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St. James's Place U.K. PLC

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St. James's Place U.K. PLC

SACP* Assessments				SACP*		Support		Ratings
Anchor	a-	Modifiers	0	a-		0		Financial Strength Rating
Business Risk		ERM and Management	0	Liquidity	0	Group Support	0	A-/Stable/--
Satisfactory								
Financial Risk		Holistic Analysis	0	Sovereign Risk	0	Gov't Support	0	
Strong								

*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Rationale

Business Risk Profile: Satisfactory

- We assess insurance industry and country risk as low for the U.K. life sector. St. James's Place PLC's (SJP) sales are almost exclusively in the U.K. life market.
- Competitive position is adequate reflecting SJP's robust position in a relatively narrow product segment, notably unit-linked pensions and savings.

Financial Risk Profile: Strong

- Risk-based capital adequacy appears extremely strong when modelled, but our overall assessment of capital and earnings is strong. Our view is tempered by the modest size of the capital base, quality of capital given substantial implicit items, and exposure to operational risks that our risk-based capital model may not adequately capture.
- We consider SJP's risk position as low risk due to the group's conservative management of its liability profile and shareholder assets.
- SJP possesses adequate financial flexibility based on our view of the group's limited capital needs and largely debt-free balance sheet.

Other Factors

- We consider management and governance to be satisfactory, reflecting the stability in the management team and its good track record in managing the business through the cycle.
- We consider liquidity to be exceptional given the degree to which shareholder assets are invested in highly liquid assets.

Outlook: Stable

The stable outlook reflects our view that SJP has sufficient competitive advantages within the wealth management sector to maintain growing sales and earnings despite a market which continues to move through a period of significant regulatory change.

Upside scenario

We are unlikely to raise the ratings on SJP over the next two years given the relative narrowness of the product profile and the resulting susceptibility to potential industry or regulatory change. At this stage we do not envisage current growth initiatives in Asia Pacific to be material enough to broaden the group's overall business profile.

Downside scenario

We may lower the ratings if:

- We believe that SJP is unable to maintain its competitive position as a result of regulatory change or increased competition in its core market segment;
- Retention rates as a percentage of average funds under management (FUM) fall to less than 90% or net flows turn negative, which could indicate a weakening in the business model; or
- The group's capital structure weakens due to greater leverage of the balance sheet, and if the fixed charge coverage ratio is below 4x.

Base-Case Scenario

Macroeconomic Assumptions

- We expect U.K. real GDP growth of 2.7% in 2014 falling to 2.4% in 2015. Where GDP growth is accompanied by confidence in the capital markets we expect this will help to support SJP's volumes and earnings.
- SJP has limited interest rate sensitivity compared to many life insurance peers, but we expect average interest rates over 2014 and 2015 on 10 year gilt yields will be 3.2% and 3.3%, respectively.

Company-Specific Assumptions

- Growth in number of tied agents: We expect the growth in the number of SJP's tied agents or "Partners" (2013 year-end: 1,958) to slow through 2014 toward historic norms of about 5%-6% per year.
- New business margins: We expect that SJP's new business margins will remain strong at over 4%.
- Net inflows: Net inflows will continue to grow by over 12% a year for the next two years, but we believe there may be a slowdown as competitors turn their focus to this segment.
- Capital adequacy: We expect SJP to continue to manage its capital adequacy at, or close to, the 'AAA' level despite our expectation of a significant increase in the dividend.
- Dividend pay-out ratio: Our expectation is that the pay-out ratio will increase to between 70%-80% of net income.
- Investments: We expect that SJP's shareholder assets will continue to be conservatively managed in a combination of 'AAA' money market funds, gilts or banks which we judge as highly systemically important.
- Financial flexibility: We do not expect any financial leverage. Borrowings will be operational leverage used to fund the network of tied agents.

Key Metrics

	2015F	2014F	2013	2012	2011
Net inflows (£ bil.)	>5.3	>4.8	4.3	3.35	3.21
Life new business margin (%)	>4.0	>4.0	4.5	4.7	4.5
Fixed charge coverage	>8x	>8x	N.M.	N.M.	N.M.

F--Forecast. N.M.--Not meaningful.

Company Description

SJP is a U.K.-based wealth manager. It focuses on customers with investable wealth of £50,000 to £5 million. As of March 31, 2014, SJP has FUM of £45.8 billion.

SJP's business model is an outsourced one, with the group providing close management and oversight. SJP distributes its unit-linked pensions and savings products exclusively through a network of tied agents called Partners. As of Dec. 31, 2014, the number of Partners was 1,958; up 9.5% on the prior year. The products that SJP sells are invested in funds, which are externally managed by a broad range of providers selected with the help of external consultants, Stamford Associates. The administration of the products is also outsourced to third parties.

Business Risk Profile: Satisfactory

We consider SJP's business profile to be satisfactory. The group achieves robust new business margins in a relatively narrow spectrum of products in the U.K. life insurance market.

Insurance industry and country risk: Majority of sales in the U.K.

SJP is exposed to the U.K. life insurance market, which we assess as having low industry and country risk, based on our view of its very low country risk and intermediate industry risk. Our view is supported by our positive opinion of the institutional framework and the sector's strong track record of minimizing asset-liability mismatch. We consider the sector to be highly competitive, but believe that it nevertheless maintains moderate levels of profitability.

We believe that the impact of the announcements made in the recent Budget will be limited for SJP. The group does not sell annuities. Where policyholders choose to defer the decision to purchase an annuity with another provider, or opt for a draw-down product, this provides scope for the assets to remain invested with SJP for longer. Increases in ISA limits will also provide an opportunity for SJP to increase its FUM.

Competitive position: Successful in overcoming challenges posed by the Retail Distribution Review

We consider SJP's competitive position to be adequate. SJP uses its network of tied agents to achieve robust new margins, given the low risk profile of the product. We anticipate new business margins on a present value of new business premiums basis to remain in excess of 4%. Overall, our assessment of SJP's competitive position is constrained by the narrowness of the business model. As a result, the group is more susceptible to industry, regulatory and reputational risks than peers.

SJP, in contrast to many other players selling savings and investment products, has managed to maintain volumes through the implementation of the Retail Distribution Review (RDR). The RDR required a significant change in business model for many intermediaries as customers were obliged to pay up-front for their investment advice. SJP positioned its advisor base well for this challenge and saw a limited number of Partners leave the organization as a result of the requirement to sit specialist exams. Net inflows of £4.1 billion in 2013 were up 28% on 2012.

In our opinion SJP has also benefited from the decision by many banks to withdraw from providing investment advice to individuals through branches as a result of RDR. In 2013 SJP hired advisors formally employed by the banks along with acquiring small intermediary firms to increase its network of tied agents; gaining an opportunity to serve more policyholders. Looking forward we believe that this phenomenon will come to an end and the Partnership will grow in the region of 5%-6% per year.

Although first quarter 2014 results would indicate continuing growth with 26% year on year increases in net inflows, we expect growth to moderate to an average of 12% a year through to 2016. This segment will become an increasing focus of competitors; although we consider SJP well-placed to respond to these challenges. This may be from direct to consumer platforms, independent financial advisors (IFAs) who have successfully adjusted their business model after RDR, or insurers increasing their own tied agent work forces which could compete for distributors.

SJP has initiatives in place to "grow its own" tied agents in response to competition for numbers of distributors. Rather than recruiting from the population of IFAs, the group is establishing centers which provide an environment for the agents to learn the necessary skills; with at least a further 50 students expected to become Partners in 2014.

SJP is looking to broaden its profile by launching into the Asia-Pacific expatriate community with the acquisition of the Henley Group. The acquisition which awaits necessary regulatory approvals before completion is small, in keeping with SJP's conservative risk appetite, but if successfully executed, will allow SJP to expand its footprint. That said, at this stage we do not believe the inflows from this operation will be sufficiently significant to diversify the product profile and merit a stronger competitive position assessment.

Table 1

St. James's Place PLC Competitive Position					
	2013	**2012**	**2011**	**2010**	**2009**
Funds under management (£ bil.)	44.3	34.8	28.5	27.0	21.4
Growth in funds under management (%)	27	22	6	26	N.M.
Life new business contribution (£ mil.)	213.6	208.9	182.5	157.9	106.3
Life PVNBP new business margin (%)	4.5	4.7	4.5	4.3	3.8
Net inflows (£ bil.)	4.3	3.35	3.21	3.00	2.30
Surrender rate as a % of average funds under management	4.7	4.9	5.2	5.0	4.0
Number of tied agents/Partners	1,958	1,788	1,649	1,552	1,464

N.M.--Not meaningful.

Financial Risk Profile: Strong

Capital and earnings: A cash generative business with limited capital needs

We consider that SJP has extremely strong levels of capital adequacy according to Standard &Poor's risk-adjusted capital model. Overall, however, we consider capital and earnings to be strong. This reflects our view that the absolute size of solvency net assets is relatively small, the lower quality of capital given implicit items, and exposure to operational risks that our model may not adequately capture in this instance. We consider the quality of total adjusted capital (TAC) to be low because it is heavily reliant on the present value of future profits, one of the softer forms of capital for which we give credit.

We believe that SJP's capital position will be sustained by its ability to generate cash from its growing FUM, which are subject to only limited capital requirements given the lack of insurance risk. The nature of SJP's product structure is that new business is cash neutral over the first six years. After this time, assets held on behalf of policyholders are cash generative. SJP's strong growth over recent years means that about 30% of FUM do not generate cash profits, but are likely to do so over the next six years. We expect the combination of the maturing back book and the group's limited capital needs to comfortably offset the material dividend growth and pay-out ratios of between 70%-80% that SJP has signalled to the market.

Table 2

St. James's Place PLC Capital					
(£ mil.)	**2013**	**2012**	**2011**	**2010**	**2009**
Net income	190.3	107.1	106.8	55.0	39.8
Total shareholder's equity	906.1	762.5	678.61	586.3	539.8

Table 2

St. James's Place PLC Capital (cont.)					
Life value of in-force	1,950.2	1,549.3	1,251.5	1,131.2	886.6
Solvency net assets	507.6	403.5	342.2	295.6	263.3
Cash result	168.8	91.7	67.0	48.3	23.5
Dividends paid	65.3	45.3	31.6	20.6	19.4

Risk position: A conservatively managed balance sheet with low levels of volatility expected

SJP's risk position is low risk and lower than that of peers in the U.K. life insurance market. The group manages its balance sheet extremely conservatively and we believe that it is likely to continue to do so. The majority of the group's shareholder assets are invested in U.K. government bonds or diversified among a range of 'AAA' money market funds. The cash balance of £197 million as of Dec. 31, 2013, is nearly all held in a number of U.K. banks that we consider to be highly systemically important. Within the group's back book there are no investment guarantees limiting SJP's exposure to interest rate risk. In addition, the group has reinsured the majority of its small back book of protection liabilities.

Table 3

St. James's Place PLC Risk Position					
	2013	**2012**	**2011**	**2010**	**2009**
Investment portfolio composition (excluding unit-linked assets) (£ mil.)	787.1	588.4	334.4	385	283.7
AAA rated money market funds (%)	66	55	62	62	57
Cash at banks (%)	25	31	14	22	24
Other (%)	0	0	0	3	1
Gilts (%)	9	14	24	12	18

Other Assessments

Enterprise Risk Management

Our assessment of SJP's enterprise risk management (ERM) is adequate with strong risk controls. This reflects our positive assessments of SJP's ability to manage its credit and emerging risks. We believe that the importance of ERM to the rating is low given the levels of capital adequacy the group possesses as well as the low risk product and investment profile.

Management & governance

We consider management and governance to be satisfactory. SJP's management team has specific financial and operational targets based on a range of metrics. We consider the group's consistent strategy – where it focuses on growing its unit-linked FUM and minimizing insurance risk – as a strength. We view the management team as proactive, as demonstrated by how it positioned its network of tied agents in the lead up to the RDR. The management team's ability to execute its strategy is demonstrated by its track record of profitable growth through the cycle.

Over recent years the composition of the Board has seen a number of changes, but we see this primarily as a function of Lloyds Banking Group selling down its stake in SJP. We do not anticipate any change in risk profile or Board oversight as a result.

Liquidity

We consider liquidity to be exceptional. The group's shareholder assets are invested in highly liquid assets, while SJP's insurance liabilities are almost entirely made up of unit-linked business, with limited liquidity risk.

SJP does not possess any directly rating sensitive contingent liabilities that could lead to calls on liquidity. However, it does have bank loans, which we view as operational leverage because they fund the agent network. Agents are able to receive financial support from SJP to set up and maintain their business. These individual loans to agents are secured on the income streams that their sales generate as well as, ultimately their other assets. Overall, this, combined with SJP's cash generation and capital solvency means we view these bank loans as bringing limited liquidity risk.

Related Criteria And Research

Related Criteria

- Insurers: Rating Methodology, May 7, 2013
- Enterprise Risk Management, May 7, 2013
- Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Capital Model, June 7, 2010
- Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- U.K. Annuity Volumes Will Suffer Until Greater Clarity Emerges On Policyholder Response to Budget, March 25, 2014
- U.K. Life Insurance Sector Carries A Low Industry And Country Risk Assessment, Nov. 6, 2013

Ratings Detail (As Of May 29, 2014)	
Operating Company Covered By This Report	
St. James's Place U.K. PLC	
Financial Strength Rating	
Local Currency	A-/Stable/--
Counterparty Credit Rating	
Local Currency	A-/Stable/--
Domicile	United Kingdom

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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