PRUDENTIAL

Long-term thinking

Prudential plc
2014 Half Year Financial Report

HK Stock Code: 2378

Profitable growth over the long term

Prudential has delivered a strong performance in the first six months of 2014 across the Group's key financial metrics of IFRS operating profit, new business profit and cash.

The broad-based and resilient financial performance we achieved in the first half of 2014 is evidence of the strength we derive from our diversification across geographies, channels and products; the quality of our strategy; and our focus on disciplined execution and delivery.

We remain confident in our ability to produce profitable growth over the long term and continue to create value for our customers and shareholders.

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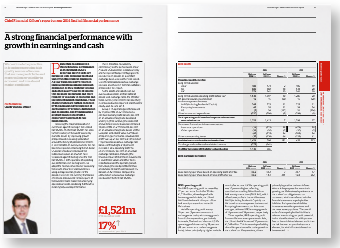

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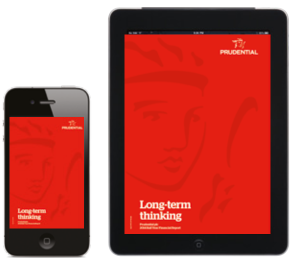


View our report online www.prudential.co.uk

Section 1

Group overview

1

Financial highlights

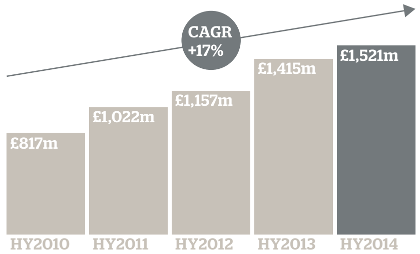
To create sustainable economic value for our shareholders we focus on delivering growth and cash while maintaining adequate capital.

Profit, cash and capital

What we measure and why | **Performance[1]** | **Commentary**

IFRS operating profit[2,3]

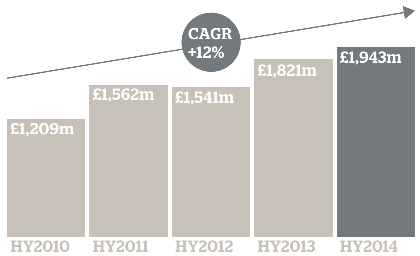
IFRS operating profit is our primary measure of profitability. This measure of profitability provides an underlying operating result based on longer-term investment returns and excludes non-operating items.



- Group IFRS operating profit in half year 2014 increased by 17 per cent on a constant exchange rate basis (7 per cent on an actual exchange rate basis), compared to half year 2013, reflecting strong growth in Asia and the US, which, on the same basis, were up 19 per cent and 28 per cent respectively.

EEV operating profit[2,4]

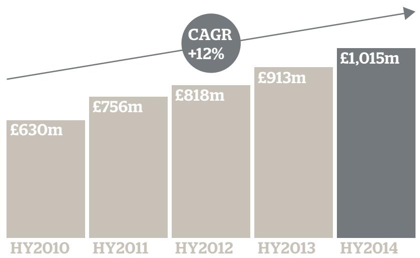
Embedded value reporting provides investors with a measure of the future profit streams of the Group's long-term businesses and includes profit from our asset management and other businesses. It is provided as additional information to our IFRS reporting. As with IFRS, EEV operating profit reflects the underlying results based on longer-term investment returns.



- Group EEV operating profit in half year 2014 increased by 18 per cent on a constant exchange rate basis (7 per cent on an actual exchange rate basis), compared to half year 2013, reflecting higher new business profits and an increased contribution from the in-force business.

EEV new business profit[4]

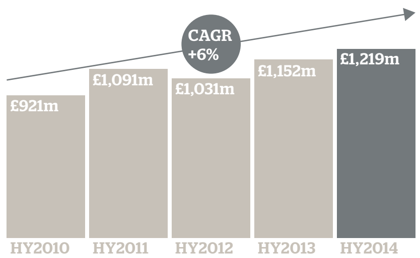
EEV new business profit represents a measure of the future profitability of all new business sold in the period. Life insurance products are, by their nature, long term and generate profit over a significant number of years. EEV new business profit reflects the value of future profit streams which are not fully captured in the period of sale under IFRS reporting.



- EEV new business profit in half year 2014 increased by 24 per cent on a constant exchange rate basis (11 per cent on an actual exchange rate basis), compared to half year 2013, driven by a combination of higher volumes and pricing and product actions to increase profitability.

Group free surplus generation[2,5]

Free surplus generation is used to measure the internal cash generation by our business units. For the insurance operations it represents amounts maturing from the in-force business during the period, less investment in new business and excludes other non-operating items. For asset management it equates to post-tax IFRS operating profit for the period.

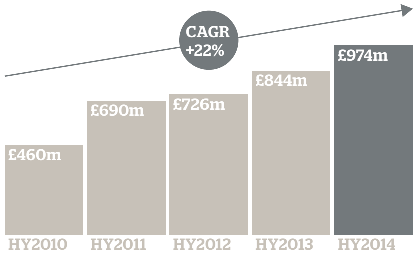


- Compared to half year 2013, underlying free surplus in half year 2014 has increased 13 per cent on a constant exchange rate basis (6 per cent on an actual exchange rate basis), driven by growth of the in-force portfolio, and continued discipline in the allocation of free surplus to new business opportunities.

What we measure and why	Performance[1]	Commentary

Business unit remittances

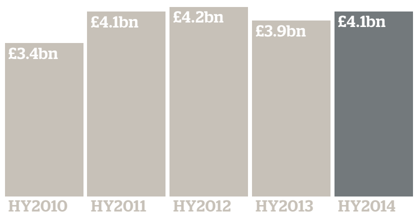
Remittances measure the cash transferred from the business units to the Group. Cash flows across the Group reflect our aim of achieving a balance between ensuring sufficient net remittances from the businesses to cover the dividend (after corporate costs) and retention of cash for reinvestment in profitable opportunities available to the Group.



- Net business unit remittances increased by 15 per cent in half year 2014 when compared to half year 2013, with higher contributions from each of our four business units.

IGD capital surplus before interim dividend[6]

Prudential is subject to the capital adequacy requirements of the European Union Insurance Groups Directive (IGD) as implemented by the Prudential Regulation Authority in the UK. The IGD capital surplus represents the aggregated surplus capital (on a Prudential Regulation Authority consistent basis) of the Group's regulated subsidiaries less the Group's borrowings[7]. No diversification benefit is recognised.



- We continue to operate with a strong solvency position, with our estimated IGD capital surplus before payment of the interim dividend covering the capital requirements 2.3 times.

Notes

1 The comparative results shown above have been prepared using actual exchange rates (AER) basis except where otherwise stated. Comparative results on a constant exchange rate (CER) basis are also shown in financial tables in the Chief Financial Officer's report on our 2014 first half financial performance. CAGR is Compound Annual Growth Rate.

2 The comparative results have been adjusted from those previously published for the retrospective application of the new and amended accounting standards, In addition, following its reclassification as held for sale, the operating results exclude the result of the Japan life insurance business.

3 The basis of IFRS operating profit based on longer-term investment returns is discussed in note B1.3 of the IFRS financial statements. The IFRS profit before tax attributable to shareholders has been prepared in accordance with the basis of preparation discussed in note A of the IFRS financial statements.

4 The EEV basis results have been prepared in accordance with the EEV principles discussed in note 1 of EEV basis results. The 2014 EEV results of the Group are presented on a post-tax basis, and accordingly, prior period results are shown on a comparable basis.

5 Free surplus generation represents 'underlying free surplus' based on operating movements, including the general insurance commission earned during the period and excludes market movements, foreign exchange, capital movements, shareholders' other income and expenditure and centrally arising restructuring and Solvency II implementation costs.

6 Estimated.

7 Excludes subordinated debt issues that qualify as capital.

Group Chief Executive's report

Strong, broad-based performance in the first half of 2014

The Group has delivered strong, broad-based performance in the first half of 2014. Our clear and consistent strategy and our focus on execution have allowed us to leverage effectively our chosen portfolio of businesses to produce good returns for our shareholders while delivering valuable products and services to our customers.

Currency volatility

The market reaction to the combination of the expected rise in interest rates in Western economies, concerns about economic growth in China and in other Asian economies and political uncertainty in Thailand and Indonesia have led to significant currency volatility during the first half of 2014 and to currency depreciation in some of our key Asian markets. There has also been more recently a significant strengthening of sterling driven by expectations that a stronger recovery of the UK economy would lead to an earlier shift in UK monetary policy. All these factors have impacted our results negatively when reported in sterling using actual exchange rates.

In that context, it is important to note that the actual flows that we collect from our customers in Asia and the US are received in local currency. We believe that in periods of currency volatility, the most appropriate way to assess the actual performance of our businesses is to look at what they have achieved on a local currency basis, in other words in terms of the actual flows they have collected rather than the translation of those flows into sterling. Therefore, in this section, every time we comment on the performance of our businesses, we focus on their performance measured in local currency (presented here by reference to percentage growth expressed at constant exchange rates) unless otherwise stated.

Group performance[1]

The Group has delivered double-digit growth across our three key metrics of IFRS operating profit, new business profit and cash with all four of our business units delivering a strong performance.

'The Group has delivered double-digit growth across our three key metrics of IFRS operating profit, new business profit and cash.'

Tidjane Thiam
Group Chief Executive

Our Group **IFRS operating profit** based on longer-term investment returns increased by 17 per cent during the period to £1,521 million (2013: £1,296 million).

- Asia life operating profit was up 19 per cent underpinned by our performance in our seven 'sweet spot' markets[2], which combined grew IFRS operating profit at a rate of 20 per cent. Our focus on proactively managing our diverse business portfolio has helped us offset the short-term headwinds experienced in a few of our markets.
- US life IFRS operating profit increased 28 per cent to £686 million (2013: £538 million). We have achieved higher levels of fee income, generated by variable annuity products written at attractive margins combined with favourable market movements which increased the value of separate account assets.
- UK life IFRS operating profit grew by 10 per cent to £374 million (2013: £341 million) benefiting from higher levels of bulk annuity transactions.
- M&G delivered operating profit of £249 million[3], an increase of 11 per cent, reflecting continued strong third-party net inflows combined with favourable market movements in the period, which together have increased M&G's external funds under management by £14.7 billion to a record £132.8 billion (2013: increase of £6.3 billion to £118.1 billion).

Net cash remittances from our businesses to the Group increased by 15 per cent to £974 million (2013: £844 million on an actual exchange rate basis) driven by strong organic cash generation and supported by robust local capital positions. Cash remittances from Asia grew by 14 per cent to £216 million, the US was up 20 per cent to £352 million, the UK was up 9 per cent to £246 million while M&G (including Prudential Capital) delivered an increase of 19 per cent to £160 million.

Underlying free surplus generation from our life and asset management businesses, a key indicator of cash generation in these businesses, was 13 per cent higher at £1,219 million (6 per cent on an actual exchange rate basis) after reinvestment in new business.

Investment in new business of £382 million (2013: £362 million) has increased less rapidly than sales volume and new business profit, highlighting the capital-efficient nature of our growth.

New business profit[4] was up 24 per cent, crossing the billion pound mark, to £1,015 million (2013: £817 million) driven by a combination of higher volumes and pricing and product actions to increase profitability. All three of our life businesses made strong contributions, with new business profits from Asia growing by 15 per cent to £494 million, the US delivering £376 million, up 31 per cent and the UK reporting £145 million, up 45 per cent.

APE sales increased by 17 per cent to £2.3 billion (2013: £2.0 billion) with double-digit growth from Asia, US and the UK. In Asia, APE sales grew by 13 per cent to £996 million with APE sales from our 'sweet spot' markets[2] growing by 15 per cent. In the US, APE sales were 18 per cent higher at £871 million (2013: £737 million) led by variable annuity sales, with continued strong growth of Elite Access, our variable annuity business without living benefits, where sales were 27 per cent above prior period levels. In the UK, APE sales grew by 22 per cent to £433 million, reflecting strong bulk annuity and investment bond volumes which offset the decline in retail annuity sales. M&G has delivered net inflows of £4.2 billion (2013: £3.8 billion) as it continues to benefit from high levels of retail sales from Continental Europe, while Eastspring Investments, our Asia asset management business, delivered third-party net inflows which were 39 per cent higher at £2.5 billion (2013: £1.8 billion).

Our balance sheet continues to be defensively positioned and at the end of the period our IGD surplus[5] was estimated at £4.1 billion, equating to coverage of 2.3 times.

We are making progress towards our 2017 objectives announced in December 2013.

Our operating performance by business unit

Asia

In the first half of 2014, Asia delivered IFRS operating profit of £525 million, up 19 per cent on the same period in 2013 (3 per cent on an actual exchange rate basis), reflecting continued growth in the scale of our in-force life and asset management businesses and highlighting the successful execution of our strategy. Free surplus generation, after funding investment in new business, increased by 19 per cent to £302 million (3 per cent on an actual exchange rate basis), underpinned by our ongoing focus on capital allocation and capital efficiency. Net cash remittances for the half year were £216 million, 14 per cent higher period-on-period.

Our strategic priority continues to be to meet the savings and financial protection needs of Asia's rapidly growing middle classes with shareholder-friendly products that deliver demonstrable value to customers and are distributed through high-quality tied agents and carefully selected bank partners. The regulatory environment remains supportive as governments look to the private sector to provide efficient and consumer friendly ways for citizens to access enhanced social welfare options as well as to channel household savings into longer-term investments in the economy. Our product portfolio in the region is tailored to →

2017 objectives

	Reported actuals			Objectives*
Asia objectives	**2012** £m[7]	**2013** £m	**Half year 2014** £m	**2017**
Asia life and asset management IFRS operating profit				
Full year	924	1,075		> £1,858m†
Half year	435	512	525	
Asia underlying free surplus generation[6]				
Full year	484	573		£0.9–£1.1bn
Half year	201	292	302	

	Actual	Objective
Group objective for cumulative period 1 January 2014 to 31 December 2017	**1 Jan 2014 to 30 Jun 2014**	**1 Jan 2014 to 31 Dec 2017**
Cumulative group underlying free surplus generation from 2014 onwards	£1.2 billion	> £10 billion

* The objectives assume exchange rates at December 2013 and economic assumptions made by Prudential in calculating the EEV basis supplementary information for the half year ended 30 June 2013, and are based on regulatory and solvency regimes applicable across the Group at the time the objectives were set. The objectives assume that the existing EEV, IFRS and free surplus methodology at December 2013 will be applicable over the period.

† Asia life and asset management pre-tax IFRS operating profit to grow at a compound annual rate of at least 15 per cent over the period 2012-2017.

£1,521m

IFRS operating profit

17%

increase on half year 2013[1]

Group Chief Executive's report continued

→ customers' needs in each of our markets and consistently delivers a high proportion of regular premiums (90 per cent of APE sales) and a significant amount of premium directed towards health and protection coverage (29 per cent of APE sales).

During the first half of this year, some of our markets experienced headwinds as a result of political and economic events such as the uncertainty over the outcome of presidential elections in Indonesia and the military takeover in Thailand. These shorter-term cyclical pressures do not detract from the long-term structural trend of growing demand for our products and services from the rapidly growing and underinsured middle classes. These supportive trends underpin the compelling prospects for profitable growth for our business over the long term. These trends are reflected in our first half performance. Single premiums, which are sentiment-led and are impacted by cyclical events fell 2 per cent while regular premiums, which are the preferred mode for consumers to save and protect themselves, were resilient, growing 15 per cent in the period.

Distribution is key to success in Asia. Over the first half of 2014 we have continued to grow in both the agency and bancassurance channels. The growing scale and increasing productivity of our agency platform is complemented by an extensive range of bank distribution partners across the region. The first half of 2014 included the first anniversary of our successful partnership in Thailand with Thanachart Bank. We also announced in the first quarter that we have further extended and expanded our long-established and market-leading partnership with Standard Chartered Bank for 15 years to 2029. The renewal of this relationship is in line with our strategy, with Standard Chartered Bank strategically positioned in the fast-growing markets of South-east Asia – our 'sweet spot' markets[2]. This gives us access to Standard Chartered Bank's existing 800 branches and 13 million customers and represents a significant growth opportunity over this period. June 2014 saw a record month for new business production from Standard Chartered Bank, continuing a strong history of delivery since 1998 that is based on the demonstrable success of working closely together under a strategic partnership framework.

Our strategic focus on the seven 'sweet spot' markets[2] of South-east Asia (including Hong Kong), where the structural growth opportunities are the most attractive, continue to explain our performance in Asia. Collectively, these markets produced 20 per cent growth in IFRS operating profit, and £455 million of new business profit, over 90 per cent of Asia's total generated, reflecting the disciplined execution of our strategy.

In **Hong Kong**, new business profit[4] increased by 32 per cent, with APE sales growth of 30 per cent. This is mainly as a result of increases in active agency manpower and in productivity, demonstrating the ongoing success of our health and protection and our participating products in Hong Kong. In addition the domestication of the Hong Kong branch of the Prudential Assurance Company was effective 1 January 2014, and established an independent Hong Kong Life Fund.

In **Singapore**, we continue to lead the market with our popular regular premium and PRU*shield* products and increases in agency productivity have supported an 11 per cent increase in APE sales. New business profit[4] was up 7 per cent, mainly reflecting the positive impact of higher sales volumes, partially offset by change in product mix in the period.

£1,015m
EEV new business profit

24%↑
increase on half year 2013[1]

Indonesia had a challenging first half with exceptional flooding disrupting sales in the first quarter, followed by uncertainty over the outcome of the presidential elections depressing the overall market in the second quarter. Given these external factors we are pleased to have held APE sales at the prior period's level and achieved a 1 per cent increase in new business profit[4]. Agency recruitment has remained strong throughout this period with the number of new agents added up 9 per cent over the prior year, and we remain very well placed for when the market normalises. Growth in IFRS operating profit of 32 per cent reflects the continued strong contribution from our in-force portfolio of recurring premium income.

In **Malaysia**, our decision to refocus our agency business on health and protection and to grow distribution by Bumiputra agents ('Bumi'), has delivered an encouraging 14 per cent increase in agency activity. However, as average case sizes are smaller in the Bumi channel and as we have deliberately de-emphasised some top-up products, the combined increase in total APE sales is 6 per cent with new business profit[4] also rising in line for the period.

Following last year's acquisition of Thanachart Life in **Thailand** and the successful execution of our exclusive bancassurance agreement with Thanachart Bank, APE sales from this market have doubled over the first half of last year. This also results from strong progress in our original business, where APE sales were up 43 per cent in the first half of the year. Volume growth and the positive impact on margin from changes in product mix have seen new business profit[4] increase 167 per cent. We have not seen any major impact on our operations from the recent political events to date and although we remain vigilant, we continue to be very positive about the longer-term prospects of our business in Thailand.

The transformation of our agency business in the **Philippines** is making excellent progress, following a significant increase in agent activity (up 36 per cent) and an increased focus on regular premium business (up 21 per cent). Lower levels of single premium and lower bancassurance sales (down 48 per cent) have driven the 12 per cent decline in total APE sales.

Vietnam had a solid first half, with APE sales growing 10 per cent and new business profit[4] by 20 per cent driven by increases in agency activity.

Our joint venture with CITIC in **China** continues to perform well with APE sales growing by 33 per cent, reflecting progress in both the agency and bank channels. We now have offices in all the major economic centres in China. In **India** our joint venture with ICICI Bank remains the leader in the private sector, but the market slowed in the first half ahead of the recent elections. There is much optimism about the Indian economy and we remain in an excellent position to benefit from any positive developments. The recently-announced budget proposed an increase in the foreign shareholding cap from 26 per cent to 49 per cent, however the exact shape of the proposals and whether they are likely to receive parliamentary approval are still to be clarified.

In **Taiwan** and **Korea**, we remain selective in our participation and as a result we are content to tolerate fluctuations in new business volumes.

We are also setting foundations for future growth in new markets. We have successfully launched in **Cambodia** with a market-leading life insurance business, we have opened a representative office in **Myanmar**, and we are in the preliminary stages of entering **Laos**.

EEV life operating profit[4] of £832 million is up 16 per cent on prior half year, largely as a result of the growth in new business profit and an 18 per cent increase in the contribution from a larger in-force book.

Eastspring Investments, our Asia asset management business, saw net third-party inflows of £2.5 billion, 39 per cent higher than last year, with success in securing new equity flows, particularly from institutional clients, mitigating lower net inflows in fixed income. Total funds under management as at 30 June 2014 were £67 billion, up 22 per cent on the prior half year as a result of net inflows and positive market movements. IFRS operating profit increased 24 per cent to £42 million, driven by the positive impact on revenue from higher levels of average assets under management.

US

In the first half of 2014, Jackson delivered life IFRS operating profit of £686 million, up 28 per cent at constant exchange rates (18 per cent on an actual exchange rate basis) from the same period in 2013. This increase was primarily driven by increased fee income from higher separate account assets. Cash remitted to Group increased 20 per cent to a record level – £352 million compared to £294 million (at actual exchange rates) in 2013. Jackson continues to focus on the delivery of IFRS operating earnings and cash, while maintaining its disciplined approach to new business and management of the in-force book, and at the same time continuing to improve its capital position.

Overall, the US economy continues to see signs of improvement with further declines in unemployment rates, signs of recovery in the crucially important housing market and stronger GDP growth, with a second quarter at 4 per cent annualised.

£1,219m
underlying free surplus generation

13%↑
increase on half year 2013[1]

During the first half of 2014, the S&P 500 Index rose 6 per cent and the 10-year Treasury rate remained significantly above the 2012 low levels. Overall, the US competitive landscape has been more stable than in recent periods, as most annuity writers appear to have committed to a particular course of action for the near term. That said, variable annuity providers continue to modify their product offerings through reductions in fund availability and increased fees. In addition, an increasing number of investment-only variable annuity products, ie variable annuities without living benefits, have been launched.

Jackson achieved total retail APE sales of £808 million, an increase of 15 per cent compared to the first half of 2013. These sales were achieved while continuing to write new business at aggregate internal rates of return well in excess of 20 per cent and with a payback period of two years. Including institutional sales, total APE sales increased 18 per cent to £871 million, driving new business profit[4] growth of 31 per cent to £376 million.

APE sales from **variable annuity** increased 24 per cent to £763 million in the first half of 2014. Sales of Elite Access, our variable annuity without living benefits, contributed APE sales of £149 million, 27 per cent above prior half year levels and exceeding the growth rate in APE sales of variable annuities excluding Elite Access, which were up 23 per cent to £614 million. The economics of our variable annuity business continue to be very attractive and with the success of Elite Access, we continue to improve the diversification of our product mix, with 32 per cent of variable annuity APE sales in the first half of 2014 not featuring living benefit guarantees (2013: 29 per cent). In line with our proactive cycle management approach, Jackson continues to actively manage the sales volumes of variable annuities with living benefits to maintain an appropriate balance of our revenue streams and to match the Group's annual risk appetite. At the end of the period, Jackson's statutory separate account assets were £71.5 billion, up 34 per cent (19 per cent on an actual exchange rate basis) compared to £53.3 billion (at constant exchange rates) for the same period in 2013, as a result of both positive net flows and the significant growth in the underlying market value of the separate account assets over the past 12 months.

Fixed annuity APE sales of £27 million remained relatively flat compared to 2013, while **fixed index annuity** APE sales of £18 million decreased 68 per cent, primarily as a result of product changes implemented in late 2013 to increase returns to shareholder capital.

EEV life operating profit[4] was £777 million, up 19 per cent from the same period in 2013, reflecting the growth in the scale of our in-force book and higher new business profit, which increased 31 per cent to £376 million. Although interest rates remain low, the beneficial impact of the product initiatives implemented in previous years enabled us to write 2014 business at overall new business margins close to post-financial crisis highs.

IFRS operating profit from non-life operations in the US decreased to a loss of £5 million (2013: profit of £31 million), due to a Curian year-to-date loss of £23 million after a £33 million provision related primarily to the potential refund of certain fees by Curian.

Jackson's strategy remains unchanged. We continue to price new business on →

Group Chief Executive's report continued

a conservative basis, targeting value over volume. Our hedging remains focused on optimising the economics of our exposures over time while maintaining a strong balance sheet. Since 1 January 2008, Jackson has remitted close to US$2.5 billion of cash to the Group. We believe Jackson's approach has translated into value for the customers and into profits and cash for shareholders, the ultimate metrics of our successful strategy.

UK, Europe and Africa

In the first half of 2014, Prudential UK delivered life IFRS operating profit of £374 million, up 10 per cent period-on-period and new business profit[4] of £145 million, up 45 per cent, primarily as a result of higher levels of bulk annuity activity and increased sales of investment bonds. Cash remitted to the Group increased to £246 million, compared to £226 million in the first half of 2013.

The UK market continues to be heavily influenced by an unprecedented level of regulatory and legislative change. In March 2014, the UK government announced significant changes to pensions regulation which will effectively remove the requirement to purchase a pension annuity from April 2015. There has since been considerable disruption to industry sales of individual annuities as the government, pension providers, advisers and consumers work through the implications of these changes. In the transitional period created by the Budget, there has been, understandably, an increase in the number of customers who have deferred converting their pension savings into retirement income. This is reflected in our first half sales of **individual annuities**, which were also impacted by the overall slowdown in the market that started to emerge through 2013, with APE sales 43 per cent lower period-on-period at £63 million. Our experience in retirement income products and investment expertise means that we believe we are well positioned to help customers through this period of change and provide solutions that meet their retirement needs.

Total APE sales of £433 million increased 22 per cent. This includes four new **bulk annuity** deals in the first half of 2014 (2013: £nil), generating APE sales of £104 million and new business profit[4] of £69 million. Through our long-standing presence in this segment of the life and pensions market, we have developed considerable longevity experience, operational scale and a solid investment track record, which together represent expertise and capabilities that are increasingly in demand. Our approach to bulk transactions in the UK will continue to be one of selective participation, looking for situations where we can both bring significant value to our customers and meet our demanding shareholder return hurdles.

Within our **retail** business, strong momentum in sales of onshore and offshore bonds was offset by a reduction in individual annuities and corporate pensions sales. Overall retail APE sales of £329 million were 7 per cent lower than the first half of 2013 and retail new business profit was 24 per cent lower, largely due to the reduced sales of individual annuities.

The strength of our investment proposition is reflected in the growth in sales of our onshore bonds. **Onshore bonds** APE sales of £102 million increased by 23 per cent, including APE from with-profits bonds of £93 million, up 25 per cent over the first half of 2013. In particular, demand for our non-guaranteed with-profits bond remains strong, attracting customers who are prepared to accept some investment risk but still want to benefit from the smoothing offered by a with-profits product with a strong track record of investment growth. We expect this to be a feature of the market going forward, with significant demand for products with managed volatility.

£974m
net cash remittances from business units

15%
increase on half year 2013[1]

APE sales from **other retail products**, principally individual pensions, income drawdown, PruProtect, PruHealth and offshore bonds, increased by 25 per cent to £85 million. Offshore bond APE sales were 57 per cent higher and income drawdown sales grew by 95 per cent, both driven by our with-profits product offering. The growth in income drawdown reflects the improving investment environment and increased customer demand, which was accelerated by the UK Budget. The Budget has the potential to open up opportunities to serve our customers further and our programme of product development remains on track to bring new products to market in 2015.

Corporate pensions APE sales of £79 million were 15 per cent lower, mainly due to a fall in with-profits sales following changes to government sector pension schemes. We remain the largest provider of Additional Voluntary Contribution plans within the public sector, where we provide schemes for 72 of the 99 public sector authorities in the UK (first half of 2013: 68 of the 99).

EEV life operating profit[4] of £388 million was 28 per cent higher than the first half of 2013, reflecting the positive impact of improvements in economic conditions and higher volumes of bulk annuity business.

Prudential's continuing focus on the delivery of excellent customer service was recognised at the 2014 FTAdviser Online Service Awards, where we received an outstanding achievement award and two Five-Star ratings in the life and pensions and investment categories.

On 27 March 2014, we completed the acquisition of Express Life in Ghana, marking the Group's entry into the nascent African life insurance industry. The business has now been rebranded to Prudential Ghana and is making good progress in growing its agency force and new business volumes. In addition, the renewal of our bancassurance partnership with Standard Chartered Bank includes an agreement to explore opportunities to collaborate in Africa, subject to existing exclusivity arrangements and regulatory restrictions.

We are positive about the long-term opportunities in Africa, where we see many of the favourable structural characteristics of our preferred Asian markets, although most sub-Saharan life insurance markets are in the very early stages of development and therefore are not likely to be material for many years.

M&G

Our European asset management business, M&G, has delivered a strong performance in the first half, with IFRS operating profit growing by 11 per cent to £227 million as a result of higher levels of funds under management. M&G remitted cash of £135 million to Group, up 24 per cent on 2013.

Net retail fund inflows totalled £3.8 billion during the first six months of 2014. Continental Europe made the largest contribution with net flows of £4.2 billion (2013: £5.6 billion). Retail funds under management from Continental Europe have increased by 32 per cent to £27.9 billion over the past 12 months and now represent 39 per cent of total retail funds under management, up from 34 per cent a year ago. Total retail funds under management now stand at £71.9 billion, up 15 per cent compared to 30 June 2013.

Following a relative slowdown in recent periods, M&G's UK sales are showing signs of stabilisation, with net outflows of £516 million in the first six months, an improvement on net outflows of £1.2 billion in the same period in 2013.

M&G's **institutional** business produced first-half net inflows of £427 million. The business again experienced a series of expected withdrawals from a single large but low-margin mandate which was originally received during 2012 and whose value at 30 June 2014 was £5.9 billion. Excluding the redemptions from this single mandate, the business has experienced a healthy positive run rate of underlying net sales. Overall, institutional funds under management have increased to £60.8 billion, up 10 per cent compared to 30 June 2013.

Consistently good investment performance, coupled with an established reputation for innovation, has led to a strong pipeline of new business for the institutional team. In particular, M&G has used its investment expertise to develop a number of products that allow institutional investors to take advantage of the gap in the lending market created by the decline in long-term commercial bank loans. These opportunities include lending to medium-sized companies, housing association-registered providers, commercial real estate borrowers and infrastructure projects.

Strong net inflows, combined with the positive impact of a 9 per cent increase in equity market levels and an 8 per cent rise in bond markets, pushed total external client assets to a new record level of £132.8 billion, 12 per cent higher than a year ago. Total funds under management now stand at £253.7 billion (2013: £234.3 billion), with third-party assets accounting for 52 per cent of the total.

'The Board has approved a 2014 interim dividend of 11.19 pence per share, which equates to an increase of 15 per cent over the 2013 interim dividend.'

Tidjane Thiam
Group Chief Executive

Underlying profit[8] increased by 10 per cent to £214 million and our operating margins improved, as M&G continues to execute against its strategy and deliver strong performance for both clients and shareholders.

The beneficial impact on revenues of higher levels of funds under management has helped to absorb a larger cost base, reflecting continued investment in headcount and operational infrastructure, and resulting in a cost/income ratio of 54 per cent that is unchanged from the first half of 2013.

Looking ahead, M&G will continue to seek diversification by both asset class and geography, while remaining focused on delivering excellent investment performance and service to its clients.

Capital and risk management

We continue to take a disciplined approach to capital management and have implemented a number of measures over the last few years to enable us to make our capital work more efficiently and more effectively for the Group. Using the regulatory measures of the Insurance Groups Directive (IGD), our Group capital surplus position at 30 June 2014 was estimated at £4.1 billion (2013: £3.9 billion), before allowing for the interim dividend, equating to coverage of 2.3 times.

In July 2013, Prudential plc was listed by the Financial Stability Board as one of nine companies to be designated as a Global Systemically Important Insurer (GSII). Since then, in July 2014 the International Association of Insurance Supervisors has released a consultation paper on the Basic Capital Requirement (BCR), one of the two types of capital requirement proposed under the GSII framework. Prudential is monitoring the development and potential impact of the framework of policy measures and engaging closely with the Prudential Regulation Authority (PRA) on the implication of this designation.

Solvency II is scheduled to come into effect on 1 January 2016 and our preparations are well advanced. We continue to work with HM Treasury, the Association of British Insurers, the PRA, trade associations and peers across Europe, to ensure that the practical details of Solvency II, including the final implementing measures, are both workable and effective.

Dividend

Due to the strong and sustained operational and financial performance of the Group, evidenced by the achievement of all our demanding 2013 'Growth and Cash' Objectives, the Board decided to rebase the 2013 full year dividend upwards to 33.57 pence per share, representing an increase of 15 per cent over 2012. As in previous years the interim dividend for 2014 has been calculated formulaically as one-third of the prior year's full year dividend. The Board has approved a 2014 interim dividend of 11.19 pence per share, which equates to an increase of 15 per cent over the 2013 interim dividend.

The Board applies strict affordability tests against a broad range of criteria before making its dividend recommendation. It is the result of these tests, combined with the Group's exceptionally strong performance in the past five years, that enabled the Board to take the unusual decision to recommend the rebase of the dividend in consecutive years, 2012 and 2013. →

Group Chief Executive's report continued

It is worth emphasising here again that although the Board has been able to recommend three upward rebases in 2010, 2012 and 2013, the Group's dividend policy remains unchanged. The Board will maintain its focus on delivering a growing dividend, which will continue to be determined after taking into account the 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.

Outlook

Our business has continued to deliver both 'Growth and Cash' in the first half of 2014. We are making progress towards the 2017 objectives announced in December 2013.

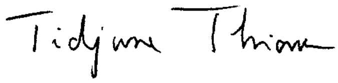
Our clear and unchanged strategy focused on cash-generative growth from our attractive and increasingly diverse geographic, product and market segments combined with our disciplined execution underpins our broad-based underlying financial performance.

There is increasing evidence that economic growth is set to accelerate in the US and the UK with emerging Asia economies forecast to continue to grow at relatively higher rates than developed Western economies. While this improving macroeconomic picture is beneficial to our businesses, there remains shorter-term uncertainty around the pace and timing of eventual interest rate increases in the US and the UK. This has mainly manifested in a strengthening of sterling. Investment markets are discounting an orderly transition to a less accommodative world. In Europe, the economic environment continues to pose significant challenges but we have little exposure to this region.

Asia remains core to the long-term growth and profitability prospects for the Group. A rapidly growing and prosperous middle class that is mostly underinsured, with very low state insurance coverage, provide a strong structural underpinning for long-term sustainable and profitable growth. In the shorter term, some Asian economies are facing cyclical headwinds from currency depreciation, political events and the effects of proactive financial tightening undertaken over the last year. Against this backdrop, we continue to actively manage our diverse portfolio of businesses across the region to secure strong returns to both our customers and our shareholders. We are also investing in further expanding our leading business platform in the region as evidenced by the renewal of our long-established and successful bancassurance relationship with Standard Chartered Bank and our successful partnerships with UOB and Thanachart Bank. Our leadership position across our 'sweet spot' markets[2], growing scale and effective distribution of our attractive product propositions across both the agency and bank channels position us well to profitably capture the long-term structural growth opportunity.

In the US, we remain focused on generating both earnings and cash. In the UK, we are leveraging our brands and existing product expertise to meet our customers' changing needs in the new regulatory landscape while delivering stable returns.

We remain confident in our ability to produce profitable growth over the long term and continue to create value for our customers and shareholders.



Tidjane Thiam
Group Chief Executive

11.19p
interim dividend

15%
increase on half year 2013

Notes

1 The comparative results referenced above and elsewhere in this document have been prepared using constant exchange rates basis except where otherwise stated. Comparative results on an actual exchange rate basis are also shown in financial tables in the Chief Financial Officer's report on our 2014 first half financial performance.

2 'Sweet spot' markets include Indonesia, Singapore, Hong Kong, Malaysia, the Philippines, Vietnam and Thailand.

3 Including Prudential Capital.

4 The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis.

5 Before allowing for interim dividend.

6 Underlying free surplus generated comprises underlying free surplus generated from long-term business (net of investment in new business) and that generated from asset management operations. The 2012 comparative is based on the retrospective application of new and amended accounting standards and excludes the 2012 one-off gain of £51 million from the sale of the Group's holding in China Life Insurance Company of Taiwan.

7 Asia 2012 IFRS operating profit of £924 million, is based on the retrospective application of new and amended accounting standards as at 31 December 2013, and excludes the 2012 one-off gain of £51 million from the sale of the Group's holding in China Life Insurance Company of Taiwan.

8 Excluding performance fees, carried interest and share of profits from associate entity, PPM South Africa.

Section 2

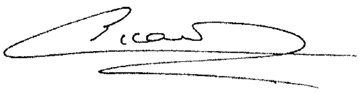
Business performance

2

Chief Financial Officer's report on our 2014 first half financial performance

A strong financial performance with growth in earnings and cash

'We continue to be proactive in focusing on growing high quality sources of income that are more predictable and more resilient to volatility in economic and investment market conditions.'



Nic Nicandrou
Chief Financial Officer

Prudential has delivered a strong financial performance in the first half of 2014, reporting growth in its key metrics of IFRS operating profit and underlying free surplus generated. All four businesses have recorded improvements in earnings and cash generation as they continue to focus on higher quality sources of income that are more predictable and more resilient to volatility in economic and investment market conditions. These characteristics are further enhanced by the increasing diversification of our business, by product, distribution and geography, and by maintaining a robust balance sheet with a conservative approach to risk management.

Following the major depreciation in currencies against sterling in the second half of 2013, the first half of 2014 has seen further volatility in the world's currency markets, driven by improving growth prospects and increasing speculation around the timing of possible movements in interest rates. In our key markets, this has been more prominent among the US dollar, US dollar-linked currencies and the Indonesian rupiah, all of which have weakened against sterling since the first half of 2013. For the purpose of reporting our performance in sterling terms, we adopt the normal convention of translating the results of our overseas businesses using average exchange rates for the period. However, the currency translation effect is so pronounced for some parts of the business that it masks the underlying operational trends, rendering it difficult to meaningfully assess performance.

I have, therefore, focused my commentary on the performance of our Asia and US businesses in local currency and have presented percentage growth rates between periods on a constant exchange basis, unless otherwise stated. Growth rates based on actual exchange rates are also shown in the financial tables presented in this report.

As the assets and liabilities of our overseas businesses are translated at period-end exchange rates, the effect of these currency movements has been fully incorporated within reported shareholders' equity as at 30 June 2014.

Group IFRS operating profit increased by 17 per cent to £1,521 million on a constant exchange rate basis (7 per cent on an actual exchange rate basis) and underlying free surplus generation (net of investment in new business) increased 13 per cent to £1,219 million (6 per cent on an actual exchange rate basis). On the European Embedded Value (EEV) basis of reporting performance, new business profit[1] was up 24 per cent to £1,015 million (11 per cent on an actual exchange rate basis), contributing to an 18 per cent increase in EEV operating profit[1] to £1,943 million (7 per cent on an actual exchange rate basis). Including the financial impact of short-term movements in investment values and other items reported outside the operating result, the Group generated profit before tax attributable to shareholders on an IFRS basis of £1,424 million, compared to £506 million (on an actual exchange rate basis) in the first half of 2013.

£1,521m
IFRS operating profit

17%
increase on half year 2013

IFRS profits

		AER		CER	
	Half year 2014 £m	Half year 2013 £m	Change %	Half year 2013 £m	Change %
Operating profit before tax					
Long-term business:					
Asia[2]	483	474	2	406	19
US	686	582	18	538	28
UK	374	341	10	341	10
Long-term business operating profit before tax[2]	1,543	1,397	10	1,285	20
UK general insurance commission	12	15	(20)	15	(20)
Asset management business:					
M&G (including Prudential Capital)	249	225	11	225	11
Eastspring Investments	42	38	11	34	24
US	(5)	34	(115)	31	(116)
Other income and expenditure[3]	(320)	(294)	(9)	(294)	(9)
Total operating profit based on longer-term investment returns before tax	1,521	1,415	7	1,296	17
Short-term fluctuations in investment returns:					
Insurance operations	(14)	(725)	98	(679)	98
Other operations	(31)	(30)	(3)	(30)	(3)
	(45)	(755)	94	(709)	94
Other non-operating items[3]	(52)	(154)	66	(135)	61
Profit before tax attributable to shareholders	1,424	506	181	452	215
Tax charge attributable to shareholders' returns	(279)	(141)			
Profit for the period attributable to shareholders	1,145	365			

IFRS earnings per share

		AER		CER	
	Half year 2014 pence	Half year 2013 pence	Change %	Half year 2013 pence	Change %
Basic earnings per share based on operating profit after tax	45.2	42.2	7	38.7	17
Basic earnings per share based on total profit after tax	45.0	14.3	215	12.8	252

IFRS operating profit

Total IFRS operating profit increased by 17 per cent in the first half of 2014 to £1,521 million, driven by profitable business growth in Asia, the US and M&G and the beneficial impact of four bulk annuity transactions in the UK life business.

Asia life operating profit was up 19 per cent (2 per cent on an actual exchange rate basis), with strong growth from all of our operations, particularly Indonesia, Thailand and Vietnam. US life operating profit increased by 28 per cent (18 per cent on an actual exchange rate basis), driven principally by higher variable annuity fee income. UK life operating profit was 10 per cent higher, reflecting contributions totalling £60 million from bulk annuity transactions (2013: £nil), which offset lower profits in the retail business. M&G (including Prudential Capital), our UK-based asset management business and Eastspring Investments, our Asia asset manager, delivered IFRS earnings growth of 11 per cent and 24 per cent, respectively.

Taken together, IFRS operating profit from our life insurance operations in Asia, the US and the UK increased 20 per cent to £1,543 million. This increase in profitability of our life operations reflects the growth in the scale of our life operations, driven primarily by positive business inflows. We track the progress that we make in growing our life business by reference to the scale of our obligations to our customers, which are referred to in the financial statements as policyholder liabilities. Each year these liabilities increase as we collect premiums and decrease as we pay claims. The overall scale of these policyholder liabilities is relevant in evaluating our profit potential, in that it is reflective of our ability to earn fees on the unit-linked element and it sizes the risk that we carry on the insurance element, for which Prudential needs to be rewarded. →

Chief Financial Officer's report on our 2014 first half financial performance continued

Shareholder-backed policyholder liabilities and net liability flows[4]

	Half year 2014 £m		Half year 2013 £m			Change %		
			AER		CER	AER		CER
	Policyholder liabilities	Net liability flows[5]	Policyholder liabilities	Net liability flows[5]	Net liability flows[5]	Policyholder liabilities	Net liability flows[5]	Net liability flows[5]
Asia	23,419	891	22,903	1,039	938	2	(14)	(5)
US	112,009	4,977	106,215	5,168	4,781	5	(4)	4
UK	52,687	(140)	50,070	(336)	(336)	5	58	58
Total Group	188,115	5,728	179,188	5,871	5,383	5	(2)	6

→ Focusing on the business supported by shareholder capital, which accounts for the majority of the life profits, in the course of the first half of 2014 policyholder liabilities increased from £180.1 billion at the start of the year to £188.1 billion at the end of June 2014. The consistent addition of high quality profitable new business and proactive management of the existing in-force portfolio underpins this increase, resulting in positive net flows[5] into policyholder liabilities of £5.7 billion in the first half of 2014 driven by positive inflows into both our US and Asia businesses. Net flows into our Jackson business grew by 4 per cent compared to half year 2013, following increased variable annuity new business premiums. Net flows into Asia continue to be positive reflecting the new regular premium business added this period, offset by higher levels of maturities of products reaching their term. Favourable investment market and other movements have contributed a further £6.3 billion to the increase in policyholder liabilities since the start of the year, offset by a £4.0 billion negative foreign currency translation effect.

Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver[6]

				AER			CER		
	Half year 2014 £m			Half year 2013 £m			Half year 2013 £m		
	Operating profit	Average liability	Margin bps	Operating profit	Average liability	Margin bps	Operating profit	Average liability	Margin bps
Spread income	557	64,741	172	535	65,424	164	499	62,492	160
Fee income	764	106,052	144	667	93,512	143	615	87,678	140
With-profits	150	98,046	31	155	97,336	32	153	96,352	32
Insurance margin	680			613			551		
Margin on revenues	808			858			749		
Acquisition costs*	(1,000)	2,300	(43)%	(1,021)	2,162	(47)%	(917)	1,974	(46)%
Administration expenses	(701)	178,649	(78)	(682)	166,130	(82)	(618)	156,839	(79)
DAC adjustments	169			175			161		
Expected return on shareholder assets	116			97			92		
Operating profit based on longer-term investment returns	1,543			1,397			1,285		

* The ratio of acquisition costs is calculated as a percentage of APE sales including with-profits sales. Acquisition costs include only those relating to shareholder-backed business.

In the first half of 2014, alongside growing the scale of our life operating profit, we have continued to focus on improving its quality by maintaining our bias for sources of income such as insurance margin and fee income, ahead of spread income; insurance income because it is relatively insensitive to the equity and interest rate cycle, and fee income because it is capital efficient. Our emphasis on growing our offering of risk products such as health and protection, has seen insurance margin grow by 23 per cent (11 per cent on an actual exchange rate basis), while fee income is up 24 per cent (15 per cent on an actual exchange rate basis), primarily reflecting the higher amount of assets that we manage on behalf of our customers. In contrast, the contribution to our profits from spread income has continued to increase at a more subdued rate of 12 per cent (4 per cent on an actual exchange rate basis). The fact that insurance margin and fee income generate a growing proportion of our income represents a healthy evolution in the quality, the resilience and the balance of our earnings.

The costs we have incurred in writing new business and in administering the in-force life businesses have also increased but at a more modest rate than total income, highlighting the advantages of increased scale as we build out our business, while maintaining control of costs.

IFRS operating profit from Asia life insurance was up 19 per cent to £483 million, driven by the increasing scale of the in-force portfolio and our emphasis on growing the proportion of our income that is sourced from regular premium health and protection business. In addition, we continue to focus on our seven 'sweet spot' markets of Indonesia, Singapore, Malaysia, Thailand, Vietnam, the Philippines and Hong Kong, which collectively increased IFRS operating profit by 20 per cent. Indonesia IFRS operating profit, our largest market on this measure, was up by 32 per cent to £139 million, reflecting increased insurance and fee income from growth in the in-force book following the high level of regular premium health and protection and unit-linked sales in recent years. We are also encouraged to see further progress among our smaller, fast-growing businesses in South-east Asia, with Thailand, the Philippines and Vietnam reporting a combined 97 per cent increase in profits to £63 million and now accounting for 13 per cent of Asia's life operating profit compared to 8 per cent in the prior half year. In particular, Thailand's contribution has benefited from the acquisition of Thanachart Life's in-force portfolio and profit on new business written through our exclusive relationship with Thanachart Bank, with IFRS operating profit up 150 per cent to £25 million.

In the US, life IFRS operating profit increased by 28 per cent to £686 million, driven by 29 per cent growth in fee income, which now accounts for 48 per cent of Jackson's total income, compared to 38 per cent in the same period just three years ago. The uplift in fee income in the period reflects average separate account assets of £68 billion in the first half of 2014 compared to £52 billion in the first half of last year, equating to an increase of 31 per cent on a constant exchange rate basis, driven by variable annuity net premium inflows and appreciation in US equity markets. We continue to focus on improving the balance of Jackson's profits and diversifying its sources of earnings and we are pleased with the continued growth in sales of Elite Access, our variable annuity product without living benefits.

UK life IFRS operating profit was 10 per cent higher than the first half of 2013 at £374 million (2013: £341 million), principally due to a £60 million profit contribution from bulk annuity transactions (2013: £nil), which exceeded a £29 million reduction in profits from new retail annuity business (from £54 million in 2013 to £25 million in 2014).

Asset management net inflows and external funds under management[7]

	External net inflows					External funds under management		
		AER		CER				
	Half year 2014 £m	Half year 2013 £m	Change %	2013 £m	Change %	Half year 2014 £m	Half year 2013 £m	Change %
M&G								
Retail	3,784	4,754	(20)	4,754	(20)	71,941	62,655	15
Institutional	427	(914)	147	(914)	147	60,830	55,484	10
M&G	4,211	3,840	10	3,840	10	132,771	118,139	12
Eastspring[8]	2,483	2,006	24	1,792	39	21,078	19,268	9
Total asset management	6,694	5,846	15	5,632	19	153,849	137,407	12
Total asset management (inc. MMF)	6,642	5,953	12	5,744	16	158,149	141,674	12

Our asset management businesses in the UK and Asia collectively contributed IFRS operating profit of £291 million, up 12 per cent on the first half of 2013. Similar to our life operations, growth in asset management operating profit primarily reflects the increased scale of this business, as measured by funds managed on behalf of external institutional and retail customers and our internal life insurance operations. Net flows from external parties into these funds (excluding MMF) were £6.7 billion in the first half of 2014 (2013: £5.8 billion on an actual exchange rate basis) and helped drive external retail and institutional funds under management (excluding MMF) to £153.8 billion at 30 June 2014 compared to £137.4 billion at 30 June 2013.

M&G's IFRS operating profit increased 11 per cent to £227 million (2013: £204 million). Underlying profits, excluding performance-related payments and earnings from associates, increased 10 per cent to £214 million (2013: £195 million), primarily reflecting an 11 per cent uplift in average external funds under management compared to the first half of 2013, following a period of strong net inflows and positive market movements. The positive business mix effect from the increasing proportion of higher-margin external retail business has seen M&G's average fee income improve to 38 basis points (2013: 36 basis points), with higher income helping to absorb the current phase of increased headcount and infrastructure investment. Reflecting this, the cost income ratio was maintained at 54 per cent (2013: 54 per cent). As in previous periods, we expect the cost/income ratio to increase by the end of 2014 as M&G's cost run rate is typically higher over the second half of the year.

Our Asia asset management business, Eastspring Investments, has also seen the benefit of higher average funds under management, with IFRS operating profit of £42 million up 24 per cent. In the US, our asset management businesses, PPM America and Curian, and our broker-dealer network, National Planning Holdings, collectively generated an IFRS operating loss of £5 million (2013: profit of £31 million at constant exchange rate) after a £33 million provision related primarily to the potential refund of certain fees by Curian.

IFRS short-term fluctuations

IFRS operating profit is based on longer-term investment return assumptions. The difference between actual investment returns recorded in the income statement and these longer-term returns is reported within short-term fluctuations in investment returns. In the first half of 2014 for our insurance operations these total negative £14 million (2013: negative £725 million on an actual exchange rate basis).

In Asia, positive short-term fluctuations of £119 million primarily reflect net unrealised movements on bond holdings following modest falls in bond yields during the first half of the year across the region.

Negative short-term fluctuations of £226 million in the US mainly represent the net value movement on derivatives held to manage the Group's exposure to market movements following rises in equity values. Jackson hedges the guarantees offered under its variable annuity proposition on an economic basis and, thus, accepts a degree of variability in its IFRS results in the short term in order to achieve the appropriate economic result. Increases in US equity markets during the first half of the year gave rise to negative mark to market movement on the portfolio of equity hedges, which were not offset by corresponding reductions in the obligations to our customers as many of the guarantees are not accounted for using a fully fair value basis. The net gains on the interest rate hedges generated by the reduction in US interest rates, were insufficient to eliminate the negative equity market effect.

Positive fluctuations of £93 million in the UK include net unrealised movements on fixed income assets supporting the capital of the shareholder-backed annuity business, reflecting the fall in bond yields since the end of 2013. →

Chief Financial Officer's report on our 2014 first half financial performance continued

IFRS effective tax rates

In the first half of 2014, the effective tax rate on IFRS operating profit based on longer-term investment returns was 24 per cent in line with the equivalent period last year.

The effective tax rate for the first half of 2014 on the total IFRS profit was 20 per cent (2013: 28 per cent), reflecting both the reduction in corporation tax rates in the UK and certain Asia jurisdictions, as well as the fact that the 2013 effective tax rate was higher than normal due to no tax relief being available on the loss attaching to the held for sale Japan life business.

Free surplus generation

Our ongoing focus on disciplined capital allocation to new business opportunities that offer the most attractive mix of returns and short payback periods, means that we have continued to produce significant amounts of capital, which we measure by reference to free surplus generated. Free surplus generation is a financial metric we use to measure the internal cash generation of our business operations. For the insurance operations it represents amounts maturing from the in-force business during the period, net of amounts reinvested in writing new business, and for asset management it equates to post-tax IFRS profit for the period.

Free surplus generation

		AER		CER	
	Half year 2014 £m	**Half year 2013** £m	**Change** %	**Half year 2013** £m	**Change** %
Free surplus generation[9]					
Asia	**469**	457	3	400	17
US	**629**	612	3	566	11
UK	**303**	304	–	304	–
M&G (incl. Prudential Capital)	**200**	175	14	175	14
Underlying free surplus generated from in-force life business and asset management	**1,601**	1,548	3	1,445	11
Investment in new business	**(382)**	(396)	4	(362)	(6)
Underlying free surplus generated	**1,219**	1,152	6	1,083	13
Market related movements, timing differences and other movements	**(27)**	147			
Net cash remitted by business units	**(974)**	(844)			
Total movement in free surplus	**218**	455			
Free surplus at 1 January	**4,003**	3,689			
Effect of domestication of Hong Kong branch	**(35)**	–			
Free surplus at end of period	**4,186**	4,144			

In the first half of 2014, our life in-force and asset management businesses generated £1,601 million of underlying free surplus before reinvestment in new business. This is an increase of 11 per cent compared to the first half of 2013 (3 per cent on an actual exchange rate basis), reflecting higher contributions from Asia, the US and M&G and an unchanged contribution from the UK. For our life insurance businesses, the growth in underlying free surplus generated is driven by our in-force portfolio, which increased its contribution by 12 per cent to £1,361 million. This is a clear indication of our continued success in capturing profitable new business flows, in those markets where growth opportunities are most attractive, and highlights the benefits of targeting low strain, high return business with a fast payback profile. The total stock of free surplus held by our life and asset management operations increased to £4.2 billion as at 30 June 2014 (30 June 2013: £4.1 billion, on an actual exchange rate basis), after financing reinvestment in new business and cash remittances from the business units to Group.

We reinvested £382 million of the free surplus generated in the period into writing new business (2013: £362 million on a constant exchange rate basis) equivalent to a reinvestment rate of 24 per cent, which is in line with recent periods. The amount of free surplus we reinvested in Asia increased 14 per cent to £167 million, while new business profit increased 15 per cent. In the US, new business investment decreased 11 per cent to £173 million despite higher volumes of new business, reflecting the beneficial effect of higher valuation interest rates, proactive actions to restrict sales of the higher strain products and changes in product mix. Reinvestment levels in the UK increased to £42 million (2013: £20 million), primarily due to the higher level of bulk annuity business written in 2014.

The internal rates of return achieved on new business remain attractive at over 20 per cent across all of our business operations and the average payback period[10] for business written in the first half of 2014 was three years for Asia, two years for the US and five years for the UK.

We continue to manage cash flows across the Group with a view to achieving a balance between ensuring sufficient remittances are made to service central requirements (including paying the external dividend) and maximising value to shareholders through retention and reinvestment of excess capital in business opportunities.

Holding company cash[11]

	Half year 2014 £m	AER Half year 2013 £m	Change %
Net cash remitted by business units:			
Asia	216	190	14
US	352	294	20
UK	246	226	9
M&G	135	109	24
Prudential Capital	25	25	–
Net cash remitted by business units	974	844	15
Net central outflows	(155)	(132)	
	819	712	
Corporate activities/other (including foreign exchange)	(537)	(70)	
Dividend paid	(610)	(532)	
Net movement in holding company cash	(328)	110	
Holding company cash at 1 January	2,230	1,380	
Holding company cash at end of period	1,902	1,490	

Cash remitted by the business units to the corporate centre in the first half of 2014 increased by 15 per cent to £974 million (2013: £844 million on an actual exchange rate basis), with increased contributions from each of our four major business units. Net remittances from Asia were 14 per cent higher at £216 million, reflecting the cash-generative nature of our business growth in the region. As in prior years, Jackson remitted its full year dividend of £352 million in the first half of the year. This remittance represents a new high for Jackson, driven by the strong capital generation in the last year. Remittances from our UK life operations were 9 per cent higher at £246 million. These also have a first half bias as they include the shareholders' share of the UK with-profit transfer of £193 million. M&G's remittance increased 24 per cent to £135 million.

The increases reflect underlying earnings growth and have been supported by our approach to hedging large non-sterling remittances 12 months in advance. Hitherto, this approach has sheltered remittances from Asia and the US from the effects of local currency depreciation relative to sterling, first observed at the start of the second half of 2013. However, the transitory benefit of this approach will unwind going forward. Furthermore, the announcements made by the UK Chancellor in the March Budget and other regulatory developments in the UK, require us to increase the level of investment in our UK pre and post-retirement customer proposition, and this will temper remittances in the short term.

Cash remitted to the Group in the first half of 2014 was used to meet central costs of £155 million (2013: £132 million) and payment of the 2013 final dividend of £610 million (2013: £532 million). In addition, £503 million (US$850 million) of central cash was used to finance the initial up front payment for the renewal of the distribution agreement with Standard Chartered Bank. Total holding company cash at the end of June 2014 was £1.9 billion compared to £2.2 billion at the end of 2013. →

£974m
net cash remittances from business units

15%↑
increase on half year 2013

Chief Financial Officer's report on our 2014 first half financial performance continued

EEV Profits[1]

	Half year 2014 £m	AER Half year 2013 £m	AER Change %	CER Half year 2013 £m	CER Change %
Post-tax operating profit					
Long-term business:					
Asia[2]	**832**	827	1	715	16
US	**777**	707	10	654	19
UK	**388**	304	28	304	28
Long-term business post-tax operating profit[2]	**1,997**	1,838	9	1,673	19
UK general insurance commission	**9**	11	(18)	11	(18)
Asset management business:					
M&G (including Prudential Capital)	**200**	175	14	175	14
Eastspring Investments	**36**	32	13	29	24
US	**(5)**	21	(124)	19	(126)
Other income and expenditure[12]	**(294)**	(256)	(15)	(256)	(15)
Post-tax operating profit based on longer-term investment returns	**1,943**	1,821	7	1,651	18
Short-term fluctuations in investment returns:					
Insurance operations	**452**	(564)	180	(528)	186
Other operations	**(20)**	(23)	13	(23)	13
	432	(587)	174	(551)	178
Effect of changes in economic assumptions	**(368)**	534	(169)	527	(170)
Other non-operating items[12]	**(73)**	156	(147)	161	(145)
Profit for the period attributable to shareholders	**1,934**	1,924	1	1,788	8

Earnings per share

	Half year 2014 pence	AER Half year 2013 pence	AER Change %	CER Half year 2013 pence	CER Change %
Basic earnings per share based on post-tax operating profit	**76.3**	71.5	7	64.8	18
Basic earnings per share based on post-tax total profit	**75.9**	75.5	1	70.2	8

→ As previously announced, from 1 January 2014 the basis of EEV results has been altered to be on a post-tax basis and, accordingly, 2014 half year results and all comparatives are shown on a comparable basis.

EEV operating profit[1]

On an EEV basis, Group post-tax operating profit based on longer-term investment returns was 18 per cent higher (7 per cent on an actual exchange rate basis) at £1,943 million in the first half of 2014. The increase is primarily due to higher profits from the Group's life businesses, which generated new business profit of £1,015 million (up 24 per cent on a constant exchange rate basis or 11 per cent on an actual exchange rate basis) and in-force profit of £982 million[2] (up 15 per cent on a constant exchange rate basis or 6 per cent on an actual exchange rate basis).

In Asia, EEV life operating profit was up 16 per cent to £832 million[2], with in-force profits up 18 per cent to £338 million[2], benefiting from increased scale across all of our operations. Asia new business profit was 15 per cent higher at £494 million, reflecting volume growth from the continued build out of our agency and bancassurance distribution platform, and management actions to improve product mix, geographic mix and pricing. The increase in new business profit continues to be driven by our seven 'sweet spot' markets of South-east Asia (Hong Kong, Indonesia, Singapore, Malaysia, Thailand, the Philippines and Vietnam), which increased their contribution by 15 per cent, despite a broadly unchanged result from Indonesia. Excluding Indonesia, new business profit from the remaining six 'sweet spot' markets was 18 per cent higher, demonstrating the benefits of operating a diverse business platform in the region.

Jackson's EEV life operating profit increased by 19 per cent to £777 million, driven by growth in new business profit, where we continue to see attractive economics. In-force profit increased by 10 per cent compared to the prior half year, reflecting higher unwind from the larger book of existing business and an increased contribution from spread, persistency and mortality experience profits, the result of our disciplined approach to the way we manage and reserve for the risks of this business. US new business profit improved significantly, up 31 per cent to £376 million, reflecting the 18 per cent increase in sales volume and the benefit of Jackson's product and pricing actions in the course of the last 12 months. The 50 basis points reduction in 10-year Treasury yields since the end of 2013 has reversed the positive movement in yields in the second half of 2013, and therefore has no impact on a period-on-period comparison of new business economics.

In the UK, EEV life operating profit of £388 million equates to a 28 per cent increase over the first half of 2013, due to a combination of both higher in-force, and new business profit. Life in-force profit increased to £243 million (2013: £204 million), mainly as a result of the positive impact of a higher unwind driven by the uplift in long-term yields. New business profit increased 45 per cent to £145 million (2013: £100 million), reflecting a contribution of £69 million from four bulk annuity transactions in the first half of 2014 (2013: £nil). In UK retail, new business profit was down 24 per cent at £76 million (2013: £100 million), on lower sales volumes of individual annuities and negative mix effects from lower proportions of higher margin individual annuities.

EEV non-operating profit[1]

EEV operating profit is based on longer-term investment returns and excludes the effect of short-term volatility arising from market movements and the effects of changes from economic assumptions. These items are captured in non-operating profit which reduced the 2014 results by a net £9 million (2013: £103 million increase on an actual exchange rate basis).

EEV short-term fluctuations[1]

Short-term fluctuations in investment returns reflect the element of non-operating profit which relates to the difference between the actual investment returns achieved and those assumed in arriving at the reported operating profit.

Short-term fluctuations in investment returns for insurance operations of positive £452 million include positive £245 million for Asia, positive £95 million for our US operations and positive £112 million in the UK.

In Asia and the UK, positive short-term fluctuations principally reflect unrealised movements on bond holdings in the period. In the US, the favourable impact of market movements on the expected level of future fee income from the variable annuity separate accounts has more than offset the net value movements on derivatives held to manage Group's equity and interest rates exposure.

Effect of changes in economic assumptions[1]

The reduction in long-term yields since the end of 2013 has an adverse impact on the future earnings that we expect to generate from our existing book of business. Once this and other changes in investment market conditions are factored into the EEV calculations they gave rise to a negative movement of £368 million in the first half of 2014 (2013: positive £534 million on an actual exchange rate basis) partly offsetting the effects of short-term fluctuations above.

EEV effective tax rates

In the first half of 2014, the effective tax rate on operating profit based on longer-term investment returns was 26 per cent (2013: 27 per cent) and on the total EEV profit was 22 per cent (2013: 23 per cent). The 2014 effective tax rates reflect the reduction in corporation tax rates in the UK and certain Asia jurisdictions.

£1,943m
EEV operating profit

18%
increase on half year 2013

Capital position, financing and liquidity

Capital position

We continue to operate with a strong solvency position, while maintaining high levels of liquidity and capital generation. At 30 June 2014 our IGD surplus is estimated at £4.1 billion before deducting the 2014 interim dividend, equivalent to available capital covering our capital requirement 2.3 times.

All of our subsidiaries continue to hold strong capital positions on a local regulatory basis. We continue to experience no defaults and modest levels of impairments across our fixed income securities portfolios. Notwithstanding, we have retained our cautious stance on credit risk and have maintained our sizeable £1.9 billion credit default reserves in our UK annuity operations. Further information on our capital and solvency position is provided in the Chief Risk Officer's summary of the risks facing our business and our capital strength.

Solvency II is scheduled to come into effect on 1 January 2016 and we continue to engage with HM Treasury, the Prudential Regulation Authority, industry bodies and our peers to ensure that the final and full requirements of Solvency II are both workable and effective. At full year 2013, we provided our economic capital position based on our Solvency II internal model. This result was based on an assumption of US equivalence, with no restrictions being placed on the economic value of overseas surplus, and the internal model on which these calculations are based has not yet been reviewed or approved by the Prudential Regulation Authority. Other key elements of the basis which are likely to be updated in the future as Solvency II regulations become clearer relate to the liability discount rate for UK annuities, the impact of transitional arrangements and the credit risk adjustment to the risk-free rate. Therefore, the results represent an estimate of our Solvency II capital position, assessed against a draft set of rules, with a number of key working assumptions, and the eventual Solvency II capital position will change as we iterate both the methodology and the internal model to reflect final rules and regulatory feedback.

On this basis at 31 December 2013, our economic capital[13] surplus was estimated at £11.3 billion, which is equivalent to an economic solvency ratio of 257 per cent. We will provide an update, factoring in developments and any PRA feedback, as part of full year 2014 reporting. →

Chief Financial Officer's report on our 2014 first half financial performance continued

Financing and liquidity

Shareholders' net core structural borrowings and ratings

	30 Jun 2014 £m			30 Jun 2013 £m		
	IFRS basis	Mark to market value	EEV basis	IFRS basis	Mark to market value	EEV basis
Shareholders' borrowings in holding company	4,146	452	4,598	3,710	360	4,070
Prudential Capital	275	–	275	275	–	275
Jackson surplus notes	146	41	187	164	25	189
Total	4,567	493	5,060	4,149	385	4,534
Less: Holding company cash and short-term investments	(1,902)	–	(1,902)	(1,490)	–	(1,490)
Net core structural borrowings of shareholder-financed operations	2,665	493	3,158	2,659	385	3,044

→ Our financing and liquidity position remained strong throughout the period. Our central cash resources amounted to £1.9 billion at 30 June 2014, up from £1.5 billion at 30 June 2013, and we currently retain a further £2.5 billion of untapped committed liquidity facilities.

The Group's core structural borrowings at 30 June 2014 were £4,567 million (31 December 2013: £4,636 million on an actual exchange rate basis) on an IFRS basis and comprised £4,146 million (31 December 2013: £4,211 million on an actual exchange rate basis) of debt held by the holding company, and £421 million (31 December 2013: £425 million on an actual exchange rate basis) of debt held by the Group's subsidiaries, Prudential Capital and Jackson.

In addition to its net core structural borrowings of shareholder-financed operations set out above, the Group also has access to funding via the debt capital markets and has in place an unlimited global commercial paper programme. As at 30 June 2014, we had issued commercial paper under this programme totalling £236 million, US$2,305 million, €75 million and AU$10 million to finance non-core borrowings.

Prudential's holding company currently has access to £2.5 billion of syndicated and bilateral committed revolving credit facilities, provided by 18 major international banks, expiring between 2016 and 2019. Apart from small drawdowns to test the process, these facilities have never been drawn, and there were no amounts outstanding at 30 June 2014. The medium term note programme, the commercial paper programme and the committed revolving credit facilities are all available for general corporate purposes and to support the liquidity needs of Prudential's holding company and are intended to maintain a strong and flexible funding capacity.

Prudential manages the Group's core debt within a target level consistent with its current debt ratings. At 30 June 2014, the gearing ratio (debt, net of cash and short-term investments, as a proportion of IFRS shareholders' funds plus net debt) was 20 per cent, compared to 20 per cent at 31 December 2013. Prudential plc has strong debt ratings from Standard & Poor's, Moody's and Fitch. Prudential's long-term senior debt is rated A+, A2 and A from Standard & Poor's, Moody's and Fitch, while short-term ratings are A-1, P-1 and F1 respectively. All ratings on Prudential and its subsidiaries are on stable outlook except PAC, which was placed on negative outlook by Moody's in April 2014 following the pension changes set out in the March 2014 UK budget.

The financial strength of PAC is rated AA by Standard & Poor's, Aa2 by Moody's and AA by Fitch.

Jackson National Life Insurance Company's financial strength is rated AA by Standard & Poor's, A1 by Moody's and AA by Fitch.

Prudential Assurance Co. Singapore (Pte) Ltd.'s (Prudential Singapore) financial strength is rated AA by Standard & Poor's.

Shareholders' funds

	IFRS			EEV		
	Half year 2014 £m	Half year 2013 £m	Full year 2013 £m	Half year 2014 £m	Half year 2013 £m	Full year 2013 £m
Profit after tax for the period	1,145	365	1,346	1,934	1,924	4,358
Exchange movements, net of related tax	(117)	232	(255)	(377)	693	(1,077)
Unrealised gains and losses on Jackson securities classified as available for sale[14]	527	(837)	(1,034)	–	–	–
Dividends	(610)	(532)	(781)	(610)	(532)	(781)
Other	30	38	15	101	(6)	(87)
Net increase (decrease) in shareholders' funds	975	(734)	(709)	1,048	2,079	2,413
Shareholders' funds at beginning of the period	9,650	10,359	10,359	24,856	22,443	22,443
Effect of domestication of Hong Kong branch	–	–	–	(11)	–	–
Shareholders' funds at end of the period	10,625	9,625	9,650	25,893	24,522	24,856
Shareholders' value per share	414p	376p	377p	1,009p	958p	971p
Return on shareholders' funds[15]	24%	21%	23%	16%	16%	19%

During the first half of 2014 the performance of the equity markets in the countries that we operate in has been broadly positive, with US S&P 500 index up 6.1 per cent and the MSCI Asia ex-Japan index higher by 5.5 per cent, while the UK FTSE 100 index was flat. Continued speculation on global growth prospects and the timing of key interest rate decisions has led to some volatility in long-term yields, with most markets experiencing a small decline in 10-year bond yields since the end of 2013. Lower yields generate beneficial value movements on our holdings of fixed income securities which have given rise to positive short-term investment variances in some of our operations.

In addition, the continued appreciation of sterling against most global currencies, referenced earlier in this report, has a negative translational impact on conversion of local balance sheets to sterling.

Taking these non-operating movements into account, the Group's EEV shareholders' funds has increased by 4 per cent during the first half of 2014 to £25.9 billion (31 December 2013: £24.9 billion on an actual exchange rate basis). On a per share basis EEV at 30 June 2014 stood at 1,009 pence, up from 971 pence at 31 December 2013.

Under IFRS, shareholders' funds at 30 June 2014 of £10.6 billion were 9 per cent higher than 31 December 2013 of £9.7 billion (on an actual exchange rate basis), reflecting positive operating results in the period and favourable movements in non-operating items.

£25.9bn
EEV shareholders' funds, equivalent to

1,009p
per share

Corporate transactions

Bancassurance partnership with Standard Chartered PLC

On 12 March 2014, the Group announced that it had entered into an agreement expanding the term and geographic scope of its strategic pan-Asian bancassurance partnership with Standard Chartered PLC. Under the new 15-year agreement, which commenced on 1 July 2014, a wide range of Prudential life insurance products are exclusively distributed through Standard Chartered branches in nine markets – Hong Kong, Singapore, Indonesia, Thailand, Malaysia, the Philippines, Vietnam, India and Taiwan – subject to applicable regulations in each country. In China and South Korea, Standard Chartered will distribute Prudential's life insurance products on a preferred basis. Prudential and Standard Chartered have also agreed to explore additional opportunities to collaborate in due course elsewhere in Asia and in Africa, subject to existing exclusivity arrangements and regulatory restrictions.

As part of this transaction Prudential has agreed to pay Standard Chartered Bank an initial fee of US$1.25 billion which is not dependent on future sales volumes. Of this total, US$850 million was settled in the first half of 2014. The remainder will be paid in two equal instalments of US$200 million each in April 2015 and April 2016. For IFRS and EEV financial reporting purposes the full value of this fee, equivalent to £731 million, has been accounted as an intangible asset. In calculating the Group's IGD surplus, the fee has been written off as no value is attributed to intangible assets under this basis.

Domestication of Hong Kong Branch

On 1 January 2014, the Group completed the process of domestication of the Hong Kong branch of The Prudential Assurance Company Limited. The branch was transferred on 1 January 2014 to two new Hong Kong incorporated Prudential companies, one providing life insurance and the other providing general insurance – Prudential Hong Kong Limited and Prudential General Insurance Hong Kong Limited. On the Prudential Regulation Authority's pillar 1 peak 2 basis £12.1 billion of assets, £12.0 billion of liabilities, net of reinsurers' share (including policyholder asset share liabilities, and £1.2 billion of inherited estate) and £0.1 billion of shareholders' funds (for the excess assets of the transferred non-participating business) have been transferred.

Agreement to sell Japan life business

The Group's closed book life insurance business in Japan, PCA Life Insurance Company Limited, has been classified as held for sale. This classification reflects the expected disposal of the business on which an agreement to sell was reached in July 2013. The sale has yet to be completed.

Acquisition of Express Life of Ghana

In April 2014 we completed the acquisition of Express Life of Ghana for £14 million.

Notes

1 The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis.
2 After Asia development costs.
3 Refer to note B1.1 in IFRS financial statements for the breakdown of other income and expenditure, and other non-operating items.
4 Includes Group's proportionate share of the liabilities and associated flows of the insurance joint ventures in Asia.
5 Defined as movements in shareholder-backed policyholder liabilities arising from premiums (net of charges), surrenders/withdrawals, maturities and deaths.
6 For basis of preparation see note I of Additional IFRS financial information.
7 Includes Group's proportionate share in PPM South Africa and the Asia asset management joint ventures.
8 Net inflows exclude Asia Money Market Fund (MMF) outflows of £52 million (half year 2013: net inflows £107 million). External funds under management exclude Asia MMF balances of £4,300 million (half year 2013: £4,701 million).
9 Free surplus generation represents 'underlying free surplus' based on operating movements, including the general insurance commission earned during the period and excludes market movements, foreign exchange, capital movements, shareholders' other income and expenditure and centrally arising restructuring and Solvency II implementation costs. In addition, following its reclassification as held for sale during 2013, operating results exclude the result of the Japan life insurance business.
10 Payback period, measured on an undiscounted basis, is the time in which the initial 'cash' outflow of investment is expected to be recovered from the 'cash' inflows generated by the investment. The 'cash' outflow is measured by our investment of free surplus in new business sales. The payback period equals the time taken for new business sales to generate free surplus to cover this investment.
11 The detailed holding company cash flow is disclosed in note IV of Additional unaudited IFRS financial information.
12 Refer to the EEV basis supplementary information – Post-tax operating profit based on longer-term investment returns and Post-tax summarised consolidated income statement, for the breakdown of other income and expenditure, and other non-operating items.
13 The methodology and assumptions used in calculating the economic capital results are set out in note II of Additional unaudited financial information in full year 2013 results. The economic solvency ratio is based on the Group's Solvency II internal model which will be subject to Prudential Regulation Authority review and approval before its formal adoption in 2016. We do not expect to submit our Solvency II internal model to the Prudential Regulation Authority for approval until 2015 and therefore these economic capital disclosures should not be interpreted as outputs from an approved internal model.
14 Net of related charges to deferred acquisition costs and tax.
15 Annualised operating profit after tax and non-controlling interests as percentage of opening shareholders' funds.

Group Chief Risk Officer's summary of the risks facing our business and our capital strength

Managing risk to generate value

'As a provider of financial services the management of risk lies at the heart of our business, and effective risk management capabilities represent a key source of competitive advantage for the Group.'

Pierre-Olivier Bouée
Group Chief Risk Officer

We generate shareholder value by selectively taking exposure to risks that are adequately rewarded and that can be appropriately quantified and managed. We retain material risks only where consistent with our risk appetite and risk-taking philosophy, that is: (i) they contribute to value creation; (ii) adverse outcomes can be withstood; and (iii) we have the capabilities, expertise, processes and controls to manage them.

The control procedures and systems established within the Group are designed to manage rather than eliminate the risk of failure to meet business objectives. They can only provide reasonable and not absolute assurance against material misstatement or loss and focus on aligning the levels of risk-taking with the achievement of business objectives.

Group Risk Framework

Our Group Risk Framework describes our approach to risk management, including provisions for risk governance arrangements; our appetite and limits for risk exposures; policies for the management of various risk types; risk culture standards; and risk reporting. It is under this framework that the key arrangements and standards for risk management and internal control that support Prudential's compliance with statutory and regulatory requirements are defined.

Risk governance

Our Group Risk Framework requires that all our businesses and functions establish processes for identifying, evaluating and managing the key risks faced by the Group. The framework is based on the concept of 'three lines of defence' comprising risk taking and management, risk control and oversight and independent assurance.

Primary responsibility for strategy, performance management and risk control lies with the Board, which has established the Group Risk Committee to assist in providing leadership, direction and oversight in respect of the Group's significant risks, and with the Group Chief Executive and the Chief Executives of each of the Group's business units.

Risk taking and the management thereof forms the first line of defence and is facilitated through both the Group Executive Committee and the Balance Sheet and Capital Management Committee.

Risk control and oversight constitutes the second line of defence, and is achieved through the operation of the Group Executive Risk Committee and its sub-committees which monitor and keep risk exposures under regular review. These committees are supported by the Group Chief Risk Officer, with functional oversight provided by Group Risk, Group Compliance and Group Security.

Group Risk has responsibility for establishing and embedding a capital management and risk oversight framework and culture consistent with our risk appetite that protects and enhances the Group's embedded and franchise value. Group Compliance provides verification of compliance with regulatory standards and informs the Board, as well as the Group's management, on key regulatory issues affecting the Group. Group Security is responsible for developing and delivering appropriate security measures with a view to protecting the Group's staff, physical assets and intellectual property.

Risk appetite and limits

The extent to which we are willing to take risk in the pursuit of our objective to create shareholder value is defined by a number of risk appetite statements, operationalised through measures such as limits, triggers and indicators. These appetite statements and measures are approved by the Board on recommendation of the Group Risk Committee and are subject to annual review.

We define and monitor aggregate risk limits based on financial and non-financial stresses for our earnings volatility, liquidity and capital requirements as follows:

Earnings volatility: the objectives of the limits are to ensure that:

a The volatility of earnings is consistent with the expectations of stakeholders;
b The Group has adequate earnings (and cash flows) to service debt, expected dividends and to withstand unexpected shocks; and
c Earnings (and cash flows) are managed properly across geographies and are consistent with funding strategies.

The two measures used to monitor the volatility of earnings are EEV operating profit and IFRS operating profit, although EEV and IFRS total profits are also considered.

Liquidity: the objective is to ensure that the Group is able to generate sufficient cash resources to meet financial obligations as they fall due in business as usual and stressed scenarios.

Capital requirements: the limits aim to ensure that:

a The Group meets its internal economic capital requirements;
b The Group achieves its desired target rating to meet its business objectives; and
c Supervisory intervention is avoided.

The two measures used are the EU Insurance Groups Directive (IGD) capital requirements and internal economic capital requirements.

In addition, capital requirements are monitored on both local statutory and future Solvency II regulatory bases.

We also define risk appetite statements and measures (ie limits, triggers, indicators) for the major constituents of each risk type as categorised and defined in the Group Risk Framework, where appropriate. These appetite statements and measures cover the most significant exposures to the Group, particularly those that could impact our aggregate risk limits. The Group Risk Framework risk categorisation is shown in the table below.

Our risk appetite framework forms an integral part of our annual business planning cycle. The Group Risk Committee is responsible for reviewing the risks inherent in the Group's business plan and for providing the Board with input on the risk/reward trade-offs implicit therein. This review is supported by the Group Risk function, which uses submissions by business units to calculate the Group's aggregated position (allowing for diversification effects between business units) relative to the aggregate risk limits.

Risk policies

Risk policies set out specific requirements for the management of, and articulate the risk appetite for, key risk types. There are policies for credit, market, insurance, liquidity, operational and tax risk, as well as dealing controls. They form part of the Group Governance Manual, which was developed to make a key contribution to the sound system of internal control that we are expected to maintain under the UK Corporate Governance Code and the Hong Kong Code on Corporate Governance Practices. Group Head Office and business units confirm that they have implemented the necessary controls to evidence compliance with the Group Governance Manual. →

Group Risk Framework risk categorisation

Category	Risk type	Definition
Financial risks	Market risk	The risk of loss for the Group's business, or of adverse change in the financial situation, resulting, directly or indirectly, from fluctuations in the level or volatility of market prices of assets and liabilities.
	Credit risk	The risk of loss for the Group's business or of adverse change in the financial position, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors in the form of default or other significant credit event (eg downgrade or spread widening).
	Insurance risk	The risk of loss for the Group's business or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of a number of insurance risk drivers. This includes adverse mortality, longevity, morbidity, persistency and expense experience.
	Liquidity risk	The risk of the Group being unable to generate sufficient cash resources or to meet financial obligations as they fall due in business as usual and stress scenarios.
Non-financial risks	Operational risk	The risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events other than those covered by business environment risk.
	Business environment risk	Exposure to forces in the external environment that could significantly change the fundamentals that drive the business's overall strategy.
	Strategic risk	Ineffective, inefficient or inadequate senior management processes for the development and implementation of business strategy in relation to the business environment and the Group's capabilities.

Group Chief Risk Officer's summary of the risks facing our business and our capital strength continued

Risk culture

We work to promote a responsible risk culture in three main ways:

a By the leadership and behaviours demonstrated by management;
b By building skills and capabilities to support management; and
c By including risk management (through the balance of risk with profitability and growth) in the performance evaluation of individuals.

The remuneration strategy at Prudential is designed to be consistent with its risk appetite, and the Group Chief Risk Officer advises the Group Remuneration Committee on adherence to our risk framework and appetite.

Risk reporting

An annual 'top-down' identification of our top risks assesses the risks that have the greatest potential to impact the Group's operating results and financial condition. The management information received by the Group Risk Committees and the Board is tailored around these risks, and it also covers ongoing developments in other key and emerging risks. A discussion of the key risks, including how they affect our operations and how they are managed, follows below.

Key risks

Market risk

(i) Investment risk

In Prudential UK investment risk arising on the assets in the with-profits fund impacts the shareholders' interest in future transfers and is driven predominantly by equities in the fund as well as by other investments such as property and bonds. The fund's large inherited estate – estimated at £7.5 billion as at 30 June 2014 (1 January 2014: £6.8 billion, after the domestication of Hong Kong business) – can absorb market fluctuations and protect the fund's solvency. The inherited estate is partially protected against falls in equity markets through an active hedging policy.

In Asia, our shareholder exposure to equities relates to revenue from unit-linked products and, from a capital perspective, to the effect of falling equity markets on its with-profits businesses.

In Jackson, investment risk arises in relation to the assets backing the policies. In the case of the 'spread business', including fixed annuities, these assets are generally bonds. For variable annuities business, these assets include equities as well as other assets such as bonds. In this case the impact on the shareholder comes from value of future mortality and expense fees, and additionally from guarantees embedded in variable annuity products. Shareholders' exposure to these guarantees is mitigated through a hedging programme, as well as reinsurance. Further measures have been undertaken including re-pricing initiatives and the introduction of variable annuities without guarantees. Furthermore, it is our philosophy not to compete on price; rather, we seek to sell at a price sufficient to fund the cost incurred to hedge or reinsure the risks and to achieve an acceptable return.

The Jackson IFRS shareholders' equity and US statutory capital are sensitive to the effects of policyholder behaviour on the valuation of GMWB guarantees. Jackson hedges the guarantees on its variable annuity book on an economic basis and, thus, accepts variability in its accounting results in the short term in order to achieve the appropriate economic result. In particular, under Prudential's Group IFRS reporting, the measurement of the Jackson variable annuity guarantees is typically less sensitive to market movements than the corresponding hedging derivatives, which are held at market value. However, depending on the level of hedging conducted regarding a particular risk type, certain market movements can drive volatility in the economic result which may be less significant under IFRS reporting or vice versa as discussed above.

(ii) Interest rate risk

Long-term rates have declined over recent periods in many markets, falling to historic lows. Products that we write are sensitive to movements in interest rates, and while we have already taken a number of actions to de-risk the in-force business as well as re-price and restructure new business offerings in response to historically low interest rates, persistently low rates may impact policyholders' savings patterns and behaviour.

Interest rate risk arises in our UK business from the need to match cash flows for annuity payments with those from investments; movements in interest rates may have an impact on profits where durations are not perfectly matched. As a result, we aim to match the duration of assets and liabilities as closely as possible and the position is monitored regularly. The with-profits business is exposed to interest rate risk as a result of underlying guarantees. Such risk is largely borne by the with-profits fund but shareholder support may be required in extremis.

In Asia, exposure to interest rate risk arises from the guarantees of some non-unit-linked investment products. This exposure arises because it may not be possible to hold assets which will provide cash flows to match exactly those relating to policyholder liabilities. While this residual asset/liability mismatch risk can be managed, it cannot be eliminated.

Jackson is exposed to interest rate risk in its fixed, fixed index and variable annuity books. Movements in interest rates can influence the cost of guarantees in such products, in particular the cost of guarantees may increase when interest rates fall. Interest rate risk across the entire business is managed through the use of interest rate swaps and interest rate options.

(iii) Foreign exchange risk

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

We retain revenues locally to support the growth of our business and capital is held in the local currency of the business to meet local regulatory and market requirements, accepting the balance sheet translation risks this can produce. However, in cases where a surplus arising in an overseas operation supports Group capital or where a significant cash remittance is due from an overseas subsidiary to the Group, this exposure is hedged where we believe it is economically optimal to do so. We do not have appetite for significant shareholder exposures to foreign exchange risks in currencies outside the local territory. Currency borrowings, swaps and other derivatives are used to manage exposures.

Credit risk

We invest in fixed income assets in order to match policyholder liabilities and enter into reinsurance and derivative contracts to mitigate various types of risk. As a result, we are exposed to credit and counterparty credit risk across our business. We employ a number of risk management tools to manage credit risk, including limits defined on an issuer/counterparty basis as well as on average credit quality, and collateral arrangements in derivative transactions. The Group Credit Risk Committee oversees credit and counterparty credit risk across the Group.

(i) Debt and loan portfolio

Our UK business is primarily exposed to credit risk in the shareholder-backed portfolio, where fixed income assets represent 35 per cent or £28.8 billion of our exposure. Credit risk arising from

£45.4 billion of fixed income assets is largely borne by the with-profits fund, although shareholder support may be required should the with-profits fund become unable to meet its liabilities.

The debt portfolio of our Asia business totalled £20.0 billion at 30 June 2014. Of this, approximately 66 per cent was in unit-linked and with-profits funds with minimal shareholders' risk. The remaining 34 per cent is shareholder exposure.

Credit risk arises in the general account of our US business, where £30.6 billion of fixed income assets back shareholder liabilities including those arising from fixed annuities, fixed index annuities and life insurance. Included in the portfolio are £2.2 billion of commercial mortgage-backed securities and £1.6 billion of residential mortgage-backed securities, of which £0.8 billion (52 per cent) are issued by agencies sponsored by the US government.

The shareholder-owned debt and loan portfolio of the Group's asset management operations of £2.0 billion as at 30 June 2014 is principally related to Prudential Capital operations. Prudential Capital generates revenue by providing bridging finance, managing investments and operating a securities lending and cash management business for the Prudential Group and our clients.

Further details of the composition and quality of our debt portfolio, and exposure to loans, can be found in the IFRS financial statements.

(ii) Group sovereign debt and bank debt exposure

Sovereign debt[1] represented 15 per cent or £10.4 billion of the debt portfolio backing shareholder business at 30 June 2014 (31 December 2013: 15 per cent or £10 billion). 42 per cent of this was rated AAA and 91 per cent investment grade (31 December 2013: 44 per cent AAA, 92 per cent investment grade). At 30 June 2014, the Group's shareholder-backed business's holding in continental Europe sovereign debt[1] was £483 million. 74 per cent of this was AAA rated (31 December 2013: 78 per cent AAA rated). Shareholder exposure to the Eurozone sovereigns of Italy and Spain is £59 million (31 December 2013: £54 million). We do not have any sovereign debt exposure to Greece, Cyprus, Portugal or Ireland.

Our bank exposure is a function of our core investment business, as well as of the hedging and other activities undertaken to manage our various financial risks. Given the importance of our relationship with our banks, exposure to the banking sector is a key focus of management information provided to the Group's risk committees and the Board.

The exposures held by the shareholder-backed business and with-profits funds in sovereign debt and bank debt securities at 30 June 2014 are given in Note C3.3(f) of the Group's IFRS financial statements.

(iii) Counterparty credit risk

We enter into a variety of exchange traded and over-the-counter derivative financial instruments, including futures, options, forward currency contracts and swaps such as interest rate swaps, inflation swaps, cross-currency swaps, swaptions and credit default swaps.

All over-the-counter derivative transactions, with the exception of some Asia transactions, are conducted under standardised International Swaps and Derivatives Association Inc master agreements and we have collateral agreements between the individual Group entities and relevant counterparties in place under each of these master agreements.

Our exposure to derivative counterparty and reinsurance counterparty credit risk is managed using an array of risk management tools, including a comprehensive system of limits. Where appropriate, we reduce our exposure, purchase credit protection or make use of additional collateral arrangements to control our levels of counterparty credit risk.

Insurance risk

The processes of determining the price of our products and reporting the results of our long-term business operations require us to make a number of assumptions. In common with other industry players, the profitability of our businesses depends on a mix of factors including mortality and morbidity levels and trends, persistency, investment performance, unit cost of administration and new business acquisition expenses.

We continue to conduct research into longevity risk using data from our substantial annuity portfolio. The assumptions that we make about future expected levels of mortality are particularly relevant in our UK annuity business. The attractiveness of transferring longevity risk (via reinsurance and other external solutions) is regularly evaluated. These are used as risk management tools where it is appropriate and attractive to do so.

Morbidity risk is mitigated by appropriate underwriting and use of reinsurance. Our morbidity assumptions reflect our recent experience and expectation of future trends for each relevant line of business.

Our persistency assumptions reflect recent experience for each relevant line of business, and any expectations of future persistency. Persistency risk is mitigated by appropriate training and sales processes and managed proactively post sale. Where appropriate, allowance is also made for the relationship – either assumed or historically observed – between persistency and investment returns, and for the resulting additional risk.

Liquidity risk

Our parent company has significant internal sources of liquidity which are sufficient to meet all of its expected requirements for the foreseeable future without having to make use of external funding. In aggregate the Group currently has £2.5 billion of undrawn committed facilities, expiring between 2016 and 2019. In addition, the Group has access to liquidity via the debt capital markets. We also have in place an unlimited commercial paper programme and have maintained a consistent presence as an issuer in this market for the last decade. Liquidity uses and sources have been assessed at the Group and at a business unit level under base case and stressed assumptions. The liquidity resources available and the subsequent Liquidity Coverage Ratio are regularly monitored and we have assessed these to be sufficient.

Operational risk

We are exposed to operational risk through the course of running our business. We are dependent on the successful processing of a large number of transactions, utilising various legacy and other IT systems and platforms, across numerous and diverse products. We also operate under the ever evolving requirements set out by different regulatory and legal regimes (including tax), as well as utilising a significant number of third parties to distribute products and to support business operations.

Our IT, compliance and other operational systems and processes incorporate controls that are designed to manage and mitigate the operational risks associated with our activities. Although we have not experienced a material failure or breach in relation to our legacy and other IT systems and processes to date, we have been, and likely will continue to be, subject to computer viruses, attempts at unauthorised access and cyber security attacks.

We have an operational risk management framework in place that facilitates both the qualitative and quantitative analysis of operational risk exposures. The output of this framework, in particular management information on key operational risk and control assessments, scenario analysis, internal incidents and external incidents, is reported by the business units and →

Group Chief Risk Officer's summary of the risks facing our business and our capital strength continued

presented to the Group Operational Risk Committee. This information also supports business decision-making and lessons-learned activities, the ongoing improvement of the control environment, and determination of the adequacy of our corporate insurance programme.

Global regulatory risk

Global regulatory risk is considered a key risk and is classified as a business environment risk under the Group Risk framework risk categorisation.

The European Union (EU) has developed a new prudential regulatory framework for insurance companies, referred to as Solvency II. The Solvency II Directive, which sets out the new framework, was formally approved by the Economic and Financial Affairs Council in November 2009 although its implementation was delayed pending agreement on a directive known as Omnibus II which, having been adopted by the Council of the European Union in April 2014, amended certain aspects of the Solvency II Directive. The new approach is based on the concept of three pillars – minimum capital requirements, supervisory review of firms' assessments of risk, and enhanced disclosure requirements.

Specifically, Pillar 1 covers the quantitative requirements around own funds, valuation rules for assets and liabilities and capital requirements. Pillar 2 provides the qualitative requirements for risk management, governance and controls, including the requirement for insurers to submit an Own Risk and Solvency Assessment which will be used by the regulator as part of the supervisory review process. Pillar 3 deals with the enhanced requirements for supervisory reporting and public disclosure.

A key aspect of Solvency II is that the assessment of risks and capital requirements are intended to be aligned more closely with economic capital methodologies and may allow us to make use of our internal economic capital models if approved by the Prudential Regulation Authority.

Following adoption of the Omnibus II Directive, Solvency II is now expected to be implemented as of 1 January 2016, although the European Commission and the European Insurance and Occupational Pensions Authority (EIOPA) are continuing to develop the detailed rules that will supplement the high-level rules and principles of the Solvency II and Omnibus II Directives, which are not currently expected to be finalised until mid-2015.

There is significant uncertainty regarding the final outcome from this process. In particular, certain detailed aspects of the Solvency II rules relating to the determination of the liability discount rate for UK annuity business remain to be clarified and our capital position is sensitive to these outcomes. Further, the effective application of a number of key measures incorporated in the Omnibus II Directive, including the provisions for third-country equivalence, are expected to be subject to supervisory judgement and approval. There is a risk that the effect of the measures finally adopted could be adverse for us, including potentially a significant increase in the capital required to support our business and that we may be placed at a competitive disadvantage to other European and non-European financial services groups. We are actively participating in shaping the outcome through our involvement in industry bodies and trade associations, including the Pan-European Insurance Forum, Chief Risk Officer Forum and Chief Financial Officer Forum, together with the Association of British Insurers and Insurance Europe.

Having assessed the requirements of Solvency II, an implementation programme was initiated with dedicated teams to manage the required work across the Group. The activity of the local Solvency II teams is coordinated centrally to achieve consistency in the understanding and application of the requirements. We are continuing our preparations to adopt the regime when it comes into force on 1 January 2016 and are undertaking in parallel an evaluation of the possible actions to mitigate its effects. We regularly review our range of options to maximise the strategic flexibility of the Group. This includes consideration of optimising our domicile as a possible response to an adverse outcome on Solvency II.

Over the coming months we will remain in regular contact with the Prudential Regulation Authority as we continue to engage in the 'pre-application' stage of the approval process for the internal model. In addition, we are engaged in the Prudential Regulation Authority's 'Individual Capital Adequacy Standards Plus (ICAS+)' regime, which is enabling our UK insurance entities to leverage the developments made in relation to the Solvency II internal model for the purpose of meeting the existing ICAS regime.

Currently there are also a number of other global regulatory developments which could impact the way in which we are supervised in our many jurisdictions. These include the Dodd-Frank Act in the US, the work of the Financial Stability Board on Global Systemically Important Insurers (G-SIIs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) being developed by the International Association of Insurance Supervisors (IAIS).

The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry within the United States that, among other reforms to financial services entities, products and markets, may subject financial institutions designated as systemically important to heightened prudential and other requirements intended to prevent or mitigate the impact of future disruptions in the US financial system. The full impact of the Dodd-Frank Act on our businesses is not currently clear. However, many of its provisions have a delayed effectiveness and/or require rulemaking or other actions by various US regulators over the coming years.

In July 2013 the FSB announced the initial list of nine insurance groups that have been designated as G-SIIs. This list included Prudential as well as a number of its competitors. Designation as a G-SII will lead to additional policy measures being applied to the designated group. Based on the policy framework released by the IAIS and subsequent guidance papers these additional policy measures will include enhanced group-wide supervision, effective resolution measures of the group in the event of failure, loss absorption and higher loss absorption capacity. This enhanced supervision commenced immediately and includes the development by July 2014 of a Systemic Risk Management Plan (SRMP) under supervisory oversight and its implementation thereafter and by the end of 2014, a group Recovery and Resolution Plan (RRP) and Liquidity Risk Management Plan (LRMP). The Group SRMP was submitted to the Prudential Regulatory Authority (PRA) in June 2014 and work is ongoing to produce the RRP and LRMP. We are monitoring the development and the potential impact of, the framework of policy measures and are engaging with the PRA on the implications of the policy measures and Prudential's designation as a G-SII. The G-SII regime also introduces two types of capital requirements, the first, a Basic Capital Requirement (BCR), designed to act as a minimum group capital requirement and the second, a Higher Loss Absorption (HLA) requirement for conducting non-traditional insurance and non-insurance activities. A consultation paper on BCR was released in July 2014. Details of the HLA are currently unknown as the IAIS has yet to begin work on this requirement. The IAIS currently expects to finalise the BCR and HLA proposals by November 2014 and the end of 2015 respectively. Implementation of the regime is likely to be phased in over a period of years with the BCR expected to be introduced in 2015 on a confidential reporting basis to group-wide supervisors.

The HLA requirement will apply from January 2019 to the insurance groups identified as G-SIIs in November 2017.

The IAIS is developing a common framework ('ComFrame') for the supervision of Internationally Active Insurance Groups (IAIG). ComFrame is designed to outline a set of common global principles and standards for group supervision and may increase the focus of regulators in some jurisdictions. One of the framework's key components is an Insurance Capital Standard (ICS), which would form the group solvency capital standard under ComFrame. In May 2014 the IAIS published a memorandum setting out the approach to the development of the ICS. The three-year development phase of ComFrame ended in December 2013 and the IAIS is now undertaking a field testing exercise from 2014-2018 to assess the impacts of the quantitative and qualitative requirements proposed under ComFrame. ComFrame is expected to be implemented in 2019.

Risk factors

Our disclosures covering risk factors can be found at the end of this document.

Risk mitigation and hedging

We manage our actual risk profile against our tolerance of risk. To do this, we maintain risk registers that include details of the risks we have identified and of the controls and mitigating actions we employ in managing them. Any mitigation strategies involving large transactions such as a material derivative transaction involving shareholder business are subject to review at Group level before implementation.

We use a range of risk management and mitigation strategies. The most important of these include: adjusting asset portfolios to reduce investment risks (such as duration mismatches or overweight counterparty exposures); using derivatives to hedge market risks; implementing reinsurance programmes to manage insurance risk; implementing corporate insurance programmes to limit the impact of operational risks; and revising business plans where appropriate.

Capital management

We continue to operate with a strong solvency position, while maintaining high levels of liquidity and capital generation. This is testament to our capital discipline, the effectiveness of our hedging activities, our low direct Eurozone exposure, the minimal level of credit impairments and the natural offsets in our portfolio of businesses which dampen the effects of movements in interest rates.

Regulatory capital (IGD)

Prudential is subject to the capital adequacy requirements of the European Union Insurance Groups Directive (IGD) as implemented by the Prudential Regulation Authority in the UK. The IGD capital surplus represents the aggregated surplus capital (on a Prudential Regulation Authority consistent basis) of the Group's regulated subsidiaries less the Group's borrowings. No diversification benefit is recognised. We estimate that our IGD capital surplus is £4.1 billion at 30 June 2014 (before taking into account the 2014 interim dividend), with available capital covering our capital requirements 2.3 times. This compares to a capital surplus of £5.1 billion at the end of 2013 (before taking into account the 2013 final dividend).

The movements in the first half of 2014 mainly comprise:

- Net capital generation (net of market and foreign exchange movements) mainly through operating earnings (in-force releases less investment in new business, net of tax) of £0.8 billion;

offset by:

- The cost of renewing the bancassurance partnership agreement with Standard Chartered PLC of £0.7 billion, representing the aggregate amounts settled and committed that are not dependent on the achievements of sales volumes;
- £0.2 billion due to reduction in the shareholders' interest in future transfers from the UK's with-profits fund asset allowance (as discussed below) and other smaller one-off items;
- Final 2013 dividend of £0.6 billion; and
- External financing costs and other central costs, net of tax, of £0.3 billion

£4.1bn
estimated IGD capital surplus covering capital requirements

2.3
times

IGD surplus represents the accumulation of surpluses across all of our operations based on local regulatory minimum capital requirements with some adjustments, pursuant to the requirements of Solvency I. The calculation does not fully adjust capital requirements for risk nor does it capture the true economic value of assets. Global regulatory developments, such as Solvency II and ComFrame, aim to ensure that the calculation of regulatory surplus evolves over time into a more meaningful risk sensitive measure.

There is broad agreement that ultimately it would be beneficial to replace the IGD regime with a regime that is more risk-based. Solvency II aims to provide such a framework and is expected to be implemented on 1 January 2016.

We continue to have further options available to manage available and required capital. These could take the form of increasing available capital (for example, through financial reinsurance) or reducing required capital (for example, through the mix and level of new business) and the use of other risk mitigation measures such as hedging and reinsurance. A number of such options were utilised through the last financial crisis in 2008 and 2009 to enhance the Group's IGD surplus. One such arrangement allowed the Group to recognise a proportion of the shareholders' interest in future transfers (SHIFT) from the UK's with-profits business and this remained in place, contributing £0.4 billion to the IGD at 31 December 2012. As per guidance received from the PRA in January 2013, credit taken for the SHIFT asset was reduced to zero at end January 2014.

Stress testing

As at 30 June 2014, stress testing of our IGD capital position to various events has the following results:

- An instantaneous 20 per cent fall in equity markets from 30 June 2014 levels would reduce the IGD surplus by £50 million;
- A 40 per cent fall in equity markets (comprising an instantaneous 20 per cent fall followed by a further 20 per cent fall over a four-week period) would reduce the IGD surplus by £350 million;
- A 100 basis points reduction (subject to a floor of zero) in interest rates would reduce the IGD surplus by £100 million; and
- Credit defaults of 10 times the expected level would reduce IGD surplus by £550 million.

The impact of the 100 basis points reduction in interest rates is →

Group Chief Risk Officer's summary of the risks facing our business and our capital strength continued

→ exacerbated by the current regulatory permitted practice used by Jackson, which values all interest rate swaps at book value rather than fair value for regulatory purposes. At 30 June 2014, removing the permitted practice would have increased reported IGD surplus to £4.2 billion. As at 30 June 2014, it is estimated that a 100 basis point reduction in interest rates (subject to a floor of zero) would have resulted in an IGD surplus of £4.4 billion, excluding the permitted practice.

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

Other capital metrics

We use an economic capital assessment calibrated on a multi-term basis to monitor our capital requirements across the Group. This approach considers, by risk drivers, the time frame over which each risk can threaten the ability of the Group to meet claims as they fall due, allowing for realistic diversification benefits. This assessment provides valuable insights into our risk profile and for continuing to maintain a strong capital position.

All of our subsidiaries continue to hold strong capital positions on a local regulatory basis. Jackson's risk-based capital ratio level as of 31 December 2013 was 450 per cent and since then it has been able to remit £352 million to the Group while supporting its balance sheet growth and maintaining adequate capital. The value of the estate of our UK with-profits fund as at 30 June 2014 is estimated at £7.5 billion after the effect of completing the domestication of the Hong Kong branch business of the PAC with-profits fund which was effective on 1 January 2014 (1 January 2014: £6.8 billion, after the effect of the transfer). The value of the shareholders' interest in future transfers from the with-profits funds in the UK is estimated at £2.4 billion (1 January 2014: £2.3 billion, after the effect of the transfer).

Furthermore, on a statutory (Pillar 1) basis the total credit default reserve for the UK shareholder annuity funds also contributes to protecting our capital position in excess of the IGD surplus. Notwithstanding the absence of defaults in the period, at 30 June 2014 we have maintained sizeable credit default reserves at £1.9 billion (31 December 2013: £1.9 billion), representing 51 per cent of the portfolio spread over swaps, compared with 47 per cent at 31 December 2013.

Capital allocation

Our approach to capital allocation is to attain a balance between risk and return, investing in those businesses that create shareholder value. In order to efficiently allocate capital, we measure the use of, and the return on, capital.

We use a variety of metrics for measuring capital performance and profitability, including traditional accounting metrics and economic returns. Capital allocation decisions are supported by this quantitative analysis, as well as strategic considerations.

The economic framework measures risk adjusted returns on economic capital, a methodology that ensures meaningful comparison across the Group. Capital utilisation, return on capital and new business value creation are measured at the product level as part of the business planning process.

Note

1 Excludes Group's proportionate share in Joint Ventures and unit-linked assets and holdings of consolidated unit trusts and similar funds.

Section 3

International Financial Reporting Standards (IFRS) basis results

3

Index to Group IFRS financial results

International Financial Reporting Standards (IFRS) basis results

Notes

A: Background

B: Earnings performance

C: Balance sheet notes

D: Other notes

Condensed consolidated income statement

	Note	2014 £m Half year	2013 £m Half year	2013 £m Full year
Earned premiums, net of reinsurance		**16,189**	14,763	29,844
Investment return		**13,379**	6,528	20,347
Other income		**1,059**	1,100	2,184
Total revenue, net of reinsurance		**30,627**	22,391	52,375
Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance		**(25,549)**	(18,143)	(43,154)
Acquisition costs and other expenditure	B3	**(3,336)**	(3,315)	(6,861)
Finance costs: interest on core structural borrowings of shareholder-financed operations		**(170)**	(152)	(305)
Remeasurement of carrying value of Japan life business classified as held for sale	D1	**(11)**	(135)	(120)
Total charges, net of reinsurance		**(29,066)**	(21,745)	(50,440)
Share of profits from joint ventures and associates, net of related tax		**147**	74	147
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)**		**1,708**	720	2,082
Less tax charge attributable to policyholders' returns		**(284)**	(214)	(447)
Profit before tax attributable to shareholders	B1.1	**1,424**	506	1,635
Total tax charge attributable to policyholders and shareholders	B5	**(563)**	(355)	(736)
Adjustment to remove tax charge attributable to policyholders' returns		**284**	214	447
Tax charge attributable to shareholders' returns	B5	**(279)**	(141)	(289)
Profit for the period attributable to equity holders of the Company		**1,145**	365	1,346
Earnings per share (in pence)				
Based on profit attributable to the equity holders of the Company:	B6			
Basic		**45.0p**	14.3p	52.8p
Diluted		**44.9p**	14.3p	52.7p
Dividends per share (in pence)				
Dividends relating to reporting period:	B7			
Interim dividend (2014 and 2013)		**11.19p**	9.73p	9.73p
Final dividend (2013)		**–**	–	23.84p
Total		**11.19p**	9.73p	33.57p
Dividends declared and paid in reporting period:	B7			
Current year interim dividend		**–**	–	9.73p
Final dividend for prior year		**23.84p**	20.79p	20.79p
Total		**23.84p**	20.79p	30.52p

* This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders. This is principally because the corporate taxes of the Group include those on the income of consolidated with-profits and unit-linked funds that, through adjustments to benefits, are borne by policyholders. These amounts are required to be included in the tax charge of the Company under IAS 12. Consequently, the profit before all taxes measure (which is determined after deducting the cost of policyholder benefits and movements in the liability for unallocated surplus of the PAC with-profits fund after adjusting for taxes borne by policyholders) is not representative of pre-tax profits attributable to shareholders.

Condensed consolidated statement of comprehensive income

	Note	2014 £m	2013 £m	
		Half year	Half year	Full year
Profit for the period		1,145	365	1,346
Other comprehensive income:				
Items that may be reclassified subsequently to profit or loss				
Exchange movements on foreign operations and net investment hedges:				
Gross		(115)	227	(255)
Related tax		(2)	5	–
		(117)	232	(255)
Net unrealised valuation movements on securities of US insurance operations classified as available-for-sale:				
Net unrealised holding gains (losses) arising during the period		1,060	(1,665)	(2,025)
Net gains included in the income statement on disposal and impairment		(37)	(42)	(64)
Total	C3.3(b)	1,023	(1,707)	(2,089)
Related change in amortisation of deferred acquisition costs	C5.1(b)	(212)	419	498
Related tax		(284)	451	557
		527	(837)	(1,034)
Total		410	(605)	(1,289)
Items that will not be reclassified to profit or loss				
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes:				
Gross		12	(28)	(62)
Related tax		(2)	7	14
		10	(21)	(48)
Other comprehensive income (loss) for the period, net of related tax		420	(626)	(1,337)
Total comprehensive income (loss) for the period attributable to the equity holders of the Company		1,565	(261)	9

Condensed consolidated statement of changes in equity

		Period ended 30 June 2014 £m							
	Note	Share capital note C9	Share premium note C9	Retained earnings	Translation reserve	Available-for-sale securities reserves	Share-holders' equity	Non-controlling interests	Total equity
Reserves									
Profit for the period		–	–	1,145	–	–	1,145	–	1,145
Other comprehensive income (loss)		–	–	10	(117)	527	420		420
Total comprehensive income (loss) for the period		–	–	1,155	(117)	527	1,565	–	1,565
Dividends	B7	–	–	(610)	–	–	(610)	–	(610)
Reserve movements in respect of share-based payments		–	–	52	–	–	52	–	52
Share capital and share premium									
New share capital subscribed	C9	–	8	–	–	–	8	–	8
Treasury shares									
Movement in own shares in respect of share-based payment plans		–	–	(34)	–	–	(34)	–	(34)
Movement in own shares purchased by unit trusts consolidated under IFRS		–	–	(6)	–	–	(6)	–	(6)
Net increase (decrease) in equity		–	8	557	(117)	527	975	–	975
At beginning of period		128	1,895	7,425	(189)	391	9,650	1	9,651
At end of period		128	1,903	7,982	(306)	918	10,625	1	10,626

Condensed consolidated statement of changes in equity continued

	Note	Share capital note C9	Share premium note C9	Retained earnings	Translation reserve	Available-for-sale securities reserves	Share-holders' equity	Non-controlling interests	Total equity
		Period ended 30 June 2013 £m							
Reserves									
Profit for the period		–	–	365	–	–	365	–	365
Other comprehensive (loss) income		–	–	(21)	232	(837)	(626)	–	(626)
Total comprehensive income (loss) for the period		–	–	344	232	(837)	(261)	–	(261)
Dividends	B7	–	–	(532)	–		(532)	–	(532)
Reserve movements in respect of share-based payments		–	–	31	–	–	31	–	31
Change in non-controlling interests		–	–	–	–	–	–	1	1
Share capital and share premium									
New share capital subscribed	C9	–	1	–	–	–	1	–	1
Treasury shares									
Movement in own shares in respect of share-based payment plans		–	–	25	–	–	25	–	25
Movement in own shares purchased by unit trusts consolidated under IFRS		–	–	2	–	–	2	–	2
Net increase (decrease) in equity		–	1	(130)	232	(837)	(734)	1	(733)
At beginning of period		128	1,889	6,851	66	1,425	10,359	5	10,364
At end of period		128	1,890	6,721	298	588	9,625	6	9,631

	Note	Share capital note C9	Share premium note C9	Retained earnings	Translation reserve	Available-for-sale securities reserves	Share-holders' equity	Non-controlling interests	Total equity
		Year ended 31 December 2013 £m							
Reserves									
Profit for the year		–	–	1,346	–	–	1,346	–	1,346
Other comprehensive loss		–	–	(48)	(255)	(1,034)	(1,337)	–	(1,337)
Total comprehensive income (loss) for the year		–	–	1,298	(255)	(1,034)	9	–	9
Dividends	B7	–	–	(781)	–	–	(781)	–	(781)
Reserve movements in respect of share-based payments		–	–	98	–	–	98	–	98
Change in non-controlling interests		–	–	–	–	–	–	(4)	(4)
Share capital and share premium									
New share capital subscribed	C9	–	6	–	–	–	6	–	6
Treasury shares									
Movement in own shares in respect of share-based payment plans		–	–	(10)	–	–	(10)	–	(10)
Movement in own shares purchased by unit trusts consolidated under IFRS		–	–	(31)	–	–	(31)	–	(31)
Net increase (decrease) in equity		–	6	574	(255)	(1,034)	(709)	(4)	(713)
At beginning of year		128	1,889	6,851	66	1,425	10,359	5	10,364
At end of year		128	1,895	7,425	(189)	391	9,650	1	9,651

Condensed consolidated statement of financial position
Assets

	Note	2014 £m	2013 £m	
		30 Jun	30 Jun	31 Dec
Intangible assets attributable to shareholders:				
Goodwill	C5.1(a)	**1,458**	1,474	1,461
Deferred acquisition costs and other intangible assets	C5.1(b)	**5,944**	5,538	5,295
Total		**7,402**	7,012	6,756
Intangible assets attributable to with-profits funds:				
Goodwill in respect of acquired subsidiaries for venture fund and other investment purposes		**177**	178	177
Deferred acquisition costs and other intangible assets		**63**	79	72
Total		**240**	257	249
Total intangible assets		**7,642**	7,269	7,005
Other non-investment and non-cash assets:				
Property, plant and equipment		**910**	868	920
Reinsurers' share of insurance contract liabilities		**6,743**	7,204	6,838
Deferred tax assets	C7.1	**2,173**	2,637	2,412
Current tax recoverable		**158**	191	244
Accrued investment income		**2,413**	2,726	2,609
Other debtors		**3,643**	2,318	1,746
Total		**16,040**	15,944	14,769
Investments of long-term business and other operations:				
Investment properties		**11,754**	10,583	11,477
Investment in joint ventures and associates accounted for using the equity method		**911**	696	809
Financial investments*:				
Loans	C3.4	**12,457**	13,230	12,566
Equity securities and portfolio holdings in unit trusts		**130,566**	112,258	120,222
Debt securities	C3.3	**134,177**	138,256	132,905
Other investments		**5,908**	6,140	6,265
Deposits		**13,057**	13,542	12,213
Total		**308,830**	294,705	296,457
Assets held for sale	D1	**875**	1,079	916
Cash and cash equivalents		**5,903**	6,840	6,785
Total assets	C1,C3.1	**339,290**	325,837	325,932

* Included within financial investments are £3,953 million of lent securities as at 30 June 2014 (30 June 2013: £5,076 million; 31 December 2013: £3,791 million).

IFRS basis results

Condensed consolidated statement of financial position
Equity and liabilities

	Note	2014 £m	2013 £m	
		30 Jun	30 Jun	31 Dec
Equity				
Shareholders' equity		10,625	9,625	9,650
Non-controlling interests		1	6	1
Total equity		10,626	9,631	9,651
Liabilities				
Policyholder liabilities and unallocated surplus of with-profits funds:				
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)		283,704	272,728	273,953
Unallocated surplus of with-profits funds		13,044	11,434	12,061
Total	C4.1(a)	296,748	284,162	286,014
Core structural borrowings of shareholder-financed operations:				
Subordinated debt		3,597	3,161	3,662
Other		970	988	974
Total	C6.1	4,567	4,149	4,636
Other borrowings:				
Operational borrowings attributable to shareholder-financed operations	C6.2(a)	2,243	2,530	2,152
Borrowings attributable to with-profits operations	C6.2(b)	864	924	895
Other non-insurance liabilities:				
Obligations under funding, securities lending and sale and repurchase agreements		2,188	2,889	2,074
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		5,262	5,394	5,278
Deferred tax liabilities	C7.1	3,855	4,102	3,778
Current tax liabilities		475	325	395
Accruals and deferred income		731	538	824
Other creditors		4,999	3,743	3,307
Provisions		534	537	635
Derivative liabilities		1,400	2,226	1,689
Other liabilities		3,970	3,661	3,736
Total		23,414	23,415	21,716
Liabilities held for sale	D1	828	1,026	868
Total liabilities	C1,C3.1	328,664	316,206	316,281
Total equity and liabilities		339,290	325,837	325,932

Condensed consolidated statement of cash flows

	Note	2014 £m	2013 £m	
		Half year	Half year	Full year
Cash flows from operating activities				
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)* note (i)		**1,708**	720	2,082
Non-cash movements in operating assets and liabilities reflected in profit before tax note (ii)		**(1,162)**	533	(775)
Other items note (iii)		**38**	70	17
Net cash flows from operating activities		**584**	1,323	1,324
Cash flows from investing activities				
Net cash outflows from purchases and disposals of property, plant and equipment		**(50)**	(140)	(179)
Acquisition of distribution rights and subsidiaries, net of cash balance note (iv)		**(534)**	(376)	(405)
Net cash flows from investing activities		**(584)**	(516)	(584)
Cash flows from financing activities				
Structural borrowings of the Group:				
Shareholder-financed operations: note (v)	C6.1			
Issue of subordinated debt, net of costs		**–**	429	1,124
Interest paid		**(169)**	(148)	(291)
With-profits operations: note (vi)	C6.2			
Interest paid		**(4)**	(4)	(9)
Equity capital:				
Issues of ordinary share capital		**8**	1	6
Dividends paid		**(610)**	(532)	(781)
Net cash flows from financing activities		**(775)**	(254)	49
Net (decrease) increase in cash and cash equivalents		**(775)**	553	789
Cash and cash equivalents at beginning of period		**6,785**	6,126	6,126
Effect of exchange rate changes on cash and cash equivalents		**(107)**	161	(130)
Cash and cash equivalents at end of period		**5,903**	6,840	6,785

Notes

(i) This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders.

(ii) The adjusting items to profit before tax included within non-cash movements in operating assets and liabilities reflected in profit before tax are as follows:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Other non-investment and non-cash assets	**(2,461)**	(1,140)	(1,146)
Investments	**(15,866)**	(8,074)	(23,487)
Policyholder liabilities (including unallocated surplus)	**15,110**	7,295	21,951
Other liabilities (including operational borrowings)	**2,055**	2,452	1,907
Non-cash movements in operating assets and liabilities reflected in profit before tax	**(1,162)**	533	(775)

(iii) The adjusting items to profit before tax included within other items are adjustments in respect of non-cash items together with operational interest receipts and payments, dividend receipts and tax paid.

(iv) The agreement entered into by the Group in the first half of 2014 expanding the term and geographic scope of its strategic pan-Asian bancassurance partnership with Standard Chartered PLC resulted in a net cash outflow during the reporting period of £503 million for acquisition of distribution rights. In addition, the acquisition of Express Life in Ghana, in the first half of 2014, resulted in a net cash outflow of £14 million. There was also a £12 million payment for a deferred consideration of the acquisition of Thanachart Life, and a further £5 million payment in respect of other distribution agreements. The acquisition of Thanachart Life and related distribution agreements in 2013 resulted in a net cash outflow of £396 million in full year 2013 (half year 2013: £376 million). A further £9 million cash payment was made in the second half of 2013 relating to the acquisition of REALIC in 2012.

(v) Structural borrowings of shareholder-financed operations exclude borrowings to support short-term fixed income securities programmes, non-recourse borrowings of investment subsidiaries of shareholder-financed operations and other borrowings of shareholder-financed operations. Cash flows in respect of these borrowings are included within cash flows from operating activities.

(vi) Interest paid on structural borrowings of with-profits operations relate solely to the £100 million 8.5 per cent undated subordinated guaranteed bonds, which contribute to the solvency base of the Scottish Amicable Insurance Fund (SAIF), a ring-fenced sub-fund of the PAC with-profits fund. Cash flows in respect of other borrowings of with-profits funds, which principally relate to consolidated investment funds, are included within cash flows from operating activities.

A: Background

A1: Basis of preparation and audit status

These condensed consolidated interim financial statements for the six months ended 30 June 2014 have been prepared in accordance with IAS 34 'Interim Financial Reporting' as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU). The Group's policy for preparing this interim financial information is to use the accounting policies adopted by the Group in its last consolidated financial statements, as updated by any changes in accounting policies it intends to make in its next consolidated financial statements as a result of new or amended IFRS that are applicable or available for early adoption for the next annual financial statements and other policy improvements. EU-endorsed IFRS may differ from IFRSs issued by the IASB if, at any point in time, new or amended IFRS have not been endorsed by the EU. At 30 June 2014, there were no unendorsed standards effective for the period ended 30 June 2014 affecting the condensed consolidated financial statements of the Group, and there were no differences between IFRS endorsed by the EU and IFRS issued by the IASB in terms of their application to the Group.

The IFRS basis results for the 2014 and 2013 half years are unaudited. The 2013 full year IFRS basis results have been derived from the 2013 statutory accounts. The auditors have reported on the 2013 statutory accounts which have been delivered to the Registrar of Companies. The auditors' report was (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

The exchanges rates applied for balances and transactions in currencies other than the presentational currency of the Group, pounds sterling (GBP), were:

	Closing rate at 30 Jun 2014	Average for the 6 months to 30 Jun 2014	Closing rate at 30 Jun 2013	Average for the 6 months to 30 Jun 2013	Closing rate at 31 Dec 2013	Average for 2013
Local currency: £						
Hong Kong	13.25	12.95	11.76	11.98	12.84	12.14
Indonesia	20,270.27	19,573.46	15,053.25	15,024.12	20,156.57	16,376.89
Malaysia	5.49	5.45	4.79	4.75	5.43	4.93
Singapore	2.13	2.10	1.92	1.92	2.09	1.96
India	102.84	101.45	90.13	84.94	102.45	91.75
Vietnam	36,471.11	35,266.15	32,161.63	32,305.17	34,938.60	32,904.71
US	1.71	1.67	1.52	1.54	1.66	1.56

Certain notes to the financial statements present half year 2013 comparative information at Constant Exchange Rates (CER), in addition to the reporting at Actual Exchange Rates (AER) used throughout the condensed consolidated financial statements. AER are actual historical exchange rates for the specific accounting period, being the average rates over the period for the income statement and the closing rates for the balance sheet at the balance sheet date. CER results are calculated by translating prior period results using the current period foreign exchange rate ie current period average rates for the income statement and current period closing rates for the balance sheet.

The accounting policies applied by the Group in determining the IFRS basis results in this report are the same as those previously applied in the Group's consolidated financial statements for the year ended 31 December 2013, except for the adoption of the new and amended accounting pronouncements for Group IFRS reporting as described below.

A2: Adoption of new accounting pronouncements in 2014

The following accounting pronouncements issued and endorsed for use in the EU have been adopted for half year 2014. This is not intended to be a complete list as only those accounting pronouncements that could have an impact upon the Group's financial statements are discussed.

Accounting standard	Key requirements	Impact on financial statements
Amendments to IAS 32: Offsetting financial assets and financial liabilities	These amendments, effective from 1 January 2014 provide clarification on the application of the offsetting rules and require offsetting of a financial asset and financial liability when there is both the legally-enforceable right to set-off and intention to either settle on a net basis or realise the asset and settle the liability simultaneously.	The Group has adopted the standard from 1 January 2014 with no material impact on the presentation of the Group's financial assets and financial liabilities.
IFRIC 21 'Levies'	This clarification, effective from 1 January 2014, provides guidance on recognition of the liability for a levy imposed by a government.	The Group has adopted the clarification from 1 January 2014 and there is no material impact on the recognition of liabilities for the levies imposed on the Group.

B: Earnings performance

B1: Analysis of performance by segment

B1.1 Segment results – profit before tax

For memorandum disclosure purposes, the table below presents the half year 2013 results on both AER and CER bases so as to eliminate the impact of exchange translation.

	Note	2014 £m Half year	2013 £m AER Half year note (v)	2013 £m CER Half year note (v)	% AER vs Half year note (v)	% CER vs Half year note (v)	2013 £m Full year
Asia operations							
Insurance operations	B4(a)	484	476	408	2%	19%	1,003
Development expenses		(1)	(2)	(2)	50%	50%	(2)
Total Asia insurance operations after development expenses		483	474	406	2%	19%	1,001
Eastspring Investments		42	38	34	11%	24%	74
Total Asia operations		525	512	440	3%	19%	1,075
US operations							
Jackson (US insurance operations)	B4(b)	686	582	538	18%	28%	1,243
Broker-dealer and asset management		(5)	34	31	(115)%	(116)%	59
Total US operations		681	616	569	11%	20%	1,302
UK operations							
UK insurance operations:	B4(c)						
Long-term business		374	341	341	10%	10%	706
General insurance commission[note (i)]		12	15	15	(20)%	(20)%	29
Total UK insurance operations		386	356	356	8%	8%	735
M&G (including Prudential Capital)		249	225	225	11%	11%	441
Total UK operations		635	581	581	9%	9%	1,176
Total segment profit		1,841	1,709	1,590	8%	16%	3,553
Other income and expenditure							
Investment return and other income		3	10	10	(70)%	(70)%	10
Interest payable on core structural borrowings		(170)	(152)	(152)	(12)%	(12)%	(305)
Corporate expenditure[note (ii)]		(138)	(128)	(128)	(8)%	(8)%	(263)
Total		(305)	(270)	(270)	(13)%	(13)%	(558)
Solvency II implementation costs		(11)	(13)	(13)	15%	15%	(29)
Restructuring costs[note (iii)]		(4)	(11)	(11)	64%	64%	(12)
Operating profit based on longer-term investment returns		1,521	1,415	1,296	7%	17%	2,954
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	(45)	(755)	(709)	94%	94%	(1,110)
Amortisation of acquisition accounting adjustments		(44)	(30)	(28)	(47)%	(57)%	(72)
Loss attaching to held for sale Japan life business[note (iv)]	D1	–	(124)	(107)	100%	100%	(102)
Costs of domestication of Hong Kong branch	D2	(8)	–	–	n/a	n/a	(35)
Profit before tax attributable to shareholders		1,424	506	452	181%	215%	1,635

Basic earnings per share (in pence)	B6	2014 Half year	2013 AER Half year note (v)	2013 CER Half year note (v)	% AER vs Half year note (v)	% CER vs Half year note (v)	2013 Full year
Based on operating profit based on longer-term investment returns		45.2p	42.2p	38.7p	7%	17%	90.9p
Based on profit for the period		45.0p	14.3p	12.8p	215%	252%	52.8p

Notes

(i) The Group's UK insurance operations transferred its general insurance business to Churchill in 2002. General insurance commission represents the commission receivable net of expenses for Prudential-branded general insurance products as part of this arrangement.

(ii) Corporate expenditure, as shown above, is for Group Head Office and Asia Regional Head Office.

(iii) Restructuring costs are incurred in the UK and represent one-off expenses incurred in securing expense savings.

(iv) To facilitate comparisons of operating profit based on longer-term investment returns that reflect the Group's retained operations, the results attributable to the held for sale Japan life business are included separately within the supplementary analysis of profit above.

(v) For definitions of AER and CER refer to note A1.

B1.2 Short-term fluctuations in investment returns on shareholder-backed business

	2014 £m	2013 £m	
	Half year	Half year	Full year
Insurance operations:			
Asia[note (ii)]	119	(137)	(204)
US[note (iii)]	(226)	(441)	(625)
UK[note (iv)]	93	(147)	(254)
Other operations[note (v)]	(31)	(30)	(27)
Total	(45)	(755)	(1,110)

Notes

(i) General overview of defaults
The Group did not experience any defaults on its shareholder-backed debt securities portfolio in 2014 or 2013.

(ii) Asia insurance operations
In Asia, the positive short-term fluctuations of £119 million (half year 2013: negative £(137) million; full year 2013: negative £(204) million) primarily reflect net unrealised movements on bond holdings following modest falls in bond yields across the region during the first half of the year.

(iii) US insurance operations
The short-term fluctuations in investment returns for US insurance operations comprise the following items:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Short-term fluctuations relating to debt securities			
Credits (charges) in the period:			
Losses on sales of impaired and deteriorating bonds	(1)	(2)	(5)
Bond write downs	(5)	(5)	(8)
Recoveries/reversals	14	6	10
Total credits (charges) in the period[note (a)]	8	(1)	(3)
Add: Risk margin allowance deducted from operating profit based on longer-term investment returns[note (b)]	38	44	85
	46	43	82
Interest-related realised gains:			
Arising in the period	20	34	64
Less: Amortisation of gains and losses arising in current and prior periods to operating profit based on longer-term investment returns	(43)	(45)	(89)
	(23)	(11)	(25)
Related amortisation of deferred acquisition costs	(7)	(8)	(15)
Total short-term fluctuations related to debt securities	16	24	42
Derivatives (other than equity-related): market value movements (net of related amortisation of deferred acquisition costs)[note (c)]	208	(380)	(531)
Net equity hedge results (principally guarantees and derivatives, net of related amortisation of deferred acquisition costs)[note (d)]	(478)	(166)	(255)
Equity-type investments: actual less longer-term return (net of related amortisation of deferred acquisition costs)	21	63	89
Other items (net of related amortisation of deferred acquisition costs)	7	18	30
Total	(226)	(441)	(625)

The short-term fluctuations in investment returns shown in the table above are stated net of a credit for the related amortisation of deferred acquisition costs of £107 million (half year 2013: £242 million; full year 2013: £228 million). See note C5.1(b).

Notes

(a) The credits/charges on the debt securities of Jackson comprise the following:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Residential mortgage-backed securities:			
Prime (including agency)	–	2	1
Alt-A	4	–	(1)
Sub-prime	3	(1)	–
Total residential mortgage-backed securities	7	1	–
Corporate debt securities	(1)	(2)	(1)
Other	2	–	(2)
Total	8	(1)	(3)

B: Earnings performance continued

B1: Analysis of performance by segment continued

(b) The risk margin reserve charge for longer-term credit-related losses included in operating profit based on longer-term investment returns of Jackson for half year 2014 is based on an average annual risk margin reserve of 23 basis points (half year 2013: 25 basis points; full year 2013: 25 basis points) on average book values of US$54.7 billion (half year 2013: US$54.3 billion; full year 2013: US$54.4 billion) as shown below:

	Half year 2014				Half year 2013				Full year 2013			
Moody's rating category (or equivalent under NAIC ratings of mortgage-backed securities)	**Average book value** US$m	**RMR** %	**Annual expected loss** US$m	£m	**Average book value** US$m	**RMR** %	**Annual expected loss** US$m	£m	**Average book value** US$m	**RMR** %	**Annual expected loss** US$m	£m
A3 or higher	27,849	0.12	(32)	(19)	27,411	0.11	(31)	(20)	27,557	0.11	(32)	(20)
Baa1, 2 or 3	24,982	0.25	(62)	(37)	24,187	0.25	(61)	(40)	24,430	0.25	(62)	(40)
Ba1, 2 or 3	1,363	1.25	(17)	(10)	1,633	1.14	(19)	(12)	1,521	1.18	(18)	(11)
B1, 2 or 3	386	3.02	(12)	(7)	608	2.73	(17)	(11)	530	2.80	(15)	(9)
Below B3	108	3.71	(4)	(2)	423	2.15	(9)	(6)	317	2.32	(7)	(5)
Total	54,688	0.23	(127)	(75)	54,262	0.25	(137)	(89)	54,355	0.25	(134)	(85)
Related change to amortisation of deferred acquisition costs (see below)			22	13			26	17			25	16
Risk margin reserve charge to operating profit for longer-term credit related losses			(105)	(62)			(111)	(72)			(109)	(69)

Consistent with the basis of measurement of insurance assets and liabilities for Jackson's IFRS results, the charges and credits to operating profits based on longer-term investment returns are partially offset by related amortisation of deferred acquisition costs.

(c) Derivatives (other than equity-related): positive fluctuation of £208 million (half year 2013: negative fluctuation of £(380) million; full year 2013: negative fluctuation of £(531) million) net of related amortisation of deferred acquisition costs.

These gains and losses are in respect of interest rate swaps and swaptions and for the Guaranteed Minimum Income Benefit (GMIB) reinsurance. The swaps and swaptions are undertaken to manage interest rate exposures and durations within the general account, including the variable annuity and fixed index annuity guarantees (as described in note (d) below). The GMIB reinsurance is in place so as to insulate Jackson from the GMIB exposure.

The amounts principally reflect the fair value movement on these instruments, net of related amortisation of deferred acquisition costs.

Under the Group's IFRS reporting of Jackson's derivatives (other than equity-related) programme significant accounting mismatches arise. This is because:

- The derivatives are required to be fair valued with the value movements booked in the income statement;
- As noted above, part of the derivative value movements arise in respect of interest rate exposures within Jackson's guarantee liabilities for variable annuity and fixed index annuity business which are only partially fair valued under IFRS (see below); and
- The GMIB liability is valued under the US GAAP insurance measurement basis applied for IFRS in a way that substantially does not recognise the effect of market movements. However, notwithstanding that the liability is reinsured, as the reinsurance asset is net settled it is deemed a derivative under IAS 39 which requires fair valuation.

In half year 2014, the positive fluctuation of £208 million reflects principally the favourable mark to market impact of approximately 42 basis points decrease in swap rates on the valuation of the interest rate swaps, swaptions, and the GMIB reinsurance asset.

(d) Net equity hedge result: negative fluctuation of £(478) million (half year 2013: negative fluctuation £(166) million; full year 2013: negative fluctuation £(255) million).

These amounts are in respect of the equity-based derivatives and associated guarantee liabilities of Jackson's variable and fixed index annuity business. The equity based derivatives are undertaken to manage the equity risk exposure of the guarantee liabilities. The economic exposure of these guarantee liabilities also includes the effects of changes in interest rates which are managed through the swaps and swaptions programmes described in note (c) above.

The amounts reflect the net effect of:

- Fair value movements on free-standing equity derivatives;
- The accounting value movements on the variable annuity and fixed index annuity guarantee liabilities;
- Fee assessments and claim payments in respect of guarantee liabilities; and
- Related DAC amortisation.

Under the Group's IFRS reporting of Jackson's equity-based derivatives and associated guarantee liabilities significant accounting mismatches arise. This is because:

- The free-standing equity-based derivatives and Guaranteed Minimum Withdrawal Benefit (GMWB) 'not for life' embedded derivative liabilities are required to be fair valued. These fair value movements include the effects of changes to levels of equity markets, implied volatility and interest rates. The interest rate exposure is managed through the derivative programme explained above in note (c);
- The Guaranteed Minimum Death Benefit (GMDB) and GMWB 'for life' guarantees are valued under the US GAAP insurance measurement basis applied for IFRS in a way that substantially does not recognise the effect of equity market and interest rate changes.

In half year 2014, the negative fluctuation of £(478) million reflects the net effect of mark-to-market reductions on the free-standing equity-based derivatives together with increases in the carrying amounts of those guarantees that are fair valued as embedded derivatives under IFRS. Both aspects reflect increased equity markets (the S&P 500 increased by 6 per cent) with the value movement on the embedded derivatives also being affected by decreases in average implied volatility levels and the decrease in swap rates.

(iv) UK insurance operations

The positive short-term fluctuations in investment returns for UK insurance operations of £93 million (half year 2013: negative £(147) million; full year 2013: negative £(254) million) include net unrealised movements on fixed income assets supporting the capital of the shareholder-backed annuity business, reflecting the fall in bond yields since the end of 2013.

(v) Other

Short-term fluctuations in investment returns of other operations, were negative £(31) million (half year 2013: negative £(30) million; full year 2013: negative £(27) million) representing principally unrealised value movements on investments and foreign exchange items.

B1.3 Determining operating segments and performance measure of operating segments

Operating segments

The Group's operating segments, determined in accordance with IFRS 8 'Operating Segments', are as follows:

Insurance operations
- Asia
- US (Jackson)
- UK

Asset management operations
- M&G (including Prudential Capital)
- Eastspring Investments
- US broker-dealer and asset management (including Curian)

The Group's operating segments are also its reportable segments for the purposes of internal management reporting with the exception of Prudential Capital which has been incorporated into the M&G operating segment for the purposes of segment reporting.

Performance measure

The performance measure of operating segments utilised by the Company is IFRS operating profit attributable to shareholders based on longer-term investment returns, as described below. This measurement basis distinguishes operating profit based on long-term investment returns from other constituents of the total profit as follows:

- Short-term fluctuations in investment returns;
- Amortisation of acquisition accounting adjustments arising on the purchase of business. This comprises principally the charge for the adjustments arising on the purchase of REALIC in 2012;
- Loss attaching to the held for sale Japan life business. See note D1 for further details; and
- The costs associated with the domestication of the Hong Kong branch which became effective on 1 January 2014.

Segment results that are reported to the Group Executive Committee include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items are mainly in relation to the Group Head Office and the Asia Regional Head Office.

Except in the case of assets backing the UK annuity, unit-linked and US variable annuity separate account liabilities, operating profit based on longer-term investment returns for shareholder-financed business is determined on the basis of expected longer-term investment returns. In the case of assets backing the UK annuity business, unit-linked and US variable annuity separate account liabilities, the basis of determining operating profit based on longer-term investment returns is as follows:

- UK annuity business liabilities: For this business, policyholder liabilities are determined by reference to current interest rates. The value movements of the assets covering liabilities are closely correlated with the related change in liabilities. Accordingly, asset value movements are recorded within the 'operating results based on longer-term investment returns'. Policyholder liabilities include a margin for credit risk. Variations between actual and best estimate expected impairments are recorded as a component of short-term fluctuations in investment returns; and
- Unit-linked and US variable annuity business separate account liabilities: For such business, the policyholder unit liabilities are directly reflective of the asset value movements. Accordingly, the operating results based on longer-term investment returns reflect the current period value movements in unit liabilities and the backing assets.

In the case of other shareholder-financed business, the measurement of operating profit based on longer-term investment returns reflects the particular features of long-term insurance business where assets and liabilities are held for the long term and for which the accounting basis for insurance liabilities under current IFRS is not generally conducive to demonstrating trends in underlying performance of life businesses exclusive of the effects of short-term fluctuations in market conditions. In determining the profit on this basis, the following key elements are applied to the results of the Group's shareholder-financed operations.

(a) Debt, equity-type securities and loans

Longer-term investment returns comprise actual income receivable for the period (interest/dividend income) and for both debt and equity-type securities longer-term capital returns.

In principle, for debt securities and loans, the longer-term capital returns comprise two elements:

- Risk margin reserve based charge for the expected level of defaults for the period, which is determined by reference to the credit quality of the portfolio. The difference between impairment losses in the reporting period and the risk margin reserve charge to the operating result is reflected in short-term fluctuations in investment returns; and
- The amortisation of interest-related realised gains and losses to operating results based on longer-term investment returns to the date when sold bonds would have otherwise matured.

B: Earnings performance continued

B1: Analysis of performance by segment continued

Jackson is the shareholder-backed operation for which the distinction between impairment losses and interest-related realised gains and losses is in practice relevant to a significant extent. Jackson has used the ratings by Nationally Recognised Statistical Ratings Organisations (NRSRO) or ratings resulting from the regulatory ratings detail issued by the National Association of Insurance Commissioners (NAIC) developed by external third parties such as PIMCO or BlackRock Solutions to determine the average annual risk margin reserve to apply to debt securities held to back general account business. Debt securities held to back separate account and reinsurance funds withheld are not subject to risk margin reserve charge. Further details of the risk margin reserve charge, as well as the amortisation of interest-related realised gains and losses, for Jackson are shown in note B1.2.

For debt securities backing non-linked shareholder-financed business of the UK insurance operations (other than the annuity business) and of the Asia insurance operations, the realised gains and losses are principally interest related. Accordingly, all realised gains and losses to date for these operations are being amortised over the period to the date those securities would otherwise have matured, with no explicit risk margin reserve charge.

At 30 June 2014, the level of unamortised interest-related realised gains and losses related to previously sold bonds for the Group was a net gain of £427 million (half year 2013: net gain of £522 million; full year 2013: net gain of £461 million).

For equity-type securities, the longer-term rates of return are estimates of the long-term trend investment return for income and capital having regard to past performance, current trends and future expectations. Equity-type securities held for shareholder-financed operations other than the UK annuity business, unit-linked and US variable annuity are of significance for the US and Asia insurance operations. Different rates apply to different categories of equity-type securities.

As at 30 June 2014, the equity-type securities for US insurance non-separate account operations amounted to £1,071 million (half year 2013: £1,188 million; full year 2013: £1,118 million). For these operations, the longer-term rates of return for income and capital applied in 2014 and 2013, which reflect the combination of risk free rates and appropriate risk premiums are as follows:

	2014	2013	
	Half year	Half year	Full year
Equity-type securities such as common and preferred stock and portfolio holdings in mutual funds	6.5% to 6.7%	5.7% to 6.5%	5.7% to 6.8%
Other equity-type securities such as investments in limited partnerships and private equity funds	8.5% to 8.7%	7.7% to 8.5%	7.7% to 9.0%

For Asia insurance operations, excluding assets of the Japan life held for sale business, investments in equity securities held for non-linked shareholder-financed operations amounted to £664 million as at 30 June 2014 (half year 2013: £526 million; full year 2013: £571 million). The rates of return applied in the years 2014 and 2013 ranged from 2.02 per cent to 13.75 per cent with the rates applied varying by territory. These rates are determined after consideration by the Group's in-house economists of long-term expected real government bond returns, equity risk premium and long-term inflation. These rates are broadly stable from period to period but may be different between countries reflecting, for example, differing expectations of inflation in each territory. The assumptions are for returns expected to apply in equilibrium conditions. The assumed rates of return do not reflect any cyclical variability in economic performance and are not set by reference to prevailing asset valuations.

The longer-term investment returns for the Asia insurance joint ventures accounted for on the equity method are determined on a similar basis as the other Asia insurance operations described above.

(b) US variable and fixed index annuity business

The following value movements for Jackson's variable and fixed index annuity business are excluded from operating profit based on longer-term investment returns:

— Fair value movements for equity-based derivatives;
— Fair value movements for embedded derivatives for Guaranteed Minimum Withdrawal Benefit 'not for life' and fixed index annuity business, and Guaranteed Minimum Income Benefit reinsurance (see note below);
— Movements in accounts carrying value of Guaranteed Minimum Death Benefit and Guaranteed Minimum Withdrawal Benefit 'for life' and Guaranteed Minimum Income Benefit liabilities, for which, under the 'grandfathered' US GAAP applied under IFRS for Jackson's insurance assets and liabilities, the measurement basis gives rise to a muted impact of current period market movements;
— Fee assessments and claim payments, in respect of guarantee liabilities; and
— Related amortisation of deferred acquisition costs for each of the above items.

Note: US operations – Embedded derivatives for variable annuity guarantee features

The Guaranteed Minimum Income Benefit liability, which is fully reinsured, subject to a deductible and annual claim limits, is accounted for in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Subtopic 944-80 Financial Services – Insurance – Separate Accounts (formerly SOP 03-1) under IFRS using 'grandfathered' US GAAP. As the corresponding reinsurance asset is net settled, it is considered to be a derivative under IAS 39, 'Financial Instruments: Recognition and Measurement', and the asset is therefore recognised at fair value. As the Guaranteed Minimum Income Benefit is economically reinsured the mark to market element of the reinsurance asset is included as a component of short-term fluctuations in investment returns.

(c) Other derivative value movements

Generally, derivative value movements are excluded from operating results based on longer-term investment returns (unless those derivative value movements broadly offset changes in the accounting value of other assets and liabilities included in operating profit). The principal example of non-equity based derivatives (for example interest rate swaps and swaptions) whose value movements are excluded from operating profit arises in Jackson. Non-equity based derivatives are primarily held by Jackson as part of a broadly-based hedging programme for features of Jackson's bond portfolio (for which value movements are booked in the statement of comprehensive income rather than the income statement), product liabilities (for which US GAAP accounting as 'grandfathered' under IFRS 4 does not fully reflect the economic features being hedged), and the interest rate exposure attaching to equity-based embedded derivatives.

(d) Other liabilities to policyholders and embedded derivatives for product guarantees

Under IFRS, the degree to which the carrying values of liabilities to policyholders are sensitive to current market conditions varies between territories depending upon the nature of the 'grandfathered' measurement basis. In general, in those instances where the liabilities are particularly sensitive to routine changes in market conditions, the accounting basis is such that the impact of market movements on the assets and liabilities is broadly equivalent in the income statement, and operating profit based on longer-term investments returns is not distorted. In these circumstances, there is no need for the movement in the liability to be bifurcated between the elements that relate to longer-term market conditions and short-term effects.

However, some types of business movements in liabilities do require bifurcation to ensure that at the net level (ie after allocated investment return and change for policyholder benefits) the operating result reflects longer-term market returns.

Examples where such bifurcation is necessary are:

Asia – Hong Kong

For certain non-participating business, the economic features are more akin to asset management products with policyholder liabilities reflecting asset shares over the contract term. For these products, the charge for policyholder benefits in the operating results should reflect the asset share feature rather than volatile movements that would otherwise be reflected if the local regulatory basis (also applied for IFRS basis) was used.

For other Hong Kong non-participating business, longer-term interest rates are used to determine the movement in policyholder liabilities for determining operating results. Similar principles apply for other Asia operations.

UK shareholder-backed annuity business

The operating result based on longer-term investment returns reflects the impact of value movements on policyholder liabilities for annuity business in PRIL and the PAC non-profit sub-fund after adjustments to allocate the following elements of the movement to the category of 'short-term fluctuations in investment returns':

- The impact on credit risk provisioning of actual upgrades and downgrades during the period;
- Credit experience compared to assumptions; and
- Short-term value movements on assets backing the capital of the business.

Credit experience reflects the impact of defaults and other similar experience, such as asset exchanges arising from debt restructuring by issuers that include effectively an element of permanent impairment of the security held. Positive or negative experience compared to assumptions is included within short-term fluctuations in investment returns without further adjustment. The effects of other changes to credit risk provisioning are included in the operating result, as is the net effect of changes to the valuation rate of interest due to portfolio rebalancing to align more closely with management benchmark.

(e) Fund management and other non-insurance businesses

For these businesses, the particular features applicable for life assurance noted above do not apply. For these businesses it is inappropriate to include returns in the operating result on the basis described above. Instead, it is appropriate to generally include realised gains and losses (including impairments) in the operating result with unrealised gains and losses being included in short-term fluctuations. For this purpose impairments are calculated as the credit loss determined by comparing the projected cash flows discounted at the original effective interest rate to the carrying value. In some instances it may also be appropriate to amortise realised gains and losses on derivatives and other financial instruments to operating results over a time period that reflects the underlying economic substance of the arrangements.

B: Earnings performance continued

B1: Analysis of performance by segment continued

B1.4 Additional segmental analysis of revenue

The additional segmental analyses of revenue from external customers excluding investment return and net of outward reinsurance premiums are as follows:

	Half year 2014 £m				
	Asia	US	UK	Intra-group	Total
Revenue from external customers:					
Insurance operations	4,336	8,321	3,629	–	16,286
Asset management	140	387	612	(194)	945
Unallocated corporate	–	–	17	–	17
Intra-group revenue eliminated on consolidation	(67)	(42)	(85)	194	–
Total revenue from external customers	4,409	8,666	4,173	–	17,248

	Half year 2013 £m				
	Asia	US	UK	Intra-group	Total
Revenue from external customers:					
Insurance operations	4,276	7,858	2,786	–	14,920
Asset management	122	421	562	(172)	933
Unallocated corporate	–	–	10	–	10
Intra-group revenue eliminated on consolidation	(49)	(43)	(80)	172	–
Total revenue from external customers	4,349	8,236	3,278	–	15,863

	Full year 2013 £m				
	Asia	US	UK	Intra-group	Total
Revenue from external customers:					
Insurance operations	8,919	15,381	5,816	–	30,116
Asset management	245	855	1,165	(379)	1,886
Unallocated corporate	–	–	26	–	26
Intra-group revenue eliminated on consolidation	(98)	(86)	(195)	379	–
Total revenue from external customers	9,066	16,150	6,812	–	32,028

Revenue from external customers comprises:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Earned premiums, net of reinsurance	16,189	14,763	29,844
Fee income and investment contract business and asset management (presented as 'Other income')	1,059	1,100	2,184
Total revenue from external customers	17,248	15,863	32,028

In their capacity as fund managers to fellow Prudential Group subsidiaries, M&G, Eastspring Investments and the US asset management businesses generate fees for investment management and related services. These services are charged at appropriate arm's length prices, typically priced as a percentage of funds under management. Intra-group fees included within asset management revenue were earned by the following asset management segment:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Intra-group revenue generated by:			
M&G	85	80	195
Eastspring investments	67	49	98
US broker-dealer and asset management (including Curian)	42	43	86
Total intra-group fees included within asset management segment	194	172	379

Revenue from external customers of Asia, US and UK insurance operations shown above are net of outwards reinsurance premiums of £134 million, £115 million and £103 million respectively (half year 2013: £96 million, £172 million and £92 million respectively; full year 2013: £190 million, £278 million and £190 million respectively).

B2: Profit before tax – asset management operations

The profit included in the income statement in respect of asset management operations for the period is as follows:

	2014 £m				2013 £m	
	M&G	US note (iv)	Eastspring Investments	Half year Total	Half year Total	Full year Total
Revenue (excluding NPH broker-dealer fees)	682	139	142	963	916	1,914
NPH broker-dealer fees note (i)	–	248	–	248	249	504
Gross revenue	682	387	142	1,211	1,165	2,418
Charges (excluding NPH broker-dealer fees)	(433)	(144)	(114)	(691)	(644)	(1,353)
NPH broker-dealer fees note (i)	–	(248)	–	(248)	(249)	(504)
Gross charges	(433)	(392)	(114)	(939)	(893)	(1,857)
Share of profits from joint ventures and associates, net of related tax	6	–	14	20	16	35
Profit before tax	255	(5)	42	292	288	596
Comprising:						
Operating profit based on longer-term investment returns note (ii)	249	(5)	42	286	297	574
Short-term fluctuations in investment returns note (iii)	6	–	–	6	(9)	22
Profit before tax	255	(5)	42	292	288	596

Notes

(i) NPH broker-dealer fees represent commissions received that are then paid on to the writing brokers on sales of investment products. The segment revenue of the Group's asset management operations is required to include this item. However, reflecting their commercial nature, equivalent amounts are also reflected as charges within the income statement. After allowing for these charges, there is no effect on profit from this item. The presentation in the table above shows the amounts attributable to this item so as to distinguish the underlying revenue and charges.

(ii) M&G operating profit based on longer-term investment returns:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Asset management fee income	462	418	859
Other income	1	3	4
Staff costs	(160)	(149)	(339)
Other costs	(89)	(77)	(166)
Underlying profit before performance-related fees	214	195	358
Share of associate's results	6	5	12
Performance-related fees	7	4	25
Operating profit from asset management operations	227	204	395
Operating profit from Prudential Capital	22	21	46
Total M&G operating profit based on longer-term investment returns	249	225	441

The difference between the fees and other income shown above in respect of asset management operations, and the revenue figure for M&G noted in the main table primarily relates to the total revenue of Prudential Capital (including short-term fluctuations) of £72 million (half year 2013: £51 million; full year 2013: £144 million) and commissions which have been netted off in arriving at the fee income of £462 million (half year 2013: £418 million; full year 2013: £859 million) in the table above. The difference in the presentation of commission is aligned with how management reviews the business.

(iii) Short-term fluctuations in investment returns for M&G are primarily in respect of unrealised fair value movements on Prudential Capital's bond portfolio.

(iv) The US asset management result includes a provision of £(33) million related to the potential refund of certain fees by Curian.

B: Earnings performance continued

B3: Acquisition costs and other expenditure

	2014 £m	2013 £m	
	Half year	Half year	Full year
Acquisition costs incurred for insurance policies	(1,307)	(1,185)	(2,553)
Acquisition costs deferred less amortisation of acquisition costs	272	419	566
Administration costs and other expenditure	(2,097)	(2,127)	(4,303)
Movements in amounts attributable to external unit holders of consolidated investment funds	(204)	(422)	(571)
Total acquisition costs and other expenditure	(3,336)	(3,315)	(6,861)

Included in total acquisition costs and other expenditure is depreciation of property, plant and equipment of £(45) million (half year 2013: £(45) million; full year 2013: £(87) million).

B4: Effect of changes and other accounting features on insurance assets and liabilities

The following features are of relevance to the determination of the half year 2014 results:

a Asia insurance operations
In half year 2014, the IFRS operating profit based on longer-term investment returns for Asia insurance operations included a net credit of £19 million (half year 2013: £31 million; full year 2013: £44 million) representing a small number of non-recurring items.

b US insurance operations
Amortisation of deferred acquisition costs
Jackson applies a mean reversion technique for amortisation of deferred acquisition costs on variable annuity business which dampens the effects of short-term market movements on expected gross profits against which deferred acquisition costs are amortised. To the extent that the mean reversion methodology does not fully dampen the effects of market returns, there is a charge or credit for accelerated or decelerated amortisation. For half year 2014, reflecting the positive market returns in the period, there was a credit for decelerated amortisation of £10 million (half year 2013: credit for decelerated amortisation of £20 million; full year 2013: credit for decelerated amortisation of £82 million) to the operating profit based on longer-term investment returns. See note C5.1(b) for further details.

Other
In the second half of 2013, Jackson revised its projected long-term separate account return from 8.4 per cent to 7.4 per cent net of external fund management fees. The effect of this change together with other assumption changes and recalibration of modelling of accounting values of guarantees gave rise to a net benefit of £6 million to profit before tax in full year 2013.

c UK insurance operations
Annuity business: allowance for credit risk
For IFRS reporting, the results for UK shareholder-backed annuity business are particularly sensitive to the allowances made for credit risk. The allowance is reflected in the deduction from the valuation rate of interest for discounting projected future annuity payments to policyholders that would have otherwise applied. Credit risk allowance comprises (i) an amount for long-term best estimate defaults, and (ii) additional provisions for credit risk premium, downgrade resilience and short-term defaults.

The weighted components of the bond spread over swap rates for shareholder-backed fixed and linked annuity business for PRIL, the principal company which writes the UK's shareholder-backed business, based on the asset mix at these dates are shown below.

	30 Jun 2014			30 Jun 2013			31 Dec 2013		
	Pillar 1 regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)	Pillar 1 regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)	Pillar 1 regulatory basis (bps)	Adjustment from regulatory to IFRS basis (bps)	IFRS (bps)
Bond spread over swap rates[note (i)]	119	–	119	157	–	157	133	–	133
Credit risk allowance:									
Long-term expected defaults[note (ii)]	14	–	14	15	–	15	15	–	15
Additional provisions[note (iii)]	47	(19)	28	49	(22)	27	47	(19)	28
Total credit risk allowance	61	(19)	42	64	(22)	42	62	(19)	43
Liquidity premium	58	19	77	93	22	115	71	19	90

Notes

(i) Bond spread over swap rates reflect market observed data.

(ii) Long-term expected defaults are derived by applying Moody's data from 1970 to 2009 and the definition of the credit rating used is the second highest credit rating published by Moody's, Standard & Poor's and Fitch.

(iii) Additional provisions comprise credit risk premium, which is derived from Moody's data from 1970 to 2009, an allowance for a one-notch downgrade of the portfolio subject to credit risk and an additional allowance for short-term defaults.

The prudent Pillar 1 regulatory basis reflects the overriding objective of maintaining sufficient provisions and capital to ensure payments to policyholders can be made. The approach for IFRS aims to establish liabilities that are closer to 'best estimate'.

Movement in the credit risk allowance

The movement during the first half of 2014 of the average basis points allowance for PRIL on Pillar 1 regulatory and IFRS bases are as follows:

	Pillar 1 regulatory basis (bps) Total	IFRS (bps) Total
Total allowance for credit risk at 31 December 2013	62	43
Credit rating changes	1	1
Asset trading	(2)	(1)
New business and other	–	(1)
Total allowance for credit risk at 30 June 2014	61	42

Overall the movement has led to the credit allowance for Pillar 1 purposes to be 51 per cent (half year 2013: 41 per cent; full year 2013: 47 per cent) of the bond spread over swap rates. For IFRS purposes it represents 35 per cent (half year 2013: 27 per cent; full year 2013: 32 per cent) of the bond spread over swap rates.

The reserves for credit risk allowance at 30 June 2014 for the UK shareholder annuity fund were as follows:

	Pillar 1 regulatory basis £bn Total	IFRS £bn Total
PRIL	1.7	1.2
PAC non-profit sub-fund	0.2	0.1
Total – 30 June 2014	1.9	1.3
Total – 30 June 2013	2.0	1.2
Total – 31 December 2013	1.9	1.3

B: Earnings performance continued

B5: Tax charge

a Total tax charge by nature of expense

The total tax charge in the income statement is as follows:

Tax charge	2014 £m Current tax	2014 £m Deferred tax	2014 £m Half year Total	2013 £m Half year Total	2013 £m Full year Total
UK tax	(272)	10	(262)	(159)	(300)
Overseas tax	(260)	(41)	(301)	(196)	(436)
Total tax charge	(532)	(31)	(563)	(355)	(736)

The current tax charge of £532 million includes £23 million (half year 2013: £8 million; full year 2013: £18 million) in respect of the tax charge for the Hong Kong operation. The Hong Kong current tax charge is calculated as 16.5 per cent for all periods on either (i) 5 per cent of the net insurance premium or (ii) the estimated assessable profits, depending on the nature of the business written.

The total tax charge comprises tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders as shown below:

Tax charge	2014 £m Current tax	2014 £m Deferred tax	2014 £m Half year Total	2013 £m Half year Total	2013 £m Full year Total
Tax charge to policyholders' returns	(245)	(39)	(284)	(214)	(447)
Tax charge attributable to shareholders	(287)	8	(279)	(141)	(289)
Total tax charge	(532)	(31)	(563)	(355)	(736)

The principal reason for the increase in the tax charge attributable to policyholders' returns compared to half year 2013 is an increase in current tax on net realised investment gains of the UK with-profits fund. An explanation of the tax charge attributable to shareholders is shown in note (b) below.

b Reconciliation of effective tax rate

Reconciliation of tax charge on profit attributable to shareholders

	Half year 2014 £m (except for tax rates)				
	Asia insurance operations*	US insurance operations	UK insurance operations	Other operations	Total*
Operating profit (loss) based on longer-term investment returns	483	686	386	(34)	1,521
Non-operating profit (loss)	115	(266)	85	(31)	(97)
Profit (loss) before tax attributable to shareholders	598	420	471	(65)	1,424
Expected tax rate†	22%	35%	22%	21%	26%
Tax charge (credit) at the expected tax rate	130	147	102	(13)	366
Effects of:					
Adjustment to tax charge in relation to prior years	–	–	–	3	3
Movements in provisions for open tax matters	1	–	–	–	1
Income not taxable or taxable at concessionary rates	(40)	(27)	(2)	(4)	(73)
Deductions not allowable for tax purposes	15	–	–	2	17
Deferred tax adjustments	1	–	(4)	–	(3)
Effect of results of joint ventures and associates	(19)	–	–	(5)	(24)
Irrecoverable withholding taxes	–	–	–	15	15
Other	(4)	(13)	–	(6)	(23)
Total actual tax charge (credit)	84	107	96	(8)	279
Analysed into:					
Tax on operating profit (loss) based on longer-term investment returns	82	206	79	2	369
Tax charge (credit) on non-operating (loss) profit	2	(99)	17	(10)	(90)
Actual tax rate:					
Operating profit (loss) based on longer-term investment returns	17%	30%	20%	(6%)	24%
Total profit	14%	25%	20%	12%	20%

* The expected and actual tax rates as shown includes the impact of the held for sale Japan life business. For half year 2014, the tax rates for Asia insurance and Group excluding the impact of the held for sale Japan life business are the same.

† The expected tax rates (rounded to the nearest whole percentage) reflect the corporation tax rates generally applied to taxable profits of the relevant country jurisdictions. For Asia operations, the expected tax rates reflect the corporation tax rates weighted by reference to the source of profits of operations contributing to the aggregate business result. The expected tax rate for other operations reflects the mix of business between UK and overseas non-insurance operations, which are taxed at a variety of rates. The rates will fluctuate from year to year dependent on the mix of profits.

	Half year 2013 £m (except for tax rates)				
	Asia insurance operations*	US insurance operations	UK insurance operations	Other operations	Total*
Operating profit based on longer-term investment returns	474	582	356	3	1,415
Non-operating loss	(264)	(468)	(147)	(30)	(909)
Profit (loss) before tax attributable to shareholders	210	114	209	(27)	506
Expected tax rate†	17%	35%	23%	23%	23%
Tax charge (credit) at the expected tax rate	36	40	48	(6)	118
Effects of:					
Adjustment to tax charge in relation to prior years	4	–	1	6	11
Movements in provisions for open tax matters	1	–	–	(10)	(9)
Income not taxable or taxable at concessionary rates	(26)	(37)	–	–	(63)
Deductions not allowable for tax purposes	51	–	–	3	54
Deferred tax adjustments	(2)	–	–	–	(2)
Effect of results of joint ventures and associates	(14)	–	–	(3)	(17)
Irrecoverable withholding taxes	–	–	–	6	6
Other	8	24	11	–	43
Total actual tax charge (credit)	58	27	60	(4)	141
Analysed into:					
Tax charge on operating profit based on longer-term investment returns	79	166	92	3	340
Tax credit on non-operating loss	(21)	(139)	(32)	(7)	(199)
Actual tax rate:					
Operating profit based on longer-term investment returns	17%	29%	26%	100%	24%
Total profit	28%	24%	29%	15%	28%

* The expected and actual tax rates as shown includes the impact of the held for sale Japan life business. The tax rates for Asia insurance and Group, excluding the impact of the held for sale Japan life business are as follows:

	Asia insurance	Total Group
Expected tax rate on total profit	25%	26%
Actual tax rate:		
Operating profit based on longer-term investment returns	17%	24%
Total profit	17%	22%

† The expected tax rates (rounded to the nearest whole percentage) reflect the corporation tax rates generally applied to taxable profits of the relevant country jurisdictions. For Asia operations the expected tax rates reflect the corporation tax rates weighted by reference to the source of profits of operations contributing to the aggregate business result. The expected tax rate for other operations reflects the mix of business between UK and overseas non-insurance operations, which are taxed at a variety of rates. The rates will fluctuate from year to year dependent on the mix of profits.

B: Earnings performance continued

B5: Tax charge continued

	Full year 2013 £m (except for tax rates)				
	Asia insurance operations*	**US insurance operations**	**UK insurance operations**	**Other operations**	**Total***
Operating profit (loss) based on longer-term investment returns	1,001	1,243	735	(25)	2,954
Non-operating loss	(313)	(690)	(289)	(27)	(1,319)
Profit (loss) before tax attributable to shareholders	688	553	446	(52)	1,635
Expected tax rate†	21%	35%	23%	23%	26%
Tax charge (credit) at the expected tax rate	144	194	103	(12)	429
Effects of:					
Adjustment to tax charge in relation to prior years	(3)	–	4	(7)	(6)
Movements in provisions for open tax matters	5	–	–	(12)	(7)
Income not taxable or taxable at concessionary rates	(45)	(88)	–	(10)	(143)
Deductions not allowable for tax purposes	61	–	–	5	66
Impact of changes in local statutory tax rates	(9)	–	(51)	5	(55)
Deferred tax adjustments	(4)	–	–	(8)	(12)
Effect of results of joint ventures and associates	(10)	–	–	(8)	(18)
Irrecoverable withholding taxes	–	–	–	20	20
Other	9	(5)	16	(5)	15
Total actual tax charge (credit)	148	101	72	(32)	289
Analysed into:					
Tax charge (credit) on operating profit (loss) based on longer-term investment returns	173	343	132	(10)	638
Tax credit on non-operating loss	(25)	(242)	(60)	(22)	(349)
Actual tax rate:					
Operating profit (loss) based on longer-term investment returns	17%	28%	18%	40%	22%
Total profit	22%	18%	16%	62%	18%

* The expected and actual tax rates as shown includes the impact of the held for sale Japan life business. The tax rates for Asia insurance and Group, excluding the impact of the held for sale Japan life business are as follows:

	Asia insurance	**Total Group**
Expected tax rate on total profit	23%	27%
Actual tax rate:		
Operating profit based on longer-term investment returns	17%	22%
Total profit	19%	17%

† The expected tax rates (rounded to the nearest whole percentage) reflect the corporation tax rates generally applied to taxable profits of the relevant country jurisdictions. For Asia operations the expected tax rates reflect the corporation tax rates weighted by reference to the source of profits of operations contributing to the aggregate business result. The expected tax rate for other operations reflects the mix of business between UK and overseas non-insurance operations, which are taxed at a variety of rates. The rates will fluctuate from year to year dependent on the mix of profits.

c Taxes paid

During half year 2014, Prudential remitted £1.2 billion (half year 2013: £0.9 billion; full year 2013: £1.8 billion) of tax to revenue authorities, this includes £337 million (half year 2013: £182 million; full year 2013: £418 million) of corporation tax, £163 million (half year 2013: £96 million; full year 2013: £236 million) of other taxes and £651 million (half year 2013: £634 million; full year 2013: £1,143 million) collected on behalf of employees, customers and third parties.

The geographical split of taxes remitted by Prudential is as follows:

	2014 £m				2013 £m	
	Corporation taxes*	**Other taxes†**	**Taxes collected‡**	**Half year Total**	**Half year Total**	**Full year Total**
Asia	90	26	41	157	101	319
US	85	20	183	288	103	292
UK	161	116	424	701	706	1,181
Other	1	1	3	5	2	5
Total tax paid	337	163	651	1,151	912	1,797

* In certain countries such as the UK, the corporation tax payments for the Group's life insurance businesses are based on taxable profits which include policyholder investment returns on certain life insurance products.
† Other taxes paid includes property taxes, withholding taxes, customs duties, stamp duties, employer payroll taxes and irrecoverable indirect taxes.
‡ Taxes collected are other taxes that Prudential remits to tax authorities which it is obliged to collect from employees, customers and third parties which includes sales/value added tax/goods and services taxes, employee and annuitant payroll taxes.

B6: Earnings per share

		Half year 2014				
	Note	Before tax note B1.1 £m	Tax note B5 £m	Net of tax £m	Basic earnings per share pence	Diluted earnings per share pence
Based on operating profit based on longer-term investment returns		1,521	(369)	1,152	45.2p	45.1p
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	(45)	73	28	1.1p	1.1p
Amortisation of acquisition accounting adjustments		(44)	15	(29)	(1.1)p	(1.1)p
Costs of domestication of Hong Kong branch	D2	(8)	2	(6)	(0.2)p	(0.2)p
Based on profit for the period		1,424	(279)	1,145	45.0p	44.9p

		Half year 2013				
	Note	Before tax note B1.1 £m	Tax note B5 £m	Net of tax £m	Basic earnings per share pence	Diluted earnings per share pence
Based on operating profit based on longer-term investment returns		1,415	(340)	1,075	42.2p	42.1p
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	(755)	189	(566)	(22.2)p	(22.1)p
Amortisation of acquisition accounting adjustments		(30)	10	(20)	(0.8)p	(0.8)p
Loss attaching to held for sale Japan life business	D1	(124)	–	(124)	(4.9)p	(4.9)p
Based on profit for the period		506	(141)	365	14.3p	14.3p

		Full year 2013				
	Note	Before tax note B1.1 £m	Tax note B5 £m	Net of tax £m	Basic earnings per share pence	Diluted earnings per share pence
Based on operating profit based on longer-term investment returns		2,954	(638)	2,316	90.9p	90.7p
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	(1,110)	318	(792)	(31.1)p	(31.0)p
Amortisation of acquisition accounting adjustments		(72)	24	(48)	(1.9)p	(1.9)p
Loss attaching to held for sale Japan life business	D1	(102)	–	(102)	(4.0)p	(4.0)p
Costs of domestication of Hong Kong branch	D2	(35)	7	(28)	(1.1)p	(1.1)p
Based on profit for the year		1,635	(289)	1,346	52.8p	52.7p

Earnings per share are calculated based on earnings attributable to ordinary shareholders, after related tax and non-controlling interests. The weighted average number of shares for calculating earnings per share:

	Half year 2014 millions	Half year 2013 millions	Full year 2013 millions
Weighted average number of shares for calculation of:			
Basic earnings per share	2,547	2,548	2,548
Diluted earnings per share	2,551	2,553	2,552

B: Earnings performance continued

B7: Dividends

	Half year 2014		Half year 2013		Full year 2013	
	Pence per share	£m	Pence per share	£m	Pence per share	£m
Dividends relating to reporting period:						
Interim dividend (2014 and 2013)	**11.19p**	**287**	9.73p	249	9.73p	249
Final dividend (2013)	–	–	–	–	23.84p	610
Total	**11.19p**	**287**	9.73p	249	33.57p	859
Dividends declared and paid in reporting period:						
Current year interim dividend	–	–	–	–	9.73p	249
Final dividend for prior year	**23.84p**	**610**	20.79p	532	20.79p	532
Total	**23.84p**	**610**	20.79p	532	30.52p	781

Dividend per share

Interim dividends are recorded in the period in which they are paid. Final dividends are recorded in the period in which they are approved by shareholders. The final dividend for the year ended 31 December 2013 of 23.84 pence per ordinary share was paid to eligible shareholders on 22 May 2014 and the 2013 interim dividend of 9.73 pence per ordinary share was paid to eligible shareholders on 26 September 2013.

The 2014 interim dividend of 11.19 pence per ordinary share will be paid on 25 September 2014 in sterling to shareholders on the principal register and the Irish branch register at 6.00pm BST on 22 August 2014 (Record Date), and in Hong Kong dollars to shareholders on the Hong Kong branch register at 4.30pm Hong Kong time on the Record Date (HK Shareholders). Holders of US American Depositary Receipts (US Shareholders) will be paid their dividends in US dollars on or about 3 October 2014. The interim dividend will be paid on or about 2 October 2014 in Singapore dollars to shareholders with shares standing to the credit of their securities accounts with The Central Depository (Pte.) Limited (CDP) at 5.00pm Singapore time on the Record Date (SG Shareholders). The dividend payable to the HK Shareholders will be translated using the exchange rate quoted by the WM Company at the close of business on 11 August 2014. The exchange rate at which the dividend payable to the SG Shareholders will be translated into SG$, will be determined by CDP.

Shareholders on the principal register and Irish branch register will be able to participate in a Dividend Reinvestment Plan.

C: Balance sheet notes

C1: Analysis of Group position by segment and business type

To explain more comprehensively the assets, liabilities and capital of the Group's businesses, it is appropriate to provide analyses of the Group's statement of financial position by operating segment and type of business.

C1.1 Group statement of financial position – analysis by segment

		2014 £m								2013 £m	
		Insurance operations									
By operating segment	Note	**Asia** C2.1	**US** C2.2	**UK** C2.3	**Total insurance operations**	**Asset management operations** C2.4	**Unallocated to a segment (central operations)**	**Intra-group eliminations**	**30 Jun Group total**	**30 Jun Group total**	**31 Dec Group total**
Assets											
Intangible assets attributable to shareholders:											
Goodwill	C5.1(a)	228	–	–	228	1,230	–	–	1,458	1,474	1,461
Deferred acquisition costs and other intangible assets	C5.1(b)	1,767	4,037	84	5,888	20	36	–	5,944	5,538	5,295
Total		1,995	4,037	84	6,116	1,250	36	–	7,402	7,012	6,756
Intangible assets attributable to with-profits funds:											
Goodwill in respect of acquired subsidiaries for venture fund and other investment purposes		–	–	177	177	–	–	–	177	178	177
Deferred acquisition costs and other intangible assets		58	–	5	63	–	–	–	63	79	72
Total		58	–	182	240	–	–	–	240	257	249
Total		2,053	4,037	266	6,356	1,250	36	–	7,642	7,269	7,005
Deferred tax assets	C7.1	68	1,819	132	2,019	115	39	–	2,173	2,637	2,412
Other non-investment and non-cash assets note (i)		2,667	6,440	8,001	17,108	1,256	4,435	(8,932)	13,867	13,307	12,357
Investments of long-term business and other operations:											
Investment properties		1	26	11,727	11,754	–	–	–	11,754	10,583	11,477
Investments in joint ventures and associates accounted for using the equity method		303	–	513	816	95	–	–	911	696	809
Financial investments:											
Loans	C3.4	916	6,130	4,389	11,435	1,022	–	–	12,457	13,230	12,566
Equity securities and portfolio holdings in unit trusts		16,775	71,775	41,916	130,466	74	26	–	130,566	112,258	120,222
Debt securities	C3.3	19,958	30,586	81,680	132,224	1,953	–	–	134,177	138,256	132,905
Other investments		49	1,349	4,433	5,831	73	4	–	5,908	6,140	6,265
Deposits		693	–	12,319	13,012	45	–	–	13,057	13,542	12,213
Total investments		38,695	109,866	156,977	305,538	3,262	30	–	308,830	294,705	296,457
Assets held for sale	D1	875	–	–	875	–	–	–	875	1,079	916
Cash and cash equivalents		1,487	677	2,121	4,285	751	867	–	5,903	6,840	6,785
Total assets	C3.1	45,845	122,839	167,497	336,181	6,634	5,407	(8,932)	339,290	325,837	325,932

C: Balance sheet notes continued

C1: Analysis of Group position by segment and business type continued

		2014 £m								2013 £m	
		Insurance operations									
By operating segment	Note	**Asia**	**US**	**UK**	**Total insurance operations**	**Asset management operations**	**Unallocated to a segment (central operations)**	**Intra-group eliminations**	**30 Jun Group Total**	**30 Jun Group Total**	**31 Dec Group Total**
Equity and liabilities											
Equity											
Shareholders' equity		3,020	3,801	3,245	10,066	2,053	(1,494)	–	10,625	9,625	9,650
Non-controlling interests		1	–	–	1	–	–	–	1	6	1
Total equity		3,021	3,801	3,245	10,067	2,053	(1,494)	–	10,626	9,631	9,651
Liabilities											
Policyholder liabilities and unallocated surplus of with-profits funds:											
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)		35,372	112,009	137,619	285,000	–	–	(1,296)	283,704	272,728	273,953
Unallocated surplus of with-profits funds		1,985	–	11,059	13,044	–	–	–	13,044	11,434	12,061
Total policyholder liabilities and unallocated surplus of with-profits funds	C4	37,357	112,009	148,678	298,044	–	–	(1,296)	296,748	284,162	286,014
Core structural borrowings of shareholder-financed operations:											
Subordinated debt		–	–	–	–	–	3,597	–	3,597	3,161	3,662
Other		–	146	–	146	275	549	–	970	988	974
Total	C6.1	–	146	–	146	275	4,146	–	4,567	4,149	4,636
Operational borrowings attributable to shareholder-financed operations	C6.2(a)	–	222	71	293	–	1,950	–	2,243	2,530	2,152
Borrowings attributable to with-profits operations	C6.2(b)	–	–	864	864	–	–	–	864	924	895
Deferred tax liabilities	C7.1	645	1,997	1,184	3,826	18	11		3,855	4,102	3,778
Other non-insurance liabilities[note (ii)]		3,994	4,664	13,455	22,113	4,288	794	(7,636)	19,559	19,313	17,938
Liabilities held for sale	D1	828	–	–	828	–	–	–	828	1,026	868
Total liabilities		42,824	119,038	164,252	326,114	4,581	6,901	(8,932)	328,664	316,206	316,281
Total equity and liabilities	C3.1	45,845	122,839	167,497	336,181	6,634	5,407	(8,932)	339,290	325,837	325,932

Notes

(i) The main component of the other non-investment and non-cash assets of £13,867 million (30 June 2013: £13,307 million; 31 December 2013: £12,357 million) is the reinsurers' share of contract liabilities of £6,743 million (30 June 2013: £7,204 million; 31 December 2013: £6,838 million). As set out in note C2.2 these amounts relate primarily to the REALIC business of the Group's US insurance operations.

Within other non-investment and non-cash assets are premiums receivable of £317 million (30 June 2013: £310 million; 31 December 2013: £345 million) of which approximately two-thirds are due within one year. The remaining one-third, due after one year, relates to products where charges are levied against premiums in future years.

Also included within other non-investment and non-cash assets are property, plant and equipment of £910 million (30 June 2013: £868 million; 31 December 2013: £920 million). The Group made additions to property, plant and equipment of £58 million in half year 2014 (half year 2013: £146 million; full year 2013: £221 million).

(ii) Within other non-insurance liabilities are other creditors of £4,999 million (30 June 2013: £3,743 million; 31 December 2013: £3,307 million) of which £4,720 million (30 June 2013: £3,487 million; 31 December 2013: £3,046 million) are due within one year.

C1.2 Group statement of financial position – analysis by business type

		2014 £m							2013 £m	
		Policyholder	Shareholder-backed business							
	Note	Participating funds	Unit-linked and variable annuity	Non-linked business	Asset management operations	Unallocated to a segment (central operations)	Intra-group eliminations	30 Jun Group Total	30 Jun Group Total	31 Dec Group Total
Assets										
Intangible assets attributable to shareholders:										
Goodwill	C5.1(a)	–	–	228	1,230	–	–	1,458	1,474	1,461
Deferred acquisition costs and other intangible assets	C5.1(b)	–	–	5,888	20	36	–	5,944	5,538	5,295
Total		–	–	6,116	1,250	36	–	7,402	7,012	6,756
Intangible assets attributable to with-profits funds:										
In respect of acquired subsidiaries for venture fund and other investment purposes		177	–	–	–	–	–	177	178	177
Deferred acquisition costs and other intangible assets		63	–	–	–	–	–	63	79	72
Total		240	–	–	–	–	–	240	257	249
Total		240	–	6,116	1,250	36	–	7,642	7,269	7,005
Deferred tax assets	C7.1	74	–	1,945	115	39	–	2,173	2,637	2,412
Other non-investment and non-cash assets*		4,427	693	9,287	1,256	4,435	(6,231)	13,867	13,307	12,357
Investments of long-term business and other operations:										
Investment properties		9,430	652	1,672	–	–	–	11,754	10,583	11,477
Investments in joint ventures and associates accounted for using the equity method		449	–	367	95	–	–	911	696	809
Financial investments:										
Loans	C3.4	3,417	–	8,018	1,022	–	–	12,457	13,230	12,566
Equity securities and portfolio holdings in unit trusts		32,104	97,363	999	74	26	–	130,566	112,258	120,222
Debt securities	C3.3	56,106	9,859	66,259	1,953	–	–	134,177	138,256	132,905
Other investments		4,145	38	1,648	73	4	–	5,908	6,140	6,265
Deposits		10,896	926	1,190	45	–	–	13,057	13,542	12,213
Total investments		116,547	108,838	80,153	3,262	30	–	308,830	294,705	296,457
Assets held for sale	D1	–	303	572	–	–	–	875	1,079	916
Cash and cash equivalents		1,671	831	1,783	751	867	–	5,903	6,840	6,785
Total assets		122,959	110,665	99,856	6,634	5,407	(6,231)	339,290	325,837	325,932

* Participating funds business in the table above is presented after the elimination on consolidation of the balances relating to an intra-group reinsurance contract entered into during the period between the UK with-profits and Asia with-profits operations. In the segmental analysis presented in note C1.1, the balances are presented before elimination in the individual insurance operations segment, with the adjustment presented separately under intra-group eliminations.

C: Balance sheet notes continued

C1: Analysis of Group position by segment and business type continued

		2014 £m							2013 £m	
		Policyholder	Shareholder-backed business							
	Note	Participating funds	Unit-linked and variable annuity	Non-linked business	Asset management operations	Unallocated to a segment (central operations)	Intra-group eliminations	30 Jun Group Total	30 Jun Group Total	31 Dec Group Total
Equity and liabilities										
Equity										
Shareholders' equity		–	–	10,066	2,053	(1,494)	–	10,625	9,625	9,650
Non-controlling interests		–	–	1	–	–	–	1	6	1
Total equity		–	–	10,067	2,053	(1,494)	–	10,626	9,631	9,651
Liabilities										
Policyholder liabilities and unallocated surplus of with-profits funds:										
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)*		99,100	107,781	76,823	–	–	–	283,704	272,728	273,953
Unallocated surplus of with-profits funds		13,044	–	–	–	–	–	13,044	11,434	12,061
Total policyholder liabilities and unallocated surplus of with-profits funds	C4	112,144	107,781	76,823	–	–	–	296,748	284,162	286,014
Core structural borrowings of shareholder-financed operations:										
Subordinated debt		–	–	–	–	3,597	–	3,597	3,161	3,662
Other		–	–	146	275	549	–	970	988	974
Total	C6.1	–	–	146	275	4,146	–	4,567	4,149	4,636
Operational borrowings attributable to shareholder-financed operations	C6.2(a)	–	3	290	–	1,950	–	2,243	2,530	2,152
Borrowings attributable to with-profits operations	C6.2(b)	864	–	–	–	–	–	864	924	895
Deferred tax liabilities	C7.1	1,211	47	2,568	18	11	–	3,855	4,102	3,778
Other non-insurance liabilities*		8,740	2,531	9,437	4,288	794	(6,231)	19,559	19,313	17,938
Liabilities held for sale	D1	–	303	525	–	–	–	828	1,026	868
Total liabilities		122,959	110,665	89,789	4,581	6,901	(6,231)	328,664	316,206	316,281
Total equity and liabilities		122,959	110,665	99,856	6,634	5,407	(6,231)	339,290	325,837	325,932

* Participating funds business in the table above is presented after the elimination on consolidation of the balances relating to an intra-group reinsurance contract entered into during the period between the UK with-profits and Asia with-profits operations. In the segmental analysis presented in note C1.1, the balances are presented before elimination in the individual insurance operations segment, with the adjustment presented separately under intra-group eliminations.

C2: Analysis of segment position by business type

To show the statement of financial position by reference to the differing degrees of policyholder and shareholder economic interest of the different types of business, the analysis below is structured to show separately assets and liabilities of each segment by business type.

C2.1 Asia insurance operations

		2014 £m				2013 £m	
	Note	With-profits business note (i)	Unit-linked assets and liabilities	Other business	30 Jun Total	30 Jun Total	31 Dec Total
Assets							
Intangible assets attributable to shareholders:							
Goodwill		–	–	228	228	244	231
Deferred acquisition costs and other intangible assets		–	–	1,767	1,767	1,103	1,026
Total		–	–	1,995	1,995	1,347	1,257
Intangible assets attributable to with-profits funds:							
Deferred acquisition costs and other intangible assets		58	–	–	58	73	66
Deferred tax assets		–	–	68	68	68	55
Other non-investment and non-cash assets		1,795	141	731	2,667	1,164	1,073
Investments of long-term business and other operations:							
Investment properties		–	–	1	1	2	1
Investments in joint ventures and associates accounted for using the equity method		–	–	303	303	328	268
Financial investments:							
Loans	C3.4	511	–	405	916	1,004	922
Equity securities and portfolio holdings in unit trusts		6,057	10,054	664	16,775	14,101	14,383
Debt securities	C3.3	10,661	2,443	6,854	19,958	20,081	18,554
Other investments		17	22	10	49	76	41
Deposits		183	197	313	693	1,141	896
Total investments		17,429	12,716	8,550	38,695	36,733	35,065
Assets held for sale		–	303	572	875	1,079	916
Cash and cash equivalents		335	371	781	1,487	1,644	1,522
Total assets		19,617	13,531	12,697	45,845	42,108	39,954
Equity and liabilities							
Equity							
Shareholders' equity		–	–	3,020	3,020	3,003	2,795
Non-controlling interests		–	–	1	1	4	1
Total equity		–	–	3,021	3,021	3,007	2,796
Liabilities							
Policyholder liabilities and unallocated surplus of with-profits funds:							
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)		15,464	12,638	7,270	35,372	33,223	31,910
Unallocated surplus of with-profits funds note (ii)	D2	1,985	–	–	1,985	84	77
Total	C4.1(b)	17,449	12,638	7,270	37,357	33,307	31,987
Operational borrowings attributable to shareholder-financed operations		–	–	–	–	5	–
Deferred tax liabilities		424	47	174	645	641	594
Other non-insurance liabilities		1,744	543	1,707	3,994	4,122	3,709
Liabilities held for sale		–	303	525	828	1,026	868
Total liabilities		19,617	13,531	9,676	42,824	39,101	37,158
Total equity and liabilities		19,617	13,531	12,697	45,845	42,108	39,954

Notes

(i) The statement of financial position for with-profits business comprises the with-profits assets and liabilities of the Hong Kong, Malaysia and Singapore operations. Assets and liabilities of other participating business are included in the column for other business.

(ii) On 1 January 2014, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. From this date, the unallocated surplus of the Hong Kong with-profits business is reported within the Asia insurance segment. Up until 31 December 2013, for the purpose of the presentation of unallocated surplus of with-profits within the statement of financial position, the Hong Kong branch balance was reported within the unallocated surplus of the PAC with-profits sub-fund of the UK insurance operations.

C: Balance sheet notes continued

C2: Analysis of segment position by business type continued

C2.2 US insurance operations

	Note	2014 £m			2013 £m	
		Variable annuity separate account assets and liabilities note (i)	**Fixed annuity, GIC and other business**	**30 Jun Total**	**30 Jun Total**	**31 Dec Total**
Assets						
Intangible assets attributable to shareholders:						
Deferred acquisition costs and other intangibles		–	4,037	4,037	4,300	4,140
Total		–	4,037	4,037	4,300	4,140
Deferred tax assets		–	1,819	1,819	2,232	2,042
Other non-investment and non-cash assets note (iv)		–	6,440	6,440	7,255	6,710
Investments of long-term business and other operations:						
Investment properties		–	26	26	30	28
Financial investments:						
Loans	C3.4	–	6,130	6,130	6,691	6,375
Equity securities and portfolio holdings in unit trusts note (iii)		71,453	322	71,775	60,385	66,008
Debt securities	C3.3	–	30,586	30,586	33,368	30,292
Other investments note (ii)		–	1,349	1,349	1,867	1,557
Total investments		71,453	38,413	109,866	102,341	104,260
Cash and cash equivalents		–	677	677	678	604
Total assets		71,453	51,386	122,839	116,806	117,756
Equity and liabilities						
Equity						
Shareholders' equity note (v)		–	3,801	3,801	3,598	3,446
Total equity		–	3,801	3,801	3,598	3,446
Liabilities						
Policyholder liabilities:						
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)		71,453	40,556	112,009	106,215	107,411
Total	C4.1(c)	71,453	40,556	112,009	106,215	107,411
Core structural borrowings of shareholder-financed operations		–	146	146	164	150
Operational borrowings attributable to shareholder-financed operations		–	222	222	23	142
Deferred tax liabilities		–	1,997	1,997	2,155	1,948
Other non-insurance liabilities		–	4,664	4,664	4,651	4,659
Total liabilities		71,453	47,585	119,038	113,208	114,310
Total equity and liabilities		71,453	51,386	122,839	116,806	117,756

Notes

(i) These amounts are for separate account assets and liabilities for all variable annuity products comprising those with and without guarantees. Assets and liabilities attaching to variable annuity business that are not held in the separate account, for example in respect of guarantees, are shown within the statement of financial position of other business.

(ii) Other investments comprise:

	2014 £m	2013 £m	
	30 Jun	**30 Jun**	**31 Dec**
Derivative assets*	600	1,010	766
Partnerships in investment pools and other†	749	857	791
	1,349	1,867	1,557

* After taking account of the derivative liabilities of £284 million (30 June 2013: £555 million; 31 December 2013: £515 million), which are also included in other non-insurance liabilities, the derivative position for US operations is a net asset of £316 million (30 June 2013: net asset of £455 million; 31 December 2013: net asset of £251 million).

† Partnerships in investment pools and other comprise primarily investments in limited partnerships. These include interests in the PPM America Private Equity Fund and diversified investments in other partnerships by independent money managers that generally invest in various equities and fixed income loans and securities.

(iii) Equity securities and portfolio holdings in unit trusts includes investments in mutual funds, the majority of which are equity-based.

(iv) Included within other non-investment and non-cash assets of £6,440 million (30 June 2013: £7,255 million; 31 December 2013: £6,710 million) were balances of £5,842 million (30 June 2013: £6,360 million; 31 December 2013: £6,065 million) for reinsurers' share of insurance contract liabilities. Of the £5,842 million as at 30 June 2014, £5,179 million related to the reinsurance ceded by the REALIC business (30 June 2013: £5,550 million; 31 December 2013: £5,410 million). REALIC holds collateral for certain of these reinsurance arrangements with a corresponding funds withheld liability. As of 30 June 2014, the funds withheld liability of £2,019 million (30 June 2013: £2,206 million; 31 December 2013: £2,051 million) was recorded within other non-insurance liabilities.

(v) Changes in shareholders' equity

	2014 £m	**2013** £m	
	Half year	**Half year**	**Full year**
Operating profit based on longer-term investment returns[B1.1]	686	582	1,243
Short-term fluctuations in investment returns[B1.2]	(226)	(441)	(625)
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC	(40)	(27)	(65)
Profit before shareholder tax	420	114	553
Tax[B5]	(107)	(27)	(101)
Profit for the period	313	87	452

	2014 £m	**2013** £m	
	Half year	**Half year**	**Full year**
Profit for the period (as above)	313	87	452
Items recognised in other comprehensive income:			
Exchange movements	(122)	293	(32)
Unrealised valuation movements on securities classified as available-for sale:			
Unrealised holding gains (losses) arising during the period	1,060	(1,665)	(2,025)
Deduct net gains included in the income statement	(37)	(42)	(64)
Total unrealised valuation movements	1,023	(1,707)	(2,089)
Related change in amortisation of deferred acquisition costs[C5.1(b)]	(212)	419	498
Related tax	(284)	451	557
Total other comprehensive income (loss)	405	(544)	(1,066)
Total comprehensive income (loss) for the period	718	(457)	(614)
Dividends, interest payments to central companies and other movements	(363)	(288)	(283)
Net increase (decrease) in equity	355	(745)	(897)
Shareholders' equity at beginning of period	3,446	4,343	4,343
Shareholders' equity at end of period	3,801	3,598	3,446

C: Balance sheet notes continued

C2: Analysis of segment position by business type continued

C2.3 UK insurance operations

Of the total investments of £157 billion in UK insurance operations, £99 billion of investments are held by SAIF and the PAC WPSF. Shareholders are exposed only indirectly to value movements on these assets.

By operating segment	Note	Scottish Amicable Insurance Fund note (ii)	PAC with-profits sub-fund note (i)	Other funds and subsidiaries: Unit-linked assets and liabilities	Other funds and subsidiaries: Annuity and other long-term business	Other funds and subsidiaries: Total	2014 £m 30 Jun Total	2013 £m 30 Jun Total	2013 £m 31 Dec Total
Assets									
Intangible assets attributable to shareholders:									
Deferred acquisition costs and other intangible assets		–	–	–	84	84	84	98	90
Total		–	–	–	84	84	84	98	90
Intangible assets attributable to with-profits funds:									
In respect of acquired subsidiaries for venture fund and other investment purposes		–	177	–	–	–	177	178	177
Deferred acquisition costs		–	5	–	–	–	5	6	6
Total		–	182	–	–	–	182	184	183
Total		–	182	–	84	84	266	282	273
Deferred tax assets		–	74	–	58	58	132	181	142
Other non-investment and non-cash assets		390	4,943	552	2,116	2,668	8,001	5,641	5,808
Investments of long-term business and other operations:									
Investment properties		477	8,953	652	1,645	2,297	11,727	10,551	11,448
Investments in joint ventures and associates accounted for using the equity method		–	449	–	64	64	513	274	449
Financial investments:									
Loans	C3.4	81	2,825	–	1,483	1,483	4,389	4,313	4,173
Equity securities and portfolio holdings in unit trusts		2,399	23,648	15,856	13	15,869	41,916	37,713	39,745
Debt securities	C3.3	2,818	42,627	7,416	28,819	36,235	81,680	82,854	82,014
Other investments note (iii)		279	3,849	16	289	305	4,433	4,098	4,603
Deposits		809	9,904	729	877	1,606	12,319	12,365	11,252
Total investments		6,863	92,255	24,669	33,190	57,859	156,977	152,168	153,684
Cash and cash equivalents		171	1,165	460	325	785	2,121	2,755	2,586
Total assets		7,424	98,619	25,681	35,773	61,454	167,497	161,027	162,493

	Note	2014 £m						2013 £m	
				Other funds and subsidiaries					
	Note	Scottish Amicable Insurance Fund note (ii)	PAC with-profits sub-fund note (i)	Unit-linked assets and liabilities	Annuity and other long-term business	Total	30 Jun Total	30 Jun Total	31 Dec Total
Equity and liabilities									
Equity									
Shareholders' equity		–	–	–	3,245	3,245	3,245	3,044	2,998
Non-controlling interests		–	–	–	–	–	–	2	–
Total equity		–	–	–	3,245	3,245	3,245	3,046	2,998
Liabilities									
Policyholder liabilities and unallocated surplus of with-profits funds:									
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)		6,890	78,042	23,690	28,997	52,687	137,619	133,290	134,632
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds)	D2	–	11,059	–	–	–	11,059	11,350	11,984
Total	C4.1(d)	6,890	89,101	23,690	28,997	52,687	148,678	144,640	146,616
Operational borrowings attributable to shareholder-financed operations		–	–	3	68	71	71	76	74
Borrowings attributable to with-profits funds		11	853	–	–	–	864	924	895
Deferred tax liabilities		46	741	–	397	397	1,184	1,289	1,213
Other non-insurance liabilities		477	7,924	1,988	3,066	5,054	13,455	11,052	10,697
Total liabilities		7,424	98,619	25,681	32,528	58,209	164,252	157,981	159,495
Total equity and liabilities		7,424	98,619	25,681	35,773	61,454	167,497	161,027	162,493

Notes

(i) The PAC with-profits sub-fund (WPSF) mainly contains with-profits business but it also contains some non-profit business (unit-linked, term assurances and annuities). Included in the PAC with-profits fund is £11.2 billion (30 June 2013: £13.5 billion; 31 December 2013: £12.2 billion) of liabilities for non-profits annuities. The WPSF's profits are apportioned 90 per cent to its policyholders and 10 per cent to shareholders as surplus for distribution is determined via the annual actuarial valuation. For the purposes of this table and subsequent explanation, references to the WPSF also include, for convenience, the amounts attaching to the Defined Charges Participating Sub-fund which comprises 3.6 per cent of the total assets of the WPSF. The unallocated surplus of with-profits funds are for PAC which at 30 June 2013 and 31 December 2013 included amounts attributable to the now domesticated Hong Kong branch.

(ii) The fund is solely for the benefit of policyholders of SAIF. Shareholders have no interest in the profits of this fund although they are entitled to asset management fees on this business. SAIF is a separate sub-fund within the PAC long-term business fund.

(iii) Other investments comprise:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Derivative assets*	1,262	894	1,472
Partnerships in investment pools and other†	3,171	3,204	3,131
	4,433	4,098	4,603

* After including derivative liabilities of £751 million (30 June 2013: £1,289 million; 31 December 2013: £804 million), which are also included in the statement of financial position, the overall derivative position was a net asset of £511 million (30 June 2013: net liability of £395 million; 31 December 2013: net asset of £668 million).

† Partnerships in investment pools and other comprise mainly investments held by the PAC with-profits fund. These investments are primarily investments in limited partnerships and additionally, investments in property funds.

C: Balance sheet notes continued

C2: Analysis of segment position by business type continued

C2.4 Asset management operations

		2014 £m				2013 £m	
	Note	**M&G** note (i)	**US**	**Eastspring Investments**	**30 Jun Total**	**30 Jun Total**	**31 Dec Total**
Assets							
Intangible assets:							
Goodwill		1,153	16	61	1,230	1,230	1,230
Deferred acquisition costs and other intangible assets		17	2	1	20	15	20
Total		1,170	18	62	1,250	1,245	1,250
Other non-investment and non-cash assets		1,111	200	60	1,371	2,113	1,475
Investments in joint ventures and associates accounted for using the equity method		34	–	61	95	94	92
Financial investments:							
Loans	C3.4	1,022	–	–	1,022	1,222	1,096
Equity securities and portfolio holdings in unit trusts		59	–	15	74	59	65
Debt securities	C3.3	1,953	–	–	1,953	1,953	2,045
Other investments		60	13	–	73	69	61
Deposits		–	14	31	45	36	65
Total investments		3,128	27	107	3,262	3,433	3,424
Cash and cash equivalents		599	61	91	751	968	1,562
Total assets		6,008	306	320	6,634	7,759	7,711
Equity and liabilities							
Equity							
Shareholders' equity		1,659	141	253	2,053	2,085	1,991
Total equity		1,659	141	253	2,053	2,085	1,991
Liabilities							
Core structural borrowing of shareholder-financed operations		275	–	–	275	275	275
Intra-group debt represented by operational borrowings at Group level note (ii)		1,950	–	–	1,950	2,422	1,933
Other non-insurance liabilities note (iii)		2,124	165	67	2,356	2,977	3,512
Total liabilities		4,349	165	67	4,581	5,674	5,720
Total equity and liabilities		6,008	306	320	6,634	7,759	7,711

Notes

(i) The M&G statement of financial position includes the assets and liabilities in respect of Prudential Capital.

(ii) Intra-group debt represented by operational borrowings at Group level

Operational borrowings for M&G are in respect of Prudential Capital's short-term fixed income security programme and comprise:

	2014 £m	2013 £m	
	30 Jun	**30 Jun**	**31 Dec**
Commercial paper	1,650	2,123	1,634
Medium Term Notes	300	299	299
Total intra-group debt represented by operational borrowings at Group level	1,950	2,422	1,933

(iii) Other non-insurance liabilities consist primarily of intra-group balances, derivative liabilities and other creditors.

C3: Assets and liabilities – classification and measurement

C3.1 Group assets and liabilities – classification

The classification of the Group's assets and liabilities, and its corresponding accounting carrying values reflect the requirements of IFRS. For financial investments the basis of valuation reflects the Group's application of IAS 39 'Financial Instruments: Recognition and Measurement' as described further below. Where assets and liabilities have been valued at fair value or measured on a different basis but fair value is disclosed, the Group has followed the principles under IFRS 13 'Fair value measurement'. The basis applied is summarised below:

	30 Jun 2014 £m				
	At fair value		Cost/ amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Assets					
Intangible assets attributable to shareholders:					
Goodwill	–	–	1,458	1,458	
Deferred acquisition costs and other intangible assets	–	–	5,944	5,944	
Total	–	–	7,402	7,402	
Intangible assets attributable to with-profits funds:					
In respect of acquired subsidiaries for venture fund and other investment purposes	–	–	177	177	
Deferred acquisition costs and other intangible assets	–	–	63	63	
Total	–	–	240	240	
Total intangible assets	–	–	7,642	7,642	
Other non-investment and non-cash assets:					
Property, plant and equipment	–	–	910	910	
Reinsurers' share of insurance contract liabilities	–	–	6,743	6,743	
Deferred tax assets	–	–	2,173	2,173	
Current tax recoverable	–	–	158	158	
Accrued investment income	–	–	2,413	2,413	2,413
Other debtors	–	–	3,643	3,643	3,643
Total	–	–	16,040	16,040	
Investments of long-term business and other operations: note (ii)					
Investment properties	11,754	–	–	11,754	11,754
Investments accounted for using the equity method	–	–	911	911	
Loans	2,123	–	10,334	12,457	12,987
Equity securities and portfolio holdings in unit trusts	130,566	–	–	130,566	130,566
Debt securities	103,666	30,511	–	134,177	134,177
Other investments	5,908	–	–	5,908	5,908
Deposits	–	–	13,057	13,057	13,057
Total investments	254,017	30,511	24,302	308,830	
Assets held for sale	875	–	–	875	875
Cash and cash equivalents	–	–	5,903	5,903	5,903
Total assets	254,892	30,511	53,887	339,290	

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	30 Jun 2014 £m				
	At fair value		Cost/ amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Liabilities					
Policyholder liabilities and unallocated surplus of with-profits funds:					
Insurance contract liabilities	–	–	227,779	227,779	
Investment contract liabilities with discretionary participation features[note (iii)]	–	–	35,636	35,636	
Investment contract liabilities without discretionary participation features	17,840	–	2,449	20,289	20,290
Unallocated surplus of with-profits funds	–	–	13,044	13,044	
Total	17,840	–	278,908	296,748	
Core structural borrowings of shareholder-financed operations	–	–	4,567	4,567	5,056
Other borrowings:					
Operational borrowings attributable to shareholder-financed operations	–	–	2,243	2,243	2,243
Borrowings attributable to with-profits operations	–	–	864	864	879
Other non-insurance liabilities:					
Obligations under funding, securities lending and sale and repurchase agreements	–	–	2,188	2,188	2,200
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	5,262	–	–	5,262	5,262
Deferred tax liabilities	–	–	3,855	3,855	
Current tax liabilities	–	–	475	475	
Accruals and deferred income	–	–	731	731	
Other creditors	279	–	4,720	4,999	4,999
Provisions	–	–	534	534	
Derivative liabilities	1,400	–	–	1,400	1,400
Other liabilities	2,019	–	1,951	3,970	3,970
Total	8,960	–	14,454	23,414	
Liabilities held for sale	828	–	–	828	828
Total liabilities	27,628	–	301,036	328,664	

	30 Jun 2013 £m				
	At fair value		Cost/ amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Assets					
Intangible assets attributable to shareholders:					
Goodwill	–	–	1,474	1,474	
Deferred acquisition costs and other intangible assets	–	–	5,538	5,538	
Total	–	–	7,012	7,012	
Intangible assets attributable to with-profits funds:					
In respect of acquired subsidiaries for venture fund and other investment purposes	–	–	178	178	
Deferred acquisition costs and other intangible assets	–	–	79	79	
Total	–	–	257	257	
Total intangible assets	–	–	7,269	7,269	
Other non-investment and non-cash assets:					
Property, plant and equipment	–	–	868	868	
Reinsurers' share of insurance contract liabilities	–	–	7,204	7,204	
Deferred tax assets	–	–	2,637	2,637	
Current tax recoverable	–	–	191	191	
Accrued investment income	–	–	2,726	2,726	2,726
Other debtors	–	–	2,318	2,318	2,318
Total	–	–	15,944	15,944	
Investments of long-term business and other operations: note (ii)					
Investment properties	10,583	–	–	10,583	10,583
Investments accounted for using the equity method	–	–	696	696	
Loans	2,268	–	10,962	13,230	13,404
Equity securities and portfolio holdings in unit trusts	112,258	–	–	112,258	112,258
Debt securities	105,043	33,213	–	138,256	138,256
Other investments	6,140	–	–	6,140	6,140
Deposits	–	–	13,542	13,542	13,542
Total investments	236,292	33,213	25,200	294,705	
Assets held for sale	1,079	–	–	1,079	1,079
Cash and cash equivalents	–	–	6,840	6,840	6,840
Total assets	237,371	33,213	55,253	325,837	

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	30 Jun 2013 £m				
	At fair value		Cost/amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Liabilities					
Policyholder liabilities and unallocated surplus of with-profits funds:					
Insurance contract liabilities	–	–	219,461	219,461	
Investment contract liabilities with discretionary participation features note (iii)	–	–	33,402	33,402	
Investment contract liabilities without discretionary participation features	17,342	–	2,523	19,865	19,872
Unallocated surplus of with-profits funds	–	–	11,434	11,434	
Total	17,342	–	266,820	284,162	
Core structural borrowings of shareholder-financed operations	–	–	4,149	4,149	4,534
Other borrowings:					
Operational borrowings attributable to shareholder-financed operations	–	–	2,530	2,530	2,530
Borrowings attributable to with-profits operations	22	–	902	924	924
Other non-insurance liabilities:					
Obligations under funding, securities lending and sale and repurchase agreements	–	–	2,889	2,889	2,899
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	5,394	–	–	5,394	5,394
Deferred tax liabilities	–	–	4,102	4,102	
Current tax liabilities	–	–	325	325	
Accruals and deferred income	–	–	538	538	
Other creditors	256	–	3,487	3,743	3,743
Provisions	–	–	537	537	
Derivative liabilities	2,226	–	–	2,226	2,226
Other liabilities	2,206	–	1,455	3,661	3,661
Total	10,082	–	13,333	23,415	
Liabilities held for sale	1,026	–	–	1,026	1,026
Total liabilities	28,472	–	287,734	316,206	

	31 Dec 2013 £m				
	At fair value		Cost/ amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Assets					
Intangible assets attributable to shareholders:					
Goodwill	–	–	1,461	1,461	
Deferred acquisition costs and other intangible assets	–	–	5,295	5,295	
Total	–	–	6,756	6,756	
Intangible assets attributable to with-profits funds:					
In respect of acquired subsidiaries for venture fund and other investment purposes	–	–	177	177	
Deferred acquisition costs and other intangible assets	–	–	72	72	
Total	–	–	249	249	
Total intangible assets	–	–	7,005	7,005	
Other non-investment and non-cash assets:					
Property, plant and equipment	–	–	920	920	
Reinsurers' share of insurance contract liabilities	–	–	6,838	6,838	
Deferred tax assets	–	–	2,412	2,412	
Current tax recoverable	–	–	244	244	
Accrued investment income	–	–	2,609	2,609	2,609
Other debtors	–	–	1,746	1,746	1,746
Total	–	–	14,769	14,769	
Investments of long-term business and other operations: note (ii)					
Investment properties	11,477	–	–	11,477	11,477
Investments accounted for using the equity method	–	–	809	809	
Loans	2,137	–	10,429	12,566	12,995
Equity securities and portfolio holdings in unit trusts	120,222	–	–	120,222	120,222
Debt securities	102,700	30,205	–	132,905	132,905
Other investments	6,265	–	–	6,265	6,265
Deposits	–	–	12,213	12,213	12,213
Total investments	242,801	30,205	23,451	296,457	
Assets held for sale	916	–	–	916	916
Cash and cash equivalents	–	–	6,785	6,785	6,785
Total assets	243,717	30,205	52,010	325,932	

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	31 Dec 2013 £m				
	At fair value		Cost/ amortised cost/IFRS 4 basis value note (i)	Total carrying value	Fair value, where applicable
	Through profit and loss	Available-for-sale			
Liabilities					
Policyholder liabilities and unallocated surplus of with-profits funds:					
Insurance contract liabilities	–	–	218,185	218,185	
Investment contract liabilities with discretionary participation features note (iii)	–	–	35,592	35,592	
Investment contract liabilities without discretionary participation features	17,736	–	2,440	20,176	20,177
Unallocated surplus of with-profits funds	–	–	12,061	12,061	
Total	17,736	–	268,278	286,014	
Core structural borrowings of shareholder-financed operations	–	–	4,636	4,636	5,066
Other borrowings:					
Operational borrowings attributable to shareholder-financed operations	–	–	2,152	2,152	2,152
Borrowings attributable to with-profits operations	18	–	877	895	909
Other non-insurance liabilities:					
Obligations under funding, securities lending and sale and repurchase agreements	–	–	2,074	2,074	2,085
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	5,278	–	–	5,278	5,278
Deferred tax liabilities	–	–	3,778	3,778	
Current tax liabilities	–	–	395	395	
Accruals and deferred income	–	–	824	824	
Other creditors	263	–	3,044	3,307	3,307
Provisions	–	–	635	635	
Derivative liabilities	1,689	–	–	1,689	1,689
Other liabilities	2,051	–	1,685	3,736	3,736
Total	9,281	–	12,435	21,716	
Liabilities held for sale	868	–	–	868	868
Total liabilities	27,903	–	288,378	316,281	

Notes

(i) Assets carried at cost or amortised cost are subject to impairment testing where appropriate under IFRS requirements. This category also includes assets which are valued by reference to specific IFRS standards such as reinsurers' share of insurance contract liabilities, deferred tax assets and investments accounted for under the equity method.

(ii) Realised gains and losses on the Group's investments for half year 2014 recognised in the income statement amounted to a net gain of £1.8 billion (30 June 2013: £0.8 billion; 31 December 2013: £2.5 billion).

(iii) The carrying value of investment contracts with discretionary participation features is determined on an IFRS 4 basis. It is impractical to determine the fair value of these contracts due to the lack of a reliable basis to measure the participation features.

C: Balance sheet notes

C3.2 Group assets and liabilities – measurement

a Determination of fair value

The fair values of the assets and liabilities of the Group have been determined on the following bases.

The fair values of the financial instruments for which fair valuation is required under IFRS are determined by the use of current market bid prices for exchange-quoted investments, or by using quotations from independent third parties, such as brokers and pricing services or by using appropriate valuation techniques.

The estimated fair value of derivative financial instruments reflects the estimated amount the Group would receive or pay in an arm's length transaction. This amount is determined using quoted prices if exchange listed, quotations from independent third parties or valued internally using standard market practices.

The loans and receivables have been shown net of provisions for impairment. The fair value of loans has been estimated from discounted cash flows expected to be received. The rate of discount used was the market rate of interest where applicable.

The fair value of investment properties is based on market values as assessed by professionally qualified external valuers or by the Group's qualified surveyors.

The fair value of the subordinated and senior debt issued by the parent company is determined using the quoted prices from independent third parties.

The fair value of financial liabilities (other than derivative financial instruments) is determined using discounted cash flows of the amounts expected to be paid.

b Fair value hierarchy of financial instruments measured at fair value on a recurring basis

The table overleaf shows the financial instruments carried at fair value analysed by level of the IFRS 13 'Fair Value Measurement' defined fair value hierarchy. This hierarchy is based on the inputs to the fair value measurement and reflects the lowest level input that is significant to that measurement.

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	30 Jun 2014 £m			
	Level 1	Level 2	Level 3	Total
	Quoted prices (unadjusted) in active markets	Valuation based on significant observable market inputs	Valuation based on significant unobservable market inputs	
Analysis of financial investments, net of derivative liabilities by business type				
With-profits				
Equity securities and portfolio holdings in unit trusts	28,796	2,711	597	32,104
Debt securities	15,870	39,756	480	56,106
Other investments (including derivative assets)	64	1,037	3,044	4,145
Derivative liabilities	(45)	(394)	–	(439)
Total financial investments, net of derivative liabilities	44,685	43,110	4,121	91,916
Percentage of total	49%	47%	4%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	97,125	200	38	97,363
Debt securities	3,546	6,313	–	9,859
Other investments (including derivative assets)	5	33	–	38
Derivative liabilities	–	(1)	–	(1)
Total financial investments, net of derivative liabilities	100,676	6,545	38	107,259
Percentage of total	94%	6%	0%	100%
Non-linked shareholder-backed				
Loans	–	259	1,864	2,123
Equity securities and portfolio holdings in unit trusts	986	79	34	1,099
Debt securities	14,271	53,853	88	68,212
Other investments (including derivative assets)	–	959	766	1,725
Derivative liabilities	–	(750)	(210)	(960)
Total financial investments, net of derivative liabilities	15,257	54,400	2,542	72,199
Percentage of total	21%	75%	4%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans*	–	259	1,864	2,123
Equity securities and portfolio holdings in unit trusts	126,907	2,990	669	130,566
Debt securities	33,687	99,922	568	134,177
Other investments (including derivative assets)	69	2,029	3,810	5,908
Derivative liabilities	(45)	(1,145)	(210)	(1,400)
Total financial investments, net of derivative liabilities	160,618	104,055	6,701	271,374
Investment contracts liabilities without discretionary participation features held at fair value	–	(17,840)	–	(17,840)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(3,902)	(134)	(1,226)	(5,262)
Other financial liabilities held at fair value	–	(279)	(2,019)	(2,298)
Total financial instruments at fair value	156,716	85,802	3,456	245,974
Percentage of total	64%	35%	1%	100%

* Loans in the table above are those classified as fair value through profit and loss in note C3.1.

	30 Jun 2013 £m			
	Level 1	Level 2	Level 3	Total
	Quoted prices (unadjusted) in active markets	Valuation based on significant observable market inputs	Valuation based on significant unobservable market inputs	
Analysis of financial investments, net of derivative liabilities by business type				
With-profits				
Equity securities and portfolio holdings in unit trusts	23,525	1,807	625	25,957
Debt securities	15,241	44,609	522	60,372
Other investments (including derivative assets)	155	757	2,924	3,836
Derivative liabilities	(156)	(883)	–	(1,039)
Total financial investments, net of derivative liabilities	38,765	46,290	4,071	89,126
Percentage of total	43%	52%	5%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	85,014	265	63	85,342
Debt securities	3,683	5,932	2	9,617
Other investments (including derivative assets)	4	21	–	25
Derivative liabilities	(2)	(5)	–	(7)
Total financial investments, net of derivative liabilities	88,699	6,213	65	94,977
Percentage of total	93%	7%	0%	100%
Non-linked shareholder-backed				
Loans*	–	242	2,026	2,268
Equity securities and portfolio holdings in unit trusts	879	33	47	959
Debt securities	13,551	54,559	157	68,267
Other investments (including derivative assets)	72	1,331	876	2,279
Derivative liabilities	–	(974)	(206)	(1,180)
Total financial investments, net of derivative liabilities	14,502	55,191	2,900	72,593
Percentage of total	20%	76%	4%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans	–	242	2,026	2,268
Equity securities and portfolio holdings in unit trusts	109,418	2,105	735	112,258
Debt securities	32,475	105,100	681	138,256
Other investments (including derivative assets)	231	2,109	3,800	6,140
Derivative liabilities	(158)	(1,862)	(206)	(2,226)
Total financial investments, net of derivative liabilities	141,966	107,694	7,036	256,696
Investment contracts liabilities without discretionary participation features held at fair value	–	(17,342)	–	(17,342)
Borrowings attributable to the with-profits funds held at fair value	–	(22)	–	(22)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(3,696)	(357)	(1,341)	(5,394)
Other financial liabilities held at fair value	–	(256)	(2,206)	(2,462)
Total financial instruments at fair value	138,270	89,717	3,489	231,476
Percentage of total	59%	39%	2%	100%

* Loans in the table above are those classified as fair value through profit and loss in note C3.1.

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	31 Dec 2013 £m			
	Level 1	Level 2	Level 3	Total
	Quoted prices (unadjusted) in active markets	Valuation based on significant observable market inputs	Valuation based on significant unobservable market inputs	
Analysis of financial investments, net of derivative liabilities by business type				
With-profits				
Equity securities and portfolio holdings in unit trusts	25,087	2,709	569	28,365
Debt securities	14,547	42,759	485	57,791
Other investments (including derivative assets)	169	1,191	2,949	4,309
Derivative liabilities	(32)	(517)	–	(549)
Total financial investments, net of derivative liabilities	39,771	46,142	4,003	89,916
Percentage of total	44%	52%	4%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	90,645	191	36	90,872
Debt securities	3,573	6,048	1	9,622
Other investments (including derivative assets)	6	30	–	36
Derivative liabilities	(1)	(3)	–	(4)
Total financial investments, net of derivative liabilities	94,223	6,266	37	100,526
Percentage of total	94%	6%	0%	100%
Non-linked shareholder-backed				
Loans	–	250	1,887	2,137
Equity securities and portfolio holdings in unit trusts	841	100	44	985
Debt securities	13,428	51,880	184	65,492
Other investments (including derivative assets)	–	1,111	809	1,920
Derivative liabilities	–	(935)	(201)	(1,136)
Total financial investments, net of derivative liabilities	14,269	52,406	2,723	69,398
Percentage of total	21%	75%	4%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans*	–	250	1,887	2,137
Equity securities and portfolio holdings in unit trusts	116,573	3,000	649	120,222
Debt securities	31,548	100,687	670	132,905
Other investments (including derivative assets)	175	2,332	3,758	6,265
Derivative liabilities	(33)	(1,455)	(201)	(1,689)
Total financial investments, net of derivative liabilities	148,263	104,814	6,763	259,840
Investment contracts liabilities without discretionary participation features held at fair value	–	(17,736)	–	(17,736)
Borrowings attributable to the with-profits funds held at fair value	–	(18)	–	(18)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(3,703)	(248)	(1,327)	(5,278)
Other financial liabilities held at fair value	–	(263)	(2,051)	(2,314)
Total financial instruments at fair value	144,560	86,549	3,385	234,494
Percentage of total	61%	37%	2%	100%

* Loans in the table above are those classified as fair value through profit and loss in note C3.1.

In addition to the financial instruments shown above, the assets and liabilities held for sale on the consolidated statement of financial position at 30 June 2014 in respect of Japan life business included a net financial instruments balance of £917 million, primarily for equity securities and debt securities (30 June 2013: £1,140 million; 31 December 2013: £934 million). Of this amount, £888 million has been classified as level 1 and £29 million as level 2 (30 June 2013: £1,038 million level 1, £74 million level 2 and £28 million level 3; 31 December 2013: £905 million level 1, £29 million level 2).

c Valuation approach for level 2 fair valued financial instruments

A significant proportion of the Group's level 2 assets are corporate bonds, structured securities and other non-national government debt securities. These assets, in line with market practice, are generally valued using independent pricing services or third-party broker quotes. These valuations are determined using independent external quotations from multiple sources and are subject to a number of monitoring controls, such as monthly price variances, stale price reviews and variance analysis on prices achieved on subsequent trades.

Pricing services, where available, are used to obtain the third-party broker quotes. Where pricing services providers are used, a single valuation is obtained and applied.

When prices are not available from pricing services, quotes are sourced directly from brokers. Prudential seeks to obtain a number of quotes from different brokers so as to obtain the most comprehensive information available on their executability. Where quotes are sourced directly from brokers, the price used in the valuation is normally selected from one of the quotes based on a number of factors, including the timeliness and regularity of the quotes and the accuracy of the quotes considering the spreads provided. The selected quote is the one which best represents an executable quote for the security at the measurement date.

Generally, no adjustment is made to the prices obtained from independent third parties. Adjustment is made in only limited circumstances, where it is determined that the third-party valuations obtained do not reflect fair value (eg either because the value is stale and/or the values are extremely diverse in range). These are usually securities which are distressed or that could be subject to a debt restructure or where reliable market prices are no longer available due to an inactive market or market dislocation. In these instances, prices are derived using internal valuation techniques including those as described above in this note with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The techniques used require a number of assumptions relating to variables such as credit risk and interest rates. Examples of such variables include an average credit spread based on the corporate bond universe and the relevant duration of the asset being valued. Prudential determines the input assumptions based on the best available information at the measurement dates. Securities valued in such manner are classified as level 3 where these significant inputs are not based on observable market data.

Of the total level 2 debt securities of £99,922 million at 30 June 2014 (30 June 2013: £105,100 million; 31 December 2013: £100,687 million), £8,813 million are valued internally (30 June 2013: £8,645 million; 31 December 2013: £8,556 million). The majority of such securities are valued using matrix pricing, which is based on assessing the credit quality of the underlying borrower to derive a suitable discount rate relative to government securities of a comparable duration. Under matrix pricing, the debt securities are priced taking the credit spreads on comparable quoted public debt securities and applying these to the equivalent debt instruments factoring in a specified liquidity premium. The majority of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

d Fair value measurements for level 3 fair valued financial instruments

Reconciliation of movements in level 3 financial instruments measured at fair value

The following table reconciles the value of level 3 fair valued financial instruments at 1 January 2014 to that presented at 30 June 2014.

Total investment return recorded in the income statement represents interest and dividend income, realised gains and losses, unrealised gains and losses on the assets classified at fair value through profit and loss and foreign exchange movements on an individual entity's overseas investments.

Total gains and losses recorded in other comprehensive income includes unrealised gains and losses on debt securities held as available-for-sale within Jackson and foreign exchange movements arising from the retranslation of the Group's overseas subsidiaries and branches.

	Half year 2014 £m									
	At 1 Jan	Total gains (losses) in income statement	Total gains (losses) recorded in other comprehensive income	Purchases	Sales	Settled	Issued	Transfers into level 3	Transfers out of level 3	At 30 Jun 2014
Loans	1,887	64	(60)	–	–	(46)	19	–	–	1,864
Equity securities and portfolio holdings in unit trusts	649	17	(2)	12	(9)	–	–	2	–	669
Debt securities	670	1	(1)	16	(123)	–	–	12	(7)	568
Other investments (including derivative assets)	3,758	158	(61)	209	(253)	–	–	–	(1)	3,810
Derivative liabilities	(201)	(9)	–	–	–	–	–	–	–	(210)
Total financial investments, net of derivative liabilities	6,763	231	(124)	237	(385)	(46)	19	14	(8)	6,701
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,327)	11	1	(2)	2	116	(27)	–	–	(1,226)
Other financial liabilities	(2,051)	(71)	65	–	–	71	(33)	–	–	(2,019)
Total financial instruments at fair value	3,385	171	(58)	235	(383)	141	(41)	14	(8)	3,456

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

	Half year 2013 £m										
	At 1 Jan	Total gains (losses) in income statement	Total gains (losses) recorded in other comprehensive income	Purchases	Sales	Settled	Issued	Reclassification of Japan life as held for sale	Transfers into level 3	Transfers out of level 3	At 30 Jun 2013
Loans	1,842	67	36	–	–	(37)	118	–	–	–	2,026
Equity securities and portfolio holdings in unit trusts	568	52	4	13	(11)	–	25	–	87	(3)	735
Debt securities	729	27	9	20	(77)	–	–	(26)	29	(30)	681
Other investments (including derivative assets)	3,335	373	137	177	(272)	–	–	–	50	–	3,800
Derivative liabilities	(195)	(14)	–	–	2	–	–	–	–	1	(206)
Total financial investments, net of derivative liabilities	6,279	505	186	210	(358)	(37)	143	(26)	166	(32)	7,036
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,224)	(80)	(2)	26	–	–	(61)	–	–	–	(1,341)
Other financial liabilities	(2,021)	(54)	(146)	–	–	50	(35)	–	–	–	(2,206)
Total financial instruments at fair value	3,034	371	38	236	(358)	13	47	(26)	166	(32)	3,489

	Full year 2013 £m										
	At 1 Jan	Total gains (losses) in income statement	Total gains (losses) recorded in other comprehensive income	Purchases	Sales	Settled	Issued	Reclassification of Japan life as held for sale	Transfers into level 3	Transfers out of level 3	At 31 Dec 2013
Loans	1,842	4	(37)	–	–	(66)	144	–	–	–	1,887
Equity securities and portfolio holdings in unit trusts	568	50	(3)	26	(73)	–	–	–	84	(3)	649
Debt securities	729	60	(4)	16	(146)	(1)	–	(28)	92	(48)	670
Other investments (including derivative assets)	3,335	426	(1)	80	(215)	–	81	–	52	–	3,758
Derivative liabilities	(195)	(6)	–	–	–	–	–	–	–	–	(201)
Total financial investments, net of derivative liabilities	6,279	534	(45)	122	(434)	(67)	225	(28)	228	(51)	6,763
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(1,224)	(57)	(1)	–	2	94	(141)	–	–	–	(1,327)
Other financial liabilities	(2,021)	3	41	–	–	144	(218)	–	–	–	(2,051)
Total financial instruments at fair value	3,034	480	(5)	122	(432)	171	(134)	(28)	228	(51)	3,385

Of the total net gains and losses in the income statement of £171 million (30 June 2013: £371 million; 31 December 2013: £480 million), £163 million (30 June 2013: £333 million; 31 December 2013: £415 million) relates to net unrealised gains relating to financial instruments still held at the end of the period, which can be analysed as follows:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Equity securities	14	50	46
Debt securities	1	10	30
Other investments	153	355	397
Derivative liabilities	(9)	(14)	(8)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	11	(80)	(57)
Other financial liabilities	(7)	12	7
Total	163	333	415

Valuation approach for level 3 fair valued financial instruments

Investments valued using valuation techniques include financial investments, which by their nature do not have an externally quoted price based on regular trades, and financial investments for which markets are no longer active as a result of market conditions eg market illiquidity. The valuation techniques used include comparison to recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation. These techniques may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments. When determining the inputs into the valuation techniques used, priority is given to publicly available prices from independent sources when available, but overall the source of pricing is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date.

The fair value estimates are made at a specific point in time, based upon available market information and judgements about the financial instruments, including estimates of the timing and amount of expected future cash flows and the credit standing of counterparties. Such estimates do not reflect any premium or discount that could result from offering for sale at one time the Group's entire holdings of a particular financial instrument, nor do they consider the tax impact of the realisation of unrealised gains or losses from selling the financial instrument being fair valued. In some cases, the disclosed value cannot be realised in immediate settlement of the financial instrument.

In accordance with the Group's risk management framework, the estimated fair value of derivative financial instruments valued internally using standard market practices are subject to assessment against external counterparties' valuations.

At 30 June 2014, the Group held £3,456 million (30 June 2013: £3,489 million; 31 December 2013: £3,385 million), 1 per cent of the total fair valued financial assets net of fair valued financial liabilities (30 June 2013: 2 per cent; 31 December 2013: 2 per cent), within level 3.

Included within these amounts were loans of £1,864 million at 30 June 2014 (30 June 2013: £2,026 million; 31 December 2013: £1,887 million), attached to REALIC and held to back the liabilities for funds withheld under reinsurance arrangements. The funds withheld liability of £2,019 million at 30 June 2014 (30 June 2013: £2,206 million; 31 December 2013: £2,051 million) was also classified within level 3, accounted for on a fair value basis being equivalent to the carrying value of the underlying assets.

Excluding the loans and funds withheld liability under REALIC's reinsurance arrangements as described above, which amounted to a net liability of £(155) million (30 June 2013: £(180) million; 31 December 2013: £(164) million), the level 3 fair valued financial assets net of financial liabilities were £3,611 million (30 June 2013: £3,669 million; 31 December 2013: £3,549 million). Of this amount, a net liability of £(228) million (30 June 2013: net liability of £(272) million; 31 December 2013: net liability of £(304) million) were internally valued, representing 0.1 per cent of the total fair valued financial assets net of financial liabilities (30 June 2013: 0.1 per cent; 31 December 2013: 0.1 per cent). Internal valuations are inherently more subjective than external valuations. Included within these internally valued net liabilities were:

- Debt securities of £80 million (30 June 2013: £80 million; 31 December 2013: £118 million), which were either valued on a discounted cash flow method with an internally developed discount rate or on external prices adjusted to reflect the specific known conditions relating to these securities (eg distressed securities or securities which were being restructured);
- Private equity and venture investments of £897 million (30 June 2013: £955 million; 31 December 2013: £878 million) which were valued internally based on management information available for these investments. These investments were principally held by consolidated investment funds which are managed on behalf of third parties;
- Liabilities of £(1,206) million (30 June 2013: £(1,311) million; 31 December 2013: £(1,301) million) for the net asset value attributable to external unit holders in respect of the consolidated investment funds, which are non-recourse to the Group. These liabilities are valued by reference to the underlying assets; and
- Other sundry individual financial investments of £1 million (30 June 2013: £4 million; 31 December 2013: £1 million).

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

Of the internally valued net liability referred to above of £(228) million (30 June 2013: £(272) million; 31 December 2013: £(304) million):

- A net liability of £(267) million (30 June 2013: net liability of £(313) million; 31 December 2013: net liability of £(380) million) was held by the Group's participating funds and, therefore, shareholders' profit and equity are not impacted by movements in the valuation of these financial instruments; and
- A net asset of £39 million (30 June 2013: £41 million; 31 December 2013: £76 million) was held to support non-linked shareholder-backed business. If the value of all the level 3 instruments held to support non-linked shareholder-backed business valued internally was varied downwards by 10 per cent, the change in valuation would be £4 million (30 June 2013: £4 million; 31 December 2013: £8 million), which would reduce shareholders' equity by this amount before tax. Of this amount, a decrease of £3 million (30 June 2013: an increase of less than £1 million; 31 December 2013: a decrease of £6 million) would pass through the income statement substantially as part of short-term fluctuations in investment returns outside of operating profit and a £1 million decrease (30 June 2013: a £4 million decrease; 31 December 2013: a decrease of £2 million) would be included as part of other comprehensive income, being unrealised movements on assets classified as available-for-sale.

e Transfers into and transfers out of levels

The Group's policy is to recognise transfers into and transfers out of levels as of the end of each half year reporting period, except for material transfers which are recognised as of the date of the event or change in circumstances that caused the transfer.

During half year 2014, the transfers between levels within the Group's portfolio were primarily transfers from level 1 to 2 of £44 million and transfers from level 2 to level 1 of £204 million. These transfers which relate to debt securities arose to reflect the change in the observability of the inputs used in valuing these securities.

In addition, the transfers into and out of level 3 in half year 2014 were £14 million and £8 million, respectively. These transfers were primarily between levels 3 and 2 for debt securities.

f Valuation processes applied by the Group

The Group's valuation policies, procedures and analyses for instruments categorised as level 3 are overseen by business unit committees as part of the Group's wider financial reporting governance processes. The procedures undertaken include approval of valuation methodologies, verification processes, and resolution of significant or complex valuation issues. In undertaking these activities the Group makes use of the extensive expertise of its asset management functions.

C3.3 Debt securities

This note provides analysis of the Group's debt securities, including asset-backed securities and sovereign debt securities, by segment.

Debt securities are carried at fair value. The amounts included in the statement of financial position are analysed as follows, with further information relating to the credit quality of the Group's debt securities at 30 June 2014 provided below.

	2014 £m	**2013** £m	
	30 Jun	**30 Jun**	**31 Dec**
Insurance operations:			
Asia note (a)	**19,958**	20,081	18,554
US note (b)	**30,586**	33,368	30,292
UK note (c)	**81,680**	82,854	82,014
Asset management operations note (d)	**1,953**	1,953	2,045
Total	**134,177**	138,256	132,905

In the tables below, with the exception of some mortgage-backed securities, Standard & Poor's (S&P) ratings have been used where available. For securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative.

a Asia insurance operations

	2014 £m				2013 £m	
	With-profits business	Unit-linked assets	Other business	30 Jun Total	30 Jun Total	31 Dec Total
S&P – AAA	640	10	84	734	720	724
S&P – AA+ to AA-	2,805	344	1,893	5,042	5,001	4,733
S&P – A+ to A-	1,772	252	1,234	3,258	3,647	2,896
S&P – BBB+ to BBB-	1,302	559	929	2,790	2,244	2,717
S&P – Other	378	219	866	1,463	1,956	1,433
	6,897	1,384	5,006	13,287	13,568	12,503
Moody's – Aaa	1,713	235	442	2,390	1,474	1,728
Moody's – Aa1 to Aa3	56	31	17	104	174	176
Moody's – A1 to A3	73	21	53	147	176	177
Moody's – Baa1 to Baa3	127	246	104	477	633	572
Moody's – Other	30	13	31	74	118	76
	1,999	546	647	3,192	2,575	2,729
Fitch	281	115	188	584	458	728
Other	1,484	398	1,013	2,895	3,480	2,594
Total debt securities	10,661	2,443	6,854	19,958	20,081	18,554

In addition to the debt securities shown above, the assets held for sale on the condensed consolidated statement of financial position at 30 June 2014 in respect of Japan life business included a debt securities balance of £380 million (30 June 2013: £452 million; 31 December 2013: £387 million). Of this amount, £351 million (30 June 2013: £420 million; 31 December 2013: £356 million) were rated as AA+ to AA- and £29 million (30 June 2013: £32million; 31 December 2013: £29 million) were rated A+ to A-.

The following table analyses debt securities of other business which are not externally rated by S&P, Moody's or Fitch.

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Government bonds*	402	387	387
Corporate bonds*	532	542	491
Other	79	185	81
	1,013	1,114	959

* Rated as investment grade by local external ratings agencies.

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

b US insurance operations
i Overview

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Corporate and government security and commercial loans:			
Government	3,385	4,017	3,330
Publicly traded and SEC Rule 144A securities*	19,530	20,376	18,875
Non-SEC Rule 144A securities	3,335	3,584	3,395
Total	26,250	27,977	25,600
Residential mortgage-backed securities (RMBS)	1,584	2,175	1,760
Commercial mortgage-backed securities (CMBS)	2,224	2,591	2,339
Other debt securities	528	625	593
Total US debt securities†	30,586	33,368	30,292

* A 1990 SEC rule that facilitates the resale of privately placed securities under Rule 144A that are without SEC registration to qualified institutional investors. The rule was designed to develop a more liquid and efficient institutional resale market for unregistered securities.
† Debt securities for US operations included in the statement of financial position comprise:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Available-for-sale	30,511	33,213	30,205
Fair value through profit and loss:			
Securities held to back liabilities for funds withheld under reinsurance arrangement	75	155	87
	30,586	33,368	30,292

ii Valuation basis, presentation of gains and losses and securities in an unrealised loss position
Under IAS 39, unless categorised as 'held to maturity' or 'loans and receivables' debt securities are required to be fair valued. Where available, quoted market prices are used. However, where securities do not have an externally quoted price based on regular trades or where markets for the securities are no longer active as a result of market conditions, IAS 39 requires that valuation techniques be applied. IFRS 13 requires classification of the fair values applied by the Group into a three level hierarchy. At 30 June 2014, 0.1 per cent of Jackson's debt securities were classified as level 3 (30 June 2013: 0.1 per cent; 31 December 2013: 0.1 per cent) comprising of fair values where there are significant inputs which are not based on observable market data.

Except for certain assets covering liabilities that are measured at fair value, the debt securities of the US insurance operations are classified as 'available-for-sale'. Unless impaired, fair value movements are recognised in other comprehensive income. Realised gains and losses, including impairments, recorded in the income statement are as shown in note B1.2 of this report.

Movements in unrealised gains and losses

There was a movement in the statement of financial position value for debt securities classified as available-for-sale from a net unrealised gain of £781 million to a net unrealised gain of £1,756 million as analysed in the table below. This increase reflects the effects of lower long-term interest rates.

	30 Jun 2014 £m	Changes in unrealised appreciation	Foreign exchange translation†	31 Dec 2013 £m
		Reflected as part of movement in other comprehensive income		
Assets fair valued at below book value				
Book value*	5,566			10,825
Unrealised (loss) gain	(299)	536	14	(849)
Fair value (as included in statement of financial position)	5,267			9,976
Assets fair valued at or above book value				
Book value*	23,189			18,599
Unrealised gain (loss)	2,055	487	(62)	1,630
Fair value (as included in statement of financial position)	25,244			20,229
Total				
Book value*	28,755			29,424
Net unrealised gain (loss)	1,756	1,023	(48)	781
Fair value (as included in statement of financial position)	30,511			30,205

* Book value represents cost/amortised cost of the debt securities.
† Translated at the average rate of US$1.6693: £1.00.

Debt securities classified as available-for-sale in an unrealised loss position

(a) Fair value of securities as a percentage of book value

The following table shows the fair value of the debt securities in a gross unrealised loss position for various percentages of book value:

	30 Jun 2014 £m		30 Jun 2013 £m		31 Dec 2013 £m	
	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
Between 90% and 100%	4,069	(126)	7,510	(317)	7,624	(310)
Between 80% and 90%	1,176	(162)	2,214	(369)	1,780	(331)
Below 80%	22	(11)	124	(61)	572	(208)
Total	5,267	(299)	9,848	(747)	9,976	(849)

(b) Unrealised losses by maturity of security

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
1 year to 5 years	(2)	(6)	(5)
5 years to 10 years	(48)	(215)	(224)
More than 10 years	(216)	(440)	(558)
Mortgage-backed and other debt securities	(33)	(86)	(62)
Total	(299)	(747)	(849)

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

(c) Age analysis of unrealised losses for the periods indicated

The following table shows the age analysis of all the unrealised losses in the portfolio by reference to the length of time the securities have been in an unrealised loss position:

	30 Jun 2014 £m			30 Jun 2013 £m			31 Dec 2013 £m		
	Non-investment grade	Investment grade	Total	Non-investment grade	Investment grade	Total	Non-investment grade	Investment grade	Total
Less than 6 months	(1)	(2)	(3)	(16)	(326)	(342)	(2)	(52)	(54)
6 months to 1 year	(1)	(1)	(2)	(1)	(345)	(346)	(12)	(329)	(341)
1 year to 2 years	(2)	(271)	(273)	(3)	–	(3)	(2)	(423)	(425)
2 years to 3 years	–	–	–	(2)	–	(2)	(1)	–	(1)
More than 3 years	(10)	(11)	(21)	(23)	(31)	(54)	(13)	(15)	(28)
Total	(14)	(285)	(299)	(45)	(702)	(747)	(30)	(819)	(849)

(d) Securities whose fair values were below 80 per cent of the book value

£11 million of the £299 million of gross unrealised losses as shown in the table (a) above at 30 June 2014 (30 June 2013: £61 million of the £747 million of gross unrealised losses; 31 December 2013: £208 million of the £849 million of gross unrealised losses) related to securities whose fair values were below 80 per cent of the book value. The analysis of the £11 million (30 June 2013: £61 million; 31 December 2013: £208 million), by category of debt securities and by age analysis indicating the length of time for which their fair value was below 80 per cent of the book value, is as follows:

	30 Jun 2014 £m		30 Jun 2013 £m		31 Dec 2013 £m	
Category analysis	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
Residential mortgage-backed securities:						
Prime (including agency)	–	–	5	(2)	–	–
Sub-prime	3	(1)	7	(2)	4	(1)
	3	(1)	12	(4)	4	(1)
Commercial mortgage-backed securities	8	(3)	13	(21)	16	(6)
Other asset-backed securities	9	(6)	24	(13)	9	(6)
Total structured securities	20	(10)	49	(38)	29	(13)
Government bonds	–	–	–	–	521	(188)
Corporates	2	(1)	75	(23)	22	(7)
Total	22	(11)	124	(61)	572	(208)

The following table shows the age analysis as at 30 June 2014, of the securities whose fair values were below 80 per cent of the book value:

	30 Jun 2014 £m		30 Jun 2013 £m		31 Dec 2013 £m	
Age analysis	Fair value	Unrealised loss	Fair value	Unrealised loss	Fair value	Unrealised loss
Less than 3 months	–	–	79	(25)	93	(24)
3 months to 6 months	–	–	2	(1)	418	(159)
More than 6 months	22	(11)	43	(35)	61	(25)
	22	(11)	124	(61)	572	(208)

iii Ratings

The following table summarises the ratings of securities detailed above by using S&P, Moody's, Fitch and implicit ratings of mortgage-backed securities based on National Association of Insurance Commissioners (NAIC) valuations:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
S&P – AAA	131	148	132
S&P – AA+ to AA-	5,352	6,162	5,252
S&P – A+ to A-	7,776	8,308	7,728
S&P – BBB+ to BBB-	10,065	10,195	9,762
S&P – Other	1,027	1,223	941
	24,351	26,036	23,815
Moody's – Aaa	175	62	65
Moody's – Aa1 to Aa3	6	25	13
Moody's – A1 to A3	86	65	65
Moody's – Baa1 to Baa3	85	36	70
Moody's – Other	10	4	10
	362	192	223
Implicit ratings of MBS based on NAIC* valuations (see below)			
NAIC 1	2,558	2,873	2,774
NAIC 2	116	252	179
NAIC 3-6	75	268	87
	2,749	3,393	3,040
Fitch	161	72	159
Other†	2,963	3,675	3,055
Total debt securities	30,586	33,368	30,292

* The Securities Valuation Office of the NAIC classifies debt securities into six quality categories ranging from Class 1 (the highest) to Class 6 (the lowest). Performing securities are designated as Classes 1 to 5 and securities in or near default are designated Class 6.

† The amounts within other which are not rated by S&P, Moody's nor Fitch, nor are MBS securities using the revised regulatory ratings, have the following NAIC classifications:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
NAIC 1	1,140	1,506	1,165
NAIC 2	1,756	2,098	1,836
NAIC 3-6	67	71	54
	2,963	3,675	3,055

For some mortgage-backed securities within Jackson, the table above includes these securities using the regulatory ratings detail issued by the NAIC. These regulatory ratings levels were established by external third parties (PIMCO for residential mortgage-backed securities and BlackRock Solutions for commercial mortgage-backed securities).

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

c UK insurance operations

	2014 £m							
			Other funds and subsidiaries			UK insurance operations		
						2014 £m	2013 £m	
	Scottish Amicable Insurance Fund	PAC with-profits fund	Unit-linked assets	PRIL	Other annuity and long-term business	30 Jun Total	30 Jun Total	31 Dec Total
S&P – AAA	244	3,971	777	3,288	350	8,630	8,725	8,837
S&P – AA+ to AA-	548	5,473	1,151	3,365	415	10,952	9,760	10,690
S&P – A+ to A-	715	10,349	1,886	7,053	877	20,880	21,535	20,891
S&P – BBB+ to BBB-	591	8,733	1,804	3,834	690	15,652	17,452	17,125
S&P – Other	164	2,191	57	284	48	2,744	3,600	3,255
	2,262	30,717	5,675	17,824	2,380	58,858	61,072	60,798
Moody's – Aaa	74	1,434	225	366	46	2,145	2,338	2,333
Moody's – Aa1 to Aa3	111	2,509	1,088	2,800	537	7,045	6,359	6,420
Moody's – A1 to A3	49	1,004	74	1,116	157	2,400	2,068	2,077
Moody's – Baa1 to Baa3	37	844	109	400	53	1,443	1,318	1,214
Moody's – Other	6	160	–	7	–	173	280	140
	277	5,951	1,496	4,689	793	13,206	12,363	12,184
Fitch	11	466	84	164	19	744	605	611
Other	268	5,493	161	2,729	221	8,872	8,814	8,421
Total debt securities	2,818	42,627	7,416	25,406	3,413	81,680	82,854	82,014

Where no external ratings are available, internal ratings produced by the Group's asset management operation, which are prepared on the Company's assessment of a comparable basis to external ratings, are used where possible. The £8,872 million total debt securities held at 30 June 2014 (30 June 2013: £8,814 million; 31 December 2013: £8,421 million) which are not externally rated are either internally rated or unrated. These are analysed as follows:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Internal ratings or unrated:			
AAA to A-	4,082	3,438	3,691
BBB to B-	3,403	3,778	3,456
Below B- or unrated	1,387	1,598	1,274
Total	8,872	8,814	8,421

The majority of unrated debt security investments were held in SAIF and the PAC with-profits fund and relate to convertible debt and other investments which are not covered by ratings analysts nor have an internal rating attributed to them. Of the £2,950 million for PRIL and other annuity and long-term business investments for non-linked shareholder-backed business which are not externally rated, £696 million were internally rated AA+ to AA-, £1,131 million A+ to A-, £926 million BBB+ to BBB-, £55 million BB+ to BB- and £142 million were internally rated B+ and below or unrated.

d Asset management operations

The debt securities are all held by M&G including Prudential Capital.

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
M&G			
AAA to A- by Standard & Poor's or Aaa to A3 rated by Moody's	1,604	1,597	1,690
Other	349	356	355
Total M&G (including Prudential Capital)	1,953	1,953	2,045

e Asset-backed securities

The Group's holdings in asset-backed securities (ABS), which comprise residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), collateralised debt obligations (CDO) funds and other asset-backed securities, at 30 June 2014 is as follows:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Shareholder-backed operations:			
Asia insurance operations note (i)	108	144	139
US insurance operations note (ii)	4,336	5,391	4,692
UK insurance operations (2014: 37% AAA, 25% AA) note (iii)	1,765	1,623	1,727
Other operations note (iv)	873	584	667
	7,082	7,742	7,225
With-profits operations:			
Asia insurance operations note (i)	225	319	200
UK insurance operations (2014: 59% AAA, 14% AA) note (iii)	5,352	5,815	5,765
	5,577	6,134	5,965
Total	12,659	13,876	13,190

Notes

(i) Asia insurance operations

The Asia insurance operations' exposure to asset-backed securities is primarily held by the with-profits operations. Of the £225 million, 98 per cent (30 June 2013: 91 per cent; 31 December 2013: 94 per cent) are investment graded.

(ii) US insurance operations

US insurance operations' exposure to asset-backed securities at 30 June 2014 comprises:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
RMBS:			
Sub-prime (2014: 9% AAA, 11% AA, 7% A)	232	283	255
Alt-A (2014: 1% AA, 4% A)	244	325	270
Prime including agency (2014: 75% AA, 2% A)	1,108	1,567	1,235
CMBS (2014: 49% AAA, 20% AA, 22% A)	2,224	2,591	2,339
CDO funds (2014: 29% AA, 1% A), including £nil exposure to sub-prime	38	49	46
Other ABS (2014: 30% AAA, 18% AA, 43% A), including £65 million exposure to sub-prime	490	576	547
Total	4,336	5,391	4,692

(iii) UK insurance operations

The holdings of the UK shareholder-backed operations include £626 million (30 June 2013: £534 million; 31 December 2013: £632 million) relating to asset-backed securities held in the unit-linked funds. The remaining amount relates to investments held by PRIL with a primary exposure to the UK market.

Of the holdings of the with-profits operations, £1,266 million (30 June 2013: £1,615 million; 31 December 2013: £1,490 million) relates to exposure to the US markets with the remaining exposure being primarily to the UK market.

(iv) Asset management operations

Asset management operations' exposure to asset-backed securities is held by Prudential Capital with no sub-prime exposure. Of the £873 million, 86 per cent (30 June 2013: 80 per cent; 31 December 2013: 85 per cent) are graded AAA.

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

f Group sovereign debt and bank debt exposure

The Group exposures held by the shareholder-backed business and with-profits funds in sovereign debts and bank debt securities at 30 June 2014:

Exposure to sovereign debts

	2014 £m		2013 £m			
	30 Jun		30 Jun		31 Dec	
	Shareholder-backed business	With-profits funds	Shareholder-backed business	With-profits funds	Shareholder-backed business	With-profits funds
Italy	58	58	51	58	53	53
Spain	1	16	1	18	1	14
France	18	–	19	–	19	–
Germany*	356	380	427	427	413	389
Other Europe (principally Belgium and Isle of Man)	49	43	46	40	45	45
Total Continental Europe	482	497	544	543	531	501
United Kingdom	3,474	2,309	3,533	2,495	3,516	2,432
Total Europe	3,956	2,806	4,077	3,038	4,047	2,933
United States†	3,125	4,805	3,598	3,117	3,045	4,026
Other, predominantly Asia	3,289	1,679	3,223	1,475	3,084	1,508
Total	10,370	9,290	10,898	7,630	10,176	8,467

* Including bonds guaranteed by the federal government.
† The exposure to the United States sovereign debt comprises holdings of Jackson, the UK and Asia insurance operations.

The table above excludes assets held to cover linked liabilities and those of the consolidated unit trusts and similar funds.
In addition, the table above excludes the proportionate share of sovereign debt holdings of the Group's joint venture operations.

Exposure to bank debt securities

Shareholder-backed business	Bank debt securities £m								
	Senior debt			Subordinated debt					
	Covered	Senior	Total senior debt	Tier 1	Tier 2	Total sub-ordinated debt	Total 30 Jun 2014	Total 30 Jun 2013	Total 31 Dec 2013
Portugal	–	44	44	–	–	–	44	42	45
Ireland	–	16	16	–	–	–	16	18	17
Italy	–	31	31	–	–	–	31	41	30
Spain	116	12	128	–	23	23	151	137	135
Austria	–	–	–	–	12	12	12	12	12
France	17	104	121	18	74	92	213	178	175
Germany	–	–	–	–	63	63	63	22	66
Netherlands	–	15	15	75	46	121	136	162	152
Total Continental Europe	133	222	355	93	218	311	666	612	632
United Kingdom	435	202	637	54	644	698	1,335	1,396	1,369
Total Europe	568	424	992	147	862	1,009	2,001	2,008	2,001
United States	–	1,794	1,794	32	453	485	2,279	2,234	2,163
Other, predominantly Asia	17	337	354	80	290	370	724	760	698
Total	585	2,555	3,140	259	1,605	1,864	5,004	5,002	4,862
With-profits funds									
Portugal	–	–	–	–	–	–	–	6	6
Ireland	6	–	6	–	–	–	6	6	10
Italy	16	58	74	–	–	–	74	82	82
Spain	165	37	202	–	–	–	202	172	149
France	12	162	174	–	59	59	233	156	237
Germany	–	29	29	–	–	–	29	12	24
Netherlands	–	223	223	–	–	–	223	164	215
Total Continental Europe	199	509	708	–	59	59	767	598	723
United Kingdom	564	436	1,000	36	520	556	1,556	1,805	1,695
Total Europe	763	945	1,708	36	579	615	2,323	2,403	2,418
United States	–	1,619	1,619	83	120	203	1,822	2,001	2,214
Other, predominantly Asia	98	837	935	206	146	352	1,287	700	1,102
Total	861	3,401	4,262	325	845	1,170	5,432	5,104	5,734

The table above excludes assets held to cover linked liabilities and those of the consolidated unit trusts and similar funds.
In addition, the table above excludes the proportionate share of sovereign debt holdings of the Group's joint venture operations.

C: Balance sheet notes continued

C3: Assets and liabilities – classification and measurement continued

C3.4 Loans portfolio

Loans are accounted for at amortised cost net of impairment except for:

— Certain mortgage loans which have been designated at fair value through profit and loss of the UK insurance operations as this loan portfolio is managed and evaluated on a fair value basis; and
— Certain policy loans of the US insurance operations which are held to back liabilities for funds withheld under reinsurance arrangement and are also accounted on a fair value basis.

The amounts included in the statement of financial position are analysed as follows:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Insurance operations:			
Asia note (a)	**916**	1,004	922
US note (b)	**6,130**	6,691	6,375
UK note (c)	**4,389**	4,313	4,173
Asset management operations note (d)	**1,022**	1,222	1,096
Total	**12,457**	13,230	12,566

Notes

(a) Asia insurance operations
The loans of the Group's Asia insurance operations comprise:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Mortgage loans*	**65**	54	57
Policy loans*	**615**	640	611
Other loans†	**236**	310	254
Total Asia insurance operations loans	**916**	1,004	922

* The mortgage and policy loans are secured by properties and life insurance policies respectively.
† The majority of the other loans are commercial loans held by the Malaysia operation and which are all rated as investment grade by two local rating agencies.

(b) US insurance operations
The loans of the Group's US insurance operations comprise:

	2014 £m			2013 £m					
	30 Jun			30 Jun			31 Dec		
	Loans backing liabilities for funds withheld	Other loans	Total	Loans backing liabilities for funds withheld	Other loans	Total	Loans backing liabilities for funds withheld	Other loans	Total
Mortgage loans*	**–**	**3,490**	**3,490**	–	3,905	3,905	–	3,671	3,671
Policy loans†	**1,864**	**776**	**2,640**	2,026	760	2,786	1,887	817	2,704
Total US insurance operations loans	**1,864**	**4,266**	**6,130**	2,026	4,665	6,691	1,887	4,488	6,375

* All of the mortgage loans are commercial mortgage loans which are collateralised by properties. The property types are industrial, multi-family residential, suburban office, retail and hotel. The breakdown by property type is as follows:

	2014 %	2013 %	
	30 Jun	30 Jun	31 Dec
Industrial	29	28	28
Multi-family residential	29	28	30
Office	11	18	13
Retail	20	17	19
Hotels	9	9	9
Other	2	–	1
	100	100	100

† The policy loans are fully secured by individual life insurance policies or annuity policies. Included within the policy loans of REALIC are those accounted for at fair value through profit and loss to back liabilities for funds withheld under reinsurance. All other policy loans are accounted for at amortised cost, less any impairment.

The US insurance operations' commercial mortgage loan portfolio does not include any single-family residential mortgage loans and is, therefore, not exposed to the risk of defaults associated with residential sub-prime mortgage loans. The average loan size is £6.5 million (30 June 2013: £6.6 million; 31 December 2013: £6.5 million). The portfolio has a current estimated average loan to value of 60 per cent (30 June 2013: 62 per cent; 31 December 2013: 61 per cent).

At 30 June 2014, Jackson had mortgage loans with a carrying value of £34 million (30 June 2013: £49 million; 31 December 2013: £47 million) where the contractual terms of the agreements had been restructured.

(c) UK insurance operations

The loans of the Group's UK insurance operations comprise:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
SAIF and PAC WPSF:			
Mortgage loans*	1,391	1,379	1,183
Policy loans	12	13	12
Other loans†	1,503	1,588	1,629
Total SAIF and PAC WPSF loans	2,906	2,980	2,824
Shareholder-backed operations:			
Mortgage loans*	1,478	1,328	1,345
Other loans	5	5	4
Total loans of shareholder-backed operations	1,483	1,333	1,349
Total UK insurance operations loans	4,389	4,313	4,173

* The mortgage loans are collateralised by properties. By carrying value, 78 per cent of the £1,478 million held for shareholder-backed business relates to lifetime (equity release) mortgage business which has an average loan to property value of 30 per cent.

† Other loans held by the PAC with-profits fund are all commercial loans and comprise mainly syndicated loans.

(d) Asset management operations

The M&G loans relate to loans and receivables managed by Prudential Capital. These assets are generally secured but most have no external credit ratings. Internal ratings prepared by the Group's asset management operations, as part of the risk management process, are:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Loans and receivables internal ratings:			
AAA	104	112	108
AA+ to AA-	–	–	28
A+ to A-	120	–	–
BBB+ to BBB-	488	667	516
BB+ to BB-	49	419	174
B+ to B-	250	24	250
Other	11	–	20
Total M&G (including Prudential Capital) loans	1,022	1,222	1,096

C: Balance sheet notes continued

C4: Policyholder liabilities and unallocated surplus of with-profits funds

The note provides information of policyholder liabilities and unallocated surplus of with-profits funds held on the Group's statement of financial position:

C4.1 Movement of liabilities

C4.1(a) Group overview

i Analysis of movements in policyholder liabilities and unallocated surplus of with-profits funds

	Insurance operations £m			
Half year 2014 movements	**Asia** note C4.1(b)	**US** note C4.1(c)	**UK** note C4.1(d)	**Total**
At 1 January 2014	35,146	107,411	146,616	289,173
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	31,910	107,411	134,632	273,953
Unallocated surplus of with-profits funds on the consolidated statement of financial position	77	–	11,984	12,061
Group's share of policyholder liabilities of joint ventures§	3,159	–	–	3,159
Reallocation of unallocated surplus for the domestication of the Hong Kong branch*	1,690	–	(1,690)	–
Net flows:				
Premiums	3,195	8,435	3,969	15,599
Surrenders	(1,133)	(2,787)	(2,240)	(6,160)
Maturities/Deaths	(548)	(671)	(3,547)	(4,766)
Net flows	1,514	4,977	(1,818)	4,673
Shareholders' transfers post tax	(14)	–	(106)	(120)
Investment-related items and other movements	2,073	3,181	5,907	11,161
Foreign exchange translation differences	(837)	(3,560)	(231)	(4,628)
At 30 June 2014	39,572	112,009	148,678	300,259
Comprising:				
Policyholder liabilities on the consolidated statement of financial position¶	34,076	112,009	137,619	283,704
Unallocated surplus of with-profits funds on the consolidated statement of financial position	1,985	–	11,059	13,044
Group's share of policyholder liabilities of joint ventures§	3,511	–	–	3,511

Half year 2013 movements	Insurance operations £m Asia note C4.1(b)	US note C4.1(c)	UK note C4.1(d)	Total
At 1 January 2013	34,664	92,261	144,438	271,363
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	31,501	92,261	133,912	257,674
Unallocated surplus of with-profits funds on the consolidated statement of financial position	63	–	10,526	10,589
Group's share of policyholder liabilities of joint ventures§	3,100	–	–	3,100
Net flows:				
Premiums	3,266	8,208	3,880	15,354
Surrenders	(1,652)	(2,420)	(2,315)	(6,387)
Maturities/Deaths	(430)	(620)	(3,883)	(4,933)
Net flows	1,184	5,168	(2,318)	4,034
Shareholders' transfers post tax	(18)	–	(102)	(120)
Investment-related items and other movements	5	2,038	2,411	4,454
Foreign exchange translation differences	1,292	6,748	211	8,251
Reclassification of Japan life business as held for sale†	(970)	–	–	(970)
Acquisition of Thanachart Life	487	–	–	487
At 30 June 2013	36,644	106,215	144,640	287,499
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	33,223	106,215	133,290	272,728
Unallocated surplus of with-profits funds on the consolidated statement of financial position	84	–	11,350	11,434
Group's share of policyholder liabilities of joint ventures§	3,337	–	–	3,337
Average policyholder liability balances‡				
Half year 2014	**36,328**	**109,710**	**136,126**	**282,164**
Half year 2013	35,993	99,238	133,601	268,832

* Up until 31 December 2013 for the purposes of the presentation of unallocated surplus of with-profits within the statement of financial position, the Hong Kong branch balance was reported within the unallocated surplus of the PAC WPSF of the UK insurance operations.

On 1 January 2014, following consultation with the policyholders of PAC and regulators and court approval, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. From this date, the unallocated surplus of the Hong Kong with-profits business is reported within the Asia insurance operations segment.

† Liabilities of £970 million in respect of the Japan life operation were removed from policyholder liabilities following its reclassification as held for sale at 30 June 2013. Outflows of £45 million at AER (£39 million at CER) in respect of Japan life have been included in net flows up to that date, and hence included in the table above. Excluding the Japan life operation the average shareholder-backed policyholder liabilities for half year 2013 was £21,473 million. No amounts are shown within the 2014 analysis above in respect of Japan life.

‡ Averages have been based on opening and closing balances and adjusted for acquisitions, disposals and corporate transactions in the period and exclude unallocated surplus of with-profits funds..

§ The Group's investment in joint ventures are accounted for on the equity method in the Group's statement of financial position. The Group's share of the policyholder liabilities, as shown above, relate to the joint venture life business in China, India and of the Takaful business in Malaysia.

¶ The policyholder liabilities of the Asia insurance operations of £34,076 million, as shown in the table above, is after deducting the intra-group reinsurance liabilities ceded by the UK insurance operations of £1,296 million to the Hong Kong with-profits business. Including this amount total Asia policyholder liabilities is £35,372 million.

The items above represent the amount attributable to changes in policyholder liabilities and unallocated surplus of with-profits funds as a result of each of the components listed. The policyholder liabilities shown include investment contracts without discretionary participation features (as defined in IFRS 4) and their full movement in the period. The items above are shown gross of external reinsurance.

The analysis includes the impact of premiums, claims and investment movements on policyholders' liabilities. The impact does not represent premiums, claims and investment movements as reported in the income statement. For example, the premiums shown above are after any deductions for fees/charges and claims represent the policyholder liabilities provision released rather than the claim amount paid to the policyholder.

C: Balance sheet notes continued

C4: Policyholder liabilities and unallocated surplus of with-profits funds continued

ii Analysis of movements in policyholder liabilities for shareholder-backed business

	Half year 2014 £m			
Shareholder-backed business	**Asia**	**US**	**UK**	**Total** note (c)
At 1 January 2014	21,931	107,411	50,779	180,121
Net flows:				
Premiums	2,195	8,435	2,094	12,724
Surrenders	(1,028)	(2,787)	(1,033)	(4,848)
Maturities/Deaths	(276)	(671)	(1,201)	(2,148)
Net flows note (a)	891	4,977	(140)	5,728
Investment-related items and other movements	1,030	3,181	2,048	6,259
Foreign exchange translation differences	(433)	(3,560)	–	(3,993)
At 30 June 2014	23,419	112,009	52,687	188,115
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	19,908	112,009	52,687	184,604
Group's share of policyholder liabilities relating to joint ventures	3,511	–	–	3,511

	Half year 2013 £m			
Shareholder-backed business	**Asia**	**US**	**UK**	**Total**
At 1 January 2013	21,213	92,261	49,505	162,979
Net flows:				
Premiums	2,379	8,208	2,090	12,677
Surrenders	(1,194)	(2,420)	(1,252)	(4,866)
Maturities/Deaths	(146)	(620)	(1,174)	(1,940)
Net flows note (a)	1,039	5,168	(336)	5,871
Investment-related items and other movements	549	2,038	901	3,488
Acquisition of subsidiaries	487	–	–	487
Reclassification of Japan life business as held for sale note (b)	(970)	–	–	(970)
Foreign exchange translation differences	585	6,748	–	7,333
At 30 June 2013	22,903	106,215	50,070	179,188
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	19,566	106,215	50,070	175,851
Group's share of policyholder liabilities relating to joint ventures	3,337	–	–	3,337

Notes

(a) Including net flows of the Group's insurance joint ventures.

(b) The £970 million liabilities of the Japan life operation were removed from policyholder liabilities following its reclassification as held for sale at 30 June 2013, an outflow of £45 million at AER (£39 million at CER) in respect of Japan life were included in net flows up to that date, and hence included in the table above. Excluding the Japan life operation the average shareholder-backed policyholder liabilities for half year 2013 was £21,473 million. No amounts are shown within the 2014 analysis above in respect of Japan life.

(c) Policyholder liabilities relating to shareholder-backed business grew by £8 billion from £180.1 billion at 31 December 2013 to £188.1 billion at 30 June 2014 demonstrating the ongoing growth of our business. The increase reflects positive net flows (premiums net of upfront charges less surrenders, withdrawals, maturities and deaths) of £5.7 billion in the first half of 2014 (half year 2013: £5.9 billion), driven by strong inflows in the US £5.0 billion and Asia £0.9 billion.

C4.1(b) Asia insurance operations

i Analysis of movements in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the movement in policyholder liabilities and unallocated surplus of with-profits funds of Asia insurance operations from the beginning of the period to 30 June is as follows:

Half year 2014 movements	With-profits business £m	Unit-linked liabilities £m	Other business £m	Total £m
At 1 January 2014	13,215	13,765	8,166	35,146
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	13,138	11,918	6,854	31,910
Unallocated surplus of with-profits funds on the consolidated statement of financial position	77	–	–	77
Group's share of policyholder liabilities relating to joint ventures‡	–	1,847	1,312	3,159
Reallocation of unallocated surplus for the domestication of the Hong Kong branch[note (b)]	1,690	–	–	1,690
Premiums:				
New business	138	547	456	1,141
In-force	862	668	524	2,054
	1,000	1,215	980	3,195
Surrenders[note (e)]	(105)	(914)	(114)	(1,133)
Maturities/Deaths	(272)	(29)	(247)	(548)
Net flows[note (d)]	623	272	619	1,514
Shareholders' transfers post tax	(14)	–	–	(14)
Investment-related items and other movements[note (f)]	1,043	798	232	2,073
Foreign exchange translation differences[note (a)]	(404)	(193)	(240)	(837)
At 30 June 2014	16,153	14,642	8,777	39,572
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	14,168	12,638	7,270	34,076
Unallocated surplus of with-profits funds on the consolidated statement of financial position	1,985	–	–	1,985
Group's share of policyholder liabilities relating to joint ventures‡	–	2,004	1,507	3,511

C: Balance sheet notes continued

C4: Policyholder liabilities and unallocated surplus of with-profits funds continued

Half year 2013 movements	With-profits business £m	Unit-linked liabilities £m	Other business £m	Total £m
At 1 January 2013	13,451	14,028	7,185	34,664
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	13,388	11,969	6,144	31,501
Unallocated surplus of with-profits funds on the consolidated statement of financial position	63	–	–	63
Group's share of policyholder liabilities relating to joint ventures‡	–	2,059	1,041	3,100
Premiums:				
New business	144	883	334	1,361
In-force	743	664	498	1,905
	887	1,547	832	3,266
Surrenders[note (e)]	(458)	(1,043)	(151)	(1,652)
Maturities/Deaths	(284)	(22)	(124)	(430)
Net flows[note (d)]	145	482	557	1,184
Shareholders' transfers post tax	(18)	–	–	(18)
Investment-related items and other movements[note (f)]	(544)	341	208	5
Reclassification of Japan life business as held for sale*	–	(377)	(593)	(970)
Acquisition of Thanachart Life[note (g)]	–	–	487	487
Foreign exchange translation differences	707	370	215	1,292
At 30 June 2013	13,741	14,844	8,059	36,644
Comprising:				
Policyholder liabilities on the consolidated statement of financial position	13,657	12,783	6,783	33,223
Unallocated surplus of with-profits funds on the consolidated statement of financial position	84	–	–	84
Group's share of policyholder liabilities relating to joint ventures‡	–	2,061	1,276	3,337
Average policyholder liability balances†				
Half year 2014	**13,653**	**14,204**	**8,472**	**36,328**
Half year 2013	13,522	14,625	7,846	35,993

* The £970 million liabilities of the Japan life operation were removed from policyholder liabilities following its reclassification as held for sale at 30 June 2013, an outflow of £45 million at AER (£39 million at CER) in respect of Japan life were included in net flows up to that date, and hence included in the table above. Excluding the Japan life operation the average shareholder-backed policyholder liabilities for half year 2013 was £21,473 million. No amounts are shown within the 2014 analysis above in respect of Japan life.

† Averages have been based on opening and closing balances and adjusted for acquisitions, disposals and corporate transactions in the period and exclude unallocated surplus of with-profits funds.

‡ The Group's investment in joint ventures are accounted for on an equity method and the Group's share of the policyholder liabilities as shown above relate to the joint venture life business in China, India and of the Takaful business in Malaysia.

Notes

(a) Movements in the period have been translated at the average exchange rates for the period ended 30 June 2014. The closing balance has been translated at the closing spot rates as at 30 June 2014. Differences upon retranslation are included in foreign exchange translation differences.

(b) Up until 31 December 2013 for the purposes of the presentation of unallocated surplus of with-profits within the statement of financial position, the Hong Kong branch balance was reported within the unallocated surplus of the PAC WPSF of the UK insurance operations.

On 1 January 2014, following consultation with the policyholders of PAC and regulators and court approval, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. From this date the unallocated surplus of the Hong Kong with-profits business is reported within the Asia insurance operations segment.

(c) The policyholder liabilities of the Asia insurance operations of £34,076 million as shown in the table above is after deducting the intra-group reinsurance liabilities ceded by the UK insurance operations of £1,296 million to the Hong Kong with-profits business. Including this amount total Asia policyholder liabilities is £35,372 million.

(d) Net flows increased 42 per cent at CER (AER 28 per cent) from £1,069 million in half year 2013 to £1,514 million in half year 2014 predominantly reflecting higher premium income as the in-force book continues to grow together with improved surrender rates in the with-profits business (point (e) below). This has been offset by a higher level of maturities in our shareholder-backed business, which moved from £146 million in the first half of 2013 to £276 million in the first half of 2014, as products reach maturity dates in some markets. For definitions of CER and AER refer to note A1.

(e) The rate of surrenders for shareholder-backed business (expressed as a percentage of opening liabilities) was 4.7 per cent in the first half of 2014, lower than the 5.6 per cent recorded in the first half of 2013. For with-profits business, surrenders, maturities and deaths have decreased from £742 million in half year 2013 to £377 million in half year 2014. The decrease was primarily as a result of an increased number of with-profits policies reaching their five-year anniversary in the first half of 2013, the point at which some product features triggered, which was not repeated in 2014. The higher levels of maturities for shareholder-backed business, which increased from £146 million in the first half of 2013 to £276 million in the first half of 2014, reflects a greater number of contracts reaching maturity dates in some markets.

(f) Investment-related items and other movements in the first half of 2014 primarily represents gains from equity markets in the unit-linked and other business portfolios in conjunction with unrealised profits on bonds within the with-profits funds following the fall in long-term bond yields.

(g) The acquisition of Thanachart Life reflects the liabilities acquired at the date of acquisition.

C4.1(c) US insurance operations

i Analysis of movements in policyholder liabilities

A reconciliation of the movement in policyholder liabilities of US insurance operations from the beginning of the period to 30 June is as follows:

Half year 2014 movements	Variable annuity separate account liabilities £m	Fixed annuity, GIC and other business £m	Total £m
At 1 January 2014	65,681	41,730	107,411
Premiums	6,591	1,844	8,435
Surrenders	(1,720)	(1,067)	(2,787)
Maturities/Deaths	(276)	(395)	(671)
Net flows[note (b)]	4,595	382	4,977
Transfers from general to separate account	708	(708)	–
Investment-related items and other movements[note (c)]	2,718	463	3,181
Foreign exchange translation differences[note (a)]	(2,249)	(1,311)	(3,560)
At 30 June 2014	71,453	40,556	112,009
Half year 2013 movements			
At 1 January 2013	49,298	42,963	92,261
Premiums	5,665	2,543	8,208
Surrenders	(1,352)	(1,068)	(2,420)
Maturities/Deaths	(259)	(361)	(620)
Net flows[note (b)]	4,054	1,114	5,168
Transfers from general to separate account	715	(715)	–
Investment-related items and other movements[note (c)]	2,323	(285)	2,038
Foreign exchange translation differences[note (a)]	3,664	3,084	6,748
At 30 June 2013	60,054	46,161	106,215
Average policyholder liability balances*			
Half year 2014	68,567	41,143	109,710
Half year 2013	54,676	44,562	99,238

* Averages have been based on opening and closing balances, and adjusted for acquisitions, disposals and corporate transactions in the period.

Notes

(a) Movements in the period have been translated at an average rate of US$1.67/£1.00 (30 June 2013: US$1.54/£1.00). The closing balance has been translated at closing rate of US$1.71/£1.00 (30 June 2013: US$1.52/£1.00). Differences upon retranslation are included in foreign exchange translation differences.

(b) Net flows in the first half of 2014 were £4,977 million compared with £5,168 million in the first half of 2013, with the decrease being driven by foreign exchange movements. On CER basis net flows increased by 4 per cent from £4,781 million in the first half of 2013 to £4,977 million in 2014, principally as a result of increased variable annuity new business volumes. For definitions of CER and AER refer to note A1.

(c) Positive investment-related items and other movements in variable annuity separate account liabilities of £2,718 million for the first six months in 2014 represents positive separate account return mainly following the increase in the US equity market in the period. Fixed annuity, GIC and other business investment and other movements of £463 million primarily reflect the interest credited to the policyholders in the period.

C: Balance sheet notes continued

C4: Policyholder liabilities and unallocated surplus of with-profits funds continued

C4.1(d) UK insurance operations

i Analysis of movements in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of UK insurance operations from the beginning of the period to 30 June is as follows:

		Shareholder-backed funds and subsidiaries		
Half year 2014 movements	**SAIF and PAC with-profits sub-fund** £m	**Unit-linked liabilities** £m	**Annuity and other long-term business** £m	**Total** £m
At 1 January 2014	**95,837**	**23,652**	**27,127**	**146,616**
Comprising:				
Policyholder liabilities	**83,853**	**23,652**	**27,127**	**134,632**
Unallocated surplus of with-profits funds	**11,984**	**–**	**–**	**11,984**
Reallocation of unallocated surplus for the domestication of the Hong Kong branch[note (a)]	**(1,690)**	**–**	**–**	**(1,690)**
Premiums	**1,875**	**643**	**1,451**	**3,969**
Surrenders	**(1,207)**	**(1,010)**	**(23)**	**(2,240)**
Maturities/Deaths	**(2,346)**	**(314)**	**(887)**	**(3,547)**
Net flows[note (b)]	**(1,678)**	**(681)**	**541**	**(1,818)**
Shareholders' transfers post tax	**(106)**	**–**	**–**	**(106)**
Switches	**(95)**	**95**	**–**	**–**
Investment-related items and other movements[note (c)]	**3,954**	**624**	**1,329**	**5,907**
Foreign exchange translation differences	**(231)**	**–**	**–**	**(231)**
At 30 June 2014	**95,991**	**23,690**	**28,997**	**148,678**
Comprising:				
Policyholder liabilities	**84,932**	**23,690**	**28,997**	**137,619**
Unallocated surplus of with-profits funds	**11,059**	**–**	**–**	**11,059**
Half year 2013 movements				
At 1 January 2013	94,933	22,197	27,308	144,438
Comprising:				
Policyholder liabilities	84,407	22,197	27,308	133,912
Unallocated surplus of with-profits funds	10,526	–	–	10,526
Premiums	1,790	1,428	662	3,880
Surrenders	(1,063)	(1,227)	(25)	(2,315)
Maturities/Deaths	(2,709)	(326)	(848)	(3,883)
Net flows[note (b)]	(1,982)	(125)	(211)	(2,318)
Shareholders' transfers post tax	(102)	–	–	(102)
Switches	(104)	104	–	–
Investment-related items and other movements[note (c)]	1,614	1,067	(270)	2,411
Foreign exchange translation differences	211	–	–	211
At 30 June 2013	94,570	23,243	26,827	144,640
Comprising:				
Policyholder liabilities	83,220	23,243	26,827	133,290
Unallocated surplus of with-profits funds	11,350	–	–	11,350
Average policyholder liability balances*				
Half year 2014	**84,393**	**23,671**	**28,062**	**136,126**
Half year 2013	83,814	22,720	27,067	133,601

* Averages have been based on opening and closing balances, and adjusted for acquisitions, disposals and corporate transactions in the period, and exclude unallocated surplus of with-profits funds.

Notes

(a) Up until 31 December 2013, for the purposes of the presentation of unallocated surplus of with-profits within the statement of financial position, the Hong Kong branch balance was reported within the unallocated surplus of the PAC WPSF of the UK insurance operations.

On 1 January 2014, following consultation with the policyholders of PAC and regulators and court approval, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. From this date the unallocated surplus of the Hong Kong with-profits business is reported within the Asia insurance operations segment.

(b) Net outflows have improved from £2,318 million in the first half of 2013 to £1,818 million in the same period in 2014, primarily as a result of an increased number of bulk annuity transactions in the period leading to an improvement of £752 million in the net flows for annuity and other long-term business. The levels of inflows/outflows for unit-linked business remains subject to annual variation as it is driven by corporate pension schemes with transfers in or out from only one or two schemes influencing the level of flows in the year.

(c) Investment-related items and other movements of £5,907 million primarily reflect a fall in long-term bond yields and gains on investment properties in the first half of 2014.

C5: Intangible assets

C5.1 Intangible assets attributable to shareholders

C5.1(a) Goodwill attributable to shareholders

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Cost			
At beginning of period	1,581	1,589	1,589
Exchange differences	(3)	5	(8)
At end of period	1,578	1,594	1,581
Aggregate impairment	(120)	(120)	(120)
Net book amount at end of period	1,458	1,474	1,461
Goodwill attributable to shareholders comprises:			
M&G	1,153	1,153	1,153
Other	305	321	308
	1,458	1,474	1,461

Other goodwill represents amounts arising from the purchase of entities by the Asia and the US operations. These goodwill amounts by acquired operations are not individually material.

The aggregate goodwill impairment of £120 million at 30 June 2014, 30 June 2013 and 31 December 2013 relates to the goodwill held in relation to the held for sale Japan life business (see note D1), which was impaired in 2005.

C5.1(b) Deferred acquisition costs and other intangible assets attributable to shareholders

The deferred acquisition costs and other intangible assets attributable to shareholders comprise:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Deferred acquisition costs related to insurance contracts as classified under IFRS 4	4,612	4,851	4,684
Deferred acquisition costs related to investment management contracts, including life assurance contracts classified as financial instruments and investment management contracts under IFRS 4	91	97	96
	4,703	4,948	4,780
Present value of acquired in-force policies for insurance contracts as classified under IFRS 4 (PVIF)	62	85	67
Distribution rights and other intangibles	1,179	505	448
	1,241	590	515
Total of deferred acquisition costs and other intangible assets	5,944	5,538	5,295

C: Balance sheet notes continued

C5: Intangible assets continued

	2014 £m						2013 £m	
	Deferred acquisition costs							
	Asia	US	UK	Asset management	PVIF and other intangibles*	30 Jun Total	30 Jun Total	31 Dec Total
Balance at beginning of period:	553	4,121	89	17	515	5,295	4,177	4,177
Reclassification of Japan life as held for sale[note D1]	–	–	–	–	–	–	(28)	(28)
Additions	93	374	–	2	745	1,214	757	1,230
Acquisition of subsidiaries	–	–	–	–	13	13	21	21
Amortisation to the income statement:								
Operating profit	(55)	(239)	(6)	(2)	(20)	(322)	(311)	(643)
Non-operating profit	–	107	–	–	(4)	103	239	228
	(55)	(132)	(6)	(2)	(24)	(219)	(72)	(415)
Disposals	–	–	–	–	–	–	–	(1)
Exchange differences and other movements	(9)	(130)	–	–	(8)	(147)	264	(187)
Amortisation of DAC related to net unrealised valuation movements on Jackson's available-for-sale securities recognised within other comprehensive income	–	(212)	–	–	–	(212)	419	498
Balance at end of period	582	4,021	83	17	1,241	5,944	5,538	5,295

* PVIF and other intangibles includes amounts in relation to software rights with additions of £10 million, amortisation of £10 million and exchange losses of £1 million and a balance at 30 June 2014 of £55 million.

Note

In March 2014, Prudential announced that the Group has entered into a new agreement expanding the term and geographic scope of our strategic pan-Asian bancassurance partnership with Standard Chartered PLC. The additions of £745 million for PVIF and other intangibles in half year 2014 includes £731 million representing the amount committed to secure this exclusive 15-year new bancassurance partnership agreement, commencing from 1 July 2014, which is not dependent on sales volume delivered through the renewed arrangements. This amount comprises payments already made during the period of US$850 million (£503 million) and a provision of £228 million for two equal committed payments due on 1 April 2015 and 1 April 2016, totalling US$400 million.

The addition of £13 million for acquisition of subsidiaries for PVIF and other intangibles in half year 2014 is for the acquisition of Express Life of Ghana in April 2014. The addition of £21 million in 2013 is for the acquisition of Thanachart Life.

US insurance operations

Summary balances

The DAC amount in respect of US insurance operations comprises amounts in respect of:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Variable annuity business	3,930	3,917	3,716
Other business	747	953	868
Cumulative shadow DAC (for unrealised gains/losses booked in other comprehensive income)*	(656)	(593)	(463)
Total DAC for US operations	4,021	4,277	4,121

* Consequent upon the positive unrealised valuation movement at half year 2014 of £1,023 million (30 June 2013: negative unrealised valuation movement of £1,707 million; 31 December 2013: negative unrealised valuation movement of £2,089 million), there is a debit of £212 million (30 June 2013: a credit of £419 million; 31 December 2013: a credit of £498 million) for altered 'shadow' DAC amortisation booked within other comprehensive income. These adjustments reflect movement from period to period, in the changes to the pattern of reported gross profits that would have happened if the assets reflected in the statement of financial position had been sold, crystallising the unrealised gains and losses, and the proceeds reinvested at the yields currently available in the market. At 30 June 2014, the cumulative shadow DAC balance as shown in the table above was negative £656 million (30 June 2013: negative £593 million; 31 December 2013: negative £463 million).

Overview of the deferral and amortisation of acquisition costs for Jackson

Under IFRS 4, the Group applies 'grandfathered' US GAAP for measuring the insurance assets and liabilities of Jackson. In the case of Jackson term business, acquisition costs are deferred and amortised in line with expected profits. For annuity and interest-sensitive life business, acquisition costs are deferred and amortised in line with a combination of historical and future expected gross profits on the relevant contracts. For fixed and index annuity and interest-sensitive life business, the key assumption is the long-term spread between the earned rate on investments and the rate credited to policyholders, which is based on an annual spread analysis. Expected gross profits also depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges), all of which are based on a combination of actual experience of Jackson, industry experience and future expectations. A detailed analysis of actual mortality, lapse and expense experience is performed using internally developed experience studies.

As with fixed and index annuity and interest-sensitive life business, acquisition costs for Jackson's variable annuity products are amortised in line with the emergence of profits. The measurement of the amortisation in part reflects current period fees (including those for guaranteed minimum death, income, or withdrawal benefits) earned on assets covering liabilities to policyholders, and the historical and expected level of future gross profits which depends on the assumed level of future fees, as well as components related to mortality, lapse, and expense.

Mean reversion technique

For variable annuity products, under US GAAP (as 'grandfathered' under IFRS 4) the projected gross profits, against which acquisition costs are amortised, reflect an assumed long-term level of returns on separate account investments which, for Jackson, is 7.4 per cent (half year 2013: 8.4 per cent; full year 2013: 7.4 per cent) after deduction of net external fund management fees. This is applied to the period end level of separate account assets after application of a mean reversion technique that removes a portion of the effect of levels of short-term variability in current market returns.

Under the mean reversion technique applied by Jackson, the projected level of return for each of the next five years is adjusted from period to period so that in combination with the actual rates of return for the preceding two years and the current period, the 7.4 per cent (half year 2013: 8.4 per cent; full year 2013: 7.4 per cent) annual return is realised on average over the entire eight-year period. Projected returns after the mean reversion period revert back to the 7.4 per cent (half year 2013: 8.4 per cent; full year 2013: 7.4 per cent) assumption.

However, to ensure that the methodology does not over anticipate a reversion to trend following adverse markets, the mean reversion technique has a cap and floor feature, whereby the projected returns in each of the next five years can be no more than 15 per cent per annum and no less than 0 per cent per annum (both gross of asset management fees) in each year.

Sensitivity of amortisation charge

The amortisation charge to the income statement is reflected in both operating profit and short-term fluctuations in investment returns. The amortisation charge to the operating profit in a reporting period comprises:

(i) A core amount that reflects a relatively stable proportion of underlying premiums or profit; and

(ii) An element of acceleration or deceleration arising from market movements differing from expectations.

In periods where the cap and floor feature of the mean reversion technique are not relevant, the technique operates to dampen the second element above. Nevertheless, extreme market movements can cause material acceleration or deceleration of amortisation in spite of this dampening effect.

Furthermore, in those periods where the cap or floor is relevant, the mean reversion technique provides no further dampening and additional volatility may result.

In the first half of 2014, the DAC amortisation charge for operating profit was determined after including a credit for decelerated amortisation of £10 million (half year 2013: credit for decelerated amortisation of £20 million; full year 2013: credit for decelerated amortisation of £82 million). The first half of 2014 amount reflects the separate account performance of 6 per cent, which is higher than the assumed level for the year.

As noted above, the application of the mean reversion formula has the effect of dampening the impact of equity market movements on DAC amortisation, while the mean reversion assumption lies within the corridor. It would take a significant movement in equity markets in 2014 (outside the range of negative 41 per cent to positive 21 per cent) for the mean reversion assumption to move outside the corridor.

C: Balance sheet notes continued

C6: Borrowings

C6.1 Core structural borrowings of shareholder-financed operations

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Holding company operations:			
Perpetual subordinated capital securities (Innovative Tier 1)note (i)	2,067	2,327	2,133
Subordinated notes (Lower Tier 2)note (iv)	1,530	834	1,529
Subordinated debt total	3,597	3,161	3,662
Senior debt:note (ii)			
£300m 6.875% Bonds 2023	300	300	300
£250m 5.875% Bonds 2029	249	249	249
Holding company total	4,146	3,710	4,211
Prudential Capital bank loannote (iii)	275	275	275
Jackson US$250m 8.15% Surplus Notes 2027 (Lower Tier 2)	146	164	150
Total (per condensed consolidated statement of financial position)note (v)	4,567	4,149	4,636

Notes

(i) These debt classifications are consistent with the treatment of capital for regulatory purposes, as defined in the Prudential Regulation Authority handbook.
Tier 1 subordinated debt is entirely US$ denominated. The Group has designated all US$3.55 billion (30 June 2013: US$3.55 billion; 31 December: US$ 3.55 billion) of its Tier 1 subordinated debt as a net investment hedge under IAS 39 to hedge the currency risks related to the investment in Jackson.

(ii) The senior debt ranks above subordinated debt in the event of liquidation.

(iii) The Prudential Capital bank loan of £275 million has been made in two tranches: a £160 million loan maturing on 20 December 2017, currently drawn at a cost of 12 month £LIBOR plus 0.4 per cent and a £115 million loan also maturing on 20 December 2017 and currently drawn at a cost of 12 month £LIBOR plus 0.59 per cent.

(iv) In December 2013, the Company issued core structural borrowings of £700 million Lower Tier 2 subordinated notes primarily to UK institutional investors. The proceeds, net of costs, were £695 million.

(v) The maturity profile, currency and interest rates applicable to the core structural borrowings of shareholder-financed operations of the Group are as detailed in note C6.1 of the Group's consolidated financial statements for the year ended 31 December 2013.

C6.2 Other borrowings

a Operational borrowings attributable to shareholder-financed operationsnote (i)

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Borrowings in respect of short-term fixed income securities programmes	1,950	2,422	1,933
Non-recourse borrowings of US operations	17	20	18
Other borrowings note (ii)	276	88	201
Total	2,243	2,530	2,152

Notes

(i) In addition to the debt listed above, £200 million Floating Rate Notes were issued by Prudential plc in April 2014 which will mature in October 2014. These Notes have been wholly subscribed by a Group subsidiary and accordingly have been eliminated on consolidation in the Group financial statements. These Notes were originally issued in October 2008 and have been reissued upon their maturity.

(ii) Other borrowings mainly include senior debt issued through the Federal Home Loan Bank of Indianapolis (FHLB), secured by collateral posted with the FHLB by Jackson. In addition, other borrowings include amounts whose repayment to the lender is contingent upon future surplus emerging from certain contracts specified under the arrangement. If insufficient surplus emerges on those contracts, there is no recourse to other assets of the Group and the liability is not payable to the degree of shortfall.

b Borrowings attributable to with-profits operations

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Non-recourse borrowings of consolidated investment funds	667	727	691
£100m 8.5% undated subordinated guaranteed bonds of Scottish Amicable Finance plc	100	100	100
Other borrowings (predominantly obligations under finance leases)	97	97	104
Total	864	924	895

C7: Tax assets and liabilities

C7.1 Deferred tax

The statement of financial position contains the following deferred tax assets and liabilities in relation to:

	Deferred tax assets			Deferred tax liabilities		
	30 Jun 2014 £m	30 Jun 2013 £m	31 Dec 2013 £m	30 Jun 2014 £m	30 Jun 2013 £m	31 Dec 2013 £m
Unrealised losses or gains on investments	**116**	261	315	**(1,611)**	(1,610)	(1,450)
Balances relating to investment and insurance contracts	**5**	10	8	**(469)**	(466)	(451)
Short-term timing differences	**2,001**	2,283	2,050	**(1,748)**	(2,019)	(1,861)
Capital allowances	**9**	16	10	**(27)**	(7)	(16)
Unused deferred tax losses	**42**	67	29	**–**	–	–
Total	**2,173**	2,637	2,412	**(3,855)**	(4,102)	(3,778)

Deferred tax assets are recognised to the extent that they are regarded as recoverable, that is to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted.

The taxation regimes applicable across the Group often apply separate rules to trading and capital profits and losses. The distinction between temporary differences that arise from items of either a trading or capital nature may affect the recognition of deferred tax assets. Accordingly, for the 2014 half year results and financial position at 30 June 2014 the possible tax benefit of approximately £123 million (30 June 2013: £164 million; 31 December 2013: £127 million), which may arise from capital losses valued at approximately £0.6 billion (30 June 2013: £0.8 billion; 31 December 2013: £0.6 billion), is sufficiently uncertain that it has not been recognised. In addition, a potential deferred tax asset of £47 million (30 June 2013: £82 million; 31 December 2013: £61 million), which may arise from trading tax losses and other potential temporary differences totalling £0.3 billion (30 June 2013: £0.4 billion; 31 December 2013: £0.4 billion) is sufficiently uncertain that it has not been recognised. Of these, losses of £39 million will expire within the next seven years. Of the remaining losses £0.6 million will expire within 20 years and the rest have no expiry date.

The table that follows provides a breakdown of the recognised deferred tax assets set out in the table above for both the short-term timing differences and unused tax losses split by business unit. The table also shows the period of estimated recoverability for each respective business unit. For these and each category of deferred tax asset recognised their recoverability against forecast taxable profits is not significantly impacted by any current proposed changes to future accounting standards.

	Short-term timing differences		Unused tax losses	
	30 Jun 2014 £m	Expected period of recoverability	30 Jun 2014 £m	Expected period of recoverability
Asia	**26**	1 to 3 years	**35**	3 to 5 years
Jackson	**1,706**	With run-off of in-force book	**–**	–
UK long-term business	**128**	1 to 10 years	**–**	–
Other	**141**	1 to 10 years	**7**	1 to 3 years
Total	**2,001**		**42**	

Under IAS 12 'Income Taxes', deferred tax is measured at the tax rates that are expected to apply to the period when the asset is realised or the liability settled, based on the tax rates (and laws) that have been enacted or are substantively enacted at the end of the reporting periods.

The reduction in the UK corporation tax rate to 21 per cent from 1 April 2014 and a further reduction to 20 per cent from 1 April 2015 was substantively enacted on 2 July 2013 and therefore was reflected in the deferred tax balances as at 31 December 2013 and as at 30 June 2014.

C: Balance sheet notes continued

C8: Defined benefit pension schemes

a Summary and background information

The Group asset/liability in respect of defined benefit pension schemes is as follows:

	2014 £m			2013 £m	
	PSPS	Other schemes	30 Jun Total	30 Jun Total	31 Dec Total
Underlying economic surplus (deficit)[note8c]	745	(54)	691	894	646
Less: unrecognised surplus	(623)	–	(623)	(821)	(602)
Economic surplus (deficit) (including investment in Prudential insurance policies)[note8c]	122	(54)	68	73	44
Attributable to:					
PAC with-profits fund	85	(52)	33	42	29
Shareholder-backed operations	37	(2)	35	31	15
Consolidation adjustment against policyholder liabilities for investment in Prudential insurance policies	–	(122)	(122)	(172)	(114)
IAS 19 pension asset (liability) on the Group statement of financial position*	122	(176)	(54)	(99)	(70)

* At 30 June 2014, the PSPS pension asset of £122 million (30 June 2013: £118 million; 31 December 2013: £124 million) and the other schemes' pension liabilities of £176 million (30 June 2013: £217 million; 31 December 2013: £194 million) were included within other debtors and provisions respectively on the consolidated statement of financial position.

The Group's businesses operate a number of pension schemes. The specific features of these plans vary in accordance with the regulations of the country in which the employees are located, although they are, in general, funded by the Group and based either on a cash balance formula or on years of service and salary earned in the last year or years of employment. The largest defined benefit scheme is the principal UK scheme, namely the Prudential Staff Pension Scheme (PSPS). PSPS accounts for 84 per cent (30 June 2013: 85 per cent; 31 December 2013: 84 per cent) of the underlying scheme liabilities of the Group's defined benefit schemes.

The Group also operates two smaller UK defined benefit schemes in respect of Scottish Amicable and M&G. In addition, there are two small defined benefit schemes in Taiwan which have negligible deficits.

Triennial actuarial valuations

Defined benefit schemes in the UK are generally required to be subject to full actuarial valuations every three years in order to assess the appropriate level of funding for schemes in relation to their commitments. These valuations include assessments of the likely rate of return on the assets held within the separate trustee administered funds.

The last completed actuarial valuation of PSPS was as at 5 April 2011. This valuation was finalised in the first half of 2012 and demonstrated the scheme to be 111 per cent funded by reference to the Scheme Solvency Target that forms the basis of the scheme's funding objective. Based on this valuation, future contributions into the scheme were reduced to the minimum level of contributions required under the scheme rules effective from July 2012. Excluding expenses, the contributions are now payable at approximately £6 million per annum for ongoing service of active members of the scheme. No deficit or other funding is required. Deficit funding for PSPS, where applicable, as applied prior to 2012, is apportioned in the ratio of 70/30 between the PAC with-profits fund and shareholder-backed operations following detailed consideration in 2005 of the sourcing of previous contributions. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity.

The last completed actuarial valuation of the Scottish Amicable Staff Pension Scheme (SASPS) was as at 31 March 2011. This valuation was finalised in the second half of 2012 and demonstrated the scheme to be 85 per cent funded. Based on this valuation, it was agreed with the Trustees that the existing level of deficit funding of £13.1 million per annum continues to be paid into the scheme until 31 December 2018, to eliminate the actuarial deficit. The deficit funding will be reviewed every three years at subsequent valuations.

The last completed actuarial valuation of the M&G Group Pension Scheme (M&GGPS) was as at 31 December 2011. This valuation was finalised in the second half of 2012 and demonstrated the scheme to be 83 per cent funded. Based on this valuation, deficit funding amounts designed to eliminate the actuarial deficit over a three-year period are being made from January 2013 of £18.6 million per annum for the first two years and £9.3 million in the third year.

The next triennial valuation for the PSPS and SASPS as at 5 April 2014 and 31 March 2014 respectively are currently in progress. The next triennial valuation for the M&GGPS is as at 31 December 2014.

Summary economic and IAS 19 financial positions

Under the IAS 19 'Employee Benefits' valuation basis, the Group applies IFRIC 14, 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. Under IFRIC 14, a surplus is only recognised to the extent that the Company is able to access the surplus either through an unconditional right of refund to the surplus or through reduced future contributions relating to ongoing service, which have been substantively enacted or contractually agreed. Further, the IFRS financial position recorded, reflects the higher of any underlying IAS 19 deficit and any obligation for committed deficit funding where applicable. For PSPS, the Group does not have an unconditional right of refund to any surplus of the scheme.

The underlying IAS 19 surplus for PSPS at 30 June 2014 was £745 million (30 June 2013: £939 million; 31 December 2013: £726 million) of which reflecting the arrangements under the scheme rules only a portion of the surplus, being £122 million (30 June 2013: £118 million; 31 December 2013: £124 million), is recognised as recoverable. The £122 million represents the present value of the economic benefit to the Company from the difference between future ongoing contributions to the scheme and estimated accrued cost of service. Of this amount, £85 million has been allocated to the PAC with-profits fund and £37 million was allocated to the shareholders' fund (30 June 2013: £83 million; 31 December 2013: £37 million).

The IAS 19 deficit of the Scottish Amicable Pension Scheme at 31 December 2013 was a deficit of £105 million (30 June 2013: £82 million; 31 December 2013: £115 million) and has been allocated approximately 50 per cent to the PAC with-profits fund and 50 per cent to the shareholders' fund.

The IAS 19 surplus of the M&GGPS on an economic basis at 30 June 2014 was £51 million (30 June 2013: surplus of £37 million; 31 December 2013: surplus of £36 million) and is wholly attributable to shareholders. The underlying position on an economic basis reflects the assets (including investments in Prudential insurance policies that are offset against liabilities to policyholders on the Group consolidation) and the liabilities of the schemes. As at 30 June 2014, the M&GGPS has invested £122 million in Prudential insurance policies (30 June 2013: £172 million; 31 December 2013: £114 million). After excluding these investments that are offset against liabilities to policyholders, the IAS 19 basis position of the M&GGPS is a deficit of £71 million (30 June 2013: £135 million; 31 December 2013: £78 million).

b Assumptions

The actuarial assumptions used in determining benefit obligations and the net periodic benefit costs for the periods ended 30 June 2014, 30 June 2013 and 31 December 2013 were as follows:

	2014 %	2013 %	
	30 Jun	30 Jun	31 Dec
Discount rate*	4.2	4.6	4.4
Rate of increase in salaries	3.2	3.2	3.3
Rate of inflation†:			
Retail prices index (RPI)	3.2	3.2	3.3
Consumer prices index (CPI)	2.2	2.2	2.3
Rate of increase of pensions in payment for inflation:			
PSPS:			
Guaranteed (maximum 5%)	2.5	2.5	2.5
Guaranteed (maximum 2.5%)	2.5	2.5	2.5
Discretionary	2.5	2.5	2.5
Other schemes	3.2	3.2	3.3

* The discount rate has been determined by reference to an 'AA' corporate bond index, adjusted where applicable, to allow for the difference in duration between the index and the pension liabilities.
† The rate of inflation reflects the long-term assumption for the UK RPI or CPI depending on the tranche of the schemes.

The calculations are based on current actuarially calculated mortality estimates with a specific allowance made for future improvements in mortality. The specific allowance made is in line with a custom calibration and has been updated in half year 2014 to reflect the 2012 mortality model from the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries (CMI). The tables used for PSPS immediate annuities in payment at 30 June 2014 were:

Male: 114.0 per cent PNMA00 with improvements in line with a custom calibration of the CMI's 2012 mortality model, with a long-term mortality improvement rate of 1.75 per cent per annum; and

Female: 108.5 per cent PNFA00 with improvements in line with a custom calibration of the CMI's 2012 mortality model, with a long-term mortality improvement rate of 1.25 per cent per annum.

The tables used for PSPS immediate annuities in payment at 30 June 2013 and 31 December 2013 were:

Male: 112.0 per cent PNMA00 with improvements in line with a custom calibration of the CMI's 2011 mortality model, with a long-term mortality improvement rate of 1.75 per cent per annum; and

Female: 108.5 per cent PNFA00 with improvements in line with a custom calibration of the CMI's 2011 mortality model, with a long-term mortality improvement rate of 1.25 per cent per annum.

Using external actuarial advice provided by the scheme actuaries being Towers Watson for the valuation of PSPS, Xafinity Consulting for SASPS and Aon Hewitt Limited for the M&GGPS, the most recent full valuations have been updated to 30 June 2014, applying the principles prescribed by IAS 19.

C: Balance sheet notes continued

C8: Defined benefit pension schemes continued

c Estimated pension scheme surpluses and deficits

The underlying pension position on an economic basis reflects the assets (including investments in Prudential policies that are offset against liabilities to policyholders on the Group consolidation) and the liabilities of the schemes. The IAS 19 basis excludes the investments in Prudential policies. At 30 June 2014, the investments in Prudential insurance policies comprise £142 million (30 June 2013: £131 million; 31 December 2013: £143 million) for PSPS and £122 million (30 June 2013: £172 million; 31 December 2013: £114 million) for the M&GGPS. On consolidation as required under IFRS, the investments are eliminated against policyholder liabilities of UK insurance operations, so that the formal IAS 19 position for the scheme in isolation excludes these items. This treatment applies to the M&GGPS investments. However, as a substantial portion of the Company's interest in the underlying surplus of PSPS is not recognised, the adjustment is not necessary for the PSPS investments.

Movements on the pension scheme surplus (deficit) determined on the economic basis are as follows, with the effect of the application of IFRIC 14 being shown separately:

	Half year 2014 £m				
		(Charge) credit to income statement or other comprehensive income			
	Surplus (deficit) in schemes at 1 Jan 2014	Operating results (based on longer-term investment returns)	Actuarial and other gains and losses	Contributions paid	Surplus (deficit) in schemes at 30 Jun 2014
All schemes					
Underlying position (without the effect of IFRIC 14)					
Surplus	646	(4)	21	28	691
Less: amount attributable to PAC with-profits fund	(457)	(2)	(10)	(8)	(477)
Shareholders' share:					
Gross of tax surplus (deficit)	189	(6)	11	20	214
Related tax	(38)	1	(2)	(4)	(43)
Net of shareholders' tax	151	(5)	9	16	171
Application of IFRIC 14 for the derecognition of PSPS surplus					
Derecognition of surplus	(602)	(13)	(8)	–	(623)
Less: amount attributable to PAC with-profits fund	428	9	7	–	444
Shareholders' share:					
Gross of tax surplus (deficit)	(174)	(4)	(1)	–	(179)
Related tax	35	1	–	–	36
Net of shareholders' tax	(139)	(3)	(1)	–	(143)
With the effect of IFRIC 14					
Surplus (deficit)	44	(17)	13	28	68
Less: amount attributable to PAC with-profits fund	(29)	7	(3)	(8)	(33)
Shareholders' share:					
Gross of tax surplus (deficit)	15	(10)	10	20	35
Related tax	(3)	2	(2)	(4)	(7)
Net of shareholders' tax	12	(8)	8	16	28

Underlying investments and liabilities of the schemes

On the 'economic basis', after including the underlying assets represented by the investments in Prudential insurance policies as scheme assets, the plans' net assets at 30 June 2014 comprise the following investments and liabilities:

	2014				2013	
	PSPS £m	Other schemes £m	Total £m	%	30 Jun* Total £m	31 Dec Total £m
Equities:						
UK	132	79	211	3	204	209
Overseas	10	312	322	5	280	329
Bonds:						
Government	4,420	339	4,759	67	4,854	4,599
Corporate	873	114	987	14	643	822
Asset-backed securities	71	23	94	1	65	62
Derivatives	127	4	131	2	208	97
Properties	44	53	97	1	129	115
Other assets	516	25	541	7	567	711
Total value of assets	6,193	949	7,142	100	6,950	6,944

* The 30 June 2013 comparatives have been reclassified to align to the 30 June 2014 and 31 December 2013's asset categorisation.

d Sensitivity of the pension scheme liabilities to key variables

The total underlying Group pension scheme liabilities of £6,451 million (30 June 2013: £6,056 million; 31 December 2013: £6,298 million) comprise £5,448 million (30 June 2013: £5,158 million; 31 December 2013: £5,316 million) for PSPS and £1,003 million (30 June 2013: £898 million; 31 December 2013: £982 million) for the other schemes. The table below shows the sensitivity of the underlying PSPS and the other scheme liabilities at 30 June 2014, 30 June 2013 and 31 December 2013 to changes in discount rate, inflation rates and mortality rates. The sensitivity information below is based on the core scheme liabilities and assumptions at the balance sheet date. The sensitivity is calculated based on a change in one assumption with all other assumptions being held constant. As such, interdependencies between the assumptions are excluded.

The sensitivity of the underlying pension scheme liabilities to changes in discount, inflation and mortality rates as shown below does not directly equate to the impact on the profit or loss and equity attributable to shareholders due to the effect of the application of IFRIC 14 on PSPS and the allocation of a share of the interest in financial position of the PSPS and SASPS schemes to the PAC with-profits fund as described above.

The sensitivity to the changes in the key variables as shown in the table below has no significant impact on the pension costs included in the Group's operating results. This is due to the pension costs charged in each of the periods presented being derived largely from market conditions at the beginning of the period. After applying IFRIC 14 and to the extent attributable to shareholders, any residual impact from the changes to these variables is reflected as actuarial gains and losses on defined benefit pension schemes within other comprehensive income.

	Assumption applied			Sensitivity change in assumption	Impact of sensitivity on scheme liabilities on IAS 19 basis			
	2014	2013				2014	2013	
	30 Jun	30 Jun	31 Dec			30 Jun	30 Jun	31 Dec
Discount rate	4.2%	4.6%	4.4%	Decrease by 0.2%	Increase in scheme liabilities by:			
					PSPS	3.3%	3.4%	3.3%
					Other schemes	5.0%	5.0%	5.1%
Discount rate	4.2%	4.6%	4.4%	Increase by 0.2%	Decrease in scheme liabilities by:			
					PSPS	3.1%	3.2%	3.1%
					Other schemes	4.7%	4.7%	4.7%
Rate of inflation	RPI: 3.2% CPI: 2.2%	3.2% 2.2%	3.3% 2.3%	RPI: Decrease by 0.2% CPI: Decrease by 0.2% with consequent reduction in salary increases	Decrease in scheme liabilities by:			
					PSPS	0.7%	0.7%	0.7%
					Other schemes	4.1%	4.3%	4.6%
Mortality rate				Increase life expectancy by 1 year	Increase in scheme liabilities by:			
					PSPS	3.0%	2.6%	2.7%
					Other schemes	3.0%	2.5%	2.7%

C: Balance sheet notes continued

C9: Share capital, share premium and own shares

	30 Jun 2014			30 Jun 2013			31 Dec 2013		
	Number of ordinary shares	Share capital £m	Share premium £m	Number of ordinary shares	Share capital £m	Share premium £m	Number of ordinary shares	Share capital £m	Share premium £m
Issued shares of 5p each fully paid:									
At 1 January	2,560,381,736	128	1,895	2,557,242,352	128	1,889	2,557,242,352	128	1,889
Shares issued under share-based schemes	5,845,737	–	8	2,036,258	–	1	3,139,384	–	6
At end of period	2,566,227,473	128	1,903	2,559,278,610	128	1,890	2,560,381,736	128	1,895

Amounts recorded in share capital represent the nominal value of the shares issued. The difference between the proceeds received on issue of shares, net of issue costs, and the nominal value of shares issued is credited to the share premium account.

At 30 June 2014, there were options outstanding under Save As You Earn schemes to subscribe for shares as follows:

	Number of shares to subscribe for	Share price range from	Share price range to	Exercisable by year
30 June 2014	7,617,023	288p	901p	2019
30 June 2013	9,014,837	288p	629p	2018
31 December 2013	10,233,986	288p	901p	2019

Transactions by Prudential plc and its subsidiaries in Prudential plc shares

The Group buys and sells Prudential plc shares ('own shares') either in relation to its employee share schemes or via transactions undertaken by authorised investment funds that the Group is deemed to control. The cost of own shares of £180 million as at 30 June 2014 (30 June 2013: £71 million; 31 December 2013: £141 million) is deducted from retained earnings. The Company has established trusts to facilitate the delivery of shares under employee incentive plans. At 30 June 2014, 9.5 million (30 June 2013: 4.2 million; 31 December 2013: 7.1 million) Prudential plc shares with a market value of £127.8 million (30 June 2013: £45 million; 31 December 2013: £94.5 million) were held in such trusts all of which are for employee incentive plans. The maximum number of shares held in half year 2014 was 9.5 million which was in May 2014.

The Company purchased the following number of shares in respect of employee incentive plans:

	Number of shares purchased (in millions)	Cost £m
Half year 2014	6.2	81.9
Half year 2013	2.9	31.4
Full year 2013	4.4	53.8

The Group has consolidated a number of authorised investment funds where it is deemed to control these funds under IFRS. Some of these funds hold shares in Prudential plc. The total number of shares held by these funds at 30 June 2014 was 7.5 million (30 June 2013: 4.2 million; 31 December 2013: 7.1 million) and the cost of acquiring these shares of £67 million (30 June 2013: £26 million; 31 December 2013: £60 million) is included in the cost of own shares. The market value of these shares as at 30 June 2014 was £100 million (30 June 2013: £46 million; 31 December 2013: £95 million). During 2014, these funds made net additions of 405,978 Prudential shares (30 June 2013: net disposals of 268,411; 31 December 2013: net additions of 2,629,816) for a net increase of £6.5 million to book cost (30 June 2013: net decrease of £2.6 million; 31 December 2013: net increase of £33.1 million).

All share transactions were made on an exchange other than the Stock Exchange of Hong Kong.

Other than set out above the Group did not purchase, sell or redeem any Prudential plc listed securities during half year 2014 or 2013.

D: Other notes

D1: Held for sale Japan life business

The Group's closed book life insurance business in Japan, PCA Life Insurance Company Limited has been classified as held for sale in these condensed consolidated financial statements in accordance with IFRS 5 'Non-current assets held for sale and discontinued operations'.

This classification reflects the expected disposal of the business on which an agreement to sell was reached in July 2013. The sale has yet to be completed.

The assets and liabilities of the Japan life business classified as held for sale on the statement of financial position as at 30 June 2014 are as follows:

	2014 £m	2013 £m	
	30 Jun	30 Jun	31 Dec
Assets			
Investments	934	1,095	956
Other assets	72	119	80
	1,006	1,214	1,036
Adjustment for remeasurement of the carrying value to fair value less costs to sell	(131)	(135)	(120)
Assets held for sale	875	1,079	916
Liabilities			
Policyholder liabilities	783	970	814
Other liabilities	45	56	54
Liabilities held for sale	828	1,026	868
Net assets	47	53	48

The remeasurement of the carrying value of the Japan life business on classification as held for sale resulted in a charge of £(11) million (half year 2013: £(135) million; full year 2013: £(120) million) as shown in the income statement. In the supplementary analysis of profit of the Group as shown in note B1.1, those amounts are included within 'Loss attaching to held for sale Japan life business', together with the income, including short-term value movements on investments, of the business.

D2: Domestication of the Hong Kong branch business

On 1 January 2014, following consultation with policyholders of PAC and regulators and court approval, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. On an IFRS basis, approximately £12.6 billion of assets, £12.3 billion of liabilities (including policyholder liabilities of £10.2 billion and £1.7 billion of unallocated surplus) and £0.3 billion of shareholders' funds (for the excess assets of the transferred non-participating business) have been transferred.

The costs of enabling the domestication in the first half of 2014 were £8 million (full year 2013: £35 million). Within the Group's supplementary analysis of profit, these costs have been presented as a separate category of items excluded from operating profit based on longer-term investment returns.

D3: Contingencies and related obligations

The Group is involved in various litigation and regulatory issues. While the outcome of such matters cannot be predicted with certainty, Prudential believes that the ultimate outcome of such litigation and regulatory issues will not have a material adverse effect on the Group's financial condition, results of operations or cash flows.

There have been no material changes to the Group's contingencies and related obligations in the six-month period ended 30 June 2014.

D4: Post balance sheet events

Interim dividend

The 2014 interim dividend approved by the Board of Directors after 30 June 2014 is as described in note B7.

D5: Related party transactions

There were no transactions with related parties during the six months ended 30 June 2014 which have had a material effect on the results or financial position of the Group.

The nature of the related party transactions of the Group has not changed from those described in the Group's consolidated financial statements for the year ended 31 December 2013.

Statement of directors' responsibilities

The directors are responsible for preparing the Half Year Financial Report in accordance with applicable law and regulations.

Accordingly, the directors confirm that to the best of their knowledge:

— the condensed consolidated financial statements have been prepared in accordance with IAS 34 'Interim Financial Reporting', as adopted by the European Union;

— the Half Year Financial Report includes a fair review of information required by:

(a) DTR 4.2.7R of the Disclosure and Transparency Rules, being an indication of important events that have occurred during the six months ended 30 June 2014, and their impact on the condensed consolidated financial statements, and a description of the principal risks and uncertainties for the remaining six months of the year; and

(b) DTR 4.2.8R of the Disclosure and Transparency Rules, being related party transactions that have taken place during the six months ended 30 June 2014 and that have materially affected the financial position or the performance of the Group during the period and changes in the related party transactions described in the Group's consolidated financial statements for the year ended 31 December 2013.

The directors of Prudential plc as at 11 August are as listed in the Group's 2013 Annual Report except for the addition of Pierre-Olivier Bouée and the stepping down of John Foley in the first six months of 2014.

Independent review report to Prudential plc

Introduction

We have been engaged by the company to review the International Financial Reporting Standards (IFRS) basis financial information in the Half Year Financial Report for the six months ended 30 June 2014 which comprises the Condensed Consolidated Income Statement, the Condensed Consolidated Statement of Comprehensive Income, the Condensed Consolidated Statement of Changes in Equity, the Condensed Consolidated Statement of Financial Position, the Condensed Consolidated Statement of Cash Flows and the related explanatory notes.

We have also been engaged by the company to review the European Embedded Value (EEV) basis supplementary financial information for the six months ended 30 June 2014 which comprises the Post-tax Operating Profit Based on Longer-Term Investment Returns, the Post-tax Summarised Consolidated Income Statement, the Movement in Shareholders' Equity, the Summary Statement of Financial Position and the related explanatory notes and Total Insurance and Investment Products New Business information.

We have read the other information contained in the Half Year Financial Report and considered whether it contains any apparent misstatements or material inconsistencies with the IFRS basis financial information or the EEV basis supplementary financial information.

This report is made solely to the company in accordance with the terms of our engagement to assist the company in meeting the requirements of the Disclosure and Transparency Rules ('the DTR') of the UK's Financial Conduct Authority ('the UK FCA') and also to provide a review conclusion to the company on the EEV basis supplementary financial information. Our review of the IFRS basis financial information has been undertaken so that we might state to the company those matters we are required to state to it in this report and for no other purpose. Our review of the EEV basis supplementary financial information has been undertaken so that we might state to the company those matters we have been engaged to state in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company for our review work, for this report, or for the conclusions we have reached.

Directors' responsibilities

The Half Year Financial Report, including the IFRS basis financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the Half Year Financial Report in accordance with the DTR of the UK FCA. The directors have accepted responsibility for preparing the EEV basis supplementary financial information in accordance with the European Embedded Value Principles issued in May 2004 by the European CFO Forum ('the EEV Principles') and for determining the methodology and assumptions used in the application of those principles.

The annual IFRS basis financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union ('EU'). The IFRS basis financial information included in this Half Year Financial Report has been prepared in accordance with IAS 34 Interim Financial Reporting as adopted by the EU.

The EEV basis supplementary financial information has been prepared in accordance with the EEV principles using the methodology and assumptions set out in notes 1 and 15 to the EEV basis supplementary financial information. The EEV basis supplementary financial information should be read in conjunction with the IFRS basis financial information.

Our responsibility

Our responsibility is to express to the company a conclusion on the IFRS basis financial information in the Half Year Financial Report and the EEV basis supplementary financial information based on our reviews, as set out in our engagement letter with you dated 9 June 2014.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity issued by the Auditing Practices Board for use in the UK. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the IFRS basis financial information in the Half Year Financial Report for the six months ended 30 June 2014 is not prepared, in all material respects, in accordance with IAS 34 as adopted by the EU and the DTR of the UK FCA.

Based on our review, nothing has come to our attention that causes us to believe that the EEV basis supplementary financial information for the six months ended 30 June 2014 is not prepared, in all material respects, in accordance with the EEV Principles, using the methodology and assumptions set out in notes 1 and 15 to the EEV basis supplementary financial information.

Rees Aronson

Rees Aronson

for and on behalf of KPMG LLP, Chartered Accountants London

11 August 2014

Section 4

European Embedded Value (EEV) basis results

Description of EEV basis reporting

In broad terms, IFRS profits for long-term business reflect the aggregate of results on a traditional accounting basis. By contrast, embedded value is a way of reporting the value of the life insurance business.

The European Embedded Value principles were published by the CFO Forum of major European insurers in May 2004. The principles provide consistent definitions, a framework for setting actuarial assumptions and an approach to the underlying methodology and disclosures.

Results prepared under the EEV principles capture the discounted value of future profits expected to arise from the current book of long-term business. The results are prepared by projecting cash flows, by product, using best estimate assumptions for all relevant factors. Furthermore, in determining these expected profits full allowance is made for the risks attached to their emergence and the associated cost of capital, and takes into account recent experience in assessing likely future persistency, mortality and expenses. Further details are explained in note 14.

Post-tax basis of presentation

As previously announced, from 1 January 2014 the basis of presentation has been altered to be on a post-tax basis and, accordingly, all comparatives are shown on a comparable basis.

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Index to European Embedded Value (EEV) basis results

Notes on the EEV basis results

European Embedded Value (EEV) basis results

Post-tax operating profit based on longer-term investment returns

Results analysis by business area

	Note	2014 £m Half year	2013* £m Half year note (ii)	2013* £m Full year
Asia operations				
New business	3	494	502	1,139
Business in force	4	339	327	753
Long-term business		833	829	1,892
Eastspring Investments		36	32	64
Development expenses		(1)	(2)	(1)
Total		868	859	1,955
US operations				
New business	3	376	311	706
Business in force	4	401	396	820
Long-term business		777	707	1,526
Broker-dealer and asset management		(5)	21	39
Total		772	728	1,565
UK operations				
New business	3	145	100	237
Business in force	4	243	204	595
Long-term business		388	304	832
General insurance commission		9	11	22
Total UK insurance operations		397	315	854
M&G (including Prudential Capital)		200	175	346
Total		597	490	1,200
Other income and expenditure note (i)		(280)	(235)	(482)
Solvency II and restructuring costs		(14)	(21)	(34)
Post-tax operating profit based on longer-term investment returns		1,943	1,821	4,204
Analysed as profits (losses) from:				
New business	3	1,015	913	2,082
Business in force	4	983	927	2,168
Long-term business		1,998	1,840	4,250
Asset management		231	228	449
Other results		(286)	(247)	(495)
Total		1,943	1,821	4,204

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis. This approach has been adopted throughout this supplementary information.

Notes

(i) EEV basis other income and expenditure represents the IFRS basis post-tax result, less the unwind of expected margins on the internal management of the assets of the covered business (as explained in note 14(c)(vi)).

(ii) The comparative results have been prepared using previously reported average exchange rates for the period. For memorandum disclosure purposes note 2 presents the half year 2013 results on both actual exchange rates (AER) and constant exchange rates (CER) bases.

European Embedded Value (EEV) basis results continued

Post-tax summarised consolidated income statement

	Note	2014 £m	2013* £m	
		Half year	Half year note	Full year
Post-tax operating profit based on longer-term investment returns				
Asia operations		**868**	859	1,955
US operations		**772**	728	1,565
UK operations:				
UK insurance operations		**397**	315	854
M&G (including Prudential Capital)		**200**	175	346
		597	490	1,200
Other income and expenditure		**(280)**	(235)	(482)
Solvency II and restructuring costs		**(14)**	(21)	(34)
Post-tax operating profit based on longer-term investment returns		**1,943**	1,821	4,204
Short-term fluctuations in investment returns	7	**432**	(587)	(564)
Effect of changes in economic assumptions	8	**(368)**	534	629
Mark to market value movements on core borrowings		**(66)**	203	152
Loss attaching to held for sale Japan life business	5	**–**	(47)	(35)
Costs of domestication of Hong Kong branch	6	**(7)**	–	(28)
Total post-tax non-operating profit		**(9)**	103	154
Profit for the period attributable to equity holders of the Company		**1,934**	1,924	4,358

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Note
The comparative results have been prepared using previously reported average exchange rates for the period. For memorandum disclosure purposes note 2 presents the half year 2013 results on both actual exchange rates (AER) and constant exchange rates (CER) bases.

Earnings per share

	2014	2013	
	Half year	Half year note	Full year
Based on post-tax operating profit including longer-term investment returns of £1,943 million (half year 2013: £1,821 million; full year 2013: £4,204 million) (in pence)	**76.3p**	71.5p	165.0p
Based on post-tax profit of £1,934 million (half year 2013: £1,924 million; full year 2013: £4,358 million) (in pence)	**75.9p**	75.5p	171.0p
Average number of shares (millions)	**2,547**	2,548	2,548

Note
The comparative results have been prepared using previously reported average exchange rates for the period. For memorandum disclosure purposes note 2 presents the half year 2013 results on both actual exchange rates (AER) and constant exchange rates (CER) bases.

Dividends per share (in pence)

	2014	2013	
	Half year	Half year	Full year
Dividends relating to reporting period:			
Interim dividend (2014 and 2013)	**11.19p**	9.73p	9.73p
Final dividend (2013)	**–**	–	23.84p
Total	**11.19p**	9.73p	33.57p
Dividends declared and paid in reporting period:			
Current year interim dividend	**–**	–	9.73p
Final dividend for prior year	**23.84p**	20.79p	20.79p
Total	**23.84p**	20.79p	30.52p

Movement in shareholders' equity

	Note	2014 £m Half year	2013* £m Half year	2013* £m Full year
Profit for the period attributable to equity shareholders		**1,934**	1,924	4,358
Items taken directly to equity:				
Exchange movements on foreign operations and net investment hedges		**(377)**	693	(1,077)
Dividends		**(610)**	(532)	(781)
New share capital subscribed		**8**	1	6
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes		**10**	(26)	(53)
Reserve movements in respect of share-based payments		**52**	31	98
Treasury shares:				
Movement in own shares in respect of share-based payment plans		**(34)**	25	(10)
Movement in own shares purchased by unit trusts consolidated under IFRS		**(6)**	2	(31)
Mark to market value movements on Jackson assets backing surplus and required capital		**71**	(39)	(97)
Net increase in shareholders' equity	11	**1,048**	2,079	2,413
Shareholders' equity at beginning of period:				
As previously reported	11	**24,856**	22,443	22,443
Effect of the domestication of Hong Kong branch on 1 January 2014	6	**(11)**	–	–
		24,845	22,443	22,443
Shareholders' equity at end of period	11	**25,893**	24,522	24,856

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis - see note 1.

Comprising:	30 Jun 2014 £m Long-term business operations	30 Jun 2014 £m Asset management and other operations	30 Jun 2014 £m Total	30 Jun 2013 £m Long-term business operations	30 Jun 2013 £m Asset management and other operations	30 Jun 2013 £m Total	31 Dec 2013 £m Long-term business operations	31 Dec 2013 £m Asset management and other operations	31 Dec 2013 £m Total
Asia operations:									
Net assets of operations	**10,769**	**192**	**10,961**	10,921	217	11,138	10,305	194	10,499
Acquired goodwill	**228**	**61**	**289**	244	61	305	231	61	292
	10,997	**253**	**11,250**	11,165	278	11,443	10,536	255	10,791
US operations:									
Net assets of operations	**7,155**	**125**	**7,280**	6,638	127	6,765	6,966	118	7,084
Acquired goodwill	**–**	**16**	**16**	–	16	16	–	16	16
	7,155	**141**	**7,296**	6,638	143	6,781	6,966	134	7,100
UK insurance operations:									
Net assets of operations	**7,654**	**9**	**7,663**	7,096	11	7,107	7,342	22	7,364
M&G:									
Net assets of operations	**–**	**506**	**506**	–	511	511	–	449	449
Acquired goodwill	**–**	**1,153**	**1,153**	–	1,153	1,153	–	1,153	1,153
	–	**1,659**	**1,659**	–	1,664	1,664	–	1,602	1,602
	7,654	**1,668**	**9,322**	7,096	1,675	8,771	7,342	1,624	8,966
Other operations:									
Holding company net borrowings at market value[note 9]	**–**	**(2,696)**	**(2,696)**	–	(2,580)	(2,580)	–	(2,373)	(2,373)
Other net assets	**–**	**721**	**721**	–	107	107	–	372	372
	–	**(1,975)**	**(1,975)**	–	(2,473)	(2,473)	–	(2,001)	(2,001)
Shareholders' equity at end of period	**25,806**	**87**	**25,893**	24,899	(377)	24,522	24,844	12	24,856
Representing:									
Net assets (liabilities)	**25,578**	**(1,143)**	**24,435**	24,655	(1,607)	23,048	24,613	(1,218)	23,395
Acquired goodwill	**228**	**1,230**	**1,458**	244	1,230	1,474	231	1,230	1,461
	25,806	**87**	**25,893**	24,899	(377)	24,522	24,844	12	24,856

European Embedded Value (EEV) basis results continued

Net asset value per share

	2014	2013	
	30 Jun	**30 Jun**	**31 Dec**
Based on EEV basis shareholders' equity of £25,893 million (half year 2013: £24,522 million; full year 2013: £24,856 million) (in pence)	**1,009p**	958p	971p
Number of issued shares at period end (millions)	**2,566**	2,559	2,560
Annualised return on embedded value*	**16%**	16%	19%

* Annualised return on embedded value is based on EEV post-tax operating profit, as a percentage of opening EEV basis shareholders' equity. Half year profits are annualised by multiplying by two.

Summary statement of financial position

		2014 £m	**2013** £m	
	Note	**30 Jun**	**30 Jun**	**31 Dec**
Total assets less liabilities, before deduction for insurance funds		**300,630**	286,583	288,826
Less insurance funds:*				
Policyholder liabilities (net of reinsurers' share) and unallocated surplus of with-profits funds		**(290,005)**	(276,958)	(279,176)
Less shareholders' accrued interest in the long-term business		**15,268**	14,897	15,206
		(274,737)	(262,061)	(263,970)
Total net assets	11	**25,893**	24,522	24,856
Share capital		**128**	128	128
Share premium		**1,903**	1,890	1,895
IFRS basis shareholders' reserves		**8,594**	7,607	7,627
Total IFRS basis shareholders' equity	11	**10,625**	9,625	9,650
Additional EEV basis retained profit	11	**15,268**	14,897	15,206
Total EEV basis shareholders' equity (excluding non-controlling interests)	11	**25,893**	24,522	24,856

* Including liabilities in respect of insurance products classified as investment contracts under IFRS 4.

Notes on the EEV basis results

1 Basis of preparation

The EEV basis results have been prepared in accordance with the EEV Principles issued by the European Insurance CFO Forum in May 2004. Where appropriate, the EEV basis results include the effects of adoption of International Financial Reporting Standards (IFRS). The EEV results are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis.

The directors are responsible for the preparation of the supplementary information in accordance with the EEV Principles. The EEV basis results of 2014 and 2013 half years are unaudited. Except for the change in presentation of EEV results from pre-tax to post-tax, as described in the additional unaudited financial information for the full year 2013 announcement, the 2013 results have been derived from the EEV basis results supplement to the Company's statutory accounts for 2013. The supplement included an unqualified audit report from the auditors.

A detailed description of the EEV methodology and accounting presentation is provided in note 14.

2 Results analysis by business area

The half year 2013 comparative results are shown below on both actual exchange rates (AER) and constant exchange rates (CER) bases. The half year 2013 CER comparative results are translated at half year 2014 average exchange rates.

Annual premium and contribution equivalents

	2014 £m	2013 £m		%	
	Half year (note 3)	AER Half year (note 3)	CER Half year	AER vs Half year	CER vs Half year
Asia operations	996	1,010	882	(1)%	13%
US operations	871	797	737	9%	18%
UK operations	433	355	355	22%	22%
Total	2,300	2,162	1,974	6%	17%

Post-tax operating profit

	2014 £m	2013 £m		%	
	Half year	AER Half year	CER Half year	AER vs Half year	CER vs Half year
Asia operations					
New business	494	502	429	(2)%	15%
Business in force	339	327	288	4%	18%
Long-term business	833	829	717	–	16%
Eastspring Investments	36	32	29	13%	24%
Development costs	(1)	(2)	(2)	50%	50%
Total	868	859	744	1%	17%
US operations					
New business	376	311	288	21%	31%
Business in force	401	396	366	1%	10%
Long-term business	777	707	654	10%	19%
Broker-dealer and asset management	(5)	21	19	(124)%	(126)%
Total	772	728	673	6%	15%
UK operations					
New business	145	100	100	45%	45%
Business in force	243	204	204	19%	19%
Long-term business	388	304	304	28%	28%
General insurance commission	9	11	11	(18)%	(18)%
Total UK insurance operations	397	315	315	26%	26%
M&G (including Prudential Capital)	200	175	175	14%	14%
Total	597	490	490	22%	22%
Other income and expenditure	(280)	(235)	(235)	(19)%	(19)%
Solvency II and restructuring costs	(14)	(21)	(21)	33%	33%
Post-tax operating profit based on longer-term investment returns	1,943	1,821	1,651	7%	18%

Notes on the EEV basis results continued

2 Results analysis by business area continued

	2014 £m	2013 £m		%	
	Half year	AER Half year	CER Half year	AER vs Half year	CER vs Half year
Analysed as profits (losses) from:					
New business	1,015	913	817	11%	24%
Business in force	983	927	858	6%	15%
Total long-term business	1,998	1,840	1,675	9%	19%
Asset management	231	228	223	1%	4%
Other results	(286)	(247)	(247)	(16)%	(16)%
Post-tax operating profit based on longer-term investment returns	1,943	1,821	1,651	7%	18%

Post-tax profit

	2014 £m	2013 £m		%	
	Half year	AER Half year	CER Half year	AER vs Half year	CER vs Half year
Post-tax operating profit based on longer-term investment returns	1,943	1,821	1,651	7%	18%
Short-term fluctuations in investment returns	432	(587)	(551)	174%	178%
Effect of changes in economic assumptions	(368)	534	527	(169)%	(170)%
Other non-operating profit	(73)	156	161	(147)%	(145)%
Total post-tax non-operating profit	(9)	103	137	(109)%	(107)%
Profit for the period attributable to shareholders	1,934	1,924	1,788	1%	8%

Basic earnings per share (in pence)

	2014	2013		%	
	Half year	AER Half year	CER Half year	AER vs Half year	CER vs Half year
Based on post-tax operating profit including longer-term investment returns	76.3p	71.5p	64.8p	7%	18%
Based on post-tax profit	75.9p	75.5p	70.2p	1%	8%

3 Analysis of new business contribution

(i) Group summary

	Half year 2014				
	Annual premium and contribution equivalents (APE) note 16 £m	Present value of new business premiums (PVNBP) note 16 £m	New business contribution £m	New business margin APE %	New business margin PVNBP %
Asia operations	996	5,378	494	50	9.2
US operations	871	8,703	376	43	4.3
UK insurance operations	433	3,741	145	33	3.9
Total	2,300	17,822	1,015	44	5.7

	Half year 2013				
	Annual premium and contribution equivalents (APE) note 16 £m	Present value of new business premiums (PVNBP) note 16 £m	New business contribution* £m	New business margin* APE %	New business margin* PVNBP %
Asia operations	1,010	5,524	502	50	9.1
US operations	797	7,957	311	39	3.9
UK insurance operations	355	2,943	100	28	3.4
Total	2,162	16,424	913	42	5.6

	Full year 2013				
	Annual premium and contribution equivalents (APE) note 16 £m	Present value of new business premiums (PVNBP) note 16 £m	New business contribution* £m	New business margin* APE %	New business margin* PVNBP %
Asia operations	2,125	11,375	1,139	54	10.0
US operations	1,573	15,723	706	45	4.5
UK insurance operations	725	5,978	237	33	4.0
Total	4,423	33,076	2,082	47	6.3

(ii) Asia operations

	New business contribution			
	2014 £m	2013* £m		
	Half year	AER Half year	CER Half year	Full year
China	13	13	12	28
Hong Kong	152	125	115	283
India	5	8	7	15
Indonesia	136	174	134	359
Korea	8	14	14	25
Taiwan	13	13	12	31
Other	167	155	135	398
Total Asia operations	494	502	429	1,139

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes on the EEV basis results continued

4 Operating profit from business in force

(i) Group summary

	Half year 2014 £m			
	Asia operations note (ii)	US operations note (iii)	UK insurance operations note (iv)	Total
Unwind of discount and other expected returns	328	192	229	749
Effect of changes in operating assumptions	9	–	–	9
Experience variances and other items	2	209	14	225
Total	339	401	243	983

	Half year 2013* £m			
	Asia operations note (ii)	US operations note (iii)	UK insurance operations note (iv)	Total
Unwind of discount and other expected returns	315	187	204	706
Effect of changes in operating assumptions	(6)	45	–	39
Experience variances and other items	18	164	–	182
Total	327	396	204	927

	Full year 2013* £m			
	Asia operations note (ii)	US operations note (iii)	UK insurance operations note (iv)	Total
Unwind of discount and other expected returns	668	395	437	1,500
Effect of changes in operating assumptions	5	76	98	179
Experience variances and other items	80	349	60	489
Total	753	820	595	2,168

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

(ii) Asia operations

	2014 £m	2013* £m	
	Half year	Half year	Full year
Unwind of discount and other expected returns[note (a)]	328	315	668
Effect of changes in operating assumptions:			
Mortality and morbidity[note (b)]	1	3	19
Persistency and withdrawals[note (c)]	–	(5)	(23)
Expense	1	1	(6)
Other	7	(5)	15
	9	(6)	5
Experience variances and other items:			
Mortality and morbidity[note (d)]	18	22	33
Persistency and withdrawals[note (e)]	(3)	(2)	36
Expense[note (f)]	(19)	(9)	(17)
Other	6	7	28
	2	18	80
Total Asia operations	339	327	753

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) The increase in unwind of discount and other expected returns of £13 million from £315 million for half year 2013 to £328 million for half year 2014 is impacted by a £(44) million adverse foreign currency translation effect. The underlying £57 million growth arises from the increase in the opening in-force value of £41 million, the effect of higher risk discount rates of £12 million and an increase in the return on net worth of £4 million.

(b) In full year 2013 the credit of £19 million for mortality and morbidity assumption changes mainly reflected the beneficial effect arising from the renegotiation of a reinsurance agreement in Indonesia.

(c) For full year 2013 the charge of £(23) million for persistency and withdrawals assumption changes reflected a number of offsetting items including the effect of strengthening lapse and premium holiday assumptions in Korea.

(d) The favourable effect of mortality and morbidity experience in half year 2014 of £18 million (half year 2013: £22 million; full year 2013: £33 million) reflects better than expected experience, principally arising in Hong Kong, Indonesia and Singapore.

(e) The negative persistency and withdrawals experience variance in half year 2014 of £(3) million (half year 2013: £(2) million) reflects the net effect of small variances across the territories. For full year 2013 the persistency and withdrawals experience variance of £36 million principally reflected favourable experience in Hong Kong and Indonesia.

(f) The expense experience variance at half year 2014 was negative £(19) million (half year 2013: £(9) million; full year 2013: £(17) million). The variance arose in operations which are currently sub-scale (China, Malaysia Takaful and Taiwan), in India where the business model continues to be adapted following the regulatory changes introduced in recent years, and from other temporary overruns.

(iii) US operations

	2014 £m	**2013*** £m	
	Half year	**Half year**	**Full year**
Unwind of discount and other expected returns note (a)	192	187	395
Effect of changes in operating assumptions:			
Persistency note (b)	–	47	47
Other note (c)	–	(2)	29
	–	45	76
Experience variances and other items:			
Spread experience variance note (d)	108	96	217
Amortisation of interest-related realised gains and losses note (e)	28	30	58
Other note (f)	73	38	74
	209	164	349
Total US operations	401	396	820

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) The increase in unwind of discount and other expected returns of £5 million from £187 million for half year 2013 to £192 million for half year 2014 is impacted by a £(15) million adverse foreign currency translation effect. The underlying growth of £20 million arises from the increase in the opening in-force value £33 million offset by the effect of lower risk discount rates £(9) million and a decrease in the return on net worth £(4) million.

(b) For half year and full year 2013, the effect of changes in persistency assumptions of £47 million primarily related to a reduction in lapse rates following the end of the surrender charge period, for variable annuity business.

(c) Other changes in operating assumptions in 2013 include the effect of changes in mortality assumptions, the capitalised effect of changes in projected policyholder variable annuity fees and the effect of other regular updates to reflect experience.

(d) The spread assumption for Jackson is determined on a longer-term basis, net of provision for defaults (see note 15(ii)(b)). The spread experience variance in half year 2014 of £108 million (half year 2013: £96 million; full year 2013: £217 million) includes the positive effect of transactions undertaken to more closely match the overall asset and liability duration.

(e) The amortisation of interest-related gains and losses reflects the fact that when bonds that are neither impaired nor deteriorating are sold and reinvested there will be a consequent change in the investment yield. The realised gain or loss is amortised into the result over the period when the bonds would have otherwise matured to better reflect the long-term returns included in operating profits.

(f) The credit of £73 million in half year 2014 for other experience variances and other items includes positive impacts for persistency experience of £39 million (half year 2013: £15 million; full year 2013: £40 million) and mortality experience. For all periods, other items also includes the impact of tax experience variances.

Notes on the EEV basis results continued

4 Operating profit from business in force continued

(iv) UK insurance operations

	2014 £m	2013* £m	
	Half year	Half year	Full year
Unwind of discount and other expected returns[note (a)]	229	204	437
Effect of change in UK corporate tax rate[note (b)]	–	–	98
Other items[note (c)]	14	–	60
Total UK insurance operations	243	204	595

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) The increase in unwind of discount and other expected returns of £25 million from £204 million for half year 2013 to £229 million for half year 2014 reflects a £20 million increase in the return on net worth mainly arising from shareholder-backed annuity business, combined with the growth in the opening value of in-force of £7 million, partially offset by the negative effect of a lower risk discount rate of £(2) million.

(b) For full year 2013, the effect of the change in UK corporate tax rates of £98 million reflected the combined effect of the reductions in corporate rates from 23 per cent to 21 per cent from April 2014 and 21 per cent to 20 per cent from April 2015 which were both enacted in July 2013. The beneficial effect arose from the increase in the present value of the post-tax projected cash flows of the in-force business at 1 January 2013.

(c) Other items of £14 million for half year 2014 (full year 2013: £60 million) principally reflect the positive effects of rebalancing the investment portfolio backing annuity business (see note 14(c)(ii)).

5 Loss attaching to held for sale Japan life business

The losses reflected in the 2013 results reflect the reductions in EEV carrying value to equal the expected net proceeds from the sale of the Group's life insurance business in Japan, PCA Life Insurance Company Ltd. when completed.

6 Domestication of the Hong Kong branch business

On 1 January 2014, following consultation with policyholders of PAC and regulators and court approval, the Hong Kong branch of PAC was transferred to separate subsidiaries established in Hong Kong. As a consequence of this restructuring, adjustments in respect of required capital, and the cost of that capital have been recognised in the EEV basis of results. These adjustments arose from the transfer of capital that was previously held within the UK business in respect of the Hong Kong branch operations and additional capital requirements that arise from the newly established subsidiaries. These have been included as an adjustment to opening balances within the movement in net worth and value of in-force business (note 12) and in the statement of movement in shareholders' equity (note 11) in 2014 as follows:

	2014 £m				
Adjustment to shareholders' equity at 1 January 2014	Free surplus	Required capital	Total net worth	Value of in-force business	Total long-term business operations
Asia operations	(104)	104	–	(40)	(40)
UK insurance operations	69	(69)	–	29	29
Opening adjustment	(35)	35	–	(11)	(11)

The net EEV basis effect of £(11) million represents the cost of holding higher required capital levels in the stand-alone Hong Kong shareholder-backed long-term insurance business.

The post-tax costs incurred enabling the domestication in the first half of 2014 were £7 million (full year 2013: £28 million).

7 Short-term fluctuations in investment returns

Short-term fluctuations in investment returns, net of the related change in the time value of cost of options and guarantees, arise as follows:

(i) Group summary

	2014 £m	2013* £m	
	Half year	Half year	Full year
Insurance operations:			
Asia[note (ii)]	245	(223)	(308)
US[note (iii)]	95	(271)	(280)
UK[note (iv)]	112	(70)	28
	452	(564)	(560)
Other operations	(20)	(23)	(4)
Total	432	(587)	(564)

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

(ii) Asia operations

The short-term fluctuations in investment returns for Asia operations comprise amounts in respect of the following business operations:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Hong Kong	121	(122)	(178)
Singapore	46	(106)	(80)
Other	78	5	(50)
Total Asia operations	245	(223)	(308)

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

These fluctuations mainly arise from decreases (2014) and increases (2013) in long-term interest rates as they affect the value of bonds in the portfolios backing liabilities. The £78 million credit for other operations in half year 2014 principally arises in Taiwan of £21 million for unrealised gains on bonds, and in Indonesia of £21 million for an increase in future expected fee income for unit-linked business. For full year 2013 the £(50) million fluctuation included £(44) million arising in Indonesia for a decrease in future expected fee income, arising from falls in equity markets.

(iii) US operations

The short-term fluctuations in investment returns for US operations comprise the following items:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Investment return related experience on fixed income securities[note (a)]	(2)	8	13
Investment return related impact due to changed expectation of profits on in-force variable annuity business in future periods based on current period separate account return, net of related hedging activity[note (b)]	75	(307)	(377)
Other items including actual less long-term return on equity based investments[note (c)]	22	28	84
Total US operations	95	(271)	(280)

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) The (charge) credit relating to fixed income securities comprises the following elements:
- The excess of actual realised gains (losses) over the amortisation of interest-related realised gains and losses recorded in the profit and loss account;
- Credit loss experience (versus the longer-term assumption); and
- The impact of changes in the asset portfolio.

(b) This item reflects the net impact of:
- Variances in projected future fees and future benefit costs arising from the effect of market fluctuations on the growth in separate account asset values in the current reporting period; and
- Related hedging activity arising from realised and unrealised gains and losses on equity related hedges and interest rate options.

(c) For full year 2013, other items of £84 million primarily reflected a beneficial impact of the excess of actual over assumed return from investments in limited partnerships.

Notes on the EEV basis results continued

7 Short-term fluctuations in investment returns continued

(iv) UK insurance operations

The short-term fluctuations in investment returns for UK insurance operations arise from the following types of business:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Shareholder-backed annuity[note (a)]	**35**	(48)	(58)
With-profits, unit-linked and other[note (b)]	**77**	(22)	86
	112	(70)	28

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) Short-term fluctuations in investment returns for shareholder-backed annuity business comprise: (1) gains (losses) on surplus assets compared to the expected long-term rate of return reflecting reductions/increases in corporate bond and gilt yields; (2) the difference between actual and expected default experience; and (3) the effect of mismatching for assets and liabilities of different durations and other short-term fluctuations in investment returns.

(b) The short-term fluctuations in investment returns for with-profits, unit-linked and other business primarily arise from the excess of actual over expected returns for with-profits business. The total return on the fund (including unallocated surplus) in half year 2014 was 4.2 per cent compared to an assumed rate of return of 2.9 per cent (half year 2013: 2.7 per cent total return compared to assumed rate of 2.9 per cent; full year 2013: 8.0 per cent total return compared to assumed rate of 6.0 per cent). In addition, for full year 2013 the amount included the effect of a partial hedge of future shareholder transfers expected to emerge from the UK's with-profits sub-fund taken out during 2013. This hedge reduces the risks arising from equity market declines.

8 Effect of changes in economic assumptions

The effects of changes in economic assumptions for in-force business, net of the related change in the time value of cost of options and guarantees, included within post-tax profit (including actual investment returns) arise as follows:

(i) Group summary

	2014 £m	2013* £m	
	Half year	Half year	Full year
Asia operations[note (ii)]	**(145)**	272	255
US operations[note (iii)]	**(158)**	40	242
UK insurance operations[note (iv)]	**(65)**	222	132
Total	**(368)**	534	629

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

(ii) Asia operations

The effect of changes in economic assumptions for Asia operations comprise amounts in respect of the following business operations:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Hong Kong	**(73)**	288	289
Malaysia	**(31)**	(27)	(62)
Indonesia	**12**	(101)	(176)
Singapore	**(11)**	62	90
Taiwan	**(29)**	52	92
Other	**(13)**	(2)	22
Total Asia operations	**(145)**	272	255

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

The negative effect of £(145) million in half year 2014 principally arises in Hong Kong, Singapore and Taiwan, mainly reflecting reductions in fund earned rates for participating business, driven by the decrease in long-term interest rates.

The positive impacts in half year 2013 of £272 million and full year 2013 of £255 million reflected the overall impact of an increase in fund earned rates for participating business, principally arising in Hong Kong, Singapore and Taiwan, mainly due to the increase in long-term interest rates. There were partial offsets arising in Indonesia and Malaysia, mainly reflecting the negative impact of calculating health and protection future profits at a higher discount rate.

(iii) US operations

The effect of changes in economic assumptions for US operations reflects the following:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Effect of changes in 10-year treasury rates:			
Fixed annuity and other general account business[note (a)]	71	(147)	(244)
Variable annuity business[note (b)]	(229)	187	382
Decrease in additional allowance for credit risk[note (c)]	–	–	104
Total[note (d)]	(158)	40	242

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) For fixed annuity and other general account business the credit of £71 million in half year 2014 principally arises from the effect of a lower discount rate, driven by the 50 basis points reduction in the risk-free rate. The projected cash flows for this business principally reflect projected spread, with secondary effects on the cash flows also resulting from changes to assumed future yields and resulting policyholder behaviour. The charge of £(147) million in half year 2013 (full year 2013: £(244) million) principally arose from the effect of a higher discount rate on the opening value of the in-force book, driven by the 70 basis points increase in the risk-free rate (full year 2013: 130 basis points).

(b) For variable annuity business, the charge of £(229) million principally reflects the decrease in the projected fee income and an increase in projected benefit costs, arising from the decrease in the rate of the assumed future return on the underlying separate account return assets, driven by the 50 basis points decrease in the risk free rate. There is a partial offset arising from the decrease in the risk discount rate applied to those cash flows. The credit of £187 million in half year 2013 and £382 million in full year 2013 reflected an increase in the risk free rate of 70 basis points and 130 basis points respectively.

(c) For full year 2013 the £104 million effect of the decrease in the additional allowance for credit risk within the risk discount rate reflected the reduction in credit spreads and represented a 50 basis points decrease for spread business and a 10 basis points decrease for variable annuity business, representing the proportion of business invested in the general account (as described in note 14(b)(iii)).

(d) The overall credit in half year 2013 of £40 million and in full year 2013 of £242 million included a charge of £(13) million for the effect of the change in required capital from 235 per cent to 250 per cent of risk-based capital.

(iv) UK insurance operations

The effect of changes in economic assumptions of a charge of £(65) million for UK insurance operations for half year 2014 comprises the following:

	2014 £m	2013* £m	
	Half year	Half year	Full year
Effect of changes in expected long-term rates of return, risk discount rates and other changes:			
Shareholder-backed annuity business[note (a)]	73	(106)	(56)
With-profits and other business[note (b)]	(138)	328	188
	(65)	222	132

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the half year and full year 2013 results are shown on a comparable basis – see note 1.

Notes

(a) For shareholder-backed annuity business the overall effect reflects changes in expected long-term rates of return and risk discount rates which incorporate a default allowance for both best estimate defaults and in respect of the additional credit risk provisions (as shown in note 15(iii)(b)).

(b) For with-profits and other business the total charge in half year 2014 of £(138) million (half year 2013: credit of £328 million; full year 2013: credit of £188 million) includes the net effect of the changes in fund earned rates and risk discount rate (as shown in note 15(iii)), driven by the 30 basis points decrease (half year 2013: increase of 70 basis points; full year 2013: increase of 120 basis points) in the 15-year government bond rate.

9 Net core structural borrowings of shareholder-financed operations

	2014 £m			2013 £m					
	30 Jun			30 Jun			31 Dec		
	IFRS basis	Mark to market value adjustment	EEV basis at market value	IFRS basis	Mark to market value adjustment	EEV basis at market value	IFRS basis	Mark to market value adjustment	EEV basis at market value
Holding company* cash and short-term investments	(1,902)	–	(1,902)	(1,490)	–	(1,490)	(2,230)	–	(2,230)
Core structural borrowings – central funds	4,146	452	4,598	3,710	360	4,070	4,211	392	4,603
Holding company net borrowings	2,244	452	2,696	2,220	360	2,580	1,981	392	2,373
Core structural borrowings – Prudential Capital	275	–	275	275	–	275	275	–	275
Core structural borrowings – Jackson	146	41	187	164	25	189	150	38	188
Net core structural borrowings of shareholder-financed operations	2,665	493	3,158	2,659	385	3,044	2,406	430	2,836

* Including central finance subsidiaries.

Notes on the EEV basis results continued

10 Analysis of movement in free surplus

Free surplus is the excess of the regulatory basis net assets for EEV reporting purposes (net worth) over the capital required to support the covered business. Where appropriate, adjustments are made to the net worth so that backing assets are included at fair value rather than cost so as to comply with the EEV principles.

(i) Underlying free surplus generated

The half year 2013 comparative results are shown below on both actual exchange rates (AER) and constant exchange rates (CER) bases. The half year 2013 CER comparative results are translated at half year 2014 average exchange rates.

	2014 £m	2013 £m		%	
	Half year	AER Half year	CER Half year	AER vs Half year	CER vs Half year
Asia operations					
Underlying free surplus generated from in-force life business	**433**	425	371	2%	17%
Investment in new business	**(167)**	(165)	(147)	(1)%	(14)%
Long-term business	**266**	260	224	2%	19%
Eastspring Investments	**36**	32	29	13%	24%
Total	**302**	292	253	3%	19%
US operations					
Underlying free surplus generated from in-force life business	**634**	591	547	7%	16%
Investment in new business	**(173)**	(211)	(195)	18%	11%
Long-term business	**461**	380	352	21%	31%
Broker-dealer and asset management	**(5)**	21	19	(124)%	(126)%
Total	**456**	401	371	14%	23%
UK insurance operations					
Underlying free surplus generated from in-force life business	**294**	293	293	–	–
Investment in new business	**(42)**	(20)	(20)	(110)%	(110)%
Long-term business	**252**	273	273	(8)%	(8)%
General insurance commission	**9**	11	11	(18)%	(18)%
Total	**261**	284	284	(8)%	(8)%
M&G (including Prudential Capital)	**200**	175	175	14%	14%
Underlying free surplus generated	**1,219**	1,152	1,083	6%	13%
Representing:					
Long-term business:					
Underlying free surplus generated from in-force life business	**1,361**	1,309	1,211	4%	12%
Investment in new business	**(382)**	(396)	(362)	4%	(6)%
Total long-term business	**979**	913	849	7%	15%
Asset management	**240**	239	234	–	3%
Underlying free surplus generated	**1,219**	1,152	1,083	6%	13%

(ii) Movement in free surplus

Long-term business and asset management operations	2014 £m Half year Long-term business note 12	2014 £m Half year Asset management and UK general insurance commission note (ii)	2014 £m Half year Free surplus of long-term business, asset management and UK general insurance commission	2013 £m Half year Free surplus of long-term business, asset management and UK general insurance commission
Underlying movement:				
Investment in new business[notes (i), (vii)]	(382)	–	(382)	(396)
Business in force:				
Expected in-force cash flows (including expected return on net assets)	1,174	240	1,414	1,345
Effects of changes in operating assumptions, operating experience variances and other operating items	187	–	187	203
	979	240	1,219	1,152
Increase in EEV assumed level of required capital	–	–	–	(59)
Loss attaching to held for sale Japan life business[note 5]	–	–	–	(56)
Other non-operating items[note (iii)]	(26)	4	(22)	(294)
	953	244	1,197	743
Net cash flows to parent company[note (iv)]	(813)	(161)	(974)	(844)
Bancassurance agreement and purchase of Thanachart Life	–	–	–	365
Exchange movements, timing differences and other items[note (v)]	29	(34)	(5)	191
Net movement in free surplus	169	49	218	455
Balance at beginning of period:				
As previously reported	3,220	783	4,003	3,689
Effect of domestication of Hong Kong branch on 1 January 2014[note 6]	(35)	–	(35)	–
	3,185	783	3,968	3,689
Balance at 30 June 2014/30 June 2013[note (vii)]	3,354	832	4,186	4,144
Representing:				
Asia operations	1,195	192	1,387	1,576
US operations	1,038	125	1,163	1,018
UK operations	1,121	515	1,636	1,550
	3,354	832	4,186	4,144
Balance at beginning of period:				
Asia operations	1,185	194	1,379	1,181
US operations	956	118	1,074	1,319
UK operations	1,079	471	1,550	1,189
	3,220	783	4,003	3,689

Notes

(i) Free surplus invested in new business represents amounts set aside for required capital and acquisition costs.

(ii) For the purposes of this analysis, free surplus for asset management operations and the UK general insurance commission is taken to be IFRS basis shareholders' equity.

(iii) Non-operating items are principally short-term fluctuations in investment returns and the effect of changes in economic assumptions for long-term business operations.

(iv) Net cash flows to parent company for long-term business operations reflect the flows as included in the holding company cash flow at transaction rates.

(v) Exchange movements, timing differences and other items represent:

	Half year 2014 £m Long-term business	Half year 2014 £m Asset management and UK general insurance commission	Half year 2014 £m Total
Exchange movements[note 12]	(53)	(9)	(62)
Mark to market value movements on Jackson assets backing surplus and required capital[note 11]	71	–	71
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	2	6	8
Other[note (vi)]	9	(31)	(22)
	29	(34)	(5)

(vi) Other primarily reflects the effect of timing differences, contingent loan funding, as shown in note 12(i), and other non-cash items.

(vii) Investment in new business includes the annual amortisation charge for amounts incurred to secure exclusive distribution rights through our bancassurance partners at a rate that reflects the pattern in which the future economic benefits are expected to be consumed by reference to new business levels. Included within the overall free surplus balance of our Asian life entities is £293 million representing unamortised amounts incurred to secure exclusive distribution rights through our bancassurance partners. These amounts exclude £818 million of Asia distribution rights intangibles that are financed by loan arrangements from central companies, the costs of which are allocated to the Asia life segment as the amortisation cost is incurred.

Notes on the EEV basis results continued

11 Reconciliation of movement in shareholders' equity

	Half year 2014 £m					
	Long-term business operations					
	Asia operations note (i)	US operations	UK insurance operations	Total long-term business operations	Other operations note (i)	Group Total
Post-tax operating profit (based on longer-term investment returns)						
Long-term business:						
New business[note 3]	494	376	145	1,015	–	1,015
Business in force[note 4]	339	401	243	983	–	983
	833	777	388	1,998	–	1,998
Asset management	–	–	–	–	231	231
Other results	(1)	–	(5)	(6)	(280)	(286)
Post-tax operating profit based on longer-term investment returns	832	777	383	1,992	(49)	1,943
Total post-tax non-operating profit	100	(68)	40	72	(81)	(9)
Profit for the period	932	709	423	2,064	(130)	1,934
Other movements (post-tax)						
Exchange movements on foreign operations and net investment hedges	(209)	(227)	–	(436)	59	(377)
Intra-group dividends (including statutory transfers)[note (ii)]	(239)	(347)	(106)	(692)	692	–
Investment in operations[note (iii)]	3	–	–	3	(3)	–
External dividends	–	–	–	–	(610)	(610)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes[note (v)]	–	–	2	2	8	10
Reserve movements in respect of share-based payments	–	–	–	–	52	52
Other transfers	17	(17)	(36)	(36)	36	–
Treasury shares movements	–	–	–	–	(40)	(40)
New share capital subscribed	–	–	–	–	8	8
Mark to market value movements on Jackson assets backing surplus and required capital	–	71	–	71	–	71
Net increase in shareholders' equity	504	189	283	976	72	1,048
Shareholders' equity at beginning of period:						
As previously reported	10,305	6,966	7,342	24,613	243	24,856
Effect of domestication of Hong Kong branch on 1 January 2014[note 6]	(40)	–	29	(11)	–	(11)
	10,265	6,966	7,371	24,602	243	24,845
Shareholders' equity at 30 June 2014[note (i)]	10,769	7,155	7,654	25,578	315	25,893
Representing:						
Statutory IFRS basis shareholders' equity	2,792	3,801	3,236	9,829	796	10,625
Additional retained profit (loss) on an EEV basis[note (iv)]	7,977	3,354	4,418	15,749	(481)	15,268
EEV basis shareholders' equity	10,769	7,155	7,654	25,578	315	25,893
Balance at 31 December 2013						
Representing:						
Statutory IFRS basis shareholders' equity	2,564	3,446	2,976	8,986	664	9,650
Additional retained profit (loss) on an EEV basis[note (iv)]	7,741	3,520	4,366	15,627	(421)	15,206
EEV basis shareholders' equity	10,305	6,966	7,342	24,613	243	24,856

Notes

(i) For the purposes of the table above, goodwill related to Asia long-term operations is included in Other operations.

(ii) Intra-group dividends (including statutory transfers) represent dividends that have been declared in the period and amounts accrued in respect of statutory transfers. The amounts included in note 10 for these items are as per the holding company cash flow at transaction rates. The difference primarily relates to intra-group loans, timing differences arising on statutory transfers, and other non-cash items.

(iii) Investment in operations reflects increases in share capital.

(iv) The additional retained loss on an EEV basis for Other operations primarily represents the mark to market value adjustment for holding company net borrowings of a charge of £(452) million (half year 2013: £(360) million; full year 2013: £(392) million), as shown in note 9.

(v) The post-tax charge for the shareholders' share of actuarial and other gains and losses on defined benefit schemes comprises:

	2014 £m	**2013** £m	
	Half year	**Half year**	**Full year**
IFRS basis	10	(21)	(48)
Additional shareholders' interest[note 14(c)(vii)]	–	(5)	(5)
EEV basis total	10	(26)	(53)

Notes on the EEV basis results continued

12 Reconciliation of movement in net worth and value of in-force for long-term business

	Half year 2014 £m				
	Free surplus note 10	**Required capital**	**Total net worth**	**Value of in-force business** note (iv)	**Total long-term business operations** note 11
Group					
Shareholders' equity at beginning of period:					
As previously reported	3,220	3,954	7,174	17,439	24,613
Effect of domestication of Hong Kong branch on 1 January 2014[note 6]	(35)	35	–	(11)	(11)
	3,185	3,989	7,174	17,428	24,602
New business contribution[notes (ii), (iii) and 3]	(382)	276	(106)	1,121	1,015
Existing business – transfer to net worth	1,116	(175)	941	(941)	–
Expected return on existing business[note 4]	58	44	102	647	749
Changes in operating assumptions and experience variances[note 4]	193	(20)	173	61	234
Development expenses, Solvency II and restructuring costs	(6)	–	(6)	–	(6)
Post-tax operating profit based on longer-term investment returns	979	125	1,104	888	1,992
Other non-operating items	(26)	59	33	39	72
Post-tax profit from long-term business	953	184	1,137	927	2,064
Exchange movements on foreign operations and net investment hedges	(53)	(74)	(127)	(309)	(436)
Intra-group dividends (including statutory transfers) and investment in operations[note (i)]	(768)	–	(768)	79	(689)
Other movements	37	–	37	–	37
Shareholders' equity at 30 June 2014	3,354	4,099	7,453	18,125	25,578
Representing:					
Asia operations					
Shareholders' equity at beginning of period:					
As previously reported	1,185	977	2,162	8,143	10,305
Effect of domestication of Hong Kong branch on 1 January 2014[note 6]	(104)	104	–	(40)	(40)
	1,081	1,081	2,162	8,103	10,265
New business contribution[notes (iii) and 3]	(167)	67	(100)	594	494
Existing business – transfer to net worth	395	(5)	390	(390)	–
Expected return on existing business[note 4]	34	–	34	294	328
Changes in operating assumptions and experience variances[note 4]	5	(14)	(9)	20	11
Development expenses, Solvency II and restructuring costs	(1)	–	(1)	–	(1)
Post-tax operating profit based on longer-term investment returns	266	48	314	518	832
Other non-operating items	112	(9)	103	(3)	100
Post-tax profit from long-term business	378	39	417	515	932
Exchange movements on foreign operations and net investment hedges	(21)	(22)	(43)	(166)	(209)
Intra-group dividends (including statutory transfers) and investment in operations	(236)	–	(236)	–	(236)
Other movements	(7)	–	(7)	24	17
Shareholders' equity at 30 June 2014	1,195	1,098	2,293	8,476	10,769
US operations					
Shareholders' equity at 1 January 2014	956	1,607	2,563	4,403	6,966
New business contribution[notes (iii) and 3]	(173)	146	(27)	403	376
Existing business – transfer to net worth	450	(124)	326	(326)	–
Expected return on existing business[note 4]	15	25	40	152	192
Changes in operating assumptions and experience variances[note 4]	169	(11)	158	51	209
Post-tax operating profit based on longer-term investment returns	461	36	497	280	777
Other non-operating items	(54)	36	(18)	(50)	(68)
Post-tax profit from long-term business	407	72	479	230	709
Exchange movements on foreign operations and net investment hedges	(32)	(52)	(84)	(143)	(227)
Intra-group dividends (including statutory transfers)	(347)	–	(347)	–	(347)
Other movements	54	–	54	–	54
Shareholders' equity at 30 June 2014	1,038	1,627	2,665	4,490	7,155

	Half year 2014 £m				
	Free surplus note 10	Required capital	Total net worth	Value of in-force business note (iv)	Total long-term business operations note 11
UK insurance operations					
Shareholders' equity at beginning of period:					
As previously reported	1,079	1,370	2,449	4,893	7,342
Effect of domestication of Hong Kong branch on 1 January 2014 note 6	69	(69)	–	29	29
	1,148	1,301	2,449	4,922	7,371
New business contribution notes (iii) and 3	(42)	63	21	124	145
Existing business – transfer to net worth	271	(46)	225	(225)	–
Expected return on existing business note 4	9	19	28	201	229
Changes in operating assumptions and experience variances note 4	19	5	24	(10)	14
Development expenses, Solvency II and restructuring costs	(5)	–	(5)	–	(5)
Post-tax operating profit based on longer-term investment returns	252	41	293	90	383
Other non-operating items	(84)	32	(52)	92	40
Post-tax profit from long-term business	168	73	241	182	423
Intra-group dividends (including statutory transfers) note (i)	(185)	–	(185)	79	(106)
Other movements	(10)	–	(10)	(24)	(34)
Shareholders' equity at 30 June 2014	1,121	1,374	2,495	5,159	7,654

Notes

(i) The amounts shown in respect of free surplus and the value of in-force business for UK insurance operations for intra-group dividends (including statutory transfers) include the repayment of contingent loan funding. Contingent loan funding represents amounts whose repayment to the lender is contingent upon future surpluses emerging from certain contracts specified under the arrangement. If insufficient surplus emerges on those contracts, there is no recourse to other assets of the Group and the liability is not payable to the degree of shortfall.

(ii) The movements arising from new business contribution are as follows:

	2014 £m	2013 £m	
	Half year	Half year	Full year
Free surplus invested in new business	(382)	(396)	(637)
Increase in required capital	276	261	461
Reduction in total net worth	(106)	(135)	(176)
Increase in the value associated with new business	1,121	1,048	2,258
Total post-tax new business contribution note 3	1,015	913	2,082

(iii) New business contribution per £1 million of free surplus invested:

	Half year 2014 £m			
	Asia operations	US operations	UK insurance operations	Total long-term business operations
Post-tax new business contribution note 3	494	376	145	1,015
Free surplus invested in new business	(167)	(173)	(42)	(382)
Post-tax new business contribution per £1 million of free surplus invested	3.0	2.2	3.5	2.7

Notes on the EEV basis results continued

12 Reconciliation of movement in net worth and value of in-force for long-term business continued

	Half year 2013 £m			
	Asia operations	**US operations**	**UK insurance operations**	**Total long-term business operations**
Post-tax new business contribution[note 3]	502	311	100	913
Free surplus invested in new business	(165)	(211)	(20)	(396)
Post-tax new business contribution per £1 million of free surplus invested	3.0	1.5	5.0	2.3

	Full year 2013 £m			
	Asia operations	**US operations**	**UK insurance operations**	**Total long-term business operations**
Post-tax new business contribution[note 3]	1,139	706	237	2,082
Free surplus invested in new business	(310)	(298)	(29)	(637)
Post-tax new business contribution per £1 million of free surplus invested	3.7	2.4	8.2	3.3

(iv) The value of in-force business comprises the value of future margins from current in-force business less the cost of holding required capital as shown below:

	30 Jun 2014 £m			
	Asia operations	**US operations**	**UK insurance operations**	**Total long-term business operations**
Value of in-force business before deduction of cost of capital and time value of guarantees	8,936	4,960	5,413	19,309
Cost of capital	(404)	(197)	(254)	(855)
Cost of time value of guarantees[note (v)]	(56)	(273)	–	(329)
Net value of in-force business	8,476	4,490	5,159	18,125

	30 Jun 2013 £m			
	Asia operations	**US operations**	**UK insurance operations**	**Total long-term business operations**
Value of in-force business before deduction of cost of capital and time value of guarantees	8,921	4,632	4,932	18,485
Cost of capital	(384)	(223)	(259)	(866)
Cost of time value of guarantees	(24)	(481)	–	(505)
Net value of in-force business	8,513	3,928	4,673	17,114

	31 Dec 2013 £m			
	Asia operations	**US operations**	**UK insurance operations**	**Total long-term business operations**
Value of in-force business before deduction of cost of capital and time value of guarantees	8,540	4,769	5,135	18,444
Cost of capital	(347)	(220)	(242)	(809)
Cost of time value of guarantees[note (v)]	(50)	(146)	–	(196)
Net value of in-force business	8,143	4,403	4,893	17,439

(v) The increase in the cost of time value of guarantees for US operations from £(146) million at full year 2013 to £(273) million at half year 2014 primarily relates to variable annuity business. It mainly arises from the decrease in the expected long-term separate account rate of return following the 50 basis points decline in the US 10-year treasury bond rate and the impact from new business written in the period, partly offset by the strong equity performance.

13 Sensitivity of results to alternative assumptions

Sensitivity analysis – economic assumptions

The tables below show the sensitivity of the embedded value as at 30 June 2014 (31 December 2013) and the new business contribution after the effect of required capital for half year 2014 and full year 2013 to:

- 1 per cent increase in the discount rates;
- 1 per cent increase and decrease in interest rates, including all consequential changes (assumed investment returns for all asset classes, market values of fixed interest assets, risk discount rates);
- 1 per cent rise in equity and property yields;
- 10 per cent fall in market value of equity and property assets (embedded value only);
- The statutory minimum capital level (by contrast to EEV basis required capital), (for embedded value only);
- 5 basis point increase in UK long-term expected defaults; and
- 10 basis point increase in the liquidity premium for UK annuities.

In each sensitivity calculation, all other assumptions remain unchanged except where they are directly affected by the revised economic conditions.

New business contribution

	Half year 2014 £m				Full year 2013* £m			
	Asia operations	US operations	UK insurance operations	Total long-term business operations	Asia operations	US operations	UK insurance operations	Total long-term business operations
Post-tax new business contributionnote 3	494	376	145	1,015	1,139	706	237	2,082
Discount rates – 1% increase	(72)	(14)	(19)	(105)	(148)	(34)	(29)	(211)
Interest rates – 1% increase	5	35	(3)	37	23	47	(1)	69
Interest rates – 1% decrease	(25)	(52)	3	(74)	(55)	(69)	–	(124)
Equity/property yields – 1% rise	20	39	5	64	45	63	10	118
Long-term expected defaults – 5 bps increase	–	–	(6)	(6)	–	–	(6)	(6)
Liquidity premium – 10 bps increase	–	–	12	12	–	–	12	12

* The 2014 EEV results of the Group are presented on a post-tax basis and, accordingly, the full year 2013 results are shown on a comparable basis - see note 1.

Embedded value of long-term business operations

	30 Jun 2014 £m				31 Dec 2013 £m			
	Asia operations	US operations	UK insurance operations	Total long-term business operations	Asia operations	US operations	UK insurance operations	Total long-term business operations
Shareholders' equitynote 11	10,769	7,155	7,654	25,578	10,305	6,966	7,342	24,613
Discount rates – 1% increase	(1,026)	(243)	(555)	(1,824)	(992)	(266)	(529)	(1,787)
Interest rates – 1% increase	(344)	38	(328)	(634)	(297)	(65)	(380)	(742)
Interest rates – 1% decrease	220	(70)	418	568	200	(12)	443	631
Equity/property yields – 1% rise	384	283	240	907	370	250	210	830
Equity/property market values – 10% fall	(187)	(157)	(284)	(628)	(183)	(90)	(238)	(511)
Statutory minimum capital	92	140	4	236	109	153	4	266
Long-term expected defaults – 5 bps increase	–	–	(116)	(116)	–	–	(114)	(114)
Liquidity premium – 10 bps increase	–	–	232	232	–	–	228	228

The sensitivities shown above are for the impact of instantaneous changes on the embedded value of long-term business operations and include the combined effect on the value of in-force business and net assets at the balance sheet dates indicated. If the change in assumption shown in the sensitivities were to occur, then the effect shown above would be recorded within two components of the profit analysis for the following year. These are for the effect of economic assumption changes and, to the extent that asset value changes are included in the sensitivities, within short-term fluctuations in investment returns. In addition to the sensitivity effects shown above, the other components of the profit for the following period would be calculated by reference to the altered assumptions, for example new business contribution and unwind of discount, together with the effect of other changes such as altered corporate bond spreads. In addition for Jackson, the fair value movements on assets backing surplus and required capital which are taken directly to shareholders' equity would also be affected by changes in interest rates.

Notes on the EEV basis results continued

14 Methodology and accounting presentation

(a) Covered business

The EEV results for the Group are prepared for 'covered business', as defined by the EEV Principles. Covered business represents the Group's long-term insurance business for which the value of new and in-force contracts is attributable to shareholders. The post-tax EEV basis results for the Group's covered business are then combined with the post-tax IFRS basis results of the Group's other operations. Under the EEV Principles, the results for covered business incorporate the projected margins of attaching internal asset management, as described in note 14(c)(vi).

The definition of long-term business operations is consistent with previous practice and comprises those contracts falling under the definition for regulatory purposes together with, for US operations, contracts that are in substance the same as guaranteed investment contracts (GICs) but do not fall within the technical definition.

Covered business comprises the Group's long-term business operations, with two exceptions:

- The closed Scottish Amicable Insurance Fund (SAIF) which is excluded from covered business. SAIF is a ring-fenced sub-fund of the Prudential Assurance Company (PAC) long-term fund, established by a Court approved Scheme of Arrangement in October 1997. SAIF is closed to new business and the assets and liabilities of the fund are wholly attributable to the policyholders of the fund; and
- The presentational treatment of the Group's principal defined benefit pension scheme, the Prudential Staff Pension Scheme (PSPS). The partial recognition of the surplus for PSPS is recognised in 'Other' operations, as described in note 14(c)(vii).

A small amount of UK group pensions business is also not modelled for EEV reporting purposes.

(b) Methodology

(i) Embedded value

Overview

The embedded value is the present value of the shareholders' interest in the earnings distributable from assets allocated to covered business after sufficient allowance has been made for the aggregate risks in that business. The shareholders' interest in the Group's long-term business comprises:

- The present value of future shareholder cash flows from in-force covered business (value of in-force business), less deductions for:
  - the cost of locked-in required capital; and
  - the time value of cost of options and guarantees;
- Locked-in required capital; and
- The shareholders' net worth in excess of required capital (free surplus).

The value of future new business is excluded from the embedded value.

Notwithstanding the basis of presentation of results (as explained in note 14(c)(iv)) no smoothing of market or account balance values, unrealised gains or investment return is applied in determining the embedded value or profit. Separately, the analysis of profit is delineated between operating profit based on longer-term investment returns and other constituent items (as explained in note 14(c)(i)).

Valuation of in-force and new business

The embedded value results are prepared incorporating best estimate assumptions about all relevant factors including levels of future investment returns, expenses, persistency and mortality. These assumptions are used to project future cash flows. The present value of the future cash flows is then calculated using a discount rate which reflects both the time value of money and the non-diversifiable risks associated with the cash flows that are not otherwise allowed for.

Best estimate assumptions

Best estimate assumptions are used for the cash flow projections, where best estimate is defined as the mean of the distribution of future possible outcomes. The assumptions are reviewed actively and changes are made when evidence exists that material changes in future experience are reasonably certain.

Assumptions required in the calculation of the value of options and guarantees, for example relating to volatilities and correlations, or dynamic algorithms linking liabilities to assets, have been set equal to the best estimates and, wherever material and practical, reflect any dynamic relationships between the assumptions and the stochastic variables.

Demographic assumptions

Persistency, mortality and morbidity assumptions are based on an analysis of recent experience but also reflect expected future experience. Where relevant, when calculating the time value of financial options and guarantees, policyholder withdrawal rates vary in line with the emerging investment conditions according to management's expectations.

Expense assumptions
Expense levels, including those of service companies that support the Group's long-term business operations, are based on internal expense analysis investigations and are appropriately allocated to acquisition of new business and renewal of in-force business. Exceptional expenses are identified and reported separately. For mature business, it is Prudential's policy not to take credit for future cost reduction programmes until the savings have been delivered. For businesses which are currently sub-scale (China, Malaysia Takaful and Taiwan) and India (where the business model is being adapted as the industry continues to adjust to regulatory changes), expense overruns are reported where these are expected to be short-lived.

For Asia operations, the expenses comprise costs borne directly and recharged costs from the Asia regional head office, that are attributable to covered business. The assumed future expenses for these operations also include projections of these future recharges. Development expenses are charged as incurred.

Corporate expenditure which is included in other income and expenditure and comprises:

- Expenditure for Group head office, to the extent not allocated to the PAC with-profits funds, together with Solvency II implementation and restructuring costs, which are charged to the EEV basis results as incurred; and
- Expenditure of the Asia regional head office that is not allocated to the covered business or asset management operations which is charged as incurred. These costs are primarily for corporate related activities and are included within corporate expenditure.

Principal economic assumptions
The EEV basis results for the Group's operations have been determined using economic assumptions where the pre-tax long-term expected rates of return on investments and risk discount rates are set by reference to period end rates of return on government bonds.

Expected returns on equity and property asset classes and corporate bonds are derived by adding a risk premium, based on the Group's long-term view, to the risk-free rate.

The total profit that emerges over the lifetime of an individual contract as calculated using the embedded value basis is the same as that calculated under the IFRS basis. Since the embedded value basis reflects discounted future cash flows, under this methodology the profit emergence is advanced, thus more closely aligning the timing of the recognition of profits with the efforts and risks of current management actions, particularly with regard to business sold during the period.

New business
In determining the EEV basis value of new business, premiums are included in projected cash flows on the same basis of distinguishing annual and single premium business as set out for statutory basis reporting.

New business premiums reflect those premiums attaching to covered business, including premiums for contracts classified as investment products for IFRS basis reporting. New business premiums for regular premium products are shown on an annualised basis. Internal vesting business is classified as new business where the contracts include an open market option.

The post-tax contribution from new business represents profits determined by applying operating assumptions as at the end of the period.

For UK immediate annuity business and single premium Universal Life products in Asia, primarily in Singapore, the new business contribution is determined by applying economic assumptions reflecting point-of-sale market conditions. This is consistent with how the business is priced as crediting rates are linked to yields on specific assets and the yield is locked-in when the assets are purchased at the point-of-sale of the policy. For other business within the Group, end of period economic assumptions are used.

New business profitability is a key metric for the Group's management of the development of the business. In addition, post-tax new business margins are shown by reference to annual premium equivalents (APE) and the present value of new business premiums (PVNBP). These margins are calculated as the percentage of the value of new business profit to APE and PVNBP. APE is calculated as the aggregate of regular new business amounts and one-tenth of single new business amounts. PVNBP is calculated as equalling single premiums plus the present value of expected premiums of new regular premium business, allowing for lapses and other assumptions made in determining the EEV new business contribution.

Valuation movements on investments
With the exception of debt securities held by Jackson, investment gains and losses during the period (to the extent that changes in capital values do not directly match changes in liabilities) are included directly in the profit for the period and shareholders' equity as they arise.

The results for any covered business conceptually reflect the aggregate of the IFRS results and the movements on the additional shareholders' interest recognised on the EEV basis. Thus the start point for the calculation of the EEV results for Jackson, as for other businesses, reflects the market value movements recognised on the IFRS basis.

However, in determining the movements on the additional shareholders' interest, the basis for calculating the Jackson EEV result acknowledges that, for debt securities backing liabilities, the aggregate EEV results reflect the fact that the value of in-force business instead incorporates the discounted value of future spread earnings. This value is not affected generally by short-term market movements on securities that broadly speaking, are held for the longer term.

Fixed income securities backing the free surplus and required capital for Jackson are accounted for at fair value. However, consistent with the treatment applied under IFRS for Jackson securities classified as available-for-sale, movements in unrealised appreciation on these securities are accounted for in equity rather than in the income statement, as shown in the movement in shareholders' equity.

Notes on the EEV basis results continued

14 Methodology and accounting presentation continued

Cost of capital

A charge is deducted from the embedded value for the cost of capital supporting the Group's long-term business. This capital is referred to as required capital. The cost is the difference between the nominal value of the capital and the discounted value of the projected releases of this capital allowing for investment earnings (post-tax) on the capital.

The annual result is affected by the movement in this cost from year-to-year which comprises a charge against new business profit and generally a release in respect of the reduction in capital requirements for business in force as this runs off.

Where required capital is held within a with-profits long-term fund, the value placed on surplus assets in the fund is already discounted to reflect its release over time and no further adjustment is necessary in respect of required capital.

Financial options and guarantees

Nature of financial options and guarantees in Prudential's long-term business

Asia operations

Subject to local market circumstances and regulatory requirements, the guarantee features described below in respect of UK business broadly apply to similar types of participating contracts principally written in the Hong Kong, Singapore and Malaysia. Participating products have both guaranteed and non-guaranteed elements.

There are also various non-participating long-term products with guarantees. The principal guarantees are those for whole of life contracts with floor levels of policyholder benefits that accrue at rates set at inception and do not vary subsequently with market conditions.

US operations (Jackson)

The principal financial options and guarantees in Jackson are associated with the fixed annuity and variable annuity (VA) lines of business.

Fixed annuities provide that, at Jackson's discretion, it may reset the interest rate credited to policyholders' accounts, subject to a guaranteed minimum. The guaranteed minimum return varies from 1.0 per cent to 5.5 per cent for all periods throughout these results, depending on the particular product, jurisdiction where issued, and date of issue. For half year 2014, 86 per cent (half year and full year 2013: 86 per cent) of the account values on fixed annuities are for policies with guarantees of 3 per cent or less. The average guarantee rate is 2.8 per cent for all periods throughout these results.

Fixed annuities also present a risk that policyholders will exercise their option to surrender their contracts in periods of rapidly rising interest rates, possibly requiring Jackson to liquidate assets at an inopportune time.

Jackson issues VA contracts where it contractually guarantees to the contract holder either: a) return of no less than total deposits made to the contract adjusted for any partial withdrawals; b) total deposits made to the contract adjusted for any partial withdrawals plus a minimum return; or c) the highest contract value on a specified anniversary date adjusted for any withdrawals following the specified contract anniversary. These guarantees include benefits that are payable at specified dates during the accumulation period (Guaranteed Minimum Withdrawal Benefit (GMWB)), as death benefits (Guaranteed Minimum Death Benefits (GMDB)) or as income benefits (Guaranteed Minimum Income Benefits (GMIB)). These guarantees generally protect the policyholder's value in the event of poor equity market performance. Jackson hedges the GMDB and GMWB guarantees through the use of equity options and futures contracts, and fully reinsures the GMIB guarantees.

Jackson also issues fixed index annuities that enable policyholders to obtain a portion of an equity-linked return while providing a guaranteed minimum return. The guaranteed minimum returns would be of a similar nature to those described above for fixed annuities.

UK insurance operations

For covered business the only significant financial options and guarantees in the UK insurance operations arise in the with-profits fund.

With-profits products provide returns to policyholders through bonuses that are smoothed. There are two types of bonuses – annual and final. Annual bonuses are declared once a year and, once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, final bonuses are guaranteed only until the next bonus declaration. The with-profits fund also held a provision on the Pillar I Peak 2 basis of £36 million at 30 June 2014 (30 June 2013: £47 million; 31 December 2013: £36 million) to honour guarantees on a small number of guaranteed annuity option products.

The only material guaranteed surrender values relate to investments in the PruFund range of with-profits funds. For these products the policyholder can choose to pay an additional management charge. In return, at the selected guarantee date, the fund will be increased if necessary to a guaranteed minimum value (based on the initial investment adjusted for any prior withdrawals). The with-profits fund held a reserve of £30 million at 30 June 2014 (30 June 2013: £52 million; 31 December 2013: £36 million) in respect of this guarantee.

The Group's main exposure to guaranteed annuity options in the UK is through the non-covered business of SAIF. A provision on the Pillar I Peak 2 basis of £421 million was held in SAIF at 30 June 2014 (30 June 2013: £325 million; 31 December 2013: £328 million) to honour the guarantees. As described in note 14(a) above, the assets and liabilities are wholly attributable to the policyholders of the fund. Therefore the movement in the provision has no direct impact on shareholders.

Time value

The value of financial options and guarantees comprises two parts. One is given by a deterministic valuation on best estimate assumptions (the intrinsic value). The other part arises from the variability of economic outcomes in the future (the time value).

Where appropriate, a full stochastic valuation has been undertaken to determine the time value of the financial options and guarantees.

The economic assumptions used for the stochastic calculations are consistent with those used for the deterministic calculations. Assumptions specific to the stochastic calculations reflect local market conditions and are based on a combination of actual market data, historic market data and an assessment of long-term economic conditions. Common principles have been adopted across the Group for the stochastic asset models, for example, separate modelling of individual asset classes but with an allowance for correlation between the various asset classes. Details of the key characteristics of each model are given in notes 15(iv), (v) and (vi).

In deriving the time value of financial options and guarantees, management actions in response to emerging investment and fund solvency conditions have been modelled. Management actions encompass, but are not confined to investment allocation decisions, levels of reversionary and terminal bonuses and credited rates. Bonus rates are projected from current levels and varied in accordance with assumed management actions applying in the emerging investment and fund solvency conditions.

In all instances, the modelled actions are in accordance with approved local practice and therefore reflect the options actually available to management. For the PAC with-profits fund, the actions assumed are consistent with those set out in the Principles and Practices of Financial Management which explains how regular and final bonus rates within the discretionary framework are determined, subject to the general legislative requirements applicable.

(ii) Level of required capital

In adopting the EEV Principles, Prudential has based required capital on its internal targets subject to it being at least the local statutory minimum requirements. For with-profits business written in a segregated life fund, as is the case in Asia and the UK, the capital available in the fund is sufficient to meet the required capital requirements. For shareholder-backed business the following capital requirements apply:

- Asia operations: the level of required capital has been set to an amount at least equal to the higher of local statutory requirements and the internal target;
- US operations: the level of required capital has been set at 250 per cent of the risk-based capital required by the National Association of Insurance Commissioners (NAIC) at the Company Action Level (CAL); and
- UK insurance operations: the capital requirements are set to an amount at least equal to the higher of Pillar I and Pillar II requirements for shareholder-backed business of UK insurance operations as a whole.

(iii) Allowance for risk and risk discount rates

Overview

Under the EEV Principles, discount rates used to determine the present value of future cash flows are set by reference to risk-free rates plus a risk margin. The risk margin should reflect any non-diversifiable risk associated with the emergence of distributable earnings that is not allowed for elsewhere in the valuation. Prudential has selected a granular approach to better reflect differences in market risk inherent in each product group. The risk discount rate so derived does not reflect an overall Group market beta but instead reflects the expected volatility associated with the cash flows for each product category in the embedded value model.

Since financial options and guarantees are explicitly valued under the EEV methodology, discount rates under EEV are set excluding the effect of these product features.

The risk margin represents the aggregate of the allowance for market risk, additional allowance for credit risk where appropriate, and allowance for non-diversifiable non-market risk. No allowance is required for non-market risks where these are assumed to be fully diversifiable.

Market risk allowance

The allowance for market risk represents the beta multiplied by an equity risk premium. Except for UK shareholder-backed annuity business (as explained below) such an approach has been used for all of the Group's businesses.

The beta of a portfolio or product measures its relative market risk. The risk discount rates reflect the market risk inherent in each product group and hence the volatility of product cash flows. These are determined by considering how the profits from each product are affected by changes in expected returns on various asset classes. By converting this into a relative rate of return it is possible to derive a product specific beta.

Product level betas reflect the most recent product mix to produce appropriate betas and risk discount rates for each major product grouping.

Notes on the EEV basis results continued

14 Methodology and accounting presentation continued

Additional credit risk allowance

The Group's methodology is to allow appropriately for credit risk. The allowance for total credit risk is to cover:

— Expected long-term defaults;
— Credit risk premium (to reflect the volatility in downgrade and default levels); and
— Short-term downgrades and defaults.

These allowances are initially reflected in determining best estimate returns and through the market risk allowance described above. However, for those businesses which are largely backed by holdings of debt securities these allowances in the projected returns and market risk allowances may not be sufficient and an additional allowance may be appropriate.

The practical application of the allowance for credit risk varies depending upon the type of business as described below.

Asia operations

For Asia operations, the allowance for credit risk incorporated in the projected rates of return and the market risk allowance are sufficient. Accordingly no additional allowance for credit risk is required.

The projected rates of return for holdings of corporate bonds comprise the risk-free rate plus an assessment of long-term spread over the risk-free rate.

US operations (Jackson)

For Jackson business, the allowance for long-term defaults is reflected in the risk margin reserve (RMR) charge which is deducted in determining the projected spread margin between the earned rate on the investments and the policyholder crediting rate.

The risk discount rate incorporates an additional allowance for credit risk premium and short-term downgrades and defaults as shown in note 15(ii). In determining this allowance a number of factors have been considered. These factors, in particular, include:

— How much of the credit spread on debt securities represents an increased credit risk not reflected in the RMR long-term default assumptions, and how much is liquidity premium (which is the premium required by investors to compensate for the risk of longer-term investments which cannot be easily converted into cash, and converted at the fair market value). In assessing this effect, consideration has been given to a number of approaches to estimating the liquidity premium by considering recent statistical data; and
— Policyholder benefits for Jackson fixed annuity business are not fixed. It is possible in adverse economic scenarios to pass on a component of credit losses to policyholders (subject to guarantee features) through lower investment return rates credited to policyholders. Consequently, it is only necessary to allow for the balance of the credit risk in the risk discount rate.

The level of the additional allowance is assessed at each reporting period to take account of prevailing credit conditions and as the business in force alters over time. The additional allowance for variable annuity business has been set at one-fifth of the non-variable annuity business to reflect the proportion of the allocated holdings of general account debt securities.

The level of allowance differs from that for UK annuity business for investment portfolio differences and to take account of the management actions available in adverse economic scenarios to reduce crediting rates to policyholders, subject to guarantee features of the products.

UK operations

(1) Shareholder-backed annuity business

For Prudential's UK shareholder-backed annuity business, Prudential has used a market consistent embedded value (MCEV) approach to derive an implied risk discount rate which is then applied to the projected best estimate cash flows.

In the annuity MCEV calculations as the assets are generally held to maturity to match long duration liabilities, the future cash flows are discounted using the swap yield curve plus an allowance for liquidity premium based on Prudential's assessment of the expected return on the assets backing the annuity liabilities after allowing for:

— Expected long-term defaults derived as a percentage of historical default experience based on Moody's data for the period 1970 to 2009 and the definition of the credit rating assigned to each asset held is the second highest credit rating published by Moody's, Standard & Poor's and Fitch;
— A credit risk premium, which is derived as the excess over the expected long-term defaults, of the 95th percentile of historical cumulative defaults based on Moody's data for the period 1970 to 2009, and subject to a minimum margin over expected long-term defaults of 50 per cent;
— An allowance for a 1 notch downgrade of the asset portfolio subject to credit risk; and
— An allowance for short-term downgrades and defaults.

For the purposes of presentation in the EEV results, the results on this basis are reconfigured. Under this approach the projected earned rate of return on the debt securities held is determined after allowing for expected long-term defaults and, where necessary, an additional allowance for an element of short-term downgrades and defaults to bring the allowance in the earned rate up to best estimate levels. The allowances for credit risk premium, 1 notch downgrade and the remaining element of short-term downgrade and default allowances are incorporated into the risk margin included in the discount rate, as shown in note 15(iii)(b).

(2) With-profits fund non-profit annuity business
For UK non-profit annuity business including that written by Prudential Annuities Limited (PAL) the basis for determining the aggregate allowance for credit risk is consistent with that applied for UK shareholder-backed annuity business (as described above). The allowance for credit risk in PAL is taken into account in determining the projected cash flows to the with-profits fund, which are in turn discounted at the risk discount rate applicable to all of the projected cash flows of the fund.

(3) With-profits fund holdings of debt securities
The UK with-profits fund holds debt securities as part of its investment portfolio backing policyholder liabilities and unallocated surplus. The assumed earned rate for with-profit holdings of corporate bonds is defined as the risk-free rate plus an assessment of the long-term spread over gilts, net of expected long-term defaults. This approach is similar to that applied for equities and properties for which the projected earned rate is defined as the risk-free rate plus a long-term risk premium.

Allowance for non-diversifiable non-market risks
The majority of non-market and non-credit risks are considered to be diversifiable. Finance theory cannot be used to determine the appropriate component of beta for non-diversifiable non-market risks since there is no observable risk premium associated with it that is akin to the equity risk premium. Recognising this, a pragmatic approach has been applied.

A base level allowance of 50 basis points is applied to cover the non-diversifiable non-market risks associated with the Group's businesses. For the Group's US business and UK business other than shareholder-backed annuity, no additional allowance is necessary. For UK shareholder-backed annuity business a further allowance of 50 basis points is used to reflect the longevity risk which is of particular relevance. For the Group's Asia operations in China, India, Indonesia, the Philippines, Taiwan, Thailand and Vietnam, additional allowances are applied for emerging market risk ranging from 100 to 250 basis points.

(iv) With-profits business and the treatment of the estate
The proportion of surplus allocated to shareholders from the PAC with-profits fund has been based on the present level of 10 per cent. The value attributed to the shareholders' interest in the estate is derived by increasing final bonus rates (and related shareholder transfers) so as to exhaust the estate over the lifetime of the in-force with-profits business. In any scenarios where the total assets of the life fund are insufficient to meet policyholder claims in full, the excess cost is fully attributed to shareholders. Similar principles apply, where appropriate, for other with-profits funds of the Group's Asia operations.

(v) Debt capital
Core structural debt liabilities are carried at market value. As the liabilities are generally held to maturity or for the long-term, no deferred tax asset or liability has been established on the difference, compared to the IFRS carrying value. Accordingly, no deferred tax credit or charge is recorded in the results for the reporting period in respect of the mark to market value adjustment.

(vi) Foreign currency translation
Foreign currency profits and losses have been translated at average exchange rates for the period. Foreign currency assets and liabilities have been translated at period end rates of exchange. The principal exchange rates are shown in note A1 of the IFRS statements.

(c) Accounting presentation

(i) Analysis of post-tax profit
To the extent applicable, the presentation of the EEV post-tax profit for the period is consistent in the classification between operating and non-operating results with the basis that the Group applies for the analysis of IFRS basis results. Operating results reflect underlying results including longer-term investment returns (which are determined as described in note 14(c)(ii) below) and incorporate the following:

— New business contribution, as defined in note 14(b)(i);
— Unwind of discount on the value of in-force business and other expected returns, as described in note 14(c)(iv) below;
— The impact of routine changes of estimates relating to non-economic assumptions, as described in note 14(c)(iii) below; and
— Non-economic experience variances, as described in note 14(c)(v) below.

Non-operating results comprise the recurrent items of short-term fluctuations in investment returns, the mark to market value movements on core borrowings and the effect of changes in economic assumptions.

In addition, operating profit for half year 2014 and full year 2013 excludes the costs associated with the domestication of the Hong Kong branch and also for 2013 the loss attaching to the held for sale Japan life business. Total profit attributable to shareholders and basic earnings per share include these items, together with actual investment returns. The Company believes that operating profit, as adjusted for these items, better reflects underlying performance.

Notes on the EEV basis results continued

14 Methodology and accounting presentation continued

(ii) Post-tax operating profit

For the investment element of the assets covering the net worth of long-term insurance business, investment returns are recognised in operating results at the expected long-term rate of return. These expected returns are calculated by reference to the asset mix of the portfolio. For the purpose of calculating the longer-term investment return to be included in the operating result of the PAC with-profits fund of UK operations, where assets backing the liabilities and unallocated surplus are subject to market volatility, asset values at the beginning of the reporting period are adjusted to remove the effects of short-term market movements as explained in note 14(c)(iv) below.

For the purpose of determining the long-term returns for debt securities of US operations for fixed annuity and other general account business, a risk margin charge is included which reflects the expected long-term rate of default based on the credit quality of the portfolio. For Jackson, interest-related realised gains and losses are amortised to the operating results over the maturity period of the sold bonds and for equity-related investments, a long-term rate of return is assumed, which reflects the aggregation of end of period risk-free rates and equity risk premium. For US variable annuity separate account business, operating profit includes the unwind of discount on the opening value of in-force adjusted to reflect end of period projected rates of return with the excess or deficit of the actual return recognised within non-operating profit, together with the related hedging activity.

For UK annuity business, rebalancing of the asset portfolio backing the liabilities to policyholders may, from time to time, take place to align it more closely with the internal benchmark of credit quality that management applies. Such rebalancing will result in a change in the projected yield on the asset portfolio and the allowance for default risk. The net effect of these changes is included in the result for the period.

(iii) Effect of changes in operating assumptions

Operating profit includes the effect of changes to operating assumptions on the value of in-force at the end of the period. For presentational purposes, the effect of change is delineated to show the effect on the opening value of in-force with the experience variance being determined by reference to the end of period assumptions.

(iv) Unwind of discount and other expected returns

The unwind of discount and other expected returns is determined by reference to:

— The value of in-force business at the beginning of the period (adjusted for the effect of current period economic and operating assumption changes); and
— Required capital and surplus assets.

In applying this general approach, the unwind of discount included in operating profit for the with-profits business of UK insurance operations is determined by reference to the opening value of in-force, as adjusted for the effects of short-term investment volatility due to market movements (ie smoothed). In the summary statement of financial position and for total profit reporting, asset values and investment returns are not smoothed. At 30 June 2014 the shareholders' interest in the smoothed surplus assets used for this purpose only, were £123 million lower (30 June 2013: £25 million lower; 31 December 2013: £136 million lower) than the surplus assets carried in the statement of financial position.

(v) Operating experience variances

Operating profits include the effect of experience variances on non-economic assumptions, which are calculated with reference to the embedded value assumptions at the end of the reporting period, such as persistency, mortality and morbidity, expenses and other factors.

(vi) Internal asset management

The new business and in-force results from long-term business include the projected value of profits or losses from asset management and service companies that support the Group's covered insurance businesses. The results of the Group's asset management operations include the current period profits from the management of both internal and external funds. EEV basis shareholders' other income and expenditure is adjusted to deduct the unwind of the expected internal asset management profit margin for the period. The deduction is on a basis consistent with that used for projecting the results for covered insurance business. Group operating profit accordingly includes the variance between actual and expected profit in respect of management of the covered business assets.

(vii) Pension costs

Movements on the shareholders' share of surpluses (to the extent not restricted by IFRIC 14) and deficits of the Group's defined benefit pension schemes adjusted for contributions paid in the period are recorded within other comprehensive income.

Consistent with the basis of distribution of bonuses and the treatment of the estate described in notes 14(b)(i) and (iv), the shareholders' share incorporates 10 per cent of the proportion of the financial position attributable to the PAC with-profits fund. The financial position is determined by applying the requirements of IAS 19 as booked for IFRS reporting.

(viii) Effect of changes in economic assumptions

Movements in the value of in-force business at the beginning of the period caused by changes in economic assumptions, net of the related change in the time value of cost of option and guarantees, are recorded in non-operating results.

(ix) Taxation

In determining the post-tax profit for the period for covered business, the overall tax rate includes the impact of tax effects determined on a local regulatory basis. Tax payments and receipts included in the projected cash flows to determine the value of in-force business are calculated using rates that have been announced and substantively enacted by the end of the reporting period.

(x) Inter-company arrangements

The EEV results for covered business incorporate annuities established in the PAC non-profit sub-fund from vesting pension polices in SAIF (which is not covered business). The EEV results also incorporate the effect of the reinsurance arrangement of non-profit immediate pension annuity liabilities of SAIF to PRIL. In addition, the free surplus and value of in-force business are calculated after taking account of the impact of contingent loan arrangements between Group companies (movements in the contingent loan liability are reflected via the projected cash flows in the value of in-force and the related funding is reflected in free surplus).

15 Assumptions

Deterministic assumptions

The tables below summarise the principal financial assumptions:

Assumed investment returns reflect the expected future returns on the assets held and allocated to the covered business at the valuation date.

(i) Asia operations[notes (b), (d)]

	Risk discount rate %					
	New business			In force		
	2014	2013		2014	2013	
	30 Jun	30 Jun	31 Dec	30 Jun	30 Jun	31 Dec
China	**10.6**	10.1	11.2	**10.6**	10.1	11.2
Hong Kong[notes (b), (c)]	**4.3**	4.3	4.9	**4.2**	4.2	4.8
India	**13.9**	13.0	14.0	**13.9**	13.0	14.0
Indonesia	**12.2**	11.1	12.5	**12.2**	11.1	12.5
Korea	**6.8**	7.3	7.4	**7.1**	7.4	7.6
Malaysia[note (c)]	**6.6**	6.0	6.5	**6.6**	6.0	6.5
Philippines	**10.8**	10.6	10.5	**10.8**	10.6	10.5
Singapore[note (c)]	**4.3**	4.5	4.6	**5.0**	5.2	5.3
Taiwan	**4.0**	3.8	4.3	**4.0**	3.7	4.1
Thailand	**10.6**	10.5	10.7	**10.6**	10.5	10.7
Vietnam	**15.4**	16.1	15.7	**15.4**	16.1	15.7
Total weighted risk discount rate[note (a)]	**7.4**	7.5	8.1	**7.0**	6.7	7.2

	10-year government bond yield %			Expected long-term inflation %		
	2014	2013		2014	2013	
	30 Jun	30 Jun	31 Dec	30 Jun	30 Jun	31 Dec
China	**4.1**	3.6	4.7	**2.5**	2.5	2.5
Hong Kong[notes (b), (c)]	**2.6**	2.5	3.1	**2.3**	2.3	2.3
India	**8.9**	8.0	9.0	**4.0**	4.0	4.0
Indonesia	**8.4**	7.3	8.6	**5.0**	5.0	5.0
Korea	**3.2**	3.4	3.6	**3.0**	3.0	3.0
Malaysia[note (c)]	**4.1**	3.6	4.2	**2.5**	2.5	2.5
Philippines	**4.1**	3.9	3.8	**4.0**	4.0	4.0
Singapore[note (c)]	**2.3**	2.4	2.6	**2.0**	2.0	2.0
Taiwan	**1.6**	1.4	1.7	**1.0**	1.0	1.0
Thailand	**3.8**	3.8	3.9	**3.0**	3.0	3.0
Vietnam	**8.7**	9.3	9.0	**5.5**	5.5	5.5

Equity risk premiums in Asia (excluding those for the held for sale Japan life business) range from 3.5 per cent to 8.7 per cent for all periods throughout these results.

Notes on the EEV basis results continued

15 Assumptions continued

Notes

(a) The weighted risk discount rates for Asia operations shown above have been determined by weighting each country's risk discount rates by reference to the post-tax EEV basis new business result and the closing value of in-force business. The changes in the risk discount rates for individual Asia territories reflect the movements in government bond yields, together with the effects of movements in the allowance for market risk and changes in product mix.

(b) For Hong Kong the assumptions shown are for US dollar denominated business. For other territories, the assumptions are for local currency denominated business.

(c) The mean equity return assumptions for the most significant equity holdings in the Asia operations were:

	2014 %	2013 %	
	30 Jun	30 Jun	31 Dec
Hong Kong	6.6	6.5	7.1
Malaysia	10.1	9.6	10.1
Singapore	8.4	8.4	8.6

(d) The local tax rates applicable for the most significant operations for all periods shown, are as follows:

	Assumed corporate tax rate %
Hong Kong	16.5 per cent on 5 per cent of premium income
Indonesia	25 per cent
Malaysia	2013 to 2015: 25 per cent; from 2016: 24 per cent
Singapore	17 per cent

(ii) US operations

	2014 %	2013 %	
	30 Jun	30 Jun	31 Dec
Assumed new business spread margins:[note (a)]			
Fixed annuity business:*			
January to June issues	1.5	1.2	1.2
July to December issues	n/a	n/a	1.75
Fixed index annuity business:			
January to June issues	2.0	1.45	1.45
July to December issues	n/a	n/a	2.00
Institutional business	0.7	0.75	0.75
Allowance for long-term defaults included in projected spread[note (b)]	0.26	0.27	0.25
Risk discount rate:			
Variable annuity:			
Risk discount rate	7.1	7.3	7.6
Additional allowance for credit risk included in risk discount rate[note (b)]	0.2	0.3	0.2
Non-variable annuity:			
Risk discount rate	4.3	4.8	4.8
Additional allowance for credit risk included in risk discount rate[note (b)]	1.0	1.5	1.0
Weighted average total:[note (c)]			
New business	6.9	7.2	7.4
In force	6.4	6.5	6.9
US 10-year treasury bond rate at end of period	2.6	2.5	3.1
Pre-tax expected long-term nominal rate of return for US equities	6.6	6.5	7.1
Expected long-term rate of inflation	2.6	2.5	2.6
Equity risk premium	4.0	4.0	4.0
Assumed corporate tax rate	35.0	35.0	35.0

* Including the proportion of variable annuity business invested in the general account

Notes

(a) The assumed new business spread margins represent the difference between the earned rate on investments, after allowance for long-term defaults, and the policyholder crediting rate. The spread margins shown above are the rates at inception. For fixed annuity business (including the proportion of variable annuity business invested in the general account) and fixed index annuity business, the assumed spread margin grades up linearly by 25 basis points to a long-term assumption over five years.

(b) The allowance for long-term defaults included in projected spread is shown as at the valuation date applied in the cash flow projections of the value of the in-force business. The risk discount rates include an additional allowance for credit risk premium and short-term downgrades and defaults. See note 14(b)(iii) for further details.

(c) The weighted average risk discount rates reflect the mix of business between variable annuity and non-variable annuity business. The decrease in the weighted average risk discount rates from half year 2013 to half year 2014 primarily reflects the effect of the decrease in additional allowance for credit risk and the effects of movement in the allowance for market risk, partly offset by the increase in the US 10-year Treasury bond rate of 10 basis points.

(iii) UK insurance operations

	2014 %	2013 %	
	30 Jun	30 Jun	31 Dec
Shareholder-backed annuity business:note (b)			
Risk discount rate:			
New business	6.9	7.2	6.8
In force note (a)	7.8	8.5	8.3
Pre-tax expected long-term nominal rate of return for shareholder-backed annuity business:			
New business	4.5	3.9	4.2
In force note (a)	4.1	4.4	4.3
Other business:			
Risk discount rate:			
New business	5.9	5.8	6.1
In force	6.5	6.2	6.8
Pre-tax expected long-term nominal rates of investment return:			
UK equities	7.2	7.0	7.5
Overseas equities	6.6 to 9.1	6.5 to 9.8	7.1 to 9.2
Property	5.9	5.8	6.2
15-year gilt rate	3.2	3.0	3.5
Corporate bonds	4.8	4.6	5.1
Expected long-term rate of inflation	3.3	3.3	3.4
Equity risk premium	4.0	4.0	4.0
Assumed corporate tax rate	20.0	23.0	20.0

Notes

(a) For shareholder-backed annuity business, the movements in the pre-tax long-term nominal rates of return and the risk discount rates for in-force business mainly reflect the effect of changes in asset yields.

(b) Credit spread treatment

For Prudential Retirement Income Limited, which has approximately 90 per cent of UK shareholder-backed annuity business, the credit assumptions used in the underlying MCEV calculation (see note 14(b)(iii)) and the residual liquidity premium element of the bond spread over swap rates are as follows:

	2014 (bps)	2013 (bps)	
In-force business	30 Jun	30 Jun	31 Dec
Bond spread over swap rates	119	157	133
Total credit risk allowance	61	64	62
Liquidity premium	58	93	71

	2014 (bps)	2013 (bps)	
Individual annuity new business	30 Jun	30 Jun	31 Dec
Bond spread over swap rates	121	116	117
Total credit risk allowance	34	38	37
Liquidity premium*	87	78	80

* The new business liquidity premium is based on the weighted average of the point of sale liquidity premia.

The overall allowance for credit risk is prudent by comparison with historic rates of default and would be sufficient to withstand a wide range of extreme credit events over the expected lifetime of the annuity business.

Stochastic assumptions

The economic assumptions used for the stochastic calculations are consistent with those used for the deterministic calculations described above. Assumptions specific to the stochastic calculations, such as the volatilities of asset returns, reflect local market conditions and are based on a combination of actual market data, historic market data and an assessment of longer-term economic conditions. Common principles have been adopted across the Group for the stochastic asset models, for example, separate modelling of individual asset classes but with allowance for correlation between the various asset classes.

Details are given below of the key characteristics and calibrations of each model.

Notes on the EEV basis results continued

15 Assumptions continued

(iv) Asia operations

- The same asset return models as described for UK insurance operations below, appropriately calibrated, have been used for Asia operations. The principal asset classes are government and corporate bonds. Equity holdings are much lower than in the UK while property holdings do not represent a significant investment asset;
- The stochastic cost of guarantees is primarily only of significance for the Hong Kong, Korea, Malaysia and Singapore operations; and
- The mean stochastic returns are consistent with the mean deterministic returns for each country. The expected volatility of equity returns ranges from 18 per cent to 35 per cent for all periods throughout these results, and the volatility of government bond yields ranges from 0.9 per cent to 2.3 per cent for all periods throughout these results.

(v) US operations (Jackson)

- Interest rates are projected using a log-normal generator calibrated to historical US Treasury yield curves;
- Corporate bond returns are based on Treasury securities plus a spread that has been calibrated to current market conditions and varies by credit quality; and
- Variable annuity equity returns and bond interest rates have been stochastically generated using a log-normal model with parameters determined by reference to historical data. The volatility of equity fund returns ranges from 19 per cent to 32 per cent for all periods throughout these results, depending on the risk class and the class of equity, and the standard deviation of interest rates ranges from 2.2 per cent to 2.5 per cent for all periods throughout these results.

(vi) UK insurance operations

- Interest rates are projected using a two-factor model calibrated to the initial market yield curve;
- The risk premium on equity assets is assumed to follow a log-normal distribution;
- The corporate bond return is calculated as the return on a zero-coupon bond plus a spread. The spread process is a mean reverting stochastic process; and
- Property returns are modelled in a similar fashion to corporate bonds, namely as the return on a risk-free bond, plus a risk premium, plus a process representative of the change in residual values and the change in value of the call option on rents.

Mean returns have been derived as the annualised arithmetic average return across all simulations and durations.

For each projection period, standard deviations have been calculated by taking the square root of the annualised variance of the returns over all the simulations. These have been averaged over all durations in the projection. For equity and property, the standard deviations relate to the total return on these assets. The standard deviations applied for all periods are as follows:

	%
Equities:	
UK	20
Overseas	18
Property	15

16 Total insurance and investment products new business[note (i)]

	Single			Regular			Annual premium and contribution equivalents (APE)[note 14(b)(i)]			Present value of new business premiums (PVNBP)[note 14(b)(i)]		
	2014 £m	2013 £m		2014 £m	2013 £m		2014 £m	2013 £m		2014 £m	2013 £m	
	Half year	Half year	Full year	Half year	Half year	Full year	Half year	Half year	Full year	Half year	Half year	Full year
Group insurance operations												
Asia	**955**	1,097	2,136	**900**	899	1,911	**996**	1,010	2,125	**5,378**	5,524	11,375
US	**8,703**	7,957	15,712	**–**	1	2	**871**	797	1,573	**8,703**	7,957	15,723
UK	**3,329**	2,435	5,128	**100**	112	212	**433**	355	725	**3,741**	2,943	5,978
Group Total	**12,987**	11,489	22,976	**1,000**	1,012	2,125	**2,300**	2,162	4,423	**17,822**	16,424	33,076
Asia insurance operations												
Cambodia	**–**	–	–	**1**	–	1	**1**	–	1	**4**	–	3
Hong Kong	**175**	85	326	**240**	205	455	**258**	214	487	**1,530**	1,204	2,795
Indonesia	**101**	212	303	**174**	219	445	**184**	240	477	**748**	1,069	1,943
Malaysia	**42**	53	114	**87**	93	197	**91**	99	208	**583**	661	1,352
Philippines	**53**	129	193	**17**	16	34	**22**	29	53	**106**	177	299
Singapore	**264**	251	571	**146**	145	304	**172**	170	361	**1,217**	1,209	2,588
Thailand	**50**	20	66	**37**	23	61	**42**	25	68	**196**	106	289
Vietnam	**1**	1	2	**23**	23	54	**23**	23	54	**91**	84	204
SE Asia operations inc. Hong Kong	**686**	751	1,575	**725**	724	1,551	**793**	800	1,709	**4,475**	4,510	9,473
China[note (ii)]	**117**	76	114	**45**	39	71	**57**	47	83	**280**	243	409
Korea	**97**	200	311	**38**	42	82	**48**	62	113	**260**	359	641
Taiwan	**45**	48	102	**49**	40	107	**54**	45	117	**214**	206	491
India[note (iii)]	**10**	22	34	**43**	54	100	**44**	56	103	**149**	206	361
Total Asia operations	**955**	1,097	2,136	**900**	899	1,911	**996**	1,010	2,125	**5,378**	5,524	11,375
US insurance operations												
Variable annuities	**6,136**	5,384	10,795	**–**	–	–	**614**	538	1,079	**6,136**	5,384	10,795
Elite Access (variable annuity)	**1,493**	1,270	2,585	**–**	–	–	**149**	127	259	**1,493**	1,270	2,585
Fixed annuities	**265**	296	555	**–**	–	–	**27**	30	55	**265**	296	555
Fixed index annuities	**182**	620	907	**–**	–	–	**18**	62	91	**182**	620	907
Life	**–**	–	1	**–**	1	2	**–**	1	2	**–**	–	12
Wholesale	**627**	387	869	**–**	–	–	**63**	39	87	**627**	387	869
Total US insurance operations	**8,703**	7,957	15,712	**–**	1	2	**871**	797	1,573	**8,703**	7,957	15,723
UK and Europe insurance operations												
Direct and partnership annuities	**100**	153	284	**–**	–	–	**10**	15	28	**99**	153	284
Intermediated annuities	**100**	293	488	**–**	–	–	**10**	29	49	**100**	293	488
Internal vesting annuities	**434**	669	1,305	**–**	–	–	**43**	67	131	**434**	669	1,305
Total individual annuities	**634**	1,115	2,077	**–**	–	–	**63**	111	208	**633**	1,115	2,077
Corporate pensions	**58**	73	120	**73**	86	161	**79**	93	173	**314**	454	686
Onshore bonds	**1,019**	825	1,754	**–**	–	–	**102**	83	176	**1,019**	826	1,756
Other products	**582**	422	901	**27**	26	51	**85**	68	140	**739**	548	1,183
Wholesale	**1,036**	–	276	**–**	–	–	**104**	–	28	**1,036**	–	276
Total UK and Europe insurance operations	**3,329**	2,435	5,128	**100**	112	212	**433**	355	725	**3,741**	2,943	5,978
Group total	**12,987**	11,489	22,976	**1,000**	1,012	2,125	**2,300**	2,162	4,423	**17,822**	16,424	33,076

Notes on the EEV basis results continued

16 Total insurance and investment products new business[note (i)] continued

Investment products – funds under management[notes (iv), (v), (vi)]

	Half year 2014 £m				
	1 Jan 2014	Market gross inflows	Redemptions	Market exchange translation and other movements	30 Jun 2014
Eastspring Investments	17,927	6,869	(4,386)	668	21,078
M&G	125,989	19,322	(15,111)	2,571	132,771
Group total	143,916	26,191	(19,497)	3,239	153,849

	Half year 2013 £m				
	1 Jan 2013	Market gross inflows	Redemptions	Market exchange translation and other movements	30 Jun 2013
Eastspring Investments	17,630	7,372	(5,366)	(368)	19,268
M&G	111,868	20,598	(16,758)	2,431	118,139
Group total	129,498	27,970	(22,124)	2,063	137,407

Notes

(i) The tables shown above are provided as an indicative volume measure of transactions undertaken in the reporting period that have the potential to generate profits for shareholders. The amounts shown are not, and not intended to be, reflective of premium income recorded in the IFRS income statement.

The format of the tables shown above is consistent with the distinction between insurance and investment products as applied for previous financial reporting periods. With the exception of some US institutional business, products categorised as 'insurance' refer to those classified as contracts of long-term insurance business for regulatory reporting purposes, ie falling within one of the classes of insurance specified in Part II of Schedule 1 to the Regulated Activities Order under PRA regulations.

The details shown above for insurance products include contributions for contracts that are classified under IFRS 4 'Insurance Contracts' as not containing significant insurance risk. These products are described as investment contracts or other financial instruments under IFRS. Contracts included in this category are primarily certain unit-linked and similar contracts written in UK insurance operations and Guaranteed Investment Contracts and similar funding agreements written in US operations.

(ii) New business in China is included at Prudential's 50 per cent interest in the China life operation.

(iii) New business in India is included at Prudential's 26 per cent interest in the India life operation.

(iv) Investment products referred to in the tables for fund under management above are unit trust, mutual funds and similar types of retail fund management arrangements. These are unrelated to insurance products that are classified as 'investment contracts' under IFRS 4, although similar IFRS recognition and measurement principles apply to the acquisition costs and fees attaching to this type of business.

(v) Investment flows for the half year exclude Eastspring Money Market Funds gross inflows of £32,065 million (half year 2013: £30,774 million) and net outflows of £52 million (half year 2013: net inflows of £107 million).

(vi) New business and market gross inflows and redemptions have been translated at an average exchange rate for the period applicable. Funds under management at points in time are translated at the exchange rate applicable to those dates.

Section 5

Additional information

5

Index to the additional financial information

Additional financial information*

* The additional financial information is not covered by KPMG independent review opinion.

Additional financial information

I: Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver

This schedule classifies the Group's pre-tax operating earnings from long-term insurance operations into the underlying drivers of those profits, using the following categories:

(i) **Spread income** represents the difference between net investment income (or premium income in the case of the UK annuities new business) and amounts credited to certain policyholder accounts. It excludes the operating investment return on shareholder net assets, which has been separately disclosed as expected return on shareholder assets.

(ii) **Fee income** represents profits driven by net investment performance, being asset management fees that vary with the size of the underlying policyholder funds net of investment management expenses.

(iii) **With-profits** business represents the gross of tax shareholders' transfer from the with-profits fund for the period.

(iv) **Insurance margin** primarily represents profits derived from the insurance risks of mortality and morbidity.

(v) **Margin on revenues** primarily represents amounts deducted from premiums to cover acquisition costs and administration expenses.

(vi) **Acquisition costs and administration expenses** represent expenses incurred in the period attributable to shareholders. It excludes items such as restructuring costs and Solvency II costs which are not included in the segment profit for insurance as well as items that are more appropriately included in other source of earnings lines (eg investment expenses are netted against investment income as part of spread income or fee income as appropriate).

(vii) **DAC adjustments** comprises DAC amortisation for the period, excluding amounts related to short-term fluctuations in investment returns, net of costs deferred in respect of new business.

Analysis of pre-tax IFRS operating profit by source

	Half year 2014 £m				
	Asia note (ii)	US	UK	Unallocated	Total
Spread income	62	364	131	–	557
Fee income	74	658	32	–	764
With-profits	15	–	135	–	150
Insurance margin	314	328	38	–	680
Margin on revenues	724	–	84	–	808
Expenses:					
Acquisition costs	(473)	(477)	(50)	–	(1,000)
Administration expenses	(304)	(333)	(64)	–	(701)
DAC adjustments	40	135	(6)	–	169
Expected return on shareholder assets	31	11	74	–	116
Long-term business operating profit	483	686	374	–	1,543
Asset management operating profit	42	(5)	249	–	286
GI commission	–	–	12	–	12
Other income and expenditure note (i)	–	–	–	(320)	(320)
Total operating profit based on longer-term investment returns note (ii)	525	681	635	(320)	1,521

	AER Half year 2013 £m				
	Asia note (ii)	US	UK	Unallocated	Total
Spread income	56	377	102	–	535
Fee income	80	554	33	–	667
With-profits	22	–	133	–	155
Insurance margin	303	262	48	–	613
Margin on revenues	778	–	80	–	858
Expenses:					
Acquisition costs	(502)	(465)	(54)	–	(1,021)
Administration expenses	(300)	(323)	(59)	–	(682)
DAC adjustments	9	173	(7)	–	175
Expected return on shareholder assets	28	4	65	–	97
Long-term business operating profit	474	582	341	–	1,397
Asset management operating profit	38	34	225	–	297
GI commission	–	–	15	–	15
Other income and expenditure note (i)	–	–	–	(294)	(294)
Total operating profit based on longer-term investment returns note (ii)	512	616	581	(294)	1,415

Additional financial information continued

I: Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver continued

	CER Half year 2013 £m				
	Asia note (ii)	US	UK	Unallocated	Total
Spread income	49	348	102	–	499
Fee income	69	513	33	–	615
With-profits	20	–	133	–	153
Insurance margin	261	242	48	–	551
Margin on revenues	669	–	80	–	749
Expenses:					
Acquisition costs	(433)	(430)	(54)	–	(917)
Administration expenses	(260)	(299)	(59)	–	(618)
DAC adjustments	8	160	(7)	–	161
Expected return on shareholder assets	23	4	65	–	92
Long-term business operating profit	406	538	341	–	1,285
Asset management operating profit	34	31	225	–	290
GI commission	–	–	15	–	15
Other income and expenditure[note (i)]	–	–	–	(294)	(294)
Total operating profit based on longer-term investment returns[note (ii)]	440	569	581	(294)	1,296

Notes
(i) Including restructuring and Solvency II implementation costs.
(ii) The profit analysis above excludes the results of the life insurance business of Japan which is held for sale.

Margin analysis of long-term insurance business – Group

The following analysis expresses certain of the Group's sources of operating profit as a margin of policyholder liabilities or other suitable driver. Details on the calculation of the Group's average policyholder liability balances are given in note (iii).

	Total								
	Half year 2014 note (iv)			AER Half year 2013 note (iv)			CER Half year 2013 notes (iv),(v)		
Long-term business	Profit £m	Average liability note (iii) £m	Margin note (ii) bps	Profit £m	Average liability note (iii) £m	Margin note (ii) bps	Profit £m	Average liability note (iii) £m	Margin note (ii) bps
Spread income	557	64,741	172	535	65,424	164	499	62,492	160
Fee income	764	106,052	144	667	93,512	143	615	87,678	140
With-profits	150	98,046	31	155	97,336	32	153	96,352	32
Insurance margin	680			613			551		
Margin on revenues	808			858			749		
Expenses:									
Acquisition costs[note (i)]	(1,000)	2,300	(43)%	(1,021)	2,162	(47)%	(917)	1,974	(46)%
Administration expenses	(701)	178,649	(78)	(682)	166,130	(82)	(618)	156,839	(79)
DAC adjustments	169			175			161		
Expected return on shareholder assets	116			97			92		
Operating profit	1,543			1,397			1,285		

Notes
(i) The ratio for acquisition costs is calculated as a percentage of APE sales including with-profits sales. Acquisition costs include only those relating to shareholder-backed business.
(ii) Margin represents the operating return earned in the period as a proportion of the relevant class of policyholder liabilities excluding unallocated surplus. The margin is on an annualised basis in which half year profits are annualised by multiplying by two.
(iii) For UK and Asia, opening and closing policyholder liabilities have been used to derive an average balance for the period, as a proxy for average balances throughout the period. The calculation of average liabilities for Jackson is derived from month end balances throughout the period as opposed to opening and closing balances only. Average liabilities for spread income are based on the general account liabilities to which spread income attaches. In addition, for REALIC (acquired in 2012), which are included in the average liability to calculate the administration expense margin, the calculation excludes the liabilities reinsured to third parties prior to the acquisition by Jackson. Average liabilities are adjusted for business acquisitions and disposals in the period.
(iv) The half year 2014 and half year 2013 analyses exclude the results of the held for sale life insurance business of Japan in both the individual profit and average liability amounts shown in the table above.
(v) The half year 2013 comparative information has been presented at AER and CER so as to eliminate the impact of exchange translation. CER results are calculated by translating prior period results using the current period foreign exchange rates. All CER profit figures have been translated at current period average rates. For Asia CER average liability calculations the policyholder liabilities have been translated using current period opening and closing exchange rates. For the US CER average liability calculations the policyholder liabilities have been translated at the current period month end closing exchange rates. See also note A1.

Margin analysis of long-term insurance business – Asia

Long-term business	Asia Half year 2014 note (ii) Profit £m	Average liability notes (iii),(v) £m	Margin bps	AER Half year 2013 note (ii) Profit £m	Average liability note (iii) £m	Margin bps	CER Half year 2013 notes (ii),(v) Profit £m	Average liability note (iii) £m	Margin bps
Spread income	62	8,472	146	56	7,220	155	49	6,653	147
Fee income	74	14,204	104	80	14,253	112	69	12,772	108
With-profits	15	13,653	22	22	13,522	33	20	12,538	32
Insurance margin	314			303			261		
Margin on revenues	724			778			669		
Expenses:									
Acquisition costs note (i)	(473)	996	(47)%	(502)	1,010	(50)%	(433)	882	(49)%
Administration expenses	(304)	22,676	(268)	(300)	21,473	(279)	(260)	19,425	(268)
DAC adjustments note (iv)	40			9			8		
Expected return on shareholder assets	31			28			23		
Operating profit	483			474			406		

Notes

(i) The ratio for acquisition costs is calculated as a percentage of APE sales including with-profits sales. Acquisition costs include only those relating to shareholder-backed business.

(ii) The analysis excludes the results of the life insurance business of Japan in both the individual profit and the average liability amounts for both 2013 and 2014.

(iii) Opening and closing policyholder liabilities, adjusted for corporate transactions, have been used to derive an average balance for the year, as a proxy for average balances throughout the year.

(iv) The DAC adjustment contains £2 million in respect of joint ventures in half year 2014.

(v) CER results are calculated by translating prior period results using the current period foreign exchange rates. All CER profit figures have been translated at current period average rates and for the average liability calculations the policyholder liability balances have been translated at the current period opening and closing exchange rates.

Analysis of Asia operating profit drivers

- **Spread income** has increased by 27 per cent at constant exchange rates (AER 11 per cent) to £62 million in half year 2014, predominantly reflecting the growth of the Asian non-linked policyholder liabilities.
- **Fee income** has increased by 7 per cent at constant exchange rates (AER 8 per cent decrease) to £74 million in half year 2014, broadly in line with the increase in movement in average unit-linked liabilities.
- **Insurance margin** has increased by 20 per cent at constant exchange rates (AER 4 per cent) to £314 million in half year 2014 predominantly reflecting the continued growth of the in-force book, which contains a relatively high proportion of risk-based products and management action on claims controls and pricing. Half year 2014 insurance margin includes non-recurring items of £3 million (half year 2013: £23 million at AER; £19 million at CER).
- Excluding the adverse impact of currency fluctuations, **margin on revenues** has increased by £55 million from £669 million in half year 2013 to £724 million in half year 2014 primarily reflecting higher premium income recognised in the period.
- **Acquisition costs** have increased by 9 per cent at constant exchange rates (AER 6 per cent decrease) to £473 million in half year 2014, compared to the 13 per cent increase in sales (AER 1 per cent decrease), resulting in a modest decrease in the acquisition costs ratio. The analysis above uses shareholder acquisition costs as a proportion of total APE. If with-profits sales were excluded from the denominator the acquisition cost ratio would become 68 per cent (half year 2013: 67 per cent at CER). The small increase being the result of changes to product and country mix.
- **Administration expenses** have increased by 17 per cent at constant exchange rates (AER 1 per cent) to £304 million in half year 2014 as the business continues to invest in developing its infrastructure to keep pace with the growth in the business. On constant exchange rates the administration expense ratio remains in line with prior period at 268 basis points.
- **Expected return on shareholder assets** has increased from £28 million in half year 2013 to £31 million in half year 2014 primarily due to higher income from increased shareholder assets offset by the adverse effects of currency translation.

Additional financial information continued

I: Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver continued

Margin analysis of long-term insurance business – US

	US								
	Half year 2014			AER Half year 2013			CER Half year 2013 note (iii)		
Long-term business	Profit £m	Average liability note (ii) £m	Margin bps	Profit £m	Average liability note (ii) £m	Margin bps	Profit £m	Average liability note (ii) £m	Margin bps
Spread income	364	28,207	258	377	31,137	242	348	28,772	242
Fee income	658	68,177	193	554	56,539	196	513	52,186	197
Insurance margin	328			262			242		
Expenses:									
Acquisition costs note (i)	(477)	871	(55)%	(465)	797	(58)%	(430)	737	(58)%
Administration expenses	(333)	104,240	(64)	(323)	94,870	(68)	(299)	87,627	(68)
DAC adjustments	135			173			160		
Expected return on shareholder assets	11			4			4		
Operating profit	686			582			538		

Notes
(i) The ratio for acquisition costs is calculated as a percentage of APE sales.
(ii) The calculation of average liabilities for Jackson is derived from month end balances throughout the period as opposed to opening and closing balances only. Average liabilities for spread income are based on the general account liabilities to which spread income attaches. Average liabilities used to calculate the administrative expense margin exclude the REALIC liabilities reinsured to third parties prior to the acquisition by Jackson.
(iii) CER results are calculated by translating prior period results using the current period foreign exchange rates. All CER profit figures have been translated at the current period average rate and for the average liability calculations the policyholder liability balances have been translated at the current period month end-closing exchange rates.

Analysis of US operating profit drivers:

— **Spread income** has increased by 5 per cent at constant exchange rate (AER reduced by 3 per cent) to £364 million in first half 2014. The reported spread margin increased to 258 basis points from 242 basis points in the first half of 2013, primarily as a result of lower crediting rates. In addition, spread income benefited from swap transactions previously entered into to more closely match the overall asset and liability duration. Excluding this effect, the spread margin would have been 185 basis points (half year 2013: 183 basis points on both AER and CER bases).

— **Fee income** has increased by 28 per cent at constant exchange rate (AER 19 per cent) to £658 million during the first half of 2014, due to higher average separate account balances resulting from positive net cash flows from variable annuity business and market appreciation over the past 12 months. Fee income margin has remained broadly consistent with the prior period at 193 basis points (half year 2013 at 197 basis points at CER; 196 basis points at AER), with the decrease primarily attributable to a change in the mix of business.

— **Insurance margin** represents operating profits from insurance risks, including variable annuity guarantees and other sundry items. Positive net flows from variable annuity business with life contingent and other guarantee fees, coupled with a benefit from re-pricing actions, have increased the insurance margin to £328 million in the first half of 2014.

— **Acquisition costs**, which are commissions and expenses incurred to acquire new business, including those that are not deferrable, have increased to £477 million reflecting higher volumes. As a percentage of APE, acquisition costs have decreased to 55 per cent for half year 2014, compared to 58 per cent in half year 2013 due to the continued shift towards producers selecting asset-based commissions which are treated as an administrative expense in this analysis, rather than front end commissions.

— **Administration expenses** increased to £333 million during the first half of 2014 compared to £299 million for the first half of 2013 at a constant exchange rate (AER £323 million) primarily as a result of higher asset-based commissions paid on the larger 2014 separate account balance. These are paid on policy anniversary dates and are treated as an administration expense in this analysis. Excluding these trail commissions, the resulting administration expense ratio would be lower at 37 basis points from 45 basis points (on both CER and AER bases) in the first half of 2013, reflecting the benefits of operational leverage.

— **DAC adjustments** decreased to £135 million during the first half of 2014 compared with £160 million at a constant exchange rate (AER £173 million) during the first half of 2013. This reflects the interplay between higher DAC amortisation charges on costs previously deferred (reflecting business growth), which is outpacing the rate at which current period acquisition costs are being deferred. Certain acquisition costs are not fully deferrable, resulting in new business strain of £103 million for the first half of 2014 (half year 2013: £86 million on CER basis; £93 million on AER basis) mainly reflecting the increase in sales in the period.

Analysis of pre-tax operating profit before and after acquisition costs and DAC adjustments

	Half year 2014 £m			
	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total
Total operating profit before acquisition costs and DAC adjustments	1,028			1,028
Less new business strain		(477)	374	(103)
Other DAC adjustments – amortisation of previously deferred acquisition costs:				
Normal			(249)	(249)
Deceleration			10	10
Total	1,028	(477)	135	686

	AER Half year 2013 £m				CER Half year 2013 £m note			
	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total
Total operating profit before acquisition costs and DAC adjustments	874			874	808			808
Less new business strain		(465)	372	(93)		(430)	344	(86)
Other DAC adjustments – amortisation of previously deferred acquisition costs:								
Normal			(219)	(219)			(203)	(203)
Deceleration			20	20			19	19
Total	874	(465)	173	582	808	(430)	160	538

Note
The half year 2013 comparative information has been presented at AER and CER so as to eliminate the impact of exchange translation. CER results are calculated by translating prior period results using the current period foreign exchange rate. See also Note A1.

Additional financial information continued

I: Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver continued

Margin analysis of long-term insurance business – UK

	UK					
	Half year 2014			Half year 2013		
	Profit	Average liability note (ii)	Margin	Profit	Average liability note (ii)	Margin
Long-term business	£m	£m	bps	£m	£m	bps
Spread income	131	28,062	93	102	27,067	75
Fee income	32	23,671	27	33	22,720	29
With-profits	135	84,393	32	133	83,814	32
Insurance margin	38			48		
Margin on revenues	84			80		
Expenses:						
Acquisition costs[note (i)]	(50)	433	(12)%	(54)	355	(15)%
Administration expenses	(64)	51,733	(25)	(59)	49,787	(24)
DAC adjustments	(6)			(7)		
Expected return on shareholder assets	74			65		
Operating profit	374			341		

Notes

(i) The ratio for acquisition costs is calculated as a percentage of APE sales including with-profits sales. Acquisition costs include only those relating to shareholder-backed business.

(ii) Opening and closing policyholder liabilities have been used to derive an average balance for the period, as a proxy for average balances throughout the period.

Analysis of UK operating profit drivers:

— **Spread income** has increased 28 per cent from £102 million in half year 2013 to £131 million in half year 2014 principally due to the increase in profit from bulk annuity transactions, partially offset by lower individual annuity sales in half year 2014. This has increased the margin from 75 basis points in half year 2013 to 93 basis points in half year 2014.

— **Insurance margin** has decreased from £48 million in half year 2013 to £38 million in half year 2014. Improved profits from the UK protection business and favourable mortality experience on the UK annuity book are offset by the non-recurrence of the benefit in 2013 of a longevity swap on certain aspects of the UK's annuity back-book liabilities.

— **Acquisition costs** as a percentage of new business sales in half year 2014 decreased to 12 per cent from 15 per cent at half year 2013, principally driven by the effect of higher bulk annuity sales in the period, which traditionally are less capital intensive. The ratio above expresses the percentage of shareholder acquisition costs as a percentage of total APE sales. It is therefore impacted by the level of with-profit sales in the year. Acquisition costs as a percentage of shareholder-backed new business sales, excluding the bulk annuity transactions, were 35 per cent in half year 2014 (half year 2013: 34 per cent).

— **Administration expenses** at £64 million are £5 million higher than for half year 2013, reflecting an increase in the proposition development spend following the UK Budget announcement. The administration expense ratio remains broadly in line with the prior period at 25 basis points (half year 2013: 24 basis points).

— **Expected return** on shareholder assets has increased from £65 million in half year 2013 to £74 million in half year 2014 principally due to higher IFRS shareholders' funds.

II: Asia operations – analysis of IFRS operating profit by territory

Operating profit based on longer-term investment returns for Asia operations are analysed below. For memorandum disclosure purposes, the table below presents the half year 2013 results on both AER and CER bases so as to eliminate the impact of exchange translation.

	Half year 2014 £m	AER Half year 2013 £m	CER Half year 2013 £m	AER vs Half year 2013	CER vs Half year 2013	Full year 2013 £m
Hong Kong	**51**	51	47	0%	9%	101
Indonesia	**139**	137	105	1%	32%	291
Malaysia	**61**	73	66	(16)%	(8)%	137
Philippines	**11**	9	8	22%	38%	18
Singapore	**99**	104	94	(5)%	5%	219
Thailand	**25**	11	10	127%	150%	53
Vietnam	**27**	16	14	69%	93%	54
SE Asia Operations inc. Hong Kong	**413**	401	344	3%	20%	873
China	**8**	6	6	33%	33%	10
India	**24**	26	21	(8)%	14%	51
Korea	**17**	8	7	113%	143%	17
Taiwan	**7**	4	4	75%	75%	12
Other	**(4)**	–	(1)	n/a	n/a	(4)
Non-recurrent items note (ii)	**19**	31	27	(39)%	(30)%	44
Total insurance operations note (i)	**484**	476	408	2%	19%	1,003
Development expenses	**(1)**	(2)	(2)	50%	50%	(2)
Total long-term business operating profit note (iii)	**483**	474	406	2%	19%	1,001
Eastspring Investments	**42**	38	34	11%	24%	74
Total Asia operations	**525**	512	440	3%	19%	1,075

Notes

(i) Analysis of operating profit between new and in-force business

The result for insurance operations comprises amounts in respect of new business and business in force as follows:

	2014 £m	2013 £m		
	Half year	AER Half year	CER Half year	Full year
New business strain*	**(19)**	(23)	(22)	(15)
Business in force	**484**	468	403	974
Non-recurrent items note (ii)	**19**	31	27	44
Total	**484**	476	408	1,003

* The IFRS new business strain corresponds to approximately 2 per cent of new business APE sales for 2014 (half year 2013: approximately 2 per cent; full year 2013: approximately 1 per cent).

The strain represents the pre-tax regulatory basis strain to net worth after IFRS adjustments; for example the deferral of acquisition costs and deferred income where appropriate.

(ii) Other non-recurrent items of £19 million in 2014 (half year 2013: £31 million; full year 2013: £44 million) represent a small number of items that are not anticipated to re-occur in subsequent years.

(iii) To facilitate comparisons of operating profit based on longer-term investment returns that reflect the Group's retained operations, the results attributable to the held for sale Japan life business are not included within the long-term business operating profit for Asia. The Japan life business contributed an operating profit of £nil in 2014 (half year 2013: profit of £5 million; full year 2013: profit of £3 million).

Additional financial information continued

III: Analysis of asset management operating profit based on longer-term investment returns

	Half year 2014 £m				
	M&G note (ii)	**Eastspring Investments** note (ii)	**Prudential Capital**	**US**	**Total**
Operating income before performance-related fees	463	111	64	139	777
Performance-related fees	7	–	–	–	7
Operating income (net of commission)[note (i)]	470	111	64	139	784
Operating expense[note (i)]	(249)	(65)	(42)	(144)	(500)
Share of associate's results	6	–	–	–	6
Group's share of tax on joint ventures' operating profit	–	(4)	–	–	(4)
Operating profit based on longer-term investment returns	227	42	22	(5)	286
Average funds under management	£242.9bn	£62.4bn			
Margin based on operating income*	38bps	36bps			
Cost/income ratio†	54%	59%			

	Half year 2013 £m				
	M&G note (ii)	**Eastspring Investments** note (ii)	**Prudential Capital**	**US**	**Total**
Operating income before performance-related fees	421	109	56	181	767
Performance-related fees	4	1	–	–	5
Operating income (net of commission)[note (i)]	425	110	56	181	772
Operating expense[note (i)]	(226)	(68)	(35)	(147)	(476)
Share of associate's results	5	–	–	–	5
Group's share of tax on joint ventures' operating profit	–	(4)	–	–	(4)
Operating profit based on longer-term investment returns	204	38	21	34	297
Average funds under management	£230.9bn	£62.7bn			
Margin based on operating income*	36bps	35bps			
Cost/income ratio†	54%	62%			

	Full year 2013 £m				
	M&G note (ii)	**Eastspring Investments** note (ii)	**Prudential Capital**	**US**	**Total**
Operating income before performance-related fees	863	215	121	362	1,561
Performance-related fees	25	1	–	–	26
Operating income (net of commission)[note (i)]	888	216	121	362	1,587
Operating expense[note (i)]	(505)	(134)	(75)	(303)	(1,017)
Share of associate's results	12	–	–	–	12
Group's share of tax on joint ventures' operating profit	–	(8)	–	–	(8)
Operating profit based on longer-term investment returns	395	74	46	59	574
Average funds under management	£233.8bn	£61.9bn			
Margin based on operating income*	37bps	35bps			
Cost/income ratio†	59%	62%			

Notes

(i) Operating income and expense includes the Group's share of contribution from joint ventures (but excludes any contribution from associates). In the income statement as shown in note B2 of the IFRS financial statements, the net post-tax income of the joint ventures and associates is shown as a single item.

(ii) M&G and Eastspring Investments can be further analysed as follows:

M&G

	Operating income before performance-related fees					
	Retail £m	**Margin of FUM*** bps	**Institutional‡** £m	**Margin of FUM*** bps	**Total** £m	**Margin of FUM*** bps
30 Jun 14	**291**	**86**	**172**	**20**	**463**	**38**
30 Jun 13	265	89	156	18	421	36
31 Dec 13	550	89	313	18	863	37

Eastspring Investments

	Operating income before performance-related fees					
	Retail £m	**Margin of FUM*** bps	**Institutional‡** £m	**Margin of FUM*** bps	**Total** £m	**Margin of FUM*** bps
30 Jun 14	**65**	**62**	**46**	**22**	**111**	**36**
30 Jun 13	64	60	45	22	109	35
31 Dec 13	127	60	88	22	215	35

* Margin represents operating income before performance-related fees as a proportion of the related funds under management (FUM). Half year figures have been annualised by multiplying by two. Monthly closing internal and external funds managed by the respective entity have been used to derive the average. Any funds held by the Group's insurance operations which are managed by third parties outside of the Prudential Group are excluded from these amounts.

† Cost/income ratio represents cost as a percentage of operating income before performance-related fees.

‡ Institutional includes internal funds.

Additional financial information continued

IV: Holding company cash flow

	2014 £m	2013 £m	
	Half year	**Half year**	**Full year**
Net cash remitted by business units:			
UK net remittances to the Group			
UK Life fund paid to the Group	193	206	206
Shareholder-backed business:			
Other UK paid to the Group	53	20	149
Group invested in UK	–	–	–
Total shareholder-backed business	53	20	149
Total UK net remittances to the Group	246	226	355
US remittances to the Group	352	294	294
Asia net remittances to the Group			
Asia paid to the Group:			
Long-term business	240	228	454
Other operations	32	33	56
	272	261	510
Group invested in Asia:			
Long-term business	(3)	(3)	(9)
Other operations (including funding of Regional Head Office costs)	(53)	(68)	(101)
	(56)	(71)	(110)
Total Asia net remittances to the Group	216	190	400
M&G remittances to the Group	135	109	235
Prudential Capital remittances to the Group	25	25	57
Net remittances to the Group from Business Units	974	844	1,341
Net interest paid	(161)	(142)	(300)
Tax received	111	114	202
Corporate activities	(93)	(89)	(185)
Solvency II costs	(12)	(15)	(32)
Total central outflows	(155)	(132)	(315)
Net operating holding company cash flow before dividend*	819	712	1,026
Dividend paid	(610)	(532)	(781)
Operating holding company cash flow after dividend*	209	180	245
Issue of hybrid debt, net of costs	–	429	1,124
Corporate transactions for distribution rights and acquired subsidiaries	(520)	(397)	(428)
Other net cash payments	–	(97)	(83)
Total holding company cash flow	(311)	115	858
Cash and short-term investments at beginning of period	2,230	1,380	1,380
Foreign exchange movements	(17)	(5)	(8)
Cash and short-term investments at end of period	1,902	1,490	2,230

* Including central finance subsidiaries.

V: Funds under management

(a) Summary note (i)

	2014 £bn	2013 £bn	
	30 Jun	30 Jun	31 Dec
Business area:			
Asia operations	**42.1**	39.9	38.0
US operations	**109.9**	102.5	104.3
UK operations	**160.4**	155.7	157.3
Prudential Group funds under management	**312.4**	298.1	299.6
External funds note (ii)	**144.8**	129.3	143.3
Total funds under management	**457.2**	427.4	442.9

Notes

(i) Including Group's share of assets managed by joint ventures.

(ii) External funds shown above as at 30 June 2014 of £144.8 billion (30 June 2013: £129.3 billion; 31 December 2013: £143.3 billion) comprise £158.1 billion (30 June 2013: £141.7 billion; 31 December 2013: £148.2 billion) of funds managed by M&G and Eastspring Investments as shown in note (c) below less £13.3 billion (30 June 2013: £12.4 billion; 31 December 2013: £4.9 billion) that are classified within Prudential Group's funds. The £158.1 billion (30 June 2013: £141.7 billion; 31 December 2013: £148.2 billion) investment products comprise £153.8 billion (30 June 2013: £137.4 billion; 31 December 2013: £143.9 billion) as published in the New Business schedules plus Asia Money Market Funds of £4.3 billion (30 June 2013: £4.3 billion; 31 December 2013: £4.3 billion).

(b) Prudential Group funds under management – analysis by business area

	Asia operations £bn			US operations £bn			UK operations £bn			Total £bn		
	30 Jun 2014	30 Jun 2013	31 Dec 2013	30 Jun 2014	30 Jun 2013	31 Dec 2013	30 Jun 2014	30 Jun 2013	31 Dec 2013	30 Jun 2014	30 Jun 2013	31 Dec 2013
Investment properties*	**–**	–	–	**0.1**	0.1	–	**11.9**	10.7	11.7	**12.0**	10.8	11.7
Equity securities	**16.8**	14.1	14.4	**71.8**	60.4	66.0	**42.0**	37.8	39.8	**130.6**	112.3	120.2
Debt securities	**20.0**	20.1	18.6	**30.6**	33.4	30.3	**83.6**	84.8	84.0	**134.2**	138.3	132.9
Loans and receivables	**0.9**	1.0	0.9	**6.1**	6.7	6.4	**5.4**	5.5	5.3	**12.4**	13.2	12.6
Other investments and deposits	**0.7**	1.2	0.9	**1.3**	1.9	1.6	**17.0**	16.6	16.0	**19.0**	19.7	18.5
Total included in statement of financial position	**38.4**	36.4	34.8	**109.9**	102.5	104.3	**159.9**	155.4	156.8	**308.2**	294.3	295.9
Internally managed funds held in insurance joint ventures	**3.7**	3.5	3.2	**–**	–	–	**0.5**	0.3	0.5	**4.2**	3.8	3.7
Total Prudential Group funds under management	**42.1**	39.9	38.0	**109.9**	102.5	104.3	**160.4**	155.7	157.3	**312.4**	298.1	299.6

* As included in the investments section of the consolidated statement of financial position at 30 June 2014, except for £0.3 billion (30 June 2013: £0.2 billion; 31 December 2013: £0.3 billion) investment properties which are held for sale or occupied by the Group and, accordingly under IFRS, are included in other statement of financial position captions.

Additional financial information continued

V: Funds under management continued

(c) Investment products – external funds under management

	Half year 2014 £m				
	1 Jan 2014	Market gross inflows	Redemptions	Market exchange translation and other movements	30 Jun 2014
Eastspring Investments[note]	22,222	38,934	(36,504)	726	25,378
M&G	125,989	19,322	(15,111)	2,571	132,771
Group total	148,211	58,256	(51,615)	3,297	158,149

	Half year 2013 £m				
	1 Jan 2013	Market gross inflows	Redemptions	Market exchange translation and other movements	30 Jun 2013
Eastspring Investments[note]	21,634	38,146	(36,034)	(211)	23,535
M&G	111,868	20,598	(16,758)	2,431	118,139
Group total	133,502	58,744	(52,792)	2,220	141,674

	Full year 2013 £m				
	1 Jan 2013	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2013
Eastspring Investments[note]	21,634	74,206	(72,111)	(1,507)	22,222
M&G	111,868	40,832	(31,342)	4,631	125,989
Group total	133,502	115,038	(103,453)	3,124	148,211

Note
Including Asia Money Market Funds at 30 June 2014 of £4.3 billion (30 June 2013: £4.3 billion; 31 December 2013: £4.3 billion).

(d) M&G and Eastspring Investments – total funds under management

	2014 £bn	2013 £bn	
M&G	30 Jun	30 Jun	31 Dec
External funds under management	132.8	118.1	126.0
Internal funds under management	120.9	116.2	118.0
Total funds under management	253.7	234.3	244.0

	2014 £bn	2013 £bn	
Eastspring Investments	30 Jun	30 Jun	31 Dec
External funds under management[note]	25.4	23.5	22.2
Internal funds under management	41.4	38.3	37.7
Total funds under management	66.8	61.8	59.9

Note
Including Asia Money Market Funds at 30 June 2014 of £4.3 billion (30 June 2013: £4.3 billion; 31 December 2013: £4.3 billion).

VI: Option schemes

The Group maintains four share option schemes satisfied by the issue of new shares. Executive directors and eligible employees based in the UK may participate in the UK savings-related share option scheme, executives based in Asia and eligible employees can participate in the international savings-related share option scheme. Employees based in Dublin are eligible to participate in the Prudential International Assurance sharesave plan, and Hong Kong-based agents can participate in the non-employee savings-related share option scheme. Further details of the schemes and accounting policies are detailed in Note B3.2 of the IFRS basis consolidated financial statements in the 2013 annual report.

All options were granted at £nil consideration. No options have been granted to substantial shareholders, suppliers of goods or services (excluding options granted to agents under the non-employee savings-related share option scheme) or in excess of the individual limit for the relevant scheme.

The options schemes will terminate as follows, unless the directors resolve to terminate the plans at an earlier date:

— UK savings-related share option scheme: 16 May 2023;
— International savings-related share option scheme: 31 May 2021;
— Prudential International Assurance sharesave plan: 3 August 2019; and
— International savings-related share option scheme for non-employees 2012: 17 May 2022.

The weighted average share price of Prudential plc for the period ended 30 June 2014 was £13.35 (30 June 2013: £10.48).

The following analyses show the movements in options for each of the option schemes for the period ended 30 June 2014.

UK savings-related share option scheme

		Exercise period		Number of shares under option						
Date of grant	Exercise price £	Beginning	End	Beginning of period	Granted	Exercised	Cancelled	Forfeited	Lapsed	End of period
28 Sep 06	4.75	01 Dec 13	31 May 14	148	–	(148)	–	–	–	–
26 Apr 07	5.72	01 Jun 14	30 Nov 14	503	–	(380)	–	–	–	123
27 Sep 07	5.52	01 Dec 14	31 May 15	1,668	–	(127)	–	–	(5)	1,536
25 Apr 08	5.51	01 Jun 15	30 Nov 15	1,544	–	(72)	–	–	(4)	1,468
25 Sep 08	4.38	01 Dec 13	31 May 14	12,317	–	(12,317)	–	–	–	–
25 Sep 08	4.38	01 Dec 15	31 May 16	10,873	–	(307)	–	–	(25)	10,541
27 Apr 09	2.88	01 Jun 14	30 Nov 14	1,655,947	–	(1,398,434)	(1,417)	(2,713)	(6,064)	247,319
27 Apr 09	2.88	01 Jun 16	30 Nov 16	171,125	–	(3,679)	–	–	(186)	167,260
25 Sep 09	4.25	01 Dec 14	31 May 15	82,407	–	(3,642)	–	–	(1,136)	77,629
28 Sep 10	4.61	01 Dec 13	31 May 14	62,431	–	(49,873)	–	(780)	(1,560)	10,218
28 Sep 10	4.61	01 Dec 15	31 May 16	122,255	–	(2,113)	–	–	(1,235)	118,907
16 Sep 11	4.66	01 Dec 14	31 May 15	434,105	–	(15,443)	(3,089)	(2,857)	(5,172)	407,544
16 Sep 11	4.66	01 Dec 16	31 May 17	178,689	–	(4,824)	(3,268)	(5,228)	(1,973)	163,396
21 Sep 12	6.29	01 Dec 15	31 May 16	940,009	–	(6,211)	(10,688)	(7,581)	(8,031)	907,498
21 Sep 12	6.29	01 Dec 17	31 May 18	140,115	–	(313)	(954)	–	(1,070)	137,778
20 Sep 13	9.01	01 Dec 16	31 May 17	418,408	–	(546)	(7,680)	(7,623)	(5,160)	397,399
20 Sep 13	9.01	01 Dec 18	31 May 19	91,054	–	–	(1,664)	(1,996)	–	87,394
				4,323,598	–	(1,498,429)	(28,760)	(28,778)	(31,621)	2,736,010

The total number of securities available for issue under the scheme is 2,736,010 which represents 0.107 per cent of the issued share capital at 30 June 2014.

The weighted average closing price of the shares immediately before the dates on which the options were exercised during the current period was £13.77.

Additional financial information continued

VI: Option schemes continued

International savings-related share option scheme

		Exercise period		Number of shares under option						
Date of grant	Exercise price £	Beginning	End	Beginning of period	Granted	Exercised	Cancelled	Forfeited	Lapsed	End of period
25 Apr 08	5.51	01 Jun 13	30 Nov 13	1,453	–	(1,453)	–	–	–	–
25 Sep 08	4.38	01 Dec 13	31 May 14	3,503	–	(3,503)	–	–	–	–
27 Apr 09	2.88	01 Jun 14	30 Nov 14	75,573	–	(63,188)	–	–	–	12,385
25 Sep 09	4.25	01 Dec 12	31 May 13	5,349	–	(5,349)	–	–	–	–
25 Sep 09	4.25	01 Dec 14	31 May 15	2,682	–	–	–	–	–	2,682
28 Sep 10	4.61	01 Dec 13	31 May 14	29,097	–	(29,097)	–	–	–	–
28 Sep 10	4.61	01 Dec 15	31 May 16	6,130	–	–	–	–	–	6,130
16 Sep 11	4.66	01 Dec 14	31 May 15	322,112	–	(1,744)	(399)	(12,602)	–	307,367
16 Sep 11	4.66	01 Dec 16	31 May 17	25,739	–	–	–		–	25,739
21 Sep 12	6.29	01 Dec 15	31 May 16	629,331	–	–	–	(35,013)	–	594,318
21 Sep 12	6.29	01 Dec 17	31 May 18	26,114	–	(596)	–	(5,451)	–	20,067
20 Sep 13	9.01	01 Dec 16	31 May 17	690,823	–	–	(998)	(31,137)	–	658,688
20 Sep 13	9.01	01 Dec 18	31 May 19	55,409	–	–	–	(1,664)	–	53,745
				1,873,315	–	(104,930)	(1,397)	(85,867)	–	1,681,121

The total number of securities available for issue under the scheme is 1,681,121 which represents 0.066 per cent of the issued share capital at 30 June 2014.

The weighted average closing price of the shares immediately before the dates on which the options were exercised during the current period was £13.40.

Prudential International Assurance sharesave plan

		Exercise period		Number of shares under option						
Date of grant	Exercise price £	Beginning	End	Beginning of period	Granted	Exercised	Cancelled	Forfeited	Lapsed	End of period
27 Apr 09	2.88	01 Jun 14	30 Nov 14	6,567	–	(5,774)	–	–	(793)	–
				6,567	–	(5,774)	–	–	(793)	–

The total number of securities available for issue under the scheme is nil at 30 June 2014.

The weighted average closing price of the shares immediately before the dates on which the options were exercised during the current period was £13.70.

Non-employee savings-related share option scheme

		Exercise period		Number of shares under options						
Date of grant	Exercise price £	Beginning	End	Beginning of period	Granted	Exercised	Cancelled	Forfeited	Lapsed	End of period
25 Apr 08	5.51	01 Jun 13	30 Nov 13	1,997	–	–	–	–	(1,997)	–
25 Sep 08	4.38	01 Dec 13	31 May 14	9,186	–	(4,798)	–	–	(2,409)	1,979
27 Apr 09	2.88	01 Jun 12	30 Nov 12	27,532	–	–	–	–	–	27,532
27 Apr 09	2.88	01 Jun 14	30 Nov 14	686,366	–	(472,463)	–	–	–	213,903
25 Sep 09	4.25	01 Dec 14	31 May 15	11,717	–	–	–	–	–	11,717
28 Sep 10	4.61	01 Dec 13	31 May 14	341,803	–	(332,969)	–	–	–	8,834
28 Sep 10	4.61	01 Dec 15	31 May 16	362,214	–	–	–	(391)	–	361,823
16 Sep 11	4.66	01 Dec 14	31 May 15	600,918	–	–	–	(8,049)	–	592,869
16 Sep 11	4.66	01 Dec 16	31 May 17	257,774	–	–	–	–	–	257,774
21 Sep 12	6.29	01 Dec 15	31 May 16	438,307	–	–	(1,431)	–	–	436,876
21 Sep 12	6.29	01 Dec 17	31 May 18	90,289	–	–	–	–	–	90,289
20 Sep 13	9.01	01 Dec 16	31 May 17	777,462	–	–	(4,910)	(1,197)	–	771,355
20 Sep 13	9.01	01 Dec 18	31 May 19	424,941	–	–	–	–	–	424,941
				4,030,506	–	(810,230)	(6,341)	(9,637)	(4,406)	3,199,892

The total number of securities available for issue under the scheme is 3,199,892 which represents 0.125 per cent of the issued share capital at 30 June 2014.

The weighted average closing price of the shares immediately before the dates on which the options were exercised during the current period was £13.67.

VII: Foreign currency source of key metrics

The tables below show the Group's key free surplus, IFRS and EEV metrics analysis by contribution by currency group:

Free surplus and IFRS half year 2014 results

	Underlying free surplus generated note 2 %	Pre-tax operating profit notes 3, 4, 5 %	Shareholders' funds notes 3, 4, 5 %
US$ linked note 1	11	17	13
Other Asia currencies	14	17	18
Total Asia	25	34	31
UK sterling notes 3,4	38	21	50
US$ note 4	37	45	19
Total	100	100	100

EEV half year 2014 results

	Post-tax new business profits %	Post-tax operating profit notes 3, 4, 5 %	Shareholders' funds notes 3, 4, 5 %
US$ linked note 1	30	27	28
Other Asia currencies	19	18	15
Total Asia	49	45	43
UK sterling notes 3,4	14	15	37
US$ note 4	37	40	20
Total	100	100	100

Notes

1 US$ linked – comprising the Hong Kong and Vietnam operations where the currencies are pegged to the US dollar and the Malaysia and Singapore operations where the currencies are managed against a basket of currencies including the US dollar.
2 Underlying free surplus generated comprises long-term business (net of investment in new business), asset management and other businesses.
3 Includes long-term, asset management business and other businesses.
4 For operating profit and shareholders' funds UK sterling includes amounts in respect of central operations as well as UK insurance operations and M&G.
5 For shareholders' funds, the US$ grouping includes US$ denominated core structural borrowings. Sterling operating profits include all interest payable as sterling denominated, reflecting interest rate currency swaps in place.

Risk factors

A number of factors (risk factors) affect Prudential's operating results and financial condition and, accordingly, the trading price of its shares. The risk factors mentioned below should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. The information given is as of the date of this document, is not updated, and any forward-looking statements are made subject to the reservations specified below under 'Forward-looking statements'.

Prudential's approaches to managing risks are explained in the 'Group Chief Risk Officer's summary of the risks facing our business and our capital strength' section of this document.

Risks relating to Prudential's business

Prudential's businesses are inherently subject to market fluctuations and general economic conditions

Prudential's businesses are inherently subject to market fluctuations and general economic conditions. Uncertainty or negative trends in international economic and investment climates could adversely affect Prudential's business and profitability. Since 2008 Prudential has operated against a challenging background of periods of significant volatility in global capital and equity markets, interest rates and liquidity, and widespread economic uncertainty. Government interest rates also remain at or near historic lows in the US, the UK and some Asian countries in which Prudential operates. These factors have, at times during this period, had a material adverse effect on Prudential's business and profitability.

In the future, the adverse effects of such factors would be felt principally through the following items:

- Investment impairments or reduced investment returns, which could impair Prudential's ability to write significant volumes of new business and would have a negative impact on its assets under management and profit;
- Higher credit defaults and wider credit and liquidity spreads resulting in realised and unrealised credit losses;
- Failure of counterparties to transactions with Prudential or, for derivative transactions adequate collateral not being in place;
- Estimates of the value of financial instruments being difficult because in certain illiquid or closed markets, determining the value at which financial instruments can be realised is highly subjective. Processes to ascertain such values require substantial elements of judgement, assumptions and estimates (which may change over time); and
- Increased illiquidity also adds to uncertainty over the accessibility of financial resources and may reduce capital resources as valuations decline.

Global financial markets are subject to uncertainty and volatility created by a variety of factors, including concerns over sovereign debt, general slowing in world growth from subdued or slowdown in demand and the timing and scale of quantitative easing programmes of central banks. Upheavals in the financial markets may affect general levels of economic activity, employment and customer behaviour. For example, insurers may experience an elevated incidence of claims, lapses, or surrenders of policies, and some policyholders may choose to defer or stop paying insurance premiums. The demand for insurance products may also be adversely affected. If sustained, this environment is likely to have a negative impact on the insurance sector over time and may consequently have a negative impact on Prudential's business and profitability. New challenges related to market fluctuations and general economic conditions may continue to emerge.

For some non-unit-linked investment products, in particular those written in some of the Group's Asian operations, it may not be possible to hold assets which will provide cash flows to match those relating to policyholder liabilities. This is particularly true in those countries where bond markets are not developed and in certain markets where regulated surrender values are set with reference to the interest rate environment prevailing at the time of policy issue. This results in a mismatch due to the duration and uncertainty of the liability cash flows and the lack of sufficient assets of a suitable duration. While this residual asset/liability mismatch risk can be managed, it cannot be eliminated. Where interest rates in these markets remain lower than interest rates used to calculate surrender values over a sustained period, this could have an adverse impact on Prudential's reported profit.

In the US, fluctuations in prevailing interest rates can affect results from Jackson which has a significant spread based business, with the majority of its assets invested in fixed income securities. In particular, fixed annuities and stable value products written by Jackson expose Prudential to the risk that changes in interest rates, which are not fully reflected in the interest rates credited to customers, will reduce spread. The spread is the difference between the rate of return Jackson is able to earn on the assets backing the policyholders' liabilities and the amounts that are credited to policyholders in the form of benefit increases, subject to minimum crediting rates. Declines in spread from these products or other spread businesses that Jackson conducts, and increases in surrenders levels arising from interest rate rises, could have a material impact on its businesses or results of operations.

Jackson also writes a significant amount of variable annuities that offer capital or income protection guarantees. The value of these guarantees is affected by market factors including interest rates, equity levels, bond spreads and realised volatility. There could be market circumstances where the derivatives that Jackson enters into to hedge its market risks may not fully cover its exposures under the guarantees. The cost of the guarantees that remain unhedged will also affect Prudential's results.

Jackson hedges the guarantees on its variable annuity book on an economic basis and, thus, accepts variability in its accounting results in the short term in order to achieve the appropriate economic result. In particular, for Prudential's Group IFRS reporting, the measurement of the Jackson variable annuity guarantees is typically less sensitive to market movements than for the corresponding hedging derivatives, which are held at market value. However, depending on the level of hedging conducted regarding a particular risk type, certain market movements can drive volatility in the economic results which may be less significant under IFRS reporting.

A significant part of the profit from Prudential's UK insurance operations is related to bonuses for policyholders declared on with-profits products, which are broadly based on historical and current rates of return on equity, real estate and fixed income securities, as well as Prudential's expectations of future investment returns. This profit could be lower in a sustained low interest rate environment.

Prudential is subject to the risk of potential sovereign debt credit deterioration owing to the amounts of sovereign debt obligations held in its investment portfolio

Prudential is subject to the risk of potential sovereign debt credit deterioration on the amounts of sovereign debt obligations held in its investment portfolio. In recent years, rating agencies have downgraded the sovereign debt of some countries. There is a risk of further downgrades.

Investing in sovereign debt creates exposure to the direct or indirect consequences of political, social or economic changes (including changes in governments, heads of states or monarchs) in the countries in which the issuers are located and the creditworthiness of the sovereign. Investment in sovereign debt obligations involves risks not present in debt obligations of corporate issuers. In addition, the issuer of the debt or the governmental authorities that control the repayment of the debt may be unable or unwilling to repay principal or pay interest when due in accordance with the terms of such debt, and Prudential may have limited recourse to compel payment in the event of a default. A sovereign debtor's willingness or ability to repay principal and to pay interest in a timely manner may be affected by, among other factors, its cash flow situation, its relations with its central bank, the extent of its foreign currency reserves, the availability of sufficient foreign exchange on the date a payment is due, the relative size of the debt service burden to the economy as a whole, the sovereign debtor's policy toward local and international lenders, and the political constraints to which the sovereign debtor may be subject.

Moreover, governments may use a variety of techniques, such as intervention by their central banks or imposition of regulatory controls or taxes, to devalue their currencies' exchange rates, or may adopt monetary and other policies (including to manage their debt burdens) that have a similar effect, all of which could adversely impact the value of an investment in sovereign debt even in the absence of a technical default. Periods of economic uncertainty may affect the volatility of market prices of sovereign debt to a greater extent than the volatility inherent in debt obligations of other types of issuers.

In addition, if a sovereign default or other such events described above were to occur, other financial institutions may also suffer losses or experience solvency or other concerns, and Prudential might face additional risks relating to any debt of such financial institutions held in its investment portfolio. There is also risk that public perceptions about the stability and creditworthiness of financial institutions and the financial sector generally might be affected, as might counterparty relationships between financial institutions. If a sovereign were to default on its obligations, or adopt policies that devalue or otherwise alter the currencies in which its obligations are denominated this could have a material adverse effect on Prudential's financial condition and results of operations.

Prudential is subject to the risk of exchange rate fluctuations owing to the geographical diversity of its businesses

Due to the geographical diversity of Prudential's businesses, Prudential is subject to the risk of exchange rate fluctuations. Prudential's operations in the US and Asia, which represent a significant proportion of operating profit based on longer-term investment returns and shareholders' funds, generally write policies and invest in assets denominated in local currencies. Although this practice limits the effect of exchange rate fluctuations on local operating results, it can lead to significant fluctuations in Prudential's consolidated financial statements upon translation of results into pounds sterling. This exposure is not currently separately managed. The currency exposure relating to the translation of reported earnings could impact on financial reporting ratios such as dividend cover, which is calculated as operating profit after tax on an IFRS basis, divided by the current year interim dividend plus the proposed final dividend. The impact of gains or losses on currency translations is recorded as a component of shareholders' funds within other comprehensive income. Consequently, this could impact on Prudential's gearing ratios (defined as debt over debt plus shareholders' funds). The Group's surplus capital position for regulatory reporting purposes may also be affected by fluctuations in exchange rates.

Prudential conducts its businesses subject to regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies and interpretations and any accounting standards in the markets in which it operates

Changes in government policy, legislation (including tax) or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which Prudential operates, which in some circumstances may be applied retrospectively, may adversely affect Prudential's product range, distribution channels, profitability, capital requirements and, consequently, reported results and financing requirements. Also, regulators in jurisdictions in which Prudential operates may change the level of capital required to be held by individual businesses or could introduce possible changes in the regulatory framework for pension arrangements and policies, the regulation of selling practices and solvency requirements. Furthermore, as a result of interventions by governments in response to recent financial and global economic conditions, it is widely expected that there will continue to be a substantial increase in government regulation and supervision of the financial services industry, including the possibility of higher capital requirements, restrictions on certain types of transaction structure and enhanced supervisory powers.

Current EU directives, including the EU Insurance Groups Directive (IGD) require EU financial services groups to demonstrate net aggregate surplus capital in excess of solvency requirements at the group level in respect of shareholder owned entities. The test is a continuous requirement, so that Prudential needs to maintain a higher amount of regulatory capital at the group level than otherwise necessary in respect of some of its individual businesses to accommodate, for example, short-term movements in global foreign exchange rates, interest rates, deterioration in credit quality and equity markets. The EU is also developing a new prudential regulatory framework for insurance companies, referred to as 'Solvency II'. The approach is based on the concept of three pillars. Pillar 1 consists of the quantitative requirements, for example, the amount of capital an insurer should hold. Pillar 2 sets out requirements for the governance and risk management of insurers, as well as for the effective supervision of insurers. Pillar 3 focuses on disclosure and transparency requirements.

The Solvency II Directive covers valuation, the treatment of insurance groups, the definition of capital and the overall level of capital requirements. A key aspect of Solvency II is that the assessment of risks and capital requirements are intended to be aligned more closely with economic capital methodologies, and may allow Prudential to make use of its internal economic capital models, if approved by the Prudential Regulation Authority (PRA). The Solvency II Directive was formally approved by the Economic and Financial Affairs Council in November 2009 although its implementation was delayed pending agreement on a directive known as Omnibus II which amended certain aspects of the Solvency II Directive. Following adoption of the Omnibus II Directive by the Council of the European Union in April 2014, Solvency II is now expected to be implemented as of 1 January 2016, although the European Commission and the European Insurance and Occupational Pensions Authority (EIOPA) are continuing to develop the detailed rules that will supplement the high-level rules and principles of the Solvency II and Omnibus II Directives, which are not currently expected to be finalised until mid-2015. Further, the effective application of a number of key measures incorporated in the Omnibus II Directive, including the provisions for third-country equivalence, is expected to be subject to supervisory judgement and approval. As a result there is a risk that the

Risk factors continued

effect of the measures finally adopted could be adverse for Prudential, including potentially a significant increase in the capital required to support its business and that Prudential may be placed at a competitive disadvantage to other European and non-European financial services groups.

Currently there are also a number of other global regulatory developments which could impact the way in which Prudential is supervised in its many jurisdictions. These include the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) in the US, the work of the Financial Stability Board (FSB) on Global Systemically Important Insurers (G-SIIs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) being developed by the International Association of Insurance Supervisors (IAIS).

The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry within the United States that, among other reforms to financial services entities, products and markets, may subject financial institutions designated as systemically important to heightened prudential and other requirements intended to prevent or mitigate the impact of future disruptions in the US financial system. The full impact of the Dodd-Frank Act on Prudential's businesses is not currently clear, as many of its provisions have a delayed effectiveness and/or require rulemaking or other actions by various US regulators over the coming years.

In July 2013 the FSB announced the initial list of nine insurance groups that have been designated as G-SIIs. This list included Prudential as well as a number of its competitors. Designation as a G-SII will lead to additional policy measures being applied to the designated group. Based on the policy framework released by the IAIS and subsequent guidance papers these additional policy measures will include enhanced group-wide supervision, effective resolution measures of the group in the event of failure, loss absorption, and higher loss absorption capacity. This enhanced supervision commenced immediately and includes the development by July 2014 of a Systemic Risk Management Plan (SRMP) under supervisory oversight and its implementation thereafter and by the end of 2014, a group Recovery and Resolution Plan (RRP) and Liquidity Risk Management Plan (LRMP). Prudential is monitoring the development, and potential impact of, the framework of policy measures and is engaging with the PRA on the implications of the policy measures and Prudential's designation as a G-SII. The G-SII regime also introduces two types of capital requirements; the first, a Basic Capital Requirement (BCR), designed to act as a minimum group capital requirement and the second, a Higher Loss Absorption (HLA) requirement for conducting non-traditional insurance and non-insurance activities. A consultation paper on BCR was released in July 2014.The IAIS currently expects to finalise the BCR and HLA proposals by November 2014 and the end of 2015 respectively. Implementation of the regime is likely to be phased in over a period of years with the BCR expected to be introduced in 2015 on a confidential reporting basis to group-wide supervisors. The HLA requirement will apply from January 2019 to the insurance groups identified as G-SIIs in November 2017.

ComFrame is also being developed by the IAIS to provide common global requirements for the supervision of insurance groups. The framework is designed to outline a set of common global principles and standards for group supervision and may increase the focus of regulators in some jurisdictions. One of the framework's key components is an Insurance Capital Standard (ICS) which would form the group solvency capital standard under ComFrame. In May 2014 the IAIS published a memorandum setting out the approach to the development of the ICS. The three-year development phase of ComFrame ended in December 2013 and the IAIS is now undertaking a field testing exercise from 2014 to 2018 to assess the impact of the quantitative and qualitative requirements proposed under ComFrame. ComFrame is expected to be implemented in 2019.

Various jurisdictions in which Prudential operates have created investor compensation schemes that require mandatory contributions from market participants in some instances in the event of a failure of a market participant. As a major participant in the majority of its chosen markets, circumstances could arise where Prudential, along with other companies, may be required to make such contributions.

The Group's accounts are prepared in accordance with current International Financial Reporting Standards (IFRS) applicable to the insurance industry. The International Accounting Standards Board (IASB) introduced a framework that it described as Phase I, which permitted insurers to continue to use the statutory basis of accounting for insurance assets and liabilities that existed in their jurisdictions prior to January 2005. In July 2010, the IASB published its first Exposure Draft for its Phase II on insurance accounting, which would introduce significant changes to the statutory reporting of insurance entities that prepare accounts according to IFRS. A revised Exposure Draft was issued in June 2013. The IASB is re-deliberating on the Exposure Draft proposals in light of comments by the insurance industry and other respondents. The timing of the final proposals taking effect is uncertain but not expected to be before 2018.

Any changes or modification of IFRS accounting policies may require a change in the future results or a retrospective adjustment of reported results.

The resolution of several issues affecting the financial services industry could have a negative impact on Prudential's reported results or on its relations with current and potential customers

Prudential is, and in the future may be, subject to legal and regulatory actions in the ordinary course of its business, both in the UK and internationally. These actions could involve a review of types of business sold in the past under acceptable market practices at the time, such as the requirement in the UK to provide redress to certain past purchasers of pension and mortgage endowment policies, changes to the tax regime affecting products, and regulatory reviews on products sold and industry practices, including, in the latter case, lines of business it has closed.

Regulators' interest may include the approach that product providers use to select third-party distributors and to monitor the appropriateness of sales made by them. In some cases, product providers can be held responsible for the deficiencies of third-party distributors.

In the US, there has been significant regulatory attention on the different regulatory standards applied to investment advice delivered to retail customers by different sectors of the industry. This focus includes new regulations in respect of the suitability of sales of certain products such as alternative investments. As a result of publicity relating to widespread perceptions of industry abuses, there have been numerous regulatory inquiries and proposals for legislative and regulatory reforms.

In Asia, regulatory regimes are developing at different speeds, driven by a combination of global factors and local considerations. There is a risk that new requirements are introduced that challenge current practices, or are retrospectively applied to sales made prior to their introduction.

Litigation, disputes and regulatory investigations may adversely affect Prudential's profitability and financial condition

Prudential is, and may be in the future, subject to legal actions, disputes and regulatory investigations in various contexts, including in the ordinary course of its insurance, investment management and other business operations. These legal actions, disputes and investigations may relate to aspects of Prudential's businesses and operations that are specific to Prudential, or that are common to companies that operate in Prudential's markets. Legal actions and disputes may arise under contracts, regulations (including tax) or from a course of conduct taken by Prudential, and may be class actions. Although Prudential believes that it has adequately provided in all material aspects for the costs of litigation and regulatory matters, no assurance can be provided that such provisions are sufficient. Given the large or indeterminate amounts of damages sometimes sought, other sanctions that might be applicable and the inherent unpredictability of litigation and disputes, it is possible that an adverse outcome could, from time to time, have an adverse effect on Prudential's reputation, results of operations or cash flows.

Prudential's businesses are conducted in highly competitive environments with developing demographic trends and continued profitability depends on management's ability to respond to these pressures and trends

The markets for financial services in the UK, US and Asia are highly competitive, with several factors affecting Prudential's ability to sell its products and continued profitability, including price and yields offered, financial strength and ratings, range of product lines and product quality, brand strength and name recognition, investment management performance, historical bonus levels, developing demographic trends and customer appetite for certain savings products. In some of its markets, Prudential faces competitors that are larger, have greater financial resources or a greater market share, offer a broader range of products or have higher bonus rates or claims paying ratios. Further, heightened competition for talented and skilled employees and agents with local experience, particularly in Asia, may limit Prudential's potential to grow its business as quickly as planned.

In Asia, the Group's principal competitors in the region are international financial companies, including global life insurers such as Allianz, AXA, AIA, and Manulife and multinational asset managers such as J.P. Morgan Asset Management, Schroders, HSBC Global Asset Management and Franklin Templeton. In a number of markets, local companies have a very significant market presence.

Within the UK, Prudential's principal competitors include many of the major retail financial services companies and fund management companies including, in particular, Aviva, Legal & General, Lloyds Banking Group, Standard Life, Schroders, Invesco Perpetual and Fidelity.

Jackson's competitors in the US include major stock and mutual insurance companies, mutual fund organisations, banks and other financial services companies such as AIG, AXA Financial Inc., Hartford Life Inc., Prudential Financial, Lincoln National, MetLife and TIAA-CREF.

Prudential believes competition will intensify across all regions in response to consumer demand, technological advances, the impact of consolidation, regulatory actions and other factors. Prudential's ability to generate an appropriate return depends significantly upon its capacity to anticipate and respond appropriately to these competitive pressures.

Downgrades in Prudential's financial strength and credit ratings could significantly impact its competitive position and damage its relationships with creditors or trading counterparties

Prudential's financial strength and credit ratings, which are used by the market to measure its ability to meet policyholder obligations, are an important factor affecting public confidence in Prudential's products, and as a result its competitiveness. Downgrades in Prudential's ratings, as a result of, for example, decreased profitability, increased costs, increased indebtedness or other concerns, could have an adverse effect on its ability to market products; retain current policyholders; and on the Group's financial flexibility. In addition, the interest rates Prudential pays on its borrowings are affected by its credit ratings, which are in place to measure the Group's ability to meet its contractual obligations.

Prudential's long-term senior debt is rated as A2 by Moody's, A+ by Standard & Poor's and A by Fitch. These ratings have a stable outlook.

Prudential's short-term debt is rated as P-1 by Moody's, A-1 by Standard & Poor's and F1 by Fitch.

The Prudential Assurance Company Limited's financial strength is rated Aa2 (negative outlook) by Moody's, AA (stable outlook) by Standard & Poor's and AA (stable outlook) by Fitch.

Jackson's financial strength is rated AA by Standard & Poor's and Fitch, A1 by Moody's, and A+ by AM Best. These ratings have a stable outlook.

Prudential Assurance Co. Singapore (Pte) Ltd's financial strength is rated AA (stable outlook) by Standard & Poor's.

In addition, changes in methodologies and criteria used by rating agencies could result in downgrades that do not reflect changes in the general economic conditions or Prudential's financial condition.

Adverse experience in the operational risks inherent in Prudential's business could have a negative impact on its results of operations

Operational risks are present in all of Prudential's businesses, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, systems and human error or from external events. Prudential's business is dependent on processing a large number of transactions across numerous and diverse products, and is subject to a number of different legal and regulatory regimes. Further, because of the long-term nature of much of the Group's business, accurate records have to be maintained for significant periods.

These factors, among others, result in significant reliance on and require significant investment in IT, compliance and other operational systems, personnel and processes. In addition, Prudential outsources several operations, including a significant part of its UK back office and customer facing functions as well as a number of IT functions, resulting in reliance upon the operational processing performance of its outsourcing partners.

Although Prudential's IT, compliance and other operational systems and processes incorporate controls designed to manage and mitigate the operational risks associated with its activities, there can be no assurance that such controls will always be effective. For example, although Prudential has not experienced a material failure or breach in relation to its legacy and other IT systems and processes to date, it has been, and likely will continue to be, subject to computer viruses, attempts at unauthorised access and cyber-security attacks.

Prudential's legacy and other IT systems and processes, as with operational systems and processes generally, may be susceptible to failure or breaches. Such events could, among other things, harm Prudential's ability to perform necessary business functions, result in the loss of confidential or proprietary data (exposing it to potential legal claims and regulatory sanctions) and damage its relationships with its business partners and customers. Similarly, any weakness in the administration systems or actuarial reserving processes could have an impact on its results of operations during the effective period.

Risk factors continued

Prudential has not experienced or identified any operational risks in its systems or processes during the first half of 2014, which have subsequently caused, or are expected to cause, a significant negative impact on its results of operations.

Adverse experience relative to the assumptions used in pricing products and reporting business results could significantly affect Prudential's results of operations

Prudential needs to make assumptions about a number of factors in determining the pricing of its products, setting reserves, for reporting its capital levels and the results of its long-term business operations. For example, the assumption that Prudential makes about future expected levels of mortality is particularly relevant for its UK annuity business. In exchange for a premium equal to the capital value of their accumulated pension fund, pension annuity policyholders receive a guaranteed payment, usually monthly, for as long as they are alive. Prudential conducts rigorous research into longevity risk, using data from its substantial annuitant portfolio. As part of its pension annuity pricing and reserving policy, Prudential's UK business assumes that current rates of mortality continuously improve over time at levels based on adjusted data and models from the Continuous Mortality Investigations (CMI) as published by the Institute and Faculty of Actuaries. If mortality improvement rates significantly exceed the improvement assumed, Prudential's results of operations could be adversely affected.

A further example is the assumption that Prudential makes about future expected levels of the rates of early termination of products by its customers (persistency). This is particularly relevant to its lines of business other than its UK annuity business. Prudential's persistency assumptions reflect recent past experience for each relevant line of business. Any expected deterioration in future persistency is also reflected in the assumption. If actual levels of future persistency are significantly lower than assumed (that is, policy termination rates are significantly higher than assumed), the Group's results of operations could be adversely affected.

Another example is the impact of epidemics and other effects that cause a large number of deaths. Significant influenza epidemics have occurred three times in the last century, but the likelihood, timing, or the severity of future epidemics cannot be predicted. The effectiveness of external parties, including governmental and non-governmental organisations, in combating the spread and severity of any epidemics could have a material impact on the Group's loss experience.

In common with other life insurers, the profitability of the Group's businesses depends on a mix of factors including mortality and morbidity levels and trends, policy surrender rates, investment performance and impairments, unit cost of administration and new business acquisition expense.

As a holding company, Prudential is dependent upon its subsidiaries to cover operating expenses and dividend payments

The Group's insurance and investment management operations are generally conducted through direct and indirect subsidiaries.

As a holding company, Prudential's principal sources of funds are remittances from subsidiaries, shareholder-backed funds, the shareholder transfer from long-term funds and any amounts that may be raised through the issuance of equity, debt and commercial paper.

Certain of the subsidiaries are restricted by applicable insurance, foreign exchange and tax laws, rules and regulations that can limit remittances. In some circumstances, this could limit the ability to pay dividends to shareholders or to make available funds held in certain subsidiaries to cover operating expenses of other members of the Group.

Prudential operates in a number of markets through joint ventures and other arrangements with third parties (including in China and India), involving certain risks that Prudential does not face with respect to its consolidated subsidiaries

Prudential operates, and in certain markets is required by local regulation to operate, through joint ventures (including in China and India). For the Group's joint venture operations, management control is exercised jointly with the venture participants. The level of control exercisable by the Group depends on the terms of the joint venture agreements, in particular, the allocation of control among, and continued co-operation between, the joint venture participants. Prudential may face financial, reputational and other exposure (including regulatory censure) in the event that any of its joint venture partners fails to meet its obligations under the joint venture, encounters financial difficulty, or fails to comply with local regulation or international standards such as those for the prevention of financial crime. In addition, a significant proportion of the Group's product distribution is carried out through arrangements with third parties not controlled by Prudential and is dependent upon continuation of these relationships. A temporary or permanent disruption to these distribution arrangements or material failure in controls (such as those for the prevention of financial crime) could adversely affect the results of operations of Prudential.

Prudential's Articles of Association contain an exclusive jurisdiction provision

Under Prudential's Articles of Association, certain legal proceedings may only be brought in the courts of England and Wales. This applies to legal proceedings by a shareholder (in its capacity as such) against Prudential and/or its directors and/or its professional service providers. It also applies to legal proceedings between Prudential and its directors and/or Prudential and Prudential's professional service providers that arise in connection with legal proceedings between the shareholder and such professional service provider. This provision could make it difficult for US and other non-UK shareholders to enforce their shareholder rights.

Changes in tax legislation may result in adverse tax consequences

Tax rules, including those relating to the insurance industry, and their interpretation, may change, possibly with retrospective effect, in any of the jurisdictions in which Prudential operates. Significant tax disputes with tax authorities, and any change in the tax status of any member of the Group or in taxation legislation or its scope or interpretation could affect Prudential's financial condition and results of operations.

Corporate governance

Hong Kong listing obligations

The directors confirm that Prudential has complied with all relevant provisions set out in the Corporate Governance Code issued by the Hong Kong Stock Exchange (HK Code) throughout the accounting period. With respect to the Code Provision B.1.2(d) of the HK Code, the responsibilities of the Remuneration Committee do not include making recommendations to the Board on the remuneration of non-executive directors. In line with the principles of the UK Corporate Governance Code, fees for the non-executive directors are determined by the Board.

The directors also confirm that the financial results contained in this document have been reviewed by the Group Audit Committee.

The Company confirms that it has adopted a code of conduct regarding securities transactions by directors on terms no less exacting than required by the Hong Kong Listing Rules and that the directors of the Company have complied with this code of conduct throughout the period.

Going concern

After making enquiries, the directors have a reasonable expectation that the Company and the Group have adequate resources to continue their operations for the foreseeable future and therefore consider it appropriate to continue to adopt the going concern basis of accounting in preparing the financial statements.

The UK's Financial Reporting Council (FRC) has published guidance concerning directors' considerations of the company as a going concern, in particular the guidance pertaining to half year statements. The directors have addressed all relevant procedures and considerations as outlined in the FRC's guidance document.

The Company's business activities, together with the factors likely to affect its future development, successful performance and position in the current economic climate are set out in the Business Performance section.

In this context, the directors have considered liquidity risk, capital and related sensitivities, which are discussed in the Group Chief Risk Officer's summary of the risks facing our business and our capital strength. Specifically, in making their going concern assessment, the directors have considered:

- The Group capital position;
- The Group's capital commitments;
- The liquidity profile of the Group's assets and liabilities;
- The maturity profile of the Group's core and operational borrowings;
- Various liquidity stress scenarios; and
- The capital and liquidity positions of its subsidiaries.

The Group's IFRS financial statements include cash flow details in the 'Condensed consolidated statement of cash flows' and borrowings information in note C6.

Significant shareholdings

The following notifications have been disclosed under the FCA's Disclosure and Transparency Rules in respect of notifiable interests exceeding 3 per cent in the voting rights of the issued share capital.

At 30 June 2014	% of total voting rights
Capital Group Companies, Inc.	10.12%
BlackRock, Inc	5.08%
Norges Bank	4.03%

No further notifications have been received since 30 June 2014 up to the date of this report.

Disclosure of interests of directors

Outstanding share options

The following table sets out the share options held by the directors in the UK Savings-Related Share Option Scheme (SAYE) as at the end of the period. No other directors participated in any other option scheme.

	Date of grant	Exercise price (pence)	Market price at 30 Jun 2014 (pence)	Exercise period		Number of options						
				Beginning	End	Beginning of period	Granted	Exercised	Cancelled	Forfeited	Lapsed	End of period
Nic Nicandrou	16 Sep 11	466	1,341	1 Dec 16	31 May 17	3,268	–	–	–	–	–	3,268
Tidjane Thiam	16 Sep 11	466	1,341	1 Dec 14	29 May 15	965	–	–	–	–	–	965
Tidjane Thiam	20 Sep 13	901	1,341	1 Dec 16	31 May 17	499	–	–	–	–	–	499

Directors' shareholdings

The Company and its directors, chief executives and shareholders have been granted a partial exemption from the disclosure requirements under Part XV of the SFO. As a result of this exemption, directors, chief executives and shareholders do not have an obligation under the SFO to notify the Company of shareholding interests, and the Company is not required to maintain a register of directors' and chief executives' interests under section 352 of the SFO, nor a register of interests of substantial shareholders under section 336 of the SFO. The Company is, however, required to file with the Hong Kong Stock Exchange any disclosure of interests notified to it in the United Kingdom.

The following table sets out the interests of directors, including the interests of persons connected with directors for the purposes of DTR 3.1.2 of the Disclosure and Transparency Rules, as at the end of the period. This includes shares acquired under the Share Incentive Plan and deferred annual bonus awards as detailed in the table on 'Other share awards' on page 174.

	1 Jan 2014	30 Jun 2014		
	Total beneficial interest (number of shares)	Total beneficial interest (number of shares)	Number of shares subject to performance conditions	Total interest in shares (number of shares)
Chairman				
Paul Manduca	42,500	42,500	–	42,500
Executive directors				
Pierre-Olivier Bouée[1]	n/a	81,284	200,418	281,702
John Foley[2]	240,047	n/a	n/a	n/a
Jackie Hunt	36,360	86,492	326,125	412,617
Michael McLintock	453,820	442,532	138,253	580,785
Nic Nicandrou	302,885	288,771	440,303	729,074
Barry Stowe[3]	401,140	276,858	437,374	714,232
Tidjane Thiam	892,684	688,724	1,198,437	1,887,161
Mike Wells[4]	405,844	441,286	910,936	1,352,222
Non-executive directors				
Howard Davies	8,316	8,456	–	8,456
Ann Godbehere	15,914	15,914	–	15,914
Alistair Johnston	10,000	10,000	–	10,000
Kaikhushru Nargolwala	50,000	50,000	–	50,000
Anthony Nightingale	15,000	30,000	–	30,000
Philip Remnant	4,709	4,709	–	4,709
Alice Schroeder[5]	2,000	2,500	–	2,500
Lord Turnbull	16,624	16,624	–	16,624

Notes

1 Pierre-Olivier Bouée was appointed to the Board on 1 April 2014.
2 John Foley left the Board on 1 April 2014.
3 For the 1 January 2014 figure, Barry Stowe's beneficial interest in shares is made up of 200,570 ADRs (representing 401,140 ordinary shares), (8,513.73 of these ADRs are held within an investment account which secures premium financing for a life assurance policy). For the 30 June 2014 figure, the beneficial interest in shares is made up of 138,429 ADRs (representing 276,858 ordinary shares).
4 For the 1 January 2014 figure, Mike Wells' beneficial interest in shares is made up of 202,922 ADRs (representing 405,844 ordinary shares). For the 30 June 2014 figure, his beneficial interest in shares is made up of 220,643 ADRs (representing 441,286 ordinary shares).
5 For the 1 January figure, Alice Schroeder's beneficial interest in shares is made up of 1,000 ADRs (representing 2,000 ordinary shares). For the 30 June 2014 figure, her beneficial interest in shares is made up of 1,250 ADRs (representing 2,500 ordinary shares).

Directors' outstanding long-term incentive awards

Share-based long-term incentive awards

The section below sets out the outstanding share awards under the Prudential Long Term Incentive Plan, Group Performance Share Plan and the awards made under additional long-term plans for the executive directors with regional responsibilities.

	Plan name	Year of award	Conditional share awards outstanding at 1 Jan 2014 (Number of shares)	Conditional awards in 2014 (Number of shares)	Market price at date of award (pence)	Dividend equivalents on vested shares (Number of shares released)[2]	Rights exercised in 2014	Rights lapsed in 2014	Conditional share awards outstanding at 30 Jun 2014 (Number of shares)	Date of end of performance period
Pierre-Olivier Bouée	GPSP	2011	48,517		733.5	4,971	48,517		–	31 Dec 13
	GPSP	2012	47,079		678				47,079	31 Dec 14
	PLTIP	2013	31,057		1,203				31,057	31 Dec 15
	PLTIP	2014		122,282	1,317				122,282	31 Dec 16
			126,653	122,282		4,971	48,517		200,418	
Jackie Hunt	PLTIP	2013	106,805		1,176		106,805		–	31 Dec 13
	PLTIP	2013	95,585		1,176				95,585	31 Dec 14
	GPSP	2013	118,040		1,176				118,040	31 Dec 15
	PLTIP	2014		112,500	1,317				112,500	31 Dec 16
			320,430	112,500			106,805		326,125	
Michael McLintock	GPSP	2011	48,517		733.5	4,971	48,517		–	31 Dec 13
	GPSP	2012	47,079		678				47,079	31 Dec 14
	PLTIP	2013	46,687		1,203				46,687	31 Dec 15
	PLTIP	2014		44,487	1,317				44,487	31 Dec 16
			142,283	44,487		4,971	48,517		138,253	
Nic Nicandrou	GPSP	2011	152,484		733.5	15,633	152,484		–	31 Dec 13
	GPSP	2012	185,374		678				185,374	31 Dec 14
	PLTIP	2013	122,554		1,203				122,554	31 Dec 15
	PLTIP	2014		132,375	1,317				132,375	31 Dec 16
			460,412	132,375		15,633	152,484		440,303	
Barry Stowe[1]	GPSP	2011	88,270		733.5	9,106	88,270		–	31 Dec 13
	BUPP	2011	88,270		733.5	8,932	86,584	1,686	–	31 Dec 13
	GPSP	2012	95,642		678				95,642	31 Dec 14
	BUPP	2012	95,642		678				95,642	31 Dec 14
	PLTIP	2013	131,266		1,203				131,266	31 Dec 15
	PLTIP	2014		114,824	1,317				114,824	31 Dec 16
			499,090	114,824		18,038	174,854	1,686	437,374	
Tidjane Thiam	GPSP	2011	374,279		733.5	38,374	374,279		–	31 Dec 13
	GPSP	2012	523,103		678				523,103	31 Dec 14
	PLTIP	2013	345,831		1,203				345,831	31 Dec 15
	PLTIP	2014		329,503	1,317				329,503	31 Dec 16
			1,243,213	329,503		38,374	374,279		1,198,437	
Mike Wells[1,3]	JNL PSP	2010	141,000		568.5		113,890		–	31 Dec 13
	GPSP	2011	197,648		733.5	20,400	197,648		–	31 Dec 13
	BUPP	2011	197,648		733.5	20,400	197,648		–	31 Dec 13
	GPSP	2012	199,256		678				199,256	31 Dec 14
	BUPP	2012	199,256		678				199,256	31 Dec 14
	PLTIP	2013	273,470		1,203				273,470	31 Dec 15
	PLTIP	2014		238,954	1,317				238,954	31 Dec 16
			1,208,278	238,954		40,800	509,186		910,936	

Notes

1 The awards for Barry Stowe and Mike Wells were made in ADRs (1 ADR = 2 ordinary shares). The figures in the table are represented in terms of ordinary shares.

2 In 2011, 2012, 2013 and 2014 a DRIP dividend equivalent was accumulated on these awards.

3 The table above reflects the maximum number of shares (150 per cent of the original conditional amount awarded) which could have been subsequently released to Mike Wells under the JNL Performance Share Plan. This maximum number of shares could have been released if stretch performance targets were achieved. For the 2010 award, 121.16 per cent of the original conditional amount awarded was released to Mike Wells.

Disclosure of interests of directors continued

Other share awards

The table below sets out the share awards that have been made to executive directors deferred from annual incentive plan payouts. The number of shares are calculated using the average share price over the three business days prior to the date of grant. For the awards from the 2013 annual incentives, made in 2014, the average share price was 1,288 pence.

	Year of grant	Conditional share awards outstanding at 1 Jan 2014 (Number of shares)	Conditionally awarded in 2014 (Number of shares)	Dividends accumulated in 2014 (Number of shares)[2]	Shares released in 2014 (Number of shares)	Conditional share awards outstanding at 30 Jun 2014 (Number of shares)	Date of end of restricted period	Date of release	Market price at date of award (pence)	Market price at date of vesting or release (pence)
Pierre-Olivier Bouée										
Deferred 2010 Group deferred bonus plan award	2011	12,083			12,083	–	31 Dec 13	31 Mar 14	721.5	1,268.5
Deferred 2011 Group deferred bonus plan award	2012	11,228		189		11,417	31 Dec 14		750	
Deferred 2012 Group deferred bonus plan award	2013	8,106		136		8,242	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		14,667	247		14,914	31 Dec 16		1,317	
		31,417	14,667	572	12,083	34,573				
Jackie Hunt										
Deferred 2013 annual incentive award	2014		29,017	489		29,506	31 Dec 16		1,317	
			29,017	489		29,506				
Michael McLintock										
Deferred 2010 annual incentive award	2011	82,838			82,838	–	31 Dec 13	31 Mar 14	721.5	1,268.5
Deferred 2011 annual incentive award	2012	38,246		645		38,891	31 Dec 14		750	
Deferred 2012 annual incentive award	2013	36,831		621		37,452	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		69,093	1,165		70,258	31 Dec 16		1,317	
		157,915	69,093	2,431	82,838	146,601				
Nic Nicandrou										
Deferred 2010 annual incentive award	2011	51,149			51,149	–	31 Dec 13	31 Mar 14	721.5	1,268.5
Deferred 2011 annual incentive award	2012	46,223		779		47,002	31 Dec 14		750	
Deferred 2012 annual incentive award	2013	39,839		671		40,510	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		34,903	588		35,491	31 Dec 16		1,317	
		137,211	34,903	2,038	51,149	123,003				
Barry Stowe[1]										
Deferred 2010 annual incentive award	2011	59,836			59,836	–	31 Dec 13	31 Mar 14	721.5	1,268.5
Deferred 2011 annual incentive award	2012	53,814		910		54,724	31 Dec 14		750	
Deferred 2012 annual incentive award	2013	38,710		654		39,364	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		30,244	510		30,754	31 Dec 16		1,317	
		152,360	30,244	2,074	59,836	124,842				

	Year of grant	Conditional share awards outstanding at 1 Jan 2014 (Number of shares)	Conditionally awarded in 2014 (Number of shares)	Dividends accumulated in 2014 (Number of shares)[2]	Shares released in 2014 (Number of shares)	Conditional share awards outstanding at 30 Jun 2014 (Number of shares)	Date of end of restricted period	Date of release	Market price at date of award (pence)	Market price at date of vesting or release (pence)
Tidjane Thiam										
Deferred 2010 annual incentive award	2011	235,444			235,444	–	31 Dec 13	31 Mar 14	721.5	1,268.5
Deferred 2011 annual incentive award	2012	107,424		1,811		109,235	31 Dec 14		750	
Deferred 2012 annual incentive award	2013	91,251		1,539		92,790	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		63,847	1,076		64,923	31 Dec 16		1,317	
		434,119	63,847	4,426	235,444	266,948				
Mike Wells[1]										
Deferred 2010 Group deferred bonus plan award	2011	96,536			96,536	–	31 Dec 13	14 Mar 14	721.5	1,346
Deferred 2011 annual incentive award	2012	98,850		1,672		100,522	31 Dec 14		750	
Deferred 2012 annual incentive award	2013	82,460		1,394		83,854	31 Dec 15		1,055	
Deferred 2013 annual incentive award	2014		99,646	1,686		101,332	31 Dec 16		1,317	
		277,846	99,646	4,752	96,536	285,708				

Notes

1 The deferred share awards for Barry Stowe and Mike Wells were made in ADRs (1 ADR = 2 ordinary shares). The figures in the table are represented in terms of ordinary shares.

2 In 2011, 2012, 2013 and 2014 a DRIP dividend equivalent was accumulated on these awards.

Shares acquired under the Share Incentive Plan

The table below provides information about shares purchased under the Share Incentive Plan (SIP) together with matching shares (awarded on a 1:4 basis) and dividend shares.

	Year of initial grant	SIP awards held in trust at 1 Jan 2014 (Number of shares)	Partnership shares accumulated in 2014 (Number of shares)	Matching shares accumulated in 2014 (Number of shares)	Dividend shares accumulated in 2014 (Number of shares)	SIP awards held in trust at 30 Jun 2014 (Number of shares)
Pierre-Olivier Bouée	2014		21	5	–	26
Jackie Hunt	2013	23	56	14	–	93
Michael McLintock	2014		21	5	–	26
Nic Nicandrou	2010	1,064	60	15	19	1,158
Tidjane Thiam	2014		21	5	–	26

Cash-settled long-term incentive awards

This information has been prepared in line with the reporting requirements of the Hong Kong Stock Exchange and sets out executive directors' outstanding share awards and share options. For details of the cash-settled long-term incentive awards held by some executive directors, please see our Annual Report.

Shareholder information

Dividends

2014 interim date	Shareholders registered on the UK and Irish branch register	Shareholders registered on the Hong Kong branch register	Holders of US American Depositary Receipts	Shareholders with ordinary shares standing to the credit of their CDP securities accounts
Ex dividend date	20 August 2014	21 August 2014	20 August 2014	20 August 2014
Record date	22 August 2014	22 August 2014	22 August 2014	22 August 2014
Payment of 2014 interim dividend	25 September 2014	25 September 2014	On or about 3 October 2014	On or about 2 October 2014

Shareholder enquiries

For enquiries about shareholdings, including dividends and lost share certificates, please contact the Company's registrars:

By post:
Equiniti Limited
Aspect House
Spencer Road
Lancing
West Sussex BN99 6DA

By telephone:
Tel 0871 384 2035
Fax 0871 384 2100
Textel 0871 384 2255
(for hard of hearing)

Calls to 0871 numbers are charged at 8p per minute plus network extras. Lines are open from 8.30am to 5.30pm, Monday to Friday. International shareholders tel: +44 (0)121 415 7026

Dividend mandates

Shareholders may have their dividends paid directly to their bank or building society account. If you wish to take advantage of this facility, please call Equiniti Limited (Equiniti) and request a Cash Dividend Mandate form. Alternatively, shareholders may download a form from www.prudential.co.uk/prudential-plc/investors/shareholder_services/forms

Cash dividend alternative

The Company has a Dividend Re-investment Plan (DRIP). Shareholders who have elected for the DRIP will automatically receive shares for all future dividends in respect of which a DRIP alternative is offered. The election may be cancelled at any time by the shareholder. Further details of the DRIP and the timetable are available on the Company's website at www.prudential.co.uk/prudential-plc/investors

Electronic communications

Shareholders are encouraged to elect to receive shareholder documents electronically by registering with Shareview at www.shareview.co.uk This will save on printing and distribution costs, and create environmental benefits. Shareholders who have registered will be sent an email notification whenever shareholder documents are available on the Company's website and a link will be provided to that information. When registering, you will need your shareholder reference number which can be found on your share certificate or proxy form. The option to receive shareholder documents electronically is not available to shareholders holding shares through The Central Depository (Pte) Limited (CDP). Please contact Equiniti if you require any assistance or further information.

Equiniti shareview service

Information on how to manage shareholdings can be found at https://help.shareview.co.uk The pages at this web address provide the following:

- Answers to commonly asked questions regarding shareholder registration;
- Links to downloadable forms, guidance notes and Company history factsheets; and
- A choice of contact methods – via email, telephone or post.

Share dealing services

The Company's Registrars, Equiniti, offer a postal dealing facility for buying and selling Prudential plc ordinary shares; please see the Equiniti address above or telephone 0871 384 2248. They also offer a telephone and internet dealing service, Shareview, which provides a simple and convenient way of selling Prudential plc shares. For telephone sales call 0871 384 2780 between 8.30am and 4.30pm, Monday to Friday, and for internet sales log on to www.shareview.co.uk/dealing

ShareGift

Shareholders who have only a small number of shares, the value of which makes them uneconomic to sell, may wish to consider donating them to ShareGift (registered charity 1052686). The relevant share transfer form may be obtained from our website www.prudential.co.uk/prudential-plc/investors/shareholder_services/forms or from Equiniti. Further information about ShareGift may be obtained on +44 (0)20 7930 3737 or from www.ShareGift.org

There are no implications for capital gains tax purposes (no gain or loss) on gifts of shares to charity and it is also possible to obtain income tax relief.

Irish branch register

The Company operates a branch register for shareholders in Ireland. All enquiries regarding Irish branch register accounts should be directed to Capita Asset Services, Shareholder solutions (Ireland), PO Box 7117, Dublin 2. Telephone: +353 1 553 0050

Hong Kong branch register

The Company operates a branch register for shareholders in Hong Kong. All enquiries regarding Hong Kong branch register accounts should be directed to Computershare Hong Kong Investor Services Limited, 17M Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong. Telephone: +852 2862 8555

Singapore shareholder enquiries

Shareholders who have shares standing to the credit of their securities accounts with CDP in Singapore may refer queries to the CDP at 9 North Buona Vista Drive, #01-19/20, The Metropolis, Singapore 1385884. Telephone: +65 6535 7511. Enquiries regarding shares held in Depository Agent Sub-accounts should be directed to your Depository Agent or broker.

American Depositary Receipts (ADRs)

The Company's ordinary shares are listed on the New York Stock Exchange in the form of American Depositary Shares, evidenced by ADRs and traded under the symbol PUK. Each American Depositary Share represents two ordinary shares. All enquiries regarding ADR holder accounts should be directed to JP Morgan, the authorised depositary bank, at JP Morgan Chase & Co, PO Box 64504, St. Paul, MN 55164-0504, USA. Telephone General +1 800 990 1135 or from outside the US +1 651 453 2128 or log on to www.adr.com

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Media enquiries
www.prudential.co.uk/media/enquiries

How to contact us continued

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Incorporated and registered in England and Wales

Registered office
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London EC4R 0HH
Registered number 1397169

www.prudential.co.uk

Prudential plc is a holding company, subsidiaries of which are authorised and regulated by the Prudential Regulation Authority and the Financial Conduct Authority.

Forward-looking statements
This document may contain 'forward-looking statements' with respect to certain of Prudential's plans and its goals and expectations relating to its future financial condition, performance, results, strategy and objectives. Statements that are not historical facts, including statements about Prudential's beliefs and expectations and including, without limitation, statements containing the words 'may', 'will', 'should', 'continue', 'aims', 'estimates', 'projects', 'believes', 'intends', 'expects', 'plans', 'seeks' and 'anticipates', and words of similar meaning, are forward-looking statements. These statements are based on plans, estimates and projections as at the time they are made, and therefore undue reliance should not be placed on them. By their nature, all forward-looking statements involve risk and uncertainty. A number of important factors could cause Prudential's actual future financial condition or performance or other indicated results to differ materially from those indicated in any forward-looking statement. Such factors include, but are not limited to, future market conditions, including fluctuations in interest rates and exchange rates and the potential for a sustained low-interest rate environment, and the performance of financial markets generally; the policies and actions of regulatory authorities, including, for example, new government initiatives related to the financial crisis and the effect of the European Union's 'Solvency II' requirements on Prudential's capital maintenance requirements; the impact of continuing designation as a Global Systemically Important Insurer or 'G-SII'; the impact of competition, economic growth, inflation, and deflation; experience in particular with regard to mortality and morbidity trends, lapse rates and policy renewal rates; the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; the impact of changes in capital, solvency standards, accounting standards or relevant regulatory frameworks, and tax and other legislation and regulations in the jurisdictions in which Prudential and its affiliates operate; and the impact of legal actions and disputes. These and other important factors may for example result in changes to assumptions used for determining results of operations or re-estimations of reserves for future policy benefits. Further discussion of these and other important factors that could cause Prudential's actual future financial condition or performance or other indicated results to differ, possibly materially, from those anticipated in Prudential's forward-looking statements can be found under the 'Risk factors' heading in this document.

Any forward-looking statements contained in this document speak only as of the date on which they are made. Prudential expressly disclaims any obligation to update any of the forward-looking statements contained in this document or any other forward-looking statements it may make, whether as a result of future events, new information or otherwise except as required pursuant to the UK Prospectus Rules, the UK Listing Rules, the UK Disclosure and Transparency Rules, the Hong Kong Listing Rules, the SGX-ST listing rules or other applicable laws and regulations.

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All material used in this report has been independently certified according to the rules of the Forest Stewardship Council (FSC). All pulps used are elemental chlorine free, and the inks used are vegetable oil based. The manufacturing mills and the printer are registered to the Environmental Management System ISO 14001 and are FSC chain-of-custody certified.

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