

Challenger

www.challenger.com.au

About Challenger Life

31 December 2016

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Who is Challenger?

Challenger Limited is a publicly listed investment management firm. Established in 1985 and listed on the Australian Securities Exchange in 1987, Challenger Limited now manages \$65 billion in assets, and is part of the S&P/ASX100 Index.

The Challenger group is focused on providing customers with financial security for retirement. It does this by providing investment opportunities for those in the savings (accumulation) phase, and delivering safe and reliable income streams for those in the spending (retirement) phase.

Challenger's funds management business, Fidante Partners, works with boutique investment managers to offer a range of investment strategies across a variety of asset classes. Opportunities for investors to convert their savings into a series of regular payments to support them during their retirement are also offered by Challenger's life company, Challenger Life Company Limited (**Challenger Life**).

Who is Challenger Life?

Challenger Life is Australia's largest provider of annuities, managing approximately \$14.6 billion in assets. An Australian life insurance company, Challenger Life is regulated by the Australian Prudential Regulation Authority (APRA).

Challenger Life has won the Association of Financial Advisers (AFA) 'Annuity Provider of the Year' for the past nine years. For further information about these awards, visit the AFA website, www.afa.asn.au.



What is an annuity?

An annuity is a secure investment that provides you with a series of regular payments, either for a chosen term or for your lifetime, in return for a lump-sum investment. It can be used with other retirement investments, like account-based pensions, to set you up with a dependable income that can last throughout your retirement.

Challenger annuities work like a pay cheque in retirement.

Annuities:

- deliver regular, dependable cash flows
- offer flexible terms and payment options
- may offer indexation to help protect against inflation
- provide tax-free income if you're over 60 and buy them with superannuation money
- may help to increase Age Pension entitlements.

In addition, some Challenger annuities offer protection against inflation and in some circumstances can increase your social security benefits. You can also tailor your Challenger annuity to provide benefits for another person, such as your spouse or another dependant.

How does a Challenger annuity work?

Just like many other investments, you buy a Challenger annuity with a capital amount. The dollar amount of your regular payments is determined at the time you invest, and is based on competitive rates set by Challenger.

You select your annuity's options, such as the:

- frequency of the regular payments (monthly, quarterly, half-yearly, yearly)
- term of the investment (a fixed term or for life), and
- level of indexation (if applicable).

Challenger Life then guarantees to make your regular payments for your chosen term.

Where do my regular payments come from?

When you buy a Challenger annuity, your money is pooled with money from other investors along with additional money from the Challenger group. Challenger Life is required by law to keep this money separate from other funds in the Challenger group, in what is known as a statutory fund.

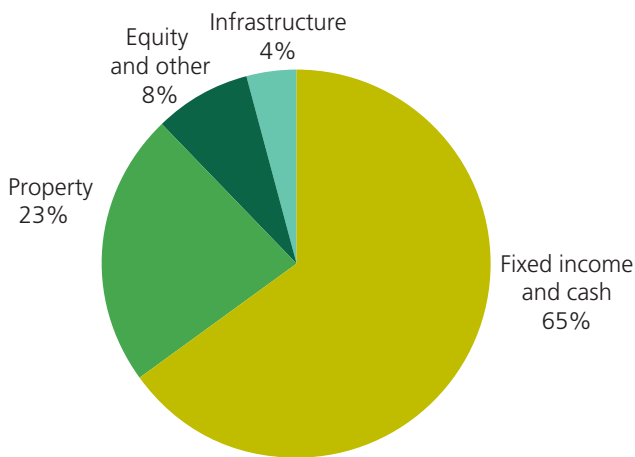
Your regular payments are made from this statutory fund. The money in the statutory fund is managed by Challenger's in-house and external investment managers.

The statutory fund

How is the statutory fund invested?

The statutory fund is primarily invested in fixed income (including cash) and property, with some investments in infrastructure and equities (Figure 1).

Figure 1: Asset allocation of the statutory fund (as at 31 December 2016)



The statutory fund is invested with the aim of achieving stable returns, to generate reliable cash flows from investments that are sufficient to meet the payments to all investors.

What happens to the investment return on the assets in the statutory fund?

All investment returns go into the statutory fund. If the statutory fund receives additional investment returns above the amount necessary to make all payments to investors, then Challenger Life can take some surplus income from it; however, it is only legally permitted to do so after it has made sure that there are sufficient funds to meet the current and future payments for all annuity investors.

How safe is the statutory fund?

Challenger Life is regulated under the Life Insurance Act 1995, which governs the provision of annuities in Australia. Under this Act, Challenger Life and its statutory fund are subject to prudential regulation by APRA, which actively supervises all Australian life companies to ensure they are able to meet their obligations to investors.

Under the prudential requirements, Challenger Life is required to hold a minimum level of capital in the statutory fund. Challenger Life holds more assets in the statutory fund than the APRA minimum.

If the money in the statutory fund falls below the level required to make payments to investors, Challenger Life is required to top it up.

The amount of capital to be kept in the statutory fund depends on the total value of current and future payments to annuity investors and the way the underlying assets of the statutory fund are invested – more risky assets such as shares require additional capital to be held, to balance the risk (Figure 2).

Figure 2: Challenger holds more assets in the statutory fund than required

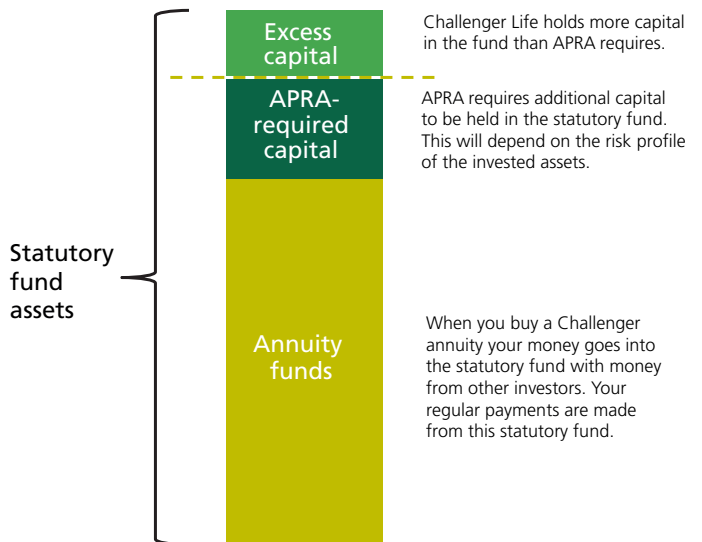


Diagram is illustrative only and not to scale.

Source: Challenger.

What happens if there's a market fall?

If market returns are low or negative, the value of the assets in the statutory fund could decrease, depending on how exposed it is to the relevant investment market and the extent of the fall.

Challenger Life has strict policies and plans in place that require us to take actions to make sure that the capital in the statutory fund stays above the APRA-required amount and therefore able to meet current and future payments to investors. These include (but are not limited to) reducing risk through reinsurance or selling assets, reducing new business and seeking further capital from Challenger Life shareholders.

What happens if a specific investment in the statutory fund fails?

The statutory fund invests in a range of assets. It is well diversified across asset classes and many different individual investments. Therefore, the impact on the statutory fund of any specific investment failing would typically be small, and unlikely to impact Challenger Life's ability to make payments to investors.

Who is APRA?

APRA is the prudential regulator of the Australian financial services industry. It oversees Australian banks, credit unions, building societies, general insurance and reinsurance companies, life insurance companies, friendly societies and most superannuation funds.

APRA has extensive monitoring and investigation powers. As with all life insurance companies, Challenger Life reports regularly to APRA and APRA reviews its financial position.

In the unlikely event that the value of the assets in the statutory fund fall below the required minimum, APRA has a wide range of powers available to it to protect the interests of annuity investors.

APRA's prudential standards are designed to ensure that there are safeguards in place so that payments to annuity investors are always met.

Where can I get more information?

For more information visit the Challenger website, www.challenger.com.au, speak to your financial adviser or call Challenger's Investor Services team on 13 35 66.

For financial advisers, call your Challenger Business Development Manager or Challenger's Adviser Services team on 1800 621 009.

Appendix – Statutory fund asset portfolio as at 31 December 2016

Fixed income

The fixed income portfolio is managed by Challenger's experienced team of fixed income managers. The portfolio is diversified across industry and asset type with more than 1,000 securities.

Figure 3: Fixed income by credit quality

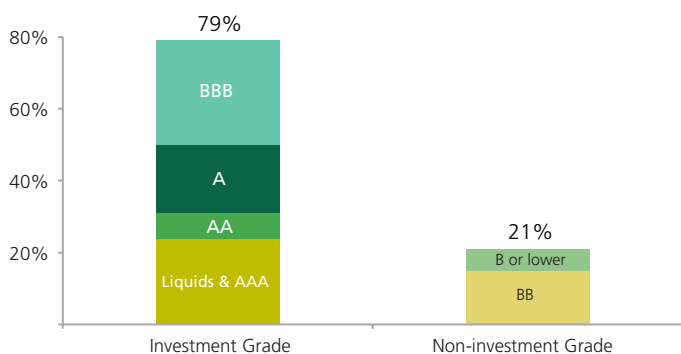


Figure 4: Fixed income by geography

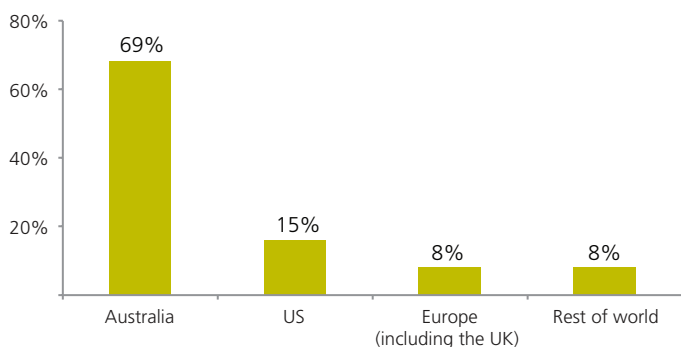
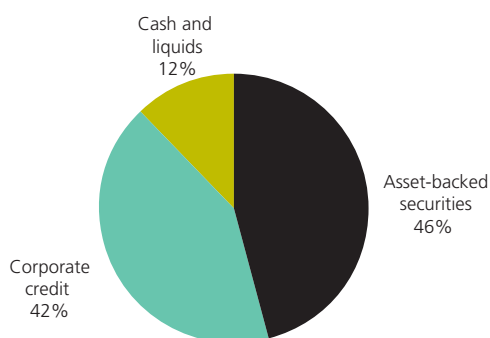


Figure 5: Fixed income by asset type



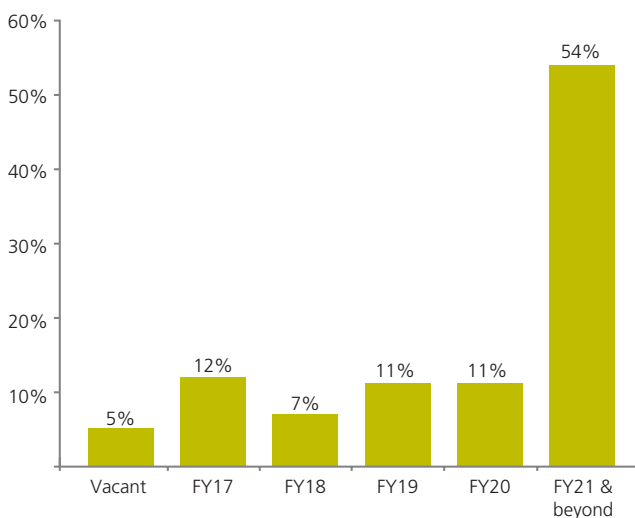
Property

The directly owned property portfolio provides predictable rental income. It is prudently managed with 51% of the tenants investment grade. The directly owned property portfolio has a weighted average lease life of 4.5 years.

Figure 6: Property portfolio

% of total portfolio	
Australian office	47%
Australian retail	28%
Australian industrial	6%
Australian listed REITs	5%
Australian unlisted REITs	3%
Australian total	89%
Japanese retail	7%
Other (including offshore)	4%
Total	100%

Figure 7: Portfolio lease expiry overview



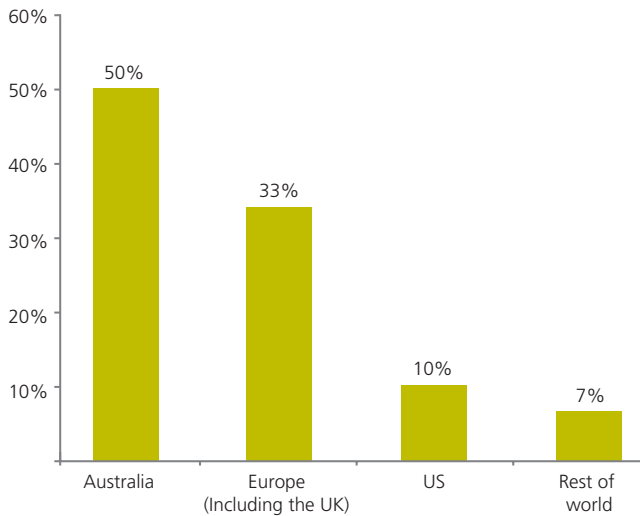
Infrastructure

The infrastructure portfolio offers Challenger Life a long-term stable income return with potential for capital growth via investment in a diversified portfolio of global utility and infrastructure assets.

Figure 8: Infrastructure asset diversification

31 December 2016	\$m	%
Logistics	68	13%
Utilities	59	11%
Patronage	85	16%
Airport	18	3%
Power Generation	30	6%
Renewable	105	20%
Core infrastructure	161	31%
Total	526	100

Figure 9: Infrastructure portfolio by geography



If you are a financial adviser and would like more information on the investments in the statutory fund, contact your Challenger Business Development Manage

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www.challenger.com.au

Challenger Limited
Level 2
5 Martin Place
Sydney NSW 2000
Telephone 02 9994 7000
Facsimile 02 9994 7777