

Group Chief Executive's review



Mark Tucker
Group Chief Executive

I am pleased to report that in the first half of the year Prudential has delivered a strong performance across the Group despite economic and financial conditions that remained challenging, and at the same time strengthened an already robust capital position.

We continue to focus on our retirement-led strategy in our chosen markets, maximising sales of our most profitable products with an emphasis on conserving capital, focusing investment onto the most value enhancing opportunities available and improving margins across the Group.

During the first six months of the year, we remained committed to strengthening our core capabilities through continued product innovation, targeted brand investment and recruiting the best talent. We also continue to invest cautiously for the future, strengthening our competitive position.

Management succession

Before providing an overview of our performance for the first half of the year, I would like to comment briefly on our management succession. Following the announcement on 19 March of my decision to leave Prudential at the end of September 2009, when Tidjane Thiam becomes Group Chief Executive, we have been working closely to ensure a smooth transition. I am delighted to be handing over to a successor as capable and committed as Tidjane, and to leave the Group with one of the strongest management teams in the industry.

In April we announced that Nicolaos ('Nic') Nicandrou will be joining the Group in October to succeed Tidjane as Chief Financial Officer. Nic joins us from Aviva, where he has worked in a number of senior finance roles, including Finance Director of Norwich Union Life. Nic's experience, technical expertise and leadership qualities make him an excellent successor to Tidjane as Chief Financial Officer.

In early July we announced the appointment of Rob Devey as Chief Executive, Prudential UK and Europe in succession to Nick Prettejohn who will be leaving the Group in September this year. Nick has made an outstanding contribution during his tenure, leading the development and implementation of a highly effective strategy that has dramatically improved the performance and profitability of the UK business.

Rob will join us from Lloyds Banking Group, where he has held senior roles in both insurance and retail banking, including Managing Director, Direct Channels UK Retail Banking. I am sure that Rob's track record of success will make him a strong leader of our UK business.

There's more:
to Prudential

more:heritage



more:momentum



The critical importance that we attach to risk and capital management was underlined in April 2009, when we announced the appointment of Thibaut Le Maire as Group Chief Risk Officer (CRO) with effect from July. Thibaut is a member of the Group Executive Committee (GEC). He currently reports directly to Tidjane and will continue to do so when Tidjane becomes Group Chief Executive. Thibaut joins Prudential from Société Générale where he was a Managing Director and Head of Insurance Europe in the Financial Institutions Group.

Group performance

Turning to our financial results, as I have already commented we have delivered a strong performance in an economic and financial environment that continues to be challenging.

International Financial Reporting Standards (IFRS) operating profit before tax from continuing operations after restructuring costs increased by six per cent over the first half of 2008 to £688 million. The increase was driven primarily by a strong underlying operating performance in Asia demonstrating our commitment to write profitable business, together with a one-off benefit from a regulatory change in Malaysia. UK operating profits also improved on the first half of 2008, with the total increase being offset by a reduction in the US operating profit, lower asset management profits and reduced investment income on central funds, all of which were influenced by external market factors.

Group operating profit before tax from continuing operations based on longer term investment returns, on the European Embedded Value (EEV) basis, was £1,246 million. This represents a decline of eight per cent on the same period in 2008. Our life businesses held their contribution at 2008 levels. However, market conditions held back the contribution from our asset management businesses and reduced income at Group level.

New business profit increased by 25 per cent to £691 million, while new business sales on an Annual Premium Equivalent (APE) basis decreased by eight per cent to £1,321 million. This demonstrates our continued focus on value over volume with more sales of products with higher Internal Rates of Return (IRRs) and shorter payback periods. This is particularly evident through the performance of our US business in the first half of 2009.

Our asset management businesses have continued to record exceptionally strong inflows, with M&G achieving record net inflows of £8.6 billion in the first half of 2009. In Asia, our asset management business recorded net inflows of £1.5 billion. Overall, operating profit in the Group's asset management operations fell by £56 million to £125 million, primarily reflecting the decline in equity markets compared with twelve months ago.

The holding company cash flow position remained healthy, in spite of the challenging environment. We are pleased to have succeeded in remaining cash flow positive, with an underlying cash flow of £22 million generated at the holding company level during the half year.

More importantly, we strengthened our already robust Group capital position. Using the regulatory measure of the Insurance Groups Directive (IGD), the Group's capital surplus was estimated at £2.5 billion at 30 June 2009 (before any allowance for the 2009 interim dividend), an increase of £1.0 billion over the year end, giving us an estimated solvency ratio of 237 per cent. In July 2009 the Group issued a bond of US\$750 million, and we estimate that this transaction will further boost our IGD capital surplus by £0.5 billion to £3.0 billion.

Our balance sheet also remains robust, with shareholders' funds at the half year on an EEV basis standing at £13.7 billion (2008 year end £15.0 billion).

Given the strong financial position of the Group, the Board has agreed an increase of five per cent in the interim dividend to 6.29 pence per share. The Board remains committed to a sustainable dividend policy, with the level of dividend determined after taking into account the Group's financial requirements, including opportunities to invest in the business at attractive returns. As previously stated, the Board believes that in the medium term a dividend cover of around two times is appropriate, based on post-tax IFRS operating profit from continuing operations.

more: transparency



more: strength



more: opportunity



Group Chief Executive's review

continued

Our strategy

Our strategy of capturing long-term growth opportunities in the pre- and post-retirement market remains unchanged. It is founded on being both highly international and very selective in the markets and products in which we compete. We maintain an internationally diverse portfolio of businesses, operating in countries that are at different stages of economic development, but which all present us with the opportunity to create a market-leading platform and sustainable long-term profitable growth.

Of course, none of our markets is unaffected by the recent turmoil in the global financial sector. Our decision to focus our investment and expansion primarily on the Asian region in recent years continues to be vindicated, with our IFRS operating profits from long-term business in Asia rising significantly during the half year. Going forward, Asia's increasing mass affluence and positive demographics will remain powerful drivers of profitable growth for the Group.

The US remains the world's largest retirement market, where Jackson is in a very strong position.

In the UK, as in the USA, the retirement and near-retirement population will represent the fastest growing and most profitable segment of the market over the next decade. Our aim is to continue to participate selectively to optimise overall Group returns on capital employed.

In each market, we benefit from an operating model that enables our businesses to stay close to their customers when formulating product and distribution strategies, while taking a consistent and disciplined Group-wide approach to managing risk, capital and cash.

We continue to tailor our franchise in our various businesses to match differing customer needs in our chosen markets worldwide. The recent difficult market conditions have underlined the value of this approach, with our brands visibly benefiting from a 'flight to quality'.

Product strategy

The need to fund retirement savings and provide for income in retirement will continue into the future, making our revenue streams highly resilient. In each of our businesses, we aim to offer a suite of products that delivers good value and meets the needs of our target customers, while also optimising our cash and capital consumption and limiting our exposure to the economic cycle.

Our product strategy in the first half of 2009 has continued to focus on generating cash by maximising the sales of our most profitable products. We have delivered against this plan, increasing our new business profit and margins compared with the first half of 2008, while reducing investment in new business.

The economic climate in Asia has remained challenging, with volatile equity markets and fears of rising unemployment. Regular premium and higher-margin protection business has remained resilient, while single premium business has decreased sharply. We adjusted our sales efforts and product mix accordingly during the first half and we believe we outperformed our competitors with satisfactory sales of good quality new business.

In the US, the continued volatility in the equity markets has seen customers seek to limit their risks by buying fixed annuities, fixed index annuities or variable annuities with guaranteed living benefits. Jackson has responded very well to these changes, and as a result has benefited across all its annuity product lines. Total APE sales rose by 10 per cent over the first half of 2008 on an Actual Exchange Rate (AER) basis to their highest ever level, although this was aided by the strong US dollar during the period. Jackson's first half 2009 retail sales at Constant Exchange Rate (CER) were also very strong, the highest in the company's history.

Prudential UK's continued focus on balancing new business with capital conservation and cash generation while maintaining margins, has driven a strong relative performance in difficult market conditions. Sales of with-profits bonds continued to grow, offset by lower sales of individual annuities, offshore bonds and corporate pensions. We also saw strong growth in PruFund sales, as consumers increasingly looked for a more cautious investment approach. Customers also responded positively to the launch of our new Income Choice Annuity, which allows them to choose an income between a defined maximum and minimum level, and re-set these levels every two years.

Despite the challenging market environment, our asset management businesses have continued to capitalise on their leading market positions and history of strong investment performance to deliver record net inflows.

M&G continued to benefit from a combination of superior investment performance, diversified business mix and well-established distribution capabilities. These attributes have helped M&G achieve an exceptionally strong first half, with net fund inflows surging to unprecedented levels – more than three times those in the same period in 2008 – at a time when many asset managers were continuing to suffer net redemptions.



The asset management business in Asia continued to be affected by market volatility, and remained focused on maintaining profitability across our internal Life client and third-party client segments.

Risk and capital management

We remain cautious on the economic outlook, and maintain our habitual prudent and proactive approach to risk and capital in the first half of 2009, focusing on building our capital base and strengthening our already robust IGD surplus.

A number of recent transactions demonstrate our commitment to increasing our capital strength. In February 2009 we announced the transfer of the assets and liabilities of our agency distribution business and agency force in Taiwan to China Life of Taiwan. On completion in June 2009, the transfer boosted our IGD capital surplus by approximately £0.8 billion.

Also, in February 2009 the regulator allowed us to recognise £0.3 billion of the shareholders' economic interest in the future transfers from the UK With-Profits Fund in our IGD capital surplus. Due to a tax change, this benefit was estimated to be worth £0.4 billion at the half year 2009. In addition, in May 2009 the Group completed a hybrid bond issue of £0.4 billion, strengthening further our IGD capital surplus. As a result of these actions, the Group's IGD capital surplus was estimated at £2.5 billion at 30 June 2009 (before any allowance for the 2009 interim dividend).

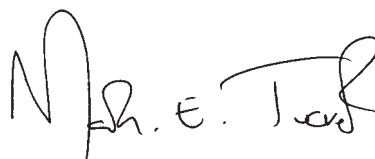
This was followed in July 2009 by a further transaction which saw the Group issue a bond of US\$750 million, raised primarily from Asian retail investors. This transaction was heavily over-subscribed, demonstrating our ability to use our good name recognition in Asia to access the recently reopened Asian retail market. We estimate this transaction will further boost our IGD capital surplus by £0.5 billion to £3.0 billion.

Outlook

We expect the business environment to remain difficult through the rest of 2009. However, the global economy will ultimately rebound.

Given this scenario, we shall maintain our defensive and prudent stance, focusing on balancing new business with cash generation, while making it our absolute priority to ensure that our balance sheet and capital position remain robust and that new business is written only on terms that increase shareholder value. Simultaneously, we will continue to invest for the upturn, strengthening our core capabilities – particularly distribution – to take advantage of any improvement in market conditions.

I end my last half year report as Group Chief Executive by restating my firm belief that Prudential's strategic and financial strength will enable the Group to continue to outperform, both through the current economic cycle and also in the years to come. I leave with an excellent management team in place and I am sure that under Tidjane's leadership the Group will go from strength to strength. The overall long-term prospects for the Group remain very positive.



Mark Tucker
Group Chief Executive

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