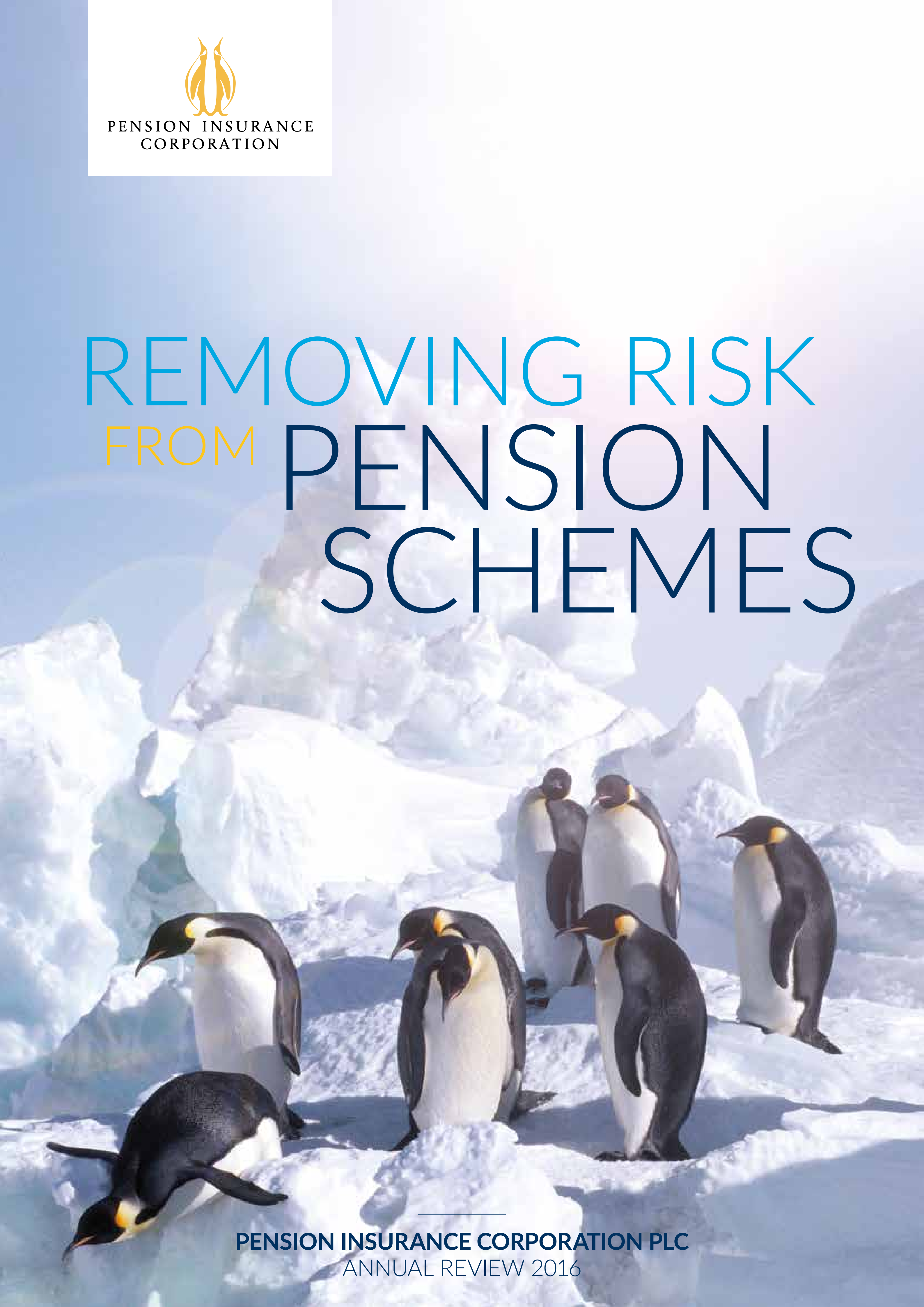
PENSION INSURANCE CORPORATION

REMOVING RISK FROM PENSION SCHEMES



PENSION INSURANCE CORPORATION PLC

ANNUAL REVIEW 2016

VALUING OUR CUSTOMERS

Pension Insurance Corporation plc is a specialist insurer, providing long-term security for our policyholders' pensions, based on superior customer service, robust risk management, and expertise in asset and liability management.

Pension Insurance Corporation plc is registered in England and Wales under company number 05706720. It is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulation Authority (FRN 454345). Its registered office is at 14 Cornhill, London EC3V 3ND.

2016 HIGHLIGHTS

Providing long-term financial security and stability for our policyholders and attractive returns for our shareholders

European embedded value (£m)

£2,567m

2016	2,567
2015	1,856
2014	1,550
2013	1,226
2012	830

2016 premiums (£m)

£2,598m

2016	2,598
2015	3,755
2014	2,646
2013	3,663
2012	1,512

Underlying operating profit before tax (£m)

£177m

2016	177
2015	133
2014	116
2013	80
2012	66

Financial investments (£bn)

£22.6bn

2016	22.6
2015	16.6
2014	13.3
2013	8.9
2012	5.4

Customer satisfaction (%)

98.5%

2016	98.5
2015	99.3
2014	99.8
2013	99.3
2012	98.7

Solvency ratio (%)

164%

2016	164
2015	151

Other 2016 highlights

The first sizeable pension insurance transaction under Solvency II

Continued investment in infrastructure: Thames Tideway, social housing and student accommodation

£4 billion
of assets held in excess of best estimate liabilities

2016 clients included Aon, Smiths Industries, ICI and GKN

£1 billion
Innovative £1 billion longevity reinsurance transaction

£250 million
of new equity capital raised by the Group

Continued popularity of our unique policyholder events, with more than 3,000 attendees during the year

Excellent levels of customer satisfaction

£250 million
of new debt issued

New Chairman appointed

AT A GLANCE

A specialist insurer and leading provider of bulk annuities to UK corporate pension schemes

BUSINESS

A specialist insurer, focused on securing the pensions of our growing policyholder base

- We secure the liabilities and risks associated with defined benefit pension funds in the UK.
- We stand for customer service and integrity in our dealings with all our stakeholders.
- We are straightforward to deal with and do what we say we'll do.

A leader in the established, and growing, market for pension insurance

- We specialise in, and only offer, pension insurance buyouts and buy-ins (bulk annuities).
- We price and structure transactions that meet individual client needs.
- We have robust risk management.
- Authorised by the Prudential Regulation Authority (PRA) and regulated by the PRA and the Financial Conduct Authority (FCA).

Focused business model

- Superior client service for policyholders, trustees and pension fund sponsors.
- No legacy business lines or product exposures.
- We deploy capital only if it meets internal economic criteria.
- Efficient operating model with substantial economies of scale.
- Fit-for-purpose IT and specialised processes.

HOW STAKEHOLDERS SEE PIC

"IN MY DEALINGS WITH THEM, THEY'VE ALWAYS BEEN VERY PROFESSIONAL, VERY DETAILED, AND WERE A PLEASURE TO DEAL WITH, WHICH YOU COULD PERHAPS ARGUE IS A REFLECTION OF A GOOD UNDERLYING ENVIRONMENT WHICH THEY HAVE CREATED WITHIN THEIR COMPANY."

Unnamed trustee quoted in Institute of Customer Service research, 2016

"YOUR ASSISTANCE AND THE WAY YOU DEALT WITH MY LITTLE PROBLEM MAKES ME BELIEVE THAT THERE REALLY ARE SOME VERY NICE PEOPLE OUT THERE IN THE BUSINESS WORLD."

PIC policyholder, 2016

CLIENTS

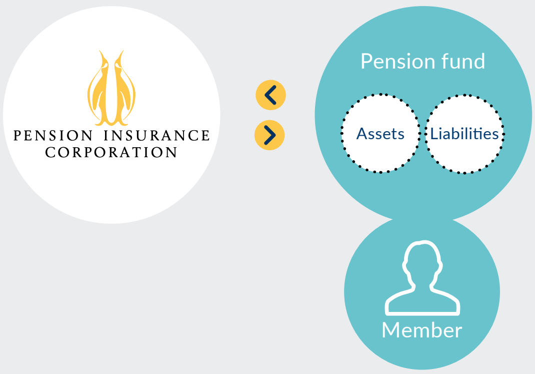
We have successfully completed buy-in and buyout transactions for clients including:

Institute and Faculty of Actuaries
HONDA The Power of Dreams
Alliance Boots
TOTAL
AON
London Stock Exchange
PENSIONS AND LIFETIME SAVINGS ASSOCIATION
Cadbury
Department for Environment Food & Rural Affairs
EMI
Civil Aviation Authority
citi

> THIS BUY-IN IS A SIGNIFICANT STEP IN OUR DE-RISKING PLAN. PIC HAS BEEN FLEXIBLE AND FOCUSED ON HELPING US ACHIEVE OUR AIMS.

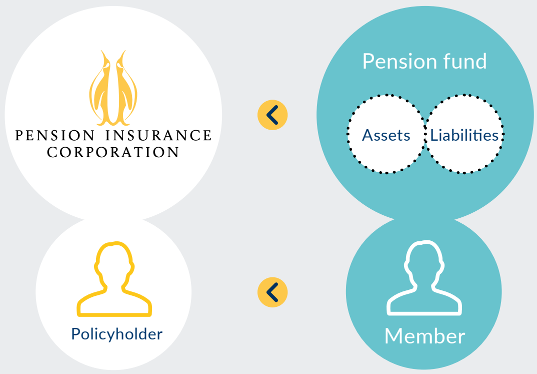
Nicholas Godden, Chairman of the Trustee of the Smiths Industries Pension Scheme (£250 million buy-in)

WHAT IS A PENSION INSURANCE BUY-IN?



- The pension plan purchases a bulk annuity insurance policy to cover its obligations to a subset of the plan members. The insurance policy is held as an asset of the pension plan.
- A buy-in is a perfectly matching investment for the insured liabilities.
- A buy-in removes the pension fund's longevity, market interest rate, inflation and other risks, as these are transferred to PIC.
- PIC has no direct relationship with pension fund members, who continue to be managed by the trustees.

WHAT IS A PENSION INSURANCE BUYOUT?



- Pension fund is typically wound up and assets pass across to PIC.
- PIC issues individual annuity insurance policies to the members of the pension plan as a replacement for their claim on the pension plan.
- A buyout removes pension assets and liabilities from pension plan and employers' financial reports. It is a full settlement of the pension fund and employers' obligations to the plan members.

HOW THE SECTOR WORKS

Insurance companies operating in the bulk annuity sector transact new business through active engagement with, and marketing to, pension fund trustees and their advisers, as well as to the corporate sponsors of such funds. Specialist advisers in this field, appointed by trustees and corporate sponsors, play a key role in any evaluation or execution of a pension insurance solution.

Why do pension funds buy insurance?

- **Scale and capabilities:** Insurance companies can manage pension risk more efficiently, benefitting from economies of scale and risk pooling. They have greater access to risk mitigation tools than most pension funds.
- **Drive to de-risk:** Pension fund trustees seek to maximise the likelihood of paying out full benefits, even in the event of employer insolvency.
- **Efficient investment and risk management:** Pension funds view insurance as efficient from a risk/return perspective when measured against other alternatives (e.g. holding gilts).

Why do employers buy insurance?

- **Unwanted liabilities:** Pension liabilities are large, volatile and can increase in an economic downturn when the employer is most likely to be in financial difficulty; precisely the sort of risk that is attractive to insure.
- **Removal of risk and settlement of obligations:** Insurance is the only route to a full and immediate settlement of the employer's pension obligations.
- **Facilitate M&A transactions and corporate activity:** Removing pension risks from the employer's balance sheet through insurance allows the employer to undertake corporate transactions which could otherwise be hampered.

CHAIRMAN'S REVIEW

"Our values remain a constant as the business develops in a changing world."

"THROUGH MANAGED, DISCIPLINED GROWTH, THE BUSINESS HAS DELIVERED TANGIBLE SHAREHOLDER VALUE."

Jon Aisbitt, Chairman

2016 was indisputably a year of change and unpredictability. Brexit, Trump, a – perhaps radical – change of leadership in the UK, combined with market volatility and continued political uncertainty, impacted the financial position of many financial institutions, including those of our clients, corporate pension funds. Headlines about the travails of the BHS and British Steel pension schemes led to a parliamentary inquiry with recommendations the Government is still considering. In the pension insurance market, the introduction of the new Solvency II regulatory regime has dominated the year.

From a personal perspective, I was delighted to take up the role of Chairman of Pension Insurance Corporation in October. As I said at the time, the three things which I always look for when investing in a company are the potential for growth, evidence of a talented and committed management team and a clear sense of purpose. When conducting my background research on the Company, I became convinced that PIC has all three. Since taking up the role, I have found that my confidence was fully justified in the talent and commitment of the whole team: Board, management and employees. There is a clear sense

SIR MARK WEINBERG

Sir Mark retired from his position as Chairman of the PIC Board in October 2016. He was one of the founders of PIC and helped guide the Company through its formative years.

Tracy Blackwell, CEO, said: "Sir Mark was instrumental in the development of our Company since it was founded and we have really benefitted from his vast experience in the insurance industry. I have also hugely enjoyed working with him on a personal level. It is therefore with real regret that we see him retire."

Sir Mark said: "I am exceptionally proud of the team we have put in place and the company that PIC has become. PIC really does lead the bulk annuity market in terms of the emphasis that it places on customer care and the wider values that it aspires to. I know that this is something that Jon takes a high level of interest in and I am sure that he is the right person to help lead the Company as it continues to grow. I wish the whole team the very best of luck and continued success."

of purpose in the Company and much work has been done to ensure that our values remain a constant as the business develops in a changing world. PIC's reputation for customer care derives from this sense of purpose.

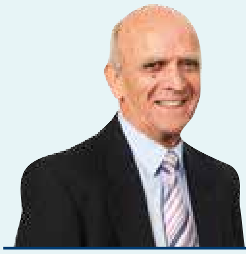
We are pleased to have been able to deliver strong underlying operating profit before tax of £177 million, with embedded value (EV) growing over the year to £2,567 million at 31 December 2016. Over the four years since year end 2012, PIC's embedded value has grown by more than 200%, which is underpinned by an underlying organic annual growth rate of over 20%. Through managed, disciplined growth, the business has delivered tangible shareholder value. But shareholders invest in a business for its future, not its past. A key factor which makes PIC an attractive investment is the future growth prospects of the Company, which are, for the reasons laid out in the next section of this document, considerable. PIC has built up a substantial store of assets in the business which can ultimately be paid back to shareholders. The growth opportunity for the pension insurance market will allow the Company to invest current and emerging surplus capital at attractive risk-adjusted returns and thus enable PIC to grow this underlying shareholder value in the future.

It is therefore vital that the Board continues to exercise the right controls and oversight over the business, both to protect our policyholders and to grow the business on a secure and sustainable basis. As outlined in the risk management and governance sections of this document, PIC has a robust corporate governance framework in place. At PIC the Board Committees are directly linked into our core business: investment and risk management are what we do.

Through the year the Board and its committees have focused on a number of key areas. Detailed consideration has been given to stress and scenario testing of the business and its ability to withstand external shocks and adverse events. The Board reviewed pricing methodology under the new Solvency II regime and later in the year spent some considerable time evaluating the impact of the EU referendum result on PIC and the investment portfolio. The PICG Board approved a debt issuance, through which the Group raised £250 million of additional regulatory capital in November. This took the total amount of new capital raised in the year to £500 million, with existing shareholder Reinet investing a further £140 million alongside £110 million from new investor Legend Holdings into the ultimate parent company. A final key area for the Board was reviewing the Company's values, standards and approach to policyholder care.

It is clear to me that the experience and quality of our people are core strengths of the business. The Board and management have a clear vision and strategy and it is for these reasons that I relish the challenges and opportunities that the years ahead will bring.

Case study



JOHN SPARKS

I have been a PIC policyholder since May 2016, following the transfer from the Philips Pension Fund. The transition process was excellent – with absolutely no problems. The levels of customer service I have received since becoming a policyholder have been excellent, with regular, clear communication.

When I heard about the Philips buyout, I was not concerned at all as I relied on the judgement of the trustees with regard to PIC's status and standing within your industry. Seeing which other pension schemes have insured with you is also reassuring.

I was very pleased to see members of the PIC team at our recent Philips Electronics Pensioner Association (PEPA) reunion. In my view, this indicates your commitment to our pensioners and the culture of PIC. This impression was reinforced by the invitation to your policyholder Christmas lunch. Your intention to attend the next pensioner reunion will further enhance your Company's image with those of us fortunate to have our pension with you.

John Sparks, former Philips Pension Fund member, now a proud PIC policyholder

SECTOR REVIEW

A large market with significant holdings of gilts and fixed income assets and the intention to de-risk

UK DEFINED BENEFIT PENSIONS: THE KEY NUMBERS

£2.1 TRILLION

- A huge market: UK DB pension schemes have total liabilities of £2.1 trillion and total assets of £1.3 trillion.[1]

£70 BILLION

- £70 billion of liabilities have been insured since 2007 through buy-ins and buyouts.[2]

87 PER CENT

- UK DB schemes that are either closed to new members or to future accrual are more incentivised to de-risk. Only 13% of DB pension schemes remain open.[3]

£650 BILLION

- £650 billion in gilts and fixed income held by UK DB schemes.[3]
- Exchanging these assets for an insurance policy has helped drive sector growth.

11 MILLION

- c.11 million members of UK DB pension schemes.[3]

£400 BILLION

- £400 billion in well-funded pension schemes.[4]
- Well-funded schemes are more likely to buyout.

Notes:
1 Data from PPF's Purple Book, December 2016.
2 LCP Pensions de-risking report, December 2016.
3 PPF's Purple Book, December 2016.
4 Company calculation based on PPF's Purple Book, December 2016.

"10 YEARS ON... AND ONE MILLION PENSIONS IN THE UK HAVE NOW BEEN INSURED THROUGH BUY-INS AND BUYOUTS."

LCP Pensions de-risking 2016, December 2016

"WE CONTINUE TO SEE THE UK BULK ANNUITY MARKET AS ONE OF THE BEST STRUCTURAL GROWTH OPPORTUNITIES IN EUROPEAN INSURANCE."

RBC Capital Markets, European Insurance 2017 Outlook, December 2016

£10.2 BILLION MARKET VOLUME 2016

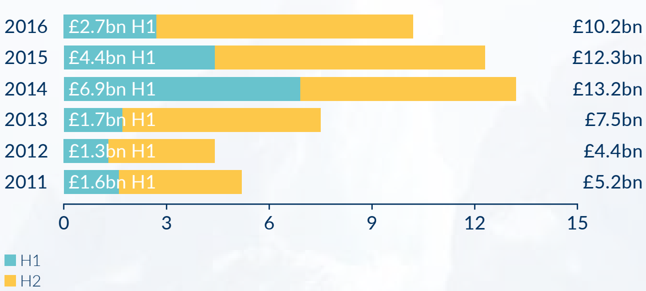
- "For pensioner deals, pricing improved in summer 2016."
  Aon Hewitt, UK Risk Settlement, February 2017

- "Pensioner buy-in pricing gets better and better at end of 2016."
  Hymans Robertson, Buy-in monitoring service, January 2017

- "...activity in the UK bulk annuity market increased dramatically in the second half of 2016 as sponsors became more determined to remove risk..."
  Mercer Global Pension Buyout Index, February 2017

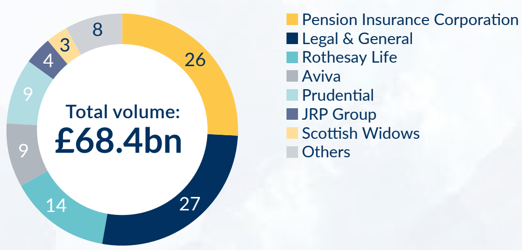
- "Despite a climate of historically low gilt yields, the clear direction of travel for the vast majority of pension schemes has been towards further de-risking as they continue to mature."
  JLT Buyout Market Watch, Q3 2016

Buy-in and buyout volumes (£bn)



Source: LCP Pensions de-risking 2016.

Share of buy-in/buyout sector by volume Q2 2008 – YE 2016 (%)



Source: Hymans Robertson and LCP buyout reports.

SECTOR REVIEW

The de-risking intentions of pension scheme trustees

1

De-risking intentions

Pension fund trustees are increasingly intent on de-risking their assets and liabilities. De-risking means reducing the expected volatility between pension schemes' assets and liabilities. This typically means pension schemes increasing their asset allocation to corporate bonds, gilts and insurance.

Industry magazine Professional Pensions conducted research into the de-risking intentions of more than 120 UK trustees and pension professionals. The research was conducted in association with PIC and published in summer 2016.

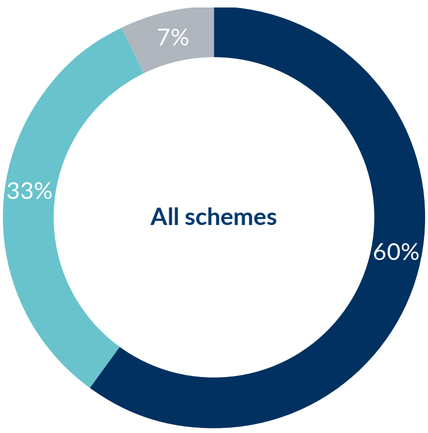
Some 60% of respondents said they expected their scheme to reduce risk over the coming 24 months, although the survey found willingness to de-risk changed markedly with scheme size, with smaller schemes less likely to de-risk over that time frame.

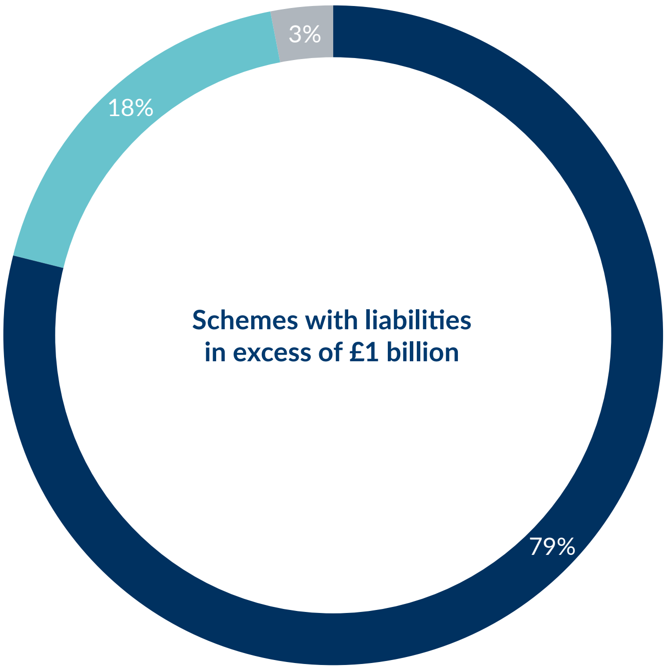
Large schemes – those with liabilities in excess of £1 billion – were most likely to reduce risk over the coming 24 months. Some 79% of these respondents said they expected to de-risk within the next two years.

Source: Professional Pensions and Pension Insurance Corporation research, summer 2016.

What is your scheme's current position with regard to de-risking?

- We expect to reduce risk in the coming 24 months
- We intend to make no changes in the coming 24 months
- We intend to increase risk in order to target higher returns, accepting that we may get lower returns





"SCHEMES ARE TYPICALLY TRADING INTO ANNUITIES FROM GILT OR LDI MANDATES, AND FINDING THE YIELD ON ANNUITIES IS COMPARABLE OR POTENTIALLY BETTER... WITH CONSIDERABLY BETTER RISK PROTECTION..."

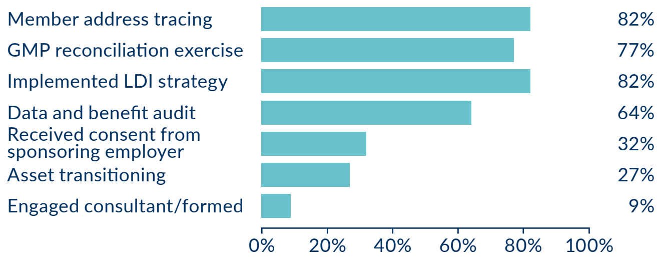
Aon Hewitt, UK Risk Settlement, February 2017

2

Buy-in intentions

Buy-ins had roughly equal popularity amongst smaller to medium-sized schemes, but were significantly more popular with the largest schemes.

Which of the following preparatory steps (if any) has your scheme taken to help achieve its long-term de-risking objectives (schemes with liabilities in excess of £1 billion)?



Source: Professional Pensions and Pension Insurance Corporation research, summer 2016.

Risk reduction/buy-in intention of schemes

SECTOR REVIEW

The means and the opportunity for pension scheme trustees to transact

3

Means to transact

Are pension scheme trustees realistically in a position to follow up their intentions?

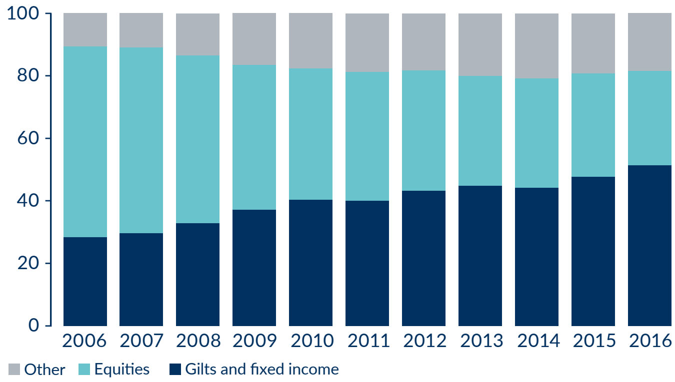
Pension schemes now hold 51% of their assets, or £650 billion, in gilts and fixed income, which can be used to purchase a pensioner buy-in for little or no incremental cost. 2016 is the first year that pension scheme holdings of gilts and fixed income has been above 50% of their total portfolio. The implication is that many pension schemes have the means to transact insurance.

The data highlighted by the following charts shows that trustees are remarkably well placed to move liabilities to the insurance sector through buy-ins today, and should gilt yields rise many more will be able to afford full buyout.

"PENSIONER BUY-IN PRICING IS CURRENTLY AT ITS MOST FAVOURABLE LEVEL SINCE 2011 RELATIVE TO HOLDING GILTS, DUE TO INCREASED APPETITE AND INNOVATIVE ASSET SOURCING BY THE INSURERS."

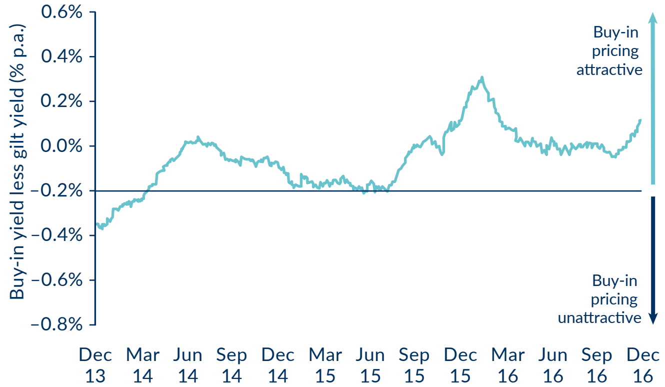
LCP Pensions de-risking 2016, December 2016

Asset allocation of DB schemes (%)



Source: Data from the PPF's Purple Book, December 2016.

Buy-in yield relative to gilt yields



The chart above shows the yield locked into based on typical buy-in pricing. This analysis varies between schemes depending on particular views over members' life expectancies. A buy-in yield of 0.1% p.a. to 0.2% p.a. below gilt yields might be viewed as a "fair" price to pay, given the reduction in longevity risk, other demographic risks and level of cash flow matching achieved.

Source: Hymans Robertson, Buy-in monitoring service, January 2017.

“FOR SOME EMPLOYERS, THE IMPROVEMENT IN YIELD LEVELS – AN IMPROVEMENT SEEN IN THE AUTUMN THAT HAS BEEN SUSTAINED SO FAR INTO 2017 – COUPLED WITH THE CHEAPER POUND WILL MAKE FULL BUYOUT A MORE VIABLE PROPOSITION THAN IN RECENT YEARS.”

Aon Hewitt, UK Risk Settlement, February 2017

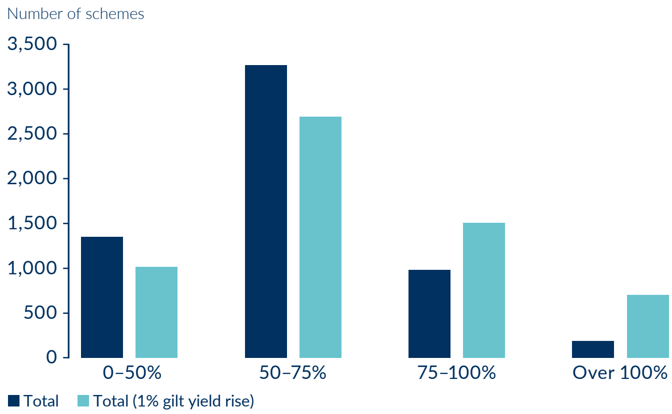
4

If real yields rise

These three factors, the intention, the means and the opportunity, have led the growing trend for trustees to de-risk their liabilities in tranches, before moving to full buyout.

If real yields rise, the market would be expected to shift from buy-ins to buyouts. As the chart demonstrates, a 1% rise in real yields would propel many more schemes into a position where full buyout was a realistic option because their deficits would have closed significantly, or disappeared entirely.

Distribution of funding on a buyout basis (%) (including estimate of how this would change should gilt yields rise by 1%)



Source: Data from the PPF’s Purple Book, December 2016, and Company analysis.

“WILLIS TOWERS WATSON IS PREDICTING THAT OVER £30 BILLION OF LIABILITIES WILL BE INSURED IN 2017, THROUGH BUY-INS, BUYOUTS AND LONGEVITY SWAPS, A SIGNIFICANT YEAR-ON-YEAR INCREASE.”

Willis Towers Watson press release, January 2017

CHIEF EXECUTIVE OFFICER'S REVIEW

"AS A SPECIALIST INSURER OUR PURPOSE IS STRAIGHTFORWARD TO DEFINE: IT IS TO PAY THE PENSIONS OF OUR POLICYHOLDERS."

Tracy Blackwell, Chief Executive Officer

Business development

I noted in our half year results summary that the first six months of 2016 were eventful. I think we can safely extend that description to the second half of the year. With insurers bedding down the transition to Solvency II, political risk translating into significant market volatility, and defined benefit pension funds continuing to wrestle with large and volatile deficits, there was no shortage of challenges throughout the year.

As a specialist insurer our purpose is straightforward to define: it is to pay the pensions of our policyholders, both now and for the full term of their policies with us. Our expertise and specialisation has allowed us to develop a deep understanding of the factors that could prevent us fulfilling this purpose, as well as a robust, sophisticated approach to managing risk. So we positioned ourselves very well to meet the types of challenges we faced in 2016 and to take the opportunities that arose to build the business. I am therefore delighted, but not at all surprised, that the Company continued to perform very well through the year.

We insured £2.6 billion of pension liabilities during the year on terms consistent with our long-term IRR targets, and maintained our long-term market share of about 26%. Our solvency ratio increased to 164% at the year end, due to capital raised during 2016, but also the effectiveness of our hedging strategies. PIC is very much in a growth phase, building an asset pool which will throw off increasingly large cash flows for very many years. As a result of this our underlying operating profit was £177 million, up from £133 million last year, reflecting our continued growth and store of long-term future profits.

Our investment strategy means we have an asset portfolio that is flexible and resilient. In spite of significant volatility it performed extremely well, due to the very close matching of our asset and liability cash flows. We continue to invest in infrastructure, including in social housing and student accommodation, through bilateral deals that are structured to be beneficial for both parties.

Bulk annuity market

The market for pension insurance during the year was £10.2 billion, which is smaller than was seen in 2015, when the market size was £12.3 billion. The first half of the year was relatively quiet and this, in our view, reflected in part the introduction of the Solvency II regulatory regime as well as volatile market conditions. In the second half of the year, after the Brexit vote, we saw a significant increase in new business volumes, writing 15 transactions compared with two in the first half of the year.

We also saw a notable increase in the very largest pension schemes looking to de-risk through insuring slices of their pension scheme liabilities, and thereby to fully insure their pension schemes over a number of years. The growth in this large market segment, in addition to the strong volumes seen in the second half of the year, point to a strong pipeline of potential business for the foreseeable future.

We were therefore delighted to be able to raise £500 million of new capital in the year to allow us to meet this projected increased demand. We raised £250 million of equity capital in June. In November, we took advantage of a window of opportunity in the markets and issued a second tranche of debt, raising a further £250 million.

Stakeholder views

We conducted research into the views of two crucial groups of stakeholders in 2016. In the first, the Institute of Customer Service surveyed our existing trustee clients. It was very pleasing to see that every single one of the trustees who responded would recommend PIC to another trustee.

The second survey was of our employees, 95% of whom believe PIC is customer focused and 90% of whom feel proud to work for PIC.

I don't believe that we achieved these results by accident. Our success flows directly from a strong sense of purpose and a culture and set of values on which the whole team is focused. This is something that we will be building on in the coming years.

Finally, we were delighted to welcome Jon Aisbitt, our new Chairman, in October. He replaced Sir Mark Weinberg, a legend in the insurance industry, who retired from PIC at the age of 85. Jon really has hit the ground running and I very much look forward to working with him.

Alongside our exceptional customer service track record, the Company has an enviable financial track record, demonstrating consistent growth and significant value generation over many years. Our results are a credit to the whole team and I am confident that we are ideally placed to continue building the business on a focused, secure and sustainable basis.

THE PURPOSE OF FINANCE

The UK needs a finance industry which serves society well, and in return is respected by society. Yet ten years after the great financial crisis, there has yet to be a decisive conversation about, or analysis of, the purpose of the financial industry.

PIC has launched a project to facilitate an industry-wide discussion examining whether establishing, measuring and regulating to the "Purpose of Finance" would mean a better, more productive financial sector.

Having a purpose goes far beyond merely providing the right products for customers. The purpose of any organisation dictates the fundamental principles on which that business is based. It is the guiding light for decisions and actions that are taken to achieve business goals.

The establishment of fit-for-purpose institutions might well lead to productivity increases and falling consumer costs.

The paper we have just published with David Pitt Watson and Harinder Mann, "Why Finance Matters", and our proposed follow-up work with a series of partners, is intended to help facilitate this discussion.

OUR BUSINESS MODEL

Rigorous management of risk underpins future profit, irrespective of new business flows

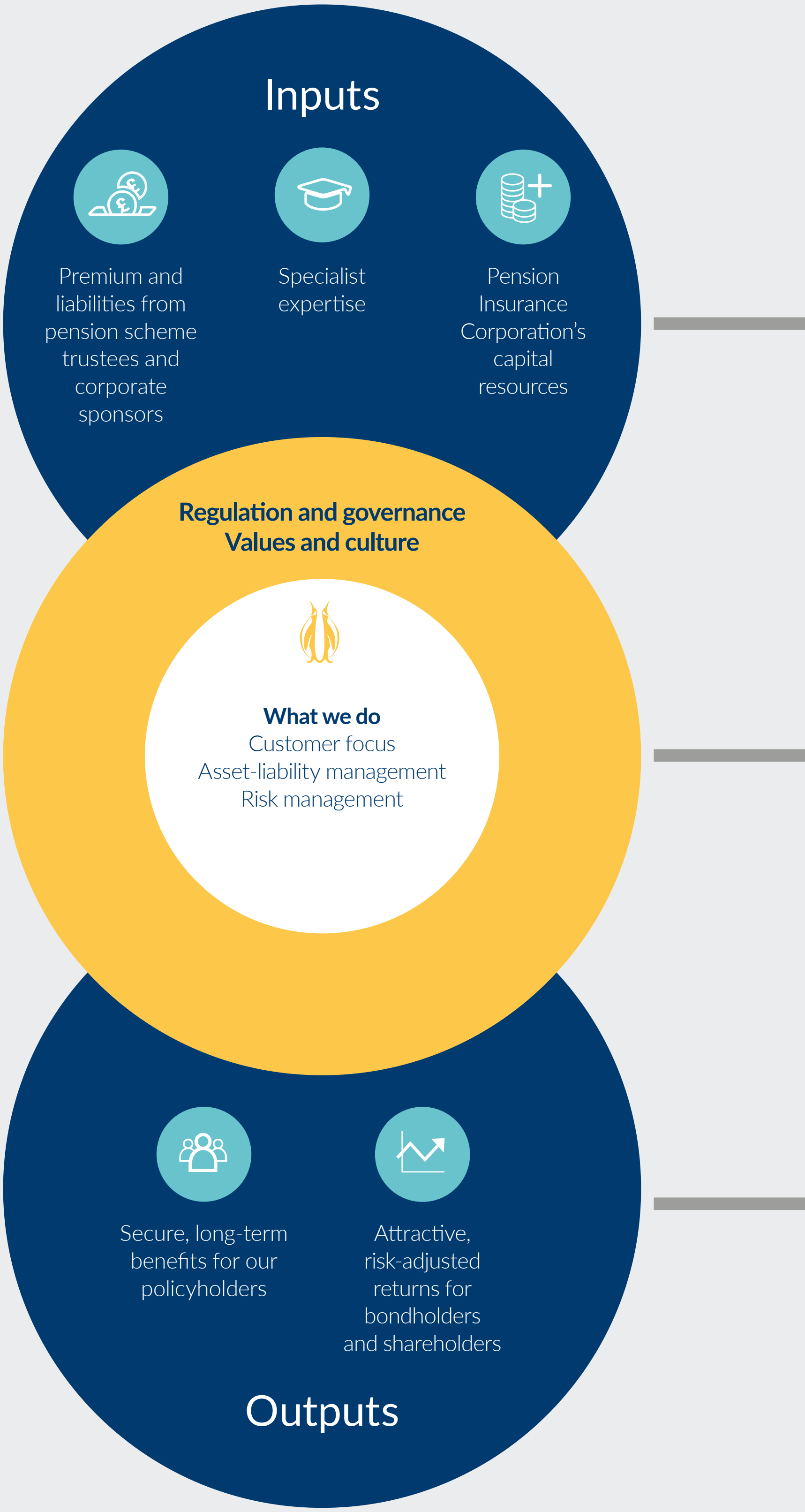
PIC uses its capital resources to insure pension liabilities through bulk annuity transactions. This process provides security for the pension benefits of policyholders and long-term returns to shareholders.

Strengths

- Safety and security for policyholder benefits.
- Key focus on risk management.
- A strong, conservatively managed balance sheet.
- Insurance solutions tailored to meet a client's individual needs.
- Outstanding levels of customer service.
- Attractive long-term, risk-adjusted returns for shareholders.

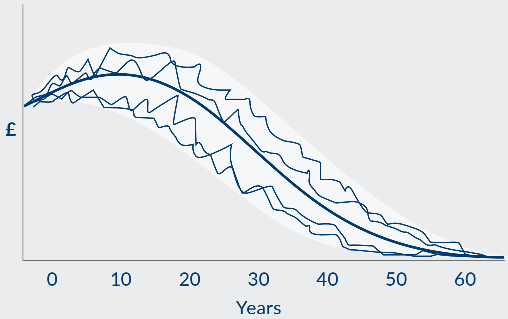
Outcomes

- Removal of longevity, market, interest rate and inflation risk from the pension fund.
- Policyholders have a guaranteed income stream, backed by PIC's regulatory capital.
- Corporate sponsor can be divested of all responsibility for supporting the pension fund.
- PIC manages its assets and liabilities such that the profit loading embedded in the premium emerges over time, as its assets deliver returns in excess of reserving and capital requirements.

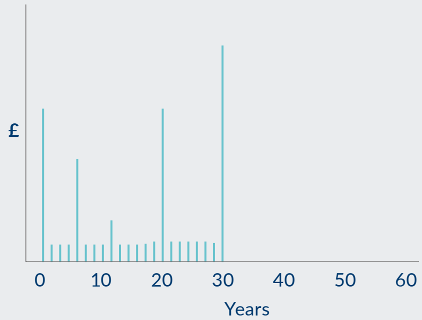


PIC'S NEW BUSINESS VALUE GENERATION, CREATING SECURITY AND ADDING VALUE

Pension scheme liabilities are uncertain in both timing and amount (longevity and inflation uncertainty)



Premium is typically received in cash and gilts and not cash flow matched to the liabilities



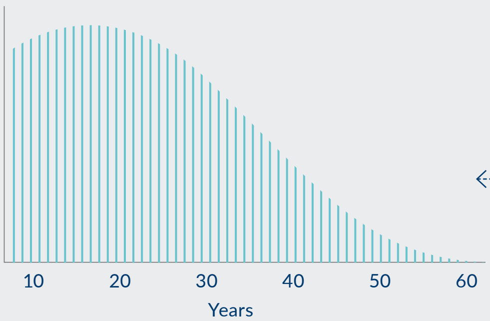
PREMIUM RECEIVED AND LIABILITIES ASSUMED BY PIC

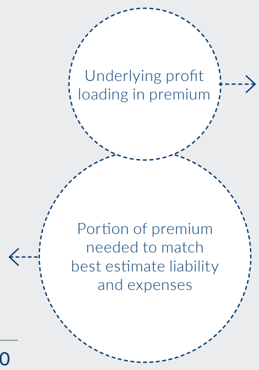
LIABILITIES HEDGED FOR INTEREST RATE AND INFLATION EXPOSURE

ASSETS RECEIVED REINVESTED TO OPTIMISE RETURNS ON A CASH FLOW MATCHED AND RISK-ADJUSTED BASIS

LONGEVITY RISK REINSURED TO REMOVE RISK, CREATE CERTAIN LIABILITY CASH FLOWS AND OPTIMISE CAPITAL DEPLOYMENT

Best estimate liabilities
made certain and cash flow matched





Underlying profit loading
in premium optimised and released over time as solvency requirements, risk and prudent margins run off

OUR BUSINESS MODEL

Continued

PIC: A STRAIGHTFORWARD BALANCE SHEET £21.6 BILLION OF TOTAL ASSETS WILL BE USED TO EITHER MEET CLAIMS AND EXPENSES, OR ULTIMATELY BE RETURNED TO CAPITAL PROVIDERS

TOTAL ASSETS: £21.6 BILLION[1]

£17.3bn

ALLOCATED TO MEETING CLAIMS AND EXPENSES, INCLUDING

£1.1bn

ALLOCATED TO RESERVE FOR DEFAULTS AND DOWNGRADES (£0.4 BILLION OF WHICH IS ANTICIPATED TO BE RELEASED IN THE MCEV CALCULATION)

ASSETS, ALLOCATED TO COVERING SOLVENCY AND RISK MARGINS

£4.3bn[2]

DEBT HOLDERS

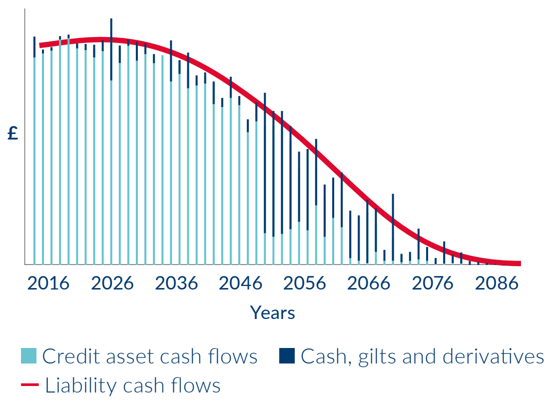
£561m

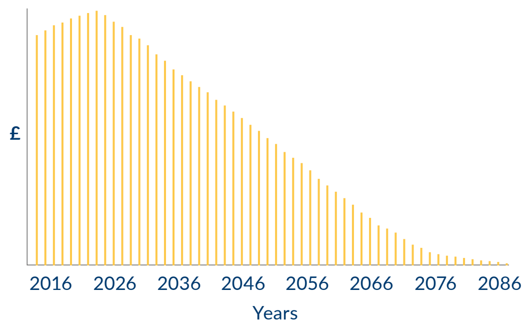
(FAIR VALUE)

£3.7bn[2]

OF UNDERLYING VALUE, EXPECTED TO BE RELEASED OVER TIME AS CAPITAL, RISK AND PRUDENT MARGINS RUN OFF

In-force asset and liabilities cash flows





Notes:
1 Comprised of financial investments, derivatives and net current assets.
2 After deducting £0.2 billion provision for deferred tax on the Solvency II balance sheet.

STRATEGIC SUMMARY

CONTINUED PROGRESS IN MEETING OUR KEY STRATEGIC OBJECTIVES

Strategic objectives	2016 progress	KPIs
01 GROWTH AND FOCUS Grow the value of the business on a focused, secure and sustainable basis	• Maintained long-term market share of c.26%. • Trustee boards with buy-in policies demonstrated their confidence in PIC by placing repeat business with us. • Raised new debt and equity capital to position us for the market opportunity. • 68% of the total longevity exposure reinsured, enabling capital efficiency and enhanced certainty. • Solvency position strengthened to 164%.	• More than 20% organic growth in PIC's embedded value over the past four years. • Portfolio has grown by 43% compound annual growth rate (CAGR) since year end 2012.
02 REPUTATION Long-term value creation through market-leading customer service	• Continued development of sector-leading customer service focus. • More than 3,000 attendees at six policyholder events in 2016. • Conducted survey of trustee clients.	• 98.5% of policyholders satisfied or highly satisfied with PIC's service levels. • 100% of PIC's trustee clients would recommend the Company to another trustee. • 95% of employees believe PIC is customer focused (always seeking to understand and meet customer needs).
03 RETURNS Deliver attractive, risk-adjusted total shareholder returns	• £2.6 billion of new business written in 2016, on terms consistent with long-term IRR targets. • Balance sheet management in volatile markets saw significant growth in shareholder returns (both profit and value).	• 28% CAGR in PIC's underlying operating profit over the past four years.
04 COST EFFICIENT A scalable business model that optimises internal and external resources	• Expenses continued to fall as a percentage of assets under management. • Implementation of measures to position the business for further efficiencies identified in 2015 review.	• Improving efficiency as the business develops.
05 KNOWLEDGE AND CONDUCT A professional and innovative team with respected business ethics	• Focus on business purpose and culture. • Values incorporated into appraisal process. • Employee Talent Management programme instituted. • Employee survey conducted.	• Knowledge and conduct is not a formal KPI; however, it provides an important foundation stone on which business support is built. • 95% of employees believe PIC is customer focused.

EXECUTIVE MANAGEMENT TEAM

Proven experience and successful leadership across pensions, insurance and the investment markets

Name and position	**Tracy Blackwell** Chief Executive Officer	**David Collinson** Head of Strategy	**Karen Dignan** Head of Internal Audit	**Giles Fairhead** Chief Risk Officer	**Matt Gore** Chief Administration Officer
Responsibilities	Primarily responsible for leading the management team in carrying out strategic plans and policies as established by the Board of Directors.	Responsible for developing the Company's strategy and business plan: identifies, investigates and implements new strategic opportunities.	Responsible for internal audit, providing independent review and opinion on governance processes, risk management and internal control systems.	Leadership over risk within the Company, ensuring the business manages and mitigates risk within acceptable limits. Reviews and analyses aggregate risk exposures and reports to the Board and its Committees.	Responsible for all post transaction client service for both trustee clients and scheme members. Oversees strategic outsourced relationships, data integrity, investment operations and reviews customer service. Overall responsibility for improving PIC's operational efficiency.
Experience	More than 25 years' experience of investment markets, focused on investment risk hedging strategies for pension liabilities. Strong knowledge and understanding of the regulatory landscape. She is a PIC Board member.	30 years' experience in pensions and insurance and qualified actuary. David has led some of PIC's largest bulk annuity transactions as well as PIC's 2016 equity raise.	More than 30 years' internal audit experience, primarily within the financial services sector. Chartered Fellow of the Institute of Internal Auditors.	Extensive experience working within the financial services regulatory environment, both at the PRA and PwC.	More than 25 years' insurance operations experience. Former Head of Operations for Prudential's Bulk Annuity product. Matt has previously been responsible for marketing, sales, pricing, operations and IT systems.

Tracy Blackwell, Rob Groves, Louise Inward and Matt Gore at PIC's London Policyholder Day 2016

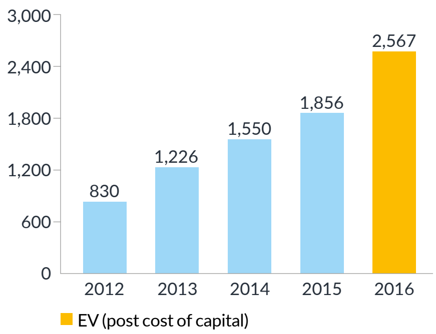
Name and position	Kim Gozzett Chief Operating Officer	Rob Groves Chief Investment Officer	Louise Inward General Counsel	Rob Sewell Chief Financial Officer	Jay Shah Chief Origination Officer
Responsibilities	Responsible for IT, HR, marketing, corporate communications, business continuity planning, and facilities. Ensures that the business strategy is supported by adequate resources and technology.	Leads PIC's asset liability management team and has overall responsibility for managing the Company's portfolio.	Responsible for ensuring the Board receives legal advice, that the Company complies with all relevant rules and regulations, and ensures appropriate governance structures are in place.	Leadership over all financial aspects of the Company, ensuring sufficiency, proper allocation and deployment of capital, whether through asset strategy, origination or the expense base.	Leads PIC's new business team, including brand promotion, sourcing new opportunities, pricing and structuring of proposals, and contract negotiations.
Experience	Over 25 years' financial services experience, covering both banking and insurance. Held numerous NED positions in financial services and other sectors. Previous roles include Managing Director of SG Hambros Bank and Trust's UK Trust Company.	Previously CIO at Friends Life, with responsibility for running investment strategies for the annuities business, with-profits and unit-linked funds.	Expert in pension regulation, having worked at the Pensions Regulator; was heavily involved in the development of the Pensions Act 2004 whilst at the DWP. Former Head of Pensions at PwC Legal.	More than 25 years' experience in the insurance sector. Formerly CEO of National Westminster Life Ltd and UK CFO of Legal & General Group plc, he is a Fellow of the Institute of Chartered Accountants in England and Wales. He is a PIC Board member.	30 years' experience in bulk annuities and the insurance sector. Previously Corporate Development Director at Prudential UK and Director, Corporate Finance at PwC. Fellow of the Institute and Faculty of Actuaries.

KEY PERFORMANCE INDICATORS

PIC uses its key performance indicators to measure its performance in four main areas:

- Growth and overall value of the business, customer service, total shareholder returns, and scale and efficiency.
- Proven track record of growth across all metrics.

Embedded value
£m

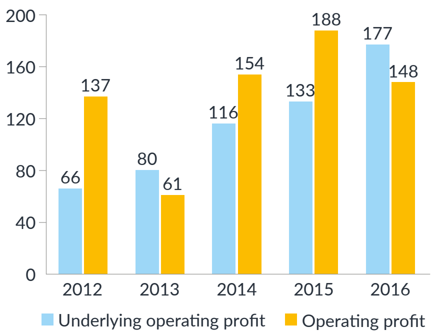


EMBEDDED VALUE

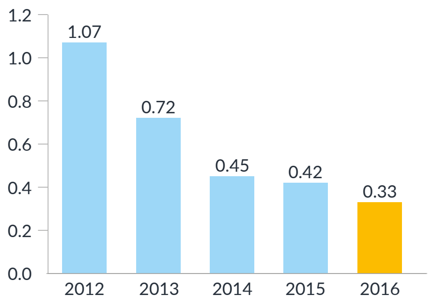
- Embedded value gives a snapshot of the value created to date and facilitates market comparisons.
- It is the key financial metric the Board uses to evaluate the progress of the business. This KPI is supported by the following two factors, which are not KPIs in and of themselves:
  - Change in embedded value split into operating and non-operating components explains how we have grown EV and demonstrates the repeatability of such growth (operating component) in the future, including new business contribution.
  - With effect from 1 January 2017 the Company has adopted the European Insurance CFO Forum market consistent embedded values principles[1] (MCEV principles) for its embedded value measurement and reporting. The Company intends to follow the MCEV methodology going forward, and will no longer prepare financial information under the EEV principles. PIC's MCEV for 2016 was £2,579 million.

Note:
1 Copyright © Stichting CFO Forum Foundation 2008.

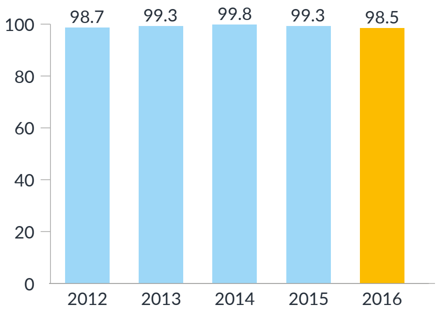
IFRS operating profits before tax
£m



Expenses as % of financial investments
%



Customer satisfied or better
%



OPERATING PROFIT

- Underlying operating profit evidences the translation of embedded value into reported profits.
- Underlying operating profit captures the returns made from the in-force book of insurance liabilities, and expected long-term returns from surplus assets.
- Growth of underlying operating profit/operating profit evidences the levels of growth we are achieving in building long-term profitability.
- Operating profit includes the immediate short-term impact of new business and reinsurance.

EXPENSE RATIO

- Expenses as a % of closing financial investments under management evidences how our cost base relates to our financial investments and hence our relative efficiency.

CUSTOMER SERVICE

- As well as the financial metrics as set out in the Annual Report and Accounts, the business also uses customer satisfaction as a key performance indicator. This is done by measuring:
  - % of customers surveyed who give PIC a satisfied or very satisfied rating, evidencing the quality of the service we have given; and
  - the number of complaints per 1,000 policyholders, which evidences how proactive our service is and the clarity and efficiency of our policyholder communications.

CUSTOMER SERVICE AND VALUES

TRUSTEE FEEDBACK

In December 2015 PIC was accredited with the Institute of Customer Service's (ICS) ServiceMark for outstanding customer service. PIC is the only company in the bulk annuity sector to have attained this distinction.

ServiceMark
Accredited from Dec '15 to Dec '18
The Institute of Customer Service

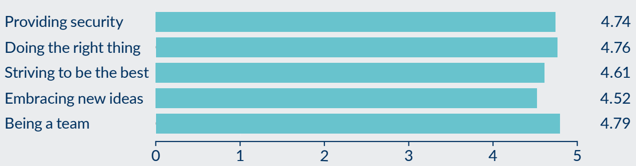
We continued our work with the ICS in 2016, when they carried out a survey of all PIC's trustee clients. We were rated on the three pillars of customer experience for buy-ins and buyouts – Trust, Price and Service.

The conclusions:

- "Excellent level of customer experience in the buy-in and buyout bulk annuity market."
- PIC was praised:
  - for its ability "...to complete buy-ins and buyouts in relatively short timescales if required, with two of our biggest deals completing in just six months, significantly shorter than others in the market."; and
  - for "...living up to expectations..." and "...living up to its corporate values... based on PIC's conduct during the transaction, transition and post-transition periods."
- Based on their experiences, our customers had a high level of trust in PIC.
- PIC was highly rated for professionalism and customer care.
- Every single one of the trustees who was interviewed for the survey was willing to recommend PIC to another trustee.

The PIC team is regarded as living up to its corporate values. Both trustees and advisers scored at least four out of five (where five is the maximum score) on each of the five corporate values based on PIC's conduct during transaction, transition and post transition. Trustees scored PIC as follows:

PIC living up to their values – ICS study



Case study

AON: REPEAT BUSINESS

In 2016 PIC concluded a pension insurance buy-in with the Aon Retirement Plan for a premium of around £900 million, covering pensioner liabilities across two sections of the segregated Plan.

PIC has previously concluded two buy-in transactions with a separate Aon-sponsored pension scheme, the Aon Minet Pension Scheme, in 2014 and 2012, for around £210 million and £100 million respectively.

This was the first sizeable pension insurance transaction under Solvency II, showing that large buy-ins priced under Solvency II remain an attractive option for trustees.

"We are very pleased to have been able to conclude this transaction at a time of considerable market volatility. By securing this buy-in asset we have taken a significant step in our long-term de-risking plan."

David Burton, independent Chair of Trustees

OUR VALUES

"HERE IS A COMPLEX BUSINESS EXERTING ENORMOUS ENERGY TO EMBRACE ALL OF ITS CUSTOMER GROUPS, ITS TRUSTEES, B2B, AND END USERS, WITH A VIEW TO DIFFERENTIATING THROUGH CUSTOMER SERVICE."

Institute of Customer Service, 2016

VALUING OUR CUSTOMERS

We value our customers (policyholders, trustees and sponsors) and work hard to provide high quality service. We listen to and we will be responsive to their needs, acknowledging the need for fair and sustainable commercial practices.

PROVIDING SECURITY:
The resilience to withstand even the harshest of economic storms

We're committed to managing risk and providing long-term stability and financial security for our customers. We respect boundaries and comply with regulations. Our strong, conservatively managed balance sheet ensures we have the resilience to withstand even the harshest of economic storms.

DOING THE RIGHT THING:
All weather friends

Every single one of our policyholders is our partner for life, which is why our strong ethos around doing the right thing is so important to us. Our policyholders must be able to trust us. So we live by a set of ethical principles and standards of behaviour and genuinely believe that fairness and honesty really count.

STRIVING TO BE THE BEST:
Leadership is second nature

We provide sector-leading expertise, operating at a level of excellence in everything we do. We listen carefully, strive to be the best and deliver a consistently high quality offering.

EMBRACING NEW IDEAS:
Adaptable enough to operate successfully in any environment

We pride ourselves on doing things differently, being adaptable enough to operate successfully in any environment and match any challenge. We go beyond existing ways of thinking to come up with innovative, personalised solutions.

BEING A TEAM:
Our nature? To nurture

We know the benefit of working together as a team. We respect, value and nurture our people both in terms of their development and engagement. And we're open to new ideas, perspectives and opinions.

POLICYHOLDER CARE

PIC's success in being chosen by our customers for buy-in and buyout transactions reflects not only our ability to price competitively and structure innovative insurance policies, but also reflects the excellence of our administration and transition teams

KEY STATISTICS

- The Company was responsible for paying the pensions of 134,900 individuals at 31 December 2016 (2015: 132,100).
- Payment of annuities grew by 24% in 2016 to £600 million (2015: £484 million).
- Total claim amounts paid were £797 million (2015: £581 million), an increase of 37% as the growth in annuities was supplemented by the growth in lump sum payments and transfers out compared to the previous year.
- At the end of 2016, PIC had 80,900 current individual policies in issue, in respect of 74 pension schemes, compared to 81,000 in respect of 64 schemes in 2015. The number of individual policies in issue reduced by 4,000 as a result of a winding-up lump sum exercise carried out during the year, whilst a number of individual policies were written as schemes converted to full buyout.

Excellent levels of customer satisfaction

Policyholder satisfaction is measured in a number of ways and is a key part of PIC's ongoing commitment to improving customer service:

- Member satisfaction levels are monitored via telephone and paper surveys.
- Monitoring of complaint levels and analysis of complaint root cause.
- Stringent oversight of administrators, such as:
  - monthly file and call review;
  - regular site visits; and
  - weekly operational catch-ups and formal monthly service review.
- Face-to-face feedback at our six policyholder events.
- Institute of Customer Service ServiceMark survey.
- All complaints reviewed by senior management and the Board.
- 98.5% of policyholders expressed overall satisfaction with our service and 86% gave us the maximum score.
- Complaints per thousand policyholders of 1.57 for the first half of 2016, and 1.45 for the second half of the year.

We have extremely high levels of policyholder satisfaction and have maintained over 98% satisfaction in the last three years.

Year	No. of respondents	Satisfied or better	Maximum score
2016	**6,590**	**98.5%**	**86%**
2015	6,250	99.3%	86%
2014	4,524	99.8%	87%

"EVERYTHING THAT WE HAVE DONE WITH YOUR COMPANY SINCE THE BUYOUT HAS BEEN ABSOLUTELY SUPER. YOU HAVE BEEN WONDERFUL PEOPLE TO DEAL WITH."

"YOUR ASSISTANCE AND THE WAY YOU DEALT WITH MY LITTLE PROBLEM MAKES ME BELIEVE THAT THERE REALLY ARE SOME VERY NICE PEOPLE OUT THERE IN THE BUSINESS WORLD."

"JUST LIKE TO THANK YOU FOR A WONDERFUL SERVICE AND ZERO WAITING TIME. MY GOODNESS, I WISH ALL HELPLINES WERE LIKE THIS."

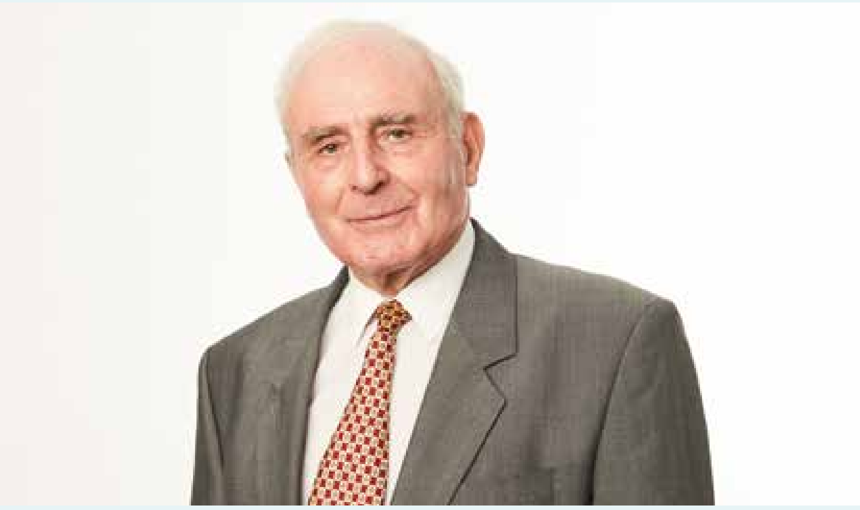
Feedback from PIC policyholders, 2016

The Institute of Customer Service

“PIC’S TRACK RECORD WITH BUY-INS AND ITS FOCUS ON DELIVERING TO TRUSTEES’ REQUIREMENTS WAS A BIG PLUS IN THEIR FAVOUR.”

Martin Couzens, Chairman of Alcatel-Lucent Pension Scheme (c.£100 million buy-in)

Case study



“MY PERCEPTION OF PIC IS THAT THE COMPANY IS VERY GOOD AT FOCUSING ON ITS CORE PURPOSE OF SECURING POLICYHOLDER BENEFITS.”

Tom Facer

TOM FACER

The Delta Pension Fund, of which I was a pensioner, was insured by PIC in 2008. I wasn’t concerned about the transaction because I had every confidence the trustees would have acted in the best interests of the members. I also wasn’t concerned that PIC isn’t a household name. Having had a personal pension plan with one well-known provider that lost a significant part of its value due to irresponsible management, whilst also having a bad experience with another well-known provider, I would have to say that household names do not have the same values as they once did.

My perception of PIC is that the Company is very good at focusing on its core purpose of securing policyholder benefits. I say this based mainly on the excellent presentations that are given by PIC’s senior management at the annual policyholder events, detailing PIC’s activities in the previous year and providing a financial update. They keep me fully informed of progress, whilst reassuring me that my pension is in safe hands. From knowing the safeguards that PIC applies, I have no concerns with regards to the security of my pension!

I did encounter one problem. Shortly after my Delta pension was transferred to PIC, my monthly pension payment did not go into my bank account on the appropriate date, which was obviously worrying! However, PIC acted quickly to correct the error and sent a letter of apology assuring me that such an error would not occur again.

True to such a statement I have not encountered any problems since. PIC exceeds my customer service expectations – and clearly has a desire to engage with its policyholders. Indeed, PIC is the only one of my five pension providers that holds events to meet policyholders. Such events make me feel a valued customer.

Tom Facer, former Delta Pension Fund member and now a proud PIC policyholder

SOLVENCY AND RISKS

> "PIC'S STRONG RISK CULTURE IS FIRMLY EMBEDDED ACROSS ALL DEPARTMENTS TO ENSURE THAT WE ARE ABLE TO PAY THE PENSIONS OF OUR POLICYHOLDERS."

Giles Fairhead, Chief Risk Officer, PIC

The overall financial strength of our insurance company is determined by our solvency position, our approach to managing risks and our ability to manage the assets and liabilities through the lifetime of each insurance policy. The key aspects of which are:

- A strong solvency ratio.
- Reserving assumptions which are suitably prudent.
- Capital focused solely on securing and managing pension liabilities.
- A disciplined risk management approach, where we focus our risk taking on those areas where we excel (investment risk) and seek to minimise unrewarded risks, for example interest rates and inflation, which are fully hedged and transferred.
- A secure and prudent investment approach, where our liabilities are closely matched by income streams from long-dated and secure assets.
- Active and proficient investor in the UK's infrastructure, including schools, hospitals, social housing and universities.
- An active approach to reinsurance of longevity risk, where we have reinsured 68% of our longevity exposure.
- Proven track record of successfully managing investments through volatile economic conditions.

The role of risk management at PIC

PIC has a strong risk culture. This is designed to:

- Protect the Company's obligations to policyholders and to always treat them fairly; and
- Seek to grow shareholder value through making informed risk-return based business decisions, resulting from a balanced awareness of the opportunities and threats. Critically, the Company will only seek to take on risks which it has the capability to understand and manage.

Our risk management approach is designed to support our business ambitions and has the following core objectives:

- To define the risks that we are able and willing to accept that can give us sustainable returns, and to set out risks we believe are unrewarded and require closely managing.
- To optimise the capital that we hold so that we can deliver our strategy.
- To provide a framework within which authority for taking risks can be appropriately delegated and controlled throughout the organisation. This enables the Board to draw assurance that the risks to which we are exposed are being appropriately identified, managed and, where necessary, minimised.
- To ensure we remain forward thinking in assessing what could happen to the business and what actions could be taken to manage or mitigate the risks.
- Effective risk management is integral to our success and is embedded through the organisation.

PIC's risk profile differs from that of a typical defined benefit pension scheme in a number of areas:

- PIC does not hold any equity shares in its portfolio.
- Tightly managed interest and inflation rate risk – reduced through assets and hedging overlays.
- Mitigated longevity risk – reduced through reinsurance.
- Granular full-term cash flow matching of assets and liabilities.

Political/legislative risk

- Political scrutiny of the defined benefit pension schemes rose during 2016, with BHS and the British Steel Pension Scheme bearing particular focus.
- In response to this, in early 2017 the Government published a consultation on the future of defined benefit pension schemes.

Longevity risk/reinsurance

Under Solvency II longevity reinsurance generally plays a more significant role in the business model of many UK annuity writers, as longevity reinsurance enables firms to reduce both their solvency capital requirements (SCR) and their risk margin (RM) for the longevity risks which have been transferred.

Prior to Solvency II, PIC was perhaps the most active reinsurer of longevity risk, having first reinsured longevity exposure in 2008. However, in response to Solvency II, a number of other insurers active in the bulk annuity sector have sought to increase the amount of longevity risk they reinsure.

In response, we have seen an increase in the number of global reinsurers who are now willing to transact with us, resulting in a growing pool of active reinsurers who we regularly speak to about future transactions.

The reinsurers with which PIC currently has longevity swap reinsurance contracts are Hannover Rück SE, Munich Reinsurance Company, Pacific Life Re Limited, Prudential Insurance Company of America, Canada Life Assurance Company and RGA Global Reinsurance Company Limited. In addition, PIC has entered into a number of tail-risk quota share arrangements with Berkshire Hathaway Life Insurance Company of Nebraska, a US-regulated insurer.

All transactions have appropriate collateral arrangements in place to manage PIC's credit exposures.

Case study

LONGEVITY REINSURANCE

In June 2016, Prudential Insurance Company of America (PICA), completed a longevity reinsurance transaction with PIC.

This is the third transaction we have completed with PICA and covered longevity risk associated with pension liabilities amounting to approximately £1 billion for around 2,900 pensioners across two sections of the Aon Retirement Scheme.

"This deal truly demonstrates that large buy-ins priced under Solvency II are still an attractive option for trustees," said Bill McCloskey, vice president, longevity reinsurance at PICA.

"This was a keenly contested process, showing continued strong demand for Pension Insurance Corporation reinsurance tenders," Khurram Khan, Head of Longevity Risk for Pension Insurance Corporation, said. "We are pleased to have placed the longevity cover within a short period."

SOLVENCY AND RISKS

Continued

Risks and uncertainties	Trend and outlook	Mitigation
Political risk – political and/or regulatory intervention.	BHS, British Steel, Openreach and other headline-making stories from 2016 ensure that DB pensions remain high on the political and regulatory agenda. Uncertainty around political priorities was highlighted by the drive for, and then abandonment of, the secondary annuities market. In early 2017 the Government published a consultation on the future of defined benefit pension schemes. The Treasury Select Committee is undertaking a review of the Solvency II regulations in the context of the decision to leave the EU.	PIC maintains an open dialogue with regulators and policymakers, and closely monitors regulatory and legislative developments. Regular horizon scanning helps identify key risks to best position PIC's strategy.
Market risk – impact of market and/or economic volatility on PIC's capital position.	Uncertainty and volatility in the global financial markets is expected to continue. This reflects uncertainty around the UK's future relationship with the EU, changing political trends across the world and threats to global trade/a rise of protectionism. PIC remains exposed to residual model risk should experience diverge from expected outcomes.	Close management of PIC's balance sheet, such that the Company actively hedges its balance sheet against adverse movements in financial markets. The models used for assessing and managing the risks on PIC's balance sheet are subject to a rigorous governance and control environment.
Economic risk – prolonged low interest rates may result in a drag on PIC's capital position.	Low interest rates increase the present value of the Solvency II risk margin (see Glossary). The risk margin calculation is complex and results in a capital requirement that is very sensitive to interest rates.	Hedging helps protect the overall capital position against adverse movements in interest rates. However, the costs associated with protecting the capital position in a prolonged low interest rate environment may impact PIC's profitability.
Default risk – on credit/debt assets in the portfolio.	While PIC has historically experienced low levels of default in the portfolio (see page 38 for historic experience), this risk continues to be significant given the growth of our balance sheet and the increased volatility of financial markets.	PIC selects and monitors its investment holdings very closely, either directly or through high quality external managers. £1.1 billion provision held for defaults and downgrades in addition to solvency capital requirements.

Risks and uncertainties	Trend and outlook	Mitigation
Counterparty risk – the possibility of failure by our reinsurance and swap counterparties who are contracted to honour their obligations in a timely manner.	The move to Solvency II and the increased volatility in the financial markets has increased the importance of third party risk transfers, for example of longevity risk.	PIC only transacts with highly rated reinsurance counterparties, and also includes collateral provisions to improve overall security, for example interest rate swaps, which are fully collateralised on a daily basis.
Longevity risk – PIC's insured policyholders may live for longer than was originally assumed when pricing new business.	PIC is exposed to factors that may lead to increases in life expectancy, such as improvements in medical science beyond those anticipated.	PIC regularly reviews its longevity experience to ensure assumptions remain appropriate, and continually seeks to enhance its understanding of the evolution of annuitant mortality. PIC aims to reinsure more than 60% of its longevity risk exposure. As at 31 December 2016, PIC had reinsured 68% of its total longevity exposure.
New business risk – business is written for a price which fails to generate an appropriate risk-adjusted return in line with our strategic objectives. This may lead to reduced profits, or even a financial loss.	PIC's specialisation and historical experience in the bulk annuity sector gives the Board and management comfort that this risk can be managed within risk tolerances.	PIC ensures that any new business meets risk appetite criteria, and that all assumptions that go into the new business quotation process are subject to rigorous governance and control.
Cyber risk – the financial services sector is increasingly becoming a target for "cyber-crime". This might include the risks that third parties may seek to disrupt PIC's operations, steal personal data or perpetrate acts of fraud.	The drivers of this risk continue to evolve rapidly as technology is changing the way firms do business and society operates. The financial services sector has seen a significant increase in the number of attempts by third parties to seek and exploit vulnerabilities in IT systems.	PIC maintains a robust IT environment to ensure protection of its data and security of its systems and those of outsourced or third parties that we work with. PIC works with its business partners to maintain controls and proactively address emerging threats. The IT environment is regularly tested internally and externally to maintain up-to-date awareness of the latest threats and how these may impact PIC.

FINANCIAL RESULTS SUMMARY

Continued strong growth in financial investments and underlying operating profit

"THE SOLVENCY RATIO STOOD AT 164% AT THE END OF THE YEAR, REFLECTING £500 MILLION OF NEW CAPITAL AND CAREFUL BALANCE SHEET MANAGEMENT."

Rob Sewell, Chief Financial Officer, PIC

At year end 2016, PIC's IFRS underlying operating profit before tax was £177 million (2015: £133 million).

PIC recorded operating profit before tax of £148 million (2015: £188 million) and IFRS profit before tax of £276 million (2015: £104 million).

During the year PIC insured 17 (2015: 13) pension funds with a total premium value of £2.6 billion (2015: £3.8 billion).

PIC now has £4.3 billion of assets held in excess of best estimate liabilities.

PIC concluded two longevity swap reinsurance transactions during the year covering longevity risk on c.£1.4 billion (2015: £3.8 billion) of insurance liabilities. At 31 December 2016, 68% of PIC's total longevity exposure on a regulatory solvency basis was reinsured to third party, investment grade reinsurance counterparties (2015: 71%).

New business transactions, together with costs incurred, and the reinsurance deals concluded during the year, initially resulted in a charge of £26 million (2015: profit of £59 million) to operating profits.

Market movements had a significant impact on financial assets, with interest rate movements partially accounting for an uplift in the size of the portfolio. Other factors to increase the overall portfolio include inflation rate movements and movements in credit spreads. Derivative assets and derivative liabilities have grown significantly since 31 December 2015. This largely reflects changes to the Company's interest and inflation hedging approach due to Solvency II. The net derivative position has increased from £(0.7) billion to £(1.3) billion, due mainly to currency movements following the Brexit referendum.

Other operational highlights

Embedded value (EV) was £2,567 million at year end 2016 (2015: £1,856 million). PIC's EV has grown by more than 200% over the past four years. The increase in EV since December 2015 of £711 million, or 38%, reflects the beneficial impacts of new business written during the year, the in-force business contribution, the issue of new share capital, and the positive impacts of investment market movements, offset by the increase in the cost of capital.

From 1 January 2017 the Company has adopted the European Insurance CFO Forum market consistent embedded values principles (MCEV principles), and has aligned the calculation approach to the recently introduced Solvency II regulatory regime. The Company's MCEV at 31 December 2016 was £2,579 million, compared to £2,567 million under the existing approach.

PIC had total financial investments of £22.6 billion (2015: £16.6 billion). PIC's financial assets have grown by more than 36% since 2015 as a result of new business transacted, capital raised and market movements.

Continued strong performance

Underlying operating profit before tax	**Increase on 2015**
£177m	**+33%**
New business premiums	**Decrease on 2015**
£2,598m	**-31%**
Financial investments	**Increase on 2015**
£22.6bn	**+36%**
Assets held to meet future pension payments and expenses	**Assets held to meet solvency and risk margins**
£17.3bn	**£4.3bn**
Embedded value	**Increase on 2015**
£2,567m	**+38%**

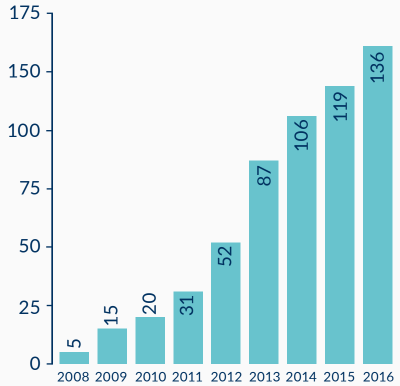
FINANCIAL RESULTS SUMMARY

Continued

PIC's financial track record – continuous growth

Number of pension schemes insured (cumulative)

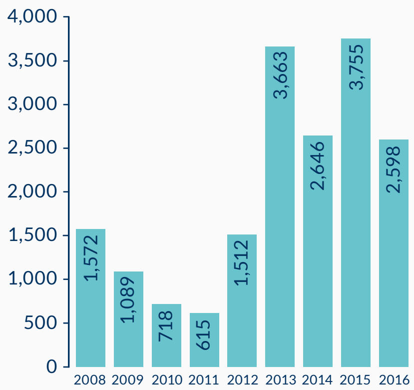
136 with 17 insured in 2016



New business premium (£m)

Premiums

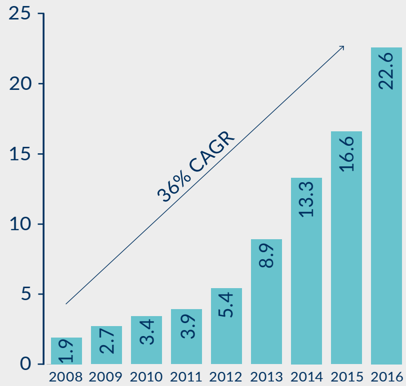
£2,598 million



Financial investments (£bn)

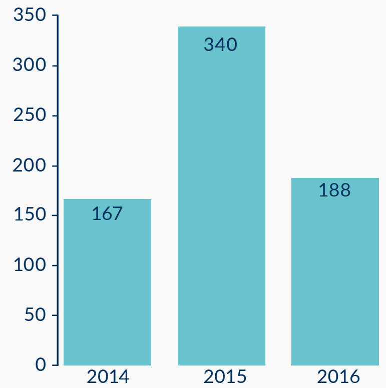
Financial assets

£22.6 billion

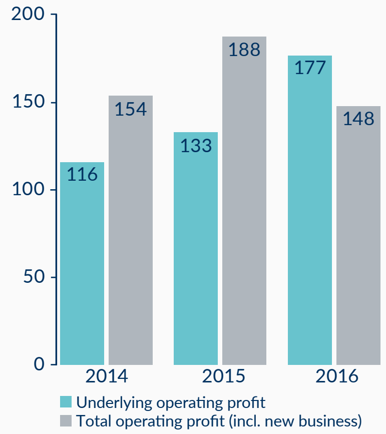


PIC's financial track record – significant value generation

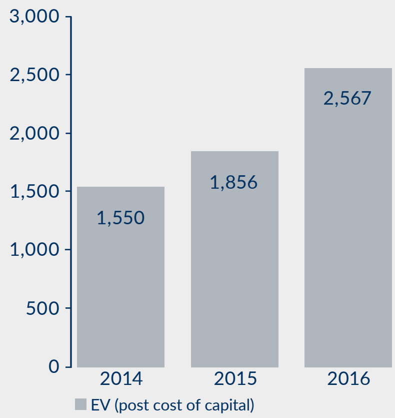
New business value (post tax) (£m)
£188 million



IFRS operating earnings before tax (£m)
Operating profit
£177 million



Embedded value (post cost of capital) (£m)
£2,567 million



- Underlying operating profit reflects stable emergence of profits from in-force (i.e. if no new business was written).
- Total operating profit includes impact from new business and reinsurance.
  - New business profits can be positive/negative at day one IFRS earning subject to mix of plans acquired.
  - IFRS non-operating profit can be further impacted by short-term fluctuations in investment return, model and assumption changes and non-recurring expenses.

FINANCIAL RESULTS SUMMARY

Continued

- Profits generated from release of prudent margins for business written in previous years.

- Return on shareholder funds based on long-term investment return assumptions.

- Profit depends on mix of plans acquired.
- New business written to target IRRs.
- Prudent margins and capital released over life of contract.
- Creates VIF asset, resulting in increased EV.
- Emergence of future profits de-risked through hedges and reinsurance.

- Short-term fluctuations in investment return, model and assumption changes and non-recurring expenses.

IFRS operating profits

£m	2016	2015
Return earned on insurance book	**122**	87
Return earned on surplus assets	**55**	46
Underlying operating profit	**177**	133
New business and reinsurance operating profit	**(26)**	59
Other changes to in-force business	**(3)**	(4)
Operating profit before tax	**148**	188
Non-operating profit/(loss) before tax	**128**	(84)
IFRS profit before tax	**276**	104

IFRS balance sheet

£m	31 December 2016	31 December 2015
Assets		
Investment properties	**97**	96
Reinsurers' share of insurance liabilities	**2,522**	1,917
Receivables and other financial assets	**216**	182
Prepayments	**34**	74
Financial investments	**22,594**	16,613
Derivative assets	**9,320**	4,900
Cash and cash equivalents	**6**	12
Total assets	**34,789**	23,794
Equity		
Share capital	**1,000**	757
Other reserves	**60**	60
Retained profit	**700**	479
Total equity	**1,760**	1,296
Liabilities		
Gross insurance liabilities	**21,741**	16,480
Borrowings	**542**	295
Deferred tax liability	**4**	5
Derivative liabilities	**10,654**	5,635
Insurance and other payables	**38**	53
Current taxation	**32**	15
Accruals	**18**	15
Total liabilities	**33,029**	22,498
Total equity and liabilities	**34,789**	23,794

PIC Solvency II ratio

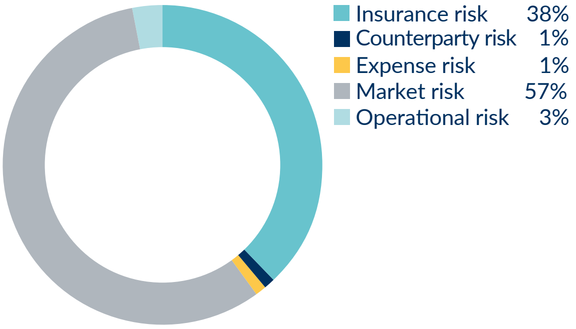
£m	2016	2015
Net assets held in excess of best estimate liabilities (BEL)	**4,256**	2,802
Risk margin net of transitional relief	**(1,122)**	(432)
Own funds	**3,134**	2,370
Solvency capital requirement (SCR)	**(1,912)**	(1,574)
Solvency II surplus funds	**1,222**	796
Solvency ratio	**164%**	151%

Key Solvency II sensitivities

- **PIC maintains various management tools to mitigate the impact of market fluctuations and manage its capital position.**
  - Pricing applied to new business and control of new business volumes.
  - New business only transacted provided it meets the Company's return on capital targets.
- **Hedging strategy structured to protect regulatory Solvency II balance sheet.**
  - Interest rate, inflation and FX risk is hedged to manage Solvency II balance sheet.
  - Longevity risk is managed through reinsurance where majority of risk is transferred.

PIC sensitivity of Solvency II ratio to changes in assumptions (£m)	Change in solvency ratio
As at 31 December 2016	**164%**
25bps increase in interest rates	5.7%[1]
25bps reduction in interest rates	(5.9)%[1]
£100 million credit default (no recovery)	(5.7)%
5% reduction in base mortality rates[2]	(8.0)%[1]

Solvency II SCR by type of risk



Notes:
1 After recalculation of transitional relief.
2 Equivalent to a 0.5 year increase in life expectancy from 23.5 years to 24.0 years for a typical male aged 65.

FINANCIAL RESULTS SUMMARY

Continued

Solvency II and IFRS balance sheets

Underlying position

£4.6 billion[1]
Assets available to back risk and solvency margins plus anticipated prudent margins

Solvency II representation

£3.1 billion
Own funds

£1.1 billion
Assets allocated to covering the risk margin net of transitional relief

£0.4 billion
Prudent margins in Solvency II best estimate liability

IFRS representation

£1.8 billion
Net asset value
(historical net profits and capital injections)

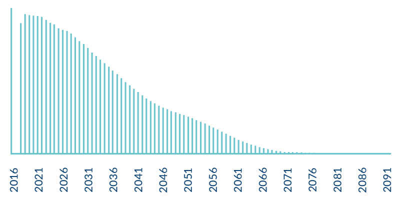
£2.2 billion
Assets backing prudent margins to be recognised in future profits

£0.6 billion
Debt repayment

Underlying value unchanged by IFRS or Solvency II representation

- Under both Solvency II (own funds) and IFRS (NAV) only a portion of the profits that will ultimately flow to shareholders are recognised at the balance sheet date. The remainder will be recognised in the future as prudent or risk margins run off.

Future profits from in-force book



Note:
1 After deducting £0.2 billion provision for deferred tax on the Solvency II balance sheet.

EEV balance sheet

Embedded value

Embedded value of PIC (£m)	**31 December 2016**	31 December 2015
Free surplus	**446**	289
Required capital	**1,235**	938
Adjusted net worth	**1,681**	1,227
Value of in-force business after tax	**1,329**	965
EV before cost of capital	**3,010**	2,192
Cost of capital	**(443)**	(336)
EV net of cost of capital	**2,567**	1,856

Analysis of movement in embedded value

Change in embedded value (£m)	**31 December 2016**	31 December 2015
Opening embedded value	**1,856**	1,550
Operating profit		
– New business contribution	**188**	340
– In-force business contribution	**97**	3
Sub-total	**285**	343
Investment variances	**292**	(108)
Other economic variance	**7**	63
Non-operating profit	**299**	(45)
Change in EV pre-cost of capital and capital investment	**584**	298
Change in cost of capital	**(107)**	(74)
Capital injection	**243**	65
Fair value of debt movement	**(9)**	17
Closing embedded value	**2,567**	1,856

MCEV

With effect from 1 January 2017 the Company has adopted the European Insurance CFO Forum market consistent embedded values principles (MCEV principles) for its embedded value measurement and reporting. The Company intends to follow the MCEV methodology going forward, and will no longer prepare financial information under the EEV principles.

31 December 2016 (£m)	Solvency II balance sheet	Allow for sub-debt	Recognise the frictional cost of required capital	Release RM DTL net of transitional, recognise cost of non-hedgeable risk	Release MA margins	Tax on future profits	MCEV
Assets	21,577						
BEL	(17,321)						
Risk margin and deferred tax liability (DTL), net of transitional relief	(1,122)						
Solvency II own funds	**3,134**						**3,134**
PVFP				1,122	361	(431)	1,052
CRNHR				(885)			(885)
FCoC			(161)				(161)
Subordinated debt		(561)					(561)
MCEV							**2,579**

Methodology overview:

Adjusted net worth

This is equal to the unadjusted own funds under Solvency II.

Present value of future profits (PVFP)

There are certain regulatory margins within the Solvency II own funds which, in a "best estimate" scenario, are expected to be released to shareholders as free capital over time.

These regulatory margins principally relate to prudence within the liability discount rate (also known as the fundamental spread), and the risk margin (net of any adjustment for the impact of transitional measures on the own funds). The present value, after tax, of the future release of these regulatory margins is equal to the "present value of future profits".

Frictional cost of required capital (FCoC)

The minimum amount of regulatory capital the Company expects to hold (the required capital) is equal to 130% of the solvency capital requirement. There is a cost associated with the assets used to support this, principally in respect of investment management fees and tax on investment income. This cost is captured as the "frictional cost of required capital".

Cost of residual non-hedgeable risks (CRNHR)

Under the MCEV methodology allowance is made for the cost of holding capital in respect of non-hedgeable risks. Market risks are assumed to be hedgeable and so no cost is allowed for any capital that might be held under the regulatory solvency regime. Longevity risk is treated as hedgeable but only to the extent that the risks have actually been hedged, typically using reinsurance. Longevity risk that has not been reinsured at the balance sheet date is treated as non-hedgeable for the purpose of calculating the cost of non-hedgeable risks.

Subordinated debt

The Company has raised a total of £550 million in subordinated debt, which counts as Tier 2 capital for regulatory purposes. As the expectation is that this debt will be fully paid at maturity, then the fair value of the debt is recognised for MCEV purposes.

Key MCEV assumptions:

The most significant ones are:

- Economic matching adjustment (MA) is similar to the Solvency II matching adjustment but with a more realistic view on the cost of default and downgrade. It is set at 15bps above the MA used for Solvency II at 2016 year end. This assumption is driven by the actual asset spread, net of the expected cost of default and downgrade.
- Cost of residual non-hedgeable risks is an allowance for the cost of the risks which cannot be readily hedged in a liquid market. In MCEV calculations the following categorisations are made for the risks:
  - We have assumed that longevity reinsurance is not a readily available hedge for insurance risk, hence this is included within CRNHR calculation.
  - We treat all market-related risks as hedgeable or having symmetric impact on shareholder value.
  - For longevity risk, if we were to assume that pensioner longevity risk is hedgeable, this would increase embedded value by £158 million. If we additionally treated unreinsured deferred longevity risk as hedgeable, this would increase the embedded value by a further £620 million.

Other differences between Solvency II and MCEV assumptions relate to:

- subordinated debt, which is treated as Tier 2 capital under Solvency II, is recognised at fair value for the purposes of embedded value;
- SCR, which is released over time and is replaced with FCoC for MCEV; and
- risk margin, which is released over time and replaced with CRNHR, with a cost of capital rate of 3.2%.

ASSET AND LIABILITY MANAGEMENT

"We have always taken an approach to investing that we like to call the weatherproofing strategy."

Rob Groves, Chief Investment Officer

The big theme of the year was without doubt political risk leading to volatility and instability in financial markets. It was also a year of furious debate about the accuracy and reliability of forecasting the economic and financial repercussions of specific risk events. I think it is fair to say that many prognosticators have been found wanting. By contrast, we have always taken an approach to investing that we like to call the weatherproofing strategy.

We don't try and forecast the outcome or likelihood of specific events. PIC has a low-risk investment portfolio that provides a steady stream of high quality cash flows that match, over the next 50 years or so, the payments that we have to make to our policyholders. We have built a talented investment team with the expertise and experience to position the portfolio to manage tail risks.

In practice, this means investing in government bonds and investment grade debt issued by strong companies which we believe will continue to pay these cash flows, even when growth is weak. We are broadly indifferent to market volatility because both sides of our balance sheet (assets and liabilities) move in tandem. We also hedge out risks we don't want to be exposed to, such as inflation and interest rate risk. So during 2016, when inflation expectations rose, credit spreads tightened and long-term interest rates fell, our portfolio actually increased over and above PIC's new business in-flows by about £3 billion. Contrast this with the very many unhedged DB pension funds which saw their deficits surge because of these same movements.

I am delighted to say that this strategy brought us through 2016 with flying colours. Our portfolio is strong, resilient and yet flexible enough to allow us to react to events in the market should we feel the need. It is also growing quickly. At year end 2012, PIC had assets of under £6 billion. At year end 2016, we had assets amounting to £22.6 billion, a compound annual growth rate of about 43% over the past four years.

The main issue for us is finding enough suitable assets to invest in that fall within our risk appetite. It is therefore disappointing that UK corporate debt issuance remains so thin. However, by looking further afield we invested quite heavily in US corporate bonds, where the market is both deeper and more liquid and provides the opportunity to add diverse names to the portfolio.

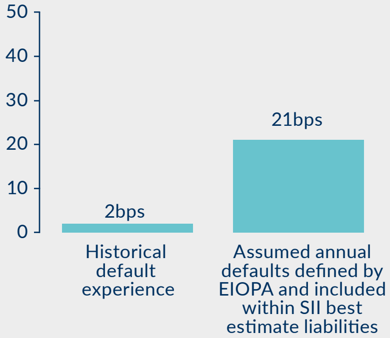
We have also built an internal team which has developed considerable experience and an exceptional track record in sourcing and investing directly into infrastructure debt. Today, we have about 30%, or just over £7 billion, of our portfolio invested in what we broadly term infrastructure. A significant percentage of this has been invested by our in-house team through bilateral deals with borrowers such as housing associations, universities, Project Finance and regulated utilities. These types of investments, because they are bilaterally negotiated, can give a higher risk-adjusted credit spread versus the market and can be tailored to match specific liabilities. This is very capital efficient and helps to better hedge the risks on our book.

The main residual risks in the portfolio, given our heavy exposure to corporate debt, are those of default or downgrades. The Regulator ensures we budget for both scenarios and, as the chart below demonstrates, our historical experience on both is excellent.

We are confident that our tightly managed portfolio will continue to perform, whatever 2017 throws at us.

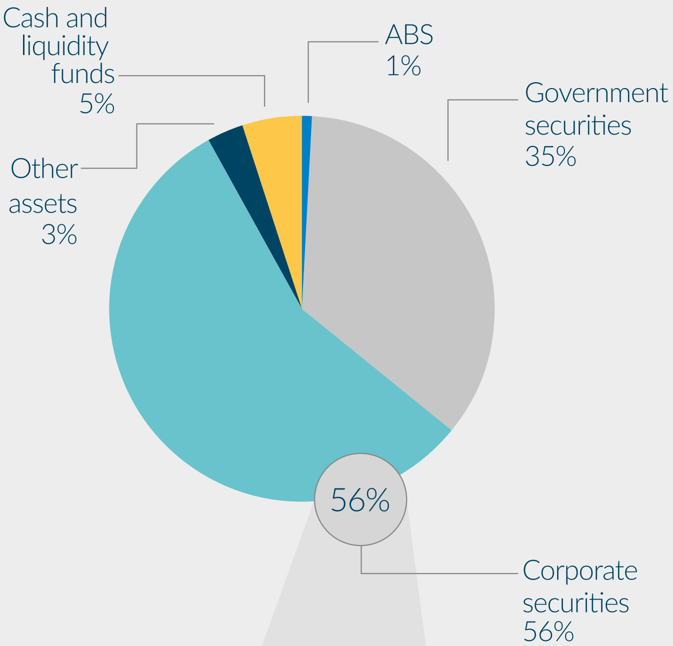
Historical default experience

bps per annum



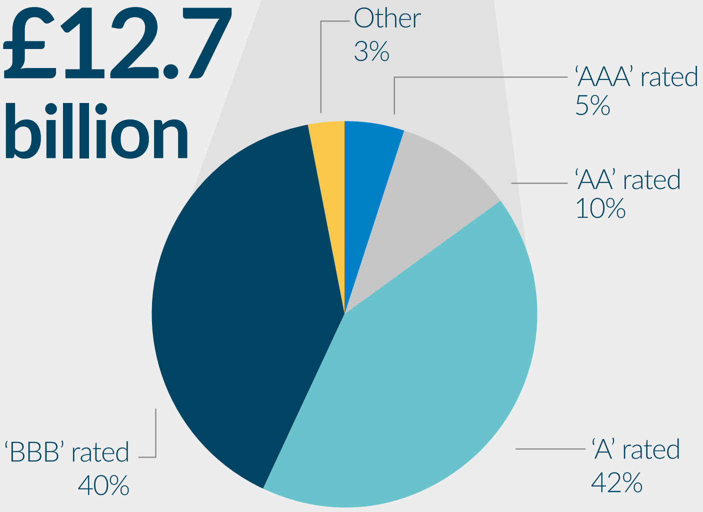
Asset portfolio by asset class (31 December 2016)

£22.6 billion



Corporate securities by rating

£12.7 billion



PORTFOLIO HIGHLIGHTS

- 91% of financial investments in government and corporate securities.
- Corporate securities: 97% investment grade rated.
- No single counterparty (excluding UK government) represents more than c.1.68% of total investment assets.
- 53% of financial investments managed by external asset managers.
- 47% of PIC's total investment assets managed directly, including UK gilts, supranational bonds, and debt private placements.
- Investment strategy designed for long-dated assets to match long-dated liabilities.
  - Discount rate applied to liabilities is set based on the asset portfolio yield net of adjustments for expected defaults and downgrades.

	31 December 2016	
Country	Market value (£m)	%
UK	5,382	42.5%
US	4,558	36.0%
Europe	1,582	12.5%
Rest of the world	1,145	9.0%
Total	**12,667**	**100.0%**

ASSET AND LIABILITY MANAGEMENT

Continued

PATIENT CAPITAL: INVESTING FOR POLICYHOLDER SECURITY AND ECONOMIC GROWTH

With non-callable pension obligations that stretch out decades into the future and a growing portfolio, PIC is the natural partner for investments that provide secure long-dated cash flows, such as infrastructure. Our business moves capital efficiently through the economy, from generally sub-scale defined benefit pension funds into infrastructure investments which support jobs and growth, as well as benefitting future generations. Our scale and expertise allow us to do this more effectively than the majority of pension funds.

We are now playing a role of real importance to the UK economy by filling the hole that has been left by the withdrawal of the banks from this space, investing in everything from social housing and university accommodation to the Thames Super Sewer ("Tideway").

We have worked hard to develop innovative, secure lending structures that accommodate quite specific requirements, such as deferred draw-down profiles, which reduce the cost of carry. These offer flexibility to borrowers, such as housing associations, and provide certainty of funding whilst reducing the cost of carry. They are not, however, facilities which every institutional investor is able to accommodate.

We have ambitious plans to partner with borrowers such as housing associations in 2017 and beyond and look forward to developing innovative structures that meet borrowers' needs whilst matching our liabilities.

We apply a strong governance framework to oversee these investments.

Case study

TIDEWAY

In 2016, PIC invested £100 million in debt secured on the Thames Tideway Tunnel, the 25km tunnel underneath the River Thames in London. This was an innovative investment which required much hard work before the deal was signed. The key aspects of the transaction:

a. The £100 million size of the transaction was split across four tranches.
b. There is a long deferral period (four to five years), providing certainty of funding cost for the borrower, but reducing cost of carry, with an unusual feature of no funding drawn on day one to help match the cash flow needs of the construction works.
c. There is a unique inflation linkage, whereby this is the first transaction with inflation linkage with such a long deferral period.
d. The maturity profile has been sculpted to match PIC's long-dated liabilities, a feature which also benefits the borrower as they require long-dated funding.

Case study

MHS HOMES

In 2016, PIC invested £40 million in secured debt issued by mhs homes, a social housing provider based in Kent. One of the largest independent landlords in Kent, mhs homes owns and manages more than 8,500 homes in Medway, Maidstone and Dartford.

Key aspects of the transaction:

- £40 million private placement, drawn in two stages over the next two years, giving mhs homes certainty of funding costs, whilst reducing the cost of carry.
- Funding to help provide more than 400 new properties.
- 34-year maturity (April 2050), to match PIC's liabilities.
- Secured on social housing properties.

"This funding will help provide over 400 new properties in Medway and surrounding areas. The flexible arrangements agreed with PIC meet the requirements of our business plan and provide the long-term funding to match our aspirations."

Bruce Shelmerdine, Finance Director at mhs homes

Building long-term relationships – how PIC's investment benefits the community

Investment from PIC	Housing provider	Wider community impact
£40 million	400+ homes provided	48 work experience placements 15 apprentices 56 residents into employment

EMPLOYEES

"PIC enjoys a history of staff retention with low turnover."
Institute of Customer Service

"I AM VERY PROUD TO WORK AT PIC... I LIKE WORKING FOR A COMPANY THAT IS HIGHLY REGARDED IN THE MARKET, BOTH FOR THE QUALITY OF ITS PEOPLE AND ITS SERVICE EXCELLENCE. I LIKE THAT EVERYONE IS WORKING TOWARDS A COMMON GOAL..."

PIC employee, December 2016

The skills, knowledge and experience of our people are critical to the success of the Company. We therefore seek to recruit and retain the very best people who are not only able to be innovative and flexible, but who also understand that the customer is at the heart of everything we do.

In order to sharpen that focus, the Company has a flat structure, with short reporting lines, modern systems and processes, and an open, entrepreneurial culture. This allows us to react quickly to customer needs. Alongside active mentoring for actuarial students, a Talent Management programme, flexible working and a generous staff benefit package, PIC is also keen to allow employees to take pride of ownership in the business, and, as such, we operate a Save As You Earn scheme (see page 43). As a result of this environment, our staff members have been with the Company for an average of four and a half years and 90% feel proud of working at PIC.

In Q4 2016 PIC ran an employee survey to gather the views of employees, measure employee satisfaction, understand how well our values have been embedded and provide a roadmap to help us achieve high levels of performance and drive business results.

The feedback from the survey was used to enable PIC to benchmark employee opinion against other comparable organisations. PIC achieved an employee engagement score of 78% (putting it in the top quartile of UK companies) and an employee enablement score of 83% (putting it in the top decile of UK companies).

Case study

Amy Liu *(right)* and colleague, Elizabeth Cain

AMY LIU

"I have worked at PIC for just over three years, joining as an intern after university. I was interested in PIC due to the size of the organisation and relatively flat hierarchal structure which meant that there would be many opportunities to learn and be exposed to different aspects of the business. I was delighted to be offered a full-time position after starting as an intern and really appreciate the overflowing support and opportunities given to me and other actuarial students to build a successful career.

One of the best things about working at PIC is being able to share in the success of the Company through taking part in the SAYE scheme.

I am really happy at PIC and see myself working here for some time. Working here has more than lived up to my expectations!"

Amy Liu, Actuarial Analyst

"WE HAVE WORKED HARD AT PIC TO ENSURE WE HAVE A STRONG CULTURE. AND WHEN WE THOUGHT BACK TO WHY THAT IS THE CASE, IT CAME DOWN TO ONE THING – OUR CULTURE COMES FROM A DEEP-ROOTED SENSE OF PURPOSE."

Tracy Blackwell, CEO

"92% OF EMPLOYEES WOULD RECOMMEND PIC AS A GOOD PLACE TO WORK – A RATING WHICH IS SIGNIFICANTLY ABOVE ALL BENCHMARKS."

Ben Hubbard, Director EMEA, Insight™ Division, Korn Ferry Hay Group

Employee feedback	Corresponding value
95% of employees believe PIC is customer focused (always seeking to understand and meet customer needs).	"Valuing our customers" is PIC's core value and something the Company spends a lot of time and effort working on. PIC works hard to ensure that employees are given the tools and are empowered to address customer needs. Almost all employees also agree that PIC provides a high quality customer service experience.
90% of employees feel proud to work for PIC.	"Doing the right thing". This result clearly demonstrates that a good understanding of the values and a focus on purpose, brings pride. Employees expressed very high levels of trust and confidence in the senior leadership team.
92% of staff would recommend PIC as a good place to work.	"Being a team" and "Embracing new ideas". Employees overwhelmingly responded that management shows care and concern for the wider team; and that they have opportunities to have their ideas adopted and put into use. Employees also agreed that the benefits provided by PIC are competitive.
98% of employees believe that PIC will be successful over the next two to three years.	"Striving to be the best" and "Providing security". Employees have a demonstrable understanding of PIC's purpose, strategy and focus on the customer. The overwhelming feedback was that PIC is effectively managed and well run.
94% of employees said they have a good understanding of PIC's values.	Our values are integral to the way that we work. Every effort is made to hire those individuals who are alive to the importance of organisational purpose, culture and the values which flow from this.

Save As You Earn

PIC offers employees the opportunity to acquire shares in the Company through a Save As You Earn scheme. This is unusual for a private company, but it is designed to develop pride of ownership, laying the foundations for a sustainable and successful company for many years to come. Launched in 2013, more than 70% of PIC staff have joined the scheme, demonstrating their belief in the future prospects of the Company and aligning their interests more closely with those of other stakeholders.

Employee benefits

Part of what keeps our employees motivated is the wide range of benefits, which include:

- generous pension contributions;
- private medical cover;
- season ticket loan;
- Company-sponsored events (including a discretionary weekend away as a reward for our staff and a thank you to their families for the support given over the year); and
- travel insurance.

A pool table in the office and well-stocked snacks cupboard keep the team happy while in the office.

CORPORATE GOVERNANCE STATEMENT

> "PIC'S BOARD COMMITTEES ARE DEEPLY INTEGRATED INTO THE DAY-TO-DAY RUNNING OF THE COMPANY."

Jon Aisbitt, Chairman

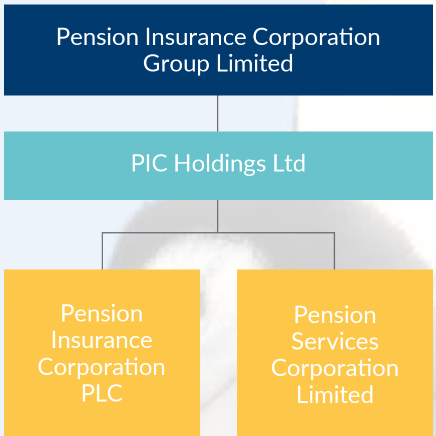
I am delighted to introduce what will be an annual PIC corporate governance report. Although I was only appointed Chairman in October, I attended Board meetings from July onwards, so had a good overview of the Board processes and structures in place. It was immediately clear to me that PIC's Board and governance structures were well developed under Sir Mark's Chairmanship, with strong oversight of the Company's activities. It was also clear that the Directors are committed, experienced and engaged and regularly challenge the management team.

As you can see from the Group Company structure chart, PIC is organised in a straightforward fashion. PIC's ultimate parent, Pension Insurance Corporation Group (PICG), is incorporated in the UK. PIC is the main operating subsidiary of PICG. Pension Services Corporation Limited is the Group's services company, employing all employees, but does not conduct any business itself.

PIC is managed by a Board of Directors (the "Board"), which at 31 December 2016 consisted of 13 members, a majority of whom are independent.

PIC's Board Committees are deeply integrated into the day-to-day running of the Company. For example, the Origination Committee oversees new business and reinsurance strategy, as well as reviewing and approving pricing for large deals. In 2016, the Risk Committee oversaw the transition of the business into the Solvency II regime, and the ALM Committee oversees PIC's asset management strategy.

It is therefore very positive that members of the Board have such a wide array of skills and expertise. I am delighted to have taken on this role as Chairman of PIC and I look forward to working with the Board as the Company secures increasing numbers of UK pension scheme members' benefits.



PIC'S BOARD OF DIRECTORS

Nomination and Remuneration Committee

- Reviews the structure, size, succession plans and composition (including the skills, knowledge, experience and diversity) of the Board and makes recommendations with regard to any changes.
- Determines and agrees with the Board the framework or broad policy for the remuneration and recruitment of the Company's Chairman, Non-Executive Directors, Chief Executive, the Executive Directors and other members of the executive management.
- Reviews PIC's Talent Management programme, overall remuneration arrangements and approves share incentive plans.

Asset Liability Management Committee

- Oversees the management of all aspects of investment policy and strategy for the Company and provides oversight of the operation of the Company's investment portfolios within the established strategy and risk frameworks.
- Focuses on asset strategies to support new business pricing and reviews the Company's hedging strategy.

Origination Committee

- Oversees the management of all aspects of the Company's new business and reinsurance origination within established strategy and risk frameworks, including conduct risk.
- The Committee also oversees all aspects of interaction with policyholders including administration, tracing and complaints; and recommends to the Board any actions needed to ensure policyholders are treated fairly.

Audit Committee

- Assists the Board with the discharge of its responsibilities with regard to internal and external audits, financial reporting, systems of internal controls and risk management.
- Main areas of consideration include readiness for Solvency II, data governance, business continuity planning and disaster recovery. Recommends to the Board appointment of the Company's external auditors (KPMG).

Risk Committee

- Assists the Board in its oversight of the Company's current and likely risk exposures, tolerances and appetite, risk measurement and risk management performance.
- Has oversight of the Company's risk policies and procedures and risk controls.
- Responsible for an oversight of the internal model and for reporting to the Board on any areas needing improvement.

BOARD OF DIRECTORS

Name and position	**Jon Aisbitt** Chairman of the Board and Chairman of the Nomination Committee	**Tracy Blackwell** Chief Executive Officer	**Amanda Bowe** Independent Non-Executive Director
Date of appointment	Jon was appointed to the Board as independent Non-Executive Chairman in October 2016.	Tracy was appointed to the Board as an Executive Director in July 2011 and appointed as Chief Executive Officer in July 2015.	Amanda was appointed to the Board as an independent Non-Executive Director in January 2017.
Background and career	In May 2016, Jon stepped down as Chairman of Man Group plc. Prior to joining Man Group plc, Jon held senior roles at Goldman Sachs. He was previously Deputy Chairman of Ocean Rig plc and Honorary Treasurer of the NSPCC. He is a Fellow of the Institute of Chartered Accountants of England and Wales.	Tracy joined PIC at its founding in 2006. Tracy was the Chief Investment Officer until she became CEO in 2015. Prior to PIC, Tracy held senior roles at Goldman Sachs.	Amanda held a number of senior roles at the Financial Services Authority during a 20-year career there. She has also held senior roles at Aegon UK. Amanda is a member of the Chartered Institute of Securities and Investments, London.
Areas of expertise	Jon has over 20 years' experience in international corporate finance. He has significant technical knowledge of capital markets and the complex regulatory backdrop in which they operate. He has significant change management experience.	More than 25 years' experience of investment markets, including matching pension assets to liabilities and risk hedging strategies. Strong knowledge and understanding of the regulatory landscape.	Amanda has considerable expertise as a financial services regulator, focused in particular on securities, insurance and investment regulation. She also has experience of managing the risks associated with financial crime and data protection.
Current external roles	Jon is a Director of New Forests Company Holdings Limited (African sustainable forestry and timber processing) and a Non-Executive Director of Pro Bono Bio plc (biotechnology).	Tracy is a Non-Executive Director of United Trust Bank.	Amanda is an independent Board Director of Standard Life Assurance Limited, Post Office Management Services Ltd and Equatex AG. She is Chair of the Audit and Risk Committee of Post Office Management Services Ltd.
Committee membership	Jon is Chairman of the Nomination Committee and a member of the Remuneration Committee. He is Co-Chair of the Origination Committee. He attends Audit and Risk Committee meetings by invitation.	Tracy is a Co-Chair of the Origination Committee. She attends Audit and Risk Committee meetings by invitation.	

John Coomber
Non-Executive Director

John was appointed to the Board in December 2007 and was Chief Executive Officer until June 2015. He remains on the Board as a Non-Executive Director.

John was Group Chief Executive Officer of Swiss Reinsurance Company until 2005. He was a member of the Board of Swiss Re from 2006 to 2014, a Director of Euler Hermes, Chairman of The Climate Group and Chairman of ClimateWise. He is a Fellow of the Institute of Actuaries and an Honorary Fellow of The Chartered Insurance Institute.

John has decades of experience and leadership within the international insurance and reinsurance industries.

John is Chairman of MH (GB) Ltd, a Director of the Financial Reporting Council and a member of the FRC Codes and Standards Committee.

John is a member of the Audit and Origination Committees.

Tim Hanford
Non-Executive Director

Tim was appointed to the Board as a Non-Executive Director in January 2009.

Tim is Managing Director and Head of Europe of J.C. Flowers & Co. Tim has previously held senior roles at FPK Capital and at Dresdner Bank. Tim has been an Executive Director of Schroders. Tim has an M.S. degree in Management from Stanford University Graduate School of Business, where he was a Sloan Fellow, and a BSc degree in Chemical Engineering from Birmingham University.

Tim has over 25 years' experience in banking and investment, including credit strategies, risk management, and mergers and acquisitions.

Tim serves on the Boards of OneSavings Bank Plc, Castle Trust and Cabot Credit Management, and is the Managing Director in charge of JCF Europe.

Tim is a Non-Executive Director and member of the Asset Liability Management and Nomination and Remuneration Committees.

Arno Kitts
Independent Non-Executive Director and Chairman of Asset Liability Management Committee

Arno was appointed to the Board as an independent Non-Executive Director in July 2016.

Arno has held senior roles at BlackRock, Henderson Global Investors and JPMorgan Asset Management, including being Chief Executive of BlackRock Life and JPMorgan Life. He has served as a director of many investment funds, some insurance companies, and the Pensions and Lifetime Savings Association (PLSA). Arno was a Member of the Council and Finance & Investment Board of the Actuarial Profession. He is a Fellow of the Institute of Actuaries and holds a PhD from Southampton University.

Arno was responsible for institutional business with clients worldwide, encompassing sales and marketing, product development and client and consultant relationship management and service. Earlier in his career, Arno was Head of Investments for an insurance company. He has been involved in investment management since 1989.

Arno is a Director of Perspective Capital Management Limited. He is a member of the PLSA Defined Benefit Council. He is the Governor of the Pensions Policy Institute.

Arno is an independent Non-Executive Director and Chairman of the Asset Liability Management Committee.

Nick Lyons
Senior Independent Director and Chairman of the Remuneration Committee

Nick was appointed to the Board as Senior Independent Director in February 2016.

Nick headed the European Financial Institutions Group at Lehman Brothers Europe until 2003. Previous roles include executive positions at JPMorgan and Salomon Brothers. Nick served as Non-Executive Chairman of Miller Insurance Services LLP, as well as a Director of Catlin Group, Friends Life Group plc and Quayle Munro plc.

Nick has considerable expertise and experience in the financial services and insurance industries. Nick also has extensive experience in serving as an independent Non-Executive Director.

Nick serves on the Boards of Directors of Clipstone Logistics Reit Plc, various Price Forbes related entities and Temple Bar Investment Trust PLC. Nick is also the Chairman of Longbow Capital LLP.

Nick is the Senior Independent Director and Chairman of the Remuneration Committee.

BOARD OF DIRECTORS

Continued

Name and position	**Roger Marshall** Independent Non-Executive Director and Chairman of the Audit Committee	**Eloy Michotte** Non-Executive Director	**Steve Sarjant** Independent Non-Executive Director and Chairman of the Risk Committee
Date of appointment	Roger was appointed to the Board as an independent Non-Executive Director in September 2015.	Eloy was appointed to the Board as a Non-Executive Director in October 2012.	Steve was appointed to the Board as an independent Non-Executive Director in November 2014.
Background and career	Roger held senior roles at PricewaterhouseCoopers, including the Chairmanship of PwC's Global Audit Policy Board and its global Corporate Reporting Task Force. Roger is a Fellow of the Institute of Chartered Accountants in England and Wales.	Eloy has held senior roles at Reinet Investments Manager S.A. and Reinet Fund Manager S.A. He has previously worked for Ford, McKinsey & Co and Bankers Trust Company prior to joining Richemont at the time of its formation in 1988. He graduated in engineering and applied mathematics from the University of Louvain in Belgium and holds an MBA from the University of Chicago.	Steve spent 20 years at Towers Watson (previously Watson Wyatt) in a number of senior roles. Prior to this, Steve held roles at Criterion Assurance Group and National Provident Institution in a variety of roles. Steve has a BSc in mathematics from the University of Bristol. He is a Fellow of the Institute and Faculty of Actuaries.
Areas of expertise	Roger spent almost 40 years at PwC and six years on the Accounting Standards Board. He has extensive experience in the risk management, finance and audit functions in the financial services industry.	Eloy has extensive experience in international business and finance, including mergers and acquisitions.	Steve has over 30 years' experience in the financial services industry including 20 years spent as an actuarial consultant at Towers Watson (previously Watson Wyatt), where he was a Managing Director in their Risk and Financial Services segment and Global Leader, Mergers and Acquisitions.
Current external roles	Roger is a member of the FRC Board, the FRC Codes and Standards Committee and the FRC Corporate Reporting Council. Roger also serves on the Boards of the European Financial Reporting Advisory Group, Old Mutual PLC and Old Mutual Wealth Management Limited.	Eloy is Non-Executive Director of Reinet Investments Manager SA. He also serves on the Boards of a number of companies in which Reinet Fund S.C.A. F.I.S. and Compagnie Financière Richemont S.A. hold interests.	Steve is a Non-Executive Director and Chairman of the Actuarial Committee for Vitality Health and Vitality Life, and an independent member of the With Profits Committee of Liverpool Victoria Friendly Society.
Committee membership	Roger is an independent Non-Executive Director, Chairman of the Audit Committee and a member of the Risk Committee.	Eloy is a Non-Executive Director and member of the Origination, Asset Liability Management, and Nomination and Remuneration Committees.	Steve is an independent Non-Executive Director, Chairman of the Risk Committee and member of the Audit and Origination Committees.

Rob Sewell Chief Financial Officer	**Mark Stephen** Independent Non-Executive Director	**Wilhelm Van Zyl** Non-Executive Director
Rob was appointed to the Board as an Executive Director in July 2008.	Mark was appointed to the Board as an independent Non-Executive Director in November 2014.	Wilhelm was appointed to the Board as a Non-Executive Director in May 2015.
Prior to PIC, Rob held leadership positions at National Westminster Life Assurance and Legal & General Group. Rob is a Fellow of the Institute of Chartered Accountants in England and Wales.	Mark was previously a partner at PricewaterhouseCoopers LLP. He is a member of the Institute of Chartered Accountants in England and Wales.	Wilhelm is the Chief Executive of Reinet Investments Manager S.A. and Reinet Fund Manager S.A. Prior to this, Wilhelm held senior roles in a long career at Metropolitan Holdings and MMI Holdings. Wilhelm holds a BCom degree from the University of Stellenbosch and is a Fellow of the Institute and Faculty of Actuaries (UK) and Fellow of the Actuarial Society of South Africa.
Rob has extensive financial and accounting experience in the insurance and regulatory markets.	Mark has over 30 years' experience of advising and working with insurance company Boards on many aspects of business, including how they adapt to the changing regulatory and business landscape.	Wilhelm has a strong background in the international financial services sector, including insurance and investment strategy.
Rob serves as a Non-Executive Director of HCT Group.	Mark serves as a Director of TransRe London Limited.	Wilhelm is the Chief Executive of Reinet Investments Manager S.A. and Reinet Fund Manager S.A. He serves on the Boards of a number of companies in which Reinet holds interests.
Rob is an Executive Director and member of the Origination Committee. He attends Audit and Risk Committee meetings by invitation.	Mark is an independent Non-Executive Director and member of the Risk, Asset Liability Management and Audit Committees.	Wilhelm is a Non-Executive Director and member of the Risk and Audit Committees.

BOARD OF DIRECTORS

Continued

Board attendance

- Full-year Board programme
- Key areas of progress/strength + main areas for development

	23/03/2016	25/05/2016	20/07/2016	21/09/016	09/11/2016	09/12/2016	
Jon Aisbitt[1]	○	○	in attendance	in attendance	●	●	2/2
Sir Mark Weinberg (C)	●	●	●	apologies	○	○	3/4
Tracy Blackwell	●	●	●	●	●	●	6/6
Rob Sewell	●	●	●	●	●	●	6/6
John Coomber	●	●	●	●	●	●	6/6
Tim Hanford	●	●	apologies	●	apologies	●	4/6
Arno Kitts	○	○	●	●	●	●	4/4
Nick Lyons	●	●	●	●	●	●	6/6
Roger Marshall	●	●	●	●	●	●	6/6
Harriet Maunsell	●	●	●	●	●	●	6/6
Chris McKechnie	●	●	○	○	○	○	2/2
Eloy Michotte	●	●	●	●	●	●	6/6
Steve Sarjant	●	●	●	●	●	●	6/6
Mark Stephen	●	●	●	●	●	●	6/6
Wilhelm Van Zyl	●	●	●	●	●	●	6/6

Note:
○ Not on the Board ● On the Board
1 Jon Aisbitt attended Board meetings prior to becoming Chairman on 14 October 2016.

Board focus 2016

At each meeting, the Board receives updates from the Chief Executive Officer and Chief Financial Officer on the execution against strategy and performance against plan. The Board also reviews regular executive reports from different business areas, including matters relating to policyholders and our obligation to treat them fairly. The Chief Risk Officer attends each meeting and also provides regular updates. The Chairmen of the Board Committees, (Risk, Audit, Asset Liability Management, Origination and Nomination and Remuneration), also provide updates to the Board. In addition, a variety of matters are covered, as listed:

- Q1 2016 – 2015 financial statements and Solvency II implementation.
- Q2 2016 – own risk assessment and treating customers fairly.
- Q3 2016 – draft business plan, debt issuance and risk appetites.
- Q4 2016 – 2017 five-year business plan and budget, compensation and cyber strategy.

Board strengths

- PIC is led by a strong and capable Board which has a good connection to the business and has a culture of challenging the management team.
- The Board is structured in such a way that each Director is able to use their experiences and skills to best effect in active engagement with the business.
- The Board encourages and supports each Director to regularly update and refresh their skills and knowledge. The Company arranges a formal induction for all new Directors and there is a Board development training programme in place which targets general regulatory and market developments, but also the Company's specific issues.
- A 2016 external review of the Board's composition was completed to progress compliance with the UK Corporate Governance Code. The Board was subsequently strengthened by appointments of a new independent Non-Executive Chairman and two independent Non-Executive Directors. A majority of independent Directors was also achieved in 2016.
- The Board operates in a collaborative way with constructive debate and challenge being an integral part of the Board's discussions. Independent views are very much encouraged and heard by the Board.

Areas for Board development

- Continued focus on the relationship between the Board and its Committees to allow a more streamlined decision-making process. This includes the Board Committees' annual programmes; the quality of information submitted for their consideration; and escalation of matters to the Board.
- Female representation and diversity of the Board is another area of development.

GLOSSARY

Annuities
A type of insurance policy that pays out regular amounts of benefit to the policyholder for the remainder of insured individual's lifetime and, in certain cases, that of their spouse and/or dependents. The payments may commence immediately ("immediate annuity") or may be deferred to commence from a future date, such as the date of retirement ("deferred annuity"). Immediate annuities and deferred annuities may be purchased for an individual and his or her dependants or on a bulk purchase basis for groups of individuals.

Assets under management (AUM)
Represents all assets actively managed or administered by or on behalf of the institution including those funds managed by third parties.

Best estimate liability (BEL)
The best estimate liability represents the value of future liability and expense cash flows. It is based on realistic assumptions with no prudent margins (other than in the default and downgrade assumptions stipulated for the calculation of the valuation discount rate) and is calculated using well-established actuarial and statistical methods.

Defined benefit (DB) pension plan
An employer-sponsored retirement benefit plan where the benefits promised to the members of the plan are defined according to a formula typically based on factors such as salary history and duration of employment. Investment risk and portfolio management are entirely under the control of the trustees of the pension plan and not the employee or employer.

Financial Conduct Authority (FCA)
One of the two bodies (along with the PRA) which replaced the Financial Services Authority from 1 April 2013. The FCA is a company limited by guarantee and is independent of the Bank of England. It is responsible for the conduct business regulation of all firms (including those firms subject to prudential regulation by the PRA) and the prudential regulation of firms not regulated by the PRA.

The FCA has three statutory objectives: securing an appropriate degree of protection for consumers, protecting and enhancing the integrity of the UK financial system, and promoting effective competition in the interests of consumers.

Minimum capital requirement (MCR)
The lower of the two capital levels required by Solvency II. It represents the minimum level of capital required to be held by an insurer before ultimate regulatory intervention is triggered.

PIC's internal model
A risk management system developed by PIC to analyse its overall risk position, to quantify risks and to determine the capital required to meet those risks. PIC has obtained appropriate approval from the PRA to use its internal model to calculate its solvency capital requirement under Solvency II.

Pillar 1
The area of Solvency II concerned with calculation of regulatory capital and defining the financial resources that a company must hold to be considered solvent. It sets out how an insurer should assess and value assets and calculate solvency capital.

Pillar 2
The area of Solvency II that focuses on an insurer's governance and risk management. The cornerstones of Pillar 2 are the own risk and solvency assessment (ORSA) and the supervisory review process (SRP). If a regulator is unhappy with an insurer's risk management processes it can require it to hold more capital.

Prudential Regulation Authority (PRA)
One of the two bodies (along with the FCA) which replaced the Financial Services Authority from 1 April 2013. The PRA is a part of the Bank of England and is responsible for the prudential regulation of deposit-taking institutions, insurers and major investment firms. The PRA has two statutory objectives: to promote the safety and soundness of these firms and, specifically for insurers, to contribute to the securing of an appropriate degree of protection for policyholders.

Risk margin (RM)
Life insurance companies hold technical provisions (reserves) calculated on actuarial bases to ensure they have sufficient funds available to pay their technical liabilities when they fall due. The technical provisions comprise a best estimate liability (BEL) and a risk margin (RM).

The RM calculation, which is prescribed under the Solvency II regulations, is determined by considering the amount that a notional third party, a reference undertaking, would require in order to take over the liabilities and have sufficient capital to support them over their future lifetime.

GLOSSARY

Continued

Solvency II
An EU-wide regulatory regime which intends to align solvency capital to an insurer's risk profile. Solvency II was implemented on 1 January 2016.

Solvency capital requirement (SCR)
The SCR represents the capital that the Company needs to hold in order to be able to survive a 1-in-200 year risk event over the 12 months following the balance sheet date. PIC calculates its SCR using a Company-specific model (the internal model) which has been approved by the PRA. The main components of the SCR are market risk and insurance risk, but the internal model also covers counterparty default risk, expense risk and operational risk.

Standard formula
A risk-based mathematical formula used by insurers to calculate their solvency capital requirement under Solvency II. The standard formula is intended for use by most EU insurers, although they may use an internal model instead, subject to regulatory approval.

Technical provisions (TP)
The value of technical provisions on the Solvency II basis is equal to the sum of a best estimate liability (BEL) and a risk margin (RM).

Transitional measures (TMTP)
PIC uses a transitional measures deduction on technical provisions in its Solvency II balance sheet. The TMTP allows companies to smooth the transition from the previous regulatory regime to the Solvency II approach, for example in having to set up the risk margin. The TMTP only applies in respect of business that was in force at 31 December 2015, and it runs off linearly to zero over 16 years.

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