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Introduction and Group Overview

Mike Wells

CEO, Prudential

Welcome

Good morning everybody. On behalf of my 23,400-plus colleagues. I want to welcome you here today. I was watching the cities flash up on that screen; that is most of my travel itinerary for the last 18 months, if you are wondering where that list came from. It has been a lot of fun to step into this role and I am starting my 22nd year with the Group. I thought I knew a lot about the company before I accepted it and I can tell you, after the initial phase in this role, it is amazing to see the people and the operations we have globally. And hopefully today we will get a chance to see some of those management teams up here. For those of you that are new to the Group, you will get a feel for the depth and breadth of the talent we have working on your behalf.

Agenda

We have a full day today. I will do a quick strategic overview and Nic Nicandrou, our Group Financial Director, will give you a financial overview: cash, capital and key metrics. Tony, and the team, from Asia, will walk you through some of the operational issues, the growth and successes we are having in that region. Following that, Barry and the team from the US, an update on what is a fascinating part of the world right now. Just a couple of questions last night at the pre-event on politics and regulation and things in the States, but a lot of opportunity for us there, and we have an interesting speaker for you on that. And then, John Foley and his team as well as Anne and her teams will walk you through what we are doing in the UK market to compete in what is again another structurally important and opportunistic market for us. So let’s get started.

Group - Strategic & Financial Overview

It has been an interesting year. I think that is probably the understatement of the morning. You have seen an amazing market for interest rates on the risk-free level in our key markets that drive and define capital regimes and set the pace for UK and US and other markets. Massive movements in absolute rate volatility, vol in equity; material regulatory changes from Solvency II to some of the changes we have seen in the UK and DOL in the US and questions about capital regimes in the US now.

Market context

All these things are going on with a very heavy political background. Not just the US, but Brexit, and a number of changes in Asia. All of this has been an interesting time, and I think the single take-away I would give you from my role is what you see with the Group is we are big enough to be impacted by any and all of these combined but, as you see from today’s numbers we put out, we are strong enough and resilient enough to adjust and often benefit from these changes. So there may be a sales impact, there may be a structural impact, they may change the way we do something, but we have the scale and markets to adjust to all of this in stride. We will hopefully demonstrate that to you today.

Clear strategy

We start with what is a well-discussed and well-proven strategy. I think the emerging piece of the change in this strategy for me – we have always talked to you about the structural opportunities in Asia, and I will give you a few minutes on that again this morning, but you are seeing clearly at the consumer level the structural issues and challenges highlighted by the political and regulatory issues in the US and the UK.

A by-product of DOL is highlighting the level of under-saving in this US retirement market, and increasing the demand for the kind of opportunities that we can provide for consumers. The changes in the UK in the advice model structures etc. and I do not talk to anyone in the UK that is not concerned or aware of the fact that they are responsible for funding their own retirement now. And they have very strong opinions about that and they are looking for solutions. And we have entities that can provide that.

Significant growth opportunities

That is what it feels like on the ground. The structural opportunities ahead of us, they contrast by region.

In the East, very young first time buyers of health and protection in markets that typically do not have government-provided health or government-provided retirement at a material level or a level that the consumer thinks is appropriate. And very high cash savings rates. So these are typically first-time buyers, very young; mid-20s.

Our Western markets, the pre-retiree retirees, who are trying to make their investments work at a combination of risk and reward that provides them competitive returns without more risk than they are comfortable taking. And any risk is to them material. So suddenly a VA with a withdrawal benefit they cannot outlive or a with-profit product that has outperformed the market, proper asset management from a firm like M&G or Eastspring are solutions which fit into where they are. And again, the advice models are in flux in these markets, and we are adjusting to those with size and scale capabilities.

'Best in class' franchises

To capture those, you need quality franchises. The structural demand in the market is not material if you are not a scale player to capture that. So we have that in each market. I think the Asia team would tell that one of the keys now, if the consumers are first-time buyers, is the scope and the breadth of your distribution model. So with 500,000 plus agents, 10,000 plus branch banks that we can distribute through, and we have a unique footprint in region which Tony and the team will walk you through.

In the US, the material change is around the advice component of the products. Jackson is unparalleled in its ability to train, develop and support advisers in the US. Its wholesaling capability – as it is referred to in the US – is the largest team, is the most effective team and, if you talk to advisers, one of the most trusted advisers they have in the business practice. And that again is 20 plus years of doing things to help advisers grow their business ethically and efficiently. And that is tremendous leverage when you go into regulatory changes and process changes that are going to vary firm to firm. Jackson's very well positioned to deliver at the wholesale level what it needs to as well as its product manufacturing capability.

And in the UK, it's consumer-centric. Can you demonstrate to a consumer that had they invested with you, you would have done well? Can you demonstrate value? Are you trusted brands? And both M&G and Pru UK have done that successfully.

The measure of success

I would measure this success in how we do not. So we have given you public targets. As you see from today's numbers we are on track to hit those. Asia is the only market we have given you a growth target, but it is growth of earnings. It is growth of free cash flow. This is cash, and this is capital creation. What is not up there is a market share number. What is not up there is a top-line number. The same is true for the Group. Growth is growth in value. Value measured, earnings, capital creation and cash.

Capital allocation focus

Now, do all markets need to hit at once? How do we allocate capital? Are we holding back capital for one market in Asia, one market in the US because of Hong Kong? I get those questions a lot. The answer is generally 'no'. The Asian markets, for example, have all the capital they need to grow, but that does not mean we deploy capital on things we do not think create value. So we look at the markets, we look at the distribution channel dynamics, and we look at the products that we think create the highest return for you when we deploy your capital.

Significant capital allocation optionality

How does that translate? If you look at the right side of this graph, what you see is the growth of insurance margin, the technical income if you will, the fee income, the life income. But what you are not seeing is a high concentration of spread income. If we were focused solely on top line, in multiple markets not just Asia, and that is the easiest button to push right now. And we think from a return on capital point of view, the least attractive. So, a disciplined execution on allocating capital.

Relative outperformance

So are the teams not interested in top line, are the teams not interested in market position? Of course not. This is some of the most competitive people I have ever worked with and the market positions reflect that. Asia is clearly number one. US, clearly number one. The UK, income draw down, pensions number one. Look at M&G's percentage of the institutional business. These are market-leading franchises and our market position should be a by-product of us executing well. But again, please do not read between the lines of my comments that we are not focused on winning on a sales front. But the measurement of value for this organisation is growth in recurring relationships that are profitable with consumers. Sales is a factor in that and, as you can see, a competitive one for us.

Absolute performance underlines intrinsic strengths

So how have we done in this tumultuous year? This is the half-year numbers. Last time we gave you a full report. You have seen earnings growth; free surplus generation, effectively cash growth; and Solvency II is, as we have told you before, sort of a poor fit for us. But even under its lens you can see the absolute capital generation. So, growth in capital, growth in cash, growth in earnings.

At a period in time when the industry is looking for growth, we have it. It is more opportunistic. It is not in all markets; it is not in all segments of a country; it is not in all segments of a distribution channel. But we have the scale to pick the pieces of the market we want to get these sorts of results for you.

Asia - Operational summary & Country 'Deep Dives'

Significant growth runway

Is Asia done growing? I get this a few times. Is the structural nature of our original thesis in Asia, going back, no longer true? The answer is 'no', and I would challenge it on four parts. There is a penetration opportunity: an under-penetrated market, under-served market. That is measurable. There is a health gap; that is clearly measurable. There is a population dynamic; just the youth and the growing development of their income and their capabilities. And of course, there is a wealth factor in that.

I would argue you do not need all of these to occur concurrently to have a very fast-growing business. Let me give you an example of just two.

Compounding growth

So if you take a look at the life business, look at the increase of our customer base. These are the blue and grey bars, if you will. Combine that with an increase in our case size and then look to the right of that, the increase in our absolute sales. The magnification of that; the compounding effect, if you will. Again, first product sales the majority of the time.

Can we successfully address these consumer needs and come back to them and have them buy a second product? Can we successfully address their concerns for their families and what they see as alleviating risk, so when they start buying and saving in asset-management products, they use Eastspring. I believe we can, and I believe that is our ability to execute and the quality of the products and the quality of the people who deliver it for us. And there is a compounding effect later on our book that is yet to materialise. But there is clearly a compounding effect you can measure, now, in the structural demand.

High quality resilient portfolio

What does that produce for you? First off, it has produced a resilient back book. Recurring, regular premium. Key, key dynamic to our Asian business. Growth of the in-force has been dramatic. That is your recurring cash flow. And diversification across markets. Why? Because the portfolio effect – if you think there is political, interest-rate, equity, regulatory changes – is critical to continuing to grow.

And that is growth of sales, growth of new relationships and impact in the region. And in Asia, it is critical to have scale for negotiations with counterparties. If we want to do business with a bank that is in five countries, we are there. And we arguably have one other competitor they can likely talk to that has a similar footprint that can service their consumer base that they care about.

Delivering profitable growth

So again, there are advantages to our business model in Asia that are unique. And they translate into recurring premium, growth of earnings for you from that back book, and it is our responsibility to take care of those consumers so they stay with us and come back time and time again with their needs.

Central to Group prospects

Is it measurable consistently? It is. Is it measurable towards the public targets? It is. And has it contributed to the growth of the Group disproportionately? It has. Asia is a material part of our growth. We have good growth in our other markets, but where you would see the out-weight, if you will, of Asia in our growth rates. And again, it comes from just the key structural demands we have discussed.

US - Strategic overview, Regulatory & Financial Update

Capabilities aligned to significant opportunity

So moving to the US, you have a changing political, regulatory and social dynamic in the States. Interesting times. I had a South East Asian regulator ask me last year about our two most politically volatile markets: the US and the UK. Which I thought was a fascinating question given our footprint globally. But people are very interested in what is going to happen there. DOL. How does this affect the delivery of products? And I am going to let Barry and the team get into the specifics of the US model.

But you are seeing, basically, two themes emerging in the States. The types of solutions that we bring retirees are moving from the VA asset pools to the advisory asset pools. And there is a tremendous opportunity there in scale if we can correctly execute on it.

Second, there were meetings over my 20-plus years here where we stood up and tried to name all 10,000 baby boomers retiring every day for you to try to add a face to that. We do not do that anymore. But I do think it is important to look at where we are in the baby boomer opportunity. We are at the beginning of the 20 years. So the structural demand in the US for solutions which provide an under-saved population assurance they will not run out of money are material. And there is quite a long time to run with that. So as Jackson adjusts its products and its services and its delivery to that opportunity, there is a long, long list of consumers who need what it is Jackson does well. So you have a broadening of the markets they are in and you have an under-served, very large population that has a good asset base.

Delivering cash

Capabilities will be everything. Not just existing product but technology, service, wholesaling; all those dynamics will be key. I get asked a question a lot on my travels: 'Do you have to believe Jackson did it differently compared to its peers in the US?' And the answer is, it did do it differently from peers. It is a better product for the consumer, and that is measurable, and we will show you that today. And it has been from the beginning. It was hedged from the beginning. It had no capital issues. Has it been tested? Yes. It went through a crisis. The capital models were tested and the hedges held up beautifully. And the team is in place that produced that outcome.

It is highly capital-generative. The fees on the VA product are good because the consumers are doing well. You have a back book that is profitable and relationships with clients that we are happy to have and happy to have them reinvest with us. And there is not another company in the US that was in this space that can say those things. So yes, it was a unique experience. It is still uniquely positioned. And I wouldn't underestimate the level of trust we have with advisers because of those combined effects. We have represented them well with their consumers and that gives us licence to do business with more of their clients. That is where trust comes from there: the experience.

It also produces high levels of organic capital which produces very good cash flow to the Group. Support dividend, other activities in the Group. But $3.7 billion of cash remittances from Jackson to the Group, collectively. And again, this is maintaining high levels of regulatory capital, maintaining Jackson's rating level. This is not stripping Jackson or putting it into runoff or diminishing its growth in any way.

UK - M&G & Life Overview

Pivoting to our strengths

Pivoting to the UK. Self-reliant structural changes here, as I mentioned, you feel more and more demand in the UK from consumers for a risk off trade that has higher return. And it is an almost impossible question to answer for them. The savers here, you hear the same thing in the States; you certainly here it more pronounced living here now in the UK. They cannot afford to live off the return they can get in a time deposit from the bank. So they start from that premise.

They have varying views of their risk tolerance; the advice models here are still relatively limited. A lot of the work is done themselves. They are very diligent about it. The number of sites and research and things people do is amazing when you talk to them. But what they want is smoothing long-term results, proven asset allocators, proven asset managers. So what you see in our UK franchises is very good results for the clients that have been with us for a long time; very good demand from new clients. And that can be measured in the proof unrelated products; that can be measured in the asset management products. And our concentration on getting the performance right is the quality measurement and the distribution is following that very effectively. But you are talking about one of the largest asset management models in the world. And our position in it now is a series of capital-light products, if you will, that address a lot of the consumers' concerns.

Group - Well-positioned to deliver across cycles

The Group itself I think is well-positioned across the cycles. We have talked about this before. You have very good earnings quality from source of earnings and diversified sources of earnings. You have very good diversification by business type. Strong currency mix; disproportionately US dollar-based. So the pound effect to us is diminished a bit. And then I think one of the key elements is the in-force earnings growth, the natural momentum inside the business, if you will, if we sold nothing, that sort of test. How do we look? Again, in an industry looking for growth, we have 13% growth in our in force alone. We think that is a very strong set of skills, set of capabilities going into any cycle. And it is demonstrating a resilience across the cycle.

Long-term track record

I have told you all before that this is one of my favourite slides. I think this is one of the best ways to look at a company like ours. And we could drive any one of these higher relative to the other two if we focused inappropriately on just one item. Could we grow top line faster and trade off earnings? Yes. Could you grow capital faster in exchange for growth? Absolutely. What you see though is very consistent long-term growth of operating profits, sales, and capital generation; cash. Across all these cycles, across all these political issues, across all these market volatility issues, across all these interest rate climates. This is a very unique picture. I have said before once, I think we compete with ourselves on this and it is not a low bar. But I think it is a very good accomplishment for the teams that are up here with you today.

Summary

So I will be back up later for the Q&A section. To wrap up my piece, the strategy has been appropriate, stays appropriate. The scale we have developed over the years in the businesses gives us optionality that peers do not have. The operational excellence of the firm improves monthly. You see that in my travels; we are better at everything we do. Ten years ago, five years ago, one year ago. As we grow, we improve. We are very good at institutional learning; having one business unit, sharing what somebody else is doing. And that is one of the dynamics we get with our footprint and the size of our team and how close they work together. So the resilience improves. And capability as well as client relationship growth, as well as back book growth, as well as earnings growth. And we think there is tremendous head room ahead of us in all of our key markets.

Group Financial Update

Nic Nicandrou

Chief Financial Officer, Prudential

Key Financial Drivers

Good morning everyone. In my presentation, I will recap on some of the distinctive financial features of Prudential Group and provide you with a trading and a capital update.

So I will skip through the normal cautionary statements and go through to the next slide, which summarises the key financial drivers that have underpinned the quality and resilience of our earnings, our capital and our balance sheet. On earnings, what defines our success is our ability to consistently attract profitable new business flows which match the quality of our large existing book.

For our Life operations in Asia, this is achieved by adding new regular premiums with a high health and protection content to our stock of recurring-premium business. In our other operations, our earnings prospects are determined by our ability to gather, retain and grow fee-paying assets. Now, while the impact of new business in any year is incremental, it is the compounding effect that promotes the Group's resilience and predictable delivery.

Each new business vintage is highly profitable, driven by our disciplined approach to capital allocation and by our relentless focus on achieving strong returns and fast payback. The capital velocity that is created by this approach means that the Group is highly cash-generative on all bases, including Solvency II, where the Group surplus rose to 11.5 billion at 31st October, equivalent to a ratio of 189%.

We combine our focus on capital generation with a conservative stance to balance sheet risk. Since the 2008 financial crisis, we have consistently prioritised credit quality over yield. In the current uncertain environment, we regard it as good business practice to hold appropriately strong solvency buffers in each business and a healthy level of cash at the Group.

Taken together, these distinctive financial attributes are a key source of strength and resilience for Prudential and provide us the flexibility to adapt to all parts of the cycle without compromising delivery.

Life Operations

I will now turn to how we have driven the business forward this year, starting with our Life operations. Prudential's overall new business production remains strong in the first nine months of 2016, at a time when most companies in the industry are finding growth elusive. On a constant exchange rate basis, new business profit was 9% higher, at £1,970 million, delivered against a backdrop of lower rates, ongoing uncertainty surrounding the DOL ruling and our deliberate actions in certain markets to preserve value.

Asia

Asia continues to power forward, growing new business profit by 23%, reflecting high sales and improved business mix. The 21% decline in Jackson's NBP is driven by lower variable annuity new premiums. In the UK, we have maintained our post-pension-reform sales momentum to deliver a 41% increase in retail NBP.

Product and pricing actions taken across all three regions have more than offset the adverse effect of lower rates. Currency tailwinds have added a further ten points to the reported growth rate, which was 19% on a sterling basis. The positive progress on this important value measure demonstrates once again the strength and resilience of Prudential's new business franchise.

In Asia, the structural drivers of life insurance demand remain intact. Our scale and geographic reach have enabled us to flex our business in response to local country conditions while maintaining strong overall momentum at a regional level. As I have already mentioned, in the first nine months of the year, PCA delivered a 23% increase in NBP, ahead of the 16% rise in sales. Many of the key country trends observed at the half-year stage persisted in the third quarter, including the strong sales performance in Hong Kong and the relatively subdued production in Indonesia.

The regional performance continues to be supported by a robust level of new regular premium sales, up 18% in the period, contributing 94% of total APE. Agency sales were up 21%, driven by improved productivity. The 27% increase in health and protection NBP underscores the quality of new business written this year and underpins the earnings momentum in the region.

US

In the US, the annuity market continues to be disrupted by the uncertainty surrounding the DOL ruling. In line with observed market trends, Jackson's variable annuity sales in the first nine months of the year were 28% lower.

As we have said before, Jackson's earnings are primarily driven by fees that we levy on separate account assets. These assets stood at $145.6 billion at 30th September, 8% higher than the start-of-year position.

The increase reflected $4.6 billion of net inflows, equivalent to an annualised growth rate of 5% on opening assets and $6.8 billion from the positive effects of market appreciation. The fact that the business flows remain positive, despite the reduction in sales, reaffirms our view that DOL is a sales not an earnings event.

UK

In the UK, as our Life business pivots towards retail, savings and investments, our success in this market will be increasingly driven by our ability to gather, retain and grow customer assets. We start from a position of strength in that we run the largest active, with-profits fund in the country and we are already the market leader in bonds.

Post-pension reform, we revamped our draw-down and personal pension products and broadened our proposition to include ISAs, all offering a popular PruFund investment option.

Our strategy is already bearing fruit, with new and recurring premiums from our refreshed retail offering rising strongly this year to 6.7 billion, you can see that in the red bar, as we look to reverse the negative flow trend from the legacy business.

The earnings signature of with-profits products is more gradual, which means that the successful extension of PruFund will take time to earn through. However, this does not detract from the fact that we are building another important store of future value in a highly efficient way.

While new annuity business is no longer an area of focus, the sizeable and well-seasoned in-force annuity book will remain an important and dependable source of core profits for a number of years to come.

Asset Management

In asset management, we have seen some more encouraging net flow trends in the third quarter. At M&G, net outflows slowed to £1.1 billion for the retail business, a much-reduced level when compared to the previous five quarters, in part reflecting improvements in investment performance. External funds under management benefited from the positive effects of market appreciation, closing 8% above the start-of-year levels. At £136.2 billion, they are now only 2% below the high-water mark of 30th March 2015, albeit the proportion of fund from the higher-margin retail business is ten points lower, at 45%.

Eastspring delivered 0.6 billion of third-party net inflows in the last quarter, to move into a positive flow position for the year. Overall funds under management are 29% higher than the start-of-year position, benefiting from the reliable internal Life business flows and positive market movements. Like M&G, Eastspring is also seeing a small drift away from higher-fee business.

Group Capital Position

Turning to capital, the Group Solvency II surplus stood at 11.5 billion at the end of October, equivalent to a ratio of 189%, some 14 points above the 30th June position. The movement in our surplus over this four-month period is analysed on the right. Operating capital generation was 0.9 billion, which brings the ten-month total to £2.1 billion, £1.7 billion of which represents underlying business performance and £0.4 billion reflects the benefit of management actions. Positive market effects and currency movements added a combined £1.3 billion of capital in the period.

I said at the half year that in taking actions to reduce the sensitivity to downside market risks, we retained the upside potential. The effect of the 20 basis points rise in UK and US long-term swap rates between June and October has therefore come through the results, accounting for almost all of the £0.7 billion market effect and contributing around five points of solvency.

With UK and US swap rates rising by another 15 and 30 basis points respectively, following the US election, the overall Group ratio today is higher.

I can confirm that at the end of October, the Solvency II position of PAC, our main UK life entity was at the upper end of the 130–150% target range. Jackson's RBC is also robust over the 400% level.

This updates confirms both the capital-generative nature of our operations, which, at an underlying level, add around 20 points of solvency each year and the robust overall surplus position, which continues to provide ample headroom to absorb any downward moves from here.

Life free capital generation prospects improve with new business

I would now like to delve a little further into our ability to generate capital operationally by looking at the capital velocity of our new business franchise. The chart on the left shows the amount of capital we have invested each year in writing new business, while the one the right depicts the undiscounted capital that we expect to generate from each vintage over the next 30 years.

As you can see, we continue to direct our new business investment in a disciplined manner, targeting high-return opportunities. The £745 million invested in 2015 is expected to return eight times the initial investment over the next 30 years, with Asia contributing the lion's share. The fact that the 2015 cohort is expect to generate more capital per pound invested than the 2011 cohort, which was written when interest rates were higher also speaks to our ability to sustain returns as the cycle changes.

In all cases, expected capital emergence is front-ended, with over 50% generated in the first ten years. Payback of the initial investment is in fact achieved in just over two years. The capital velocity created by successive additions of these highly-profitable new business vintages is what underpins the Group's growth and cash objective.

Growing life in-force underpins Group cash generation prospects

As you can see on this next slide, the contribution from the five most recent new business cohorts, written between 2011 and 2015, shown in blue, has doubled the capital that we expect to generate over the next ten years from the pre-existing base. The people on the ground, who delivered this powerful dynamic, remain in place.

Now, the expected releases from life operations are not our only source of capital generation, this slide captures all of the Group's sources and uses of capital over the last four calendar years. Working across the page and starting on the left, the set of bars in the box represent the capital that we expected to generate each year, from both the 2010 life in-force book in red and from each new business vintage written since that date in blue.

Some £9 billion was generated in aggregate from this source, representing the largest component of the stack bar shown in the middle. Over this four-year period, positive experience in our life book added £1.9 billion and our combined asset management operations contributed a further £1.9 billion of capital. Some £2.6 billion was deployed to finance new business, with a further £1.2 billion covering the adverse market impacts.

A net total of £9 billion was therefore generated from all our operations during these four years, £5.6 billion of which was remitted to Group, with a balance retained locally. This 5.6 billion of cash remitted by BUs covered central costs and funded £3.3 billion of external dividends, around two-times the aggregate payouts to shareholders in the previous four-year period.

What this analysis highlights is that our cash generation is predominantly driven by the expected releases from our large Life in-force book, which is our most reliable and predictable source of capital. It also illustrates how our capital velocity has produced meaningful step-ups in both remittances to Group and dividends to shareholders.

Capital Dynamics and Dividend Philosophy are Unchanged

The capital dynamics that I have summarised in the previous four slides remain intact. We continue to focus on growing the underlying free surplus generation of each business and we retain our disciplined approach to capital investment and risk management. All four businesses are able to self-finance their organic growth needs and hold appropriate capital buffers locally to enable them to invest in new opportunities and cover unplanned events, such as the effect of markets, or a market stress, or new regulatory capital shocks.

Remittances from business operations are informed by this assessment and by the Group's requirement to service these providers of capital and maintain a healthy level of central cash to finance in-strategy opportunities and provide flexibility in times of stress.

Our approach to setting the external dividend is also unchanged. We set the annual dividend at a level which is affordable and can be increased safely, even under stress. We believe that this philosophy has served the Group well. Our current payout level is strongly covered by all the measures that we use to assess it.

Now, when you combine this with the strong capital dynamics of our business model, we have a high degree of confidence in our ability to grow the dividend by 5% per annum. In line with the approach that we adopted in recent years, we will continue to assess the potential for addition distributions, such as dividend step-ups, but we will only make these if we are convinced that in doing so we will not jeopardise the 5% growth rate, going forward.

We will assess the affordability of such additional distributions by reference to a variety of financial indicators, as shown on the slide, alongside evaluating the opportunities available to accelerate our growth. In updating our dividend policy, all we have sought to do is to align the wording to what we actually do in practice. So there is no new news here. You should not, therefore read this as signalling a change in either the prospects or the earnings outlook for the Group. In my view, it signals confidence, balancing certainty for investors with sensible flexibility.

Balance Sheet Remains Defensively Positioned

Before I close, I would like to briefly touch on balance sheet quality. Overall, there is little new to report here. Our portfolios have remained defensively positioned, well diversified and are subject to strict concentration limits.

In the UK, we have maintained our high-credit-quality bias while in Asia we continue to invest predominantly in sovereign and investment-grade securities. In the US, the portfolio has been significantly derisked since 2009. The middle box shows that today Jackson has a much-increased allocation to cash and treasuries, a high proportion of investment-grade assets and, importantly, a substantially reduced exposure to RMBS and high-yield securities. Overall, our credit portfolios have performed well in the third quarter, with Jackson reporting only $2 million of impairments.

Summary

I will conclude my presentation by reiterating two points. The first is that the Group has maintained its forward momentum this year, in the face of some meaningful regulatory, economic and market headwinds. Asia's structural opportunities continue to underpin our momentum, enabling PCA to grow new business profit by 23%, year to date. Our disciplined approach here and elsewhere, coupled with our ability to flex in response to local conditions is producing another highly valuable new business vintage in 2016. In our fee-based businesses, the more subdued flows this year are not hindering our ability to grow assets managed.

The second point is the consistency with which our business generates capital operationally, not only on a Solvency II basis, where £2.1 billion was delivered by end October, but also on other established bases. Our broad geographic, currency and product reach is an important source of strength which, combined with our prudent approach to risk management, creates a highly resilient Group and one which is able to trade profitably at all points in the cycle.

With this, I will now hand you over to Tony.

Asia Overview

Tony Wilkey

CEO, Prudential Corporation Asia

Introductory Remarks

Good morning. Good morning, I am here today with the team from PCA to give you an update on our businesses in Asia, a series of businesses which we are all incredibly proud of. Joining me are Adrian O'Connor, Chief Financial Officer, Ms Lilian Ng, Chief Executive - Insurance, Guy Strapp, Chief Executive of Eastspring.

In the audience, we also have Steve Bickell, Chief Risk Officer, who goes everywhere with us, and Michele Bang Deputy Chief Executive of Eastspring.

This is an incredibly talented team with over 100 years of experience. I think Steve might actually have that much experience himself. This is the team that has been in place for at least the last 10 years and has delivered a quite exceptional set of results across the region.

Diversified Market Participation Advantage

No one else can paint this picture on this scale. We started our Life Insurance business in India, in 1923 followed by Malaysia in 1924. Almost close to 100 years of experience in the region, and today we have 13 insurance companies in 12 countries, and we are quite proud of the fact that we hold top three positions in nine out of the 12 markets. For asset management, from humble beginnings in Singapore, in 1994, Eastspring today is the number one Asian asset manager by FUM, excluding Japan.

Leveraging the growth of the life business, growing retail and institutional, Eastspring now has 12 asset management businesses in 10 Asian countries. Developing experience over time is critically important, especially as we grow and expand. One great example of this is Laos, where we entered earlier this year. We were able to ramp up quickly in this new market, by leveraging sales practices and techniques from Thailand, underwriting and claims expertise from Cambodia, IT support and expertise from Singapore. This enabled us to move very quickly and scale up, something that will be very important when hopefully next year Myanmar opens up. Speaking of scale, and you know we like to substantiate any statements that we make with facts, we have become quite a sizable business.

Today, we have y 60,000 customer interactions every day. New customers are on-boarded at the rate of 5,000 per day. New policies are issued at the rate of 260,000 per month. Every month we recruit 17,000 agents and process 120,000 claims. PCA has indeed become quite a large, yet fast moving business.

Our Geographical Coverage Advantage

I think we have been leading the conversation for many years about the investment case for the emerging middle class in Asia. The total population in PCA's footprint estimated by IMF, by 2020, will be 3.7 billion people. That is five times the population of the G7. Further, based on estimates, there will be an addition of 178 million working age people over the next 15 years in our footprint.

This means our core segment of emerging middle class will continue to grow. It is estimated by 2017, that is next year, there will be over 450 million households with disposable incomes of $10,000 or more. That is our target market. In addition to this, the protection gap has continued to widen as people earn higher incomes and raise their living standards. This translates into, on average, a protection gap of about $100,000 per person or per family. Clearly, the level of protection sold in the region to date has been inadequate. All these fundamentals have and still today create incredibly strong demand for the products and services offered by our insurance business, and by Eastspring investments.

Unique Two-pronged Business Model Advantage

Our markets can broadly be divided into different segments, dependent upon their respective stages of development. You can see GDP per capita scale on the right. This is populations or countries where GDP per capita is lower than $1,000. These people typically seek out relatively simple savings and protection products, mass market, mass affluent, 5,000 to 40,000 per capita, looking for slightly more advance products, and then the high net worth segment 40,000 or above, looking for more personalised, quite sophisticated investment products.

Scale and Leadership

Protection needs tend to be more pronounced in the mass affluent and mass market segments. There are opportunities for life protection in the high net worth space, but for us, this will mean larger ticket life, critical illness type products. Most of the insurance products sold in that space in Asia today tend to be in the form of universal life, which is something we do not particularly have a strong appetite for.

Further, typically, when GDP per capital crosses $10,000, the mutual fund market emerges, and that is where basically where North Asia is and where we have been able to grow significantly. You can see the split between ASEAN emerging market economies broadly where life is and has prospered very well, and North Asia, complementary, where we have grown a mutual fund business very well through Eastspring.

As you noted from our recent exit, we excited Japan for life insurance a few years ago, and then recently announced that we are exiting Korea.

A Growth Franchise

Okay, I think our performance on life and asset management is quite exceptional, and it is really based on continuous focus on executional excellence. Life businesses have grown materially over the last few years, particularly in ASEAN, and, as I mentioned earlier, Eastspring has become the largest Asia (ex Japan) retail onshore asset manager.

This is a real powerhouse in the making, Guy is going to go into a little bit more detail in a minute. Spotting the opportunity in Asia was not difficult, everybody could see it, but actually capitalising and taking advantage of the opportunity through crisp execution, the right business model, the right products, the right distribution channels, the right team and significant instincts and expertise in the region is what made us quite successful.

Agency is our core channel, Mike mentioned earlier, over 500,000 agents, but it is not about the size of the agency force, it is about the quality of the agency force. We talk in terms of productivity.

One metric we are quite proud of is year-to-date NBP per agent is up 37%. It is not APE per agent, it is what they actually sell. As you know, they sell a lot of health and protection which tends to drive pretty robust NBP. It is about maximising the value of the franchise we built, not just driving volume.

Mike also mentioned about out bancassurance platform. We have access to over 10,000 active branches. This is more than two times the size of our next nearest competitor in the bancassurance space. We have been working hard to extract more value with our bancassurance partners by focusing our bank sales on higher value regular premium products. Nine months, year to date, regular premium through bancassurance accounted for 92%, up from 85% prior year, so moving away from single premium products with the banks and growing more regular premium.

Eastspring on the distribution front have over 350 distributors, that is excluding India, institutional clients have over 150, and hundreds of direct sales folks across 10 markets in Asia.

I think pulling all these together, and again, to reemphasise the key to success here has really been in the management team. Not only the folks who are with us today in the room but also the thousands that work and toil on a daily basis in the Asian markets.

Turning over to Adrian now.

Asia Financial Update

Adrian O'Connor

Chief Financial Officer, Prudential Corporation Asia

Growing Base Driving Future Earnings

Thanks, Tony. I am going to talk about, over the next two slides, about earnings potential and earnings resilience. Two key metrics have grown dramatically over the last 10 years. We picked 10 years on this slide for the reason that actually Tony says, this team has been together for 10 years. Actually, Tony has been here for 10 years. I was a year later. We picked it for that reason. Those two key metrics, value, on the life insurance side, and funds under management, on the asset management side, they are the key drivers of future earnings, of future earnings.

I was very, very surprise to see on the embedded value. You can see end of 2005, embedded value was 2 billion, at the end of the half year 2016 it is over eight times that amount, equivalent to about 23% CAGR over that period. What does that actually mean?

Well, IFRS equity at the end of the half year was £6 billion, so we got £10 billion in the in-force as Nic related to, earlier on. £10 billion in the in-force, of future profits. That compares with annual profits after tax of just less than £1 billion. In the in-force, we have 10 years of profits there.

On the Eastspring side, funds under management drive revenue, drive profits. Again, we see the dramatic increase over the period from the end of 2005. From £26 billion, it quadrupled to £115 billion. There is potential in the in-force, both on the insurance side and on the asset management side critically.

Multiple Earnings Levers

Resilience

Now turning to resilience. Resilience is driven by a number of what we call an earnings levers on a number of dimensions, and we got three dimensions here to talk about. The first one, the most critical one is the one on the left, and it is about geographical diversification. As you know, and as we have repeated, over the last 10 years, we have delivered year in, year out, and the volatility and growth has been reduced because of that diversification, because we have been able to flex in countries and increase production where others are falling off.

The really interesting thing is, in 2005, the two biggest producers were India and Taiwan; 2010, it was Indonesia. Today, it is Hong Kong.

Switching now to sources of earnings, which we pride ourselves upon. The core is 60% coming from insurance, the difference between what we receive in charges and what we pay out on health insurance, on critical illness and on pure life insurance.

That is underpinned by at least 25% of our APE over the last 10 years coming from insurance products, H&P as we call it. It is still not stable. It dropped off a little bit in the last couple of years because Indonesia has come off, but it still is driving those numbers.

Then the other two sources, main sources of income that we like, are charges on our ILP and profits from Eastspring. Very robust, and as you can see, between 2010, the inner doughnut, the outer doughnut, the mix has not changed that much.

Eastspring

Finally, turning to Eastspring. Eastspring funds under management are under pinned by the assets from the life insurance business. As you know, it is regular premiums, so with a constant flow coming in. The 70% of the funds under management is the life insurance business.

In addition to that on the retail side, where it is more profitable, there are basically two powerful engines at the moment. One is what we call North Asia – Japan, Korea, Taiwan, very different to the insurance business – and the other is our joint ventures in both India and China.

Both Nic and Mike referred to it that we have confidence in delivering our targets in 2017. We are confident because of the performance in IFRS and FSG to half year 2016 because of the potential shown and also because the resilience of those earnings.

With that, I am now going to turn back to Tony who will go to the – start talking about the countries and businesses.

Rise of China

Tony Wilkey

CEO, Prudential Corporation Asia

Our Geographic Expansion

China, several of you have asked for a little bit more colour on our business and opportunity in China, so we are going to give you a little bit of flavour. We have said this many times in the past: over the long term, to really be truly successful in Asia, you have to be successful in China, I mean it speaks for itself. China is not a country, it is a continent; it is a continental-sized opportunity, 31 provinces, eight of which have populations over 65 million.

Five provinces have GDP over 1 trillion. Life penetration, less than 2% and a large mortality gap of $30 trillion.

Three-quarters of the population could be defined as middle income by 2030, again, our target market. Our life JV in China was established in the year 2000 with Citic Group. As we have said in the past, we enjoy an exceptional as in good relationship with Citic Group. We were the first UK insurer awarded a licence in China.

Today, we have expanded our footprint from six provinces 10 years ago to 15 provinces and 65 cities. That is an average expansion of five cities per year, tier one and tier two cities. We are not done. We are continuing to expand our footprint. In fact, just last month, we opened a new province, Anhui, right next to Shanghai which is being dubbed the Silicon Valley of China. Interestingly, when you look at it from the air, the centre of town resembles the Union Jack. We should do quite well there.

Our current coverage, where we are across China, gives us access to about 70% of the GDP of the country, and 60% of the population. We are in nine of the 10 top provinces as ranked by gross premiums.

Closer Look at Guangdong

Drilling down a little bit further, Guangdong province, what used to be Canton many years ago. This is the largest gross premium contributor in the China market and a proxy for the wealthy eastern seaboard. It is also the birth place of Citic Pru, although we subsequently moved our headquarters to Beijing to be closer to the regulator; a good relationship with the regulator is very important in doing business in China, and I think we have worked hard to build those relationships.

Based on IMF estimates, the GDP of Guangdong province in 15 years will likely overtake that of the UK. Today's population of Guangdong is in excess of 120 million people. Life insurance penetration in Guangdong, 1.9%, still very low, and the State Council, as many of you may know, has come out with a proclamation, which is to grow insurance penetration by 2020 to 5%. When the State Council gets behind driving policy in China, things really start to happen. We are very well positioned to capitalise on this opportunity supported by government initiatives.

It is a big business today. If you look at new business sales, APE for China on a year-to-date basis, we count them at 50%, which is our shareholding level, but if you look at them on 100% basis, today, this is our second largest business. It is actually starting to become quite material within PCA. It is still woefully under where it needs to be, to capitalise on the opportunity that resides there. I am going to ask Lilian to talk in a little bit more detail about what we are doing in China and in the other markets.

PRU Asia

Lilian Ng

CEO, Insurance Prudential Corporation Asia

CITIC-PRU China

Accelerating value contribution

Thank you, Tony. I think everyone appreciates the scale of the opportunity presented in China's insurance sector. The key to capture that opportunity is to expand distribution reach for value creation.

For agency in Citic Pru, we measure growth in terms of active agents rather than just body count. This all starts with recruitment. We have selected 16 cities out of the 65, to lead this recruitment drive where we have provided specific resources, guidance and training to reach their goals.

Now in order to increase the chance of success, each city, actually utilise analytic to identify the optimum profile of the recruit in their own specific profits. At the same time, we continue to reform the agency operating model, we have general agency management for cost effective expansion.

We now have 30,000 agents and the active agents actually grew by 73% over the year. For bancassurance, we have moved from a product driven strategy to a customer oriented strategy. Now our insurance specialists in the banks were up skilled to deliver solutions to fit customers. We have also chosen to limit the volume of deposit replacement products and focus on regular premiums.

Actually, we started this shift in quarter four of 2015, and that is well in advance of CIRC circular to limit the sales of short term products in March this year. With that, 85% of our bancassurance sales are now regular premiums compared to 53% from our peer group.

Now for value creation, we have a risk management framework that help guide the distribution strategy that I have just outlined. Now our risk management capabilities are very well recognised. We are the only foreign insurance company invited by CIRC to participate in the China-US Solvency workshop that was held in August this year.

I think the recent Singles' Day online shopping spree, which I am sure you have all heard about, showcased China as having the world's most digitally savvy consumers. There are now over 700 million Chinese online. Now to cater for the demand of these consumer group, Citic Prudential is making it easy for consumers to have an interactive digital journey across the value chain. We partnered with a mobile insurance service platform to provide training, sales support and customisation of products. And then the distributor can step through with our customer from application to underwriting and rounding off with the issue of policy, all electronically. This takes around 30 minutes to complete. When it comes to the moment of truth, customer can elect to submit and settle claims through a WeChat-based application.

Now as customers demand efficient engagement, they are also looking beyond just the product, they are looking for holistic solutions. Recently, Citic Pru launched a health and insurance management campaign, covering health screening, online medical consultation, expanded coverages and access to top medical institutions. Now all of these customer-led activities have actually resulted in 71% growth in our health and protection sales for the year.

We are the only foreign insurer awarded an A rating in the annual service assessment reviewed by CIRC.

PRU Hong Kong

Advantaged platform for delivery

Now across the border to Hong Kong, there have been a lot of attention to the Hong Kong insurance market of late. Actually, the life insurance market in Hong Kong has experienced double digit growth over the past decade.

Now this consistent growth is a reflection of the strong demand for insurance. Purchase preferences are driven from a wealthier ageing population that is more health conscious. Insurance solutions help diversify risk, protect families and wealth. These attributes also appeal to mainland Chinese visitors going to Hong Kong.

Now with the growth in the industry, the regulator has been active in introducing guidelines with emphasis towards market conduct and consumer protection. Now this is demonstrated with the implementation of guidance note 16, focusing on treating customer fairly and, the important factor for mainland policy holders, to ensure mainland Chinese customers acknowledge the risk of buying insurance in Hong Kong.

Now Prudential Hong Kong has the right platform to tap into the continued demand. We have a market leading multi-distribution that is the envy or the industry. We offer comprehensive and innovative range of solutions. Wrapped around this, we have a comprehensive and robust infrastructure for execution. Prudential Hong Kong has built a balanced portfolio that has been actively managed. This portfolio has delivered consistently across multi-dimensional metrics.

Customer experience

Now to keep up with the pace of delivery, the business needs to evolve to maintain growth quality. To stretch a high performing agency further, we have refreshed the approach to recruitment. Starting from profiling, to get to the right agent, depending on the attributes of the recruit, we put them through differentiated onboarding in order to strengthen areas requiring improvement. This is made possible because we have an award-winning training platform and team. The impact, we do not only have the largest agency force, our productivity is 60% higher than the market average.

Moving to bancassurance. In line with Standard Chartered Bank's strategic direction, the partnership has been investing in digit technology to increase customer touch points and enhance customer experience. Riding on this, and recognising the customer preferences, our insurance specialist team is reconfigured to promote protection. Now this has resulted in our health and protection sales growth of 35% over the year.

For our distributors, we have deployed a suitability framework to align with customer expectation. We see the adoption of best practices as a competitive advantage while staying head of regulatory requirements.

Now Prudential Hong Kong customer engagement strategy is based on the motto of digital first. Now having a mobile sales platform and a 24/7 online servicing platform is now the new norm. This is the expectation from our customers. Our digital first playbook goes beyond that with innovative enhancement.

As part of our protection drive, we launched MyDNA. This is the first commercial deployment of a genomic technology in Hong Kong. It uses the customer DNA to identify pre-dispositional facts relating to his or her health and wellbeing, delivered on a mobile platform.

Now when we do all this, we are not there just to create noise. We track, we monitor impact, and ensure the conversion to financial results. The waiting number of protection policies doing the promotion increased from 31% for the year compared to 20% in the previous year.

PRU Indonesia

Building on success

Moving to another of our mature market, Indonesia. I think the Indonesian markets are often being referred to as one of the most attractive within ASEAN. There has been success in growing the insurance industry, but penetration, I think as we have heard, remains low.

50% of the population is below age 30, and the size of the consuming class is tripling in the next 15 years, to 135 million. Outlook for long-term growth is very positive. This is reinforced by the financial services sector master plan OJK with the ambition of financial inclusion and strengthening of the Sharia financial service sector.

Prudential Indonesia is the leading insurer. We have the widest footprint for customer reach, covered by 400 sales offices in 160 cities. Early mover advantage in establishing presence and brand recognition in the second tier cities enable us to leverage for future growth. Our agency market share is nearly three times that of the number two.

Now, being the only insurer with above 90% brand awareness reflected our brand dominance. Our platform is actually well-positioned to capture future growth. However, this will not be sufficient for us to win in the future. As the market and consumers' behaviour change, the business needs to evolve. To build on our success, we are investing now for the future. I think you have heard a lot about our mass agency recruitment model. This will continue to serve us well to build scale in the second tier city.

At the same time, we are formulating proposition to attract the young ones, the Millennials as we call them, to build the business as long-term career with Prudential. 53% of our agent and 32% of leaders are younger than 35. Now, with the support of PRUforce, we are now recruiting around 7,000 agents a month. PRUforce is mobile agency portal for onboarding, client management, performance monitoring and integrated learning.

To pave way for future growth, we are strengthening the infrastructure to nurture our core agents and leader with tailored compensation, training, campaign and recognition. Results so far are in the right direction. 78% of our agents are what we call core producers, compared to only 59% a year ago. The overall agency productivity improved by 5%.

We are transforming processes to increase capacity and efficiency, again, with electronic point of sales and online servicing. Our electronic point of sale, PRUsmart, has actually reduced the time from receipt to issuance by 50%.

To echo OJK ambitions, we have identified Sharia as a material growth engine. Currently, Sharia is a product line and we are the market leader in this space with 38% market share. However, Sharia contribution is less than 8% of the total issuance premium in the market. We are building Sharia as a business.

First step is to reinforce our sales force. We actually have 97,000 Sharia licensed agent, the largest in the country. We are conducting Sharia-specific recruitment seminars, supported by training with motivational speakers specialised that field. Now, our continued investment to evolve the business is important so that we have the right capabilities, resources, knowhow to execute and to deliver sustainable profit.

PRU Singapore

Now, similar to Sharia Indonesia, Tony earlier mentioned about the protection gap. The protection gap in Asia actually poses opportunity for us as an insurer. The issue of protection gap has been recognised for years in Singapore. There is some progress but slow. The average coverage is less than SGD150,000 compared to the required coverage of SGD350,000. The obstacle is actually cultural with most believing that they could insure themselves through savings rather than transferring the risk.

Prudential Singapore recently conducted a survey. The survey said that 9 out of 10 did not have life insurance coverage being recommended at the time of purchase. 73% of those not fully covered are underprotected because of budget constraints. Now, this result and the sentiment highlighted a need to educate consumers on having adequate protection for themselves and their families. We have an all-embracing platform to drive awareness that lead to appropriate solution and digitally enabled.

To raise awareness, we have launched a PRU relationship index to highlight the need to protect oneself and their families. We have seen an increase in protection sums insured by 41% in the first half of the year, so we are moving towards narrowing the gap.

PRU Malaysia

In Malaysia, Prudential is the pioneer in selling protection link. Riding on the success of Singapore, we will be expanding the launch of the relationship index in Malaysia to reinforce protection. This is in line with Bank Negara's goal of increasing penetration of life insurance to 75%.

Now, with all the activities to drive protection, the impact is our health and protection sales is growing faster than overall sales by 25%. While the sum assured per ringgit of APE sale increased by 11%, so another path to closing the gap.

PRU Vietnam and Philippines

We are scaling up the high performance businesses as future growth engines. Vietnam and Philippines are the high growth markets with favourable outlook. Prudential is the leader in both markets and it is important that we invest to increase operation capacity and deliver service excellence.

In Vietnam, with all the activities on transformation, we have seen the improvement across a variety of metrics including 60% of policy now underwritten automatically. In Philippines, with the automation and realignment of processes, we are seeing significant improvement in turnaround time and the issuance rates have improved by more than 90%.

Now, other than the areas I covered, one other aspect for PCA insurance to win is to optimise our investment outcome. This is a good time for me to pass to Guy, my fund manager, to speak on the exciting happenings in Eastspring.

Eastspring Investment

Guy Strapp

Chief Executive Officer, Eastspring Investments

Eastspring Investments

Okay, some snapshots on Eastspring. It is a wonderful franchise, a business I am incredibly proud to be a part of. Here, we show some FUM with a record level as of the end of Q3 at a £115 billion. We are not going to take all the credit for that because clearly some of that is pound weakness, but the theme that has driven the numbers that have already been shown in terms of underpinning Eastspring's growth relate to constant strong inflow both from third party and from our life client. This is planned, not accidental growth. As I will talk about in a moment, it is something that we are focussing on in terms of sustainability of our growth, going forward.

You will see on the right-hand side that we had a slower start to this year in terms of quarterly flow. Really came about from the middle of last year when we saw some China market interference both in terms of currency and stock market. It destabilised investors, sentiment deteriorated in Asia and we saw our outflow in the first two quarters of this year, a rebound in Q3 and I get the sense that sentiment is starting to turn, albeit fairly slowly. It is a low interest rate environment; it is difficult to find investment opportunities. Asian investors have not had the best of time investing in the Asian equity market, so if you look at the MSCI Asia (ex Japan) index over the last say five years, it has significantly underperformed other markets in the world. It will take time for third party confidence to resume in the market. However, as I said, we are enjoying wonderful flow from our life colleagues. We had record flow in 2014, we followed that up in third party space with record flow in 2015. 2016 is a bit softer and I think that is explainable.

Importantly, though, in those numbers and Tony mentioned we are in ten markets. Eight of those ten markets year to date have experienced positive flow, so there is underlying reasonable strength across the franchise. One of the real takeaways in our look over the last 12 years is that in every year Eastspring has experienced positive net flow aggregating up both life and third party.

Investment Performance

Just turning to investment performance, we live and die by the numbers. You can see here that this is the rolling three-year returns taking a fairly lumpy measure of the total picture of the performance of all portfolios. So if we are performing above benchmark, the index, we get a tick. If we are below benchmark, we get a cross.

We aimed to have about two-thirds or slightly more of our funds on sale, if you like, so outperforming the competition or outperforming the benchmark. You can see deterioration here over the last four or five years. We are a value manager. Value in Asia has been particularly hard hit. As I mentioned, investor sentiment has not been strong. Where it has been strong is investors have chased high-yield defensive stocks. That has been very much the theme really for the last four to five years.

Interestingly, there has been a little bit of a reversal. It will take time to come through the numbers. This is more uptick, but I would not read too much into that; these are rolling three-year numbers. There has been something of a reversal in confidence and investors reassessing their appetite for securities, so buying into cyclical and value stocks at the cost of exiting what are very expensive multiples on some of the high-yielding securities.

For us, this is not a massive reversal yet. It is a pointer in the right direction. It has been backed up since the US presidential election, so we have seen a further evidence of a rotation towards cyclical, towards value stocks at the expense of expensive defensives.

Good signs, but we are not going to claim any victory until we are back at least two-thirds of our funds outperforming. We have retained, importantly, our number one position. We have been for four years in the retail market. Importantly, over the same time period or over that last four years, we have improved our institutional ranking from about number 12, currently to number 3. We have made inroads there.

In many respects, Eastspring does not chase aggressively institutional opportunities. I have the biggest institutional client sitting next to me. We are sensible about how we utilise our capacity, our scarce capacity and asset classes, by not necessarily chasing institutional business which, as you all know, can be at significantly lower margins.

We have a sensible approach to our institutional opportunities. However, we are there available. We certainly seize those chances.

Progressing Strategic Growth Initiatives

I have quickly talked about growth. I think my mandate is to ensure the sustainability of growth and there are several initiatives that we are embarking on to ensure that for the next five and the next 10 years, firstly around talent.

Attracting investment talent

On Monday, we announced the appointment of Virginie Maisonneuve as Chief Investment Officer for Eastspring. It is a position that I have been doing, but more and more part-time. It was a role I originally took ten years ago when I joined the business.

However, having been chief exec over the last three or four years, I found that other things are occupying my time, not the least of which is to grow the franchise. Virginie is a world class hire. It is an important one for us, not only to secure what we have in terms of business as usual and the $140 billion of assets that we run, both in Singapore and around the region. She has a full remit, but it is also critical that we have somebody who can think about the broadening and deepening of our investment capabilities.

One thing I am passionate about is Eastspring not becoming a niche Asian play. It is great to be an Asian specialist, but I want us to be relevant to our constituent clients over the next ten years and beyond. To do that, we need to do more than what we currently do in terms of our manufacturing. A key hire, investment in talent. There have been other investments in talent and we will continue to do that.

Expanding investment capabilities

We are also expanding investment capabilities. We have been doing that mostly organically. In talking with Tony and Mike, there is a bit more of a willingness to consider that inorganic opportunities. Virginie is part of that. We have already discussed ideas around team lift outs and the like to complement what we already do and expand on that, but some organic initiatives that we have undertaken. We have built a quant team. We are running low vol strategies. We built a global emerging market equity team that is highly rated. All we need to do is see a bit of a sentiment swing back to emerging markets and that team will be well rewarded.

John Foley in the UK life team, gave us a top up just recently of another $1 billion in preference to external third party managers. Just on the track record, I think the team is about 10% ahead of the global index over the last 12 months and doing a great job.

The case study here is infrastructure. I think at the last analyst day I mentioned infrastructure. Tony Adams and his team, closest thing we have ever done to a lift out. He is ex-JP Morgan. He brought along two of his former colleagues. We have $1.2 billion from life, $1 billion in debt, 200 in equity. We are about to put ink on paper with a really interesting deal with the World Bank infrastructure around IFC in global, emerging market, debt-related infrastructure. That is a $500-million transaction and we are happy to talk about that more another time.

However, a really great solution for life. It is diversified, it gives duration extension, it gives yield pick-up, it ticks all the boxes. The beauty about doing these things within the business and for life is that we then look for third-party opportunities to commercialise these sorts of capabilities. Not surprisingly, in infrastructure with like-minded insurance companies in Asia and the life sovereign wealth funds, we are already engaging in what will be the next step after we deploy the billion dollars for life.

Then pulling all that together for talent and investment capabilities is an investment in the focus on our infrastructure and our technology. The way in which we are doing that is to redesign what we call our target operating model. It is the foundation of what we build all of our asset management capabilities and client experience on. We have probably under-invested and it is time that we do invest if we are going to double and redouble this business again over the next four years and so on.

We have got to have a more robust platform. We are doing that, looking at our technologies right through mid-office and front office, which will give our investment professionals a better experience and give our client base a better experience. Part of that is the digital experience. Our joint venture in India generates now about 20% of their sales through an app called iPru. It is a fragmented market, India, and their point of sale is often in a rural environment, so the app brings the client complete with AML and all the tick boxes that are required, brings them to the mutual fund opportunity in their location.

We are looking at that sort of opportunity, the digital experience, in other markets where we do business to consumer, B2C. Taiwan is a great example. We are about to do a trial there where we have direct sales and we are going to digitise the client experience and make that a more robust one for them.

Digital By Default

Tony Wilkey

CEO, Prudential Corporation Asia

Leading Since the Last Millennium

We are running a little bit tight on time here, so I will summarise the next couple of slides.

For digital, Guy mentioned this and Lilian, really, two terms to take away for PCA in terms of digital: digital by default and digital dividend. Digital by default, this is not new for us. I mean, we could tell you that we opened our digital loft or garage, or whatever people choose to call them, in Singapore 14 years ago.

Fourteen years ago, we set up a team to build the first e-submittable applications for life insurance in Singapore. We have been doing this a long time simultaneously and I think more importantly than fancy front-end apps is the plumbing has to work. We spend a significant amount of time and money making sure the infrastructure was stable, scalable and secure. Now we are rolling out more and more applications.

Today, 13 of our life businesses are using e-submission of applications, five of our life businesses have 100% utilisation of e-submission of applications. This in a country like China and Vietnam where there is a lot of high-volume small tickets coming through the machines. A lot of work has been done there.

Digital dividend, we will not take up initiatives in this space just to talk about it. Everything we do in the digital space has to clearly demonstrate to us that it is going to add value to our P&L. We will continue to work on data analytics, propensity modelling and all these kinds of stuff but it has to be provable that it will actually drive repeat sales rate, incremental new business profit and so on.

Making an Impact with Our Wellness Initiatives

Something else that is also talked about quite a lot in our business is wellness. You can see from the slide we have done an awful lot of work here. We tend to take a little bit of a barbell approach.

SAFE STEPS

If you look on the left, SAFE STEPS, this is a very important initiative in the region. All thanks to Barry Stowe for starting this through the Prudence Foundation a couple of years ago. This is important work.

One person dies every 30 seconds in Asia in a road traffic accident. Five hundred children die a day in Asia in road traffic accidents. We have put together a whole bunch of programmes, and this with Michelle Yeoh who is a very famous Asian personality actress. If you watch National Geographic, you will see our educational – they are only 30-second clips – but teaching people basics like we may have learned years ago, look left, look right, look left before you cross the road. If you are on a moped, which are everywhere in Asia, wear a crash helmet; how to prepare for tsunamis, typhoons and so on.

We have a lot of work. We need to keep people alive before we can give them Fitbits and ask them to walk 10,000 steps a day. That is a lot of work being done in emerging markets and this is something again we are very passionate about.

myDNA

The other end of the extreme, Lilian talked about this with myDNA, which is a first to market that we launched in Hong Kong. Take the swab and it will tell you where you might have deficiencies in terms of you need more vitamin B or Omega-3 and stuff like this. Then it connects through an app directly to nutritionists on the phone who will advise you what you should be eating and so on and so forth.

Ultimately, this will migrate to real-time chat box using artificial intelligence in the background. That is the plan to make this more widespread and, as Lilian said, people had bought policies – since we have launched this initiative, they had actually come back to buy another policy to participate in the programme.

Winning in Asia Today

I mean, this is our track record. This is our CV. I think you all know it well. Earnings over the period have grown by 6 times. Our weighted life premiums last year were £10 billion, over 3 times what they were in 2006. Eastspring FUM has trebled over the period. I think overall a fairly acceptable set of results, but based on the opportunity we discussed earlier, there is a lot more work to be done.

Winning in Asia Tomorrow

I think this slide is fairly self-explanatory but on the right side, I mean where we are focussing? Obviously, it goes without saying we are focussing on continuing to execute well for the delivery agenda. However, we have to do a much better job in China. We have made good progress but it is not enough.

We have core advantages in ASEAN that we need to capitalise on better. Grow the protection gap is profound. It is not only an opportunity for us to make money but it is an important thing for us to do for the people who live in the countries where we live, work and operate. Lilian mentioned we have made good progress there.

Step-change Eastspring, doing okay but there is a lot more to do and Guy has got that in motion. Innovate where it makes sense and it can have an impact in driving results for us.

I think that is it. I think now we take Q&A.

Q&A

Arjan van Veen (UBS): Thank you. Two questions related to China, please. Firstly, the most obvious one. Obviously, a couple of weeks ago, UnionPay made some changes, so to the extent you can, if you can update on the impacts or potential impact to your business and whether there has been any clarification from either SAFE or CIRC around definitions on that announcement?

Secondly, given it is your first priority in terms of acceleration of China, your margins there are somewhat low, which I presume is because they are still bancassurance dominated. Your agency growth has been extremely strong. You have overtaken one of your key peers in terms of number of agents. I think, Tony, if I heard you correctly there, it was 16 out of 65 countries where you are really focussing in terms of growing that agency force.

If you can talk about in terms of if you think about the growth rate there going forward and how easy it is. What are the key obstacles, one, in terms of growing agents, quality agents, and then, secondly, on the margin side if there is a potential obviously to quadruple that or whatever in terms of getting good quality product? Thank you.

Tony Wilkey: Okay. Let me take the macro and Lilian can add some detail. I will take the second one first on the margins in China. I mean, this has been a very deliberate effort which probably started about 18 or 24 months ago to de-emphasise bancassurance. Our partner is Citigroup, Citibank is a big bank in the country. However, a lot of the appetite for product in China through bancassurance, similar to some other markets, is single premium into sensitive type products on Visa deposit replacing products where we are uncomfortable, so we backed away from that.

In fact, within the foreign sector, we used to rank number one or number two within bancassurance. I think we have dropped to number 5 or number 6, and we have no problem with that. As we moved away from bancassurance single premium, we focussed more on growing the agency. Lilian mentioned we are at record levels in terms of size but also productivity. Agency is able to deploy that richer product mix of health and protection which drives margin, solves needs that customers are looking for. I think we are making some good progress there.

Lilian Ng: Yes. I think in terms of the products being sold by our agency versus our competitors, it is actually as rich. It is a whole life, critical illness type of product. I mean, maybe later Adrian can comment on some of the financial assumption and need. However, bear in mind we are evolving to that richer portfolio, at the same time also bancassurance. I think, going forward, you will be able to see improvement on margin year on year.

Tony Wilkey: I think, Arjan, to put it in context, ten years ago working with our partner, CITIC, we would have had a tough time convincing them to move to a slightly different distribution focus and a different product mix because especially for many of the domestic Chinese companies, one of the most important metrics is market share.

As you know, for us market share is not an objective, it is an outcome. We have worked very hard to get them in this position of creating value. The China team, the most heavily weighted bonusable KPI is growth in embedded value.

Lilian Ng: That is right.

Tony Wilkey: Which would literally have been a foreign concept years ago.

On the first question which is how could we come here and not have a question on UnionPay and China, right? This is much a Hong Kong thing as it is a China thing. This is again not new. This started – interesting timing – on the Friday just before Chinese New Year in February with some guidance coming out of Safe and has subsequently been mulled on throughout the years with something coming down a couple of weeks ago.

Lilian Ng: Actually, it is not a change by UnionPay. All they are doing is affirming that the use of a UnionPay type cash card is not suitable for capital account type products. It is including insurance products with the investment and savings component. That is something that is actually reinforced and triggered by our payment solution provider through the banks.

Since that reinforcement, if I may call it, our customers are just using the right means of payment, mainly bank checks, direct debit, cash. Actually, we have not seen any negative impact as a result.

Tony Wilkey: We have all lived in Hong Kong for an extended period of time; there is generally not a lot of news in Hong Kong. There are some interesting stuff going on with the legislator right now but generally there is not a lot of news. Stuff like this, it gets a lot of visibility in the media and, from our perspective, draws a lot more attention to it than really causes us concern in terms of impact to the continuity of the business.

Most of our, I think, survey says 80% of our mainland Chinese customers who buy products in Hong Kong, 80% have Hong Kong bank accounts. It is just the UnionPay is like an Oyster card and it has just been very convenient. I think there are 17 or 18 alternative payment channels available.

Jon Hocking (Morgan Stanley): Good morning, everybody. I have got two questions, please. Firstly on China, I was wondering whether you could comment on your degree of strategic alignment with CITIC. Are they interested in growing this business to a large size, interest in capital return? You have mentioned you have managed to de-emphasise the bank channel with them. How do you think about it when you sit down with them in terms of business planning? Then linked to that, ultimately, is the ambition here to have a wholly-owned Chinese business when that becomes an option?

Then second question on Eastspring. In terms of distribution, you mentioned the $10,000 GDP shift when mutual funds become more of a sort of standalone product. How do you see the distribution of Eastspring evolving and how are you preparing the ground for that in terms of the sort of country mix and channel mix? Thank you.

Tony Wilkey: Sure. I think Guy can take the Eastspring thing and, again, let me do the macro on China. Lilian can add some colour.

I mean, again, I think as I stated earlier, the relationship with CITIC is as good as it has ever been. I mean, the Chairman of CITIC, Chairman Chang Zhenming, came from the insurance business and is incredibly interested and passionate about the business. They have been incredibly supportive of the direction in which the business is going. They have brought to bear significant assets. I mean, CITIC Group is a massive state-owned enterprise and they have brought a lot of distribution and asset and other types of opportunities to the business that we have been able to grow.

The JVs in China are really run through the board and we have equal representation on the board and so we do the business planning jointly and make sure the strategic direction, the financial KPIs, all flowing in the right direction and, again, weighting on value more than volume and getting them off that, you know, we must have significant market shares has been an interesting exercise.

The law today in China is 50/50 for foreigners. There is one exception. Frankly, most, as you have seen over the years, many of our foreign competitors have actually sold down and there has been a lot of pressure in the marketplace from the local partners. We obviously resisted that. Where the opportunity presented to increase, I think that is something we would have to look at very closely.

Lilian Ng: I think on the business planning side, I think the last couple of years, we have been working very hard to actually educate our other partners, CITIC, in terms of what is the value of an insurance company. It is more than a market share. Over the last 12 months and I mentioned earlier about shifting our strategy towards regular premium, actually, this is endorsed by one of the directors who sits on the CITIC-Prudential board. She is actually the chairman of CITIC Bank now and I think she saw how we have been able to increase value in the right way. I think it was a bit of a challenge. Probably, if you look back 12/18 months ago, I think, going forward, I think they understand what does it mean to drive value in insurance company, so very, very supportive.

Guy Strapp: Jon, on distribution, you can think of Asia – gross generalisation – but there is North Asia and South Asia, basically, and we look at the reciprocal of the life business. We generate most of our sales in North Asia. Most of that is intermediated, sophisticated investors through securities and brokerage houses in Japan and then, if you come South, it is private banks, regional banks, local banks. That is successful. I am fully aware that the pressure on banks to generate a return, and so commissions is on trail, always a sensitive topic, and conscious of not being dis-intermediated away from the end client.

Yes, I think the successful programme that they have run in India in terms of digital access to clients is a really interesting model. We are looking at that in Taiwan. In Malaysia, we actually use some of the agents. We use both some independent agents as well as Pru Life agents to distribute some mutual funds. Again, it is on a pretty small scale but these are all models that we are kind of considering in terms of ways to access the client.

I think as Southeast Asia becomes more affluent and that 10,000 barrier is breached, we have had several strategic discussions about wealth propositions and how we can utilise the top tier of agents without cannibalising the Life sale. We are thinking about that as well.

Time is on our side because a lot of those Southeast Asian economies are still some ways away from getting to that 10,000 level but it is on the radar and it is going to be relevant in the next five years.

Blair Stewart (Bank of America Merrill Lynch): Thanks. Thanks very much indeed. I have two questions. Firstly, on Hong Kong and mainland Chinese business into Hong Kong, how do you assess the risk of a more draconian approach, for example, to stop the business being done completely? If that did happen, what would your approach be? Would you be able to migrate any of that business back onto the mainland?

Secondly, just an indication, really, as to the rate of change in Indonesia at the moment? At what points would you expect to see a positive new business growth coming back on stream again, please? Thank you.

Tony Wilkey: Sure. I think relative to potential risks, Blair, in Hong Kong, we have taken the approach, the strategy fairly consistently that you need to be prepared and actually winning on both sides of the border, which is precisely why building and ramping up our China business is very important to us. I do not think anybody has a crystal ball, but OCI, the Hong Kong regulator, and CIRC in Beijing, the China regulator, are very familiar with the flows. They have been measuring and monitoring for an extended period of time. I think it will be very challenging for them to completely close the border at this stage.

Lilian Ng: I think by the fact that I think I mentioned earlier about the implementation of the important fact sheet for mainland Chinese policyholder buying insurance in Hong Kong. Actually, that is also in partnership with CIRC. I see there is a formalisation that they are endorsing the purchase but we are ensuring the consumers understand what they are buying.

Tony Wilkey: Yes. I mean, there is obviously a concentration in the Hong Kong business today. As, I think, Adrian mentioned five years ago, Indonesia was the big engine. Ten years ago, it was Korea and India. If we do our jobs well, five years from now it should be China. Hopefully, you will not be complaining that we have concentration risk in China at that point.

The second one, in terms of Indonesia, where we are, I do not know if you want to add a little bit colour?

Lilian Ng: We are evolving our agency model. What we are tracking on them is make sure there is month-on-month momentum to drive that growth. Hopefully, when the economies pick up, we will see probably growth stepping up. I think we believe, I think, this will be the last quarter and there will be an inflection point starting 2017.

In terms of the market, I think if you look at the market stat, there seems to be some growth there. A lot of this is actually generated from the local player using very short-term products. Some of them is as extreme, as you say, quarterly renew products, so they count the premium four times in a year.

I think if you just look at where we are, so we focus on growing our agency, continue to grow there for the regular premium space.

Tony Wilkey: Yes. I mean, in Indonesia, we are not sitting there waiting for the market to turn. We continue to execute on a daily basis. We have improved our agency selection tools, our onboarding, continue to open new GA offices around the region at times like this. We kind of went through similar times with global financial crisis back in 2008/2009. I hate to sound terribly tactical but you have to micro or nano-manage the business on a daily basis, are the agents active, are they seeing enough clients, so on and so forth; sales, regular sales metrics. We have been driving that consistently throughout the year, looking at month-on-month progress, so direction of travel, month-on-month throughout the year looking positive, so feeling better.

Lance Burbidge (Autonomous Research): A couple of questions and sorry to dwell on Hong Kong and mainland China business, but I appreciate it is hard to tell how China could shut it down, but let us say it did somehow, what would the agents that are focussed on that business actually do and how would you cope with that transition? I wonder if Adrian could give some idea about if it were to disappear, the impact on the IFRS profits for the overall Asia business and over the next few years as to how much that would impact.

Then on China as well, I am a little bit confused as to where we are in the process of what we are seeing. I mean, obviously, our new business profit growth was only about 10% in the first half, so I assume some of that is bancassurance drifting off and the agency business growing. Could you kind of give an idea in terms of what agency growth was and where you might expect that to go, because, obviously, some of your competitors are seeing much or very rapid growth on that side?

Tony Wilkey: Sure. I mean, should the border close completely, what would happen to the agents? It is difficult to tell. I mean, these agents, all by licencing requirements, have to have Hong Kong ID residency cards. However, originally, many of them came from the mainland. One could conceive that there might be opportunities elsewhere should that happen. However, again, that is something we are not expecting nor anticipating.

In terms of the margin movement, I do not know, Adrian, if you want to talk about that a little bit.

Adrian O'Connor: Well, if you actually refer back to in terms of profitability, refer back to one of the slides in Hong Kong, that does actually show the split of EV between mainland and local and, even now, it is significantly local. I mean, the in-force block of business in terms of producing profit is still coming. This phenomenon is not, in terms of profit in the short-term or even the medium-term, not great, not a big issue.

Mike Wells: Guys, the other thing, I think, just for context, so again, 15% of Hong Kong's business to China, it is about 70 basis points of group earnings. I know there is a lot of attention on the topic, but again, I think in the extreme, the team has got it well-handled and an impact to a group our size is very manageable.

Andy Hughes (Macquarie): Hi, guys. Three questions if I could. The first one is on India, it is maybe a group question. However, obviously, we heard the focus on cash over top line growth. I am kind of wondering how India fits into this because if India is currently worth three times embedded value, it is not going to be a huge cash generator relative to the market value of the holding. I noticed there were no slides on India today on the life side of your presentation.

Second question is on Hong Kong, but slightly different this time. Interest rates are ticking up in the US, which may or may not mean that reversionary bonus rates go up because, obviously, the IFRS earnings from the with-profit fund are pretty low as interest rates have been low. Where are we on the reversionary bonus rates for the kind of with-profit business in Hong Kong? Is that still on its way down? However, as interest rates tick up, do you expect that to increase and how sensitive to earnings is that, please?

The final question on Indonesia. Obviously, you mentioned the master plan which I think is a one million agent target which is around 7,000 a month. As a market leader, that is going to take a long time to get to one million agents. I am just wondering, is the slowdown in Indonesia driven by lower agent growth because I look at the consumer confidence index that you highlighted last time for Indonesia and that has actually recovered to very strong levels, which would suggest that the market confidence is still there amongst consumers. I am wondering why you think it is going to be 2017 before it turns a corner. Thank you.

Tony Wilkey: On India, as you will have seen – well, before the IPO, let us back up, the regulations changed earlier in the year, permitting foreign companies to go from 26% to 49%. Within that, what was very clear was even if you bought up to the 49%, you would not get control of the operations. In many ways, you just memorialise the fact that you are an investor in that market and to truly leverage our IP, I think, in that market required control.

Further, I mean, there were some small placements of Indian businesses that you might have seen that were, from our perspective, I think quite excessive multiples coming through. We did not buy up. I mean, our business in India, again, a great partner, it is one of the biggest and considered one of the best insurance companies in the country. From a PCA perspective, it is probably one of the lower value businesses we have in the portfolio. The regulatory environment there is incredibly complicated and dynamic, and so there were a whole series of reasons for not doing that.

We went through the IPO in September, and you are right. They are priced at the high-end of the range, 3.4 times embedded value. ICICI floated a piece of their share. We maintained our 26%. We have optionality going forward, that is pretty much where we are.

Adrian O'Connor: On the Hong Kong question, I mean, I will just again refer you back to my presentation earlier this year because a vast majority of the current profits come actually from the protection piece. The second thing to mention is that the design of our par products throughout the region actually is probably different to what you find here. Reversionary bonus is probably a third of the bonus and two-thirds comes from additional bonus. We offer a total return proposition. Yes, reversionary bonus has been coming down because of the low interest rate environment, but the impact in profitability in the short term is very small.

Lilian Ng: I think in terms of the aspiration of the government, I think what they are looking for is spreading the agency programme. That is why to echo that, we are embarking on getting the Sharia business up and running and where we see that is how the agency footprint can expand.

Actually currently, what we are seeing in the overall agency in the market is not growing. I think the challenge I think we have mentioned many times given the difficult challenging market, if we recruit in Asia it is very difficult for them to close a case. It is not about difficulty in recruiting, it is difficulty challenging and activation of the agents to make them earn enough to sustain themselves as an agent. I think that is what we are seeing.

Hopefully, with the economic environment recovering, they are able to close better and we will be able sustain more agents.

Tony Wilkey: The Sharia point is very important. As you know in Malaysia, we lead the market in Takaful. In Indonesia and it is 250 million people, the majority of the population are Muslim and uptake of Sharia has been incredibly limited. I mean broadly if you look side by side, the profit signature from product of conventional versus Sharia, it is generally the same.

As Lillian mentioned, this is a business, it is not a product line, and we have got close to 100,000 agents licensed to sell that product and we think there is great opportunity to expand in that area. Sharia tends to be a little bit more provincial than Jakarta-based. Most of the competitors that fight in over the business in Jakarta, 16 to 18 million people in Jakarta, whereas we built the platform out in the provinces and much like what we did in Vietnam and less competitive space, great opportunity.

Nick Holmes (Société Générale): Thank you. Back to Hong Kong, just wanted to ask, irrespective of UnionPay and regulatory intervention, what is the basic attraction to the mainland Chinese of the product? How sustainable aside from all of the regulatory side is this level of massive inflow? And I fully appreciate, by the way, Mike's comment that it is not relevant to earnings, but to sales obviously just the moment it is. Thank you.

Tony Wilkey: Actually, it is more than the product proposition. Frankly, I think we have got a lot of successful traction based on who we are. If you look at our name – why is our name not up there in Chinese? If you look at our name in Chinese, it is Yīngguó jǐnshèn[?], UK Prudential. A lot of the mainlanders feel like they are buying a piece of the UK when they buy product from us, which has a great history of law and stability and so on and so forth. Our service is exceptional in Hong Kong I think compared to what might be broadly realised on the mainland, and so it is a complement of different pieces.

Lilian Ng: Diving into the technical products, the products in Hong Kong are more attractive. In Hong Kong it is principle-based regulation, so there is more flexibility for insurers to price the products; whereas in China it is more rules-based. Actually, this has been actually discussed by the CIRC to see how they can create a more competitive set of products.

That is why it is also important for us to win in China. Going back to our strategies, we need to do well in both.

US Overview

Barry Stowe

Chairman & CEO, North America, Prudential plc

Introduction

Good morning. Yes, good morning. I hope everyone is well. For the next quite a while, I think we have a total of about three hours on stage before you today, myself and the Jackson team. It is an exciting time for our business in North America. It is an exciting time in North America, as you have all read and seen. Some interesting things going on and the political scene and the regulatory scene is obviously going to be woven through the story we tell today because it is important, but there is a very big story to tell here and it is consistent with the story we have told you in the past.

American Retirement Crisis

The slide that you see before you now, this is not the first time you have seen this slide. You have seen it for many years. I mean, I have been with the group for over ten years now and I can remember at my very first investor conference, Clark Manning standing up and talking about baby boomers and this wave of baby boomers that are coming towards us. This has consistently been the linchpin of our North American story.

It is happening. Everything we said was going to happen is happening. We have been talking about it for a long time. Again, referring to the events of last week, most of the pundits are suggesting, and I think accurately, that one of the reasons that President Elect Trump was successful is because he was listening to voices that others did not hear. He tapped into anger and frustration amongst a segment of the population that believed its issues and its needs were not being listened to.

Many people in this group fit that description. You look at these cohorts. Last year, in 2015, that is when the people born in 1950 turned 65. You see, we are only a few years into the baby boom. The number of people that are going to be retiring each year for the next decade is going to go up and up and up. Here is an interesting factoid. If you look at these people, if you look at American households where the principal householder is between 65 and 74 years old, the median net worth of that household is $232,000, and that includes the equity that that family has in their home.

These people are not going to live to be 72 like their parents or their grandparents did. They have every expectation of living into their 90s. This is a real problem. It is a problem that has not up to now been effectively addressed and it is one that now, finally, there is broad bipartisan support in Washington recognising the gravity of this issue and wishing to deal with it. It will be a public approach. Particularly with a unified Republican government, you will not get Trumpcare, Trump retirement. That would not be on the table.

This is a private approach enabled by political and regulatory leadership. It is an interesting moment in our industry in the United States where there is a real prospect, a real opportunity for those who lead the industry to be influential in helping to shape how America grapples with this problem. If you want to participate, if you are leading the industry, when we do lead the industry commercially and I would suggest to you in this retirement space, where we play, this guaranteed retirement income space which is the dimension of the marketplace that leadership, political and regulatory leaders are focussed on, we are the leader in that space.

We have a track record of capability and competence and performance that no one else can match. We are engaged very much in this process. It is important to be engaged and I think over the course of the last year, we have learned a lot. We have taught a lot, but we have recognised that there is a real opportunity to shape the future.

A lot of the questions that you have been asking over the last several months have been related to regulatory change, generally, but specifically to the DOL rule and to the NAIC, the prospect that there could be changes through the NAIC in terms of capital regimes and so forth. We will address all those issues today.

What we want to do first is address the DOL issue. We have stood before you in the past and we have talked about our view of DOL, how we think we will be prepared for it, how we think it could benefit us, what the short-term positive or negative impact might be. However, we thought it would be useful for you to listen to someone for a little while this morning and have the opportunity to interact with someone who can speak to this topic with enormous credibility.

Seth Harris

Seth Harris, I think he is probably most accurately described – you can see his CV, but he is most accurately described as the go-to guy for left of centre politicians in the United States on everything relating to labour. He studied labour issues in university, has spent his entire career dealing with labour issues, advising both the Clinton Administration and obviously the Obama Administration where he acted as Deputy Secretary of Labor and then as Secretary of Labor for President Obama.

He left government service about two years ago now and went back to academia and to the private sector. We have gotten to know Seth over the last six months. He has brilliant insights into this issue. Obviously, he is uniquely qualified to talk about the rule because he was in the room when it happened. We have blamed him for it on occasion in the past, but he says no, he was not the only author of it, but certainly was influential in crafting the rule.

I think what you will hear him say about the rule and the view of regulatory authorities in Washington, how they feel about the products that we sell and how we sell it may surprise you a little bit. However, I do not want to eat into any more of his time, so would you join me in welcoming Secretary Harris to the stage?

DOL's Fiduciary Duty Regulation

Seth Harris

Former Acting United States Secretary of Labor and Deputy United States Secretary of Labor

Introduction

Thank you very much. Good morning, everyone. You may have heard that my former colleagues at the US Department of Labor produced a new regulation that a lot of people are calling an epical regulation that is going to transform the US retirement industry. What I would like to be able to do is give you a little insight into what the thinking was and perhaps what the effect will be of the regulation.

The Customer's Best Interest

The rule essentially says, and let me say it is 1,000 pages long and extraordinarily complicated. I will leave the details to others who are going to present shortly. However, the rule essentially says that advisers who are making recommendations to individual retirement investors, individuals who are trying to get advice about retirement, about their retirement investments, and the adviser is getting compensation for providing that advice, as virtually everybody in the business does, those advisers must give advice that is in the investor's, the customer's best interest. Not the adviser's best interest, not the adviser's employer's best interest, but in the customer's best interest.

Leakage

The rule was designed to deal with a problem that in policy circles we call leakage – and that is investors' retirement savings should not go to excessive fees or excessive commissions or undue risk. Retirement investors saved this money. They need their money to be able to support themselves through retirement. To the extent possible, we want to keep that money in their hands, in their retirement accounts.

It is important to note that the regulation does not target particular products. Different products are treated a little bit differently in different parts of the rule, but as a general matter, it is a rule about distribution of retirement products and all retirement products. Generally speaking, all advice about all products must be provided in the best interest of the investor, of the customer.

It is also important to point out the US regulation is not the UK regulation. We were fortunate that your regulators went first and we had an opportunity to see the results and the turmoil, the controversy, and the US regulation is significantly less prescriptive. It is a principles-based regulation. The core principle, the most important principle is this best interests principle, that everything that is done by the adviser must be done in the best interest of the customer.

I believe here is what we thought. Here is what was in our minds when we were promulgating this regulation. For the ordinary American, figuring out how to invest their savings so that they would have sufficient money to support themselves through the rest of their lives after retirement is much too hard. It is extraordinarily complicated. The products are extraordinarily complicated.

As some of the consumer and worker advocates have said to me since I left government, it is just too much work for ordinary Americans. It is too hard to understand everything they need to understand, to do a really good job making sophisticated investment decisions, so they need expert advice. They need help from someone who really knows the business.

The role of the adviser

Now, that creates sort of an interesting opportunity and maybe a counterintuitive result, I think, from the rule. Let me talk a little bit about what the adviser does, although you all know this business far better than I do. However, the premise of the rule is that the adviser essentially has two tasks. One, they have to help the customer, the investor, to understand the investor's needs like how long am I going to live and, therefore, how long do I need to have income, right? How much risk can I tolerate? What assets do I bring to the table? What sources of income do I have available to me among many, many other questions – morbidity risks and other things. That is task number one. Task number two is there are a dizzying array of products that are available for people who are trying to invest their retirement savings. The adviser is supposed to be not merely expert in helping the customer to understand their needs, but also understanding the products and then figuring out which products best serve each individual investor, customer's needs, right? Boy, is that a hard job. That is a very, very, very difficult task.

What this rule says is in the process of conducting that work, everything you do must be in the best interest of the customer. What is the sort of counterintuitive take on this? I do not want to sugar-coat this, the consequences of this regulation. This is a very complicated regulation. It requires a tremendous amount of work to comply. I am advising a number of clients. Jackson actually is not one of them, but I am advising a number of clients about how to come into compliance with this regulation.

It requires lots of paperwork, lots of disclosure, lots of policy changes, system – it is a lot of work. I do not want to suggest that this is all a breeze. However, there is a reaction in the business community. I think the initial reaction almost always is new regulation is bad. I want to tell you how this new regulation – I am not going to try and sell you that it is good, but I am going to try and sell you that maybe there is something counterintuitive and interesting and important that is going to happen here.

Leakage is not the only problem in American retirement security, and Barry referenced this point, but he did not label it, so I will label it. Millions and millions and millions and millions of Americans are arriving at my age, a little older, maybe significantly older, without enough money for retirement. They do not have traditional pensions that will pay them a reliable amount of money every month in retirement. In the US, we call those defined benefit pensions. You all heard that phrase before, right?

They have a pot of money and it is not big enough. That is called adequacy or, more precisely, inadequacy. They have inadequate savings, so they need to grow their savings. Because they do not have a traditional pension, they need a guarantee of a lifetime income flow.

This rule requires that the advisers sit down with investor and talk about which products will satisfy that need. Now, not everybody has that need. There are high worth individuals who are essentially self-insured who maybe do not need that help, maybe they do, but there are lots and lots of folks who need to grow and need a guarantee.

The best interest standard says that the adviser must at least introduce into the discussion the products that will provide that kind of service, that kind of an outcome, variable annuity as being one of them. I would go so far as to say that if you are not as an adviser or a broker dealer or some other kind of company that provides retirement advice, if you are never introducing those kinds of products into the discussion, variable annuities and others into a discussion with anyone, you are likely violating the best interest standard because you are supposed to marry needs to products. In some number of cases, variable annuities and other products that guarantee lifetime income and that allow you to grow your wealth, you accumulate further retirement savings, are necessary products for the customer.

The Trump Effect

That may well create an interesting business opportunity. Okay. Now, before I turn over to Q&A to you, let me ask the question that you all have in your minds. What about Trump? Let me just say, that is the question he would want me to ask as well. If he were here, he would be upset that it took me this long to get to him.

Maybe to put a finer point on the question, will the regulation survive a Trump presidency? I will not comment on whether anything else will survive a Trump presidency, but will the regulation survive a Trump presidency or, more precisely, will it be modified? Will it be killed? What will happen?

The honest answer is we do not really know yet, right? Precisely four people have been hired for the Trump Administration: the President Elect, the Vice President Elect, the Chief of Staff and a Senior Adviser. We do not know who the Secretary of Labor is going to be, my former position, the person who will be most directly involved in this, the person who runs the agency that promulgated the regulation within the Labor Department. We do not know any of that. We do not know who the topic economic advisers are going to be in the White House. There are lots of rumours floating around. Decisions may well have been made but they certainly have not yet been made public.

There are going to be some calls to get rid of the rule entirely. However, one way to understand the election, and I think we are all still trying to figure out what the election meant, is as follows. It was the revenge of the working class and middle class in America. They have been left behind by globalisation and technological modernisation. They are angry that the government seems to help everyone but them. They are uncertain about their place in society. They are worried about their economic future and their children's opportunities. Does that ring a bell with anybody from the UK? Very similar, I think. Not identical, but very similar.

While those voters may not be able to tell you about this regulation or even know that it is out there, we intended this regulation to serve those voters, to protect the retirement interests of those voters, among others. There is sort of a complex little line that the Trump Administration is going to have to walk. If you believe that President Obama and my successor and friend, Tom Perez, won the debate over how retirement products are distributed and the risks that are attending that, well then repealing the regulation creates a potential political problem for the Trump organisation, the Trump Administration and their political base.

If you do not believe that, then he maybe has a little bit more freedom of movement. We are in for – I think the phrase 'interesting times' was used. We are in interesting times in the US, so let us make this more interesting times by opening it up to Q&A from you.

Q&A

Jon Hocking (Morgan Stanley): Good morning. The comment you made about having to consider the retirement security of the individual from an adviser's point of view, is that limited to the products they have got on the shelf? Is the obligation to act in the best interest of the client given the toolkit you have got available as an adviser or is that not a defence?

Seth Harris: That is a superb question to which we do not yet have a complete answer from my friends in the Labor Department. The question is, in essence, whether the decision regarding what products you include on your shelf is itself a recommendation that is subject to the best interest standard. I have sort of rephrased what you said but I think that captures what you are saying.

In the case of organisations that are selling entirely proprietary products, it is permissible to limit your shelf to proprietary products subject to a much more extensive set of disclosures and an explanation as to why you are only offering proprietary products.

With respect to independent agents or hybrid agents who have products from multiple manufacturers, it is much more complicated. I think the answer will probably – I do not want to over predict here but my educated guess would be that you are not required to have a comprehensive set of products on your shelf. You can have a limited shelf but you must be able to justify that shelf and the advice must include an explanation that there are other products out there, you may want to talk to someone else.

Here is why I think that is what is going to happen. It would not be reasonable to expect, for example insurance agents, to become experts in more exotic retirement vehicles simply because that is not what they do. They are not intended to be deliverers of that kind of a product, distributors of that kind of product. My guess would be that as long as there is clarity about why the shelf is limited and that the investor should look at other options as well, I think a more limited shelf will not itself violate the best interest standard. Is that fair?

Marcus Barnard (Numis Securities): If the agent has got an obligation to sell something that is appropriate and in the best interest, is there any liability if that product does not subsequently do what it was supposed to do? I mean, does that fall back to the agent or to the product provider? Is there is any sort of redress if it does not provide the income expected?

Seth Harris: That is another excellent question about the rule. First, I want to distinguish between best interest and acceptability. The standard under other laws is a version of an acceptability standard. This is a different standard. The advice must be in the best interest given all the circumstances in which the investor finds him or herself. It really does require understanding the needs of the investor and then understanding the products and matching them up.

The suitability, which is the literal phrase of the standard under other laws, is a different kind of standard. I am going to say something here that is counterintuitive to a lot of people, I think. The fact that an investment performed poorly in and of itself is not sufficient to violate the best interest standard, in my view. The best interest is judged at the time at which the advice is given. I think it would be unreasonable for anyone to expect that any kind of retirement adviser is going to be able to predict into the foreseeable or even unforeseeable future how any particular product is going to perform.

Having said that, the failure of a product to perform as expected is likely to spawn law suits. That is one of the big changes in this rule, the enforcement mechanism. I am not going to get into a lot of detail about the rule but, very simply, if you want to give retirement advice in return for compensation, you must enter into, in most cases, not all cases, but in most cases, you must enter into a contract with the retirement investor. That contract subjects the adviser and probably the adviser's employer or the adviser's financial institution, as the phrase that is used, to a private lawsuit or, worse, a class action lawsuit by that investor and perhaps similarly situated people. Those lawsuits will be brought in either state court or federal court in the United States, courts that have not encountered these kinds of retirement income issues before in most cases.

That enforcement mechanism is – I do not want to overstate the case or try to speak for everyone – it is certainly one of the top two, or three, or four issues among people in the retirement industry with this regulation. They are worried about their litigation risk arising out of the rule.

Andy Hughes (Macquarie): Just catching up on that litigation point, some guys have volatility controlled funds. Are they something that is particularly worrying in this market environment? My second question was, if I am thinking about best advice, I would not even know how to start to compare a variable annuity with guarantees and work out what the value is for the client versus a straightforward mutual fund. I mean, is that the problem is just not easy to prove that you gave best advice and that it was value for money?

Seth Harris: I am not the right person to ask about vol control funds in the market. That is not my area of expertise. Vol control funds are treated like any other product. Under the rule, they are subject to the best interest standard. They are subject to disclosure requirements. I do not think that they are uniquely disadvantaged by the rule except to the extent that there is really a requirement there of a full explanation of what the product does and does not do. Vol control is going to be a challenge to explain to ordinary Americans and the risk that it will not come out the way it has promised is not insubstantial, as I understand it. You all are more expert again than I am.

Explaining the difference between mutual funds and variable annuities requires the adviser to be expert on the products and be able to explain the products in a manner that is accessible to ordinary Americans, although the rule does not literally say that. In order to understand and articulate their best interest, I think that that is going to be what is required.

The question of a guarantee which is available on a VA which is, as I understand it, certainly not available in any of mutual funds that I own, that is a consequence of this dialogue between the adviser and investor. How important is a guarantee to the investor? I am hypothesising to you that because defined benefit pensions are – they are not quite unicorns in the United States but if you work in the private sector and do not work for a unionised corporation, they are approaching unicorn status. I think that guarantees at least have to be a part of the conversation when an investor says, 'Gee, I do not know what I am going to do about making sure I can make my house payments, making sure I can support my kids. I need some reliability.' When that kind of language comes up, I think that has to be a part of the conversation in best interest.

It does not mean that every single time that that is the product that has to be bought or sold, but it is unimaginable to me that you are operating in someone's best interest and not having that conversation.

Now, having said that, there is the shelf question that we talked about before. Not everybody offers every product but I think it is going to be very difficult to not have those conversations and satisfy the best interest standard.

Lance Burbidge (Autonomous Research): When Secretary Perez gave his evidence, the first thing that he mentioned was the expense of variable annuity effectively or the unsuitability of variable annuities to the wrong person. I wonder how that squares with your point that actually you think it is an acceptable product. I mean, do you think it is an acceptable that is too high charging and so the charges have to come down or something else?

Seth Harris: Secretary Perez was talking about distribution. I do not think that he was painting all VAs with the same brush. I think that more than anything else what he was doing was commenting on the complexity of not merely the product but the manner in which the product is compensated, how it is paid for by the retirement investor.

However, I do not think he intended to say variable annuity is bad always. He is a dear friend of mine, but I would also say even if that were his view, that is absolutely not what this rule says. The original version of this rule, as we originally proposed it in 2010, was extremely prescriptive and guided retirement investors towards low risk, low fee investments. That was the push of the rule.

Again, it was partly an answer to this question, how do we deal with the fact that retirement investing is fantastically complex for the ordinary American and it is too much work, they cannot figure it out. The answer was we will make the decisions for them. We will either set up a set of defaults or we will just outright make the decisions for them. That was greeted unenthusiastically in the political environment. Is that fair? Maybe I am understating it a little bit.

This rule does not do that. It mildly favours certain simpler products by requiring less for those who sell them but very few products are treated that way. Very, very few and they are very, very simple and low risk and low fee.

This rule treats VAs like every other product that if it is in the best interest of the customer, you got to at least talk about it and if it is the right thing, you got to recommend it and when we also say, 'They got to sell it,' they then have to sell it. Again, if you take adequacy seriously, as I know my colleagues, the current colleagues in the Labor department do, they are deeply worried about it. They care very deeply about lifetime income. There is legislation pending in the United States Senate right now that will push annuities very aggressively, create new opportunities for annuities that is supported in large part by the Labor department.

In fact, some of the provisions are based on rules that the Labor department has in draft, ready to go, that advocate for lifetime income illustrations for example. Lifetime income is at the core of the retirement debate in the United States and the folks in the pension agency and the Labor department want that. They want folks to move towards lifetime income because they understand, without defined benefit pensions, this is the only way you can go.

I am getting the red flashing light. Should I take one more? No? No, I should not. I should not take one more. Let me just say, I apologise to those of you who I just teased. I am staying for lunch, so if you can grab me at lunch, I would be delighted to answer more questions. Thank you for your time.

US Distribution

Barry Stowe

Chairman & CEO, North America, Prudential plc

A Confluence of Trends

Thank you. There is something interesting going on here. When these rules first come out, we wringed our hands as an industry and we say, 'They are after us again. They must be listening to Suze Orman on TV who says annuities are always bad and no one should ever buy one.' However, something is going on here and you heard it from Seth who is the most credible person I can think of on the topic. Through Seth, we have had the opportunity to meet people within the Department of Labor, to meet people within the Department of Treasury, to meet people and consumer activist groups who focus on the needs of retirees, groups like AARP and lots of others.

What we hear consistently when we sit down with them and say, 'Let us take all the noise out of the room and explain to you what we are trying to do, what we think our product is meant to do when it is sold properly,' we get enthusiastic thumbs up from everyone. This is great. This sounds like exactly the product that people need. As Seth said, there is a bill that has just moved out of committee in the US Senate that would require people receiving distributions in certain instances for retirement be shown an illustration for a product that provides a lifetime income. Mandatory provision of that illustration, that is obviously very good for us. That bill moved through the Senate Finance Committee with – I think it was unanimous – broad bipartisan support. Something is happening here.

There is the political support in Washington for this. There is a trajectory of regulation that is focussed on consumer centricity, higher quality in every respect. There is going to be a drive towards quality in every respect. I think what we will see as we go forward is a drive for higher quality advice, for higher quality product, for better performance for consumers. I am going to answer your question here in the next few minutes about vol control funds. The slides are not copyrighted. You can have it laminated and show it to people. In terms of service, in terms of how we interact with people. That is what is going to the mandate about our industry.

Companies that are well suited to this environment as I think we are because hopefully, you will leave today having even stronger conviction than you already have that Jackson is clearly the best in class operator in this retirement space. I believe that there is a confluence of things happening here that is going to precipitate higher quality, a flight to quality and potentially a dramatic expansion of this market.

The VA market specifically has almost halved in scale over the last several years, down to about 100 billion in flows last year. When you look at that slide I showed you earlier, the baby boomers and the trajectory of the number of people retiring, the demand is going up so there is a disconnect there that I think the trends in the marketplace are going to correct.

Let us think about these four things I noted: quality of advice, quality of product, quality performance and quality service. Let us start with advice.

Advice

If you look at the bottom of this chart, what you see there really in terms of the industry, there is about 100,000 advisers who characterise themselves as regular sellers of annuity products. Of those, about 50,000 wrote a Jackson policy last year so you look at that and say, 'Holy cow, 50% market share.' 13,000 of the 50, we call it top producers. They gave us, on behalf of customer assets of at least \$0.5 million, at least 500,000 in flows. Those are our top producer, 13,000 of those last year.

This is always how we have characterised our marketplace. This is how we have talked about distribution, always in this context. There are these people that sell this product and the ones that sell it, they really like us. However, as you move up what you realise is there is over 300,000 retail financial advisers in the United States. Most of them have not been selling this product. I think our future as an organisation and our industry's future is tied not to just to the 100,000 but to the 300,000. As the regulatory environment evolves and you heard Seth say this, and in delivering messages like this because there is no one more credible than Seth. As the regulatory environment involves more and more financial advisers are going to realise perhaps be told by their compliance departments that you need to be illustrating products that are for a guaranteed lifetime income.

There is an enormous segment of the market out there in terms of the distribution landscape that do not currently sell these products that should be. Now, what are the obstacles to this? One of the principal obstacles to this has been the fact that VAs and other annuity products have always been sold with commission-based compensation versus fee based. For many of these 300,000, that is the principal obstacle. They do not like the idea of taking commissions, they like fees. You can a rational argument with sensible people about which is better for consumers but they believe that a commission by its very nature indicates that perhaps they have chosen in their best interest not in the client's best interest and so they simply avoid the problem by not selling commission-based products.

We have now launched an advisory-based product and you have seen us with products like Elite access in the past take new products ideas and get traction very quickly and grow them into significant flow and revenues streams and I have every confidence that you will see that with the advisory product as it takes off in the coming quarters.

There is a huge opportunity here, an untapped marketplace if you will, in the advisory space. As these advisers, again, are seeking high quality lifetime income solutions, we will benefit from that. It is natural that the company who has managed this with discipline and with positive outcomes for all constituencies through the cycles for its entire history will benefit significantly as more advisers start selling these products.

Product

Let us talk about product for a minute. I think, again, as the standards increase for the provision of advice, as regulatory regimes emphasise the importance of lifetime income, you have to believe that our product has much greater appeal.

Look at some of the options. In the world in which we live, these are the products that people talk about. We have listed here the key considerations. The things that a retail investor, this typical baby boomer, these are the things he is going to look at it and say, 'Here are the things that I might need. I would love to have a lifetime income without giving you my money irrevocably and can never get it back because I want to have the prospect of liquidity if I need it. I would like to have a death benefit. I would, after having drawn down income, I would like to leave something for my kids or for my grandkids.' That is a need that many people desire to have.

'I need protection.' We are an organisation. Our industry, the thing that defines us, that makes us different than mutual funds or banks or anyone else, is that we can sell protection. This is how we get paid. We sell protection and I talked to you for years about the protection story in Asia. The fact that matter is we have a tremendous protection story to tell in North America, different kind of protection that we are providing to a different demographic but it is basically a protection product that drives our organisation.

They want the ability to select investments. The reason they want the ability to select investment is because they do not just want, they need access to uncap market returns. You heard Seth talked very clearly about the adequacy issue. You address the adequacy issue by giving people equity market returns. There is no other place to invest in this environment and I would suggest to you for the foreseeable future that we will offer the retail investor the upside that the equity markets will. Many of these people would like to have tax deferral. Tax deferral is a very useful thing. It is not as important to the guy that has got a net worth of $232,000, but as you move up the food chain the tax deferral benefit is material.

These are the sort of things they may be thinking about. You can read this. I do not have to go with the punchline. Only our product has the prospect of filling every need. It is a unique product proposition. It allows the customer to decumulate, to take a guaranteed lifetime income. It cannot go down but it could go up based upon the performance of his portfolio within the product which if he gets it right he finds himself in the position where he is accumulating faster than he is decumulating comes out at the end of every year having – after having taken his income, he has got more than he started with.

That is the ideal scenario. It does not always work that way. You might not pick the right stock or so forth but we do give enormous amounts of freedom to consumers, 91 different funds from which they can choose, some of which would be very familiar to some of you, some of which have your brand name on some of those funds. By giving them that flexibility it creates a very strong story for that retail investor.

Performance

Performance. Which is really like the second part of product. We have shown you things similar to this before. You see the number of living benefit funds. What that refers to is if you buy our variable annuity product with an income guarantee or a withdrawal guarantee I should say, these are the number of funds that you have to choose from around which we will wrap that guarantee, that protection. We offer 91 funds. Now, you noticed it drops off dramatically after that. That is because every other competitor in the marketplace today, if you buy the guarantee, it forces you to choose from vol control funds which consistently underperform the market.

It is an interesting statistic, so if you look at the 91 funds we offer, 21 of those funds over the last three years have offered return of 7% or greater over the three-year period, 7% per year over three years, 21 of the funds, about a quarter. Because they are being forced into vol control funds with other competitors' products, none of the other competitors have a single fund that has performed at that level. If you assume for a moment you are taking a 5% withdrawal every year as your level of income and you are getting a 7% return, then that creates that ideal scenario. In 25% of the cases roughly, 20% of the cases that you can conceive with the Jackson product, you achieve that ideal scenario of continued accumulation with a lifetime income. None of the competitors are offering that because they are forcing people into vol control funds.

My view, I will answer your question, is that this candidly ought to attract regularly attention because the very premise of the product is accumulation and income. When someone says, 'Okay, I want that product,' then you say, 'Great, we have got that. Here is your income,' the accumulation just went away. I do not see how that could possibly be best advice.

If you need a VA product, it must be a VA product with investment freedom and we have talked to a number of distributors and Seth has been kind enough to join us at some of these meetings with some of our major distributors, the Raymond James, the Merrill Lynches and so forth, LPL, etc., all across the country and talking at a very senior level and talking about the issues around DOL and the state of the market and so forth. What many of them are saying is that they will struggle having on their platform accessible to their advisers variable annuity products they do not offer investment freedom. My hope is you will actually see more competitors coming back and offering investment freedom. I think that is good for consumers and that is good for the marketplace. That is healthy for the marketplace and that is our hope.

Service

Now finally, let us spend just a moment talking about service. We have gone through this. We genuinely do have a real operational advantage, a real competitive advantage in the marketplace by virtue of the technology and service platform that has been built in Lansing, Michigan, which is truly extraordinary. To my knowledge, we are the only life insurance company operating in the United States on a single administrative platform.

I have talked to some of my peers at other companies who have been bemoaning the fact that they have 14 operating platforms. They have consolidated different companies over the years that just never dealt with the IT dimension of the integration. Jackson has always been very disciplined when we have done a couple of bolt-ons, as you will recall, every time within a year that is on the Jackson platform. That is one of the reasons we were able to operate from a cost perspective at half the industry average and a third of that of some of our principal competitors. It is incredibly flexible and efficient for advisers as well. It is easy to deliver service through an adviser or through our customer service people. All of that capability remains in place and it is useful.

I get a report every month that shows customer satisfaction. For October, 99.79% customer satisfaction. Of the people that interacted with us that month, 99.79% said they had a positive interaction with Jackson. We can always do a little better. We have 21 basis point in there we are working on but it is a pretty good outcome.

The important point on this slide is the last one. We are only selling really through a universe of 100,000 reps and about half of those are selling our product and there is 300,000 people who are fee-based RIAs, whatever, who do not currently sell our product. And I talked about compensation as an obstacle. One of the other obstacles there is that many of those advisers are accustomed to doing their business, managing all of their client's interest on a single wealth management platform and they only sell the products and the services that can be sold directly through that platform.

It simplifies their life. It is point, click. They can sell, do service through that integrated platform. If you are not on that platform, you are not going to sell much. Now, there are organisations who do sell for us, wire houses, who operate off these wealth platforms as an example. They do sell for us but it is a very cumbersome process because they are talking to their customer and they got everything on the screens like, 'Oh, now we are going to about lifetime income and we shut this down. Let me go to the different website. Let me log in.

Let me find what I need.' It just makes it a more cumbersome process and it should be obvious that it is a deterrent to sales.

We have been working out for almost a year on what we call the plumbing to integrate our products in to the wealth management platforms in North America where the vast majority of the assets get managed. That will facilitate the rise of our prospective advisory product in terms of volumes. That will make it very easy to access that product because you could now sell that product very easily on that wealth platform on a fee basis. You can service your client then on that platform – that Jackson product, on that platform. You can even go in if things are happening in the market and you say, 'We are going to move out of fund x, y, z into fund ABC,' and he has got exposure to that fund through some money that is just sitting directly in the fund and he has also got that fund within a Jackson annuity. You can quickly go in and make both trades. It is much simpler process than what they have to go through today. This is an extremely important point.

Scaling the Opportunity for our Industry, and for Jackson

Now we talked just a few moments ago, tried to scale the opportunity, tried to measure the opportunity by talking about the number of advisers who are out there that do not sell the product. Let us look at it a little differently by assets. Here are the various different distribution sources that we currently work today and here are the assets that we generate from those.

You can see independent broker dealer – we have always talked about this. The independent broker dealer is the most significant exposure we have but we get a lot of business from banks. We get a lot of business from the hybrids, the guys who worked some cases on a commission basis but in other cases on a fee basis. We get very little from the IRAs because they are normally pretty disciplined about commissions. They do not like commissions. They do not like to write products that entail commissions. There are a big broker dealers, like the LPLs is an example within we do a fair amount of business, and the wire houses, the Merrill Lynches and so forth. It is complicated for them as I just described to do business with us but they do.

Adviser distributed assets

Now let us look at it not in terms of the level of assets that these different distribution channels give to us but rather the assets that they actually manage. If you look where we have always concentrated, independent broker dealer, we have probably got 20% share there. That is probably about where it should be. That is probably all in, it is probably about the percentage of assets for their entire client base that they should be giving to Jackson to fund a retirement income and then they invest in other things as well.

We have done a really good job with the independent broker dealers but we have faced obstacles everywhere else that principally relate, as I said before, to the way the product is – you get paid for selling the product and what you have to do logistically to manage the transaction. We now have a fee-based product. We are doing the work on plumbing so we will be integrated, not this month, not this quarter, but over time we will become more deeply and deeply integrated onto these wealth platforms and that is going to make an enormous difference.

There is $16 trillion of assets sitting out there. There is $24 trillion of assets sitting in qualified accounts right now. IRAs, principally 401(k)s. There are some overlaps. Some of that IRA money will obviously already be, you know, on these platforms through these channels. Think about it. 16 trillion sitting there now over 20 trillion moving towards these channels as these people move towards retirement.

Flight to quality

The scale of this opportunity is gigantic and if you believe, which I believe, that it will be about a flight to quality, it will be about embracing higher standards, it will not be about rescinding the DOL rule, it will be about modifying it to make it work more efficiently and more effectively for consumers. Seth says, one of the things that surprise – even Elizabeth Warren is now fussing at the Labor department saying 'We published this new rule and annuity sales are going down. What is wrong with you people? It is supposed to go up' because they are, you know, they did not realise that this whole, you know, class action suit might be annoying to some distributors. You know, they missed a very important point there.

If you accept that regulation will be more consumer-centric, will focus the industry on quality and if you accept that there is a real desire to drive the sale of more lifetime income products and that that is going to be pushed in a bipartisan fashion by political and regulatory leadership in the United States and then you look at this, you have to believe this is an extraordinary story.

I am absolutely convinced that this is one of the greatest commercial opportunities that this Group has faced and we have the advantage of being perfectly positioned, highly competent, a strong track record of capability to take advantage of this from a shareholder perspective but, to speak less commercially, to actually solve a gigantic problem in American society where our skills are uniquely suited to do so. Which I think is an incredibly positive situation to be in.

We want to spend a little bit of time now getting a little more granular on DOL. We want to demonstrate to you how we think this impacts us and importantly demonstrate to you the high level of preparedness we have for the rule as it exists today. There is the prospect that the rule may not be implemented when we think it will be in April and then with full implementation in January of next year. There certainly is the prospect in a Trump Administration, which is fundamentally sceptical of regulation, that there is scope for the rule to change and that there are things about it that should change. In any event, it should be important to you and it is important for us that you understand that we are fully prepared to deal with it.

I am going to ask Drew Bowden who is our Senior Vice President General Counsel of Jackson and then Alison is going to come up as well and Alison is the Executive Vice President in charge of operations for Jackson National Life Distributor.

DOL Industry-Wide Implications

Drew Bowden

Senior Vice President, General Counsel, Jackson

Introduction

Good morning. My name is Drew Bowden. I am the General Counsel of Jackson's operations in North America. I have been with Jackson for a year and a half. Prior to that I ran the examination programme at the United States Securities and Exchange Commission for three and a half years before that I was in the industry. What Alison and I want to do with you today is really try to answer a couple questions that you had asked in advance about the DOL. Talk a little bit more specifically about what did the DOL do and its rules? We will get through that. Two, talk about what impact do we think that the DOL rules will have on the industry at large, sort of, across the entire industry. Then I am going to turn it over to Alison and Alison is going to share with you what we have been seeing from our distribution partners from a Jackson perspective and the preparations that we have been making at Jackson in order to be ready for the rules when they do go in to implementations. Does that sound okay? I know we are coming up on our time so we will move quickly.

Department of Labor (DOL) Fiduciary Rules

I am going to start first with what did the DOL do. Seth gave you some of the, sort of, the philosophical, theoretical policy imperatives that were behind the rule. I want to get down to a little bit more just brass tacks and talk to you about what the rules did. The first is I sometimes hear people's misnomer. People call it the DOL rule – it actually was a package of rules. It was new rules and rule amendments that total – well more than a thousand pages. What you have in front of you in the following four bullet points might be the shortest executive summary of the DOL rules in the history of man and I am going to try to get to them quickly for you. These are the key takeaways that I think if you want to really want to understand the rule and the levers that it is pulling that you have to know.

Expanded the definition of fiduciary

The DOL expanded the definition of fiduciary so the DOL has jurisdiction over what are called qualified assets so, retirement assets, pension funds, 401(k), IRA. Think of it as money that individuals have set aside for their retirement in a tax advantaged account. It is advantaged by the government.

If you and I ran a distribution firm, if we were in the business of advising retail investors, depending on what firm we are in somewhere between 50% to 70% of the total assets in our firm would be qualified assets. The DOL in theory – potentially their rules could impact between half to 70% of your business. The first thing is the DOL rules only impact – the only come into play over that part of your business – if you are deemed to be a fiduciary as the DOL describes that term.

With these new rules the DOL substantially expanded the definition of fiduciary. It used to be under the old rules – the DOL had a five-part test that had been in place since 1975. It used to be that in order to be a fiduciary you had to, among other things, give regular advice and there had to be a mutual understanding or agreement that your advice was going to form the primary basis for the decisions made by the investor.

There was this concept in the old DOL rules of what I would call a distinction between, sort of, a sales person and a fiduciary. A sales person – episodic one time. I come to you, I offer you something, you either buy it or you do not and I go away. I could engage in that type of a relationship with you without being a fiduciary in that part of my book and therefore not covered by the DOL rules. With the new change, what the DOL did is they expanded the definition of fiduciary to literally include any communication that a reasonable person might consider to be a suggestion that a person act or refrain from acting in a particular way.

My shorthand for that in the interest of time is the DOL rewrote the rule. Now if you smile at someone who has retirement assets, you are a fiduciary and there is no getting out of it. That is 50%-70% of your book. You are now subject to the DOL rules where maybe potentially you might have been some of that before but now it is all of it.

Adopted a new PTE

The second thing you do is you have to understand how the DOL rules work. Right? Under the DOL rules once you become a fiduciary you are prohibited from using that investor's assets in a way that benefit you or any of your affiliates. It is prohibited. That is the starting point so commissions is a perfect one. If I am a fiduciary and I am in a situation where I can sell you a mutual fund or get paid A or another product and get paid A times two, I am conflicted. I am a fiduciary. That is prohibited under ERISA. The only way you get out of it is, I use the short end up here, adopted a new PTE. That is a prohibited transaction exemption. There are about 57, I think by last count, prohibited transaction exemptions.

If you engage and you want to use client assets in a way that will benefit you through variable compensation, I have a conflict, will benefit your affiliates, I am going to sell you a product that one of my affiliates manufactures or manages or sells, then if you want to do that lawfully you have got to do it under a prohibited transaction exemption. The DOL passed a new one that you have seen called the BICE. That is intended probably will be the most heavily used by all the people who are now fiduciaries where they were not before and came under the rule.

In the interest of time I will not go through all of the ramifications but the BICE has fiduciary standards written into it, hardwired, I would argue elevated fiduciary standards above anything that existed in the business and those applied to everyone who is a fiduciary, whether you work on a fee basis or whether you work on a commission basis.

The second part of the BICE is if you get paid variable compensation, if you get paid commissions or if you get paid variable comp by product manufacturers – so, mutual fund A pays you X to distribute its product and mutual fund B pays X minus two, variable comp in any way then you have to also sign the contract that Seth referenced to and you have to enter into a contract to your client with agreements, warranties, disclosures and certain other provisions in it. The BICE is a pretty significant lift in order to comply with the prohibited transaction exemption.

Removed fixed index

The third thing that the DOL did and the third big takeaway is they removed fixed index and variable annuities from a pre-existing prohibited transaction. That was 8424 so, the easiest way to think of this is if you were a fiduciary under the old rules – right, a big if could you operate it in a way to not be a fiduciary because you did not want to deal with those rules. If you were a fiduciary under the old rules and you sold an insurance product, you did it under prohibited transaction 8424. Prohibited transaction 8424 is much less burdensome than the BICE. Think of the lift to get through the BICE is here, 8424 the standard in selling an insurance product was basically the deal that you struck had to be as good as the deal you could strike on an arm's length basis, and the comp had to be reasonable and there were certain other disclosures. BICE significant lift 8424 not perceived to be as significant a lift.

When the rules were proposed by the DOL in 2015 they proposed to take variable annuities out of 8424 and put them into the BICE. To leave fixed annuities and fixed index annuities in 8424 which would have created an uneven playing field. Variable annuities would have had to comply with the BICE fixed and fixed index, a lesser standard. When the rules came out in 2016 to the surprise of many people, the DOL removed not only variable annuities but also fixed index annuities from 8424. Much less burden.

Introduced new private right of action and enabled enforcement through class action litigation

The last thing on the rule that I would say is significant that Seth mentioned is from a former regulator's perspective – an interesting piece of regulation where the rules were written – again not with the expectation that they would be enforced by the DOL or the IRS or any other regulatory authority. The rules were literally written with the idea that they would be enforced in courts by litigants. People selling products would get sued by their clients to enforce the rules so significant impact there. Those are the four big takeaways from the DOL rules that I think are driving some of the things we are seeing.

DOL Industry-Wide Implications

Let us pretend we had all gone back in time and we just read the thousand pages of the DOL rules and had a conversation to say okay, how do this even plays out? How does it affect the industry? What happens from here? These are some of the things we came up with.

Product

First on the product side the new rules discourage commission-based products and encourage fee-based products. Remember under the BICE, everybody has to meet the impartial conduct standards. If you get differential commissions, you have to do a contract and do a whole bunch of other stuff. This is nothing new from a regulatory perspective. The industry has been moving the fee-based business for years. When I was with the SEC we did a paper for the chair of the SEC and we called it the migration to fee-based. I think these rules just accelerate that migration.

The next two on product really go together. It says the distributors want to reduce product conflicts and menus. I will start with menus. Again, if we ran a firm I think many people who were in the business of advising retail investors thought of their client as their advisers. If we had a firm – I will pick a number. We had 10,000 advisers typically our product menu, not exclusively but in large part, was my advisers want to sell this so I put it on the platform. They want to sell this; they put it on the platform. You get a proliferation of funds and insurance products and other types of securities that your advisers are selling because that is what they want to sell.

Well now, under these new rules, you are a fiduciary. Somebody had mentioned what if a product goes wrong. You are potentially at least on the hook so the natural inclination is going to say – all right, I am going to narrow the field of products that I offer to ones that I could do diligence on and feel really good about. The second thing you want to do is you want to reduce product conflicts so, under those rules any type of differential compensation puts you at risk. Once you have said I will use mutual funds for the time being because there is so many of them. Once you have said okay, I am going to narrow my menu of funds I offer, now the game becomes I want to get paid the same thing by every mutual fund company. I do not want to be conflicted to choose one fund over another. I want it to be level. These two really go together from a product standpoint – from a Jackson perspective as your clients are now going to want to do business with potentially fewer manufacturers. And when they do choose their manufacturers, they are going to want their product to look similar. For us from product perspective it used to be when you launched a new product you had features, you had options, you put it out on the market and people sold it; we are moving into a phase where you were going to see a little bit more white labelling. Where your partners are going to say 'I would like to only offer the following options'. 'I would only like to offer the following compensation scheme at my firm.' So, that happens.

Our projection is we will see increased lead time and filings so people are going to come up with new products. They are going to come up with customised products. Not a huge deal but I do think in some of the state insurance departments, they are going to see more flow of product that they are going to have to review and approve than they have in the past, so potentially longer lead time.

Distribution

Next on distribution, distributors must decide whether to offer to commission-based products under the BICE. Again, simply put again, if we went back in time and we ran our firm and these rules came out, I think looking at that 50% to 70% of our business that was qualified and therefore now under the DOL rules, you could arguably say one of three things.

One, I do not want to advise any qualified assets. I want to get out of that business entirely because it is too high risk for me. I am just not going to advice people on their retirement assets. A second would be: I am going to advise people on their retirement assets, I am willing to do it but I want to do it on a fee basis, not on a commission basis, because fee basis is less burdensome potentially and potentially lower risk. The third is, I am just going to use the BICE and I am going to continue to sell products on a commission basis and operate from there, maybe changing the mix overtime. Alison will sort of pick-up with you what we have actually seen out of our distribution partners on that.

Data infrastructure and delivery, Barry talked some about plumbing. I will not go on about this one too much, but I think it is probably one of the underestimated parts of the DOL rules. With the BICE and the contract, they are extensive disclosure obligations that distributors have to meet with their clients, so they are now obliged to deliver information in a systematic, periodic and accurate way to their clients, in particular for us, about variable annuities.

There was no central clearing house or standard industry format to capture data about fees and expenses and features in variable annuities previously. As a result of this rule, people had to come together and for the first time we do have an industry standard. I think it has 700 data elements in it to capture all of the basics of the various variable annuity products, which is, again, laying the ground work and paving the way, I think, for the plumbing to be built for greater utilisation of the product.

Mix of business, with FIA's, this may be a little bit too arcane for now. I will try to do this in 30 seconds. Unless, so under US Securities law we mentioned insurance products, generally fixed annuities, fixed index and VAs. Under US Securities laws, only variable annuities were securities. If you sold variable annuity, you are subject to regulation by the DOL, by the Securities and Exchange Commission and FINRA. Fixed annuities and fixed index annuities were not securities products. They are just insurance contracts.

Going back in the past, you or I could have had a business where we sold fixed annuities or fixed index annuities and we did not have to be affiliated with the broker dealer. We decided to be an insurance agent. Under the rules, what the DOL said is if you are selling fixed index annuities you have to be affiliated or be designated as a financial institution which is a broker dealer, an insurance company or a bank.

Those people who have been in the business of selling exclusively or predominantly fixed index annuities now have to figure out how they are going to associate or be designated as a financial institution so that they can comply with the rule. Alison will explain to you how that is important as well.

Legal & Regulatory

Legal and regulatory, I will not go much into that. I will turn it over to Alison. Short-term uncertainty, the interesting thing to me about the rules is when they came out being the General Counsel at Jackson, the question I often got, people would come and say, 'What can we do under the new rules? How do they work? What can we do and what can we not do?'

One of the most interesting things about these rules, they do not prohibit anything. Seth made this point. You can do anything. You can sell any product. You can arguably have any comp scheme that you want to have. Do what you want, it will be decided after the fact in courts whether or not you have acted in the client's best interest, your compensation is reasonable, you have any structural conflicts in your interest. Nothing black and white.

From a legal and regulatory perspective in the short to medium term, it has created a lot of uncertainty about what you can and cannot do in this business. Another point on that, I would put this, the DOL issue, sort of its first full set of frequently asked questions under the new rules which were designed to sort of clarify and clear up any misperceptions or misunderstandings that people had about it a couple of weeks ago, and they came out, and I think they may have sowed as much confusion as they cleared up. People got it and said to themselves, including me, well, I did not think that is what the rule said.

There has a lot to be sorted out in those. Increased liability, the new rules increased regulatory risk, the important point there is it is for distributors. The rules directly apply to distributors of the product, not manufacturers. With that, I am going to turn it over to Alison.

Jackson's DOL Preparedness

Alison Reed

VP for Product and Investment Management, Jackson

Introduction

I am going to spend the next few minutes covering two topics. The first being our broker dealer partners' assessment of the DOL rule. Secondly, Jackson's DOL preparedness.

Broker dealer assessment of DOL rule

First I will start with the broker dealer assessment. As you saw from Barry's slides, Jackson has extensive relationships with the top broker dealers in the US, and it is these broker dealers that are directly impacted by the DOL rule. Since the rule has been released, Jackson's had on-going conversations with our broker dealer partners, specifically related to their assessment of the rule.

I am going to share with you four trends, key trends, that are emerging from these conversations. These include their intention to comply with BICE; their definition of reasonable compensation; their intention to limit their product menus and the applicability of BICE to non-qualified accounts.

Intention to comply with BICE

Let me start with intention to comply with BICE. You have heard that broker dealers and our distribution partners, they do have several choices under the DOL fiduciary rule. They can comply with BICE and continue to offer commissionable-based product. They can move away from commissionable-based sales and go to a fee-only platform for their qualified business, or they can preserve choice and do a combination of both.

What we are finding is that 17 of our top-20 firms based on 2015's sales will comply with BICE under the DOL rule. Only two firms have said they will not comply with BICE and they will move over to a fee-only platform for their qualified business. This is a positive trend for Jackson because of the 17 firms Jackson has historically been predominantly a commission-based product manufacturer.

It is also important to note of those 17 firms that they do intend to offer fee-based product, preserved choice, so give their advisers the choice to offer commissionable or fee-based products to their clients.

Reasonable compensation

Next I want to talk about reasonable compensation. Under BICE, broker dealers will need to standardise compensation by product type. This is an area where broker dealers have been a little slower to comment. That said, seven of our top 20 firms have indicated that they will reduce upfront compensation in the range of 5% to 6% upfront with a trail commission ranging from 25 to 50 basis points. Only two broker dealers thus far have indicated that commissions will come in lower than 5%.

Another important takeaway, as you see, no green in this table. Green is the highest upfront only commission. Broker dealer partners have indicated to us that they are going to move away from that high all upfront compensation. Again, Jackson views this as a positive. It is a positive because commissions are coming down less significantly than we originally anticipated with the release of the rule.

Limitation on product menu

The third thing I want to cover is limitation on product menu. You have heard this a couple of times. Eighteen of our top 20 broker dealers have indicated that they will likely or will limit product menus. In fact, one of our top wire house firms have indicated that they will limit their product menu to four carriers effective in January, Jackson being one of those VA carriers. Again, we feel that Jackson is going to find their way on these limited product menus because of the strong consumer value that our products offer to their clients; one being the customisable product offering, the ability for the rep and the client to pick and choose the features and benefits and pay for only that corresponding charge.

Also, no investment restrictions associated with a living benefit guarantee and superior performance. That superior performance will result in greater accumulation in the likelihood for increased guaranteed retirement income for the consumer.

BICE to non-qualified

Then finally, I want to touch on BICE to non-qualified. Clearly, the DOL rule addresses qualified accounts and IRA accounts. But based on our conversations with broker dealers, at least half of the firm so far have indicated that they are going to apply BICE standards to their non-qualified business.

When I say BICE standards that means limiting the product menus and applying their definition of reasonable compensation to their non-qualified accounts. They will not require their clients to sign the best-interest contract for non-qualified sales. They are doing this primarily for consistency purposes, consistency at the firm level in terms of similar policies and procedures to be monitored at the firm and then also consistency at the client level in terms of the products being offered for both account types as well as how they are getting paid for both types of accounts.

Jackson's DOL Preparedness

Next I want to talk about Jackson's DOL preparedness. Since the release of the proposal in 2015, Jackson's established a formal governance structure related to the assessment of the DOL rule and its impact to Jackson. As Drew mentioned, we have broadly categorised this into three main areas including product, distribution, and legal and regulatory.

Product

Let me start with product. Again, fiduciary changes. At the product level, again, broker dealers have a choice and we do feel like and we know that most broker dealers will comply with BICE initially. However, because of the additional requirements, as well as the liability associated under BICE, we do feel like there will be a trend or a movement towards fee-based accounts.

Now, Jackson launched its first fee-based variable annuity perspective advisory in September of this year. This is our first entry into the fee-based VA space. When we enter this space, we introduced a unique product structure as compared to what is currently offered in the marketplace today. That structure offers a short, modest or undercharged schedule.

What this does is it reduces the overall fee to the client, reducing fee drag overtime and getting more opportunity for accumulation and step up to increase that guaranteed retirement income.

Jackson will also launch its first fee-based IOVA, investment-only VA, in January of next year.

In terms of product standardisation, broker dealers under BICE will need to eliminate any share class conflict. In terms of that, Jackson was one of the first product manufacturers to voluntarily close its standalone L-share contract and we did in July of this year. At the same time, we introduced a bundled share class, and what this share class does is it effectively eliminates share class conflict for our distribution partners.

In terms of distributor-driven customisation, as I mentioned, the definition of the reasonable compensation, a lot of our distribution partners are going to standardise the commission by product type. In July of this year, we also launched a streamline process to more quickly implement those commission changes on behalf of our broker dealer firms. In terms of lead time, we do think lead time for product filings will extend and Jackson has an experienced and dedicated product implementation team that has reduced the product launched cycle as compared to our peers.

Distribution

We move on to distribution, again, we are going to see fiduciary changes, and that is the majority of the distributors we feel overtime will shift over to fee-based products. Fee-based variable annuities are not new to the industry. However, historically, they have been fairly unsuccessful, with over the last five years representing about a 5% market share in the industry. Now, we feel like Jackson will have a competitive advantage in this space because of our effective and largest wholesaling team. We also have the strong relationships with our existing partners and those large pools of assets. Then we have product launch experience specifically with the success of a lead access.

In terms of data infrastructure and delivery, again, as Drew mentioned, under the BICE agreement, there is significant transactional disclosure that our broker dealer distribution partners are going to have to comply with. At Jackson we took a leadership role in designing and implementing these standardised data feeds so broker dealers can consume that information and comply with the disclosure requirements.

In terms of mix of business, 2016, it is likely going to be another record year for FIA sales. Jackson feels like we are going to be the benefactor of FIA sales being on a level playing field with VA sales. This will be because FIAs are going to be subject to standardised products, the definition of reasonable compensation as well as reduced compensation from an incentive basis. The other impact to FIA, as Drew mentioned, is the impact on independent agents. Independent agents will have to affiliate with a financial institution to sign that BICE contract.

Independent agents have historically sold about 60% of the FIA business and Jackson is subject to this. However, it has an immaterial impact on Jackson's business because last year only 0.5% of our overall annuity sales were sold through independent agents.

Legal & regulatory

Finally, legal and regulatory. Jackson spent significant resources from an internal legal perspective. We have also participated actively in industry trade groups as well as worked with some of the most experienced outside counsel, and that assessment has resulted in that the DOL rule directly impacts our broker dealer partners, not the product manufacturer. In fact, our assessment has concluded that the class action risk that has been talked about with the best-interest contract is borne by the distributors, not the product manufacturers.

With that, I am going to turn it back to Barry. He is going to close out the morning session.

Summary

Barry Stowe

Chairman & CEO, North America, Prudential plc

Just before we got to lunch, what we have tried to do this morning, and we will continue to do it after lunch a bit more as well, is to remind you of what I think you already know about Jackson, which is we are the leading manufacturer of prudently-priced, consumer-centric retirement solutions, best-in-class here that Alison referred to, best-in-class, most professional, most productive, most efficient face to the advisory marketplace. The scalable, efficient operations I have already alluded to, the low expense ratios that those drive, strong risk management. This afternoon, right after lunch, we will come back and chat. We will take you through the finance deck, dealing about risk management, the economics of the business as we see here today which I think will be encouraging to you. All of this activity is driven by what I consider to be best-in-class senior management team. It is a very, very strong proposition, a terrific enterprise in an extraordinarily positive space right now to deal with the changes coming in. On that positive note, I will release you to lunch. Enjoy your lunch.

US Financials

Chad Myers

Executive Vice President & Chief Financial Officer, Jackson

Introduction

Good afternoon welcome back to the rest of the Jackson presentation. What we hope to accomplish over the next six or seven hours here is a complete and total understanding by everybody of the VA business. No, anyway so general topics for today. I am going to talk about net flows, market position and general update of the health of the VA in-force book as we typically do in these venues. We will get on to the assumption review. We just finished that up in our 2016 process. So I will give you a bit insight into that, and it seems like there have been a few questions about the NAIC Review of Variable Annuity Framework and so we will spend a little time on that as well.

Annuity Industry Trends

So starting by jumping right into kind of where we are in the market. So we have heard some of this before, but just to put some numbers in front of it.

We are obviously in a very challenged environment in the US right now with the regulatory environment being what it is, and we have seen something come out that we have not seen in a couple of decades, which is that fixed and indexed annuity market is now larger than the variable annuity market, which has happened just over the last year or so. A big part of that came in the form of the DOL regulations that were coming through and there was the expectation that the indexed annuity products would be exempted. And so what you saw was folks saying here is a low regulatory risk product that I can earn a big commission on, sort of gets me market participation. And frankly in the market that we participate in right now. Barry was talking about the vol control funds and just how poorly they generally perform, there is not as much daylight between an indexed annuity and a vol control fund as there is between our variable annuity and an indexed fund. So that has really fuelled a lot of the growth that we have seen there, and obviously variable has fallen off at the same time.

What we have seen though is since the rule came out, and we had clarification and indexed annuities got pulled back into or got kicked out of 84/24, is stabilisation there. And I think the index annuity market is going to be much more challenged coming into next April than it has been so obviously we have seen an inflection point there. And the market now pauses and thinks about what kind of risk it is taking by selling these indexed annuity products as well.

And so where we sit right now is still a lot of people sitting on their hands, still a lot of broker-dealers that are making decisions about what reasonable comp is and we saw Alison's slides. There is been a lot of decisions made there are still more to be made and even though those have been made in many cases, they have not been communicated out to the reps as it is more with the carriers that they have been having these conversations. So we should get more clarity in the upcoming months and that will hopefully start to get these lines back in the more historical proper context, but clearly a big headwind that we have had.

Another one that is also not terribly clear necessarily is if you look at the captive share of variable annuity sales in the US, they have moved up quite a bit and then if you think about the fact that in a captive distribution force you have much more control over the distributor. So if the end the rep is a little queasy about selling variable annuities and you want them to sell your variable annuity there is obviously more say market power there, if you will, to get that through.

So this also is not a trend that's particularly helpful to us because we do not sell in the captive channels. So what you have seen is a pretty big headwind for us. Overall, we are slightly better than the variable annuity industry, which if you think about the fact that we have gained the market share over this period, and we will definitely continue to see some benefits from the consolidation of distributors that we see coming out of the whole BICE DOL reg. It is again a good performance and a bad market. I do not think you can get a better picture than the one on the right. Here we are talking about the overall total growth of us versus the industry.

I will get more the net flows in a few minutes, but our positive performance is really a function of a couple of things. It is good net flows, which is again fairly unique in the industry at the moment as well as good performance because we have not put everybody into these constrained balanced portfolios or vol controlled funds. We actually have seen the performance come through and so what you have seen is good growth and AUM for us versus an industry that is going backwards.

Consistent Variable Annuity Volumes

This is a slightly different look than if you look at the general top line of VM. I think we have had this one up here before in a slightly different context. Historically, where we have shown this is we are controlling the risky, also known as really high margin portion of our business, and this has really been a range when we have been dealing with the sales cap and managing the risk of the overall book. This is really the range we have been at over the last several year so, despite the turmoil we have in the market, what you do see is that we are really just kind of in the low end of the range that we have been for quite a while when you look at specifically living benefit type VA sales, which clearly are going to be more of the focus as you have heard so far today of sales going forward.

If you are sitting down doing the financial plan, the investment only VA, the Elite Access type of product, is not necessarily favoured in that conversation because really all you are selling is tax deferral. What you see is that income guarantees, the fact that this part of the market has held up pretty well for us is actually quite encouraging.

Strong Variable Annuity Net Inflows

If you look at overall net inflows, so again the grey bars are the sales, so sales are in the low end of the range that we have had over the last several years. And the red bar is the annuity surrenders that have come through, and you can see those have been building as the blocks were building, which makes sense.

When we talked about coming into DOL, when there was much less certainty, we had a lot more ability to absorb bad news than most of our competitors do. And we have been able to withstand a relatively significant shock in the market, thinking back to that prior slide, yet we are still generating positive net flows. Through nine months, a little over $5 billion of positive net flows against an industry – we have only had data through Q2. That was $15 billion as a whole. So, you know, a very stark performance difference between us and the rest of the industry.

Separate Account Growth

So I think one of the things we are seeing now it is a little bit of a nuance relative to prior years, it has been a lot more of a net flow story coming out of the crisis. We started with a small book and most of the growth that we are seeing out of Jackson is coming out of the net flow side. The market performance on a small block just was not enough to be that impactful. What you are seeing is obviously we have lower net flows this year just due to the issues in the market. But with the size of the book now at $145 billion, even if we were to go back to the heyday of $12-13 billion of net flows, you are really talking about a situation where 9% or 10% move up in the market is every bit as important as you would see record net flows.

So you are coming into more of a balance where modest market growth coupled with modest net flows, even if we could not find a way to grow from here you still have a pretty good growth trajectory on the business with reasonable markets underpinning it. So really just to point out the net flows are not as important as they used to be. They still are important. We still want to grow the business and fulfil those consumer needs that are out there, but it is becoming much more of an AUM story than the net growth or net flow story.

Economic Backdrop

There is a little refresher over the last several years, so clearly we have been in a pretty strong bull market from 2011 to 2014, flattish since 2014 in terms of the S&P 500.

Ten-year treasuries have been in a broad trading range but obviously also on a pretty severe downtrend for the last two years since oil reversed and all it takes is one good election to overcome what quantitative easing could not do. And then on the right-hand side, I will get back to this a little bit later, but just to introduce the topic because this does bear on some of the accounting.

This is the 30-year treasury rate versus 30-year swap rate and what we have seen is a severe dislocation. There were 30 swaps trading about 55 to as much 60 basis points under treasuries, which is not an economically supportable theory or would not be supported by economic theory. But nonetheless that is where we are; a lot of that is Dodd-Frank and Basel type regulation that is driving things, but just thinking about the context of, over this period of time we obviously had a lot of accounting volatility. And so I just wanted to go back to a couple of slides, which will be familiar to many in the room. But just to kind of take a lot of the accounting volatility we have seen in the various equity and rate markets and just boil it back down to cash flows, which is the way we tend to look at it.

Economic Value of VA Book Has Improved Over Time

So there is a whole bunch of these coming up so I am going to pause for a minute and just walk you through what we are looking at here.

So this is the guaranteed book only. This is not the core contract. There are no M&E fees in here. This is just the benefits we expect to pay out on the withdrawal benefits and the fees that we collect from the policyholder on those. This is just a prospective look so what you see is again setting the top guarantees fees only using our statutory prudent best estimates so it is the best estimate with the margin type of assumptions for all the policyholder behaviour. The assumption within this, just to keep it simple, is a static model of 5% gross returns, that is before any fees are taken out. We are not taking account of any of the fees that have been collected to date. We are not taking account of any reserves that are currently set up for these benefits.

So we are looking at here is the grey bars are the fees we collect, the red bars would be the benefits we are going to pay overtime. This goes back at 2011 so it is going to have to kind of roll forward. And you see going back 2011 PV of fees are $3 billion. PV of benefits $0.5 billion so, a good economic position to be in back in 2011 if you think about the fact that a fairly good portion of this block was written pre-crisis. I think it is overall a pretty strong story.

So now we start rolling forward. If you bring 2012 into there so what happened in 2012? We had a 14% positive return in the separate account. Rates went down a little bit. We had strong sales GMWB sales, and again what you saw which is probably fairly sensible. Fees went up. Benefits went down because the market was up a fair bit and the net PV moved up. Again the accounting would not necessarily be reflective of this, depending which accounting metric you are looking at, but this is underlying cash flows.

Roll forward to 2013, you see again very good year in equity markets 20% separate account return. Rates were up. Sales were off a little bit from the prior years. We are starting manage sales down at this point in time. And what you saw was again good progression there. Fees up, benefits basically flat because it was there was some point at which they kind of floored out. You think about when you get out to the tails there, and that is mostly longevity-type of risk that is there, not so much market risk, and really no increase in the benefit so therefore again net PV continues to climb.

If you roll through to 2014, modest return in the equity markets. Rates dropped, again $15 billion in sales we saw. We continue to see the grey bars build, not that much build in the red bars. NPV continues to climb so, again, a good story there.

2015, we saw basically a slight negative return in the equity markets. This is all pre-fees so if you think about the average contract it is going to have 3-3.5% and fees on it. So an effective return after that of closer to negative 4-5%.

What you see now is fees continue to go up because we are putting new business on the books. And as you also have lower equity returns, people start to go on the money. Persistency goes up so we have more people sticking around, which means two things. It means more benefits, but it also means more fees in the meantime. This year we start to see benefits climb a little bit, but you see still the net PV or the cash flows continue to be positive. And then rolling forward to 30 September 2016 we saw a reasonably good performance through nine months although that 7.2% does not tell a whole lot of the story given what we have seen so far this year, a couple of mini bear markets and Brexit, and the election does not get captured.

What you saw then was again a good progression in terms of the profitable business coming on, continued build in the NPV and we find ourselves in a position now where again the guarantee book, as we have seen all along, has been very healthy, a lot of cash out there to support with any benefits we are going to have in the meantime. I think I did neglect to say at the beginning there is no hedging in this. This is just if we assume no hedging we just have cash, cash in cash out.

GMWB Cash Flow Stress Scenarios

Now if I move forward to the stressed scenarios that we look at as well. So you will see the upper left hand corner would be the same graph in the prior chart. Again very strong position there if you think about there is a lot of noise in the IFRS below the line, first half which is rate-driven. I will get on to a little bit more than that in a few minutes, but realistically you think about what happens to rates, the cash flow, bottom left-hand corner, is a 100-basis-point rate shock down. But does not really change underlying cash flows, it just changes the discounting of those cash flows because, again, this is a steady 5% gross return. So irrespective of the accounting, which would say that this is a very volatile business, actually look at underlying cash flows and you have a 100-basis-point rate shock from 9/30, not much impact.

If you step over here to the bottom right side, down 40% shock, you see we actually go negative there on PV fees less benefits. Again, this does not include reserves. It does not include hedging or any of that. So if you think about down 40 shock on an on unhedged basis, not the worst outcome in the world, the fact is we are hedged though. So just for reference if you wiped out the guarantee fees because if you assume we just spend the guarantee fees on hedging, the hedges we had in place at that point in time would generate about $16 billion in gains relative to the $11 billion of fees so we would still be on a fairly strong net positive position on a hedge basis. So the position of the VA book, the guarantee book continues to be very strong really. It is kind of a no-news type of thing and I know it took 10 slides to get to nothing is changed. But, nonetheless, thought that it would be helpful to get the context.

Reserves are based on Conservative Return Assumptions

Speaking of context, so I think I had this one up in the previous meetings, but just again just kind of a refresher to think about how things are coming through. The green bars are the S&P historical returns. And if you look at how basically it is the middle quartile that is what is in the bars and so the mean return on the S&P over the 20-year period you can measure; it is about 9.3%. If you think about EEV – which is more of an equity risk premium type of model over interest rates – what comes out of the EEV model is about 4.4%. So probably not that unreasonable and unrealistic given the dynamics that we have in the market these days.

From Economic to IFRS

Step to statutory, now this is an historical-based distribution, but we are out in the tail. So this is the 90 CTE, the average of the 10% worst scenarios that shows a 20-year return of about 2.2% compounded, which of course is basically the worst 20-year experience we have had historically. And then you get into IFRS, which is the market consistent type of analysis, and the red bar there actually works out to a -0.3% return. That is not a tail measure. That is the mean. So you are then going to calculate your distribution based off of that so IFRS clearly taking a fairly dire view and if anybody is curious about why that number is negative, even though rates are positive, that really just has to do with geometric returns. If we think about a 50% drop, 50% increase, we need 100% increase to get back up from the 50. So when you do stochastic analysis and you average it, you get to something that actually goes negative because it is so close to zero. So keeping this in mind terms of where the underlying returns are, I think it is fair to say all of our accounting basis take a reasonably conservative view on returns at least relative to historical. And clearly IFRS would be the most severe and the most interest rate geared.

So if we think about now rolling this forward into more the accounting basis, so the $8 billion, this is the same graph we looked at placed before, the one with a three-piece graph and one with the three quarter 2016 number. All we have done here is we have gone from the 5% annual growth rate gross to move down to a risk neutral return, so you basically go into treasury type or swap type of returns. And what that does is you get better discounting in terms of the PV of fees, but you also go to a huge increase in the benefits, which makes sense if you think about it because if you are basically at zero equity return and you are deducting 3% or 3.5% fees every year off the contract, all these contracts are going to go into the money fairly quickly, then they are going to have low persistence or high persistency. They will stick around and you are going to have some benefit from fees from policy sticking around but you are going to have a big increase in benefit. So if you believe that basically zero growth is the story for the next 50 or 60 years, this would be more of the cash flow profile you are looking at. And note that it still is a net positive.

Moving on the next step on IFRS, so IFRS can use the risk neutral assumption and also within IFRS you cannot book a gain on sale for a guarantee. So under FAS 157, the guarantee is an embedded derivative. You pull the derivative out of the market at the beginning, and effectively we have more fees coming in than would be required for the benefits that are assumed to come through. So there is this kind of excess pot of money. That excess pot of money cannot go into the reserve. So it comes in basically as earned. It is not sitting in the reserve. So when you think about the PV of all this type of stuff and where the reserves go, roughly half the fees that we collect do not end up on the reserve.

So now you get to a point where this might look a little bit more like what you think of the IFRS numbers. But you have also gone from a kind of a reasonable scenario into a fairly dour look at rates and then you are ignoring half the fees. So for those of you who continue to scratch your head over how IFRS can continue to be so volatile and look so messy in years like this, that is really the dynamic that we are dealing with there.

Economic Backdrop

So just bringing this back up again, you know, we talked about the longer-term trend within that. I will get into some of the metrics on the VA book and move towards the assumptions I'll focus more on the last little bit of this, which is the 2014 to 2016 range where we have been a little bit flatter in equities, the more recent downturn we have seen in interest rates and then the big negative move in swaps.

Cohort Analysis

So we had shown this years ago, and I think it is just instructive to go back again because this is one of those examples of how we look different than the rest of the industry. This is broken into the pre-crisis and post-crisis block. And what you see is about 85% or 90% of our in-force is written post-crisis and even for that business that was written pre-crisis, if you look at the GMDB over on at left, that cohort of policies is still barely in the money at 3% of the money on average, the post-crisis cohort on the GMDB is about 10% out of the money. Then you look at the GMWB, and remember all these products or many of these products have ratchets and roll-ups and things like that which is why you will never get too far away from the money. You look at the GMWB side again, and it is like 45,000 policies pre-crisis on average about 4% of the money.

This goes back to the ability to invest outside of all controlled worlds. And the performance that comes along with that helps when markets go down. You also get the benefit of markets coming back up. And that is what we have seen there. For a lot of our competitors, if you put this same graph up there, they would have a much higher degree of moneyness for that block and thus the reasons why they continue to work to mitigate those or reduce them or buy them back or whatever the case may be. For the post-crisis cohort, you see that is again the lion share of the overall policies we have, on average at 9/30 about 6% in the money. That should make sense if you think back to 2014-2016, the market was relatively flat. A slight trajectory upward but relatively flat, and so you got fees coming out. You also have for those people who are not yet taking their income, they will have bonuses applied to their policies, and so if you think about over a couple years that is about where you would expect the average policy to be.

Variable Annuity Surrender Experience

So as we start thinking about some of the characteristics of the annuity block, you see here we have gone back to about five years ago. This is just the overall variable annuity withdrawal rate that we are seeing or surrender rate. You can see it has been very, very stable over that period time, right around 5%. So I think what we are seeing is we are getting more and more supporting data for, if you think about the assumptions, that this is the product that has not been around all that long relative to other financial products that have been out there. So we are still trying to build a policyholder behaviour set as an industry, trying to figure this out as a company. The nice thing here is that I think we have got some good indications of the stability of the block over of this period to think about markets have gyrated a fair bit there in this time. Rates have been up and down. Volatility has been up and down. Lots of things have happened over these five years, but it has been pretty stable. Again, these are people's retirement assets. They are not treating it like their own personal hedge fund. They are actually out there saving, retiring and growing their assets and withdrawing to support the lifestyle. So what we are seeing is a pretty robust data set now of at or near the money in terms of what lapses look like for our block.

Of course, what we do not have is a real rich data set on deep in the money lapses. I am not wishing that upon us. I just assume never actually have to have that data set if we do not need it. But we do not really have many in the money policies, as you can see from the prior graph, and even in the periods where we did see is things deeper in the money, the market just did not stay down long enough for us to get a really good set of data. When we think about setting those types of assumptions where we do not have the data, we generally err on the conservative side. That is where we try to be. We do have the ability to look at other similar products and product types that might be deep in the money. There are some relatively high guarantee old life type products that are still on various books where there is no economic incentive for people to surrender so you can draw across from that. Some of our more unfortunate peers have a little bit more fulsome data set on deep in the money lapses so we are able to draw some stuff from the industry data. At some point I am sure we will get more deep in the money lapse data but, from what we know, things are pretty stable and continue to track as expected.

Also in the category of things, we were feeling better and better about through time is allocation. So we have taken a fair bit of heat over the years from competitors especially, in some cases analysts or shareholders, about the investment freedom aspect of our business. So you know we do not force allocation. As Barry was talking about we've got 90 different funds that people can allocate to within the guaranteed structure and we obviously are taking some level of risk of people gaming us on that. What you see here at the dotted line across the top is the assumption that we have within our pricing, set at about 84% which it has been for quite a long time. And going back 12 years now, policyholders have almost always been below that line in terms of their allocations.

You will see some movement in that line, but if you superimpose the S&P 500 over that, what you would see is that our customers are not actively rebalancing, broadly speaking. They tend to just ride up and down with the market. The market reallocates them and we see a very stable selection of funds and holding of funds within that. So again this gives us more comfort over the types of assumptions we can make and what we can build a business on. Clearly investment freedom is a huge portion of our offer to the market and we got a good experience there to be able to rely on.

Variable Annuities with GMWB

If we look at our current kind of demographics if you will of the book, so within the GMWB book if everybody wanted to start taking withdrawals today, what you can see there is roughly 40% would be less than or equal to 4%, a little bit more than that potentially in the greater than 4-5%. So if you think about it, the bulk of the book basically looks like in a flat market 20-25 years of payments before people would run out of money, so just thinking about it keep the maths simple. If you think about the fact that our average policyholder is going to be early to mid-60s when they start taking income, that puts them into the mid-late 80s. So this is why the product is built the way it is. That is why it is sustainable.

What we are effectively saying is if you live a long time, we will cover you there. If the market drops a lot, we will cover you there. But we are not writing effectively in the money guarantees at policy issuance, so I think that that range is helpful to understand the business a little better.

VA Account Value by Optional Benefit Guarantee Type

In terms of the bonuses, again people can select different bonuses within the products we have. And an unbundled product allows them a lot of choice in terms of the actual options that they choose within AC 6% is the most common. Differentiated charges for each of those so the more risk they give us the more fees we will take from them and 6% is the most common. It is a simple interest bonus so if you're lining this up against competitor, is also important to note that many are compounding annual bonuses.

This is a simple interest bonus. And I think the other thing that is important to recognise, too if you think about this again on a more simplistic basis, if I take a 5% withdrawal rate, it is going to take 20 years to exhaust my fund, again in a flat market. People only get a bonus if they defer withdrawal. So if you do not take a withdrawal in a year, then you get a bonus. So if you think about something in that 5-6% range, just again remembering that simple interest that part gets a little bit more confusing. But effectively what they have given up is 1/20th or 5% of the potential benefit that they are going to claim over the lives because presumably not going to live any longer because they bought one of these guarantees.

So the trade-off between the bonus and effectively the available amount to withdraw is an economically neutral bonus and so I mean that is actually why these bonuses exist; they are not there just to give away money. So what you do see is a prudent business model. Set at income levels, that makes sense for people and makes sense for us, and really gets back to we are covering people in the tails of longevity or the tails of the market.

Assumption Bases

So moving on to assumptions; again just a little bit of a refresher here. We did really two sets assumptions we have to think about, best estimate, which is really just kind of middle of the fairway type of a guess at what the assumptions ought to be, going forward. Typically in IFRS and EEV with the exception of 157, FAS 157, you see, we use the best estimate type of assumptions.

Under the prudent estimates, so it is basically take the best estimate at a margin. That is required in the statutory reporting side. And so if you look at our statutory numbers there is prudence already built into the assumption set. The last point is to have a significant degree of judgement with lapses in particular, to some extent utilisation as well. These are things that we do not have all the answers on yet. So we do have to use judgement there, but we do typically take a conservative view on setting those assumptions. And I think as you have seen throughout the years, we have not had any game changing type of assumption resets. In fact, in general, our experience variances and things like that have been positive.

Assumption Review Outcome

So annual process, we have just wrapped it up. We are going through all the governance type of aspects of it. So I am not going to give you the actual numbers, but I can give you some guidance on it. The magnitude of changes is similar to recent years. So we have seen, for instance, VAs tend to have very modest decreases in persistency, for instance. That is something that continues to kind of come through at a similar pace, small changes in mortality. The overall trends that we are seeing for VA are lower lapses. I think that one has been in place for a while.

We saw this year a little bit of a decline in the VA mortality, which basically ends up being like a little bit of more persistency when you think about the guarantee world, and we saw expenses coming through modestly higher. On the expense side we got things like risk and governance that continue to increase just in the financial sector in general, cyber security things like that. DOL is obviously something recent. So we do have a small expense adjustment coming through this year. The mortality impacts really differ across the different business lines. Again, to the extent mortality is effectively looking like better persistency in the VA, and that will tend to look like lower lapses. And then just generally better persistency across the board, driven by VA, and so, again, just a refresher, if you think about this little box down here.

Better persistency could be good, could be bad. It depends on the market you are in and on the product you sold. And it also very much depends on the reporting metric. So IFRS, typically speaking, if we look at better persistency, lower lapses under IFRS, and that is typically a modest negative. Think back to that chart a few charts back where we were assuming basically risk neutral market returns and ignoring half the fees. So if you assume the policy sticks around longer you are going to have more benefits to pay, but you only get half the fees coming through in the reserve so that tends to be on IFRS negative. EEV tends to be a positive because you have something a little closer to a realistic equity sort of returns and you get to include the fees, and then statutory tends to be neutral to slightly negative.

So if you think about this year, I mean what we are seeing is nothing really out of context of what we have seen in the last several years. You will get the same kind of dynamics playing through there. Obviously, the books bigger so the numbers will trend over time to be a little bit bigger each year, but what we are generally seeing coming out is a modest negative for IFRS, EEV positive and statutory, a little hit mostly due to things like the expenses and mortality impacts coming through. But we are talking at levels that are very, very small so nothing again, nothing to get terribly excited about within the assumption set.

NAIC Review of Variable Annuity Framework

So just speaking of exciting topics, NAIC. So I think it is important to understand a little bit of the context here too because it is become an interesting process. There is been a lot of speculation and concern where there really are not a whole lot of facts to be able to work-off. I can give it to you the best that we know at the time. If you think about back to where we were, this started out a year and a half ago as a targeted improvement on captive insurers in the US. VA companies were struggling. Some VA companies, depending on what kind of benefits they had and what kind of hedging they were doing, were struggling with some of the accounting noise that was coming through either on IFRS or Stat. So they set up captives to be able to change effectively the accounting and try to do it in a way that is a little more opaque.

I do not know that they themselves were that bothered by it but the commissioners were getting a lot of feedback from analysts, shareholders and such that what is it about this system that you set up that has all these people wanting to be captives. Is there anything you can do about this? So they basically started looking at what can we do to reduce the incentive to use captives. Not that they are trying to outlaw captives, but just trying to fix technically whatever it was that was going to cause the captives to need to be in place.

So in the process of doing this, they engaged Oliver Wyman to come in and do a quantitative impact study, again extensively looking at the captive issue. And then that took on a bit of a life of its own, in terms of effectively a complete re-proposal of the entire statutory system of capital and reserves, which then, of course, got industry interested and a lot of others. And there is a lot of pushback there, a lot of concern. What is interesting is I think the Oliver Wyman report was more of a flash point because it was not expected to be exactly what it came out to be. And I am not even sure that the NAIC was necessarily thinking they were going to get what they got. But Oliver Wyman basically re-proposed the whole system. And you also had some rhetoric about that time coming out of the working group about 'we need to implement this as soon as possible. We need to get this in by 01/01/2017 if we can.'

Anybody who is worked around the NAIC knows that nothing happens in less than generally three to four years typically for something big like this because there is a process there. So it is not just a knee jerk kind of 'we got a new idea; let us try it' kind of group. So what we have seen now is Oliver Wyman has come out with their proposal. We just finished the comment period yesterday. So all the industry comment letters went in yesterday and as well as the industry spokespeople like the ACLI and the American Academy; interested parties would have put things in there.

During this process and while there was this kind of a couple weeks' firestorm that seemed to brew over the Oliver Wyman report coming out, there was a lot of conversation with the commissioners with the working group. And it became very clear that they were not looking to rush anything through. They were trying to be deliberative about this. And I think the process maybe got a little bit ahead of where they had expected it to go. So in the conversations I have had with some of the commissioners and some of the industry folk where we really stand right now is they are going to get the comment letters in. They are going to take a deep breath. They are going to take a look at this and say is the Oliver Wyman way to go the right way to go? Are there other ways that we might want to look at this? What is the full subset? Well, if we are going to re-propose the entire VA reserving the capital structure, we need to do so with due deliberation.

So, again, they will take a look at the comment letters and that will determine what the next quiz looks like. The next quiz may be a refinement of the Oliver Wyman study. It may be something completely different. You may even get a request for comments on a whole new system or ways to change the existing system. So I think there are a lot of potential possibilities to go from here. One thing is clear: it is going to be slow and deliberate. They are not going to rush into anything. The next quiz study is likely to take six to nine months. There is a possibility of things, if everybody got into agreement and things went on a fast track, that you could see something in 2018 if it changed. I would say it is more likely 2019 given the amount of work that needs to be done. And that said it is not clear much is going to change because, again, we have kind of wandered away from the original remit, which was to deal with the captives.

At this point there is not enough information to be able to just say okay here is the number with, here is the number without. There are some relatively significant features within the Oliver Wyman proposal anyways. I am sure many of you are aware of these, but I will just walk through them. The higher CTE thresholds, the regs currently call for a 90 CTE capital threshold. They are taking at the 98 CTE, but they are taking it to 98 CTE and then basically dividing by 4; so the difference between 98 and 70 gets divided by 4. So what does that mean? Well, that is part of the problem with this is. It is kind of hard to tell. So that is why we need more analysis on this. Generally speaking, at least when we look at that, that higher CTE threshold – and what they are trying to do with this really is trying to get more credit for specifically interest rate hedging coming through this. That is part of the feedback they've got and maybe part of the reason why the captives exist. So they are figuring if they push it far enough into the tails that the hedging will be more, will come through better, which is part of why they are at the 98.

So the 98 CTE divided by 4, it seems to be broadly neutral from there we can tell on our book anyways. The worst of which would be risk-free swap rates, specifically swap rates. Think back to that chart where swap spreads have inverted. Going from swap rates to corporate discount rates, and that is huge, huge positive in terms of reduction reserves and capital requirements broadly speaking. There was a proposal potentially for standardised policyholder behaviour. That one is probably not a good idea just in general.

I mean the industry is moving more towards principles-based and if you think about the wide dispersion between GMIB, GMWB, GMAB, GMDB, you think about people who have deep in the money policies, broken back books or people who do not, there is such a wide discrepancy of potential policyholder behaviour coming outto standardise it. If they are going to standardise it, likely they are going to do it on a more conservative basis. That is probably a net negative if they go in that direction. Again, this is all the type of things would be vetted in the next quiz study in more detail. On deferred tax assets, so they are looking at recognising more deferred tax assets within this.

So some positive, some negative, some big, some small. I think, broadly speaking, our view on this would be that if you are taking a best guess of where some of this might be parameterised and looking at it on our book, capital would be roughly similar to what it is now. Reserves would be roughly similar to what it is now. It would probably be a little more stable than it is currently, mostly due to the discount rate piece. So I do not think is necessarily any hugely bad news in the proposal, again depending on where things get parameterised.

The only caveat to that would be that there was a kind of afterthought 'we have not really done a whole lot of work on this yet' type of comment from Oliver Wyman in the report which basically went to effectively kind of a market consistent view of equity drift with a spread, so maybe risk-free +2 or risk-free +3 or something like that. That would not be helpful, but that also does not seem to be very well developed. And I will say that there is a very strong pushback in the US, both at the regulatory side and the insurance company side, against going to a more consistent world. I think the lessons of Solvency II and similar types of approaches have been well figured out in the US and nobody seems to be interested in going there.

On the next steps, I would say that within this you could go the Oliver Wyman route. There could be something completely brand new. There are actually some relatively small technical fixes which you could do to the current regime that would actually fix this. So you would not have to go to a brand-new regime with all this complexity. There are some relatively minor tweaks you could do to get to the similar outcome. And I think that will also be part of the conversation. I think broadly speaking we are pretty relaxed about where this is going and the pace that it is going on. And we will just have to see. I mean any time you open something like this up there is risk, but it seems to be heading in a reasonable direction.

They have finished the comment period, they are going to synthesise all that, come out with what will be some sort of next step quantitative impact study. We will have to see what comes out of that. I assume if they get reasonable numbers in a reasonably robust industry-wide outcome then they will look to propose that. That will likely fall sometime in the second half of the next year and most likely gets implemented in 2019. So that is kind of where we sit with respect to that and I am sure we will have Q&A in a few minutes. So I am sure and there will be some questions on that.

Statutory Framework –Voluntary Reserves

Just a little bit of background on this. So if you think about the current risk-based capital framework in the US, it is a regulatory standard set more at a kind of triple B type of level. Double A type of capital levels tend to be around 3.5 to 4.5 times that regulatory capital minimum or required capital minimum. So it is a much more levered version of a capital ratio than we typically see in Europe, for instance. What is a little complicated within that is that the historic structure is more of a formula-based, factor-based approach for most everything outside of VA where this kind of four times capital/three times capital type of requirement makes sense.

The VA with the C3 phase II being what it is, is more akin to a European-style solvency regime, and does not really make as much sense within this overall framework. And so it does not make as much sense at a 400% type of ratio, especially when you get into the tails and things start becoming a little bit more interesting. So that is part of why they are looking at this because there is it is a little bit of square peg/round hole type of problem. A lot of this again is manageable. I mean we have been able to manage through that. We were not out there saying 'hey, can you please fix this?' We have been able to manage around it with things like our permitted practice on interest rates and voluntary reserves, which I will get onto in just a minute.

But so just a refresher, if you look at what is referred to as example one there, this would be a pretty standard for the more factor-based formula-based ratio. If you said you had 4 billion in capital, a billion of required capital, 3 billion of excess and you have got an RBC ratio that pops out of that of 400% so there would not be a lot of required capital probably in a VA. So that would be a more benign equity environment or industry environment. If you get back to right-hand side and you think about if you properly hedged it so over required capital has not changed. What has changed is the required capital coming out of the model. And I will get into in a minute why that might move, but you have basically taken a similar financial position, you have more capital than you had before. You have hedged it properly, but your ratio has dropped. So that would be the way the regime works now.

So with us, you could do a couple different things. You could just report different lower numbers, which are going to be a little bit confusing I think to the market. If you have VA and non-VA companies spread between 200% RBC and 700% RBC, you cannot measure anything consistently in terms of the actual financial strength of the company. So you could do nothing. You could set up a captive insurer, which a lot of our competitors have done and that effectively brings you back over to the left-hand side or you can do what we have done, which is to setup voluntary reserves. In this case, if we just basically set reserves higher and took capital down, reserves go up and capital goes down by a billion, you have moved yourself right back to 400% RBC. It is really just a different way of looking at the exact same problem. So what we have tended to do is report with voluntary reserves and disclose the number without. So it is very transparent, anybody can take a view of what they think the financial strength is or is not of the company in that way.

This is the general problem that we are facing with the current regime which the voluntary reserves do solve. So you have got the red line just being the AG 43 type reserves, the black line being generally the CTE 90, the C-3 Phase II type of scenario. There are different scenarios where you get some dislocations here, but lower interest rates are the biggest problem. Again because the reserve calculation is a completely different calculation and it is done off of more of a portfolio rate or corporate type of rate. The black line there, the required capital is being done off of risk free, and in this case specifically swaps, not treasuries. So, you know, what we have seen with swap curve inverting is a much more onerous view of the required capital, as treasuries have been as low as they have, swaps even lower. It is a pretty dire view in terms of discounting. If you think about what you are using this rate for, conceptually let us say we had a drop in the market, and we had to put up $10 billion of reserves. So we have $10 billion of reserves, so what are we going to do with them? Well, we are not going to put them in cash and we are not going to put them in swaps because you cannot buy a swap. We are going to put them in corporate bonds or possibly treasuries but we are going to put them in something like that. That is the discount rate that makes sense when you are looking at what is the present value's liability. It is that disconnect within the kind of the technical pieces of the overall framework that causes this issue. So when we use the voluntary reserves, that blue line that is going up there, what we are really doing is just stabilising the difference between those two lines in the tail where you get this kind of non-economic implication coming through on the right side.

Hopefully that makes some level of sense and I think what we have seen too is if you look at the Oliver Wyman type proposals what they would tend to do is raise the reserves and required capital would be somewhat more consistent with where it is now. It would raise the reserves and really kind of codify what we are really already doing through voluntary reserves. There were a couple of things that they could do with the existing framework. One would be to change the discount rate on the required capital side just to narrow that gap. The other issue would be, for instance, with voluntary reserves you run into deferred tax asset admissibility. So you do not get, necessarily, a full-blown after tax benefit of those reserves going up because those are not the actual tax reserves that come through. So, again, that is another technical fix that could be done pretty simply and we will see how the overall dynamic plays out.

Jackson Produces Results

So just a couple of more slides to wrap up here and we will get to Q&A. You know we have talked about the fact that obviously it has been a rough market environment to be in. We continue to see good strong asset growth driven by again good net flows. Not as high as they were, but still strong net flows. All this growth done with a stable RBC ratio and strong remittances back to Group. So, you know, we are quite pleased with the overall performance of the book and how it is coming through.

A note on the RBC ratio, we have got a little blue bar there. So, we have this permitted practice in the US where we basically are allowed to carry our interest rate swaps at book value as opposed to at market, which is consistent with the Michigan code but not consistent with the NAIC, the SAP 86 type of approach. So we have a permitted practice and we will do that. They are bonafide hedging transactions, so we effectively get hedge accounting for them. For the most part, generally speaking, we have permitted practices in place to keep from having a dislocation and higher rate environments. So if rates go up, these are swaps to protect against down rates. So rates go up, we are going to get a mark on the swaps under SAP 86 that we will not get a release of on reserves, because the reserves will floor out on stat. They do not, for instance, do not floor out on IFRS. They do floor out on stat. And so you would get a dislocation there. So we have had this permitted practice in place for about ten years at this point. It makes sense from a hedging and accounting perspective. What it does do, though, is it keeps us at book when the market is lower and when you think about going back to this one, as you get to the far left of that graph, you get this big dislocation due to interest rates. We are carrying our swaps at book in that case and so we are not getting the full benefit of that.

What we are showing here is really the effect of that permitted practices of the impact of carrying those swaps at book. There was conversation around whether we would look to remove the permitted practice this year, just given the fact that the swaps at this point in time are much more aligned with the economics in this extreme low rate environment. But since the entire world seems to have been changed in the last week and rates are significantly higher, we would probably leave the permitted practice on. And, of course, this is through September and rates have been much higher since then. So we will see much less pressure. In effect, we will have moved a fair bit back up that curve on the right-hand side there, from left to right so permitted practice will be less of an issue.

But it is worth noting that as of September 30, despite the fact that it is been a relatively volatile year in both rates and equities and the fact we paid the bulk of our dividend at midyear, ex permitted practice we were basically up on capital for the year. So capital formation is still good and strong despite some of these headwinds.

Superior Operating ROE

This is one of my favourite graphs, which is probably why I keep putting it up. We have talked about a differentiated approach to the market, a differentiated back book in-force, so everything we have done is different and I think disciplined. And what you see is that coming through here. We do not have a broken back VA book to have to drag along. We have very profitable vintages of VAs that we have sold. And we have been able to manage despite the huge drop in interest rates. We have been able to manage the spread business to a pretty consistent and high level. And you see all that coming through here. And what this does do is it gives us – you know if you think about just the - you roughly double the ROE in the industry. It gives us a lot of room to absorb whatever kind of shocks come along.

I mean even if you took the view that there is going to be a significant increase in capital coming out of the NAIC thing, which I would not subscribe to, you would still see massive outperformance relative to the industry and very strong returns just across the board. So we are quite happy with the performance here. Again, in a volatile market this is a good place to be. So with that I will turn it back over to Barry to wrap up.

Summary

Barry Stowe

Chairman & CEO, North America, Prudential plc

So just to wrap up our presentation before we open the Q&A, I just really wanted to say – in case you missed it the first and second and third time I said it – one more time for old time's sake, we genuinely are in a unique position and maybe one of the most positive positions we found ourselves in North America in a very long time, because the regulatory trajectory is moving towards us. It is going to result in outcomes that play perfectly to our skill set, and not the skill set as we define it but the skill set as defined by our history and our capability, which I think are well known to you and well known amongst the industry.

So you know a key to that capability is our ability to navigate the macroeconomic environment. And nobody knows what lies ahead. It could be volatile but, as Chad has just demonstrated, we continue to manage this business very capably and with incredible discipline to produce the right outcomes for shareholders and for consumers. So we are hugely optimistic, and I know that this has been a year when maybe the world has not been hugely optimistic about the space in which we play. But what I hope you have learned today is that maybe that glass which you thought was half empty is actually half full, maybe more than half full, that the prospects of this enterprise are brighter than they have ever been. And that, again, we are just incredibly well positioned to take advantage of the environment which we see emerging. And with that then I will ask, Chad is already up here, if Drew and Alison come on up and let us answer some questions.

Q&A

Jon Hocking (Morgan Stanley): Hi there, I have got three questions please. Firstly thinking about this little fee-based VA product, that was seen to be something that is sort of less cash and capital consumptive from a strain point of view. Can you comment on the returns and payback potential of that product versus the sort of commission-based products? The second question: I think in recent history you have said that the hedge programme is pretty short dated and you are rolling the programme. I just wondered whether the potential change in the interest rate environment changes that and whether there is a chance to extend the duration of that portfolio and whether that is something you are looking at. And then just finally, I did not quite understand on slide 32, when you are going through these various scenarios of the fees and the benefits, that there is a big jump in the benefits, the PV of the benefits on I think from year 40 to 50. I did not fully understand what was driving that. Thank you.

Chad Myers: So starting with the first question on the new fee-based type of products. It may not be completely intuitive but it is actually from a statutory perspective there will be – well, it depends exactly on how we distribute it. But the expectation will be that there will be some strain there. If you look at the product that we have, we currently have out there is a small surrender charge. That surrender charge covers the upfront policy issue cost and general marketing type of cost. You know there is the possibility, possibly even likelihood, of going to a fully liquid type of market. I mean we have seen good acceptance on the surrender charge. It does make sense to protect ourselves that way. Realistically the payback is fast enough on these products that a fully liquid version could make sense. It will just be more expensive to the consumer. So it is the question whether they are going to want to pay the extra to have the full liquidity. It may not be enough of an up-charge to make that problematic.

If it does go to fully liquid then we would see some strain in year one, but I think we are still typically seeing year paybacks by year two or three on those. So it is still a very attractive dynamic there. If you think about the current environment, the surrender charges are sufficient to be able to cover all that upfront commission costs. So there is really no meaningful strain as is. On the hedging, we have seen a nice move back up in rates. We have backed away slightly from the precipice. I would not say we are quite to the point of a healthy rate environment yet. So, we are basically on the ten year back to where we were at the beginning of the year where. Absent a bigger increase, probably a 100-150 basis points, this is probably where we needed to go from here higher and call it the three to five-year portion of the curve. We will likely stay on the short end. This might give us a little bit of scope to move a little bit further out. But I do not see any major changes. And what was the third question, sorry?

Jon Hocking: Slide 32. It was a great slide.

Chad Myers: That was great, yes, one of my favourites. So the pop in benefits in 2015 was the question, right. So basically what you got going on there is you had negative separate account or negative equity growth in 2015. And so what you would have seen through that is, you know, if you think about fees of call it 3% just for round numbers. The vast majority of our policyholders at this point are not taking income yet. They are still deferring, so the vast majority of them are getting bonuses. So if you think about a 5% or 6% bonus, you know plus the fee drag and plus the negative market, you would expect an increase in benefits down the road. And that is the dynamic we are seeing come through there.

Nick Holmes (Société Générale): Three questions for Chad again. Looking firstly at the variable annuity stat reserves, you did increase these very significantly in 2015 by some 900 million. Now I know, as you described, you do not want to get into the accounting noise, and the reserving is also pretty weird. But can you tell us why you had to strengthen reserves so much in 2015? And what the outlook is for this year? And then second question is looking at your cash flow projections, which are very good but, as you say, they do not include hedging, they do not include reserving or accounting noise. Can you tell us what the impact would be on reserves if the S&P 500 did fall by 40%, which is what you show? I mean I hope that does not happen by the way.

Then thirdly, could you tell us what you think of the basis risk within your hedge programme? Because and correct me if I am wrong here, but one of the attractions of the prospective product is the wide asset allocation as you described. Now this is very difficult to hedge, right? I mean most people would say that. So in your scenarios I assume you are not actually taking into account the potential basis risk, which is pretty difficult to measure anyway. But could you talk us through the basis risk because in the financial crisis the thing that cost the VA writers so much, a lot of it was the basis risk. Thank you.

Chad Myers: Sure. Okay so if they are all going to be for me, I am going to be have to write something down, or I am going to be have to keep asking you. So let me start with the last one since that is the one I remember first. So with respect to basis risk what we have seen is we look at the underlying betas of all the individual funds. It is not something as simple as we just assume everything is S&P 500 and run from there. So we do hedge the actual underlying funds as they behave. Similarly, if you look at where the biggest piece of the basis risk tends to come from is really international and currency. And so we do actually hedge a component of both the ether and the emerging markets off of that. That is the vast majority of the basis risk. Had we not done that, then you would have seen actually some more volatility in the numbers this year. But actually with that hedge it is quite effective. Generally speaking, we have not seen material amounts of basis risk enough to really affect the economics.

The best example I can give you is from the crisis, so this is a little dated. But generally speaking, what we found is most funds are going to have some at least mild amount of cash in them just for transactional purposes. And the fact that the funds that we have in general, if you look at the underlying positions, tend to be more equal weight than you get out of something like the S&P where it is much more concentrated. I would say, generally speaking, a little bit more of a value tilt. So what tends to happen is when we get big draw-downs in the market, we do experience basis risk. But it is a good basis risk, meaning that our funds do not drop as much as the larger indices. We do track it. We hedge the parts that are material to it. We have obviously been at this for quite a while. We have had investment freedom as a core piece. Actually, what is funny is we call it investment freedom and that is the way the industry has always been until the crisis happened and everybody went to vol controlled funds. But I think we have got a long enough track record that we are pretty comfortable with it.

The basis risk you are referring to in the crisis, I mean at least one competitor I can think of was much more concentrated with one fund family. And you know that got to be the bigger issue. If you look at ours, you know our largest single fund is typically around 7% of the underlying portfolio. And they tend to be – if you look at the larger funds, they tend to be more asset allocation and balance type of funds. And so, again, we tend to get a little more of a defensive tilt on that piece of it. What were the other two questions, sorry about that?

Nick Holmes: Strengthening reserves?

Chad Myers: So strengthening reserves, so the voluntary reserves you are talking about presumably?

Nick Holmes: Just to recap it was the 2015 increase in the voluntary reserves. And also if the S&P 500 did fall 40%, what sort of number in reserves, can you give us any feel for that? Thank you.

Chad Myers: What I can tell you is I do not have the number, the reserve number off the top of my head and obviously it matters a lot kind of month to month in terms of where the hedge book is positioned. Broadly speaking, $16 billion was the number at 630 that our hedge program would pay off in an instantaneous down 40. The reserve change would be in the general vicinity of that because we are typically – that is down 40 is a limit that we have in our limited framework. So we do not let those two wander too far apart. With respect to the reserves last year, generally speaking voluntary reserves are almost exclusively being driven off of rates. And again this is back to C-3 Phase II and the swap curves. So what you saw is the more inverted the swap curve became or the more negative the swap basis became, the more voluntary reserves have gone up. So we saw an increase in volunteer reserves in the first half of this year as well, a lot of which is now getting backed out as rates have gone back up.

Oliver Steel (Deutsche Bank): Barry, you have sorted of painted a fantastic scenario for VAs going forwards. But your sales were done 28% at the nine months' stage. So I was wondering if you can just give us a bit more of a sort of feel for how you expect things to pan out between the first nine months and your view of the future and what you are sort of hearing from agents as of now?

Barry Stowe: Yes, I hope I said in there somewhere and if not I meant to that this, you know, this does not happen overnight. But what has caused the disruption in the market this year around annuity sales is obviously the uncertainty introduced by the Department of Labor rule change, the prospect that without full clear grandfathering, which is the current rule does not have, that by writing VAs, advisers could be actually creating liabilities for themselves which they do not yet fully understand, their broker dealers not having gone through the rule with a fine-tooth comb. Even before the rule was published, in anticipation of it this time last year you saw sales slacking off. And then when the rule changed it was more severe.

I would tell you that I would not expect there to be a significant uptick in the next quarter or two. You have a lot of people that are saying well, might the litigation that is currently you know in play against this rule, you know might that have some impact, and no one knows. Now there was one case that was filed in the DC district courts, which I think most observers said was probably not a particularly strong argument, not necessarily the way to go at the rule. And that they kind of got their heads handed to them, the litigants in that. The case that most people are watching is the one where the US Chamber of Commerce is the lead. Eugene Scalia is the counsel for the litigant on that side, and that is in Texas District Court. The oral arguments in that case are tomorrow; we would expect maybe by mid-January you would probably have some sort of sense of where that is going. That could change everything.

But what is clearly happening is we have engaged differently in Washington. There is a sort of a coalescing has taken place and a recognition that if you can actually get people on both sides of the political aisle to sit down and talk about an issue, you sometimes miraculously find that if you drew a Venn diagram of the beliefs that there is about an 80% overlap. And you know the 20% around which there is disagreement is manageable. So I kid you not when I say we have spent months talking to people who the industry has always assumed was hostile towards these products. And what we are hearing is we are not hostile towards the products. We love what the products do. Maybe we have concerns about how the products get sold. Maybe we want to understand the fees. You know what we get a lot is, 'VAs are really expensive because it is really just a mutual fund, all you get is tax deferral and you know you pay four to five times what you pay for a mutual fund'. And then when you remind people that the VA has a guarantee which often at times is lost on them, it completely changes the dialogue.

I will tell you this too. To give you an idea of the level of misunderstanding around these issues and the need for there to be more transparency and more clarity in messaging, the ACLI, American Council of Life Insurers which is the trade group for life insurance companies, just conducted some consumer research. And they went out to a scientific group and they asked them some questions about retirement. And some of the data points there were shocking. They asked people if you felt that as part of your retirement plan you would like to have a product that provides you a guaranteed income throughout your retirement, an income you can outlive, to what vendor would you go to buy that product? Would you go to your bank? Would you go to a mutual fund? Would you go to an insurance company, whatever? 0.5% of the consumers said they would go to an insurance company, when in fact it is the only place you can go. 40% of those people thought they had a guarantee through their mutual fund.

So there is work to be done. You know we talk about you know the advice that gets given. There is work to be done in terms of more clearly articulating the story for our industry in general, for this product specifically and the unique role it should play in the retirement plan of most middle-class Americans. It will not happen overnight.

Abid Hussain (Credit Suisse): Hi, two questions if I can. Firstly, on the fee-based VA. I was just wondering what are the barriers to entry for a platform fee-based VA product? I am just trying to understand is this going to be a competitive space or not? And then, secondly, on the market-consistent approach if that is actually applied to the book? Is it just a case that we have to get used to a lower RBC ratio of 200% or whatever rather than 400%? Or will you have to put up more capital?

Barry Stowe: Barriers to entry for fee based? I mean if you can manufacture a VA with a commission you can manufacture a fee based on that. I do not know that there is any unique barrier to entry in terms of manufacturing that product. Are you referring to getting it on the platforms that I spoke of earlier? The barrier is not just the manufacture of the product itself, but it is actually getting it onto those wealth platforms. So that the advisers that are accustomed to working on a fee basis and are accustomed to having, you know, really quite a simple approach where virtually everything that they offer can be sold from and captured on this platform; none of the VA writers are currently on those platforms.

I can tell you we have been working on this now for almost a year and working closely with a handful of the largest distributors, most of whom have their own sort of proprietary wealth platform. It is not a small task. This is not something you will have in the first quarter of next year. I mean to get it fully integrated it will take quarter after quarter after quarter. But it will slowly happen. Does it become a competitive space? I would assume so. And candidly I would hope so because the right place for the industry to be is for all advisers to have multiple reasonable options to show to a client or a prospective client. That is where you want the industry to be. We do not want to be the only one on the platform. I think that weakens the case for the product.

I do think that you will find that we are the first or amongst the first to get to the full integration because we are working on it already. And I am not suggesting that others are not, but by virtue of the fact that we are already working on it, that is very useful. And by virtue of the fact that we have highlighted earlier the prowess we have around IT generally, and if you look at our current system that advisers have to use, even though they have to come out of their system and go into our system to do it, they find that system to be very user friendly. We have got really an incredibly high quality platform driven by an incredibly high quality team. And I have a lot of confidence in their ability to craft these solutions, and get them into the platforms faster than others. So am I answering your question?

Abid Hussain: Yes, I think so. I was just trying to not understand if it is going to take a long time for others to catch up on the platform space; it sounds like that is the case.

Barry Stowe: It is going to take a while for anybody to get there. I would think we would be first. Those that are not working on it yet, those that have not conceived of this yet will be behind.

Chad Myers: We do not really want to see a bunch of proprietary platforms get built. Ideally what we will see is some industry standards coalesce so you actually get a pretty open architecture. You know we are happy to compete on products. We do not need to compete on the plumbing aspects of it, and it will be a bigger and better market. Again, if you look at the size of the opportunity, we cannot do this alone. So the industry has got to be over with us, so there will be plenty for everybody. So I think there is that part.

The marking[?] system point within the NAIC, I assume that is what you are referring to. So I would say that one is highly unlikely to go that direction. There is enough pushback, even specifically within the regulatory side. By and large the commissioners, the state commissioners that make up the NAIC are not enthusiastic about marking system at all. And so for them to adopt something that is marking system, it would not make a whole lot of sense. The other aspect is from a timing perspective, that is likely to be a battle that is drawn out for quite a long time. So if you are trying to get something sensible done for the bulk of it, and then you have got this other thing hanging out there that requires a lot more study and a lot more you know visceral reactions from people, it is likely that that would not get packaged together. I am not saying it could not. But I think in the hypothetical world you are talking about, you have seen the cash flows, you have seen the way this all comes together. I think we do not need any more capital to economically support the business. Then I think it just really gets down to more of a question of where do [inaudible] come out, where do you know rating agencies come out. If they do not move the corridors on company action level and things like that, then you end up with, yeah you would have to do more capital to support that.

Abid Hussain: It sounds like this is being pushed by the consultants as opposed to the regulators, is that right or –

Chad Myers: It is hard to say exactly. I mean I think the regulator was interested in a question and I think the consultants got pretty excited about the project and off they went.

Barry Stowe: You gave a very broad answer to a fairly specific question.

Chad Myers: Yes, and if you think about it, I mean Oliver Wyman was you know one of the major movers behind Solvency II as well. So I mean they have a general direction in those sort of things.

Barry Stowe: They have a point of view.

Blair Stewart (Bank of America Merrill Lynch): Thanks very much. And three questions I think. Firstly Chad on utilisation of the withdrawal benefit, what proportional of people who are eligible to do so actually make a withdrawal, can you give us an idea of that please? And Barry, secondly on the DOL, is there anything you foresee in the coming say three to six months that may emerge with regards to be a quicker change of wording or maybe a delay to the process, what do you expect in the next few months on that, given the change of Administration? And thirdly on NAIC, how should we assess the risk coming from standardised assumptions on policyholder behaviour, etc., where is the debate on that at the moment, thank you?

Barry Stowe: Let me take the last one first. There has not been much conversation about that other than a conceptual idea. You know again I think this is not coming out of the commissioners. This is a point of view of Oliver Wyman would be my impression. And I think they would like to see in their opinion things get standardised. You know it is obviously very problematic to try to standardise something as broad as those assumptions. I mean if you said we need one lapse assumption for the industry no matter the product, that would make absolute no sense. You know if you said we are going to make it this for GMIBs, this for GMWBs, you know by vintage or something like that I do not know. Maybe you could get to some sort of reasonable place, but again I think the distribution force that it is sold through is important. The type of compensation structure that is there is important.

There is just a lot of variables that would make it very difficult to make standard assumptions unless you are coming at it similar to the way the current structure is in play. You think about you got a principles-based layer which is C-3 Phase II on the stochastic side. And then you have got this relatively onerous, relatively blunt instrument, which is the standard scenarios; it is similar to the standard scenario type of mindset. You know I think that there is broad consensus that the standard scenario is not overly helpful in the current regimes. That would be another one of those things that I would tick off that you know besides rates and DTAs. Then the standard scenario adds a lot of noise over certain sectors. This would be akin to the standard scenario, so you know that is kind of the wild card of if they do re-propose and reopen this whole thing, do you get a wide consensus that is there? And then somebody comes in at the last minute and slaps something on top of it that makes it not work. I mean that is always a possibility of the NAIC. It is you know it is happened before. But there have been no specific proposals that I have seen so far on what the parameters would be for a standardised set of policyholder behaviour assumptions. Is that helpful?

Blair Stewart: What is your opinion about [inaudible]?

Chad Myers: Well, we are not supportive of that. What we have laid out is in our comment letter is really along the lines of if this is going to be a broader project then just trying to talk about captives, then we need to get all parties in there. I think they agree. You know to get something like the American Academy of Actuaries was not involved in this. If you think about the way this came about. Oliver Wyman went out, the companies volunteered to participate in it at their own cost. So you basically had fifteen companies in this initial quiz study. And even the companies that were providing data were getting very little feedback from Oliver Wyman in terms of what the ultimate thing was going to look like. So it was a big reveal at the end of the process for everybody. So you have got a lot of interested parties, a lot of brilliant minds out there that have not had an opportunity to do anything with this yet until the comment letters came about.

So from our perspective it is, if we are going to open this up we need to take a broad look at this including is there something we can do to fix the existing regime, is there some better regime out there. And then, thirdly, what are the parameterisations you would look at under Oliver Wyman's proposal. That is more our position on it. Did I address that question?

Okay, I say that one other point I think I forgot to mention earlier. This whole thing started as a way to get rid of the captives and make things a little bit more transparent. There is nothing in what has been proposed that would make captives go away. And in my conversations with the commissioners, they are not interested in – because I mean the easiest way to do this would have just been to say no captives. That fixes the problem. They are not inclined to want to go that direction because captives are used for good reasons on a lot of different lines. And it would be very difficult to just say no captives over here, and captives everywhere else. So it seems pretty certain that the whole ability to use captives is going to stay in place. To the extent that that happens, if they do something particularly onerous here, then all it is going to do is increase the use of captives not decrease the use of captives. So I think that is an important backdrop to this whole thing because that certainly would not be the outcome that they want.

Back to your first question on utilisation, what we tend to see is utilisation is very much age driven. When we first started writing the product back in the mid-2000s, we thought it would be a little bit more moneyness driven but it is really very clearly age driven, at least on our block. And you tend to see some people would come in with an intent to get income right away. So they will come in and immediately start effectively utilising. The vast majority though will typically wait anywhere between four and six years to start taking withdrawals. And even in the people that are much more in the withdrawal and heavy [inaudible] for utilising in mid-70s, by then you should be taking income probably if you are going to. Even there we see that 80% maybe, it is kind of a high end up where we see that come out. There are some people who clearly buy these just for the flooring. Do not necessarily intend these if they do not have to.

Barry Stowe: On your question about DOL and what might what happen now? We had done a lot of work preparing for either a Clinton or Trump Administration. We met Seth, who you met today, as part of that work of engagement into what would have been a Clinton populated Labor Department. And our view was that regardless of who won the election that there was the prospect that the DOL rule could be modified – and we were getting very strong signals to that effect – that it could be modified in a way to make it work better and genuinely accomplish what it set out to accomplish, which was to raise the quality of the advice, raise the standard for the provision for advice. In so doing make people more comfortable that if you were advised to buy an annuity product that was based on higher quality advice it was a good decision to make. And so, again, the intent was that more people would buy products with lifetime income guarantees, not less. Now that we are dealing with a Trump Administration, I mean candidly the conversation is easier because we will have in place an Administration that is openly sceptical about proliferation of regulation and aims to undo a lot of the regulations have been put in place during the Obama Administration. So in some respects, we are now pushing at an open door on some of these issues.

We do not advocate the repeal of the rule. I alluded earlier to this litigation in the Texas district court. If they were to come back and say the Department of Labor had no grounds to do this on whatever basis and they knock the rule completely back and say it is gone. My view would be we then as an industry we should have next day immediately sit down with the Department of Labor and say let us figure out exactly what it was you were trying to solve, and let us solve that and do it in a more sensible way with more collaboration. And if the court is telling us that actually whatever we come up with needs to be legislated, not made via the rule-making process, that we have a unified Republican Congress. And if we go to them from a Republican Administration and say the industry likes this, the regulator likes this, you know the department likes this. Let us pass this legislation and the odds are we can get that done.

All of this stuff takes time. The manner in which this was implemented made it go sort of beyond just being a rule. It becomes law. And so there are different paths for changing different portions of it, some of which take a long time and some of which what take a short time. Legislation takes a while. Overall rule change takes a while, doing something simple like just going into the BICE agreement is easier. There is a much shorter process for that. Our view is that what was likely to happen is a delay of the implementation; that is what all that is what the industry seems to be coalescing around. That is what we are hearing pretty consistently in Washington is there ought to be a delay of some period so that all the parties that sort of have a dog in this fight, if you will, can come back into the room and sit down and talk about this further; the premise being that the comment period maybe was not long enough or was not taken seriously enough or whatever. There is the prospect of getting everybody back in the room, collaborating, coming up with a better rule and then implementing that. And I think what would be important to that is during that period of delay, in order to sort of remove the paralysis that we currently have in the market, what we would advocate is that the Administration come out when they announced, if they announced this delay, and say by the way transactions up until the ultimate effective date of the rule, whatever rule it is that gets put in place, will be grandfathered. So that advisers operating under the current law, which worked reasonably well for a pretty long period of time, would be comfortable going out and offering these solutions to consumers and not worrying about class action lawsuits and liabilities that candidly they just do not understand.

So long answer, but hopefully that covered the ground.

Chad Myers: One thing I would add to that too is just it is more than just DOL. To fix this it is SEC then it really wants to bring both parties together.

Barry Stowe: Yeah now that is I think a prospect that we have that we might not have had under a Clinton Administration is to say let us do not just fix this one rule, but let us step back and look at this marketplace that is regulated by SEC, by DOL, by State Insurance Commissioners, by FINRA. We are all talking about how complicated this is. You bet it is complicated. What if we simplified it? What if we used different words? What if we stopped talking about VAs with GMWBs and DBs and started talking about retirement income for life that might go up, but cannot go down. And we talked in terms that people understand so there is the prospect in this environment that we could actually accomplish some real range that would benefit consumers and advisers, make it a lot easier for advisers to do their job.

Andy Hughes (Macquarie): Hi, two questions if I could. And the first one is about kind of if DOL came in and if you were selling fee-based products, the liquid version I guess with limited surrender charges. I got the impression that are not worried about the volumes of that because obviously you got to have an issue of kind of interest rates go up and everyone leaves and you had a big hedging loss. So will you have to constrain the volumes in the new world because you do not have the protection of the surrender penalties that you currently have? And the second question was on the NAIC stuff. So I think you ticked off most of the points on NAIC. So there is just thing you mentioned which was the equity drift, because I think that affects you and probably nobody else because they have volatility adjusted funds where they are all stopped out of equities by the time you get a big equity shock. And I think you mentioned that it might be capped at 200 basis points over risk-free, so I was just wondering kind of what are you assuming currently and how sensitive would that be if it was to reduce to the 200 bps over risk-free? Thanks.

Chad Myers: Yeah so, that on that one, I think that was again they bracketed a lot of things on this. And I am just going off of memory. I think it was 200 over risk-free that was proposed as a potential. The stat is a historic base so I think if I remember off the top of my head I think it is 7.5-ish to think about the mean return on stat. So it would be a drop from where we are today of some amount. The bigger issue is the volatility that introduces and this is the same kind of issues you get in Solvency II. You can capitalise up to a point, but it just becomes a very volatile calculation. Again I just do not really think it is going to go that direction, but that is the answer to the question.

That first one was a good question. So what we do not know yet is what the policyholder behaviour would look like on a fully liquid position. We have some read across that we can get from, you know, Alison mentioned the L-share earlier. Those have shorter surrender charges so we see presumably people are paying for shorter surrender charges. They would be more likely to be liquidating contracts. We also have the post surrender charge experience so we can read across that.

Sort of like with the fund allocations, when people buy one of these contracts they are not really buying it to see can they get a better deal two or three years out typically. I mean if you had a regime change, rates went to 10 and all of a sudden guarantees are free, that is a risk. And if we get some movement, but even there once people are locked into their benefits it becomes a little more complex for them to economically want to move. Number two now in the fiduciary world it is much more difficult to move these policies. So you do have that dynamic as well. But it is one of those things we will take a measured approach to when we want to roll those out.

Barry Stowe: But it is a product that you would hope was purchased thoughtfully; you know that the adviser gave the recommendation thoughtfully. This is not a mutual fund where you are in this one today and you flip in three months and just constantly chasing yield. That is not the role that this product plays in someone's portfolio. And so you would hope that people do not view the product that way. And all the evidence today – and we now we do not have a product without surrender charges – but all the evidence to date is that consumers treat this product differently than they do other parts of their portfolio.

Andy Hughes: Is there not a revised duty for the adviser to phone you up if, a year into the contract, interest rates have gone up 2% or 3%, and suddenly someone else is offering 6% a year for life to switch?

Chad Myers: What is interesting about it from the adviser perspective is, under the new world, they are not going to get a commission for doing it. So, the incentive for the adviser to be more proactively moving policies around is not what it used to be. That is part of why we had the DOL rule to begin with, because having upfront commissions does incentivise some people, who are not doing the business the way they ought to be doing it in the best interests of the customer, to generate more commissions for themselves. I think that behaviour has abated quite a bit, even pre-DOL, from what we have seen in the industry. However, in a fee-based world, flipping from one contract to another does not help the rep, so it has to be very clearly to the benefit of the policyholder for them to do that.

The other thing to mention on that is the pros and cons of having a shorter-dated hedging programme; we are able to adjust for those types of movements a lot quicker. If you said we were going to go out and buy ten- or 20-years puts, if somebody leaves then you have a big mark left on that. We are able to adjust for lapses pretty quickly in the shorter-dated rolling of the contracts.

Lance Burbidge (Autonomous Research): Thanks. A couple of relatively quick ones. For Chad, you talked about making very conservative lapse assumptions on in-the-money contracts, because you do not have any experience. Would you give some kind of quantification as to how conservative you mean, relative to the assumptions you are making on policies that are not in the money?

Secondly, why would anyone buy an investment-only VA, so why are you putting one on the platforms?

Thirdly, you are obviously incredibly enthusiastic, Barry, about the prospects, and this is the only growth area in the insurance industry, if it is a growth area; there is not anything else. Why are your competitors not enthusiastic; would you care to speculate? In fact, they are selling their business, some of them.

Barry Stowe: I cannot speak for why they might not be as boisterous in their presentations as we are today. I think it is a great opportunity for our industry. I think it uniquely positions Jackson because of our unique level of performance, in every respect, through the cycles going back ten years. There are fewer people writing VAs today because there has been drama in the space; not because there is something fundamentally wrong with the product, but because you can make mistakes and not do it right: you do not hedge or you hedge improperly, or you are not disciplined when you define what the benefits looks like and you guarantee income rather than guarantee withdrawals; you know the technicalities of this.

We are optimistic about it because we are very confident in our capabilities. There is no doubt that this environment is emerging, and we do not believe that it is appropriate to step into that space and say, 'We are going to change the world with fixed indexed annuities,' because they do not really do the job. They provide an income, but it does not provide the level of guarantee and the accumulation opportunity that you heard Seth say is part and parcel of the real problem for American retirees. While it does offer some protection, it is protecting people from the modest loss and not from the catastrophic loss. It is like buying auto insurance that pays if someone dings your car at the grocery store, but does not pay if it gets hit by an asteroid. So, it is not providing the right kind of protection.

I think part of why we are enthusiastic is because we feel so incredibly well equipped to deal with the issue. You would have to ask our competitors how well equipped they believe they are.

Alison Reed: Why would someone buy an IOVA? Really, there are a couple of reasons. When you look at our breakdown of the IOVA business, it is primarily a non-qualified sale, so 70% of our total allocation is going to non-qualified in our Elite Access product. So, they are primarily looking for tax deferral and the advantages associated with tax deferral.

A couple of other reasons. One is access to alternatives or non-traditional investments. A lot of the investments on our Elite Access platform, if you go to the retail market you are going to see higher minimum premium amounts to invest; with Elite Access, you can get in at as low as $5,000, $10,000 to some of these non-traditional investment options.

Then also, comparing to a fee-based platform: within the VA wrapper you get free round-trip transfers, up to 15 a year, so a lot of that is cost savings overall for the consumer, because that is packaged into the overall product.

Chad Myers: With respect to your lapse question: it is not a simple one to answer, because obviously models are pretty complex. I would say, broadly speaking, once something is deep in the money we are typically going to be somewhere in the ballpark of a third of the base lapse rate that we would assume. That said, we have overlays or effectively caps on how high lapses can go for deep in the money policies that are getting close to running out of money; those that tend to drop would looking something more like 15%, maybe, of base lapses. So, on some policies they would get as low as mid-1%s, but I would say somewhere between 1.5% and 3% is probably the range where we would get to in deep in the money. That is consistent with old whole life policies, for example: they are not tax deferred, they are tax-free pay-outs; they have 6% interest rate guarantees on them, and we still see 1.5–2% lapse rate. That is a reasonable read-across for something like that.

Arjan van Veen (UBS): On the NAIC changes, it sounds like from your point of view it does not really change the way you run your capital at this point in time? It is not like you are going to err more on the side of conservatism? I just wanted to double-check that.

Then with the asset-based charges changing as of 1st January 2017, do you have any quantum you can give us around that? One of your peers has come out saying it is about a 20–25 points reduction in RBC.

Chad Myers: Yes, what you stated is correct: we are not at this point, based on the NAIC, looking at any changes to the capital regime that we would envision. It is still very early days, so we will see what happens probably mid-next year as there starts to be more conversation around what comes out of the next quantitative impact study, and if there are any parameterisations that start to gel or even what the model looks like.

In terms of the credit factors, I would say that is generally the right range; I think 20–30 points is about where everybody in industry seems to be. Our book is not massively different from the rest of the industry. We would have to look at the portfolio at the time, but I do not think that is indicatively off.

M&G

Anne Richards

Chief Executive, M&G Investments

Introduction and agenda

Good afternoon everybody, and thank you for coming back. I think this is the home straight now although it is quite a long home straight. But I am Anne Richards. I took over at M&G in June. As most of you know I think, some two weeks before the referendum on membership of the EU and as I have said to Mike on a number of occasions I have gone back and I checked my job spec. There was no mention of Brexit in my job spec so it certainly made the initial couple of months a bit more challenging than might otherwise been the case.

In comparison with some of the other technical stuff you have been hearing about from other parts of the Group today, I think asset management is a business you all understand. It should perhaps prove less taxing on the brain cells. It is a relatively simple industry, but that is not to say that is the same thing as an easy industry. There is a lot going on in our industry at the moment. And so over the next half hour or so I would like to give you an update on M&G which will remind you of where our key capabilities and strengths are. I would then like to take that on to cover off some of the cyclical challenges that we face as a business and I shall go back to the agenda so you can see that. Although we are a fee-based business, it is a somewhat cyclical industry, and for reasons which I think it is worth just reiterating or reminding everybody about.

And then I want to go on and then talk about some of the structural changes, secular trends that are affecting the industry and there are quite a few of them. Some of you have written about them. I think when I look at the industry in the last 25 years and probably longer than that we are probably facing the greatest degree, the greatest pace of change in that whole period so I am going to talk to you about how that is affecting the industry and how we as M&G are responding to that. And so I will wrap all of that into where I think the future is and what this means for the future of M&G.

M&G's Key Investment Capabilities

So first of all, what do we do? As is already been mentioned, we manage something like £266 billion of assets under management and that is across a full spectrum of investment capabilities. It includes just about every flavour of fixed income. It includes equity. It includes real estate and it includes a variety of other alternative asset classes. And our fixed income business in particular has one of the deepest benches in the industry, particularly in respect of the quality and the strength of the credit analysis that we perform there. Our equity business, I think most of you will know, it is very fundamentally led. It is bottom-up led. It is very conviction led. So an unconstrained style and it includes a lot of specialised strategies where there are special situations, income oriented or even impact investing.

Our real estate is one of the market leaders. It is expanded its business very successfully from its initial UK foundations, look increasingly to invest in Europe and Asia and North America. We have multi-asset team. It is very long established as a team. It has a top-down approach, driven by really a very innovative use of behavioural economics to inform the positions that we take in funds. And, finally, our alternatives business has a really I think quite enviable track in seeking out opportunities and in some of the harder to access parts of the investment landscape including things like real estate financing, direct lending and infrastructure equity investment.

M&G's investment expertise: supporting the needs of a diverse range of clients

Now across that full spectrum of capabilities, we look at our client base through three main lenses and I will come into this a little bit more detail later on. It is the handy shorthand, but in fact of course, the world is rather more complicated than that. But it is a neat way of just breaking down the book of business that we look after. And, of course, the single largest part of our business is our internal client and you are going to hear from John immediately after me. And I like to say frequently and often how much we love him, how much we love his business. We manage a full range of asset classes for the UK, but also for other parts of the Prudential Group and it is a close relationship. It is one that has an element of a win-win situation to it because it allows us to develop jointly new ideas, new investment ideas, which benefit both businesses.

Rising to Cyclical Challenges

The OEIC range is the major part of retail assets

The next slide which is part of our business is our institutional asset management business and that is around 74 billion sterling of assets under management. Again, it is a very broadly-based, very sophisticated business and it is growing. And finally, in the centre you have a retail business which is roughly 62 billion of assets under management and the majority of that is through our UK domiciled OEIC structures. And although something like 40% of the clients invested in this OEICS are actually based in Europe.

Now as those of you will know who attended our last Investor Day where Michael McLintock discussed some of the challenges that the business was facing, we are in what is an inherently cyclical industry. That is partly because markets themselves are cyclical. It is partly because investment performance is cyclical and is partly because customer risk appetite, as we have seen in the last month or so which feeds into product demand, is also cyclical. And sometimes it is easy to forget in that broad view of the strength of the fee-based business that it does not go up in a straight line. There are peaks and troughs even within that growth trend that we have there. And particularly, I think when dealing with the first of these investment performance, the challenge is always to figure out when under performance is due to lack of skill or when it is due to external style factors, and that really matters a lot because customer behaviour varies depending on which of those problems you have.

Customers are likely to walk if you do not change the fund manager when it is due to the lack of a skill, which is a pretty reasonable position to have. But, conversely, they are just as likely to walk if you do for example, change a fund manager when the issue is actually the external style factors at work rather than a lack of skill. So what we try to do is go through team-by-team, individual-by-individual and work out whether they are doing anything differently to what they have done historically which is leading to underperformance or whether that underperformance is consistent with the factors in the broader conditions in the market. And that will tell you either to take action, which you sometimes need to do or simply do nothing intelligently. And doing nothing is often the hardest thing to do because we are as creatures as humans quite disposed to action. But sometimes patience is the single best investment.

So we have been through that exercise and we have made certain changes and we have looked at where actually what we need to do is simply wait patiently. Now what I want to do is drill down specifically into the open-ended fund range because this has had some focus of attention in the past.

And when you look at these funds we have seen quite significant performance pressure rolling back 12 months ago. If you look to this split by quartile of the performance of our open-ended funds, you could see that only some 36% of funds were above median over one year to the end of September 2015. And that is a pretty tough backdrop to have. But rather more encouragingly if you roll forward to the end of September this year, you can see quite a meaningful recovery in performance over that one year number so that something like 53% of funds are above median so still not quite in the sweet spot which we would like, which would be two-thirds and more. But, nonetheless, the trend is absolutely in the right direction. And it will take time for the one year number to feed through into the three- and the five-year number, just because of the way that the numbers feed through the system.

But it is really encouraging if you focus on that last column there, the fund manager tenure. You can see that an impressive 63% of funds are ahead of the median since fund manager tenure. So I think that is a strong signal that the direction of travel is right.

Pace of outflows from retail funds is slowing as investment performance improves

And therefore, it is not a surprise if you then turn to outflows that, having had a really difficult period through 2015 where we saw that very, very strong pattern of outflows month-by-month from the retail business, that that pattern has noticeably stabilised through 2016 as performance has improved. So it is not quite sufficient yet. We obviously need to get it up to a meaningful and sustainable positive number, but nonetheless it is very encouraging as a picture; obviously a bit of a blip around Brexit. But even then, you can see that that was a relatively short-lived effect.

M&G Optimal Income Fund has led the recovery in performance

Now the single largest open ended fund is the Optimal Income Fund which did have a pretty tough time in 2015. And it has had a particularly strong year and so this is a very, very significant part of our portfolio and it is very important to see this, very encouraging to see this really strong recovery coming through. And I would highlight, if you look at the since-inception number – this is 2007, which was the inception of Richard running this fund – you have seen above 7% return per year over that whole period from a bond fund, which is a really strong add performance from the portfolio.

Market environment has been testing for M&G's equities style for some time

We also obviously have a sizeable equities business as I mentioned already, which is very much fundamentally-driven, very bottom-up driven. And we have also seen fairly strong challenges in performance over the last year. Now there is no single explanation for this, for bottom-up led or individual stock-led. But it is quite interesting if you look at the following pattern.

So here is the yield. You have already seen this. So here is the yield on the US ten year, just as an example, and obviously over this period, since 2002, you have seen those yields fall significantly. If you then plot against that using MSCI data, the value versus quality indexed stocks, for one thing the pattern is as you can see remarkably correlated. And although our equity funds are not simply value biased in isolation, and it will be overly simplistic to say that this explains all of the underperformance, you can see the extent to which quality stocks, strong dividend paying stocks, have been pushed to a premium versus value stocks as they have acted as bond proxies against this backdrop of falling yields.

So we have begun to see a recovery in performance in the equity funds this year and that tally is very much with this uplift in yields that you have seen and this end of the performance of quality stocks versus value stocks in the broader market. So, that has been helpful for us and we hope that that trend will continue.

M&G's institutional client base

If we then move on to the institutional client base, and this is something historically which we have probably not talked about as much as we should have done as a business, it has quite a different mix of assets to our open-ended funds because it is much more heavily orientated towards alternatives, towards alternative fixed income and towards multi-asset portfolios.

And if you look at the five-year track record of both the real estate funds and the fixed income funds that we run in all the different varieties within the institutional business, those of them that have benchmarks – and there are some absolute return targets and do not have specific benchmarks – but those with benchmarks, all of them without exception have outperformed over that five-year period. And with that performance backdrop, you can see how that is been reflected in the performance of the institutional assets under management, where we have gone from something like £14 billion back in 2003 to well over £70 billion in 2016 so a five-fold increase, give or take, so quite a strong and impressive performance in that.

If you look at the top right, this is our pipeline. This is mandates which we have been awarded, but they have not yet been funded, or where we had capital waiting to be deployed as the right investment opportunities come up. And we have got something like £4 billion of a pipeline, awarded mandates not yet deployed and across the whole range of different asset classes within this broad institutional business. So very encouraging in terms of the flow that we see coming through over the next 12 to 18 months or so.

On the bottom right, you can see our client base quite spread and is probably will not be a surprise to you to see that it is still dominated by the UK. But we are increasingly seeing signs of interest in the different strategies that we offer in Europe and even further field in Asia and occasionally in the US as well. All interested in these somewhat more esoteric strategies that we have to offer.

But to give you a feel of how we are ranked in the institutional space, particularly in the UK, we manage money for something like 32 of the top 50 UK pension funds and we have something like £3.5 billion of assets from third party European insurance companies. We have won multiple awards in both fixed income and real estate, including this year the Fixed Income Manager of the Year at the Local Authority Pension Fund Investment Awards. So it is a really strong part of our portfolio and is one we probably spend more time talking about.

Adapting to Structural Change

Changing demand leads to strong growth prospects for alternatives, solutions and passives

If we then move on to some of the secular, the structural challenges, which the industry is facing. I think that most of them will be pretty familiar to you. And the first one is a chart that many of you will have seen before on many occasions I am sure. But if you roll back to 2003 and you looked at how the global assets around the world were distributed by product, active core, whether in equity or in fixed income, was well over half of the typical asset breakdown that you had. You had something like an additional 20% and different types of specialty active and relatively modest amounts at that stage in alternatives, in solutions and in passives generally.

Roll forward to 2015, and the picture is very, very different. So that core active part has slipped to less than 40%, and you have seen the growth over that period in passives and ETFs, which has almost doubled, and alternatives which is up some 70%, and in different flavours of solutions capability which has more than doubled as a proportion of the assets invested around the world. These are BCG numbers by the way, but on the right-hand side we have the projection of how that is likely to be shaped over the next three or four years, and most projections – this included – show the trend very much continuing, with flows into solutions forming about half of the effect, passive over 40% and alternatives almost a third. As you will have noticed, that does not add up to 100%. Where is that being sourced from? It is being sourced from that core active piece. So, the industry is changing. It is changing quite dramatically, and we have to respond to that.

Global asset management industry faces margin pressure with an increased focus on costs

The effect of this changing shape, this changing pattern, has begun to feed its way through to pressure across the industry on margins, and dealing with that margin pressure is one of the hot topics around the industry talking tables around the world. You can see in this chart the net revenues, which is the green bar, where have seen back in 2007 the average revenue fee basis points were a little below 34 basis points. That has shrunk to just under 28 basis points currently. That has partly been a mix effect. It has partly been increased pressure for rebates, for example, for intermediaries but it has had that effect of pulling down basis points and revenues.

The industry has probably been better than generally advertised at managing its costs in response to that. Back in 2007, costs were just over 20 basis points on average, and that is now down to about 17 basis points. As a result of that the margin, although it has slipped – which is the orange line that you can see across the top – from a 40% average operating margin across the industry to something like 37% today. Nonetheless, that pressure has been clear, despite the fact that global assets have been rising across the board. Another feature which I think is part of this pressure is that we have definitely seen higher churn across quite a lot of the investment book as an industry over this time period. That is the first secular challenge.

More complex distribution landscape

The second secular challenge has been the increased complexity of the distribution landscape. If you went back 25 years, we had a relatively simple world which could be divided neatly into direct to customer, billboard advertising, Tube advertising, retail and institutional, which was predominantly dominated by defined-benefit pension schemes. If you look at the landscape today, and this is an attempt to draw this picture with end customers along the top and with different flavours of intermediation along the bottom, you can see the whole range of different flavours of intermediation which come between us as asset managers – in the research that we do, in the portfolios that we manage and in the wrappers that we put around those products – before it gets to all of those different individuals. That chain, of course, is partly led by regulation, but you can also see where the pressure on the whole cost chain has come from, because suddenly there are an awful lot more parts which have to be fitted into the same fee base.

So, it probably does not cover all of the nuances that are out there, but it does show you that, in dealing with this, we need to get more sophisticated in the way we look at and choose how we distribute into this environment.

Wave of regulatory development

The third challenge, which I have already touched on a little bit, is simply the tidal wave of regulation which washes over us on a fairly regular basis. I would struggle to explain to you what each and every one of these abbreviations stands for; I hope there is somebody in the room who could if we needed to do that. However, this alphabet soup that we are all dealing with, all of these things touch asset managers in one way or another, intentionally or unintentionally. All of these different regimes and regulations have to be evaluated and managed within the business. There is no sign yet that this wave of regulation is going to stop any time soon.

Of course, sometimes these regulations do collide in unanticipated ways. As an example, PRIIPs, MiFID and AIFMD all have somewhat slightly different interpretations in things that we had to do, in terms of the way we communicate with our customers. Too often, the regulation that comes to us is internally consistent in terms of solving one particular problem, but not necessarily joined up, and there are unintended consequences of that.

Developing new capabilities led by investor needs

Those are the secular challenges; what do we do to respond to them? The first thing as an asset manager that you have to do is keep finding new capabilities that meet specific customer needs. In particular, in this environment where there is pressure and there is competition, they have got to be capabilities that are relatively hard to commoditise; things that somebody actually cannot just turn into a passive product if they want to. To do that, you need to know your customers' problems very, very well, because that is how you can work out what it is you can do that can meet their needs. Distressed debt is one example of that; you cannot hurry work-out situations, you need a lot of patience and a lot of expertise to be able to unlock the value that can sit, sometimes within quite difficult situations. Private debt is another example of that; direct lending is another example.

M&G Inflation Opportunities Funds

I am always nervous in a forum like this, because I know there are direct competitors potentially sitting in the room here, but I did want to talk through one very specific example of what I mean in terms of strategies that add real value and meet particular client needs.

We have a strategy, a capability, called Inflation Opportunities Funds, it was launched in 2012. It currently has an AUM of just under £2 billion, and it consists of two co-mingled funds and three single-investor funds. It is essentially a very, very long duration fund, looking at a duration of 15–20 years. It targets RPI +2.5% on a rolling basis. Its remit is very wide-ranging; it is essentially a multi-asset fund, but a multi-asset illiquid credit fund that can invest in a range of assets, but the asset has to have a contractual link to UK inflation. So effectively, what clients are doing is giving up liquidity and taking credit risk, but in return for generating a higher return and, in particular, meeting their inflation liabilities. This is a product for a UK pension fund, for example, that has long inflation-linked liabilities and is a long-term investor so can afford to give up liquidity. It is a perfect match of a product and an individual investor need.

When you look at what actually sits in the portfolio, there is a broader point which is interesting in this respect. If you look at these different assets, this gives you a flavour of the sorts of things that we are talking about across what is a very diversified, multi-asset credit portfolio. Drax power station: we loaned Drax the money to finance the conversion of three coal-fired businesses and convert them to biomass. Sainsbury's, there: we bought the Dulwich site from them, and we have leased it back to them on a 25-year lease. The Shoreditch and Islington Housing Association there: we loaned them the money to finance a portfolio of social housing, much-needed social housing in the area. In the top right, you can see you Royal College of Music. We financed the build of student accommodation there, complete with rehearsal space, performance areas and – they did not tell me this, but I am assuming – really, really good sound insulation. We leased that back to the Royal College of Music for 45 years. The final one on the bottom right, Lighthouse Solar, is project finance for a portfolio of solar parks which provide clean energy to something like 30,000 homes a year. That particular deal won a whole host of different awards: the environmental bond of the year, the best European solar deal of the year and so on and so forth. It was highly commended for Infrastructure Investor's deal of the year.

I think this is interesting, because it is not just that this is matching a need for the clients. There is a lot of talk: the government has a lot of talk in this area at the moment, and everybody wants to be seen to be doing infrastructure investing, but nobody is quite sure what it means. This is the kind of stuff, actually – investing in real, meaningful infrastructure that benefits society, that has a real meaningful impact on society as a whole – that we want to do more of. It is about being that intermediary between a societal need and an individual need for investment opportunities, and marrying that up with the pension funds, for example, who have the asset base that can make it happen.

However, it is not enough just to have a good purpose in something like this, of course; the key is, actually, has it done the business? As ever with something like this, we are talking about four years; this is not the entirety of a cycle. However, the performance has been absolutely excellent. You would not expect me to show rubbish performance for the case study that I chose. Performance is good, it has comfortable beaten its target. Importantly, if inflation does pick up then this should be a really important part of client portfolios.

You can see that that strength of performance and that client need has been met in the way that the assets have roughly quadrupled over the four years that it has been in existence. So, it is one example of how we try to protect our top line, by developing really strong, good, innovative products to meet this changing backdrop that we see in the industry as a whole.

Simplification and scalability are key to meeting industry-wide margin pressure

However, of course, that is just one side of the equation; we also have to manage our costs. It is not just about growing the top line; it is about managing the cost line as well. I do think that, as an industry, we are remarkably analogue in our approach, and we have been for many years. We have been very slow to adapt in the industry to some of the changes that some of the other financial sectors have actually been ahead of us in terms of moving forward on. We have to simplify what we do, and we have to make it scalable. We have been awfully good as an industry at making things very complicated, and we are now going through the stage of unpicking that. Guy earlier mentioned target operating models; absolutely the buzzword of the moment. It is all about streamlining, simplification and scalability. That is the key to growing through the cycle.

Adapting distribution to meet increasingly complex customer channels

So, what are we doing within M&G to address some of the cost challenges that we have? Well, I break this down roughly into two main families of things – this is not all that we are looking at, but here are two important parts of what we are looking at. The first is the data and the digital agenda.

We have mentioned Aladdin this morning already. It is a very important part of what we need to do. I think Mike was saying that he had an email from somebody who may or may not have been a fund manager at BlackRock possibly commenting on that saying, 'Yeah it is not all it is cracked up to be.' I think it was tongue in cheek, it is really good. Actually, it is not actually just about that front end and how it touches the fund manager that makes this really interesting. It is much more about what is happening beneath the bonnet of it all. Guy talked about the plumbing, and the plumbing is really important in all of this. We have a bit of a Heath Robinson style of plumbing across most of our businesses – sorting that out, streamlining that, getting the pipes in nice straight lines – very, very important that we do that.

But the plumbing is not just what it is about. If you think of a plumbing system, the normal thing that flows through the plumbing is water. Well, our equivalent of water is data, and too often we have not worried enough about whether that water is clean and pure and fit for purpose. We have just stuffed the data down it and then manipulated it every time it pops out of a leak somewhere here or there, mess around with it, stick it in a spread sheet – that is all horrible, horrible stuff. Aladdin gives us a much cleaner data set, which then has the effect of radiating out across our business and making our operating model much simpler as a result. And we think that within M&G, as a result of the Aladdin implementation, we will reduce the number of systems that we have to mess around with all this data in different ways, from something like 600 to 300 or perhaps even less. So it is a very meaningful change to the way our whole operating infrastructure works.

I mentioned a few other things up there as well that we are touching on as well, looking at how we design and maintain our website, at how we designed and maintained our whole suite of things around the way we send information to customers and the marketing plans that go around the way send information to customers and the marketing plans that go around about those very, very important things, and simplifying our business and making them much less onerous to maintain and manage.

On the right-hand side, this is how we are trying to use Brexit as perhaps an opportunity to simplify our business rather than just thinking of it as an additional cost, which it is tempting to do at different moments in time, particularly when we have no clear view of what Brexit is actually going to mean for the fund management business. But it is giving us the opportunity to develop and integrate this new operating model into a single super ManCo in Luxembourg, which we are aiming to do, which will simplify and streamline all of our fund offering. And that will include the establishment of a Europe ex UK MiFID company to be the management company of all of that.

So, as I said, we do not know all the detail yet, obviously, of where the Brexit negotiations are going to get to in terms of what passporting regime we will have, for example, but what we do know is that we will create through this mechanism the options that we need to have in the business, the optionality in the business, to allow us to respond to whatever finally comes out of the negotiations.

And if you think back to that slide that I showed you about the increasingly complex distribution world that we live in, we are looking at how we can adapt what we do internally to map better onto that very complex set of slides about the different touch points we can have with different sorts of institutional customers, different sorts of intermediaries, platforms and the end customer. So we are thinking more about sub advisory opportunities, we are thinking more about how we can do joint product development with our customers along the lines of the inflation-linked fund that I talked to you about, we are thinking about digital distribution, what that means for our business, and lots of conversations going on in that area at the moment; nobody seems really to have cracked it. We are thinking about strategic partnerships and of course thinking about the implications of what Brexit are for the way that we manage and shape our offering to the outside world.

We have also announced that we are aiming to launch in the next couple of months two new funds in the new SICAV account that we established in Luxembourg, so we are, as I say, continuing to generate momentum around the Brexit opportunities that come from that.

The regulatory tide shows no sign of turning

And then the final part of the secular challenge is around regulation. And as I said, the tide shows no sign of turning there, but there is not really a great deal of point to sitting and lamenting about it. Our aim, really, is to engage constructively with regulators and policymakers wherever we can, trying to point out the unintended consequences of what they might do, but we are deeply engaged in a number of different conversations around some of the proposed changes to different parts of the market in different ways, and we intend to keep on with that.

Now, the regulatory trend does bring us, I think, towards increased complexity. It does, in general, give us a greater administrative burden, and I am sure that will be familiar to everybody in the room, because the trends tends to be that if you cannot evidence that you did something right, the supposition therefore must be that you have done something wrong. However, it is the world we are in. There is no point in worrying about it, we just have to try and get on the front foot. So very much trying to be constructive and trying to get ahead of the game where it is appropriate to do so. One of the examples of that is that we were one of the first companies to say that we would take the costs of research directly onto our own P&L. That became really a totemic issue across the industry. And we will try to the best extent that we can to maintain that positive relationship, and I think welcome any moves towards harmonisation and towards improved transparency that come out of the regulatory frameworks as they develop.

The Future of M&G

So that is a bit about the structural change. Where do we go from here? Well, I think it is really important not to lose sight of the fact when we think of some of these things that are going on as a backdrop that notwithstanding the fact there is some cyclicality to the industry, it is a growth industry. And there are not so very many industries that have the potential to grow in the way that asset management does, so we must not lose sight of that. The prospects for the industry as a whole, I think, remain extremely good. But we have to focus on what we need to do to succeed in this environment, and I think for any fund management company – for any company of any sort, in fact – it is all about thinking about what is the capability that you need to meet the customer demand. So if you speak to a Google or a Facebook or any of the tech companies, their first question is not how much you make out of a product, their first question is, 'What is it that is an untapped need that is out there, and what can we do to fill that need?' And that has got to be our starting point for how we think about engaging with our customer base and what we need to develop strategically as we go forward.

The keys to M&G's continued success

Clearly, we need to keep delivering investment performance and it has to offer value for money for customers, and it has to meet customer expectations. We live or die by that. We have to align our distribution with this rapidly evolving customer base, and think about how we can change it in order to meet the many new, different and complex routes to market. And if we are to do the fourth bullet point correctly, we need to do it through investment and simplification and scalability. And I think as an industry we have probably underinvested historically in some of the areas that we are now playing catch up with. But the other side of this, I think when you look at fintech, when you look at regtech, when you look at some of the really quite exciting developments which are coming out of this new world and landscape that has developed over the last four or five years, we do have the potential to leapfrog some of the really scale investments that we might have had to do ten years ago if we were making the sort of difference to our infrastructure that we are now talking about doing today. I think we can leapfrog some of that, and that is an advantage, but it is going to cost money.

So what does that mean in terms of numbers and margins? Well, you would not expect me to give too many forward-looking statements and I certainly will not do that, but M&G has historically had a pretty competitive cost-income ratio by industry standard. We estimate the peer group average is something like 62% and we typically come in underneath that. Last year the number was 57%. But because we are going to be reinvesting in the business, we are likely to see pressure on that cost-income ratio, so what we are aiming to do and what we are talking about internally is our aim is to keep that cost-income ratio on average below the peer-group average on a through-cycle basis, but we do it with the knowledge that we must invest now in order to create the scalability of the operating platform in the future. And there you can see what our trend has been historically over time.

Concluding Remarks

So just to finish, then, I think M&G has a very long tradition of creativity in the investment management space, and we need to keep developing those capabilities to find ways of converting the ideas into really practical vehicles in which our clients can invest. We have no shortage of channels where we can see a client need, and what really our challenge is how we prioritise those. It is not for want of choice or things to do. So continuing to capture that spirit of innovation, which is very much alive I am happy to say, in M&G, which is actually its history – its DNA. That is really going to be key to our success going forward and that is absolutely front and centre of our mind as we go into 2017. Thank you, and over to John.

Prudential UK

John Foley

Chief Executive, Prudential UK & Europe

Opening Remarks

Thank you, Anne. Thank you for those really kind comments about the internal client. £120 billion buys a lot of love. Good afternoon, ladies and gentlemen. It is my great pleasure to be joined on the platform by John Warburton, who leads our distribution effort. We are your double act for this afternoon. For Q&A we will be joined by Jeremy Deeks, who is the recently appointed CFO for the UK insurance business.

Now, I met many of you at the last investor conference – so this is Investor Conference 2016 Part 2 – when it was day one for me on the job. A number of things have moved on since then, but as we go through this presentation I hope you will note that the strength of our business continues to be demonstrated by our results, as well as the progress that we are making to reengineer our operating environment.

Agenda

So, this is our agenda today. There are some key messages I will highlight on the first few slides, and then I will hand over to John Warburton to explain and update you on the proposition, distribution and our new business performance. He will also show you a short film that we use internally at Prudential, which will provide more colour on our direct and intermediaries channels. This will give you an insight into why many of our partners and employees value working for our Group. And I will come back towards the end to talk about the work we are doing on our operating environment.

The Cornerstones of Prudential UK

Now, before we move on, I think it is worth reiterating a few truisms about Prudential UK. We discussed them in January, but they are the cornerstone of how we think about our business and our role in the Group. The UK continues to be a cash generative business. The back book is important to that cash generation, and we will cover this in more detail in this presentation. The recent changes in our marketplace offer a business with our unique combination of capabilities a new and significant opportunity for profitable and capital efficient growth. As John will explain, this business is already demonstrating strong customer-centricity, validated by excellent retail growth, and this is the cornerstone of what we are doing.

Prudential UK's three key capabilities

Now, three key capabilities underpin our ability to capture this opportunity. The first is our life fund, and particularly our unique with-profit PruFund platform. Over time, we have broadened to six different funds, all accessible through Isa, bond, pension and drawdown wrappers. We are enjoying superb growth in PruFund new business across all these wrappers, as you will see shortly.

The second is our outstanding long-term investment performance. Over the long term, our with-profit fund has outperformed the market consistently. The average return of our life fund over the ten years to last year was 6.1%, and total AUM at that point was £116 billion. Around a third of all with-profit assets across the whole market is represented by this fund, and it could be said this is the only life fund left in town. And crucially, this performance translates into materially better outcomes for our customers – that is why we are here.

Third, our market-leading distribution capabilities. Through the combination of our intermediated and direct channels, we have not only weathered the changes brought on by RDR, but have executed on a plan to grow and strengthen our franchise.

Our intermediated model is rightly admired in the market, and has built up on a first-class service and capability. Allied to our Prufund proposition, our intermediary business has gone from strength to strength, doubling sales volumes from 2013 to reach £640 million APE in the first nine months of 2016. Now, in order to sustain this momentum, I have hired a new management team to re-engineer the operating model for our business. This is providing capacity and capability to ensure the continued success of this operation into the future. Those are the main messages that I want to share with you this afternoon.

UK&E Business and Capabilities

We showed this slide last year, but I think it provides an excellent recap of what our business is about. Pru UK is a significant operation, with over 6 million customers, for whom we have delivered excellent investment returns over the medium term. In doing this, we leverage other group capabilities, including, as you have heard, M&G, Eastspring and PPMA. Note that Eastspring and PPMA did not thank me and show me much love. We will come back to that. Significantly, also, PPMG; this is Prudential Portfolio Management Group, and it is PPMG that develops the strategic asset allocation for over 150 billion of these funds, and is the source of much of the performance success.

Prudential continues to prevail as the leading retirement and savings brand in the market. This brand is extremely important to us, and clearly the Man from the Pru has not been forgotten. As I have already said, we have great intermediated distribution capability, and now a growing advice channel in PFP. Finally, our financial strength. We deliver strong and predictable free surplus and cash generation, underpinned by our with-profit fund. Even in today's Solvency II capital regime, the with-profit fund is highly efficient, and through this fund, we will continue to write new investment business.

Our model

Our model has not changed. This slide covers the two key segments: retail growth on the left, and the management of the in-force business on the right. Absolute focus on the segmentation will ensure we continue to deliver our strategy consistently over time. Today, we are going to focus on retail growth, which John will cover in more detail. In-force optimisation, as you will guess, is about making sure we use our resources appropriately, and with the right focus to deliver value for customers and shareholders.

You will likely have questions regarding our plans for annuities book. Our thinking regarding annuities is evolving, but our stance for the moment remains unchanged. Simply put, under Solvency II, the economics of writing annuities business does not work, at least for us. Nic and I have covered this repeatedly, but to quickly recap: the capital intensity makes little sense in the context of opportunities that we may have elsewhere in the Group. Even with reinsurance and other management actions, when combined with this ongoing low-interest-rate environment, this is not an attractive new business opportunity for us. However, we do continue to see substantial scope to create additional value from the back book, in terms of investment optimisation, and we continue to make good progress with that activity.

Today, most of our focus is on the success we have been enjoying in our retail growth business, and the value that that is creating. That seems like a good moment to pass over to John W.

Retirement Market Set for Sustained Growth

John Warburton

Executive Director of Distribution at Prudential UK & Europe

Market Opportunity

Thank you, John, and good afternoon, everyone. As John said, I am going to focus on the retail growth strand of our participation strategy, and I thought the ideal place to start really was the market opportunity that we see, and what is driving that opportunity. You will have seen from the results that we delivered in 2015 that we have had excellent sales growth. I am delighted to say you will have seen from the numbers today that we continued that momentum into 2016, and this slide encapsulates the opportunity that we are seeking to address in the market.

We are targeted on the over 50s in the UK; our brand plays particularly strongly with that group of customers. It is a very large cohort of customers in the UK market. They do own and control over 70% of the liquid assets in the UK. As you will see, because of our own baby boom here in the UK, that cohort is set to grow by 1.3% CAGR over the period to 2030. Just to give some sort of context there, that is equivalent to the growth rates at an aggregate level you see from developing economies, so it is a large growing customer base that owns a significant proportion of the liquid assets in the UK.

Structural changes

We are also seeing some structural changes in the market. You will be well aware of these. That is the transfer from state and corporates to personal ownership in terms of risk. We are moving increasingly to a situation where individuals have to be able to manage and take responsibility not only for their own savings, but actually the investment risk, the longevity risk, and the inflation risk as well. Overlay on top of that pensions freedom, which has no doubt given a lot of freedom and flexibility to UK consumers, but with it a lot of complexity and responsibility as well. That is driving a huge demand from consumers in the UK for flexible solutions that enable them to meet and manage the risks that they have. That is the need, that is the opportunity, and we have indicated in the centre of this chart the sort of growth rate that we think you will see emerging within that market segment over the next few years and actually well beyond that point, driven by those underlying.

PruFund Range

A unique customer proposition

That is the opportunity; how have we leveraged it, how are we delivering the results that we have today, and what gives us the confidence that we can continue to do that? The first one is around the proposition. PruFund is a unique proposition in the marketplace. What we have outlined here are if you like some of the key features that really make it stand out in the marketplace. The first point to make is, PruFund is not a single fund. We have a range of PruFunds that are available. That range of PruFunds covers the risk-reward spectrum, and they enable advisers and consumers to choose the fund that is right for their appetite for risk and also their capacity for loss, as well. That opens up a broad part of the market for Prudential. The second one is the diversification, so PruFund is a hugely diversified fund, it is a multi-asset fund, it has 25 different asset classes that is diversified globally. The third one – and John has already alluded to this – is actually the asset allocation capability through PPMG, Prudential Portfolio Management Group, which has been recognised as an award-winning and leading multi-asset management capability. The final element – and a critical element – is obviously the smoothing that we can offer, with it being in the with-profits fund, which is really important to consumers who are in the latter stages of accumulation and then moving through into decumulation and seeking to take their retirement income.

PruFund investment performance

You can see that actually, that has not come at a cost of performance. Here, we demonstrate – and I think Mike had this in his opening slides, as well – that actually, PruFund – we have taken the growth of PruFund here – in absolute terms has delivered really strong performance for our customers, but has also, through the smoothing mechanism, done that in such a way that it has taken a lot of the volatility out of those returns. You will all be aware of the debate that was raging when freedoms first came in and income draw-downs started selling, about the sequence of returns and the impact that has on individuals as they start to draw down the income. Again, smoothing can play an incredibly important part in terms of helping the consumer to mitigate those risks, as well, so PruFund: incredibly important.

Growth in AUM, policy count and proposition development

The evolution of PruFund; so, this was not an overnight wonder. It was not an overnight success either. It has actually been 12 years in the making. As I say, there has been an evolution and innovation in terms of how this fund and range of funds have been developed, and how we offer them to the market as well. It actually goes back, it pre-dates this. We first launched in 2004, and that was with PruFund Growth through a single-bond wrapper, which was at that point in time called Prudential Investment Plan, which was an onshore bond. It was a single fund in a single wrapper without a track record, and made little or no traction at that point. As we started to establish a track record, it started to grow slowly, as you can see at the start of this chart. We then expanded the range on offer through the launch of PruFund Cautious, and you can see the first real tick-up that we are seeing in sales delivery here, and the performance track record is building throughout this period of time. We then added the Risk Managed range to cover that spectrum. We added additional wrappers on to that. Then more latterly, we made it available through an ISA, an incredibly important financial planning tool. More recently, we have actually made it available through our new Retirement Account, which is our digitally enabled offering into the marketplace. Through that series of innovation and development, we have been able to drive the type of growth that you have seen in the assets under management here, taking it today to, as you can see, at least at the nine-month point, £22.8 billion. We have really seen it grow over the recent past.

PruFund inflows: diversification and fall in proportion guaranteed

From an overall business model point of view, though, the other thing that has happened, through that development and evolution and meeting a wider range of needs, the shape of the business has changed materially, as well. What we are showing you here on the right-hand side is, if you wind the clock back to 2011, what you saw was over 90% of our sales were through bonds, 75% of those sales had some form of protection guarantee attached to them, so quite a concentrated portfolio. What you have seen through that development at the end of the nine months in 2016 is a much better balanced portfolio across that range of wrappers, meeting a range of needs, and the other thing is, only 5% of those sales now have a guarantee or a protection on. That has not come at the expense of growing sales; you have seen the exponential growth in sales, but that reduction means that it is not only more or less capital-consumptive because of lower guarantees, but actually a much better balanced portfolio, as well. That is the proposition.

Distribution

Multi-channel distribution capability

How do we bring it to market? We bring it to market through a multi-channel operation that we have. We have four routes to market, which is through independent advisers, third-party advisers; through our own advice business, Prudential Financial Planning; through our own retail voice contact centre; and finally, in the workplace, through our corporate pensions division, as well. The two key drivers of the retail growth that you are seeing are actually own advice business, and through third-part intermediaries, as well. PFP, a brand-new advice business, so we took a contracyclical view here, so when the retail distribution review was landed, we saw it as not only a threat but an opportunity to actually develop our own advice business, because we did anticipate the market would shrink in terms of availability of advice, and in fact it did, as you well know. We created PFP, we built it organically from zero, we have grown it to a situation where, as you can see, at the end of nine months, this year, we had 269 advisers; we refer to them as partners. Actually, we have grown assets under advice to £3.6 billion at that point in time. These are employed by Prudential, they operate under our risk framework. This is a robust business delivering a quality service to clients, meeting their full financial planning needs.

Number of adviser firms dealing with Prudential

In terms of the advice market, so this is third-party intermediaries, we are seeing really strong growth, that John has already alluded to there, because of the strength of the proposition that we have to meet a real customer need. We are really playing into that sweet spot of what customers are looking for. You will see the market generally – and we were in line with the market after the introduction of the retail distribution review – declined in terms of number of advisers. The number of firms that were supporting us declined in line with that. What you have seen since then is that we have more than rebuilt that supporter base, so we have grown it by a CAGR of 12%, so 39% more advisory firms are supporters of Prudential today than they were in the year immediately following the introduction of the retail distribution review. Not only that, but the penetration has increased as well, so if you roll back to 2011, 44% of our advisory firms were recommending Pru for one product, or more than one product; today, 60% are recommending us for more than one product, so we have not only expanded the support base, but we have deepened the support base, as well, and that has come as a result of the innovation that I spoke about before in relation to PruFund.

With that, I think we will now cut to the film that John alluded to as well, and you will see the power of the proposition and distribution, and what advisers and our own colleagues think.

[VIDEO]

Sales

You heard there the strength of the proposition, the strength of distribution, the strength of the brand, and what we have delivered to the market and to advisers' customers as well. All of that has translated into the growth you have seen. In the first nine months of 2016, we sold nearly as many retail products as we did in the whole of 2015, which was a high bar for us at that point in time. You can see that continued momentum into 2016, a CAGR at 60% since pension freedom was announced.

Retail Growth Sales

How has that been delivered? It has been delivered through a broad base of the product wrappers. This is showing you what we refer to as our retail growth portfolio in terms of the product wrappers, and what you are seeing is really strong growth right across it, from bonds, where we are already the market leaders in bonds; we have still seen strong growth of 19% CAGR over that period. In individual pensions and income drawdown, where we have really seized the opportunity that pensions freedom created to fill that customer need, we have seen CAGRs of over 100% in both of those product ranges. Again, in PruFund ISA, since we have launched that, we have seen a CAGR of over 100%, as well, so really strong performance across those.

Growing Share of the Retail Investment Market

We do not target market share, as you have heard. Similar to other business units, we are about value rather than volume, but actually, this is an out-working of that, and it shows that our relative performance in the market has been incredibly strong. In the total market that we participate in, we have grown our market share by 60%, and in the two growth engines of income drawdown and individual pensions, you can see that we have tripled and quadrupled our market share respectively since pension freedom was announced. That has not come at the expense of value, and I will hand back to John on that note.

Financials

John Foley

Chief Executive, Prudential UK & Europe

With-profits and PruFund Range

As we have said, retail sales and retail new business EEV profit are growing at over 40% year on year. We have delivered this growth while maintaining our retail new business margins, so volumes have increased but not at the expense of one of our key metrics.

This is a busy slide, but on the left-hand side of this slide, we show an acceleration of the value creation through PruFund. Turning to the middle part of the slide, the red segment shows the value that has been added to the existing shareholder transfer from the with-profit business. The light-red segment on top, so the pink-ish bit, represents potential shareholder value creation from future PruFund new business if we continue to grow the business broadly in line with market. Now, this is a projection based on a straight 7% per annum growth in PruFund new business from the start of 2017 onwards. This is of course indicative only, but it is a reasonable view of what might be achievable given the strong underlying market growth. That is the best we can do in response to the question that we have been asked about the outworking of IFRS in the with-profit fund, without making any solid predictions. As I said earlier, the UK continues to deliver cash remittances to group, and what you can see here is that we will continue to benefit for years to come from the business growth that we have delivered to date.

Re-engineering Our Operating Model

Now, as John has highlighted, the success of our retail growth strategy continues, but to maintain momentum and also to execute the second leg of the strategy, which is around cash and in-force optimisation, as I said, I have recruited a new management team. Some of these folks have been with the Pru a while and have transferred into the UK business, and some with specific skills and experience have been hired from the market.

You may have seen some of these appointments being announced, but I wanted to draw your attention just to a couple of the roles. The latest recruit is Clare Bousfield; she is the CEO of our Insurance business, and brings a wealth of experience in the insurance and financial service industry more widely, and we are delighted to have Clare on board. We are delighted to have all these folks on board. Given our large legacy estate and our 18 policy administration systems, I recognise the need for external expertise to accelerate our infrastructure modernisation and change agenda. I hired Steve McGregor as our Chief Transformation Officer, a role he absolutely nailed when he was at Commonwealth Bank of Australia; no pressure on Steve.

Summary

In summary, our performance for the first nine months of 2016 demonstrates the strength of our business. As we said in January, by focusing on retail growth and in-force optimisation as two distinct segments, we have a clear model on which to drive forward. The customer proposition and demographics are supportive. Our brand is one of the best in the financial services industry, and our product range is in the sweet spot. My view is that this is a great business with great people, but we need to relentlessly focus on our customers and use our core capabilities, notably the key assets of our life fund, our strong and diversified distribution, not forgetting our investment performance. We can continue to deliver value for both our customers and our shareholders. Thank you very much.

Q&A

Jon Hocking (Morgan Stanley): Two questions, please. First of all, are PruFund sales constrained in any way by the strength of the fund? Obviously, I think you have done fabulously well in maintaining the stability of the with-profit fund over many, many years. Are these sales actually adding to the estate over time, and is there any upper constraint on what you can sell?

The second question, just on the brand. The brand is obviously very resonant; people remember the Man from the Pru. Given the Group has been on the back foot a little bit in terms of advertising and profile of the market over the last ten years, are you worried about the relevance of the brand to people in their 20s or 30s or 40s?

John Foley: The brand is extraordinarily resilient. One of the first things I did when I joined was I went to visit our operation in Warsaw. They still refer to a building that Pru occupied before the war as the Pru Building, and there is no signage on this building; it is extraordinary. It does resonate. Do we need to do something about that and refresh? It is certainly in our consideration, yes. We do not feel the need to spend a lot of money on it, but there are some things we think we can do, and we have a new brand proposition that we are just bringing to fruition in the next couple of months, so you should be seeing some more activity in that space.

As to constraining PruFund, the short answer is, not really. This fund has been going a very long time, but the rate of growth is not causing any particular strain or drain in any particular asset segment, so no, we do not see any constraints around the growth of that and the ability to outperform, but we do keep a very close eye on it, and one of the key metrics for us obviously is the investment performance and how we manage that.

Lance Burbidge (Autonomous Research): First question is for Anne on broad investment. Are we going to see quite a lot of global offices opening? A certain Scottish insurance company did a similar kind of thing, so I just wondered whether that was what you were thinking about?

There was a slide on the remittances from the UK business, and there was £131 million in 2015 from non-shareholder transfer. As far as I am aware, PRIL has not ever paid a dividend. Could you just explain what kind of products that is coming from, and are they in run-off or not?

Anne Richards: I would be surprised to see a swathe of global offices. One of the great things about being part of the Pru is there are lots of offices around the world if we ever need to go and park ourselves in them. We have a strong European network, and there is clearly a lot more potential for us in Europe. I am just back from a week in Asia visiting our operations out there, of course, dwarfed by the sister company Eastspring. I think you will see us use existing infrastructure rather than feeling we have to go out and take lots of fantastic new real estate around the place.

Jeremy Deeks: In terms of the non-with-profit transfer and where that cash is coming from, the PRIL book has been reassured into PAC for a while, so actually, that money is coming from run-off of annuities and the rest of the book coming through as cash remittances, and coming through up to the centre from there.

Andy Hughes (Macquarie): The first question was also on the cash flow. You have obviously seen the fund merger between PRIL and PAC, and there is a £1.3 billion dividend being paid to PAC from PRIL. Is any of that going to emerge as shareholder dividends from PAC, or does that stay in PAC or is there going to be a knock-on dividend to shareholders of an exceptional nature from the UK business as a result of the fund merger?

The second question is, I guess when I look at the PruFund sales and I compare them to the retail APE growth for the nine months, it is sort of 715 versus 652. Does that mean that nearly all the sales in the UK are PruFund, and basically only 60 million APE of other stuff? Presumably that is not the long-term situation.

The final question on PruFund. Thank you very much for the chart on page 14. As I understand it, PruFund only pays profits to shareholders when people take money out of the fund, and that means you have this very back-end-loaded profile, which I guess in IFRS terms does not look quite as attractive as other things. Is there a possibility to finance against the bonus payments in PruFund, given this delay versus what you would normally have on a with-profit contract where some of it was realised for shareholders much earlier? Will that give you more freedom in terms of the UK business to grow in other things?

Jeremy Deeks: In terms of the cash remittance profile from the UK, I think we previously guided somewhere in the £300 million to £350 million mark. That remains unchanged going forwards, so I think that is how we would like to see the remittance profile going forwards.

John Warburton: The second one, the majority of our sales are through the PruFund range. It is our unique and differentiated proposition in the market. You will be aware that we have unit-linked funds, and we also have collective sales. We will be looking to sort of develop those. The reality is, our unique offering in the market is PruFund, and therefore you should expect and will see that PruFund will still be the predominant part of our retail sales.

John Foley: The outcome from PruFund, I think you have probably given us an idea to just about every banker in the room, so I look forward to all those conversations. No is the answer; we have not given a great deal of consideration to that.

Nick Holmes (Société Générale): I wondered, are you concerned about the churn in the old with-profit book in the changing savings environment? Is that a threat to the with profit book, because most of the profits come from that old book at the moment? I just wondered what your thoughts were.

John Warburton: I suppose there are a couple of observations on that. As you would expect, we obviously monitor the persistency of the books on a quarterly basis. We report on those internally and review that, and actually, the persistency is very resilient and very strong. What we have seen generally speaking since the retail distribution review is less churn, so rightly or wrongly, the view was that commission might have been an incentive for churn in the past. Commission has obviously gone out of the UK market, there is no particular incentive or financial reward for an adviser to recommend a change. Of course, what you have are quite valuable and accumulated benefits and guarantees within traditional with-profits. If we did see a tick-up. The irony is, in the short term, of course, the shareholders would benefit because the terminal bonus itself would crystallise a further shareholder transfer. Basically, we are seeing a very resilient position against our underlying assumptions.

Abid Hussain (Credit Suisse): Just a quick question on the consolidation. I am just wondering if you are interested in possibly consolidating with-profit books across the market, or even perhaps annuity books, where you may be able to grandfather the old solvency rules?

John Foley: We are obviously looking at a whole range of options on annuities. I would doubt that we would become a consolidator, but I think just about every other part of the range you can think of, we are interested in or we are thinking about. As to with-profits, our business is going really well. We understand it. I think to consolidate in that area, you would need to understand very clearly what was in the other propositions. We are pretty happy with where we are right now.

Marcus Barnard (Numis Securities): Can you just say what you are planning to do with your partner numbers in your financial planning? Is that an area for growth that is sort of 5% to 10% per year? Do you have any particular targets in mind in terms of coverage or size? Do you want to be the size of St James's Place? Can you say a bit more about that?

John Warburton: We are growing it organically and we are growing it steadily. From our point of view, it is more about building a quality and resilient business. Part of our model is that we do support our partners with lead generation activity, so part of it here is about the extent to which we can help and support the driving of lead generation for them, to make them productive. It is a highly productive advisory business for us. It is actually a business that, although it is relatively new in its own right, as a standalone advisory business it will be making profit in its own right next year, which you can say for very few advisory businesses in the UK. We do not have a particular target in terms of a glass ceiling; it is about growing it incrementally and organically. We are not going to get to St James's Place level in anywhere near the near-term future. There is a big difference between the number of partners that we have and the number of partners that SJP have, but what you will see is that we continue to grow that number year on year incrementally, and you have given your own steer in the sense; of 5% to 10% growth in partner numbers is probably about what we would expect to see.

Blair Stewart (Bank of America Merrill Lynch): To the extent you can, any comment on the FCA investigation into annuity selling practices? Post-Brexit, if we move into a higher-interest-rate world and the PRA has a bit more flexibility around the risk margin, could that see you enter the annuity market again or re-enter the annuity market?

John Foley: Yes, I do not rule anything out in terms of annuities. We have a big book, and we had a very strong proposition, but Solvency II pretty much stymied that for us. If that changes, it is back on the table; we will review it when and if that happens.

As to the regulatory matters, I am afraid we cannot comment, we do not comment. I said that at the results, and I am afraid we have to stick with that policy.

Lance Burbidge: I remember what my other question was on. I think the FCA have said they are going to publish their interim review on asset management on Friday, so I wondered if you have any predictions for what might be in it?

Anne Richards: I am guessing they will not have spent a lot of time, months and months and months, wading through spreadsheets to come up with something that says, 'Everything in the garden is rosy and therefore there is nothing for the industry to do.' So we anticipate that there will be findings out of it. It is an interim report; obviously, it is not the final version but, to be honest, we have no more insight than anybody else has. So we just wait and see with baited breath at 07.00 on Friday morning.

Final Q&A

Jon Hocking (Morgan Stanley): Could I just ask the dividend question, just to clear it up? So, on the dividends, so, I appreciate practically nothing has changed here, but just in the interest of clarity, so as you say getting rid of the aspiration to go sort of two times IFRS cover or below, does that sort of work on the other side in terms of you being around the sort of 40% payout ratio, so 2.5x cover? Notwithstanding the guidance, you want to grow 5%, would you let the payout ratio go below 40% in any sensible scenario?

Nic Nicandrou: Look, I do not know how to answer that question without necessarily undoing or changing what the new guidance is. The reality is, you know, we have a number of opportunities that we look at, and we assess that every time we do it. IFRS is one of a number of metrics that we use, but unfortunately just does not capture the amount of capital that you have to deploy when grow your new business, which is why over the last two years we have referenced the other bases as well. We have talked about the growth opportunities that we have today, so I guess in the same way as it is entirely possible that we will go closer to 50 than 40, in the event that we have a stress event, and we said that, we will drill down on cover in that situation. It is entirely possible that it may go below 40 as well.

Nick Holmes (Société Générale): Thank you very much. A question for Mike, which is, what sort of level of group growth do you think is realistic over the next three to five years, and I am thinking in particular, in the past, you have had very strong growth, double-digit, but it has come from the US, I think, as much as from Asia. Now, there is a lot of uncertainty about the US. I know Barry has a clear vision. But what would your thoughts, or what would your guidance be for us about the realistic level of growth? Could you still maintain double-digit, or realistically should we be considering single-digit growth over the next medium term? Thank you.

Mike Wells: Well, I am pleased you are interested in our growth rate, Nick. I think the way to look at it, and we are not going to give forward projections on growth, but I think we have shown you the resilience of the back book, which you have seen, and its growth rate without sales. I think we have shown you where we are in the marketplace is where we are growing, where we are allocating capital, our capabilities by market, our ability to grow by market, our leadership by market, so do I have concerns about us being a growth company going forward? No, I do not. Am I going to give a number? No. But I do think you can see from the resilience of the back book, there is a better growth in Prudential, and I think that is one of our unique strengths.

Andy Hughes (Exane BNP Paribas): Hey guys, just a quick question about M&A of the group, because obviously it feels as if you have kind of got more headroom for different types of M&A in the outlook today. Am I getting that incorrect? Because it was previously very narrow bolt-on deals in certain business units, and now it feels like you will consider maybe larger deals. Do you know what hurdle rate you will be applying if you do M&A, and what the outlook is, please?

Mike Wells: I do not think our view on M&A has changed materially. I think one of the advantages we have, Andy, is we have the capabilities, the footprint, the talent that we need. I think one of the things hopefully that you have seen today is that we can attract new talent to the organisation in each of our markets. You have met some of the new folks in the UK, you have met someone and heard some of the new folks going into Asia, both asset management and life, and also the same thing in the US. So, the question becomes, is there reliability stream we want, a back book of earnings that we think is correctly priced. You get back into the bolt-on sort of space. Guy was very clear that we would look at lift outs in asset management. It is a little different than acquiring an asset manager. I think you are all experts in that field, so one of the challenges of acquiring an asset manager is when you acquire the asset manager, you acquire the managers. It is no different than broker-dealers.

So we are well aware of the challenges. But I think for us, we continue to extend the franchise by acquiring talent, however that is defined, just getting good people to come and work for us. That is again the capabilities, what we are reinvesting in the business, the growth of the business, the tools we provide them, all of those things that make it attractive. The bolt-ons in the US in particular, still interested, still opportunistic, they still look good. The team looks at dozens of deals, there is nothing that has transpired in the US in the last four years or five years that we have not looked at all been there and had an opinion about. So it is not like we are missing something. John's point about the bankers, every investment bank knows we are a buyer of certain types of liabilities, technical income, basically, and then in Asia there is very few blocks or existing companies to buy. So I think with our confidence and our footprint and its capabilities and to this point its growth, we have to be careful that we do not buy somebody else's problems, and we distract the management team onto an integration exercise versus a growth and execution. And at this pace, I am highly sensitive to people being distracted, and there is no sarcasm in that at all. These guys are working hard.

Oliver Steel (Deutsche Bank): So, three questions. First of all, in the VNB mix that you showed us this morning, you talked I think about a 5% uplift in the margin because of management actions and mix. I was wondering if you could break that out on what you are doing to have delivered that. Secondly, there has been a slight sort of theme in some of the presentations today about sort of extra costs, restructuring costs in the UK, expansion costs at M&G, I think at Eastspring as well. I guess the DOL effects in the States must have cost you quite a bit of money. So I am just wondering whether that can be brought in within business as usual costs or whether we should be thinking some figure? And then finally, if the UK solvency ratio is pushing up towards the top end of the range, what happens when it pushes out the top end of the range, if it does?

Nic Nicandrou: Okay. I mean, the VNB mix has been there earlier in the year as well. At the half year, we contributed four points to the half year on half-year growth; it is now contributing five. I mean look, there is a number of things that are happening. Clearly, some of that has to have to do with the interest rate environment, and there is a number of places in Asia where we have just withdrawn or drawn back, scaled back if you like, from some of the interest rate sensitive products. In a number of parts again in Asia, we are going harder at the H&P proposition. It is no coincidence that you saw the 27% increase in NBP. Some of that is volume, some of that is of course more favourable economics but some of that is mix. And then even within Jackson and within the UK, you get nuances having kind of lower Elite Access, for example. Elite Access is good in terms of internal rates of return, but just does not report a good NBP margin. So, that is perversely helping that particular ratio. Similar points in the UK as well. So it is pretty much across the piece.

On the solvency, it is still early days in the adoption of Solvency II. It has been a baptism of fire, candidly, it comes in on 1st January, and then within six weeks you get the first leg down in interest rates, followed by Brexit, followed by further drops in Q3. Okay, the last six weeks have been better. And when we did set this out, to say 130% to 150%, we said we are going to test and learn. I always envisaged it that it would be volatile and, believe me, it has been. So yes, we will take the learnings and we will react to that as this thing beds down. And it is still too early in its life cycle.

Mike Wells: You asked about the costs, so there are clearly a couple of things going on. There are changes in the fundamentals of some of our markets that we are adjusting to, and then there is elements of scale we are trying to, I would say, monetise and not just defend but extend beyond competitors' capabilities or their incremental costs, if you will. So, you are seeing reinvestment. I think we have been clear that we are more than willing to reinvest in the asset management platforms and the various businesses. Is it something adjusting models? Not particularly. It is mostly businesses as usual. You have timing of your various expenses – BlackRock, the Aladdin platform globally as it comes in – but it's not relative to our earnings and relative to our normal expense base.

There are other things we are doing where we are reducing expenses as well. We are not going to stand here and tell you we are cutting our way to growth. But we are very careful on expenses, and we do review expenses across the Group, and are doing that consistently across all the business units. So, a lot of the incremental investment you are seeing, there is other activity going on that is bringing expenses down. Some of that savings is being spent is probably a fair way to look at it. And temporarily, we get lift out of all of these.

Blair Stewart (Bank of America Merrill Lynch): Thanks very much. I did not expect Barry to move from Asia to the US and become even more bullish. A slight surprise.

Barry Stowe: Protection and savings is just what we do. No matter where we are, it is what we do.

Blair Stewart: That was not my question. You have said in the past that you do not want too much exposure to one particular cohort or one particular part of the economic cycle in the US. You have talked about constraining sales etc. So just maybe an update on how you marry up the VA opportunity, if DOL goes well, versus your capital and risk management and how you communicate to investors your ability to manage risk as that VA book gets bigger and bigger?

Mike Wells: Okay, do you want to give him a little bit on how we are starting some of those more advanced models we are looking at and on appetite?

Penny James: Sure. I guess I would say a couple of things. We have a risk function and the risk framework around that business as well, so we look at it from a number of dimensions, both from group and in the US. In terms of sales volumes and I think Chad made the point earlier on clearly, the in-force drives a lot of the risk profile, more than the sales do. I think historically we have had a pretty binary limit to the sales. What we are looking at now is using something a little bit more sophisticated that looks at the risk weighting within individual products and looks at it over a period of time, so we have less constrained over a particular sales level but we are looking at it over the totality of the in-force book. So, I think the business will have more flexibility, even though we are monitoring that risk profile very carefully.

Marcus Barnard (Numis Securities): Can I ask if the sale of Korea means you will be taking a more focused look at what businesses are core to the group and which stay in, or whether it was just an opportunistic sale? I mean, I am thinking more here Taiwan, perhaps even India in the longer term?

Tony Wilkey: I think that we have made it fairly clear over the years that for Korea, from an insurance perspective, if we were not there, we would not be entering today. It is a very complicated market. It consumes a disproportionate amount of management bandwidth for the value that was attributed back to PCA, and it was very opportunistic that in Mirae we had a very keen buyer stepping forward to take the asset, and we are working through regulatory approval right now. So, a good outcome from a strategic perspective. I think beyond that, there is nothing else.

Mike Wells: Korean asset management business, do you want to give them a feel for it?

Tony Wilkey: It is kind of like North Asia. If you go back a couple of years, we exited Japan on the life side but we have a very vibrant asset management business in Japan. And the same in Korea. Eastspring Korea is doing very well, growing, a great performance and we plan on continuing to invest in that business.

Lance Burbidge (Autonomous Research): Bizarrely, I am going to ask a question about Korea as well. I assume it absorbed a disproportionate amount of capital as well, so would it have a significant impact on the Group solvency position? Just also to clarify on the dividend. Just, the sentence where you say potential for additional distributions, I just want to make sure that that is still potential in terms of special dividends and rebasing? And then finally on a question for Barry, how important do you feel that the legislation that you mentioned in terms of getting advisers to actually talk about guaranteed income in retirement, how important is that to actually get the product sold in a fee world, where it takes a lot of time to sell a VA?

Nic Nicandrou: So, in the overall scheme of things, given 24.5 billion of owned funds and 13 or so billion of SCR, Korea just does not feature that prominently. Sorry to disappoint. On the additional distributions, clearly nothing is ruled out. I would not rule out a special,but rebasing would be the format that we have used most frequently in the past, and there is no reason to change our bias towards that.

Barry Stowe: I pointed that out in one respect to illustrate what is happening in Washington, the bipartisan view that lifetime income products are an important component and I think we are in a position where we can get the government to consider leveraging the sales of these products. One of the ways they can do it is saying, when you receive a distribution from this sort of account, you are required to be shown amongst the options you are required to be shown a living benefit of lifetime income option.

It has to be useful. The fundamental issue though that you are talking about, about how difficult it is to sell the product, and we are talking about the three appointment sales process to sell a VA, a lot of that I think is self-inflicted. It starts with the fact that as an industry I think we lost control of the narrative around the product. As evidenced by the fact that if you go to consumers and ask, 'Where do you go to get a guaranteed income product?', only 0.5% figured out that the only place you can get it is a life insurance company. There has been noise around the products that have historically gone unanswered, and I think we have just got to move through a period where we reclaim that narrative, and we have got a lot of work going on there to basically change people's mindset around these products.

And I think if we are successful in that work, and I expect that we will be, I think if we are successful in leveraging the very useful and appropriate, I think, attitude amongst political and regulatory leaders, that is going to really be helpful. If we do the job we ought to do on constantly improving the quality of advice, how these products get sold, I think that is useful.

I think we have got to simplify the way that we talk about this too. I think I mentioned that from the stage, and I know I mentioned that to some of you last night at cocktails. We have got to stop talking about PII, VA, GMWB with DB. And confusing people with step ups and so forth, because while what we have to do in some respects around the hedging and the risk management and so forth does make VA a complicated product from your perspective, it need not be nearly as complicated as we make it from the consumer perspective. I use the analogy of going and buying an automobile. When you go to buy an automobile, you sit in the car, you make sure it is comfortable, yes, it will take me from point A to point B comfortably, with satellite radio, in air-conditioned comfort, and it is going to do for me everything that I know I need. I do not need to understand how an internal combustion engine works. There is a way for us to simplify this. To do a better job of giving consumers, potential customers, the information that they need to make sensible decisions, without making this so darned complicated.

Jonathan Morris (Lazard Asset Management): Well, thanks for a great day. It is just that all your good work could be undone, if UnionPay issues a press release tomorrow. We need a bit more information on it because it is all our fund managers want to talk about. Wrongly, I agree. You say that there are 16 other forms of payment that you take. Perhaps you could give us a bit more detail on that? Could you just stop accepting UnionPay as a means of payment? What would that do? The issue, really, is deposit replacement products; could you tell us how you are not selling deposit replacement products in Asia, and give us more detail on that?

Mike Wells: That is a great point.

Tony Wilkey: Let us see if we can put this Hong Kong thing to bed with UnionPay. There are other payment mechanisms available. What happens, and I think I mentioned this earlier, is the card is very convenient; it is actually a debit card, and it is very convenient. What has been happening, especially on the second, third and subsequent premiums, is there has been a natural migration away from UnionPay to these other payment mechanisms, which can be

TT, direct deposit or cash. We can actually provide you with a list of what the mechanism are and what is available. It is interesting: when you look at the data, the percentage of second premiums that are coming through UnionPay is in the low teens, I think; it is a very, very small percentage. So, there has been this natural migration. In a way, shame on us because we have not driven that more aggressively, through marketing schemes and so on and so forth. So, we are driving that now.

If UnionPay goes away tomorrow? Well, it sort of has in a way for cash value or investment-type products. So, our EGS, our PAR product and any investment link that would be sold; we are not taking UnionPay on that type of product, which is a large proportion of what we sell. What has been the impact? People continue to buy the product, but they are using other mechanisms today.

What comes next beyond that out of China? We cannot predict. However, clearly the demand is there. Interestingly to note – and the media has had a kind of field day with this stuff – since the last few weeks or month, it has actually created more demand for the product, seriously. Such that customers are showing up at our branches saying, 'I read about this in the paper, I am really interested in buying one of these products;' some of them unrepresented by agents. So, I guess they are unintended consequences, which are not necessarily a negative thing. I do believe that the consumers will migrate to other mechanisms, and that is happening.

I think the key point, and I hope we made this clear earlier, is: this is an important risk to understand, but we really need to be winning on both sides of the board. This is why we have been ramping up our business quite successfully in China; and as you saw, if you look on a 100% basis, that is our second-largest business now; NB profit is moving in a good direction, and so on. So, I think it is manageable; again, we can give you a list of the 17 different facilities that are available in that regard.

In terms of the deposit replacing stuff with bancassurance, I think the greatest example of that was perhaps the universal life in Singapore that you may remember, which has a lifetime guarantee on the product and a declared rate for a certain duration. It actually puts a lot of stress on the balance sheet, based on interest rate movements and credit spreads. We pulled that product; in pulling that product, as you can imagine, some of our bank partners had some degree of consternation. However, part of the transition is working with them, working with the sales force and so on to convince them to start selling more regular premium products, and that is exactly what we have done. You saw the metric earlier. If you look at the nine months to date, the percentage of regular premium in all our bancassurance across the region has grown by about 10%. So, it is manageable.

We have talked a lot over the years about selling health and protection through the banks. It is a tougher sell, it takes a little bit longer, the sell is a little uncomfortable, but we have actually made progress in that regard, and we are selling critical illness through a lot of, if not all of our bank partners now.

I think the essence of the single premium, deposit replacing is that one has to be disciplined and prepared to walk away from those opportunities and, as a result, lose market share. Singapore is classic: we held number one market share; that was interesting. We have dropped to three or four now; somebody else has taken the lead by selling a lot of single-premium universal life. Let them have it; that is not the way we are going to play the game.

Mike Wells: I think the other thing that aligns with that out of China is C-ROSS; the changes effectively put materially more strain on short-term, deposit-stripping product and reward longer-term products. So, I think you are seeing a fairly consistent message from the regulator on multiple fronts here, and I think certainly the changes in C-ROSS, there was nothing there that is unintentional. That is their primary capital regime, so I think there is a strong message there as well, which aligns with what we are doing there; we have benefited from the changes, net.

Ravi Tanna (Goldman Sachs): I just had a couple of questions, please, on Solvency II. The first relates to the review that is being conducted by the Treasury Committee post-Brexit, and I understand some of the submissions from companies have been going in. I was wondering: to the extent that you are able to – and I appreciate there is still a lot of uncertainty – what are your views generally speaking, and what do you see as the potential range of possible outcomes likely to ensue from that review?

The second was a very simple one. You have taken a lot of management actions in the first half of the year to boost the solvency ratio, as it were. Are there other thoughts in your plans going forward, and should we anticipate more of that to come?

Mike Well: Nic is an expert on both, but I will speak on both, really quickly. From the political point of view, we have said all along, and I know I have said today: Solvency II is not a particularly good fit for us, in the way it treats Asia and the US. We have worked with the regulator to make it work. Our argument all along is it is quite pro-cyclical and massively sensitive to interest rates. If rates go back up, I think you will see how levered it is the other way. We would not tie a distribution metric or anything to it, and I think you will see the challenges that come with that, because it does not necessarily reflect the generation of cash. So, again, I have my overly obvious focus on cash flows.

We have been very public, I think, and consistent with what we think are the improvements that could be made if they are going to keep it. There are some that are UK-centric, so around the risk margin, around credit, around longevity; the triple conservatism embedded there. We will be formally sharing those comments with the Committee, and I think it is great that the Committee is taking a look at that. There is clearly a lot of complexity around where the Committee's work is, where the regulator's work is and where the Brexit agenda is and the government. I have met some of the principals involved in that socially; I would not want that task, given the Rubik's cube of regional politics that are attached to any changes to that, because I do not think they are simple and I do not think they are single-dimensional, by any means.

We are fine. As Nic has said, our ratios are strong; our UK business is fine, strong. The management actions were to make sure that is true. Given the value of what we have, we can always monetise assets; so, as we have told you, what we are really doing is pulling earnings forward in those scenarios, as someone does with any reinsurance-type transaction. Sometimes you do it because you think they have got the pricing wrong on the other side of the table, and they think you have got it wrong or they would not be there; other times, you do it because you want to create liquidity from future earnings, and we have to make sure we convey that to you that we have done that, and I think we have been very transparent that we do that. However, just given the value of our businesses and the consistency of earnings off our back books, those options are ours. If we felt we needed to do it to maintain the ranges we have told you we need capital-wise, we would, but otherwise we will not.

Did I steal everything you were going to say?

Nic Nicandrou: I can maybe give a little more colour. We submitted our response to the Treasury Select Committee last Friday, I believe. We have consented, should the Treasury Select Committee choose to do so, for it to be made public. There is nothing in there that we would not say publicly. It is no secret that we are not fans of Solvency II; in fact, we have been quite critical in the past. We see no reason to pull our punches in relation to that. Yes, in an ideal world we would like to see the whole thing dropped.

Mike Wells: I was going to stop just short of saying that, but alright. I am trying to learn this English discretion.

Nic Nicandrou: No, I am not going to mince my words. Whether that will happen or not remains to be seen; I think it will be linked to what sort of Brexit the government is able to negotiate. The notion, though, of keeping something when we are not around the table as the methodology evolves is not necessarily that smart, so we will see what happens there.

Now, as a minimum – Mike touched on the areas – we are urging that the UK consider the types of areas that are very UK-specific; risk margin is an example. On annuities, some of the gold plating that is in place around matching adjustment can also be relaxed, and it can be made a little friendlier when it comes to investments in the real economy. We are also, though, urging the Select Committee to make changes in areas which promote the ability of the UK businesses, such as Prudential, to compete and succeed successfully overseas. So, we are looking for a more lenient adoption of the kind of rules that have resulted in us having to bear a haircut in relation to our Asia surplus, and we are seeking permanent equivalence in terms of adopting RBC as we move forward. So, we will see where that goes, but we are participating actively in relation to that.

In terms of the actions taken: there are some that, assuming Solvency II continues unchanged, which has to be our base assumption we can take, we still do not have a full optimisation in terms of the matching adjustment eligibility, of the assets that back annuity liabilities. We are quite high at 96.5%, but there is still a rump we can go after, and we are doing a bit of that. Then the rest will be a combination of actions to take should we need to, and candidly opportunistic actions if the value/risk trade-off is appropriate. That is what is informing our decisions around that.

Wrap Up

Mike Wells

CEO, Prudential

I just wanted to repeat something I said at the beginning: it is clearly an interesting time. That is probably the understatement of the day. The questions at the break-out, and the lunch and things, the discussions about politics, about regulation. My challenge to you at the beginning was that I said we are big enough and we have the global footprint to be affected by all of this, and you see we have. However, I hope you have also seen today that we are resilient enough that the impact of this for us has been, in some cases, on sales, but the growth of earnings, the growth of the franchise, the growth of the capabilities and the growth of the talent all continues. So, I think it is a testament to the scale of the business, the capabilities, the back book; we are talking about the value of the proposition we have with the clients and, disproportionately, the team.

I said this when I started, I was joking about the screens, all the cities flashing up here. I have been to a lot of our offices in the last 20 months or so globally. I am sure every CEO stands in front of you and says they have exceptional people and the best in the industry; we keep putting more and more of them in front of you, there are lots of our colleagues here: we do. I think they lead in their markets, and I think we can demonstrate that in execution. I can tell you in just the last year, the difference in our capabilities in markets, there is not a single business unit where there was not something they talked about today that they could not do a year ago. So, this is a business that is growing; this is a business that is reinvesting in its capabilities, reinvesting in its talent, and reinvesting in its markets because we think we have a winning proposition in the right places with the right product set.

I appreciate your support, and I certainly appreciate you sitting here for what I am sure is eight hours. Thank you for your day, and enjoy the evening.

[END OF TRANSCRIPT]