial terms and conditions.

Loans to Directors and key executives

There were no loans made to Directors or key executives as at 30 June 2021 (30 June 2020: nil).

Group products

From time to time, Directors or key executives of the Company or their related entities may purchase products from the Group. These purchases are on the same arm's length terms and conditions as those offered to other employees or customers.

Total remuneration of Key Management Personnel and Non-Executive Directors[1]

KMP and Non-Executive Directors	Short-term benefits $	Post-employment benefits $	Share-based payments $	Other benefits $	Total $
Non-Executive Directors					
2021	**1,621,501**	**88,358**	**—**	**—**	**1,709,859**
2020	1,660,179	103,398	—	—	1,763,577
KMP					
2021	**5,651,994**	**112,345**	**5,021,664**	**208,107**	**10,994,110**
2020	3,878,943	105,015	5,248,471	143,573	9,376,002
All KMP and Non-Executive Directors					
2021	**7,273,495**	**200,703**	**5,021,664**	**208,107**	**12,703,969**
2020	5,539,122	208,413	5,248,471	143,573	11,139,579

1 No termination payments were made to KMPs or NEDs during the period.

Section 7:Other items

This section provides information that is less significant in understanding the financial performance and position of the Group perhaps due to lack of movement in the amount or the overall size of the balance. Nevertheless, these items assist in understanding the Group or are required under the Australian or International Accounting Standards, the *Corporations Act 2001* and/or the *Corporations Regulations*.

Note 25 Goodwill and other intangible assets

	30 June 2021 $m	30 June 2020 $m
Goodwill	**579.9**	**579.9**
Other intangible assets		
Software at cost	32.1	32.6
Less: accumulated amortisation	(15.2)	(10.7)
Less: asset impairment[1]	(1.1)	(4.1)
Less: asset reclassification[2]	(7.5)	(1.3)
	8.3	**16.5**
Commercial agreement	0.9	5.9
Less: accumulated amortisation	—	(0.7)
Foreign exchange gain	—	0.7
Less: impairment	—	(5.9)
	0.9	**—**
Identifiable intangible (Assetsecure)	1.7	1.7
Less: accumulated amortisation	(0.1)	(0.1)
Less: asset reclassification[3]	(1.6)	—
	—	**1.6**
Total other intangible assets	**9.2**	**18.1**

1 Impairment of capitalised software following management assessment for indicators of impairment.
2 Reclassification of previously capitalised cloud computing software deployment costs following the IFRS Interpretations Committee guidance issued in April 2021.
3 Reclassification of Assetsecure identifiable intangible to capitalised software.

	Goodwill		Software		Commercial agreement		Identifiable intangible	
	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m
Balance at the beginning of the year	579.9	557.3	16.5	18.0	—	5.9	1.6	—
Additions	—	22.6	4.9	6.9	0.9	—	—	1.7
Impairment	—	—	(1.1)	(4.1)	—	(5.9)	—	—
Amortisation expense	—	—	(4.5)	(3.0)	—	(0.2)	—	(0.1)
Foreign exchange gain	—	—	—	—	—	0.2	—	—
Reclassification	—	—	(7.5)	(1.3)	—	—	(1.6)	—
Balance at the end of the year	**579.9**	**579.9**	**8.3**	**16.5**	**0.9**	**—**	**—**	**1.6**

Note 25 Goodwill and other intangible assets (continued)

Accounting policy

Goodwill

Goodwill acquired in a business combination is initially measured at cost, being the excess of the fair value of the consideration for the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units (CGUs), or groups of CGUs, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units.

Each unit, or group of units, to which the goodwill is allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes. Impairment is determined by assessing the recoverable amount of the CGU (or group of CGUs) to which the goodwill relates.

When the recoverable amount of the CGU (or group of CGUs) is less than the carrying amount, an impairment loss is recognised and allocated first to reduce the carrying amount of any goodwill allocated to that CGU, then to reduce the carrying amount of the other assets in the unit on a pro rata basis. Impairment losses recognised for goodwill are not subsequently reversed.

CGUs within the Group are predominantly business operations.

When goodwill forms part of a CGU (or group of CGUs) and an operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this manner is measured based on the relative values of the operation disposed of and the portion of the CGU retained.

Other intangible assets

Other intangible assets acquired are recorded at cost less accumulated amortisation and impairment losses. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition.

Amortisation is calculated based on the timing of projected cash flows over the estimated useful lives.

Certain internal and external costs directly incurred in acquiring and developing on-premise software have been capitalised and are being amortised on a straight line basis over their useful lives.

Software-as-a-Service (SaaS)

SaaS arrangements are service contracts providing the Group with the right to access the cloud provider's application software over the contract period. As such the Group does not receive a software intangible asset at the contract commencement date. The Group does not have control over the software nor can it restrict others' access to the benefits of the software.

The following outlines the accounting treatment of costs incurred in relation to SaaS arrangements:

Accounting treatment	Costs
Recognise as an operating expense over the term of the service contract	• Fee for use of application software
Recognise as an operating expense as the service is received	• Configuration costs • Customisation costs • Data conversion and migration costs • Testing costs • Training costs

Key estimates and assumptions

Goodwill recoverable amounts

The Group assesses whether goodwill is impaired at least annually in accordance with the accounting policy. The recoverable amount of each CGU is determined based on value in use calculations that utilise cash flow projections based on financial forecasts approved by senior management which cover an appropriate time horizon. In determining these cash flow projections management considers:

- current and expected performance of each CGU;
- Board and management-approved budgets and strategic plans; and
- changes in Australian and international economic and market environments.

Note 25 Goodwill and other intangible assets (continued)

Key estimates and assumptions (continued)

The impact of COVID-19 has had a profound effect on economies and markets. In addition, the duration and extent of the pandemic together with government responses to it remains uncertain. Notwithstanding, management has made reasonable assumptions of the impact of COVID-19 when determining the cash flow projections to be used for the value in use calculations.

The cash flow projections determined by management are discounted using an appropriate discount rate. The determination of the discount rate is a matter of judgement and is based on a number of factors including a theoretical calculation, observation of third party reports and discount rates used by comparable financial services companies.

The relevant assumptions in deriving the value of the CGU are as follows:

- the budgeted net profit after tax for each CGU for each year within the cash flow projection period;
- the discount rate; and
- growth rates, which are consistent with long-term trends in the industry segments in which the CGUs operate.

The derived values in use for each CGU are in excess of the carrying values of goodwill.

The following CGUs represent the carrying amounts of goodwill:

			Discount rate		
CGU	30 June 2021 $m	30 June 2020 $m	30 June 2021 %	30 June 2020 %	Cash flow horizon (years)
Life	452.3	452.3	10.2	10.0	5
Funds Management	127.6	127.6	9.7	10.0	5
Total	**579.9**	**579.9**			

Sensitivity to change in assumptions

Management is of the view that reasonable changes in the key assumptions, such as an increase in the discount rate by 1% or a change in projected cash flows of 5%, would not cause the respective recoverable amounts for each CGU to fall short of the carrying amounts as at 30 June 2021. All goodwill is non-current.

Other intangible assets amortisation

Useful lives of intangible assets used in the calculation of the amortisation expense are examined on an annual basis and where applicable, adjustments are made on a prospective basis.

Intangible	Life	Depreciation method
Goodwill	Indefinite	Not applicable
Software	3-10 years	Straight line basis over its useful life, usually a period of five years
Commercial agreement	5.5 years	Straight line basis over the life of the intangible, based on the terms of the agreement.

Note 26 Lease assets and liabilities

Right-of-use lease asset

	30 June 2021 $m	30 June 2020 $m
Cost	45.4	37.1
Less: accumulated depreciation	(10.7)	(4.7)
Right-of-use lease asset	**34.7**	**32.4**

	Office premises[1]		Property, plant and equipment[2]	
	30 June 2021 $m	30 June 2020 $m	30 June 2021 $m	30 June 2020 $m
Balance at the beginning of the year[3]	32.0	36.7	0.4	—
Additions	8.4	—	(0.1)	0.4
Depreciation expense	(6.0)	(4.7)	—	—
Balance at the end of the year	**34.4**	**32.0**	**0.3**	**0.4**

1 The Group has entered into commercial leases for the rental of properties where it is not in the best interests of the Group to purchase these properties. These leases have terms ranging between one and 12 years with renewal terms included in the contracts. Renewals are at the specific option of the entity that holds the lease.
2 Property, plant and equipment relates to leases for photocopying equipment.
3 The balance in prior year arose due to the adoption of AASB 16.

Lease liabilities

Maturity analysis of contractual discounted cash flows	30 June 2021 $m	30 June 2020 $m
Amounts due in less than one year	8.0	6.3
Amounts due between one and two years	8.2	6.8
Amounts due between two and five years	26.7	22.4
Amounts due in greater than five years	27.4	32.1
Total lease liabilities	**70.3**	**67.6**

	30 June 2021 $m	30 June 2020 $m
Current	8.0	6.3
Non-current	62.3	61.3
Total lease liabilities[1]	**70.3**	**67.6**

1 Refer to Note 15 for interest expense on lease liabilities and the Statement of cash flows for total cash outflow for leases.

Accounting policy

Right-of-use-lease assets

The Group recognises right-of-use lease assets at the commencement date of the lease (i.e. the date the underlying asset is available for use). Right-of-use lease assets are measured at cost, less any accumulated depreciation and impairment losses, and less any adjustments for any remeasurement of lease liabilities. The cost of right-of-use lease assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received.

Unless the Group is reasonably certain to obtain ownership of the leased assets at the end of the lease term, the recognised right-of-use lease assets are depreciated on a straight line basis over the shorter of its estimated useful life and the lease term. Right-of-use lease assets are subject to impairment.

Lease liabilities

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments), less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees.

Note 26 Lease assets and liabilities (continued)

Accounting policy (continued)

The lease payments include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating a lease, if the lease term reflects the Group exercising the option to terminate.

The variable lease payments that do not depend on an index or a rate are recognised as an expense in the period in which the event or condition that triggers the payment occurs. In calculating the present value of lease payments, the Group uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Significant judgement in determining the lease term of contracts with renewal

The Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

The Group has the option, under some of its leases to lease the assets for additional terms. The Group applies judgement in evaluating whether it is reasonably certain to exercise the option to renew. That is, it considers all relevant factors that create an economic incentive for it to exercise the renewal. After the commencement date, the Group reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not exercise) the option to renew.

Note 27 Contingent liabilities, contingent assets and credit commitments

Warranties

Over the course of its corporate activity the Group has given, as a seller of companies and as a vendor of assets, including real estate properties, warranties to purchasers on several agreements that are still outstanding as at 30 June 2021. Other than noted below, at the date of this report no material claims against these warranties have been received by the Group.

Parent entity guarantees and undertakings

The Company has extended the following guarantees and undertakings to entities that form part of the Group:

1. a guarantee supporting the corporate banking facility and certain other financial commitments, such as hedging arrangements;
2. letters of support in respect of certain subsidiaries in the normal course of business. The letters recognise the Company's intention to provide support to those subsidiaries so that they can continue to meet their obligations;
3. Australian Financial Services Licence deeds of undertaking as an eligible provider; and
4. guarantees to support contractual commitments on warranties to certain third parties.

Third party guarantees

Bank guarantees have been issued by third party financial institutions on behalf of the Group and its subsidiaries for items in the normal course of business, such as rental contracts. The amounts involved are not considered to be material to the Group.

Contingent future commitments

CLC has made capital commitments to external counterparties for future investment opportunities such as development or investment purchases. As at 30 June 2021 there are potential future commitments totalling $867.9 million (30 June 2020: $419.7 million) in relation to these opportunities.

The Group has made capital commitments to associates to subscribe for up to $11.8 million (30 June 2020: $7.2 million) of non-redeemable preference shares to enable them to meet their working capital requirements. Contractual obligations for future property repairs and maintenance are in place but cannot be quantified until required.

On 23 December 2020, Challenger entered into an agreement to acquire MyLifeMyFinance Limited, an Australian-based customer savings and loans bank, for an acquisition price of $35.0 million. The acquisition price is subject to a completion adjustment and based on a net asset value of $18.0 million. Challenger has paid a deposit of $1.8 million with the remaining balance expected to be completely settled by August 2021.

Note 27 Contingent liabilities, contingent assets and credit commitments (continued)

Subsidiary guarantees

CLC has provided a guarantee to a third party regarding the performance of its subsidiary in respect of certain reinsurance arrangements.

Contingent tax assets and liabilities

From time to time the Group has interactions and matters under review, audit or dispute with the Australian Taxation Office in relation to the taxation treatments of various matters including reportable tax positions.

Any potential tax liability resulting from these interactions is only provided for when it is probable that an outflow will occur and a reliable estimate of the amount can be made. No specific contingent liability amounts have been disclosed in relation to these matters as it is considered that it would be prejudicial to their conduct and outcome.

Analysis of credit commitments	30 June 2021 $m	30 June 2020 $m
Contracted capital expenditure		
Amounts due in less than one year	2.6	18.7
Amounts due between one and two years	0.8	0.8
Amounts due between two and five years	2.9	—
Amounts due in greater than five years	7.3	—
Total capital expenditure commitments	**13.6**	**19.5**
Non-cancellable operating leases – Group as lessor		
Amounts due in less than one year	(219.8)	(221.0)
Amounts due between one and two years	(174.5)	(213.5)
Amounts due between two and five years	(412.8)	(511.3)
Amounts due in greater than five years	(784.3)	(954.3)
Total operating leases – Group as lessor	**(1,591.4)**	**(1,900.1)**
Other contracted commitments		
Amounts due in less than one year	—	6.2
Total other contracted commitments	**—**	**6.2**
Net commitments owed to Group	**(1,577.8)**	**(1,874.4)**

Other information

In the normal course of business, the Group enters into various contracts that could give rise to contingent liabilities in relation to performance obligations under those contracts. At the date of this report, the possibility of any outflow in settlement is remote.

Operating leases

Group as lessor

Investment properties owned by the Group are leased to third parties under operating leases. Lease terms vary between tenants and some leases include percentage rental payments based on sales volumes.

Contracted capital expenditure commitments

These represent amounts payable in relation to capital expenditure commitments contracted for at the Statement of financial position date but not recognised as liabilities. They primarily relate to the investment property portfolio and property, plant and equipment.

Other contracted commitments

This represents amounts payable in relation to fitout commitments and acquisition of investment properties that have exchanged prior to the balance date and will settle subsequent to the balance date.

Note 28 Employee entitlements

	30 June 2021 $m	30 June 2020 $m
Annual leave	8.4	7.8
Long service leave	9.9	9.4
Employee[1] entitlements provision	**18.3**	**17.2**

1 The total number of employees of the Group at 30 June 2021 was 738 (30 June 2020: 735) on a full-time equivalent (FTE) basis.

Accounting policy

Superannuation funds

Obligations for contributions to superannuation funds are recognised as an expense in the Statement of comprehensive income as they are incurred. The Group does not hold or pay into any defined benefit superannuation schemes on behalf of employees.

Wages, salaries, annual leave and non-monetary benefits

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled wholly within 12 months of the Statement of financial position date, are recognised in respect of employees' services up to the Statement of financial position date. They are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for accumulated sick leave are recognised when the leave is taken and are measured at the rates paid or payable.

Long service leave

A liability for long service leave is recognised as the present value of estimated future cash outflows to be made in respect of services provided by employees up to the Statement of financial position date. The estimated future cash outflows are discounted using yields from Australian corporate bonds which have durations to match, as closely as possible, the estimated future cash outflows. Factors which affect the estimated future cash outflows such as expected future salary increases, experience of employee departures and period of service, are included in the measurement.

Share-based payment transactions

Long-term equity-based incentive plan

The Group has an employee share incentive plan for the granting of non-transferable share rights to executives and senior employees. Shares in the Company held by the employee share trust are classified as Treasury shares and presented in the Statement of financial position as a deduction from equity.

Employees of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services in exchange for shares or rights over shares (equity-settled transactions).

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined using an option pricing model.

Share-based payment transactions (continued)

In accordance with Australian Accounting Standards, the cost of equity-settled transactions is recognised in the Statement of comprehensive income, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (vesting date).

At the Company level, the cost of Treasury shares is recognised as a reduction in equity. On vesting of the award they are subsequently recognised as an increase in equity and a reduction in share-based payment reserve at an average acquisition price.

The cumulative expense or investment recognised for equity-settled transactions at each Statement of financial position date reflects the extent to which the vesting period has expired and the best estimate of the number of awards that will ultimately vest.

No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date. This results in the share-based payment expense being recognised in the Statement of comprehensive income and an increase in equity being recognised even if the market performance conditions are not met at the vesting date and the share rights ultimately lapse.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled award is cancelled during the vesting period (other than an award cancelled when the vesting conditions are not satisfied), it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately.

However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award.

Note 28 Employee entitlements (continued)

Accounting policy (continued)

Employee share acquisition plan

Share-based compensation benefits are provided to employees via the Challenger Performance Plan (CPP). The Group has formed a trust to administer the Group's employee share acquisition plan (CPP Trust).

The CPP Trust is consolidated, as the substance of the relationship is that the trust is controlled by the Group.

Through contributions to the CPP Trust, the Group typically purchases shares in the Company on market. Shares acquired are held by the CPP Trust, are disclosed as Treasury shares and are deducted from contributed equity.

In addition to shares held by the CPP Trust, the Group has entered into forward purchase agreements (CPP deferred share purchases) to hedge unvested performance share rights. The CPP deferred share purchase agreements have exercise dates that broadly match the vesting dates of the performance rights issued by the CPP and they require the delivery of Challenger Limited shares to the CPP Trust, by a third party, for the contracted price. The shares to be purchased under these agreements are treated as Treasury shares from the date of the agreement.

In such deferred contracts, changes in the fair value arising from variations in market rates do not affect the amount of cash to be paid or the number of Challenger shares to be received, and these contracts are classified as equity instruments. Changes in the fair value of an equity instrument are not recognised in the financial statements. The liability to the third party is recorded on the balance sheet at present value and the discount is unwound through the Statement of comprehensive income over the duration of the contract.

Deferred Performance Share Rights (DPSRs)

This instrument is a performance right which gives a right to a fully-paid share in the Company at the end of the vesting period. The vesting period is typically between one and four years on existing awards.

The table below sets out the details of the DPSRs granted under the CPP during 2021 and movements on previous issues.

Grant date	Latest date for vesting[1]	Reference price $	Fair value at grant $	Outstanding at 1 July 2020	Granted during the year	Vested during the year	Expired during the year	Outstanding at 30 June 2021
7 Sep 2020	1 Sep 2024	4.010	3.35	—	339,587	—	(2,756)	336,831
7 Sep 2020	1 Sep 2023	4.010	3.50	—	339,587	—	(2,756)	336,831
7 Sep 2020	1 Sep 2022	4.010	3.67	—	534,315	—	(4,136)	530,179
7 Sep 2020	1 Sep 2021	4.010	3.84	—	552,996	—	(4,136)	548,860
11 Nov 2019	1 Sep 2023	6.633	7.87	15,377	—	—	—	15,377
11 Nov 2019	1 Sep 2022	6.633	7.55	15,377	—	—	—	15,377
11 Nov 2019	1 Sep 2021	6.633	7.23	23,065	—	—	—	23,065
11 Nov 2019	1 Sep 2020	6.633	6.94	23,065	—	(23,065)	—	—
9 Sep 2019	1 Sep 2023	6.633	5.93	201,696	—	—	(1,015)	200,681
9 Sep 2019	1 Sep 2022	6.633	6.19	201,696	—	—	(1,015)	200,681
9 Sep 2019	1 Sep 2021	6.633	6.45	302,572	—	—	(1,523)	301,049
9 Sep 2019	1 Sep 2020	6.633	6.73	302,573	—	(302,573)	—	—
11 Sep 2018	1 Sep 2021	10.368	9.66	352,306	—	—	(13,501)	338,805
11 Sep 2018	1 Sep 2020	10.368	9.94	355,854	—	(355,854)	—	—
11 Sep 2017	1 Sep 2020	12.264	11.39	289,229	—	(287,191)	(2,038)	—
Total				**2,082,810**	**1,766,485**	**(968,683)**	**(32,876)**	**2,847,736**

[1] At the date of vesting, fully-paid shares are transferred to the individual and released from the CPP Trust.

Note 28 Employee entitlements (continued)

Accounting policy (continued)

Hurdled Performance Share Rights (HPSRs)

This instrument is a performance share right that gives a right to a fully-paid share in the Company at certain vesting dates, subject to the achievement of performance conditions based on total shareholder returns (TSR). The HPSRs are awarded based on a range of criteria reflecting, in addition to current year performance, the longer-term ability for an employee to add significant value to Challenger and for retention purposes. The award of HPSRs ensures longer-term alignment of interests between Challenger and its employees.

For grants made between 1 July 2015 and 30 June 2020, subject to continued employment and meeting the absolute TSR performance target, two-thirds of a HPSR award will be eligible to commence vesting on the third anniversary and the final third on the fourth anniversary following grant. For grants from 1 July 2019, subject to continued employment and meeting the absolute TSR performance target, a HPSR award is eligible to commence vesting on the fourth anniversary and is subject to a final cumulative test on the fifth anniversary. This change has the effect of increasing the vesting period.

To the extent that the absolute TSR performance targets are not satisfied for a particular tranche of award, unvested HPSRs have the opportunity to vest at the end of the following tranche's vesting period, subject to the higher absolute TSR performance requirements which reflect another year of compound growth. Unvested awards have the opportunity to vest on the fifth anniversary following grant. Any unvested awards lapse at the end of the fifth anniversary following grant. This approach is applied to ensure that Key Management Personnel and employees are motivated to deliver strong long-term performance. HPSRs are converted to ordinary fully paid shares upon vesting.

The table below sets out details of the HPSRs granted under the CPP during 2021 and movements on previous issues:

Grant date	Expected date for vesting[1]	Reference price $	Fair value at grant $	Outstanding at 1 July 2020	Granted during the year	Vested during the year	Expired during the year	Outstanding at 30 June 2021
10 May 2021	1 Sep 2024	4.497	2.64	—	132,848	—	—	132,848
2 Nov 2020	1 Sep 2024	4.497	2.58	—	848,268	—	—	848,268
7 Sep 2020	1 Sep 2024	4.497	1.87	—	6,511,001	—	(589,563)	5,921,438
9 Dec 2019	1 Sep 2023	6.729	4.22	432,483	—	—	—	432,483
11 Nov 2019	1 Sep 2023	6.729	4.42	90,618	—	—	—	90,618
9 Sep 2019	1 Sep 2023	6.729	3.10	3,187,371	—	—	(387,079)	2,800,292
11 Sep 2018	1 Sep 2022	11.720	3.94	680,175	—	—	(107,489)	572,686
11 Sep 2018	1 Sep 2021	11.720	4.56	1,175,334	—	—	(185,741)	989,593
11 Sep 2017	1 Sep 2021	12.732	5.42	552,924	—	—	(76,416)	476,508
11 Sep 2017	1 Sep 2020	12.732	6.11	980,933	—	—	(135,566)	845,367
12 Sep 2016	1 Sep 2020	9.017	3.80	698,334	—	—	(98,681)	599,653
12 Sep 2016	1 Sep 2019	9.017	4.33	1,225,732	—	—	(173,207)	1,052,525
13 Sep 2015	1 Sep 2019	7.013	2.84	820,577	—	—	(820,577)	—
Total				**9,844,481**	**7,492,117**	**—**	**(2,574,319)**	**14,762,279**

1 At the date of vesting, fully-paid shares are transferred to the individual and released from the CPP Trust.

Note 28 Employee entitlements (continued)

Key estimates and assumptions

Share-based payments

The Group measures the cost of equity-settled transactions with employees granted during the year by reference to the fair value of the share rights at the date at which they are granted. The fair values are determined by independent external valuers using a Black-Scholes model for DPSRs and a Monte Carlo simulation model for HPSRs which utilises the TSR share price hurdles. Key inputs into the valuation models for equity awards granted during the year are as follows:

Input	7 Sep 2020 PSR DPSR[1]	7 Sep 2020 HPSR DPSR[1]	2 Nov 2020 HPSR HPSR[1]	10 May 2020 HPSR HPSR[1]
Dividend yield (%)	4.6	4.6	4.6	4.6
Risk-free rate (%)	0.26-0.44	0.26-0.44	0.11-0.28	0.08-0.67
Volatility[2] (%)	N/A	43	43	44
Valuation ($)	3.84 - 3.35	1.87	2.58	2.64

1 Staggered deferred vesting applies to these grants.
2 Forecast volatility rate implied from historic trend.

Note 29 Remuneration of auditor

Amounts received or due and receivable by Ernst & Young (Australia) relating to:	30 June 2021 $	30 June 2020 $
Full year audit and half year review of the Group financial report	1,896,553	1,928,488
Other audit services – audit and review of trusts and funds	574,733	525,568
Other assurance services	843,358	633,388
Other services in relation to the Group		
– taxation services	74,000	157,500
– other assurance services	—	45,000
	3,388,644	**3,289,944**
Amounts received or due and receivable by other overseas member firms of Ernst & Young (Australia) for:		
Fees for auditing the financial report of any controlled entities	416,795	391,810
Other services in relation to the Group		
– taxation services	68,000	90,238
	484,795	**482,048**
Total auditor remuneration[1]	**3,873,439**	**3,771,992**

1 Auditor's remuneration for the Group is paid by Challenger Group Services Limited, a wholly owned entity within the Group.

Note 30 Subsequent events

On 23 December 2020, Challenger agreed to acquire 100% of MyLifeMyFinance Limited, an Australian-based customer digital bank, for $35.0 million. The acquisition price is subject to a completion adjustment and is based on a net asset value of $18.0 million. Provisional Goodwill on acquiring the business is estimated to be approximately $17.0 million and may be subsequently adjusted in accordance with the requirements of AASB 3 *Business Combinations*. The acquisition received formal approval from the Treasurer of the Commonwealth of Australia on 29 July 2021 and was completed on 30 July 2021.

The acquisition is highly strategic and provides Challenger the opportunity to significantly expand its secure retirement income offering, including entering Australia's term deposit market. In the 2022 financial year, the Bank will represent a third operating segment of the Group.

At the date of this financial report no other matter or circumstance has arisen that has, or may, significantly affect the Group's operations, the results of those operations or the Group's state of affairs in future financial years which has not already been reflected in this report.

Directors' declaration

In accordance with a resolution of the Directors of Challenger Limited, we declare that, in the opinion of the Directors:

a) the financial statements and notes of Challenger Limited and its controlled entities (the Group) are in accordance with the ***Corporations Act 2001*** (Cth), including:

   (i) giving a true and fair view of the Group's financial position as at 30 June 2021 and of its performance for the year ended on that date; and

   (ii) complying with Australian Accounting Standards and the ***Corporations Regulations 2001*** (Cth);

b) the financial statements and notes of the Group also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board, which is disclosed in Section 1(i) Basis of preparation and statement of compliance;

c) there are reasonable grounds to believe that the Group will be able to pay its debts as and when they become due and payable; and

d) this declaration has been made after receiving the declarations required to be made to the Directors from the Chief Executive Officer and Chief Financial Officer in accordance with section 295A of the ***Corporations Act 2001*** (Cth) for the financial year ended 30 June 2021.

On behalf of the Board

P Polson
Independent Chair

9 August 2021

R Howes
Managing Director and Chief Executive Officer

9 August 2021

Ernst & Young
200 George Street
Sydney NSW 2000 Australia
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Independent auditor's report to the shareholders of Challenger Limited

Report on the Audit of the Financial Report

Opinion

We have audited the financial report of Challenger Limited (the Company) and its subsidiaries (collectively the Group), which comprises the consolidated statement of financial position as at 30 June 2021, the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the ***Corporations Act 2001***, including:

a) giving a true and fair view of the consolidated financial position of the Group as at 30 June 2021 and of its consolidated financial performance for the year ended on that date; and
b) complying with Australian Accounting Standards and the ***Corporations Regulations 2001***.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the ***Auditor's Responsibilities for the Audit of the Financial Report*** section of our report. We are independent of the Group in accordance with the auditor independence requirements of the ***Corporations Act 2001*** and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 ***Code of Ethics for Professional Accountants (including Independence Standards)*** (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the ***Auditor's Responsibilities for the Audit of the Financial Report*** section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

1 Valuation of Life Contract Liabilities

Financial report reference: **Note 8**

Why significant to the audit	How our audit addressed the key audit matter
The Group recognised a provision for future claims associated with life insurance policies. The valuation methodology to estimate the provision adopted by the Group involves complex and subjective judgments about future events. Key assumptions used in the Group's model to determine the value of the life contract liabilities include: • Discount rates • Inflation • Future claims administration expenses • Mortality rates and redemptions These assumptions, along with policy information, are used as inputs to the Group's model to calculate the Life Contract Liabilities. This was a key audit matter due to the value of the balance (30 June 2021: $13,669.9 million), relative to total liabilities and the degree of judgment and estimation uncertainty associated with the valuation.	Our audit procedures involved an assessment of the effectiveness of relevant controls over assumptions and policy information used as inputs into the Group's model. Our IT specialists were involved to assess whether policy information was extracted accurately from the Group's underlying administration system into the valuation process. Our audit procedures included the following in the evaluation of the assumptions used by the Group: • Considered the Group's governance process and controls to determine the methodology and assumptions. • Assessed the results of the experience investigations carried out by the Group to determine whether they supported the assumptions used by the Group. • Assessed the movements in modelled profit margins and best estimate liabilities for insurance risk transactions. • Performed a recalculation for a sample of the life contract liability valuations. Where appropriate, we involved our life insurance actuarial specialists in the above procedures and overall assessment of the valuation methodology, key assumptions and models deriving the valuation of the life contract liabilities. We assessed the adequacy of the related financial report disclosures.

2 Valuation of Level 3 Non-Property Investment Assets

Financial report reference: **Note 19**

Why significant to the audit	How our audit addressed the key audit matter
The Group holds a portfolio of assets carried at fair value, for which an observable market value is not readily available. These assets are classified as Level 3 assets within the fair value hierarchy of the financial report. Level 3 assets require judgment to be applied in determining their fair value, as the valuation inputs for these assets are not based on observable market transactions or other readily available market data. The Group exercised judgment to arrive at their best estimates of fair value of these assets. There is complexity in this process, as well as uncertainty associated with the valuation and modelling methodologies and the assumptions adopted. This was a key audit matter due to the value of the balance relative to total assets (30 June 2021: $5,852.9 million), and the degree of judgment and estimation uncertainty associated with the valuation.	The valuation of Level 3 assets is inherently subjective given that there are alternative assumptions and valuation methods that may result in a range of values. Our audit procedures included the following, using sampling techniques: • Considered the Group's controls over the valuation of Level 3 assets. • Tested the mathematical accuracy of the valuation models and consistency with the Group's documented methodology and assumptions. • Our valuation specialists assessed the Group's valuation and modelling methodologies and assessed the key judgmental inputs used in the year-end valuations, including the discount rate and the terminal value. • Obtained valuation statements provided by external investments managers in respect of unit trusts and alternate funds. We assessed the valuations of investments as provided by external investment managers, including an assessment of the reliability of the information received and the appropriateness of the underlying valuation method. We assessed the adequacy and appropriateness of the related financial report disclosures.

3 Valuation of Level 3 Property Investment Assets

Financial report reference: **Note 6**

Why significant to the audit

The Group owns a diversified portfolio of investment property assets. The carrying value of investment properties is measured at the fair value of each property, which is assessed by the directors with reference to external independent property valuations and based on market conditions existing at the reporting date.

The fair value of investment property is inherently subjective and impacted by factors such as prevailing market conditions, its geographic location, expected future income and the characteristics and attributes of the subject property.

As at 30 June 2021 there is significant valuation uncertainty arising from the COVID-19 pandemic and the response of Governments to it. This means that the property values may change significantly and unexpectedly over a relatively short period of time.

Given the market conditions at balance date, a number of independent valuers have reported on the basis of the existence of 'material valuation uncertainty', noting that less certainty, and a higher degree of caution, should be attached to the valuations than would normally be the case. In this situation the disclosures in the financial statements provide particularly important information about the assumptions made in the property valuations and the market conditions at 30 June 2021.

We have considered this a key audit matter due to the number of judgments required in determining fair value and the value of the balance relative to total assets (30 June 2021: $3,389.7 million).

How our audit addressed the key audit matter

The valuation of investment properties is inherently subjective given that there are alternative assumptions and valuation methods that may result in a range of values. The impact of COVID-19 at 30 June 2021 has resulted in a wider range of possible values than at past valuation points.

Our audit procedures included the following:

- We assessed the following matters with management:
- movements in the Group's investment property portfolio;
- changes in the condition of selected properties;
- controls in place relevant to the valuation process; and
- the impact that COVID-19 has had on the Group's investment property portfolio including rent abatements offered to tenants and tenant occupancy risk arising from changes in the estimated lease renewals.
- We performed the following procedures for selected properties, using sampling techniques:
- Evaluated the key assumptions and agreed key inputs to tenancy schedules. These assumptions and inputs included market and contractual rent, occupancy rates including forecast occupancy levels, forecast rent, lease terms, re-leasing costs, operating expenditure and future capital expenditure. We assessed the effectiveness of relevant controls over the leasing process and associated tenancy reports which are used as source data in the property valuations by testing a sample of the relevant controls.
- Assessed whether COVID-19 relief provided to tenants had been factored into the valuations and that changes in tenant occupancy risk were also considered.
- Where relevant we compared the valuation against comparable transactions utilised in the valuation process.
- Evaluated the suitability of the valuation methodology across the portfolio based on the type of asset. We considered the reports of the independent valuers to gain an understanding of the assumptions and estimates used and the valuation methodology applied. This included the impact that COVID-19 has had on key assumptions such as the capitalisation, discount or growth rate and future forecast rentals. We have also considered and responded to restrictions imposed on the valuation process, if any, and the market conditions at balance date.

Where appropriate, we involved our real estate valuation specialists in the above procedures.

We assessed the adequacy and appropriateness of the related financial report disclosures, in particular those relating to the valuation uncertainty.

4 Recoverability of Goodwill

Financial report reference: **Note 25**

Why significant to the audit	How our audit addressed the key audit matter
Goodwill has been recognised as a result of the Group's historical acquisitions, representing the excess of the purchase consideration over the fair value of assets and liabilities acquired. On acquisition date, the goodwill has been allocated to the applicable Cash Generating Units (CGUs). An impairment assessment is performed at each reporting period, comparing the carrying amount of each CGU containing goodwill with its recoverable amount. The recoverable amount of each CGU is determined on a value in use basis. This calculation incorporates a range of assumptions, including future cash flows, discount rate and terminal growth rate. This was a key audit matter due to the value of Goodwill relative to total assets (30 June 2021: $579.9 million), and the degree of judgment and estimation uncertainty associated with the impairment assessment.	Our audit procedures included the following: • Assessed the valuation methodology used to calculate the recoverable amount of each CGUs. • Agreed the projected cash flows used in the impairment models to the Board approved five-year plan of the Group. • Compared the Group's implied growth rate assumption to comparable companies. • Considered the accuracy of historical cash flow forecasts. • Assessed the methodology and assumptions used in the calculation of the discount rate, including comparison of the rate to market benchmarks. • Tested the mathematical accuracy of the impairment model for each CGU. • Considered the carrying amount of the net assets of the Group against its market capitalisation at 30 June 2021 and subsequent to year end up to the date of our opinion. • Considered the Group's sensitivity analysis and evaluated whether any reasonably foreseeable change in assumptions could lead to a material impairment. Our valuation specialists were involved in the above procedures where appropriate. We assessed the Group's determination of the CGUs to which goodwill is allocated and the adequacy of the related financial report disclosures.

Information Other than the Financial Report and Auditor’s Report Thereon

The directors are responsible for the other information. The other information comprises the information included in the Company’s 2021 Annual Report, but does not include the financial report and our auditor’s report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon, with the exception of the Remuneration Report and our related assurance opinion.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the Group’s ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group’s internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors’ use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated to the directors, we determine those matters that were of most significance in the audit of the financial report of the current year and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on the Audit of the Remuneration Report

Opinion on the Remuneration Report

We have audited the Remuneration Report included in pages 42 to 51 of the Directors' report for the year ended 30 June 2021.

In our opinion, the Remuneration Report of Challenger Limited for the year ended 30 June 2021, complies with section 300A of the *Corporations Act 2001*.

Responsibilities

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the ***Corporations Act 2001***. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Ernst & Young

T Johnson
Partner

Sydney
9 August 2021

G McKenzie
Partner

Sydney
9 August 2021

Investor information

Substantial shareholders

The number of shares held by substantial shareholders and their associates, based on the latest substantial shareholder notifications, and the 20 largest individual shareholders are as follows:

Substantial shareholders as at 31 July 2021	Number of shares	% of issued capital
Apollo Global Management, Inc. / Athene Life Reinsurance Ltd[1]	121,858,736	18.02
MS&AD Insurance Group Holdings Inc	98,633,303	14.59
Allan Gray Australia Pty Ltd and its related bodies	33,836,621	5.00
20 largest individual shareholders as at 31 July 2021		
1. Citicorp Nominees Pty Limited	156,899,769	23.21
2. J P Morgan Nominees Australia Pty Limited	128,955,594	19.07
3. HSBC Custody Nominees (Australia) Limited	123,303,301	18.24
4. HSBC Custody Nominees (Australia) Limited <Euroclear Bank SA NV A/C>	50,432,547	7.46
5. National Nominees Limited	16,406,498	2.43
6. UBS Nominees Pty Limited	13,529,545	2.00
7. CS Third Nominees Pty Limited <HSBC Cust Nom Au Limited 13 A/C>	7,561,457	1.12
8. Argo Investments Limited	5,440,311	0.80
9. BNP Paribas Noms Pty Limited <DRP>	4,675,881	0.69
10. BNP Paribas Nominees Pty Limited <Agency Lending DRP A/C>	3,568,245	0.53
11. Australian United Investment Company Limited	2,310,000	0.34
12. National Nominees Limited <N A/C>	1,965,270	0.29
13. BNP Paribas Nominees Pty Limited Six Sis Limited <DRP A/C>	1,696,429	0.25
14. Citicorp Nominees Pty Limited <Colonial First State Inv A/C>	1,460,598	0.22
15. HSBC Custody Nominees (Australia) Limited - A/C 2	1,455,857	0.22
16. Sandhurst Trustees Limited <Endeavor Asset Mgmt Mda A/C>	1,418,830	0.21
17. CPU Share Plans Pty Limited <CGF Performance Plan A/C>	1,389,083	0.21
18. BNP Paribas Nominees Pty Limited Hub24 Custodial Serv Limited <DRP A/C>	1,021,794	0.15
19. BNP Paribas Noms (Nz) Limited <DRP>	996,821	0.15
20. HSBC Custody Nominees (Australia) Limited <NT-Comnwlth Super Corp A/C>	972,788	0.14
Total 20 largest individual shareholders – issued capital	**525,460,618**	**77.73**
Total remaining shareholders balance	**150,595,874**	**22.27**

[1] 3% of this shareholding is subject to to regulatory approval.

Distribution of shares (as at 31 July 2021)

Range	Number of shareholders	Number of shares	% of issued capital
1 – 1,000	18,662	8,639,030	1.28
1,001 – 5,000	17,207	42,048,904	6.22
5,001 – 10,000	3,824	27,819,275	4.11
10,001 – 100,000	2,502	52,027,578	7.70
100,001 and over	98	545,521,705	80.69
Total	**42,293**	**676,056,492**	**100.00**

Unmarketable parcels	Minimum parcel size	Holders	Units
Minimum $500.00 parcel at $5.69 per unit	88	1,561	58,951

ASX listing

Challenger Limited shares are listed on the ASX under code CGF. Share price details and company information can be accessed via either the Company website:

› **challenger.com .au**

or the ASX website:

› **asx.com.au**

Voting rights

On a show of hands, every member present at the meeting in person or by proxy shall have one vote and upon a poll each share shall have one vote.

Investor information (continued)

Buy-back

There is currently no market buy-back.

On market acquisitions for employee incentive schemes during the financial year ended 30 June 2021

No Challenger Limited ordinary shares were purchased on market to satisfy entitlements under Challenger's employee incentive schemes.

Top 20 noteholders of Challenger Capital Notes 1 as at 31 July 2021

20 largest individual noteholders as at 31 July 2021		Number of notes	% of issued notes
1.	HSBC Custody Nominees (Australia) Limited	27,378	9.87
2.	Australian Executor Trustees Limited <IPS Super A/C>	22,303	8.04
3.	Strong Motorcycles Pty Limited <Coffrefort Super Fund A/C>	12,555	4.53
4.	Aurisch Investments Pty Limted	10,000	3.61
5.	Estate Late Frances Claire Fox <Thomas J Beresford Will A/C>	10,000	3.61
6.	BNP Paribas Nominees Pty Limted Hub24 Custodial Serv Limted <Drp A/C>	7,982	2.88
7.	Nulis Nominees (Australia) Limited <Navigator Mast Plan Sett A/C>	7,389	2.66
8.	Australian Executor Trustees Limited <IPS Idps A/C>	7,355	2.65
9.	Navigator Australia Limted <MLC Investment Sett A/C>	6,403	2.31
10.	Netwealth Investments Limited <Wrap Services A/C>	6,146	2.22
11.	Vincentcare Victoria	6,000	2.16
12.	Australian Executor Trustees Limited <IPS Ioof Employer Super A/C>	5,626	2.03
13.	Mrs Connie Joan Folino + Mr Frank William Folino + Francon Investments Pty Limted	5,000	1.80
14.	J P Morgan Nominees Australia Pty Limited	3,766	1.36
15.	Netwealth Investments Limited <Super Services A/C>	3,729	1.34
16.	Pakvasa Consultants Pty Limted <Superannuation A/C>	3,200	1.15
17.	Bond Street Custodians Limited <Dtome - F01938 A/C>	3,100	1.12
18.	Futong Nominees Pty Limted <Fu Tong Super Fund A/C>	2,790	1.01
19.	Banyule Community Health	2,500	0.90
20.	Simone Neal Superannuation Nominees Pty Limted <Simone Neal Superan A/C>	2,500	0.90
Total 20 largest individual noteholders – issued notes		**155,722**	**56.15**
Total remaining noteholders balance		**121,658**	**43.85**

Distribution of notes (as at 31 July 2021)

Range	Number of holders	Number of notes	% of notes
1 – 1,000	297	89,437	32.24
1,001 – 5,000	27	58,806	21.20
5,001 – 10,000	9	66,901	24.12
10,001 – 100,000	3	62,236	22.44
100,001 and over	0	0	0.00
Total	**336**	**277,380**	**100.00**

Unmarketable parcels	Minimum parcel size	Holders	Units
Minimum $500.00 parcel at $100.655 per unit	5	—	—

Investor information (continued)

Top 20 noteholders of Challenger Capital Notes 2 as at 31 July 2021

20 largest individual noteholders as at 31 July 2021		Number of notes	% of issued notes
1.	HSBC Custody Nominees (Australia) Limited	395,627	8.60
2.	J P Morgan Nominees Australia Pty Limited	176,891	3.85
3.	BNP Paribas Nominees Pty Limited Hub24 Custodial Serv Limited <DRP A/C>	168,807	3.67
4.	Australian Executor Trustees Limited <IPS Super A/C>	96,667	2.10
5.	Citicorp Nominees Pty Limited	72,130	1.57
6.	National Nominees Limited	63,046	1.37
7.	Netwealth Investments Limited <Wrap Services A/C>	59,639	1.30
8.	Taverners No 11 Pty Limited <Brencorp No 11 Unit A/C>	54,689	1.19
9.	BNP Paribas Nominees Pty Limited <Pitcher Partners Drp>	54,109	1.18
10.	Navigator Australia Limited <JB Were List Fix Int Sma A/C>	51,447	1.12
11.	Mutual Trust Pty Limited	48,700	1.06
12.	Navigator Australia Limited <MLC Investment Sett A/C>	43,507	0.95
13.	Australian Executor Trustees Limited <IPS IDPS A/C>	31,447	0.68
14.	Trustees Of Church Property For The Diocese Of Newcastle <Savings & Development A/C>	29,270	0.64
15.	Nulis Nominees (Australia) Limited <Navigator Mast Plan Sett A/C>	28,205	0.61
16.	HSBC Custody Nominees (Australia) Limited - A/C 2	27,396	0.60
17.	Lbl Investment Pty Limited <L&B Family A/C>	24,700	0.54
18.	Certane Ct Pty Limited <Charitable Foundation>	23,129	0.50
19.	Australian Executor Trustees Limited <IPS IOOF Employer Super A/C>	21,223	0.46
20.	G C F Investments Pty Limited	20,000	0.43
Total 20 largest individual noteholders – issued notes		**1,490,629**	**32.42**
Total remaining noteholders balance		**3,109,371**	**67.58**

Distribution of notes (as at 31 July 2021)

Range	Number of holders	Number of notes	% of notes
1 – 1,000	4,969	1,576,278	34.27
1,001 – 5,000	517	1,120,320	24.35
5,001 – 10,000	31	235,044	5.11
10,001 – 100,000	30	927,033	20.15
100,001 and over	3	741,325	16.12
Total	**5,550**	**4,600,000**	**100.00**

Unmarketable parcels	Minimum parcel size	Holders	Units
Minimum $500.00 parcel at $103.30 per unit	5	4	5

Investor information (continued)

Top 20 noteholders of Challenger Capital Notes 3 as at 31 July 2021

20 largest individual noteholders as at 31 July 2021		Number of notes	% of issued notes
1.	HSBC Custody Nominees (Australia) Limited	485,867	12.62
2.	J P Morgan Nominees Australia Pty Limited	394,282	10.24
3.	BNP Paribas Nominees Pty Limited Hub24 Custodial Serv Limited <DRP A/C>	111,785	2.90
4.	BNP Paribas Nominees Pty Limited <Pitcher Partners DRP>	104,627	2.72
5.	Diocese Development Fund - Catholic Diocese Of Parramatta	76,177	1.98
6.	Citicorp Nominees Pty Limited	52,288	1.36
7.	National Nominees Limited	48,069	1.25
8.	Eastcote Pty Limited <Van Lieshout Family A/C>	41,600	1.08
9.	Mutual Trust Pty Limited	40,494	1.05
10.	Australian Executor Trustees Limited <IPS Super A/C>	40,246	1.05
11.	Netwealth Investments Limited <Wrap Services A/C>	32,608	0.85
12.	Sandhurst Trustees Limited <Endeavor Asset Mgmt Mda A/C>	26,140	0.68
13.	BNP Paribas Nominees Pty Limited <IB AU Noms Retailclient DRP>	24,554	0.64
14.	MF Investments No 1 Pty Limited	21,493	0.56
15.	GCF Investments Pty Limited	20,000	0.52
16.	270 King Street Pty Limited	17,600	0.46
17.	Netwealth Investments Limited <Super Services A/C>	17,463	0.45
18.	BNP Paribas Noms Pty Limited <DRP>	17,206	0.45
19.	Certane Ct Pty Limited <Ect Cap Stbl Fnd>	16,939	0.44
20.	Nulis Nominees (Australia) Limited <Navigator Mast Plan Sett A/C>	16,681	0.43
Total 20 largest individual noteholders – issued notes		**1,606,119**	**41.73**
Total remaining noteholders balance		**2,243,881**	**58.27**

Distribution of notes (as at 31 July 2021)

Range	Number of holders	Number of notes	% of notes
1 – 1,000	3,356	1,137,274	29.54
1,001 – 5,000	377	774,318	20.11
5,001 – 10,000	28	200,094	5.20
10,001 – 100,000	26	641,753	16.67
100,001 and over	4	1,096,561	28.48
Total	**3,791**	**3,850,000**	**100.00**

Unmarketable parcels	Minimum parcel size	Holders	Units
Minimum $500.00 parcel at $103.30 per unit	5	3	9

ASX listing

Challenger Capital Notes 1 are listed on the ASX under the trade symbol CGFPA. Challenger Capital Notes 2 are listed on the ASX under the trade symbol CGFPB. Challenger Capital Notes 3 are listed on the ASX under the trade symbol CGFPC. Note price details can be accessed via the ASX website:

› **asx.com.au**

Voting rights

Challenger Capital Notes 1, 2 and 3 do not confer any voting rights in the Company but if they are exchanged or converted for ordinary shares in accordance with their terms of issue, then the voting rights of the ordinary shares will be the same as for ordinary shares.

Shareholder queries

For any administrative matters in respect of your Challenger Limited shareholding or noteholding, please contact the Company's share registrar, Computershare:

Computershare Investor Services Pty Limited

Level 3, 60 Carrington Street, Sydney NSW 2000

Telephone: 1800 780 782

Website: › **computershare.com.au**

To assist with all enquiries, please quote your unique Security Reference Number (SRN) and your current address when dealing with Computershare.

Additional information

Principal place of business and registered office in Australia

Level 2
5 Martin Place
Sydney NSW 2000

Telephone: 02 9994 7000
Facsimile: 02 9994 7777

Investor services: 13 35 66

Directors

Peter Polson (Chair)
Richard Howes (Managing Director and Chief Executive Officer)
John M Green
Steven Gregg
Masahiko Kobayashi
Heather Smith
JoAnne Stephenson
Duncan West
Melanie Willis

Company secretary

Linda Matthews

Website

> **challenger.com.au**

Manage your shareholding at Computershare Investor Services

Computershare Investor Services Pty Limited
Level 3, 60 Carrington Street
Sydney NSW 2000
Telephone: 02 8234 5000

> **computershare.com.au**

Auditor

Ernst & Young
200 George Street
Sydney NSW 2000

Go electronic

Challenger can deliver all of your shareholder communications electronically, by updating your details via Computershare Investor Services.

Online digital version of this report

The 2021 Annual Report is available at:

> **challenger.com.au/annualreport2021**

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