Prudential 2016 Full Year Results

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2016 Operational Highlights

Mike Wells

Group Chief Executive, Prudential plc

Introduction

I think I know most of you. I am Mike Wells, I am Group Chief Executive of Prudential. Starting my 22nd year with the Group, and some of you I have known a decent part of that. Those of you who are new, welcome. I am obviously very pleased with the results for the year. I was kidding with a colleague in the States who called at a very early hour. He said, 'It looks like you guys had a very easy year.' I do not think there is anybody in the team here or anybody in the audience who would suggest last year did not have its challenges. We saw regulatory changes, we saw political changes and we saw rate movements that were volatile, I think is a fair description, and equity movement across all of our geographies. Against that backdrop, I am exceptionally pleased with the results.

Group

2016 headline results

I am going to assume you have all read and reviewed the normal caveats about forward-looking statements etc. and get right to it. How did the year look and how did the year finish, more importantly? We ended up with £4.3 billion of IFRS operating income and we think that is a very good number for the year. The £3.6 billion of cash equally as important, up 10%. The Asian earnings driving that, up 15% to £1.6 billion, and again their cash up 15% as it should be to £859 million. Strong progress towards the objectives. I will give you a bit of an update on those in just a minute. Then from a Solvency point of view, we are pretty well rehearsed on our view that Solvency II understates our capital position. However, even on that basis we came in at over 200%, £12.5 billion of surplus. We think that shows the strength and resilience on any metric you would like to measure the Group. Again, pleased with that outcome and just how much capital this Group can generate. Then finally, did that translate through to dividend? It is a 12% increase in the 2016 ordinary dividend, so we think the breadth and the consistency of the results across the year and across key metrics were key. What is embedded in there a bit, it is a little harder to see, was how good the second half was for us. When we were up here for 2015 we said it was a tale of two years. I think the 2016 was almost to the week, but what you did see in the second half was broader success in Asia, better inflows in M&G, a shift in direction of winds in the US, and I will get into those a bit. However, the second half of the year felt better than the first.

Delivering profitable growth at scale

I did review some of my previous presentations with you prior to today, and one of the terms I use a lot is scale. I wanted if I could, if you will indulge me, to put a little context around the thinking in that and how we view it. I think it is important when we talk about the Group, why you own it and also how it competes in its capabilities. One of the measurements of scale, and this is arbitrary and you could argue it is a bit self-serving, is our ability to increase our earnings by £1 billion. I would argue that is scale. It is an adult number. One of the measurements of whether you can see the business that you own improving is the frequency at which we can get that additional £1 billion of earnings. I think if you look at that, it would imply the underlying business has to be doing things more efficiently and more effectively with its capital and its resources to accelerate that growth, so that would be one argument I would make with you. Again, I think the growth is unique to the sector, and certainly that level of growth is unique to the sector.

Translating into strong shareholder returns

That is frequency; how do I measure the quality of the scale? How do I know that you are actually building something that is sustainable? How do I know that it actually produces measurable, tangible results that will come back to the shareholder? That is, I think, the dividend. A lot of discussion around dividend. Let us look at it in the short term and long term. Up 12% year over year. Now totalling £6.8 billion of dividend to our shareholders in the last decade. Again, that scale is translating to quality measured in terms of simply nothing more complicated than: can it produce cash? Forgetting any insurance accounting.

Geographic footprint aligned to significant demand

Then I think the biggest challenge I heard over the year in 200-plus investor meetings we did was: is it repeatable? Can you do it again? Is it possible that Prudential can continue to grow? Today in the results that we are going to talk about, most today are about the red bars here, the portion of which we have penetrated, where our successes are. Some of this is well rehearsed and we will go through it a bit again with you as the day progresses. The upside, the structural demand in these markets, is the grey piece. Is there room in our various markets for us to continue to grow? I think there is. I think we have chosen our markets carefully, and I think you are seeing that execution today. There is significant upside in the businesses and in the markets we have chosen to play, and it is our responsibility not just to deliver the results we gave you this year but to make sure the franchises are built to address that demand.

Disciplined execution delivering strong returns

We have said it is a value over volume strategy. Discipline is a word that I know gets thrown around. We are disciplined with your capital. We are disciplined with the way we run the firm. Can you measure that? Yes, the allocation choices we make. The businesses we have chosen to exit, UK annuities and effectively universal life business in Asia, Japan and Korea. When we choose to go further into a JV or not, these are all conscious decisions made by this Group to look at the shape of the earnings that we have for you in total. We look at the total rate of return, we look at the source of the earnings and we look at the return of the capital. What is the frequency of that? Can you measure that? You can. You can measure that in an IFRS ROE number, which for us is 26%. We think we are reinvesting for you at rates of return that are highly competitive, and payback periods that are very short. This is what we mean when we say a capital-light, agile, learning organisation.

Asia

Consistent new business growth

Is it repeatable? Asia has probably got one of the most dramatic slides in the deck on this. This is their 30th consecutive quarter of year-over-year growth. To be clear, this is not with a top line orientation other than the competitive nature of the team. They are not paid on market share; they are not given every product that they could sell, that competitors have, to drive market share. There is no product in the sector, in the broadest definition of Asia, that we cannot replicate if we choose to. There is no secret sauce, if you will, right now in Asia or any other market we are in. They are conscious decisions where we have or have not chosen to allocate our people, our systems and our capital. The growth we are getting is in the segments we chose, leaving behind certain segments, and I think it is still extremely compelling. Again, why? Because it aligns with market demand.

Compounding revenues

How do you measure quality of earnings in Asia? One of them is recurrence. Again, 93% of what they are selling we have a long-term client relationship that continues year after year after year, in both the benefit we provide that consumer and the earnings that it provides our investors. I think this one is an interesting look at the revenue of our Asian model. This captures the historic success. Clearly, these numbers are dramatic. If you look at the £3.5 billion in the blue on the bottom here, what is the effect of that revenue from the previous slide? It is very dramatic. It is also the level of the back book roughly in 2008. What you are seeing here is the compounding effect of the existing clients as those vintages we are talking about are staying with us year after year. All the success our teams have, all the great choices they have made, the correct choice of markets, products etc., we have grown in this slide from seven million to 15 million clients. A little upside left there, given the greater population in Asia. Second, that is an increase in 20 basis points of market share, effectively ex China. Is this team capable of doing more? Absolutely. Tony and the team since November have been looking at what Asia should look like at the next five and ten years, and we will come back to that a little bit more later in the day. We will give you a lot of detail on that later in the year at the Investor Day. However, we think there is much, much more to do, and the simple structural demand of Asia is measurable. The success we have had at these sorts of incremental levels has produced a dramatic result financially. I think the relevance of this is there.

Growing assets

You are not going to get there without asset management. It is an incredibly low penetration business still in Asia, while wealth is growing at a multiple of it, so we think there are tonnes of upside. We have told you we are investing in systems and people. At Eastspring, you have seen us do that and we will continue to do that. Eastspring had another great year.

Delivering compounding growth

Is it producing profitable growth? Yes. This is driving towards the objectives. Multiple times now, this Asia business has doubled in its operating income. You see the trajectory from the previous slides: it is earning power from those existing relationships, having sold the right products, having priced the products correctly, the tailwind that gives you. We are obviously very pleased with it.

US

Disciplined execution

Going to the US, a fairly material shift in the winds here politically. You may have noticed there was an election. The major impact for us was the DoL change. There is lots going on in the country. Are lower taxes good for us? At the consumer level, yes. Are they good for us at the corporate level? Yes. There is bipartisan support, I think, for both. The Department of Labor language that was in the previous administration's past changes can certainly use a clearer, more consumer-centric review. It is getting that now. That has, we think, shifted from a bit of a headwind to a tailwind. Is it a flight to quality? Is it saying that advice should be better or products should be better? It is. There is bipartisan agreement on that. A flight to quality in the US, as you have seen previously, is a flight towards Jackson. It has the best products in the segment, it has the best technology in the segment, it has the best wholesaling in the segment. All those capabilities will be key where it is going, but it had a very good year last year. It captured the majority, if not 100%, of the industry's net inflows in the variable annuity business. It had good growth for the consumers and the shareholders of the separate account assets, and you saw a very strong capital position. Again, this is after we renewed a permitted practice.

UK

Navigating change

In the UK, as we shift these businesses to a capital-light model, the demand we are addressing here is the self-reliant savers in the UK. A lot of pieces moving. I talk to a lot of retirees here, talk to a lot of pre-retirees here socially; people are trying to figure out, as they are in the States, how to navigate their retirement assets in a relatively or an absolutely low-yield environment where they are going further and further up the risk spectrum. We have unique products and services through that. We have an excellent asset management firm, and Pru UK can generate smooth, blended products, be it drawdown or accumulation, that are working very well in the marketplace. As the consumer gets more and more control of their assets, they are demanding more stability of the underlying product. They are getting longer-term in their thinking. That is our piece of the market; that is our segment. We are not a short-term trading account, we are the part that they want stability and predictable returns as they head into retirement and as they are in retirement. Again, the structural demand is there. Both our UK businesses are meeting it, and on the institutional side you see M&G Pru seeing the unique, longer-term, in some cases less liquid solutions for institutional clients at scale.

Group

Strong progress on 2017 objectives

The objectives, feeling pretty good about them now. I will let you back into your forecasts, and if you think we will hit them or not from here. However, you can see where we are in progress of them. We think they are solid. Also, think they were the right metrics. Again, you are measuring earnings and cash, back to how we look at the business. Again, we think with the support at the Group level and what we have seen in Asia, we are consistent with what we stood up here and told you when we placed these targets in front of you.

Key take-aways

Finally, before I hand it over to Nic, just a quick recap. We do not see any material change in the structural demand we have for the products or services of the company. If anything, in the US and a bit in the UK that demand is up. Asia continues to underpin the growth, just given the absolute scale of the structural demand of that part of the world and our ever-improving capability to address their needs. Our ability to execute in a variety of climates, political, regulatory, interest rate, equity, continues to improve. I think we have demonstrated that. I think we are agile, and agile is good for a firm our size. It is something that we challenge ourselves with. Can we compete? That can be anything from an entrance to a new market to an exit from a market. Both require the same basic skills corporately, and I think we have demonstrated that. Then you see a very strong balance sheet, very defensively positioned – again, the right way to be, we think, in this sort of climate – and well positioned to capture some very long-term value for you. With that, I want to turn it over to Nic and let him walk you through some of the more granular financial details.

2016 Full Year Results

Nic Nicandrou

Chief Financial Officer, Prudential plc

Key financial highlights

Continued delivery of 'Growth and Cash'

Good morning everyone. In my presentation, I will take you through our full-year results highlighting the key drivers of our performance in 2016, and I will then cover the Group's capital position. Starting with the financial headlines, in 2016 Prudential delivered another strong performance across our main 'Growth and Cash' measures, and achieved new highs during a very challenging year. As you can see, new business profit increased by 11% to £3,088 million, IFRS operating profit moved to £4,256 million and free surplus generation was up 10% to £3,588 million. Currency effects have been a significant positive, adding between 8 and 13 points to our results when reported on a sterling basis.

This performance demonstrates once again the benefit of the Group's structural positioning, the strength of our earnings diversity by geography, currency and source, and our ability to execute with discipline and focus. The sizeable contribution from operating earnings combined with our effective management of the balance sheet have driven our Group solvency surplus higher to £12.5 billion, and increased our embedded value by 22% to over £15 per share. Our strong performance during 2016 has enabled us to rebase the full-year ordinary dividend to 43.5 pence per share, representing an increase of 12%. While last year was a true test to the qualities of our Group's strategic and financial attributes, in my view these results tick all the boxes, with strong earnings and cash levels backed by a robust balance sheet.

Strong progression in key earning drivers

Asia Life growing in scale and quality

Before looking at the results in detail, I want to take a few minutes to remind you of the key drivers that underpin the Group's earnings momentum, both now and in the future. We said on a number of occasions that the diversity, quality and scale of our franchises provide us with enormous strategic flexibility. Asia exemplifies these attributes and anchors the Group's performance. Our platform in this region has become adept at consistently capturing recurring revenue across market cycles. PCA's broad product offering, wide distribution reach and pan-regional presence saw it attract £3.4 billion of new regular premiums in 2016, up 20% on the previous year. Adding this new business cohort to our already sizeable in-force book increases the recurring premium base by 21% to £12.6 billion, a clear illustration of the power of compounding.

Underlying this growth in premium revenues is a relentless focus on quality. Our preference for health and protection income, which is uncorrelated to markets, is a well known fact. We have maintained our emphasis in this area during 2016 and increased the contribution from insurance income by 24% to over £1 billion for the first time. This growth is broad-based and, as shown in the chart on the right, all our Life operations have reported healthy increases. Our strategic choices, product, country and distribution mix continue to translate these revenues into profitable earnings growth. The enduring nature of consumer demand in the region, and the consistency of our execution, drive a strong annual profit progression and underpin the long-term outlook of our business in Asia.

Asset management businesses building fee-earning base

Moving to our asset-gathering businesses, the dynamics here are similar in that we are accumulating assets in our chosen market segments in a disciplined manner. Our ability to grow earnings in these businesses is dependent on consistently attracting profitable new flows while retaining existing assets, and on managing costs with discipline. In 2016 we were amongst the very few in the US industry to generate positive flows into our variable annuity business. This is a commendable performance in a year that has been disrupted by regulatory uncertainty, and highlights the strength of Jackson's position in the industry. Overall, separate account assets were up 11% to $148.8 billion.

In the UK, we continued to benefit from the strong consumer preference for PruFund's smoothed return multi-asset characteristics, which we make available through a broad range of products. Our strong momentum here is generating significant inflows which are close to reversing the outflows from our legacy portfolio that have been present for many years.

In our asset management businesses, we saw an improved picture in the second half of the year, with Eastspring generating external net inflows of £2.2 billion in this period and M&G reporting positive retail net flows of £0.9 billion in the fourth quarter. Taken together with the effect of the market rebound, M&G grew third-party assets by 8% to £136.8 billion and Eastspring increased total AUM by 13% to a new high of £117.9 billion. This positive momentum in our four asset-gathering businesses bodes well for future earnings.

Capital allocation

High capital velocity

Our ability to translate top-line growth into earnings and then quickly into cash remains a distinctive feature of our Group. We do this by consistently directing our new business investment in a disciplined manner, targeting capital-light opportunities with high-return and fast-payback characteristics. This value and cash-based risk management philosophy pervades everything that we do as a business. We will not hesitate to take actions which protect our ability to grow future cash, even if this means that we have an uncomfortable top-line message in a given quarter or year. Consistent with this philosophy, during 2016 we took a number of steps to scale down our presence in UK annuities, stopped selling Universal Life in Asia and took multiple pricing actions in response to low rates. As a result, the £903 million invested last year will be recouped in just over two years, and will generate sizeable free cash thereafter. The capital velocity created by successive additions of profitable new business vintages, combined with the disciplined management of our large in-force book, underpin the Group's future 'Growth and Cash' momentum.

Group solvency position

High-quality and resilient capital

The capital-generative nature of our business comes through on all financial metrics, including Solvency II. Driven largely by organic capital generation, our year-end Solvency II surplus increased to £12.5 billion, equivalent to a cover of 201%. By taking actions throughout the year, we also improved the resilience of our solvency to market shocks, as illustrated by the more muted sensitivities at the end of 2016. I will repeat my previous comments that Solvency II is an imperfect fit for Prudential, given our predominantly non-EU business footprint. As I have shown you before, Solvency II underplays the true strength of the Group as it excludes meaningful sources of real economic value which are shown on the right.

So what my introductory slides demonstrate is that Prudential enjoys a distinctive set of financial attributes which are our key sources of strength and resilience, and provide us with the flexibility to adapt to all parts of the cycle without compromising delivery.

Group IFRS profit

Growth in Asia and US fee business underpin 2016 earnings

Returning to our results for the year, IFRS operating profit increased to a record level in sterling terms of £4,256 million, equivalent to a return on equity of 26%. Once we exclude the positive currency effects, IFRS profit was 2% lower in 2016, influenced by the areas of anticipated decline that I referenced last year, which have played out largely as expected. These areas related to lower spread earnings from the US due to the effects of declining yields; weaker profit from M&G as a result of retail outflows; and a slightly reduced UK core profit, reflecting the effect on annual earnings of higher longevity reinsurance.

The financial impact of these items is summarised in the grey box on the right. The chart also shows the contribution from UK non-core, being annuity profits in the white boxes and those from management actions and other items in pink. These were lower overall in 2016, and I will come back to the reasons later in the presentation.

We have seen strong growth from our two largest contributors to profits, namely Asia where earnings increased by 15%, adding £213 million to our total profit; and Jackson's fee business, where profits rose by 21% adding a further £266 million. Between them, these two components account for 76% of our IFRS profits. The ongoing strength of our performance here has enabled us to absorb both the cyclical challenges in other parts of the Group and the reduction in UK non-core items.

Asia Life

Strong and consistent growth across key metrics

Turning to the results of each business, I will start with Asia where we continue to deliver strong and consistent growth across all metrics. New business profit increased by 22% to £2,030 million, outpacing the 19% growth in sales. This three-point uplift is primarily driven by favourable country mix. The contribution to NBP from health and protection remains significant, rising 22% in the year.

We saw strong new business momentum in the fourth quarter, with APE exceeding the £1 billion mark for the first time and eight countries posting sales growth of more than 20%. This pattern of broad-based growth has continued in the first two months of 2017. Sales in

Indonesia stabilised in the final quarter of 2016 and were broadly in line with the fourth quarter of the previous year. Here, the long-term prospects remain strong, and we continue to take steps to enhance our capabilities and extend our distribution reach.

Life IFRS profit in the region increased by 15% to £1.5 billion, for all the reasons that I outlined earlier, with earnings in six of our markets growing at an even faster rate. Free surplus generation was also 15% higher, reflecting disciplined business growth. This strong cash generation is being delivered alongside growing our store of future value, represented by PCA's embedded value of £18.7 billion, up 35% from the previous year and twice as big as four years ago.

US

Disciplined execution of fee-based strategy

In a year where the US Life market experienced significant regulatory disruption, Jackson generated positive variable annuity net flows and delivered higher earnings, whilst at the same time positioning the business for the new environment post DoL. Although VA sales were down 25% overall, roughly in line with the industry, new business profit declined at a lower rate of 13% due to a shift in mix towards higher-margin sales. In line with our guidance, spread margins declined to 217 basis points as the impact of lower yields is now feeding through. We still expect spread margin to trend towards the 150-basis-point mark over the next two to three years. While risk-free rates have risen since we last updated our guidance, the impact on yields has been offset by narrower credit spreads.

Fee income remains the key contributor to our US earnings, representing roughly three quarters of Jackson's total IFRS profit. Fee income rose in line with the growth in average separate account assets, with fee business profit rising faster due to a combination of lower strain, ongoing cost efficiencies and a positive effect of DAC deceleration. The $10 billion increase in separate account assets in the second half of the year is a clear positive for Jackson going into 2017.

UK Life

Retail propositions driving growth in new environment

The results from our UK Life business have a number of moving parts in 2016. Before I cover some specifics, I will summarise the three key take-aways for the year. The first is that we experienced strong demand for the PruFund product proposition, reflecting its structural advantages in the current environment and its excellent performance track record. The strong volume increase in 2016 was primarily driven by market share capture in drawdown, personal pensions and ISA new business flows, products where we historically punched below our weight. Going forward, market-penetration-led growth will inevitably moderate.

The second take-away is that the contribution from the core with-profits and annuity in-force business continues to track in line with our guidance, producing a stable earnings stream which totalled £601 million in 2016. The third take-away is that the UK Life result is entirely driven by the outcomes of commercial transactions, with no contribution from reserve releases.

Turning now to a few specific items. In the second half of the year we took further actions to underpin PAC solvency which, combined with those taken earlier in the year, delivered

£197 million of profit from longevity reinsurance deals and £135 million of profit from repositioning the asset portfolio. Our longevity reinsurance programme now covers £14.4 billion of annuity liabilities, which is 42% of the book. While the value trade-off is appropriate, the additional reinsurance will reduce the 2016 core earnings base by a further £15 million per annum. Furthermore, we have established a provision of £175 million for the costs of undertaking a review of internally vested annuities written since July 2008 and the related potential redress. While the outcome remains uncertain, please note that we have not factored any potential insurance recoveries of up to £175 million.

Finally, new annuities profit declined in 2016 as we scaled down our presence in this market. From February this year, vesting customers wishing to annuitise are being directed to a panel of third-party providers, so you should expect this line to fall further in 2017.

Asset management

Improved performance in second half

Turning to our asset management operations. After a more difficult start to the year, M&G and Eastspring both reported improved performance in the second half of 2016 in terms of profits, net flows and assets managed. At M&G, profit declined by 4% to £425 million, reflecting the negative revenue impact of six consecutive quarters of retail net outflows; the effect of which was only partially mitigated by higher fee income from institutional business. Improved fund performance produced a positive retail flow picture in the fourth quarter, which has continued into the first two months of 2017. In line with our guidance, the cost/income ratio moved higher to 59%, as M&G continues to invest in its proposition, develop its infrastructure and take structural steps in relation to its European-sourced business. For these reasons, you should expect the cost/income ratio to remain around the 60% level in 2017.

Eastspring had another good year, with double-digit growth in both profit and AUM. Revenue growth was slower at 5% due to a shift in business mix; however, our tight control of costs drove a two-point improvement in the cost/income ratio.

Group

Free surplus generation momentum maintained

Moving to cash generation, free surplus after investment in new business increased by 10% to £3,588 million. This result primarily reflects higher contributions from our Life in-force portfolios, driven mainly by Asia and the US. Experience remains positive, and includes the net benefit of the UK non-core items and a £236 million contribution from a contingent financing transaction on certain US term life reserves.

Asia remains the primary destination of our new business investment. Here, strain has grown at a slower rate than sales, reflecting shift in business mix. The unchanged strain in the US is also mix-related, driven by higher GICs and lower Elite Access sales. It also reflects the higher proportion of new VA premiums directed to the fixed account option, which was up four points to 23%.

The increased strain in the UK is driven by the higher capital intensity of annuity business under Solvency II which, despite the modest level of sales, consumed £110 million of capital.

I have provided you with further analysis on this next slide, which draws out those aspects of free surplus generation that are part of our normal recurring activities and those which are less regular in nature, or are not expected to recur. You can see in the pink bars that the total contribution from all capital optimisation activities net of the provision was higher in 2016 at £442 million. Working the other way was the additional strain on UK annuities which, as I said a minute ago, will decline in 2017. The recurring component of our 2016 free surplus generation, shown in the red bar, is both substantial and growing at a healthy rate.

Resilient free surplus and strong central cash

The next slide shows how the annual free surplus generation has impacted stock on the left and cash on the right. Free surplus stock grew in 2016 as our organic generation has absorbed the negative market effects, and supported increased remittances to Group of £1.7 billion. Asia became the largest remitting business in 2016, exceeding the £500 million threshold for the first time. US remittances were lower than those in the previous two years, when more supportive markets enhanced capital formation. Finally, at the end of 2016 central cash was also higher at £2.6 billion.

Equity shareholders' funds

Operating performance drives positive movement

Completing the overall earnings picture for the year, operating performance remains the dominant contributor to the overall increase in shareholders' equity, under both IFRS and EEV. The negative IFRS investment variance of £1.2 billion is primarily driven by the asymmetry between the asset and liability accounting in the US. Jackson continues to hedge on an economic basis, and its hedging programme has remained effective. However, under IFRS reporting, as equity markets rose, equity derivatives marked down immediately, while the hedged liabilities reset more slowly. This negative IFRS variance runs counter to the fact that the higher end-2016 equity and interest rate levels are a clear economic positive for Jackson.

Under EEV, which more closely reflects underlying economics, the negative effect is more muted. Here, the variance reflects the cost of increased downside protection, bought when equity markets were low during the year.

Further down the earning statement, currency movements were a large positive; a consequence of our sizeable non-sterling assets. So, after dividends and the loss and the disposal of Korea, shareholders' equity on an IFRS basis rose by 13% to £14.7 billion, while on an EEV basis it increased by 22% to £39.0 billion, equivalent to £15.10 per share.

Solvency II

Strong capital position at Group and local level

Moving to capital, this next slide summarises the solvency position of our main regulated businesses. As you can see, at the end of a very volatile year solvency levels have improved across the board, demonstrating the strength of our operational delivery and the quality of our risk-management programmes. While the Group position incorporates Asia on a Solvency II basis, it is the local solvency regimes that define both capital capacity and strength in each operation. We continue to hold appropriately strong local solvency buffers in all our businesses across the region.

Jackson's RBC ratio stood at 485% at the end of 2016. We renewed the permitted practice, and have therefore excluded from Jackson's capital the unrealised gains on interest rate swaps of $413 million, thereby reducing the RBC ratio by 38 points.

In the UK, operating capital generation and management actions have combined to improve the solvency of PAC's shareholder business to 163%. The solvency position of PAC's with-profits business has also remained strong.

Strong Group capital position and lowered sensitivities

Turning now to the Group's Solvency II position, you can see on the left that the main driver behind the improvement this year was our strong operating capital generation. Together with the management actions, our businesses collectively generated to £2.7 billion of capital, roughly equivalent to 25 points of solvency. The negative drag from market effects improved from minus £2.4 billion at the half year to minus £1.1 billion shown on the slide. This impact was softened by favourable currency movements.

We took proactive steps during the year to improve the resilience of this measure to market shocks, which included longevity and other liability actions, asset switches, duration lengthening and additional hedging. The benefit of these actions is captured in the updated sensitivities on the right, which demonstrate that the impact of these stresses is manageable. In summary, our performance on this measure in 2016 demonstrates that we have both the operational and financial levers to respond to market cycles without compromising our strategic delivery.

Transitional amortisation not expected to impact capital generation

We have also disclosed today the contribution of transitionals to the Group's Solvency II surplus, which totals £2.5 billion. As we have said before, transitionals constitute core tier one capital which we can legitimately include in our base solvency, and can take credit for in our dividend planning. I would remind you that this concept was established on transition to Solvency II, designed to offset the negative day-one impact created by the introduction of the risk margin. It only applies to business in force at 1st January 2016, and is not available to offset the risk margin on business written after that date.

For us, the transitional is primarily held against the risk margin attaching to our UK annuities, and will be amortised in a straight line over the next 15 years. However, the fact that we have stopped writing new annuity business means that this amortisation effect will be covered by the run-off of the risk margin in our now-closed UK annuity block.

Group

Dividend rebased

Turning to dividend. As I indicated at the November Investor Day when commenting on the updated dividend policy, our approach to setting the external dividend is unchanged. We assess affordability by reference to a number of financial measures, and pay close regard to the strong growth prospects of our business with a need for investment, and the vulnerability of our earnings and cash to events outside our control, such as market stresses. We then set the dividend at a level which provides us with a high degree of confidence that we can grow it by 5% each year. At the annual assessment point, the Board considers the potential for additional distributions, but these would only be made if we are convinced that the 5% growth track is not put at risk.

So, our decision this year to rebase the annual ordinary dividend upwards to 43.5 pence, representing an increase of 12%, took account of the strong performance in 2016 and reflected the output of the annual assessment exercise. We remain focused on growing the dividend, given its importance to our shareholders, and in doing so we aim to strike the right balance between certainty for investors and sensible flexibility.

Long-term value creation

The results that we achieved in 2016 underlined the strength of Prudential and its franchises. We operate at scale in some very attractive markets with the right products, the right capabilities and we are executing well. Each year, we are adding to our asset base by attracting consistently high-quality new business flows, and we work hard to retain them by delivering value to our customers. This not only provides the foundation for growth in the Group's earnings, it also increases our resilience to unexpected events and affords us the flexibility to adapt to all parts of the cycle. Our highly efficient, high-return, low-capital-intensity business model has enabled us to consistently grow the intrinsic value of our business, while increasing payouts to shareholders.

Summary

I will conclude by summarising on this final slide the key financial measures which best demonstrate our strong and consistent progress. As I said at the start, 2016 was a true test of the qualities of our strategic and financial attributes. By staying true to our disciplines and our beliefs, we ensured that our structural value drivers have remained intact, we have improved the scale and quality of our business, and have enhanced the strength and resilience of our capital. With that, I will now hand you back to Mike.

Priorities

Mike Wells

Group Chief Executive, Prudential plc

Overview

I just want to spend a few minutes on our priorities. So, one of the questions that I get when talking to various stakeholders is, 'What is it your management team is focused on?' Obviously, execution is first and foremost in each of the markets, but where are we going next; what are the things on the future agenda? So, I want to spend just a couple of minutes with you on this. There are a couple of things I have to position very carefully with you. One is: we already reinvest in all of our businesses, so let's start with that. When we look at how we invest in the businesses, we think about it in terms of: when we cost savings, what do we need to do to compete at levels of price and levels of structure with new entrants, with competitors, etc.? If we reinvest those savings, what do we expect for those returns? The same discipline you would think on capital, on new products, we apply on how we look at our costs. So, there are a couple of major themes I want to take you through that we are most focused on.

One is accelerating Asia. Now, given the success our team has had in Asia, that sounds like fixing something that is not broken. However, the work that Tony and team started in

November was first with a question of, 'Are we positioned for what is coming next in the next five to ten years in Asia?' You can address that from the point of view of if you started over today with a blank sheet of paper, but more importantly, starting from the strengths we already have: what can we do that others cannot do? I think that is a critical distinction when you look at some of these markets. Our existing positions give us options that competitors do not have. So, I will spend a little bit of time on that.

In the US and the UK, we have changing landscapes: regulatory, political, product demand-wise. I want to take you through where we are committing resources there.

At the Group level, as you have heard repeatedly over the last few years, the focus is on how we view capital and what we think we can do with that going forward and the structure.

Asia: accelerate

Leverage scale

Let's go right to Asia. The left-hand side of this chart is effectively what we have, and again it is unique. You have an excellent agency force, you have excellent access to consumers through branches, you have strong leadership positions in key markets. Of the 3.3 billion people in the serviceable universe for us, that we could bring solutions to, we have about 15 million of them as clients. So, it is fair to say there is some upside.

Two-thirds of those clients, we are their first financial transaction. We are the first financial product they have purchased. So, a variety of things need to happen for us to succeed in Asia, at another level, to grow even further. That is, we have to continue the relationships with existing clients that we have, and give them that second and third and fourth opportunity across the pitch to have a lifetime relationship with Prudential.

We need to expand the capability of the already best-in-class agency force. Why? Because advice, time and time again, comes out of the surveys in Asia as a key part of how people make decisions. So, we need to continue to make sure that our agency force has the tools – that is products, services, technology – to compete with anyone and to better service their clients. In the bancassurance business, we need to move it from wealth products, which is a traditional model that we created, effectively, in the region, to health and protection on top of the wealth solutions we brought to that category.

Then, when you hear the term 'digital', the trend there to watch most closely is convergence; we see this in the West as well. Do we have the capabilities to stay with the client, provide the convenience that the client wants, if they want to look at a statement online and they want advice? Can we meet a client anywhere across that spectrum of advice, from no advice to light advice to heavy advice? Do we do that in a way that provides the statements and interactions on technology that they want to see? This is not a new direction of travel for us. We spend almost US$1 billion as a Group on technology, just to be clear. There is no unique piece of technology out there that we have not looked at or embedded in our business models. We are looking at the same thing everyone else is in terms of what some of the new tools can or cannot provide for the marketplace. However, we do that that from enhancing relationships we already have. We own the clients, we have a great relationship with our consumers; the question is, what elements of technology further lever that?

On the convergence side, I would suggest you look at some of the online life providers, robo-advisers, some of the very creative Chinese mobile-based technologies. All of them are trying to figure out how you get a person in front of that consumer. We own that relationship. All we are doing is enhancing some of the technology around it, and a lot of it is already existing for us. So, you will see us continue to expand our capability there. This is not a new journey for us or new travel.

Expand health and protection

One that you may not have focused on is our success in health. This is a huge need, as I mentioned earlier, in Asia. Very few of the countries we do business in have state-supported healthcare. The models are evolving quickly at the health provider level, some very innovative and interesting things there. There is quite an interesting blur between health and wellness, if you will, on a variety of fronts, and we are participating in that. If you look at the APE numbers there on the left, we are already one of the largest providers in the marketplace, with tremendous upside here. So, you will see us continue to expand that footprint. There is much more we can do in this space. There are some innovative things coming that we are participating in, but we think this is a key element of our strategy in Asia going forward. Most of our markets have this structural demand.

Penetrate wealth

Then the last piece, of course, is retail asset management. You have seen tremendous growth of wealth in Asia and tremendously low penetration levels of the fund business, still low teens, relative to Western markets where there are highly penetrated markets in terms of households. As I told you a few years back, we are investing in Eastspring and its technology, its scalability, its people, the breadth of its portfolios; all of the things we need to do to make sure, as those clients grow in net worth, we are a logical place for them to leave those assets that are targeted for accumulation. You will continue to see this. So, that is the acceleration of Asia.

US: grow

In the US, the political shift is important. The social shift in the investment community has got a different dynamic to it. This started post crisis, and it has come now to a regulatory-political discussion that is critical. It is the shift from accumulation of assets to, 'How much income do I have per month at retirement?' It is a much more granular discussion. Candidly, I think it is a better discussion for the consumer. It occurred in financial planning offices, when clients did financial plans. But, the social narrative in the US is shifting. The political discussion of, 'Are illustrations going to be required? What do they look like?' These illustrations are not, 'How much do the accounts grow to?' The illustrations would be, 'What does my income look like in retirement with various assumptions?' That is a material shift that will drive retail behaviour in the US market. It will not happen overnight, it will not happen second quarter, but it is clearly the direction of travel.

Jackson's product suite and its capability in manufacturing product is in the secured-income space. The product they effectively produce better than anybody in class is a fully funded personal defined benefit plan. That is how it functions in practice. That sort of product set is suddenly getting a very different conversation, in the last year or so, with key distributors. How it is integrated into their technology, the larger asset pools, the RAA space and the platforms versus the variable annuity and insurance space, is ongoing. It is in-flight work. The regulation is catching that work now as it changes. I think that is a fair summary. We are not waiting for something to pass to start.

The broker-dealers in the United States, the advice providers, are looking at their models differently. You can read that in the industry trades. We are a good partner for them in providing those solutions for consumers long-term. So, there is a material shift occurring in the US. Is it two months out? No. Is it predictable what month it lands or what quarter it lands? No, there are variables here. It will be capability-based. Can you manufacture the technology? Do you have the quality of product that competes with the other offering? Do you have the ability to train the advisors at scale in a new regulatory, new consumer paradigm? All of those things are the best parts of Jackson's business model. So, we feel very good about where this is going. Does it lever technology you own? Yes. Does it preclude bolt-ons? No. Are there other things we can do concurrently with that? Absolutely, you saw that last year. It is not abandoning markets we are in, but it is positioning in front of what is a material shift in the marketplace there.

UK: enhance

In the UK, there are a lot of reasons we are doing this but, as we have told you here before, we are driving these businesses toward highly efficient, capital-light, consumer-solution-based asset management and wealth management products. Part of it is regulatory; the capital requirements of the annuity business do not meet our risk-adjusted return hurdles. Part of it is consumer demand; the number of consumers that actually want to lock in a yield at this point, versus want to participate in some potential upside in the market from well managed, well positioned products. Also, the demand for asset management continues to grow. You have seen Anne and the team shift not only product launches but preparation for whatever Brexit might look like, to make sure they can address their European clients. So, there is movement in this marketplace. Underlying all this is a desire to get the businesses more efficient, more effective in their service, more consumer-centric, and operate at lower and lower marginal costs, so we can pass on some of those savings to the consumer and some of that earnings gain to our investors. There is no strategic piece missing for us in the UK. We have quality products, quality brands and the management teams that compete in this market with anybody.

Group

Optimise capital

On capital, we start from a very strong capital position, well rehearsed today. That said, we have more opportunities as a management team and as a company to deploy capital profitability than we have capital; let us just be clear. I mentioned earlier, there is nothing occurring in any of our market places that has some black-box model that we cannot unwind. The question is, how does that deployment of capital affect our other objectives?

Those objectives are: what is the payback period on that capital for our shareholders? What are the risks associated with it? Interest rate, equity, currency, political, regulatory, competitive; those are all factors in the environment. All of those things go into our decisions on where we do or do not deploy capital. It is a very, very disciplined process.

We recognise that shareholders want a growing dividend. The narrative on this is well rehearsed, and I am not sure we have ever correctly landed it. Our intent is to have the dividend be incredibly resilient across cycles. One of our tests when we look at capital is, would it impact our ability to grow our dividend at the stated levels we have given you across the cycle? It is a part of the capital allocation discussion, but so is the growth of the business. Does that redeployment of capital give us the ability to get a return that is consistent with options we have globally? We are a global firm. Does entrance of a market have a long-term potential of adding J-curves and structures, business lines we do not have? Africa is a good example of that. Yes, it does. Do we enter new markets in Asia? Are we trying to fill a map with pins to say we are in every market? No; we strategically enter some markets, we strategically exit some markets. We strategically exit product lines in certain businesses, sometimes because of rates or equities, sometimes because of competitor behaviour.

That is the optionality on the bottom. We have a broad enough footprint that we do not need to stay and play in any one market that gets irrational. Lots of things can drive irrational behaviour. You task us with the long-term look at the return on capital and the long-term management of the company. Given the decisions made, even ahead of a lot of us, the options we have are broad and vast. So, there are a lot of places we can go to get return. We do not need to bet on a single market to produce an outcome. We have the ability to diversify that, and I think the benefit of that is clear in today's results. So, high capital velocity, adapt to the changing landscapes and maintain agility and optionality in what business lines we are in and what markets we emphasise and do not emphasise.

Long-term track record

I have commented before, this is my favourite slide. It stays there. A challenge to you, it is ours. We compete with firms that choose one or two of these graphs. If 22 years from now, someone looks back and says, 'What has Pru done?' If we maintain the relationship between these numbers, if we maintain the integrity and discipline to grow our profits, our sales and our cash, with some reasonable relationship over time, then you have a well balanced business that is incredibly resilient and will succeed across cycles.

Any one of these, we can change the shape of quickly, usually at the cost of the other two. This is the key, this has always been the key, and we can take this back further than this chart. When I say we compete against ourselves, this is the hardest thing to do day in and day out, and the most important that this team is delivering on. These should all grow in relationship. There are macro cuts in this you could do ten different ways, but it produces the same general question to us: are you growing one of these at the expense of the other? I would argue we are not. It is good, balanced, incredibly high-quality growth.

Summary

So, what have you got? You have a strategy that is well rehearsed, and we think you know where the enhancements are coming. We will show you a more granular look at that at the Investor Day towards the end of the year. You have material leadership positions with Prudential in the markets that we think provide the greatest opportunity. It gives us a great franchise to continue to build and grow from. We think the operational execution and the resilience of that across markets is well proven. That was not a linear period of time that those charts were produced in, right? The markets bounced around and the results were far more consistent than the variables in the market. That continues to be a strength of the firm.

Again, you are seeing the emergence of the leverage of this firm's scale. Go back to the slides from before Nic came up: if we do a good job for these consumers, they stay with us. If they stay with us, we just keep adding cohort and cohort and cohort of successful relationships with clients, and that grows the earnings of this firm materially faster than the sales can grow, even though the sales are growing as fast as anybody in the industry. That combination is unique. That is what we are trying to deliver for you. That is what you own, and we think it positions us well for the future. With that, I would like to ask my colleagues to come and join us for the Q&A.

Q&A

Jon Hocking (Morgan Stanley): Good afternoon, everybody. I have got three questions, please. The first question: on DoL, it is obviously quite an unclear picture; I wonder if you could talk about what your expectations are in terms of the process from here? What should we be looking for in terms of signposts for the fee-based VA to be rolled out, and what the penetration could be there at a reasonable timeframe? That is the first question.

Second question on the US again: in terms of the capital remittance, I can see the headwinds this year. For 2017 it looks more promising, given the growth in the account values the second of the year, the permitted practices have already been rolled over, etc. What should we be thinking about in terms of remittance from the US for 2017?

Finally, on the UK annuity book: given you are closed to new business now on individual and bulk, is the Group exploring ways to release capital from that block? Thank you.

Mike Wells: Barry, Do you want to give an update on the DoL process? You are as close to that as anybody.

Barry Stowe: Sure. We have been deeply engaged in this from the very beginning. It is a complicated bureaucratic process to get a rule in place and so, as you can imagine, there is an equally complicated bureaucratic process to get rid of the rule. It started when President Trump on 3rd February issued an executive order asking some questions about the impact of the DoL rule: would it impact access? Would it create turmoil in the retirement investment market? Would it spur additional litigation? Obviously, even without the applicability of the rule being firmly in place, there is already evidence to suggests it does all those things and more.

We are now in the midst of a process that we believe will produce a delay in the applicability of the rule. I would not expect that you would see the delay actually formally, finally announced in a definitive way until right about the time that it was meant to be applicable; in other words, the first week of April or so. That is the timing we believe will play out, because there are so many steps and comment periods and so forth that we have to go through in order to achieve the delay. The delay is obviously just the first step of a long endgame.

The intent of the DoL rule was to raise standard of advice that retiring consumers are given, and obviously we are a huge proponent of that. We just think that the ultimate rule created a lot of unintended consequences that we would like to repair. Ideally, and I think there will be bipartisan support for this, we would like to see the new rule put in place not via the rule-making process, which is what the Obama administration did, but rather through legislation. We have spent a lot of time in Washington meeting principally with Democratic senators who are very interested in this issue, and we are optimistic that once the delay is put in place and they see that the rule will change, we can get a broad bipartisan group together to craft a bill that does all of the good things that the rule did but eliminates some of the downsides, and effectively opens these products to greater numbers of Americans who are approaching retirement.

Mike Wells: On the remittance, Jon, I think we are going to pass on a forecast on the US, but it is a strong business; you have the historics, and we will leave it at that if you do not mind. Do you want to say any further than that?

Nic Nicandrou: No, other than to say that it would be a little disrespectful to the Michigan regulator to guide the market before we have a conversation with them. Look, you see on slide 75 in the appendix that the size of all remittances that we have had from the US clearly will depend ultimately on capital creation in the year. The business is producing good capital, so we will look to it to return an appropriate share.

Mike Wells: On the optionality of the UK book, speaking for John and the team, there are two ways to look at. It is a very profitable, successful book for us. You see the earnings impact of it. I know in a market place that makes it desirable to others, I have read those reports. I think there is work we can always do with existing products and services we have to improve capital efficiency, and there is strategic work we can do. We always look at both, Jon, but I am not going to comment on either at this point.

Greig Paterson (KBW): Good morning, three questions and a request. I note the Asian Life outflows – I note that is the statistic we used to look at a few years back – has improved from 13% last year to 11%. It is still pretty high. I was wondering if work is being done there, or if there is some capacity to get that down? I am talking about the unit-linked surrenders and maturities in the Asian book.

Second thing is, last year I think your productivity increase in the Asian agency channel was 25% year on year. I could not find it in today's release; I wonder if you could give us that number?

The third question is just in terms of the Solvency II, the 201% number: have you done a pro forma recalculation of the transitional there, or have you assumed no transitional recalculation because the test has not been passed?

Then Nic, just a reminder, if we could get the required capital splits per region under EEV? You took that disclosure out last year, it would be useful for modelling purposes. Thanks.

Mike Wells: Tony, do you want to talk about Asia Life and just generally on productivity?

Tony Wilkey: Sure. You know the various sides of productivity. If you look first at the growth in manpower across the region – and we can look at the macros but it is very important to then go country by country, because the dynamics is very different – manpower reached an all-time high. Closing manpower for the year was 601,000 agents, so an all-time high. Much of the growth came in China, and strong recruiting growth as well in Indonesia. The productivity dramatically varies by country. We can give you the breakdown: Singapore is very high productivity, as is Hong Kong, and that is obviously skewed by the mainland Chinese business which are slightly larger tickets than the domestic piece. However, across the board manpower was slightly stronger than productivity last year, with the exception of Hong Kong and Singapore.

Nic Nicandrou: On surrenders on the unit-linked side, okay. I will point you to slide 67, which actually gives you the calculation of those ratios. Part of the reason for the decrease that you referenced, Greig, is the fact that now Korea is not included in these numbers, and Korea was a big outflow company. What we did on slide 67, we recast the historic information to exclude Korea. What you will actually see when you turn to that is that we held on to the improvement we saw last year, and therefore no real change in the underlying position in the course of 2016.

Mike Wells: Nic, the Solvency II question?

Nic Nicandrou: Okay, Solvency II. What has happened is, we recalculated the transitional at the half-year point with the PRA's approval. In the second half of the year, interest rates improved so the risk margin came down, and therefore it follows that the transitionals should come down as well. For the purposes of what we published today, the £12.5 billion, the 201%, we have done the virtuous thing of reducing the transitional to compensate.

We have applied to the PRA to have their recalculation approved. They are in the process of considering that application. They said they would let us know before we have to file our QRTs and produce the SFCR for the market. If we get that approval, then we will publish on the basis of the numbers that you see here. If we do not, then the numbers will increase by £0.4 billion, which is equivalent to around four points of solvency at the Group level. As I have said, we have done the virtuous thing and moved the transitional down to compensate for the favourable movement in risk margin in the second half.

Andy Hughes (Macquarie): Thank you very much. Three questions if I could. The first one, again on the US transfer: the finance that you put in place, has that impacted the transfer or is that post the transfer this year? Is that a new thing that would be taken to account by the regulator for the 2017 transfer? I am looking for some guidance as to how you would expect the US transfers to correlate with the surplus generated in the US, because clearly the surplus is quite big and the transfers are following a different path at the moment. Any guidance you could give on that would be helpful.

On the UK, you hinted that the orphan estate is getting bigger in the UK and the business is getting smaller, albeit that the PruFund is offsetting the net flows and the PruFund requires much less capital. I am just wondering how close you are to doing something with the excess surplus, if there is, any in the UK?

Also, could you give us a PruFund number ex-bonuses? Because the problem with PruFund is obviously that it is not really generating any earnings in IFRS terms, so it would be quite good to track how much the bonus component has grown of PruFund, so we can see how much you have in the bank, if you like. Thank you.

Nic Nicandrou: Okay. In terms of the US transfers: yes, it is effectively a XXX transaction in relation to part of the term life book that we bought at the time of REALIC. It produced around 30 points of RBC solvency. It is included in the RBC number, so it is good capital in that sense. I guess I will repeat my answer to Jon that, if you look at our track record, we have remitted a considerable proportion of Jackson's annual stat basis generation each year, and you should continue to expect us to do that as we go forward.

Now, in relation to the UK solvency, clearly the with-profit solvency position will move up and down depending on investment performance and on the reinvestment, as we reinvest the estate into writing more PruFund business. Your question was on the shareholder side: 163, I appreciate that that is outside the range that we guided you last year, but I did say at the time that it was not a hard range. I said that if we fell below 130, it did not mean we could not take out dividend. Equally, if we go above 150, it does not mean that there is suddenly quite a lot of excess capital. We continue to keep the range under review. 2016 has proven to us that these things can swing, that solvency can swing from the top of the range to the bottom, back up to the top. We are comfortable with where it is. At 163, yes I would agree we have some surplus capital, but I would not express that as having significant excess capital.

Blair Stewart (Bank of America Merrill Lynch): Thanks very much. Good afternoon. Three questions. Firstly, on the US: Barry, can you give us any update on the NAIC proposed changes, where that has got to over the last few months and what impact that might have moving to an economic approach?

Indonesia and Hong Kong, often talked about. I just wonder if you could clarify a little bit more about what is going on with Indonesia? Just towards the end of the year, you have stated there has been a real pick-up, and I was wondering what is driving that? Also, you have hinted that there is no real impact from the more stringent exchange controls in Hong Kong; just a little bit of extra colour on that, if possible?

Final question: Nic, if you could just remind us what is left in the tank from FX tailwinds going into this year, if possible? Also, on the fee-based business, where are current AUM or end-of-year AUM relative to the average of last year? Again, what is the tailwind going into 2017? Thank you.

Mike Wells: Chad or Barry?

Barry Stowe: Yeah, I will say a few words and see if Chad wants to add some additional colour. I think the process is moving along, first of all, to answer your question simply. We are in QIS 2 now. We are maintaining close contact with the commissioners generally, and with some very influential commissioners in particular, to make sure we are in tune with what their thinking is and helping to guide their thinking where we can.

I think the important thing to understand is that at the highest levels of NAIC right now, this is not really a front-of-mind issue. We were are at the most recent meeting out in California, commissioners' meeting, and asked the question: 'Because this work is going on at lower levels, does it imply that you have some concern about capitalisation of the industry in the United States?' The definitive answer was absolutely not. While there is work going on at lower levels, and there are people that are taking an enormous level of interest in this, I do not think it would be accurate to suggest that at the highest level of the organisation, where ultimately policies are made and decisions are made, that there is a high level of concern – or any level of concern, candidly – about the capitalisation in the industry. We will continue to monitor this closely and, again, try to shape the outcome if you will; at this point we are not alarmed by it, but we are obviously very watchful of it. Chad, I do not know if you want to add any more technical detail? Chad has had some more detailed discussions with some of the commissioners

Chad Myers: I guess I would just say: keep in mind that this started off as a process to go through looking at getting rid of captives in the US, or alleviating the need to have captives, not to get rid of it; the concern being that there was non-economic reserving going or, to the extent that there was, it was not matching up with the way some people were hedging, so they were using captives to really bridge that gap. That is what this started off as.

It has grown into something bigger, and I would say a couple of things on that. One is, if it goes off the rails for some reason, what that is really going to do is drive more into captives and not less into captives, so that is clearly not where the regulators want to go. Back to what Barry said, they are not stating a view that we have an undercapitalised industry; they are just trying to get more alignment between the reserves and the hedging.

That said, we are just kicking off QIS 2. That process is going to run for the rest of this year. On a highly optimistic basis, if you were Oliver Wyman who is running the process, 1st January 2019 would probably be as good as you are going to get at this point. That is assuming nothing comes out of QIS 2 that stalls that more. I think what we have seen is we have a long way to go through the QIS 2 process, we are engaged in the QIS 2 process – we are in some respects leading portions of it on the industry side – and we think we will get to a reasonable resolution. Like I said, if for some reason it does not get to a reasonable resolution, captives become a viable alternative to make sure you have reasonable capital there.

Tony Wilkey: Indonesia: I think we talked about this at the Investor Day, how when these businesses are going through challenging conditions, we tend to micro- or even nano-manage the businesses, and look at sequential progress in new sales and push where and when appropriate. What you have is, in terms of momentum, second half grew over first half by 10%, Q4 grew over Q3 by 57%. December was our biggest month all year, and showed positive growth for the year. Underlying that was average recruiting throughout the year of 6,000 agents. We on-boarded 244,000 new customers throughout the year. That is something like 650 new customers per day, so pretty good underlying momentum in the machine there.

I think it is important to bear in mind that, while Prudential Indonesia just celebrated its 21st-year anniversary, it is essentially a ten-year old business. That is when we really galvanised it and started to drive it. Further, if you look at the penetration, an interesting statistic in the market there is: there are only 18 million policies in force in Indonesia, in the whole country. There are 31 million people living in Jakarta, there are 250 million people living in the country, so it is still very, very much early days, and the momentum is progressing quite well.

Hong Kong, we were plagued with events during last year in this regard. Where we find ourselves today, and I think what we indicated to you last year, was the mainland customers who buy products in Hong Kong, something like 80% of them have bank accounts in Hong Kong. The series of events we saw was the cessation of the UnionPay card and then onto MasterCard and VISA and certain limitations. Today, the majority of new business premiums are being paid via Hong Kong bank accounts.

The shape of the business has changed somewhat. You may recall that towards the middle of Q2 last year, we backed away from the broker business. This is typically larger cases that we are not comfortable with, for a whole series of reasons. As you carve that piece out, the average case sizes started to come down on the mainland business being written in Hong Kong. However, momentum continues, agency force at record high in Hong Kong, 18,700, recruiting 400-plus every month, and a pretty solid story.

Nic Nicandrou: On FX, clearly we only picked up half the benefit that we saw in the year, given that we are using an average for the year, so the early part of the year sterling was stronger, weaker in the second half. In your appendix, slides page 120 and 121, we illustrate to you what the 2016 results would have been on our various operating metrics – IFRS, free surplus, our new business, EEV – had we used the year-end spot rates, and that gives you a sense of how much, using your expression, gas there is in the tank. Clearly, of course, these things will depend what actually happens in the course of 2017, so bear that in mind before you put those in your models.

Your second question on the difference between average and closing: so, in the US, the average growth in separate account assets was about 5%. It compares with an 11% growth in the closing. Again, that gives you an indication of some tailwind there. In Eastspring, the average was up 9% and the closing was up 13%. However, before you put the full 4% in, we did see a slight shift in the mix of business towards bond/institutional-type products, so you should factor that as well. In M&G, the average was slightly down, minus 2%, broadly in line with what you saw in revenues, and the closing was plus 8%. However, again, the closing is boosted by a bigger growth rate in the institutional business, which is lower margin than the retail.

Arjan Van Veen (UBS): Thank you, two questions on Asia please. Firstly, on Hong Kong. We saw a very strong improvement in the margin, first half on second half: 62% in the first half, 79% in the second half. I assume it is partially to do with the broker/agent mix, but also the stuff you talked about in the presentation around more protection and health. You have given the level of margin now in Hong Kong: is there also an ability to take that outside to other markets? It sounds like you have maybe done some pilots there, or initiatives in Hong Kong.

The second question is on China. You spent quite a bit of time talking about the opportunity in China at the Investor Day, talking about the margin opportunity there, and we have gone from 20% in the first half to 46% in the second half. It feels like the way you were talking at November, there is still somewhere to go in the margin there in China, so maybe you can give a bit of colour?

Tony Wilkey: China, I think we started flagging the opportunity some years ago, and also in the context of the Hong Kong business, our strategy long-term of needing to win on both sides of the border. We have been expanding with a clear intent, and that is to grow the agency force to sell more health and protection, and that is exactly what has happened. The closing manpower for China was 33,000 agents. It is still a terribly small number for China, but it is high quality. Within that, they ramped up from 15,000 18 months ago to 33,000, and activity levels stayed the same which is an excellent reflection of discipline. They are selling a lot of health and protection, which is directly driving the margin.

It is also important to note that we have simultaneously expanded the footprint; not many of our foreign competitors in China are able to do this. Last November, we expanded into Anhui province, which is essentially the Silicon Valley of China, and recently we just announced we got CIRC approval to enter Sichuan province. Sichuan province is the fourth most populous province in China, it has 80 million people. Look at this like we just added another Vietnam. It is like adding another country. When the One Belt, One Road goes through Sichuan, the economy is going to continue to go from strength to strength, and so is our opportunity. You know it is a joint venture with CITIC Group; 15 years old now and the relationship is on an excellent footing. The conversations in the boardroom are around growth in NBP and embedded value, very different than what one might have seen ten years ago where the conversation would focus on market share. It is a quality story moving in the right direction in China.

Nic Nicandrou: Maybe some specifics on the margin. Really, we guide you not to take these things segmentally, because they are impacted by what interest rates do. There is also another effect: the way we calculate NBP at the half year, for example, on any business that we have written up until that stage is to count the profit only in relation to what was produced in the first six months, so there is an effect when we bring in the second-half profits. I would echo what Tony said: the improvement in the margin for Hong Kong is driven by mix predominantly; in China, also mix, and also now the business is getting to a scale where we are beginning to see some efficiencies come through the numbers as well.

Oliver Steel (Deutsche Bank): Thank you very much, three questions. First of all, I guess I have to ask about M&G, and whether, in the light of Standard Life's announced merger, you feel it is too small?

Singapore: sales, unless I got my forecasts badly wrong, appear to have surged quite a lot in the second half, so I am just wondering what is driving that?

Then a slightly techy question: the normal amortisation of your US DAC seems to have fallen year on year against, I assume, an increase in the actual size of the DAC. I am just wondering what drove that, and whether you have a guidance figure for 2017 on that basis?

Mike Wells: Anne, do you want to go first on M&G, and we will see if we have the same answer?

Anne Richards: Well, I think after the news from the First Minister yesterday, Aberdeen-Standard Life is no longer the biggest story in Scotland, which is interesting. I think it is interesting when you look at the deals that we have seen recently: there is a big conversation going on in the industry around scale, and scale is important, but I think scale is sometimes confused with having large single strategies, and when they go off the boil, what looks like scale then starts perhaps not to feel so much like scale.

From our point of view, we are much more focused on having propositions that are exciting and interesting for a client base at every point in the market cycle, and so we are very much focused on that, ensuring that the continued innovation is going through; then on the stuff that we can deliver, around the systems and the way we can produce that product in a cost-effective way. So, we are really focused on the stuff that we can control. As you have seen from the sales figures in the fourth quarter, when we get that stuff right, the business continues to move along in a positive way, and I think that is very much where our internal focus is, so we are not looking over our shoulder in that respect.

Mike Wells:I think it is well said. As I mentioned earlier, I think size and scale are confused, and asset management business is a classic example of a space where it happens all the time. We do not need every portfolio that is available in the marketplace. Some of them, the clients are choosing to access that sort of return in different ways. We have to have value for the consumer across the cycle. We have to have where they are likely to go with the money if they move out of one investment class into another. We have to have cost synergies and effectiveness and tools that make us able to keep with anybody. Candidly, some of that in the industry now you can lease, some of that you need to own, and we certainly have the size and earnings and assets and talent to access the best of what is out there.

I do not view us as lacking anything with M&G. Eastspring, we said we want to continue to develop the talent. We do not need to buy anything there. We certainly lift out teams that we thought filled gaps that we do not have in portfolio management, but they are getting the same systems and capability that we are putting into M&G. Our business in the US is more institutional focused but, again, aligns with those strategies as well.

There are other benefits that roll back to the Group from that sort of discipline. Penny's area in risk, our ability to look quickly at counterparties and positions holistically, matters. Those are intangibles you get from getting proper systems and proper capability in place. Then obviously, the earnings that come from running it well and having clients stay longer because the funds do well, all that rolls up as well. I think we have size and we have scale, and we will continue to improve the attributes of scale in the asset management businesses.

You also asked about Singapore?

Tony Wilkey: Singapore, very strong second half across the board. Agency is very strong; recruited 1,000 agents in Singapore throughout the year, which may not sound like a large number, but it is in the context of Singapore taking our agency force there to 4,200, the largest it has ever been. It is the most productive agency force in Singapore. The LIA results, the local organisation results, just came out: we are the number one provider of regular premium products in Singapore, and we are the number one agency company, so that is the perfect fit for how we like to deliver those types of products in Singapore.

Also, excellent rebound in the second half for our bank partners. There are both Standard Chartered Q4 was a record for SCB in Singapore, largest quarter ever, and UOB coming back more on the basis of product mix, selling a lot more regular premium than they had in the past which flows through to the new business profit margin.

Nic Nicandrou: On the DAC, there was a £93 million effect in the full year for DAC deceleration. Around £20 million of that related to the fact that the separate account return was higher than what we had assumed in the mean reversion number, and the balance of around £70-odd million comes from the way the mean reversion works: 2013 dropped off, and that had a very strong performance into that calculation, and that gave us an uplift. There is the usual analysis that we provide on appendix slide 76, which effectively gives you that colour.

Nick Holmes (Société Générale): Couple of questions on the US again, I'm afraid. First one is: how concerned are you about the growth in fixed indexed annuities? Because these products are really taking the market by storm at the moment and I wonder, is it a product you are actually tempted to offer yourself?

The second question, again on the US, is: can you tell us more about review of the policyholder behaviour assumptions in your variable annuity book? How are your assumptions holding up? I imagine, given markets, they are probably pretty good. However, is there anything that you would be concerned about that you would give us a bit more colour about? Thank you.

Barry Stowe: There has been a surge in fixed-income product. A lot of that, I would attribute to the presumption that fixed-index annuities would not lose their status under 84-24; they did in the new DoL rule. Now, who knows where they will come out. I think that is going to mute, to some degree, the prospect for fixed indexed annuities going forward.

Fundamentally, there is nothing wrong with the concept of the product. We have a product in the marketplace. Ours is not very competitive, because we believe in this environment it is difficult to manufacture one that is extremely competitive, and to do so in a way that provides solid benefits for the consumer and for the shareholder. We have struggled with that a little bit. Conceptually, in the right environment, would we be willing to write FIAs? Yes, we would. We have in the past, we would again. Fixed annuities as well, if you get a change in the interest rate environment, just a plain old vanilla fixed annuity can be a logical thing for a lot people.

The reason we focused on VAs, first and foremost, is because we think in an environment where we expect interest rates to be relatively low for a long time, and in an environment where most Americans approaching retirement are undersaved, that it is really only by being able to invest with a great deal of freedom in the equities market that we can do the real job that the consumer needs done, which is allow them to have a guaranteed amount of income that they know they can count on, that they cannot outlive, and that is insulated, protected from whatever investment decisions they make which may be good or bad. Only the VA really does that. It is because of the consumer-centricity of that product that we have focused on that product, and we continue to see that, in our view, that product is going to be from a social utility perspective the strongest product in the marketplace.

Your other question was on policyholder behaviour: I guess the short answer is no. We spend an enormous amount of time sweating the details on this and we review it frequently, regulators review it as well, and in our view there is nothing in there right now that would cause us any concern. Which is not to suggest we would never change it, because it gets tweaked constantly as we see emerging trends, but there is nothing in there right now. Chad, do you want to add any more colour to that?

Chad Myers: Okay, thanks. The only thing I would add is thematically, what we have seen over the years is a little bit more persistency, so lower lapses. It is a thematic thing; very minor tweaks, but the general trend has been towards that. That is a little bit difficult to ferret out whether that is really where the market is going, more desire for the income, or whether there are just not any really good products to 1035 into at this point in time. That is the only one trend I would point out, and it is a good one for us economically.

Barry Stowe: You can make a strong case that it is actually the latter, because as you may know, we are the only variable annuity writer in the marketplace today that offers investment freedom. We will write the guarantees around all 91 funds on the platform; no one else is doing that. So, if they said, 'I am going to take my Jackson policy and move it to X, Y, Z, and I want to buy guarantees and they are going to be whatever their platform is, call it 90 funds,' they are going to be forced to choose form ten vol-controlled funds which consistently underperform the market. A rational investor would not leave investment freedom and go for vol-controlled funds.

Chad Myers: Also, the compliance department on the other side would have a hard time approving that trade.

Barry Stowe: That is a good point. Yeah, the broker-dealer would never let it get through, because it is not as good a product.

Abid Hussain (Credit Suisse): Hi, two questions if I can. Firstly, on Solvency II: how should we think about the potential management actions on Solvency II capital going forward? Will you be seeking to increase longevity reinsurance or hedging elsewhere? Could you provide a flavour of possible actions going forward, please?

The second question is on your 2017 targets. It looks like you can achieve the Group cumulative free surplus target of at least £10 billion by the half year. I am just wondering, should we be expecting new targets at that point?

Nic Nicandrou: On optimisation, there is still an array of actions we can take if we needed to, whether it is more longevity insurance; clearly, there is a trade-off there with earnings. There is a little more we can do on the matching adjustment. We have got around 96.5% eligibility, there is a bit more we can do. There is always tweaking, and we will evaluate it as and when the opportunity arises, or as and when we deem it appropriate.

Mike Wells: On the targets, let us get there first. I think one of the problems with targets is everybody declares victory before you actually cross the line. There is quite a bit of work still to do. Relative to the marketplace, I think they are impressive if we accomplish them.

If you look at the Asia-centricity of the targets, I have seen three sets now in my career here: I think they were an attempt at a proof of concept in the market. The first discussion was, can you take this NBP-centric business and double it again, and convert it to more cash metrics, and it is still scalable the third time? All these were the discussions in this room and rooms like it along the way.

I think we have demonstrated that that is a real business, and that it is producing real returns. So, I would say I do not think we need to do a similar exercise again. They are limiting at some level; if there is something strategically we wanted to do, we will review it. We will review it at the Board level, we will decide what we want to do. However, I think the original objective of the targets was to give you some understanding of what Asia could look like. I would like to think at this point that given the recurring earnings, the scale of it, its market positions, that point has been made. I would like to think that point has been made.

Edward Houghton (Bernstein): Can you sustain an IFRS ROE above 25% for the next five years?

Mike Wells: Ed, can I pick all the assumptions on interest rates and equity? It is obviously very forward-looking, but there are variables in the market that go with those sorts of returns. I think that is why a single metric is not the right way to look at it, but that is good one and we are proud of it.

Okay, thank you everybody for a full session. We appreciate your support. We will be around individually if you have any last questions, and enjoy the afternoon. Thank you.

[END OF TRANSCRIPT]