MARKET RELEASE

CHALLENGER LIMITED 1H14 RESULTS

Annuity sales of $1.75 billion, including record retail sales of $1.46 billion, up 38%
Resurgence in lifetime annuity sales continues, with first half sales higher than all of FY13

Funds Management FUM reaches $45 billion, up 27%
Challenger moves up from 9th to 7th largest fund manager in Australia

Interim dividend of 12.5 cents per share, up 32%
Shareholders set to benefit from partial franking and rise in dividend payout ratio for 2H14.

18 February 2014, Sydney – Challenger Limited (ASX: CGF) today announced continued strong flows into its annuities and funds management businesses, with total funds and assets under management rising by 27% to $48.8 billion over the year. This resulted in interim normalised NPAT* of $164 million, an increase of 10% on the previous corresponding period (pcp). Statutory NPAT was higher than normalised NPAT at $166 million for the half.

The company's interim normalised EPS grew 14% to 31.8 cents per share (cps), while the interim dividend (unfranked) rose 32% to 12.5 cps. Challenger expects to increase its 2H14 dividend payout ratio to between 40% to 45% of normalised NPAT, an uplift on the range increase announced last August, and today confirms its intention to frank approximately 40% of that final dividend.

Chief Executive Officer Brian Benari said: "We're very pleased with the performance of both businesses. Annuity sales are being propelled by product innovation and the rising tide of baby boomer retirees, while our funds under management are growing in line with strong boutique performance and mandated superannuation flows. From now until June we'll focus on marketing and selling lifetime and care annuities, and supporting our boutique managers in their quest for outperformance".

Challenger has continued to exhibit strong operating leverage with a further reduction in its cost to income ratio to 34%, well within the targeted range of 32% to 36%. Challenger's post-tax normalised return on equity was 16.2% for the half.

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Capital management

Challenger remains well-capitalised, holding $1.13 billion more capital than APRA's required minimum, inclusive of group cash, as at 31 December 2013. Challenger Life targets a Prescribed Capital Amount (PCA) ratio range of between 1.4 to 1.6 times. The PCA ratio is 1.8 times when including the full LAGIC transition balance and 1.4 times without.

During the half, $25 million of capital was used to fund the acquisition of self-managed super fund (SMSF) service provider, Bendzulla Actuarial. This investment meets the Group's pre-tax RoE hurdle of 18% and is expected to be earnings accretive in the first year of ownership.

No shares were bought back in the first half of the year. While Challenger maintains sufficient flexibility to operate its on-market buy back program, management does not expect to buy back shares in the second half of the year because of the capital allocation to Bendzulla and intended increase in the 2H14 dividend payout ratio range. In the medium term, the company continues to target a combined dividend and buy back payout ratio of 50% of normalised NPAT, subject to capital allocation priorities and prevailing market conditions.

Life (annuities)

"We sold more lifetime annuities in six months than the entire 2013 year, dispelling doubt about the revival of the Australian lifetime annuities market", said Mr Benari.

Total annuity sales for the half reached $1.75 billion, comprising institutional sales of $290 million and retail sales of $1.46 billion. Retail annuity sales increased by 38% and constitutes a record result for any six month period in the company's history. Of the $1.46 billion in retail sales, $1.19 billion were fixed term annuities. Lifetime annuities comprised the balance of $270 million, up from $101 million in the pcp. Challenger's entire FY13 lifetime annuity sales result was $257 million.

Strong annuity sales delivered an additional $540 million to Challenger's retail annuity book (representing 8% growth) and prompted an increase in the full year growth target from 8% to a range of 10% to 12%, excluding maturities relating to the Challenger High Yield Fund annuities.

Challenger Life had $10.9 billion in assets under management as at 31 December 2013, 7% more than twelve months prior. The average margin of 4.4% remained unchanged on 2H13 to deliver Life cash operating earnings (COE) of $237 million, an increase of 5% for the pcp.

The sustained trend to longer tenor annuity sales is benefitting Life's earnings, with the average term of new annuity business rising to 6.4 years from 6.2 years in FY13. In FY09, the average term of new annuity business was only 3.5 years.

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Funds Management – Fidante Partners and Challenger Investment Partners

"With net flows of $1.1 billion in the half-year and strong asset markets, we now have the seventh largest fund manager in Australia^, up from ninth when we reported in August, and are pleased to announce the recent formation of a new boutique, Tempo Asset Management", said Mr Benari.

Total funds under management increased by 27% for the 12 months to $45 billion, while EBIT for the half grew 60% to $21 million. The Fidante Partners business accounted for $33.7 billion of Funds Management's FUM, up 40% on the pcp. The balance of $11.3 billion of Challenger Funds Management's FUM is managed by Challenger Investment Partners, the business division previously named Aligned Investments. While its name has changed, the division's principal brief remains the same; to advise and invest with like-minded institutional investors in high "relative value" investments in fixed income, property and infrastructure.

Distribution, Product and Marketing

Challenger continues to evaluate new products and services to offer the retiree customer segment, along with innovative ways to educate, market and communicate the role and benefits of these products and services. To this end the company completed in February 2014 the acquisition of SMSF service provider, Bendzulla Actuarial.

"It's very early days yet but we're exploring the provision of additional SMSF trustee services with the Bendzulla team, who are highly regarded by the accountant community Australia-wide", said Mr Benari.

Since 2009, Challenger has been seeking to establish itself as a leading retirement income brand among consumers and their advisers, and this goal remains an enduring one for the Group. The latest December 2013 brand benchmarking survey confirmed that the company is building on its pre-eminence as a retirement incomes provider, with 89% of financial advisers polled recognising the company as a category leader.

While not yet as well known to consumers, the Challenger brand is set to become further associated with retirement investing following the launch of the company's second national advertising campaign in September 2013.

"We don't have a direct sales force, physical branches or retail shopfronts so advertising, PR and digital are keys to building our brand with consumers", said Mr Benari.

Outlook

Exceptionally strong annuity sales, particularly in the first quarter of the year, have given management the confidence to increase retail net book growth and Life cash earnings targets.

"The signs are there that this bigger book will grow by between 10% and 12% over the full year rather than by the 8% initially targeted, and should produce cash operating earnings around $5 million higher at between $470 million to $480 million", said Mr Benari.

"While funds management flows and markets are harder to predict, boutique performance is strong and we expect to finish the year well".

Overview

Metric	1H14	1H13	Movement
Normalised NPAT ($m)	163.5	148.7	10%
Statutory NPAT ($m)	166.3	222.0	(25%)
Normalised EBIT ($m)	192.8	177.8	8%
Normalised EPS - basic (cps)	31.8	28.0	14%
Statutory EPS – basic (cps)	32.3	41.8	(23%)
Normalised ROE – post tax (%)	16.2	16.6	(40) bps
Statutory ROE – post tax (%)	16.5	24.9	(840) bps
Dividend (cps)	12.5	9.5	32%

*As required by Life insurance accounting standards, statutory NPAT includes realised and unrealised movements in the value of assets and liabilities. The Normalised profit figures are non-statutory amounts and in Challenger's view better reflect the underlying operating performance of the business. The Normalised profit figures exclude investment experience, being the difference between actual investment gains and losses (both realised and unrealised) and the normalised gains and losses (being based on Challenger's long term assumed returns). The Normalised profit framework and a reconciliation to statutory profit have been disclosed on Page 20 in the Director's Report and Note 2 – segment information, in the Challenger 31 December 2013 financial report. The Normalised Profit is not audited but has been subject to a review performed by Ernst & Young.

^ Consolidated FUM for Australian fund managers – Rainmaker Roundup September 2013.

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