Jackson National Life Insurance Company®
Insuring your financial future®

JNL ANALYST AND INVESTOR TRIP

Transcripts of Chicago Day

November 1-3, 2005

Chicago, IL and Lansing, MI

PRUDENTIAL

Contents

Opening Comments

Mark Tucker

Group Chief Executive, Prudential plc.

Welcome

1. Introducing the Meeting

Good morning and welcome to Chicago. I think the timing of this event is excellent, given last week's strategy review and the update that we gave. Coming to this event with the views and statements we made last week about Jackson National Life (JNL) and our commitment to the US being a very clear "Yes," gives a very clear context for the next couple of days and is critically important for all of us.

2. The Agenda

In terms of what the guys will go through over the next couple of days, you will hear about the demographics of the US, the economics of the industry, and about JNL and its positioning within the US marketplace. The two days are open, and are there for you to get a better understanding of JNL and the business it is in, as well as to get a feel for the people and the operation. The JNL team is a senior team that has fundamentally worked together for the last decade. They are a team that has been enormously successful in taking this business forward and are well-respected within the industry and certainly within the Prudential Group.

You will also take a visit to Lansing tomorrow. Contrary to what Clark said yesterday, Lansing is a great place with wonderful people. The fundamental reason why I left Lansing had nothing to do with the company or the people; it was entirely to do with the weather. As you will see tomorrow, it is forecast for 65 degrees in Lansing in November, and this is global warming to the next level, because Lansing in mid-winter is as cold as you will ever want to be. Tomorrow, when you see Lansing, you will get a sense of the business there, particularly through meeting the back-office and product people, and seeing George Napoles and his administration team. You will get a sense of how powerful a business it is.

3. JNL

When I was at JNL in the early 1990s, it was fundamentally a fixed annuity provider, with a single distribution channel. Since then the company has changed dramatically, and for the better. It is significantly multi-product and multi-channel, and enormously successful in any measure you want to make. As I said at the strategy update last week, JNL is a critical and important part of the group.

To my mind, in terms of product, distribution, administration and capital, JNL is the best insurance company in the US. When you add the critical element of the people on top of that, I think you will see why I am as excited and committed to the US and to JNL. Without further ado, I will pass to Clark. At the board meeting last week I gave him a pretty poor introduction. When we were talking to the board about the US, I said that Clark was one of the 77 million Baby-Boomers coming to retirement- for which he has never forgiven me. Clark has been here for ten years plus and has led the company superbly as President and CEO, and he will take us through the rest of the day.

JNL – In a Clear Winning Position

Clark Manning

President and CEO, JNL

I. Introduction to JNL

1. Welcome

On behalf of the management team, we are very excited to have you here so that we can tell you more about JNL; the environment that we operate in, the opportunities we see in that environment, how we intend to execute against those opportunities. In particular we are excited to have the ability tomorrow to show you the operation and to introduce you to the people who run it, close-up.

2. History of JNL

JNL is a success story. It is a success story in terms of its sales, where we have one of the fastest organic growth rates in the industry; its growth, where we have tripled the size of the balance sheet since 1994; and its returns, where we have been able to self-finance our growth through the free cash flow that we have created. We have got ourselves to a position where we can continue to self-finance our organic growth, and remit increasing amounts of capital to the centre.

JNL is also an operational success story, with some of the best service in the industry, but at one of the lowest cost ratios. That will be a key theme that will come out during the course of the next couple of days. Over the next 30 minutes, I would like to set the stage by giving you an overview of everything that you are going to hear over the next two days.

One of things you will probably note is that I have a background of being an actuary and, while that is a great background for understanding the industry, in many respects, it brings with it a certain disease. That disease is an unhealthy fascination with metrics. I may fling around some metrics as we go, but you do not need to write all this down. I am giving an overview to set the stage and give you an understanding of the environment in which we operate. The speakers that follow me will go through this in much greater detail.

II. Overview of the Annuity Market

1. Size, Structure and Demographics of the Market

Let's start with a high-level overview of the market, in terms of its size, structure and demographics. The US market is enormous. In 2004, the financial assets of the US market were $44 trillion, compared to $26 trillion in the Euro zone, $7 trillion in the UK, and $5 trillion in China – so it is an enormous market. If you narrow that down to the segment of the market that interests JNL – the retirement savings segment – the US has about 60% of the retirement savings assets in the world. If you narrow that further still, down to the demographics that we find interesting, about 60% of those assets are held by people aged 55 and above, nearing or at retirement. The size of the annuity market, in which we compete, is about $220 billion of annual sales. So every point of market share represents an excess of $2 billion of annual sales. Also note that annuities in the US means something a little different to annuities in the U.K., where a product is referred to as in the "payout phase," while we generally refer to a product in the "accumulation phase" with payout options. These are savings products, primarily with payout options.

2. Fragmentation

The US annuity market is very fragmented, much more so than what I think you are used to. In 2004, companies ranked 21st and below in the market accounted for twice as much share as the number one player. That is a fragmented market. In 2004, JNL was the tenth largest annuity writer in the US, with a 3% share. That is a fragmented market. With market fragmentation, comes many opportunities and a lot of headroom for our business.

3. Baby-Boom Demographics

For my entire career, the demographics of the US market have been dominated by the Baby Boom, people born in the post-war years of 1946-1964. It is a huge generation and has had a very great impact on the financial services landscape. Now they are starting to approach retirement. The oldest Baby-Boomer reaches age 60 next year, which is the median age for retirement in the US.

As the Baby-Boomers begin to retire, there will be a huge impact on the financial services market in the US. I think it will be the biggest event in the history of the US financial services market because your typical Baby-Boomer is grotesquely under-saved. The propensity of the US Baby-Boomers to spend rather than save has reached legendary proportions. While they were saving, they were interested in efficient accumulation vehicles for their savings. Mutual funds got a disproportionate share of those assets, although insurers did participate, but as the Baby-Boomers move into retirement, their needs change. They have and will become much more interested in guarantees and longevity protections, than they were in their savings years. On the longevity element, if you asked most people how long do their savings have to last into retirement, they will say “I don’t know, average life expectancy in the US is 78 and we are reasonably healthy, so it probably has to last till we are 82 or 83.” That is not even close. If you have a couple aged 65, there is a 50-50 chance one member of that couple will live to age 92. Life expectancy is improving. If you overlay those increases in longevity with the savings level of most Baby-Boomers and their misperceptions of the possible returns on their assets, particularly as they move to de-risk their portfolio as they move into retirement, they have an issue. It is an issue that we, as an industry, are well poised to help them with.

4. JNL’s Aims

Let’s talk about how JNL fits into that. Typically, before retirement, a person will seek advice, because they will have received a check from their qualified retirement plan. It will be the largest check and the last check from an employer most of them will ever see. Therefore, they have got to get it right. They tend not to do it themselves and tend not to trust product providers to help them with this decision. They want advice that they perceive to be unbiased. Typically, they seek this advice five years to six months before they reach retirement age.

At that point in time, the money becomes very hot. It is going to be moved and deployed with different objectives than it was during the savings phase. When the money is redeployed for savings purposes, it becomes very sticky. You may chase alpha in returns, during your savings phase, but once you put into place a retirement plan based on guarantees, you are not going to re-jiggle that every year in search of returns. So you have very hot money that has the potential to become very sticky. To access that money, you are going to need a position in the advice-based channels, as the more money someone has the more likely they are to access advice in getting their money deployed.

Where does JNL fit in the advice-based channels? We have worked very hard on our position in those channels, and we think we are well situated. Let’s start with our own independent broker-dealer network, National Planning Holdings, Inc, a multi-tie independent advisors, similar to IFAs in the U.K. NHP is the sixth largest broker-dealer network in the US, with 2,500 representatives and $9 billion worth of annual product sales, some of JNL’s products and some of other product providers. Again, they are open architecture.

5. Independent Broker-Dealer Networks

In addition to our position in the advice channels with NPH, we do business with other independent broker-dealer networks. In fact, with a 9.3% market share, we are the fourth largest provider of annuities through independent broker-dealers. We are seeking relationships with advisers whose focus is on planning for their clients, rather than doing transactions for their clients, because we think those are the best advice relationships. Since we are targeting a particular type of adviser, we have had to construct our model in a particular fashion. We have to be able to deliver our product to those advisers.

How do we do that? With something that we call a relationship-based wholesaling model. We hire and train wholesalers, the best in the business because the way they approach advisers is by saying, “How can I help you grow your business?” and not by saying, “Here is JNL’s sales idea.” For your typical independent adviser in the independent broker-dealer world, they are responsible for their overhead, paying their office staff and electricity, and time is money for them. They do not need to hear our product sales ideas. But because the advisers we are seeking relationships with are the cream of the crop, they are trying to provide planning advice to their clients, and not just procure transactions with their clients. The best way for us to gain a relationship with them is to be able to help them grow their business.

6. Perspective II

Access to the advisers using our wholesalers is necessary, but it is not enough. We need to be able to give them something they can sell, which fits into an advise-based sales mentality. There are multiple examples of how we do that, but the one I will use is our flagship variable annuity product Perspective II. Perspective II is a totally unbundled variable annuity. By that I mean that the representative, and his or her client, start with a product that is really nothing more than a variable annuity wrapper. As with all variable annuities, it gets deferred tax treatment of inside build-up and has basic annuitisation, or payout, options, but it really has very little else. This is a fairly cheap variable annuity wrapper, which is enough for some people. They want a low-cost wrapper and they don’t need a lot of guarantees or other features.

Then, from that low-cost wrapper, the representative, and his or her client, build the product that they want from the ground up. Do you want an enhanced death benefit? Are you going to take market risk. If you die in the next several years, and the market is down, is that a problem? If so, yes, here’s the suite of enhanced death benefits that we offer. Do you need particular liquidity provisions? We have a lot of liquidity options, so which ones do you need? Do you want flexibility in how you withdraw the money, but still want guarantees, in terms of return of principal, so that you won’t outlive the income stream? We have a whole suite of guaranteed minimum-withdrawal benefits and guaranteed minimum-income benefits. Do you want us to give your heirs a lump sum to pay the taxes on the inside build-up? We have an option for that, and a countless number of potential combinations, which is not limited by anything from a systems standpoint.

Each of these options is individually priced, so you only pay for what you need, but what you need you do pay for. If you think about how that product lines up with wholesaling force, with the type of adviser we are targeting, and with the opportunity in the market that we are seeking, you will see that it is all consistent. We are pursuing a plan and formula here, in terms of how we are trying to deliver product to market. We are not trying to deliver all types of product to all segments of the market. We are trying to pursue a specific opportunity in the US market that we think is material and can be profitably accessed.

III. Specifics About JNL

1. JNL's Affiliates

Now, I am going to back up a bit and talk, in more detail about JNL and some of its attributes that are material in our ability to access the opportunities we see in the market.

Let's start with how we are configured. First, JNL National Life Insurance Company and JNL National of New York are our flagship companies and are responsible for the vast majority of our US profit. We do business in all 50 states and are truly national. Most of our business is written in the largest states, like everybody else's, but we are truly a national, 50-state operation. We have $65 billion of GAAP assets. Through the first three-quarters of this year to date, retail sales stood at $5.5 billion and total sales at $7.2 billion, so we are a productive organization. Affiliated with JNL, we have NPH, the sixth largest and most rapidly growing independent broker-dealer network in the country, with product sales over $9 billion per year and product revenues in excess of $400 million per year. NPH is profitable. They pay their own way in our group. Curian is a start-up and an expansion of our capabilities into the separately managed account space, operating in the registered investment adviser, or the fee-based channel. Prudential Portfolio Managers of America is our asset manager, predominantly an institutional asset manager managing fixed income assets, for JNL and other Prudential affiliates. They manage a lot of life fund money and funds for PCA in Asia. They have about $73 billion worth of assets under management.

2. Target Demographics

Where do we fit in the US market? Let's start with our target demographics. Historically, JNL has targeted the mass market, but most of our growth has been coming above the mass market. So we really target the mass market, through the upscale, to the mass affluent sections of the market. Think in terms of investible assets from $25,000 up to $1 million, or maybe $2.5 million. That is where most of the assets in the US reside. There is about 86 million households, in the mass market, and about 16 million in the mass affluent market. So there are a lot of assets and a lot of people to target in those segments. We don't target the high network segments, because it is not what we do. We mass customise advice for the mass market and mass affluent. If you are dealing with a high net worth, then there are a lot of companies who say they are, you are dealing with bankers, accountants, and lawyers, and coming up with absolutely customised solutions, which is not what we do. We use technology and our advice delivery mechanisms to deliver a mass customised product. We do that through various channels. JNLD-Guaranteed is our historical distribution channel, which Cliff Jack will talk about. They predominantly sell fixed annuities.

3. The Expansion of JNL

Since 1995, when a lot of the current management team was brought together, we have been expanding the scope of JNL:

- JNLD-Registered, which markets through the independent broker-dealer channel;
- Regional broker dealers in 2002;
- Institutional marketing group in 1994;
- Curian, a start-up, NPH, our broker-dealer, in 1998;
- The Southeastern Agency, which is career-agency distribution that we acquired with Life of Georgia (LOG), and is actually off to a very good start as part of the JNL family, representing about one third of our life insurance applications.

The net result of this expansion is that we have very good positions in our various product channels. Based on gross flows, or total premiums, we are the 12th largest seller of variable annuities, which, in the US market, is a substantial position. Based on net flows, or premiums minus surrenders, we are the fifth largest in the US market, due to the persistency of our assets being good, because our product construction and the reasons that the sale was made were good. That means we are one of the fastest-growing variable annuity companies in the country. We are the eighth largest writer of traditional fixed annuities in the US, which is JNL's historical forte. We still do a lot of it, but we do a lot less than we used to; today it accounts for only about 20% of JNL's retail sales. We are the tenth largest equity indexed annuity provider, or fixed indexed annuities, as they are now being called. We have substantial positions in our market and substantial breadth in our distribution, but we don't distribute through all channels. These are the channels we have chosen and think we can access profitably.

4. Opportunities in the US Market

I have talked about the demographics, now for the opportunities in the US market. You have 43 million households moving into retirement in the 20 years between 2010 and 2030. Today, the ratio of people in retirement, aged 65+, to people in their working years, aged 25 to 64, is 23%. It is going to remain relatively flat until 2010, and then it is going to take off, to where, by 2030, it will have roughly doubled, projected to be in excess of 45%. When I talk about a fundamental shift of the demographics in the US, it is very profound. The opportunities for people who can deliver products with guarantees are very profound. One of the things that we will discuss is that the Social Security safety net is not near what it is compared to the rest of the industrialised world. People need these guarantees, and they are looking to the private sector to deliver, in much greater proportions than elsewhere in the world.

5. Consolidation

So what are our opportunities? We operate in the largest market in the world, a market that will undergo a great deal of turmoil, or shifts, because of the demographics. We operate in a market where consolidation has been, and continues to be a big question, in terms of the impact of consolidation. I read a lot about what the impact of consolidation will be, particularly in respect to JNL, and I don't agree with much of it. When I entered the industry in the early 1980s, the two big themes were, "one-stop shopping financial supermarkets," which went by the wayside, and consolidation in the industry.

The market has been consolidating. The pace of consolidation has been measured, but the market has been consolidating. In the ten years that most of the current manager team has been together, we have been competing against this trend and I believe we have done pretty well. There are a number of reasons why consolidation hasn't been an issue for us: First, a lot of the inorganic consolidation that occurs, at a measured pace, will not make sense. Most large deals that are done destroy shareholder value. From an individual company perspective, large deals cause distractions, through succession distractions, the so-called "social issues," operational and strategic distractions, as you try to merge product lines and cultures. The other reason why consolidation does not concern me is because there are two types of consolidation, organic and inorganic. Typically, organic consolidation precedes inorganic, with companies getting together because they are not able to distribute as much as they would like or are unable to get the operational scale they would like, individually. For the last ten years, we have competed with organic consolidation, which is occurring in the US market, and have actually been a participant in it, with our increasing market shares. At JNL, we have the distribution scope that we want, and some of the lowest cost ratios in the industry, so we are competing against consolidation. Consolidation will continue and we will deal with it. We may even continue to participate in it, at a very low level, in terms of bolt-ons, but large-scale consolidation is not an issue for JNL.

There has been speculation about the impact of the Lincoln National Jeff-Pilot deal on JNL. I am not going to throw any rocks at that deal, as I think it is a pretty good deal getting Jeff-Pilot for $56 a share, if that happens. But it will not impact on JNL, in our channels. A metric demonstrates that in all of the league tables we look at, in terms of product and distribution rankings in specific channels, not one of those rankings change as a result of this deal. We will still compete in the marketplace as we always have, and our cost ratios are lower than the combined companies, even with the cost energies that they have announced. We will compete fine against that deal, and we have competed fine against the deals that have occurred to date.

6. Distribution

Looking at money in motion, distributions from retirement plans are hot money. In 2004, there were $500 billion worth of distributions from qualified retirement plans. As Baby-Boomers start retiring that is supposed to accelerate quickly, to over a $1 trillion by 2012, and approximately $13 trillion, estimated, over the next decade. This is money that we think we can, and are trying to, access.

From an operational standpoint, how do we do it? Start with the distribution model. Fundamental to our distribution strategy is our model that I have already talked about. The other part of it is the way we run our distribution channels—we sell product to create value, not to run up sales numbers or market share. That is the way we have always run our channels. The team has been run under that philosophy, and the senior management of the company have been in place using it for a long time. That philosophy does a lot to your distribution channels. We don't target market positions, per say. I am not standing here saying, "We are going to be top-five gross sales in variable annuities by 2008" or something like that, because that is not how we think.

We think about using our attributes to gain the share that the market will give us profitably, and try to gain that share by being better, not by saying that we are going to gain share. From a distribution company standpoint, that means we stand up at every wholesalers meeting and say, "You do not, and will never, have best priced product in the industry, therefore you are going to have to compete based on something else - based on you being better and more efficient than your competitors, and the delivery of advice in the relationship-based model, rather than based on price." I think that, fundamentally has given us a better distribution system than we would have had otherwise. It has created a process-driven sales culture, the culture that I talked about, where we try to add value to the representative rather than just drive transactions for the representative. To deliver that, we can't just beat on the distribution channel by saying, "You will be value-added and not sell best-priced product." We have to give them something better that they can sell, which means we have to be innovative. There are lots of ways in which we do that, but the one I want to talk to you about in a moment is Perspective II.

But to sum up our distribution strategy, we have some of the best wholesalers in the industry, which means we have some of the most expensive. They need to be more productive, with greater sales per wholesaler. That requires rigorous activity management, a great deal of attention to the sales material and other sales delivery devices that we use, how we use them and the cost of assembling them, as well as a great deal of attention to the use of technology in managing a sales force. Cliff Jack will talk more about this later. We know this is a different way of operating from our competitors, and it gives us headroom. This is the right way to operate.

IV. Innovative Platforms

1. Perspective II

Perspective II is a very flexible product. Again, we have a base product, with all sorts of options that we can layer on top of it. That makes us very flexible in the marketplace. We do not need to replace a product to change it. Instead, we pull benefits off and put other benefits on. That is a lot easier to do than re-launching a product. It means we are in a continual innovative phase. The measure of that can be seen in the last three years, where 80% of our retail sales have come from options, or benefits, or products that did not exist two years earlier. We have done that three years running. During the early part of this decade that figure was around 22%, which is pretty good compared to the industry, but it is not how we operate now. We need to be better.

We have had 32 product launches since 2004 and are continually rolling out different features, like the new suite of guaranteed minimum withdrawal benefits launched in September, and we were already working on the next wave we were going to roll out before we launched that set. That lets us be current in the marketplace, with what the marketplace wants, and be very responsive to our distribution partners, in terms of what they are asking and looking for. If we can deliver it profitably we can manufacture it quickly. It also helps avoid price competition, because we can adjust our benefits very quickly, into market slots where we don't see the competition and we have something that is not directly comparable to what other people are selling. By doing that, we avoid direct price competition. This has resulted in steadily increasing market share. We are at 3.3% total annuity market share right now, which is up from 2.5% in 2003. Looking at the variable annuity market, over that same time period, we are up from 2.6% to 3.5%. The share percentages may sound small, but the market is large and fragmented and those are large dollar increases in sales. VA sales are up 300% since 2001, as we have been consciously focusing on the VA segment of the market and have been very successful there.

Perspective II is the fourth best selling contract based on gross flows, and the best selling contact in the US based on net flows, so it is a very successful product. More significant, in my mind, though, is that in the independent broker-dealer channel, which is the channel we built that product for, it is the number one selling variably annuity product based on gross flows, net flows, or however you want to measure it. Clearly all of this has to be backed by a lot of innovative technology, and George Napoles will discuss how we use that to deliver excellent service at low cost. The key is that we could not deliver economically with the complexity and flexibility of product that we have without outstanding technology—better technology than our competitors have. We have no legacy issues whatsoever in that platform.

2. Superior Cost Models

Against the competitors that we track, JNL has the lowest cost ratio. Our expenses to assets ratio is 43 basis points, which is very significant, because it means we have to take 43 basis points out of the customer's return before we begin to pay our distribution partners anything for selling our product or repatriate anything to the shareholder. So that directly impacts the competitiveness of the products that we can offer. The average cost ratio of the top ten annuity companies in the US is 74 basis points. We have a significant lead on them. The average cost ratio of the top 25 annuity companies is 68 basis points, less than the top ten. To me, that demonstrates size does not equal scale. It is how you build the size, and not how big you are, that matters. A lot of the top ten built through acquisitions and so are in consolidation mode right now.

3. Frontline Compliance Model

We embed our compliance people in the business operations, rather than centralised operations. That is very consistent with modern corporate governance theory. We also make line management responsible for the compliance and control activities of their organization, and we hold them accountable, which is efficient and works.

4. Diversified Earning Stream

As a management team, one of our primary objectives is to get greater diversification of the revenue and earning streams of JNL. That has tangible capital benefits, which show up in our regulatory models, and also in the actual operation of the company. With diversified revenue streams, we have flexibility in managing the assets, liquidity, duration management, and the amount of credit risk needed in the portfolio. Therefore, we actively seek diversification. We have a big spread-based book, the historic fixed annuity book of JNL, and we have been rapidly growing our fee-based revenues, with variable annuity fees up 150% since the beginning of 2003.

5. Underwriting Revenue

The third type of revenue we are seeking is underwriting revenue, which is why we did the Life of Georgia (LOG) deal. We figured the best way to grow underwriting revenue quickly, and profitably, would be via a bolt-on acquisition, as opposed to organic growth. The US life insurance market has been flat for a decade, due to the demographics, and therefore gaining share organically is not profitable. It would be a single-digit return, “slug-it-out-with-entrenched-competitors” exercise. In terms of bolt-ons, you have 1,200 life insurance companies in the US, most of which are, by definition, extraordinarily subscale. There are larger companies with books of business that they cannot afford to integrate because they are doing something else that is more important to them. We believe we can achieve profitable diversification, assuming the returns, the capital, and the operational capacity, are all there, to do a full and rapid integration, and thereby to gain underwriting revenue. That is why we did LOG; that is the prototype of what we look to do there. We closed that transaction on 18 May and are over 85% converted after acquiring 1.6 million policies. We will have that company fully integrated by the end of the year.

6. Returns On Equity

If you are not profitable, the rest of it really does not matter. The best comparable to the US industry would be GAAP returns since they all publish it. We have other measures that we publish for Prudential, and we always feel like the lone ranger in publishing those other earnings metrics in the US market. Last year, the GAAP return on equity was 13.6%, compared with an industry average of about 10.5%. We liked that even better considering that the industry comparables had their leverage on their balance sheet where we have our leverage at the parent, so JNL is essentially an un-leveraged return. It also reflects the excess capital that we carry in our balance sheet, about $800 million, beyond what we need to support our ratings. Therefore, because of our profitability in the generation of free cash flow, we can self-finance our organic growth and return money to the centre. We have been returning increasing amounts of money to the centre, and we will continue to do that. Two years ago, we sent the centre $82 million, last year $120 million, and this year $150 million. The amount of money that we are returning to the centre now is in line with dividend yields, as a percentage of capital, for the US life insurance industry, but, because of our profitability, our expectations are that that will continue to increase over time.

V. Summary

How do you put what you are going to hear over the next couple of days into a framework? We look at it like we have multiple stakeholders that we need to satisfy if we are to be successful over the long term. These include shareholders, policyholders, advisers, as well as employees and regulators. Anybody can achieve apparent success over a short period of time, by letting those relationships get out of balance. You can buy share, at the expense of your shareholder, or at the expense of good relations with the regulator, and you could gain profits and cash flow, at the expense of your distribution and policyholder relationships. Our goal is to keep them all in balance, because that is a sustainable strategy. That has been our focus over the last ten years. By utilising the expertise of the organization, our execution capabilities, and innovation, we focus on showing profitable growth, running our back office different from our competitors, and offering the marketplace something different, and better, too. That is what we are trying to do, and that is the framework in which to think about what you are going to hear over the next couple of days.

At that point, I am happy to take some questions, with the qualifier that you are going to hear a lot of detail. So any detailed questions I would rather defer, until we get to the detail, but if there are any high-level questions, for this point in time, feel free, or I will be standing up again at the end of the day, and at various points tomorrow.

Questions and Answers

Participant:

Back in 2000, I think your advantage, in terms of expenses to assets, vis-à-vis the top 25, was over 40 basis points. The competition has been getting leaner, over time, and I think your advantage is now 25 basis points. Do you see that narrowing continuing?

Clark Manning:

I see us getting continually better. The other big competitors among the industry did a ton of high-profile acquisitions in the late 1990s—most of which did not work out for them, from a shareholder value or operational standpoint. But they are now in the process of integrating what they bought, and their cost ratios are coming down. Will we maintain a 25 basis point over time? I don't know, because I don't know where they will go. What I know is that we have been steadily decreasing our ratio, over time, and we expect it to continue, because we have extremely low marginal costs. If you look at the growth we have achieved over the last five years, we have done it on a fairly flat expense and head-count base. George will give some additional statistics there. I know what we can do. What can the competitors do? They will get better. Will they narrow with us? I don't know. Will we stay lower than them? I think we have a fundamentally better operating model and technology model, so I would expect us to be able to stay lower than them. We don't have to beat them by 40 basis points. If we beat them by 40 basis points consistently, and thought we could over the next 20 years, then that would probably portend bad things for the industry as a whole, because other financial services providers would clobber us pretty badly.

Participant:

Two questions, if I may. First of all, one of the traps that other companies who have a similar model to yours find is getting the line right between when they are providing a service offering to advisors, and when they start to become a crutch and are actually subsidising advisors in trouble. We saw that particularly in the last bear market. How do you deal with that?

The second question is, one of the barriers you have in the U.K. market to the idea of keeping the product, but just switching options, is that it advisors lose the opportunity to churn the book products, for want of a better word. How does that work out with the advisors that you have got, that they don't lose an opportunity to say to the customer, "Well, if you want a different option, here is a whole new product and thanks for the commission?"

Clark Manning:

On the first question, I will ask Cliff Jack to address it in more detail when he stands up, but in terms of subsidising the advisor, we take our acquisition cost ratios very seriously. In the way that we price and develop products, acquisition costs, or internal costs of delivery, are just part of the marketing mix. If we want to run those up, it is at the cost of commission, and competitiveness of the product. The aggregate acquisition cost ratio is the constant. We control that very carefully. If we are going to subsidise them in some way by running up our level of service, or something else that will drive up our acquisition cost, that will be come out of another element of the distribution mix. Cliff will be able to talk tangibly about what that means in the field.

As far as the problem with representatives churning their business, and PII not being a friendly product for that, you are right. That is why our net flow ranking is better than our gross flow ranking. Keep in mind that the representatives we are looking for are not ticket-based representatives. We pay and have trail options so that they get continued revenue off of their sales, but we are not looking for relationships that will be looking to churn the business as soon as it comes off of surrender charge.

We are looking for continual asset growth, not just sales growth. For instance, we don't do any business in the wirehouse channel right now, and the reason is they have had worse persistency. They want a ticket-based product. They do not want PII, which is a more involved sale than most of them want. Their persistency is not good; therefore it doesn't work in our pricing models. So we are targeting a certain type of representative, who is not looking to place the money with us so that they can churn it. We will pay them fees to leave it with us. They are looking for share of wallet, as opposed to turnover.

Participant:

I have two questions. First, what is your cost structure, if you remove the medium-term low-margin assets?

Clark Manning:

I don't remember last year's number, where the 43 was last year. This year, at the mid-year, it was 48 basis points excluding the institutional liabilities, which are low-cost liabilities.

Participant:

Do you have a number for the same ratio for the top three players, as opposed to the top ten players?

Clark Manning:

Not off the top of my head, but it is attainable. We can get that to you separately. The institutional markets question is interesting, and let me elaborate on that, because institutional assets are cheaper, and we internally measure our progress of that ratio, excluding institutional assets, as they cost essentially nothing to administer. The problem in industry comparisons is we have trouble reliably separating those out of industry competitors. At 48 basis points, we are still very competitive, even compared to the industry with institutional assets in. It's a good question.

Participant:

I think you said you had $800 million of surplus capital. Presumably you think your economic capital requirement is lower.

Clark Manning:

Yes.

Participant:

Why are you holding that excess capital?

Clark Manning:

The excess capital was built up because JNL is generating a lot of free cash flow right now, because the back book is profitable, and the business we are writing is not capital-intensive, being primarily unit-linked business. So free capital has been accumulating very rapidly in JNL, which gives us a lot of flexibility. It is beyond what we need for our rating agencies, the $800 million excess, but it means we can self-finance our organic growth and we can finance a limited amount of inorganic growth, and we can meet the Prudential cash flow needs and requirements, as they put them to us. The way the

Group manages capital is, what's not needed to back our ratings is Group capital, and they will deploy it based on the best opportunities that they see around the group. The capital is relatively fungible, but we have been generating a lot of it recently, and it is in our balance sheet. It is reflected in our planning and in Prudential's cash flow expectations from JNL, prospectively.

Let me cut this off. You will get a lot more detail during the day, and I will take more questions at the end of the day. I would like to introduce Greg Salsbury, the Executive Vice-President with JNL National Life Distributors, who is going to talk about the retirement situation in the US.

The Retirement Challenge

Greg Salsbury

Executive Vice-President, JNL National Life Distributors

I. Retirement Situation in the US

My mission over the next few minutes is to offer you a high-level overview of the retirement landscape in the US I think it is important to note, as we examine the retirement challenge, that, from a historical perspective, retirement is a relatively new concept. Earlier this year, National Public Radio in America broadcast a story on retirement and Social Security in the US They interviewed a 94-year-old woman named Helen. She pointed out that people simply worked until they died, and, if they were unable to work any longer, they moved in with relatives. She recounted how this was the case for her own grandfather, who ran a neighbourhood grocery store up until his death in his 60s, at which point her grandmother had come in to live with them in their tiny, one-bedroom apartment in the Bronx. This was the norm then. In fact, prior to World War II, 87% of Americans who were 85 and over lived with relatives, compared with just 43% today. At that point in time, the concept of having a well-funded, leisurely back-end of life was reserved exclusively for the wealthy.

Then, in 1935, Americans got a New Deal. As you know, the biggest part of FDR's New Deal was the Social Security Act, but the purpose of that has since been somewhat misconstrued. At the time, legislators were preoccupied with persistently high unemployment rates that ran into the high teens. Their motivation was really to give older workers an incentive to leave their jobs, and make room for younger workers to take them. So, in this regard, Social Security was more of a "jobs act" than it was a "pension act," and a bit of an unintended consequence was planting the seed for the retirement wave that would follow. For the first time, millions of Americans had leisure time and a little bit of money. They weren't wealthy, but it was still a type of lifestyle that had been previously unknown. As time went on, employers could afford to supplement that lifestyle by offering robust pension plans, which offered healthcare benefits and other post-employment benefits. They could afford these because they were having to fund them, on average, for just a handful of golden years, because of still relatively high retirement ages and relatively low life expectancies.

Just as the American Dream was being realized—they had money, leisure time, a governmental safety met, support from employers, improved health—the pieces started to come apart. First to go by the wayside, were the frugal saving and spending habits learned from leaner times, like the Great Depression. Increasing number of Americans started to see money as something you spent rather than saved. Also, as Social Security became overburdened by the disproportionate number of contributors per beneficiary healthcare costs went up. Healthcare benefits became so expensive that employers began to rethink pension plans, and the benefits within them began to dwindle. All of a sudden, responsibility had shifted back to the individual to take care of his own back end of life.

The truth of the matter is that did not happen all that suddenly. We evolved to this point over several decades. It is now 2 November 2005 and, in less than two months, the first of America's Baby-Boomers turn 60. As Clark mentioned earlier, that is the median age for retirement in America, and for the 77 million Baby-Boomers who stand right now at retirement's door, it feels as though this transition has taken place with the speed of flicking a light switch. We stand with a bifurcated America, bifurcated between those who are wholly unprepared for this and those who are somewhere in the middle. Those who are wholly unprepared face a dismal fiscal situation indeed. They are both under-saved and over-spent. We have the lowest savings rates since the Great Depression. Some 40% of America's workers have saved nothing at all for retirement, while 28 million American households have no retirement savings account whatsoever. The typical American family has saved a whopping total of about $18,750. Simultaneously, they are overspent. Last year, we had a record consumer debt of $2 trillion. If you work that out on a household basis it comes to, guess how much – about $18,700. Furthermore, we had record personal bankruptcy filings last year of about 1.6 million; we are on pace to surpass that this year; and the percentage of credit cards that have reached 30 days past due status now stands at 4.81. That is the highest rate ever recorded. Therefore, we have a very substantial part of the US population that is under-saved, overspent and ready for their comfortable retirement.

1. Mass, Middle and Emerging Markets

Now, for the rest of them, the mass, middle and emerging markets, their situation is not quite as dismal, but they face challenges as well. Challenges that are both psychological and economic. At the top of the list of psychological challenges is a focus on accumulation, and this does not only pertain to the investors. Investors and advisors alike remain, in many cases, mentally mired in the glory days of the bull, and it is somewhat understandable: this is a generation that cut its investing teeth on the greatest bull market mankind has ever witnessed. When the bull finally died, it ended a 20-year period where the S&P 500 produced average annual returns of 18.5%. Embedded within those two decades was a spectacular five-year period in which it produced five consecutive years of 20%-plus returns. Thus, it is not perhaps so surprising that Paul showed that investors ended the decade of the 1990s with expectations of average annual returns on their portfolios of 19%. Furthermore, the research shows they expected those returns to continue for at least another ten years. As you all know particularly well, that is not what they received. What they received instead was the fiercest bear market since the Great Depression, in many cases wiping out all of their gains and then some. In fact, the latest EBRI research shows that for Americans 50 years old and over who have 401K accounts, those accounts, on average, are still down 9.3% below pre-bear levels.

2. Distribution

Now those people are five years older and they need to begin thinking about distribution and about decumulation, as Cerulli and Associates refers to it. That is complicated by this process that they are very unfamiliar with, which is distribution. It is not something that was focused on. When we did a search in the LexisNexis database on the phrase "retirement planning" for the year 1985, we received a grand total of 55 hits. We did the same search this year, same database; we are on pace for about 10,000 hits. People are suddenly waking up to the fact that they are older and they need to think about retirement income planning. However, the process for doing that is far, far more complex than simple accumulation. Accumulation is fairly simple: you have X amount of money, you have Y number of years, you assume Z return, you are going to end up with T amount of money. Not so for distribution. A common question I will ask our advisors at some of the seminars we conduct is, 'If we have a 65-year old married man and he wants $60,000 a year for the rest of his life, and he wants to know how much in lump sum savings he needs currently to support that lifestyle, what is the answer?' I receive answers that are all over the board. The answer, of course, is dependent upon a host of very unpredictable and subjective factors. For example, what is the life expectancy of one and both spouses? What is the assumed accumulation rate of the underlying assets? What is the assumed withdrawal rate of the underlying assets? Is it the 7-8% that many financial planners use or is it the more conservative 4-5%? What is the assumed inflation rate during that time period? Is it the historical 3.1% or is it a more conservative 5%? Is there a desire to take care of heirs, legacy issues? Are there any special healthcare or long-term care issues that have to be accounted for? Also, of course, what is the degree of risk that the investor is willing to assume during this time period? Depending upon how all of those questions are answered, the correct number turns out to be, usually, somewhere between $1-4 million. I can assure you that the typical investor is shocked to learn that the operative word at the end of that number is "million" versus "thousand." He is even more distressed to learn that it might well be a multiple of that million, not thousand. They are very unprepared to deal with this; it is part of why they very much need financial advisors.

Those are just a couple of the psychological challenges that that population is battling. Then we have a list of economic challenges that include increased longevity, faltering pensions, social insecurity, the tax bite, inflation and escalating healthcare costs.

II. The Retirement Landscape

1. Introduction

What does all of this mean with regard to the retirement asset pool here in America? What does it mean to the wants and needs of pre-retirees and retirees? How significant are these economic challenges to their wants and needs and, specifically, what does this mean for the American financial services industry and to JNL? In the next few minutes I will try to give you a little more insight into all of these issues. Specifically, we will look at the retirement landscape, where the assets are, who has them and how sizeable they are. We will look at a little more detail on the economic challenges to retirement that I have just outlined and explain why we believe all of this creates a tremendous opportunity for JNL.

2. Assets

Let us start by taking a look at where the assets are. As Clark mentioned earlier, the US holds the largest pool of retirement assets on the globe. It is about 60% of the world's retirement assets. Individual retirement accounts account for about $3.5 trillion and is expected to grow to about $5 trillion by the year 2010. The average individual retirement account right now is $27,000. 401(k) accounts represent $2.1 trillion. The average 401(k) account is about $34,000 and growing. All together, total retirement market assets total $12.9 trillion and these assets are quite fluid – as Clark says, "hot money." About $1 trillion over the next ten years each year are expected to flow from these maturing plans into the marketplace, creating tremendous opportunities for companies like JNL that participate in the retirement market. It is the Baby Boomers and older who control these assets. People who are 55 and over control about 60% of all investable assets or a pool of about $13.8 trillion.

Cerulli and Associates breaks up the American market into six tiers of wealth with Tier I being the wealthiest and Tier VI being the least wealthy. It is Tiers IV, V and VI that JNL has always targeted, and continues to target, particularly Tier V, those people with somewhere between $100,000 and $500,000 in assets. We are capable of dealing with and have attracted those people with anywhere from $25,000 to $2.5 million, as Clark mentioned earlier, but typically that middle market of $100,000-500,000 in assets tends to be our sweet spot, the intersection of the fastest-growing part of the population and those with the most assets. There are about 36 million Americans today who are 65 and over; that will be about 62 million people by the year 2030.

3. Social Welfare Spending

We have to digress a little to discuss social welfare spending to fully explain the opportunity that exists for Jackson here in American. The reason that is so is that people from the outside will often look at the tax rates for the US and assume they are relatively modest. However, they do not see them as quite so modest when they fully comprehend how little of that tax comes back to the individual in the form of governmental support. Compared with other industrialised nations, the US spends a relatively small amount on social welfare spending as a percentage of GDP, about 14.8%. That is about half of what countries such as Germany, France and Sweden spend on their social welfare. The largest factor driving the disparity is healthcare. When comparing the same countries in relation to healthcare, the US stands out as the only country that provides only limited government healthcare benefits with only about one-third of the population covered. Hence, that is a bit part of what is driving the disparity. Again, all of this is putting a greater onus on the individual to be responsible for his own expenses, his own back end of life.

4. Projected Growth

The projected growth for individual retirement accounts is about $5 trillion by the year 2010 and about $2.7 trillion in 401(k) accounts by that same time.

III. Economic Challenges to Retirement

1. Longevity

Let us take a look at a little more detail regarding some of these economic challenges. The first one is longevity. Americans are living longer, retiring sooner, and spending more time in retirement. This may be the first generation that spends more time in retirement than they did working. The average age at retirement is now about 62, average time in retirement 20-plus years. Not only is America living longer, but the proportion of our older population is growing quite dramatically as well. The over-80 population is growing five times faster than the overall population. Not only has life expectancy doubled since 1900, but just in the last 50 years the odds of reaching 90 years of ages have increased a full 130%. The bottom line here is that never have the odds of outliving your money been greater for American retirees. By the way, as an aside, Hallmark cards now sells about 85,000 centenarian birthday cards a year.

2. Pensions

This, as you know, has been particularly well covered in the last couple of years. We have seen the percentage of American workers covered by defined benefit pension plans plummet since 1985 from 80% to just 24% today and falling. Forty-four million Americans are already impacted by pension defaults and more are on the way. The under-funding of America's pensions systems nationwide is estimated at about $450 billion at present. Four of America's five leading airlines are flying while bankrupt. In each case, the key decision to enter bankruptcy was largely because of the great expense of post-employment benefits and the largest part of that, of course, being healthcare benefits.

3. Social Security

Social security has been another popular topic as of late. It is misunderstood; I could spend a lot of time talking about it, but there are two important messages to convey. Number one is that it does not pay very much. The average Social Security cheque is just $11,460, which is just a couple of thousand dollars above the poverty line. The reason that is significant is that the original intent of Social Security has been stood on its head. Social Security was originally intended as a supplemental income source for a minority of Americans. It has become the predominant retirement income source for a majority of retirees. Half of America's retirees would live in poverty without Social Security, so we have a very large part of the population dependent upon it. It does not pay a great deal, so for the mass middle and emerging markets it is not very attractive as a retirement tool, as it were.

However, the other problem is that it is in trouble fiscally. Depending on whose math you believe, it is under-funded by somewhere between $4 trillion and $12 trillion. The Deputy Commissioner from the

Social Security Administration, James Lockhart, himself says, "To attain sustainable solvency would require about $10.4 trillion in today's dollars, or about $100,000 per family." There is an oft-quoted survey from last year that found that most young adults believe they have a better chance of seeing a UFO than of ever seeing a Social Security cheque, and there is good reason for that.

4. Taxes

Another economic challenge is the escalating tax bite. Taxes now comprise about 30% of the typical American family's expenditures and that number continues to rise. Forty percent of America pays no income tax whatsoever, leaving the entire burden to the remainder of the population. Furthermore, for the upper end of the population that burden continues to grow. What the upper 10% of wage earners have paid as a portion of the federal income tax bill over the last several decades has grown substantially. In 1981, the upper 10% of wage earners was responsible for 48% of the federal income tax burden. By 1991 that had grown to 56% and by 2001 it had grown to 65%. Who know what it will be in 2011? I am going to guess higher.

5. Inflation

Sometimes called "the invisible enemy," inflation is one of those things that people seem not to think about. There is the joke about when oil prices spiked up recently people said, "Well I am not that concerned about rising gasoline prices because I always just put in $20-worth anyway." That sounds ridiculous, but it is an example of how little people understand about what this does. My own father is a professional engineer, very bright man, but I can remember having the debate with him about the risk he was taking by having all of his money in certificates of deposit: "How is that a risk? You may be college-educated, son, but you just do not understand. I have it all 100% protected." Using just a 3% rate of inflation, if someone needs a $50,000 a year income, they will need more than double that in 25 years.

One of the most requested tables from our financial advisors is the one that shows historical rates of inflation over the last several decades. What it shows is in the 1970s inflation averaged 7%, in the 1980s it averaged 5% and only once we reached the 1990s did it go back down to 3%. If you show the table to the typical investor and say, "What rate of inflation do you think would be prudent to assume for your retirement planning?" they may not choose 7%, but I can assure you very few of them choose 3%. The vast majority of them believe that 5% is the more prudent number. In fact, Dr. Blitzer of Standard & Poor's says he believes that is the correct number to use for the inflation factor in retirement planning.

The significance of this is easy to see. If you assume a 5% rate of inflation, the value of $10,000 is eroded by nearly two-thirds over the course of 20 years. This is why investors, even retirees, desperately need something other than fixed instruments in their retirement portfolios. They need something like a fixed index annuity or something like a variable annuity with a guaranteed minimum withdrawal benefit that gives them a safety net but provides the opportunity for growth, because without the opportunity for growth they can be eaten alive by inflation.

6. Healthcare

Healthcare is the elephant in the living room that no one wants to talk about. The same formulae that show Social Security's under-funding at $10-12 trillion show the under-funding on Medicare closer to $62 trillion. This is because Americans spend more on healthcare than any other country on the planet by at least 50%, and that average expenditure is now at about $5,700 per capita with expectations that it will rise further, again, with very limited governmental support for that. Hence this is the wildcard. An example of this is General Motors, which estimates that about $1,500 of the cost of every new car goes to just the healthcare benefits for employees and retirees.

IV. The Opportunity for JNL

1. Targeting Pre-Retirees is Key

How does all this create opportunity for JNL? I have explained a little bit of that, but I will try to give you some further detail.

The retirement wave, we believe, is the single most significant event in the history of the financial services industry. That wave is rolling. It is not out there on the horizon coming towards us; we are in the middle of it now. Government assistance is waning; employer assistance is waning. All of this is simultaneously our greatest challenge and our greatest opportunity. Our key to all of this is targeting the pre-retirees. As Clark mentioned earlier, the money is very “hot” in pre-retirement; it gets very sticky in retirement. The McKinsey research is quite clear here. It shows that pre-retirees are three times more likely to seek financial advice than retirees. Once in retirement, not only do they tend to be locked into plans that make it more difficult often for those assets to move, but they tend to be loyal to the advisors who helped them plan for this and brought them into retirement.

2. Understanding Target Market

The key to targeting the pre-retirees is having a very detailed understanding of the Baby Boomers and at JNL we do. We have an excellent Market Research Department, we have access to the best industry databases, and we have been working with Boomers for a long time. Much of our marketing techniques, which you will learn about over the next day and a half, will show you how we do a particularly good job of understanding those audiences. We know that the typical Boomer household has 0.95 children; 40% of them anticipate that an adult child will move back in with them; 14.2% of them are divorced, often times because of that adult child moving back in with them. Thirty-seven percent of them say that their favourite TV show growing up was *Star Trek*. The average Boomer drinks 3.8 cups of coffee per day; only 7.3% of them are below the poverty line and, most importantly to us, 97% of them are uncomfortable with the amount of money that they have put away for retirement. We know the Baby Boomer. We know their likes and dislikes. We know what they want in their products, in their investment options.

3. What Does America Need?

a. Advice

What is it that Americans want? This is what they want: they want advice. The bear market taught them that brain surgery and investing are better left to professionals. Fifty percent of those investors who did not have a professional advisor during the bear market consulted one following it. They know they need help.

b. Choices

They want choices. Americans want choices in everything. They want choices in their products, in their services and their investment options. Ben & Jerry’s offers 17 different flavours of ice cream in the UK; they offer 40 to Americans. Coca Cola offers 12 different types of soft drinks in the UK; they offer 34 here in the US. It is no different with investment options. Standard & Poor’s estimates that you need somewhere between ten and 12 distinct mutual funds to provide ample diversification for a portfolio; according to ICI we now have over 8,000 mutual funds in America – about 90% of those, by the way, were added during the 1990s.

c. Income

According the National Association of Variable Annuity Research, the number one concern of retirees is running out of money and having to downgrade their lifestyle. Income is critical.

d. Safety

The bear market, again, taught them that their portfolios can be radically damaged in just a matter of months. The bear market is indelibly inked on them. If you recall, Cisco Systems lost something like $310 billion of market cap in a matter of six months. They know that their portfolio can be absolutely devastated in just a matter of months and they know that there is not the time left to repair the damage.

e. Guarantees

They want guarantees on all of this. The VARDS/Greenwald research completed earlier this year showed that the majority of retirees want no chance of deprivation later in life; not low chance, no chance and only guarantees can provide that for them.

4. Why Consumers Want Annuities

There are several reasons why annuities are particularly attractive to investors today. They provide safety, growth, income and choice. Only annuities can provide all of these options within a single product.

V. Conclusion

That is part of why Jackson is particularly well positioned. We have the largest pool of retirement assets here in the America. Retirees are dramatically under-served and our advisor base is particularly well positioned to help them with this. It is particularly why we have targeted the independent financial advisors. The age wave is rolling, and the levee has cracks. Those cracks are simultaneously the obstacle to saving, in some cases, but they are also the motivation to save and it provides great opportunity for Jackson. The assets are fluid: $1 trillion a year flowing into the marketplace from these plans.

All of this leaves us very well positioned, we believe. We have the right advisors and the right distribution team as the tip of our sword. We have a diverse product menu with many of those products capable of providing a guaranteed income stream for life. We have the right market research, the right sales and marketing tools to be able to not only attract but educate the Baby Boomers. With all of this, we are confident that JNL has its greatest opportunities and successes ahead of us. Thank you.

I would now like to introduce Mr. Clifford Jack, who is Executive Vice President and our Chief Distribution Officer, who will introduce our next speaker.

Clifford Jack, EVP and Chief Distribution Officer, JNL

VI. Introduction to Mark Casady

I have had the opportunity to hear Greg present some of the facts, and I think I may want to move to the UK in light of that! I will be addressing you all later, but we have a very special guest with us today, and I think you will find his presentation to be fascinating. What we have tried to do is give you a slightly different view, a non-Jackson view, if you will, of the industry. Mark Casady is with us today. He is very gracious with his time: as he will probably mention to you, he has just had a very successful transaction close, an important transaction in the US financial services market, and I am sure he will incorporate that into his presentation. However, one of the things I think you will find about Mark is that he really understands our business. He understands it from the back end of, say, the asset management business to the front end of the asset management business, to the back end of the brokerage business to the front end of the brokerage business. He understands a little bit about the UK culture having spent some time in London. He has also had the opportunity to work with a couple of different major European financial services companies, so he has had a chance to speak to people like you. Without further ado, I would like to introduce Mr. Mark Casady, Chairman and CEO of Linsco Private Ledger (LPL). Thank you for being with us.

The Broker-Dealer Perspective

Mark Casady

Chairman and CEO, Linsco Private Ledger

I. Introduction

Thank you. Good morning, everyone. As Cliff mentioned, I had the opportunity to work in Europe for many different years with a ten-year gap in between. My last job, believe it or not, was to be the European managing director for an asset management company, which meant that what I got to do was take a set of German asset managers, Italian asset managers, Swiss asset managers, English asset managers and bring them all together. We always met in Zurich – we were owned by Zurich Insurance at the time and it seemed to make sense there – and if ever there was a stereotype at play it was there. We constantly would meet and the brash American would say, "We must do it this way. I do not understand why you folks do not understand how to run asset management companies." The English, of course, would believe, "we rule the world, why is there even a question that we should do something different?" The Germans would constantly try to take the next German-speaking country as part of what they try to do; the Swiss, of course, tried to make everybody feel comfortable and it was all going to be okay; and the Italians often went out for a smoke. Thus, the reality is that we all live in a global economy and we all have a range of opinions that are formed by our backgrounds and our cultures and way of doing business. The good news is that the world has globalised and, therefore, a lot of those stereotypes are, of course, not true any more. We have fabulous asset managers in each of those locations. We had a fantastic point of view about the business when we were running Scudder Investments in those days and we were trying to bring together a global asset management company. However, it certainly was fun because, at the end of the day, it is about the human relationship: how do you think about an issue, how do you influence somebody, how do you get them to move from point A to point B?

II. Agenda

That is exactly what Linsco Private Ledger, or LPL Financial Services, is about, but on a much different scale. What I love about the company that I work for today is that, number one, I do not travel internationally; we are solely based in the US, providing financial advice on a very local basis. I will talk about that in a little more detail. What we are trying to do is exactly what Greg just outlined: influence people to think about how life might be different if they did something different. What I want to try to do today is talk to you about the independent financial advisor space in America and then talk specifically about Linsco Private Ledger. I am going to spend a little bit of time around some of the industry issues that we face in a variety of markets and then talk to you as a consumer of Jackson National's products and be happy to give you our perspective about how that works.

III. Independent Advisor Market Segment

Let us begin with the financial advisor channels generally across the US. One of the things that surprises people is only in the last two or three years independent broker-dealers, like LPL or Jackson National's own independent broker-dealer, are not the largest segment advisors in the US. It is a phenomenal number (106,688) and it is growing every day by the number of advisors who are deciding to go from an employee model into an independent contractor model. To make it very basic, it means that somebody who worked for Merrill Lynch yesterday walks out of Merill Lynch and decide to set up their own business where they are the owner, the CEO, if you will, of that particular enterprise, and they are providing advice to their clients now as a business owner. Of course, the great thing for them is often economics. At the end of the day, they are able to take home more money and able to have a better lifestyle than they would if they worked in the employee model. Secondly, they have a business they can sell at a later date. They might choose to sell it to a son or a daughter or a cousin or another LPL advisor. Ultimately, they are building an asset. I can tell you that at our conference, when we have a chance to meet people who come to us, particularly from the wirehouses, it is not unusual to have someone come crying to the podium. Imagine, you have just given a presentation to 3,000 people and somebody comes up who is probably 65 or 70, tears in his eyes, 32 years at Merrill Lynch, “Why did I not do this 20 years ago?”

I want to convey to you the emotion that comes with making a decision to go independent. It is an incredibly powerful model for the individual broker or advisor who wants to set up their own business and we think we are only at the tip of the iceberg. Independents only became leading in terms of number of advisors in the last two or three years and we think that this will be a major trend throughout the US market over the next five to ten years.

Obviously, there are plenty of other competitors and they will continue to be great competitors in other markets. There are some wonderful models for people who are getting into the business to learn the business inside wirehouses and insurance companies and other places, but you do have to think about the independent as a unique model in terms of how we deliver our services and capabilities.

IV. The Industry

1. Overview

The other thing that is happening in our industry is consolidation. Jackson National, in fact, has been part of that consolidation in buying a number of independent broker-dealers and bringing them together under one roof, which is relatively unusual, as we will talk about in a moment.

Secondly, we see that the market is still terribly fragmented. Therefore, when I look at the opportunities as Linsco Private Ledger, what we see is, firstly, a chance to bring more people into the independent and, secondly, continue the consolidation that has occurred. We purchased the independent broker-dealers of the Phoenix Life Insurance companies last year, and we are hopeful that there are other opportunities for us to do that in other cases. We believe the movement from the employee model to the model of independent space will be a phenomenal one in terms of what will happen to our particular business and what we see happening to the independent advisor space.

The last point is what Greg talked about: there is tremendous opportunity as Boomers need more help and advice. We know that they are seeking unbiased advice. It is provided by LPL, by Jackson National and its independent broker-dealer; you have to have a wide array of products available. What happens is that you are able to provide that Baby Boomer with many more choices then help them go through those choices and think about how important it is to save. I think ultimately that is what the independent advisor does so well. They have one of the toughest jobs here in the US. They have to convince an individual to not buy the next new car. Whether it is from GM or Toyota does not matter; the reality is that car is going to be worth less two years from now than it was worth when they drove it off the lot. They have to convince someone not to redo the kitchen at $90,000 but redo it at $45,000 and put the difference away for their retirement or for the college savings plan for their 0.95 child or whoever. Thus, at the end of the day, it is a very difficult job that advisors face, whether they are employees of wirehouses or in their own independent model.

2. Headcount

If you look at a measure in terms of head count, even though we have a large number of advisors who are in the independent space, it is still very diverse in terms of where those advisors live. Linsco Private Ledger had 5,825 advisors at the end of last year; we are now at 6,322 as of September of this year. Thus, we see continued growth in terms of the amount of brokers who are moving in the space. Morgan Stanley, for example, had 10,962 at the end of 2004; the figure is down by at least 1,000 advisors, if not more, since they announced lay-offs. We think those who are in the wirehouse business in particular will continue to head towards much more of a private banking model. They want to emulate what Goldman Sachs has done in private wealth management; they want to emulate to some degree what UBS has done and that means their sales forces will become smaller, and they will continue to chase a very wealthy clientele of families in excess of probably $20-$30 million of assets.

We think that there is a great opportunity in the mass affluent market, as Greg was saying. There are huge amounts of consumers who are scared to death about the need for retirement, who worked all their lives and made $50-75,000 a year and have saved perhaps $100,000, $200,000 and they need help with what to do with that money. Our particular model delivers that help in a local market and I will talk about that a little later. We think we have a geographic advantage in the way that we deliver advice and how we get to the mass affluent client; I think we would also mirror what Jackson National terms of the independent advisor space.

3. 2004 Independent Broker-Dealer Rankings

Among independent broker-dealers, LPL has been the number one broker-dealer for ten years in a row. We have managed to do that consistently for a number of years and we think that ultimately it is because we try to listen to what our advisors tell us to do. If they say, “We have a problem with X,” we try to solve “X” for them. If they think they have an idea for “Y,” we try to provide “Y” for them in terms of what they do. We have been very lucky to have a nice track record of growth over those ten years, which I will talk about in a moment.

Regarding other competitors, the nearest public company to us is Raymond James, and they have both an employee model and an independent model. They also have asset management and investment banking. Hence the model is slightly different from what we do at LPL. We concentrate solely on the independent advisor space for our business.

4. Market Share

The other thing that is important about the independent advisor space is market share. What happens is that products are sold through a variety of ways – obviously through captive agencies in the case of variable annuities, but independent firms are huge sellers of variable annuities and therefore are very important in terms of the coverage. Therefore, when I think about our relationship with Jackson National, part of what we measure is what the products are like, how the sales force cover us and what is the unique relationship that we can build with that organisation versus others who offer competing products. Again, I will touch on that in a little more detail, but this sets up the idea that it is important to make sure that we cover this market very well.

V. Linsco Private Ledger

1. Recent Transaction

Let us talk about LPL. As Clifford said, we announced last Thursday that we have sold a 60% interest in our company. The company this year will have about $1.4 billion in revenues and we sold the 60% interest to two private equity firms, Hellman & Friedman, which is based in San Francisco and that you may have heard of – it manages about $9-10 billion of assets in private equity. We also have an equal partner with Texas Pacific Group, who has about $10 billion of assets under management. They have purchased a 60% interest in LPL. The transaction is likely to close by the end of this year. We are going in for regulatory approval, in fact, this week. They valued the firm at roughly $2.5 billion, so that means if you measure us on revenues it is not quite two times revenues in terms of that valuation level, but it gives you a sense of the value of independent advice. We think it is a huge endorsement for the value of independent advice in terms of outsiders, if you will, private equity firms, taking a look at the business model and putting a valuation to it.

As we have discussed with the press and with our advisors, it is not only about a capital transaction, but it is also about the fact that they understand how important it is for independent advisors to work with our clients and provide a variety of products and how much this market is quite different from anything that has come before it. We are the classic company that is trying to change the way that people do business in this particular space and Jackson National is also, with their independent broker-dealer. We think independent broker-dealers, broadly speaking, do have a superior business model to those who are trying to sell captive products or based on an employee model such as the wirehouses. Therefore, we think this transaction is a wonderful endorsement in that way.

2. Reasons for Transaction

As we look at the transaction, part of the reason we were doing it was because we are owned by an individual. There is a single individual owner who has been in the business for 20 years and founded Linsco at that time. He did two things. One was that he took a year off last year, went around the world, came back and said, “Do you know what? Being off was fun. I think what I would like to do is spend more time not working and so I would like to have some liquidity for financial planning purposes and I would like to be able to go and do some other things.” He is very interested in the environment and, in fact, one of the great things that will come out of this transaction for him and, frankly, for the environment, is that he will be funding a number of projects that will allow Scripps and other organisations to do research on the seabed and reefs. It is a particular interest of his and something that he would like to spend all his time doing.

The second issue from our perspective is the need to become an institution. If we are individually owned and, God forbid, something happened to our owner, we would be forced to sell the company. He is the majority owner, so we had to find a way to transition our structure towards more of a corporate structure, which is why we looked at a variety of ideas. We contemplated going public, but our view was that we are in such a heavy growth phase, it would be very tough for analysts to agree that we could continue to grow the top line at 20% and the bottom line at 40%. That is what we have achieved for the last few years, but the reality is that it is tough for people to accept that that is likely to continue. Therefore, our view was that it was better to stay private, let that growth occur and then inevitably as we slow down a little in a few years’ time, and that is the time to probably go to the public markets and get additional capital. As we see an opportunity for consolidation in the market, we also would like to do that consolidation as a private company. We now have two private equity owners who would like to put more capital to work in our particular space in the industry and this gives us a chance to tap that capital as well.

3. Outcome

We are pleased with the transaction, but our advisors, frankly, were not that excited by it, meaning that they did not have many questions, but saw it as a transition of capital, which is what we wanted it to be, and our day-to-day life is the same. As we said to our employees, we are announcing no change. There will be no change to their lifestyle, no changes to the management team who is going to continue to run the business the way we have run it for the last three years. What is important here is we have been able to create an institution as a result of this capital change.

4. Company Overview

That gives you an overview of the transaction that has just occurred. The other thing about LPL is, as we have said before, its unique nature of bringing in a wide variety of products. We have over 100 mutual fund families, over 70 different variable annuity families, over 25 different life insurance families and a variety of other alternative investments that we offer to our advisors who offer them to their clients and they decide which is best. Our view is that we want to make sure and do the right job in compliance, the right job in product overview, but ultimately we want each of our advisors to have their own choice. That is a key enduring principle that we have.

We also want to make sure that we are providing unbiased advice, so we are not in the manufacturing business. We do not do any asset management or investment banking, and we are not a life insurance company. We believe that there is a much better model out there in our world, which is to focus on distribution as the core skill. Thus, we are not a very diverse company; we are all about distribution in the independent advisor space and do not do any other things that Jackson National or other companies do because they do a great job of it. Our view is how do we bring them together in a way that is technologically interesting, use our research to talk to our advisors about it, provide great support and service to those advisors and then help train them in how to use those products and how to think about issues like retirement planning and other things.

5. New Product Creation

We also try to find places where we can create new products. We have created a product in the mutual fund side called “Optimum Market Portfolios,” where we create asset allocation devices. It allows us to use technology in an intelligent way and then that lets our advisors use that product in a way that allows them to work with their smallest accounts and be more efficient in running them. One of the tough things about an advisor’s job is that they have a lot of accounts that are $10,000 or $20,000 and it is hard for them to make money in the business servicing those clients. Therefore, we have tried to create ways that use technology and service to let them effectively outsource that to us. We do it in the mutual fund area, we have just recently done it in the annuity, and we also just recently did it in the separate account area. In fact, Curian Capital, which is one of the Jackson National companies, is one of the companies that we looked at very closely. We think the separate account platform that is there is very intelligent. In our world, we do the platform part, so it is hard to let somebody else come in and do the platform part, as Cliff knows. However, we love what it is they have done, and we think that for different organisations where they are not going to invest the kind of money that we have in that platform. It is a very intelligent use of technology and we have flattered Cliff by copying it, in many cases.

6. The Firm

Let us talk a little bit about the firm. I mentioned that we are at 6,322 in advisors, and we are growing about net 75-100 per month. We have 389 financial institutions. A small part of our business is providing broker-dealer services for credit unions and for banks; the CIA Credit Union is a client of ours, as well as Boeing Credit Union and others. Hence it is an important part of our business, and it is a wonderful business because it is very locally based.

Among distributors of products we are typically very high in rankings, and I will talk about that shortly. Our revenue growth rate 1992-2004 has been 23%. Last year in 2004, it was 27%; this year it will be about 21%. Thus we have seen phenomenal growth in terms of our revenues as a result of our advisors coming into an environment where they can do the best for their client. Their clients react well to that because it is unbiased advice and that tends to lift all the boats inside the firm.

We have roughly $95 billion in assets and that can be in money market funds, in assets that we have in our advisory programme; it can be assets in our managed account programme such as our separate account business, Manager Select. Thus it is a variety of places that we help advisors place money.

a. Competitors

In relation to our competitors in the independent space, in terms of revenue and new advisor growth, we are starting to see more and more space develop between our business and others. We think that is the advantage of scale. When you have been number one for ten years you have scale advantages that others do not and our job is to exploit those scale advantages in running the business.

b. Growth

In 1996 we had 2,400 advisors at LPL; today we have 6,322, as I said earlier. Similarly, our revenues have grown from $284 million in 1996 to $1,397 million estimated for 2005. 2001 was the only year we had revenues below the previous year. In 20 years history of LPL we have only had one year in which revenues were down. We do not disclose profits, but it would be fair to say that profits, in fact, were up in 2001 despite the fact that revenues were down. In 2002, profits were flat as we absorbed some of the costs from what we were doing in 2001. Thus we have never really had a down year in profitability unless we were doing some major investment in the business. It is a very unusual business in that it has the characteristic of very little fixed cost and high recurring revenues. We are little like an asset management company, and we are a little like a broker-dealer without the capital intensity of a broker-dealer.

c. Product sales

To give you a sense of our size in the marketplace through this year, load mutual funds will be $6.3 billion. If you were to ask the American funds, for example, where we rank with them, we will typically be number six or seven in the country. We will be the largest independent, but we will be in the top 10 in sales. With Platinum Funds, Scudder Funds and other organisations, we are typically going to be in the top five. For many fund companies, we are often the number one or two selling fund firm because they are not able to go into the wirehouses and get distribution there because the wirehouses have limited distribution of their product.

We are the second-largest seller of annuities in the country. I will talk about Jackson National's penetration in our system shortly, but suffice it to say we see a lot of variable annuity product, and we spend a lot of time understanding how it is used. We spend a lot of time on the regulatory environment related to it as it is an important area for us in terms of our relationship with advisors and their clients.

Managed accounts are basically our advisory-based programme that is mutual fund wrap programmes and separate accounts as well. Life insurance, frankly, we are not that large in. It is an area that we have targeted. We think we are probably middle of the road in terms of sales and we purchased a brokerage general agency last year and are working with Jackson National as a life distributor trying to create a general agency process in our world. Our advisors sell a lot of insurance, but as you may know, under US regulation, they can do that with anybody; they do not necessarily have to do it with their broker-dealer. In the securities business they have to do all their business with us, so we need to be more competitive in life, and we have undertaken to do that this last year.

Alternative investments are hedge funds, REITs and other specialised areas. They are an important area for our clients, particularly as they seek retirement income, so there are many products here that provide a great income for them in retirement.

7. Summary

Finally, in terms of LPL, I have talked a little bit about our ranking and we think there are four keys that are our strategic advantage in talking to advisors. Therefore, if we were sitting down and I was trying to help you decide to come to LPL or stay where you are, what I would say to you is that we provide that non-proprietary best of breed, if you will, in terms of products and we have a research department that is going to publish that information to you daily. In this way, you will know all about the products that are in the system.

Secondly, we have spent an enormous amount of money on infrastructure and technology to make sure that they have the support they need. Moreover, we will be releasing a study in about a month's time that will quantify that an advisor in our system is materially more efficient, we think about 15-20%, in their practice as a result of our support and technology versus others. We think that that is a key advantage for us.

We do focus clearly on the financial advisor. We consider the financial advisor our client. If you were to come to our offices in San Diego or Boston, what you would see are our commitment creeds in every office and conference room. That is all about defining our relationship with our client, the advisor, and making sure that they are centre to our life and our success as a broker-dealer.

Finally, this last year, in 2005, we decided to make training the centrepiece and add it as one of the four keys to success for the firm. Prior to that, we did a lot of training; we did not receive much credit for it and, frankly, we did not do a great job in delivering it. Therefore, we have is to go on something called a "city tour," which allowed us to take our national conference to 12 different cities across the US. Jackson National participated as a sponsor, so they were there helping to teach classes and to be able to talk to our advisors. Importantly, about 80% of the attendees to those conferences had never gone to one of our national conference. Thus, even though a product provider might be at our national level they would not have seen these advisors because, for whatever reason, they did not attend. Therefore, it was a great opportunity to get out and talk to those advisors, do education and training over a two to three day event and we have found it has been tremendously successful. If we measured it by a headcount at meetings and people who attend web conferences or phone conferences, each of our advisors about will go through training in our system twice a year. That means two times a year they are spending serious amounts of time away from their business being taught about some issue or idea. It might be financial planning, it might be variable annuity ideas, it might be sales concepts and so on in terms of building their business. We think that is a key mechanism for us to support them on a going forward basis.

VI. Industry Challenges: The Distributor Perspective

1. Dynamic Regulatory Environment

Let us switch to the industry and come out of the LPL story a little. It is obviously a story we like to tell, not surprisingly. As a private company, I can say whatever I want, which is a rare moment these days. The distributor perspective is from our point of view. If we look at the regulatory environment, to say it is dynamic would be an understatement. Someone asked me recently during due diligence of this process with the private equity firms, "Describe the worst scenario you can imagine in a regulatory environment." I said, "That would be 2004 and the early part of 2005, so we have been through it. The worst I can imagine has happened." That has been the mutual fund break point issues with A shares and US mutual funds, B and C share sales practices, revenue sharing has gone through, there is some work going on now in variable annuities, but I think we have been through the worst in terms of the regulatory environment that we are in the US. I think we have discovered practices that, frankly, needed to be changed. There are definitely things that we discovered that we did wrong. Our point of view was to fix those, pay the fines on behalf of our brokers, make restitution to their clients and pay all of that for them because we felt they were processes we should have had in place.

In other cases, the regulators are trying to make a statement. They are saying, "We do not like the practice that has developed in the industry, so we are going to stop it by fining you." I am not sure that is fair, but at the end of the day, that is the route that have chosen and our point of view has been to settle, deal with the issue and move on to whatever the next issue is. Therefore, I think we are through the worst of it in terms of broad sets of issues, but clearly what has changed is the way that we sell, how we sell and certainly disclosure to the client is a key part of what we do.

In the variable annuity space we developed a tool called the "VA Sales Tool." Our sales force calls it the "sales prevention tool," of course, but what it does is in a number of situations, if a client is over 70 for example, that sheet has to be filled out by the advisor. They sit down with the client and go through it and the client signs off on all the features and benefits they are either giving up or receiving in the new variable annuity. If it is a sale where the variable annuity has only been held for three years or less, firstly, we review it and in many cases we do not allow that to happen, but if we do allow it to happen, again, the same sheet of paper is gone through with the client and the client signs off. That will not change in terms of how we support variable annuities or how we support regulatory disclosure, and that is one of the keys to the way the world has changed in the last couple of years.

2. Other Issues

Obviously, we have to keep up with all the new products that are developed from Jackson National and others. We certainly have much more complex due diligence requirements; again, part of the NASD review of regulatory practices. In addition, certainly we want to continue to focus on what is good for the end client in terms of the features and benefits that are coming through the products that we see.

VII. Industry Challenge: The Product Provider Perspective

1. Different Sales and Marketing Support Required

From the perspective of somebody who is providing products, you have all those same points, plus you have the issue that certain systems are difficult to cover or require different types of sales. Our system is very difficult to cover. We have 3,000 offices and I know there are none here in downtown Chicago. Where you start to see our offices is when you get to the suburbs of Chicago, probably 20 minutes or half an hour from here, and then you see them in small towns across America. Therefore, if you are running a distribution company like Jackson National, it means that you need our help to know where to go. You cannot just cover 3,000 offices with a 50 or 75-person sales force. You have to know that 100 of them are the ones that really matter for your particular product. So part of what we try to do in conjunction with the product providers is to help them understand where to go in our system. Wirehouses are much easier to cover. They gather everyone together, are almost always in a downtown location or in the heart of the suburbs and almost never in small towns, and there are just not as many of them. Hence you can see that you have to have very different ways to sell to those channels.

2. Flexible Technology Infrastructure

You have to have a technology, whether it is product-based technology or one for sales coverage, to make sure that you can be flexible with a variety of ideas. I will talk about that and its importance shortly.

3. Good Products

Of course, at the end of the day, is the product a good product? Does it make sense for the consumer and the advisor? Is it a good idea in terms of what you are trying to achieve? Does it offer asset allocation? Does it offer features and benefits on the VA side that are useful to try to deal with the concern people have over the loss of principal? There are some fantastic things that have been done in the last five years in variable annuities to protect people from downside risk.

When we spend time with regulators one of the things we talk to them about is they do not understand that people are concerned about losing principal because many of them are, frankly, pretty well off. They are paid well by their particular regulatory body or they come from backgrounds where this has not been as much of a concern. They do not understand why you would turn money over to a variable annuity contractor to provide that service. When you talk to the regulators about the fear the consumers have and about the worries they have for losing their money, they start to see that there is a need for that product and it has to make sense in that context.

VIII. LPL and Jackson National

1. Flexible Technology

Finally, let us talk about our relationship with Jackson National and let us come back to that flexible technology. We are going through a very interesting time in variable annuities here in that there are a number of different points of view about pricing. My general belief, as the head of LPL, is that capitalism takes care of all things, that ultimately the market sets prices and the market sets certain behaviours and what we have to make sure of is these things work together in an intelligent way. In addition, we have to look for the outliers, where are things that do not make sense, that are just not good ideas, and where are things that make a lot of sense that perhaps are not getting the kind of promotion they need. Clearly, having an ability to price flexibly in variable annuities is about to become, I think, critically important.

One of the things I did before I came to speak to you is I went to back to the people who are in charge of the relationship with Jackson National and all of our relationships and asked them for a debriefing on what they saw as the one key item that this firm has that is different from others. They said it is the flexible technology and pricing. Instead of having to go back and rework systems and spend an enormous amount of time and energy being able to re-price a product, Jackson National has an ability to do that. Indeed, I would predict that that will become a much, much more important tool as the firm goes forward, because that is the phase we are about to enter: much more complex pricing on variable annuities than we have seen before and appropriate pricing as it relates to the way that consumers are using these products and the features and benefits that they try to take. Thus, I think technology has always been an advantage for every firm in every industry and if they have the latest one out, they are going to be able to beat those people who have to spend an enormous amount of money to retool.

2. Sales Growth

If we look at the numbers, sales are up enormously in our system on the VA and fixed annuity side. For Jackson National that represents several things going quite well for them. Number one, making sure they are focusing on the right offices. Therefore, working with us and the home office to say is it the office in Hoffman Estates in Illinois or is the office in Peabody, Massachusetts that wants to know more about variable annuities and can do a good job understanding what is unique about the products that are here.

Secondly, it is all about participating in our training programmes, at our national conferences and being visible. Our advisors are relationship people; they like relationships. They want to know that you are going to be there in the good times and in the bad. One of the big mistakes companies make, as you well know, is they withdraw from the marketplace when something goes wrong. The best companies are there whether it is wrong in their company or whether it is wrong in the environment. The key, in our world, is just to be there talking about the issues that are going on in the industry and continuing to provide great product advice and good information, and doing that a bit agnostically. It is not about, “Let me sell you this product today, advisor at LPL;” it is about ‘Where does this product work in your repertoire of tools or your choice of products that you can use?’ We think the firm does a great job of doing that.

Finally, it really is about all the new ideas that are coming along related to features and benefits that we think will make a big difference for consumers and for financial advisors. As well look at it, we think that there is a way to put together a range of products that makes sense that allow advisors to do a better job for their clients and, ultimately, we think that that is the power of what LPL and other independent firms do, providing that ultimate flexibility – if you will, that capitalism – in terms of making choices and decisions.

I will stop there and take any questions about the firm, our transactions, or anything else.

Questions and Answers

Participant:

How are you interpreting what seems to be a segmenting of the brokers with the moves like Merrill's to focus only on high net worth and retrench from the mass affluent?

Mark Casady:

Well, a part of me loves it. I think they should do more of it because what ends up happening is they withdraw from certain cities. Thus, about three years ago, Merrill Lynch withdrew from all their small town offices and we ended up, frankly, as a huge beneficiary of that move because those offices looked very similar to our other offices and they knew other LPL advisors in that town or the next town over. I think if I was running a wirehouse I would ask myself the question who is it I am trying to serve? Am I going to really be America's financial advisor? Probably not. Am I going to be able to serve a very wealthy clientele with unique products and capabilities? I probably could do that. Therefore, they have to find their particular niche, as large as they are, in that. I think that is what we are seeing the wirehouses do. They are saying, let us go upmarket and try to mimic the Goldman strategy, which as you know is very high, at $100 million or more in family wealth. They will not go that high, but they know they have to get their advisors to probably $1 million average a year. In our system, our average advisor is about $220,000, but we can make money doing that and they can make money doing that because they live in Columbus, Indiana, where I was born, and they can buy a very nice house there for $250,000, believe it or not. They can have a very good life that way. They cannot work for Merrill Lynch doing that, in our view. Therefore, we think they will continue to shrink a little bit, but importantly, stay focused to very high-end producers and very high-end clients.

Participant:

Do you see something forcing them to make that decision, because it would seem, from what we are hearing, that mass affluent is pretty attractive?

Mark Casady:

It is if you are able to deliver the technology and certainly, again, you would think those are wonderfully entrenched competitors, they do a great job in many areas, but I am not sure they understand how to make money in a $15,000 account. If you look at the activities they have done, as you know, they have pulled together a service centre model for smaller accounts. First of all, we would never do that because we are not an employee model, but I can tell you our advisors would never do that, where they try to hive off smaller accounts, because they view them as the seeds for future growth for themselves. Therefore, what we have done instead is we have worked out a way to make money for the advisor and for ourselves in smaller accounts. That, to my mind, is different. I am not sure I would be motivated to do that if I was running Merrill Lynch or Morgan Stanley, because

I think there is as much bigger game at play here, which is how do I work with the people who build structured products, whether that is in the form of IPOs or income investments or whatever. There is a lot more money to be made there than working out how to deal with a $15,000 IRA rollover; that is just the reality. We are happy to be, as a company, focused in that market because we think that is a very natural market for us to be in.

You would probably not see us in Manhattan, for example, and open an office for LPL advisors and try to attract million-dollar brokers. That is not our particular sweet spot either, so we will naturally stay away from what they are doing.

Participant:

We are constantly told about Jackson National's product, Perspective II, and how it has an advantage because it is customisable and unbundled. My experience has been that product design in itself never gives you a long-term advantage. Could you tell us from your point of view how unique is Perspective II and, if it is so good, why are not other people doing it?

Mark Casady:

I think if you look at our numbers you can see many more people are doing it in our system and these things do not happen overnight in terms of unit growth. My perspective is that I think product innovation is critically important. I have a very simple view about the brokerage business: whether you are an investment management product provider, a variable annuity product provider, or you are in the broker-dealer business like we are, you are either being bought or you are being sold. It is as simple as that. The reality is there is more money coming into the system, but you are constantly fighting for market share and your client's wallet, if you will. That means that if you are not there with the latest innovative product, the other guy is. If you are not there trying to talk about the exciting new feature that you have, the reality is that the other guy is. It is a competitive marketplace. I think once you enter the minds of a sales force like our 6,000 people and you capture them with those good product ideas and they see that you are trying to be innovative in that process, what will happen is there will be a bit of a cheer for that. People love to see that occur and they start to talk to each other and other people in the system about it, at our national conference, for example, and that is how sales start to move along very quickly because you create a bit of a buzz around that particular product. Thus, you start as with all things, a little bit as a drip and then, as it gets into the system wider and wider, you start to get the network effect occurring. We see it in our system all the time. You will see good unit growth and suddenly, if it is well managed and the sales force is out there telling the story, you will then start to see it really pick up in terms of sales.

Participant:

What I was trying to get at was there must be many other product providers apart from JNL who could provide that service and I am just trying to get a feel for how unique they are and why you think other people are not copying them with the idea that you have an unbundled, innovative product.

Mark Casady:

Well, you have probably three tiers of providers in the world. There are the people at megalith levels of sales and those are the ones you are trying to displace. My view, as I was saying to Cliff last night, is that what Jackson National has done a good job of is saying, "How do we break out of the tier we are in and get to that next level?" and I think the beginnings of that are there. Therefore, they have to have those products and features in order to compete with the much, much larger producers of VAs; that is just the reality. What they have to do is show that there is some unique characteristic that they are providing.

You are quite right, people will copy the best product ideas, but if your underwriting is more sound and, secondly, your ability to price is more flexible, which is what I think is unique about Jackson National and I do not think the pricing part of it has quite come into play yet. We have had fairly standard pricing in the US with bonus shares and L shares and B shares and things that I start to lose track of, but the reality is that has been fairly solid for a long time; that is not going to remain solid for much longer. That is where this company is uniquely poised. Without trying to, frankly, over-endorse Jackson National, with all due respect, the reality is that that pricing flexibility will become more important; I just do not think we have seen it yet. Thus, you are right, up until now underwriting features and benefits are probably relatively well copied, but you have to do them to be in the game.

In addition, as you get to the next level of competition, which will be around price, it is inevitable, what will happen here is that you have a more flexible technology to compete. That is what we believe in terms of how we think about our relationship with this firm. Frankly, part of our job is to identify those who we think are winners; because the reality is that we want to be with the winners as they start to move up and penetrate our system. We want to help them be successful because it is obviously in our interest and our sponsorship systems are very straightforward: at the end of the day, the more we can sell for you, the more we expect to get paid – it is simple maths – and at the end of the day, you are going to make more money because you have more unit sales. Thus, believe me, we are in the business of trying to identify the people who we think have a real advantage in the next wave of competition. I hope that answers your question.

Participant:

How does JNL's level of fees that they pay you compare with other major product providers to yourselves? Secondly, does the agent receive the same level of remuneration irrespective of which company's products they push, namely you receive the differential but not the agent?

Mark Casady:

That is a great question and thank you for asking it. Our system is a little unique in that everybody, at whatever tier of sponsorship they are in, pays exactly the same fee. We do not cut special deals for our agents and we do not cut special deals for our sponsors. If you are participating annuity sponsor, as Jackson National is, your fee is exactly the same as every other participating annuity sponsor. We think that is important because we believe it is an important business principle around how we compete. All 6,300 of our advisors have exactly the same contract. We have never cut a special deal in 20 years, which means that Fred did not walk in last week and get a better deal than Jane just because Fred was a better negotiator. We think that is bad business in the long term. We think the same is true for sponsorship.

Secondly, we do not have any differential payout to the advisors themselves, so whatever the payment mechanism is, it comes to us and then whatever we are paying out is exactly the same for every single product. Therefore, fortunately or unfortunately, there is not an advantage for Jackson National in our system to say, "We would like to pay you more and then you pass that along to the advisor." We do not allow it in the system because we think it takes away the unbiased nature of the advice people provider. However, it is an example where you do have to pay and, at the end of the day, the relationship has to be that if we can have you help us with sponsoring training or we can have that product company help us, essentially, pay for the technology investments that we make, as long as we have set the playing field level that is going to continue. That is not going to change from a regulatory standpoint and as long as it is disclosed if the firm is getting a payment, everything that we have worked with the regulators on says that that is fine.

Participant:

The changing compliance standards for the sale of indexed annuities, will these be important enough to have a significant impact on your selling costs? If the answer is yes, would you expect to pass some of that back to the provider?

Mark Casady:

It will not have an impact to us that will go to the provider; it will have an impact to the seller. Therefore, our advisors today do not have to bring equity-linked annuities in, as you know, and that change is occurring, there is no doubt about it. We are in the process of gathering data from all the product providers about what is sold, but that is a good example of a product that falls outside of our system, advisors can do it anywhere. We do not sell a lot of index-linked annuities; we are not particularly large in that area. However, what will happen in our system is that the advisor will now have to pay their override to us. Before, they received 100% of the commission; they will now, on our system, receive 90-92% of the commission and the balance will come to us. That is what will pay us for the compliance overview and the surveillance of that product. Therefore, in our world, it will not affect any of the manufacturers in terms of their margins, it will affect the individual advisor and that is fine. I do not see any particular rebellion that will occur among the advisors for that because they understand that this is just the cost of doing business.

Thank you very much.

Clifford Jack:

Mark, again, thank you very much for joining us today.

Retail Distribution and Operational Overview – Our Primary Engine for Growth

Mike Wells

Vice Chairman and Chief Operating Officer, JNL Insurance Company

I. Introduction

My name is Mike Wells, and I have responsibility for our retail businesses, distribution operations, technology, administration, and a variety of other corporate issues. Together with Clifford Jack and George Napoles, I will aim to discuss what we think is JNL's positioning and advantage. They will give you a granular look at how we do some of the things we do, and why we think that positions us well for the marketplace. I intend to bridge some of the concepts you have heard about so far this morning, such as the opportunity, prerequisites and culture, with the reason why we do them, in order to reach a picture that we think is more complete.

The format of this section will include an overview of the market and its landscape items, and I will cover some of the questions that were posed during the break, following Mark Casady's comments. I will also talk through some of the areas that we see as core competencies at JNL:

- Our product manufacturing, intermediary management – including how we deal with a firm like Linsco/Private Ledger (LPL) – and acquisition management.

- Some of the attributes that appear as a consequence of these competencies.

- Our belief that the combined impact of levering those competencies gives you, as shareholders, higher value.

II. Market Landscape

1. Product Manufacturing

A number of you have commented that you think it would be relatively easy for a competitor to replicate our VA unbundled product, but I want to talk you through the barriers to product manufacturing:

- Corporate inertia at some firms with which we compete.
- The value of the VA business in a larger, multi-line company.
- Technology: most of our competitors use a single-technology platform that has been sourced from an industry provider, and are not capable of replicating the optionality of our contract.
- The desire to adjust entire business models to that.

I will discuss the attributes of success in a moment, but that is not how many of our competitors have chosen to define their business plan. Therefore, the product would be very difficult to replicate, it is a question of capital, time and effort – but the impact on a number of competitors' business models would be very disruptive in terms of them having to change to that direction.

2. Key Landscape Issues

The key landscape issues are some of the things you heard about in Greg and Mark's presentations, in terms of "the consumer." The VA business has been built on the Baby Boomers. When they anticipated returns to be 19%, the idea that tax on them could be deferred in the US was extremely attractive. They had funds that were generating returns of more than 40%, such as NASDAQ and various internet-related funds. At one point, Transamerica had one fund that experienced a 127% quarter. There was a period, then, where the value of the tax deferral was front-of-mind to the VA investor, who was focused on accumulation.

3. Features

The industry, in the absence of equity performance, started to create features, which Mark referred to. The features included:

- Escalating death benefits, providing some value to heirs in excess of the account value, which were well-received by the market.

- Providing guarantees of income and, in the case of some of our competitors, guarantees of account balances; Chad Myers will explain to you later why we do not do this.

- Providing guaranteed withdrawal benefits, which JNL has participated heavily in and which guarantee some level of income.

All of these features relate back to Greg's comments around the fact that these Baby Boomers are maturing and looking at their current circumstances and, suddenly, the concept of income has become important.

4. Retirement Income

There is no bigger distinction between the US and UK markets than the way in which consumers look at retirement income. 3% of Americans annuitise our accumulation contracts to date. The idea that an annuity is a payout vehicle is a very unique concept to Americans, and particularly to American investors: they receive a large cheque and they have to deal with it. We look at that sort of behaviour from the consumer. These are the Baby Boomers and they have redefined this process; just as Greg told you how they like things customised, they want these products customised, and this has been one of the advantages for JNL. A number of you would think nothing of going to Starbucks and paying $5 for a cup of coffee, which is typical Baby-Boomer behaviour; however, they will not pay $5 for a cup of coffee that they cannot customise and which does not taste good. There is no detachment from value there, and that is exactly the same way in which they are approaching the solutions they receive in retirement.

5. More Asset Allocation

In the sales process, they currently perceive no asset class to be “the right place” for money, which has not happened for a long time:

- Deposit rates are too low.
- They are scared by equities.
- They do not believe that a single segment, such as technology stocks, is the obvious place to invest a large proportion of their money.

They tend to be biased towards their own companies, but there is no obvious place for their money. One of the very positive outcomes from that, according to advisors, is that we are seeing a lot more asset allocation and better-diversified portfolios. Mark commented that a challenge for advisors is persuading the client not to rebuild their kitchen, for example. The one I hear most from ours is having a client diversify a position that is up, or to buy into something that was not up. They have historically chased performance, particularly if it is validated by a third party, so having clients develop those disciplines that you would see in pension funds and corporate accounts is a huge challenge for these advisors.

6. Increased Value of Advice

In this climate, therefore, one of the by-products of there being no obvious place for the funds is that the value of the advice of diversifying the risk has increased in the client’s perception. We provide the tools and products for that; we allow them to customise allocations, with options for passive or active management, and options to choose what they do and do not pay for. This aligns very closely with the behaviour of these Baby Boomers.

III. Regulatory Climate

1. State versus Federal Rights

One of the Baby Boomers is New York State Attorney General, Eliot Spitzer. The regulatory climate, as Mark Casady alluded to, has been redefined by people like him. There has been a very interesting debate in the last 24 months in the US, which is essentially around state rights versus federal rights and who governs this process: if mutual funds are listed with the Securities and Exchange Commission (SEC), and governed by the National Association of Securities Dealers (NASD) in terms of sales practices, but sold in New York, whose jurisdiction is that? We saw a very interesting battle in that respect during the last two years, which the consumer won. Arthur Levitt, tonight’s predinner speaker, was the longest-serving head of the SEC, and I would suggest you think of some questions on his views on that.

2. Greater Transparency

However, whether the state or federal authorities won, the consumer is ultimately better off as a result of the process, since it has led to greater transparency. Mark referred to how revenue-sharing occurs between manufacturers and distributors; our industry is probably now the most transparent of any in the US. I often hear the analogy of our industry being very similar to the pharmaceutical business: we are marketing an intangible and trying to reserve the mental 'shelf space' of an advice-giver, whose biggest challenge is compliance. Patients visit their doctor because they do not feel well; they are prescribed antibiotics and, halfway through the course of treatment, they start to feel better and fail to finish it.

This is exactly what our representatives have to face. Once a client has spoken to them about their plans for retirement, they will start saving. One or two funds will perform better than expected, so they will stop saving as much as they were. The same compliance element is there. That is all embedded in this process but, like that process, the regulatory model continues to build. One of the larger regional firms has stipulated that, before a presentation can be made to a client, the client information is gathered, populated in a series of forms, shown to the branch manager for approval, and approved or not. Only then can the advisor talk to the client, and these are not "rookies," but advisors with decades of experience. It is a quality firm, with no particularly unusual regulatory history, but that is the environment in which we are in. The regulation, therefore, has redefined the marketplace. It has redefined revenue-sharing and its transparency, and the sales process.

3. Enforcement

A UK-type issue has also arrived in the US. Our regulators are divided into two groups at the federal level: a policy unit, which writes the codes and procedures that we follow, and an enforcement unit. If you are meeting with enforcement, you will probably need to bring an attorney with you, since these are very serious people who like to find fault wherever they can. They are the people who take firms "out of the game" if they do not like their behaviour. Currently, there is some disconnect between the two.

The enforcement unit is ahead of the policy unit, in that they are implying, on the US market, a climate of best practice. You have "reasons why" letters in your marketplace, so that may sound trivial, but the standard for securities or product sales in the US was suitability: with my age, income, liquidity and investment experience, is it suitable for me to own this type of contract, and is that a suitable provider? There has never been a standard around whether JNL is the best company and Perspective II is the best solution for that client. That is very much implied in the current climate; it is not policy, but that is the way in which enforcement is dealing with firms and representatives.

It is a very good thing for the consumer, but very complicated for the advisor. Greg showed you that there are 8,000 mutual funds and 500 VAs; our contract alone has thousands of combinations. It is, therefore, an interesting market if one expects the advisors to be the expert on all of these things, and we are seeing behaviour, which, in some way, reduces risk for the advice-providers and the firms. Major wirehouses in New York now have a "style box" on their sales desk, with value versus growth, and large cap versus small cap. In that grid are the top-performing funds out of the thousands that are available in each category, and a strong recommendation from the firm that you stay inside that box. They do not want to take the risk of not having had a reason for their recommendation.

4. Persistency

Clark mentioned persistency in the wirehouses. It has improved persistency around what is being sold today in the wirehouses, because there is less of a feeling that you can simply move a product once the surrender charges disappear. We have always had rules in the US that there should be a good reason for a sale, independent of the good reason for the new purchase; suddenly, the idea of locking in a higher death benefit may not be appropriate enough. Again, we think that that is good for consumers and is shaping what sections of the market are profitable, how you do business, and how accurate you are at collecting and managing data.

5. Inorganic Consolidation

Clark talked about inorganic consolidation; this year, 1,600 firms have reduced to 1,100. There are more entities than that, but we consider JNL to be one life company, and we would not take our holding companies into account. In terms of the sales of the organisations, on the organic side, there has already been quite heavy consolidation. For the balance of my presentation, I will focus on the VA business. If we are trying to convince you that JNL is a very good play in this fairly easily-defined opportunity in the US, the solution that is most likely to be attractive to those clients is a VA contract. That does not mean that index annuities and fixed contracts do not have value, but simply that, more likely than not, that is the sort of thing you are likely to see, and all the major players are in that space.

IV. Three Strategies Deployed by Top US Players

1. Overview

The top 15 companies control the market organically, and they do this in three ways; there are only three strategies deployed in the US by the top players. There are many other business models used by smaller players but, other than entertainment value, there is not much value in discussing them. The attributes I will outline are visible in all companies at various levels:

- Sub-account selection.
- Feature and price leadership.
- Producer-focused distribution.

Companies have tried having a price-only model, but have failed; they have tried having bad sub-accounts and being good at the other two, but they have failed. You have to be competitive in the areas that you are not focused on.

2. Sub-Account Selection

If you have the right mutual fund managers running your sub-accounts, you get huge lift from that. Mark mentioned American Funds, which currently controls about two-thirds of the net mutual fund flows in the US. At this point in time, therefore, the funds that partnered with them are enjoying some lift from that. The advantage is that, when those fund families are up, so are your sales; the disadvantage is that, when those fund families are done, so are your sales, and your net redemptions or transfers are up. However, in any case, you need strong, competitive asset management options for the client, and you can gain huge lift from having a particular manager who is in vogue.

3. Feature and Price Leadership

Feature and price leadership takes on different aspects in the VA business. It can be an easily-measured price advantage. Firms will have fixed accounts inside the variable annuities; currently, about 28% of funds are inside a guaranteed account. There is a hybrid of them, called dollar-cost averaging (DCA) accounts, which you have to come out of over a series of payments, with the idea that you will enter the market slowly with the cash. A very popular promotion has been around spiking the rate of the DCA, and the representative who sits down with a client who does not know whether now is the time to enter the market says, “Don’t worry about it – we’ll start the money in a DCA, which is currently yielding 8%. We’ll slowly move the money into equities in the following allocation. You’ll enter the market over time, which has been a historically prudent way to do so.”

If someone spikes that account, we can very easily back into the promotion cost, because it is simply an interest expense. You just take the duration of the promotion and the liquidity, and you can come up with how much those cost, so that is a measurable promotion. There were commission promotions but, in the current regulatory climate, few firms who distribute product are interested in them. They want their pricing to look neutral to who is paying them wide, which is a prudent business model, and they do not want commission to be the driving factor around why they choose one company over another. They are not unique in that view, so commission promotions are less likely to occur.

Feature promotions fall into two categories: measurable and non-measurable. You can subsidise the price of a feature, and you may or may not disclose that to the marketplace, but a mis-priced or aggressively-priced feature will very successfully acquire market share. What these clients are trying to avoid is running out of money, so if you mis-price or aggressively price an income feature, it is very attractive to these clients and their advisors. Depending on the structure, it is measurable; some are not. We see guaranteed minimum account balance promotions. We have seen the ability to have your account guaranteed – that is, made whole at the end of ten years – regardless of what you invested in or how it performed, for as little as ten basis points. That means that, for ten basis points, someone has hedged NASDAQ funds, emerging market funds and high-yield funds, and I am positive that everyone in this room realises that ten basis points will not hedge that sort of risk. However, for a client in the accumulation phase, that is a very attractive way of looking at participating in the equity market, so it is effectively a feature promotion.

Those have worked brilliantly; the challenge with pricing promotions is that somebody can immediately come in on top of you on price. It is a question of pain threshold, excess capital and a desire to have market share versus profit or value. Clark referred to the firms that do not provide any accounting on the profitability of what they are currently selling. This is true of the majority of our competitors, and it took quite a long time for that to play out, so it does not always have the immediate impact on the reported numbers that you would see or the accounting methodologies that you are used to.

4. Producer-Focused Distribution

This model is the hardest to implement, the slowest to build, and very difficult to maintain. The question around it is whether you are doing things that are material to the advisor, in helping them to build their business, whereby you become engrained in their business. Going back to the pharmaceutical analogy, are you their source of training and accurate information? Have you demonstrated enough expertise for them to trust you when you say, “This is how you handle this situation. These are your choices – we are one of them?” How do you get money out of an individual retirement account (IRA) if the client is laid off early? There are fairly complicated regulations in this respect. We not only provide this kind of service, but we guarantee the calculations to them. How do you address state issues? How do you structure these contracts to create different types of benefits? How do you build their practice?

We probably receive 50 requests a year for Greg to be the keynote speaker at conferences such as LPL’s, in order to deliver a message that JNL has built as a module to develop business to their audience. That did not happen in one year; it took ten years of reputation and of them trusting us, and we now receive the invitations before they know the topic. The producer-focused model is where JNL plays. We think it is a very competitive and sustainable model. We understand there is an ongoing investment in terms of time and effort, but all have elements of that.

V. Competitive and Market Landscape

1. Gross and Net Sales

Depending on the quarter, the top 15 players generate 75-80% of VA sales. They have all focused on one of those three elements in different ways, but those elements reflect the business strategy of all 15 of those companies. We added gross and net sales. Other than VARDS, another source cited in the US is FRC, which also tracks net sales. You will see a difference in the two. FRC tends not to count fixed assets inside the VA; it is interested in your separate, equity-type account balances. It is a bit slower at producing results than VARDS, but both are good.

2. Net Flows

Net flows are the key metric. As shareholders, if that number is going up, so are the numbers in the assets. It also demonstrates your choice of channels; the channels with higher turnover will reflect, sooner or later, in your net numbers. It will reflect the balance of choices you made on pricing profitability, and it will reflect service. If clients are not happy, they will leave, and that is an asset retention issue that goes straight to the bottom line.

The opportunity that we are talking about is the space that JNL is currently playing in; this is not somewhere we will be in 2012. You saw some very grand and impressive projections of where this business is going to be, but it is here now. We do business with these people and their advisors now. In terms of the clients who we acquired in the first half of 2005, we are building the products that they want and selling them through the advisors who they consult. This is our space now, so when we believe we are well-positioned to participate, it is because we are participating here.

3. Product Manufacturing

The industry provider of software could replicate all of our capabilities with Perspective II, in which case 45 of the top firms would have the ability to do that – they would have product-specific capability. Many of you were with us in London three years ago, when we talked about platforms. JNL has built, across its business, platforms rather than product chassis. It is a subtle difference, but if you compare our insurance business with that of Curian or National Planning Holdings (NPH), you will see that we cube data, connect to the marketplace in every way possible, and add options to the front end that clients can choose from. That is what the advisor sees. If we want to populate an application, or if the client wants to make a choice, we have the information. That is very different to a product engine, which is specific and siloed around one particular offering.

4. Platform or Product Engine?

If Vantage, one of our competitors, came out with a software suite that replicated Perspective II, one of the dynamics that competitors would have is that it would be yet another iteration of their product engine – it is not their IT platform. This distinction is critical, because it goes to speed to market and innovation, and to delivery and service. There are thousands of combinations on Perspective II. How do you get that to somebody's desk in Lansing when my dad calls, as an owner, and he wants to know what choices he has and cannot have? We have state variations, contract variations and the choices he has already made, so how do we manage that information to our worker in Denver in Lansing? That is a key element of going to these complex products: can you manage the complexity of service?

5. "A Dog with a Note in Its Mouth"

On the front-end, on the distribution models, if your wholesale strategy is to have lots of good, hard-working wholesalers, your typical model is giving them a very tight story, making them practice saying it and, when they can say it well, sending them out to tell it to a lot of people. Our people nickname it “a dog with a note in its mouth.” It is a very different approach to saying, “We’re going to sit down in your office with a needs-based plan and to discuss a product with lots of possible outcomes. The only ones we’re going to go through are those that apply to your clients and your business. We’ll probably sift through your book of business after the second or third meeting and discuss what aspects of it would be appropriate for which clients.”

One is transaction-oriented, making quick entries and exits and seeing lots of people; the other is a consultative-type sale. It is harder and slower and it assumes trust. It requires us to demonstrate expertise, but if you are going to offer customised solutions, you cannot send in a “rookie” wholesaler with one sales idea. It will not work, because the product is too complex. There is more to the manufacturing process than replicating the IT platform.

6. Intermediary Management

We have talked about intermediary management with you for ten years. The choice of channels is everything. We measure the profitability of our distributors to the representative. If our JNL Distributors (JNLD), regional broker-dealer (RBD) or bank channels have a representative surrendering product, we know it right away. The same people talking to them about selling JNL product begin talking to them about why they are taking assets out of JNL, what those clients’ opportunities look like, and what is happening at the business practice. We are the only player in the industry to do that. Your choice of the representatives, firms and channels defines whether the whole exercise is profitable. If you get into a channel that has no headroom, you spend a lot of money investing in a space that has no growth; if it does not have enough margin in it, it is not profitable. You are looking for channels that have a fairly odd combination, which is sustainable growth and some material barriers to entry.

VI. Market Segments

1. Independent Financial Advisors (IFAs)

LPL resides in the IFA market. The bottom 19% is NPH, which is our own broker-dealer. We compete in that firm in the same way as we do in LPL – there is no commission or other promotional incentives for our advisors and we have to compete for space with them. There is some friction with them around selling house product, because they want to be seen by their clients as independent, so we have to succeed, at quite a high standard in our own firm, to have them recommend our products.

The industry does about 31% of their business in the IFA channel; we do 73%. This channel comprises the clients’ neighbours, friends and associates. They live in the same communities and attend the same church, yacht club or golf course. The key dynamic here is that, if you embarrass them in their business practice, you embarrass them in their social circle. If you damage their reputation with a service mistake, you damage their potential for future business in that sphere of business. They absolutely understand that, and nothing offends them more than a vendor who does not understand that. If we mess up a statement, for example, they will not say, “JNL messed up my statement;” they will say, “The product that my advisor sold me does not work – they cannot even get the statement right,” and the advisor’s integrity is damaged. The link between service and distribution is, therefore, key.

2. Regional Firms

All these firms have cycles, and we try to time our entrance and participation around what we see as the most advantageous points in the cycle. We decided to expand into regional firms because they are becoming more planning-like, which is an aspect that we like.

- They are scattered more through the Midwest and offer full service.

- These people are employees, rather than independent contractors.
- They are moving further and further into the planning-oriented space, which is a good fit for us.
- They are extremely difficult to wholesale and act like independent advisors.
- They are smaller offices and are difficult to gain access to, but they control a very large client base and are effective for us. We have enjoyed some real success there.

3. Banks

We have always liked banks, which is where the money still is. Many client assets go from time deposits to these more equity-based products. The banks' incentive there is to diversify revenue and try to retain clients. Their success at developing advice models varies wildly between firms. Their ability to manage advisors and put a proposition together is still relatively limited as an industry. There are a few clear winners but, for the most part, they are rolling over their own assets, converting them from spread to fee. However, clients trust and like them. They have very stable relationships and these are very good places for us to do business. Because their ability to give advice is underdeveloped, our ability to add value there is huge.

We have gone into some of these thrift and credit unions and small banks and given them everything on a campaign; we have trained their people, helped them with the distribution materials and regulatory issues, assisted them in meetings and seminars, and had a material impact on their business. It is very fertile ground if you have a distribution-focused organisation, because they need distribution help, although they have assets. This is the opposite issue to that which advisors have; advisors have the distribution experience but are trying to accumulate assets. It is a great space, which we love, and you will continue to see us competing and doing business there.

4. Captive Agencies

Following the acquisition of Life of Georgia, we had a few hundred representatives in the south-east agency, which we have now consolidated down to the producers who we thought had the most potential and a particular focus on asset retention for us. They are the contradiction to my upcoming comments, but they were not priced into the transaction. That does not mean that we do not value them, but just that we would not look to buy into the captive agency market. We sell index, fixed and life products here, because they are non-registered products that do not require a securities licence. They are not done through the captive agency's broker-dealer, but directly through the representatives. We have access to these representatives with our traditional products. We do not want to build a captive agency, because we do not want to continue to feed one. If you build a large agency, your product manufacturing is now based on the fact that you have costs embedded in that distribution channel. These are, for the most part, employees, and you need to provide a certain amount of product to keep them productive and competitive. If we do that, we lose the flexibility we currently have to pull back or accelerate our focus on a given segment of the industry product-wise.

The second issue which is material and current is that there is an implied climate that says that it is probably not acceptable to own manufacturing and distribution. The largest example of that is Citicorp. In the US, Citicorp has done a deal with Legg Mason, where one party takes the representatives and the other the asset management. We do not believe that that conflict exists; the way to mitigate the regulatory risk of that is never to create one: do not advantage the products commission-wise or in any way that you would not show a client and maintain transparency around who manufactures the product.

In the captive agency model, however, if you take the regulatory climates we have discussed so far and bring them together, they are challenging. It is very difficult to have best product as an implied standard if you have only one company's product. It is hard to suggest that there is no pressure or incentive if all you have is house brand. In the US, therefore, captive agencies are broadening their product menus, looking to move out of the "only sell house brand" model. In our opinion, this diminishes the value of the captive agency to the firm paying for it, because they are now moving very closely to an IFA-type model but doing it without the economics, the structure, and some of the other benefits of the IFA model. That is why we are not in that space, in terms of growing into it, or trying to find firms that have that sort of model.

5. Direct Response

Direct Response makes up 1% of the market, and is represented by Fidelity. Fidelity has a very unique model currently, where it is pushing annuities. It has filed some products in addition to the VA contracts we have been talking about this morning. It has an excellent retirement plan site, where it tries to be the advice-provider for people with 401k plans. The issue for 401k-providers is that more than 95% of the assets leave on retirement. Fidelity is a major plan provider and has done an outstanding job in that space. It administers our plan and is a very good company, but it wants to keep some of that money, so it has come up with a fairly unique set of tools for a non-advice-based model, very similar to what an advisor would do candidly with their client, and has put it out their for its clients to use. For a very small segment of the market, it will be very effective, since it is a quality offering. Fidelity Life Assurance offers VAs with income products similar to those that we offer.

6. Wirehouses

The final 11% is comprised of wirehouses. We have not, historically, participated in wirehouses. ten years ago in London, this was one of the major topics. I spent a fair amount of my career at Smith Barney, running insurance and annuities so, at that point in time, I had relatively current information. It is now tainted by ten years with JNL, but we see them as expensive then. At the peak, you could spend $2.4 million just to be on one of the wirehouse's product list, even before you sell any product. There is an expectation of coverage, and there are lot of them, so your wholesaling expense is high. There is a transaction orientation and they are still trying to establish what their model is going to be.

This is a fairly dangerous space for us to be in. If, for example, Smith Barney were to merge with Legg Mason, they would come up with one list. You could, therefore, have invested a decade in relationships in Smith Barney, and you would now be faced with the challenge of a Legg Mason being in charge of financial services, which is highly likely in that model, and your relationships there do not exist. There are some interesting dynamics in that space. The regulatory climate has improved the tariffs and the persistency, and it is something that we would look at opportunistically, but under no circumstances would I say that it is something that we are looking to do. The difference between this channel 10 years ago and today is that it makes up an ever-diminishing part of the marketplace. It is not necessarily where we need to be. We cover just over half the market, which we like.

7. Acquisition Management

We have acquired broker-dealers SII and INVEST, and ICA, Jackson Federal, and Life of Georgia, and we have integrated them successfully. The reason for including this in today's presentation is not to go through the economics of each, but to make the argument that, if you look at US insurers' handling of acquisitions, they are a reasonable test for their administrative and IT capability, their financial expertise, the depth of their in-house staff and, most importantly, their discipline. We have integrated everything that we have acquired.

The rationale for the Life of Georgia transaction was around a very attractive return and scale. We hardly ever say we want scale, but we had a life platform that was up and running and had huge capacity, and we knew that it could handle materially higher policy counts. We acquired 1.6 million life policies, which tripled the number we had on the system at that time and delivered material improvements in unit cost. There is no question that making it bigger helped us.

It draws on and demonstrates competencies that we have. We do not price marginally, but allow me to give you an example of what it does to our cost basis. Those 1.6 million policies will cost us an additional $8 million a year on a $244 million expense base. That $8 million is in the first year, since we have additional IT and integration costs related to the conversion. I have asked George Napoles to cover the staffing changes that Life of Georgia impacted Jackson with, because they are material to how we do business.

Why do it again? It diversifies earnings and, on the asset liability management side, it gives us different options, all of which we think are good. They are good for our shareholders and provide the kinds of benefits that we like from bolt-ons, through more predictable earnings and more clients at an attractive acquisition rate. In terms of the $254 million expense base, we are confident that it generates 12% internal rate of return (IRR). It moves our life reserves from 10% to 12%. More impressively, as at May, we were over 80% converted on the transaction; in other words, more than 1.3 million policies already on our books. We think that that demonstrates how we do business.

VII. Conclusion

You have a day and a half left with us. Our intention on this trip is to have you see our people. We do not have tangible products; what we have is our execution, our ability to innovate, and our people's expertise. We know that everybody who stands in front of you says, "we have better people," we think that the best proof of that is to show you the processes, the people, and how we work. Our belief is that you will look at this and say, "Jackson has the attributes to grow. Its platforms are scaleable. Its disciplines are not specific to a set product, but are ones that go to the market space we are in and how we want to do business." Our ability to grow talent is unique, and most of the people you will meet have been with JNL for a long time. They were not cherry-picked by tenure – that is just our model. You are welcome to ask anybody about how they got there, how long they have been here and why. However, we think that the model produces an outcome that positions JNL, currently and in the future, in front of all the assets that Greg spoke about.

The attributes of a company that is going to succeed are speed to market, innovation, execution and proven expertise. The expertise element, with the representatives and clients, has a different impact. Every time we demonstrate expertise, we receive a little more permission from them. If a representative's first contract goes well, they will give us the second one; by the fifth or sixth transaction, we are part of their business. If the first policy comes back on time and accurate, a huge level of trust is gained. Silly things like the timeliness of a single, simple statement, the tax information, and how well they are treated on the phone, goes to how much they trust us and how long they stay with, which then goes to your return as the stakeholder. All of that is consistent throughout the company. We take the same approach, and you will see the same attributes in technology, distribution, administration, our broker-dealers, and Curian, because one of the most unique things about the company is its consistent culture across the board.

JNL's Distribution Advantage in the Era of the Boomer

Clifford Jack

Executive Vice President and Chief Distribution Officer, JNL

I. Preamble

Mike gave you an overview of our approach to service, technology and distribution; Greg covered the markets and their size; Mark gave you an outsider's perspective of our market space. I would like to drill down and focus on three areas:

- An overview of our distribution companies.
- The markets we participate in.
- The reasons why we think we are advantaged in those particular markets.

II. Overview of Distribution Companies

1. Wholesale

We have two major distribution channels: wholesale and retail. There are tremendous synergies across the top of these organisations. Many opportunities present themselves when you own a retail franchise as well as a wholesale franchise. We understand both sides of these businesses and I hope to be able to prove that to you during this presentation. Clark mentioned the various channels that we participate in, and the fact that we have dedicated wholesaling forces. I will try to remind you of some of the specific nuances of those channels as we proceed.

a. Market size

I would like to frame the size of the market a little differently to what you have seen in some of the previous presenters' presentations. The US annuity market space, at least in 2004, which consists of indexed annuities, fixed annuities and variable annuities, is about $220 billion in size. That is represented by approximately eight categories. We have made conscious decisions to be in the four distribution channels that we operate in because we like their economics. We think that we can differentiate ourselves and that, ultimately, these channels are more profitable from the shareholder standpoint.

I would also like to draw your attention to the size of the market space that we are in. Of the $220 billion, the four markets in which we participate make up approximately $136 billion. In 2004, as you know, we had a $6.6 billion retail segment, in terms of sales. Our market share in each distribution channel ranged between 2% and 10%. One question consistently posed to us is whether we have headroom in the markets where we currently participate, and I would like to demonstrate that we do, supported by some facts.

b. Strategy

It is important to note that you can pick your markets and be right about them, but you can still fail, so we look at the world from a strategic and tactical standpoint. It is also true that you can have a good strategy but fail at execution, and we believe that a good strategy with failed execution is a poor business plan. I would like to take you through how we look at the businesses from a strategic standpoint, and how we look at the tactics of executing in that business.

We have a process-driven and -oriented sales culture. We have a tremendous track record in home-growing talent, which is a wonderful benefit for us, since it allows us train people in our way of doing things. It may not be the right way for everyone else, but it is the right way for us and it is a cultural fit. It also generates significant loyalty, and earlier speakers have alluded to the fact that we have people who have been with us for quite some time. I think that part of the reason for that is that we have been able to give them the upside opportunities and to train them in our culture.

We are also quite demanding; we terminate people's employment more readily and more rapidly than any other player in the industry. We do that because we do not believe that we can afford to carry people who do not carry their own weight and drive these processes throughout the organisation. Some people may view that as a harsh culture; we believe that it is a performance-based culture and we think that, by demanding the best, we bring out the best and enable effective performance. We also have a differentiated distribution model. We bring things that others choose not to focus on, such as a science and metrics, to our distribution sales model, which, in other organisations, is more of an art.

We have a very complex business model in the context of a distribution company. The best example I can give you is last night. Mark Casady and I have known each other for a while, and we had scheduled a two-hour dinner; it turned out to be a four-hour dinner, followed by two hours of drinks afterwards. If you looked over at any given time, you may have thought that we were arguing; you may have thought that we were having a good time. The reality is that that is a microcosm of our business. If you think about our challenge, Mark said that we are a product provider to LPL. He is number one, and we are the sixth-largest independent broker-dealer that has been quite successful in growing market share in its own right. Part of the conversation goes to asking how we compete, and still play well, with our clients. Last night, therefore, was a very good example of that.

If you are a product provider exclusively to the firms that you do business with, you become a commodity; if you provide more value than just the product feature set, you are more than a commodity to any individual. 99% of what we talked about was not JNL products, but the industry and its direction. It was a collaborative conversation about the things that we could do together. It involved discussions of the regulatory environment. As an organisation, that is something that we can bring and that gives us an advantage in our distribution model.

c. Tactics

None of that, however, really matters if people do not trust you. One of the benefits of having been around for a while and of having consistency in our management team, our philosophy, and the way that we do things, is that we do not embarrass people. We are consistent and they know what to expect and what not to expect from us. Our reputation is something we guard very closely and has been developed over quite some time. However, the strategy is only part of the equation, and tactics are what make us different.

We have a dedicated wholesaling force on a channel and product basis. We track activity like nobody else does, and I will tell you how we bring science to the art of wholesaling and prove to you that this is a process that has been developed over time. It would be very difficult to replicate, and we think we do it well. In terms of home-growing our talent, the golf-ball analogy is something that we have used for years.

In the old days of selling, people who were low-handicap golfers, who bought nice lunches and dinners, and who bought lots of golf balls, typically won the business. It did not really matter what product you had; some people would say those were 'the good old days'. Those people do not work in our organisation; they would fail. They are typically people who lead with the product feature, play a round of golf, end with the product feature, mention a commission, and win the business – that is not us. Today, the market is too complex and the advisors are being squeezed in every direction by regulatory and margin pressures. The representatives are challenged every day, so the people who win business today are those who solve the representatives' problems, which are time and money. If you can find a way of solving those problems, you have an advantaged model in their mind.

JNL Distributors

2. Four Divisions

It is not golf balls - it is time and money. If you can find a way to solve the representative's problems, you have an advantaged model, in their mind. Let me take you through some of the specifics of each of the distribution companies.

As you know, JNL Distributors is made up of four individual divisions. As stated earlier, we are in the financial institutions, the regional broker-dealers, and the independents - through both the guaranteed-product side of our business, and the registered-product side – which, altogether, add up to approximately 230 internal and external wholesalers, who are representing the Jackson National product suite out in the market. They sell all of the things that we manufacture, including variable annuities, fixed annuities, fixed index annuities, and, of course, life insurance.

In any given year, the wholesalers talk to some 83,000 registered representatives and agents who are appointed to do a piece of Jackson National business. Many of those representatives are appointed through a selling agreement, which is a broker-dealer relationship, if you will. 83,000 is a big number, but is it a meaningful number? The question is, who cares?

3. Headroom and Market Share

Let me step you through that. $136 billion is what we chase, and we have about a 5% market share in those particular markets. Still, far more important than the 83,000 appointed agents is the headroom. What is the opportunity for us in the markets that we serve, and where do we currently stand? To me, the most important figure, when looking at our distribution opportunities, is the comparable between the 300,000 that are available and the 22,000 that do business with us currently. This effectively means we have a 7% share of the advisors, on a producing advisor basis. That, to me, means we have got headroom.

There are a number of ways to obtain market share and to push all the numbers up. First of all, it has to be business as usual. As indicated by the sales results and market penetration, etc., we think we are doing things well, but you have to continue to innovate. Both Mike and Clark used a slide in summary that contained "innovation." If you do not innovate, you die. It is not just product innovation - it is everything that we do. What we did five years ago is not what we do today. What we did five months ago is what we planned a year ago. You have to constantly push yourself in this business. There are some organizations that are better at that than others, and we think that is one of our core competencies.

4. Metropolitan Statistical Areas

We talked about the science and the math in the art of wholesaling. This is going to look like a very odd map, and let me try to step you through it. In the US, there are some $32 trillion of investible assets, $20 trillion of which are considered "movable," in other words the owner of that asset, if they choose, has the opportunity to move it from one place to another. So, there is $32 trillion in total, and $20 trillion of movable assets. It is our job to find out where those assets are, and we do not look at the world by simply saying, "Let's go find a good wholesaler and, wherever that person lives, say Chicago, then we are going to put our office there." The way that we look at the world is through Metropolitan Statistical Areas - I keep saying "the world," and I apologise, that is a very American comment. We look at the US through MSAs. Why does that matter?

It makes for a nice chart, with a lot of interesting round circles that are very difficult to read. I live in the state of Colorado, where there are four MSAs. If you are trying to wholesale Colorado and you do not wholesale those four MSAs, you are not going to be effective. Even further, if you do not know about the assets in Colorado, or where they are, how do you effectively pursue those assets? As a distribution company, we know how many assets there are available for us, as movable assets, in variable annuity products, and in other related products. We know how many assets we have, so we know what our market share is, broken down by MSAs, and we place our people where the money is. We hold them accountable to go out and pursue that. So there is science, and a mathematical equation.

5. Internal Contact

Knowing where the money is and getting the money are two different challenges. This is how we go about getting the money, with some more large numbers for you to sift through. I will walk you through the most important elements. On an annualized basis, we will make approximately 500,000-plus internal contacts and telephone calls, by which I mean our internal wholesalers will have successfully made contact, and have had substantive conversations, with representatives in the field more than 500,000 times. In any given year, our external wholesalers, located in the MSAs, will have made 174,000 contacts. In addition to that, they will do just under 70,000 – and that number continues to increase – in-person meetings with registered representatives and advisors, all across the country. What does that mean?

III. National Planning Holdings

1. Four Firms

It means our producers see, hear, and buy from us more often. We talked about the wholesaling side of the business in JNLD, and I would like to shift to National Planning Holdings (NPH), which, as you will have heard from several of the speakers, including our guest speaker, is an independent broker-dealer. I will step you through some of the metrics for NPH, some of which you will have seen.

NPH consists of four firms. One we grew from scratch, in fact the largest that we grew from a zero base, which is National Planning Corporation, launched in July 1998. We purchased SII Investments in 1998, and the other two firms in 2000. All of that rolled up makes us now the sixth-largest independent broker-dealer in the country. We are growing very rapidly relative to the competition. Through the first three-quarters of the this year, we had a little over $7 billion in sales, and over $300 million in revenue, generated by those 2,500 individual representatives. The value proposition of our broker-dealers is probably different from any firm that you will come across in this environment. The value proposition for our retail broker-dealers is high payout, high technology, and low touch. That may sound very odd, but it works.

We have believed for a long time that solving the advisor’s problems are paramount to success, in both our wholesaling and retail companies. Our representatives are demanding very high payouts, relative to, say the wirehouse business, because they are moving away from a wirehouse model and becoming the CEO of their own businesses, looking at gross revenues and trying to increase their margins as much as possible. People who can facilitate the services required at a high payout level are the people who have been successful. How do you do that and make money yourself?

2. Technology

You do that through investing in technology, which performs the services the advisors are expecting and need, and solves their problems. One in two is solving their problems, and it gets back to time and money. Our technology allows for the advisor to maximise their time, to do it in the most compliant and efficient manner in the marketplace today, and to still receive an attract payout, relative to the competition. How do we pay for all of that?

3. Retail Broker-Dealers

We have a very efficient back office, with respect to the number of people that we employ, that service those representatives. We tell the representatives coming in, and this is never a surprise to them. The value proposition and the take-up rate have been very strong. The other benefit is we have had a very high degree in selling Jackson National product through our retail broker-dealers. We do not do that because they are forced to do anything, as in some cases they are concerned by perceived conflict of interest, and we make no special payouts or presidential letters to induce this business.

What ends up happening is they are appreciative of the work the broker-dealers have done for them, in solving some of their problems, and that the two companies have worked closely together, in joint technology and roll-out initiatives. We listen and have had a very nice take-up rate, not just of our variable annuity products, like Curian. It is a wonderful opportunity for us to have intelligence that is not otherwise available to competitors who do not have a retail broker-dealer. Everyday we live the challenges of owning a retail broker-dealer. We know what the problems are before they are evident to people who are simply in the wholesaling business, and we think there is tremendous value in owning NPH, aside from some of the other obvious benefits. Of course, NPH is profitable too.

4. Opportunity For Growth

I want to stress that we have lots of opportunity for growth. We think the pool of registered representatives is currently just shy of 125,000, and we have just below 2,500 of them, or approximately 2%. The other thing that is important to note is that the shift from other distribution companies, and broker-dealers, into the independent space is pretty significant, and tough to ignore. We think we are in the right spot and there is plenty of headroom in that space. Then the question again is, “how do we go about pursuing that?”

I do think it is business as usual. We are good at what we do, but it cannot just be business as usual for us. We cannot ever be satisfied that what we have now, because we are very proud of it, in terms of the value proposition, is good enough, as it is not and it never will be. We have got some ideas that we are working on which we hope to share with you when they come to fruition.

IV. Curian Capital

1. Customisable Mutual Fund

For those of you who are not as familiar with the separate account space we have alluded to, I would like you to think about it as a customisable mutual fund. That is not a perfect description – it is a perfect description with five minutes left in the presentation – but it is a customisable mutual fund.

I have broken it down into three categories: benefits to the company, benefits to the representatives, and benefits to the ultimate owner of these products, which coincides with the benefits from the regulatory perspective. This is a big and growing business. The separate account business is $620 billion per annum, and the expected compounded rate is roughly 13%. It is also a business that is built off of things that we already do very well, so we are able to strengthen our relationships with current advisors, and add new advisors into the system.

Solving the representatives’ problems is one of the benefits of doing business with Curian. I talked to you about time, and paper is a time-waster. Curian is 100% paperless, and that has worked well. Compliance is a time-waster in the representative’s mind. Although they know it is a necessity, they do not like it. The more time that they have to spend on compliance the less time they are generating revenue. They would highly value someone who could solve their compliance issues. We have automated compliance tools to do just that.

2. Liquidity Event

One of things that all advisors in the US are talking about today is the liquidity event. Many people will tell you that the day that they leave Merrill Lynch is the day they start to think about the liquidity event. Advisors long ago recognized that if they have recurring revenues in their practices, in the form of fees versus transaction revenues, their practices are more valuable.

3. Transparency

From a client's standpoint, Curian and the separate account industry are fully transparent, on a 24-by-seven basis, which is very attractive. There are tax efficiencies relative to the mutual fund industry. There is customisable ability, to exclude stocks and sectors and industries, and we allow for clients to have access to institutional-quality money managers, which they otherwise would never have access to, at low-account minimums of $25,000. There is less than a 2% share of the 116,000 registered investment advisors, and the number of advisors is growing even more dramatically than the percentage of assets on a compounded basis. People are pursuing this business and we think we have an opportunity here. Again, we think it is a combination of doing business as usual, and then a number of other things that we are working on now to stay ahead of both the competition and our advisors' needs.

4. Unique Business Plan

I am not sure that people who have my job in other firms would think about things in the same way that we do. You do not come to work for our firm if you want to sell the hot product. We could pursue a number of sales people that we know will be with us for 18 months, during which time we will either have made a decision to compress our pricing and do something to gain market share, or we have wrongly priced a product and they will take advantage of that, because they are very good. As soon as you are no longer wrongly priced or pursuing market share, the sales person will move onto the next "you," whatever that is. We have never chosen to pursue that business plan.

The middle area here, particularly the shareholder, is surprisingly top in mind for our sales people. We talk constantly about the overall returns and the value that we are attempting to add to our portion of the Prudential's business plan. They are educated on it, they understand and value it, and it is something that makes us a bit unique, from a distribution company standpoint.

I appreciate your time and the opportunity to drill down a bit on our distribution companies. I would like to introduce Mr. George Napoles.

Service And Information Technology

George Napoles

EVP, Chief Administrative Officer, JNL

I. Operations Areas

1. Introduction

Thank you, Cliff. My name is George Napoles and I am the Executive Vice-President, and Chief Administrative Officer, at Jackson National. I am also JNL's Chief Information Officer. Although I have responsibility for both areas, I will focus my presentation on our operations areas, and their capabilities and efficiencies.

2. IT Capability

Our IT plant is excellent, but I believe the best way to demonstrate IT capability is by looking at the impact that technology has on those departments which are critically dependent on its services. The question one might ask is not "Is JNL different?" because, from all the metrics we have seen today, we know that we are. The real question is, "What makes JNL so unique?"

Our approach to differentiating ourselves is not to throw money at the problem, but by the application of common sense and innovation, to achieve cost effective solutions that provide us with a clear, competitive advantage. I obviously do not have time to discuss all facets of our operations, but I would like to give some examples of the types of innovations that we have implemented. Those that I have selected well represent our common sense approach to the application of technology to support our services and marketing areas. In this quick survey of JNL's capabilities, I will give examples in three areas: our IT platform – its flexibility and scalability – our ability to provide personalized service to our clients, and our execution efficiencies.

II. JNL's Unique Advantages

1. Our IT Platform

a. Perspective II

A great example that demonstrates how innovation provides us with unique advantages is in our implementation launch of our unbundled variable annuity, Perspective II. When this product was specified, its features were unique to the insurance industry and there were no computer systems on the market that were capable of administering unbundled variable products. At that time, the ability of our clients to select individual benefits was foreign, and modifying administrative systems to support the thousands of benefit combinations was, and still is, very complex. By using the same VA system that most of our competitors use, we were able to design and implement our IT model in only six months, and at a very modest cost.

However, we did not merely hard-code a quick solution. In this very short timeframe, we implemented a highly flexible design that continues to support a variety of new product features that were not envisioned at the time of launch. Our ability to continue rolling out our new products with new features at great rapidity and with no service issues is a testimony to our application of ingenuity to solve this problem.

This product was introduced three and a half years ago. Since its introduction, it has been one of the hottest selling products on the market. In fact, today it enjoys the position of being the number one product in the US in terms of net flows. Given the popularity of Perspective II, you would think that it has fierce competition, but it does not. One of the primary reasons for that is because of its complexity. Even after three and a half years, other companies still have not been able to modify their systems to support this product. Many companies would love to enter this space, but they just do not know how. Eventually, however, these companies will be able to implement the required enhancements to support an unbundled product, but this does not mean that we will then lose our competitive advantage. The features of this product are constantly changing and becoming ever more complex. For the same reasons that companies were not able to quickly react to initial products, they will continue to struggle in adapting these new features in their inflexible computer systems. We are the market leader for the introduction of innovative products, and we know of no other company who can keep pace with us in our product changes. Unlike other organisations, everything we have done in IT has been designed to accommodate future changes.

b. Disaster recovery strategy

Another example of our common-sense application of innovation is in our disaster recovery (DR) strategy. At one time, our DR plan entailed the use of a hot site from one of the well known vendors. They guaranteed a recovery of 48 hours in case of a catastrophic failure. This meant that if we had an outage projected to be less than two days, we had no choice; we just had to stay down until our systems became available. The cost of that 48-hour disaster recovery solution at today's rates would have been $1.5 million per year.

That 48-hour recovery window is common within our industry today, but we believed we could do better. We still owned our old building, which had a data centre that could be used for our own disaster recovery site. We connected our old building to our home office computer centre, connected it with glass fibre, recycled our old hardware, installed our software, and began transmitting data real-time for redundancy. We also have desks at that DR site that are configured with telephones and PCs connected to our own networks, so we now have a recovery time within an hour as opposed to two days, and at a fraction of the cost of the 48-hour recovery period.

Unfortunately, we recently had a real-life episode that gave us an opportunity to demonstrate the effectiveness of our DR plan. Because of a suspected gas leak in our home office, we were forced to vacate the building. We triggered our DR plan, and within one hour we were again able to service our clients from the old building. With the reconfiguration of the Denver service centre, they will automatically take phone calls intended for Lansing during the brief period of time it takes us to move to our backup centre.

c. Accurate servicing options

Our clients have options to use the type of service with which they are most comfortable. They can service their policy, by telephone, by interactive voice response (IVR), by our website, by email or by post. Through cost effective innovation, JNL delivers highly personalised and accurate information to our clients. Even though we are low cost, we do provide service of the highest quality. For example, our telephone service representatives are accurate over 98% of the time in answering our clients' questions. This explains why our service complaints are currently running at a record low of only third complaints per 100,000 clients on an annualised basis.

2. Providing Personalised Service

Accuracy is not the only measure of good service. Our presentation, good listening skills and customer empathy are equally as important in achieving customer satisfaction. At JNL, not only do we believe that we combine all these facets of good service; it has been independently demonstrated by the receipt from Service Quality Management to Jackson National of an award for the best service within the financial services industry.

a. Product reference guide

Our product reference guide is our online reference manual. At face value, this might appear ordinary and the same as many other companies use. What makes ours different is that our guide is linked to the online screens and displays information that is unique to the policy being serviced. Because our industry is highly regulated by each state, each product has many variations, dictated by these regulatory bodies. Except for language, our state regulatory climate would be equivalent to Prudential selling business in 50 different European countries. As you can imagine, because of the thousands of product permutations, an incredible amount of knowledge is required to service a policy and provide answers to our clients. Our product reference guide automatically extracts information like plan, age, gender and state, and then, using this data, it dynamically composes and displays information regarding contract provisions and our standard operating procedures that are tailored to that individual policy being serviced. This significantly reduces errors, increases productivity, and results in better customer service. Needless to say, the product reference guide also significantly reduces the training time for our new service associates, and it facilitates bringing new products to the market. A non-intuitive benefit is that it ensures that we are in regulatory compliance. It was invaluable in enabling us to easily absorb the Life of Georgia block.

b. Contact history

Another system that we have is contact history. For each call, we automatically capture demographic information about the client or contact. This includes things about who is calling, including their name, gender, zip code, agent, line of business and more. With a few simple keystrokes, our service representative completes a stub by adding the reason for the call, the results of the call, and other pertinent information like alerts or problems that a subsequent operator should be aware of if the client calls back.

Lots of companies have similar contact histories, so why is ours so different? We can push messages and previous alerts so that the representative has the information available when they answer the call. We are enhancing the system to automatically extract and save information from our communications screens that can be used to serve for future verification. We are analysing why people call to a very granular level, and we will soon use this data for predictive hold messages that will actually reduce the number of phone calls that we take.

‘One-and-done’ is an important metric when we measure the quality of service. Most depend on the judgement of the agent to signal ‘one-and-done’ service, but we will use contact history to analyse our repeat phone calls to objectively determine if, in fact, the service issue was truly resolved. Another service twist that we are incorporating into our history is the ability of our agent to temporarily elevate a client’s future priority. This will help atone for a service disappointment and help rebuild the client’s confidence by providing enhanced services for future calls. Finally, with ring alert as part of contact history, we can schedule not only the date but also the time for returning a call that is most convenient to our client. At present, contact history only includes telephone calls, but we are in the processing of enhancing it for all other forms of contact, including mail and email.

c. Predictive hold messages

Although we know at a fairly high level why people are calling today, until contact history, this information was not granular enough to be used to proactively alter our service behaviour. As we begin to understand exactly why people call, we can leverage this information to provide them with the likely answers before the call is answered by a live message. For example, if we know that 35% of our term assurance calls are to find out either if the last premium payment was made or when the next premium payment is due, then we can replace the hold music with a message that says something like, “While you are waiting, we would like to inform you that your last premium payment of $123 was received on October 22, and your next payment of $135 is due on November 12.” This message will only be played if our operators are busy and we force the call to be put on hold. We will use this type of knowledge for all products where we can establish call relationships.

This message can be tailored dependent on how busy our representatives are. The busier we are, the longer the wait time, thus allowing for a more complete message. The more complete the message, the higher the probability that the question will be answered without the need of an operator's assistance. The ability to provide customised hold messages by individual policy will greatly assist our handling of special circumstances, like those that exist today for our policyholders in the Gulf Coast, whose policies have been suspended for billing and other activity. We believe that by providing probable answers in advance of taking the call, we will lower our costs and improve our service.

3. Execution of Efficiencies

a. Key what you see

"Key what you see" is software that we believe is unique to JNL. When fully implemented, it will greatly improve productivity, reduce costs, and improve service. In the old days, keypunchers keyed and verified data into keypunch cards at an incredible rate of speed – literally tens of thousands of strokes per hour. They keyed much faster than our current terminal operators do today. However, it was inefficient because knowledge workers were typically required to transcribe data from forms onto keypunch sheets prior to them being coded and entered into the computer. With the advent of online systems, it was quicker and more efficient for the knowledge workers to key directly into the terminal rather than code to data sheets, and subsequently have them keypunched. After processing, the data was usually verified on site for accuracy. This also had its disadvantages. It required expensive knowledge workers to spend their time searching through forms to find the data, translate it, and enter it; furthermore, site verification, particularly for items like name and address, is notoriously error-prone.

With "key what you see," we have, in essence, combined the two methods. We are again using keypunchers to input and verify data directly from forms, which are then scanned. The data to be keyed is extracted from the image and displayed, and our operators then key exactly what they see. This is much faster because, like in the old days, it is a purely mechanical process and the keyers are highly specialised. There is no mental pausing to digest, correct or translate the information. The data is then routed to a rules engine that translates the captured information, analyses it for completeness and accuracy, and, if clean, it automatically sends a transaction to our back-end systems to process without manual intervention.

The benefit of key what you see is that data is captured at a very economical cost, and it gets to our systems quicker than before. Our expensive knowledge workers only have to focus on work that truly requires their judgement for processing, and the quality of our service has significantly improved because key verify is much more accurate than site verification. This technology is already operational in much of our new business area, and we are implementing it for all of our processes.

b. Policy assembly software

JNL has thousands of plans, each of which is unique. The size and many variations of benefits and features normally associated with new products are exacerbated because of the many state variations that might alter a policy's provisions. The result is that there are literally hundreds of thousands of possible combinations for assembling a policy. Added to this, to produce a policy, a photocopy of the application is required to be inserted, and frequently a separate illustration is required to be run on our PC system and included. Endorsements must be typed for all changes to the policy that have occurred during the issue process, and unique policy pages from literally hundreds of thousands of combinations have to be selected, merged with manually produced documents, and assembled in the proper order.

As you can see, policy assembly in the United States is a very arduous and time-consuming process. In fact, at one time we had 23 people at JNL whose sole responsibility was to assemble policies. These did not include those who were keeping track of and typing endorsements, running illustrations and photocopying applications. At the time we had these 23 assemblers, our products were much fewer and simpler than they are today. We did not have VA, universal life (UL) or variable universal life. We estimate that if we were manually assembling policies today, we would need 83 full-time people, but because of the software, we only have two. Policy assembly is a very intricate technological feat that currently marries an assortment of technologies to automatically select, sequence and print all of the documents required in a policy. I cannot say definitively that no one else has solved this problem. However, at industry conferences we go to, we have yet to meet a single person who did not tell us that we were well ahead of our competitors in this area.

c. Skill-based routing

Skill-based routing is another technology that many have, but we believe that our use of it is unique. As with other companies, our service representatives are certified in the skills necessary to perform a service, and our work with the telephones or paper are routed based on these skills. The benefits of skill-based routing are obvious: it gets work to the people with the knowledge to process it, and it is a prerequisite for good service and high productivity. Not so obvious, however, is that skill-based routing, if cleverly used, greatly facilitates the hiring process and reduces the impact of turnover because, by forecasting turnover, volume, and the skills to be available, we can also forecast skillset shortages resulting from turnover.

This forecast of skillset shortages allows us to pre-train our employees in these skills in advance of them being needed. We do this at every level so that when we have turnover, we have a bubble-up approach where a pre-trained skill shifts, or bubbles up, to fill the void above it. The shifting up of skills is repeated at the next lower level to replace the skills of the previous bubble-upper. The ultimate result of this progressive process is that all higher-level skills are immediately filled by knowledgeable representatives, and the hole that is eventually left is at the lowest skillset level. Filling the lowest skillset is obviously the easiest and most economical alternative. The net effect of this entire process is that there is little, if any, disruption caused by turnover. Finally, our ability to absorb rapid growth is greatly enhanced by this process because we grow staff at the lowest skillset level and are required to hire a minimal number of highly skilled and consequently expensive new associates.

d. Training

Staffing and training is inextricably linked to our bubble-up philosophy and is a prerequisite for success. Our training department models all of our work processes. They then design training modules that are specific to these models, and they train or pre-train our associates to be ready for their next assignment. As mentioned earlier, our bubble-up process allows our training department to get new associates on the floor quicker than ever before and our bubble-up accumulation of skills at the associate level enables them to fulfil their career objectives.

In IT, we also have our own seven-month training programme where we train entry-level staff to become programmers. An interesting detail about this programme is that we typically do not recruit computer science majors. We look for people who have good business knowledge and view technology as a means to enhance our business capability. Although we are highly technical, we do not view our IT shop as a technology centre, but as a business centre that provides technical solutions. This is a subtle but key difference in explaining why we are more productive and efficient than our peers. Training new associates and our approach to technology have been very successful. In fact, graduates of our training programme are overly represented in our top quartile, even though they have less average tenure than the experienced programmers we hire from the outside.

III. Life of Georgia: Bringing It All Together

What does all of this really mean? I think Life of Georgia is a perfect illustration of how all of the above, and many other innovations, have come together. Because of the abilities of our IT and operations group, our success to date has been extraordinary. The Life of Georgia acquisition included in excess of 1.5 million policies. We closed at the end of May, and in only five months we have converted to our systems over 1,300,000 policies without a single significant service incident. Even though the conversion turned out to be much more complicated than we had anticipated – in fact, we have coded and tested over 800 [inaudible] to support this conversion – we still remain on schedule to complete the conversion by year end, and substantially within budget.

However, speed of conversion is not our only achievement. Equally as impressive and revealing are the metrics regarding our ability to economically absorb this block. Prior to Life of Georgia, we had 673 associates in our operating department, and that is the sum of those numbers. After the Life of Georgia aquisition, we will have 722. What this means is that we will be able to support the entire Life of Georgia block by adding only 49 new associates to our operations department; another telling metric is that we will only need to add eight associates to our IT department. Between operations and IT, we have therefore added 57 employees to handle this whole block. Because of our skill-based routing and bubble-up process of bringing new people to staff, we were able to quickly and economically recruit and train the 49 associates required to handle this increased volume. Our ability to absorb Life of Georgia as quickly and as economically as we have been able is not by accident, but is the culmination of the innovation that we have been building into JNL for 10 years.

IV. Conclusion

We have been able to achieve the Holy Grail that many companies have been striving for, but which few have succeeded in attaining: namely, great customer service at a very low cost. We not only have excellent service, a highly scalable and agile IT system, and very innovative service processes, but we have succeeded in accomplishing all of this and remain the most cost efficient company among our peers.

I hope that from my presentation today I have shown that within operations and IT, we too embrace the traits that are the hallmark of JNL. With our innovative processes, our extremely cost-effective and world-class service, and our IT platforms that are extraordinarily flexible and scalable, I believe that we have demonstrated that we also subscribe to the model of expertise, execution and innovation that makes Jackson National such a great organisation.

Financial Overview

Andy Hopping

EVP, Chief Financial Officer and Treasurer, JNL

I. Agenda

Good afternoon, everybody. I think this is the area that financial analysts are most interested in. We will spend quite a bit of time talking about finance, accounting, economics, investing, hedging and asset/liability management. I would like to start at a high level, talking about how we see the market and the evolution of financial reporting in the US. I will give you some background on how we got to where we are and where we see that going. Hopefully my presentation will give you some context around how we see Jackson's performance and the economics of the market going forward.

I will then spend some time looking at the economics of both fixed and variable annuity (VA) products and give you more information on exactly how we do pricing in that area. I will talk a bit about capital as well. I got a lot of questions about capital at the reception last night, so we will spend some more time talking about that. I will also cover our industry-leading expense advantage and how we maintain and leverage that advantage. My colleagues will then drill down a bit further into the financial results and our risk management approach. At the end of the three presentations, we will be happy to take your questions.

II. Financial Reporting

1. Overview

As you are aware, despite the well-intentioned efforts of rule-makers, regulators and practitioners, financial reporting continues to get more complicated and more difficult. That is despite the fact that everyone is trying to make it simpler, more consistent and more transparent. Since all of you are well-equipped to offer constructive criticism on your own, I thought I would spend some time talking about what we see as the best and most useful of those various methods. I will also spend some time talking about how we got to where we are in the US, particularly from a GAAP perspective.

2. Background

How did we get to where we are today? As a young accounting major a few years back – or perhaps more than a few years back – we were expected to learn a lot of rules. At that time, there were some major elements in GAAP accounting that were emphasized over rules: matching, conservatism and consistency, plus a preoccupation with historical cost accounting. These key principles were the foundation for the judgment and the theory that professionals were expected to exercise in public accounting and later in roles as controllers and chief financial officers of major companies. Much of this judgment has now been replaced with hundreds of thousands of pages of rules attempting to codify good theory and good judgment. Our collective destiny appears to be more rules and evermore complicated financial reporting methods.

3. Market Value

As you know, historical cost accounting was once pretty sacred, but we are clearly moving toward more market value. The only problem with market value is that when you look at a balance sheet, some of the elements are quite easy to value and others are quite difficult. The other problem we have is that when you think about these elements and marking them to market, we have a geography problem as well in that some of the elements are marked to an income statement, others are marked to the equity section and some are not marked at all.

Despite this complexity, I think you will continue to see more market value. One of the trade-offs is that you will see more volatility in income statements, particularly in Jackson where we have a large hedge book and we have not attempted to match up the accounting at the expense of how we do the economic hedging. With the growing complexity of our products and our myriad reporting methods, to really feel like an expert in insurance accounting today you need to be more expert than ever in a variety of disciplines. That would include accounting, finance, statistics and the actuarial sciences. At Jackson we work more closely together than we ever have and I suspect that will be the future for us.

4. Key Questions

In the end, when you step back from all this well-intentioned complexity you are really just trying to answer a couple of simple questions. Is a company's absolute performance better, worse or about the same? Is their relative performance, relative to their competitors, better, worse or about the same? From there, we all attempt to predict the future. I am sure there are plenty of opinions in this room on the future.

III. Profit Signatures of Annuity Contracts

Let us turn to the profit signatures of annuity contracts. This is an example of a fixed annuity (FA) contract. For some of you this will be pretty basic, but I will go over it quickly. In this example, under statutory accounting we expensed the upfront commission and have negative distributable earnings. On the other hand, under EEV or achieved profits, we have upfront recognition of the profit over the life of the contract. EEV is clearly a much more aggressive accounting method, with the statutory method being the most conservative. Down the middle, the GAAP line is the red line. By design, the GAAP accounting is a well-matched model of revenues and expenses over the life of the contract. The whole idea of GAAP accounting is to show nice, steady margins over the life, not changing those unless you clearly need to.

Under statutory accounting, you get capital strain and negative distributable income in the beginning. You get substantial upfront gains under EEV and nice, steady operating profit under GAAP. One thing I do want to emphasize, particularly for European analysts, is the value of statutory accounting. There has been a lot of interest in capital and in cash. Statutory accounting is all about capital and cash. For the most part, it is a cash-based accounting system. Later today we will show how, under different accounting methods, everything ultimately converges around cash. Statutory accounting probably does the best job of showing the upfront capital that is required, as well as the capital required to back the products after the acquisition costs have been expensed.

On the other hand, you see a lot of interest in the US today in achieved profits and EEV-type accounting. When I meet with the CFO peer group that I am part of in the insurance industry, a lot of the industry is looking at ways of adding those metrics – even though they do not need to, from a European parent standpoint. They see it as a better way of getting at the value that is being created in the business and they like it as a method to tie compensation to value-added, rather than simply looking at GAAP measure, which are pretty smooth and do not necessarily get at the value that is being added each year and cash flows out into the future on a risk-adjusted basis.

IV. Accounting Methods

As I mentioned, there has been a lot of criticism of the complexity in accounting. Certainly over the last couple of years our financial group has worked really hard to transition from MSB to IFRS and AP to EEV. We deal with a number of methods, particularly because of the transition, and certainly there is a lot of work involved. No one relishes the work that is required to report under all those methods and to do all the planning, but there are some key benefits from the methods. In fact, I would argue that the difference in the methods is where the benefit comes. If you can understand insurance accounting by looking at statutory accounting, GAAP accounting and achieved profits accounting and take the best elements of all those methods, you really get a complete view of how an insurance company is performing. If you just look at one or two of them, I do not know that you would necessarily get that. That is why I would recommend that you spend more time looking at the blue books and the statutory accounting.

We also see that statutory reporting is clearly the basis for insurance acquisitions in the US. We like to look at Jackson National as an acquirer would, with that emphasis on cash flows and the ability to look at the sustainable profitability of the business. Again, statutory underlies most of the acquisition accounting. It is clearly good discipline in terms of looking at cash flows, as well as looking at the capital that is held in an insurance company.

As I mentioned, GAAP and IFRS both do a good job of presenting the long-term earnings power of a company and good comparability across the industry on a US basis. EEV does the best job of looking at the value that is being added. It is also a good basis for looking at the overall value of an organization, assuming you add other elements of market value, in terms of distribution, to the base embedded value. We will say a bit more about EEV later today, as well as our first public disclosures of some of the sensitivities we have worked up recently under EEV. The Pru will be reporting in December of this year on a worldwide basis.

I want to reiterate that out of all these methods, we feel that US statutory reporting is clearly one of the most valuable due to its emphasis on cash flows and the conservative nature of the accounting, but it is one of the least used, particularly by the analyst community.

V. Variable Annuity Contracts

This slide shows our two main annuity contracts. I will start with the VA contract. This is our base contract, without some of the guaranteed but it does include the basic return-of-premium death benefit. If you look at our fee structure and what we earn on a VA contract today, most of the fee comes from the mortality and expense component, which is 125 basis points. We then take our share of the fund management fees, which is about 45 basis points, and a little bit from policy administration. We end up with 172 basis points, on a gross basis, in terms of the fee revenue.

If you look at the acquisition costs – this is a B-share type of contract, which has the largest upfront commission – a 7.5% upfront commission plus our internal marketing costs run at around 185 basis points per year. Our issue costs are around 19 basis points. Under GAAP accounting we defer all that as deferred acquisition cost and then amortize that over eight years, which is based on a seven-year surrender charge plus one year in addition. That gives you 119 basis points of annual cost on a GAAP basis, in terms of amortization. Our admin costs are about 13 basis points. In this example, we are assuming an $80,000 average contract size on a VA. We then have our expected mean cost of return-of-premium of about five basis points. If you take all those costs into consideration on an amortized basis, you end up with a profit margin on a base VA contract of about 35 basis points.

We are using a point and a half of capital here, which is fairly conservative. That gives you a ratio, before tax and before the return on the money held as capital to back the product, of 23.3%. Then we add back 5.5%, which is about what we can earn on bonds today, and tax effect that at a federal rate of about 35% in the US.

Returns approach 19% in this example. This clearly supports why we like the VA contract in the US. It has excellent margins, very low capital requirement and very good return on capital. The other benefit to Jackson, being a large FA book, is the diversification benefits that we mentioned earlier, in terms of the growing fee-based business as further diversification of the fixed business.

VI. Fixed Annuity (FA) Contracts

Let us turn to a FA contract. In this example, we start with a gross yield on a bond portfolio; assuming this is a largely fixed income, investment-grade portfolio of 5.6%. In this case, we have factored in the average long-term cost of default as well as our investment expenses through PPMA. It gives you a net yield of around 5.25%. In this example the customer gets a crediting rate of 3.5%, which gets us to our current target spread of 175 basis points or better.

There is a slight difference in the acquisition costs as compared to the VA contract. The commission in this example is slightly lower at 6% upfront; marketing costs are the same at 185 basis points; and the issue costs are about 19 basis points. The acquisition costs are slightly lower than in a VA contract. The amortization period is slightly longer at 10 years, which is based on nine years for surrender charge plus one year. That is 80 basis points a year, with similar admin costs. The average size of a FA sold today is about $55,000 for Jackson National, so the average size is slightly smaller in terms of upfront premium.

Deducting those costs we get a profit margin of 81 basis points. As I mentioned, the capital requirements on an FA are obviously much higher than they are on a VA. In this case we are using 6.5%, which gives a ratio of 12.5%. The investment return on the capital is similar and there is a similar tax rate at 35%. You end up with an after-tax return on an FA of nearly 12%. This is fairly consistent with where we are pricing today.

VII. Resettable Annuities

The other thing I would point out is that the product we are selling today, not unlike what we have sold historically, is an annually resettable annuity. Where there are concerns about interest rates falling or low interest rates, this is based on a 2% guarantee and we are starting out at 3.5%. The other thing to note is that if you think about an FA in terms of a cost of funds, in terms of a liability, then take the 3.5% and add the amortized costs per year of 94 basis points, the 80 plus the 14, and you can see that our all-in cost of the liability is about the cost of a five-year Treasury Bond at 4.44%.

We can clearly make good returns at that rate, though in the FA business, for us, we need to see higher interest rates in the US and higher spreads available on bonds to make it as attractive as it once was for issuers. Even though these are good returns at 12%, the customers still do not see 3.5% as all that attractive. You see more VA interest, as well as indexed annuity interest, to can get slightly higher upside returns. Frankly, they do not expect to earn much less than 3.5% with an indexed annuity. These products are not quite as popular as they once were, but we continue to sell them and we continue to believe they will have their day, as they have had in the past. We want to be well-positioned to sell whatever is popular at any given time and returns are still good at 12%.

VIII. Capital Considerations

As I mentioned, I received a number of questions last night on capital. In broad terms, if you think about how Jackson looks at capital, there is clearly a whole range of capital. We have multiple accounting methods and even more ways of looking at capital, from the lowest regulatory levels of capital all the way up to our actual levels of capital and different levels of capital depending on the accounting method. There are clearly a lot of ways of looking at the numerator and the denominator and trying to gauge performance. For us, if you boil it down, the lowest level of capital that we take into consideration would be how Prudential looks at capital under their Financial Conglomerates Directive-type of capital. That would be the lowest and frankly the least relevant for us, given how much capital we are carrying and how well we are doing, but it is one benchmark that we follow.

For JNL, however, the work we have done recently on economic capital would be what we consider our best thinking on the capital that is really needed on a risk-adjusted basis for the business today. That number is obviously higher than the S&P-type level but substantially lower than rating agency capital or the actual capital that we carry.

From a pricing discipline standpoint, I went over the pricing on the FAs and variable annuities (VAs). We continue to use what we consider AA rating agency capital levels, because that is what the market expects us to carry to be AA. Our pricing discipline is based on that higher capital level. Our actual capital levels are even higher; most of that piling up in the last couple of years with very high earnings and much higher sales of VAs and less capital-intensive product.

For internal purposes, we look at our IFRS results and our EEV results relative to those economic capital levels. We consider that to be the best way of looking at the business, just from a pure economic standpoint without regard for the different accounting methods and some of the comparability. Frankly, we look at all these measures and we do all the accounting methods each month.

JNL is well-capitalized. We are clearly over-capitalized against all benchmarks. We are also returning significant cash to the Group through higher repatriation levels. We anticipate raising that level to $150 million this year. As we continue prosper, I think the expectation is that level would be raised in the future.

The other thing to keep in mind when you look at the capital levels is that they clearly demonstrate the realization of our pricing discipline over time and support our ability to grow rapidly, as well as to finance internally modest bolt-on acquisitions.

IX. Excess Capital

If you think about how an insurance company has to prosper over time, some of you might ask: why do you not sell any product you can that is over the bond return, if you have excess capital? These are long-term products and we are not interested in putting product out there to earn 7-8% chasing sales, just to have the sales or slightly higher short-term returns. We want to get really strong long-term returns in the 13-14% range, given the length of the product. We are not willing to sacrifice our pricing discipline or chase share just because we are sitting on a little extra capital at the moment.

As of year-end 2004, we estimate that we have in excess of $1.5 billion of capital relative to the economic capital of $1.9 billion. More recently, as at June 30 of this year, we estimate $800 million of excess capital relative to our AA ratings standard. If you do the math on $800 million excess capital, you can see that even at a fairly conservative capital level of 7.5% that would support an additional $10 billion of general account assets today and, on a VA basis, $50 billion of VA assets. There is a lot of capacity in the $800 million and we will do our best to put that money to work. Cliff is going to sell a lot of VAs. We have a running joke about how he is going to redeploy that $800 million in the VA business. He is running about as fast as he can.

The other thing to keep in mind is that our capital levels have continued to improve. Earnings have been strong and we are still mostly selling VA product.

X. Use of Capital

Questions we have been receiving sometimes confuse capital with cash flow. They are highly related on a statutory basis, but they are not exactly the same thing. This chart shows capital formation, using 2004 as an example, so it includes a dividend. It shows that on a statutory basis, where cash is king, we had net income of $625 million in 2004. A lot of capital was being generated just on a statutory basis. Capital was also freed up from runoff of business, which is a different way of looking at capital. It is not generating capital so much as it is freeing up capital that is already there to be redeployed in other ways. In this case, nearly $2 billion in 2004 of capital was either being generated or freed up to reinvest in the business.

The chart also shows how we used that capital. Most of our capital goes back into new product writings: upfront commissions, acquisition costs and so on. Most of that money goes to the things we showed earlier in terms of upfront acquisition costs. The other side of acquisition costs is the capital you need to carry just to back the growth in the balance sheet. Even if you do not sell anything, you have compounding of earnings – hopefully the stock market is growing – and you have compounding on FAs. You still have to carry capital to back those assets. This chart shows how much of that is being freed up on an estimated basis. You have to sell a lot; we obviously have a lot of capacity to grow organically. In recent years we have had the capacity to do acquisitions, as we did with Life of Georgia.

There is one other point I want to make. People have asked: why do you carry the excess capital? We look at it from a Jackson standpoint; on a stand-alone basis it is excess capital. At a Pru level it is clearly not excess capital. Capital needs to be managed on a consolidated basis and the decision as to whether capital is pulled or invested is more of a Group decision.

XI. Managing Expenses

Now let me turn to one of my favorite topics: expenses. You have heard a lot about our expense ratios and leading expense advantages. I joined JNL in 1994, 11 years ago, and there was no question that Jackson was a low-cost company. The problem with the company at that time was not that it was not low-cost; it was clearly that they were under-investing in both people and technology. Back then, everything was a function of “need to have” or “nice to have”; the company really was not spending enough money to grow the business and be competitive. It was just cheap more than it was efficient.

As George Napoles mentioned earlier, we made a conscious decision to focus on industry-leading service and turning IT into a competitive advantage rather than a necessary evil. At the time, the company looked at IT as something they outsourced; they did not want to spend a lot of money on it and there was no way that IT was going to be a competitive advantage. It took a long time to build up what George has today in terms of that level of expertise to be innovative and faster than everybody else. You need to have your own people; otherwise, you are destined to be average or worse than average.

Fortunately for us, we have proven that doing things right the first time and investing for the long term is entirely consistent with expense discipline and efficiency. Our platform has made it easier to add new business at a low marginal cost and adding blocks of business, in bulk, at even lower marginal cost. We have done a good job of building what we have without spending too much money. I think we have done a good job of avoiding spending time and resources on projects and initiatives that would not have added value.

XII. Focus on Efficiency

As anybody here will tell you, I love to find ways to improve our efficiency. You cannot cut your way to greatness. We are pretty good where we are today. It will be harder to get better, but I am committed and I believe we will continue to do better. It just gets tougher, the better you get. Obviously the growth helps an awful lot, as you can add business at low marginal cost.

Our philosophy continues to be one of focus and discipline, coupled with a culture of continuous improvement and a near-obsession with measurement. We have lots of measurement and people really manage to it. As I say to people in budget meetings, I do not find it impressive that we got the work done right; what I am looking for is how we are improving the business now and for the future. We really do have a culture of continuous improvement and people embrace that.

This chart shows that we are number one in terms of expense ratios. There was a question earlier about how some of the bigger companies look. This chart is sorted by expense ratio; it shows us at the top at 43 basis points and where the other companies are. There are obviously some differences in the mix of business, but on any measure we are very competitive in terms of costs.

XIII. Industry Consolidation

I have a couple of points to make on this chart. Firstly, bigger is not necessarily better. Secondly, the companies that have grown through acquisition have not demonstrated a great deal of efficiency out of those acquisitions. I think they will start to do that over time, but integrating businesses is not the fun part. The fun part is buying the company and announcing the transaction. I think we have the kind of people in our organization that will do the hard, dirty work of systems integration, conversion, selling off the real estate – all that integrating. That is what you really have to do to make these things valuable and we are committed to doing that going forward.

Clark mentioned this morning the proposed Lincoln National/Jefferson Pilot merger, both of whom are on this chart. Their public announcement was that they hoped to take $180 million out of their expense levels on a combined basis. That is a pretty good effort, but I would point out that if they achieve that it will only move them up to second quartile on this chart. They will still be running at approximately twice our level of expenses. It is some improvement, but again that is a pretty good margin and one we do not take for granted. We continue to work on improving our expense ratio year in, year out.

XIV. Summary

In closing, I hope you found it useful to get at a high-level perspective of how we look at our various reporting methods and the economics of the annuity business today. I spent quite a bit of time talking about the details of the annuity contract. I hope that is helpful. In looking at how the products are priced, you can get a feel for why we think our ongoing internal rate of return is more in the 13-14% range on a blended basis. As you have seen, our capital position is very strong. We can clearly support a lot of organic growth. We can also support a pretty good level of external growth through acquisitions and things. We also have a great expense advantage and I believe we can continue to improve on that measure.

We look forward to your questions at the end of these financial presentations. Next, I would like to welcome my colleague, Jim Binder, who is Vice President of Finance and Strategic Planning. Thank you.

JNL Accounting Metrics

Jim Binder

VP, Finance and Corporate Strategy, JNL

I. Agenda

Good afternoon and welcome to Chicago. Thank you for taking the time to learn about Jackson. During this session I will quickly review the half-year results, which I am sure you are familiar with, discuss the EEV risk discount rate as it applies to Jackson National, and provide a number of EEV sensitivities as it relates to the value of the in-force for North American operations.

II. Half-Year Results

1. Overview

Our financial results have been excellent. As you will see, they are among the best in the industry. I will begin with the IFRS results for the first half of the year. I assume you have all seen these, so I just want to drill down on a couple of items. We are quite happy with the IFRS results, where we recorded a 12% year-on-year increase in operating profits. This solid performance is driven by improvements in VA fee income, excellent FA spread income, good credit experience and outstanding expense control.

2. Operating Income

As you know, under the old modified statutory basis of accounting investment gains and losses were smoothed into operating income over a five-year period. I want to take a moment to review the methodology for including gains and losses in operating income under the IFRS methodology. With effect from January 1, 2005, operating income now includes a default provision equal to 100% of the long-term expected bond losses. For H1 2005, this was a $46 million charge against operating income. Also included in operating income is the amortization of interest-related gains or losses arising from the sale of corporate bonds held as investments. For H1, this was a $42 million positive adjustment. Finally, limited partnership (LP) and equity returns are normalized at a long-term rate equal to Treasury plus 400 basis points. During the first half of 2005, $27 million of private equity earnings were included in operating income. These three items – the gains, amortization and LP returns – are subsequently adjusted to actual below operating income in short-term fluctuations. Also included in the short-term fluctuation are consolidation of investment entities and the derivatives marked to market.

3. Net Flows

On this slide, I simply want to highlight the powerful impact of VA net flows on earnings. As you have heard throughout the morning, our net flows have been outstanding. JNL has consistently recorded positive net flows in 2001, 2002, 2003, 2004 and in 2005. These strong net flows allow JNL to retain top-tier VA sub-advisors and to have pricing advantage over those sub-advisors. JNL has the fastest-growing organic VA platform. This allows JNL to negotiate industry-best pricing. In fact, not a single insurer in the US has better pricing with the sub-advisors that underlie the JNL VA products.

Further, and more to the bottom line, the impact of consistent positive net flows drops to the bottom line as fees are earned on an ever-growing separate account balance. This comes through JNL numbers in VA fee income, which is up 41% year-on-year for H1 2005. This is a continuing trend, as VA fee income in H1 2005 is equal to 250% of VA income in H1 2003. JNL continues to post strong, positive VA net flows.

4. Achieved Profits

Achieved profits results were also very strong, with new business profits up 28% year-on-year. Pre-tax operating income from continuing operations are up 29% year-on-year, even after excluding the term life insurance premium increase that was brought through as a non-economic assumption change during the first half of the year.

5. Spread Income

On the following two slides I want to discuss two items that positively impacted H1 operating results: the spread variance and the non-economic assumption change that I just noted. A positive $82 million spread variance is the main contributor to the $84 million experience variance. JNL has the ability to manage interest rates that we credit to policyholders, so we are confident that the spread targets remain achievable. The investment portfolio is earning 5.86% and we are crediting an average of 3.94% to policyholders. The result is an annualized operating spread of approximately 192 basis points. While we are crediting 3.94% to policyholders, the June 30 minimum guarantee on our contracts is 3.29%. This leaves over 60 basis points of cushion against our minimum guarantee to policyholders. Further, as JNL issues more fixed business with a 2% minimum guarantee rather than the 3% minimum guarantee in place for most 2003 in-force business, the average minimum guarantee rate will drop further, providing additional cushion. Note that on this slide we have normalized at 8% the LP earnings included in the investment yield calculation. Actual annualized LP income for H1 2005 was approximately 24% of the book value. To summarize, JNL's spread income is trending well and because of the resettable nature of our general account liabilities, our spread targets remain achievable.

6. Non-Economic Assumption Change

JNL brought through a non-economic assumption change in H1 2005 to reflect increased renewal premiums of two blocks of older-term life insurance. These premium increases were driven by poor expected future mortality experience. The increases are contractually allowed and are subject to guaranteed maximum levels. The change results in annual renewal premiums on the affected policies increasing from $75 million to approximately $125 million. The impact of this is a $263 million non-economic assumption change as the present value of the change is brought through earnings.

Best estimates of persistency and mortality were given due consideration when calculating the change. This assumption change brings the blocks of business to a break-even position.

III. European Embedded Value (EEV)

1. Underlying Assumptions

Over the next couple of slides I will discuss the EEV risk discount rate applicable to JNL and a number of EEV sensitivities. Before delving in, I want to cover some of the underlying assumptions that are key to putting these numbers into perspective.

Prudential uses a bottom-up approach when setting risk discount rates to reflect the characteristics of the individual business units and their respective regions, and to reflect the characteristics of various product cash flows. A risk margin is included in the risk discount rate to reflect the risk associated with the emergence of distributable earnings that are not provided for elsewhere.

Consistent with the majority of reporting companies to date, the calculation is not a market-consistent approach. Cost of capital is determined using AA-calibrated economic capital as a basis. The intrinsic cost of options and guarantees is included in the present value of in-force business on a deterministic basis. Stochastic modeling is performed to reflect a wide range of negative and positive scenarios such as tail events are adequately considered. The difference between the stochastic result and the intrinsic cost is included in embedded value as the cost of options and guarantees.

Credit defaults are specifically accounted for when determining cash flows that are being discounted. We start with a gross spread that is approximately 200 basis points. From this we subtract a weighted average default provision that is currently around 25 basis points. It is the net result of approximately 175 basis points that is discounted back. It is worth noting that the default provision used under EEV is absolutely in line with the default charge that we use in the economic capital model, which is determined using a stochastic model. Finally, increases in interest rates used in the modeling approximate the forward curve.

2. Risk Discount Rate

a. Overview

Let us look at the discount rates. On June 2, Prudential disclosed an aggregate risk discount rate of 5.8% for the Jackson National in-force block of business as of December 31, 2004. Underlying this were two separate discount rates. One rate is for the VA book, which has a good deal of exposure to equities. The other is for general account product cash flows, which have virtually no equity exposure. The aggregate rate is weighted based on the respective value of the in-force business.

b. Variable annuities

First, let us look at the calculation for VAs. We start with a risk-free rate of 4.26%, which is based on an annualized 10-year US Treasury rate. We add to that a 300 basis point equity risk premium that has been multiplied by beta, with beta representing the sensitivity of cash flows to movements in the equity markets. Beta is calculated based on an analysis of the impact on cash flows of a marginal change in equity. The resulting beta for the VA in-force block is 0.83, which, when multiplied against the 300 basis point equity risk premium, adds 250 basis points to the annuity discount rate calculation. Note that the beta calculation relates to total product cash flows, meaning it includes all VA cash flows; both separate account and general account. If the general account cash flows were excluded, the beta would be higher than 0.83.

Moving on, an additional Prudential margin of 50 basis points is added. Finally, the calculation is rounded to the nearest 10 basis points, resulting in a 7.3% risk discount rate for VAs.

c. General account

On the general account product side, we start with the same risk-free rate. Remember that here we are only providing for risks that are not accounted for elsewhere. As mentioned earlier, we have already taken credit risk into account using a default provision based on the long-term cumulative default studies, which is validating using a stochastic credit model. There is no adjustment for credit risk in the discount rate because cash flows have already been reduced to reflect credit risk. We have also already taken into account the full cost of options and guarantees, which have been modeled on a stochastic basis and have been incorporated into the value of the in-force business as the cost of options and guarantees.

On the general account side, we do have a knock-on effect of interest rates being impacted slightly by changes in the equity market. That is captured in the equity risk premium on the general account side, with a low beta of 0.08 multiplied against the 300 basis point equity risk premium to add 24 basis points to the risk margin.

What remains is a stream of earnings stripped of guarantees, stripped of options, stripped of credit exposure and with very little remaining equity exposure. What you have left is pretty close to a risk-free set of cash flows. As with the VA risk discount rate, an additional 50 basis point Prudential margin is added. The result is a 5% discount rate for in-force general account products. Again, this results in a 5.8% risk discount rate the in-force block and an aggregate rate in the new business of 6.1%. The in-force is weighted on the value of in-force and the new business piece is weighted by new business sales. That is affected both by the sales level and the margins on the individual products.

3. Sensitivities

At December 31, 2004, JNL had an EEV of $4.9 billion. To put this into context, it is quite close to GAAP equity and close to the old PPMA embedded value. The numbers on this slide represent a number of EEV sensitivities, shown as an after-tax impact on the embedded value. Note that these are unaudited numbers. The key economic sensitivities presented here include the following. Firstly, it includes impact of an absolute 1% increase in the discount rate, which lowers embedded value by approximately $158 million. Of this, $127 million, or roughly 80%, relates to the general account. The remaining 20% relates to VA products. Secondly, it includes the impact of a 10% decrease in the market value of equities lowers embedded value by approximately $103 million. Thirdly, the impact of an absolute 1% increase in equity yields provides an approximate $46 million increase in embedded value. We have also laid out a number of sensitivities related to non-economic items including maintenance expenses, lapses, mortality and morbidity. While the numbers on this page are clearly meaningful, they are not material to JNL's overall embedded value of $4.9 billion.

IV. Capital Generation

As you have seen, JNL is generating capital at an impressive rate through a combination of strong earnings and robust sales of VAs, which consume little capital. In addition, we are repatriating capital to the Group at a level that is in line with the dividend payout ratios of the US companies with which we compete. This slide shows the GAAP returns on equity that result from the last four years of reported numbers. On this graph JNL has a 13.6% return, which is near the top of the range. Note that these are unadjusted public results.

While the companies shown on the slide average 21% gearing, JNL carries very little balance sheet debt because leverage is more efficiently carried at the Group level. Additionally, the denominator has not been adjusted for the excess capital that we are carrying on the balance sheet, as noted in Andy's remarks. We are not showing these adjustments here but we suggest and ask that you consider these elements when computing JNL's returns as part of your valuations. Still, JNL is well-above the 10.5% industry average.

V. Summary

In conclusion, US markets are strong and improving. Jackson National has strong and improving financial fundamentals. Our spread products are performing above target and we retain the ability to re-price a significant portion of our liabilities, if necessary, to continue meeting our spread targets. Our VA net flows are near the top of the industry and related fees that we earn on this business clearly drop through to enhanced bottom line results. Our expenses have been and continue to be well-managed. Finally, we have been generating above-market returns. We are able to do this because of the strong fundamentals noted above and by participating in profitable segments of the market. These attributes have served JNL well and we believe they position us well for the future.

At this point I will turn it over to Chad Myers, Senior Vice President of Asset/Liability Management, who will provide a risk update.

Economic and Investment Review

Chad Myers

SVP, Asset/Liability Management, JNL

I. Agenda

Good afternoon and welcome. I will give you a broad picture of our risk management process, including some background on our investment policy, as well as an overview of our approach to hedging and our current risk positions. PPMA will follow this with some more information on how they implement the policy I will discuss.

II. Liability Profile

To set the stage for this discussion, I would like to spend a few moments discussing our liability profile; how it is evolving over time; and how it compares to the US life industry. JNL's liability profile has changed significantly over the past decade, shifting from an almost exclusive focus on FAs and life insurance to a much broader and better diversified mix of business.

On this chart, the order of the product lines roughly follows the amount of embedded policyholder optionality. At the top we have annuities with book value surrender, where JNL provides a fixed rate of interest that is declared annually. The policyholder has access to the money at any time at a value equal to the premium plus the credited interest, less a fixed surrender charge that typically starts at 7-9%. If rates increase significantly the fixed surrender charge may not be enough of a disincentive to keep them from moving to a competing product with higher rates. In this case, JNL would face interest rate-related losses on the bonds backing the departing policy. In a declining rate environment JNL's ability to lower crediting rates helps to maintain spread, subject to a regulatory minimum rate that is currently set at 2%. Our focus on other product lines as resulted in this particular grouping more than halving as a proportion of liabilities over the last 10 years. It now represents about one-third of our book.

III. Product Lines

1. Market Value Adjustment

The next category is annuities with market value adjustment (MVA), which is similar to the first category but with one important difference: JNL retains the right to change crediting rates on an annual basis, but the presence of an MVA feature means the cash value of the policy more closely tracks that of our underlying investments. This also differs from much of what our competitors sell in the MVA space in that, typically, they do not retain the ability to change crediting rates annually. In other words, they have locked in the rate for the life of the policy.

2. Fixed Index Annuities

Next, fixed index annuities (FIAs) offer the customer the ability to participate in the upside of an equity index, while retaining a guarantee of their principal. Economically, this is the combination of a zero-coupon bond and a series of equity call options. The lack of a direct tie to current interest rates, coupled with the difficulty of comparison across competing products, makes these annuities less sensitive to movements in interest rates. As with regular fixed products, JNL retains the ability to adjust equity participation rates annually on the bulk of these sales.

3. Other Lines

The “other” line is primarily annuities in payout phase, which essentially looks like a fixed set of cash flows. The “life insurance” line contains both term and permanent life policies and is primarily mortality-based, with a modest exposure to interest rate risk. Importantly, the directionality of this interest rate risk is opposite to that of the annuity book and thus offers JNL a natural offset. This is in part why we have been keen to increase our footing in the life business over the past few years and why Life of Georgia was such a good fit for us.

Institutional products consist of funding agreements and MTNs sold to institutional customers such as pension funds, money managers and bond investors. When properly hedged, these products leave us with little or no interest rate risk. There is no optionality embedded in these products either. Finally, VAs do not expose JNL to interest rate risk, except through the rate sensitivity of options underlying the equity base guarantees. I will discuss this point in future detail later in my presentation.

IV. Product Mix

As this chart shows, the product mix has migrated down the page; ultimately meaning less risk to JNL and, in particular, less exposure to policyholder-driven rate optionality. The growth in our liabilities continues to be concentrated in the VA and FIA lines, which is keeping this trend intact. When compared to the industry, JNL has about twice the allocation to fixed rate annuities and about half the allocation to life and VAs. As annuities are more spread-intensive than life insurance, JNL has a higher-than-average focus on spread lending. As a result, we have implemented a strong process for this part of our business, with clearly defined risk parameters and prudent risk retention limits.

V. Investment Policy

1. Portfolio Methodology

This starts with our approach to strategic asset allocation and the development of our investment policy. There are a large number of potential portfolios we could use to back our spread-based liabilities but many of them would not be appropriate. We use simulation techniques to assess the fit of a variety of portfolios, subject to a number of constraints. The resulting portfolio must be able to generate sufficient spread above our AA-based funding costs. As such, you will not see government bonds, agency debt, AAA or AA bonds in our investment policy.

As rating agency and regulatory capital models are heavily skewed against riskier assets, our model portfolio becomes constrained by the efficient use of capital and limits the exposure to these types of assets. Liquidity plays an important part as well. Despite the desire to capitalize on illiquidity premiums available in the market, the liability mix allows for only a limited amount of these investments given our very conservative posture towards liquidity.

From the remaining portfolios, after consideration of these constraints, we choose one that meets the objectives and fits within our risk appetite. The result is a benchmark portfolio that clearly defines our risk tolerance and can be used to manage interest rate risk and credit risk to a neutral position.

2. Benefits

What are the benefits of the benchmark approach? While it is difficult to know where you are in the risk spectrum if you have not defined a neutral position, by doing so we can better evaluate investment decisions going forward. This allows us to gain some of the benefits of a total return framework; something that is often difficult to implement in an insurance company context. We have implemented what we call a ‘modified total return approach’, which adapts the framework by limiting turnover, asset allocation, trading gains and so on. This helps to preserve reported spread while still allowing for significant trading discretion.

The benefits of this approach include the ability to assess PPMA and the relative competencies, especially in the context of our chosen risk posture. By better representing the investable universe through a benchmarked index, our portfolio is more likely to look like a slice of the US economy and can scale upwards quite easily as we grow.

3. Limitations

Of course, there are some limitations to looking like a slice of the US economy. One is that you tend to allocate more to certain mega-type issuers than you would otherwise deem prudent. An example of this would be the US auto companies, which used to comprise a very large part of the unconstrained investment-grade index. Without modification, we would have held close to 2% of our neutral portfolio in General Motors alone. To avoid these types of situations we have capped large issuers within our indices and have put floors on smaller issuers, as the ability to source these bonds in the market is limited. To better match our liabilities we have also limited ourselves to the one- to 10-year maturity universe.

4. Policy Benchmarks

Up to this point I have essentially been talking about neutral policy benchmarks. PPMA has discretion – and in fact is encouraged – to allocate more or less of the portfolio to a given name. In order to control risk within this framework we have implemented what we call 'soft policy limits', which require investment committee approval to exceed. We also have hard limits that cannot be exceeded. The soft limits are: 80 basis points for issuers A and above; 60 basis points for BBB issuers; 25 basis points for BB issuers; and 10 basis points for B issuers. Hard limits are set at 1% for any investment-grade name; 50 basis points for any BB name; and 25 basis points for a B name. It is important to note that these limits do not just relate to purchases; they are dynamic over time. This leads us to automatically reduce positions as the credit becomes more risky and would leave us with very modest exposure before a default would occur.

At this point, there is only one credit above any soft policy limit and that is due to a recent merger. The position is currently being worked down. Again, this is something that would have the approval of the investment committee. The position is being worked down and should be back within soft policy limits by the end of the year.

The policy also contains asset class maximums. The purpose of these limits is to restrict the impact on capital of asset allocations through high-yield liquidity and commercial real estate and on interest rate risk through residential mortgage-backed securities.

5. Neutral Benchmark Portfolio

This graph shows the neutral benchmark portfolio. As you might expect, it is overwhelmingly fixed income-based with a large allocation to corporate bonds. Investment-grade corporate bonds make up 60%, with investment-grade non-corporate – in this case, meaning commercial mortgage-backed securities, asset-backed securities and residential mortgage-backed securities – making up an additional 15%.

Within the investment-grade component the benchmark is weighted 60% BBB and 40% A, compared to a roughly 50-50 split in the market between BBB and A issuers. Non-investment-grade corporates account for 8% of the neutral portfolio, with 70% weighted towards BB and 30% towards B, compared to a market weight of about 50-50. Commercial mortgages at 13% complete the fixed income portfolio, with an additional 4% targeted for equity investments.

There is a conscious choice to overweight BBB, as this portion of the credit spectrum gives PPMA ample room to outperform without taking on undue risk. Bs are very capital inefficient and often provide poor risk-adjusted returns, so they were underweighted in the policy. As mentioned earlier, JNL has a larger portion of its liabilities in spread-based business than the industry average. That number is approximately 20% of liabilities and accounts for JNL's roughly 14% overweight in BBBs relative to the industry. Other asset classes are broadly in line, with a close-to-industry weight in non-investment-grade and less in equity and real estate. As I mentioned, PPMA will address policy implementation in more detail a bit later.

VI. Product Risks

Returning to product-type risks, we talked about the product lines. We can look at the risks attached to the particular product lines. I will also talk a bit about the risks in the market that we are not particularly crazy about.

1. Interest Rate Risks

By far, the largest individual risk is the interest rate exposure associated with FAs. In the case of a rapid rise in interest rates, we would face higher surrenders with a bond portfolio that was under water. Because of the surrender charge protection in these contracts, it would take a reasonably large move in interest rates – typically 250-300 basis points – before we felt any major effects. The ability to adjust crediting rates annually provides us with significant flexibility over a wide range of rate shifts. In order to protect against the more severe moves, we have for a long time employed a swaption-based hedging program. Under this program we currently have around $40 billion notional of deep out-of-the-money payer swaptions, which protect our solvency and any upward interest rate shock. This is by far the largest of its kind in the US.

There is also some risk associated with a prolonged period of extremely low interest rates. This risk is limited to moderate spread compression on the annuity block and under no circumstances does it threaten solvency. As Jim noted, we currently have over 60 basis points of room between our current crediting rates and the minimum guarantees. This compares favorably with our competitors, many of whom have already reached their contractual minimums and are incurring some level of spread compression as we speak.

Additionally, with new sales going on at a 2% floor our average minimum rate is dropping roughly 10 basis points per year. In a low-rate scenario it would take several years for our portfolio to turn over enough to overcome our ability to lower crediting rates and to maintain our target spreads. With a weighted average life of about six years on the existing FA block, any eventual spread compression would ultimately be short-lived.

2. Fixed Index Annuities

The main risk related to FIAs is that of hedging the equity risk. This is something we have been doing for around nine and a half years and it is something we are quite comfortable with. I will go into more detail on our hedging of equity risk in a moment.

3. Variable Annuities

As mentioned this morning, there is stiff competition in the market for VA guarantees. Some competitors are willing to mis-price the VA guarantees to gain market share. I can assure you that we are not one of those companies. We take a very disciplined approach to determining which guarantees we will offer and under what terms.

An example of one we will not take is the guaranteed minimum accumulation benefit (GMAB), where the company guarantees the account value will not be lower than some floor, often the initial premium, at some future period of time – typically 10 years. This is simply the sale to the customer of a 10-year put option on actively managed funds inside a contract with a relatively high fee base dragging down performance. Those who offer GMABs do not price them at an adequate level to hedge the risk with Wall Street.

If we cannot receive fair compensation for a risk, we are not interested in taking it. All of our VA guarantees are priced to stand on their own and to provide a return on required capital. Because of our unbundled VA platform our pricing is very transparent; it is not subsidized by the base M&E fees, as is sometimes the case with our competitors.

We have similar issues with the risk in the guaranteed minimum income benefits (GMIBs). The problem here is determining the utilization of the customer's option to annuitise the contract in the future. Annuitization rates in the US are quite low; typically under 3% per year. In a case where a GMIB is deep in the money, it is difficult to predict what percentage will take the income stream. There is a lot of room between 3% and 100%. Since the industry tends to price at the lower end of this range, it is not a risk we wish to retain. However, in this case we have been able to find reinsurance at a cost commensurate with the fee we can charge and so we have been able to offer this benefit, but we do not keep the risk.

Guaranteed minimum death benefits and guaranteed minimum withdrawal benefits make up the whole of our VA guaranteed benefit exposure. These are risks with which we are comfortable, from a design perspective, and which offer sufficient fees to hedge to a conservative scenario.

4. Institutional Portfolio

Finally, the main issue to do with the institutional portfolio relates to the floating-rate nature of the liabilities and the fixed-rate nature of the assets that back the portfolio. This risk is hedged very tightly with a target duration mismatch of one-tenth of one year. Partial durations are matched tightly as well.

VII. Risk Hedging

1. Limits

I will now explain how we hedge these risks. As a life company we are in the business of taking on risk. The key is managing this risk to within acceptable levels. As it is often cost prohibitive and inefficient to pursue a perfect immunization strategy with respect to risk, our approach is to clearly define the limits and manage within them to maximize value. In doing this we gain the ability to more easily rebalance hedges when necessary and we retain the ability to profit from market dislocations.

An example of this would be when we were in the midst of the bear market, a few years back. Long-term volatility in the equity markets had spiked from the high-teens up into the mid-30s, which was clearly unsustainable in an economic context. We were able, within our risk limits, to replicate our equity index annuity options that we were selling to policyholders at 30-something and buy those back when the market return to long-term norms, at a profit.

We have an overall limit on equity exposure equal to 5% of the general account assets. 4% is the target and 5% is the overall limit. In measuring this limit we look at unaffiliated equity that is on the balance sheet, primarily the LP portfolio that was discussed earlier. We also consider the equity risk embedded in the liabilities that we originate. All embedded options are measured at their market value using a market-consistent approach.

We further define this limit using a 30% instantaneous drop in the market to capture the impact of the embedded options. Currently, in the case of a 30% drop in the market our equity exposure reaches the equivalent of about 2% of the general account, most representing our on-balance sheet equity investments through LPs. As I mentioned, this compares with a target of 4% in our investment policy. We are underweight equity at the moment.

Overall interest rate risk is managed within a tolerance of one year, although the portfolio is typically matched much tighter than that. The current duration gap is around one-quarter of a year. There are a number of other risk limits in place on both the interest rate and equity sides. I will not go through all of those here, but I will pick up on liquidity in a moment.

2. Tail Events

A bedrock of our risk philosophy is the need to hedge the tails of the distribution. We are quite comfortable using replication techniques, within our clearly defined limits. We utilize these to hedge movements in the body of the distribution. We use option-based strategies to manage the exposure to tail events. In the case of market shocks, replication strategies can break down due to things like discontinuous or gapping markets, lack of availability of hedging instruments or just the prohibitive cost of the replicating instruments. In these circumstances, companies are often forced to accept levels of risk they would otherwise not accept, simply due to the cost of hedging in that environment. By using option-based strategies our only exposure to these events is counterparty risk, which we manage very tightly – including requiring collateral from even the very highest-rated entities. For example, our maximum counterparty exposure to AA-rated counterparties would be $10 million. For lower-rated counterparties it would be even less.

3. Internal Hedging

Being one of the very few scale players in each of FAs, FIAs, institutional products and VAs puts us in a unique position from a hedging perspective. There are risks within each of these product lines that have offsets in another. We look to hedge these positions internally before going to the market. To accomplish this, we have set up an Internal Derivatives Desk (IDD) to act as a clearinghouse for risk. The IDD trades with individual product lines and aggregates the risk at a company level. The net position is then hedged externally to be within the constraints of our policy. By doing this we eliminate a significant amount of external trading, including several billion dollars of interest rate swaps and approximately half a billion dollars of equity options in our current books.

It is only very recently that consultants have started to publicly advocate the risk trade-off between VAs and FIAs, trying to move companies in this direction. I have yet to see any evidence of such a system being used at any other major insurer. In fact, we recently engaged a major US consulting firm to benchmark our ALM practices against those of our major competitors. We were cited as the only company with such a well-developed approach for internally offsetting risk. The one downside to this risk is that it is not accounting-friendly. In accounting for derivatives the accounting standards have taken a decidedly micro approach, looking for one-to-one risk offsets at a very low level of granularity. Although we implicitly do this through our IDD mechanism, it is the external macro-level hedge that is being scored by the accounting frameworks. We do show our external hedging to be highly effective in the same way and using the same metrics the accountants would use to define it; however, there is no provision in the rules for such a high-level approach. This results in only one side of the balance sheet being marked to market and distorts results. We have chosen to retain our business model and accept the accounting volatility rather than losing the efficient structure we have built and the cost savings that go with it.

4. Embedded Liability Options

This graph depicts our equity risk position due to embedded liability options as at September 30. To reiterate, 2% on-balance sheet LPs are not included in this. This is just exposure due to the embedded options. By selling an FIA we become short a call option or short the market. By selling VA guarantees we become short a put option and thus long the market. Over certain ranges these two positions offset each other, as the market cannot be up and down at the same time. As the market moves further in either direction, one option will cease to lose value as fast as the other option gains value. These are the scenarios we address through the option-based hedging program.

This graph shows the market value movement net of hedges on embedded options, covering roughly $20 billion of notional between our VA and FIA lines. It is an economic analysis, not an accounting-based analysis. Also, there is no assumption of rebalancing positions as the market moves. Most replication-based hedging strategies or hedging programs would make such an assumption. As is evident, JNL has a minimal level of equity risk even in the most extreme scenarios. Due to the efficiencies gained through our internal hedging approach we have been able to put this hedge in place at a cost approximating one-quarter of the expected fees collected on VA guarantees.

VIII. Interest Rate Sensitivity

Moving on to interest rates, this graph looks at the sensitivity of our business to large changes in rates. It is an analysis involving a detailed model of all of our assets and liabilities, projected over 20 years. We look at the ending surplus discounted back to present value. It does not include the initial surplus position but it does include the effect of new business. Without the hedge there is meaningful diminution of value when the rates increase in a significant fashion. This is not the case for more modest movements, as surrender charges and crediting rate flexibility protect the business. The previously mentioned swaption program is intended to address the risk of large rate moves and does a very nice job of protecting value.

IX. Economic Capital

Moving on to another important risk tool, I will now discuss our economic capital results. We take a multiyear stochastic approach that looks at the probability of insolvency calibrated to a ratings-based threshold. The model generates a number of variables stochastically, including interest rates, equity returns, exchange rates and credit defaults. We target an AA limit internally. The red bar on this chart shows the number of defaults we could absorb per year on an AA basis. The blue bar shows the number of defaults we actually have under this particular scenario. Eight failures out of 1,000 scenarios over 10 years would be the threshold for AA. The chart also shows the limits for other thresholds.

We solve for the amount of initial capital required to meet our constraint. As of year-end 2004, we needed $1.9 billion of initial capital to meet an AA test, compared to available capital at that time of $3.4 billion.

In looking at the breakdown of our various risks within this model, a couple of things become evident. First, the hedging we do on both the equity and interest rate risk proves to be effective and they consume a small amount of economic capital relative to their size. Second, with a majority of our business being spread-based, credit risk is our single largest consumer of economic capital. This is due in part to the lack of viable hedging solutions and also to our strategy of attempting to add value through credit selection and a well-diversified portfolio. Finally, JNL is well-capitalized relative to the risk we have assumed. 43% of the available capital was unallocated at year end; a larger proportion than any one of our single risks.

X. Liquidity Analysis

Of course, no risk analysis would be complete without addressing liquidity. As the rating agencies would be quick to tell you, this is the leading cause of financial company defaults. This graph depicts our liquidity position and a run on the bank scenario. Only liquid assets are considered a source of liquidity; even then, we assume a market stress discount in looking at that availability. Liabilities are assumed to surrender very efficiently; in fact, faster than any insurance-related failures from years gone by. The available liquidity from the assets is then matched against the demand from the liabilities. Under this scenario JNL maintains, on a 30-day basis, about $6 billion of excess capital or about 2.25 times what our liabilities would require. On a one-year basis we are looking at about $14 billion of excess liquidity, or about 1.7 times what would be required. This is a closed-block only analysis; we also we also evaluate on a going concern liquidity basis through our dynamic solvency analysis.

The more extreme of the scenarios we consider within this particular analysis assumes a 300 basis point rise in rates, which of course moves surrender rates up and puts a strain on liquidity. At the same time, we assume that sales volumes decrease by half. Even in this relatively harsh environment JNL requires no liquidity from the existing portfolio.

XI. Summary

I have covered a lot of ground in a relatively short period of time. It is a lot of information and figures to digest but, in conclusion, I hope that I have left you with the impression that JNL is serious about risk management. At the core, it is what customers pay us to do. We do so in a very cost-effective manner and within well-defined and prudent limits. If we can find a reasonable way to mitigate a risk, we are willing to take it; if we cannot, we will not. We have a sharp focus on tail risk and do not expose ourselves to it. We seek innovative ways of assimilating risk and believe our risk aggregation and economic capital approaches to be industry best practice in the US.

Thank you for your attention. With that, we can move into what promises to be an interesting question and answer session.

Questions and Answers

Participant 1

I have two questions on hedging. Firstly, I do not really understand the point about the offset between the FIAs and VAs because your FIA book is around $3 billion and your VA book is around $11 billion. Of course, you will not have 100% equity participation in the FIAs either.

Secondly, for a GMWB with a roll-up, for example, how much is it costing you to replicate your hedging for non-extreme events? What is the cost of hedging for the extreme events? Also, what are you charging?

Chad Myers

On your first question, I did not mean to imply there is a perfect offset between the FIA book and the VA book. What I meant to say is that the risk goes in different directions. There is a portion that we can offset. I mentioned there are about $500 million of equity options that we are currently able to offset internally, but we have a lot more than $500 million of notional equity options on our books at the moment. However, it is an efficiency we are able to capture because we are in both of those businesses. We are one of the few companies of any scale in the US that is in both of those product lines. Some consultants are trying to encourage people to get into the FIA business – with their help, their models and so on – as a way to offset VA more efficiently. There is a conversation starting about that, but it is something we have been doing for quite a long time.

Your other question is a bit difficult to answer because it really depends on the mix of business at any point in time. At the moment, we have hedged out our entire existing book at about one-quarter of the expected fees on the VA. That does not include the efficiencies that we pick up on the FIA book. To take one contract, you would get a different answer because you would be looking at it in isolation; you would not be looking at the offsets.

That will change over time because we are now selling a lot more VA than FIA. It used to be that we were very scale in FIA and growing rapidly from a small base in VA. Those two are a bit closer to parity. As we continue to see VAs grow faster than FIAs, that mix will change. The fact we sell a lot of VAs does not necessarily mean we have a guarantee attached to every one of those. Because of our unbundled approach, we get much lower utilization of guaranteed benefits than competitors, who have a more bundled approach and take on the risk whether the customer wants it or not.

Participant 1

As an example, what do you charge for a GMWB-type of risk, perhaps with a roll-up?

Chad Myers

We do not have a GMWB with a roll-up but we charge 40 basis points for our 7% roll-up, which is the more aggressive of them. I think Lisa will present a chart tomorrow that includes the charges for all of them. I think we charge 55 basis points for our most aggressive GMDB.

Participant 1

Is that in line with competitors?

Chad Myers

Yes. Those are generally in line with competitors. I think GMWB-type of products would range from as low as 35 to as high as 50-55 basis points. All of our charges are competitive, which is a nice thing because the market did not previously allow us to price at those levels. There was huge rationalization after the bear market and people are actually charging what they ought to be charging. The key is that the market allows us to charge enough that I can go into the market and hedge out that risk. We may choose not to, because we do not want to pay 23 or 24 volatility for a 10-year option when that is not typically what you are going to see. We will retain some of the volatility risk on our books, within our limits, but at some point we will hedge it out. That is the dynamic we see at the moment.

Participant 2

I have a couple of questions, if I may. Firstly, if the annual reset mechanism is so useful to you in FAs, why does the competition not replicate it? Secondly, you said the return on equity of VAs is about twice that of FAs. Why is the VA margin higher, given that it only uses a quarter of the capital? Does it suggest that the riders are very profitable or are the riders on the FAs unprofitable?

Chad Myers

On your first question, you have to realize that in the US market there are basically two FA choices. You could guarantee a rate for five years with a five-year surrender charge. There is no element of trust in that, other than trusting the company is going to be in business in five years to provide that. The product we are selling has a nine-year surrender charge with a one-year guarantee that we can reset annually. The customer places a huge amount of trust in us that we will not abuse the ability to reset those credit ratings annually. Because we have a long track record of fair renewal rates we are able to provide that product and people are willing to trust us and buy those policies from us. For some of our competitors the strategy is to issue the contract and then within two years you drop to very low rates to widen spreads and maximize profits. You burn your distributors; they are never going to sell that type of product to you again.

Andy Hopping

If I heard your question correctly, you are asking what accounts for the significantly higher returns on a VA versus a FA in the example that I gave. To me, it is mostly just a function of such a low capital base relative to a FA. At 35 basis points the margins are pretty good; more like what you would see in a mutual fund business, but with very low capital levels.

Participant 2

My question was really about EEV margins being higher on VAs than FAs, which is surprising given the much lower capital requirement. Given that you are doing double the return on a quarter of the capital, you would not expect to see that. Are you making a lot of money on the guarantees and so forth, given the prices you are charging and the hedging costs you have having to incur?

Andy Hopping

I am not sure of the best way to answer that question from an EEV perspective. The margins we report on the VA under EEV are higher than they are on the FAs, but not in proportion to the return on capital ratio.

Chad Myers

The spread assumption on those FAs was 155, grading to 175. Because of the flat yield curve in the first half of the year and the tight corporate spreads in our FA pricing, it had a graded spread assumption. For that reason, you would have ended up with less than a 12% rate of return on an EEV basis. The example that was given here was based on current interest rates and current pricing of FAs. That is not meant to be an example of what the EEV pricing would have looked like. The EEV pricing for FAs was less than that in the first half of the year.

Participant 3

I have a couple of questions. The first question is on FAs. On your indicative income statement, I noticed there was no deduction for surrender option costs. Could you talk about that?

The second question is about your expense structure. I looked at your income statement, took your operating costs and added the non-commission distribution cost. I get 35 basis points versus the 48 for the on-balance sheet that was mentioned. Could you explain the difference between those two figures?

The third point is about the net ratio when you do the statutory returns. Our US analysts say Hartford's operating profits are around 20 basis points on a GAAP basis and around 30 basis points on a statutory basis. You have 75 basis points. Are there some distribution costs that you have not included in your operating profit that other companies do include?

My fourth point is that it appears you are running an experience variance loss. Does that indicate that your assumptions in your income statement, possibly your pricing assumptions, are not tying in with reality?

Finally, it is accepted financial economic theory that you would use a risk-neutral technique or a market-consistent stochastic model. If we were an investment bank with a prop book, that is how we would price it. If that technique did not hold true, then we could make money just shorting governments and going long corporates; we would not be having this conversation. What made you decide not to go with the accepted route in terms of market-consistent valuation? Why did you go a different route?

Jim Binder

On the market-consistent valuation, we did it consistent with the Group approach and the Group methodology, which is an actuarial appraisal-based approach. We have not calculated the market-consistent values because that is not the approach we are using at the moment.

Andy Hopping:

If and when we do market-consistent, we will do market-consistent. In the meantime, we have not even done the work to show what it would be. It would clearly make a big difference on a FA, where you would not bring in any of the profits on the spread. That would be the biggest difference.

Chad Myers:

Another of the questions was about an experience variance loss on EEV versus pricing assumptions.

Jim Binder:

Most of our experience variance arose from spread. The experience variance for expenses was very minimal at the half-year and for last year. The negative in 'other' was very likely an adjustment for MVA charges.

Andy Hopping:

On your first question, on FAs and the surrender, were you talking about the pricing model?

Participant 3:

Yes. On the FA pricing example, there was no item for the cost of surrender guarantees. I was wondering why you had omitted that cost on your income statement. Do you feel it is zero?

Chad Myers:

There are a couple of answers to that question. The option the policyholder has against us broadly offsets the option we have against them. Those two net pretty close to zero. The other issue is that with the swaption program we have in place, we have effectively mitigated that at an extremely low cost, around one or two basis points. It basically rounds to zero.

Andy Hopping:

Also bear in mind that in the examples I gave, even though there was perhaps more detail in the examples than we have typically shown in the past, those are not the precise pricing models that are used to do the pricing. Actuaries have a model for each product based on the cash flows implicit in those products. Those models are much more sophisticated than what I showed, but they were fairly indicative of base pricing and the pricing on a product today, though not necessarily what is coming through on the back book or what has come through in the last year and a half in terms of financial results. I showed today's pricing going forward.

Clark Manning:

Let me jump in on a couple of these questions. I made notes as Greg was speaking. On the pricing example, as Andy said, that is a high-level model. The actual pricing is done using very detailed actuarial models. The actuarial department, along with the asset/liability management group, test those assumptions stochastically, in terms of what the actual returns are going to be.

On the expense question regarding the 35 versus 43 basis points, the example shown here is based on our current average sizes. For the issue cost of VAs, for example, the fully allocated issue cost is $150 per policy. The average size of a policy is approximately $80,000. On the maintenance side for VA, the maintenance cost is $105 per policy, again divided by the initial average size. For a FA, the initial acquisition cost is $105 per policy, divided by an average size of approximately $55,000. The maintenance cost is $75 per policy, divided by an average size of approximately $55,000.

On the experience variances, I would note that the aggregate experience variances were positive. The pricing, in aggregate, is meeting the assumptions. There may have been some offsets between positives and negatives, but we were showing a large positive variance on the spread.

On the distribution cost/expense analysis, I did not do the analysis but I suspect what we were looking at was total exhibit five expenses divided by assets.

Jim Binder:

It would be general expenses from the statutory income statement divided by average net admitted assets.

Clark Manning:

You can look at the mix of business and how that impacts those. You can do policy analysis rather than asset analysis. There are a lot of different ways you can look at it. The point of that slide is not that Jackson is the lowest-cost company in the world, or anything like that. There are lots of different ways you can split it, such as by line of business. You can actually get into company functional cost analysis and look at per policy costs used in pricing and whether that is fully allocated, etc. There are a lot of different ways to look at that.

The point is that the scale question has been dogging Jackson for a long time. Our goal is not to be the low-cost provider; our goal is to be a low-cost provider and be able to provide excellent service at that low cost. I would encourage you to do your own analysis on the expense side; split the expenses amongst lines of business however you feel is most appropriate; do a GAAP analysis or a statutory analysis; use policy count, liabilities or whatever you think is most appropriate in the denominator; and then reach your conclusion. We look at it in all of these different ways. We did not want to show 12 different slides on it, but we look at it in all of these different ways. When you look at it, you reach the conclusion that Jackson is a low-cost provider, that we do have administrative scale. That is the point of the slides. It is not our goal to be the low-cost provider because our goals are much more in terms of the quality of service we provide, but we are able to provide that quality of service at our current size and still remain very competitive in our expense structure.

Participant 4:

I have a question on capital generation and the trends going forward. At the moment you have quite a favorable boost coming from the maturity of a capital-rich book, predominantly the FA book, and you are writing products which are less capital-intensive. Going forward, you said this morning that your product mix would shift to a post-accumulation type with a high level of guarantee – and presumably a higher level of capital – and yet your book will be moving to a less capital-intensive book. Do you expect the current trends on capital generation to reverse going forward?

Andy Hopping:

I do not think we expect that anytime in the near future. We actually hope the FA business comes back a little bit so that we can deploy more of that capital on the FA side, but I do not think we will see a lot of change anytime soon in the way VA products require capital or in payouts on annuities. It is a longer-term trend to do with Baby Boomers and money coming out of VAs. For us, given the amount of earnings we have and the runoff on the back book that you mentioned, I do not think we have any problem with consuming more capital than we are generating.

Chad Myers:

We are talking about guaranteed income going forward, but that does not necessarily mean you are back into a fixed payout annuity. You could have that guarantee, like we are currently doing with the GMWB, where the policyholder still retains the separate account asset structure; they have a guarantee effectively on their income underlying that, but it is much more capital-efficient than issuing an immediate or deferred annuity.

Participant 5:

From what we are hearing, the trend going forward would be to write more capital-intensive products generally, compared to what you are writing now. The runoff from your book will be relatively less.

Clark Manning:

It is a macro-level question about what we are planning to be writing and what is in our business plans. I think the long-term trend is towards unit-linked product. My prediction would not be that the capital consumptiveness of the business we are writing is going to decrease, but there is a cyclical phenomenon that you have to layer over that; when equity markets are poor, the yield curve is steeper and credit spreads are wider, it is a more favorable environment for FAs. However, I think the long-term trends are running against them. We have had a real good run of free cash generation. Do I project that is going to reverse? I have not seen anything that indicates that. I am not going to make any forward-looking statements or Rebecca will join me up here, but when we look at our business we have made some statements that we think we can self-fund our projected growth opportunities and still return an increasing amount of cash to the Group. That is based on the free cash generation that we see in the book and based on the mix of business we would expect to see on the book. Tell me the economic environment and I will tell you what we see. I do not think the current situation is abnormal; in some respects, it is consistent with what we are writing today, with the profit characteristics of that business.

Participant 6:

I have three questions. Firstly, you mentioned that the fairly vanilla VAs required about 1.5% of capital and that FAs required 6.5%. Can you give us numbers for the GIC-type products and for your average VAs these days, with the various guarantees in them, on the same basis as the 1.5% and the 6.5%? The example you gave was a fairly vanilla VA, without guarantees attached to it.

Chad Myers:

On the institutional side, it would be about 20 or 30 basis points less than the fixed because there is no C4 risk that attaches to those. On the S&P, I think in the current model they charge a flat number of your net amount at risk for an in-the-money option and they charge you something for an out-of-the-money option. I think it is 1% for out-of-the-money and 2% for in-the-money on the VAs. At this point, it takes up hardly any capital at all. Just to be clear, the 1.5% does not include any VA guarantees; that is just the base chassis. We would assume something in the neighborhood of 1-1.5% more for the VA guarantees.

Participant 6:

On the FAs, you said that once you take out all the options and guarantees you get back to something fairly close to a risk-free discount rate, which makes sense. Do you have a rough idea of the effect of options and guarantees, and what the discount rate might be if they were all back in?

Jim Binder:

No, it has not been calculated on that basis.

Participant 6:

Finally, for EEV you are using your AA internal model, which is a long, long way below the S&P model, which is determining how much capital you are actually using. Do you have a number for the impact on the embedded value of using the S&P AA rather than your own? If you do not, can we be assured that when the numbers come out in December those sensitivities will be given for both the EEV and the new business profitability?

Clark Manning:

I think the sensitivities are an issue for the Group. I think they will probably be given on the same basis they have been given. When you look at the capital being consumed at the Group level, where the EEV numbers are really most relevant in the total Group context, any economic capital difference with US rating agency capital is actually a Group capital synergy. The capital being consumed at the Group level, which is run on an economic capital basis, is the economic capital. When the Group adds up its capital requirements, does it need to take the greater of this or that, by business unit, and do that across the whole thing? From my perspective, from a Group standpoint, I think the economic capital is reality. If Jackson was a standalone company and wanted to be rated AA, then Jackson needs to use AA capital. The fact that we are part of the larger Group acts as a Group synergy.

Chad Myers:

S&P is making some movement towards an economic capital framework as well. They are not saying they will take our economic capital models at the end of the year and use those, but it is an encouraging sign from a usually very conservative group of folks to say they are willing to look at something a little more cutting-edge than their static models.

Participant 7:

I have two questions, if I may. Firstly, on the return on equity, you put up a slide showing that you were above median in terms of return on equity. If you were to adjust that for the leverage and the excess capital, how much is the margin you have over the industry driven by business mix? How much comes from expense advantage? How much comes from pricing? That is the first question.

Secondly, I think Chad alluded to changes to the S&P model that may be in train. He thought they would start looking at internal models, etc. What realistic opportunity do you think there is in the foreseeable future to increase the $800 million of tangible surplus capital that you have over the rating agency margin?

Clark Manning:

On untangling our return versus others, we have not done that level of analysis. We try to analyze our own numbers pretty carefully; I do not think we have tried to rip apart all the balance sheets of the other companies.

Chad Myers:

On the S&P, the easy answer is "not anytime in the real near future." As they typically do when they come across something new and cutting-edge, they first try to slap you around a little bit with it. The first assessment they will do with the economic capital approach is to make sure that anybody who is not doing something like that gets sufficiently penalized it. The phase two we hope to see is that they will move to something that looks much more like economic capital models. That is probably a three- to five-year time horizon, just reading their body language on this.

Another important thing to remember is that we are one of the few large US companies that is a subsidiary of a UK or European parent. Companies in the UK or Europe are dealing much more with economic capital. US-based companies probably have not even heard the words yet. There will be a learning curve in the US for a lot of the larger companies to get up to speed on learning about economic capital, getting the models in place and then getting rating agencies comfortable with it. It is still a little ways off.

Jim Binder:

There was also a question on the composition of return on equity. The return on equity as reported was 13.6%. Adding in the 21% gearing would raise it to around 15.5%. If you were to strip out the excess capital, which might be doubling on a little bit, that raises it another point to around 16.4%. It is an interesting question – I have not looked at the aggregation of how much of that is related to the expense advantage and so forth. We are quite comfortable. It is not just the GAAP measure; you can also look at our returns on statutory capital, which are in the 13-14% range. If you look at AP shareholder funds, we grew those at 15.1% last year, including the dividend. If you take out the dividend it is about 12.3% growth. I think we had another 12% to shareholder funds during the first half of the year. On any basis, earnings look strong.

Participant 8:

What is the current split of revenues? You have given us the management fees on the separate account business, but what is the split between spread income and underwriting income? I want to get a sense of the balance of where the current earnings lie. Also, if you looked in your crystal ball ten years into the future, roughly what proportion would you like to have between general and separate account assets? You are now at 20% separate account assets; where would you anticipate that moving to?

Clark Manning:

I will take your questions in reverse order, starting with separate accounts. We do not really have a target. I see the separate accounts going up, but we do not really have a target for mix of business. We know that we are very light on underwriting income relative to where we want to be, but we do not have a target mix. I think target mixes could get you into trouble if you press too hard to meet an arbitrary target. On the separate account, you have seen a lot of growth in the separate account over the last several years. If present trends continue and we can maintain the same level of net flows you will see us move up the separate account assets league table rather smartly over the course of the second half of this year and into next year. I would expect to see the separate account percentage continue to increase.

What we showed was the split of reserves rather than earnings by line of business. We have not published line of business earnings so I do not want to discuss those in that format here. The numbers for spread income are not in my head but it is fairly easy to get out of the income statement what the spread income is and what the fee income is. Underwriting revenue would essentially be the premium line in the GAAP, because under US GAAP, the spread income does not come through premiums and the VA premiums do not come through premiums; those come through fees. It would be looking at the premium number, which I believe is in the $500-600 million range per annum. The mix of revenue is fairly easy to get to out of the GAAP income statement.

Participant 9:

Going back to the original cash generation chart, you gave us the costs for writing new business. Could you also let us know how much extra solvency capital you will need for the existing business as that grows from year to year as well? That is a strain that you have to fund. At the moment you have $450 million left after new business, so it is actually in excess of the $120 million you are paying out.

Clark Manning:

Is your question about the growth of the book in terms of separate account growth and that kind of compounding?

Participant 9:

Yes, that is right.

Clark Manning:

If we are compounding at 4%, for example, on the FA book in total, we would assume about 7% in the separate account. I am not sure where I would get to on an aggregate basis, but a rough estimate would be around 4-5% of asset growth is simply compounding, if you take the mix of the separate account versus compounding on the FA book. As a rough measure we use 7.5% of that balance sheet as a rough capital requirement. That is probably on the high side but it gives you some idea of the capital you need to keep just because the book is growing on a compounding basis.

Participant 10:

If that works out to be another $100-200 million per annum, you are still generating surplus cash of about $300 million a year in excess of that. You are only paying $150 million this year to the holding company. According to that basic math, there is substantial room to increase that dividend to the holding company.

Clark Manning:

How much capital is repatriated is a Group question, based on their needs and uses for the capital, whether we are approved to do any additional inorganic consolidation and where they want excess capital to be around the Group. It is true that Jackson is generating a lot of free cash flow at the moment. In terms of a projection of how that is going to impact cash flows out of the US, I do not know. That is more forward-looking.

Participant 11:

I have another very quick question. What happens to your required capital on a regulatory basis under C3 phase two initially and then later on as the rules settle?

Chad Myers:

They are still in flux but, as we stand today, the current GMDB reserves under statutory accounting are very punitive. For instance, you cannot assume any surrenders, so you basically have to eat all that risk. Those are less conservative under C3 phase two, but then of course there is no reverse in place at all for the living benefits, which will come in place. We do not expect there to be much impact at all, net net.

Participant 12:

Last year you did a rights issue and you went through a lot of pain, as we discussed two or three months ago. You also had excess capital last year. Why was that capital not distributed up to the holding company? It seemed slightly contradictory. The Group went through such pain when there was a block of excess capital sitting there. It does not square. I do not understand it.

Clark Manning:

I will answer part of this, though the rights issue is beyond the scope of what we will discuss here. When you look at the capital position of the Group, you need to look at it on a Group basis. The US has an excess capital position. When the Group looks at its capital requirements, it is on an economic capital basis and other relevant measures at the Group level. At this meeting we are not doing a reconciliation of the US capital to the aggregate capital situation, because I think stuff like that has already been provided. This is really just about the US capital situation.

Participant 13:

Looking at your risk analysis, you have 34% of your overall risks in credit risk. Given the issues you mentioned earlier about the airlines, General Motors and the economy-wide problem of burgeoning healthcare costs and so on, are you comfortable with 34%? Would you prefer it to be higher or lower? Is there more you could do to mitigate that risk going forward? I am thinking about CDOs or credit protection. What is your long-term thinking on this?

Chad Myers:

It is an interesting problem to have. If you say something is 34% of the total, you have to look at what it is. The easiest way to make it less than 34% is to have more equity risk or more interest rate risk. We do not actually have a target for what percentage of the pie that ought to be. Having said that, there are things we can do to reduce credit risk through CDS, CDX-type indices and so on. Those are things we will review but we do not have a specific target on an economic capital basis. We just want to be able to live within our means. Our primary way of gauging how much credit risk we are taking is really through the investment policy and the feedback loop with PPMA. As I mentioned, we overweight BBBs. Using our benchmark approach and looking at how they do it, if it turns out that they are awful at managing BBB assets then of course we need to make changes to our policy or our manager.

Portfolio and Investment Strategy

Leandra Knes Johnson

President, Chief Executive Officer and Chief Investment Officer, PPM America

I. Opening Remarks

Good afternoon. My name is Leandra Knes Johnson, and I would like to introduce you to PPM America, Prudential PLC's investment management arm in the USA. I will begin by telling you who we are, then we will describe a few of our competitive advantages and discuss our results.

Joining me today are Brion Johnson, our Head of Public Fixed Income and Portfolio Management and Jim Young, Our Chief Credit Officer and Head of our Structured Finance Unit.

II. Company Background

We were founded in 1990 as the North American investment arm for Prudential PLC. Our headquarters are here in Chicago. The vast majority of the funds we manage are for our internal affiliates. JNL (JNL) is our number one client; Prudential Life Fund is the second, and we also manage money for Asia as well as some collateralized bond obligations (CBOs) and external equity mandates.

We have about 180 employees in our Chicago and New York investment offices. A recent survey by Crain's Chicago Business pegs us as Chicago's third largest money manager, ranked by assets under management. Over 90% of what we manage is bonds and the majority is internal. This is a deliberate focus. We feel that attaining even our target performance bogy of 25 basis points on the $73 billion that we manage provides more value to the shareholder than chasing external bond mandates at potentially razor-thin fee levels.

III. Adding Value For Clients

How do we add value for our clients? First, we feel it is critical to have a well-diversified menu of asset-class choices for their portfolios. Second, we have structured our process to revolve around our clients. While this may be typical for third-party investment managers like yourselves, we believe it is unusual for in-house investment managers to treat their insurance affiliates in this manner. In fact, I know of no one who aligns their objectives as completely as we do with their insurance affiliates. Third, as a major fixed-income investor, we have the resources to staff a consequential credit function. Our discipline is to underwrite each and every name that goes into Jackson's investment portfolio, including the investment grade credits. We do not believe that is the norm for Jackson's competitors. Finally, we believe our structure provides value-added results.

We manage a broad array of fixed-income and equity assets. We have fairly traditional asset classes and several firm-wide functions including financing operations which contain all investment support such as HR, IT, Legal, Compliance and the back office reporting functions; portfolio management, the embodiment of our client-objective focus in the Group; quantitative analysis where we benchmark ourselves against Wall Street, not other insurance companies. Several years ago we were lagging in this area but we made some key staff additions and now we consider ourselves to be best of breed. Credit analysis, a core competency and source of competitive advantage, and the workout area, a stand-alone area which provides expertise to distressed credits.

Reflecting our clear alignment with our clients, over 90% of our bonus pool is determined by investment results. The remaining 10% reflects how well we manage the company. Unlike third-party managers, we participate in the same long-term performance plan as Jackson so our long-term incentive comp is completely aligned with theirs. For each client mandate we work with them to ensure that our compensation relates to their desired business results. Jackson's performance metrics are total return performance, spreads, losses, cash invested and a discretionary bucket. Each January the weights on these categories are determined based on importance. For example, in a year where we expect higher than average defaults in the US credit markets, the loss bucket would be more heavily weighted.

IV. Market Conditions

As Chief Investment Officer of the company, it is impossible for me to stand here and not give you at least a brief overview of market conditions in the US. As you know, our economy has proved remarkably resilient despite many challenges. Even with these extraordinary events, the current GDP, unemployment and inflation metrics represent textbook conditions.

However, most recently with oil rallying over 40% it has caused pressure on our producer prices. It is really tough to envisage a scenario where that will not ultimately translate to increased pressure on rates and growth.

Reflecting our generally good macro-economic conditions and the health of individual companies, evaluations remain quite tight. That makes it difficult for us to maintain entry spreads supportive of Jackson's fixed annuity business. Reflecting this and our close communication with Jackson, they have shifted their growth towards variable annuities.

High-yield conditions in the US have also been quite favourable in the last few years, with defaults well below historic averages. However, tight valuations, particularly in the lower-rated tiers, create a challenge. That said, we believe we are structured and incentivised in ways that lead us to approach these challenging markets in a way that produces successful results for our clients.

Brion Johnson, our head of portfolio management, will now talk about the process that we use to sift through market opportunities in order to focus on producing the desired customer results in their portfolio. Then Jim Young, our chief credit officer, will talk about our underwriting discipline in detail, mainly on corporate credits, which is the vast majority of the assets in our clients' portfolio. Once Brion and Jim have spoken, I will come back and give you a rundown of our results.

Market Opportunities

Brion Johnson

Head of Public Fixed Income and Portfolio Management, PPM America

I. Invest Philosophy and Approach

I hope to impress three things upon you. One, we are client-focused. We are not just trying to beat their benchmarks; we are trying to support their business. Two, we are organised to draw on the total resources of PPM America's asset managers across the firm. We think that is critical in supporting Jackson's business. Three, while emphasising a team approach that uses all the professionals in the organisation, we maintain individual accountability. We think that is absolutely critical to get the right result.

We have various primarily affiliated accounts and are structured to serve their differing needs. Client Project Managers (PMs) act as our liaisons with those accounts. They communicate investment policies, work with the clients to establish appropriate benchmarks for their accounts and within our firm, guide the asset allocation that supports their objectives. Their pay relates directly to the performance on the account. Asset Class Managers have the final accountability for exposure to public fixed income securities. These highly liquid and easily priced assets are core to most fixed-income portfolios and become the benchmarks for substitutions that we make of other asset classes. We hired our quantitative team from Merrill Lynch. We have daily automated portfolio and analytic reporting. We have complete portfolio transparency throughout the firm. We have automated performance attribution, and we use risk management tools like tracking error analysis to augment our risk management approach. Finally, we centralised trading in our firm to get the most bang for our $73 billion with Wall Street.

II. The Investment Process

Every decision passes through various filters. First, how does it stack up among other market opportunities that are available to us across all the assets that we manage? We have several forums for looking at that. We have markets meetings; we have informal meetings around the trading desk, and we have asset class discussions. This is where our asset class PMs and our traders have most input.

After an initial screening, potential opportunities are passed through underwriting and valuation. For corporate credits, this work is done by the credit team, which Jim Young will describe. Even if we determine that the asset is a good one, it is not necessarily appropriate for all the accounts. It has to be suitable for the client and their objectives. Client PMs have the final say for this when it comes to our client portfolios. Our process is client-focussed but team-oriented so we get the benefit of all the expertise throughout the firm. Every investment decision passes through multiple layers of investment judgement, but our structure ensures individual accountability for that decision, rather than compromise.

III. Strengthening and Diversifying the Business

Many of us have been around the company for over ten years. I am one of those people. There has been a fairly consistent theme about how we approach the business, which is to strengthen and diversify it. Over those ten years, we have moved away from the interest rate risk of mortgage-backed securities towards a more balanced portfolio that performs better throughout various economic and market cycles. In fact, PPMA's multiple asset class capabilities were built up for that very purpose. The assets that have been added over time are commercial mortgage loans; invested grade private placements; asset-backed securities and commercial mortgage-backed securities. These assets do not have the interest rate sensitivity of the residential mortgage-backed securities they replaced. They provide better option and risk-adjusted spreads. This diversification was achieved while Jackson's portfolio approximately doubled in size.

IV. JNL's Portfolio

Like any annuity portfolio, JNL's portfolio is credit-intensive. This is essential for a spread-based business. Versus peers, who generally have a lower proportion of spread-based liabilities; JNL has a higher concentration of triple-B investment grade bonds, in an area where we believe our Credit Team can add value. Of course, you cannot have more than one thing without having less of something else. In terms of risk assets, we have less common stocks and limited partnerships in other long-term assets like equity investments and real estate. While offering upside, the use of these assets needs to be limited in these portfolios since they do not match up well to the liabilities.

1. Portfolio Transition

There has been long-term migration away from mortgage-backed securities towards investment grade bonds. While our goal has been the transition of portfolio without damaging spreads, we did not give in to the temptation of junking it up in order to maintain them. High-yield investments are lower - strategically because Jackson lowered its investment policy target from 10% to 8% - and tactically because when we evaluate assets for addition to Jackson's portfolio, we do it in a context of their long-term historical default cost. In today's market, lower-rated investments are priced very near and sometimes through their historical default costs, resulting in little or no net spread and inadequate returns on capital for Jackson. Despite generally good credit conditions, our use of this long-term perspective has naturally pushed us away from these investments.

2. JNL's Current Portfolio Positioning

We are duration neutral. That is the long-term posture of this fund, given that it funds specific liabilities. We are slightly underweight in credit assets, reflecting the tight valuations that I mentioned earlier. Instead, we try to add value using structured products like MBS, ABS, and CMBS.

Within corporates we are positioned somewhat defensively. We have overweights in sectors like banking, insurance and brokerage where investment grade ratings are very important to their business, and we are underweight in telecommunications, technology and electronics where we have a concern about the risk of technological substitution.

We are also underweight in retail, reflecting heightened LBO risk in a world where more money has been raised for such activity than at any prior time in history.

We have been underweight in autos and auto parts, and we have no airline exposure. We are also underweight in high-yield corporate credits. In addition, the high-yield portfolio is higher quality than the benchmark. The benchmark is 70% double-BB; 30% single-B and the portfolio is 80% double-B and 20% single-B. While this implies giving up a total return while credit remains good, we feel we are better positioned for the time when the market is priced for more risk than it is today.

The Underwriting Approach

Jim Young

Chief Credit Officer, PPM America

I. Opening Remarks

I am Jim Young, Chief Credit Officer for PPM America. My role is to chair the credit committee and approve credits; I manage the credit research team and I manage the credit research process. My goal today is to explain the credit team and credit process and show how they lead to solid results.

II. PPMA's Approach

PPMA is a very credit-intensive shop. We have 19 analysts organised by industry. On average, each analyst covers about two industries and about 40 to 50 names. We support publics, privates and bank loans. My analysts do a full underwriting and go to committee for all new deals, both investment grade and high-yield. This is very different to most of our competitors who do not go through this process, particularly for investment grade deals.

I cannot stress enough that we know our credits on a real-time basis. We are an active manager. We are not a buy-and-hold shop. Therefore, I tell my guys they need to be in a position to buy, hold or sell recommendation on every name in their portfolio on every single day. My analysts focus on both credit and relative value. In fact, we issue two opinions. Our internal rating focuses on credit, and it is stated in terms of triple-B plus, double-B minus etc. Our relative value opinion focuses on value – whether this spread is appropriate given our internal rating. These opinions are buy above, which would be an overweight, buy at, which would be an even weight, and buy below, which would be an underweight.

Our credit-intensive approach is clearly working. We have outperformed significantly since the last analyst meeting.

I want to discuss our auto exposure and how we tend to lighten our exposure as events dictate. Let me give you three examples. The first is General Motors. In June 2004 we held $210 million of this name with an internal rating of triple-B flat and a relative value opinion of buy at. By the end of last year, we became much more pessimistic about this name, both from a credit perspective and a relative value perspective and downgraded our internal rating to triple-B minus and our relative value opinion to buy below or underweight. In conjunction with this, we lightened from $210 million down to $124 million. In the first half of this year we became even more bearish and downgraded our internal rating to double-B plus and kept our relative value opinion at buy below. In conjunction with this, we further lightened to $84 million. This exposure of $84 million was far below the neutral index size and over half of this holding was in GMAC rather than General Motors core.

Ford was a very similar story. At the end of last year we owned $148 million of this name and it had an internal rating of triple-B minus. By the middle of this year we had put a negative outlook on our triple B-minus, which was a clear indication to our portfolio managers that we were likely to downgrade this to high-yield sooner rather than later. In conjunction with this we lightened from $148 million to $104 million. Again, this holding was far below the risk neutral index size position.

Finally, Delphi, a name that has been in the news recently when it filed for bankruptcy. At the end of last year we held $40 million of this name and had a double-B plus internal rating. In the first few months of this year, we became very pessimistic about this name and thought there was a good chance it would file for bankruptcy. In conjunction with this, we lowered our relative value opinion to sell, and we sold out of that position completely. When it filed for bankruptcy, we held none of this name for JNL. While we did sell it at a loss, our sale price was significantly above the current prices today.

There are three lessons here. Firstly, we are very active managers. Our exposure will change as events dictate. Secondly, active lightening does reduce our losses. Finally we are very well positioned in the auto sector.

III. Portfolio Performance

The entire portfolio is doing very well. I think there are three reasons why our problem credits are minimal. First, we are in the middle of a very good credit cycle. Our portfolio is highly correlated to the overall credit environment and right now the credit market is very strong. Secondly, we do not have any leftovers from the last cycle. You know as well as anyone that we took our medicine there in the last downturn. Finally, the process and team we have been talking about has a lot to do with these solid results.

IV. Credit Outlook

Our credit outlook going into 2006 is relatively bullish. The economy, while certainly not growing at a phenomenal rate, is growing fast enough. Balance sheets remain healthy and fraud, while always a concern, is certainly less of an issue than it was two to three years ago. Therefore, strong balance sheets and a resilient economy should keep the credit environment strong well into 2006.

Company Results

Leandra Knes Johnson

I. Strong Performance

You have now heard about our people and processes. Let us turn to results. We have outperformed our credit and paramount expectations. This is in part a reflection of the benign credit environment, but it is also due to our ability to consistently position the portfolio to outperform market indices.

On the return on corporate investments, although total return is only one component of our metrics, and there are a number of factors which influence our portfolio positioning, we are very pleased that we have been able to outperform our benchmarks in each of the last two calendar years, both absolutely and duration-adjusted.

II. Summary

You have heard that we are quite proud of our processes, people and results. We have highly credentialed people who have a client-focus mentality. We have a consistent philosophy across the firm with an emphasis on bottom-up fundamental research. We have a benchmark and score card focus and are fortunate to have the broad resources available as part of a significant global financial enterprise.

Questions and Answers

Participant:

You say you actively manage your holdings so you sell out as things are looking to get downgraded. Could you give us a sense of how much capital loss you have incurred, perhaps on the auto sector?

Jim Young:

Our lightening of General Motors and Ford was done at a zero loss. I think we gained $2 million on our General Motors lightening, and we lost $2 million from a GAAP standpoint on the Ford lightening. Therefore the net loss was minimised; I think it was less than $1 million.

Participant:

Overall every year, how much would you lose from lightening?

Jim Young:

I think we are at a net gain on it.

Leandra Knes Johnson:

Certainly we are, including private equity gain.

Participant:

Your committee approach to making decisions – how often does that meet? Do you ever find that the delay caused by a committee decision leads to any problems? How many decisions that are put to committee do you accept or reject?

Jim Young:

That is a great question. First of all, there is very little delay – maybe two days between the time we hear about a deal and the time we can turn it around. Generally, we have time to go to committee before we purchase any. There are times when, if we think the bond is liquid, we will purchase some of the amount in front of the committee and go to committee one or two days later. If for some reason we were turned down in committee, we are confident that we could that. However, we are fairly confident before we go to committee that we are going to have some type of purchase recommendation.

The committee meets every time there is a new deal that we do not already cover. As we cover more and more index names on the public side, the committee does not meet so often because we have covered so many names already. Remember, at committee we are approving a buy above, buy at or buy below, so all those recommendations could result in some type of purchase. Even an underweight is not a completely negative position. Only a sell would be that, as you saw on Delphi.

As far as the number of deals we turn down, it is really a two-pronged process. On the public side it is not that many because we have the three opinions that result in some sort of purchase decision. On the private side it is well over half. I would say it is probably 75% to 80% of the bank loans and the traditional private placements that we look at. Some of that is done by asset class managers and they do not even make it to my credit team.

Brion Johnson:

I would like to separate out that we do not make committee decisions about how much of a credit should be in a portfolio. The committee that Jim is referring to is the credit committee where we approve the credit for purchase or not. When a decision is made about putting it in a portfolio, you generally have an asset class manager, a client PM and a trader standing around a desk while the deal is live, with a credit person standing right there with them, making the decision to go or not go or how far to go. If it is a brand new deal, which would be an unusual circumstance, it requires a new underwriting they would underwrite it. If it is not, if there is already an opinion in the database, we can move on the opinion right there.

Participant:

How much of the portfolio has an equity kicker built into it? Also, how important is tax in managing the portfolios? Is that dictated to you by Jackson?

Leandra Knes Johnson:

I am unaware of any equity kickers. We looked at potentially doing some deals with equity kickers but decided to rather to bifurcate it and go with pure equity risk through our private equity team. They focus on that tranche of the market instead of the bond risk. We also have public equity that we manage, so I am unaware of any equity kicker.

Brion Johnson:

Jackson is a very active manager of his business. We meet with Jackson formally every month in investment committee to talk about whatever constraints there may be, which could include tax constraints in respect of how the portfolio would be managed. We also have weekly phone calls with them to touch base on things. In general, JNL is way ahead in its capital planning, its tax planning and everything else so we normally have plenty of mobility in terms of how we manage the portfolio.

Leandra Knes Johnson:

However, it is a good question and one of the things that we always say is that when you are dealing with general account insurance investing, it is really more of a linear programme. You are not just maximising total return – you are maximising total return within a number of constraints. Tax is one of them. Therefore it is different and Brion has two different approaches on his team; for the life fund it is far more optimised total return because there are fewer constraints. The other is the more general account investing. They do a really good job on both in maintaining the firm-wide expertise while keeping those approaches separate.

Participant:

I wonder if you could give us those numbers on defaults for 2001 and 2002, just to give us a better backtrack. Secondly, I wondered if you had thought about going into hedge funds on the credit side; whether you would try to take your skills into different areas and whether that was interesting. For example, could you buy the bonds and then short treasuries against it and lock in some of the credit defaults?

Leandra Knes Johnson:

On the numbers for 2001 and 2002, I am sure most people are quite familiar with our default situation. We would really like to assure you that the process changed so significantly in 2002 – in fact, the reorder occurred on 10th September, 2001. Obviously we were not able to fire-test it during the week of the 11th in 2001 when there was severe market disruption. The 2002 recession was really a three standard deviation event. We also think there are several types of recession – credit-led recessions, real estate recessions and consumer-led recessions. That was clearly a credit-led recession, with problems on corporate balance sheets as well as fraud. For Jackson, which is obviously a corporate player in the annuity line, it was the perfect storm. We do not feel that situation is repeatable but should it be, we are not saying we would be 100% loss-free by any means, but we feel the approach we have described today greatly changes the kind of numbers you would see.

The benchmark approach greatly reduces and sizes the positions that we are taking to much more normalised sizes. The investment policy also provides significantly enhanced diversification. Last but not least, this active approach that we have discussed is very different. In the portfolio management world, it makes a world of difference. A classic example is Global Crossing, which was one of our bigger default positions. The buy-and-hold way we managed it before we changed to total return was a significant loss because we held it all the way down. That is what happens with a buy-and-hold mentality. We held the same position in an actively-managed variable annuity comp and sold it at $95. The same portfolio manager, the same company. Therefore we are highly confident that should we see that kind of US market condition again, we would not experience the same severity of losses.

Brion Johnson:

The other thing I would add is that there is no question that defaults come in lumpy. They do not come in at the average that occurs over time. Jackson’s pricing provides for those defaults with everything they write, all the time. They were probably five years ahead of 2001 and 2002 where there were no credit losses in pricing. It is important to recognise that over a cycle, pricing will marry up with default rates because that is where the charge is coming from.

Participant:

The second question was that given that credit spreads are so far ahead of where you think defaults were, I wondered if you could try to capture that through a hedge fund.

Jim Young:

As far as investing in hedge funds or investing in CDS?

Participant:

You could provide a hedge fund-type approach for either third-party money or shareholder money. It would seem quite lucrative.

Leandra Knes Johnson:

We feel that we are playing with additional spread by investing purely in those assets. We had experience in CBOs in the 1990s where we invested in that for our business. We feel our focus is so much better for the shareholder when we invest in our internal funds that I think the third-party idea is one that we have ruled out, at least for the immediate future. We really would prefer to focus on the shareholder funds because we think they provide significant value. Issuing a hedge fund is something we talk about. I guess a CBO has its roots in a hedge fund because you are essentially arbitrating a spread differential and leveraging it. We believe focussing our analysts on ensuring that you are getting other people’s money invested versus focussing on the $73 billion of internal funds was not an appropriate shareholder-value approach.

Participant:

In terms of Legal & General’s capacity and functioning, are there any cross-synergies that you pool from the two operations or are you pretty much autonomous in the group?

Leandra Knes Johnson:

That is an excellent question. We absolutely do. We work very closely with Simon Pilcher and his team and a lot of people on Michael McLintock’s full team but particularly with Simon Pilcher’s because of the bond nature in general of our approach. There are a number of initiatives on the credit side where we share information. Certainly if a company in which we invest is domiciled in Europe, we would exchange information with them and we even do some specific credit work for them which Jim will describe.

Jim Young:

I have a very close relationship with Stephen Wilson Smith, who runs their research team. The way it works is that we have a list of all their holdings and they have a list of all our holdings. Any US name that they hold, whenever we send out an e-mail, a credit update or an opinion change, the analysts in the UK receive that e-mail or update and can obviously call my analysts. It works in the same way in reverse; if they have an update on a UK name, they let our guys know. Therefore we are in close contact on a name-by-name basis. Also, when it comes to some of the third-party CBOs, they will talk to my guys on a slightly more formal basis on US holdings that they hold, relying on us for some of the credit work that is done on those. Therefore it is a very good relationship. Nothing would happen on a US name they hold that we would not inform them about and vice versa.

Closing Remarks

Clark Manning

President and CEO, JNL

Thank you all; it is the end of a long day, and I hope it was helpful to you. What we tried to do today was to give you an overview of the US market and the trends that underlie it. In particular you have heard a lot about the demographic trends at play in the US as we believe that these will define a lot of savings behaviour in the market. We talked about our response to these trends and where we think Jackson fits in as a provider of retirement income-oriented products.

We talked about our distribution and gave you a third-party perspective of our primary channel, the broker-dealer channel. We discussed our participation in that channel and how we approach it in order to differentiate ourselves so that we are able to compete in that channel on a basis other than price.

We spoke about the company's financials. We are generating good cash flow, and we have a good expense base. I hope we have buried questions of scale, as that is something that has been following us for a couple of years and it is not legitimate. We do have scale. We are generating good cash flow and are able to self-fund our growth. We have a good story to tell there.

On the investment side, we talked about how we have re-oriented the way that PPMA invests. We have done some de-risking of the investment portfolio. We have not entirely de-risked because a large portion of our business is still a spread-based business, but it has been de-risked relative to five years ago. We manage that portfolio in a much more active fashion, and there was some discussion about how we compare results relevant to indexed results so that we are able to benchmark their performance and measure them in a way that is not altogether dissimilar to the way that someone running a fund would be measured.

Tomorrow will be run on a different format, and our objective is to show you the operation up close in Lansing. You will have the chance to talk to some of the distribution people in the field, talk to some of the service people to see what they are doing, go through a session with our product development team and talk to them about how they originate and manage ideas and product initiatives, so you get a better feel for the organisation. I hope that is interesting for you; I think it is a little different to what you normally see and we thought it would give you a much better feel for the organisation than you would get by just sitting in a hotel ballroom listening to us.

Thank you all.