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

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.

Business review

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**

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

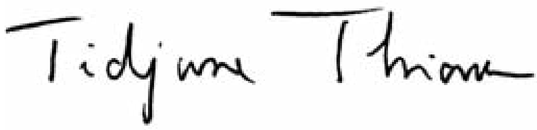
The Group currently operates three defined benefit schemes in the UK, of which by far the largest is the Prudential Staff Pension Scheme (PSPS) and two smaller schemes, Scottish Amicable (SAPS) and M&G.

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