EEV disclosure

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European Embedded Value (EEV) basis results

PRUDENTIAL PLC 2008 PRELIMINARY ANNOUNCEMENT

EUROPEAN EMBEDDED VALUE (EEV) BASIS RESULTS

SUMMARY CONSOLIDATED INCOME STATEMENT

	2008 £m	2007 £m
Asian operations	1,335	1,099
US operations	593	635
UK operations:		
UK insurance operations	1,081	859
M&G	286	254
	1,367	1,113
Other income and expenditure	(302)	(297)
Restructuring costs	(32)	(20)
Operating profit from continuing operations based on longer-term investment returns	**2,961**	2,530
Short-term fluctuations in investment returns	(5,127)	174
Mark to market value movements on core borrowings	656	223
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(15)	(5)
Effect of changes in economic assumptions and time value of cost of options and guarantees	(581)	748
(Loss) profit from continuing operations before tax (including actual investment returns)	**(2,106)**	3,670
Tax attributable to shareholders' (loss) profit	771	(927)
(Loss) profit from continuing operations for the financial year after tax before minority interests	(1,335)	2,743
Discontinued operations (net of tax)	-	241
(Loss) profit for the year	**(1,335)**	2,984
Attributable to:		
Equity holders of the Company	(1,338)	2,963
Minority interests	3	21
(Loss) profit for the year	**(1,335)**	2,984

Earnings per share (in pence)	2008	2007
Continuing operations		
From operating profit, based on longer-term investment returns, after related tax and minority interests	88.6p	74.5p
Adjustment from post-tax longer-term investment returns to post-tax actual investment returns (after minority interests)	(150.3)p	6.1p
Adjustment for effect of mark to market value movements on core borrowings	26.6p	9.1p
Adjustment for post-tax effect of shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(0.5)p	(0.2)p
Adjustment for post-tax effect of changes in economic assumptions and time value of cost of options and guarantees (after minority interests)	(18.5)p	21.8p
Based on (loss) profit from continuing operations after tax and minority interests	(54.1)p	111.3p
Discontinued operations		
Based on profit from discontinued operations after tax and minority interests	-	9.9p
Based on (loss) profit for the year after tax and minority interests	**(54.1)p**	121.2p
Average number of shares (millions)	2,472	2,445

Dividends per share (in pence)

	2008	2007
Dividends relating to reporting period:		
Interim dividend (2008 and 2007)	5.99p	5.70p
Final dividend (2008 and 2007)	12.91p	12.30p
Total	18.90p	18.00p
Dividends declared and paid in reporting period:		
Current year interim dividend	5.99p	5.70p
Final dividend for prior year	12.30p	11.72p
Total	18.29p	17.42p

EUROPEAN EMBEDDED VALUE (EEV) BASIS RESULTS

OPERATING PROFIT FROM CONTINUING OPERATIONS BASED ON LONGER-TERM INVESTMENT RETURNS*

Results Analysis by Business Area	2008 £m	2007 £m
Asian operations		
New business	**741**	643
Business in force	**568**	399
Long-term business	**1,309**	1,042
Asset management	**52**	72
Development expenses	**(26)**	(15)
Total	**1,335**	1,099
US operations		
New business	**293**	285
Business in force	**293**	342
Long-term business	**586**	627
Broker-dealer and asset management	**10**	13
Curian	**(3)**	(5)
Total	**593**	635
UK operations		
New business	**273**	277
Business in force	**764**	578
Long-term business	**1,037**	855
General insurance commission	**44**	4
Total UK insurance operations	**1,081**	859
M&G	**286**	254
Total	**1,367**	1,113
Other income and expenditure		
Investment return and other income	**47**	49
Interest payable on core structural borrowings	**(172)**	(168)
Corporate expenditure:		
Group Head Office	**(130)**	(129)
Asia Regional Head Office	**(41)**	(38)
Charge for share-based payments for Prudential schemes	**(6)**	(11)
Total	**(302)**	(297)
Restructuring costs**	**(32)**	(20)
Operating profit from continuing operations based on longer-term investment returns	**2,961**	2,530
Analysed as profits (losses) from:		
New business	**1,307**	1,205
Business in force	**1,625**	1,319
Long-term business	**2,932**	2,524
Asset management	**345**	334
Other results	**(316)**	(328)
Total	**2,961**	2,530

* EEV basis operating profit from continuing operations based on longer-term investment returns excludes short-term fluctuations in investment returns, the mark to market value movements on core borrowings, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes, and the effect of changes in economic assumptions and changes in the time value of cost of options and guarantees arising from changes in economic factors. The amounts for these items are included in total EEV profit attributable to shareholders. The directors believe that operating profit, as adjusted for these items, better reflects underlying performance. Profit before tax and basic earnings per share include these items together with actual investment returns. This basis of presentation has been adopted consistently throughout this preliminary announcement.

** Restructuring costs comprise the charge of £28 million recognised on an IFRS basis and an additional £4 million recognised on the EEV basis for the shareholders' share of costs incurred by the PAC with-profits fund.

The results for continuing operations shown above exclude those in respect of discontinued banking operations, which were sold on 1 May 2007. In addition, there have been some minor adjustments to 2007 comparatives, as detailed in notes 4, 5 and 10.

EUROPEAN EMBEDDED VALUE (EEV) BASIS RESULTS

MOVEMENT IN SHAREHOLDERS' EQUITY (excluding minority interests)

	2008 £m	2007 £m
(Loss) profit for the year attributable to equity shareholders	**(1,338)**	2,963
Items taken directly to equity:		
Exchange movements (note 14)	**2,010**	64
Unrealised valuation movements on securities classified as available-for-sale of discontinued banking operations	**-**	(2)
Movement on cash flow hedges	**-**	(3)
Related tax	**119**	3
Dividends	**(453)**	(426)
New share capital subscribed	**170**	182
Reserve movements in respect of share-based payments	**18**	18
Treasury shares:		
Movement in own shares in respect of share-based payment plans	**3**	7
Movement on Prudential plc shares purchased by unit trusts consolidated under IFRS	**(25)**	4
Mark to market value movements on Jackson assets backing surplus and required capital	**(148)**	(13)
Net increase in shareholders' equity	**356**	2,797
Shareholders' equity at beginning of year (excluding minority interests):		
As previously reported	**14,779**	11,883
Effect of adoption of principles of IFRIC 14 for pension schemes (note 10)	**(179)**	(80)
After adoption of IFRIC 14	**14,600**	11,803
Shareholders' equity at end of year (excluding minority interests)	**14,956**	14,600
Comprising:		
Asian operations:		
Net assets	**5,431**	3,837
Acquired goodwill	**172**	172
	5,603	4,009
US operations	**4,453**	3,686
UK operations:		
Insurance business	**4,919**	6,497
M&G:		
Net assets	**147**	271
Acquired goodwill	**1,153**	1,153
	6,219	7,921
Other operations:		
Holding company net borrowings at market value (note 9)	**(818)**	(873)
Other net liabilities	**(501)**	(143)
Shareholders' equity at end of year (excluding minority interests)	**14,956**	14,600
Representing:		
Long-term business operations (note 12)	**14,522**	13,828
Other operations	**434**	772
	14,956	14,600

EUROPEAN EMBEDDED VALUE (EEV) BASIS RESULTS

SUMMARISED CONSOLIDATED BALANCE SHEET

	2008 £m	2007 £m
Total assets less liabilities, excluding insurance funds	**186,209**	195,596
Less insurance funds*:		
Policyholder liabilities (net of reinsurers' share) and unallocated surplus of with-profits funds	**(181,151)**	(189,534)
Less shareholders' accrued interest in the long-term business	**9,898**	8,538
	(171,253)	(180,996)
Total net assets	**14,956**	14,600
Share capital	**125**	123
Share premium	**1,840**	1,828
IFRS basis shareholders' reserves	**3,093**	4,111
Total IFRS basis shareholders' equity	**5,058**	6,062
Additional EEV basis retained profit	**9,898**	8,538
Shareholders' equity (excluding minority interests)	**14,956**	14,600

* Including liabilities in respect of insurance products classified as investment contracts under IFRS 4.

NET ASSET VALUE PER SHARE (in pence)

	2008	2007
Based on EEV basis shareholders' equity of £14,956m (2007: £14,600m)	**599p**	591p
Number of issued shares at year end (millions)	**2,497**	2,470

RETURN ON EMBEDDED VALUE**	**15.0%**	15.4%

** Return on embedded value is based on EEV operating profit from continuing operations after tax and minority interests as a percentage of opening EEV basis shareholders' equity.

EUROPEAN EMBEDDED VALUE (EEV) BASIS RESULTS

NOTES ON THE EEV BASIS RESULTS

1. Basis of preparation of results

The EEV basis results have been prepared in accordance with the EEV Principles issued by the CFO Forum of European Insurance Companies in May 2004 and expanded by the Additional Guidance on EEV Disclosures published in October 2005. Where appropriate the EEV basis results include the effects of adoption of International Financial Reporting Standards (IFRS).

The EEV results for the Group are prepared for 'covered business', as defined by the EEV Principles. Covered business represents the Group's long-term insurance business for which the value of new and in-force contracts is attributable to shareholders. The EEV basis results for the Group's covered business are then combined with the IFRS basis results of the Group's other operations.

The definition of long-term business operations is consistent with previous practice and comprises those contracts falling under the definition of long-term insurance business for regulatory purposes together with, for US operations, contracts that are in substance the same as guaranteed investment contracts (GICs) but do not fall within the technical definition. Under the EEV Principles, the results for covered business incorporate the projected margins of attaching internal asset management.

With two principal exceptions, covered business comprises the Group's long-term business operations. The principal exceptions are for the closed Scottish Amicable Insurance Fund (SAIF) and for the presentational treatment of the financial position of two of the Group's defined benefit pension schemes. A very small amount of UK group pensions business is also not modelled for EEV reporting purposes.

SAIF is a ring-fenced sub-fund of the Prudential Assurance Company (PAC) long-term fund, established by a Court approved Scheme of Arrangement in October 1997. SAIF is closed to new business and the assets and liabilities of the fund are wholly attributable to the policyholders of the fund.

As regards the Group's defined benefit pension schemes, the liabilities attaching to the Prudential Staff Pension Scheme (PSPS) and Scottish Amicable Pension Scheme are excluded from the EEV value of UK operations and included in the total for Other operations. The amounts are partially attributable to the PAC with-profits fund and shareholder-backed long-term business and partially to other parts of the Group. In addition to the amounts recognised as attributable to shareholders under IFRS, a 10 per cent share of the amount attributable to the PAC with-profits fund is recognised for EEV reporting purposes.

The directors are responsible for the preparation of the supplementary information in accordance with the EEV Principles.

The EEV basis results for 2008 and 2007 have been derived from the EEV basis results supplement to the Company's statutory accounts for 2008. The supplement included an unqualified audit report from the auditors.

2. Methodology

Embedded value
Overview
The embedded value is the present value of the shareholders' interest in the earnings distributable from assets allocated to covered business after sufficient allowance has been made for the aggregate risks in that business. The shareholders' interest in the Group's long-term business comprises:

- present value of future shareholder cash flows from in-force covered business (value of in-force business), less a deduction for the cost of locked-in (encumbered) capital;
- locked-in (encumbered) capital; and
- shareholders' net worth in excess of encumbered capital (free surplus).

The value of future new business is excluded from the embedded value. In determining the embedded value or the profit before tax no smoothing of market account balance values, unrealised gains or investment returns is applied. Separately the analysis of profit is delineated between operating profit based on longer-term investment returns and other constituent items, as explained in note 4.

Valuation of new business
The contribution from new business represents profits determined by applying non-economic assumptions as at the end of the year.

In determining the new business contribution for UK immediate annuity and lifetime mortgage business, which is interest rate sensitive, it is appropriate to use point of sale economic assumptions, consistent with how the business is priced. For other business within the Group end of period economic assumptions are used.

Level of encumbered capital
In adopting the EEV Principles, Prudential has based encumbered capital on its internal targets for economic capital subject to it being at least the local statutory minimum requirements. Economic capital is assessed using internal models but, when applying the EEV Principles, Prudential does not take credit for the significant diversification benefits that exist within the Group. For with-profits business written in a segregated life fund, as is the case in Asia and the UK, the capital available in the fund is sufficient to meet the encumbered capital requirements. For shareholder-backed business the following capital requirements apply:

- Asian operations: the economic capital requirement is substantially higher than local statutory requirements in total. Economic capital requirements vary by territory, but in aggregate, the encumbered capital is broadly equivalent to the amount required under the Insurance Groups Directive (IGD).
- US operations: the level of encumbered capital has been set to an amount at least equal to 235 per cent of the risk-based capital required by the National Association of Insurance Commissioners (NAIC) at the Company Action Level (CAL), which is sufficient to meet the economic capital requirement.
- UK insurance operations: the economic capital requirements for annuity business are fully met by Pillar I requirements being four per cent of mathematical reserves, which are also sufficient to meet Pillar II requirements. For unit-linked and other shareholder-backed business the encumbered capital held reflects the statutory minimum Pillar I requirement, as required by the UK regulatory authorities.

Valuation movements on investments
With the exception of debt securities held by Jackson, investment gains and losses during the period (to the extent that changes in capital values do not directly match changes in liabilities) are included directly in the profit for the period and shareholders' funds as they arise.

The results for any covered business conceptually reflects the aggregate of the IFRS results and the movements on the additional shareholders' interest recognised on the EEV basis. Thus the start point for the calculation of the EEV results for Jackson, as for other businesses, reflects the market value movements recognised on the IFRS basis.

However, in determining the movements on the additional shareholders' interest, the basis for calculating the Jackson EEV result acknowledges that for debt securities backing liabilities the aggregate EEV results reflect the fact that the value of in-force business instead incorporates the discounted value of future spread earnings. This value is not affected generally by short-term market movements on securities that are broadly speaking held with the intent and ability to be retained for the longer term.

Fixed income securities backing the free surplus and required capital for Jackson are accounted for at fair value. However, consistent with the treatment applied under IFRS for securities classified as available-for-sale, movements in unrealised appreciation on these securities are accounted for in equity rather than in the income statement, as shown in the movement in shareholders' equity.

3. <u>Economic assumptions</u>

(a) Deterministic assumptions
In most countries, the long-term expected rates of return on investments and risk discount rates are set by reference to period end rates of return on cash or fixed interest securities. For the Group's Asian operations, the active basis is appropriate for business written in Japan, Korea and US dollar denominated business written in Hong Kong. Except in respect of the projected returns of holdings of Asian debt and equity securities for those countries where long-term fixed interest markets are less established, the 'active' basis of assumption setting has been applied in preparing the results of all the Group's US and UK long-term business operations.

For countries where long-term fixed interest markets are less established, investment return assumptions and risk discount rates are based on an assessment of longer-term economic conditions. Except for the countries listed above, this basis is appropriate for the Group's Asian operations. Similarly, the projected returns on holdings of Asian securities in these territories by other Group business are set on the same basis.

Expected returns on equity and property asset classes in respect of each territory are derived by adding a risk premium, also based on the long-term view of Prudential's economists, to the risk-free rate. In Asia, equity risk premiums range from 3.0 per cent to 7.0 per cent (2007: 3.0 per cent to 6.0 per cent). In the US and the UK, the equity risk premium is 4.0 per cent above risk-free rates for both 2008 and 2007.

Assumed investment returns reflect the expected future returns on the assets held and allocated to the covered business at the valuation date.

The tables below summarise the principal financial assumptions:

Asian operations

	China	Hong Kong (notes iii, iv, v)	India	Indonesia	Japan	Korea	Malaysia (notes iv, v)	Philippines	Singapore (notes iv,v)	Taiwan (notes ii, v)	Thailand	Vietnam
	31 Dec 2008	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**	**31 Dec 2008**
	%	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Risk discount rate:												
New business	**11.75**	**3.8**	**14.25**	**15.25**	**4.8**	**8.2**	**9.1**	**15.75**	**6.15**	**9.1**	**13.0**	**16.75**
In force	**11.75**	**3.9**	**14.25**	**15.25**	**4.8**	**8.2**	**9.0**	**15.75**	**6.85**	**9.7**	**13.0**	**16.75**
Expected long-term rate of inflation	**4.0**	**2.25**	**5.0**	**6.0**	**0.7**	**2.75**	**2.75**	**5.0**	**1.75**	**2.25**	**3.0**	**6.0**
Government bond yield	**8.25**	**2.3**	**9.25**	**10.25**	**1.6**	**4.3**	**6.5**	**9.25**	**4.25**	**5.5**	**6.75**	**10.25**

	China	Hong Kong (notes iii, iv, v)	India	Indonesia	Japan	Korea	Malaysia (notes iv, v)	Philippines	Singapore (notes iv, v)	Taiwan (notes ii, v)	Thailand	Vietnam
	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007	31 Dec 2007
	%	%	%	%	%	%	%	%	%	%	%	%
Risk discount rate:												
New business	11.75	5.7	15.75	16.75	5.1	9.7	9.3	15.75	6.4	9.1	13.0	16.75
In force	11.75	6.0	15.75	16.75	5.1	9.7	9.1	15.75	6.8	9.8	13.0	16.75
Expected long-term rate of inflation	4.0	2.25	5.0	6.0	0.0	2.75	2.75	5.0	1.75	2.25	3.0	6.0
Government bond yield	8.25	4.1	9.25	10.25	2.0	5.8	6.5	9.25	4.25	5.5	6.75	10.25

	Asia total 31 Dec 2008 %	Asia total 31 Dec 2007 %
Weighted risk discount rate (note (i)):		
New business	**8.8**	9.5
In force	**7.8**	8.7

Notes

(i) The weighted risk discount rates for Asian operations shown above have been determined by weighting each country's risk discount rates by reference to the EEV basis operating result for new business and the closing value of in-force business.

(ii) For traditional business in Taiwan, the economic scenarios used to calculate the 2008 and 2007 EEV basis results reflect the assumption of a phased progression of the bond yields from the current rates applying to the assets held to the long-term expected rates.

For 2008 the projections assume that in the average scenario, the current bond yields at 31 December 2008 of 1.4 per cent trend towards 5.5 per cent at 31 December 2018. This compares to the 2007 results for which the projections assume that in the average scenario, the current bond yields at 31 December 2007 of around 2.5 per cent trend towards 5.5 per cent at 31 December 2013.

The expected long term rate is a function of expectation of inflation and real rates of interest, on which the Company has taken external expert advice. It is considered that the outlook for long-term interest rates in Asia will be strongly influenced by the trend in the projection of comparable US long-term real interest rates. Consequently assessment of the expected rates for Taiwan has taken into account the structural factors of government borrowing, savings rates, short-term interest rates, government intervention and non-market influences that could affect Taiwanese real interest rates over the projection period. Together with a central inflation projection for Taiwan, the Company considers that the long term rate of 5.5 per cent is appropriate in the longer-term.

In projecting forward the Fund Earned Rate, allowance is made for the mix of assets in the fund, future investment strategy, and further market value depreciation of bonds held as a result of assumed future yield increases. These factors, together with the assumption of the phased progression in bond yields, give rise to an average assumed Fund Earned Rate that changes from 6.6 per cent for 2008 to 6.7 per cent for 2019. The assumed Fund Earned Rate falls to 3.35 per cent in 2009 and subsequently to 1.2 per cent in 2010, then increases to 5.15 per cent by 2018. Thereafter, the assumed Fund Earned Rate fluctuates around a target of 6.7 per cent. This projection compares with that applied for the 2007 results of a grading from an assumed rate of 0.5 per cent for 2007 to 6.4 per cent for 2014.

Consistent with the EEV methodology applied, a constant discount rate has been applied to the projected cash flows.

On 20 February 2009, the Company announced that it had agreed to transfer the agency business of the Taiwan Life business to China Life. Further details are given in note 11.

(iii) The assumptions shown are for US dollar denominated business which comprises the largest proportion of the in-force Hong Kong business.

(iv) The mean equity return assumptions for the most significant equity holdings in the Asian operations were:

	31 Dec 2008 %	31 Dec 2007 %
Hong Kong	**6.2**	8.1
Malaysia	**12.5**	12.5
Singapore	**10.2**	9.3

To obtain the mean, an average over all simulations of the accumulated return at the end of the projection period is calculated. The annual average return is then calculated by taking the root of the average accumulated return minus 1.

(v) For 2008 and 2007, cash rates rather than government bond yields were used in setting risk discount rates for Malaysia, Singapore, Taiwan and for Hong Kong dollar denominated business.

US operations (Jackson)	**31 Dec 2008 %**	31 Dec 2007 %
Risk discount rate (note (i)):		
New business	**4.6**	7.0
In force	**3.9**	6.0
Expected long-term spread between earned rate and rate credited to policyholders for single premium deferred annuity business	**1.75**	1.75
US 10-year treasury bond rate at end of period	**2.3**	4.1
Pre-tax expected long-term nominal rate of return for US equities	**6.3**	8.1
Expected long-term rate of inflation	**1.5**	2.4

Notes

(i) The risk discount rates at 31 December 2008 for new business and business in-force for US operations reflect weighted rates based on underlying rates of 6.2 per cent for variable annuity (VA) business and 3.0 per cent for other business. The decrease in the weighted discount rates reflects the decrease in the US 10-year treasury bond rate of 180 bps and a change in the product mix with the 2008 results seeing an increase in the proportion of new and in-force business arising from other than VA business.

(ii) Credit risk treatment

The projected cash flows incorporate the expected long-term spread between the earned rate and the rate credited to policyholders. The projected earned rates reflect book value yields which are adjusted over time to reflect projected reinvestment rates. The expected spread incorporates a Risk Margin Reserve (RMR) allowance of 25 basis points for longer-term defaults as described in note 4.

In the event that longer-term default levels are higher then, unlike for UK annuity business where policyholder benefits are not changeable, Jackson has some discretion to adjust crediting rates, subject to contract guarantee levels and general market competition considerations.

The results for Jackson reflect the application of the low discount rates shown above. In the event that US 10-year treasury rates increase, the altered embedded value results would reflect a lower contribution from fixed annuity business and a partially offsetting increase for variable annuity business as the projected earned rate, as well as the discount rate, would increase for this type of business.

The book value yields, net of RMR allowance, are in excess of the risk discount rate. To correct for the anomalous effect that would otherwise occur no credit has been taken for the cost of capital benefit that this feature would give rise to for fixed annuity business.

UK insurance operations	31 Dec 2008 %	31 Dec 2007 %
Shareholder-backed annuity business:		
Risk discount rate (notes (i) and (iv))		
New business	**9.6**	7.8
In force	**12.0**	7.8
Pre-tax expected long-term nominal rate of return for shareholder-backed annuity business (note (iii)):		
Fixed annuities	**6.4 to 6.7**	5.4 to 5.6
Inflation-linked annuities	**5.7 to 5.8**	5.0 to 5.2
Other business:		
Risk discount rate (notes (ii) and (iv))		
New business	**6.7**	7.0
In force	**6.75**	7.9
Pre-tax expected long-term nominal rates of investment return:		
UK equities	**7.7**	8.55
Overseas equities	**6.3 to 10.25**	8.1 to 10.2
Property	**6.0**	6.8
Gilts	**3.7**	4.55
Corporate bonds – with-profits funds (notes (iv) and (v))	**5.2**	6.0
– other business	**5.2**	6.25
Expected long-term rate of inflation	**3.0**	3.2
Post-tax expected long-term nominal rate of return for the PAC with-profits fund:		
Pension business (where no tax applies)	**6.6**	7.85
Life business	**5.8**	6.9

Notes

(i) The new business risk discount rate for shareholder-backed annuity business for 2008 reflects the assets allocated to back new business with an allowance for credit risk based on point of sale market conditions, consistent with how the business was priced. The allowance for credit risk for new business at point of sale is determined using the same methodology for in-force business described in note (iv) below.

(ii) The risk discount rate for new business and business in force for UK insurance operations other than shareholder-backed annuities reflect weighted rates based on the type of business.

(iii) The pre-tax rates of return for shareholder-backed annuity business are based on the gross redemption yield on the backing assets net of a best estimate allowance for future defaults.

(iv) Credit spread treatment

For with-profits business, the embedded value reflects the discounted value of future shareholder transfers. These transfers are directly affected by the level of projected rates of return on investments, including debt securities. Given the current exceptional fixed interest market conditions, and the Company's expectation that the widening of credit spreads observed in 2008 will not be maintained, the Company considers that it is most appropriate to assume an unchanged level of credit spreads, an unchanged level of longer-term default allowance and an unchanged risk discount rate methodology relative to those used at 31 December 2007.

For UK annuity business, different dynamics apply both in terms of the nature of the business and the EEV methodology applied. For this type of business the assets are generally held to maturity to match long duration liabilities. It is therefore appropriate under EEV methodology to include a liquidity premium in the economic basis used. The appropriate EEV risk discount rate is set in order to equate the EEV with a "market consistent embedded value" including liquidity premium. The liquidity premium is derived from the yield on the assets held after deducting an appropriate allowance for credit risk. For Prudential Retirement Income Limited (PRIL), which has approximately 90 per cent of UK shareholder-backed annuity business, the allowance for credit risk at 31 December 2008 is made up of:

a 16 bps for fixed annuities and 13 bps for inflation-linked annuities in respect of long-term expected defaults; this is derived by applying Moody's data from 1970 onwards uplifted by between 100 per cent (B) and 200 per cent (AAA) according to credit rating, to the asset portfolios.

b 11 bps for fixed annuities and 9 bps for inflation-linked annuities in respect of long-term credit risk premium for the potential volatility in default levels; this is derived by applying the 95th worst percentile from Moody's data from 1970 onwards, to the asset portfolios.

c 56 bps for fixed annuities and 48 bps for inflation-linked annuities in respect of additional short-term credit risk, reflecting the extreme market conditions at 31 December 2008; this is derived as 25 per cent of the increase in credit spreads over swaps that has occurred since 31 December 2006 based on a set of externally published indices weighted to reflect the asset mix.

On a weighted basis for fixed annuities and inflation-linked annuities the allowance is 15 bps for long-term expected defaults, 11 bps for long-term credit risk premium, and 54 bps for short-term credit risk.

Pillar I reserves are calculated using a similar allowance for credit risk. For EEV reporting the allowance for short-term credit risk is assumed to be released gradually over the five year period following the valuation date.

The Pillar I allowance of 80 bps per annum is financially equivalent to 185 bps for the years 2009 to 2011 and 45 bps thereafter for the life of the book.

The overall allowance for credit risk is prudent by comparison with historic rates of default and would be sufficient to withstand a wide range of extreme credit events over the expected lifetime of the annuity business.

The risk discount rate for new business profits reflects the assets allocated to back new business and an allowance for credit risk based on point of sale market conditions, consistent with how the business was priced. The allowance for credit risk at the point of sale is determined using the same methodology for in-force business. In both cases, the allowance for credit risk included in setting the discount rate reflects the three constituent elements of long-term expected defaults, long-term credit risk premiums, and additional short-term credit risk.

(v) The assumed long-term rate for corporate bonds for 2007 for with-profits business was determined after taking account of the purchase of credit default swaps.

(b) Stochastic assumptions

The economic assumptions used for the stochastic calculations are consistent with those used for the deterministic calculations described above. Assumptions specific to the stochastic calculations, such as the volatilities of asset returns, reflect local market conditions and are based on a combination of actual market data, historic market data and an assessment of longer-term economic conditions. Common principles have been adopted across the Group for the stochastic asset models, for example, separate modelling of individual asset classes but with allowance for correlation between the various asset classes.

Details are given below of the key characteristics and calibrations of each model.

Asian operations

The same asset return models as used in the UK, appropriately calibrated, have been used for the Asian operations as described for UK insurance operations below. The principal asset classes are government and corporate bonds. Equity holdings are much lower than in the UK whilst property holdings do not represent a significant investment asset.

The stochastic cost of guarantees is primarily only of significance for the Hong Kong, Malaysia, Singapore and Taiwan operations.

The mean stochastic returns are consistent with the mean deterministic returns for each country. The expected volatility of equity returns for 2008 ranges from 18 per cent to 30 per cent (2007: 18 per cent to 25 per cent), and the volatility of government bond yields ranges from 1.4 per cent to 2.4 per cent (2007: 1.3 per cent to 2.5 per cent).

US operations (Jackson)

- Interest rates are projected using a log-normal generator calibrated to actual market data;
- Corporate bond returns are based on Treasury securities plus a spread that has been calibrated to current market conditions and varies by credit quality; and
- Variable annuity equity and bond returns have been stochastically generated using a log-normal model with parameters determined by reference to historical data. The volatility of equity fund returns for both 2008 and 2007 ranges from 18.6 per cent to 28.1 per cent, depending on risk class, and the standard deviation of bond returns ranges from 1.5 per cent to 1.6 per cent (2007: 1.4 per cent to 1.7 per cent).

UK insurance operations

- Interest rates are projected using a two-factor model calibrated to actual market data;
- The risk premium on equity assets is assumed to follow a log-normal distribution;
- The corporate bond return is calculated as the return on a zero-coupon bond plus a spread. The spread process is a mean reverting stochastic process; and
- Property returns are modelled in a similar fashion to corporate bonds, namely as the return on a riskless bond, plus a risk premium, plus a process representative of the change in residual values and the change in value of the call option on rents.

Mean returns have been derived as the annualised arithmetic average return across all simulations and durations.

For each projection year, standard deviations have been calculated by taking the square root of the annualised variance of the returns over all the simulations. These have been averaged over all durations in the projection. For equity and property, the standard deviations relate to the total return on these assets. The standard deviations applied to both 2008 and 2007 are as follows:

	%
Equities:	
UK	18.0
Overseas	16.0
Property	15.0

4. Accounting presentation

Analysis of profit before tax
To the extent applicable, presentation of the EEV profit for the year is consistent with the basis that the Group applies for analysis of IFRS basis profits before shareholder taxes between operating and non-operating results. Operating results reflect the underlying results of the Group's continuing operations including longer-term investment returns. Operating results include the impact of routine changes of estimates and non-economic assumptions. Non operating results comprise short-term fluctuations in investment returns, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes, the mark to market value movements on core borrowings and the effect of changes in economic assumptions and changes in the time value of cost of options and guarantees.

Operating profit
Investment returns, including investment gains, in respect of long-term insurance business are recognised in operating results at the expected long-term rate of return. For the purpose of calculating the longer-term investment return to be included in the operating results of UK operations, where equity holdings are a significant proportion of investment portfolios, values of assets at the beginning of the reporting period are adjusted to remove the effects of short-term market volatility.

For the purposes of determining the long-term returns for debt securities of shareholder-backed operations, a risk margin charge is included which reflects the expected long-term rate of default based on the credit quality of the portfolio. For Jackson, interest-related realised gains and losses are amortised to the operating results over the maturity period of the sold bonds and for equity-related investments, a long-term rate of return is assumed, which reflects the aggregation of risk-free rates and equity risk premium. For US variable annuity separate account business, operating profit reflects the expected longer-term rate of return with the excess or deficit of the actual return recognised within non-operating profit, together with the related hedging activity.

For UK annuity business, rebalancing of the asset portfolio backing the liabilities to policyholders may from time to time take place to align it more closely with the internal benchmark of credit quality that management applies. Such rebalancing will result in a change in the risk adjusted yield on the assets used to determine the valuation interest rate for calculating the carrying value of policyholder liabilities. Operating profit includes the effect of rebalancing the portfolio calibrated to investment conditions at 31 December 2006 i.e. prior to the exceptional spread widening in 2007 and 2008. Non-operating profit incorporates the effect of rebalancing calibrated by reference to changes to credit spreads since 31 December 2006.

Previously, for the purpose of presentation of the Group's operating results, the return on capital held centrally to back the economic capital requirements for the Taiwan life business has been allocated to the operating result for Asian operations with a consequent reduction in Group shareholders' other income for EEV basis reporting. In the 2008 results this approach has no longer been applied. The presentation of the 2007 comparative results has been adjusted accordingly, as explained in note 6(iv).

Effect of changes in economic assumptions and time value of cost of options and guarantees
Movements in the value of in-force business caused by changes in economic assumptions and the time value of cost of options and guarantees resulting from changes in economic factors are recorded in non-operating results.

5. Margins on new business premiums

	New Business Premiums		Annual Premium and Contribution Equivalents	Present Value of New Business Premiums	Pre-Tax New Business Contribution (notes (ii) and (iii))	New Business Margin (note (i))	
	Single	Regular	(APE)	(PVNBP)		(APE)	(PVNBP)
2008	£m	£m	£m	£m	£m	%	%
Asian operations (note (iv))	**1,457**	**1,216**	**1,362**	**7,308**	**741**	**54**	**10.1**
US operations	**6,917**	**24**	**716**	**7,140**	**293**	**41**	**4.1**
UK insurance operations (note (vi))	**6,929**	**254**	**947**	**8,081**	**273**	**29**	**3.4**
Total	**15,303**	**1,494**	**3,025**	**22,529**	**1,307**	**43**	**5.8**

2007	New Business Premiums Single	New Business Premiums Regular	Annual Premium and Contribution Equivalents (APE)	Present Value of New Business Premiums (PVNBP)	Pre-Tax New Business Contribution (notes (ii) and (iii))	New Business Margin (note (i)) (APE)	New Business Margin (note (i)) (PVNBP)
	£m	£m	£m	£m	£m	%	%
Asian operations (notes (iv) and (v))	1,793	1,108	1,287	6,906	643	50	9.3
US operations	6,515	19	671	6,666	285	42	4.3
UK insurance operations (note (vi))	6,632	247	910	7,736	277	30	3.6
Total	14,940	1,374	2,868	21,308	1,205	42	5.7

Notes

(i) New business margins are shown on two bases, namely the margins by reference to Annual Premium and Contribution Equivalents (APE) and the Present Value of New Business Premiums (PVNBP). APEs are calculated as the aggregate of regular new business amounts and one-tenth of single new business amounts. PVNBPs are calculated as equalling single premiums plus the present value of expected premiums of new regular premium business, allowing for lapses and other assumptions made in determining the EEV new business contribution.

(ii) In determining the EEV basis value of new business written in the year the policies incept, premiums are included in projected cash flows on the same basis of distinguishing annual and single premium business as set out for statutory basis reporting.

(iii) In general, as described in note 3, the use of point of sale or end of period economic assumptions is not significant in determining the new business contribution for different types of business and across financial reporting periods. However, to obtain proper measurement of the new business contribution for business which is interest rate sensitive, it is appropriate to use point of sale economic assumptions, consistent with how the business was priced. In practice, the only area within the Group where this has a material effect, particularly in light of the dislocation of markets in 2008, is for UK shareholder-backed annuity and lifetime mortgage business. The 2008 results for shareholder-backed annuity and lifetime mortgage business have been prepared on the basis of point of sale rather than end of period economic assumptions which previously applied for EEV reporting. New business profits would have been £111 million lower if end of year economic assumptions had been applied. The reduction is reflected in non-operating profit. The £111 million primarily reflects the level of credit spread widening since the point of sale. For 2007, the effect of the use of point of sale market conditions would not have been material.

New business contributions for all business represent profits determined by applying non-economic assumptions as at the end of the year.

(iv) The results for Asian operations include those of the Taiwanese life operations for which the Company agreed to transfer its agency business to China Life on 20 February 2009. Details are included in note 11.

(v) The tables for Asian operations above reflect the inclusion of CITIC-Prudential Life Insurance Company Ltd, the Group's life operation in China as a 50 per cent held joint venture for 2008 and 2007 reflecting the economic interest throughout both years. Previously, for presentational purposes, the 2007 results reflected the inclusion of CITIC-Prudential as a subsidiary undertaking up to 29 September 2007 and 50 per cent thereafter following the change of management arrangement after this date, with appropriate minority interest accounting to reflect the 50 per cent economic interest. The presentation of the operating profit for 2007 has been adjusted to allocate £10 million of profit from the result for new business to business in-force to prevent distortion of the published new business margin.

(vi) To align with the treatment in the 2008 results, the tables for UK insurance operations above for 2007 reflect the inclusion of the Group's UK health insurance joint venture operation, PruHealth, with an APE of £13 million and PVNBP of £107 million.

6. Operating profit from business in-force

2008	**Unwind of discount and other expected returns (note (i))**	**Effect of change in operating assumptions (note (ii))**	**Experience variances and other items (note (iii))**	**Total**
	£m	**£m**	**£m**	**£m**
Asian operations	**434**	**135**	**(1)**	**568**
US operations	**233**	**(17)**	**77**	**293**
UK insurance operations	**569**	**-**	**195**	**764**
Total	**1,236**	**118**	**271**	**1,625**

2007	Unwind of discount and other expected returns (note (i)) £m	Effect of change in operating assumptions £m	Experience variances and other items (notes (iii), (iv) and (v)) £m	Total £m
Asian operations	340	54	5	399
US operations	240	(24)	126	342
UK insurance operations	592	67	(81)	578
Total	1,172	97	50	1,319

Notes

(i) The increase in unwind of discount and other expected returns in 2008 over 2007 mainly arises in Asian operations, reflecting the growth in opening value from 1 January 2007 to 1 January 2008 on which the value of in-force business unwinds.

(ii) The effect of changes in operating assumptions for Asian operations in 2008 of a credit of £135 million reflects favourable effects arising from changes in mortality and morbidity assumptions of £58 million, the effect of changes in lapse rates of £36 million, the effect of changes in expense assumptions of £26 million and the impact of incorporating the benefit arising on the change of corporate tax rate in Indonesia of £15 million.

(iii) Experience variances and other items for UK insurance operations in 2008 are in aggregate a credit of £195 million. Consistent with the methodology applied in previous years, this amount includes a credit of £118 million resulting from part of the effect of rebalancing the asset portfolio backing annuity business on the valuation interest rate for determining Pillar I liabilities. The rebalancing reflects changes to the portfolio to more closely align the credit quality with management benchmark. The £118 million effect of rebalancing included in operating profit reflects longer-term levels of credit spread evident as at 31 December 2006 i.e. prior to the exceptional credit spread widening in 2007 and 2008. The additional increase in the Pillar I valuation interest rate due to rebalancing at the credit spreads at which assets were traded in 2008 is reflected within non-operating profit together with, via the increase in discount rate, the additional allowance for credit risk for the portfolio as a whole as described in note 8. The £195 million credit also includes a cost of capital charge of £(34) million for the effect of holding the short-term credit risk reserve for statutory reporting, as described in note 3, and releasing it over an assumed five year period. Also included in operating profit for business in-force is a credit of £56 million in respect of the release of certain annuity business reserves, a credit of £24 million in respect of the release of prior period provisions relating to Credit Life business, and a net credit of £31 million for other items.

Experience variances and other items for US operations of £77 million for 2008 include a credit of £54 million in respect of spread experience variance.

(iv) The 2007 comparative result for Asian operations has been increased by £10 million for the adjustment in respect of China (as explained in note 5) and reduced by £(4) million for the discontinuance of the allocation of notional return on centrally held economic capital in respect of Taiwan from shareholders' other income to the result for Asian operations, as explained in note 4. Other income is increased by an equivalent amount. Total profits are unaffected by these adjustments.

(v) The 2007 comparative result for UK insurance operations has been reduced by £4 million in respect of the separate disclosure of UK general insurance commission. Total operating profit from UK insurance operations is unaffected by this adjustment.

7. Short-term fluctuations in investment returns

	2008 £m	2007 £m
Insurance operations:		
Asia (note (i))	**(1,063)**	226
US (note (ii))	**(1,344)**	(9)
UK (note (iii))	**(2,407)**	(42)
Other operations (note (iv))	**(313)**	(1)
Total	**(5,127)**	174

Notes

(i) Asian operations

	2008 £m
Singapore	(310)
Hong Kong	(284)
Taiwan	(163)
Other operations	(306)
	(1,063)

For Singapore and Hong Kong, the short-term fluctuations primarily reflect the effect of substantial equity market falls on unit-linked and with-profits business. The short-term fluctuations for Taiwan principally reflect the equity market fall and a £(40) million value reduction for an investment in a CDO fund.

(ii) US operations (Jackson)

The short-term fluctuations in investment returns for US operations primarily reflect the impact of impairment losses on debt securities and the effects on the value of variable annuity business of adverse movements in US equity markets. The fluctuations for US operations comprise the following items:

	2008 £m	2007 £m
Realised impairment losses:		
Actual losses on fixed income securities	**(466)**	(78)
Less: Risk margin charge included in operating profit	**54**	48
	(412)	(30)
Loss due to changed expectation of profits from fees on in-force variable annuity business in future periods based on current period equity returns, net of related hedging activity*	**(733)**	(16)
Actual less longer-term return on equity-type securities	**(148)**	51
Other	**(51)**	(14)
	(1,344)	(9)

* This adjustment arises due to the market returns being lower than the assumed longer-term rate of return. This gives rise to lower than expected year end values of variable annuity assets under management with a resulting effect on the projected value of future account values and hence future profitability from altered fees. For 2008, the US equity market returns were approximately negative 38.5 per cent compared to the assumed longer-term rate of return of 5.8 per cent.

(iii) UK insurance operations

The short-term fluctuations in investment returns for UK insurance operations for 2008 arise on the following types of business:

	2008 £m
With-profits (note (a))	**(2,083)**
Shareholder-backed annuity (note (b))	**(213)**
Unit-linked and other (note (c))	**(111)**
	(2,407)

Notes

(a) For with-profits business the charge represents the negative actual investment return on the PAC with-profits fund of (19.7) per cent against an assumed rate of 6.6 per cent.

(b) Short-term fluctuations on shareholder-backed annuity business represents the unrealised loss on surplus assets and default experience.

(c) The charge of £(111) million relates primarily to unit-linked business and predominantly represents the capitalised loss of future fees from the fall in market values experienced during the year.

(iv) Other operations

Details on the charge of £(313) million for short-term fluctuations for other operations is shown in note F to the IFRS basis results.

8. Effect of changes in economic assumptions and time value of cost of options and guarantees

The (losses) profits on changes in economic assumptions and time value of cost of options and guarantees resulting from changes in economic factors for in-force business included within the (loss) profit from continuing operations before tax (including actual investment returns) arise as follows:

	2008			2007		
	Change in economic assumptions £m	**Change in time value of cost of options and guarantees £m**	**Total £m**	Change in economic assumptions £m	Change in time value of cost of options and guarantees £m	Total £m
Asian operations (note (i))	**(34)**	**8**	**(26)**	201	9	210
US operations (note (ii))	**267**	**11**	**278**	81	8	89
UK insurance operations (notes (iii) and (iv))	**(783)**	**(50)**	**(833)**	466	(17)	449
Total	**(550)**	**(31)**	**(581)**	748	0	748

Notes

(i) The effect of changes in economic assumptions in Asia for 2008 of a charge of £(34) million includes a negative effect in Taiwan of £(185) million reflecting a charge of £(239) million for the impact of extending the phased bond yield progression period in Taiwan out by five years from 31 December 2013 to 31 December 2018, as described in note 3, offset by the impact in other territories, mainly reflecting the reduction in risk discount rates.

(ii) The credit for the effect of changes in economic assumptions for 2008 for US operations of £267 million primarily arises as a result of the impact of a change in the risk discount rate of £454 million, partially offset by the impact of a decrease in the variable annuity separate account return of £(230) million, both movements reflecting the 180 bps reduction in the 10-year Treasury rate as shown in note 3.

(iii) The effect of changes in economic assumptions of a charge of £(783) million for UK insurance operations comprises the effect of:

	Shareholder-backed annuity business (note (a)) £m	With-profits and other business (note (b)) £m	2008 £m
Increase (decrease) in portfolio yields	**83**	**(1,082)**	**(999)**
(Increase) decrease in risk discount rates	**(394)**	**668**	**274**
Other changes	**(6)**	**(52)**	**(58)**
	(317)	**(466)**	**(783)**

Notes

(a) For shareholder-backed annuity business (i.e. held in PRIL and the PAC non-profit sub-fund) the impact of the change in risk discount rate of £(394) million includes £(400) million in respect of strengthening credit risk assumptions (excluding the strengthening required in respect of the £2.8 billion rebalancing of the asset portfolios). The impact of the change in portfolio yields of £83 million includes a profit of £231 million in respect of the rebalancing, calculated by reference to changes in credit spreads since 31 December 2006.

(b) For with-profits and other business the decrease in fund earned rates and risk discount rates primarily reflects the reduction in gilt rates of (0.85) per cent.

(iv) The effect of changes in time value of cost of options and guarantees of a charge of £(50) million primarily relates to with-profits business reflecting the effect of the reduction in fund earned rates, as described in note (iii)(b) above.

9. Holding company net borrowings at market value

Holding company net borrowings at market value comprise:

	31 Dec 2008 £m	31 Dec 2007 £m
Holding company borrowings:		
IFRS basis	**2,785**	2,367
Mark to market value adjustment	**(802)**	(38)
EEV basis (note)	**1,983**	2,329
Holding company* cash and short-term investments	**(1,165)**	(1,456)
Holding company net borrowings	**818**	873

*Including central finance subsidiaries.

Note

EEV basis holding company borrowings comprising:

	2008 £m	2007 £m
Perpetual subordinated capital securities (Innovative Tier 1)	**513**	679
Subordinated debt (Lower Tier 2)	**737**	817
Senior debt	**733**	833
	1,983	2,329

10. Adoption of the principles of IFRIC 14 for pension schemes

To provide consistency with the basis applied for IFRS reporting, the EEV basis results reflect adoption of the principles of IFRIC 14 for pension schemes. The impact of the adoption is as follows:

	2008			2007		
	Previous basis £m	**Effect of adoption £m**	**Revised basis £m**	As published £m	Effect of adoption £m	After change £m
Operating profit from continuing operations based on longer-term investment returns	**2,992**	**(31)**	**2,961**	2,542	(12)	2,530
Short-term fluctuations in investment returns	**(5,127)**		**(5,127)**	174		174
Mark to market value movements on core borrowings	**656**		**656**	223		223
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	**17**	**(32)**	**(15)**	116	(121)	(5)
Effect of changes in economic assumptions and time value of cost of options and guarantees	**(581)**		**(581)**	748		748
(Loss) profit before tax	**(2,043)**	**(63)**	**(2,106)**	3,803	(133)	3,670
Tax	**754**	**17**	**771**	(961)	34	(927)
(Loss) profit after tax	**(1,289)**	**(46)**	**(1,335)**	2,842	(99)	2,743
Discontinued operations	**-**	**-**	**-**	241	-	241
Less minority interests	**(3)**	**-**	**(3)**	(21)	-	(21)
(Loss) profit for the year	**(1,292)**	**(46)**	**(1,338)**	3,062	(99)	2,963
Other movements in reserves	**1,694**	**-**	**1,694**	(166)	-	(166)
Shareholders' equity at beginning of year	**14,779**	**(179)**	**14,600**	11,883	(80)	11,803
Shareholders' equity at end of year	**15,181**	**(225)**	**14,956**	14,779	(179)	14,600

The changes reflect the aggregate of those under IFRS, as shown in note Q to the Group IFRS results, and the shareholders' 10 per cent interest in the PAC with-profits element of the effect of the change in accounting policy reflected under EEV reporting.

11. Intended sale of legacy agency book and agency force in Taiwan to China Life Insurance of Taiwan

On 20 February 2009, the Company announced that it had entered into an agreement to sell the assets and liabilities of its agency distribution business and its agency force in Taiwan to China Life Insurance Company Ltd of Taiwan for the nominal sum of NT$1. In addition, Prudential will invest £45 million to purchase a 9.95 per cent stake in China Life through a share placement. The business being transferred represents 94 per cent of Prudential's in-force liabilities in Taiwan and includes Prudential's legacy interest rate guaranteed products. The transfer is subject to regulatory approval.

After taking account of EEV shareholders' funds at 31 December 2008 of the business and restructuring and other costs the Group's EEV shareholders' equity is expected to increase by approximately £90 million.

The movement in shareholders' EEV equity of the total Taiwan life business for 2008 comprised:

	£m
Operating profit based on longer-term investment returns from:	
New business	120
Business in force	(16)
Total	104
Short-term fluctuations in investment returns	(163)
Effect of changes in economic assumptions and time value of cost of options and guarantees	(185)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(3)
Loss before tax	(247)
Total tax	12
Minority interests	2
Loss for the financial year	(233)
Investment by parent company (note (i))	93
Exchange and other reserve movements	(53)
Net movement	(193)
Shareholders' equity at 1 January 2008	(12)
Shareholders' equity at 31 December 2008	(205)

Note

(i) Comprising £66 million for solvency capital and £27 million for business developments.

12. Movement in Embedded value

The following analysis shows the movements in embedded value arising from the Group's underlying business activity and the effects of the current extraordinary market conditions.

Group		Free Surplus (note (ii)) £m	Required Capital (note (iii)) £m	Net Worth £m	Value of in-force £m	Total £m
Underlying movement						
New business		(825)	472	(353)	1,290	937
Business in force	- expected transfer	1,413	(416)	997	(997)	-
	- unwind of discount, effects of changes in operating assumptions, operating experience variances and other operating items (note (vii))	(11)	299	288	928	1,216
		577	355	932	1,221	2,153
Investment movements and economic effects:						
UKIO additional credit provisions (note (iv))		(770)	41	(729)	705	(24)
Jackson impairment losses in excess of longer term expected returns net of defaults		(268)	0	(268)	0	(268)
Other investment movements and effect of changes in economic assumptions (note (v))		(647)	165	(482)	(3,145)	(3,627)
		(1,685)	206	(1,479)	(2,440)	(3,919)
Net cash flows to parent company (note (viii))		(166)	0	(166)	(132)	(298)
Other items (note (ix))		253	686	939	1,819	2,758
Net movement		(1,021)	1,247	226	468	694
Balance at 1 January 2008		1,468	2,870	4,338	9,490	13,828
Balance at 31 December 2008		447	4,117	4,564	9,958	14,522

Notes

(i) All figures are shown net of tax.

(ii) Free surplus is the market value of the net worth in excess of the capital required to support the covered business. Where appropriate, adjustments are made to the regulatory basis net worth from the local regulatory basis so as to include backing assets movements at fair value rather than cost so as to comply with the EEV principles.

(iii) Prudential has based required capital on its internal targets for economic capital subject to it being at least the local statutory minimum requirements, as described in note 2.

(iv) The increase in UKIO credit provisions reflects the allowances explained in note 3.

(v) Other investment movements and effect of changes in economic assumptions represent:

	Free Surplus (note ii) £m	Required Capital (note iii) £m	Net Worth £m	Value of in-force £m	Total £m
Other investment movements (note (vi))	(681)	(27)	(708)	(2,496)	(3,204)
Effect of changes in economic assumptions (note (vii))	34	192	226	(649)	(423)
	(647)	165	(482)	(3,145)	(3,627)

(vi) Other investment movements primarily reflect temporary market movements on the portfolio of investments held by the Group's shareholder-backed operations together with the shareholders' 10 per cent interest in the value movements on the assets in the with-profits funds.

(vii) The underlying movement in free surplus includes £85 million for the effect of rebalancing the asset portfolio for UK annuity business, as described in note 6. The effect of changes in economic assumptions on free surplus includes a credit of £166 million in respect of rebalancing as described in note 8.

(viii) Net cash flows to or from parent company reflect the flows for long-term business operations as included in the holding company cash flow at transaction rate.

(ix) Other items represent:

	Free Surplus (note ii) £m	Required Capital (note iii) £m	Net Worth £m	Value of in-force £m	Total £m
Exchange movements (note 14)	76	823	899	1,535	2,434
Mark to market value movements on Jackson assets backing surplus and required capital	(148)		(148)		(148)
Other (note x)	325	(137)	188	284	472
	253	686	939	1,819	2,758

(x) The effect of other items on total embedded value of £472 million primarily relate to the impact on free surplus of an intra-group capital adjustment in respect of UK insurance operations of £320 million, an adjustment for funds loaned to the parent company of £133 million from Singapore and an adjustment of £50 million to reflect the cash flows to parent company at year end rates of exchange consistent with the closing embedded value. Also included is a net overall charge of £(40) million for the reallocation of certain statutory reserves for UK insurance and US operations, an adjustment to required capital and the reallocation of surplus note borrowings for US operations. The effect of these adjustments is a decrease in free surplus of £(187) million, a reduction in required capital of £(137) million and an increase in the value of in-force business of £284 million.

13. Expected transfer of value of in-force business to free surplus

The discounted value of in-force and required capital at 31 December 2008 can be reconciled to the analysis of free surplus crystallisation as follows:

	2008 £m
Required capital (note 12)	4,117
Value of in-force (VIF) (note 12)	9,958
Add: Cost of time value of guarantees	474
Other items	(181)
	14,368

Other items includes the deduction of the value of the shareholders' interest in the Estate, the value of which is derived by increasing final bonus rates so as to exhaust the Estate over the lifetime of the in-force with-profits business. This is an assumption to give an appropriate valuation. To be conservative this item is excluded from the value of the Estate from the expected free surplus generation profile below. Offset against this value are amounts treated as capital for regulatory purposes (and hence treated as capital for net worth purposes) but which are deducted in full against the VIF (i.e. the full undiscounted value).

Cash flows are projected on a certainty equivalent basis and are discounted at the appropriate risk discount rate. The modelled cash flows use the same methodology underpinning the Group's embedded value methodology reporting and so is subject to the same assumptions and sensitivities.

The table below shows how the VIF generated by the in-force business at 31 December 2008 and the associated required capital is modelled as emerging into free surplus over future years.

		2008				
		Expected period of conversion of future post tax distributable earnings and required capital flows to free surplus				
	Total £m	1-5 years £m	6-10 years £m	11-15 years £m	16-20 years £m	20+ years £m
Asian operations	5,373	1,746	1,150	859	564	1,054
US operations	4,374	2,415	1,167	460	180	152
UK insurance operations	4,621	2,297	975	600	389	360
Total	14,368	6,458	3,292	1,919	1,133	1,566
		45%	23%	13%	8%	11%

14. Exchange movements

To be consistent with the basis applied for IFRS reporting, EEV basis results for the year are translated at average exchange rates. Shareholders' funds are translated at year end rates with exchange movements recognised in EEV basis shareholders' equity as follows:

	2008 £m	2007 £m
Long-term business operations:		
Asian operations	**1,170**	80
US operations	**1,264**	(53)
	2,434	27
Other operations (primarily reflecting US$ denominated holding company borrowings and hedge positions)	**(424)**	37
Total	**2,010**	64

TOTAL INSURANCE AND INVESTMENT PRODUCTS NEW BUSINESS

INSURANCE PRODUCTS AND INVESTMENT PRODUCTS

	Insurance products		Investment products		Total	
	2008	2007	**2008**	2007	**2008**	2007
	£m	£m	**£m**	£m	**£m**	£m
Asian operations	**2,673**	2,901	**46,957**	38,954	**49,630**	41,855
US operations	**6,941**	6,534	**36**	60	**6,977**	6,594
UK operations	**7,183**	6,879	**16,154**	14,745	**23,337**	21,624
Group Total	**16,797**	16,314	**63,147**	53,759	**79,944**	70,073

INSURANCE PRODUCTS - NEW BUSINESS PREMIUMS AND CONTRIBUTIONS (note (i))

	Single		Regular		Annual Premium and Contribution Equivalents (APE)		Present Value of New Business Premiums (PVNBP)	
	2008	2007	**2008**	2007	**2008**	2007	**2008**	2007
	£m	£m	**£m**	£m	**£m**	£m	**£m**	£m
Asian operations								
China (note (iv))	**63**	45	**32**	24	**38**	29	**230**	167
Hong Kong	**507**	501	**154**	117	**205**	167	**1,612**	1,196
India (Group's 26% interest)	**60**	26	**202**	177	**208**	180	**747**	728
Indonesia	**94**	118	**167**	109	**176**	121	**649**	494
Japan	**115**	122	**30**	22	**42**	34	**217**	214
Korea	**78**	179	**211**	241	**219**	259	**1,097**	1,267
Malaysia	**28**	41	**99**	78	**102**	82	**570**	472
Singapore	**341**	593	**78**	67	**112**	126	**961**	1,047
Taiwan	**153**	132	**189**	218	**204**	231	**1,037**	1,121
Other	**18**	36	**54**	55	**56**	58	**188**	200
Total Asian operations	**1,457**	1,793	**1,216**	1,108	**1,362**	1,287	**7,308**	6,906
US operations								
Fixed annuities	**1,724**	573	**-**	-	**172**	57	**1,724**	573
Fixed index annuities	**501**	446	**-**	-	**50**	45	**501**	446
Variable annuities	**3,491**	4,554	**-**	-	**349**	455	**3,491**	4,554
Life	**7**	7	**24**	19	**25**	20	**230**	158
Guaranteed Investment Contracts	**857**	408	**-**	-	**86**	41	**857**	408
GIC-Medium Term Notes	**337**	527	**-**	-	**34**	53	**337**	527
Total US operations	**6,917**	6,515	**24**	19	**716**	671	**7,140**	6,666
UK operations								
Product summary								
Internal vesting annuities	**1,600**	1,399	**-**	-	**160**	140	**1,600**	1,399
Direct and partnership annuities	**703**	842	**-**	-	**70**	84	**703**	842
Intermediated annuities	**497**	555	**-**	-	**50**	56	**497**	555
Total individual annuities	**2,800**	2,796	**-**	-	**280**	280	**2,800**	2,796
Income drawdown	**75**	34	**-**	-	**8**	3	**75**	34
Equity release	**242**	156	**-**	-	**24**	16	**242**	156
Individual pensions	**115**	38	**3**	1	**14**	5	**124**	42
Corporate pensions	**221**	283	**88**	84	**110**	112	**645**	737
Unit-linked bonds	**109**	243	**-**	-	**11**	24	**109**	243
With-profit bonds	**869**	297	**-**	-	**87**	30	**869**	297
Protection	**-**	-	**6**	5	**6**	5	**38**	26
Offshore products	**551**	434	**4**	4	**59**	47	**573**	455
PruHealth (note (v))	**-**	-	**16**	13	**16**	13	**146**	107
Total retail retirement	**4,982**	4,281	**117**	107	**615**	535	**5,621**	4,893
Corporate pensions	**227**	198	**116**	115	**139**	135	**653**	604
Other products	**132**	190	**21**	25	**34**	44	**219**	276
DWP rebates	**153**	143	**-**	-	**15**	14	**153**	143
Total mature life and pensions	**512**	531	**137**	140	**188**	193	**1,025**	1,023
Total retail	**5,494**	4,812	**254**	247	**803**	728	**6,646**	5,916
Wholesale annuities (note (iii))	**1,417**	1,799	**-**	-	**142**	180	**1,417**	1,799
Credit life	**18**	21	**-**	-	**2**	2	**18**	21
Total UK operations	**6,929**	6,632	**254**	247	**947**	910	**8,081**	7,736

Channel Summary								
Direct and partnership	**2,352**	2,385	**215**	212	**450**	451	**3,268**	3,313
Intermediated	**2,990**	2,284	**39**	35	**338**	263	**3,226**	2,460
Wholesale (note (iii))	**1,434**	1,820	**-**	-	**144**	182	**1,434**	1,820
Sub-total	**6,776**	6,489	**254**	247	**932**	896	**7,928**	7,593
DWP rebates	**153**	143	**-**	-	**15**	14	**153**	143
Total UK operations	**6,929**	6,632	**254**	247	**947**	910	**8,081**	7,736
Group Total	**15,303**	14,940	**1,494**	1,374	**3,025**	2,868	**22,529**	21,308

INVESTMENT PRODUCTS – FUNDS UNDER MANAGEMENT (note (ii))

	1 Jan 2008 £m	**Market gross inflows £m**	**Redemptions £m**	**Market and other movements £m**	**31 Dec 2008 £m**
Asian operations	17,393	46,957	(46,102)	(3,016)	15,232
US operations	55	36	(32)	(9)	50
UK operations	51,221	16,154	(12,747)	(7,631)	46,997
Group Total	68,669	63,147	(58,881)	(10,656)	62,279

Notes

(i) The tables shown above are provided as an indicative volume measure of transactions undertaken in the reporting period that have the potential to generate profits for shareholders. The amounts shown are not, and not intended to be, reflective of premium income recorded in the IFRS income statement.

Annual premium and contribution equivalents are calculated as the aggregate of regular new business amounts and one tenth of single new business amounts. PVNBPs are calculated as equalling single premiums plus the present value of expected premiums of new regular premium business, allowing for lapses and other assumptions made in determining the EEV new business contribution. New business premiums reflect those premiums attaching to covered business, including premiums for contracts classified as investment products for IFRS reporting. New business premiums for regular premium products are shown on an annualised basis. Department of Work and Pensions rebate business is classified as single recurrent business. Internal vesting business is classified as new business where the contracts include an open market option.

The format of the tables shown above is consistent with the distinction between insurance and investment products as applied for previous financial reporting periods. With the exception of some US institutional business, products categorised as "insurance" refer to those classified as contracts of long-term insurance business for regulatory reporting purposes, i.e. falling within one of the classes of insurance specified in part II of Schedule 1 to the Regulated Activities Order under FSA regulations.

The details shown above for insurance products include contributions for contracts that are classified under IFRS 4 "Insurance Contracts" as not containing significant insurance risk. These products are described as investment contracts or other financial instruments under IFRS. Contracts included in this category are primarily certain unit-linked and similar contracts written in UK insurance operations and Guaranteed Investment Contracts and similar funding agreements written in US operations.

(ii) Investment products referred to in the table for funds under management above are unit trust, mutual funds and similar types of retail asset management arrangements. These are unrelated to insurance products that are classified as "investment contracts" under IFRS 4, as described in the preceding paragraph, although similar IFRS recognition and measurement principles apply to the acquisition costs and fees attaching to this type of business.

(iii) The tables above include for 2007 the transfer of 62,000 with-profits annuity policies from Equitable Life on 31 December 2007 with assets of approximately £1.7 billion. The transfer represented an APE of £174 million.

(iv) Subsequent to 29 September 2007 following expiry of the previous management agreement CITIC–Prudential Life Insurance Company Ltd (CITIC-Prudential), the Group's life operation in China, has been accounted for as a 50 per cent joint venture. Prior to this date CITIC–Prudential was consolidated as a subsidiary undertaking. All premiums for CITIC–Prudential are shown at 50 per cent on a like for like basis, reflecting the constant economic interest before and after the management changes in line with the original agreement with CITIC.

(v) The tables above for full year 2008 and 2007 reflect the inclusion of the Group's UK health insurance joint venture operation, PruHealth.