

## Presenters

- Richard Ward
- Luke Savage
- Rolf Tolle

**Richard Ward:** My name is Richard Ward, I am CEO and I will be doing a brief introduction on our results this morning. I am joined by Luke Savage, Finance Director he will take us through more of the detail on the financial results and Rolf Tolle Franchise Performance Director who is here to take questions along with Luke and myself at the end of this session. If I can now just briefly move into the annual results and the financials gross written premiums for 2007 sitting at 16.4 billion roughly unchanged with respect to 2006, if you do it at a constant exchange rate and take out the exchange rate fluctuations then gross written premiums rose 5% up on gross written premiums for '06. Looking at our profit before tax line, profit is up 5% up at 3.846 billion as compared to 2006 and Luke will go through a lot of the drivers behind that profit that we have seen for last year.

Combined ratio - roughly unchanged on 2006 sitting at 84% and finally return on capital, a great number on return on capital of 29.3% that actually gives us a five year average of 19.4% return on capital for the markets so I we are very pleased with that performance indeed it is excellent to ROC.

Just looking at how we performed against our peer group and we have used these four groupings ever since we have been reporting on an annual accounting basis since 2001. So hopefully these are familiar to you; here I am plotting out the combined ratio from 2003 through to 2007 for Lloyds and then looking at the US P&C industry, US reinsurers, the European insurers and Bermudian re-insurers. And again we have continued to out-perform all our major peer groups and our combined ratio

of 84% compares very favourably with US P&C at 94% or the US reinsurers at 95 and the Europeans who clearly were affected by quite a few of the catastrophes and things such as windstorm kyrill at 96%. The Bermudians down at 85% but even there we have beaten the Bermudians by a percentage point. Of course if you look at individual businesses in these classes they will have lower and higher combined ratios as we do in the Lloyds market when we look at our individual syndicates but we are plotting out here is the average of our combined ratio.

Our ratio performs well because of our diversity, we have good diversity in classes of business that we write and good geographic diversity; I do believe those two factors have lead to us continuing to out-perform all our major peer groups.

Finally, I'll just look at the non financial performance in 2007, it has been a good year for Lloyds. We have made significant progress on business reform initiatives, in particular I am sure that you are aware of the drive behind electronic claims files and the processing of premium related documentation electronically, both those initiatives have progressed in 2007 and we are now looking at over 90% of new claims being processed electronically in our market place and nearly 80% of all original premium documentation being processed electronically; so that is a very good step forward in the modernisation of our market place and improving the efficiency and effective of our market place and we are grateful for the support we have had from both managing agents and brokers in achieving those targets.

Good progress around ratings, we obviously got our rating upgrade from both Fitch and S&P to A+. In part on the back of the Equitas transaction and the completion of the Equitas transaction last year, but also I think in part because of the progress we are making around business process reform and the progress that we are making around our performance framework. In the performance framework we now have fully implemented the 3 minimum standards around claims, underwriting and risk management; those standards are in place they were developed with the market place, they have been accepted by the managing agents; they are now fully operational and Rolf and his team are visiting managing agents to ensure that they are actually adhering to those standards that we have put in place. Through those standards of course we will be able

to more effectively manage the cycle and assist our market in focusing on underwriting discipline and on underwriting for profit.

On global distribution we have continued to expand our footprint and expand our franchise; last year in April we opened our Shanghai operation in China. We increased the number of participants in Singapore, we have now got 13 managing agents operating in Singapore, and we have applied for a licence in Brazil for admitted reinsurance status. We are applying for licences in Poland, Czech Republic, Austria and Portugal. We have a representative in Poland now as well and we are also looking at the Middle East and how we might expand our presence in the Middle East.

So we are continually looking at opportunities to expand the Lloyds franchise; we are not saying that we are looking to write business from these regions but what we are doing is establishing a presence so that when the market conditions are right our market place, our managing agents can take the opportunities that arise from those markets and capitalise on those opportunities, and finally I know it's all in the timing but we did have a very successful subordinated debt issue last year, we raised over £500 million worth of Tier 1 subordinated debt in the early summer. As a result of raising that debt we have been able to repay the syndicate loans of roughly £330 million, Luke will come on to that in a little bit more detail, but that in itself is again a measure of how Lloyds is viewed by the financial community the fact that we can go and raise £500 million worth of Tier 1 debt, a very successful issue.

These developments around business process, around the performance framework, around ratings are having an impact on our market place. We undertake surveys on a very regular basis, we survey over 500 of our customers, we surveyed over 400 of our managing agents and as a result of those nearly a thousand surveys that we have had completed, we are able to track how our stakeholders view Lloyds and how they view our performance across a wide range of areas, whether it is business process reform or whether it is things such as capital efficiency or performance framework; so we do monitor how we are performing, and it is very pleasing to see the results from those surveys that have just come in that we are seeing continued improved customer satisfaction with the service that we are providing to our market place. And that is also reinforced by brand surveys that we undertake and we do that on a bi-annual basis, and again our brand strength has improved year-on-year certainly looking at

the one undertaken two years go and the one undertaken this year we have seen an improvement in how our brand is viewed by the market place and particularly by the reinsurance market place.

Another indicator that we use in looking at how attractive we are as a market place is the interest of course we have from new entrants, there has been a lot of coverage of new entrants in the press. We continue to be an attractive place for people to do business and whether it is new syndicates being established or whether it is Bermudians wanting to come in and buy Lloyds businesses as we have seen just very recently, Lloyds is an attractive place for new entrants to establish themselves. I should say on new entrants not all new entrants get through our door we have a very rigorous process that we have put in place to actually examine any new entrants and to ensure that they meet the standards that we set as a market and so probably nine out of ten new entrants do not get past the front door at Lloyds. But those that do come do bring new business to us and so we welcome them. Good year for Lloyds based on the financial side, but also on the non financial side, now I will pass over to Luke who will go – bit more details of the financials.

**Luke Savage:** Thank you Richard and good morning ladies and gentlemen. So the P&L and as Richard said the flat written premium actually underlies that a 5% increase offset by the weakening dollar. Net incurred claims up marginally, not surprising we have seen a little more catastrophe activity this year which I will come back to in a moment. Operating expenses up in line with earned premiums but there are some ups and downs which we will touch on in a moment, and then one of the big stories from this slide is our investment return which is up almost 21% year-on-year and has broken through the £2 billion barrier for the first time.

Other income less expenses; one big driver in there, the payment of the £90 million Equitas premium that Richard referred to a moment ago, so all of that drives a bottom line combined ratio of 84%. And let's turn and look at how that is derived. In the left hand bars you can see the accident year, excluding catastrophes, which is out slightly by 1.9%. A couple of things within that, part of it is us starting to see some claims coming through on sub-prime related policies, but mostly it is just general market softening. Moving across in the red bars you can see that 2006 was an exceedingly benign year from a catastrophe perspective, this year at 3.8% on the

combined ratio it is far more in line with normal and I'll come back to some of the main drivers behind that on the next slide.

Prior year movements; we saw £856 million of prior year reserve release this year, that's up from £270 million last year, although it's fair to say that the £270 million last year would have been significantly higher if you backed out the specific impact of KRW, but put that lot together and 84% little change from last year. So let's just look at the catastrophe experience for a moment. On the chart here in the blue bars we show the insured industry loss going back over the past 14 or 15 years and the blue line shows Lloyd's catastrophe losses over that same period and what we have done is we have adjusted the scale so that the average of both of those has the same height so you can see on the right hand side the orange bar and the blue dots are scaled to be at the same height. So you can see that in 2007 the right hand with one bar, the purple one, that the industry as a whole saw slightly below average losses compared to the period overall and that Lloyd's share of those losses was below average for us and not really surprising if you look at the graph generally; what it shows is that when the market as a whole, the industry as a whole has higher losses we tend to pick up a bigger share than when the industry as a whole has below average losses we pick up a smaller share.

The reserve releases; we saw those coming up in all classes and across all lines and you can see that with the benefit of those prior year reserve releases all lines turned in a profit. I think that it is fair to say and there is a slide later which Richard will show you that had we not had that benefit the picture would not have been looking so good and there's actually a lot more underlying softening in this chart would at first suggest.

Whilst we're on the subject of prior years, let's look for a moment at our open years; now to be clear to anyone who is not sure what an open year is. An open year is which at the end of the three years underwriting period has not been able to find a year into which to reinsure to close and a RTC contract has not been put in place and that typically happens because there has been a lot of uncertainty so perhaps in the claims around 9/11 are still uncertainties on. And what you can see from this chart is that we peaked with a 104 open years in 2004 and that the reserves relating to those open years peaked at £7 billion in 2005 but what is quite clear is that there is now a strong downward trend, we managed to get 37 years closed this year we are down to 54. We had 2.7 of gross reserves and

£1.6 billion of net reserves now outstanding; and that is a trend that we would expect to see continuing through in '08 and '09 given that there is now a lot more appetite in the market for writing reinsurance. I think that we now have some 11 players willing to offer reinsurance to close.

On sub-prime; first point I make is that the policies that are affected are generally on a claims made basis, that means if the claims don't come through or notifications don't come through during the period in which the policies are on risk, then you are free and we are making sure that as part of the renewals that the terms and conditions are being altered so that we don't leave ourselves on ongoing risk once those policies have renewed.

We are not in a position at this point to try and put a figure on what the claims may end up being in total; what we are willing to say and what we do know for sure is that having got our fingers somewhat burnt back at the beginning of the decade with the likes of Enron laddering, Worldcom and so on, the market changed its underwriting habits and we now write far less of the kinds of classes of business that will be impacted – so whatever the ultimate claims figure is it will end up being an order of magnitude less than the kind of claims that we saw earlier this decade.

Finally, whilst we are on underwriting let's look at our operating expenses. Acquisition costs up 8%, part of which is attributable to the increase in net earned premiums and part of it is attributable to a shift in business mix, different classes of business attract very different commission rates so if you get a shift between different classes from one year to the next that can skew the picture. What we are comfortable with is that to date in the 2007 reported figures, we haven't seen any general drift upwards in the acquisition cost for any line of business and one of the first signs of a softening market is that you see the acquisition cost as a percentage of premium starting to go up, that is not in the 2007 numbers but it is fair to say that when we look at the business that is being written now we can see that drift and we would expect the 2008 acquisition cost of the percentage of premium to be on the up.

Admin expenses; despite the large jump, they are under control, the driver there is increasing profit commission payable to managing agents. So the more the managing agent makes for a syndicate the higher profit commission they will earn and that figure has jumped from under £100 million last year to in excess of £200 million this year. Now I would argue

strongly that if you are trying to compare Lloyds versus the company market you should actually add that figure back in because in the company market you make a profit and that is it, end of story. It's only in the Lloyds market where we then choose to take that profit and segregate part of it and take it out of P&L and say that belongs to the underwriters rather than belonging to the capital providers. So say for like-for like comparison I would argue put that back in.

Finally on this slide we have got the gain and loss on exchange. This is by and large an accounting anomaly that comes through as a result of having certain items which you don't revalue in the balance sheet at year end when your re-valuing one side of the balance sheet and not the other. It throws out a big gain or loss in exchange but at the end of the day it's a timing difference and it reverses out the following year as the premium in the balance sheet that's not re-valuing earns through. So hence the reason why it can swing wildly from the loss last year to a big gain this year.

So in summary on underwriting, you can see from the set of bars here that 2007 current year underwriting still made a strong contribution to the overall result but it is quite clearly down on the past few years. In the second set of bars the absent large windstorms there is nothing we have taken out this year. Then in the third set of bars you can see the ongoing trend where back early in this decade we having to strengthen reserves significantly 672 million back in 2003 to a position now where we are releasing reserves. I think we take comfort from the fact that when we look at the IBNR which is the reserve set up for claims that have not yet come through, as a percentage of the total reserves figure it is as strong now as it has been for the past few years. So we don't believe that any syndicate are dipping into reserves in order to boost this years P&L.

So that just leaves the investment return which as I say has more than doubled since 2003 and broken through £2 billion for the time. So let's take a little look at that. Here the coloured bars show the average assets base earning returns over that period. You can see there has been an increase it's up somewhere around 35% over that five year period. But the more striking increase is in the return that we have been earning on those assets which is the blue line where we have gone from less than 3% to approaching 6% overall. I think a lot of that is testament to the much more sophisticated asset management skills which we increasingly see

both around the market but also here in the centre of the corporation as well.

That is it, I think we do remain relatively conservatively invested compared to the industry as a whole. I think that has actually helped us over the past few months. I think where people with perhaps more aggressive investment policies have been getting their fingers burnt on sub-prime we have actually I think benefited from the flight to quality and the falling yields as government is trying to stave off recession.

If we look at the asset mix, across the top half of the chart here you can see the asset breakdown in the three principal asset buckets of syndicate level assets, funds at Lloyds, central assets and then the total. In most of those buckets you can see there has not been a great deal of change year on year. The one exception being our central assets which I will come back to in a moment. The bottom half of the chart you can see how each of those buckets performed and you can see that in all three of those areas we have seen improvement year on year. The most noticeable is again in central assets. So let's look at what it is that has been going on there.

We fundamentally changed the way we manage our central fund over a couple of years and I think this pie chart demonstrates it very clearly. The left hand shows our asset breakdown two years ago and you can see that we had almost exclusively US and UK bonds and equities. So fairly high concentrations to a relatively small geographical split and asset split whereas on the right hand side you can see our current disposition. As part of our change we are now invested globally and we are invested across far more asset classes. In theory and so far in practice that should give us a much better return, a much less volatile return for any given level of risk. As I say so far that seems to be paying off nicely. So for example we have only been in hedge funds for seven months but we found that has generated a 5% return in that seven months and it has proved uncorrelated to the other classes that we hold.

So how do those assets fit into the overall balance sheet. You can see on the top line cash and investments are up 5% we have got almost £37 billion in investable assets and moving down you can see that our reinsurance receivables at £8.3 billion are the lowest they have been for many years. Not only are we pleased with how far that figure has come

down but we're also very comfortable with the underlying asset quality over 95% is A- or better.

There is not really much else to say on the top half of the balance sheet other than to note that unearned premiums are still in excess of £7 billion to earn through in 2008 but in aggregate that is driven an increase in net resources of 8.5%. Now that is despite us having repatriated in excess of £1.5 billion of profits to our members during the course of 2007. This is an important change from the market last time there was a softening cycle. Under the old Lloyds rules when people made profits they would be trapped within the system until after the end of the three year period. So we trapped their profits in the system, they were not able to generate money on them other than by continuing to try and write business. So in the past couple of years we have introduced early profit release they can now take that money out and it removes that rather perverse incentive to continue writing into a softening cycle. Also worth noting that as well as the £1.5 billion we released during 2007 we expect there to be up to another £2 billion that we release in the next couple of months off the back of these results. So the final contributor to the increase then is our big increase in central assets and let's take a look at what has gone on there.

The bars show the magnitude and mix of assets available to essentially support the mutuality of the Lloyds market and you can see that has gone from strength to strength. From £1.3 billion to almost £2.5 billion now. Richard mentioned repayment of the syndicate loans you can see the little orange bars in the third and fourth that were building up in 2005 and 2006 have gone and instead they have been replaced by the new Tier 1 debt issue. Against that, if you look at the blue line, you can see that our solvency deficits have been falling sharply. The solvency deficits are the solvency shortfalls plus a minimum regulatory margin that the FSA requires to calculate. In combination you can see that not only do we have a much bigger, stronger more diversified central fund we have actually got much smaller solvency deficits outstanding that could end up being claims against that central fund. So I think overall it positions us very, very well for the coming soft market.

So how have we built that fund? We have got contributions of £168 million, 1% of capacity for existing members, 2% for new members. Worth noting that for 2008 we have reduced that contribution rate to half a

percent. So mutuality will now be the cheapest it's been I think since R&R.

Next line you can see the repayment of the syndicate loans £211 million and you could argue that from the perspective of the syndicates and the members looking at those two rows together we have actually given them cash back in 2007. We gave them more back in syndicate loans than we took in contribution so you could argue that we actually paid people for the benefit of mutuality last year.

Contributions to Equitas-Berkshire Hathaway. We have actually paid over 72 million of the 90 the other 18 will be payable upon completion of phase 2 of the deal which is when we get a part 7 transfer through that actually novates the liabilities from the names and ends their involvement with Lloyds once and for all.

On the next line claims and provisions has reversed its sign. Now this the line where we put through the undertakings that council give at their discretion to meet the shortfalls of insolvent members. For several years that has been a large debit to the P&L. In 2007 it has ended up being a credit. It's ended up being credit because those members are running off sufficiently well that undertakings that we've previously given we have now concluded some of those will no longer be necessary either in the short term or indeed the long term. Worth noting that at its meeting yesterday the council approved undertakings for 2008 with £13 million, one three, so across 2007 and 2008 combined our current expectation is that we will basically be flat in terms of central fund undertakings.

Moving down, you can see a big pick up in the corporation of Lloyds and its subsidiaries. I would not pay any attention to it because if you move to the penultimate line you can see other adjustments for solvency purposes have gone the other way. The re-evaluation of our pension scheme liabilities under IFRS is very volatile. It has created a big credit in our assets this year and increased our assets, but that isn't off-set by much more solvency adjustments, so those two net out.

Finally then you can see the Tier 1 subordinated debt issue coming in, put all that lot together and we end up at almost £2.5 billion or central resources up over 20% year on year. So I guess by way of conclusion on the funds I would say another strong year with a pre-tax return that over

the five year period now has given us almost a 20% return on capital. We have clearly put the problems of the past behind us with the Equitas deal and that together with the strong back year developments, the credit on undertakings and so on leaves us in a very, very strong position from which to face the downturn in the market that we are now seeing. So on that point, I will hand back to Richard.

**Richard Ward:** Thanks Luke. Luke mentioned the downturn we are now seeing. We have had a good year in 2007, we have had strong profits driven by good underwriting environment, driven by strong investment returns benign Cat season and also prior year releases and I am being continually asked as we were this morning by the media – what does this mean going forward. The very clear message going forward is that market conditions are getting a lot tougher, the cycle is clearly softening, business is clearly softening and we now really have to focus on managing the cycle, underwriting discipline, underwriting for profit. That position is just bought out by this one slide where on the left hand side I have just plot out the combined ratio for re-insurance, property and casualty. Those three lines account for roughly three quarters of all the premium that we write in the Lloyds market and so you have got the calendar year combined ratio and whilst it is showing slight deterioration against 2006 it's not that significant; for instance re-insurance moving 81% to 82% on a combined ratio basis. On the right hand side I am plotting out the combined ratio for those three classes of business on an accident year basis so we have stripped out the prior year releases. There you can see the deterioration in rates far more easily to the extent that casualty on a calendar year basis is showing a combined ratio of 93% on an accident year basis for 2007 is showing a combined ratio of 102%.

So that is just an indication of the challenges that we are going to face in 2008 and the softening cycle that we are going to have to deal with along with quite clearly the financial turmoil that we have in the market. So what is our focus going to be in 2008. It's quite clearly going to be cycle management. Building on our strengths and building on the position that we have developed over the past five years and really focusing in on cycle management, focusing on underwriting performance and underwriting for profit. We do believe we are well positioned to do that. Lloyds today in 2008 is not the Lloyds of the early 2000's. We are a very different business today than we were then. Primarily we have franchise performance structure in place; we have our performance framework in

place. As I mentioned earlier we have these minimum standards now for risk management for underwriting and for claims. Rolf and his team go out and visit our managing agents and syndicates on a regular basis to ensure that they meet those minimum standards. Through adherence to those minimum standards we do believe we will be able to focus on underwriting discipline and focus on underwriting for profit.

Luke has talked a lot about our capital position – we are in a robust financial position. Central assets over 2 billion now for the first time we have gone through the 2 billion level. We have a very strong capital position. We have a good ICA process in place. It's now been running for three years, this is our third year. That has been well accepted by the market and by the FSA and through that ICA process the capital setting process and our central fund, we do have a strong financial position. On the rating side we have had our rating upgrade to A+, we are now on a stable outlook, and I think that as a result of that with our A+ rating and a stable outlook we are able to attract the right sort of business that we want to be seen in the Lloyds market place. Lot of discussion and I am sure we'll get questions on sub prime and the credit crunch and the impact it has on Lloyds as you have seen from Luke's side, the impact has been minimal and in part that's because we have taken a conservative approach, particularly on our asset side and on our asset mix to the extent we have no sub prime exposure on the asset side. So that conservative approach has done us well in 2007 and I am sure that will be helping our position as we go through 2008 and the turmoil that we are seeing in the financial markets.

And of course, finally, we have produced our three-year plan at the beginning of this year. That plan sets out the work we are going to undertake around performance management, around capital, around market access, around business process reform and through the delivery of that plan we continue to build on the strengths of Lloyds and ensure that we remain the efficient, the effective market place for the trading of specialist risks. And the attraction of Lloyds is seen by the interest that we now have across the globe in businesses wanting to either acquire Lloyds businesses or set up inside Lloyds. We will continue our work to deliver that three-year plan and build on what we have achieved to date.

So in summary it is a good financial performance for 2007, but it is going to be a difficult environment in 2008 and looking forward and that

environment is being driven by the deteriorating underwriting conditions as well as the turmoil that we have in the financial markets.

So with that I will show you our disclaimer, which I am sure you have all read, and now move on to questions. And when asking questions based from the web, if we have any questions from the web or from the floor, would you mind stating your name and company, just for those who cannot see who you are or where you are, know who you represent. Any questions?

**Joanna Parsons:** Joanna Parsons, ABN Amro. Morning. A couple of questions if I may. Firstly, on sub prime as a generic issue, I have heard people comment that it could in fact have an impact that is not dissimilar to KRW in terms of financial capital impact. I was wondering what you would, how you would comment on that. Do you think it could have the impact on the insurance industry, obviously it has had a big general financial impact but whether it would have the same sort of impact on the insurance industry? And my second question is, you talked about doing a survey on customer satisfaction. Is that satisfaction from the people who are actually the users of Lloyds, i.e. the businesses or is this also the end customer and how they are perceiving you because I would imagine that, as we go into a soft cycle, service becomes of increasing importance, and that is how you will tend to differentiate yourselves? And my last question is on investment strategy. Again there is the theory that as underwriting risk capital reduces that one might want to increase perhaps a bit, maybe not quite today, but the investment appetite a little bit more and if you could comment on that as well?

**Richard Ward:** If I could take the second question on customer satisfaction and ask Rolf to comment on sub prime and Luke on the investment side. On the customer satisfaction survey, we do actually interview a wide variety of stakeholders, so for instance we interviewed 500+ what I deem to be customers which are brokers and insurance policy holders, people having to deal with Lloyds on a regular basis. In addition to that we are undertaking a separate survey of our managing agents, where we actually spoke to 400+ staff in the managing agents to get their view of the service that we are providing. We ask different questions obviously of the different stakeholder groups, but the very clear message that we are getting out from both these groups at this point in time is that the work we are undertaking particularly around improving the efficiency around the

processing of claims, around the issuing of documentation, around the speed of quotes; those three areas we are seeing significant improvement in the quality of service we are providing, so we can link that back to initiatives such as ECF, initiatives such as A&S and the contract certainty work that started in 2005, and delivered in 2006 and 2007, we can link that improvement in performance back to those three initiatives.

Going forward we will have to see what the customers say at the end of 2008 when we start the survey in the beginning of 2009, and as we go through the softening cycle, I am absolutely convinced the ultimate customer, the insured, will be more and more concerned about the quality of service they are getting from Lloyds as a marketplace, and we do know that brokers are now focusing on this issue of quality of service, speed of paying claims, speed of issuing policy documentation and they are starting to differentiate markets and playing that back to the customer so the customer is aware and can make an informed choice of where they want to place their business. But I believe that through the initiatives that we have we will continue to improve the quality of service and ensure that we remain the marketplace of choice for those who wish to trade specialist risks. Rolf, could you take the first question.

**Rolf Tolle:** Thank you Richard. If I can split the answer within two things. I think one is sub prime impact into the world wide insurance industry. I think comparing to KRW, in my opinion is quite a stretch because as you know KRW is a 60-billion loss to the industry and the highest number I have seen so far being presented is 8-billion for sub prime. If we limited sub prime because there is another issue which is called credit crunch which is a much wider issue which I think will involve many areas on the liability and on the asset side. But if we concentrate on sub prime then I think from a Lloyds perspective as Richard and Luke said earlier, it is by magnitude, a much smaller event for us than we had with Enron, Worldcom and laddering; and the reason for that is the portfolio is different. What we have done in the meantime is we have systems in place where we pick up all notifications which are relating to sub prime, we have also given the market a definition what we mean by that, because there is this vagueness if you will where certain losses were definitely not sub prime get thrown into the sub prime pot, but we have given a definition we are following up, we've said publicly the less than 100 notifications by the end of February. We are well below the £100-million mark from the gross perspective. I have in addition spoken to everybody who has been

involved and also have had discussions on their reserve policy and I am very satisfied what I have heard. I think the market has addressed it in a very conservative way. So rest assured, it is not as big a problem or a challenge as KRW was for this market.

**Luke Savage:** We have been asked the question do we think that sub prime, credit crunch generally might put a squeeze on the capital available to the Lloyds market. So far we have seen no signs of that whatsoever and we have been talking to our principal bankers who support the market. There is nothing to suggest that that would be the case. In fact we think that a lot of our capital comes from letters of credit. It is actually great for a bank that they can earn their risk premium without having to find the liquidity in terms of the cash to put up, so we do not think there is any issue there either.

Just on the investment strategy I entirely agree with you, and I think one of the things we have seen as a result of the increase in sophistication of the asset management resources across the market is that as people are cutting back on their underwriting appetite, we are seeing some explicitly saying they are shifting risk appetite from the liability side of the balance sheet to the asset side of the balance sheet. We are comfortable with that, we are comfortable with it because of the level of expertise that is overseeing it within the managing agents. We are comfortable because it is coming from what is generally a very conservative place to begin with. As far as our central assets are concerned, and the assets we manage centrally as well as central fund another £3.5-billion that we look after on behalf of syndicates, our focus there is not necessarily on taking more risks, it is on actually just optimising the asset disposition for any given risk level. So we have not increased our risk appetite at this point, what we have done through the diversification is get ourselves to a point where we think we get better, less volatile returns for that same given level of risk.

**Richard Ward:** Thanks Luke. Any questions from the Webcast at all? No. Any questions from the floor?

**Derek Campbell:** Derek Campbell from Legal & General. Can I just follow up Luke on the investment strategy. I understand you are comfortable with the investment strategy. You have done very well on hedge funds, but only been in them for seven months. How comfortable are you that you

can liquidate those positions in a timely fashion should you need to and how many hedge funds are you invested in.

**Luke Savage:** Some context here. Our hedge funds are only something like 5% of our surplus assets i.e. if you take the total central assets, knock off those that are hedging the subordinated debt liabilities, knock off those that are earmarked to meet the undertakings that council have given, if you take the surplus part it is only something like 5% of that pot. We are not invested directly in any hedge funds, we are invested in funds of funds and we are doing that through a managed portfolio approach where we can liquidate within a matter of weeks.

**Richard Ward:** Any other questions.

**John Borgas:** John Borgas from Equity Development. Are you increasing the ICA's for syndicates in an inverse proportion to the fall in premium rates for their classes; and if so have you got a very sophisticated computer programme to do it?

**Luke Savage:** We do not have to increase the ICA's as rates fall; the very nature of the ICA models that the managing agents use, mean that their own ICA's will increase as rates fall because there is less inherent profitability in the business that will just drive up the amount of capital that their ICA throws off as being needed to support that business. So to be clear the syndicate ICA's are not something which we create in the centre. Every managing agent prepares their own capital calculation for their own book of business. We validate that and make sure that they are being prepared appropriately and sufficiently conservatively, but it is their number and they will naturally increase as the market softens.

**Richard Ward:** Any other questions? Well if there are no further questions, thank you very much for your attendance here and on the web. Thank you.