

Business unit review

Insurance operations

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 | | | CER ⁶ | |
|--|-------------------------|-------------------------|-------------|-------------------------|-------------|
| | Half year 2009 £m | Half year 2008 £m | Change % | Half year 2008 £m | 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.

Business unit review

Insurance operations

United States

The United States is the world's largest retirement savings market. Each year as more of the 78 million baby boomers¹ 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.

Business unit review

Insurance operations

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 | |
|-----------------------------------|----------------------|----------------------|-------------|----------------------|-------------|
| | Half year 2009 £m | Half year 2008 £m | Change % | Half year 2008 £m | Change % |
| United Kingdom | | | | | |
| 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.

| | AER ⁶ | | | CER ⁶ | |
|---|-------------------------|-------------------------|-------------|-------------------------|-------------|
| | Half year 2009 £m | Half year 2008 £m | Change % | Half year 2008 £m | Change % |
| M&G | | | | | |
| 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.

Asia

| | AER ⁶ | | | CER ⁶ | |
|-----------------------------|----------------------|----------------------|-------------|----------------------|-------------|
| | 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.

Business unit review

Asset management

United States

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.

PPM America

Total IFRS operating profit

| | AER ⁶ | | | CER ⁶ | |
|-----------------------------|-------------------------|-------------------------|-------------|-------------------------|-------------|
| | Half year 2009 £m | Half year 2008 £m | Change % | Half year 2008 £m | Change % |
| Total IFRS operating profit | 3 | 1 | 200 | 1 | 200 |

US broker-dealer

Revenue
Costs
Total IFRS operating profit

| | AER ⁶ | | | CER ⁶ | |
|-----------------------------|-------------------------|-------------------------|-------------|-------------------------|-------------|
| | 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) |

Curian

Gross investment flows
Revenue
Costs
Total IFRS operating profit/(loss)

| | AER ⁶ | | | CER ⁶ | |
|------------------------------------|-------------------------|-------------------------|-------------|-------------------------|-------------|
| | 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.