

## St. James's Place U.K. PLC

**Primary Credit Analyst:**

Mark Button, London (44) 20-7176-7045; mark\_button@standardandpoors.com

**Secondary Contact:**

Oliver Herbert, London (44) 20-7176-7054; Oliver\_Herbert@standardandpoors.com

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# St. James's Place U.K. PLC

## Major Rating Factors

### Strengths:

- Strong capitalization supported by low risk profile.
- Resilient earnings profile.

### Weaknesses:

- High operational leverage.
- Relatively concentrated business model.

**Operating Company Covered By This Report**

**Financial Strength Rating**

*Local Currency*

A-/Stable/--

## Rationale

The ratings on St. James's Place U.K. PLC (SJPUK), a wholly owned subsidiary of U.K.-based wealth management group, St. James's Place PLC (SJP), reflect the SJP group's strong capitalization and low risk profile. The capital position is maintained by earnings which have proved resilient over the economic cycle. Offsetting factors include SJPUK's high operational leverage and relatively concentrated business model, which focuses on the higher-net-worth U.K. life and pensions market. SJP had £31.0 billion of assets under management on March 31, 2012.

Standard & Poor's Ratings Services' base-case assumption is that SJP's direct distribution sales force, the Partnership, will grow more slowly in 2012 than in 2011 as SJP rides out the challenges presented by the introduction of the Financial Services Authority's Retail Distribution Review (RDR). However, we expect the Partnership's growth rate to pick up in 2013. We also anticipate that the company's competitive capabilities will allow SJP to continue experiencing present value of new business premium (PVNBP) margins above 4.0% over the next two years; and 2012 will see the company achieve annual premium equivalent (APE) sales of over £700 million.

Though operating performance is highly dependent on the markets, SJPUK has reported robust earnings through the economic downturn, demonstrating resilience in its earnings and business model. We expect this to continue, with cash generation likely to grow to more than £80 million a year by 2013 as the business continues to mature. SJPUK's earnings resilience also extends to its capitalization, reflecting its low risk profile. Hence, we anticipate regulatory solvency coverage over the rating horizon will be maintained at more than 2x.

We assess SJP as not strategically important to Lloyds Banking Group (LBG; A-/Stable/A-2), which has a 58% stake in the company. We do not incorporate any explicit support in the rating as a result of this majority ownership. The stand-alone credit profile (SACP) of SJPUK is 'a-'.

## Outlook

Under our base-case assumptions, we do not expect the ratings on SJPUK to be raised or lowered in the next couple of years. This incorporates our view that its earnings and capital position will remain robust.

SJPUK's investment performance is an important factor supporting the company's competitive position, operating

performance, and ability to successfully earn out its embedded value of in-force business. We may consider lowering the rating should retention rates as a percentage of average funds under management fall below 90% or if net flows were to turn negative.

We see limited potential for a positive rating action in the short-to-medium term, owing to the concentration of SJP's business model.

## Corporate Profile: Niche Insurer Focused On High-Net-Worth U.K. Life And Pensions Market

SJPUK is a niche player in the U.K. life and pensions market, and focuses its sales on higher-net-worth individuals. The company is a wholly owned subsidiary of SJP, a publicly listed enterprise that is majority (58%) owned by LBG. LBG acquired its shareholding following its acquisition of HBOS PLC (A-/Stable/A-2) in 2009. SJP wrote £642 million of new business on an APE basis in 2011 (£582 million in 2010) and had £28.5 billion of funds under management on Dec. 31, 2011.

The group also sells a wider product range, including offshore life products through St. James's Place International and unit-trust products through St. James's Place Unit Trust Group Ltd.

LBG is the largest retail bank in the U.K. and has a significant involvement in the U.K. long-term savings market through its stake in SJP and full ownership of Clerical Medical Investment Group Ltd. (A/Stable) and Scottish Widows PLC (A/Stable). The investment in SJP provides LBG with access to the higher-net-worth market.

SJP represents less than 2% of LBG's equity, and as such we do not consider it to be strategically important to the banking group. The company's operations are not viewed as being integral to the bank's strategy and there is no shared branding. Furthermore, SJP is operationally independent from its parent. Going forward, we do not expect ties to strengthen further.

## Competitive Position: Niche Market Player Supported By Partnership Distribution

**Table 1**

| <b>St. James's Place U.K. PLC/Competitive Position*</b> |                           |             |             |             |             |
|---|---------------------------|-------------|-------------|-------------|-------------|
| <b>(Mil. £)</b>   | <b>Year ended Dec. 31</b> |             |             |             |             |
|   | <b>2011</b>               | <b>2010</b> | <b>2009</b> | <b>2008</b> | <b>2007</b> |
| Annual premium equivalent                               | 410.5                     | 362.4       | 281.6       | 258.6       | 266.5       |
| Growth in annual premium equivalent (%)                 | 13.3                      | 28.7        | 8.9         | (3.0)       | 22.7        |
| <b>Analysis of annual premium equivalent</b>            |                           |             |             |             |             |
| Annual premiums (%)                                     | 21.4                      | 19.9        | 23.6        | 24.9        | 21.3        |
| Single premiums (%)                                     | 78.6                      | 80.1        | 76.4        | 75.1        | 78.7        |
| Gross premium written                                   | 3,531.8                   | 3,183.8     | 2,405.5     | 2,183.7     | 2,316.0     |
| Net premium written                                     | 3,470.7                   | 3,126.7     | 2,365.6     | 2,156.4     | 2,295.0     |
| Reinsurance utilization                                 | 1.7                       | 1.8         | 1.7         | 1.3         | 0.9         |
| Linked (%)  | 99.7                      | 99.4        | 99.5        | 98.8        | 98.8        |
| With-profit (%)   | 0.0                       | 0.0         | 0.0         | 0.0         | 0.0         |
| Non-profit (%)  | 0.0                       | 0.0         | 0.0         | 0.0         | 0.0         |

Table 1

| St. James's Place U.K. PLC/Competitive Position* (cont.) |      |      |      |      |      |
|--|------|------|------|------|------|
| Composition of new business by product line (%)          |      |      |      |      |      |
| Protection   | 0.3  | 0.3  | 0.4  | 1.1  | 1.1  |
| Pension savings  | 55.4 | 49.9 | 54.4 | 53.5 | 46.8 |
| Life savings   | 38.3 | 42.3 | 39.7 | 39.3 | 46.2 |
| Annuities  | 6.1  | 7.5  | 5.6  | 6.0  | 5.9  |
| Other  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  |

\*Data from returns to the Financial Services Authority for St. James's Place U.K. PLC.

SJP's competitive position is only considered good, and thus a relative weakness to the rating. The company's competitive position and brand are defined by an advice-driven, high-quality sales force. However, our view of competitive position is constrained by a concentrated business model whose performance is dependent on the investment markets.

### Historical

SJPUK is a niche player with highly concentrated geographical, product, and distribution capabilities. Its target market comprises higher-net-worth individuals and their businesses. Product strategy primarily focuses on unit-linked life and pensions products. Of the products sold by SJP, 91% are manufactured internally. Those products that do not fit within the company's risk tolerance--including stakeholder pensions and some protection business--are offered through panels of other U.K. insurers.

SJPUK's product mix and high proportion of single-premium business leaves the company highly dependent on the investment markets. Despite this, new business at SJPUK has grown strongly in recent years. SJPUK achieved APE sales of £410 million in 2011, up 13.3% on 2010. Further, around 80% of sales in 2011 were composed of single-premium business. Despite the volatility of markets, single-premium volumes continued to grow by 11.1% over the year.

Management has expanded the investment options available within SJP's product wrapper to include more-cautious funds, as well as beginning to offer wealth management and private banking services. In our opinion, these should provide more resilience to SJP's profile, although diversification benefits will remain modest.

SJP's distribution model differentiates it from most of the market. Product distribution is through the highly experienced, and highly productive, Partnership. Partners are highly experienced, self-employed individuals. The Partnership exhibited further strong growth in 2011, up 6.3% to 1,649 partners (up 6.0% in 2010), and retention remains very high. Incentives are geared toward high producers on a stepped scale, which includes share options in SJP, and the Partnership and SJP have aligned goals through business retention and growth of funds under management. SJP's growth strategy is based on building partnership numbers and increasing productivity.

In previous years, SJP's strong investment performance has been a key differentiator for the group. More recently, the proportion of funds outperforming their benchmarks has dropped. To date, this has not unduly affected the implied surrender rate as a percentage of funds under management (5.2% in 2011, 5.0% in 2010). A substantial period of underperformance could weaken one of SJP's key competitive advantages; affecting the organization's ability to attract and retain business in what is a highly competitive market.

## Prospective

SJPUK is well positioned in a customer segment that values financial advice. Standard & Poor's expects SJP to continue to build on its competitive position in the high-net-worth segment and continue to gradually diversify the product portfolio.

SJP is well positioned to maintain its competitive position once the RDR--which is aimed at improving transparency surrounding the cost of providing financial advice to consumers--is implemented on Jan. 1, 2013. By year-end 2011, 80% of SJP's partners had passed the five exams required under the new legislation. Of the remaining 20%, 11% have one or two exams left to do. We understand that the remaining 9% can be broadly split in half between those who joined in the past 18 months and those who, in any case, are less productive or who are likely to retire early, rather than invest time in passing the qualifications. This combination of early retirements and individuals who have not qualified may restrict the growth of the Partnership in 2012. On the other hand, some independent financial advisors may be forced out of business because the RDR bans commission-based sales. This could provide SJP with potential recruits for the Partnership in the medium term.

## Management And Corporate Strategy: Focused Niche Strategy, Extensive Outsourcing

SJPUK's management and corporate strategy score is considered marginally positive. Its sub-scores are mostly positive, and it has no negative sub-scores. We assess all the governance and financial policy scores as neutral.

### Strategy

SJPUK's strategy is defined and constrained by its niche market, distribution strategy, and low absolute levels of capital. The strategy is simple, but effective--to focus on areas of strength and outsource the balance. The company therefore focuses on managing the relationship between the client and the advisor, but outsources the fund management and policy administration. The key strategic focus is organic growth of low-capital-intensive products in the U.K. higher-net-worth market segment.

SJPUK's strategy is well-suited to a market that is polarizing between low-margin commodity products and high-value-added products and services. The company's approach is to offer customers high added value. It does not aim to differentiate its products in terms of design, nor does it compete on charges. Instead, the company's competitive focus is on superior investment performance and the provision of high-quality financial advice.

Management is committed to selling solely through a high-quality direct sales force, focusing on higher-net-worth customers and their businesses. The upcoming regulatory changes in the intermediated distribution sector appear to offer SJP the opportunity to expand the Partnership. Based on its concentrated business model, SJP appears to be managing its risks with respect to regulatory changes very well.

Scale and capital intensity define the products that can be produced internally and those that need to be outsourced. The outsourcing agreements include "no cross-sell" language to prevent third parties from penetrating existing business. Despite giving the impression of progress toward being solely a distribution and sales organization, SJPUK manufactured 91% of products sold in 2011 and 2010.

### Operational management

Group strategy is uncomplicated, but execution is not without risk because of high operational leverage. Expense overruns could be material if sales fall because of SJPUK's relatively small capital base and its limited ability to scale

back costs quickly. However, the potential impact from this risk is reducing, due to the strong unwind expected from the in-force business over the medium term.

More than half of the SJP board comprises independent nonexecutive directors. These have been carefully selected to bring additional knowledge on marketing and risk and regulatory background into the organization. The management team is highly experienced at operating direct sales forces in the U.K.

Unlike many other direct sales offices, SJPUK has always been selective about the quality of its sales recruits. Even though the cultivation of customers is delegated to individual partners, the Partnership can still be regarded as one of the most productive sales forces in the industry. SJP has taken a proactive, and seemingly successful, approach to new regulations and educational requirements for its sales force, in advance of the RDR.

All administration is outsourced to three specialist providers, including a subsidiary of The Prudential Assurance Co. Ltd. (AA/Stable/--). Long-term agreements are in place and the fee structure effectively gives SJPUK some scale economies and the ability to scale back certain expenses if sales fall.

### **Financial management**

The dynamics of SJPUK's business differ from those of peers. The company carries virtually no direct market or credit risk in its asset portfolio and has outsourced administration. At group level, it has no conflicting financial management priorities because SJPUK is effectively the only capital-consuming operation. The group retains high operating leverage, however. A significant proportion of the company's expenses are broadly fixed.

Financial strategies are focused on embedded-value growth and increasing sales by 15%-20% per year, while expenses grow by less than 10%.

## **Accounting: Embedded Value Figures Are Core To Standard & Poor's Analysis**

SJPUK prepares accounts under U.K. applicable accounting standards and SJP prepares accounts under International Financial Reporting Standards (IFRS) and on a European embedded value (EEV) basis.

2011 saw SJP make a minor change in the way that the EEV profit from existing business is calculated. The company used to calculate the profit from existing business using the closing discount rate. From 2011 onward, it will use the opening discount rate. Overall, this does not affect the EEV profit. However, under the old methodology the unwind of the discount rate would have been £119.0 million in 2011, rather than the stated figure of £91.2 million.

## **Enterprise Risk Management: Relatively Risk-Averse, Adequate Overall**

SJP's enterprise risk management (ERM) is viewed as adequate with strong risk controls. This assessment indicates the group's adequate risk management culture and systems and a mixture of adequate and strong controls for the key risks. The main risks are insurance, operational, and (indirect) market risks. The risk profile is viewed as stable and we do not expect it to materially change over the short-to-medium term. Given the low risk profile, we view ERM as being of low importance to SJP. The ERM assessment is likely to stay at adequate with strong risk controls over the rating horizon.

An adequate culture of risk management exists at SJP. Risk ownership appears typically at middle management and

board level and communication of risk appears widespread. Co-ordination of ERM with SJP's largest shareholder, LBG, appears limited.

SJP's main risks are (indirect) market and operational, particularly regulatory, outsourcing, and compliance issues surrounding the Partnership distribution. Because most of the portfolio is unit-linked with matching investments, SJP is less exposed to direct market risk than other insurers. However, sizable adverse market movements would hit SJP's earnings and new business volumes. Investment risk controls appear adequate and the nonlinked fund is invested in a low-risk, highly liquid, portfolio. Operational risks comprise a significant proportion of SJP's risk profile, but appear adequately controlled.

Due to its business model, SJP is a risk-averse company compared to other U.K. insurers. It also benefits from an absence of legacy risks because of its relative immaturity.

SJP's risk models are assessed as adequate. Development of economic capital will strengthen the risk models and assist with strategic risk management, which is currently viewed as adequate.

Monitoring of mortality and morbidity insurance risks appears regular and robust and SJP is not exposed to longevity risk. Expense risk is somewhat mitigated through outsourcing arrangements with third-party administrators. The business profile and the reinsurance program reduce extreme event risk and emerging risks appear strongly assessed.

## Operating Performance: Strong New Business Margins And Earnings, Fixed Expenses Remain High

**Table 2**

| St. James's Place U.K. PLC/Operating Statistics*                       |                    |      |      |       |      |
|--|--------------------|------|------|-------|------|
| (%)  | Year ended Dec. 31 |      |      |       |      |
|  | 2011               | 2010 | 2009 | 2008  | 2007 |
| Growth of long-term fund   | 5.9                | 25.6 | 30.5 | (6.7) | 20.9 |
| Growth of long-term fund (excluding transfers)                         | 5.9                | 25.6 | 30.5 | (6.7) | 20.9 |
| Growth of linked funds (excluding management units)                    | 6.0                | 25.6 | 30.8 | (6.6) | 21.2 |
| Regular premium persistency ratio                                      | 77.7               | 82.1 | 77.5 | 80.7  | 83.7 |
| Total expense ratio - gross of reinsurance                             | 10.0               | 10.3 | 11.2 | 11.7  | 11.1 |
| Total expense ratio - net of reinsurance                               | 10.2               | 10.5 | 11.4 | 11.9  | 11.2 |
| Total expenses/long-term fund brought forward - net of reinsurance     | 1.9                | 2.3  | 2.4  | 2.1   | 2.6  |
| Acquisition expense ratio - gross                                      | 51.3               | 53.5 | 54.5 | 54.8  | 54.2 |
| Initial commission/total new business premiums - gross                 | 3.5                | 3.6  | 3.6  | 3.7   | 3.7  |
| Renewal commission/long-term fund brought forward - net of reinsurance | 0.4                | 0.4  | 0.4  | 0.4   | 0.4  |
| Maintenance expense ratio - gross                                      | 2.0                | 2.2  | 2.7  | 3.1   | 2.5  |
| Nonrecurring expense ratio - gross                                     | 0.0                | 0.1  | 0.2  | 0.1   | 0.4  |
| Acquisition commission expense ratio - gross                           | 28.1               | 29.4 | 28.6 | 28.7  | 29.8 |
| Maintenance commission expense ratio - gross                           | 2.0                | 1.9  | 2.0  | 2.0   | 1.9  |
| Increase in noncommission expenses - gross                             | 5.3                | 13.0 | 3.5  | 3.0   | 21.8 |

\*Data from returns to the Financial Services Authority for St. James's Place U.K. PLC.



SJPUK's operating performance is considered strong. The business model itself leads to high operational leverage and earnings volatility. However, as the business continues to mature, we expect the company to maintain its earnings growth.

SJPUK's business model leads to high operational leverage and earnings volatility. The business written by the company is high margin, but profitability can be affected by expense overruns and the buildup of unrelieved tax losses. Sales growth has been the key to offsetting the buildup of sizable expense overruns that arose due to the high fixed cost base (administrative costs remained fairly flat in 2011). The leveraged profile is perpetuated by the indirect impact of equity markets on sales and asset management fees.

SJPUK's new business margins (new business profit divided by PVNBP) on the life and the unit trust business were very strong in 2011. The margin on total business was 4.6% in 2011 (4.4% in 2010), while the margin on life and pensions business grew to 4.5% (4.3% in 2010), offset by a fall in the margin on unit trust business to 4.6% (4.8% in 2010). We understand the change in margins over 2011 was largely due to an initiative by SJP to move toward equalizing the commission structures across all its products to 3.0% initial commission, followed by 0.5% trail. This process is now complete; commission structures are now equalized for business written since Jan. 1, 2012.

Based on EEV, operating profit before tax for life and unit trust business grew strongly in 2011 to £379 million, from £339 million in 2010, up 11.8%. The increase in operating profit primarily stems from the contribution from new business (up 12.9% in 2011 and 40.2% in 2010). Total embedded value rose to £1,900 million on Dec. 31, 2011, 10.7% up over the year. Of the gain, 75% came from an increase in value in force (VIF).

On an IFRS basis, total profit before shareholder tax for the year was £109.7 million (up 30% on 2010), based on higher income from funds under management. Profit after tax was up 94.2% to £106.8 million in 2011.

Of the £28.5 billion of funds under management held by SJP as at year-end 2011, £10.2 billion have yet to contribute to the cash result. For the first six years of the assets being held by SJP, they are cash-neutral. As the business matures, it starts to contribute to cash profits. This helps SJP to mitigate moves in market values, because so long as policies do not lapse these maturing funds under management will continue to contribute positively to company profits. The proportion of funds exiting the surrender change period remains relatively high, supporting the strong growth in the cash position.

Prospective operating performance will remain highly dependent on the investment markets; however, we expect the positive trend in earnings to continue as the strong sales from recent years come out of their initial surrender period. The outlook for persistency of the in-force book remains exposed to volatility in equity markets and uncertainty in the U.K. economy. However, we expect SJP to continue its recent trend toward increasing resilience and that new business margins will exceed 4.0%, based on PVNBP. We expect SJPUK's margins to remain at the upper end in the U.K. life market.

## Investments: Unit-Linked Funds Dominate, Strong Performance A Key Competitive Advantage

Table 3

| St. James's Place U.K. PLC/Investment Statistics*  |                    |       |        |        |       |
|--|--------------------|-------|--------|--------|-------|
| (%)  | Year ended Dec. 31 |       |        |        |       |
|  | 2011               | 2010  | 2009   | 2008   | 2007  |
| Money-weighted rate of return for return of unit-linked funds                            | (1.0)              | 14.3  | 20.2   | (13.4) | 11.1  |
| Non-linked investment return   | 29.3               | 75.2  | (24.2) | (65.1) | 22.6  |
| Return on assets backing with-profit liabilities and required capital margin             | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Linked assets/total policyholder assets  | 98.7               | 98.3  | 98.8   | 98.1   | 97.7  |
| <b>Non-linked portfolio composition</b>  |                    |       |        |        |       |
| Cash   | 7.0                | 22.7  | 1.8    | 0.9    | 6.8   |
| Bonds  | 31.4               | 18.9  | 27.5   | 26.0   | 14.7  |
| Equities   | 61.6               | 58.4  | 70.7   | 73.1   | 78.5  |
| Properties   | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Affiliates   | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Mortgages and loans  | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Derivatives  | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Other  | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| <b>Split of fixed interest assets by investment grade, speculative grade, and other:</b> |                    |       |        |        |       |
| Investment grade   | 100.0              | 100.0 | 100.0  | 100.0  | 100.0 |
| Speculative grade  | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |
| Other/unrated  | 0.0                | 0.0   | 0.0    | 0.0    | 0.0   |

\*Data from returns to the Financial Services Authority for St. James's Place U.K. PLC

SJPUK's investment portfolio has minimal direct credit or market risk. We view the company's investments as very strong. At year-end 2011, 99% of assets were linked. Investment performance has been a strength and a key marketing tool, although recent performance has disappointed.

### Credit risk

SJPUK's investment portfolio has a low risk profile. All nonlinked investments are held in cash and other fixed- and variable-income securities. Looking across the group, SJPUK held liquid assets of £334.4 million as at year-end 2011. Of this, £80.1 million was held in U.K. government debt, £207.8 million in 'AAA' rated money market funds, and the remaining £46.5 million was held in cash.

### Market risk

Almost all assets back unit-linked liabilities and are managed by a selection of respected external fund managers. The balance is held in high-quality bonds or cash. Direct market risk is therefore low.

The business is highly dependent on indirect market risk, however, as fluctuations in asset values affect both earnings and the ability to gain tax relief on incurred expenses.

### Investment performance

Fund performance has been a strength for SJP, as demonstrated by its outperformance over the medium-to-long term of other U.K. managed life and pension funds. This benefits SJPUK's marketing and its earnings.

SJPUK imposes no investment guidelines on its fund managers other than the broad parameters for the particular fund sector and regulatory requirements. The group's investment committee does, however, monitor both the level

and volatility of fund performance for each manager, in conjunction with an independent consultant, Stamford Associates. New, non-equity-based funds have been launched in recent years and offer diversified investment opportunities and investment alternatives to equity funds. The significant growth in assets under management (AUM) may make it harder for the investment committee to maintain its reputation for outperformance. That said, SJP is expected to continue to successfully manage the strong growth in AUM.

## **Liquidity: Mostly Unit-Linked Assets, With Nonlinked Funds Highly Liquid**

Liquidity is not a significant issue for SJPUK given that its book is predominantly unit-linked. Nonlinked assets are held in liquid form, and unit-linked funds are readily realizable. SJP's property funds maintain liquidity and additional measures are available to SJPUK if withdrawals increase. SJP maintains a cash reserve and additional access to liquidity is expected to be available through LBG.

Cash flow is a modest positive to the rating. In particular, the front-end loaded structure of SJPUK products helps negate new business strain and in effect immunizes the company against the normal effects of rapid sales growth. Product features in the property fund investments mitigate liquidity concerns for SJP.

## **Capitalization: Strong Capitalization, But Low Absolute Level Of Capital**

SJPUK's capitalization is strong, but absolute levels of capital are low. The statutory solvency position at SJPUK was very strong at the end of 2011, reporting 395% for the life business and 263% for other regulated business.

### **Capital adequacy**

The capital model result is extremely strong, but our assessment is offset by the small size of the capital base relative to the operational risks that may arise from a decentralized direct sales force as well as considerations concerning quality. In particular, the company relies significantly on the softer elements we give credit for, such as the VIF.

SJPUK's capital base is small, but is not inappropriate given the size and nature of business written. The quality of capital remains relatively weak, given the large proportion of total adjusted capital within Standard & Poor's insurance capital model supported by VIF. Capital resource requirement coverage in 2011 was 2.7x, compared with 2.6x in 2010.

### **Reinsurance**

Reinsurance with highly rated counterparties is used to significantly reduce SJPUK's principal regulatory risk requirements, and mortality and morbidity risk. In 2008, SJP created an internal reinsurance vehicle to internally reassure pensions business. The arrangement reduces the new business strain of writing new pensions business, and thus boosts cash flows and capitalization more quickly than was previously possible.

### **Prospective**

Standard & Poor's expects SJPUK's capital to remain modest in absolute terms, but that the regulatory minimum margin coverage will be maintained above 2x. We expect risk-adjusted capitalization to remain at least strong. In the longer term, the company is expected to strengthen capital generation through a suite of measures, including the emergence of statutory profits, scrip dividends, and the likely exercise of share options.

## Financial Flexibility: Strong And Further Options Available

Table 4

| St. James's Place U.K. PLC/Financial Statistics*                              |                    |          |          |          |          |
|---|--------------------|----------|----------|----------|----------|
| (%)   | Year ended Dec. 31 |          |          |          |          |
|   | 2011               | 2010     | 2009     | 2008     | 2007     |
| Total long-term admissible assets (mil. £.)                                   | 19,472.8           | 18,453.9 | 14,609.2 | 11,236.8 | 12,190.4 |
| Total admissible assets (mil. £.)   | 19,508.3           | 18,488.7 | 14,631.4 | 11,274.3 | 12,197.5 |
| Inadmissible assets: no value and in excess of market and counterparty limits | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| Long-term capital resources (mil. £)  | 96.5               | 86.5     | 85.2     | 76.1     | 94.4     |
| Growth in capital resources over the year                                     | 11.6               | 1.5      | 11.9     | (19.4)   | (5.9)    |
| <b>Components of capital resources:</b>                                       |                    |          |          |          |          |
| Core Tier One capital (after deductions and restrictions)                     | 100.0              | 100.0    | 100.0    | 100.0    | 100.0    |
| Tier One waivers  | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| Other Tier One capital  | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| Upper Tier Two capital (after restrictions)                                   | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| Lower Tier Two capital (after restrictions)                                   | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| CRR (mil. £)  | 36.3               | 33.5     | 31.6     | 33.7     | 30.0     |
| Long-term ICR coverage ratio (x)  | 2.9                | 2.8      | 3.0      | 2.5      | 3.3      |
| Long-term MCR coverage ratio (x)  | 2.7                | 2.6      | 2.7      | 2.3      | 3.1      |
| Long-term CRR coverage ratio (x)  | 2.7                | 2.6      | 2.7      | 2.3      | 3.1      |
| With-profit regulatory free asset ratio                                       | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| With-profit realistic free asset ratio  | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| RCM (mil. £)  | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| RCM coverage ratio (x)  | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| With-profits equity backing ratio   | 0.0                | 0.0      | 0.0      | 0.0      | 0.0      |
| Investment leverage   | 136.6              | 188.1    | 133.0    | 158.6    | 167.2    |
| Gearing   | 70.4               | 76.4     | 0.0      | 0.0      | 0.0      |
| High-risk asset exposure  | 100.0              | 148.3    | 107.2    | 109.7    | 160.3    |

\*Data from returns to the Financial Services Authority for St. James's Place U.K. PLC.

SJPUK's financial flexibility is strong. SJP, which is quoted on the London Stock Exchange, has no conflicting priorities when it comes to supporting SJPUK

Due to SJP's business model, the company carries relatively little insurance risk on its balance sheet. Rather than being directly affected by insurance, market and credit risks, we believe that the key sensitivity for SJP is to the operational risks inherent in a partnership-based, direct-advice business model. Otherwise, capital needs are likely to be limited to funding growth in the business.

SJP's debt is limited to bank finance, which is used to fund loans to partners, secured on the future income stream of the relevant partner.

The primary source of SJP's financial flexibility lies in its own strong earnings. An additional buffer is provided by an "implied reserve", which SJP sets aside to fund the cost of a dividend a year in advance. The company expects this fund to be around £40 million. SJP has some flexibility because it can issue scrip dividends, rather than cash.

Furthermore, some weaker forms of capital, such as stock options, may crystallize, but these remain largely dependent on the performance of the investment markets.

## Related Criteria And Research

- Group Rating Methodology And Assumptions, Nov. 9, 2011
- Principles Of Credit Ratings, Feb. 16, 2011
- Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- Holding Company Analysis, June 11, 2009
- Interactive Ratings Methodology, April 22, 2009
- Counterparty Credit Ratings And The Credit Framework, April 14, 2004

| <b>Ratings Detail</b> (As Of May 18, 2012)   |                |
|--|----------------|
| <b>Operating Company Covered By This Report</b>  |                |
| <b>St. James's Place U.K. PLC</b>  |                |
| Financial Strength Rating  |                |
| <i>Local Currency</i>  | A-/Stable/--   |
| Counterparty Credit Rating   |                |
| <i>Local Currency</i>  | A-/Stable/--   |
| <b>Domicile</b>  | 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. |                |

### Additional Contact:

Insurance Ratings Europe; [InsuranceInteractive\\_Europe@standardandpoors.com](mailto:InsuranceInteractive_Europe@standardandpoors.com)

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