CHALLENGER LIMITED
ANNUAL GENERAL MEETING
CHAIRMAN AND CEO ADDRESS
28 OCTOBER 2014

CHAIRMAN ADDRESS

For several reasons that I shall touch on briefly, the 2014 financial year was an extremely good year to be a Challenger shareholder.

As a financial services organisation that has investment management at its core, the total amount of money we manage is a key indicator of our success.

In financial year 2014, Challenger’s total assets under management grew by 13% to $50.7 billion. This includes the invested capital in our annuities business, together with the funds we manage on a fiduciary basis across various asset classes, both for our retail and institutional clients.

As you will be aware, Challenger’s name is synonymous with guaranteed income investments and this year retirees invested $3.4 billion in our annuity products.

This included a record $2.8 billion in retail annuities, which are predominately recommended to clients through third party financial advisers.

Notably, as a subset of total annuity sales, our retail annuity sales consisted in part of a record $613 million in lifetime annuities, which was not just a Challenger sales record, it was a record for the entire lifetime annuity industry. That is, Challenger sold more lifetime annuities in one year than the entire industry has raised in any year.

This is a remarkable achievement of which your company is extremely proud.

Through innovation in product design, sales and marketing, Challenger has undeniably reinvigorated the Australian market for annuities and in particular lifetime annuities.
While growth of this magnitude may not be sustained indefinitely, at $613 million in annual sales, Challenger has put lifetime annuities firmly back on the investment roadmap for Australia’s Baby Boomer generation.

While undoubtedly a very important strategic outcome, this was not the only part of your company which continued to grow in 2014.

Our funds management business is now Australia’s 7th largest and one of the fastest growing.

This year we added five new investment managers within Fidante Partners and across asset classes which included international equities, infrastructure and fixed income.

We continued to increase our funds under management and with growth of 15% we reached $47 billion this year. We have also created approximately the same amount again in new capacity across our various boutique investment managers and their products.

We are advancing toward our ambition of managing $100 billion diversified across asset classes, while at the same time holding our position as Australia’s largest annuities provider.

All of this growth is only worthwhile if it increases our overall profitability.

As you would have seen in the press, and via Company announcements, strong profit growth has been achieved.

Challenger grew its normalised profits and earnings, and delivered to you a 30% increase in total dividends for the year taking last year’s distribution from 20 to 26 cents. Over the past five years, dividends to you our shareholders have doubled.

When added to the rise in our share price, your total return from owning Challenger shares over the financial year was 91%, and was the highest of any company in the ASX 100 index. A pleasing result, particularly considering the volatile capital market environment we have experienced.

While total shareholder return is only one measure of your company’s performance and value, in the short term it can be influenced by events outside of our control.

Most important from your Board’s point of view, are the longer term results and looking back over five years, Challenger’s total shareholder return has been 272%. This reflects in my view, a continued re-rating of the Company amongst its peers and endorsement of our strategic direction.

Consequently your company has significantly outperformed the All Ordinaries Accumulation Index, the ASX200 Accumulation index and the diversified financial sector over various time horizons.

Further enquiry: Stuart Kingham, Head of Investor Relations, Challenger Limited, 02 9994 7125
Stuart Barton, General Manager, Corporate Marketing and Communications, Challenger Limited, 02 9994 7008
Today, like most listed companies, our share price is sitting below the levels we reached earlier in the year due to recent declines in the overall market.

Share market volatility is, on the one-hand unfortunate because of the effect it has on our share price. However, on the other hand it reminds our customers and potential customers of the value of guaranteed annuities, where return is fixed at the outset and not impacted by market fluctuations.

Remuneration Report

To those shareholders who are new to Challenger and might regard us as a short term success story, I would like to remind you that today’s rewards for shareholders have been a long time in the making.

They are a product of strong alignment between the Board and executives who share a strategic vision and together with the staff have implemented it through extremely hard work.

Our executives are motivated to excel, and are rewarded for doing so in a way that is highly aligned with the value they provide to you, our shareholders.

In fact, a large proportion of their remuneration is put at risk, with their long term financial incentives entirely dependent on achieving superior total returns for you, our shareholders.

When considering remuneration, the Board has always been alive to changes in community expectations and best practice without compromising on maintaining highly motivated executives who are aligned with shareholder outcomes.

Because Challenger’s remuneration policies are not immune from Challenger’s philosophy of continual improvement, in 2014 we have made some incremental changes to them to further align the relationship between shareholders and management.

- We have limited our pool for short and long term incentives to between 10%-15% of normalised net profit before variable reward and tax;
- We have increased the minimum vesting period for long term incentives from 2 years to 3 years;
- We have increased the deferral period for some short term incentives from 2 years to 3 years; and
- Finally, the Board has increased the minimum shareholding requirement for your CEO and non-executive Directors.

Reflected in these adjustments you can see that your Board is highly motivated to ensure an equitable balance between the rewards to executives and shareholders. Alignment with shareholders is reinforced through performance-based compensation and long term incentives which are hurdled by appropriate total shareholder return targets.
We will continue to seek to refine our remuneration policies in the interest of good governance and contemporary market practice, providing, of course, that we believe changes will drive long term performance.

When we turn to the business of the meeting, you will be asked to vote on the company’s Remuneration Report. Before the vote is taken, you will have an opportunity to ask questions about the report and our remuneration policies.

I am pleased to say that this year the institutional and retail proxy advisory firms have all recommended that shareholders vote in favour of our 2014 Remuneration Report.

**Capital management initiatives**

As some of you may know, for each annuity we sell, we must hold capital as an additional buffer to protect customers, so we always fulfil our financial promise to them.

In the interests of prudent capital management and our growth expectations, we announced on the 20th of August that we were raising $250 million in equity capital from institutional investors and targeting $30 million via a Share Purchase Plan predominately for existing retail shareholders. This figure was eventually increased to $40 million due to strong retail investor demand.

By honouring this oversubscription from existing retail investors, Challenger raised a slightly higher percentage of equity from its retail shareholder base than they actually represented as a proportion of Challenger’s total shareholder base.

Your company also announced that it would launch a subordinated convertible debt instrument on the ASX, Challenger Capital Notes, which separately has raised $345 million.

The majority of the proceeds of the equity raising and all of the proceeds from the Capital Notes will be used to fund Life’s regulatory capital to support the expansion of our annuities business.

If you were one of those investors who participated in the equity raising or Challenger Capital Notes, thank you for your continued support.

**Outlook**

It was good to be a Challenger shareholder throughout the 2014 year, and we hope you agree that it’s good to be a Challenger shareholder today.

Customer demand across Challenger’s annuities and funds management businesses is being driven by two relentless forces – the progressive retirement of the largest and wealthiest generation in history,
and the progressive shift of age pension liabilities from the government, to the individual, which is helping to drive the growth of Australia’s funds management industry.

While the forebear to Challenger Limited, Challenger International, was established many years ago, it’s fair to say that your company’s current contribution to the creation and management of retirement wealth is still at a nascent stage.

Guaranteed income stream products like annuities comprise less than 5% of new retirement flows.

We have a long way to go, but the good news is that we’re set to get there a little faster, thanks to our new relationship with Colonial First State, which will see Challenger annuities available on their investment and superannuation platforms from mid-2015 onwards.

And while the superannuation industry enjoys regulatory sponsored growth, competition for investment mandates has never been more intense - so Challenger’s Funds Management business will continue to strive to grow faster than the overall market by responding nimbly to demand for domestic, international and alternative asset classes.

In closing, I would like to emphasise that your Board and management will continue to focus on growing the total return for Challenger’s shareholders. In support of this objective we hope to increase the 2015 dividend and re-instate full franking in the final dividend this coming year.

Thank you again for your faith in Challenger - particularly those shareholders who have supported us on this transformational journey of the last five or so years.

I will now hand you over to your Chief Executive Officer Brian Benari to talk through the finer points of a successful year.
Thank you Peter and good morning to everyone joining us today.

It’s a pleasure to provide you with an update on Challenger’s 2014 performance.

In many ways, the market's recognition of your company’s position and potential has been significant over the past year, if the re-rating of our share price is anything to go by.

However, as many of you will appreciate, there has been no sudden change in our strategy or its execution. Our vision is very clear and consistent – that is, to provide Australians with financial security in retirement. We aim to do this through both of our businesses by participating in Australia’s ever growing superannuation system.

Our Funds Management business is focused on the “super savings” or pre-retirement segment while the Life, or annuities business, targets the super “spending” or post-retirement segment. Both segments are growing rapidly with Australia’s pool of superannuation assets now exceeding $1.9 trillion and forecast to grow to in excess of $4 trillion over the next 10 years.

This structural growth provides great opportunities for Challenger.

I am pleased to report that all key 2014 financial metrics exceeded our expectations.

Total assets under management across Life and Funds Management passed $50 billion for the first time and finished 13% higher for the year. Normalised profit after tax increased to $329 million, similar to underlying operating cash flow.

Normalised earnings per share increased by 9% to 64 cents per share and the growth in underlying operating cash flow has allowed the Board to again lift the dividend payout ratio.

Our recent marketing efforts have ensured that Challenger has the leading brand in annuities, however Challenger is not just about annuities.

We are also committed to re-inventing the funds management model through our institutional focused Challenger Investment Partners, and our boutique funds management business, Fidante Partners.

In fact in 2014, Fidante Partners added five new managers and attracted net flows of $2.4 billion, helping Challenger’s Funds Management division end the year with a 15% increase in funds under management to $47 billion.

This increase resulted in a 27% rise in pre-tax earnings to $43 million, with our fee income growing at over four times the rate of underlying costs.
This represents outstanding operating leverage, and demonstrates the long term earnings potential of the Funds Management business.

Importantly, Funds Management is well positioned to grow further, because this year’s expansion in new managers and products means we now have an additional $50 billion of new investment capacity.

That is, we have the teams, the products and the infrastructure to potentially double our funds under management and substantially increase our net income, while gaining further leverage benefits in terms of costs.

Now turning to our Life, or annuities business.

As our Chairman noted, in 2014 we broke an industry record, with $613 million in lifetime annuity sales, an increase of 139% over the prior year.

When added to our term annuity sales, we achieved a retail annuity sales record of $2.8 billion, an increase of 28% over 2013.

Importantly, this very strong growth in lifetime annuity sales helped our underlying net retail annuity book growth to exceed our target and finished at 12.5% for the year.

This translated into Life cash operating earnings of $481 million.

Strong sales growth over the past five years has doubled the size of Challenger Life’s investment assets which is now over $11 billion.

As the leading provider of annuities in Australia, Challenger has the expertise and experience when it comes to design, distribution and marketing of annuities.

We’ve been doing it for around 20 years and are committed to the success of this product category.

Our leadership in product innovation and financial adviser support continues to be externally recognised. Our lifetime annuity product won the Chant West ‘Best Longevity Fund 2014’ award. The judges recognised the product’s unique qualities and our commitment to educating advisers on product features and benefits.

We take our educational responsibilities seriously, with our highly regarded technical services team having presented to over 5,000 advisers this year, that’s educational face-to-face contact with around one-third of the adviser market.
This educational theme is central to all of our product communication efforts. We have taken what some in the industry regard as complex products and concepts and simplified them. This is well-illustrated in the following animation which features on our website.

**Investing in retirement is different (animation)**

I hope you enjoyed the animation which is a small illustration of our educational leadership in the annuities market.

We continue to strengthen brand recognition with consumers and our leadership position among advisers. The latest independent benchmark survey showed 89% of advisers consider Challenger to be a leader in retirement incomes.

This retirement incomes leadership position is creating further opportunities to grow our business.

During the year we acquired the Bendzulla SMSF actuarial certificate business. We have now fully integrated the business, its performing to plan and generating new earnings growth for Challenger. The business has today announced a brand refresh. It will be called Accurium going forward and the team is busy exploring new pension phase services to offer its SMSF customer base.

Another opportunity is the recent signing of a landmark agreement with Colonial First State to put our annuities on their superannuation and investment platforms, which are used by around half of Australia’s financial advice businesses. This is a first in Australia and will see Challenger annuities sit alongside managed funds, term deposits, direct equities and other similar investments from mid next year.

Most importantly, it demonstrates annuities have returned to the mainstream, are now widely accepted by financial advisers, and are already being included in numerous retirement income portfolios. Retiree’s want income security and annuities deliver just that.

Our Chairman has already outlined the capital initiatives we completed following our results announcement in August. Our balance sheet is extremely strong, with new capital now being put to work. We are in an enviable position to take advantage of the next growth phase for our business.

**Deferred lifetime annuities**

Retirees’ concern with outliving their savings, together with our product innovation capability, places Challenger in a very strong position to enter the deferred lifetime annuities market.

Deferred annuities are a type of lifetime annuity where income payments commence sometime in the future and provide retirees with certainty of income late in life.
Deferred annuities do more than provide retirees with peace of mind that they won’t outlive their savings. They deliver guaranteed income to help retirees maintain their financial independence, and their dignity as they grow older.

While readily available overseas, Australian retirees cannot buy deferred annuities as our tax and superannuation laws do not contemplate them. This was unintended, not deliberate, and has resulted in them being unfairly taxed.

The campaign to bring deferred annuities onto a level playing field with other products has been running for some time. The last ‘holistic’, root and branch review of our taxation system, the Henry Review, identified that deferred annuities have a role to play in our super system due to our ageing population.

In addition to the Henry Review, they have been considered by numerous government forums, including:

- Jeremy Cooper’s Super System Review;
- The Ministerial Superannuation Advisory Committee;
- The Tax Forum;
- The Superannuation Roundtable; and
- Most recently David Murray’s Financial System Inquiry.

There were no less than 14 submissions to the Financial System Inquiry supporting the introduction of deferred annuities.

The Financial System Inquiry Interim Report said removing the barriers to developing income products, like deferred annuities is not a retirement income policy reform, but rather the ‘base case’ on which any further reforms will be built.

Over the past five years, in a total of seven forums and reviews, the merit of deferred annuities has been analysed, debated and accepted.

Indeed, Treasury is now specifically considering the design and implementation of deferred lifetime annuities through its Review of Retirement Income Stream Regulation.

The time to act is now.

In around 30 years, the fiscal pressure from our ageing population is expected to peak, in terms of age pension, aged care and health care costs.
If we have deferred annuities commencing payments at this time, they will take the pressure off.

The Deloitte Access Economics analysis we commissioned for the 2011 Tax Forum showed with only a $10,000 average premium paid by retirees aged 65, it would cost the government nothing. In fact, government combined outlays on the Age Pension and aged care will fall by 3% in 2050 as a result.

Deferred annuities help deliver a core objective of our compulsory superannuation system – the transfer of longevity risk from the public to the private sector.

Five years ago we started the campaign to introduce deferred annuities, which was two years before the Baby Boomers started retiring.

We’re now three years into the 20 year Boomer retirement phase. Three years of retiring Boomers have missed an opportunity to purchase pure longevity insurance in the form of a deferred annuity – a product which is readily available in many other retirement savings systems.

This is why it is so important these changes are implemented as soon as possible.

All we and others are asking for, is that deferred annuities are placed on an equal footing with other income stream products.

There is broad industry consensus that deferred annuities provide unique benefits, fill a gap in the retirement product range and provide more choice for our retirees.

Numerous studies and inquiries have supported their introduction and recognised the benefit they would have on Australia’s long term fiscal position.

If we make some small and painless legislative changes today, we will reap an enormous payback in welfare and fiscal benefits in decades to come.

With the Government’s review of Retirement Income Stream Regulation almost complete it’s time to finish what was started five years ago.

The government has a great opportunity to get done what the previous government could not.

Our people

Reflecting further on our performance last year, I would like to take this opportunity to publicly thank our employees for their commitment and contribution.

As a financial services business, our people are key and their engagement and determination drives our success.

Further enquiry:  
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Stuart Barton, General Manager, Corporate Marketing and Communications, Challenger Limited, 02 9994 7008

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Disclaimer: The forward looking statements, estimates and projections contained in this release are not representations as to future performance and nothing in this release should be relied upon as guarantees or representations of future performance.
One area of ongoing focus over 2014 was on the diversity of our workforce. At Challenger we seek to provide a diverse and inclusive workforce and value the capability and experience that a wide variety of employees brings to the organisation.

This year, we formally established a Diversity Committee. The committee is charged with developing and implementing a strategy to ensure the best people can make a contribution and succeed in our business, regardless of their gender, age, ethnicity, sexual orientation, disability or carer status.

Your Board and executives believe diversity is a necessity for a high performing organisation. An ability to harness diverse thinking and working styles will drive superior long term outcomes for our customers, employees and shareholders.

Outlook

I have today outlined the key achievements of what was a successful 2014.

It was a very active and rewarding year. The energy and enthusiasm amongst our employees is extremely high, driven by the opportunities that are currently in front of us in fulfilling our vision to provide Australians with financial security in retirement.

These opportunities position us to continue to grow earnings and increase dividends for you, our shareholders.

Now, some four months into 2015, I am pleased to reaffirm our 2015 guidance metrics. We expect to:

- Increase Life’s Cash Operating Earnings by around 12% to a range of $535 to $545 million;
- Grow Life’s retail annuity book by between 12% and 14%; and
- As the Board has previously indicated to lift the dividend payout ratio to between 45% and 50% of normalised profit and full dividend franking is expected to return for the final dividend.

On behalf of all Challenger employees I would like to thank you, our shareholders, for your continued support and I look forward to speaking with you following today’s meeting.

I’d now like to hand back to our Chairman.

Thank you.

ENDS
Challenger Limited
2014 Annual General Meeting
Mr Peter Polson
Chairman
Total Shareholder Return to 30 June 2014

Long term outperformance

Challenger
All Ords Accum.
ASX 200 Accum.
ASX 200 Div Fin Accum.
Mr Brian Benari
Managing Director and CEO
Challenger

Track record of sustained earnings growth

FY14 performance

- Normalised NPAT up 7% to $329m
- Underlying operating cash flow of $321m
- Statutory NPAT of $341m
- Total group AUM up 13% to $50.7bn
- Normalised RoE (pre tax) of 19%
Challenger

Earnings growth translating into higher shareholder dividends

Normalised EPS (cents)

Dividend per share (cents)
Funds Management
Benefiting from strong FUM growth

FY14 performance

- Net flows of $2.4bn
- FUM up 15% to $47bn
- Profit up 27%
- RoE up to 33%
- 5 new managers added in 2014
- $50bn of capacity in Fidante Partners
Life

Long term sales accelerating

FY14 performance

- Retail annuity sales up 28%
- Lifetime sales up 139%
- Retail annuity book growth of 12.5%
- Life AUM of $11.1bn
- Cash earnings of $481m
- Award winning annuity products
Life

Investing in retirement is different

Deferred Lifetime Annuity
Provides longevity protection

Longevity risk underestimated\(^1\)

DLAs provide income later in life\(^1\)

Important note

The material in this presentation is general background information about Challenger Limited activities and is current at the date of this presentation. It is information given in summary form and does not purport to be complete. It is not intended to be relied upon as advice to investors or potential investors and does not take into account the investment objectives, financial situation or needs of any particular investor. These should be considered with professional advice when deciding if an investment is appropriate.

Challenger also provides statutory reporting as prescribed under the Corporations Act 2001. The full year financial report is available from Challenger’s website at www.challenger.com.au. This presentation is not audited. The statutory net profit after tax has been prepared in accordance with Australian Accounting Standards and the Corporations Act 2001. Challenger’s external auditors, Ernst & Young, have reviewed the statutory net profit after tax. Normalised net profit after tax has been prepared in accordance with a normalised profit framework. The normalised profit framework has been disclosed in the Directors’ Report and Note 2 – segment information, in the Challenger Limited 30 June 2014 full year financial report. The normalised profit after tax has been subject to a review performed by Ernst & Young. Any additional financial information in this presentation which is not included in Challenger Limited’s full year financial report was not the subject to independent audit or review by Ernst & Young.

This document may contain certain ‘forward-looking statements’. The words ‘forecast’, ‘expect’, ‘guidance’, ‘intend’, ‘will’ and other similar expressions are intended to identify forward-looking statements. Forecasts or indications of, and guidance on, future earnings and financial position and performance are also forward-looking statements. You are cautioned not to place undue reliance on forward looking statements. While due care and attention has been used in the preparation of forward-looking statements, forward-looking statements, opinions and estimates provided in this announcement are based on assumptions and contingencies which are subject to change without notice, as are statements about market and industry trends, which are based on interpretations of current market conditions. Forward-looking statements including projections, guidance on future earnings and estimates are provided as a general guide only and should not be relied upon as an indication or guarantee of future performance and may involve known and unknown risks, uncertainties and other factors, many of which are outside the control of Challenger. Actual results, performance or achievements may vary materially from any forward-looking statements and the assumptions on which statements are based. Challenger disclaims any intent or obligation to update publicly any forward-looking statements, whether as a result of new information, future events or results or otherwise.

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