ISSUED
August 2009

COMPANY PROFILE & FINANCIAL STRENGTH

REPORTS

Scottish Widows

AKG

Accessible - Comparative - Independent

Analysis by AKG Actuaries & Consultants Ltd

Background

AKG's Company Profile & Financial Strength Reports are designed to meet the information needs of advisers and analysts in assessing the relative strengths of UK long term insurers. Two different styles of report are published by AKG - FULL reports and SHORT reports. A FULL report is produced for each of the leading provider companies in the market, which participate in the production of the reports. For each remaining provider company which is covered, a SHORT report is produced.

This is a FULL report.

Each report collates relevant information from a range of sources such as a company's returns to the FSA, its report & accounts and material provided by the companies themselves, and incorporates expert independent assessment. For FULL report companies, the process is augmented by regular meetings and other communications with AKG.

PLEASE NOTE: This report should be read in conjunction with AKG's User Guide to AKG's Company Profile & Financial Strength Reports, a copy of which is available on-line at www.akg.co.uk

About AKG

AKG is an actuarially based consultancy specialising in the provision of ratings, information and market assistance to the financial services industry.

Assistance to Provider Companies

AKG assists providers in:

- Financial strength analysis, ratings and presentation
- Data and information provision
- Actuarial consultancy
- Distribution consultancy

Assistance to Financial Intermediaries

AKG assists intermediaries in:

- Financial strength analysis
- Best advice panel services
- Data and information provision
- Actuarial and technical support

Information Products

AKG also provides other regularly updated information products to assist providers and intermediaries, including:

AKG's Offshore Profile & Financial Strength Reports
Available free of charge to IFAs registering online at www.akg.co.uk

AKG's UK Life Office With Profits Report
Designed to provide further depth in the assessment of with profits funds.

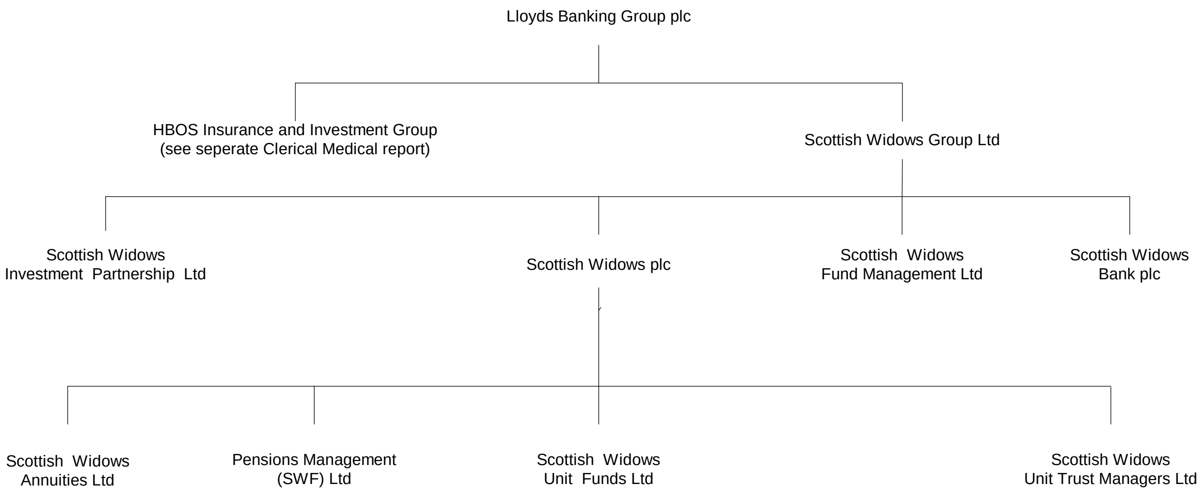
For further details, please contact AKG: Tel: +44 (0)1306 876439 or email akg@akg.co.uk

Index

Overview

Lloyds TSB Group plc was renamed Lloyds Banking Group plc (LBG) in January 2009 following the acquisition of HBOS plc, to form the largest retail bank in the UK, part owned 43% by HM Treasury. Within this the Insurance Division encompasses all the insurance companies that previously operated within the two banks. Scottish Widows, acquired by Lloyds TSB plc in March 2000, distributed through the Lloyds branch network, IFAs and directly via the telephone and the internet. There are four UK life subsidiaries which operated under the Scottish Widows brand - the main company Scottish Widows plc, together with the specialist subsidiaries Scottish Widows Unit Funds Ltd (SWUFL - linked life and pensions business), Scottish Widows Annuities Ltd (SWAL - non-profit pension annuities), and Pensions Management (SWF) Ltd (PMSWFL - managed pension fund business). HBOS operated on a multi-brand, multi-channel approach, with Clerical Medical Investment Group (CMIG), Halifax Life, St. James's Place and St Andrew's Life. CMIG was the primary intermediary product provider, together with Clerical Medical Managed Funds Ltd (CMMF), CMI Insurance Co (an Isle of Man based company) and HBOS Investment Fund Managers Ltd (OEICs). CMIG is also the main product provider to the Clerical Medical Europe (CME) business, which writes business, including with profits, in several mainland European countries. The integration of two significant financial services organisations represents both a risk and an opportunity and it is likely to be some time before the final shape of the combined organisation is determined. At the time of writing this report it has been decided that with effect from July 2009 the LBG Insurance Division distributes its intermediary life, pensions and investment business through a combined salesforce operating under the Scottish Widows brand for pensions business. The Clerical Medical brand will be retained for some investment business for the time being but the intention is to phase out the Clerical Medical brand for new business in 2010. In August 2009 LBG announced that it had agreed to sell Insight to BNY Mellon for £235m, following which the management of Clerical Medical funds, currently managed by Insight, will switch to Scottish Widows Investment Partnership (SWIP). Further integration in terms of the bank distribution and rationalisation of component life companies to drive capital efficiencies is also anticipated in the medium term.

Corporate Structure (simplified)



Ratings

Company	Financial Strength Ratings				Supporting Ratings		
	Overall	With Profits	Non Profit	Unit Linked	Service	Image & Strategy	Annual Review
Scottish Widows plc	**B+**	★★★★	★★★★★	★★★★	★★★★★	★★★★	★★★★★
Scottish Widows Unit Funds Ltd	**B+**	▣	▣	★★★★	★★★★★	★★★★	★★★★★
Scottish Widows Annuities Ltd	**B+**	▣	★★★★★	▣	★★★★★	★★★★	★★★★★
Pensions Management (SWF) Ltd	**B+**	▣	▣	★★★★	★★★★★	★★★★	★★★★★

Summary Financial Data

Key Financial Data (for y/e: 31/12/08)

LT Admissible Assets (by	2006 £000's	2007 £000's	2008 £000's
Scottish Widows plc	26,492,081	24,795,521	19,546,182
Scottish Widows Unit Funds Ltd	22,236,027	24,948,075	21,609,775
Scottish Widows Annuities Ltd	5,538,624	6,003,250	6,072,977
Pensions Management (SWF) Ltd	2,510,969	2,670,608	2,025,478
Total Assets	56,777,701	58,417,454	49,254,412

LT Admissible Assets (by asset type)	2006 £000's	2007 £000's	2008 £000's
Fixed Interest	12,392,011	11,334,156	10,566,812
Equities	8,970,412	8,443,621	5,257,913
Property	1,352,890	1,307,440	1,069,972
Linked	29,833,457	32,343,405	26,789,925
Other	4,228,931	4,988,832	5,569,790
Total Assets	56,777,701	58,417,454	49,254,412

LT Liabs & Margins (by type)	2006 £000's	2007 £000's	2008 £000's
Non Linked Non Profit	5,990,404	6,602,954	7,002,940
Non Linked With Profits	6,512,319	5,996,180	5,705,354
Accum'lg With Profits	7,679,059	6,921,801	6,300,067
Linked	29,930,862	32,464,770	26,913,529
Surplus c/f	396,768	121,097	109,188
Other liabilities	859,799	842,707	754,118
Investment Reserves	5,408,491	5,467,945	2,469,216
Total Liabilities/Margins	56,777,701	58,417,454	49,254,412

Net Inflow Data (for y/e: 31/12/08)

Net Inflow (by Company)	2006 £000's	2007 £000's	2008 £000's
Scottish Widows plc	-2,256,296	-1,796,233	-1,592,383
Scottish Widows Unit Funds Ltd	2,470,795	1,878,377	1,251,617
Scottish Widows Annuities Ltd	282,103	217,060	-105,545
Pensions Management (SWF) Ltd	-248,514	4,153	-333,580
Net Inflow(-Outflow)	248,088	303,357	-779,891

Net Inflow (by payment type)	2006 £000's	2007 £000's	2008 £000's
Premiums	6,854,389	7,730,484	6,661,507
Death/disability pmts	240,700	235,016	266,323
Surrenders	4,834,618	5,399,651	4,783,125
Annuity Payments	476,068	513,298	540,888
Maturities	1,054,915	1,279,163	1,851,062
Net Inflow(-Outflow)	248,088	303,357	-779,891

Net Inflow (by business type)	2006 £000's	2007 £000's	2008 £000's
UK Life	-635,427	-842,212	-1,260,949
UK Pension	970,210	1,172,936	492,912
Overseas	-86,695	-27,367	-11,854
Net Inflow(-Outflow)	248,088	303,357	-779,891

New Business Data (for y/e: 31/12/08)

New Single Premiums (by Company)	2006 £000's	2007 £000's	2008 £000's
Scottish Widows plc	4,612,179	5,402,924	4,231,836
Scottish Widows Unit Funds Ltd	0	0	0
Scottish Widows Annuities Ltd	2	0	0
Pensions Management (SWF) Ltd	720	151,877	79
Total (Direct + External Reins)	4,612,901	5,554,801	4,231,915

New Single Premiums (by business type)	2006 £000's	2007 £000's	2008 £000's
UK Life	1,265,704	1,483,974	887,877
UK Pensions	3,347,198	4,070,827	3,344,038
Overseas	0	0	0
Total (Direct + External Reins)	4,612,901	5,554,801	4,231,915

New Regular Premiums (by Company)	2006 £000's	2007 £000's	2008 £000's
Scottish Widows plc	429,445	420,988	549,745
Scottish Widows Unit Funds Ltd	0	0	0
Scottish Widows Annuities Ltd	2	1	2
Pensions Management (SWF) Ltd	52,204	11,330	8,453
Total (Direct + External Reins)	481,651	432,319	558,200

New Regular Premiums (by business type)	2006 £000's	2007 £000's	2008 £000's
UK Life	53,862	56,074	65,019
UK Pensions	427,789	376,246	493,182
Overseas	0	0	0
Total (Direct + External Reins)	481,651	432,319	558,200

2008 saw the group move from net inflow to net outflow, with lower premium income and increasing claims. It is life business where the outflow is occurring; pensions still shows inflows albeit reduced from 2007. Lower surrenders were more down to depressed values rather than a real slowdown in surrender activity. The bias towards pensions is clear and will be reinforced by the decision to market pensions under the Scottish Widows brand from mid 2009, with life investment products being sold under the Clerical Medical brand into CMIG.

Combined assets within the various UK life companies within the Insurance Division of LBG were in excess of £107bn as at December 2008.

Corporate Data

Ownership	Lloyds Banking Group plc
Open to New Business?	Yes
Year Established	2000
Head Office	69, Morrison Street Edinburgh EH3 8YF
Tel:	0131 655 6000
Fax:	0131 662 4053
Administration Office	As above
Website - Consumer	www.scottishwidows.co.uk
Website - IFA	www.scottishwidows.co.uk/ifa

Key Personnel

Chairman	Lord A P Leitch
Managing Director	A D Briggs
Group Finance Director	J McConville
Marketing Director	J Warburton
Client Services Director	J Stevens
IT Director	P Penney
Intermediaries Director	S Massey
Actuarial Director	A M Eastwood
With Profits Actuary	K M Doerr

Company Background

In 1815, the Scottish Widows Fund and Life Assurance Society opened as Scotland's first mutual life office, for the widows, sisters and other female relatives of deceased members. It set up a managed pension fund subsidiary in 1968, a unit-linked subsidiary in 1981, and Scottish Widows Bank was launched in 1995.

In March 2000, when Lloyds TSB plc completed an agreed takeover of Scottish Widows, Scottish Widows plc was established to acquire the assets and liabilities of the Society, with the exception of an element of conventional non-profit pensions business, which was transferred to the newly formed subsidiary SWAL.

There has been a series of reshuffles within the group. In 2004, the majority (£7.4bn) of the business of Lloyds TSB Life Assurance Company Ltd was transferred into the company. In 2005 the company became the owner of Abbey Life Assurance Company Ltd (subsequently sold to Deutsche Bank in 2007) and in 2006 it became the owner of Scottish Widows Unit Trust Managers Ltd (SWUTML).

Overall Financial Strength B+

The company is both strong and well managed in itself and can be considered as such even on a standalone basis. Coverage for it Capital Resource Requirement improved in 2008. However, a key component of its financial strength is derived from its parent, Lloyds Banking Group, whose strength has diminished following the HBOS acquisition. Notwithstanding this, the acquisition itself brings with it a number of positive aspects, not least the large scale additional distribution it affords and the scale it can add to the Scottish Widows brand from non-organic activity. On the flipside though, in the current environment this banking parent also brings reputational challenges, potential susceptibilities to political unpredictabilities given its part government ownership and the demands of a significant integration exercise as a result of the HBOS acquisition.

Reinsurance

Approach

Whilst there are a number of reinsurance treaties in force, providing conventional risk protection, with a variety of external reinsurers, the major part of the company's reinsurance arrangements are with other companies in the group. These include arrangements to reinsure certain liabilities to its specialist subsidiaries SWAL (pension annuity business) and SWUFL. Linked life business that had previously been reinsured with SWUFL was recaptured on 1 January 2009. Reinsurance premiums paid to other companies in the group through these arrangements totalled £4.08bn in 2008 [2007: £5.6bn].

Analysis of Reserves	**2006 £000's**	**2007 £000's**	**2008 £000's**
Gross reserves	45,701,572	47,625,043	42,724,590
Reinsurance ceded - external	427,330	632,682	939,150
Reinsurance ceded - internal	25,281,211	28,536,875	25,330,240
Net mathematical reserves	19,993,031	18,455,486	16,455,201

Non Profit Business

General

Most non profit pension annuity business is reinsured to SWAL. This arrangement also includes a small amount of pension term assurance business. All reinsurances are on an original terms basis, adjusted to reflect administration expenses borne by the parent. Much of the old mutual company's pensions annuity business was transferred directly into the subsidiary, but some went to Scottish Widows plc and was then reinsured to the subsidiary. Gross non profit reserves increased to £5.4bn at the end of 2008, of which £4bn was reinsured out.

Non Profit Reserves	**2006 £000's**	**2007 £000's**	**2008 £000's**
UK Life	257,410	432,000	577,262
UK Pensions	581,410	568,501	854,651
Overseas	2,327	2,341	2,287
Total net NP reserves	841,147	1,002,842	1,434,201

Non Profit Financial Strength ★★★★★

Retained non profit business forms a relatively small part of the company's business with a majority of liabilities reinsured to a subsidiary. In addition to the support from free assets, comfort is derived by the volume of with profits business in force, and from the parentage.

A similar level of financial strength is deemed to apply to non profit business held elsewhere in the Lloyds Banking Group.

Unit Linked Business

Approach

Scottish Widows offers a wide range of funds from ready-made investment portfolios to specialist funds, the aim being to meet differing investment needs. The funds are grouped into four categories: Scottish Widows core life and pensions funds (managed by SWIP) including a fund of fund offer; Scottish Widows Manager of Manager funds (in conjunction with Russell Investment Group); Scottish Widows With Profits Funds and Scottish Widows Externally Managed Funds. Whilst an open architecture option is available through the Retirement Account, giving access to over 1,000 external funds through FundsNetwork, a guided fund range is generally available for other products. This fund range was reviewed in 2007 and the outcome of this review was a core selection of funds managed by SWIP and links to 12 external fund managers (down from 17). Scottish Widows is committed to ongoing monitoring and governance of these funds and their managers, with the intention of providing access to quality funds, maintaining credibility and providing a source of differentiation.

The vast majority of the company's property linked business is reinsured to SWUFL, the specialist unit linked subsidiary, whilst the majority of index-linked business is retained within the company. Linked liabilities reinsured out amounted to £22bn at the end of 2008 [2007: £25.1bn] but will reduce in 2009 following the life recapture (see below).

The reinsurance arrangements now only apply to unit linked pensions business following the recapture of life unit linked business in January 2009. From April 2001, it has also covered substantially all of the expense risks associated with the range of Pensions Solutions products and stakeholder pension policies and from 2007 the Retirement Account. The subsidiary is entitled to substantially all of the charges from the latter policies in exchange for a reinsurance commission which is paid back to the company as the new business is written. All managed pension fund business is written directly by the specialist subsidiary, PMSWFL.

Some consolidation of unit linked funds appears inevitable as the integration with Clerical Medical proceeds. Specifically the life unit linked funds will be effectively closed to new business post July 2009 with the dropping of Scottish Widows life unit linked range in favour of Clerical Medical's.

Linked Reserves	2006 £000's	2007 £000's	2008 £000's
UK Life	4,894,008	4,453,619	2,891,983
UK Pensions	92,454	103,231	122,986
Overseas	34,844	34,028	25,548
Total net linked reserves	5,021,306	4,590,877	3,040,518

Unit Linked Financial Strength ★★★★

Although the company's linked business is primarily reinsured to a subsidiary, its fortunes are bound up with this company. In addition to the support available from the free assets, a high degree of comfort is derived by the volume of with profits business in force, and from the presence of the wider parental group.

Unit linked business held elsewhere in the Lloyds Banking Group is deemed to enjoy similar financial strength.

With Profits Business

Approach

The With-Profits Fund contains conventional with profits, the with profits investment element of unitised with profits (including offshore) and certain non profit policies allocated to the fund. The Flexible Options Bond introduced With-Profits Growth and Income Funds (both within the With-Profits Fund).

With Profit Reserves	2006 £000's	2007 £000's	2008 £000's
UK Life	4,511,708	3,845,548	3,228,252
UK Pensions	9,501,620	8,937,949	8,689,302
Overseas	117,250	78,270	62,929
Total net WP reserves	14,130,578	12,861,767	11,980,482

Profit Sharing Philosophy

The aim is to safeguard solvency without assuming recourse to extra capital, whilst managing the business in line with PRE. Factors (other than contractual entitlements) taken into account include past practice of the Society and industry and representations made to policyholders. At demutualisation, a memorandum account was set up, available to cover the cost of meeting GAO liabilities. The company expects this to be sufficient but shareholders will meet any excess. Enhancements to payouts under provisions in the demutualisation scheme are currently around 1% (previously 2%).

Asset Allocation

Most with profits business had an asset share EBR of 53% at the end of 2008 [2007: 66%]. For Flexible Options products, asset mix differs by fund: the With-Profits Growth Fund aims at 85% equity and property, whilst the With-Profits Income Fund invests entirely in corporate bonds and property. The main fund returned -18% during 2008 [2007: 5%]. Put options are now in place to protect the fund from further falls.

Distribution of Surplus	2006 £000's	2007 £000's	2008 £000's
To Policyholders	388,956	548,439	580,516
Other Transfers	18,000	38,000	23,000

Realistic Balance Sheet	2006 £000's	2007 £000's	2008 £000's
Working capital	1,124,280	944,977	258,975
Risk capital margin	57,167	76,106	241,000
Realistic excess available	1,067,113	868,871	17,975
Working capital ratio	5.8%	5.3%	1.9%
RCM as % of assets	0.3%	0.4%	1.8%
Realistic xs available ratio	5.5%	4.9%	0.1%

Market movements meant working capital reduced substantially, and this together with the increased cost of financial options saw the RCM increase to £241m. Under the Scheme of Transfer the With-Profits Fund has access to support assets external to the fund and at the year end these amounted to £371m [2007: £1bn]. The WPICC fell to £206m [2007: £2.8bn].

With Profits Financial Strength ★★★★

Retained business in this company is predominantly with profits. Whilst it has been impacted by the recent market falls, the position of the fund remains satisfactory.

Key Financial Data (for y/e: 31/12/08)

Capital Resources	2006 £000's	2007 £000's	2008 £000's
Core tier one capital	8,816,733	8,143,887	5,484,047
Tier one waivers	0	0	0
Other tier one capital	500	0	0
Tier one deductions	-906,666	-953,664	-1,088,182
Total tier one capital	7,910,567	7,190,223	4,395,865
Tier two capital	533,052	540,863	603,823
Adjustments and deductions	-555,766	-979,506	-1,326,957
Total Capital Resources	7,887,853	6,751,580	3,672,731
CR outside the fund	2,186,461	1,180,488	1,150,738

Market falls have impacted overall capital resources. The company has followed a course of repatriating capital to the parent, some £3.8bn since 2005, including £220m in 2008. The group is currently reviewing its capital structure following the HBOS acquisition.

Long Term Business Admissible Assets	2006 £000's	2007 £000's	2008 £000's
Fixed Interest	7,288,962	5,851,562	5,265,939
Equities	8,970,412	8,443,621	5,257,913
Property	1,352,890	1,307,440	1,069,972
Linked	5,067,978	4,610,510	3,067,132
Other	3,811,839	4,582,388	4,885,226
Total Assets	26,492,081	24,795,521	19,546,182

Equity and property holdings have reduced. The EBR of the With Profits Fund has reduced further since the 2008 year end, to 52%, and is protected through put options. All non profit equities have since been sold and remaining property is also to be sold.

Free Assets	2006 £000's	2007 £000's	2008 £000's
Free Assets (Exc Fin Eng)	3,681,161	2,728,469	2,292,981
Financial Engineering	0	0	0
Free Assets (Published)	3,681,161	2,728,469	2,292,981

Free Asset Ratios	2006 %	2007 %	2008 %
FAR (Exc Fin Eng)	13.9	11.0	11.7
FAR (Published)	13.9	11.0	11.7

CRR Coverage Ratios	2006 %	2007 %	2008 %
CRRCR (Exc Fin Eng)	187.5	167.8	266.2
CRRCR (Published)	187.5	167.8	266.2

Free assets proved resilient in the face of the market movements and solvency levels improved, somewhat against the market norm.

Long Term Business Liabilities & Margins	2006 £000's	2007 £000's	2008 £000's
Non Linked Non Profit	841,147	1,002,842	1,434,201
Non Linked With Profits	6,512,319	5,996,180	5,705,354
Accum'lg With Profits	7,679,059	6,921,801	6,300,067
Linked	5,021,306	4,590,877	3,040,518
Surplus c/f	239,847	46,973	0
Other liabilities	789,912	768,903	596,826
Investment Reserves	5,408,491	5,467,945	2,469,216
Total Liabilities/Margins	26,492,081	24,795,521	19,546,182

Retained business is still predominantly with profits, although the level of unit linked business will change following the January 2009 recapture, of approximately £4bn. There is also a significant proportion of linked business relating mainly to the ex-Lloyds TSB Life portfolio. During 2008, volumes of with profits business in force continued to shrink. The company has substantial exposure to guaranteed annuity options, which were expected to cost £1.3bn at the end of 2008 [2007: £1.09bn]. There is a provision of £66.3m in relation to pensions mis-selling.

Key Revenue Items	2006 £000's	2007 £000's	2008 £000's
INCOME			
Premiums	1,096,225	1,312,618	1,592,699
Investment Income	1,062,234	998,676	969,070
Investment Increase	-517,131	84,880	-853,866
EXPENDITURE			
Commissions	248,962	682,077	646,026
Policy claims	3,352,521	3,108,851	3,185,082
Expenses	302,907	277,419	258,144
TRANSFER to P&L	750,000	300,000	110,000
INCREASE in fund	-2,817,433	-1,735,005	-2,078,533

The revenue account clearly shows the policy of transferring monies form the long term fund to the shareholders fund to support dividend payments over recent years: £110m in 2008 following £1.05bn in the two previous years. Other items in the revenue account (shown on a net basis) are distorted by intra-group reinsurance. Gross premiums fell by almost 15% on lower single premium business. Gross surrenders also fell, by over 18% but the effect of reinsurance led to a net decrease of 30%. Both initial expenses and commissions fell commensurate with falling new business levels. Overall the group experienced a net outflow in 2008.

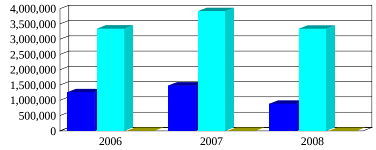
Expense Ratios	2006	2007	2008
New business (% APE)	41.2	84.2	69.6
Renewal (% reg premiums)	10.6	8.3	12.0
Renewal (% p.a. of mean fund)	0.68	0.59	1.03

Renewal expense ratios were impacted by a 5 fold increase in renewal commissions.

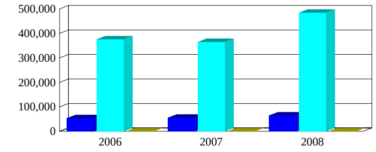
New Business Data (for y/e: 31/12/08)

		Single £000's	Regular £000's
Investment			
Bonds	With Profits	0	0
	Unitised WP	8,154	0
	Unit Linked	409,657	0
Endowment	With Profits	0	0
	Unitised WP	0	14
	Unit Linked	0	853
Guaranteed Bonds		0	0
ISA / tax exempt		0	0
Annuities		1,224	0
Miscellaneous		0	0
Protection			
Whole Life	With Profits	0	0
	Unitised WP	0	0
	Unit Linked	0	8
Term	Ordinary	0	17,146
	Pension	0	56
IP	Individual	0	2,264
Critical Illness		0	22,372
Long Term Care		12	66
Miscellaneous		0	16,040
Pensions			
Individual	With Profits	0	576
	Unitised WP	91,394	4,835
	Unit Linked	1,967,495	120,895
CPA		642,893	0
Bulk Transfer Annuities		0	0
Miscellaneous		0	0
Group Business			
Pension		640,513	358,357
Life		468,830	2,024
IP		0	76
Critical Illness		0	4,163
Miscellaneous		0	0
TOTAL DIRECT BUSINESS		**4,230,172**	**549,745**
Overseas Direct (inc above)		0	0
External Reins (exc above)		1,665	0
Intra-Group Reins (exc above)		0	0
Industrial Branch (inc above)		0	0

New Single Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	1,265,704	1,483,974	887,877
UK Pensions	3,346,476	3,918,950	3,343,959
Overseas	0	0	0
Total (Direct + External Reins)	4,612,179	5,402,924	4,231,836
Growth Rate	17.0%	17.1%	-21.7%
Reins Accepted (Intra-Group)	0	0	0



New Regular Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	53,862	56,074	65,019
UK Pensions	375,583	364,915	484,727
Overseas	0	0	0
Total (Direct + External Reins)	429,445	420,988	549,745
Growth Rate	23.2%	-2.0%	30.6%
Reins Accepted (Intra-Group)	0	0	0



The majority of Scottish Widow's new long-term business is written into this company, with only £8.5m APE into PMSWFL, negligible amounts into SWAL and none into SWUFL in 2008. In new business terms pensions business continued to dominate during the year, particularly given the significant fall off in unit linked investment business, down over 50%. With profits bond sales rose over 60% but from a very small base. The group also saw increasing levels of protection business. Individual pensions saw good increases with Retirement Account now accounting for more than 50% of pre-retirement business and almost half of drawdown. Corporate pensions also performed well during the year.

Looking at the combination of all Scottish Widows' life, pensions and OEIC operations in 2008, the biggest element, IFA sales, fell 8%. Bancassurance sales were up 4% where a fall in sales of equity backed OEICs was partly offset by increased sales of capital protected savings products.

Scottish Widows Unit Funds Ltd

Corporate Data

Ownership	Lloyds Banking Group plc
Open to New Business?	Yes
Year Established	1981

Key Personnel

Chairman	J McConville
Director	C Clarke
Director	A M Eastwood
Actuarial Function Holder	K M Doerr

Company Background

The company, a wholly owned subsidiary of Scottish Widows plc since March 2000, operates as the Scottish Widows specialist linked life and pensions subsidiary. It does not write any business directly: all of its business is reinsured in from Scottish Widows plc. In 2004, this was extended to the reinsurance of an element of the business transferred from Lloyds TSB Life, involving a one-off reinsurance premium of £4bn. The company has a wide range of linked funds, mirroring the parent's marketing approach. Fuller details are contained in the section of the report relating to Scottish Widows plc.

In January 2009 the company ceased reinsuring linked life business, which from that date was retained within Scottish Widows plc. Approximately £4bn of assets and liabilities were transferred to the parent. The company continues to reinsure linked pensions business. Previously, the reinsurance arrangement involved the unit-linked liabilities under virtually all Scottish Widows plc's (including ex-Lloyds TSB Life) property-linked life and pension policies, as well as part of the life and critical illness risks for some linked life policies. From April 2001 it has also covered substantially all of the expense risks associated with the range of Pensions Solutions products and stakeholder pension policies and from 2007 the Retirement Account. The company is entitled to substantially all of the charges from the latter policies, less any reinsurance commission paid back to the parent as the new business is written [2008: £260m].

From 2001-2005, the company experienced valuation deficits each year due to the high volumes of business reinsured from the parent. During this period the company received capital subscriptions from its parent totalling £152m, followed by a further injection of share capital of £106m in 2008. Also in 2008 the company received further funding in the form of an additional contingent loan of £62m, bringing the total outstanding contingent loans to £614.7m including £115m of outstanding interest.

Overall Financial Strength B+

The company declared a profit of £2.8m for 2008 [2007: £5.4m]. Whilst the company has had increasingly negative basic free assets in its own right in recent years, despite having received regular capital subscriptions and contingent loans it continues to demonstrate a small, but positive, level of published free assets. Notwithstanding the decision, in Q1 2009, to repatriate reinsured linked life business to the parent and any potential post acquisition restructuring the company remains an integral part of the Insurance Division of Lloyds Banking Group and AKG believes that it would receive any necessary financial support from its parent, just as it has done over the last few years.

Key Financial Data (for y/e: 31/12/08)

Long Term Business Admissible Assets	2006 £000's	2007 £000's	2008 £000's
Fixed Interest	136,620	77,784	120,820
Equities	0	0	0
Property	0	0	0
Linked	21,982,978	24,771,726	21,413,028
Other	116,429	98,565	75,927
Total Assets	22,236,027	24,948,075	21,609,775

Free Assets	2006 £000's	2007 £000's	2008 £000's
Free Assets (Exc Fin Eng)	-381,953	-500,636	-546,911
Financial Engineering	475,166	526,432	614,722
Free Assets (Published)	93,213	25,796	67,811

Free Asset Ratios	2006 %	2007 %	2008 %
FAR (Exc Fin Eng)	-1.7	-2.0	-2.5
FAR (Published)	0.4	0.1	0.3

CRR Coverage Ratios	2006 %	2007 %	2008 %
CRRCR (Exc Fin Eng)	-683.1	-868.1	-988.4
CRRCR (Published)	291.1	149.9	234.9

Long Term Business Liabilities & Margins	2006 £000's	2007 £000's	2008 £000's
Non Linked Non Profit	0	0	0
Non Linked With Profits	0	0	0
Accum'lg With Profits	0	0	0
Linked	22,123,774	24,908,975	21,559,739
Surplus c/f	67,874	12,652	38,883
Other liabilities	44,380	26,448	11,153
Investment Reserves	0	0	0
Total Liabilities/Margins	22,236,027	24,948,075	21,609,775

New Business Data (for y/e: 31/12/08)

New Single Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	0	0	0
Overseas	0	0	0
Total (Direct + External Reins)	0	0	0
Growth Rate	0.0%	0.0%	0.0%
Reins Accepted (Intra-Group)	3,958,996	4,344,763	3,458,349

New Regular Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	0	0	0
Overseas	0	0	0
Total (Direct + External Reins)	0	0	0
Growth Rate	0.0%	0.0%	0.0%
Reins Accepted (Intra-Group)	359,358	286,293	369,180

Scottish Widows Annuities Ltd

Corporate Data

Ownership Lloyds Banking Group plc

Open to New Business? Yes

Year Established 2000

Key Personnel

Chairman	Lord A P Leitch
Deputy Chairman	A G Kane
Managing Director	A D Briggs
Executive Director	J McConville
Actuarial Function Holder	A M Eastwood

Company Background

The company is a wholly owned subsidiary of Scottish Widows plc, set up at the time of Scottish Widows' demutualisation in March 2000 to act as the group's specialist pensions annuity subsidiary. It writes (mainly via reinsurances accepted from other group companies) UK non-profit pension annuity business - immediate annuities, deferred annuities, reversionary annuities, and lump sum death benefits in connection with such annuity business. There is also a small amount of pension term assurance business. All business is non-linked, apart from a small amount of index-linked annuities. The bulk of the business is written on a single premium basis. From January 2008 the company ceased to write vesting with profits annuities business from GAOs previously reinsured from the parent. On 31st December 2004, an element of the long term business of Lloyds TSB Life Assurance Company Ltd was transferred to the company, consisting of UK pensions annuities in payment and pensions term assurance business. The acquisition involved the transfer of £613.6m of assets.

In March 2000, some of the old mutual company's pensions annuity business was transferred directly into this company, but some of it was transferred to Scottish Widows plc and then reinsured to this company. Since demutualisation, virtually all new business has arisen from reinsurances accepted from Scottish Widows plc and Pensions Management (SWF) Ltd. All reinsurances are on an original terms basis, adjusted to reflect administration expenses borne by the parent. Valuation deficits arising in 2001 and 2002 within the company led to a capital injection of £65m in 2002, followed by £200m of subordinated loan capital from Scottish Widows plc during 2004. In 2008 the company issued some £216m of additional share capital, at which time the subordinated loan of £200m was cancelled.

Overall Financial Strength B+

The company recorded a loss of £140m in 2008, a fact that the company attributes to the significant widening of credit spreads in 2008, a feature which alone led to losses of £180m over the year. A capital restructure during the year saw the company swap tier two subordinated debt for tier one share capital, followed by a small injection of £16m later in the year. Free assets again fell, along with coverage for the Capital Resource Requirement, although this remains adequate. The fall in new business is due to the decision not to reinsure vesting with profit annuities from January 2008, reducing new business by approximately £264m. The company remains relatively small, but, as an integral part of the Insurance Division of Lloyds Banking Group, AKG believes that it would receive any further future necessary financial support from its parent.

Key Financial Data (for y/e: 31/12/08)

Long Term Business Admissible Assets	2006 £000's	2007 £000's	2008 £000's
Fixed Interest	4,966,429	5,404,810	5,180,053
Equities	0	0	0
Property	0	0	0
Linked	271,532	290,561	284,287
Other	300,663	307,879	608,637
Total Assets	5,538,624	6,003,250	6,072,977

Free Assets	2006 £000's	2007 £000's	2008 £000's
Free Assets (Exc Fin Eng)	403,202	234,362	125,916
Financial Engineering	0	0	0
Free Assets (Published)	403,202	234,362	125,916

Free Asset Ratios	2006 %	2007 %	2008 %
FAR (Exc Fin Eng)	7.3	3.9	2.1
FAR (Published)	7.3	3.9	2.1

CRR Coverage Ratios	2006 %	2007 %	2008 %
CRRCR (Exc Fin Eng)	278.8	185.6	150.0
CRRCR (Published)	278.8	185.6	150.0

Long Term Business Liabilities & Margins	2006 £000's	2007 £000's	2008 £000's
Non Linked Non Profit	5,149,257	5,600,112	5,568,739
Non Linked With Profits	0	0	0
Accum'lg With Profits	0	0	0
Linked	274,863	294,360	287,844
Surplus c/f	89,047	61,472	70,305
Other liabilities	25,457	47,306	146,089
Investment Reserves	0	0	0
Total Liabilities/Margins	5,538,624	6,003,250	6,072,977

New Business Data (for y/e: 31/12/08)

New Single Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	2	0	0
Overseas	0	0	0
Total (Direct + External Reins)	2	0	0
Growth Rate	-92.6%	-100.0%	0.0%
Reins Accepted (Intra-Group)	628,471	601,899	307,312

New Regular Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	2	1	2
Overseas	0	0	0
Total (Direct + External Reins)	2	1	2
Growth Rate	100.0%	-50.0%	100.0%
Reins Accepted (Intra-Group)	137	62	53

Pensions Management (SWF) Ltd

Corporate Data

Ownership Lloyds Banking Group plc

Open to New Business? Yes

Year Established 1968

Key Personnel

Chairman	J McConville
Director	A M Eastwood
Director	A J November
Director	D Buckley
Actuarial Function Holder	K M Doerr

Company Background

Since inception, the company has operated as the specialist managed pension fund subsidiary within the Scottish Widows group.

When the old mutual company demutualised in March 2000, ownership of this company passed to Scottish Widows plc. The company is limited by guarantee and it does not have any ordinary share capital. Scottish Widows plc holds £50k of 7.5% debenture stock.

All business is written directly in the UK by the company on a unit linked basis (apart from £7.7m of non-linked vesting annuities, which are fully reinsured to the sister company SWAL). No premiums were paid under this treaty in the period 2005 to 2008.

Volumes of new business have tended to fluctuate from year to year, but have generally been fairly modest. Single premium new business in 2005 and 2007 was significantly higher than normal.

Overall Financial Strength B+

The company operated profitably in 2008, declaring a profit of £174k [2007: £179k]. It has negligible free assets in its own right but adequately covers its Capital Resources Requirement The parent provides a guarantee to the company that it will support a guarantee provided to the company by another subsidiary of the parent. Additionally, in 2003 and 2004, the company increased its minimum guarantee fund to comply with a new solvency requirement via gifts of £0.65m and £1.85m respectively from Scottish Widows plc. Repayment of this amount is not expected while the solvency requirement remains. The available capital resources of £4.7m are all held outside the long term business fund and consist entirely of core tier one capital.

As an integral part of the Insurance Division of Lloyds Banking Group, albeit a relatively small part, AKG believes that it would receive any further necessary financial support from its parent.

Key Financial Data (for y/e: 31/12/08)

Long Term Business Admissible Assets	2006 £000's	2007 £000's	2008 £000's
Fixed Interest	0	0	0
Equities	0	0	0
Property	0	0	0
Linked	2,510,969	2,670,608	2,025,478
Other	0	0	0
Total Assets	2,510,969	2,670,608	2,025,478

Free Assets	2006 £000's	2007 £000's	2008 £000's
Free Assets (Exc Fin Eng)	2,167	2,254	2,141
Financial Engineering	0	0	0
Free Assets (Published)	2,167	2,254	2,141

Free Asset Ratios	2006 %	2007 %	2008 %
FAR (Exc Fin Eng)	0.1	0.1	0.1
FAR (Published)	0.1	0.1	0.1

CRR Coverage Ratios	2006 %	2007 %	2008 %
CRRCR (Exc Fin Eng)	201.3	201.0	185.0
CRRCR (Published)	201.3	201.0	185.0

Long Term Business Liabilities & Margins	2006 £000's	2007 £000's	2008 £000's
Non Linked Non Profit	0	0	0
Non Linked With Profits	0	0	0
Accum'lg With Profits	0	0	0
Linked	2,510,919	2,670,558	2,025,428
Surplus c/f	0	0	0
Other liabilities	50	50	50
Investment Reserves	0	0	0
Total Liabilities/Margins	2,510,969	2,670,608	2,025,478

New Business Data (for y/e: 31/12/08)

New Single Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	720	151,877	79
Overseas	0	0	0
Total (Direct + External Reins)	720	151,877	79
Growth Rate	-99.7%	20,994.0%	-99.9%
Reins Accepted (Intra-Group)	0	0	0

New Regular Premiums	2006 £000's	2007 £000's	2008 £000's
UK Life	0	0	0
UK Pensions	52,204	11,330	8,453
Overseas	0	0	0
Total (Direct + External Reins)	52,204	11,330	8,453
Growth Rate	25.9%	-78.3%	-25.4%
Reins Accepted (Intra-Group)	0	0	0

Distribution

Method

Prior to the acquisition of HBOS by Lloyds Banking Group, Scottish Widows operated on a multi-channel basis, with its products available through IFAs (although protection products were no longer sold through IFAs), the Lloyds Bank branch network and directly from Scottish Widows via a call centre and the internet. The takeover of HBOS by Lloyds Banking Group has resulted in the need for a revised strategy which incorporates the combination of the capability afforded under the Scottish Widows operation and that of the HBOS life, pensions and investment operations. Perhaps the biggest element of this is the final shape of delivery through the combined bancassurance channel. However to date this remains to be decided, although some indications might be drawn from decisions that have been made in respect of the intermediary channel and common elements of rationale supporting this. Indeed in May 2009, the group announced a clear strategy to utilise the Scottish Widows brand for intermediary distribution, including a combined sales force from July 1st 2009. incorporating within this the existing product strengths of the Scottish Widows and Clerical Medical companies within a streamlined product range. Clearly Scottish Widows intermediary distribution now has the opportunity to cement a more significant footprint in terms of intermediary market share, afforded it by the integration of Clerical Medical. Post integration Scottish Widows will have 136 face to face account managers and 46 telephone based account managers in the intermediary channel. In addition it will have 19 sales managers, 13 key account managers and 11pensions and investment specialists. This capability, along with a greater use of account segmentation, positions the company well, albeit subject to an overarching requirement for a smooth integration within the wider business, which will be challenging.

Distribution Split	Regular Premium %	Single Premium %
IFAs	61.0	51.0
Multi-Ties	0.0	0.0
Tied Agents	23.0	43.0
Direct Sales	16.0	6.0
Direct Marketing	0.0	0.0

Image and Strategy

★★★★

Scottish Widows continues to be well placed to deliver on its key distribution and capital management objectives, not least because of its strong brand position, which enjoys a high level of recognition and is very highly regarded, relative to its life and investment company peers. The integration of HBOS life companies brings with it major challenges in terms of brand usage (the temporary retention of the Clerical Medical brand is potentially confusing) and a requirement to maintain image in a potentially difficult and turbulent period. This integration, however, also affords Scottish Widows significant opportunities for growth and other strategic developments, broadening, as it does, the product set and bancassurance distribution.

Further, the background environment includes the banking crisis and credit crunch, which has seen governmental involvement in the Lloyds Banking Group amongst other things and in general a further erosion in confidence and respect for the banking sector in the public consciousness.

Products

Overall Product Philosophy

A continued focus on more profitable and capital efficient products has meant a number of 'existing product' developments, rather than shifts in focus or approach. Product development is arranged so as to best meet the needs of the company's distribution within a co-ordinated framework. A wide range of products is offered, now with much more emphasis on unit linked. It revamped its corporate pensions offering in 2005. In 2006, in addition to a number of changes and additional options in existing product designs, new protection products marketed under the Virgin Money brand were introduced, a creditor product providing life cover for secured loans offered by Lloyds TSB Bank was introduced through the bank, a new range of protection products was launched under the Protection for Life wrapper, an insured SIPP was introduced, and pension term assurances were withdrawn. The Retirement Account was launched in a bid to meet the increasing flexibility demanded by customers without having to move to a SIPP structure, and reflects a move to RDR friendly products. In addition to the insured products shown below, OEICs and ISAs are offered via subsidiaries.

Products Currently Marketed

Investment Products

Written in Scottish Widows plc

Annuities
Investment Bonds (Capital Protected)
Regular Savings Plan

Protection Products

Written in Scottish Widows plc

Term Products
Critical Illness (rider & stand-alone)
Income Protection
Creditor insurance

Pension Products

Written in Scottish Widows plc

DSS Rebates
S32
Trustee Investment Bond
Conventional Annuities
Personal Pensions and Pension
Payment Cover Plan
Small Self Administered Scheme
Self Invested Personal Pension
Income Drawdown Plan
Unitised Annuity
Phased Retirement Plan
Stakeholder Pension Plan
Executive Pensions

Group Products

Written in Scottish Widows plc

Group Occupational Pensions
Stakeholder Pension Plan
Group Personal Pensions
S32A
CIMPs
Institutional Investment Bond

Written in Pensions Management (SWF) Ltd

Unit Linked Managed Pension Funds

Service

★★★★★

Approach

Scottish Widows aims to deliver excellent service and deliver on its vision of being 'the best life, pensions and investment company in the UK'. The specific service vision is stated as ‘to meet customer requirements, right first time, all the time, efficiently and with minimum variation’. Within this the company has been focused on a conscious shift from being product-centric to a more customer-centric ethos. Processes used for improvement include LEAN and Six Sigma.

The takeover of HBOS by Lloyds Banking Group, the resulting corporate development and the subsequent need for managing or integrating different businesses within a short and relatively unforeseen timescale is a significant threat within the Scottish Widows service component of its brand indentify as well as to operational performance. That said, the Scottish Widows business is approaching the significant workload and potential pitfalls of integration from a position of generally continued operational improvement over the last year, and a set of key metrics which continue to be at the upper end of industry experience. Integration activity is now evolving with both tactical and strategic work streams, across seven key areas. Success here will be vital to the operational health of what will become a business of increased size and complexity in the short to medium term.

e-Business

The company has a strong e-business focus and has won a number of accolades for e-business components in a number of product areas, most notably in retirement planning. From July 1 2009, online service from both Scottish Widows and Clerical Medical was available through one combined extranet homepage.

Service Standards & Awards

Scottish Widows recovered its service reputation following a temporary blip post-demutualisation. Following a number of poor years the Company has since achieved some of the highest ratings in industry service awards.

Outsourcing

The Lloyds TSB Group had a programme of outsourcing and offshoring a number of its processing and back office operations, primarily overseas, using the third party provider Xansa, which is already part of the Lloyds TSB infrastructure in India. 2007 saw a further phase in the continuation of the business administrative realignment. This included the opening of a second Indian site, and with the closure of its Chatham site, the movement of activity within the UK. Numbers of employees now offshore (all non customer facing) are now approaching 500. Decisions as to further outsourcing must await the outcomes of the integration.

Investment

Overall Approach

Internal funds under the Scottish Widows brand are managed by Scottish Widows Investment Partnership (SWIP). SWIP was created in 2000 following the merger of Scottish Widows Investment Management and Hill Samuel Asset Management. The SWIP focus is principally B2B, based on building investment solutions for institutional and wholesale clients and partners. It has an external as well as an internal focus.

SWIP's approach focuses on detailed, fundamental, proprietary research which it believes is key to making investment decisions. Companies are analysed over a full five year business cycle, giving SWIP a long term outlook. Whilst the greatest emphasis is on company research, bottom-up findings are validated with an analysis of wider macro-economic issues. SWIP does not follow market trends - stock are selected on their individual merit, aimed at delivering alpha within a controlled risk framework.

In August 2009 LBG announced that it had agreed to sell Insight to BNY Mellon for £235m, following which the management of Clerical Medical funds, currently managed by Insight, will switch to Scottish Widows Investment Partnership (SWIP).

Funds Under Management

At the end of 2008, the Scottish Widows long term insurance companies had around £49bn of funds under management, whilst Scottish Widows Investment Partnership’s total funds under management amounted to around £77.3bn at 30 March 2009.

Annual Review

★★★★★

Whilst 2008 was a solid year for Scottish Widows in terms of new business, the group moved from net inflow in 2007 to net outflow on lower premium income, reflecting the difficult market conditions during the year.

However, the year was very much overshadowed by the decision by Lloyds TSB to take over HBOS. Given the extensive range of insurance companies and brands within the enlarged group, this naturally led to some uncertainty as to how the group might emerge post any consolidation. Early 2009 saw the group confirm that it would retain the Scottish Widows brand within the intermediary space in preference to, and effectively dropping, the Clerical Medical brand. The group operates from 1st July 2009 with a combined single branded intermediary sales force. It is as yet not clear how the various corporate entities will fare in the consolidation, an exercise that may takes some years to finally complete. There is real potential for economies of scale and the merger has the potential to create a massive bancassurance player, notwithstanding its intermediary presence.

Financial Strength Ratings - Introduction

The aim of AKG's financial strength ratings is to assist IFAs and others to assess the relative strengths of individual provider companies. AKG's concept of 'financial strength' starts with the fundamental issue of a company's ability to meet all of its guaranteed payments to policyholders, but extends beyond this by aiming to factor in the degree to which a policyholder's expectations are likely to be met - or even exceeded - in the long-term. For performance-related products, where the eventual return generally depends largely upon a company's success in consistently delivering superior investment performance, and in containing expense charges, a company's ability to meet expectations is likely to be heavily dependent upon whether or not it is able to sustain its operations in the relevant market, and whether or not it can maintain, or improve, its competitive position.

As a result, AKG believes that, ideally, the evaluation of 'financial strength' should depend upon the type of product under consideration. A particular company may be judged as very strong in the context of one particular product line, but it may be weaker in another context. An illustration of this concept is a company that currently only markets unit linked business, but which has a very small closed block of with profits business, written many years ago. Such a company may be judged as 'good' for unit linked business, whilst considered 'poor' in respect of with profits business.

Since the inception of AKG's Company Profiles and Financial Strength Reports, AKG has consistently promoted and developed the concept of providing financial strength ratings separately for each of the three major product categories - With Profits, Non Profit and Unit Linked.

All AKG's financial strength ratings should be used with care, since even the more detailed approach described above represents something of a simplification. To illustrate this point, for example, the 'Non Profit' category covers a multiplicity of different products. It is clear that slightly different criteria should be used for, say, short-term policies with fully guaranteed terms (e.g. Guaranteed Bonds), than for longer-term policies with terms that can be varied at the company's discretion (e.g. Renewable or Reviewable Term).

AKG assesses financial strength using consistent methodology and objective measures wherever possible, and based on the detailed analysis of the company's particular strengths and weaknesses. The objectives and criteria for each of the financial strength ratings are summarised below:

With Profits Financial Strength Rating

The objective is to assess the overall strength of the company's with profits funds. The initial concern is the company's ability to meet its ongoing guaranteed, or promised, commitments, i.e. existing sum assured and bonuses. However, the company's ability to continue to compete successfully in the with profits market is also particularly relevant, given that closed funds are sometimes bad news for policyholders. In such situations, overall expenses tend to increase as a proportion of the fund and investment performance may well deteriorate. These, together with other factors, may make it difficult for companies in such situations to maintain competitive bonus rates at future declarations, although existing declared bonuses are not affected (other than possibly by MVRs).

✮✮✮✮✮	Excellent
✮✮✮✮	Very good
✮✮✮	Good
✮✮	Adequate
✮	Poor
▤	Not rated

The main criteria taken into account are: capital base and free asset position, with profits realistic balance sheet position, the amount of with profits business in-force, parental strength (and likely attitude towards supporting the company), and image and strategy.

NOTE: More detailed analysis of with profits companies is included in AKG's UK Life Office With Profits Report.

Non Profit Financial Strength Rating

The objective is to assess the company's ability to meet all guaranteed payments arising from such contracts as term plans, annuities etc.

✮✮✮✮✮	Excellent
✮✮✮✮	Very good
✮✮✮	Good
✮✮	Adequate
✮	Poor
▤	Not rated

The main criteria taken into account are: free assets, structure (and size) of funds within the company, parental strength (and likely attitude towards supporting the company), and image and strategy.

Unit Linked Financial Strength Rating

Whilst this is essentially a non profit line, and the primary objective is to assess the company's ability to meet all guaranteed payments arising, AKG also seeks to take into account the extent to which the company is likely to be able to sustain its unit linked operations, and whether or not it is likely to be able to maintain, or improve, its competitive position. Thus strategic issues are also relevant, because of their bearing on the quality of investment management offered, and because of companies' rights to increase charges etc.

✩✩✩✩✩	Excellent
✩✩✩✩	Very good
✩✩✩	Good
✩✩	Adequate
✩	Poor
▤	Not rated

The main criteria taken into account are: free assets, structure (and size) of funds within the company, parental strength (and likely attitude towards supporting the company), typical fund performance achievements, and image and strategy.

Overall Financial Strength Rating

The objective is to provide a simple broad-brush indication of the general financial strength of a company. In addition to an assessment of the company's ability to meet all of its guaranteed payments to policyholders, AKG also aims to factor in the degree to which policyholders' expectations are likely to be met - or even exceeded - in the long-term. This involves an assessment of a company's ability to survive in its current form for the long term. The overall rating inherently reflects the mix of business in-force within the company, since different types of policyholder have different expectations, and the company's particular strengths and weaknesses in respect of its key product areas.

A	Superior
B+	Very strong
B	Strong
B-	Satisfactory
C	Weak
D	Very Weak

The rating takes into account those of the following criteria which are relevant (depending upon the company's mix of business in-force): capital base and free asset position, with profits realistic balance sheet position, structure (and size) of funds within the company, parental strength (and likely attitude towards supporting the company), typical fund performance achievements, and image and strategy.

Supporting Ratings - Introduction

Supporting ratings are provided only in full reports, and are assessed at the brand level. AKG assesses three key supporting areas, using consistent methodology and objective measures wherever possible. The aim is to assist IFAs and others to consider the relative merits of the brands that they deal with. AKG's objectives and criteria for each of these ratings are summarised below:

Service Rating

The objective is to assess the quality of the organisation's service to the intermediary market in respect of the brand concerned.

✩✩✩✩✩	Excellent
✩✩✩✩	Very good
✩✩✩	Good
✩✩	Adequate
✩	Poor
▤	Not rated

Criteria taken into account include: performance in surveys, awards and benchmarking exercises (external and internal), the organisation's philosophy, service charters, the extent of investments designed to improve service, and feedback from intermediaries.

Image and Strategy Rating

The objective is to assess the effectiveness of the means by which the organisation currently positions itself to distribute its products for the brand concerned and the plans it has to maintain and/or develop its position.

✩✩✩✩✩	Excellent
✩✩✩✩	Very good
✩✩✩	Good
✩✩	Adequate
✩	Poor
▤	Not rated

Criteria taken into account include: overall trends in the company's market share position, brand visibility and reputation, feedback from intermediaries and industry commentators, and AKG's view of the company's general strategy.

Annual Review Rating

This is an end of year view for the last year for which Report and Accounts, returns to the FSA, etc., are available, together with comment on any significant post-balance sheet events. It is an assessment of how the brand has fared against its peers, and how it is perceived externally.

✩✩✩✩✩	Excellent
✩✩✩✩	Very good
✩✩✩	Good
✩✩	Adequate
✩	Poor
▤	Not rated

Criteria taken into account include: increase/decrease in market shares, expense containment, publicity - good or bad, press or market commentary, regulatory fines, and competitive position.

AKG Actuaries & Consultants Ltd
Anderton House, 92 South Street
Dorking, Surrey RH4 2EW

Tel No: +44 (0) 1306 876439
Fax No: +44 (0) 1306 885325

e-mail: akg@akg.co.uk

www.akg.co.uk

AKG is an actuarially based consultancy specialising in the provision of ratings, information and market assistance to the financial services industry