

Vitality UK



WHO WE ARE

VitalityLife provides individual and business clients with life, capital disability, severe illness and income protection cover. The Serious Illness Cover benefit protects policyholders for nearly four times as many conditions as other providers. In 2016, we paid out 99.4% of life insurance claims and 92.7% of critical illness claims. VitalityLife is the only life insurer who encourages and rewards policyholders for being healthy through its range of optimiser products.

VitalityHealth offers an integrated medical insurance and wellness proposition to individuals and, predominantly, small and medium enterprise clients. The holistic healthcare solution integrates prevention and health promotion with traditional illness cover. The business has achieved record-level growth through its direct channels.

Both businesses continue to invest in the Vitality brand and the strong delivery of the Vitality Shared-Value Insurance proposition. This has resulted in robust financial and actuarial performance, and the delivery of additional tangible value for clients in the UK.

Performance highlights



HEALTH AND LIFE INSURANCE



Vitality LIFE INSURANCE

Value of new business margin improved to 36% for the full year.

THE ANNUALISED VALUE OF NEW BUSINESS MARGINS FOR THE YEAR WAS: 5.20%

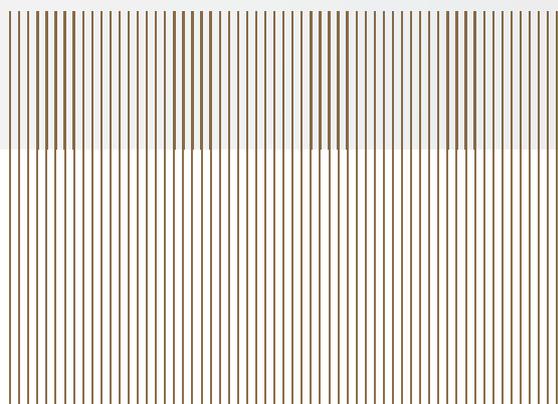
This shows encouraging signs of resilience, driven by product enhancements, capital-efficient offerings, and an improved optimised business mix.



Vitality HEALTH INSURANCE

Operating profit for VitalityHealth was up 89% for the year at £16.4 million.

New business growth was strong at 4% to **£56.2 million**, particularly in the profitable direct and individual channels, which grew by 13% and 9% respectively.



INCREASING VITALITY BRAND AWARENESS IN THE UK

The private medical insurance market in the UK is complex, given that take-up is relatively low (at around 11%) among the general population. In addition, traditional providers of private medical insurance tend to focus on care rather than prevention. Both of these issues can be linked to the ubiquity of the National Health Service in the delivery of healthcare in the UK.

These issues necessitate an increased public awareness of health and wellness, and to create greater accountability among consumers for their wellbeing. This informs the products of Vitality UK, the brand, and the marketing approach. From a product perspective, we inform people of their risks and reward them for making healthy choices. From a brand perspective, we have created a retail franchise around health through our sponsorship assets and marketing campaigns.

During the year, we built on our campaigns to amplify awareness of the Vitality brand, including introducing a number of ambassadors, sponsorships, events, and charitable campaigns. Vitality UK grew its ambassador portfolio to include Joe Root (England cricket captain), Maro Itoje (England rugby team), and Ellie Simmonds (paralympian). In addition to our existing football and wellness partnerships, Vitality UK also announced an expansion of our partnership with parkrun, to become the headline partner of the initiative, which is now branded as Vitality parkrun. Other new partnerships include Great British Chefs and the Telegraph Junior Golf Championship.

During the period, Vitality Ambassador, Jessica Ennis-Hill, was involved in supporting numerous national campaigns that encourage physical activity. Vitality UK also launched VitalityMove, a music-themed running festival, while Everyday Athlete focussed on physical activity and social media campaigns such as Bring a Ball, and Where's your Wicket?

VITALITYLIFE

VitalityLife produced a steady performance and showed continued resilience in the face of a complex period. This included an unpredictable economic climate with volatility in long-term interest rates. There was strong growth of 15% in term sales, offset with a decrease in whole-of-life sales. The net effect of these conditions was a decrease in new business of 20% in rand terms to R1 068 million (1% down to 61.8 million in GBP). Normalised operating profit was also lower by 11% to £28.1 million (down 28% in rand terms to R485 million). In our reporting over the period, we saw the negative effect on profitability as a function of lower economic assumptions, exchange rates movements and margin releases in the previous period.

With a focus on value over volume, VitalityLife saw continued adoption of the Vitality integrated model over the period. We also witnessed better-than-expected overall claims experience dynamics (net and gross of reinsurance).

VitalityLife maintained a high market share of more than 10% for protection business in the independent financial adviser market. We continued the drive towards more capital-efficient products, and launched new initiatives which are all market-firsts in the UK:

- Wellness Optimiser designed to reflect health-related behaviour change through discounts on health checks (premiums change based on Vitality status).
- Enhanced Severe Illness Cover with a cancer relapse benefit, whereby clients can get Severe Illness Cover if there is a cancer relapse after one year in remission.
- Vitality Nurses, a convenient online booking system, including a range of medical screening and nursing services, aimed at supporting the underwriting process. A nurse goes to clients for their Vitality screening and non-laboratory medical diagnostic testing, and completes the process in as little as two hours. Besides fast policy activation, clients also have immediate information to engage with Vitality and improve their health.

VITALITYHEALTH

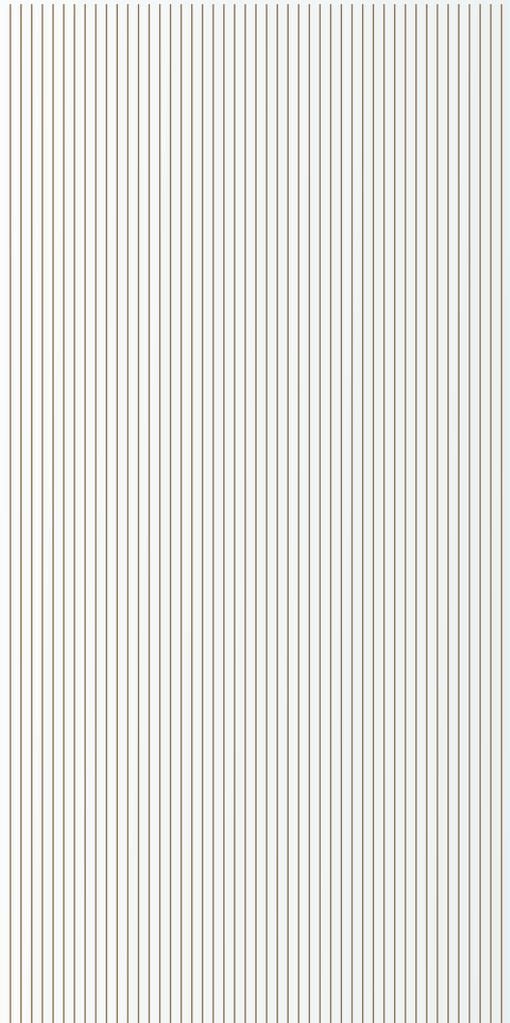
Despite the complex economic environment and political landscape, the period under review saw the acceleration of trends established during the first half of the year. New business volumes, loss ratios, operating profit and Vitality engagement all reached best-ever performance levels.

Operating profit for VitalityHealth was up 89% for the year at £16.4 million. From a cash flow perspective, the business became self-sustaining for the first time with the in-force portfolio generating £42.9 million of cash. This more than offsets the cost of writing new business.

New business growth was strong at 4% to £56.2 million, particularly in the profitable direct and individual channels, which grew by 13% and 9% respectively. This growth offset the reduction in corporate new business for the year – from £3 million previously to £1.8 million, as VitalityHealth maintained its value over volume stance in this competitive sector of the market. Importantly, individual business made up 50% of overall new business, indicating the appeal of the Vitality product in this market. Further countering this trend, a high proportion of individuals joining Vitality in the period were previously uninsured, particularly those joining through direct channels.

The period was characterised by excellent actuarial dynamics, with a continuation of good loss ratio and retention performance. There was a five percentage point reduction in the loss ratio over the period. This was driven by the combination of positive new business selection, the positive effects of Vitality on risk and retention, the purchasing power of the Healthcare Purchasing Alliance (a joint venture with Aviva), the re-engineering of our claims management processes, and the treatment pathways through which care is delivered through new products such as Consultant Select, (a consultant-led directional care pathway delivered in partnership with Alliance Surgical).

Vitality Shared-Value Insurance reinforced the strong value proposition, offering Vitality members rewards and incentives that increased from £48.6 million in the previous period to £62.7 million in the period. Of individual members who engage in the Vitality wellness programme, 26% generated more value through health discounts and rewards than they paid in policy premiums, while 46% generated more than half the value of their policy premium.



VITALITY IN THE UK

The Vitality enhancements launched during the period resonated strongly with the market, and further encouraged significant behaviour change in the areas of physical activity and nutrition.

The HealthyFood benefit in partnership with Ocado has seen over

14 600

REGISTRATIONS TO DATE
AND A **19%** INCREASE

in the HealthyFood items included in food baskets during the first six months.

PARTNERSHIP WITH UNICEF:

Donate a day's food pack when a Vitality member first shops at Ocado.

OVER

30 000

FOOD PACKS DONATED TO UNICEF
WITHIN THE REVIEW PERIOD.

MAKING **APPLE WATCH** AVAILABLE AS
PART OF VITALITY ACTIVE REWARDS.

OVER

25 000

Apple Watches purchased. And an increase of **34%** of Vitality members who were not active, becoming active.

(For the period October 2016 to April 2017).

Intellectual leadership continues to be emphasised through the **Britain's Healthiest Workplace** study, which saw 32 000 individual employees and 167 employer groups participate in 2017. A key output this year has also been the production of a new productivity model, built in partnership with RAND Europe, which links employees' distinct lifestyle behaviours to short-term productivity outcomes. Through demonstrating the cost of ill-health for employers, this research is contributing to build the business case for investment in workplace health.

Material issues

This section outlines key issues and focus areas Vitality UK managed during the year.

Vitality LIFE INSURANCE

01

MANAGING LOW INTEREST RATES

The economic uncertainty surrounding Britain's exit from the European Union has had a number of implications for VitalityLife. The most significant implication has been low and volatile long-term interest rates, which has negatively impacted profitability. The business is closely tracking the effects of the interest rate.

Against these conditions, the business remained strong over the period, with both lapse rates and claims ratios below expectations. We maintained an intense focus on business mix together with steady and continued development of products that are priced effectively to respond to market conditions. Introduction of new products in response to the environment include Premium Rate Optimiser, Interest Rate Optimiser and Wellness Optimiser. Vitality linked products now comprise over 70% of all new business uptake rates. These products are optimally priced based on actual client risk profiles, and the Wellness Optimiser, specifically, rewards clients for improving their health status. Up to 63% of all new business annual premium equivalent for the year was optimised (Vitality and Wellness Optimiser specifically).

Adoption of the Vitality integrated model has been a key driver of the increasing value of new business margin, experienced in the second half of the financial year. The continued upward direction and improvement of key metrics over the second six months, have been encouraging. It shows the resilience of the business in a challenging economic environment, and the remedial and preventive action in response to the difficult economic environment.

The business continues to meet solvency requirements against Solvency II, with cash flow requirements on track.



02

CONTINUED PRODUCT INNOVATION

During the financial year, VitalityLife further embedded wellness into its product range. The most notable addition was the Wellness Optimiser, a product which rewards consumers based on an improving health status. Integration of Vitality with life insurance products has added value to products and increased client persistency, as displayed in low lapse rates.

In 2018, we are introducing Vitality Lite, a product with selected Vitality offers at a lower price, which is expected to further increase the uptake of Vitality and the value created through the business model.

VitalityLife also aims to maintain its competitive advantage obtained through capital-efficient products with the development of an Optimiser Lite product in the new financial year. These products will remove minimum-premium requirements currently in place for other Optimiser products.

Vitality HEALTH INSURANCE

01 MANAGING CHALLENGING EXTERNAL CONDITIONS

As with VitalityLife, VitalityHealth was impaired by the current economic uncertainty surrounding Britain's exit from the European Union, which has had a number of implications for VitalityHealth. Low interest rates have impacted negatively on investment income, while the effect of poor economic performance in the uptake of private medical insurance, poses a significant risk on the industry. VitalityHealth seeks to mitigate this through offering increased demonstrable value to members through our products and Vitality Shared-Value Insurance model, whether or not members need to claim.

Service delivery within the National Health Service is a key challenge for the UK public sector, with increasing waiting times and pressure on availability of health professionals. Even small shifts in spend from the public to private sector present an opportunity for private medical insurance providers. VitalityHealth is uniquely positioned in the market due to our focus on prevention, alongside delivery of quality care.

02 CONTINUED PRODUCT INNOVATION

Engagement in Vitality continued to deliver clear benefits from both a claims and retention perspective. Member engagement is at record levels, both in terms of unique members engaging, and volume of activities. During the year, point-earning events increased exponentially, with over 24 million activities completed. Active rewards continue to be a key driver of weekly engagement, with a 10-fold increase in members reaching weekly activity threshold, and 34% of members who were inactive, becoming active.

Vitality members who increased their wellness engagement had a claims cost of around 20% lower than those who maintained their starting level of engagement. The effect on the lapse rate was even more pronounced, with this being halved for Vitality members who were actively engaged.

VitalityHealth's product launch in September 2016 included a number of key enhancements to the wellness and private medical insurance components of our value proposition. This included the addition of Consultant Select, a consultant-led directional care pathway, and the introduction of a new approach to individual renewal pricing, which moves away from the traditional no-claims discount model. These new products offer personalised help to members who take an active approach to managing their health, and Vitality linked renewal pricing, ensuring persistency for the business and value for members.

03 OPERATIONAL QUALITY AND EFFICIENCY

Key developments in the period included the completion of the migration to a single-platform administrative system, following the exit last year from the Transitional Service Agreement with Standard Life. A number of other projects have been delivered aimed at driving greater operational efficiency, while also enhancing the customer journey. These include the interactive voice response system for call centre services, enhancement of adviser self-service, and the refinement of the online offering to improve members' ability to interact with Vitality. The success of these initiatives has been demonstrated by the fact that despite member interaction with Vitality increasing dramatically due to growing engagement with Vitality's partners and rewards, the actual service load has been managed downward over the past three years.

04 NAVIGATING REGULATORY DEVELOPMENTS

Insurance Premium Tax imposed on general insurance, including private medical insurance, has doubled from 6% in October 2015 to 12% in June 2017. This has resulted in considerable increases in insurance premiums. Uncertainty remains around the future level of Insurance Premium Tax and whether or not further increases will be imposed in future. Through our shared-value approach and Vitality-linked products, we remain price competitive, and will monitor the effects of any changes in the Insurance Premium Tax against our value proposition.

The regulation implemented by the Financial Conduct Authority surrounding transparency of the previous year's premiums at renewal, was introduced in April 2017. It aims to address consumer treatment and engagement at policy renewal stage, and to promote effective competition with more transparent price increases. To demonstrate the additional value delivered to members through Vitality partners and rewards, a project was implemented to display a 'value-statement' on renewal notifications, displaying the possible savings available to our members during the course of the year. This, combined with our unique approach to renewal pricing linked to Vitality engagement, as well as the value delivered whether or not a member makes a claim in a given year, places us in a strong position relative to the market.

Another regulation we are preparing for is the General Data Protection Regulation, aimed at strengthening data protection for all individuals. This regulation comes into effect in May 2018.

OUTLOOK

VitalityLife

Key objectives for the coming financial year include keeping track of the effects of the interest rate against our projections to respond effectively. We also aim to:

- Significantly enhance distribution capability of profitable products through:
 - Increasing the franchise footprint and number of account managers.
 - Building a responsive technical marketing capability that supports our sales growth ambition with analytical tools and insights that highlight Vitality's competitive advantage and establishes a position of thought leadership in the market.
 - Focusing and targeting higher sales of indexed benefits with a review of the indexation structure to ensure simplicity and to improve customer outcomes. This will also build up additional tier-two margins, improve capital efficiency and mitigate interest rate risk.
- Enhance the service experience for clients, specifically our digital channels, and building the distribution channel and number of account managers.
- Expand our profit lines through the development of products that focus on affordable pricing and value.
- Develop the direct to consumer channel, which experienced a 77% increase in generating new business compared with the previous year.
- Ensure capital efficiency as the VitalityLife book grows on its own statement of financial position. Part VII of the business that was written on the Prudential Assurance Company's balance sheet needs to be completed by November 2019.

VitalityHealth

Key objectives for the coming financial year include pursuing further new business growth across all markets.

We will also continue to drive engagement and behavioural change through Vitality to achieve lasting changes in the health of clients, which results in reduced claims costs, delivered by our Shared-Value Insurance model.

In terms of ensuring greater operational efficiency and performance, we will focus on two key areas:

- Improvement of the client journey by positioning service as a key differentiator.
- Increased efficiencies in our digital channels for improved service, and growing our franchise footprint and the number of account managers.

INTRODUCING INVESTMENT PRODUCTS IN 2018

The potential for integration opportunities between the long-term protection and long-term savings products in the UK have driven the development of the investment offering. Vitality UK plans to launch a suite of investment products in the first quarter of 2018, subject to regulatory approval. While developing the offer for the UK market, we rely on our experience of the product overlap in our primary market of South Africa, and strong relationships we have formed within our current financial adviser force that focusses on investment and savings products.

