Prudential: Half-Yearly Financial Results

Presentation to Analysts & Investors

31st July 2008

Duration: 01:36:49

PRESENTATION

Mark Tucker (Group Chief Executive):

Well, good morning and welcome to our 2008 interim results presentation. We know it's an exceptionally busy morning in the market and we understand we are with fifteen other companies' results this morning, we appreciate you being here.

I am very pleased to welcome Tidjane Thiam to his first results meeting. And also joining us are my Executive colleagues to assist in the questions and answers at the end.

I'm delighted to be presenting a strong set of results this morning. The first half of 2008 has been a very good period for Prudential, both in absolute terms and, I'm sure after this reporting season, relative to our peer group. And our figures show a continuation of the great momentum that our Group has now sustained over the last three and a half years.

This morning I'm going to talk briefly about the strategic growth drivers that underpin our successful performance, and explain why these will remain appropriate for the long term. I'll then take you through the Group's headlines, new business and profit performance, followed by the top-line commercial developments in our individual business units. Tidjane will then go into much more detail on the financials and then I will conclude with some comments on outlook.

But first I want to remind you briefly of our strategy. At Prudential we focus primarily on the enormous opportunities offered by the rapidly growing pre- and post- retirement market around the world. Quite simply that is where the major growth opportunity in our industry is to be found. We remain confident that we have got all the key ingredients to continue driving sustainable value for shareholders. And those ingredients include our focus on a retirement led strategy, our international business mix and an unrelenting emphasis on generating profitable growth and excellent delivery.

Now, we're all well aware that these are times of great uncertainty and volatility and of course that makes for an extremely challenging environment. But in spite of that you can see that we have delivered a strong performance. It's been driven by our clear strategic positioning and the advantages of our business model.

So the headlines. Growth in new business across the Group was up 12% and new business profit increased by 11%. Our asset management businesses performed exceptionally well in a highly volatile environment with net in-flows of £4.1 billion.

EEV operating profit increased by 7% and IFRS operating profit by 13%. The cash profile of the Group continued to improve and overall the capital position of the Group remains very robust. We estimate the IGD surplus at the half year stage was 1.4 billion – a cover of some 1.7 times.

Naturally there is a great deal of focus at the moment on our credit environment and, as I said back at our prelims in March, we came into this environment in a defensive position. Indeed we have been actively managing upwards the quality of our credit portfolio over the last couple of years. Because of that and because of our defensive positioning it had no material impact on our results.

Tidjane will update you further on the credit position and capital and in some detail later.

As a reflection of our continuing confidence in the business and in our balance sheet we are proposing a 5% increase in our interim dividend.

I use this slide of the 2007 year end presentation and said then that the good geographic diversification of earnings and risks are absolutely fundamental to the Prudential model. They give us a hedge, particularly in times of economic volatility. We operate businesses in different cycles of maturity and in economies of varying growth and affluence. So you would expect us to deliver stronger overall performance than we could achieve if we were overly dependent on any one market. And I think today our figures demonstrate the success of this diversification.

Without doubt Asia is our core driver of growth and profit, providing 56% of new business profit and, in fact, nearly 80% of our total new business profit is now generated overseas.

If you look at life EEV operating profit and the scale of our achievements in Asia that I've just mentioned you can see that the region now accounts for around 40% our business on this measure.

On an IFRS basis the UK business remains a very significant contributor, combining the continued strength and success of the with-profits fund with a growing contribution from the shareholder annuity business.

Finally, the rapid growth achieved in our asset management businesses means that they now account for around a quarter (around 25%) of our IFRS profits.

We've achieved that performance by maintaining a clear strategy and by delivering excellence in the implementation of our plan across all of our markets.

Let's move on to look at the businesses and firstly in Asia.

For the first half Asia continued to perform strongly, with new business up 14% and new business profit ahead 15%. It's important to remember here, and Tidjane will go into more detail, that we achieved significant growth in Taiwan in the first half of 2007. That's over 100% growth that we saw in the same period last year. Excluding Taiwan, which gives you a better sense of the true underlying growth in the region, new business across Asia grew by an excellent 29% and new business profit increased by 26%. With that in mind we remain confident of achieving and doubling our 2005 new business profit by the end of 2008. That's a year ahead of our previously stated target of 2009.

One factor that continues to differentiate us from the other life insurers operating in the region, and one that gives us a great advantage, is the unique breadth and depth of our operations. We are not over reliant on any one market. We've got more top three market positions than anyone else in Asia – around seven now – and we truly have a pan-Asian business.

There were a number of very strong performances and let me highlight a couple of these.

Indonesia was up 96%, driven by growth in agency numbers and increased productivity and those of you here that were with us in Jakarta a few months ago would have seen it first hand the power of the agency model, and the depth and professionalism of the training in place. Additionally Takaful products are a significant growth opportunity and accounted for almost a quarter of our new business in the period. And the regulatory and political environment is stable, and the market offers a huge opportunity for us as the market leader.

Hong Kong was up over 50%. Really an outstanding result given this is one of the most competitive markets in the world today.

But underpinning our growth across the region is the strength of our multi-channel distribution model. Across the region we now have over 420,000 agents and a profile of these men and women of the Pru vary by market and vary by country. For example in Korea it's typically a 35 year old male graduate, whereas in Taiwan it's a 40 year old woman with second year education.

Our focus on agency management training, on productivity and on our processes reinforces our position as agency employer of choice for all of these people, and that's been fundamental to our success. It protects the quality of the business we write and our market reputation, altogether a virtuous circle.

We are also unique in the breadth and depth of partnership distribution we have. We have got partnership relationships with over eighty financial institutions in the region, and I was particularly pleased to announce on Monday the deepening of our very successful relationship with Standard Chartered bank. We are extending that relationship to new markets, to Thailand and Japan, and that puts the number up now in total markets to eight. And we are broadening our product offering to include health.

The proportion of linked business, and this is clearly a critical driver, has remained in line with previous years despite the current market conditions. And also what has remained in line is the level of regular premium new business, which accounted for about 86% of Asia's APE in the first half. Both these elements demonstrate that we are very much on track and this is very much business as usual. These two factors give us very good indicators of the powerful underlying trends and of the strength of the savings culture in Asia.

We are also seeing an increased proportion of health and protection business, which is up 56% this year, in line with the work that Barry and his team have been doing and our strategic push in this area.

There has been a lot of debate about the Asian economies in recent months, and I want to give you my perspective on that. The table on the left gives a view of forecast GDP growth in the main Asian markets. As you can see there is no expectation of a significant or worrying slowdown. Indeed cooling is desirable in some places to avoid inflationary surges. Asia is clearly not decoupled from what is happening in the West but by and large it is becoming more and more capable of supporting growth internally.

In April Barry and his team talked about the significant growth drivers that we see in the region, including rapid urbanisation, a growing mass affluent class, change in family structures and an increasing self-reliance for financial wellbeing. These are all dramatic and unprecedented changes and give us a tremendous opportunity to provide a range of financial solutions given our experience, breadth and depth of operations and importantly our proven track record.

Prudential is exceptionally well-placed to capture a large share of the value that will emerge. We remain very confident in the long-term growth dynamics in Asia.

Moving to the US. Getting into the US is exceptionally challenging, but our performance there has been resilient and indeed picked up in the second quarter. As we expect at this point in the economic cycle, risk averse customers are moving from variable to fixed annuities and some of the competitive pricing behaviour we've seen from others is clearly unsustainable.

As we have said before, it is very important to have a set of products that means we can deal with varying economic conditions and the Jackson model being top ten in fixed, fixed income and variable annuities has held up very well. We've responded to changes in customer behaviour and product innovation, including new GMWBs, an investment option to the VA range, as well as expansion of the fixed annuity product offerings.

Total new business in the US was £356 million and that made it a record first half. Retail new business of £274 million was down 4% and new business profit was down 5%, affected by the change in product mix – the switch clearly from variable to fixed. But importantly at the net flow level we are continuing to see very good performance across the annuity books. Indeed the second quarter, the last quarter, saw the highest quarterly net flows in JML in the last five years.

As we look into the second half, we expect the VA market to remain challenging but conditions should remain positive for fixed annuities. VAs will remain our largest product by some distance but for a return to growth we will need to see some improvement in the equity markets, and even then there will likely be a lag in consumer behaviour as we have seen before with previous market dislocations. But with the breadth of our product range we believe our performance will be resilient.

We will also maintain our pricing discipline and, as we've shown before, we are prepared to lose share if the economics don’t work. We will not pursue volume over value.

In the current conditions there are an increasing number of sellers of life-backed books; the pricing we see at more realistic levels. As we've said before, the backed book bolt-ons are a particular target for us, where we can take advantage of our scalable platform to integrate and reduce costs as we did with the Life of Georgia acquisition. There are not too many updates here; we are still clearly looking at this market.

Let me move onto the UK. The UK has performed exceptionally well in the first half. We have seen an 11% increase in retail new business APE and an overall increase including wholesale operations of 18%. New business profit was up 19% and the Internal Rate of Return on new business was 15%.

These figures demonstrate that the disciplined and focused delivery of our UK strategy is producing the anticipated and positive financial results. As you know our strategy has three key themes. First to capitalise on our strengths in the retirement income market; second to reshape our approach to retirement savings, to improve returns and take advantage of our with-profits capabilities; and third to reduce the cost base which, as we all know, is essential to generating adequate returns.

In retirement income our leading position in the retail annuity market continues to be supported by the strong internal flows from maturing pensions. And that’s contributed approximately 50% of individual annuity sales in the first half. That combined with our partnership business gives us a very, very strong base.

We also continue to build successfully in the lifetime mortgage market and that’s a strategically important market for the future. We believe that at the end of the first half to be a market leader with a market share of about 25%.

Our approach in wholesale remains consistent and value driven. It’s clear that in the bulks markets pricing differentials have narrowed, creating opportunities for us and during the period we completed a bulk annuity reinsurance contract with Goldman Sachs for the reinsurance of just under 300 million of Rothesay Life’s non profit annuity liabilities. This is an interesting development for us in terms of bringing alternative risk management solutions to the defined benefit bulk market. However, we’ll continue to be selective and we’ll only commit capital when returns meet our demanding criteria.

Moving now to retirement savings where we targeted, as you know, major change and we've worked very hard to improve returns. In the current market conditions the Prudential brand in particular, as well as the cautiously managed profile of with-profits makes us very attractive to more conservative customers seeking capital and income guarantees. Across the retail product range in the UK 46% of new business was with-profits related and there was particularly strong growth of with-profit bonds, which almost trebled. We also remain the clear market leader in with-profits annuities.

We are continuing to make excellent progress in delivering our cost savings target. The latest milestone was the commencement of the outsourcing deal signed late last year with Capita and which went live in April. We've also been in the process of establishing a group wide data centre based at our facilities in the US and during the first half of this year the UK business completed the migration of their data centre to Lancing.

As you already know, we announced in June that we will not be proceeding with the reattribution of the inherited estate having concluded that the current operating model was better suited to the long-term interest of shareholders and policy holders.

Turning now to asset management where I mentioned earlier we achieved excellent net inflows of £4.1 billion. M&G in particular performed superbly across both the retail and institutional sectors of the market. They've had net inflows of £2.4 billion in total and good flows across all asset classes with the exception of property. I would expect M&G to have significantly outperformed the market. Critically in terms of investment performance, I think is fundamental to the basis of the success of M&G, is that we've seen this year that half of M&G's branded retail funds measured by funds under management had performance in the top decile. The flagship funds such as Global Basics, the Recovery Fund, Optimal Income Fund and American Funds were strong performers and over three-quarters of our funds were actually in the top quartile, which again gives you the underlying investment performance begins that virtuous flow. If you have the performance you'll get the inflows, you'll get the profitability.

On the institutional side there was again excellent performance with almost 70% of mandates exceeding benchmark. Operating profit was £146 million, slightly ahead of that reported in the first half of last year. In these market conditions investment performance is more important than ever and M&G's exceptional track record is serving it well. The outstanding performance was recently recognised by investment week when it named M&G Best Global Fund Management Group 2008.

We had a successful half-year in Asia as well with net inflows of £1.6 billion, an excellent performance given the 20% plus aggregate fall in the local stock market indices. 900 million of those net inflows went to longer term equity and fixed income products. We continue to extend our product range, including major fund launches in Taiwan, Korea, Japan and a third new fund in China. The significant falls in equity markets had a modest effect in operating profit, which fell just £4 million to 29 million.

We have continued to develop the breadth for this business. In Vietnam we again broke new ground with the launch of the country's first institutional property fund. In Japan where we are the second largest foreign asset manager, we established a new distribution relationship in Nomura, our third mega distributor relationship. And lastly, in our more recently established Middle East operations we have already secured 14 distribution agreements.

What I'd like to do at this point and to let you hear more about our performance is hand you over to Tidjane.

Tidjane Thiam (Group Chief Financial Officer):
Good morning. There were suggestions by some of my colleagues that we should provide you with simultaneous translation in English, but we decided against that so you're just going to have to put up with my accent. I am very pleased to be here today and to present to you my first set of results as Pru CFO.

Since I started four months ago I have had three clear priorities. The first one is to deliver a strong performance on our key financial metrics; we have made a number of commitments on which we will deliver. The second one of course in these volatile times has been to manage capital. And the third one is to over time provide you with enhanced disclosures. I have had a chance to go around the Group and familiarise myself with our businesses and my challenge is to make you as enthusiastic about them as I am, with better and simpler disclosures.

So let's start with how we have delivered on our key financial metrics. Mark has already given you an overview of this page so rather than trying to cover it exhaustively I will simply focus on a few select items: EEV new business profits, IFRS operating profits, holding company cash flows and finally, EEV shareholders funds. So let's start with new business profit.

On a constant exchange rate basis our new business profits have increased by 11% over the same period last year. Looking at our key markets new business profit in Asia is up 15%; a very strong performance given the exceptional level of the 2007 comparative, and I will come back to that.

The US experienced a decrease in NBP of 5% whilst maintaining an 18% IRR, which I consider a resilient performance in a difficult market environment. And finally, a truly exceptional delivery in the UK across the board with NBP up 19% and a strong IRR of 15%. We are in a strong position in the UK; we have a very good set of results, which stand out in this very challenging context of the UK economy. Retail and new business profits grew by 10% to £124 million and with £5 million new business profit achieved in wholesale reflects the bulk annuity contract that we completed with Goldman Sachs. An average new business margin of 30% was achieved consistent with the same period last year.

I'd like now to cover in more depth both the US and Asia where there have been some significant evolutions in the first half of 2008, turning first to the US. As you can see from the top end of the slide we have experienced over H108 a shift in product mix between variable annuities, VAs and fixed annuities, FAs. In the VA segment we are staying true to our value over volume philosophy. This contrasts with some of our competitors who are pricing their products, notably the living guarantees, at what we believe is an uneconomic level. Going after volume growth is not a strategy we want to follow when there is limited appetite from customers for this product. As a result VA APE and new business profits, were down respectively 20 and 15%.

In the FA segment we have experienced some good growth as customers have turned their interest towards these products, which is typical at this point in the economic cycle. APE was up 121% while NBP grew nearly threefold. Overall Jackson's margins evolution reflects the product mix changes. I want to say that we manage our businesses to generate a strong return on capital and that we are pleased that in spite of all the challenges observed in the US market this year we have been able to maintain our IRR at 18% from 07 to 08.

Let us now turn our attention to Asia. Mark has already highlighted the strong 2007 sales comparative for Taiwan. What you see on this slide, which I borrowed shamelessly from Barry, is the exceptional impact of our What's Your Number campaign and of the launch of our new VA product in the second quarter of 2007. Barry and his team generated £113 million of APE in Q2 07, more than three times the average quarterly 06 sales. Please also note to your right that the Q2 07 results are good, some of our best results we have been increasing market share from 3.2 to 3.7%. So with this exceptional comparative in 07 it is easy to miss the real strength of our current performance in Asia to which I would like now to turn.

As you can see, if you exclude Taiwan, our businesses in Asia delivered a 29% growth in APE while new business profit grew 26%. I would like to highlight our achievements in a number of key territories.

In Hong Kong the success of our two new linked products has driven NBP up 63% on the back of a 53% growth in APE and of margins moving up from 62 to 66%. In China we are also progressing strongly. Both volumes and margins are up on a comparable basis. Remember that we shifted in 08 to a 50% basis versus 100% before. So volume and margins are up driven by 35% increase in the number of agents and an 86% in agent productivity. We are pleased to have obtained a preparatory license in the Fujian Province, one of the wealthier regions with a population of over 35 million people.

India, another important country, had an excellent semester with sales growing 45%, supported by an increase in the number of agents, which now total over 280,000 and a 10% increase in their productivity. Margins which were down to 12%, you will remember at the year-end, are back up at 16%.

Finally, our Indonesian business continues to thrive with volumes up 96%, NBP up 80% and strong margins. This is another illustration of the value that our current platform and capabilities in Asia allows us to generate when we are a first mover. Our sales force has reached 54,000, an increase of 62%, while productivity improved by close to 10%. These results should help you understand why we remain confident in the quality and the profitable growth potential of our activities in Asia.

Let's move now to IFRS profits. Operating profit before tax increased by 13% to £674 million. Our performance in Asia within this is worth highlighting with Asia life IFRS operating profit up 28%. We are understandably pleased to see our IFRS life profit in Asia grow. All this NBP growth, IFRS profit growth is very good to have especially in today's environment, but at the end of the day I firmly believe that what matters is for all of this to translate into cash, so let's talk now about cashflow.

Holding company cashflow is £86 million positive, up £52 million. This is the balance between net inflows of £511 million and net outflows of £425 million. Both the UK life fund transfer and the M&G transfer have increased, so has the scrip dividend.

Asia has contributed £11 million net as a result of remittances of £148 million, which I think is a good number and investments of £137 million. Overall, the Group is on track to achieve positive holding company cashflow this year.

I would like now to finish this section on financial metrics by reviewing the evolution of our EEV shareholders' funds.

We are all familiar with this slide I believe. As you can see our EEV shareholders' funds have moved down from £14.6 billion to £14.0 billion, 13.977, if you round that, £14.0 billion over the first half, which is £5.61 per share. This reflects both a strong operating performance and the impact of current market conditions. You can see in columns B, new business profits; C, in-force profits; and D, asset management, the strength of our business performance.

In column F the £1.949 billion negative short-term fluctuations are a function of current market conditions, which had the following impacts: a negative £959 million in the UK, reflecting lower than expected returns on the with-profit funds. We had -6.8% versus 4.1% in our assumptions, so that's a difference of 10.9% - and you do the maths, it just gives you the 959, it's quite straightforward. A relative £300 million in the US resulting mainly from reduced investment returns on VAs and from the impact of our bond impairment and I will come back in more detail later to the impairments. And a negative £536 million in Asia reflecting primarily adverse market performance in Taiwan and in Vietnam.

Let's move now onto capital. It is important to take a balanced and holistic approach when managing capital across a group as large and as diverse as ours. Therefore we focus on a series of different measures, all of which we believe are important. You can see here that we are in a strong position on each of these measures. If we take solvency capital, we estimate our IGD surplus to be £1.4 billion, down slightly from the £1.6 billion we had at the end of 07. We are ranked strong by S&P. Only two of our peers are categorised as excellent, Aviva and ING. There was a bet on this, it happened - I lost – AXA and ING. We have a strong economic capital surplus, £2.8 billion and our EEV and our shareholder funds are strong.

In today's environment it is more important than ever to remain solvent, so I would like now to cover in some more depth our IGD position. I have already mentioned the strength of our IGD capital position. It is worth taking just a few moments to describe the main drivers of IGD for us, Prudential. I got that one right. The first important point is that UK with profit funds are ring-fenced from an IGD perspective and there is no pass through to a Group IGD position and when you see the size of the with-profit fund, setting that aside is an important consideration.

Now, if you move onto equity markets, evolution in equity markets impact IGD capital to two channels; for direct shareholder equity exposure and the value of equity linked guarantees embedded in our products. In our case direct IGD exposure to equities is limited as most of our equity holdings, as you know outside the UK with profit funds, are for unit-linked and VA accounts. Also in the US our hedging programme significantly reduces the impact of adverse developments in equity markets.

Another important consideration is credit spreads. The impact of an increase in credit spreads or in default losses will depend upon the size and quality of our asset books. And finally, exposure to interest rate risk from an IGD perspective is dependent on the extent to which liabilities are duration matched with the assets supporting them. You know that IGD basically, if you have the ability and intent to hold the assets to maturity it doesn't penalise you for movement, which is actually I think correct and quite useful. Interest rates are also the level of interest rates guarantees of course embedded in our products, which are an important driver. So in this context changes in interest rates mostly impact our Asian and US businesses as our UK annuity book is mostly run on a matched basis.

In Asia our exposure results mainly from guarantees on traditional shareholder-backed life products. In the US where most of the debt security portfolio is made of assets held to maturity, the main impact on IGD of interest rates is stemming from the mark-to-market of the FA derivatives. So that's the logic.

Let's look now at the sensitivities and we've run them at the half-year. Our Regulatory capital position is resilient, as you can see, to stresses on equity, credit or interest rates. All sensitivities here are assumed to take effect on 30th June 2008 and no management actions are contemplated in this analysis. And of course, results are estimated as mutually exclusive events so these numbers are not to be added. I think the numbers speak for themselves; we have a strong and resilient position from an IGD perspective, which allows us to really withstand any set of circumstances we can reasonably imagine today, including a 40% fall in equities from today's levels.

The next area I'd like to cover is our debt securities portfolio. The overall shape of our debt securities portfolio has seen minimal change since year-end. Out of the £84 billion in the portfolio £37 billion is within the UK with profit funds. For the rest of the UK where we have about £20 billion, which corresponds mainly to assets backing our annuity book, the remainder is mainly unit-linked in the UK. Asia's portfolio is mostly invested, as I said earlier, for unit-linked and with-profit fund and those two areas, unit-linked and with-profit funds represent more than two-thirds of the portfolio. So the focus of this conversation really should really be Jackson. The quality of Jackson's overall investment portfolio is good having benefited from the actions implemented by our management team, led by Clark and Leandra over the past years.

Let me give you some more colour on how we manage this portfolio. Jackson, as you can see, has increased over time the quality of the securities it holds. Diversification has also been significantly increased to reduce concentration risk. The top 20 high yield holdings represent now 36% of our high yield holdings versus 50% eight years ago in 2000/1, so we've changed things quite a bit in that respect.

Also PPMA have adopted a modified total return approach, which has allowed them to move away from a buy and hold strategy used previously, which could lead to large losses on lumpy positions, a much better approach to risk management. In addition, since the middle of last year PPMA has repositioned its portfolio more defensively, reducing the impact of a subsequent widening of credit spreads. PPMA has gone from four analysts a few years ago to 21. It has strengthened all its processes, relying on its own ratings and putting in place a credit committee as well as strong peer reviews on all ratings.

So let's have a look at our residential mortgage-backed security exposure. The RMBS bonds represent £3.141 billion in assets at Jackson, a little more than 10% of the overall portfolio. Of this 3.141, £254 million are sub-prime, £723 million Alt-A, 2.164 billion are prime. We hold 510 RMBSs. 21 are considered impaired at this point in time; out of those, 15 are Alt-A and 6, prime. Therefore we have provided you with some more detail on the Alt-A portfolio for your reference after this meeting.

So let us now turn to our impairments. Please bear with me because this is going to take a while, I'm afraid. Under the Group's application of IAS39 the majority of Jackson debt securities are classified as available-for-sale, AFS, and are carried in the balance sheet at fair value. Movements in unrealised gains and losses on AFS securities are recorded directly in shareholders' equity; however, impairment losses are recorded as a charge in the income statement. Under IAS39 an asset is impaired only if there is objective analytical evidence that the net present value of future cashflow is likely to be less than the principle. If the cashflow analysis identifies an expected loss on the principle or shortfall, IAS39 requires a write-down to include the full mark to fair value of the security in addition to the expected economic loss.

On this basis our decision to write-down the bond is therefore based on detailed cashflow modelling. The model used begins with the current delinquency experience of a collateral pool that supports the bonds. By applying assumptions about how much of these currently delinquent loans will eventually default and by multiplying this by an assumed loss severity we calculate the magnitude of the expected loss for the collateral pool. Additionally, to account for the loans that are performing, but may later become delinquent and default, we add 1% of the currently performing loans to a default.

So a total estimated collateral pool loss is then run through a model of the specific bond structure to calculate the expected future cash flows of the bond. It is this cashflow simulation which indicates whether there is a shortfall on the principle or not. As an additional step, we then benchmark what we've done against a fixed rating report to confirm that our assessment is correct. We therefore believe that our practice on impairments is rigorous.

If you look at the figures from left to right, the 21 bonds I mentioned, the 15 Alt-A and the 6 prime RMBS bonds impaired in 2008 first half, had total expected economic losses of £38 million, so a result of the cashflow simulations, £38 million. In addition, considering the market value today, we had to mark these bonds to fair value and that triggered a loss of £44 million. There are 21 million additional write-downs in other securities, with most of this £18 million arising from the corporate bond portfolio. With the additional impact of losses on sales of impaired and deteriorating bonds, £5 million here, this takes us to a total of £108 million, which you've seen in your papers.

So on the other side, out of these losses, £23 million impact the operating profit through the risk margin reserve, the RMR charge, to allow for our estimated long-term average default. The remaining £85 million are recorded within short-term fluctuations in investment returns.

A final and important item is the development over time of unrealised losses, which we show you here. What you see is that the total unrealised losses stand at 30th June at £989 million versus £794 million when we updated you at Q1. So we've seen a slight deceleration in the volume of the unrealised losses in Q2, and if you look at the breakdown of the 989, 719 are for securities where fair values are 80%

or more, so quite a high proportion of that is above 80 today. It is also interesting to note that if you take the below 80, the £270 million, 89% are of investment grade.

The value of the bonds that have been below 80, which we show in the bottom part, and this date at 30th June, for three to six months £168 million and for less than three months £82 million gives you some indication of a pipeline and of the value at the end of June 08 of what is expected to fall into the more than six months category later in the year. But I'd like to stress one thing about that, is that number, the 270 you see there is very volatile. I cannot say that enough times. It is determined by the market level, it's the pricing of the bonds, whether 75, 65 or something, that number will move. You are aware that July was a very difficult month so this number will move up and down and this is a snapshot at a given date, so you shouldn't draw too many conclusions from the number itself, but it gives you an indication of where things stand at a given date.

So as we close this section on capital I would like to stress once more Prudential's financial strength. Our capital position is strong by all measures and we have a clear view on our exposure to credit risk, which we believe remains limited at this stage. To finish my presentation - I only have three more slides - I'd like to talk about our disclosures. From the meetings I've had with investors since starting in my role it is quite clear that there is a significant appetite for an increased emphasis on IFRS disclosure. I personally believe that it is important to achieve a better balance between our key metrics, embedded values, IFRS and cash.

Let me now take you through a few examples of the kind of disclosures I'm thinking about. The first one is a slide presenting the development of a pre-tax IFRS operating profit of our US business over a few years. This breakdown of IFRS earnings between underwriting, spread and fee income, we believe is insightful and very useful in terms of strategic thinking. Clark and his team use it as a valuable tool to manage our US business and you can see the evolution over time as the VA business is built, the fee business and a better balance is achieved. You should expect to see more of this type of analysis in the future.

Now moving onto Asia; I've been working with our teams there with Barry, Sandeep, Pete Lloyd, who are all here, to develop more in-depth cashflow analysis at a country level. For every year what we're trying to do is to look at cash flows that are post-tax, post-solvency margin and thus correspond to distributable cash. So in dark blue you see here the projected free surplus. In light blue we have a variance against the projected free surplus, which is important to track to see if you are expecting in force cashflow are growing steadily over time with only small adjustments from expected to actual. These two elements together make the free surplus emerging from the policies enforced at the end of each year. It is good to see it strong and growing.

So in white we enter the new business strain for each year as this illustration is for rapidly growing business. As a consequence this strain is of course larger than the inforce profits. The total net cash flows for the specific country are represented then by the red bricks. The red cashflow profile generally leads to concerns as regards the value of operating in a given market. However, we are confident that as a business reaches maturity and the growth rate abates, the in-force cashflow will cover new business strain and the business will move into cash positive territory. With this type of analysis and disclosure we will be able to make more explicit the value created by many of our growing businesses and I will come back to you in future meetings with more information along these lines.

Now, if we step back and look more broadly at Asia, back in April we gave you a breakdown of our IFRS numbers by country and said that we would increase our IFRS disclosures. IFRS is complex as you know, is a mix, particularly in Asia, of grandfathered rules, US GAAP, etcetera. And what we have here is a new disclosure. This slide shows you the IFRS operating profits of the total Asian business for HY 08 and 07, split between the profit from the existing business and the new business strain, which we disclose here and which represents 10% of APE sales on average. Other significant variations will exist between products and countries of course. This indicates clearly that we are growing our IFRS profits in Asia net of new business strain. We will continue to develop and refine these types of analyses.

Before handing over to Mark to talk about our outlook, I would like to share two final thoughts with you. We are facing a tough environment, however, I believe that our strengths, our strategy, our geographic presence, our brands, our strong and diversified distribution, our capital and most importantly our people will allow us to outperform in this challenging period. The second thought again is of a more personal nature. As some of you may know I have had an interest in this company well before joining it. One thing I've discovered since I joined is that our businesses are even better than I thought. My challenge as a CFO is to find clear and compelling ways to communicate that value to you. It is a challenge I very much look forward to, so Mark over to you now.

Mark Tucker (Group Chief Executive):

Thank you, Tidjane. Let me just spend a couple of seconds on the outlook. This is obviously an extraordinary challenging time with a range of distinct factors creating uncertainty for both markets and economics. The macroeconomic environment will doubtless continue to be difficult for some while. I expect Asian growth to remain relatively strong, but beneath the peak levels of recent years and I believe that the region is now less reliant, as I've said before, on the West than it was a decade or so ago. But importantly vast and that was the macroeconomic picture. The fundamentals underpinning our Asian growth remain highly positive.

Jackson will continue to show resilient performance in the short-term and I remain confident will outperform over the cycle. And in the UK you can see from this morning's figures and from the figures from last year that we are clearly delivering on our strategy. And in asset management we are exceptionally well placed to capitalise on the strength of our operations. Overall I would expect to outperform all of our competitors.

We have a clear agenda and a retirement led strategy in our business model with this geographic mix and diversification, is extremely robust and as Tidjane has just taken you through, our balance sheet, capital and cash position have been very resilient. Overall we believe the prospects for the Group remain positive.

Q&A

Mark Tucker (Group Chief Executive):
At that point in time we just end the presentation and what we'd like to do is begin the Q&A, so let me hand over to you guys. Andrew.

Andrew Crean (Citigroup):
A couple of things I was just thinking about; you've raised the dividend 5% off quite a low yield, a company yesterday raised it 10% off double the yield. You've got growing and strong cash flows, you've got a strengthening balance sheet and increasing your UK businesses coming from the with-profit fund, which doesn't need shareholder financing; can you give us some idea as to when you're going to accelerate this dividend from a 5% level? Second question was on, doubling Asian new business profits in 2008 means that you've got to do £490 million of new business profit in the second half versus £336 million in the first, which either means you've got a rabbit in your hat or there's something about the words "by the end of 2008". How do we crosscheck given the fact you don't give quarterly new business profit figures, how are we going to crosscheck whether you've actually hit that target?

Mark Tucker (Group Chief Executive):
Let me take that in reverse order and let me give two seconds on Asia before handing over to Barry to give you some detail. I think with the nature of the business there, what you have seen is continued growth over a 14 year period. I don't know of any other companies that have grown at 26/27% top line for 14 years, that is per annum growth for 14 years, we don't believe anything is in place that will stop us doing 20% plus this year. I think in terms of the detail of Asia and our commitment to that target, Barry will give you some more colour of why we are so confident about that.

Barry Stowe (Chief Executive, PCA):
Sure thanks Mark. Two or three things, first of all, specifically on the NBP, if you look historically over the last five years we have generally done around 40 to 41% of the full year NBP in the first half. There is a seasonalisation to how NBP flows. If you do the math with that we are actually getting pretty close so it does require that we continue to run fast as we have in the past, but let me talk about that a little bit. To really understand what is happening in Asia you really do have to look at the results with a little more granularity, you need to look at this Taiwan effect that happened. If you look at our growth rate in the first half of 2007 without Taiwan we grew 29%; if you look at our growth rate in the first half of 2008 without Taiwan we grew 29%

so the fundamental underlying growth rate of the business is what it was. Again Tidjane showed you the slide so it is graphically depicted but I think it is really important to understand that. Also important to understand that one of the effects of this Taiwan phenomenon was that you might get the impression that May and June of 2008 must not have been very good months in Taiwan. They were the two best months in the history of the company save for May and June of 2007 which were off the charts. So there is nothing fundamentally wrong here, this is still an extremely strong story.

Agency growth is 37%, that is the average number of agents which is the principal metric you should be looking at. Productivity in that agency force, as was mentioned, continues to improve. You saw our good news earlier this week on SCB, I think that is really good news indeed not just because of the extension of the existing very successful relationships but the expansion into new lines of business and into new territories. You have got Hong Kong, China both growing over 50%; you have got India that grew at 45% with an accelerating growth rate, in fact in the Second Quarter over the First Quarter. You have got Indonesia approaching triple digit growth, Vietnam is doing well, in Korea we picked up market share again, all of these things you have either seen or heard already today; but you amalgamate all that and I think what it should say to you is that this continues to be a very, very strong story. There are headwinds that are there now that were not there a year ago but in spite of those headwinds, this is still a very, very strong story.

Mark Tucker (Group Chief Executive):
In terms of the second part, the dividend, I think Andrew, as you aware, we came out with a dividend policy a couple of years ago to say that we would get two times cover to feel comfortable. We are not quite at two times cover yet; we're pretty close but we are not there. I think the dividend history of the company again we want to be absolutely certain in our own minds about sustained growth, and I think the cash flows coming out of that, we are confident of cash emergence but we did think it was appropriate at half year to be conservative on that and we will look again at year-end, but I think again we are very much focused on the dividend policy which we set at two times and we will look again in those circumstances.

Andy Hughes (JP Morgan):
Hopefully you can clarify something on the US business without using any animal analogies. (Mark Tucker: Can't promise that!)

Basically when I look at the VA margins you report that they seemed very high, they are comparable with AXA with about 40% of APE and obviously if I look at the other guys AGEON and ING, their margins are a lot lower for 2007 more like 10% of APE. That is a huge difference and obviously the concern is in the current market environment one of the different reasons could be explained by things like distribution but also it could also be described by the quality of the hedging that is backing these assets. How long does the bear market have to continue before you have to start revising take up assumptions on some of the options in the US and also VAs elsewhere for example Taiwan I remember that Old Mutual recorded losses on their Asian international business because it could not hedge the Asian element of the VA, could you also talk about how you are hedging that as well please?

Clark Manning (President & Chief Executive Office, Jackson National Life):
As far as the margins on the business go as compared to competitors, I can't tell you specifically what the differences are between our margins and their margins because that is very difficult to untangle from the information that is out there. What I can tell you relating to the topics that you raised is that all through the last cycle and all through the last calendar year or last twelve months is the financial problems in the US market have rolled out. We have taken a very hard line that we needed to price the benefits that we were giving, particularly the guarantees, at a level where we could hedge them. We have not backed away from that in the face of what has been very intense price competition in the US as I think people are trying to hold the dollar volume of their VA sales in the face of a market that is just not accommodating to that. As a result if you look at the hedge results that we have, on an economic basis we had a gain on our hedging in the first half of the year of about $50 million and the reason is that leading up into the end of the second quarter of last year when oil was cheap and we were concerned about the valuation of the market, we bought a bunch of options and we basically over hedged our position. We over hedged vega, we over hedged delta and that served us well. From an accounting standpoint you got a bunch of plusses and minuses between our economic hedge results and what flows through the accounting statements, but I think it was about $45 million positive result that flowed through the IFRS statements. We had a positive effect of cost guarantees in the EEV statements. So while the comparisons are hard to do and I certainly don’t want to talk about any specific competitors, it is very competitive over there right now with people trying to hold volumes. We are not playing there, we are not walking away from share, we are not happy about the share we have lost, we have added wholesalers and our activity levels for those wholesalers are at all time highs, but what we have not done is compromised pricing in any way and what we have done on the hedging side is remain fully hedged. That is what we are going to do. That is our response to the market, that will be the response as long as the market remains in its current state of turmoil.

Barry Stowe (Chief Executive, PCA):
The VA product that we sold in Taiwan was essentially a fairly stripped down product, a very simple product unlike what is sold in the US, effectively there is virtually no guarantee to hedge - Pete, I don't know if you want to add anymore detail.

Peter Lloyd (Actuarial Director, PCA):
Yes it I think it's worth pointing out the difference between the VAs in Asia and the VAs in the US. We don't put on guarantees in the same way. The only one specifically in Taiwan is the guaranteed minimum death benefit (GMDB) rider up to retirement date so it is essentially a decreasing term insurance at a very low cost to us; so as you say it is quite right that it is difficult to hedge.

Raghu Hariharan (Fox-Pitt, Kelton):
Just three questions if I may please. First on the IGD capital position; I was a bit surprised that the capital requirements are static at 2.1 billion Sterling despite such good growth, can you give us a sense of what the drivers are and if there is any capital efficiency or if regulatory requirements have come down because of product mix. Secondly the cash flow run rate or target for Jackson for the full year, if that is possible. And the third one I was wondering on the US, how does a regulator look at impairment of the bond portfolio and how does that impact your regulatory capital?

Mark Tucker (Group Chief Executive):
Clark are you happy to take in reverse order the regulator view and regulated capital and the cash flow.

Clark Manning (President & Chief Executive Office, Jackson National Life):
Right now the US regulatory standard is that you don't write down a security until it is cash flow impaired, effectively until the expected yield on the thing drops below zero. There is a proposal SSAP 98 that will probably take effect at this year end (would be my guess, that's the latest draft of the thing) that would require a recognition of losses prior and, would put in place something similar to an OTTI Standard, although it doesn't appear to be an OTTI Standard exactly. And we expect that to happen, we model it carefully, as far as its impact on our expected cash flow of the group this year, it has no effect, our capital position is very robust. As far as our cash payment to the group, within the constraints that Mark would probably put me in, it is projected to increase over last year, a moderate rate of increase, reflecting the development of the capital within Jackson.

Tidjane Thiam (Group Chief Financial Officer):
The two things driving the required capital, is fundamentally the business mix as you said and FX effects. There's been a change, the rounding doesn’t show it - you get the same numbers, the numbers are slightly different. We have a detailed brief of that and we can provide you with an update. But the balance is almost zero.

Greig Paterson (KBW):
Three questions, one is the Standard Chartered deal. I wonder if you could give us an idea what the impacts on margins would be in Hong Kong from the new deal? And when the new regions will come online, will it be the second or third quarter? That’s question one. The second is, market consistent EV, two of your competitors are actually on record saying that UK annuities and US fixed annuities will take a haircut. Do you have a view on that? And the third question is, I notice you did an assumption change in your US VAs and your positive assumption change of your VIF, something to do with higher future margins on VA products. I just thought in this environment that seemed to be odd. I would have thought it would have gone the other way. I wonder if you could just explain that?

Mark Tucker (Group Chief Executive):
Okay just dealing in reverse order Clark, on the assumptions and VAs.

Clark Manning (President & Chief Executive Office, Jackson National Life):
Change was the recognition of the dividend received deduction (DRD) on the VA. It’s something that we put in there, it’s always been in place. It’s something that should be reflected in the assumption so we made that change.

Tidjane Thiam (Group Chief Financial Officer):
Fixed annuities, Greig you're asking me if there will be a hit. You know how MCEV works fundamentally; you have to assume that you're making the swap rate on those investments. We believe that that’s not really reflective of the economic reality. But there is a very mechanistic effect due to that. That’s the way it works.

Mark Tucker (Group Chief Executive):
Whether or not it gives the true economic picture.

Tidjane Thiam (Group Chief Financial Officer):
It will give you a negative margin at the start.

Mark Tucker (Group Chief Executive):
In terms of Standard Chartered I think Barry perhaps can talk about when they will come online. There's no economic effect, it won't affect margins at all.

Barry Stowe (Chief Executive, PCA):
That's exactly right and in terms of when the new territories will come online. Given our model which involves identifying, training and putting pretty experienced FSCs in the branch, it takes a few months to get new territories up and running. So it's not the sort of thing where you see a dramatic impact I think even in the second half of the year you'll probably see more going into next year. The thing that would be more likely to have more immediate impact would be the introduction of new health products through the existing territories where we already have well trained sales people in the branches.

Mark Tucker (Group Chief Executive):
I think the other thing Barry with Standard Chartered would be the bank insurance the Hsinchu acquisition in Taiwan will begin to also come through in the second half.

Barry Stowe (Chief Executive, PCA):
It absolutely will, in fact the results on that are improving pretty dramatically month over month, in Taiwan.

Jon Hocking (Morgan Stanley):
Two questions, could you just put some scale on the Standard Chartered opportunity in Japan please? And secondly in the UK, on the bulk annuity business, are you back in this market aggressively and could you give some comments on the pipeline you see there please?

Mark Tucker (Group Chief Executive):
The scale of opportunities in Japan, can we put a scale around that – no. I think you wouldn't expected us to. In terms of bulk annuities, I'll let Nick talk about that. But I think the important thing Jon and, the important myth first of all to dispel there, is we were never out of that market, we've always been in that market. We've been selective but we've been in that market; and I'll let Nick talk you more through that and particularly what's happening.

Nick Prettejohn (Chief Executive, UK & European Insurance Operation):
You've stolen my first line Mark. We've always been in the market. We've been active and looking at deals. We've chosen actively not to look at many deals. The rate of activity in the market at the moment is significantly higher than it was in the

first half last year. So in terms of our pipeline, if you're interested in the pipeline. The pipeline is much much much larger; I could put what I regard as a meaningless value on it. But the reason why I think it's meaningless is just because deals are potentially in the pipeline doesn't mean you're actually going to write them. So I could give you a number, you could get very excited about it, and we could land up writing no business in the second half of the year or, we could land up writing a significant amount of business in the second half of the year. Our approach in that market has not changed one iota. We will continue to look at deals, we will continue to maintain our financial discipline in looking at those deals; and we will either write them or not write them on that basis. But the team is extremely active at the moment, whether that activity turns into actual business we'll see.

Mark Tucker (Group Chief Executive):
In the context of the UK, I think it's clearly worth noting, when you're seeing 18% top line growth and you're seeing margins and our IRR maintained, now that's a business that's performing exceptionally well and across the spectrum.

James Pearce (Cazenove):
First of all, thank you for slide 26, but could you explain why interest rates going up is good for your solvency, is bad for the embedded value? Second, could you explain the different outcome of your Orphan assets negotiations compared to other unmentionable company?

Mark Tucker (Group Chief Executive):
Sorry what was the second question James?

James Pearce (Cazenove):
Can you explain why you gave up on Orphan assets, whereas Tidjane's former employers just announced a deal? And then thirdly; why is with-profit good in this bear market whereas it was absolutely useless in the last bear market? What are the differences, why are you not having problems with MVAs and that kind of thing that soured the with-profit market five years ago?

Mark Tucker (Group Chief Executive):
Let's take that in reverse order, in terms of with-profits I think, Nick do you want to say a few words.

Nick Prettejohn (Chief Executive, UK & European Insurance Operation):
Yes I'll say a few words about that. I think you are grouping all with-profits products into one size fits all category when you talk about their performance. In the last

bear market actually our products performed pretty well through the last bear market. I think what's attractive for customers and advisors at the moment is the combination of smoothing and on the case of our Pru Fund product that's a transparent smoothing mechanism, there are no market value reductions in the Pru Fund product. But also the capital guarantee, which in the first half of the year about 70% of customers took. Actually what we are finding is that customers and advisors are extremely attracted to those features of our With Products product; and I would also I guess make the usual observation that our with-profits performance has been the best with-profits performance on one, three, five and ten year basis. So outstanding performance, strong product features, very attractive in the current market.

Mark Tucker (Group Chief Executive):
I think just for the reattribution I think was the perfect setup for that, Nick's first line was one size fits all, or one size doesn't fit all and that's exactly the same position. There are different types of funds, our fund is an open fund, is a growing fund. When you look at the amount of inherited estate as a percentage of a fund ours is around 10%, whereas Aviva's was double that. The factors, all of these different factors and the history of the funds just makes it a very different proposition. And it was our very clear view that it was in the best interest of shareholders and policy holders, the best long term interest not to go ahead with the attribution. Would you add anything to that Nick?

Nick Prettejohn (Chief Executive, UK & European Insurance Operation):
Maybe one other point, sort of pivotal to our conclusion about the inherited estate was the fact that we don't believe that we have a surplus for distribution within the funds. So we believe that fund is necessary to support the activities of the with-profits fund and to support the superior investment performance and security that's so attractive to our policy holders. That's attractive to our policy holders, it's also important to our shareholders as well.

Tidjane Thiam (Group Chief Financial Officer):
I said that when we were matched in an asset/liability management (ALM) sense, IGD is neutral. The problem is in a number of places we are not matched, if you take Korea for instance. What we have on the asset side is mostly DAC which is not an admissible IGD asset. So when the interest rates go up your liabilities will go down, so that it reduces your required capital and increases your surplus. And you have a number of places like that. So it's just ALM and interest rate impact on both sides of the balance sheet.

Mark Tucker (Group Chief Executive):

It is purely technical.

Trevor Moss (MF Global):

Three questions please. Having not written much fixed annuity in recent years, I was quite impressed actually by the way you almost seamlessly switched to the selling FA from VA during the first half of this year and particularly in the second quarter. Could you talk a little bit more about how easily that was achieved and what the outlook might be there? Secondly, you majored on health insurance a little bit at the Asian conference, I wondered if Barry might give us an update of the rollout of that programme and how we've progressed in the second quarter? Thirdly, a slightly different question. I think your shares are trading quite a long way below your sum of the parts Mark; and I was wondering how long you might be letting the shares trade so far below this number before considering taking some action to address the discount; and indeed what measures you might consider in that regard?

Mark Tucker (Group Chief Executive):

I think the shares are trading materially below the sum of the parts and they have been for some while. The way we look at this, particularly on the insurance side, is quite interesting compared to the banking sector. Because if you look at the two they are increasingly differentiated; in the banking sector you are seeing sort of almost winners and losers in terms of the share price. You are seeing the RBS' and the HBOS' at 55%, 60% falls. And you're seeing the Standard Chartered and the HSBC at the other end 5%, 6%, 7% falls and they're being quite resilient in this market. In the insurance sector you're seeing almost no differentiation. And I think it's interesting when you look at the factors that are behind Standard Chartered and HSBC, we have exactly the same ingredients, when you look at the openness to the emerging markets, and the emphasis is on emerging markets, the distribution mix, the non-reliance in any one country; all of these factors to us are almost the same as the banks, as Standard Chartered and HSBC. I think increasingly, we see there will be a differentiation as again markets begin to see the value of our businesses and our franchises. In this market place, I think what we're determined to do is to continue to deliver. I think we clearly have a number of ideas and things that we may or may not do in the future, but the focus has got to be on delivery. If we don't have delivery, we have nothing. That is the focus. To watch share price everyday, I think you can get seriously dizzy. I think the basis of what we do is, we must concentrate on what we can control. I was PA to a Group Chief Executive here many years ago, who said to me two things, he said if any Chief Executive who thinks they can either control the share price or the media or the analyst community, is delusional. And those words ring absolutely true. In terms of health insurance - Barry?

Barry Stowe (Chief Executive, PCA):
Sure. In short it's going very well. I think Mark or Tidjane, one showed you the 56% growth rate number. It's becoming a larger share of our overall premium production which is really good news. We're moving very strong and steadily in terms of getting product launched in different territories. We've had a couple new products in Taiwan, one just launched, kind of early to say what the results would be, but we're very optimistic about that. Health products just launched in Japan about a month ago, very optimistic about that. To remind you of the impact this has, if you go back and look at Singapore where we launched our first sort of new generation product which was now about 14, 15 months ago. The margins coming out of Singapore have moved up materially in a very significant and helpful way. So we're on a steady course and so far that's just all good news.

Mark Tucker (Group Chief Executive):
Clark, the third question.

Clark Manning (President & Chief Executive Office, Jackson National Life):
Fixed annuities, almost all of what we sell in the US in fixed annuities is annually re-settable. So we can reset the credited rate every year. As a result, what we compete against are typically short term certificates of deposit (CDs). Over the last several years with the flat yield curve, we could not be competitive with say one year CDs and as a result we didn't sell much. As the curve has steepened, sales naturally flowed into the product. It didn't want to flow into equity products right now because of the perceptions of equity market volatility. So it wants to flow into fixed. We left the wholesaling force in place, we kept the relationships intact, it was a very frustrated wholesaling force for several years. But we held everything together and so the sales just naturally flow into the fixed annuities in this sort of equity environment and with this shape of the yield curve.

Yousseff Ziai (RBS):
Two questions please. One is on China, when we visited Asia, we were told that pension business had prospects of opening up in China. I wonder if you could perhaps update us on that. And secondly, I'm thinking vis-à-vis your arrangements with Standard Chartered Bank. Given where your share price is, if there was another bank which was capital strong and wanted to have a go at you. Is there financial penalty in breaking the Standard Chartered agreement and is that a large penalty?

Mark Tucker (Group Chief Executive):
With the latter, we don't talk about the detailed terms, so I'm not going to give you any sense of the commercial terms. You would expect us, as you would expect Standard Chartered to take that position. What I can say is we have an exceptional relationship that's been going on. We're now in our tenth year of this relationship and we see this continuing as we've announced well into the future. With commercial terms I don't think you'd expect us to give. Barry in terms of China and pensions?

Barry Stowe (Chief Executive, PCA):
Well there are going to be enormous opportunities and in fact there's already a lot of work going on to pursue those opportunities. No big announcements yet, but there's absolutely no doubt that there's going to be, not just in China but in a number of Asian markets there's going to be some large scale pension opportunities and we've got a very highly qualified and experienced team on the ground, that's pursuing opportunities now. So we're very optimistic about that.

Mark Tucker (Group Chief Executive):
Blair, we'll get to you eventually.

Blair Stewart Merrill Lynch):
I've got three quick questions. Could you give as an idea of how far you are away from the market in VA pricing in terms of what your charges are relative to the average in the market? You talked about some irrational pricing. Secondly, I think Mark you were quoted on the newswires as saying you expected margins in Asia to finish the year around the current levels. I don't know if that was a misquote or if you were referring to product by product margins, can you perhaps clear that up because I think there was an indication that margins are seasonally stronger in H2? Thirdly, you talked about the impact on your solvency from a certain level of defaults versus expectations. Could you comment on that in respect of what happened last time particularly in the US and what your expectations are going forwards for that?

Mark Tucker (Group Chief Executive):
In terms of the VA side, Clark do you want to take that at VA pricing compared to competitors?

Clark Manning (President & Chief Executive Office, Jackson National Life):
The benefits all differ slightly, so I can't say this is an identical product. But when we run our pricing models against some of what are the current hot benefits out there, we're generally 20 to 40 basis points off of those. Sometimes, in a couple of instances more, but that's kind of a good general range and that wouldn't be off of every benefit in the market, it's off of some of the hot ones right now.

Mark Tucker (Group Chief Executive):
I think again, I wouldn't be the first Chief Executive to say they were misquoted during the conference call. I think I said at or around current levels and you're right there is a seasonal factor in the second half, we would expect that to kick in again, there's no reason why it wouldn't kick in. In terms of solvency, Tidjane will respond.

Tidjane Thiam (Group Chief Financial Officer):
Okay what we've done is quite stringent because we applied this default across the board, across the market you'll see that generally between the long-term trend and the worst of the credit cycle you will get three to five times more credit default than you had before. But even five times is comparable with what we had in the US last time Clark is that correct? We went from 2% to 10% are the numbers I have in mind so it's pretty extreme again.

Mark Tucker (Group Chief Executive):
On regulatory capital, the IGD position we had in going into 2002/2003 was FCD then, was clearly significantly lower than it is today. I think in 2005 (my numbers may be wrong) we had sort of 600 to 800 today it's £1.4 billion.

Tidjane Thiam (Group Chief Financial Officer):
Twice stronger in this period.

Mark Tucker (Group Chief Executive):
Yes.

Tidjane Thiam (Group Chief Financial Officer):
So we're starting from a stronger position and as I've explained the way we manage on that is also fundamentally different so the impact will be different.

Mark Tucker (Group Chief Executive):
Five times would be £220 million.

Tony Silverman (Standard & Poor's Equity Research)
I'd just like to come back on the bulk purchase annuities in the UK where you mentioned you had a very busy pipeline but it may turn out to be no different. Are you finding you're getting to the second round of these bulk transactions more frequently than say six months ago? I think the noise in the industry is that you are, so I wondered if you could perhaps give us some colour on that. I'd also like to ask if there may be any opportunities, or you'll give us some colour on fixed index annuities in the US and perhaps whether the possible requirement for distributors to be registered with the SEC may for example present any opportunities.

Mark Tucker (Group Chief Executive):
Clark, you want to start?

Clark Manning (President & Chief Executive Office, Jackson National Life):
I think you have to keep the FIA market in the US in context. There were in the First Quarter, the last date we have industry statistics available, there was $63 billion worth of annuities sales, fixed indexed annuities were 6 billion of that. Variable annuities is really where it's at, at 42 billion. Fixed indexed annuities are under a lot of market conduct pressure in the US right now, there was Dateline show – Dateline's one of these news magazine shows and you have the camera crew busting in on an FIA sale and it's really, really bad for perceptions of the product. The SEC is responding to that and some of the pressure coming from the Attorney Generals of some of the States related to that product type. I think we have seen this coming and we've talked about some event like this coming. Our focus has been in the broker dealers and in the banks selling product that is more straightforward than the product sold in the general agency segment of the market. As a result our position has been we're No. 1 in the broker dealers and right now we're No. 2 in the bank - we bounce back and forth between No.1 and No. 2 in the banks; we like those positions given this. We've been filing all of our sales material with FINRA to get it reviewed by them, so that it basically meets FINRA's standards. We've been holding seminars with broker dealers about how they would properly supervise FIA sales in light of the bulletin 0550 in which they strongly advise broker dealers to supervise fixed index annuity sales by registered representatives. So we've positioned ourselves I think very strong on this and have good positions in what is really just a sliver of the FIA market.

What will happen as a result of this, my guess would be, the market will shrink. The business is being written non-registered today I don't see just flipping over to be written registered, because the reps that write it, while they maybe registered can they really write similar products through a broker dealer. I'm sceptical there, that's not what our strategy is built around. If I had to guess, my guess would be it's going to take a couple of years but this requirement for registration will probably go through in some form and that will be good for our position and the banks and the broker deals and we'll have our larger share in a smaller market, but it's not our primary focus.

Mark Tucker (Group Chief Executive):
Nick anything further on the bulk side.

Nick Prettejohn (Chief Executive, UK & European Insurance Operation):
Reiterate the point that we haven't changed our return criteria so nothing's changed in terms of what we're doing. I guess what's happened is partly good old fashion supply and demand. If you look back to the first half of 2007 there were an awful lot of people who had capital that they wanted to deploy and there weren't actually that many deals to write, whereas now there are a significant number of deals out there. Some people have rather hastily deployed their capital and I think perhaps we're reaping the benefits of that in that some of the competition that may be now looking at the returns that they achieved on the deals that were written during the course of the last year. Hare and tortoise I think we've been very cautious in this market place and maybe that caution is being rewarded.

We are reaching the second round of more transactions, that isn't as I say because we changed our return criteria. I think interestingly what's happened we've seen in a number of situations there is a real appetite to do business with the Prudential; to do business with a strong brand that is saleable to pensioners and also a business that has very strong financial security.

Tidjane Thiam (Group Chief Financial Officer):
Can I just say a word on it, as a new CFO, you can imagine I'm not keen to move any hurdles and what I've seen with Nick and his team is that the deals they're bringing absolutely match the hurdle rates we have. So it's probably something going on in the market that drives that evolution, there are good deals and, we are hitting our hurdles.

Andrew Crean (Citigroup):
I want to clarify Tidjane; you talked about margins on a MCEV basis and US fixed annuities being negative. I don't think you answered the UK annuities part of Greig's question; and just going on from that I noticed that since a year ago your assumed corporate bond spread in the UK has now gone up from 70 to 170 basis points. The liquidity premium in swaps is probably only 50 or 60. What would be the impact and

I assume also there'll be a problem in the US where you're assuming spreads of 175 basis points. What will be the impact of market consistent on your EV as well as on that UK annuity question?

Tidjane Thiam (Group Chief Financial Officer):

I think Andrew it's a very interesting question (actually, I think the liquidity premium went from 84 to 101) but the point is, we are committed to disclosing the MCEV numbers in due course. There's been a 25 basis point increase in the spread and we've considered 75% of that (i.e. 17 basis point) as liquidity and 25 as credit. That is what we've done and it's in the papers; but the point is we will communicate in due course on the impact of MCEV so we wouldn't expect me to go any further here today but in due course we will present all these impacts. As a whole, I think it's not really productive to pick individual products and try to have that discussion now, we will in due course talk about it in adequate level of detail.

Mark Tucker (Group Chief Executive):

Yes I think, generally we're focused on running the business on an economic value basis, on the economics not the accounting. I think we will come back and do that in some depth but I think we've got to have a clear focus. David Belsham, is there anything else you want to add to that? No - fine, next question from Matt.

Matt Lilley (Lehman):

Just on the margins in Asia you showed the year-on-year comparisons and they're very similar but as Blair mentioned they are down a bit country-by-country from the full-year; so Hong Kong was down 7 percentage points, Korea down 4, Taiwan down 7. If that is seasonality what is it? Is it lower volumes or different products and what will happen in the second half of the year?

Mark Tucker (Group Chief Executive):

I think there's a mix - I saw that as one of your questions that you sent out this morning so I'm glad you asked it and we're of course well prepared to answer it. But I think the basis Matt, it is a mix and I think it was Barry who said earlier you've seen margins in Hong Kong go up and there are general movements throughout the portfolio during the year. Overall at that 46% margin we expect that to be at or around I think it was the terminology, not to recommit myself to anything but I think we expect it to continue to move up. We manage this in the individual countries; we don't manage the overall margin. Andy?

Andy Hughes (JP Morgan):
It's a follow up question from Andrew and Greig's questions on MCEV. You mentioned that the economics are important and not the accounting, but obviously if you look at your current accounting treatment it looks as if there's not a lot going on in terms of the US credit impact because you got a buy and hold strategy in the US. The market value of the bonds fall, it doesn't really impact the EV at all. When you move to MCEV and potentially when there's new regulatory changes implemented in the US, things will change. Will that change your appetite to buy and hold? Will you then become more sensitive to managing your embedded value or will you just tolerate spread movement and the impact on the embedded value?

Mark Tucker (Group Chief Executive):
Clark are you happy to take that?

Clark Manning (President & Chief Executive Office, Jackson National Life):
In the US, the regulatory accounting is book value accounting so MCEV *per se* won't do anything on that. The SSAP 98 will have some impact on surplus from the OTTI marks - let's say it's not clear that fair value is going to be the standard in the US though right now as SSAP 98 doesn't appear to be moving towards fair value as the standard, just a tighter standard than recovery of principle. But that will have some impact on surplus but if you look at our current surplus position, current surplus Risk Based Capital ratio (RBC) ratio is 535. If we look at our largest competitors their average RBC ratio is 450, and the median RBC ratio is 383. If we disgorge a billion dollars out of our surplus RBC ratio is 419 so we have a very strong capital position. If we have to absorb some of these losses, fine. As far as the appetite for fixed annuities in the US - if the accounting conventions became so awful that you had to start carrying a buffer on regulatory capital to take into account just surplus swings, well at the end of the day true economics or cash flow and cash flow is defined by regulatory accounting so that would have an impact. Right now the accounting is such that we're able to look through to what we think the economics are in that position and it's stuff that's on the table right now, I don't think it really changes our position or various lines of business.

Greig Paterson (KBW):
Sorry mine was just a point of clarity, if I'm not mistaken under US statutory solvency regime don't you only smooth it over a number of years into the surplus number and hence, it's quite a significant buffering effect? Am I correct in that understanding?

Clark Manning (President & Chief Executive Office, Jackson National Life):
It depends on the characterisation of the loss; on whether the characterisation of the loss is as credit or interest rate related. If you take a credit impairment on a bond that you hold, my understanding of SSAP 98, and again this isn't anything but a proposal right now, so we're speculating about speculations. As SSAP 98 is right now, as I understand it, if it's credit impairment you'll mark it through your asset valuation reserve (AVR) which is typically counted as capital. Normally you'll get capital in the US on a regulatory basis as capital surplus and AVR. If you sell a bond, if it's not been downgraded more than two NAIC categories where that would equal two notches from a rating agency category like from A to BB. If it's gone down two notches at least, then it goes into AVR and, if it's not gone down two notches, it goes into Interest Maintenance Reserve (IMR). The gain or loss in the IMR is amortised over the remaining life of the security as if you had continued to hold it, the AVR charge is a time specific charge through that reserve.

Mark Tucker (Group Chief Executive):
You asked for that! Thank you for coming today, we appreciated your time and we'll see you soon.

[END]