# Prudential plc 2019 Half Year Results

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# Group Strategy and Demerger Update

Mike Wells

*Group Chief Executive, Prudential plc*

## Agenda

Good morning everybody. Thank you for coming out on this warm and sunny London summer day. First off, thank you for joining us, on a little more serious note; and those of you via telecast and I know, on the phone, thank you for joining us. I am Mike Wells, Group Chief Executive of Prudential.

Our structure today is going to be a little different format than we have used previously. I am going to do a quick overview of the strategy and a demerger update. Then we are going to ask Nic to do an update on Asia and the success we have had in the first half of the year in quality, quantity, all the various metrics. Michael Falcon will come up to walk you through Jackson's success and also his view of some of the strategic challenges and where he wants to go with that business, opportunities it has. Mark will walk you through some of the financial highlights and then I will come back and make some closing remarks. We should do this in less than an hour and leave you plenty of time for any questions you have. However, we think it is important to shift to have the business heads discussing the business performance with you more directly, so we will get your feedback on the format after we are done.

## Key messages

I guess the key message is we are moving forward with the demerger this year, the fourth quarter. That tells you what is done and the amount of work that went in to unwinding 170-plus years of relationships inside the company and structure and things. I could not be prouder of the work that was done. But also, we told you originally we are doing this from a position of strength, that that was one of the key drivers and we had to maintain that. So, the businesses themselves had to continue to perform, grow, add dimensions and all the things that you see in these first half results while we were doing the work on the demerger. I am incredibly proud of the team for getting all of that done at the same time. As I have told a number of you, I have always believed the bandwidth of this organisation is unique and I think you have seen that.

## Financial highlights

So, done from a position of strength; what did the financial performance look like? Well, it is broad, it is high quality, it is Asian-led, all of the key metrics in Asia, let us start there. For John's benefit and Clare is with us too here in the front row, from a standard accounting procedure point of view, the UK businesses from this point will be considered discontinued. It is a fairly harsh term for businesses of that quality that are growing and doing well, so my apologies to my colleagues of many years but that is the framing. So, we talk about continuing operations, that refers to the United States, Asia and Africa. So, the results of continuing operations – Asia growth up 10%; Asia value, the new business metric up 10%; earnings up 14%; cash, again, free surplus generation, one of our favourite metrics, up. At the group level, the dividend is up 5% in line with our policy and at this stage, effectively a mechanical calculation. Then, at the group level, again including our colleagues at M&GPrudential embedded value up to £53 billion.

So, all key metrics strong. Again, as we have said many times up here, all of the metrics that we think are critical are going up, a similar growth rate and the kind of performance we would like to think you expect from us. What is behind that? I will let the CEOs get into the specifics but eight out of ten markets in Asia with double-digit growth of earnings. US up 14%, Mark will get into the calculation of where that comes from; Eastspring, outstanding performance in earnings and in net flows; in the US, you are going to see diversification of product on the organic side, the integration of their last bolt-on, the Hancock transaction. Then, quality-wise, I will let Nic get to the specifics but both in regular premium and in recurring premium, the client relationships, these metrics are in the nineties. So, the absolute quality of the earnings that we are producing has never been better.

**Strategic and operational delivery continues**

So, we are continuing to invest in organic, as you see from the materials. Again, I appreciate there are a tonne of materials you have been given today in a new format, given the change, so we will try and give you some guidance on where to look and then, obviously, it will take a little while to go through them. However, the inorganic and organic investments we are continuing to make are material and they are paying off. On the organic side, you saw £500 million invested in new business in the first half of the year. I often get the question, 'Does Asia need more capital?' There is no market we have in Asia that does not have all the capital it needs for organic growth, okay? Then the inorganic activity is driving a number of objectives. It is extending and broadening distribution relationships. So, in the case of United Overseas Bank, we renewed that partnership. It is not only the 400-plus branches they have in five markets but it is also we are working with them on TMRW, their new digital bank platform; that is the name of it. It brings another dimension to that relationship.

I think a number of you saw is; we launched Pulse. Nic and I and a number of us were in the front row. We were in Malaysia last week with the Minister of Health and his team launching our new health ecosystem platform; and again, that is going to be rolled out across ten markets in the next year. We met with our key agents in the morning and the leaders of our largest businesses there in Malaysia and they understand the dimensions it brings, the brand recognition, the client acquisition, the positioning. Of course, from a social point of view, they see the value of something with that capability coming to the market that addresses prevention, postponement of illness, better information, those sorts of things. So, the investment on that is to the point now where it is actionable and in the field.

We continue to upgrade the value chain across the globe of the businesses. 80% plus of the business in Asia came in electronically in the first half of the year. Again, this is efficiency of agency operation, this is the tools they have, this is our ability to process faster and to interact with clients in the ways they want to be interacted with.

Then modernising some of our distribution capabilities; you may have seen the partnership with OVO we announced. That's the largest payment provider digitally in Indonesia, so it is 115 million devices that their technology reaches. Again, I will let Nic give you a little bit more colour on that.

**Proven track record of disciplined capital allocation**

So, modernisation of what is already working, broadening, deepening all of it. This gets to the decisions on how we allocate capital. So, we are continuing to grow these businesses organically. We are looking first and foremost at markets with structural growth. That will be the first lens for any business in the international group. Second is risk-adjusted returns, a variety of other metrics that we are going to keep a little close to the vest but at the end of the day, the portfolio needs to include markets where the products that we produce are in demand. That sounds simple but for insurers, that is a finite number of markets globally. We think we have leadership positions in those markets and we think we are demonstrating we are broadening those positions with a variety of initiatives. Again, I am going to let Nic give you a little colour on the types of things we are doing and testing. I have never seen this organisation better at moving good ideas across business units. That is part of our scale and where we expect a benefit to come from our scale.

Risk-adjusted, high-quality returns. You cannot say that and not be willing to exit businesses. You see some of the businesses that we have invested heavily in and the types of returns we are getting on the right; that is organic. You also see some of the businesses we have exited. This is not necessarily a reflection on the quality of the business but it is a reflection of our view of where it fits inside the group.

**Expected demerger timetable**

So, to that, a very high-quality business that will no longer be part of the group is M&GPrudential. So, there are a number of things going on around the demerger. I come back to from our position of strength, why are we doing it. It is a great business. It is alignment, so capital, investor base, currency, regulatory model, shape of the earnings, cash flows, all those sorts of things are getting very different. The synergies, as we discussed at the time, more and more limited. We think this gives you, as a shareholder, the ability to decide if you want to hold or if you want to sell or buy more. It will be dividended to our existing shareholders in the fourth quarter, so they can decide the combination of the investment characteristics of these two companies that they think is appropriate for their portfolio.

Again, we think that is a decision you should make. So, there is no IPO, there is no equity raise. I can tell you if you talk to these teams after the session today what you will find is this sort of exercise brings a level of focus that is unique. You look at everything. I was commenting to a friend on a weekend, it is the opposite of M&A. M&A, you present an idea to your board and then your shareholders and say, 'This is what we are going to buy and this is what we think we can do with it in the 18 months after; this is what the finished product will look like.' In this case we said to you, 'This is what the finished product has to look like,' and we did the work first.

So, these businesses are tuned up, are in great shape, the management teams are focused and they have never been more competitive in their marketplaces. I say that with 24 years of being with the group.

The final steps involved; there is a process where we have to produce the prospectus and other documentation available to you and the marketplace. John's team will do a markets day again, numerically-centric to give you more detail and get everybody comfortable with what the demerged entity will look like. We will have an extraordinary general meeting, an EGM and then of course a vote with the shareholders to approve the demerger. We anticipate having all of that done, again, in the fourth quarter.

With that, I am going to turn it over to Nic to give you an update on some of the success we are having in Asia.

## Asia Highlights

Nic Nicandrou

*Asia CEO, Prudential plc*

**Delivering on strategic priorities**

Thank you, Mike, for the opportunity to present on the business. Good morning everyone. It feels a little like old times presenting to you during interim results. In my presentation, I will provide an update on the progress that we are making in delivering our strategic priorities and cover how these are driving our current financial performance while building a platform for sustainable, high-quality growth.

Prudential Corporation remains focused on the four clear strategic priorities shown here, which we first outlined in 2017. Through these we are looking to extend our reach and build on our established business strengths through a broader range of products, wider market access and seamless customer experience.

Let me step through a few operational highlights. Starting with enhancing the core in the top part of this slide. Our new product initiatives such as the launch of group insurance and the high-net-worth propositions in Singapore, our entry into retail pensions in Hong Kong and our enhanced non-linked offering in Indonesia have contributed around half of the NBP increase in the first half of this year.

On distribution, our renewal of UOB for another 15 years across five markets in our region has re-energised this partnership, delivering our best ever performance for a six-month period, with sales up 27%. Our joint teams are hard at work to make our offering accessible to a wider UOB customer set both in branch and digitally. Meanwhile, our increased emphasis on high-end agency has seen our MDRT qualifiers across the region rise by 11% to over 8,000 for the first time.

Moving next to health, Mike and I were in Kuala Lumpur last week for the official launch of our AI-powered digital health platform, branded Pulse by Prudential. This offers Babylon's health services alongside telemedicine, wellness and other bespoke services to 32 million Malaysians. Pulse will be available in ten markets by this time next year with Singapore, Hong Kong and Indonesia launching the app in the fourth quarter. To support this region-wide rollout, we have secured digital services from ten partners so far, with more to come as we look to enrich the Pulse offering.

The Pulse platform significantly broadens our current business remit through developing new customer solutions which cover the entire spectrum from wellness, diagnosis and treatment to recovery, Pulse markets Prudential's move towards taking a more preventive role alongside our established protection role. With over 20,000 registered users already, we're off to a very good start.

At Eastspring, we are beginning to see the benefit of the investment made across multiple business dimensions over the last 18 months. Our geographic expansion through TMB Asset Management in Thailand and the WFOE in China has delivered a positive start. In

Thailand, South-East Asia's largest and fastest-growing mutual fund market last year, we have an opportunity to further consolidate our market entry through the acquisition of a controlling stake in Thanachart fund management company, the ninth largest player with AUM of £5.4 billion.

In China, our expanded presence, built-out of distribution and new product launches have delivered a strong first half for new business sales and profits in both absolute and relative terms. More on this later in my presentation.

So, in summary, we are not only building accelerants to sustain our current performance, we are also looking to build new future growth engines at the same time. This is good news for shareholders, as the power of our brand, customer propositions, broad distribution reach and proven execution track record position us exceptionally well to deliver on our sector's multi-decade opportunity in Asia.

**All-round delivery**

Delivering results is in PCA's DNA and the first half provided yet another proof point. APE and NBP were both up 10% on constant currency, the latter despite a two-percentage-point drag from lower rates and up 14% and 15% respectively on a reported basis. IFRS operating profit and free surplus generation were also up 14% and 13% respectively on constant currency. Finally, on this slide, both AUM and EV rose by 23% compared to a year ago, a clearly positive development for our future earnings momentum.

**Delivering high-quality, diversified and consistent growth**

Our strong headline performance continues to be underpinned by three key attributes, namely diversity, quality and momentum. The power of our diverse business platform is evident in multiple ways, firstly, through the number of markets delivering double-digit APE growth in both quarters this year, secondly and more importantly through NBP where performance was broad-based both geographically and by distribution channel. As you can see, both agency and bank-sourced NBP grew strongly and seven of our Life markets grew NBP at a double-digit rate, producing a 17% increase outside Hong Kong, while Hong Kong's underlying increase of 10% was dampened by the effect of lower rates. Lastly, the power of diversity is also evident through nine businesses delivering double-digit growth in IFRS operating profit.

Our focus on quality, which provides low correlation to investment markets, is evident through the high regular premium content of our sales at 93%, through our strong customer retention rate of 95% and through our continued emphasis on driving health and protection, where NBP was up 8%, premiums received were up 12% and IFRS insurance margin was up 14%.

Finally, on this slide, our forward momentum is evident through the increase in our recurring revenue base, which benefited from the addition of another regular premium cohort and sustained high customer retention. The compounding nature of this growth delivered through thick and thin over many years also brings us considerable earnings resilience to go along with our capital resilience with the aggregate local solvency position of our policyholder and shareholder funds at 30th June staying roughly level at 312% relative to the equivalent position at end 2018.

**Life**

The growing level of recurring premium revenue and high consumer loyalty delivered a 23% rise in our total liability base, year on year, to a new high of £94.6 billion. As we have said before, this liability base is a good proxy for our IFRS earnings base. The combination of a higher balance sheet and the rich protection content of our business has driven total Life IFRS earnings 14% higher, with eight Life businesses growing at a double-digit rate, led by Hong Kong, up 29%; Singapore up 18%; Malaysia up 10%; China up 28% on an after-tax basis, with only Indonesia seeing a fall in earnings, reflecting the impact of declining sales in recent periods.

Finally, our earnings exposure to interest rates remains *de minimis*, given our health and protection product bias and modest reliance on spread business.

**Market highlights**

I will now give you some market colour on the four largest contributors to our Life results, starting with Hong Kong. This business has developed the playbook that we want all our businesses to follow. On products, Hong Kong continues to leverage its with-profit strengths and to innovate in health. It successfully launched a tax-deferred retirement offering on 1st April, which contributed 14% of sales in the second quarter. Prudential Hong Kong has maintained its market leadership in agency, growing sales by 9% through this channel and headcount by 16% to over 23,000 agents. Our business has benefited from resilient and rising mainland China consumer demand, supported by a 16% increase in visitor numbers in the first half of this year to over 27 million. Local sales have also grown through success enjoyed in the government-led annuity and VHIS initiatives.

All of Hong Kong's key lead earnings indicators are growing at a double-digit rate, supported by a 98% regular premium/new business mix and a 99% customer retention rate. As a result, customer numbers are 10% higher; renewal premium is 16% higher and embedded value is 29% higher than a year ago. All these factors contributed to the 29% increase in Hong Kong's IFRS operating profit.

I am sure that you are all familiar with recent developments in Hong Kong. We did not see an impact in our July sales, which maintained their positive growth trajectory, but of course we are monitoring developments on a daily basis. The earnings dynamic of a strongly compounding revenue base here immunises our business from any potential short-term sales fluctuations.

Turning next to our China joint venture operations, in the last 12 months we continued to broaden our presence by entering two new provinces, Hunan and Shaanxi, and opening offices in another 12 cities. At the same time, we have deepened our presence within our current footprint, with both channels delivering NBP growth in excess of 25%.

Post-tax IFRS profit was up 28%, supported by a 27% increase in regular premium sales and 97% customer retention. Like Hong Kong, the key lead indicators of our China JV point to strong future earnings growth track, with year-on-year customer numbers up 14%, to 1.4 million; total assets up 35% to £10.5 billion and EEV up 37% to £3 billion on a 100% basis.

I believe that we remain uniquely positioned amongst the foreign players to benefit from both operational delivery, given our low penetration and our access to over 80% of China's GDP and from strategic tailwinds, given the foreign ownership relaxation.

Moving next to Indonesia, the team here has been working hard to drive a return to growth by addressing both the lack of product diversification and agency channel effectiveness. A broader product suite was introduced over the last year, including a new non-linked savings product in January, an upgraded medical offering for the mass market in April, supplemented by our entry into the employee benefit insurance space in June, using the digitally-enabled Pruworks platform. Additionally, we made progress in segmenting and retooling our agency, with good early results from the elite segment. Encouragingly, sales rebounded in the second quarter once these initiatives took traction, increasing by 48% compared to the same period of 2018, with sales from the elite agents more than doubling.

Our product pipeline in the second half will see us introduce a new Sharia non-linked savings product and an affluent version of our flagship linked protection product. Our agency modernisation initiatives will continue as we equip leaders, core and rookie agents with new tools and pursue greater productivity from the elite segment.

As Mike referenced earlier, we have also entered into a strategic partnership with OVO, Indonesia's leading mobile payments platform, present in over 115 million devices. We are working jointly to develop new digital propositions for OVO's platform users encompassing both savings and protection products and we are targeting an end-2019 launch date.

There is still a lot that we need to do in Indonesia to realise the full potential of this business but the team has notched up some encouraging early wins.

Finally, on this slide, as I mentioned at the start, Singapore has led the way amongst our businesses in expanding our reach to new customer segments such as the high-net-worth individuals and group insurance for larger corporates and SMEs. These new offerings contributed 11% of our first-half sales in this market.

Our focus on quality and innovation, so Prudential lead the way in Singapore in introducing flexible premium terms on savings products and no-claims features in retail protection products ahead of regulatory changes. These initiatives have driven a market-leading 13% increase in regular premium and new business and a 12% rise in individual health and protection sales.

Importantly, NBP increased by 13% in the first half, with both channels delivering double-digit growth on this measure, and IFRS profit was also higher by 18%. Singapore is therefore well on the way to support our regional growth agenda.

**Eastspring**

At Eastspring, the work initiated in the last 18 months to improve performance, broaden offering, expand geographic reach and re-energise distribution is beginning to pay off. The £3.1 billion of net third-party inflows represent a high water mark for a six-month period, with six markets, namely Thailand, Singapore, Korea, India, Japan and Taiwan, producing over £250 million in net inflows. Around 45% of these inflows came from strategies not available 18 months ago, with a further 23% coming from institutional client top-ups on the back of strong investment performance.

These positive third-party flows, combined with the more reliable structural flows from our Life businesses, positive market movements and the acquisition of TMB Asset Management, drove Eastspring's AUM 23% higher than a year ago, to £169.5 billion. Consequently, profits rose by 12% to £103 million, in line with average AUM, as the more muted revenue growth following changes in asset and client mix was offset by action on costs. I believe this performance makes Eastspring stand apart from its global and regional peers in what has been a difficult operating environment for asset managers.

**Summary**

So, in conclusion, we have extended our double-digit growth trajectory for our key profit and value metrics, supported by strong new business and net flow momentum. Our new segments, products, channels and digital initiatives are broadening our capabilities and are beginning to contribute meaningfully to our results with much more to come. The structural drivers of demand across Asia remain intact and notwithstanding cyclical headwinds, our proven execution record coupled with the power of our diverse portfolio, our focus on quality and our strong business momentum will see us continue to deliver relative outperformance.

With this, I will now hand you to Michael for an update on Jackson.

## Jackson Highlights

Michael Falcon

*Chief Executive Officer, Jackson, Prudential plc*

**Introductory comments**

Morning. Thank you, Nic. I am pleased to be here with all of you today. My name is Michael Falcon and I joined Prudential and Jackson at the start of the year. I have had almost eight months in the business, meeting associates across our company, regulators, distributors and customers. When I accepted the role, one of the key things that Mike and the executive committee were looking for was a fresh and in-depth review of Jackson's business and strategy. There remains, I think, a broad consensus that Jackson, as strong and dominant as we have been in the market, can be more than it is today and that we still, somehow, punch below our weight. Our challenge, my challenge is to find the opportunities to unleash value and capability that realise a more robust and fully-valued Jackson. Our review, while ongoing, is fulsome, it is without limitation in scope and without pre-conceived outcome or conclusion. As my leadership team and I move past initial assessment stages, I want to share some relevant observations as well as covering the first half 2019 results. I will include thoughts on indicated actions throughout and conclude with a roadmap on how we expect to go forward. So, let us start.

**Strategic assessment**

Strategically, I would summarise my assessment in three simple points. First, Jackson is an outstanding business with even greater demonstrated capabilities than are usually noted. Second, the US retirement market, where we remain committed and focused, is large, growing and offers tremendous opportunities for us. Third, Jackson, I believe can deliver a step-change in value by more actively diversifying our business mix. I think this reduces requisite hedge costs and thereby increases free cash surplus generation, this to support both growth and increased remittances.

*Strength of business*

Jackson is a great business with a long and strong history of success. We have a history of innovation, including the modern annuity product where we continue to lead, but we are also leading in new product initiatives, such as advisory. Jackson, I think, was well placed to grow rapidly in the withdrawal benefit part of the annuity market a decade ago, growing our share to 17%. We remain well-positioned today, given our pricing discipline and risk management approach. Our sales distribution capacity and capabilities are outstanding. Advisers, customers and platforms rate our sales teams, products and service deliveries very highly and they all want to do more with us. We are operationally efficient and excellent, with best-in-class industry cost structure, quality and a single-stack technology. We are scalable and we have demonstrated this through numerous bolt-ons. Our regulatory, operational and risk management record, I believe, is strong and it’s highly respected. We have proven resilient through numerous market cycles and market conditions. Finally, we operate in a massive, fast-growing, albeit complex, US retirement market. However, understand that people want what we provide – guaranteed Lifetime income and protection of principle to and through retirement.

*Market outlook*

The industry is certainly going through a disruptive change but I believe that in general it is changing for the better. We see a clearing of the regulatory fog. The SEC regulatory best interest rule has been issued. We have bi-partisan, legislation pending, with safe harbour rules for insurance and retirement plans and the most problematic aspects of the previous DOL initiative are less likely, while benefits, I think, of a smarter and better regulatory framework are being enhanced. Further, media sentiment towards annuities is softening, even warming and the customer sentiment towards well-run and trusted financial partners is improving. Most importantly, the direction of intermediary distribution in the US advisory markets are changing, recognising the benefits that our products can provide. This, I believe, is being driven by technology and the ability to integrate the benefit of guarantees into client portfolio outcomes, in planning, in portfolio construction and in analysis. It is still early days but the integration of annuities into core advice, asset allocation and operating systems is finally happening. For the first time, advisors are increasingly able to model the cost benefit for clients and then execute all within their core workstation.

There are, of course, still some headwinds. We remain a relatively high-friction product in terms of complexity and the selling, contracting process but that is improving and I think it is going to continue to improve. We also are deep into the longest expansion in modern US history and a period of, dare I say, even lower for even longer interest rates. The economics of these risks and volatility actually speak quite well to the benefits our products provide. However, the behavioural finance results, of course, can vary in terms of end-client behaviour, especially in the near term.

*Priorities*

So, where does that leave us in terms of strategic assessment and priorities? Jackson has become highly concentrated in variable annuity, driven by the higher returns and lower capital requirements of the VA product. Additionally, over the last few years, companies with what I will call challenged GMIB, guaranteed minimum income benefit, back books have come to market. There are big differences in the economic risk profile and accounting dynamics between GMIB and GMWB risks. Fairly or not, I think these elements combine and today I feel they negatively impact our valuation. That said, we have an opportunity to increase value through more accelerated diversification, which will serve many benefits, both commercially as well as from a capital return perspective. We have a strong business with organic growth that includes non-VA products, plus we are an experienced and logical consolidator and operator of Life insurance and annuity blocks. To be clear, Jackson understands and likes VA risks and returns. They represent attractive, long-term through-cycle returns and we are comfortable and capable to manage the associated risks. Also, to be clear, today Jackson is well-capitalised for its current book of business. Still, we have opportunities to improve shareholder returns, with increasing remittances by growing into a more diverse book. This can happen organically, as has already been started but also inorganically through a more active stance on bolt-ons. Our organic and inorganic growth will require investment which might, at times, outpace statutory capital generation. Statutory capital generation is of course the constraining factor on remittances, which are important for Jackson and the group. To meet potential needs, we are flexible as to funding options, including but not limited to third-party financing within the US corporate structure. This could also include reinsurance deals and structures similar to others that exist which are not uncommon in our market. As a practical matter, given the size of our book, natural ageing, attrition and the current market trends, we do not expect significant organic net growth through VA flows in the near term. However, we remain bullish on the longer-term VA growth opportunities in the US market. We are not looking to shrink our VA exposure but we do want to reset the mix of business going forward. This will diversify the calls on capital and free up cash flow by reducing hedging needs, executing the strategy while maintaining our current risk appetite. Again, we like guaranteed minimum withdrawal benefit risk profile. It's often the best solution for investors, the liquidity is supported by NAV, the claims are deferred and it is a high-value product with fees and fee accumulation that supports the risk transfer.

**H1 2019 financial performance**

*Sales shift in H1 2019*

Now let us take a look at mid-year results; I will start with sales. After a weaker second half last year, further impacted by fourth-quarter markets and an even more depressed January, our commercial results are improving. We have seen month-on-month performance build in year-to-date sales for the first half finish only 4% below prior year and 15% above the second half of 2018. This improvement actually has continued year to date.

We have launched a competitive FIA product early in the year and volume built steadily through the first quarter and continues on pace, despite the recent cap reductions we took in response to lower rates. Again, I would remind all of you of our pricing discipline. While competitive, we are not the price or cap leader. We sell based on the quality of our product and service and not teaser or loss-leader pricing or features.

Fixed index and fixed annuities now make up, year to date, roughly 20% of sales. That is up from about 5% last year. That said, this change in current-year sales does not meaningfully impact our overall business mix yet, given the size of our in-force separate account block. It's important to remember that the VA business will grow with markets and the S&P was up 17% in the first half of the year. Of course, I will note the margins on VA business are fundamentally more attractive than other product lines, as well as less capital-intensive. We see this reflected in new business profit being down this year, which includes both the shift in mix but also the impact of interest rate decline during the period. We have details of that in the EEV disclosures.

*Income measures*

Turning to 2019 first half income metrics, our first half IFRS operating profit grew 14%, primarily due to the DAC amortisation slowing, related to the 17% increase in US equity markets. The drop in equity markets at the end of 2018 reduced our separate account balances at the start of the period and therefore fee income in the current period. Improving markets through June and the performance of our underlying funds had allowed asset values to fully recover at mid-year, resulting in fee income close to flat for the current period.

Current interest rates, however, drove a reduction in spread income. As Jackson has experienced before, the significant drop in interest rates in the first half caused a below-the-line IFRS loss. As a reminder, the IFRS equity drift rate is based on current risk-free rates, without a risk premium or mean reversion, so sudden rate drops are notably punitive to below-the-line results. Despite the impact of IFRS methodology on VA reserves, overall IFRS shareholder equity was actually up, both on a six and 12-month basis.

Moving to the middle column, stat operating capital generation was up over prior year, this due to the release of reserves from the John Hancock bolt-on transaction in late 2018. Adjusting for this impact, operating capital generation was down slightly but generally in line with that of the first half of 2018. Stable operating capital formation, along with continued effective hedging supported a 17% increase in remittances to £400 million, despite these volatile markets. Including the impact of the dividend remittance, stat capital was slightly lower at mid-year, reflecting the net impact of reserves and hedging. Again, given the 17% increase in US equity markets, the net hedging result was negative due to the liability starting to floor out. Additionally, the first half saw an increase in the non-admitted deferred tax asset of close to $200 million. As a reminder, stat capital is very conservative and it restricts admission of the deferred tax asset. Despite these headwinds, June RBC, including the impact of permitted practice, held above 400% and we expect it to remain in the range of 400–450%.

Turning to EEV, which we think captures a more complete and economic view of EA cash flows, net income of £900 million was flat to prior year. More importantly, overall, the EEV of shareholder funds, a representation of our market value in force, increased 9% from a year ago to £15.3 billion, this even after paying the increased dividend. Notwithstanding the importance of stat capital metrics, we see EEV as the best relative indicator of long-term value creation.

**Roadmap**

So, bringing this all together, Jackson delivered strong business performance in the first half of 2019. Top-line growth has recovered since the second half of 2018 on the strength of our diversification efforts. We are well-positioned for growth, with improved regulatory clarity, better market narrative and growing distribution. We understand price and manage annuity risks effectively and we have a proven history of delivering consistent operating returns. Jackson is well capitalised for its current book of business and we are managing risk accordingly. To that end, we have already paid the full expected 2019 remittance. As noted, we have opportunities to improve shareholder returns by growing into a more diversified book. The opportunity now is to accelerate Jackson's pace of diversification and to use the resulting natural hedge to reduce external hedge costs. By reducing requisite third-party hedge cost, we can improve cash surplus generation to self-fund growth and increase remittances. Diversification will be organic, as we have already started, as well as inorganic, with a more active approach to bolt-ons. As the investment required to fund our growth specifically through bolt-ons might at times outpace organic free-stat capital generation, we are flexible as to funding options, including third-party financing and reinsurance. The goal is a more diversified and balanced Jackson with more growth, well-managed risk and increasing remittances.

I now turn it over to Mark FitzPatrick.

## Group Financial Highlights

Mark FitzPatrick

*Group CFO & COO, Prudential plc*

**HY2019 financial highlights**

Thank you, Michael, and good afternoon to you all. I would like to cover three main topics today. Firstly, as you have just head from the CEOs on the performance of their businesses, I will start by taking you through how the financial performance of PCA and Jackson rolls up into the group results. Secondly, I will cover capital and will introduce the new group regulatory capital framework that will apply after the demerger. Finally, I will update you on the final stages of the demerger process.

Our strong performance in the first half was achieved after a mixed market backdrop. While we generally benefited from the increase in equity markets, we saw the S&P 500 up 17% in the first half of 2019, rates saw a sharp pullback, particularly in the US, where the ten-year government bond yields fell nearly 70 basis points.

Over time, we have taken actions to position the business to succeed across the economic cycle. In Asia, regular premium contracts continue to account for 93% of APE sales and their earnings profile is far less correlated to investment markets. In addition, the proportion of new sales represented by health and protection products remain significant. However, lower rates are a headwind, most notably in the US in respect of spread margins. From a financial, as well as a strategic perspective, our businesses are strong and are very well-placed for the demerger.

I would draw your attention to the following. Asia new business profits of £1.3 billion is up 10% from a high base and driven by higher sales in almost every market. In the US, new business profit was 30% below the prior year, at just under £350 million. About half the reduction in new business profits is the result of the negative impact of economic assumptions using lower period-end rates. Lower variable annuity volumes and changes in business mix explain the remainder. Both the US and Asian businesses delivered 14% growth in IFRS operating profit and both are strong cash generators, each delivering a healthy increase in the period. After the demerger, we will consider the phasing of remittances across the calendar year as we look to optimise capital generation.

In Asia, our investment for the future has been significant. Over the past 18 months, this has included the renewal of our regional strategic bank assurance alliance with UOB for a total initial fee of £662 million, the acquisition of a 65% stake in TMB Asset Management in Thailand for £197 million and investing £738 million of free surplus in new business. This investment to grow value in the business has been achieved while retaining strong local and group solvency. As we said in March, our dividend policy will remain unchanged until demerger; as in previous years, the first interim dividend has been set equal to a third of the preceding full-year ordinary dividend. This equates to a mechanical increase of 5%. Looking forward, the individual dividend policies of Prudential PLC and M&GPrudential will be included in the demerger documentation.

Moving on to the IFRS results in more detail, the first thing to note is that our headline group IFRS statements look rather different for this reporting period, as Mike has said. You should also note that while the profit from continuing operations includes only our Asia and US businesses, it reflects the full interest costs of our current pre-demerger group structure. Walking down this page, I would like to pull out a number of points, starting with our business unit results. As you have heard from Nic in Asia, the 14% growth in IFRS operating profit reflects our focus on recurring premium, health and protection products. This builds our stock of in-force business and in turn drives a steadily increasing contribution from high-quality insurance margin, which is now over 70% of Asia IFRS income. In the US, IFRS operating profit also grew by 14% with a positive DAC outcome as a result of strong equity markets, offsetting largely stable fee income and a reduction in spread income. This reduction in US spread income reflects the same three drivers we have discussed on a number of occasions, namely the contribution from swaps continues to become less material, the impact of lower reinvestment rates over recent yields on portfolio yield and we were also impacted by portfolio mix, including the John Hancock acquisition. Assuming market interest rates and business mix remain stable at end-June levels, we would expect the overall spread margin to remain in the region of 100 basis points. Clearly if rates stayed materially below end-June levels, this would lead to further downward pressure on spread margins.

Moving to interest expense, we issued a £300 million note in July, bringing the total debt that can be substituted to M&GPrudential to £3.2 billion. The annualised interest cost of core structural borrowings which will remain with the group post-demerger is estimated at approximately £230 million based on end-June FOREX rates. Turning to corporate expenditure, this essentially relates to group head office and Asia regional head office costs. We are assessing the efficiency and effectiveness of our group-wide functions to ensure that they better reflect the future needs of the business. Updates on this process and an overview of expected benefits and costs to be incurred will be given in due course.

Moving down to short-term fluctuations, which are largely driven by the US, where higher equity markets resulted in equity hedge losses. These were only partially offset by a reduction in policyholder liabilities as the full benefit of the uplift in equity markets was limited by lower long-term interest rates and accounting mismatch effects.

Finally, a few words on M&GPrudential. M&GPrudential's performance over the first half was consistent with the dynamics and trading conditions outlined at the investor day in July. PruFund was again a highlight, with positive net flows of £3.5 billion in the period, which helped mitigate a tougher asset management market environment.

Collectively, the core Life and Asset Management pre-tax operating profits were up 11%, as stronger annuity-related earnings offset a lower contribution from Asset Management. M&G revenues fell as a result of lower average assets under management compared with the prior period. Non-core Life earnings included £127 million benefit of update to annuitant mortality assumptions and the adoption of the CMI 2017 model.

Having made the update to assumptions in the first half, further developments are not anticipated in the second half of the year unless experience materially deviates from assumptions. Overall, the resilience of M&GPrudential's results in the first half show the benefits of diversification and a strategic positioning as both asset owner and as asset manager. I will come back to M&GPrudential's capital position shortly but you can expect to hear more from John and his team once we move into the next stage of the demerger process.

To conclude this section, standing back, our businesses have delivered a positive performance for the period, driven by Asia-led growth.

**Capital development**

Turning to my second main topic this afternoon, which is capital, I will cover off Solvency II and our new capital basis, set by the Hong Kong Insurance Authority. Assuming completion of the demerger in quarter four, this is the last occasion on which Prudential PLC will report on a Solvency II basis.

The movement in the group position over the period remains underpinned by continued strong operational capital formation, consistent with the circa 20 percentage points of annual capital generation reported over recent periods. This is offset by the payment of the 2018 second interim dividend in May and the net impact of market movements in the period. In addition, we redeemed subordinated debt and continue to invest in our franchise, notably with the renewal of the UOB distribution agreement which I mentioned earlier. This, combined with small model changes, led to a modest three-percentage-point reduction in the group solvency ratio. With the Solvency II surplus of £16.7 billion and a cover ratio of 222%, this is a very good place from which to begin the final stage of the demerger process.

**Hong Kong regulatory framework**

As we look post-demerger, the Hong Kong Insurance Authority will assume the role of the group-wide supervisor. Our regulatory pillar one capital basis from the point of demerger will be the local capital summation method, the LCSM, rather than Solvency II, as agreed with the HKIA. The LCSM is expected to transition to a new group-wide supervision framework in due course. The LCSM approach really is what it says, a summation of the available capital and a required local capital of each business for regulated entities and IFRS net assets with adjustments for non-regulated entities. Some of the key calibration components are highlighted here on the slide.

We have agreed with the HKIA that the subordinated debt expected to be retained by Prudential post-demerger will contribute to the LCSM capital resources. On a pro forma basis, we expect this to be around £3.4 billion. Senior debt of £0.8 billion is excluded from our LCSM capital resources. Our internal economic capital metric will be retained as pillar two within this regulatory framework and continues to be an important component of our group risk framework. As I just mentioned, the regulatory framework for all Hong Kong based groups is expected to transition to a new group-wide supervisory standard in due course. This is subject to further industry consultation and is not expected to come into force until the second half of 2020 at the earliest, subject to Hong Kong legislative process.

**LCSM overview**

So, what does all this really mean? On this LCSM basis, at the end of June, excluding M&GPrudential and after demerger adjustments, the group would have a strong solvency surplus of £7.7 billion, with a cover ratio of 340%. This pro forma group result reflects strong capital positions, with Jackson's RBC ratio remaining above 400%.

The group LCSM measure aligns relatively closely with our established free surplus generation framework, under which we have been reporting for many years. The key difference is that the LCSM basis reflects surplus over MCRs, whereas in our free surplus measure, we allow for additional capital requirements. For example, in the US, our free surplus measure uses a 250% RBC capital requirement, whereas we use 100% in the LCSM. Local solvency positions are the key driver of remittance capacity and therefore the group LCSM will deliver closer alignment between capital and cash management.

To conclude on group capital, whichever lens you look at our business through, we have a robust and resilient capital position.

**M&GPrudential Solvency II update**

So, a few words on M&GPrudential's Solvency II position. As you can see, this is in good shape, with a cover ratio of around 170%, both at the end of June and on a pro forma basis. We have updated and condensed the waterfall charts we shared with you previously; these illustrate the adjustments from the end of June to the pro forma position. Based on the market conditions at the end of June, we expect to transfer £3.2 billion of debt to M&GPrudential, compared with the circa £3.5 billion previously indicated. Despite recent volatility in markets and in particular significant movement in interest rates, we expect M&GPrudential's capital position to remain relatively resilient.

**Good progress towards demerger**

Finally, on to my third topic, that of the demerger. Agreement of the new regulatory framework with the HKIA is just one of the many steps we have taken since we last met in March. In particular, we now have £3.2 billion of debt, with substitution clauses that enable transfer to M&GPrudential. Its head office functions are on track to stand alone and you have heard directly from the M&GPrudential executives at their showcase in July. We are in the final stages of preparing the completion of the transaction and Mike has highlighted our indicative demerger timetable to you. I look forward to meeting many of you again after we have published the demerger documentation. And with that, I will hand back to Mike. Thank you.

## Closing Remarks

Mike Wells

*Group Chief Executive, Prudential plc*

**Opportunity set is substantial**

Thank you, Mark. To wrap up here, we think the businesses are positioned extremely well to grow across the cycle. What I think has changed in the intermediate term is their ability to execute on more than one axis. You are seeing expansion of distribution, expansion of geographic footprint, you are seeing expansion of product segments we are in and success in each market at executing at those. Again, so, how we grow now has more dimensions than it did just a few years ago. I think that is a key reason we believe, looking forward, that we are uniquely positioned. With John's team, with M&GPrudential, the ability – if you look at those first half results, that with-profit product to act in a completely different manner than the asset management business in the UK and Europe, you have a series of growth engines embedded in that business that appeal to consumers across different cycles. Again, that is going to be the key for both these companies going forward is to not try and play cycles – to benefit from them when they are appropriate but they have a product line and products that consumers want and need cross-cycle. Again, I think both businesses are set up to capture that moving forward.

I hope you see we are doing this from a position of strength. The breadth and quality of the earnings in the first half of the year, the sales growth, the expansion of capabilities, the new relationships and distribution, the invigorating some of the existing relationships on distribution, the change in political headwinds in the US on policy and advice and commission, all of these things, again, we like the direction of all of them, and we think it puts us in a position to demerge M&GPrudential from a position of strength and give us a unique position in the future.

So, I am going to wrap up with this one. We have had a lot of conversations in the management team about what it is that we think we have to be good at going forward; what is it separates us from other teams, what is it that separates the company. And there are attributes we all inherit; there is the brand, there is the existing portfolio of businesses, there are regulatory relationships we have had for decades in markets.

When you look at something like Pulse, that is an example of something that I do not believe another firm could have done, because of the number of stakeholders you had to bring together, plus the technology, plus the brand, plus the relationships with the governments in ten markets in Asia, our execution on that was unique to us. And again, it puts us in a situation where customer acquisition and our social role and responsibility changes in a way that is geometric. It’s those sorts of things are where this Group is now, capability-wise. The technology the US business has, if – the advice channel – if RIA is how retirement products in their broadest definition is sold, you better have a good back office, you better have a single stack technology model, you better be able to connect with the most sophisticated broker-dealer platforms in the US to distribute those products, because that is how those advisers want to do business.

So, again, this is meeting client and distributor needs, advice provider needs, where they are. And we think we are demonstrating that across all of our businesses. Structural demand as I said earlier is absolutely a key lens. All of these markets we are in, clients want and need products that we are providing. We have leading positions. So, as markets evolve, we are a logical partner for new relationships, be it distribution, technology, even governments, to extend into those markets and new directions.

Capital allocation discipline; I think we have shown you that, and the demerger is a prime example of the fact we will look at any part of this Group carefully; into its fit and its capability and when it is best owned as part of Prudential, and when it is not, and how to maximise the value and the future success of that entity. And again, no part of that portfolio, nothing in Asia, no market we are in in Africa, no market we are in, period, does not get that same lens applied to it. That discipline needs to be there in the way. We will be active portfolio managers.

Risk management across cycles, you are now looking at a business with 80% of the results you are seeing, little to no correlation to interest rates. This is a good, well-positioned business for whatever might come in rates. You all have your own views; if rates are going higher, lower, in what markets, positive, negative, etc. But again, the recurring revenue, the quality of the sources of earnings and the type of earnings are less and less correlated every year to capital markets. And I think that is a key driver.

And then finally, we are good at leveraging our scale. You are seeing that. You are seeing good ideas taken from one market and shared across others. That is a relatively recent development in our firm; we tended to be a bit siloed historically and there was some of that informally but now it is a core discipline, and you are seeing that across the organisation. Again, I challenge you to talk to our people around the Group. M&GPru, you are seeing it, and you are certainly seeing it in Prudential itself.

So, let me stop there and we will open it up to questions. We are pretty close to the time we promised you.

## Q&A

**Jon Hocking (Morgan Stanley):** Good afternoon everybody. It’s Jon Hocking from Morgan Stanley, I have got three questions please. Firstly, starting with Jackson, can you talk a little bit about what firepower you see for inorganic opportunities? It sounds from the way you are talking, Michael, that you have ruled out getting any capital from the Group. Can you talk a little bit more about the full suite of options? Are there any circumstances where you would consider selling an equity stake in Jackson at subsidiary level?

And then, secondly, also of Jackson, am I right to think that you said the risk appetite for Jackson would not change? I think one of the problems with valuing the businesses business is trying to find a steady state number. At the moment, we have this hedging programme which protects the economic balance sheet, but it is hard to see the benefit of that in any of the reported numbers. Is the risk appetite the same or is there a balancing point where you could hedge less and produce more earnings pre-diversification?

And then just finally, Nic, on the Chinese operations, you mentioned that foreign ownership changes are a sort of tail-wind I think you said. What is the current state of thinking in terms of the stake with Citic? And absent changing the equity ownership, what is the benefit for Pru from the change in regulation?

**Michael Falcon:** From an acquisition standpoint, I do not think we rule out or in anything. There are a number of properties that trade in the US marketplace and around the Life space that we are comfortable with. We have participated more actively at certain times than others as you have seen with the Hancock acquisition late last year. And I see a number of properties either in the market now or that we would expect to be able to come to market to be available. I do not want to tip my hand or front run anything in the marketplace, but we are interested in a lot of things and, obviously, we are aware it is a pretty transparent marketplace.

In terms of the expectation from Group, obviously, our wording is very intent. I do not feel that the investor base or from a Group perspective we are looking at increasing Group capital against the existing profile of Jackson. That is why I emphasised that I think from a current book of business we are well-capitalised to manage that. I think there is an opportunity that relates to your second point around the question around risk appetite, but I think there is an opportunity for us to improve the remittance profile and the growth of remittances, by diversifying the base. And the thesis to that is by diversifying the risk, if you will, or the calls on capital deployed, albeit more capital deployed, we can lower that external hedge cost and free up cash for return.

So, I do not see that it would preclude capital coming from Group, though more importantly, I think we have access to third party financing that could help us do things faster to create that change and free up cash remittance to Group. And I think that is the measure that you and others are looking for, and it is certainly an important measure. It is not the only measure that we look at, but it is an important measure that we are looking at.

From a risk appetite perspective, I think what I mean to say is that we are not looking to change the return profile by taking on more risk. There is a lot of debate and wordsmithing around hedge costs, allowing hedge costs or hedge efficiency. I actually think our hedge efficiency effectiveness is very, very good. It has been proven long before I got here through market cycles and conditions that have been stressed. I think it is extremely efficient; and when I sanity-check that against other market players and against market counterparts, that is the feedback that I get, openly and directly. So, we are going to hedge as much as we need to, to protect ourselves, because of the risk appetite and the control environment that we run.

That said, if we have less requisite hedging need, we will hedge less and experience less cost. So, what I mean to say is we are not going to drive return by taking more risk in investment portfolios or exposure. We maintain our risk appetite but we think we can reduce the demand, if you will, for third-party hedging.

**Nic Nicandrou:** On the strategic point, look, we have said this before. Before, we had two hurdles to overcome. One was the regulation precluded ownership of a controlling stake. That was hurdle number one, and the second hurdle was the appetite of our partner to sell a proportion of that business to us. The first hurdle has been removed; and if anything, the timing which full ownership will now be allowed has in fact been brought forward by the Chinese government. But there is no change in the position and the relationship we have with Citic at this moment. It simply introduces the option to do so at some point in the future.

The other development of course on the asset management side, again, announcements earlier in July where they said that wholly foreign-owned entities no longer have to have a three-year track record as a private fund management company before they can operate into the retail space. So, again, we have the optionality of using that new vehicle to access a bigger part of the asset management space. So, whilst no change in the 50-50 and the relationship with Citic, the option is there on our relationship.

And as we have said before, really the value in what we are focusing on is on the operational leverage of this business. We have now 0.63% of the market. If we can increase that by 10 bps a year and you overlay the projected growth in gross written premiums in that market of plus 12%, then this business five years from now will produce three and a half times the NBP . In the first six months of this year, we increased our market share by 16 bps. So, that is what we are focused on, and on the ownership it is just future optionality.

**Blair Stewart (Bank of America Merrill Lynch):** Thank you. Two questions please. First one from Michael; just maybe a little bit more colour on what you mean by use of reinsurance third-party capital, can you give us a theoretical example of how that might work?

One of the issues – and Jon alluded to this – is the tail risk on the existing VA book. Would reinsurance be a solution to that potentially, or are you just looking to diversify the risk and therefore lower the hedging cost? Do you see reinsurance as a way to facilitate a bolt-on deal, or is it a way to perhaps swap some of the earnings stream from the existing book into a new earnings stream from a bolt-on? Hopefully that makes sense.

And secondly, just on the Asian solvency, how should we contextualise the 260%, Mark? Is there any way to do that? And what is the outlook for the risk-based model that the Hong Kong authorities are looking at? Presumably then on a risk-based approach you would get some credit for your in-force book or such like? Maybe just a bit more colour on the outlook for that. Thank you.

**Michael Falcon:** Again, I will go first. I see reinsurance and third-party financing as a way to execute bolt on transaction where the size or relative size of what we might want to do to step change the balance in book would outpay short-term free capital generation in a period. So, you saw with the Hancock acquisition which I think represented roughly 10% increase in general account balance, we are able to handle that basically within the organic capital generation of the business last year. So, things of similar size can maybe be handled based on market environment in a current year flow, but others might require third party financing, and reinsurance might be a way to bring some of that risk in either over time or to make something smaller that would otherwise be larger by transferring risk.

I don't see right now reinsurance as a strategic path on laying off risk in the current VA book. I think we understand and manage that VA risk I think quite well and any of the other buyers in the market are going to be looking – There is an economic return profile and there is a scale and a cost advantage in terms of hedging and managing that risk. And anybody that we would transfer part of that risk to is going to want a return on that transfer and they are going to be arguably be sub-scale, or sub-efficient or effective in terms of the hedging component. You would have to believe that a buyer would be able to add more value than we could to it to sort of have a mark and a value on that that would be interesting to us from a return standpoint. So, I think shrinking is expensive in that regard. Our preference is to grow and diversify the book going forward, not offload the current risk.

**Mark FitzPatrick:** And then in terms of the LCSM – it will roll off your tongue soon enough – unfortunately, Blair, that is just us. It is a bespoke arrangement with the HKIA and until such time as the new group-wide capital standards come in, and the new Group-wide supervisory regime comes in through Hong Kong, that will affect the whole industry, at this stage, the LCSM will continue to be a regime that applies to us that has been agreed individually with the HKIA.

As for the Hong Kong solo, their risk-based capital work that the HKIA is undertaking for that, that continues to go through QIS interactions with the industry. We are expecting another QIS to come out later on this year and I think when the feedback from that comes out, it will give us, the industry and the HKIA a sense of where that might land and where that might go. But there are a number of years yet before that actually comes into effect.

**Oliver Steel (Deutsche Bank):** I am going to start with another question from Michael. I wonder if you can give us some sort of indications about relative sensitivities, so what sort of size deals do you need to do, or what sort of type of deals do you need to do to save what proportion of hedging costs, or improve the capital base by so much? Anything you can give on that would be helpful.

Secondly for Nic, Indonesia sales, plus 48% in the second quarter but only plus 4% overall in the first half. So, was the first quarter impacted by retraining on to the new products? Does that therefore nullify the 48% growth in the second quarter if that was just a catch-up? Anything you want to give on that would be helpful.

And thirdly, for Mark, you talked about phasing of remittances changing. Can you expand?

**Michael Falcon:** [Inaudible] So I get to start again, which is fine. The honeymoon is over, the cellophane is off. It is all good. And I have been eight years now; it is perfect.

We have done and continue to do a lot of analysis relative to the types of assets that might be available on the market and the dynamics of how that would affect our book and risk and hedging. I am not going to share specific trade-offs or rules of thumb because it is very, very property-dependent; and, two, we are going to have to buy these – anything that we do in an M&A sense and a bolt-on sense is competitive in a market and goes to the underlying evaluation. I can tell you that I think we understand pretty well the dynamics. When I say 'we,' I mean me. I am informed by people who have fortunately decades of very, very good experience to all this. What I can tell you is we are looking at things that are close to home, that within the product sets that we already sell and/or service within our book and there are a number of different ways and [inaudible] that we can do this. We are not under any particular time pressure or constraint, though I do think through market cycles we are going to see opportunities in the market. We want to be positioned to act on those opportunistically. But there is no single path and I do not think there is any shortage of aggregation that we could do to affect the type of change that we want to see.

**Nic Nicandrou:** On Indonesia, let me answer the question then give you some colour. No, the second quarter performance really coincides with putting in place many of those new products and some of the early benefits of retooling the high end of our agency force. So, it is not substitution for a low first quarter.

In terms of a little more colour, and we see this from market statistics that are made available, the first quarter was a slow quarter across the whole industry in Indonesia. I have said before that there are broadly four buckets of market in Indonesia. There is the linked agency which across Indonesia has been in decline, and that continued to decline through the first quarter, indeed through the second quarter. The second bucket, and that is about 22% of the market. There is a 12% part of the market that is agency-traditional, which also declined in the first quarter across the market. And we were not present in that. The bancassurance is another 30% of that market, also in decline in the first quarter, and the only part of the market that was rising was the 30% odd that comes from the Group insurance. And again, we were not in that.

So, what has happened as we went into the second quarter? We launched a new flagship product that was in the linked agency space. It takes a while when you have 260,000 agents to properly train them. That took through most of the fourth quarter last year into the first quarter of this year. And that is now gaining traction, and coupled with the medical product, the rider that we put on it, we bucked the trend. So, our agency linked is now up, when the market is coming down. We now have a foothold in the traditional space which we did not have before through the very simple product that we launched, and we have done a little better than everyone else in banca and again through some interesting new ideas that we brought in. And we now have an entry into the employee benefit space through the PRUworks platform.

So, market is down. We beat the market both in Q1 and Q2 on the back of all these propositions that are coming in. And the retooling of the agency particularly with the high-end, the MDRTs, the elite has started and we are seeing some early benefit. So, as I said, it is early days, but so far so good and we are pleased with the performance in the second quarter and many of the ingredients that drove that clearly are in place and in play.

**Mark FitzPatrick:** Oliver, on the remittances, effectively the element of rebalancing. Effectively what that is looking at is, traditionally we have taken pretty much the lion's share of the US remittances in the first half, and what it is, is trying to effectively balance them out throughout the calendar year. It is effectively trying to balance capital efficiency and cash flow needs to the centre.

**Johnny Vo (Goldman Sachs International):** Three questions if I may, in terms of the US business in particular. I guess the statutory reserves do not use market interest rate assumptions and I am pretty sure you do not hedge for interest rates. So, is the effect of low rates on your business the effect on the drift rate? Is that how I should think about it?

The second thing is, in terms of assumptions with regard to surrender rates as well, given the low rate environment, you will have an assumption with regards to how many policy-holders are in the money that would surrender; do you need to think about reviewing surrender rates at some point if interest rates remain very low?

And the third question again, just in terms of diversification. If you are moving into fixed annuities and fixed indexed annuities, as far as I understand, that is a credit game. So, are you just swapping out equity risk and policy-holder behaviour risk for credit risk?

And last question on China, as well. The volumes were up quite substantially but the margins were down. Could you just explain that movement? Thank you.

**Michael Falcon:** I will go in reverse order on the Jackson question. In terms of the diversification to FIA and FA risk, we would be adding, in a sense, rate risk as opposed to the equity risk component. But the deployment of that against common capital base creates advantages in the hedging. We are not excusive to spread business; there is also mortality risk that is available in the market, and that is something else that we would look at which has different dynamics relative to the efficiency in hedging, though Chad can speak better to that.

In terms of the assumptions around surrenders and all the actuarial assumptions, it is not that we would need to go back and to review the actuarial team, which is over 70 people, is constantly reviewing policy-holder behaviours and expected sensitivities or impacts relative to behaviours and outcomes from an actuarial perspective. And again, I can ask Chad to comment on some of that as well, but to date we have not seen big changes in those behaviours, nor have we seen them through prior financial shocks or crises. So, they tend to move, I do not want to say predictably, because it is circular, but they have not moved suddenly. However, we obviously do sensitise for those moves and risks. And from a lower rate perspective, I think my comments, if I understand the question correctly, were less related to stat and more talking about the asymmetry of the IFRS reporting. And so, IFRS is particularly punitive in short term relative to fast rate drops because you are getting all of the pain and none of the benefit, and no assumption on any sort of risk premium on equity return or mean reversion on equity return, both of which we would expect from a long-term capital market. Again, it is why we think structurally it is a better lens relative to value and value creation.

Chad, if there are comments on the FIA, FA, or behaviour?

**Chad Myers:** Just to pick up on that, specifically on the VA stat and how we are thinking about how we hedge the interest rates there. It is not the market consistent type of view that IFRS takes. So, what we are looking at there, is any payments that we are making under VA is going to be contingent on equity market returns. So, if you get bad equities, you then generate claims and the out years [inaudible], you will have a discounting mechanism with that; that is the part that we hedge. So, you will see in the accounts that we do have interest rate hedges; actually, quite substantial interest rate hedges. And that is what that is going against. But you are correct that stat, generally speaking, is not super-interest sensitive. It does get more interest rate sensitive in extreme low rate scenarios, especially where equities are lower, because you do get the discounting mechanism that comes in.

Just with respect to the surrender rates, I would just add that we have seen low rates before. As fun as this is right now going back precipitously, we did see this back in 2016, and I would say the surrender rates that we saw back then would be consistent with what we would have assumed and we have not had to retool anything off that, we are generally going to be expecting pretty low lapse rates for those types of policies in low rate environments. But I would also mention on that, because of the way people use these products, they need the cash flow – they are using this for retirement; they are using it to support their Lifestyle – so, it is not something they can necessarily hold onto indefinitely. You will see surrenders, you will see withdrawals coming through.

**Nic Nicandrou:** On China, no, we have not secured the sales by lowering the economics of what we sell. We have held onto the economics; the effect that you see coming through is simply a question of mix. So, in the first half of this year, we sold a little more savings and we sold a little more through banks. And that is what is coming through. So, 45% up on sales, 29% up on NBP. Interestingly, that is the flip of what we saw last year. We had flat sales and NBP up 15%. When the markets were slow, particularly on the savings in 2018, we used up proprietary distribution to go after quality, which is the shape of sales and NBP we had last year. This year, appetite for savings returned in the market. So, we captured that and we pushed on the accelerator for health and protection as well.

So, if you like, over a two-year horizon, our sales are up 47, and our NBP was up 49. So, that tells you what has happened vis a vis mix. But the economics are intact.

**David Motemaden (Evercore ISI):** Hi, good morning. I have a question for Michael. Firstly, on the change in the business mix that you are looking to diversify away from VA, I just wondered what the optimal mix that you are targeting two to three years down the line.

And then secondly, just on the remittances out of the US; the remittance levels have been around 20-40% of IFRS earnings over the past five years. Is there a specific target in terms of where you want this to go?

And then, finally, could you talk about your comfort level under the new VAT reform considering where interest rates are versus when you gave the guidance of the 40% point hit from adopting the new framework? Thank you.

**Michael Falcon**: The first two I think was what is the optimal mix; the second was regarding the 20-40% remittance of IFRS and would we have a target for going forward.

**Patrick Bowes:** And the last one was on impact of interest rates on regulatory capital.

**Michael Falcon:** So, I would say we have a range of where we think we can get and want to get to in the current environment but I am not going to disclose it this time. I think the direction of travel is more balance to the book. I do not know the percentage of IFRS remittances what we would incur on going forward, because of all of the shortcomings relative to economics as well as stat capital. So, I think the better constraints or indicators to look at rather are the EEV and value creation within the book and how we are growing, as well as the stat capital generation, because I think stat capital is more the constraining mix on that. And relative to the rates, I will turn to Chad.

**Chad Myers:** So, David, the dynamic right now with VA and low rates in the new model, I think what I mentioned before in previous conversations was that we thought we would see a modest hit to RBC within that, and that it would be less sensitive to market levels. And as we are parallel testing that right now, I would say those are coming true. We do see less sensitivity, so we expect there would be less sensitivity to rates in the tails under the new methodology which is good. And I would say that based on what we are seeing, it is hard at this point to necessarily reconfirm exactly what the hit will be on RBC because one is moving and the other is moving at the same time, and not quite the same dynamics given the low rate scenario.

So, what I would say there is, we are still comfortable as I said before in that 400-450 range post-paying dividends, post having gone through the NAIC regime. So, we are reasonably happy with where the model came out, and that should be pretty tractable for us going forward.

**Greig Paterson (Keefe, Bruyette & Woods):** Just three questions. One is, given where we are with spreads, I wondered if you want to talk about the Jackson BBB book, and the whole theme of fallen angels and whether there is a potential for downgrades there hurting the numbers.

Second, in terms of the Pulse roll out that we are seeing now, I am just trying to understand from Nic whether it is going to result in a spike in APE, or it is more like an evolutionary type in terms of timing and when you will see the benefits thereof.

And then the third thing is, you mentioned on the FIA you changed the caps recently. I was wondering, does that mean that you are going to expect a slowdown on the trajectory of your move into the FIA space, or the industry move their caps as well proportionally and your pricing relativity did not change?

**Nic Nicandrou:** I think you asked me the same question last time, Greig. We are in the very early roll out phase of what we are doing on Pulse. Malaysia was our first market; as I said in my prepared remarks, Hong Kong, Indonesia and Singapore will follow. Really, our focus and our priorities in the next year are to get this out to ten markets across the region where we are contracted to work with Babylon exclusively to ramp up the number of users. We want people downloading it; we want people registering – in other words, giving us their details in terms of how to contact them, and then we want them to use it on a regular basis. And through that we will get to understand more about the users; and in time, provide them with products, propositions, either through offline or online channels. So, that is where we are, that is where we are focused, as opposed to necessarily counting on this to give us a spike of APE in the immediate future. There are many other things; we have many other initiatives going on at the moment across high net worth, employee benefit, retirement, and other health initiatives on the critical illness side that will drive our growth in both top line and profitability. Pulse will come in but it will be a slower burn.

**Michael Falcon:** On the FIA cap reduction, I think it was aligned with market rates and competitor moves as well. We have not seen a slowing in the FIA flow or the forward book. The market does not move quite that fast but it does move and we move it with competitors. We are not leading or lagging I do not think materially in that case.

In terms of the underlying credit book in BBB exposure, it is obviously important, and again we are long and late in an expansionary cycle. At some point, there will be credit cycle and contraction in credit markets. I think we have really good policies, controls and analytics in place around that and the quality of the book has actually been improved over the last several quarters. We hold less BBB minus, we restrict and limit, we weight underweight the financials within the BBB where we would see probably more vulnerability in the types of market conditions that could cause stress in credit markets. We have limits on positions and holdings with single issuers. So, I think there is a lot of prudence in the management of that book.

We also within the framework of the larger portfolio steer clear relative to competitors, under index high yield and lower credit qualities. We play in mortgage and asset backs, and in safer parts of the market, our CLO exposure is substantially less than others and higher in the stack. I do not know if there is anything else you would add to that.

**James Turner:** The only thing I would say, Michael, in addition, is that 85% of the book is BBB or BBB plus. It is very conservatively positioned, very well reserved for downgrades and default shocks, and, as you say, is very tightly controlled and monitored.

**Andrew Baker (Citigroup):** Three questions please. First, as part of the merger for M&GPru, we will get an update in terms of numbers, presumably targets. Is there any plan during the same process to come out with new Group targets for PLC in terms of earnings growth, capital targets, sales or anything of that nature? Second, Hong Kong. Appreciate the comment that no impact on July sales. If you look at second quarter year over year growth versus first quarter, there was some slowing there. Is that just a base effect or is there anything else that we should be aware of?

And then third, just on the Group capital. Going from LCSM, transitioning to the Group-wide supervision by second half 2020. This transition and any uncertainty during that transition, does it have any impact on the way that you think about capital deployment during that timeframe?

**Mark FitzPatrick:** On the Group capital piece over the transition period we are going to be working and talking very tightly and very closely to HKIA. What we have at the moment in terms of the LCSM is what we are going to be using, what we are going to be deploying against, and how we are going to be managing and running the business. As was said for quite some time, when we talk about Solvency II, the thing that truly bites is the underlying capital level in terms of the underlying businesses, especially around Asia, and effectively the LCSM gives us a more direct read across on that particular piece. So, we are looking to use that for the foreseeable future.

**Nic Nicandrou:** On Hong Kong, yes, it is a base effect. If we look back in 2018, we had a slow first quarter, and what we did then was we brought forward new product launch initiatives, particularly around critical illness, and new marketing campaigns into the second quarter. As I said, the momentum that we carried coming into this year was strong. We are balancing out the campaigns, we are balancing out the timing of product initiatives, and therefore what you are seeing is the outworking of that. And to give you one other data point, if you took June alone, 30% of our first half sales in 2018, 30% came in June. So, that was the emphasis that we had put into these campaigns last year, whereas this year, 22% of our first six-month sales came in June. So, much more even, much more normal pattern in 2019.

**Mike Wells:** And Andrew, on target, I think the -- I'll do that one (inaudible) pick that. No, on the Group side you won't – For M&GPrudential, will be for the board and management teams to determine. But we did them as proof of concept multiple times, particularly out of Asia, and it proved that the businesses could generate cash flow. There are some very good things about targets and this organisation has hit them. There are some negatives to them in that they tend to be the only thing the organisation focuses on if we put them in place. So, knowing the culture well, our intent going forward is to keep giving you a more granular look at the key businesses so you can see the depth and breadth of the success versus trying to give you a rounded-up number that says this is how it looks. And again, we will watch that.

But I think Indonesia, Singapore, Malaysia, Eastspring, Hong Kong, all could be listed entities at this point. So, I think we are past the proof of concept stage and it is more of a show us how each one is working and we will continue as we did today to give you a more granular look at the core businesses and so you have a better feeling for the environment as well as the depth and breadth of the performance.

**Andrew Crean (Autonomous Research):** Good morning. Michael, sorry to come back to you. I am still a bit confused. You do not want to write more VAs, and in fact you are in net outflows, but they are the highest return lowest capital requirement business you do. You want to write more FIAs and FAs which are lower return but higher capital intensity. And you will fund some of that, the inorganic bit, with third parties. Why does that lead to higher remittances from the Group, and why does that lead to a higher valuation of the Group by analysts? I suppose what I am really going to, is it is so complicated with EV, IFRS, and STAT all going in different directions. Why do you not give us a target for what you think remittances will do from your US business over the next five years?

**Michael Falcon:** It is a fair question and let me clarify the first point part of the premise. We are interested in writing more VA business and we are in slight outflow, based on the size of the book and where the VA market is today in the US. So, long term, I am bullish on it. I am trying to give an outlook to set a baseline in terms of expectations. We are continuing to write; we are a leader in VA. We think long-term there is growth but in the short term, the VA market has generally been contracting. That contraction has slowed. Total VA market is actually growing from the last half of last year and in through the first half of this year. But a lot of that growth is in what we would term the structured VA or registered product, in those are more spread products in a VA wrapper than what we would see as a traditional VA. It is also not a part of the market that we have participated in yet.

So, I would not want the message to be that we do not want or do not expect to write more VA, and I do not see the book in run off at all. And over time, I do think we can grow opportunity. From an operating return standpoint from strictly a product, you are right, VA has better operating cash flow generation and lower capital requirement from STAT standpoint. The issue with that is against the hedging dynamics and sort of those below the line costs. And the benefit of having a more diversified book is to reduce those external hedge costs by having an additional asynchronous return on capital with an asynchronous call. And so, the payoff, if we raise financing to buy a stream of income from spread block and you assume that we buy effectively and manage that effectively, and you are using that return to support that financing and actually pay it down, so you keep the value that you bought, that is going to reduce the requisite hedge spend that we have against that VA book and free up cash for remittance.

In terms of target, I am going to have to confer with my executive committee about how we come back and would or would not issue target. My understanding is we do not generally issue those types of guidance.

**Mike Wells:** Andrew, we understand the importance of demonstrating growing remittance in Jackson; they are up 17% this year. But again, you have to then pick equity market assumption, rate assumption, M&A assumption, finance costs. We are not going to put a target on that.

**Nick Holmes (Société Générale):** Thank you very much. I will keep this super brief. First question is, obviously, on the diversification plans for Jackson. Why have you not done this before? What reason is there for not having done this before? Secondly, can you remind us of the rationale for the UK demerger rather than the US? Clearly all the questions are on the US not the UK, which is a rather nice business in many ways. So, why not the US? Thank you.

**Michael Falcon:** Nick, appreciate the questions as always. They are challenging and interesting. The diversification in the US is where we are on appreciation on the accounts and the product has performed as it should for consumers. So, you look at the first half of the year, they have participated in the rising equity markets again. Took a fresh look at the business and the process and decided this was the right time to do this now. So, there is no logic on why it was not done before, but if you are looking for the point in time, we continue to see the underlying performance for the consumers. We are together in Singapore. You saw a little bit of a strained market since then. Those accounts have grown back. So, again, looking forward, which is our job, this is the time to do something like this. As far as looking backwards on the US/UK demerger, there are a number of reasons; the market has structural growth; we have a competitive advantage; it is a higher return on equity business. And we like the dynamics of it, we like the alignment of capital, all the things we said on the demerger. I appreciate looking backwards, four competitors with GMIB books have exited that business in the US, that is not how we base strategy.

[END OF TRANSCRIPT]