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Interview with James Turner

Tom Mackenzie

Now, let's get to another earnings story and crossover to Hong Kong, because Prudential's new business profit dropped 14% and fell short of analysts estimates in a year that the UK-based insurer pivoted to focus on Asian and African markets. The reporting period coincided with Hong Kong and mainland China. Two, of course, of Prudential's biggest markets exiting three years of COVID zero restrictions. Joining us now is James Turner, the CFO of Prudential. Good morning, or good afternoon for you, James. Thank you for joining us. Let's start with the top line on your results, then your key takeaways, and how you think it positions the business for the quarters and year ahead.

James Turner

Okay, Tom. Listen, thanks for having me on the call today. Look, I think we're presenting a very solid set of results. Our AP is up 9% on a constant exchange rate basis. Our NBP was down 11. We've delivered significant growth in operating profits, very strong balance sheet, high capital ratio, strong liquidity. We are really poised for growth.

Tom Mackenzie

Talk to us about the new business profit, the drop of 14%, missing the estimates for the full year. Does a turnaround seem likely? Are you seeing improve momentum there?

James Turner

Tom, on a constant exchange rate basis, our NBP dropped 11 that three is because of exchange rates. And really, this is almost all driven by economics. If you strip out economics, our NBP was down four, which I think will compare very favourably against a really challenging time in 2022 for the industry. And really, that economics was also driven by Hong Kong. And so, if you strip out Hong Kong, then actually our NBP was up 5%. And the reason that Hong Kong was so impacted is because we sell largely US dollar business. And as you know, the US dollar went up 240%, and we marked to market the whole of our NBP based on the year-end interest rate.

Tom Mackenzie

Okay. Interest rates is clearly a factor and we will maybe unpack that story a little bit more in the minutes ahead. The life insurance business, of course, really, really important as a driver for the business, and the reopening of the borders between Hong Kong and China, presumably a catalyst for Prudential going forward. How much demand do you expect to see for the life insurance part of the business?

James Turner

In terms of IFRS operating profit, we've just reported an 8% growth. That was driven by a 15% uplift in our insurance and fee income. So, health and protection, regular premium, long-term business key to our business.

Now, in terms of the Hong Kong, China mainland border opening, we are really encouraged by that. We're seeing strong momentum in the first two months. We've given the overall impact on our sales in January, February of it being plus 15%. And what we're seeing is that visitor numbers are increasing every month.

Tom Mackenzie

Okay. So, you continue to see that demand from those visitors coming over from China. You are now able to, or at least mainland investors are now able to buy the stocks via the Shanghai-Hong Kong Stock Connect. How much demand do you expect to see coming through from that, James?

James Turner

In 2021, we did just over two billion share issuance on the Hong Kong line. And we were delighted in mid 2022 to get inclusion in the Hang Seng Composite Index. This gave us access to the Shanghai Connect and now the Shenzhen Connect. And what we've seen is absolute doubling of volumes on the Hong Kong line. We see this as incredibly positive as we're starting to see that southbound flow.

Tom Mackenzie

What is the balance sheet exposure? How much exposure do you have, if any, to Silicon Valley Bank, and indeed the commercial lenders in the US?

James Turner

We have always positioned. I used to be the chief risk officer. We've always positioned our balance sheet very conservatively. Our actual exposure to SVB, to the whole of that small tier US banking is relatively de minimis.

Tom Mackenzie

Can you give us a little bit more clarity on what relatively de minimis means, James, in terms of that exposure?

James Turner

Absolutely. I think for SVB, it was \$1 million out of a debt portfolio of 23 billion.

Tom Mackenzie

Okay. Changes, of course, at the top recently at Prudential, a new CEO taking the helm. What is the strategy going forward for you and the team?

James Turner

I'm delighted to have Anil on board. He's really hit the ground running. You'll get a chance to see him in the investor roadshows for all of our investors, but we're not announcing any major shift in strategy at this point. He's been in the office for just about three weeks, I think.

Tom Mackenzie

Okay. So, we'll give him a bit more time. Major changes meanwhile in the mainland around the regulatory bodies overseeing insurance and banking. What do you think are going to be the impacts and the changes that are coming down the pipe from regulators in Beijing?

James Turner

Look, again, it's early days, but for the NFRA, we see this as a positive. Because if I look back, two things that they've done recently, first of all, they've said that they want to increase insurance penetration to 5% in the mainland. It's currently about 3%, so that's really driving this health and protection, which is the heart blood of what we're selling.

The second is that they're really opening up of the pensions market. And therefore for foreign insurers with strong capital, with a strong experience of being able to sell retirement and manufacture retirement products, so companies like Prudential, these are really great signs for the growth. The structural growth of the Chinese market.

Tom Mackenzie

Okay. Before we let you go, James, I want to circle back to the rates environment. You touched on this. I know we're looking ahead to the Federal Reserve decision next week. Investors now expecting a hike from the Fed. The Hong Kong unit, of course, of the business impacted in terms of new business, I believe dropping around 47% in terms of new business profit largely as a result of those high rates. Is that a theme? Is that an evolution you expect to continue in the quarters ahead? And how are you adjusting to that?

James Turner

We take a long term view. In actual fact, what's happening is we are discounting all of those future cash flows. So, it's not that it's having a direct impact. We're selling predominantly health and protection business. That is not sensitive to interest rates, but because it's long term, what we're doing is we're discounting all of those future cash flows at a higher interest rate. Our NBP methodology has this mark to

market philosophy. So, we're marking to market to whatever the interest rate is at a given point in time, and then discounting those cash flows at that, in this case, higher interest rate.

Tom Mackenzie

Okay. James Turner, CFO of Prudential. Thank you very much for your time on the back of these earnings and looking ahead to the quarters ahead for, of course, that insurance and asset manager based, of course, out of Hong Kong. James Turner, thank you.

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