Annual statement from the Chairman of the Remuneration Committee

Anthony Nightingale CMG SBS JP
Chairman of the Remuneration Committee

Dear shareholder,
I am pleased to present the Remuneration Committee's report for the year to 31 December 2019.

The Committee's report is presented in the following sections:

1 An 'at a glance' summary of the Group's remuneration arrangements on pages 142 and 143. This includes a summary of the key features of operation of the current Directors' remuneration policy and outlines our proposed changes to the policy for 2020. The current policy was approved by shareholders at the 2017 AGM;

2 Our Annual report on remuneration on pages 144 to 173 which describes how the Committee applied the Directors' remuneration policy in 2019 and the decisions it has made in respect of 2020;

3 Our new Directors' remuneration policy on pages 174 to 191 which describes how we propose paying Directors from 14 May 2020. This will be subject to an ordinary resolution of shareholders at the 2020 AGM; and

4 Supplementary information on pages 192 to 195.

By way of preface, I would like to share the context for the key decisions the Committee took during 2019, in particular, the decisions we took in connection with the demerger, how we rewarded performance achieved during the year, the remuneration arrangements for those stepping down from the Board and the decisions relating to remuneration arrangements in 2020 and the new Directors' remuneration policy. In line with our approach to shareholder engagement and given the above, I corresponded with and met the majority of our major shareholders, as well as organisations that represent and advise shareholders during late 2019 and early 2020. I am pleased to say that we have had the benefit of substantive feedback from 41 per cent of our shareholder register and that the majority of shareholders and advisory bodies who provided input were content with our proposals and commended the manner in which we conducted the consultation process. On behalf of the Committee, I would like to thank the shareholders and advisory bodies for their engagement to date and look forward to continuing this open dialogue into the future.

Further, I am delighted to welcome Amy Yip, who joined the Committee in September 2019.

Demerger-related decisions

The M&G plc business demerged from the Group with effect from 21 October 2019. As I described last year, the Committee established a set of principles to underpin decisions on remuneration relating to the demerger, including:

- Executives should not be advantaged or disadvantaged by the demerger; the value of outstanding awards and their key terms (release dates, holding periods, malus and clawback provisions) should be unaffected;
- Where performance conditions need to be revised, the new conditions should be no more or less stretching than those originally attached to the awards; and
- Where the Committee has applied discretion, this will be disclosed clearly.

These principles were the basis for the decisions taken by the Committee, including the treatment of outstanding share awards which was set out in the Shareholder Circular published on 25 September 2019 and voted upon and approved by shareholders at the October 2019 General Meeting. This treatment, together with adjustments made to the targets of in-flight Prudential Long Term Incentive Plan (PLTIP) awards as a result of the demerger, are detailed in 'Remuneration decisions taken in relation to the demerger' section of this report.

Changes to the executive team

The Company made a number of changes to the senior leadership team of the Group in preparation for the demerger. On 16 May 2019, John Foley, Chief Executive of M&GPrudential, Nic Nicandrou, Chief Executive of Prudential Corporation Asia, and Michael Falcon, Chairman and Chief Executive Officer of Jackson Holdings LLC stepped down as Executive Directors of Prudential plc. They did not receive any loss of office payment in respect of their service as Executive Directors. Details of remuneration earned in respect of their service on the Prudential plc Board is provided in this report. When John Foley left the Group on the demerger of M&G plc, his outstanding PLTIP and deferred bonus awards were exchanged for replacement awards over M&G plc shares of an equivalent value and subject to equivalent malus and clawback provisions, and performance conditions which the Remuneration Committee of M&G plc determined were no more or less onerous than those which originally applied. Mr Foley's 2019 bonus will be assessed and determined by M&G plc Remuneration Committee and will be paid by M&G plc.

In July 2019 Mark FitzPatrick, in addition to his role as Group Chief Financial Officer, became Chief Operating Officer while James Turner, Group Chief Risk Officer, became additionally responsible for the Group Compliance function. Their titles were changed to reflect these new duties.

In August 2019, Mr Turner relocated to Hong Kong to support our dialogue with the Hong Kong Insurance Authority (Hong Kong IA), our Group-wide supervisor from the date of the demerger. The Company supported Mr Turner's relocation and, in order to recognise the expansion of his role and his development since joining the Board, he received an uplift in salary of 9 per cent and an increased bonus opportunity from 160 per cent of base salary to 175 per cent from the date of his move. No changes were made to Mr Turner's long-term incentive award level or to Mr FitzPatrick's 2019 remuneration arrangements.

Key
- Continuing
- Discontinued (M&G plc)
- Continuing
- Continuing operations after hedge modelling changes
- Hedge modelling changes

Rewarding 2019 performance

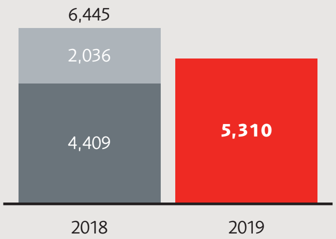
Prudential's executive remuneration arrangements reward the achievement of Group, business, functional and personal targets, provided that this performance is delivered within the Company's risk framework and appetites, and that the conduct expectations of Prudential, our regulators and other stakeholders are met.

As set out in the 'Strategic report' section earlier in this Annual report, the Group delivered results which demonstrate operating earnings growth and the benefits of the diverse portfolio in Asia. These results have been achieved in parallel with the demerger of the M&G plc business. The table below illustrates achievement of KPIs:

Performance measures | *Group performance ($m)*[4] | *2018-2019 growth*[5] | *2019 bonus achievement*[6]

Adjusted operating profit[1]

Prudential's primary measure of profitability and a key driver of shareholder value.



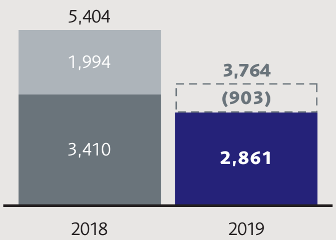
+20%

Above target, approaching stretch target level.

Adjusted operating profit accounted for **35 per cent** of Group financial bonus targets.

Group free surplus generation[2,3]

A measure of the internal cash generation of our business units.



+10%

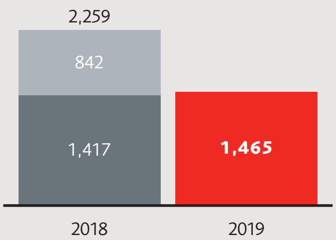
before hedge modelling changes

Above stretch target level.

Group free surplus generation accounted for **30 per cent** of Group financial bonus targets.

Business unit remittances[7]

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



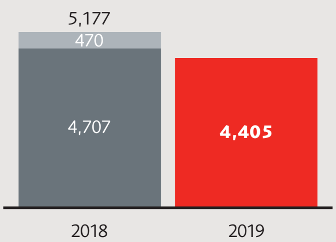
+3%

Above target, approaching stretch target level.

A cash flow measure was used to determine **20 per cent** of the Group financial bonus targets.

EEV new business profit

A measure of the future profitability of the new business sold during the year and indicates the profitable growth of the Group.



-6%

reflecting economic conditions, US product mix changes and Hong Kong protest disruption. PCA ex Hong Kong +29%

Above target, approaching stretch target level.

EEV new business profit accounted for **15 per cent** of Group financial bonus targets.

Notes
1. In this report 'adjusted operating profit' refers to adjusted IFRS operating profit based on longer-term investment returns and are as previously reported.
2. For insurance operations, operating free surplus generated represents amounts maturing from the in-force business during the period less investment in new business and excludes non-operating items. For asset management businesses, it equates to post-tax operating profit for the period. Restructuring costs are presented separately from the underlying business unit amount.
3. Operating free surplus generated before US modelling changes. During 2019, as part of the implementation of the NAIC's changes to the US statutory reserve and capital framework enhancements were made to the model used to determine the cost of hedging for US statutory reporting which have been incorporated into the EEV model, resulting in a fall in operating free surplus of $(903) million from a lower expected transfer to net worth. After allowing for this, operating free surplus generated is $2,861 million, down 16 per cent on a constant and actual exchange rate basis.
4. As reported basis.
5. Growth rates on continuing operations.
6. Executive Directors' bonus awards have been assessed against targets that assumed M&G plc performance up to the date of demerger. Targets and the level of achievement are set out in the 'Annual bonus outcomes for 2019' section of the Annual report on remuneration.
7. Group cash flow includes BU remittances net of dividends and corporate costs.

2019 Adjusted operating profit was 20 per cent higher than prior year on a constant exchange rate basis reflecting the performance outlined in the business performance review, which delivered a result approaching the Board approved stretch targets.

Group EEV new business profit was 6 per cent lower than prior year on a constant exchange rate basis. This reflected the significant reduction in interest rates during the year and the challenging trading environment in Hong Kong in the second half of the year as a direct result of political unrest in the region. Excluding Hong Kong, Asia new business profit was 29 per cent above prior year and given the strong performance of NBP absent the Hong Kong protests, the Committee considered it appropriate to adjust the EEV new business profit target to reflect the reduction in Hong Kong sales driven by the protests, which was considered to be outside of management's control. Allowing for this adjustment, Group EEV new business profit was between target and stretch target.

Group free surplus generation was 10 per cent higher than 2018 on a constant exchange rate basis, excluding the impact of EEV methodology changes outlined in the CFO report (Operating Free Surplus Generation is 16 per cent lower than prior year including the impact of EEV methodology changes). This result was above the Board approved stretch target.

All of our business units achieved target remittance levels, which were 3 per cent higher than 2018 for our continuing operations, enabling us to maintain significant cash stock at the centre, after dividends, corporate costs, demerger effects and investing in profitable opportunities within the business units. The business unit remittances contributed to Group cashflow, which approached the stretch target level.

The Group achieved these results while maintaining appropriate levels of capital and while operating within the Group's risk framework and appetites. The Committee believes that the bonuses it awarded to Executive Directors for 2019 (between 93 per cent and 96 per cent of executives' maximum AIP opportunities) appropriately reflect this performance.

Performance in 2019 has continued to deliver on the momentum achieved in recent years. The Group delivered total adjusted operating profits of $19,021 million in the 2017, 2018 and 2019 financial years. Based on this strong cumulative adjusted operating profit performance over the period and performance against our sustainability scorecard, the Committee determined that between 61.75 and 68.75 per cent of the Prudential Long Term Incentive Plan (PLTIP) awards made to Executive Directors in 2017 would vest (depending on the business unit). These awards will be released to participants from April 2020. The portion of the awards related to Prudential's total shareholder return (TSR) lapsed as TSR performance was ranked below median of the peer group.

The total 2019 remuneration or 'single figure' for the Group Chief Executive, Mike Wells, is 11.25 per cent lower than his total restated 2018 'single figure', notwithstanding his exceptional leadership and personal performance. This chiefly reflects his housing support ending in November 2018 and the impact of the lower value of the 2017 PLTIP vesting compared to the 2016 PLTIP vesting due to lower share price growth over the performance period.

Reviewing the Directors' remuneration policy

Ahead of the renewal of the Directors' remuneration policy at the AGM in 2020, the Committee carefully considered and debated a range of potential remuneration models, taking into account the demerger of the M&G plc business from the Group, the views of our shareholders, the UK Corporate Governance Code and the broader regulatory and competitive environment. The Committee concluded that the current model continues to connect remuneration with the achievement of the Group's ambitious goals to build long-term shareholder value by continuing to focus on achieving sustainable, profitable growth and retaining a resilient balance sheet, with a disciplined approach to active capital allocation. In addition, the Committee decided to retain the key features of the current remuneration model since it is appropriate for a growth company, is well understood and drives the right behaviour and outcomes. On this basis, the Committee decided to retain the current remuneration model while making a number of improvements to ensure that it continues to be aligned with the Group's remuneration principles, business priorities and evolving stakeholder expectations.

The proposed new Directors' remuneration policy set out on pages 174 to 191 has been designed to:

1 Align reward with the strategic priorities and capital framework of the post-demerger business

The Committee intends to align the Prudential Long Term Incentive Plan (PLTIP) performance conditions with the strategic priorities of the post-demerger business by introducing a new a return on equity performance measure, operating return on average shareholders' funds, for the 2020 PLTIP awards, incentivising the efficient use of capital as well as shareholder returns. Using this metric alongside our established metrics of Total Shareholder Return (TSR) and a sustainability scorecard will ensure that the full value of long-term incentive awards is attained only where capital is effectively deployed in a way which creates shareholder returns superior to those delivered by peers while conduct and diversity expectations are met.

The proportion of 2019 long-term incentive awards which will vest for threshold performance was reduced to 20 per cent (from 25 per cent for previous awards). This level of threshold vesting is formalised in the 2020 policy and will apply to all future awards.

The proposed new Directors' remuneration policy seeks to reintroduce a financial element to the bonus for the Group Chief Risk and Compliance Officer from 2020, effectively reverting to a similar approach used until 2015. Specifically, it is proposed that the 2020 bonus for this role is based on 40 per cent functional objectives, 40 per cent Group financial measures and 20 per cent personal measures. This is in line with the current draft of the Hong Kong IA's guideline on the remuneration of key persons in control functions and reflects our view that it is important that this role and other control function staff continue to demonstrate long-term commercial sensitivity and are rewarded in a way which allows the Company to recruit the very best talent to these roles.

Following the Hong Kong IA assuming the role of our Group-wide supervisor, Prudential ceased to be subject to Solvency II capital requirements. It is therefore proposed that the Solvency II underpin under the AIP and the Solvency II capital metric within the PLTIP sustainability scorecard are replaced with measures aligned to the Hong Kong IA capital framework.

2 Strengthen the community of interest between executives and other shareholders

The Committee has decided to build on the share ownership guidelines which apply to executives during their employment by introducing a formal, post-employment shareholding guideline. This guideline will require Executive Directors to hold their full in-employment share ownership guideline for a period of two years from the date of their retirement from the Board (or their actual shareholding from this date if lower).

As described above, Mr FitzPatrick's role expanded in July 2019 when he became Chief Operating Officer in addition to his role as Group Chief Financial Officer. In this capacity, he became responsible for a number of key Group functions including Legal, Government Affairs and Communications. In recognition of Mr FitzPatrick's expanded role and responsibilities, together with the Board's view of his strong performance, potential and criticality to the Group, the Committee propose increasing the value of his 2020 long-term incentive award to 300 per cent of base salary (from 250 per cent at present). The Committee chose to recognise the increased scope of Mr FitzPatrick's role in this way to promote stewardship and long-term focus.

It is imperative that incentive payments are based on performance which is well-founded and sustainable. The Committee currently has the scope to reduce, cancel or recover these payments and intends to build on these discretionary powers in the 2020 policy by formalising and extending the circumstances which might trigger the use of malus and clawback to include non-financial issues and personal conduct which falls short of the Company's expectations.

3 Foster alignment between the remuneration of executives and the wider workforce

The Committee is aware that the greater alignment of reward arrangements of executives with those of the wider workforce is an area of attention for many investors, particularly in light of the expectations set out in the UK Corporate Governance Code. The Committee intends to reflect this focus in a number of ways, including those set out below.

The Committee is mindful of the need for continued restraint in base salary increases. With effect from 1 January 2020, salary increases of 2 per cent were awarded for all Executive Directors. 2020 will be the eighth consecutive year in which the increases generally offered to executives have been below or close to the bottom of the salary increase budget ranges for the broader workforce.

Subject to approval of the new Policy, it is proposed that Executive Directors recruited externally or internally from the date of the 2020 AGM will be offered pension benefits of 13 per cent of salary, aligned with the employer pension contribution available to the UK workforce. We also propose to reduce incumbent Executive Directors' pension benefits from 25 per cent to 20 per cent of salary by May 2021. The Committee recognises that pension benefits are an increasingly important area of focus and believe that the proposal is an active step towards aligning executives with the wider workforce whilst recognising the existing contractual commitments in place. This is an area where market practice is evolving rapidly and one which the Committee will keep under close review.

In conclusion

I trust that you will find this report a clear account of the way in which the Committee has implemented the Directors' remuneration policy during 2019 and of the Committee's proposed new Directors' remuneration policy.

Anthony Nightingale, CMG SBS JP
Chairman of the Remuneration Committee

10 March 2020