Chief Financial Officer's overview

Tidjane Thiam
Chief Financial Officer

In the first half of 2009 Prudential has continued to balance profitable growth, capital conservation and cash generation to both protect the Group's financial strength and preserve its long-term growth potential. We have focused on generating significant levels of sales of profitable and capital efficient products.

Our results, as summarised below, show that we have achieved our dual objectives of higher profitability and lower levels of investment in new business at a time when market conditions remained challenging for the insurance industry. This highlights our focus on value over volume as we manage investment in new business to meet our capital management targets. In addition we have been able to strengthen our capital position and have continued to generate a positive Group holding company cash flow.

Performance and key metrics

	AER[6]			CER[6]		AER[6]
	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %	Full year 2008 £m
New business[note 1]						
Annual premium equivalent (APE) sales	**1,321**	1,442	(8)	1,662	(21)	2,879
Present value of new business premiums (PVNBP)	**9,657**	10,636	(9)	12,436	(22)	21,729
EEV new business profit (NBP)	**691**	555	25	653	6	1,200
NBP margin (% APE)	**52%**	38%		39%		42%
NBP margin (% PVNBP)	**7.2%**	5.2%		5.3%		5.5%
EEV basis operating profit[note 1]						
On long-term business[notes 2,3]	**1,303**	1,301	–	1,508	(14)	2,810
Total	**1,246**	1,350	(8)	1,561	(20)	2,865
Net investment flows	**10,069**	4,091	146	4,475	125	4,266
External funds under management	**72,336**	67,477	7	69,780	4	62,279
IFRS operating profit based on longer-term investment returns[notes 1,3]	**688**	647	6	746	(8)	1,283
Balance sheet and capital						
EEV basis shareholders' funds	**13.7bn**	14.0bn	(2)	14.9bn	(8)	15.0bn
IFRS shareholders' funds	**4.7bn**	5.6bn	(16)	5.9bn	(20)	5.1bn
IGD capital surplus (as adjusted)[note 4]	**2.5bn**	1.4bn	79	n/a	n/a	1.5bn
Free surplus – investment in new business[note 5]	**331m**	350m	(5)	418m	(21)	806m
Holding company cash flow	**22m**	86m	(74)	n/a	n/a	54m

Notes
1 New business and operating profits exclude the results of the Taiwan agency business for which the sale process was completed in June 2009.
2 Long-term business profits after deducting Asia development expenses and before restructuring costs.
3 Operating profits are determined on the basis of including longer-term investment returns. EEV and IFRS operating profits are stated after excluding the effect of short-term fluctuations in investment returns against long-term assumptions, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes, and the effect of disposal and results of the Taiwan agency business, for which the sale process was completed in June 2009. In addition for EEV basis results, operating profit excludes the effect of changes in economic assumptions and the time value of cost of options and guarantees, and the market value movement on core borrowings.
4 Insurance Groups Directive capital surplus (as adjusted). The estimated surpluses shown for half year 2009 and half year 2008 are before allowing for the interim dividends for 2009 and 2008. The surplus for full year 2008 of £1.5 billion was determined before allowing for the 2008 final dividend, after final adjustments of £0.1 billion included with the filing to the FSA in April 2009 and before the benefit previously disclosed of £0.3 billion allowed by the FSA in February 2009, for a portion of the shareholders' interest in the future transfers from the PAC with-profits fund. This benefit was estimated to be worth £0.4 billion at the half year 2009, due to a change in the tax applied.
5 Free surplus – investment in new business – represents EEV net worth strain together with EEV required capital to support the new business acquired.
6 Actual Exchange Rate (AER) and Constant Exchange Rate (CER).

In this review, comparisons of financial performance are on an actual exchange rate (AER) basis, unless otherwise stated.

We expect the business environment to remain challenging throughout the rest of 2009. However, our long-term growth and profitability potential remains intact and we are well positioned to take advantage of opportunities in the pre- and post-retirement market in our chosen geographies. We will continue to focus on balancing new business with cash generation and capital preservation and to manage risk in a prudent but proactive manner.

In a more difficult economic and market environment, there has been downward pressure on our operating earnings. The performance achieved this first half highlights the resilience and strength of our business model throughout our geographies.

Total EEV basis operating profits based on longer-term investment returns of £1,246 million were down eight per cent from half year 2008.

The EEV operating profit for long-term business was flat at £1,303 million as the effects of strong new business profit (up by £136 million to £691 million) driven by the US were offset by a reduction in the contribution from in-force business (down by £134 million to £612 million) due primarily to the impact of strengthening operating assumptions for persistency in Asia and lower unwind of discount on in-force business in the UK. The Group EEV operating profit was also held back by the negative impact of lower asset values due to market conditions on the contribution from the asset management businesses (down £56 million to £125 million) despite significant inflows reflective of the investment performance delivered by our businesses. There was also a negative impact on Group EEV operating profit from other income and expenditure due to the non-recurrence in 2009 of one-off items for a net amount of £19 million in the half year 2008 results and lower returns earned on central funds (lower by £32 million to £6 million).

The total EEV profit before tax for half year 2009 of £67 million compares to a loss of £635 million for half year 2008. The impact of market conditions has remained negative but less so than in 2008 with a reduced aggregate impact of short-term fluctuations in investment returns, changes in economic assumptions, and other recurring categories of volatile short-term profitability.

The short-term fluctuations in investment returns include a one-off £216 million cost arising from the hedge temporarily put in place during the first quarter, to protect the Group IGD capital surplus in the light of exceptional market conditions. During the extreme equity market conditions experienced in the first quarter of 2009, with historically high equity volatilities, the Group entered into exceptional overlay short-dated hedging contracts to protect against potential tail-events on the IGD capital position, in addition to our regular operational hedging programmes. The vast majority of the costs related to the hedge have been incurred in the first half 2009, with £216 million being included in the profit and loss account in this period. At 30 June 2009, the Group held equity options for this potential exposure with a remaining fair value of £36 million. We fully anticipate that these options will be held to their expiration, with all options expiring before the end of 2009.

Since the beginning of the year, management actions have led to a very material increase in the Group's IGD surplus position to £3.0 billion including the net proceeds of the Tier 1 hybrid debt issued in July. As a result and as planned, such exceptional hedging will not be renewed. Among those management actions, it is worth noting the repayment of £249 million of senior debt, the issuance of £400 million of subordinated debt in May, and the raising of an additional US dollar $750 million (c£455 million) of hybrid debt in July, the cost of which compares favourably with that of the one-off exceptional hedging.

Our IFRS operating profit has increased by six per cent to £688 million. This was due to higher profits from the Life businesses in Asia and the UK offset by (i) lower asset management profits due to difficult market conditions and (ii) a difference of negative £69 million in other income and expenditure mainly due to lower returns earned on central funds and the non-recurrence of net positive one-off items for the half year 2008 results. In the UK, operating profits for our long-term business increased by £31 million to £303 million. Operating profits increased in Asia by £137 million of which £74 million was due to a combination of higher insurance margin, lower new business strain and foreign exchange and the remaining £63 million was due to a one-off benefit arising from a regulatory change in Malaysia.

The total IFRS profit before disposal of Taiwan agency business was £545 million in the first half of 2009, significantly higher than for the first half of 2008 (loss of £62 million) reflecting increased operating profits and more favourable short-term fluctuations partially offset by a charge for the costs of hedging the Group IGD capital surplus. Total loss before tax on the IFRS basis was £76 million in the first half of 2009 as a result of the disposal of the Taiwan agency business which was completed in June 2009.

Our IGD surplus at 30 June 2009 is estimated to be £2.5 billion, before allowing for the 2009 interim dividend, an increase of £1.0 billion from the finalised figure at 31 December 2008 of £1.5 billion (before any allowance for the final dividend). This increase includes the benefit in 2009 of £0.8 billion arising from the sale of the Taiwan agency business and £0.4 billion arising from new hybrid debt issued by the Group in May 2009 partially offset by the impact of impairments over the first half for the year of negative £0.3 million. In July 2009 the IGD surplus was increased further by the raising of a further US dollar $750 million (c£455 million) of hybrid debt and we estimate it at £3.0 billion at 31 July 2009.

Jackson's gross unrealised losses reduced by £1.0 billion during the first half of 2009 to £2.2 billion at 30 June 2009. The change reflects the benefits of some normalisation of the credit markets.

In the volatile economic environment experienced during the first half of 2009, we maintained our strong focus on risk, capital and cash management. We have also been able to continue to be cash flow positive at the holding company level, with a positive contribution of £22 million.

EEV results

To 30 June 2009, Prudential Group's total EEV basis operating profit based on longer-term investment returns was £1,246 million, down eight per cent from half year 2008.

The Group generated long-term profits of £1,303 million, comprising new business profits of £691 million (2008: £555 million), in-force profits of £617 million (2008: £749 million) and development expenses of £5 million (2008: £3 million). New business profits, at £691 million, were 25 per cent higher than in 2008 on an AER basis, as higher margins in all businesses, particularly the US, were slightly offset by reduced sales volumes year-on-year. The average Group new business profit margin was 52 per cent (2008: 38 per cent) on an APE basis and seven per cent (2008: five per cent) on a PVNBP basis. This rise reflects increased average margins across the businesses as we concentrated on maximising sales of our most profitable products. In-force profits decreased by 18 per cent on 2008 to £617 million, due primarily to adverse persistency on investment related products in Asia mostly due to premium holidays in Korea, Hong Kong and Singapore and lower unwind of discount on in-force business in the UK.

Operating profit from the asset management business decreased to £125 million, down 31 per cent from £181 million in 2008, reflecting reduced market levels in the first half of 2009 compared to 2008.

EEV basis operating profit

	AER[6]			CER[6]	
	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Insurance business					
Asia	**401**	460	(13)	554	(28)
US	**501**	354	42	468	7
UK	**406**	490	(17)	490	(17)
Development expenses	**(5)**	(3)	(67)	(4)	(25)
Long-term business profit	**1,303**	1,301	–	1,508	(14)
UK general insurance commission	**27**	14	93	14	93
Asset management business:					
M&G	**102**	146	(30)	146	(30)
Asia asset management	**21**	29	(28)	36	(42)
Curian	**(3)**	0	–	0	–
US broker dealer and asset management	**5**	6	(17)	8	(38)
	1,455	1,496	(3)	1,712	(15)
Other income and expenditure	**(195)**	(131)	(49)	(136)	(43)
Restructuring costs	**(14)**	(15)	7	(15)	7
Total EEV basis operating profit	**1,246**	1,350	(8)	1,561	(20)

EEV basis profit after tax and minority interests

	AER[6]	
	Half year 2009 £m	Half year 2008 £m
EEV basis operating profit based on longer-term investment returns	**1,246**	1,350
Short-term fluctuations in investment returns		
Insurance operations	**(566)**	(1,711)
IGD hedge costs	**(216)**	–
Other operations	**75**	(157)
	(707)	(1,868)
Mark-to-market value movements on core borrowings	**(108)**	171
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	**(71)**	(98)
Effect of changes in economic assumptions and time value of cost of options and guarantees	**(384)**	(100)
Profit on sale and results of Taiwan agency business	**91**	(90)
Profit (loss) before tax	**67**	(635)
Tax	**(52)**	162
Minority interests	**(1)**	(2)
Profit (loss) for the period after minority interests	**14**	(475)

Note
See page 8.

Other income and expenditure totalled a net expense of £195 million compared with £131 million in 2008, a difference of negative £64 million of which £19 million was due to the net impact of (i) the non-recurrence in 2009 of a positive one-off 2008 item of £47 million of profit on the sale of a seed capital investment in an Indian mutual fund and (ii) a £28 million saving on project costs against last year. The balance of £45 million principally related to lower interest received on central shareholders' funds as a result of falling interest rates.

Short-term fluctuations in investment returns

In our calculation of EEV operating profit, we use longer-term investment return assumptions rather than actual investment returns achieved. Short-term fluctuations represent the difference between the actual investment return and the unwind of discount on the value of in-force business and expected returns on net worth.

Short-term fluctuations in investment returns for insurance operations of negative £566 million comprise a positive £101 million for Asia, negative £304 million for our US operations and negative £363 million in the UK.

For our Asian business, short-term fluctuations of positive £101 million, reflected the effect of strong equity market performance across the region offset by the impact of negative bond returns, particularly in Hong Kong, Malaysia and Singapore.

For our US business, short-term fluctuations in investment returns were negative £304 million (versus negative £297 million in 2008), primarily arising from a negative £287 million for the difference between the actual investment returns and the assumed long-term investment returns included in operating profit in respect of fixed income securities and related swap transactions. The balance is the combination of (i) negative £75 million for equity type investments and other items, in respect of the difference between actual investment returns and longer-term returns, and (ii) a positive £58 million resulting from the capitalisation of changes in the expectations of future profitability on variable annuity business in-force, due to the return on the actual variable investment account ('separate account') being in excess of the long-term return reported within operating profit, offset by the impact of the associated hedging position.

For our UK business, the short-term fluctuations in investment returns were negative £363 million, including negative £270 million relating to with-profits business, reflecting the difference between the negative 1 per cent actual investment return for the with-profits life fund and the long-term assumed return for the half year of 3.3 per cent and negative £60 million relating to shareholder-backed annuity business, primarily representing the unrealised loss on surplus assets.

As indicated earlier, the £216 million cost related to the exceptional IGD hedge has been included in short-term fluctuations.

For other operations the positive £75 million mainly comprises unrealised value movements of £69 million on swaps held centrally to manage Group assets and liabilities.

Mark-to-market movement on core borrowings

The mark-to-market movement on core borrowings was a negative £108 million, reflecting a narrowing of credit spreads applied to the market value of the debt.

Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes

The shareholders' share of actuarial and other gains and losses on defined benefit pension schemes of a negative £71 million reflects the effects of changes in economic assumptions, the shortfall of market returns over the long-term assumption, and change to provision for deficit funding obligation.

Effect of changes in economic assumptions and time value of cost of options and guarantees

The effect of changes in economic assumptions and time value of cost of options and guarantees of negative £384 million comprises negative £410 million for the effect of changes in economic assumptions partially offset by positive £26 million for the change in the time value of cost of options and guarantees arising from changes in economic factors. In our Asian business, economic assumption changes were negative £86 million primarily driven by increases in risk discount rates across a number of territories. In our US business, economic assumption changes were negative £60 million, primarily reflecting an increase in the risk discount rates following an increase in the US 10-year Treasury rate, partially offset by the effect of an increase in the separate account return assumption. In our UK business, economic assumption changes were negative £264 million, £159 million of this change arises in shareholder-backed annuity business and £105 million relates to with-profits and other business.

Profit on sale and results of Taiwan agency business

In June 2009, the Group completed the sale of our Taiwan agency business. The half year 2009 result of £91 million reflects the profit on sale. The half year 2008 loss of £90 million is the total result for the business, including short-term fluctuations in investment returns.

Effective tax rates

The effective tax rate at an operating tax level was 29 per cent (HY 2008: 28 per cent), primarily due to a lower tax rate in Asia. The effective tax rate at a total EEV level was 78 per cent (HY 2008: 26 per cent) on a profit of £67 million, primarily reflecting a reduction in the deferred tax credit relating to Jackson losses on fixed income securities.

IFRS results

Group operating profit before tax based on longer-term investment returns on the IFRS basis after restructuring costs was £688 million, an increase of six per cent on 2008.

In Asia, IFRS operating profit for long-term business increased from £75 million in 2008 to £212 million in 2009, £63 million of this increase is due to a one-off release of reserves in the Malaysian life operations. This release has been determined after assessing the measurement basis for liabilities for policyholders, following the implementation of a Risk Based Capital regime by the Malaysian regulatory authorities. Excluding this item, Asia delivered a strong underlying operating performance resulting in an increase of £74 million to £149 million from £75 million at half year 2008. Our more mature markets of Malaysia, Hong Kong and Singapore together with Indonesia continue to record increases in operating profit. In Indonesia, the results increased from £24 million to £42 million, reflecting the strong underlying growth of the business and the low level of new business strain in the territory. In Malaysia, IFRS operating profit of £32 million excluding the one-off credit was up 68 per cent on 2008, driven mainly by the growth in the in-force business, reductions in new business capital strain and positive sales and claims expenses. Hong Kong recorded an increased operating profit up 56 per cent to £25 million, due mainly to lower new business strain from lower sales, higher participating fund bonuses and positive claims variances. Singapore saw a slight increase in operating profit to £51 million mainly as a result of foreign exchange movements. Whilst Japan, Korea and our remaining business in Taiwan (excluding the Taiwan agency business) posted operating losses, these were all lower than for the same period in 2008.

In the US, the long-term business operating profit was down by six per cent on 2008 to £217 million in the first half of 2009, primarily as a result of lower separate account fee income, lower spread income and higher hedging costs reflecting equity market and interest rate falls. These falls were offset by the effect of favourable exchange rate movements and a related reduction in DAC amortisation.

In our UK business, the long-term business IFRS operating profit of £303 million increased by 11 per cent reflecting a 39 per cent growth from the shareholder-backed annuity business, partially offset by lower contribution from the with-profits business of £147 million from £198 million in 2008. The lower profit from the with-profit business reflected the impact of rate reductions in the February 2009 bonus declaration made in response to recent volatile investment performance. Profit from UK general insurance commission increased to £27 million in the first half of 2009 from £14 million in 2008. As a result, the total IFRS operating profit increased by 15 per cent in the first half of 2009 to £330 million.

M&G's operating profit for the first half of 2009 was £102 million, a decrease of 30 per cent over 2008. This reflects the relative levels of equity markets between 2008 and 2009 with the FTSE All Share being on average 31 per cent lower than in 2008.

The Asian asset management operations reported operating profits of £21 million, down by 28 per cent on 2008, largely as a result of lower average Funds Under Management (FUM), change in asset mix and a one-off loss of £6 million in India.

The increase of £69 million in other income and expenditure to negative £179 million primarily reflects a reduction in the earned return on central funds of £32 million and the non-recurrence of one-off items of positive £19 million in 2008.

IFRS basis operating profit based on longer-term investment returns

	AER[6]			CER[6]	
	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Insurance business:					
Long-term business					
Asia	**212**	75	183	92	130
US	**217**	232	(6)	307	(30)
UK	**303**	272	11	272	11
Development expenses	**(5)**	(3)	(67)	(4)	(25)
Long-term business profit	**727**	576	26	667	9
UK general insurance commission	**27**	14	93	14	93
Asset management business:					
M&G	**102**	146	(30)	146	(30)
Asia asset management	**21**	29	(28)	36	(42)
Curian	**(3)**	0	–	0	–
US broker-dealer and asset management	**5**	6	(17)	7	(29)
	152	195	(22)	203	(25)
Other income and expenditure	**(179)**	(110)	(63)	(110)	(63)
Restructuring costs	**(12)**	(14)	14	(14)	14
Total IFRS basis operating profit based on longer-term investment returns	**688**	647	6	746	(8)

Note
See page 8.

Since last year we have improved the way in which we analyse our results by classifying pre-tax operating profits from our life businesses into five distinct areas reflecting the specific nature of each profit stream:

- Investment spread;
- Asset management fees;
- Profits derived from taking on insurance risk;
- Shareholder transfers from the Group's with-profits funds; and
- Net expense margin (defined as operating expenses and DAC amortisation charged to operating profit net of relevant expense charges and loadings).

We believe that this approach provides a better understanding of the underlying trends in our markets and a simpler and more effective framework to present our results.

IFRS basis results – Analysis of life insurance pre-tax IFRS operating profit based on longer-term investment returns by driver

Investment spread has increased by £92 million to £514 million for the first half of 2009. This has been driven by an increase in our UK investment spread income of £40 million principally arising from UK shareholder-backed annuity business reflecting both our disciplined approach to annuity pricing and the higher returns arising from increased shareholder assets. The balance arises primarily from favourable exchange rate movements offsetting the fall in spread income in Asia and the US.

Asset management fees have fallen by eight per cent to £203 million in 2009 with lower fee income earned as a result of falling asset values being offset by favourable exchange rate movements.

The *net expense margin* represents expenses net of relevant charges and loadings and has improved by 16 per cent on an AER basis to a net expense of £209 million in 2009. This benefit arises predominantly as a result of lower new business strain in Asia primarily reflecting lower new business volumes and the non-recurrence of one-off expenses incurred in the UK.

Net insurance margin has increased by 71 per cent, reflecting strong growth in the Asian in-force book and positive claims experience in the US.

Profits from *with-profits* business were £158 million in the first half of 2009 compared with £210 million in the same period in 2008, reflecting lower bonus rates as a result of market falls.

2009 includes a £63 million one-off credit arising from the *release of regulatory reserves in Malaysia* following a change in reserving basis with the introduction of a Risk Based Capital approach.

Other of negative £59 million is primarily as a result of increased hedging costs in the US.

IFRS basis results – Analysis of life insurance pre-tax IFRS operating profit based on longer-term investment returns by driver

	AER[6]		CER[6]
	Half year 2009 £m	Half year 2008 £m	Half year 2008 £m
Investment spread	514	422	512
Asset management fees	203	221	274
Net expense margin	(209)	(249)	(294)
DAC amortisation (Jackson only)	(160)	(165)	(218)
Net insurance margin	217	127	155
With-profits business	158	210	214
Non-recurrent release of reserves for Malaysian life operation	63	–	–
Other	(59)	10	24
Total	727	576	667

Business review

IFRS basis profit after tax

	AER[6]	
	Half year 2009 £m	Half year 2008 £m
Operating profit based on longer-term investment returns	688	647
Short-term fluctuations in investment returns		
Insurance operations	61	(460)
IGD hedge costs	(216)	–
Other operations	75	(157)
	(80)	(617)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(63)	(92)
Profit/(loss) before loss on sale and results of Taiwan agency business	545	(62)
Loss on sale and results of Taiwan agency business	(621)	(40)
Loss before tax from continuing operations attributable to shareholders	(76)	(102)
Tax	(182)	(12)
Minority interests	4	(2)
Loss for the period attributable to equity holders of the Company	(254)	(116)

Note
See page 8.

Chief Financial Officer's overview
continued

The total profit before disposal of Taiwan agency business was £545 million in the first half of 2009, significantly higher than for the first half of 2008 (loss of £62 million). The improvement reflects the increase in operating profit based on longer-term investment returns and more favourable short-term fluctuations in investment returns partially offset by a charge for the costs of hedging the Group IGD capital surplus. The total loss before tax on the IFRS basis was £76 million in the first half of 2009, compared with a loss of £102 million for the first half of 2008, as a result of disposal of the Taiwan agency business which was completed in June 2009.

In calculating the IFRS operating profit, we use longer-term investment return assumptions rather than actual investment returns achieved. The difference between actual investment returns recorded in the income statement and longer-term returns is shown in the analysis of profits as short-term fluctuations in investment returns.

IFRS Short-term fluctuations in investment returns

Short-term fluctuations in investment returns for our insurance operations of £61 million comprises negative £41 million for Asia, positive £165 million for US operations and negative £63 million in the UK.

The negative short-term fluctuations of £41 million for our Asian operations primarily reflect the unrealised losses on the shareholder debt portfolio.

The positive short-term fluctuations of £165 million for our US operations primarily comprises £339 million for market value movements on the free standing derivatives used to manage the fixed annuity and other general account business, negative £247 million in respect of debt securities, and positive £73 million of other items. The negative £247 million for debt securities reflects the levels of realised gains and losses in excess of the allowance for longer-term defaults and amortisation of interest-related gains included in the operating result.

The negative short-term fluctuations of £63 million for our UK operations reflect principally value movements on the assets backing the capital of the shareholder-backed annuity business.

Short-term fluctuations for other operations, in addition to the previously discussed IGD hedge costs of £216 million, were £75 million positive, primarily comprised of unrealised value movements of £69 million on swaps held centrally to manage Group assets and liabilities.

Sale of Taiwan agency business

On 20 February 2009 we announced our agreement to transfer the assets and liabilities of the agency distribution business in Taiwan, including the capital consuming in-force book, to China Life Insurance Limited (Taiwan). We completed the transaction on 19 June 2009 following regulatory approval being given on that day. The transfer has resulted in a one-off negative pre-tax impact of £621 million. After allowing for tax, and other adjustments, the effect on shareholders' equity was £607 million. In the February announcement we estimated the one off impact to the IFRS shareholder's equity to be £595 million. The difference of £12 million reflects a number of minor adjustments. The overall size of loss reflects the carrying value of the IFRS equity of the business as applied in the calculation of the loss on sale and the application of 'grandfathered' US GAAP under IFRS 4 for insurance assets and liabilities. US GAAP does not and is not designed to include the costs of holding economic capital to support the legacy interest rate guaranteed products, as recognised under the Company's supplementary reporting basis under European Embedded Value principles. The loss on sale reflects this element of the economic value. Separately, it is to be noted that under IFRS there is no recognition of the enhanced IGD capital surplus position arising on completion.

Effective tax rates

The effective rate of tax on operating profits, based on longer-term investment returns, was 26 per cent (HY 2008: 29 per cent). The effective rate of tax at the total IFRS profit level for continuing operations was 239 per cent (HY 2008: 12 per cent) due to the loss on the disposal of the Taiwan agency business receiving no tax benefit.

Earnings per share

	2009 p Half year	2008 p Half year
Basic EPS based on operating profit after tax and minority interest		
EEV	35.4	39.2
IFRS	20.5	18.6
Basic EPS based on total profit/(loss) after minority interests		
EEV	0.6	(19.3)
IFRS	(10.2)	(4.7)

Dividend per share

The Board has agreed an interim dividend of 6.29 pence per share to be paid on 24 September 2009 to shareholders on the register at the close of business on 21 August 2009. The interim dividend for 2008 was 5.99 pence per share.

The Board will maintain its focus on delivering a growing dividend, which will continue to be determined after taking into account our Group's financial flexibility and our assessment of opportunities to generate attractive returns by investing in specific areas of the business. The Board believes that in the medium term a dividend cover of around two times is appropriate.

Movement on Shareholder's funds

EEV

On an EEV basis, which recognises the shareholders' interest in long-term business, shareholder funds at 30 June 2009 were £13.7 billion, a decrease of £1.3 billion from the 2008 year-end level. This reduced level of shareholders' funds reflects the profit after tax of £14 million, the adverse effects of exchange movements of £1.1 billion, dividend payments of £0.3 billion, which are partially offset by new share capital subscribed of £0.1 billion.

The shareholders' funds at the end of first half of 2009 relating to long-term business of £13.7 billion comprise £5.2 billion for our Asian long-term business operations, £3.8 billion for our US long-term business operations and £4.7 billion for the UK long-term business operations.

At the half year, the embedded value for our Asian long-term business operations was £5.2 billion. The embedded value for the established markets of Hong Kong, Singapore and Malaysia was £3.7 billion. There is also substantial embedded value in Korea (£286 million), Indonesia (£376 million) and Vietnam (£222 million).

For Prudential's other Asian markets, following the sale of the Taiwan agency business, the embedded value was £577 million in aggregate.

IFRS

Statutory IFRS basis shareholders' funds at 30 June 2009 were £4.7 billion. This compares to the £5.1 billion at 31 December 2008, a decrease of £0.4 billion.

The movement reflects the loss for the year after tax of £0.3 billion, exchange translation losses, principally on Jackson of £0.3 billion and dividend payments of £0.3 billion offset by the positive effect of a reduction in the level of net unrealised losses on Jackson's debt securities of £0.4 billion and other items of £0.1 billion.

The decline in the net unrealised losses of Jackson (net of DAC and tax) during 2009 was £ 0.4 billion. This reduction reflects the benefits of some normalisation in credit markets with spread tightening. Also, with markets for structured securities reverting to being more active in the period to 30 June 2009, nearly all the structured securities which had been valued at 31 December 2008 using internal valuation models due to inactive and illiquid markets, have now been valued based on external quotations.

Movement on Shareholder's funds

	EEV			IFRS		
	Half year 2009 £m	Half year 2008 AER £m	Full year 2008 AER £m	Half year 2009 £m	Half year 2008 AER £m	Full year 2008 AER £m
Operating profit based on longer-term investment returns	**1,246**	1,350	2,865	**688**	647	1,283
Items excluded from operating profit	**(1,179)**	(1,985)	(4,971)	**(764)**	(749)	(1,733)
Total profit (loss) before tax	**67**	(635)	(2,106)	**(76)**	(102)	(450)
Tax and minority interest	**(53)**	160	768	**(178)**	(14)	54
Profit (loss) for the period	**14**	(475)	(1,338)	**(254)**	(116)	(396)
Exchange movements, net of related tax	**(1,104)**	49	2,129	**(298)**	46	510
Unrealised gains and losses on Jackson securities classified as available for sale[note 1]	**–**	–	–	**423**	(285)	(831)
Dividends	**(322)**	(304)	(453)	**(322)**	(304)	(453)
New share capital subscribed	**96**	137	170	**96**	137	170
Other	**80**	(30)	(152)	**17**	12	(4)
Net increase (decrease) in shareholders' funds	**(1,236)**	(623)	356	**(338)**	(510)	(1,004)
Shareholders' funds at beginning of period	**14,956**	14,600	14,600	**5,058**	6,062	6,062
Shareholders' funds at end of period	**13,720**	13,977	14,956	**4,720**	5,552	5,058
Comprising						
Long-term business[note 2]						
Free surplus	**1,365**	1,143	447			
Required capital[note 2]	**2,799**	3,117	4,117			
Net worth	**4,164**	4,260	4,564			
Value of in-force	**9,510**	9,025	9,958			
Total	**13,674**	13,285	14,522			
Other business	**46**	692	434			
Total	**13,720**	13,977	14,956			

Notes

1 Net of related change to deferred acquisition costs and tax.

2 The reduction in required capital from £4,117 million at 31 December 2008 to £2,799 million at 30 June 2009, principally reflects the sale of the Taiwan agency business. Detailed explanations of the movements in the component elements of the EEV shareholders' funds are shown in the 'Movement in Shareholder's Equity Statement' of the EEV financial statements.

Free surplus and holding company cash flow

Free surplus generation

Sources and uses of free surplus generation from the Group's life and asset management operations

Group free surplus at the end of the period comprises free surplus for the insurance businesses, representing the excess of the net worth over the required capital included in the EEV results, and IFRS net assets for the asset management businesses excluding goodwill. The free surplus generated during the period comprises the movement in this balance excluding foreign exchange, capital movements, and other reserve movements. Specifically, it includes amounts maturing from the in-force operations during the period less the investment in new business, the effect of market movements and other one-off items.

For asset management operations we have defined free surplus generation to be total post-tax IFRS operating profit for the period. Group free surplus generated also includes the general insurance commission earned during the period and excludes restructuring and shareholders' centrally arising other income and expenditure.

During the first six months of 2009 we generated total free surplus from the retained businesses of £79 million. Underlying free surplus generated from the in-force book increased eight per cent from £843 million in the first half of 2008 to £912 million in 2009, reflecting both the change in exchange rates and the underlying growth of the portfolio in 2008, offset by negative changes in operating assumptions and variances of £37 million in the period for our life businesses.

Underlying free surplus generated has been used by our life businesses to invest in new business. Investment in new business has fallen by £19 million to £331 million in the first half of 2009. On a CER basis investment in new business has fallen by 21 per cent from £418 million in the first six months of 2008. This reduction reflects the Group's focus on conserving capital and delivering value over volume.

The negative impact on free surplus of market related items has increased by £258 million in the first half of 2009 to £502 million. This is driven mainly by the adverse impact on free surplus of impairments and credit downgrades within the US together with higher US hedging costs given the volatility of the market in the first half of 2009.

In June 2009 we completed the sale of the Taiwan agency business for £nil proceeds. As anticipated, this gave rise to an increase in free surplus by £987 million, representing the release of negative free surplus that previously applied. This compares to an increase in IGD capital of £800 million. The difference arises predominantly because the calibrations underpinning the capital requirements on a regulatory (IGD) basis are different from those applied on an economic capital (EEV) basis.

Movement in free surplus net of tax in the period

	AER[6]		
	Half year 2009 £m	**Half year 2008** £m	**Full year 2008** £m
Free surplus generation			
Expected in-force cash flows (including expected return on net assets)	**949**	812	1,623
Changes in operating assumptions and variances	**(37)**	31	(65)
Underlying free surplus generated in the period	**912**	843	1,558
Provisions for additional allowance for credit risk	**–**	(187)	(770)
Market related items	**(502)**	(244)	(689)
Investment in new business	**(331)**	(350)	(806)
Free surplus generated in the period from retained businesses	**79**	62	(707)
Effect of disposal and trading results of Taiwan agency business	**987**	(198)	(276)
Net cash remitted by the business units	**(375)**	(334)	(515)
Other movements and timing differences	**241**	86	442
Total movement during the period	**932**	(384)	(1,056)
Free surplus at 1 January	**859**	1,915	1,915
Free surplus at end of period	**1,791**	1,531	859
Comprised of:			
Free surplus of insurance business	**1,384***	1,143	447
IFRS net assets of asset management businesses excluding goodwill	**407**	388	412

* Free surplus of insurance business comprises £1,365 million relating to long-term business and £19 million of other assets.

Note
See page 8.

Value created through investment in new business by life operations

Overall, the Group wrote £1,321 million of sales on an APE basis during the period generating a post-tax new business contribution to embedded value of £479 million (2008: £395 million). To support these sales, we invested £331 million of capital (2008: £350 million). Over the first half of the year, we estimate the Group's internal rate of return to be greater than 20 per cent. This amount covers both new business strain, including commissions, of £111 million and the required capital of £220 million. Management's focus in the first half of 2009 was on capital preservation and so capital investment was focused on those areas which added most value to the Group, either in terms of new business profitability or to meet the Group's long-term strategic aims by maintaining distribution capability in key Asian territories in a challenging economic environment. Overall investment in new business has fallen as a result of this strategy but the amount of post-tax new business profit created per £1 million of free surplus invested increased by 27 per cent to £1.4 million (2008: £1.1 million).

In Asia, investment in new business was £118 million, which is flat compared to 2008 on a CER basis (£117 million). For each £1 million of free surplus invested we generated £1.7 million of post-tax new business contribution to embedded value (2008: £2.1 million). This fall arises predominantly from the structural change in Malaysia with the move to the Risk Based Capital regime increasing the required capital needed for new business. It also reflects cyclical changes in product mix, as customers in general are being more cautious about investing in single premium savings orientated products but demand for protection products remains resilient. The sale of these products has helped the Group to maintain its agency distribution capacity which will be beneficial once markets begin to recover. The average free surplus undiscounted payback period for business written in the six months to 30 June 2009 was 4 years (12 months to 31 December 2008: 4 years).

Value created through investment in new business by life operations

	Half year 2009				Half year 2008 [6]			
	Asia £m	US £m	UK £m	Group £m	Asia* AER £m	US AER £m	UK AER £m	Group AER £m
Free surplus invested in new business	(118)	(168)	(45)	(331)	(100)	(157)	(93)	(350)
Increase in required capital	29	149	42	220	12	140	61	213
Net worth invested in new business	(89)	(19)	(3)	(111)	(88)	(17)	(32)	(137)
Value of in-force created by new business	292	209	89	590	302	106	124	532
Post tax new business profit for the period	203	190	86	479	214	89	92	395
Tax	74	102	36	212	75	48	37	160
Pre-tax new business profit for the period	277	292	122	691	289	137	129	555
New business sales (APE)	553	392	376		648	356	438	
New business margins (% APE)	50%	74%	32%		45%	38%	29%	
Internal rate of return	>20%	>20%	>15%		>20%	18%	15%	

	Half year 2008 [6]			
	Asia* CER £m	US CER £m	UK CER £m	Group CER £m
Free surplus invested in new business	(117)	(208)	(93)	(418)
Increase in required capital	14	185	61	260
Net worth invested in new business	(103)	(23)	(32)	(158)
Value of in-force created by new business	357	140	124	621
Post tax new business profit for the period	254	117	92	463
Tax	89	64	37	190
Pre-tax new business profit for the period	343	181	129	653
New business sales (APE)	752	472	438	
New business margins (% APE)	46%	38%	29%	
Internal rate of return	>20%	18%	15%	

* Half year 2008 comparatives for Asia exclude amounts in respect of the Taiwan agency business that has been disposed of.

Note
See page 8.

In the US, our investment in new business was £168 million, 19 per cent lower than 2008 on a CER basis (£208 million). For each £1 million of free surplus invested we generated £1.1 million of post-tax new business contribution to embedded value (2008: £0.6 million), reflecting the increase in spread margins as Jackson reduced crediting rates as part of the Group's priority of capital preservation. The Group continues to balance the opportunity to invest in products offering attractive returns with its focus on capital management. We therefore actively chose not to reduce investment further in the US in 2009 in order to take advantage of the high product profitability currently available in the market, as a result of the dislocation observed over the last 12 months. The average free surplus undiscounted payback period for business written in the six months to 30 June 2009 was 2 years (12 months to 31 December 2008: 5 years).

In the UK, for each £1 million of free surplus invested we generated £1.9 million of post-tax new business contribution to embedded value (2008: £1.0 million). This reflects the UK's disciplined approach to individual annuity pricing and its focus on capital preservation with an increase in with-profits bonds sales and no bulk annuity transactions in the first half of 2009. The average free surplus undiscounted payback period for business written in the six months to 30 June 2009 was 5 years (12 months to 31 December 2008: 6 years).

Holding company cash flow

	2009 £m	2008 £m	
	Half year	Half year	Full year
Cash remitted by business units:			
UK Life fund paid to Group	284	279	279
Other UK paid to Group	–	–	46
Group invested in UK	(16)	(42)	(126)
UK net	268	237	199
US paid to Group	–	–	144
Group invested in US	–	–	–
US net	–	–	144
Asia paid to Group			
Long-term business	80	145	163
Other operations	31	3	234
	111	148	397
Group invested in Asia			
Long-term business	(34)	(104)	(310)
Other operations	(56)	(33)	(82)
	(90)	(137)	(392)
Asia net	21	11	5
M&G paid to Group	44	72	106
PruCap paid to Group	42	14	61
Net remittances to Group from Business Units	375	334	515
Net interest paid	(92)	(80)	(128)
Tax received	30	87	130
Corporate activities	(65)	(86)	(177)
Total corporate costs	(127)	(79)	(175)
Holding Company* Cash flow before dividend	248	255	340
Dividend paid net of scrip	(226)	(169)	(286)
Holding Company* Cash flow after dividend	22	86	54
Exceptional Item – Cash flow arising from sale of Taiwan agency business	(125)	–	–
Cash flow after exceptional item	(103)	86	54

* Including central finance subsidiaries.

Holding company cash flow

We are managing cash flows across the Group with a view to achieving a balance between ensuring sufficient net remittances from the businesses to cover the progressive dividend (after corporate costs) and maximising value for shareholders through the reinvestment of the free surplus generated at business unit level in the particularly profitable opportunities available to the Group given its privileged access to key Life Insurance markets. On this basis, the holding company cash flow statement should generally balance to close to zero.

Holding company cash flow for the first half of 2009 before dividend was £248 million broadly in line with the first half of 2008. After dividend, the holding company cash flow was £22 million, £64 million lower than 2008 reflecting the higher dividend paid in 2009 and a higher scrip take-up in 2008.

The holding company received £375 million net remittances from business units in the first half of 2009, (including £314 million which relates to long-term business operations) up from £334 million in the first half of 2008. Gross remittances were £481 million, slightly down from £513 million at half year 2008.

The reduction in cash remitted from Asia was mainly due to the exceptional £50 million release of risk based capital in Singapore in 2008. This reduction was partly offset by an increase in remittances from Asia's asset management businesses from £3 million in 2008 to £31 million in 2009. Remittances from the Group's UK asset management businesses totalled £86 million in both periods.

Capital invested in business units in 2009 was £106 million compared to £179 million for 2008. Injections into Asia and the UK were both down from 2008 levels due to lower new business growth and reduced requirements for regulatory capital in a number of our Asian businesses.

Net interest paid in 2009 increased from £80 million to £92 million as falling interest rates led to reduced interest received on central shareholders' funds by £17 million.

Tax received in 2009 was £30 million, down £57 million from 2008, due to lower UK taxable profits available for offset. Payments for corporate activities at £65 million were £21 million lower, mainly because costs in 2008 related to investigating the potential reattribution of the inherited estate, did not feature in 2009.

After corporate costs, there was in the first half of 2009 a net cash inflow before dividend of £248 million compared to £255 million for the first half of 2008. The dividend paid net of scrip, was £226 million in 2009 compared to £169 million in 2008. The take-up of scrip dividends in 2009 continued to be significant at £96 million (2008: £134 million).

As a consequence, overall, we reported a positive underlying cash inflow of £22 million in 2009. There were also exceptional payments of £125 million in connection with the sale of the Taiwan agency business to China Life, comprised of £45 million to purchase a 9.99 per cent stake in that company and £80 million for transaction related expenditure including restructuring costs.

Based on current projections, depending on the opportunities available, we continue to expect the UK shareholder-backed business to be cash flow positive in 2010.

Balance sheet
Summary

	AER[6]		
	Half year 2009 £m	Half year 2008 £m	Full year 2008 £m
Investments	179,457	194,668	193,434
Holding company cash and short-term investments	1,252	1,498	1,165
Other	18,677	14,989	20,943
Total assets	199,386	211,155	215,542
Less: Liabilities			
Policyholder liabilities	165,047	169,113	173,977
Unallocated surplus of with-profits funds	7,061	12,560	8,414
	172,108	181,673	182,391
Less: shareholders' accrued interest in the long-term business	(9,000)	(8,425)	(9,898)
	163,108	173,248	172,493
Core structural borrowings of shareholders' financed operations (IFRS book value basis)	2,899	2,526	2,958
Other liabilities including minority interest	19,659	21,404	25,135
Total liabilities and minority interest	185,666	197,178	200,586
EEV basis net assets	13,720	13,977	14,956
Share capital and premium	1,966	1,962	1,965
IFRS basis shareholders' reserves	2,754	3,590	3,093
IFRS basis shareholders' equity	4,720	5,552	5,058
Additional EEV basis retained profit	9,000	8,425	9,898
EEV basis shareholders' equity (excluding minority interest)	13,720	13,977	14,956

The following sections focus on key areas of interest in the balance sheet.

Shareholders' net borrowings and debt ratings

Shareholders' borrowings at 30 June 2009:

	Half year 2009 £m			Full year 2008 £m		
	IFRS basis	Mark-to-market value	EEV basis	IFRS basis	Mark-to-market value	EEV basis
Perpetual subordinated						
Capital securities (Innovative Tier 1)	(950)	338	(612)	(1,059)	546	(513)
Subordinated notes (Lower Tier 2)	(1,248)	192	(1,056)	(928)	191	(737)
	(2,198)	530	(1,668)	(1,987)	737	(1,250)
Senior debt						
2009	–	–	–	(249)	–	(249)
2023	(300)	46	(254)	(300)	12	(288)
2029	(249)	58	(191)	(249)	53	(196)
Holding company total	(2,747)	634	(2,113)	(2,785)	802	(1,983)
Jackson surplus notes (Lower Tier 2)	(152)	12	(140)	(173)	19	(154)
Total	(2,899)	646	(2,253)	(2,958)	821	(2,137)
Less: Holding company cash and short-term investments	1,252	–	1,252	1,165	–	1,165
Net core structural borrowings of shareholder-financed operations	(1,647)	646	(1,001)	(1,793)	821	(972)

Note
See page 8.

The Group's core structural borrowings at 30 June 2009 totalled £2.9 billion on an IFRS basis, compared with £3 billion at the end of 2008. In May 2009, senior debt of £ 0.2 billion was repaid on maturity and new hybrid debt of £0.4 billion was issued. In addition there were exchange translation gains of £0.2 billion on US dollar denominated borrowings in the period.

After adjusting for holding company cash and short-term investments of £1.3 billion, net core structural borrowings at 30 June 2009 were £1.6 billion compared with £1.8 billion at the end of 2008. The reduction of £0.2 billion includes the gains of £0.2 billion mentioned above, further gains of £59 million in respect of a US dollar $0.6 billion net investment hedge and the previously discussed positive cash flow of £22 million offsetting the exceptional payments of £0.1 billion and fair value and other adjustments of negative £30 million.

Prudential plc has strong debt ratings from Standard & Poor's, Moody's and Fitch. Prudential long-term senior debt is rated A+ (stable), A2 (negative) and A+ (negative) from Standard & Poor's, Moody's and Fitch respectively, while short-term ratings are A-1, P-1 and F1+.

Investments

Total investments held by the Group at 30 June 2009 were £179.5 billion, of which £88.4 billion were held by participating funds, £37.7 billion by unit-linked funds and £53.4 billion by shareholder-backed operations. Shareholders are not directly exposed to value movements on assets backing participating or unit-linked operations, with sensitivity mainly related to shareholder-backed operations.

Of the £53.4 billion investments related to shareholder-backed operations, £2.8 billion was held by Asia long-term business, £27.4 billion by Jackson and £20.0 billion by the UK long-term business respectively.

The investments held by the shareholder-backed operations are predominantly debt securities, totalling £2.0 billion, £20.9 billion and £17.0 billion for Asia, the US and the UK long-term business respectively, of which 70 per cent, 92 per cent and 96 per cent are rated either externally or internally, as investment grade. Included within debt securities are Tier 1 and Tier 2 bank holdings of £3.7 billion, of which Tier 1 holdings of UK bank securities is £278 million, with exposure being £nil million, £20 million and £258 million for Asia, the US and the UK long-term business. Within Tier 2, our exposure to UK banks is £1.0 billion, with exposure being £nil million, £109 million, £798 million and £96 million for Asia, the US, the UK long-term business and other operations.

In addition £3.2 billion was held by asset management operations, of which £3.0 billion was managed by Prudential Capital, and a further £0.2 billion in central operations.

Investments

	Half year 2009				Full year 2008
	PAR Funds £m	Unit-Linked £m	Shareholder-backed £m	Total Group £m	Total Group £m
Debt securities	41,753	6,763	40,883	**89,399**	95,224
Equity	26,098	29,295	676	**56,069**	62,122
Property Investments	8,507	616	1,356	**10,479**	11,992
Commercial mortgage loans	149	–	4,401	**4,550**	5,473
Other Loans	1,632	47	2,384	**4,063**	5,018
Deposits	6,300	780	1,726	**8,806**	7,294
Other Investments	3,917	235	1,939	**6,091**	6,311
Total	88,356	37,736	53,365	**179,457**	193,434

Policyholder liabilities

	Shareholder-backed business			
	Asia £m	US £m	UK £m	Total £m
At 1 January 2009	12,975	45,361	33,853	**92,189**
Premiums	1,296	3,850	1,823	**6,969**
Surrenders	(291)	(2,244)	(827)	**(3,362)**
Maturities/Deaths	(33)	(404)	(948)	**(1,385)**
Net cash flows	**972**	**1,202**	**48**	**2,222**
Investment related items and other movements	1,396	884	166	**2,446**
Disposal of Taiwan agency business	(3,508)	–	–	**(3,508)**
Change in reserving basis in Malaysia	(63)	–	–	**(63)**
Foreign exchange translation difference	(1,574)	(5,955)	(1)	**(7,530)**
At 30 June 2009	10,198	41,492	34,066	**85,756**
Add policyholder liabilities of with-profits funds				**79,291**
Total policyholder liabilities				**165,047**

Business review

Chief Financial Officer's overview
continued

Policyholder liabilities

Policyholder liabilities related to shareholder-backed business fell by £6.4 billion from £92.2 billion to £85.8 billion. The reduction reflected the disposal of the Taiwan agency business (negative impact of £3.5 billion), a £63 million reduction in liabilities following the change in reserving basis in Malaysia and foreign exchange movements of negative £7.5 billion.

Importantly, however, the Group had positive net cash flows (premiums less surrenders and maturities/deaths) into shareholder-backed business of £2.2 billion in the period to 30 June 2009. This predominantly reflected strong net inflows in Asia (£1 billion) and the US (£1.2 billion).

Investment related items and other movements were £2.4 billion during the period principally reflecting the growth in the Asian equity markets and investment income credited to policyholder liabilities in the US.

Financial position on defined benefit pension schemes

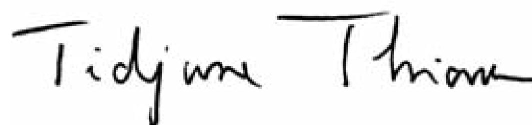
The Group currently operates three defined benefit schemes in the UK, of which by far the largest is the Prudential Staff Pension Scheme (PSPS) and two smaller schemes, Scottish Amicable (SAPS) and M&G.

Defined benefit schemes in the UK are generally required to be subject to a full actuarial valuation every three years, in order to assess the appropriate level of funding for schemes in relation to their commitments. The valuations of PSPS as at 5 April 2008 and SAPS as at 31 March 2008 were recently finalised. The valuation of PSPS demonstrated the scheme to be 106 per cent funded by reference to the Scheme Solvency Target that form the basis of the scheme's funding objective. Accordingly, the total contributions to be made by the Group into the scheme has been reduced from the previous arrangement of £75 million per annum to £50 million per annum effective from July 2009.

The valuation of SAPS as at 31 March 2008 demonstrated the scheme to be 91 per cent funded, representing a deficit of £38 million. Based on this valuation, deficit funding amounts of £7.3 million per annum designed to eliminate the actuarial deficit over a 7 year period are being made from July 2009.

The valuation basis under IAS 19 for the Group financial statements differs markedly from the full triennial actuarial valuation basis. For PSPS, the Group has not recognised its interest in the underlying PSPS IAS 19 pension surplus of £416 million net of related tax relief at 30 June 2009 due to the Group not having an unconditional right of refund to any surplus in the scheme. Further, the Group has also recognised a provision under IAS 19 for a deficit funding obligation of £57 million net of related tax relief in respect of PSPS based on the new funding arrangements as described above. Although the contributions will increase the surplus in the scheme, the corresponding asset will not be recognised in the Group financial statements under IAS 19. Deficit funding for PSPS is apportioned in the ratio of 70/30 between the PAC with-profits fund and shareholder-backed operations.

As at 30 June 2009, on the Group IFRS statement of financial position, the shareholders' share of the liabilities for these UK schemes amounted to a £87 million liability net of related tax relief. The total share attributable to the PAC with-profits fund amounted to a liability of £110 million net of related tax relief.



Tidjane Thiam
Chief Financial Officer

Capital management

Prudential is subject to the capital adequacy requirements of the European Union (EU) Insurance Groups Directive (IGD) as implemented by the Financial Services Authority (FSA) in the UK. The IGD capital adequacy requirements involves aggregating surplus capital held in our regulated subsidiaries, from which Group borrowings, except those subordinated debt issues that qualify as capital, are deducted. No credit for the benefit of diversification is permitted under this approach.

Our capital position has been further strengthened during 2009, driven by our prudent but proactive risk management. Our IGD capital surplus is estimated at £2.5 billion at 30 June 2009 (before any allowance for the 2009 interim dividend) giving an estimated solvency ratio of 237 per cent. After allowing for the July hybrid debt issuance, the Group IGD capital surplus is estimated to be £3.0 billion leading to an estimated solvency ratio of 262 per cent. This compares to a position (before allowing for a dividend) at the end of 2008 and at the end of the first quarter 2009 of £1.5 billion and £1.6 billion respectively. The movement from £1.5 billion at 31 December 2008 to the estimated £2.5 billion comprises:

- Internal capital generation of £0.3 billion;
- The impact of the sale of our agency distribution business in Taiwan of £0.8 billion;
- Additional hybrid debt, issued in May 2009, of £0.4 billion; and
- Additional recognition of a £0.4 billion part of the shareholders' interest in the future transfers from the PAC with-profit fund by FSA (up from £0.3 billion recognised in February 2009).

Offset by:

- Final 2008 dividends, net of scrip, of £0.2 billion;
- Credit related impairments and default losses in the US of £0.3 billion;
- Other market related impacts of £0.2 billion; and
- Foreign exchange movements of £0.2 billion.

We have strengthened our IGD capital position in challenging markets. We continue to have further options available to us to manage available and required capital. These could take the form of either increasing available capital (for example, through financial reinsurance or debt issuance) or reducing required capital (for example, through the level and the mix of new business, notably by maintaining pricing discipline and through the use of other risk mitigation strategies such as hedging and reinsurance).

In addition to this strong capital position, the total credit reserve for the UK shareholder annuity funds, which protects our capital position in excess of the IGD surplus, has been maintained at £1.4 billion. This reserve is equivalent to 85 bps per annum over the lifetime of the assets and would allow us to withstand a repeat of the average default experience during the Great Depression occurring every year throughout the life of the portfolio.

As already mentioned, during the extreme equity market conditions experienced in the first quarter of 2009, with equity volatilities at historically high levels, the Group entered into additional one-off hedging contracts to protect the Group's IGD capital position against a tail-event of an instantaneous 40 per cent drop in equity market level with no recovery. The vast majority of the costs related to that hedge have been incurred in the first half and the hedge will not be renewed as the Group's capital surplus has been significantly enhanced since then and market concern about such extreme events has receded.

As at 30 June 2009, the impact of a more realistic instantaneous 20 per cent fall in equity market levels would not be significant. A 20 per cent one day fall with no recovery is equivalent to the worst historic daily fall in the S&P. Were equity markets to fall by more than 20 per cent, we consider that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which we would be able to put into place mitigating management actions including the rebalancing of our hedging position. For example, we have estimated that the impact (net of mitigating management actions) of an additional 20 per cent fall in equity markets over a four week period following an instantaneous 20 per cent fall would be an estimated reduction in the IGD surplus of a further £200 million.

These equity sensitivities are assumed to be in addition to the 28 per cent fall the equity markets had already experienced in the twelve months prior to 30 June 2009.

In summary, the findings of our stress testing and sensitivity analysis, which are part of the continual process of assessing the resilience of the Group's IGD capital position to withstand significant further deterioration in market conditions include:

- An instantaneous further 20 per cent fall in equity markets from 30 June 2009 levels would not have a significant impact on IGD surplus;
- A 40 per cent fall in equity markets (comprising an instantaneous 20 per cent fall followed by a further 20 per cent fall over a four week period) would reduce the IGD surplus by £200 million;
- A 150bps reduction (subject to a floor of zero) in interest rates from 30 June 2009 would reduce the IGD surplus by £300 million; and
- Credit defaults of ten times the expected level would have an impact of £650 million in excess of the annual reserve release.

The results of these stress tests, together with our Group's strong underlying earnings capacity, our established hedging programmes and our additional areas of financial flexibility, demonstrate that we are in a position to withstand possible significant further deterioration in market conditions.

We also use an economic capital assessment to monitor our capital requirements across the Group, allowing for realistic diversification benefits and continue to maintain a strong position. This assessment provides valuable insights into our risk profile and is used for both risk measurement and capital management.

The EU is developing a new solvency framework for insurance companies, referred to as 'Solvency II' which will be very important for the insurance industry. There will be continued uncertainty until the rules are finalised and Prudential is actively participating in shaping the outcome through our involvement in industry bodies, including in the Chief Risk Officer and Chief Financial Officer Forums, and progressing with our implementation plans.

Risk management

As a provider of financial services, we recognise that the managed acceptance of risk lies at the heart of our business. As a result, effective risk management capabilities represent a key source of competitive advantage for our Group. To maximise this advantage, we have embedded a risk and capital management framework and culture that drives our rigorous risk and capital management and the optimisation of risk adjusted returns across the Group.

The Group's risk appetite framework sets out our tolerance to risk exposures as well as our approach to risk management and return optimisation. Under this approach, we monitor our risk profile continuously against agreed limits. Our core strategies for managing and mitigating risk include asset liability management, the use of financial instruments to hedge relevant market risks, and implementing reinsurance and corporate insurance programmes.

Our risk exposure and approach to risk management were described in detail in our 2008 year end report and remain valid.

Equity risk

We have an exposure to equity risk that varies between each of our main operations. Most of the equity exposure in our UK business arises from the with-profits fund which includes a large inherited estate, estimated at £5.0 billion at 30 June 2009, which can absorb the impact of market fluctuations and protect the fund's solvency. The inherited estate itself is partially protected against falls in equity markets through an active hedging policy. In the first half of 2009 we have reduced the fund's exposure to UK equities whilst increasing the proportion of bonds and cash.

In Asia, a high proportion of our in-force book is made up of unit-linked products with limited shareholder exposure to equities. We have minimal direct shareholder exposure to Asian equity markets outside our unit-linked holdings and this has been further reduced during the first half of the year.

In the US, where we are a leading provider of variable annuities, there are well-understood risks associated with the guarantees embedded in our products. To protect the shareholder against the volatility induced by these embedded options, we use both a comprehensive hedging programme and reinsurance.

In our variable annuity sales activities, we focus on meeting the needs of conservative and risk averse customers who are seeking reliable income in retirement and who display little tendency to arbitrage their guarantees. We seek to sell at a price where we can hedge or reinsure our risks, for example in 2009 we discontinued the GMIB guarantee and repriced certain GMWB guarantees.

We take a macro approach to hedging that covers market risk in the US business, including all exposure to GMDB and GMWB guarantees. Within this macro approach we make use of the natural offsets that exist between the variable annuity guarantees and the fixed-indexed annuity book, and then use a combination of over the counter options and futures to hedge the residual risk, allowing for significant market shocks and minimising the amount of capital we are putting at risk. The hedging programme covers both the in-force book and new business for the 'greeks' – i.e. changes in equity market levels, the rate of change in market levels and equity market volatility, as well as interest rate movements. We also hedge the fees on variable annuity guarantees.

Interest rate risk

Interest rate risk arises primarily from Prudential's investments in long-term debt and fixed income securities. Interest rate risk also exists in policies that carry investment guarantees on early surrender or at maturity, where claim values can become higher than the value of backing assets as a result of rises or falls in interest rates.

Interest rates primarily impact our Asia, US and UK with-profits businesses. However, the sale of the agency-based business in Taiwan has significantly reduced our exposure to interest rate risk in Asia. The remaining risk relates mostly to guarantees on traditional shareholder-backed life products and asset-liability mismatches, primarily in Japan and Korea. This exposure is within our risk appetite, and we monitor and manage it carefully on an ongoing basis. We have a range of risk mitigation options available to us should we wish to reduce this exposure further.

In the US there is interest rate risk across the portfolio. We manage fixed annuity interest rate exposure through a combination of interest rate swaps and interest rate options, to protect capital against rates rising quickly, and through the contractual ability to reset crediting rates annually. On variable annuities business interest rate risk has natural offsets within Jackson's other liabilities, particularly fixed annuities and guaranteed investment contracts. The net position is then hedged externally in order to achieve the desired risk profile.

In the UK the investment policy for the shareholder-backed annuity business is to match the cash flow from investments with the annuity payments. As a result, assets and liabilities are closely matched by duration. The impact of any residual cash flow mismatching can be adversely affected by changes in interest rates, but the impact is expected to be small.

Foreign exchange risk

Prudential operates in 13 countries in Asia, in the US, in the UK, and in Continental Europe. The geographical diversity of our businesses means that we are inevitably subject to the risk of exchange rate fluctuations. Prudential's international operations in the US and Asia, which represent a significant proportion of our operating profit and shareholders' funds, generally write policies and invest in assets denominated in local currency. Although this practice limits the effect of exchange rate fluctuations on local operating results, it can lead to significant fluctuations in our consolidated financial statements when results are expressed in pounds sterling.

We do not generally seek to hedge foreign currency revenues, as these are substantially retained locally to support the growth of the Group's business and meet local regulatory and market requirements. However, in cases where a foreign surplus is deemed to be supporting Group capital or shareholders' interest, this exposure is hedged if we deem it economically optimal to do so. Currency borrowings, swaps and other derivatives are used to manage exposures.

Credit risk

Debt portfolio

Our debt portfolio on an IFRS basis was estimated at £89.4 billion at 30 June 2009. £40.9 billion of these assets backed shareholder business, of which 93 per cent were investment grade, compared to 96 per cent at 31 December 2008. This change was a result of downgrades, largely occurring in March and April, with the pace of downgrade significantly slowing subsequently.

Asia

Asia's debt portfolio totalled £8.3 billion at 30 June 2009. Of this, approximately 76 per cent was invested in unit-linked and with-profits funds with minimal shareholder risk. The remaining 24 per cent is shareholder exposure and is invested predominantly (70 per cent) in investment grade bonds. For Asia, the portfolio has performed very well, with no default losses in the first half of 2009.

UK

The total debt portfolio for UK insurance operations was £59.2 billion, including £37.4 billion within the UK with-profits fund. Shareholders' risk exposure to the with-profits fund is limited as the solvency is protected by the large inherited estate which absorbs market fluctuations. Outside the with-profits fund, £4.8 billion was held in unit-linked funds where the shareholder risk is limited, and the remaining £17.0 billion (of which 78 per cent is rated AAA to A, 18 per cent BBB and four per cent non-investment grade) was backing the shareholder annuity business and other non-linked business. Despite downgrades of £3.4 billion mostly in the first quarter of 2009, (85 per cent of these being in Financial Institutions) the quality of the portfolio remains high with 96 per cent of the portfolio rated investment grade, compared to 99 per cent at 31 December 2008.

On a statutory basis we have maintained the credit reserve within the UK shareholder annuity funds of £1.4 billion to allow for future defaults. This reserve can withstand the equivalent of the average default experience during the Great Depression occurring every year over the life of the portfolio. In the first half of 2009, we have experienced credit defaults for UK operations of £11 million that relate to shareholder funds (0.1 per cent of the portfolio).

US

The most significant area of exposure to credit risk for the shareholder is Jackson in the US. At 30 June 2009 Jackson's fixed income portfolio was £20.9 billion, comprising £14.9 billion of Corporate Debt, £1.7 billion of Commercial Mortgage Backed Securities (CMBS), £3.4 billion of Residential Mortgage Backed Securities (RMBS) and £0.9 billion of other instruments. We entered the present credit cycle in a defensive position and continue to manage the portfolio rigorously.

The US Corporate Debt portfolio of £14.9 billion is 91 per cent investment grade, compared to 92 per cent at 31 December 2008. Concentration risk is low, with the top ten holdings accounting for only 5 per cent of the portfolio. The high-yield portfolio is also well diversified with an average holding of £9 million. Our largest sector exposures, in the investment grade portfolio are Utilities and Energy both at 15 per cent. We actively manage the portfolio and will sell exposure as required.

Within the RMBS portfolio of £3.4 billion, the agency guaranteed portion is 64 per cent. Another 19 per cent of the portfolio relates to investments with pre-2006/2007 vintages, where experience has generally been more positive than later vintages. Our exposure to the 2006/2007 vintages totals £406 million of which £304 million is invested in the senior part of the capital structure, thereby significantly reducing the risk of defaults and the magnitude of loss if a shortfall were to occur. In a typical RMBS structure the non-AAA tranches are relatively thin, so as collateral losses increase, non-AAA tranches can be hit very hard. The senior/AAA tranche, on the other hand, is very wide, and thus, the actual economic loss is much more contained and much lower than the current price declines driving reported accounting values. The actual exposure to non-senior 2006/2007 Prime and Alt-A RMBS is only £102 million. This portfolio has an average fair value price of 76 cents in the dollar.

The CMBS £1.7 billion portfolio is performing well, with 89 per cent of the portfolio being AAA and none below investment grade. We materially reduced our non-AAA purchases after 2004 in response to the significant deterioration in underwriting standards observed in the market and in line with rating agencies' guidelines. The entire portfolio has an average credit enhancement level of 30 per cent. This provides significant protection, since it means the bond has to incur a 30 per cent loss, net of recoveries, before we are at risk.

Jackson experienced less than £1 million of bond default losses during the first half of 2009. As part of our active management of the book we incurred net losses of £42 million on the sale of impaired bonds. IFRS write-downs excluding defaults for the half-year were £324 million.

The impairment process reflects a rigorous review of every single bond and security in our portfolio. We believe that the accounting rules for impairments are necessarily conservative and not always consistent with economic losses. So, while the accounting requires us to book them as losses through our income statement, we would expect only a proportion of these impairments eventually to turn into defaults, and some of the impaired securities to recover in price over time.

In considering potential future losses for Jackson, it is essential to examine the key components of the debt portfolio. As at 30 June 2009, 92 per cent of Jackson's total debt portfolio of £20.9 billion consisted of investment grade securities and 8 per cent were high yield. To put potential future losses in context, the highest global annual default rates over the past 50 years were 0.5 per cent for investment grade and 10 per cent for high yield, and the highest global annual default rates during a recession have been 1.6 per cent for investment grade and 15.4 per cent for high yield, although not necessarily in the same year (Source: Moody's Investors Service – February 2009).

Applying peak annual default rates and making conservative assumptions for recoveries to our US debt portfolio would generate losses of approximately £330 million for one year that could be absorbed by our current IGD surplus as estimated at 30 June 2009.

Asset management

The debt portfolio of the Group's asset management operations of £978 million principally comprises £966 million related to Prudential Capital operations. Of this amount, debt securities of £923 million were rated AAA to A- by S&P or Aaa by Moody's.

Loans

Of the total Group loans of £8.6 billion at 30 June 2009, £6.8 billion are held by shareholder-backed operations comprising of £4.4 billion commercial mortgage loans and £2.4 billion of other loans.

Of this total held by shareholder-backed operations, the Asian insurance operations held £0.3 billion of other loans; the majority of which are commercial loans held by the Malaysian operation that are investment graded by two local rating agencies. The US insurance operations held £4.3 billion of loans, comprising £3.8 billion of commercial mortgage loans, all of which are collateralised by properties, and £0.5 billion of policy loans. The US commercial mortgage loan portfolio does not include any single-family residential mortgage loans and therefore is not exposed to the risk of defaults associated with residential sub-prime mortgage loans. The UK insurance operations held £0.6 billion, the majority of which are mortgage loans also collateralised by properties.

The balance of the total loans amounts to £1.6 billion and relates to bridging loan finance managed by Prudential Capital. The bridging loan assets generally have no external credit ratings available, with internal ratings prepared by the Group's asset management operations as part of the risk management process, with the majority being rated BBB+ to BBB-.

Unrealised credit losses in the US

Jackson's gross unrealised losses reduced from £3.2 billion at 31 December 2008 to £2.2 billion at 30 June 2009. This change reflects the benefits of some normalisation of the credit markets. The entire market for fixed income securities has been re-priced downwards from historically tight spreads of approximately 100 bps experienced during the first half of 2007, with average spreads on investment grade paper in excess of 331 bps at 30 June 2009. Wider credit and liquidity spreads are causing the average investment grade security to trade around the mid to high 90s as a per cent of book value. Unrealised losses on securities priced at less than 80 per cent of face value were £1.5 billion at 30 June 2009. It is our intention to hold these fixed income securities to maturity – an approach which in economic terms limits the impact of the current market dislocation.

With the return of liquidity in most segments, of structured securities, virtually all the non-agency RMBS, ABS and certain CMBS that, at 31 December 2008, were valued using internal valuation models due to the dislocated market conditions in 2008, have now been valued using external prices.

We believe that the accounting impact of these unrealised losses significantly overstates the risk of economic losses on our portfolio at current price levels.

Insurance risk

The processes of determining the price of our products and reporting the results of our long-term business operations require us to make a number of assumptions. In common with other industry players, the profitability of our businesses depends on a mix of factors including mortality and morbidity trends, persistency, investment performance, unit cost of administration and new business acquisition expenses. We continue to conduct rigorous research into longevity risk using data from our substantial annuitant portfolio. Prudential's persistency assumptions reflect recent experience for each relevant line of business, and any expectations of future persistency. Where appropriate, allowance is also made for the relationship – either assumed or historically observed – between persistency and investment returns, and for the resulting additional risk.

Liquidity risk

Our liquidity position remains very strong, both at holding and subsidiary company level. The holding company has significant internal sources of liquidity which are sufficient to meet all of our expected requirements for the foreseeable future without having to make use of external funding. In aggregate the Group has £2.1 billion of undrawn committed facilities, of which, in February 2009, we renewed £1.4 billion of the undrawn syndicated committed banking facility for a further three years. We also have two £100 million undrawn bilateral committed banking facilities expiring in 2011 and 2012, with the balance being an annually renewable £500 million committed securities lending facility. In addition the Group has access to liquidity via the debt capital markets, which was demonstrated most recently through the two hybrid instruments, £400 million of Lower Tier 2 debt issued in May and US dollar $750 million (approximately £455 million) of Innovative Tier 1 debt issued in July.

Non-financial risk

Prudential is exposed to operational, business environment and strategic risk in the course of running its businesses. We process a large number of complex transactions across numerous and diverse products, and are subject to a number of different legal and regulatory regimes. We also have a significant number of third-party relationships that are important to the distribution and processing of our products, both as market counterparties and as business partners.

We use quantitative analysis of operational risk exposures material to the Group to inform our decisions on the overall amount of capital held and the adequacy of our corporate insurance programme.

Risk factors and contingencies

The Group published details of its risk factors and contingencies in its 2008 Annual Report. There have been no changes in the nature of the risk factors during the period. Note R of the IFRS basis condensed consolidated financial statements gives an update on the position for contingencies.

Asia

Demographic trends will continue to drive sustained demand for savings and protection products in Asia, particularly in the large and still developing markets such as China, India, Indonesia and Vietnam. We remain fully committed to leveraging our already strong operations in the region to deliver superior and highly profitable growth over the long term.

Although the IMF have recently revised upwards its forecasts for Asian growth in 2009 and 2010, indicating that the recovery is getting underway, market conditions remained challenging in the second quarter of 2009. Excluding the Taiwan agency business, Prudential's new business APE of £553 million for the first half 2009, was 15 per cent lower than in the first half 2008 and although market data is not yet available, we believe this to be generally in line with the market as we are maintaining our new business rankings with eight life operations in the top three in their respective countries. New business profits were only four per cent lower than the same period last year thanks to higher margins driven by higher proportions of regular premiums and protection products. IFRS basis profits driven by the increasing scale of the in-force book grew very strongly, even before counting the one-off reserve release in Malaysia for £63 million.

While each market in our portfolio has its own unique features, there are some common themes. In a more volatile economic environment, customers have generally been more cautious about committing lump sums to savings orientated policies, particularly policies with direct market exposure such as unit linked products. As a result, during the first half of 2009, single premium business was down from £931 million for the first half of 2008 to £365 million and the proportion of single premium in the APE mix was seven per cent compared to 14 per cent for the same period last year. It is worth noting that single premium sales in the first half last year did include an exceptional boost from Central Provident Fund (CPF) related business in Singapore. Regular premium sales of £517 million were just seven per cent lower than in the first half of 2008 reflecting the resilience of these products despite challenging market conditions. Total sales of unit linked products on an APE basis of £221 million represent 40 per cent of the product mix compared to 61 per cent for the first half of 2008 equivalent to £392 million.

We continue to make excellent and crucial progress in the area of protection products, where demand continues to be strong, in line with our expectations and our stated priority of increasing our focus on these products. Over the last 12 months we have launched several new products that have contributed to the increase of the proportion of 'protection' APE from 22 per cent (£140million) in the first half of last year to 30 per cent (£164 million) for the first half of 2009. Protection products have also proven to be useful in maintaining agency momentum as they address one important customer need and typically have lower premiums making them more affordable when household budgets are stretched. New business profits from protection products have increased 17 per cent over the first half 2008 and have made a material contribution to Prudential Asia's overall increase in new business profits margins from 45 per cent for first half 2008 to 50 per cent for the first half this year, primarily driven by product mix and pricing.

As a result of the financial crisis we have experienced an increase in the number of unit-linked policies where customers are opting to take a 'premium holiday', especially in Korea where this affected higher premium cases and to a lesser extent in Hong Kong and Singapore. Although 'premium holiday' customers suspend premium payments, their policies do stay in force so long as they have sufficient value attached to them to cover the costs of the insurance cover. Customers do have the option to start paying premiums again at a later date, however, for prudent EEV accounting purposes, we treat these policies as having stopped premiums. During first half 2009 we tightened our persistency assumptions, which included premium persistency, with a £60 million charge to embedded value and also booked £47 million of negative persistency experience variances. In the context of the total post tax shareholder embedded value of £5.2 billion, these adjustments remain relatively small (at two per cent of the embedded value of Asia at year end 2008).

A very significant development in the first half was the transfer of the Taiwan agency force and the related back book to China Life. As a result of that transaction, which was announced on 20 February 2009 and received regulatory approval on 19 June 2009, Prudential's Insurance Groups Directive (IGD) capital surplus increased by approximately £800 million. Prudential is still active in the Taiwan life market through its non agency distribution principally through two strategic partnerships with Standard Chartered Bank (SCB) and E.Sun Bank. In addition, as announced on 20 February we have invested £45 million in a 9.99 per cent stake in China Life.

Asia	AER[6] Half year 2009 £m	AER[6] Half year 2008 £m	AER[6] Change %	CER[6] Half year 2008 £m	CER[6] Change %
APE sales	553	648	(15)	752	(26)
NBP[1]	277	289	(4)	343	(19)
NBP margin (% APE)	50%	45%		45%	
NBP margin (% PVNBP)	10.2%	8.4%		8.4%	
Total EEV basis operating profit*[1]	401	460	(13)	554	(28)
Total IFRS operating profit*[1]	212	75	183	92	130

* Operating profit from long-term operations excluding asset management operations, development costs, Asia regional head office expenses and the sold Taiwan agency business.

Notes
See page 8.

Financial performance

New business profits of £277 million are four per cent lower than the same period last year with lower new business volumes being offset by an increase in average margins from 45 per cent to 50 per cent. In line with the Group's strategy, a strict focus was maintained on value creation by continuing to focus on profitable new business alongside capital conservation and cash generation. The main drivers of the increase in margins were higher proportion of protection and regular premium business. For example in Hong Kong the proportion of protection business in the APE increased from 12 per cent to 21 per cent and consequently average margins increased from 66 per cent to 76 per cent. In total, seven operations reported higher new business profit margins and for those that did not the main driver was changes in the distribution mix e.g. higher proportions of bank business in China.

Operating EEV profits of £401 million were 13 per cent lower than last year driven by operating assumption changes and adverse experience variances. Operating assumption changes of net £64 million negative were principally driven by the prudent provisioning for policies going on 'premium holiday' in Korea (£23 million) and Hong Kong (£14 million).

Experience variances and other items for half year 2009 were a charge of £(60) million primarily comprised of £(47) million for negative persistency experience mainly arising in Korea and Singapore due to higher than expected 'premium holidays' and expense variances.

IFRS profits, at £212 million increased by 183 per cent compared to the first half of 2008. This includes a one-off exceptional profit of £63 million from the release of regulatory reserves in Malaysia following the introduction of a Risk Based Capital reserving, but nevertheless is a clear demonstration of the business's long-standing commitment to profitable products and the increasing scale of the back book. Insurance margins remain the most significant driver of the IFRS profits.

For the first half 2009, Asia continued to be a net contributor of capital to the Group with a net remittance of £21 million which compares favourably to the net £11 million remitted in the first half of last year. The IRR remains in excess of 20 per cent and the payback period averages four years.

Looking at developments in each market in more detail:

In China, new business APE for the first half 2009 from our joint venture CITIC Prudential Life was £21 million, up 11 per cent compared to the first half of 2008. The agency channel has been particularly affected by the economic climate and in general recruiting and retaining good quality agents remains a challenge. However, bank distribution was encouraging with growth of 77 per cent over last year meaning this channel generated 44 per cent of the new business.

Sentiment towards single premium business via the bank channel in Hong Kong remains negative due to the lingering impact of the Lehman Brothers mini bond issue. Prudential and SCB are working together on their sales management model to increase focus on regular premium business. Prudential's total APE of £95 million for the first half this year was 16 per cent lower than last year, but encouragingly the second quarter this year was seven per cent up on the first quarter indicating an inflexion point as agency activity has picked up.

ICICI-Prudential Life in India has seen some erosion of market share this year. Prudential's share of new business APE at £76 million is 40 per cent lower than last year reflecting a particularly challenging market and our stated policy of concentrating on value over volume. Given the long-term potential of this market and the significance attached to the quality of our brand and service, we are not prepared to jeopardise this for short-term market share. Sales bounced back in June and we have been able to maintain our position as the largest private player over the first half of 2009, while continuing to focus on profitable business.

Our business in Indonesia has grown very rapidly over the last few years. At £83 million, new business APE is only six per cent lower than the first half of 2008 in spite of challenging market conditions in the first half of 2009. This growth has been driven by a rapid expansion in our agency force and our team continues to focus on finding ways to manage more effectively in a market downturn. Momentum is now gathering in the business again and the second quarter this year was up 21 per cent on the first quarter.

The market in Korea continues to be particularly challenging with activity tending to be driven by 'hot' products in an increasingly 'open architecture' environment. Currently guaranteed or interest rate sensitive products with low or negative profitability are preferred over our core Variable Unit Linked (VUL) offering, particularly through the bank channels. New business APE of £66 million for the first half is down 46 per cent over the same period last year, with the bank channel down 89 per cent. Our proprietary agency channel has been targeted by competitors as they look to move into the more professional financial adviser space. A new marketing campaign 'Magic Number' backed up by new whole life protection products is scheduled for the second half.

Having lagged Prudential's other Asian operations in terms of new business growth during 2006 and 2007, following the re-engineering of the agency model in early 2008 Malaysia is now delivering very strong results, with new business APE of £52 million up 33 per cent over the first half last year. Momentum is also encouraging with the second quarter of 2009 up 21 per cent on the first quarter.

Singapore recorded APE of £52 million which is 20 per cent lower than the first half of 2008. Singapore had a very strong first half in 2008 driven by exceptional volumes of CPF business ahead of a regulatory change but even allowing for this, the market has been affected by the downturn. We have successfully re-entered the single premium market in Singapore and the APE for the second quarter of £30 million was up 36 per cent on the first quarter and was the highest since the first quarter 2008, when APE was £38 million.

Non agency business in Taiwan for the first half 2009 of £51 million is more than double the £18 million recorded for the first half of 2008. This reflects the ongoing success of our relationships with SCB and E.Sun Bank. Although this business has low profit margins, work is now underway to improve the product mix.

The scale of Prudential's life business in Japan remains small and this business is being managed tightly to minimise expense overruns and capital strain. Vietnam has seen a good turnaround in agency activity and combined with the other smaller operations in Thailand and the Philippines, APE is down only seven per cent on the first half of 2008 and the second quarter of 2009 was up 15 per cent on the first quarter this year.

United States

The United States is the world's largest retirement savings market. Each year as more of the 78 million baby boomers[1] reach retirement age, additional amounts of retirement assets will shift from asset accumulation to income distribution. There are already $2 trillion of assets generating retirement income in the US – and this amount is forecast to rise to some $7.3 trillion by 2029.[2]

During the first half of 2009, the US financial services industry continued to face many challenges: the S&P 500 index fell to a 12-year low in March before rebounding to post a small year-to-date gain by the end of June; the US Federal Reserve kept its interest rate target at an historic low; and rating agencies downgraded the financial strength ratings of most of the largest US insurance companies. However, conditions in equity and credit markets improved in the second quarter. As a result, many financial services businesses took advantage of the opportunity to issue new debt and/or equity in an effort to rebuild their capital base.

Further uncertainty arose in the market, as several companies scaled back their product offerings due to capital constraints which, combined with multiple financial strength downgrades, caused consumers to question the long-term financial stability of product providers. At the same time, tightening credit spreads and a second-quarter rally in equity markets created more favourable market conditions for the sale of variable annuities. These developments in the annuity market provided a competitive advantage to companies with strong financial strength ratings and a relatively consistent product set.

Financial performance

Jackson delivered total APE sales of £392 million in the first half of 2009. By contrast to last year, all the sales were retail sales as a result of the Group's focus on capital conservation. The performance in retail sales was very strong, with the highest first half in terms of APE at CER in the company's history, as we clearly benefited from the consumer flight to quality during the period. This achievement continues to demonstrate the resilience of our business model and the importance of diversification within our product portfolio.

In light of continued volatility in US equity markets, customers are increasingly seeking to mitigate risk through the purchase of fixed annuities, fixed index annuities and variable annuities with guaranteed living benefits. Jackson has benefited from this trend across all of our annuity product lines.

Variable annuity APE sales of £252 million through June 2009 were up 40 per cent from the same period of 2008 at AER, reflecting the second-quarter equity market rally, the relative consistency of our product offering and disruptions among some of the top VA sellers in the US market. In the first quarter of 2009, we ranked 8th in new variable annuity sales in the US with a market share of 5.0 per cent, up from 12th and a market share of 4.4 per cent in the first quarter of 2008.[3]

Fixed annuity APE sales of £70 million were up nine per cent over the prior year on an AER basis, but were lower on a local currency basis as we balanced new business opportunities with our goals of capital and cash conservation. We ranked ninth in sales of traditional deferred fixed annuities during the first quarter of 2009, with a market share of 2.7 per cent, compared to ninth and a market share of 3.3 per cent in the first quarter of 2008.[4]

Fixed index annuity (FIA) APE sales of £58 million in the first half of 2009 were up 190 per cent over the first half of 2008 at AER. Increased industry FIA sales have been driven by higher customer demand for products with guaranteed rates of return, which also offer additional upside potential linked to stock market index performance. Additionally, our FIA sales have benefited from the company's strong financial strength ratings and further disruptions among some of the top FIA sellers. We ranked sixth in sales of fixed index annuities during the first quarter of 2009, with a market share of 5.0 per cent, up from 10th and a market share of 3.4 per cent in the first quarter of 2008.[5]

Retail annuity net flows increased by 63 per cent at AER (24 per cent higher at CER), reflecting the impacts of record sales and continued low levels of surrender activity.

As indicated above, there were no institutional sales during the first half of 2009, as we focused on managing new business strain and capital consumption.

Notes
1 Source: US Census Bureau
2 Source: Tiburon Strategic Advisers, LLC
3 Morningstar, Inc.
4 LIMRA
5 The Advantage Group

United States	AER[6]			CER[6]	
	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
APE sales	392	356	10	472	(17)
NBP	292	137	113	181	61
NBP margin (% APE)	74%	38%		38%	
NBP margin (% PVNBP)	7.5%	3.9%		3.9%	
Total EEV basis operating profit*	501	354	42	468	7
Total IFRS operating profit*	217	232	(6)	307	(29)

* Based on longer-term investment returns excludes broker-dealer, fund management and Curian.

Note
See page 8.

EEV basis new business profits of £292 million were more than double the first half of 2008 at AER (61 per cent higher at CER), reflecting a 10 per cent increase in APE sales and significantly higher new business margins. Total new business margin was 74 per cent, compared to 38 per cent achieved in the first half of 2008.

The variable annuity new business margin increased from 49 per cent during the first half of 2008 to 71 per cent in the same period of 2009, as a result of changes to policyholder behaviour and spread assumptions, coupled with changes in the level of benefits offered by the VA products.

The fixed index annuity new business margin increased from 26 per cent in the first half of 2008 to 85 per cent in the first half of 2009 due to increased spread assumptions. The fixed annuity new business margin increased significantly from 24 per cent to 77 per cent. For both products, the spread assumptions increased due to the exceptional combined benefit of high investment yields with a net annualised yield on new assets of seven per cent during the first half of 2009 and of lower crediting rates as Jackson sought to preserve capital. Average fixed annuity crediting rates in the first half of 2009 were 3.6 per cent compared to a market average of 4.6 per cent.

These revised assumptions include a provision that crediting rates and spreads will normalise in the future. Thus, the assumption for new business spreads for fixed annuities and the proportion of variable annuity business invested in the general account is set at the higher new level for the first five years before reducing over the following ten years. As before, the valuation of new business takes into account an assumed associated risk of increased lapse under certain interest rate scenarios.

The aggregate IRR on new business rose comfortably above 20 per cent from 18 per cent in 2008 due primarily to the increased spread assumptions noted above. The 2009 IRR is consistent with a payback period of two years.

Total EEV basis operating profit for the long-term business in the first half of 2009 was £501 million, compared to £354 million in the first half of 2008 at AER (£468 million at CER). In-force EEV profits of £209 million for the first half of 2009 were four per cent below the first half 2008 profit of £217 million at AER (27 per cent below profit of £287 million at CER). Experience variances and other items were £44 million higher in the first half of 2009 at AER, due primarily to favourable expense, mortality and persistency variances that were only partially offset by a lower spread variance.

In the first half of 2009, Jackson invested £168 million of free surplus to write £392 million of new business. This equated on average to £43 million per £100 million of APE sales (2008: £44 million). The reduction in absolute capital consumption year-on-year was caused predominantly by the differing business mix in the first half of 2009 where we have written a higher proportion of variable annuity business and lower amounts of institutional business while maintaining a very disciplined approach to fixed and fixed index annuity pricing.

IFRS operating profit for the long-term business was £217 million in the first half of 2009, down six per cent from £232 million in the first half of 2008 at AER (£90 million lower at CER). This decline was primarily due to lower separate account fee income and higher hedging costs. Higher hedging costs were primarily a result of the volatile nature of market movements during the first half of 2009 (a 26 per cent decline followed by a 38 per cent rally off the market lows) relative to the timing of changes in our hedge position during the period. As a leading provider of variable annuities we have a well-developed understanding of the risks associated with the guarantees embedded in our products. To protect the shareholder against the volatility induced by these embedded options we use a comprehensive hedging programme. Whilst the principal objective of this programme is one of risk management, over the eighteen month period to 30 June 2009 IFRS operating profits of £60 million have been generated, comprising £611 million of derivative gains and fee income less claims offset by £551 million in respect of increased guarantee values and DAC.

At 30 June 2009, we had £15 billion in separate account assets. Separate account assets were an average of £1 billion lower than during the same period of 2008 at AER (£5 billion lower at CER), reflecting the impact of the market decline during the second half of 2008. This was more than offset by exchange rate movements during the first half of 2009 and, as a result, VA fee income increased to £204 million from £190 million during the first half of 2008 at AER (decreased from £252 million at CER).

For the first half of 2009, our bond default losses totalled less than £1 million. As part of our active management of the book, we incurred net losses on the sale of impaired bonds of £42 million. Additional write downs were £324 million, including £80 million on corporate bonds and £239 million on RMBS, of which £123 million were prime, £98 million Alt-A and £18 million sub-prime.

Net unrealised losses in the balance sheet reduced from £2.9 billion at 31 December 2008 to £1.8 billion at 30 June 2009. As mentioned above, this reduction reflects the benefits of some normalisation in the credit markets with credit spreads tightening. Also, with markets for structured securities reverting to being more active in the period to 30 June 2009, nearly all the structured securities which had been valued at 31 December 2008 using internal valuation models due to inactive markets, have now been valued based on external quotations.

United Kingdom

Prudential UK continues to focus on realising value from the opportunities created by rapid growth in the need for retirement solutions. We compete in selected areas of the UK's pre- and post-retirement markets where we believe that we can generate attractive returns. This strategy saw us deliver a strong relative performance in the first half of 2009. In line with the Group's strategy, we maintained a strict focus on value creation, continuing to concentrate on balancing profitable new business with capital conservation and cash generation.

We remain a market leader in the UK, in both individual annuities and with-profits, as well as parts of the corporate pensions market. The capital and equity markets remained difficult in the first half of 2009 and Prudential UK benefited from consumers increasingly seeking greater certainty and security through trusted and financially strong brands. The business has a unique combination of competitive advantages including our longevity experience, multi-asset investment capabilities, strong brand and financial strength. These put us in a strong position to generate attractive returns across our Retail and Wholesale businesses.

Financial performance

Total APE sales for the first half of 2009 of £376 million were 14 per cent down on 2008, with Retail sales of £374 million down eight per cent. This resulted in a reduction in New Business Profit of five per cent to £122 million but with the underlying new business margin increasing to 32 per cent (2008: 29 per cent). This was a strong relative performance in extremely difficult and volatile market conditions and was entirely consistent with Prudential UK's continuing focus on balancing profitable new business with capital conservation and cash generation.

This disciplined approach led to lower sales of individual annuities than in the equivalent period of 2008. The deterioration in market conditions also impacted sales of some other product lines such as offshore bonds. These reductions were partially offset by strong growth in PruFund sales as consumers increasingly looked for a more cautious investment approach and to protect themselves from market downturns through the product's five-year capital back guarantee.

We write with-profits annuity, with-profits bond and with-profits corporate pensions business in the life fund, with other products backed by shareholder capital. The weighted average post-tax IRR on the shareholder capital allocated to new business growth in Prudential UK was in excess of 15 per cent, reflecting the lower capital usage of annuity business in the first half of 2009.

We have a strong individual annuity business, built on a robust profit flow from our internal vestings pipeline from maturing individual and corporate pension policies. The strong internal vestings pipeline is supplemented by strategic partnerships with third parties where we are the recommended annuity provider for customers vesting their pensions at retirement.

During the first half of 2009, we actively managed our sales volumes to reduce capital consumption. This resulted in very strong margins but overall individual annuity new business sales fell by 17 per cent to APE £114 million. Part of this reduction was due to consumers delaying taking out an annuity as well as lower pension pots available for annuitisation as a result of weak investment returns. Internal vestings continued to perform well with sales up one per cent to £73 million.

We have taken steps to build scale within a number of other product areas. In the second half of 2008, we made our highly successful multi-asset, smoothed investment plan (PruFund) available as a fund option, enabling consumers to invest in a range of bonds, both onshore and offshore, as well as individual pensions and income drawdown. We also launched the new PruSelect range of unit-linked funds, more than doubling the number of available funds.

Prudential was early to embrace 'factory-gate pricing'. As a result, we are well placed to compete in the post 'Retail Distribution Review' market, and to avoid the excessive strain caused by initial commission in the savings market.

In the first half of 2009 with-profits bond sales of £71 million were up 48 per cent on the same period in 2008. This strong sales growth reflects the attractiveness of our with-profits offering including in particular PruFund in which over £1.5 billion has been invested since it was launched. In July 2009, we extended the PruFund range of investments with the launch of the PruFund Cautious series which will sit alongside the PruFund Growth series as a fund link within Prudential's Flexible Investment Plan, an on-shore bond wrapper.

	AER[6]			CER[6]	
United Kingdom	**Half year 2009** £m	**Half year 2008** £m	**Change** %	**Half year 2008** £m	**Change** %
APE sales	376	438	(14)	438	(14)
NBP	122	129	(5)	129	(5)
NBP margin (% APE)	32%	29%		29%	
NBP margin (% PVNBP)	4.0%	3.5%		3.5%	
Total EEV basis operating profit*	433	504	(14)	504	(14)
Total IFRS operating profit*	330	286	15	286	15

* Based on longer-term investment returns.

Note
See page 8.

Individual pensions sales of £24 million were 50 per cent higher than the first half of 2008. Sales of the Flexible Retirement Plan, our factory-gate priced individual pension product, have continued to grow with sales in 2009 of APE £10 million up 131 per cent. This strong growth was due to the overall strong proposition with the PruFund and with-profits guarantees, together with a service which follows up fund transfers on behalf of advisers. The Flexible Retirement Plan is well suited to customers looking to consolidate their pension funds.

We entered the equity release market three years ago, and saw our market share grow to 23 per cent by the end of 2008. The demographic opportunities within this market are compelling, however while house price volatility continues, we have maintained our strict pricing discipline and this action has resulted in the fall in sales volumes in the first half of 2009. We will maintain this conservative stance until such time as market conditions improve.

The PruHealth joint venture uses the Prudential brand and Discovery's expertise to build branded distribution in Health and Protection. Since its launch, PruHealth has developed its product and established itself rapidly in the marketplace. It now has 210,000 lives insured, an increase of 22 per cent over the last year. Gross written premiums for the first half were £50 million, up 10 per cent on the same period last year. The focus for PruHealth is to increase sales volumes, grow the in-force book and manage its claims ratio.

PruProtect, also a joint venture with Discovery, relaunched its product range in November 2008 together with an improved distribution model, and this resulted in sales for the first six months of £6 million, compared to £1 million in the first half of 2008.

We are a leader in the UK corporate pensions market serving over 20 per cent of FTSE 350 companies as well as being one of the largest providers of pension schemes to the UK public sector. We now administer corporate pensions for over 600,000 members. For the first half of 2009 corporate pension sales of £115 million were nine per cent lower than 2008 and growth into existing schemes has remained healthy.

We have maintained our strict focus on value in the bulk annuity and back-book markets. In the first half of 2009, Prudential UK did not write any new business in this market reflecting our disciplined approach of only participating in transactions that meet our strict return on capital requirements.

EEV new business profits decreased by five per cent to £122 million in the first half of 2009 from £129 million in 2008, reflecting lower sales volumes which were partially offset by an increase in new business margin to 32 per cent from 29 per cent.

EEV basis total operating profit based on longer-term investment returns of £433 million (before restructuring costs of £9 million and including £27 million of general insurance commission), was down 14 per cent compared with the first half of 2008. This was mainly the result of the in-force operating profit (at £284 million) being down 21 per cent on the first half of 2008. The major component of this decline in in-force operating profit was the reduction compared with last year by £59 million of the unwind of discount to the value of in-force business to £291 million. This was mainly due to a lower opening embedded value caused by the negative investment returns in 2008.

We continue to manage actively the retention of the in-force book. During the first half of 2009, our experience at an aggregate level has been in line with our long-term assumptions.

The average free surplus undiscounted payback period for business written in the first half of 2009 was five years.

Total IFRS operating profit increased by 15 per cent in 2009 to £330 million. The increase of 11 per cent achieved for the long-term business reflects a 39 per cent growth from the shareholder-backed annuity business, the non-repetition of one-off 2008 losses, partially offset by a 26 per cent reduction in profits attributable to the with-profits business of £147 million. This reflected the impact of bonus rate reductions in the February 2009 bonus declaration made in response to recent volatile investment performance. Non-long-term business IFRS profit reflected a profit of £27 million from general insurance commission.

Financial strength of the UK long-term fund

On a realistic valuation basis, with liabilities recorded on a 'market consistent' basis, the free assets were valued at approximately £5 billion at 30 June 2009, before a deduction for the risk capital margin. The value of the shareholder's interest in future transfers from the UK with-profits fund is estimated at £1.6 billion. The financial strength of PAC is rated AA+ (negative outlook) by Standard & Poor's, Aa2 (negative outlook) by Moody's and AA+ (negative outlook) by Fitch Ratings.

Reflecting continued difficult conditions in financial markets, the with-profits sub-fund achieved a negative one per cent investment return in the first half of the year.

Inherited estate of Prudential Assurance

The assets of the main with-profits fund within the long-term insurance fund of PAC comprise the amounts that it expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the with-profits fund is equal to the policyholders' accumulated asset shares plus any additional payments that may be required by way of smoothing or to meet guarantees. The balance of the assets of the with-profits fund is called the 'inherited estate' and has accumulated over many years from various sources.

The inherited estate represents the major part of the working capital of PAC's long-term insurance fund. This enables PAC to support with-profits business by providing the benefits associated with smoothing and guarantees, by providing investment flexibility for the fund's assets, by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies. The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

Business unit review
Asset management
M&G

Global

The Group's asset management businesses provide value to the insurance businesses within the Group by delivering sustained superior performance. They are also important profit generators in their own right, having low capital requirements and generating significant cash flow for the Group.

Our asset management businesses are well placed to capitalise on their leading market positions and strong track records in investment performance to deliver net flows and profit growth as well as strategically diversifying the Group's investment propositions in retail financial services markets that are increasingly favouring greater product transparency, greater cross-border opportunities and more open-architecture investment platforms. Wholesale profit streams are also growing.

The Group's asset management businesses operate different models and under different brands tailored to their markets and strengths. However they continue to work together by managing money for each other with clear regional specialism, distributing each others' products and sharing knowledge and expertise, such as credit research.

Each business and its performance in the first half of 2009 is summarised below.

M&G

M&G is our UK and European fund manager, responsible for £149 billion of investments as at 30 June 2009 on behalf of both internal and external clients. M&G is an investment-led business, which aims to deliver superior investment performance and maximise risk-adjusted returns in a variety of macro-economic environments. Through M&G we seek to add value to our Group by generating attractive returns on internal funds as well as growing profits from the management of third-party assets.

External funds now represent 37 per cent of M&G's total funds under management (FUM). Our overall strategy is to focus first and foremost on investment performance, by recruiting, developing and retaining market-leading investment talent, and by creating the environment and infrastructure this talent needs to perform to its full potential.

In the retail market, our strategy is to maximise the value of our centralised investment function through a multi-channel, multi-geography distribution approach. Key themes in recent years have included growing the proportion of business sourced from intermediated channels and the increased sale of cross-border products. Our diverse product portfolio has proved its worth during the recent turmoil in financial markets as, for example, bond funds have become more popular than equity based products.

Our institutional strategy centres on leveraging capabilities developed primarily for internal funds into higher-margin external business opportunities. In recent years this has allowed us to operate at the forefront of a number of specialist fixed income strategies, including leveraged finance and infrastructure investment. The recent upheaval in capital markets has provided interesting opportunities in fixed income which we have been able to exploit by drawing on our core research and investment expertise.

M&G	AER[6]			CER[6]	
	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Net investment flows	**8,625**	2,437	254	2,437	254
Revenue	**195**	235	(17)	235	(17)
Other income	**7**	12	(42)	12	(42)
Staff Costs	**(85)**	(101)	16	(101)	16
Other Costs	**(42)**	(42)	–	(42)	–
Underlying profit before performance-related fees	**75**	104	(28)	104	(28)
Performance-related fees	**–**	9	(100)	9	(100)
Operating profit from asset management operations	**75**	113	(34)	113	(34)
Operating profit from Prudential Capital	**27**	33	(18)	33	(18)
Total IFRS operating profit	**102**	146	(30)	146	(30)
FUM	**149bn**	159bn	(6)	159bn	(6)

Note
See page 8.

Financial performance

Net fund inflows during the first half of 2009 reached an unprecedented level of £8.6 billion, more than treble the £2.4 billion taken during the same period last year. We believe that this success is primarily the result of a relentless focus on investment performance. Over the three years to the end of June 2009, 69 per cent of M&G retail funds under management were invested in funds which delivered top quartile performance, whilst over the same period, 71 per cent of fixed income segregated mandates performed at or above benchmark.

In the retail market, net inflows were £4.1 billion (£0.9 billion in 2008), breaking the previous record for full year inflows of £3.1 billion in 2006. A very high proportion of the money is continuing to go into our market-leading range of top performing fixed income funds. During the six months, retail investors placed more than £3 billion in our bond funds as they sought to take advantage of highly attractive opportunities in the corporate bond markets. Key equity funds, such as M&G Recovery and M&G Global Basics, also continued to attract net inflows.

Our institutional business recorded net inflows of £4.5 billion, compared with £1.6 billion for the same period in 2008. A single fixed income mandate valued at £4.0 billion accounted for the majority of the inflows.

In the face of a very challenging economic environment, M&G recorded operating profits of £75 million in the first half of 2009, down from £113 million in the same period in 2008, a decline of 34 per cent. Our underlying profit, which excludes volatile performance related fees (PRFs) and carried interest earned on private equity investments, remained at £75 million in the first half of 2009, down from £104 million in the same period in 2008, a decline of 28 per cent.

The year-on-year fall in profits reflects a number of factors, including significantly lower equity market levels compared with this time last year, lower investment income and the depressed conditions of the commercial property market. We continue to focus on effective cost management to limit the impact of lower revenues on bottom-line results.

The impact of strong net inflows coupled with positive market movements has seen our overall external FUM increase to £55.9 billion, up from £47.0 billion as at 31 December 2008. Our total FUM at 30 June 2009 were £149 billion, six per cent higher than at the start of the year.

M&G continues to provide capital efficient profits and cash generation for the Prudential Group, as well as strong investment returns on our long-term business funds. Cash remittances of £44.1 million to date in 2009 to Group provided strong support for the Group's corporate objectives.

Relative performance

Relative to our competitors, M&G has had an exceptionally strong first half in 2009. In the UK, our retail assets under management have grown 28 per cent to the end of June compared with eight per cent growth for the market as a whole, according to the Investment Management Association (IMA).

Prudential Capital

Prudential Capital manages Prudential's balance sheet for profit by leveraging Prudential's market position. This business has three strategic objectives: to operate a first-class wholesale and capital markets interface; to realise profitable proprietary opportunities within a tightly-controlled risk framework; and to provide professional treasury services to Prudential. Prudential Capital generates revenue by providing bridging finance, managing investments and operating a securities lending and cash management business for our Group and its clients.

This business has continued to grow in terms of investment, infrastructure and personnel in a controlled way, while maintaining the dynamism and flexibility necessary to identify and realise opportunities for profit. Prudential Capital is committed to working more closely with other business units across the Group to exploit opportunities and improve value creation for Prudential as a whole. At Prudential Capital, we are also taking a more holistic view on hedging strategy, liquidity and capital management for the Group.

Prudential Capital has a diversified earnings base derived from bridge lending, investments and wholesale markets. Despite the continued difficult market conditions we delivered a good financial result from this business in the first half of 2009, generating half year operating profits of £27.3 million. A cash remittance was made to the holding company of £42.0 million.

Business unit review
Asset management
Asia

Volatility in the equity market conditions persisted in the first half of 2009. In the first quarter, the MSCI Asia (ex-Japan) index rose by a mere one per cent. However, by the end of second quarter, the index had achieved year-to-date increase of 19 per cent. Amid this volatility, growth observed in the Asian mutual funds market was mainly driven by money market funds inflows in markets such as India, Korea and Taiwan as investors risk appetite remained low.

Against this backdrop, our Funds Under Management (FUM) for the first half of 2009, at £35.8 billion, were three per cent higher than year-end 2008 (excluding the FUM related to the sold Taiwan agency business). The overall FUM level was comprised of £4.6 billion assets from the Group, £14.8 billion from Prudential's Asian life funds and £16.4 billion from external clients.

Net flows from external clients for the first half of 2009 were only 11 per cent lower than the same period in 2008 at £1.5 billion, out of which £1.3 billion was contributed by a stronger second quarter. Net flows from external clients were wholly contributed by money market funds and together with positive market movement of £2.5 billion, these resulted in retail funds under management of £16.4 billion. External client's funds under management for the first half of 2009 were four per cent higher when compared to the same period in 2008 and eight per cent higher when compared to beginning of 2009.

IFRS profit of £21 million to 30 June 2009 was boosted by improved market conditions in the second quarter. However, this was mitigated by lower average FUM, shift in asset mix, a one-off loss in India and restructuring costs, resulting in 28 per cent decrease when compared to the first half of 2008. Excluding the one-off loss in India and restructuring costs, IFRS profit for the first half of 2009 was £27 million, seven per cent down from 2008.

Despite the difficult market environment, we remained focused on anticipating and meeting the investment needs of our clients. In the 10 markets in which we have a retail presence, we maintained our strong market positioning as the only foreign fund manager with more top-five onshore mutual fund market positions relative to our regional competitors.

In addition, we continued investing in the business to ensure we are well-positioned to capitalise on growth opportunities.

Our investments in building up our asset management capabilities yielded promising results. This is evident from our strong year-to-date investment performance where 64 per cent of our funds outperformed their peers or benchmarks. In China, two out of five 'CITIC-Prudential' products were awarded the top class fund recognition by the China Galaxy Securities (a Chinese fund rating agency), while its third product, the Blue Chip Equity Fund was ranked first out of 196 equity funds by Morning Star.

On the products front, we have extended our range to include Latin American Equity products and are expanding our private equity investment management through the newly established PPEM entity. Our well-timed and innovative product launches also met with success. 'ICICI-Prudential' introduced the Target Returns Fund in April 2009, investing mainly in large caps and providing investors the option to switch out investments. The one-month IPO raised £105 million (INR8 billion). In China, CITIC-Prudential's Pure Bond Fund also successfully raised £163 million (RMB 1.6 billion) at the close of its IPO in March.

We remain committed to our strategy of building a multi-channel network. PCA Japan established new relationships with Nikko Cordial Securities, a mega distributor and Resona Bank, the fourth largest bank in Japan. Dubai-based PAMD also successfully secured a new distribution agreement with the largest bank in UAE, Emirates National Bank of Dubai. Similarly, PCA Korea and PCA Taiwan concluded agreements with six third-party Life insurers for their unit-linked products to feed into our funds. The focus on insurance companies' funds will help us to build a more stable and profitable funds under management base.

	AER[6]			CER[6]	
Asia	**Half year 2009** £m	**Half year 2008** £m	**Change** %	**Half year 2008** £m	**Change** %
Net investment flows	**1,456**	1,642	(11)	2,023	(28)
Total IFRS operating profit	**21**	29	(28)	36	(42)

Note
See page 8.

US asset management

PPM America (PPMA) manages assets for Prudential's US, UK and Asian affiliates. PPMA also provides other affiliated and unaffiliated institutional clients with investment services including collateralised debt obligations (CDOs), private equity funds, institutional accounts, and mutual funds. At PPMA, our strategy is focused on managing existing assets effectively, maximising the benefits gleaned from synergies with our international asset management affiliates, and leveraging investment management capabilities across the Prudential Group. PPMA also pursues third-party mandates on an opportunistic basis.

Financial performance

IFRS operating profit in the first half of 2009 was £3 million, higher than the £1 million in the same period of 2008, at both AER and CER.

At 30 June 2009, funds under management of £41 billion were as follows:

PPMA funds under management £ bn

	Half year US	Half year UK	Half year Asia	Half year Total
Insurance	26	10	0	36
Unitised	0	1	3	4
CDOs	1	0	0	1
Total	27	11	3	41

US broker-dealer

National Planning Holdings (NPH) is Jackson's affiliated independent broker-dealer network. The business is comprised of four broker-dealer firms, including INVEST Financial Corporation, Investment Centers of America, National Planning Corporation, and SII Investments.

We continue to grow NPH's business through strong recruiting efforts. By utilising our high-quality, state-of-the-art technology, we provide NPH's advisers with the tools they need to operate their practices more efficiently. At the same time, through its relationship with NPH, Jackson continues to benefit from an important retail distribution outlet, as well as receive valuable insights into the needs of financial advisers and their clients.

Financial performance

NPH generated revenues of £191 million during the first half of the year, an increase from £162 million in the same period of 2008 at AER, on gross product sales of £4.6 billion. Our network continues to experience profitable results, with IFRS operating profit through 30 June 2009 of £2 million, a 60 per cent decrease at AER from £5 million in the first half of 2008. We also increased the number of registered advisers in our network to approximately 3,535 at 30 June 2009.

Curian

Curian Capital, Jackson's registered investment adviser, provides innovative fee-based separately-managed accounts and investment products to advisers through a sophisticated technology platform. Curian expands Jackson's access to advisers while also providing a complement to Jackson's core annuity product lines.

Financial performance

At 30 June 2009, Curian had total assets under management of £1.6 billion, compared to £1.8 billion at the end of 2008 (£1.6 billion at CER) and £1.7 billion at 30 June 2008 (£2.1 billion at CER). We generated deposits of £270 million through June 2009, down 20 per cent from the same period in 2008. The decline in both deposits and assets under management at CER were mainly due to difficult conditions in the equity markets, with the S&P 500 index falling to a 12-year low in March. In the second quarter, Curian's performance rebounded along with the market, with deposits up 88 per cent at CER from the first quarter of 2009.

The IFRS basis loss of £3 million during the first half of 2009 (2008: nil at AER and CER) was driven by the decline in assets under management.

	AER[6]			CER[6]	
PPM America	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Total IFRS operating profit	3	1	200	1	200

	AER[6]			CER[6]	
US broker-dealer	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Revenue	191	162	18	214	(11)
Costs	(189)	(157)	20	(207)	(9)
Total IFRS operating profit	2	5	(60)	7	(71)

	AER[6]			CER[6]	
Curian	Half year 2009 £m	Half year 2008 £m	Change %	Half year 2008 £m	Change %
Gross investment flows	270	339	(20)	448	(40)
Revenue	14	13	8	17	(18)
Costs	(17)	(13)	(31)	(17)	–
Total IFRS operating profit/(loss)	(3)	0	–	0	–

Note
See page 8.