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PRUDENTIAL

Prudential plc

英國保誠有限公司*

(Incorporated and registered in England and Wales under the number 01397169)

(Stock code: 2378)

PRESS RELEASE AND ANNUAL RESULTS FOR THE YEAR ENDED 31 DECEMBER 2017

NEWS RELEASE

PRUDENTIAL

14 March 2018

PRUDENTIAL PLC FULL YEAR 2017 RESULTS

2017 FINANCIAL OBJECTIVES DELIVERED AND SUSTAINED GROWTH IN PROFIT AND CASH

Performance highlights on a constant (and actual) exchange rate basis

- Group IFRS operating profit[4] of £4,699 million, up 6 per cent[1] (up 10 per cent[2])
- Asia double-digit broad-based growth in new business profit[3], up 12 per cent[1], IFRS operating profit[4], up 15 per cent[1] and underlying free surplus generated[5], up 19 per cent[1]
- US separate account net inflows[6] of £3.5 billion contributing to separate account assets 19 per cent[1] higher at £130.5 billion
- M&G Prudential assets under management[7] up 13 per cent to £351 billion, driven by record net inflows into M&G and PruFund
- Full year 2017 ordinary dividend increased by 8 per cent to 47 pence per share
- Group Solvency II surplus[8,9] estimated at £13.3 billion, equivalent to a cover ratio of 202 per cent

Mike Wells, Group Chief Executive, said: 'Our clear, consistent strategy, high-quality products and constantly improving capabilities have enabled us to deliver excellent progress across the Group, led by double-digit growth in our Asia business. We have also achieved all of our 2017 objectives[10], which we set in December 2013. This represents the third set of objectives successfully achieved within the last 10 years.

'The performance of our Asia business is testament to the strength, scale and diversity of our platform in the region, our focus on recurring-premium health and protection business and the quality of our execution. Our Asia life businesses delivered a 15 per cent[1] increase in IFRS operating profit[4] and a 12 per cent[1] increase in new business profit over the year, while assets under management at Eastspring increased by 18 per cent[2]. We continue to develop our capabilities in Asia, building scale and enhancing quality.

'In the US our life business, Jackson, remains focused on meeting the retirement income needs of the growing numbers of baby boomer retirees and extending our products and reach to improve access to the large asset pools of the fee-based advisory market. Jackson delivered positive separate account net inflows[6] of £3.5 billion, with separate account assets increasing by 19 per cent[1].

'During 2017 we announced that we were combining our asset manager, M&G, and Prudential UK & Europe to form M&G Prudential, a leading savings and investment business in the UK and Europe well positioned to target growing customer demand for comprehensive financial solutions. M&G Prudential has delivered record levels of external asset management net inflows of £17.3 billion, contributing to total assets under management[7] of £351 billion.

'Our strategy is aligned to structural trends: the savings and protection needs of the fast-growing middle class in Asia, the retirement income needs of the baby boomers in the US and the increasing demand for managed savings solutions among the ageing populations of the UK and Europe. The Group's performance demonstrates that we are highly effective in accessing the opportunities arising from these trends, and that we are meeting the needs of our customers better than ever before. I am confident that, given the extent of our opportunities and our proven ability to execute and innovate, we are well positioned to continue to grow profitably.'

Summary financials	2017 £m	2016 £m	Change on AER basis	Change on CER basis
IFRS operating profit based on longer-term investment returns	**4,699**	4,256	10%	6%
Underlying free surplus generated[5,11]	**3,640**	3,566	2%	(1)%
Life new business profit[3]	**3,616**	3,088	17%	12%
IFRS profit after tax[12]	**2,390**	1,921	24%	21%
Net cash remittances from business units	**1,788**	1,718	4%	-

	2017 £bn	2016 £bn	Change on AER basis
IFRS shareholders' funds	**16.1**	14.7	10%
EEV shareholders' funds	**44.7**	39.0	15%
Group Solvency II capital surplus[8,9]	**13.3**	12.5	6%

Notes
1 Year-on-year percentage increases are stated on a constant exchange rate basis unless otherwise stated.
2 Growth rate on an actual exchange rate basis.
3 New business profit on business sold in the year, calculated in accordance with EEV principles.
4 Based on longer-term investment returns.
5 Underlying free surplus generated comprises underlying free surplus generated from the Group's long-term business (net of investment in new business) and that generated from asset management operations. Further information is set out in note 11 of the EEV basis results.
6 Variable annuity separate account inflows.
7 Represents M&G Prudential asset management external funds under management and internal funds included on the M&G Prudential long-term insurance business balance sheet.
8 The Group shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds and staff pension schemes in surplus. The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.
9 Before allowing for second interim ordinary dividend.
10 The 2017 financial objectives were for Asia to deliver a compound annual growth rate for IFRS operating profit based on longer-term investment returns of at least 15 per cent between 2013 and 2017 and underlying free surplus generation of £0.9 billion to £1.1 billion in the year to 31 December 2017 and for the Group to deliver cumulative underlying free surplus generation of at least £10 billion between 1 January 2014 and 31 December 2017.
11 The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3 of the IFRS financial statements. On re-presentation, Prudential Capital is excluded from underlying free surplus generated.
12 IFRS profit after tax reflects the combined effects of operating results determined on the basis of longer-term investment returns, together with negative short-term investment variances, which in 2017 largely arose within Jackson, profit (loss) on disposal of businesses, amortisation of acquisition accounting adjustments and the total tax charge for the year.

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Notes to Editors:

1. The results in this announcement are prepared on two bases: International Financial Reporting Standards (IFRS) and European Embedded Value (EEV). The results prepared under IFRS form the basis of the Group's statutory financial statements. The supplementary EEV basis results have been prepared in accordance with the amended European Embedded Value principles dated April 2016 formulated by the CFO Forum of European Insurance Companies. The Group's EEV basis results are stated on a post-tax basis and, where appropriate, include the effects of IFRS. Year-on-year percentage increases are presented on a constant exchange rate basis unless otherwise stated. Constant exchange rates results are calculated by translating prior year results using the current year foreign exchange rate ie current year average rates for the income statement and current year closing rates for the balance sheet.

2. Annual Premium Equivalent (APE) sales comprise regular premium sales plus one-tenth of single premium insurance sales.

3. Operating profit is determined on the basis of including longer-term investment returns. EEV and IFRS operating profit is stated after excluding the effect of short-term fluctuations in investment returns against long-term assumptions, which for IFRS in 2017 principally arose within Jackson, and profits and losses arising on the disposal of businesses. Furthermore, for EEV basis results, operating profit based on longer-term investment returns excludes the effect of changes in economic assumptions and the mark to market value movement on core borrowings. Separately on the IFRS basis, operating profit also excludes amortisation of accounting adjustments arising principally on the acquisition of REALIC completed in 2012.

4. Total number of Prudential plc shares in issue as at 31 December 2017 was 2,587,175,445.

5. A presentation for analysts and investors will be held today at 11.30am (UK time) / 7.30pm (Hong Kong time) in the conference suite at Nomura, 1 Angel Lane, London EC4R 3AB. The presentation will be webcast live and available to replay afterwards using the following link http://www.investis-live.com/prudential/5a6f2d8725d9c011009ed48f/lzqo

To register attendance in person please send an email to investor.relations@prudential.co.uk

Alternatively, a dial-in facility will be available to listen to the presentation: please allow time ahead of the presentation to join the call (lines open half an hour before the presentation is due to start, ie from 11.00am (UK time) / 7.00pm (Hong Kong time). Dial-in: 020 3936 2999 (UK Local Call) / +44 20 3936 2999 (International) / 0800 640 6441 (Freephone UK), Participant access code: 378321 – Once participants have entered this code their name and company details will be taken. Playback: +44 (0) 20 3936 3001 (UK and international excluding US) / + 1 845 709 8569 (US only) (Replay code: 043060). This will be available from approximately 3.00pm (UK time) / 11.00pm (Hong Kong time) on 14 March 2018 until 11.59pm (UK time) on 28 March 2018 / 6.59am (Hong Kong time) on 29 March 2018.

6. 2017 Second interim ordinary dividend

Ex-dividend date	29 March 2018 (UK, Ireland, Hong Kong and Singapore)
Record date	3 April 2018
Payment of dividend	18 May 2018 (UK, Ireland and Hong Kong)
	On or about 25 May 2018 (Singapore and ADR holders)

7. About Prudential plc

Prudential plc and its affiliated companies constitute one of the world's leading financial services groups, serving over 26 million customers and it has £669 billion of assets under management (as at 31 December 2017). Prudential plc is incorporated in England and Wales and is listed on the stock exchanges in London, Hong Kong, Singapore and New York. Prudential plc is not affiliated in any manner with Prudential Financial, Inc., a company whose principal place of business is in the United States of America.

8. 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, the timing, costs and successful implementation of the demerger described herein; the future trading value of the shares of Prudential plc and the trading value and liquidity of the shares of the to-be-listed M&G Prudential business following such demerger; future market conditions, including fluctuations in interest rates and exchange rates, 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; the political, legal and economic effects of the UK’s decision to leave the European Union; the impact of continuing designation as a Global Systemically Important Insurer or ‘G-SII’; the impact of competition, economic uncertainty, inflation and deflation; the effect on Prudential’s business and results from, in particular, 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 internal projects and other strategic actions failing to meet their objectives; disruption to the availability, confidentiality or integrity of Prudential’s IT systems (or those of its suppliers); 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 and regulatory actions, investigations 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.

Summary 2017 financial performance

Financial highlights

Life APE new business sales (APE sales)[1]

	Actual Exchange Rate			Constant Exchange Rate	
	2017 £m	2016 £m	Change %	2016 £m	Change %
Asia	**3,805**	3,599	6	3,773	1
US	**1,662**	1,561	6	1,641	1
UK and Europe	**1,491**	1,160	29	1,160	29
Total Group	**6,958**	6,320	10	6,574	6

Life EEV new business profit and investment in new business

	Actual Exchange Rate						Constant Exchange Rate			
	2017 £m		2016 £m		Change %		2016 £m		Change %	
	New Business Profit	Free surplus invested in new business	New Business Profit	Free surplus invested in new business	New Business Profit	Free surplus invested in new business	New Business Profit	Free surplus invested in new business	New Business Profit	Free surplus invested in new business
Asia	**2,368**	**484**	2,030	476	17	2	2,123	500	12	(3)
US	**906**	**254**	790	298	15	(15)	830	313	9	(19)
UK and Europe	**342**	**175**	268	129	28	36	268	129	28	36
Total Group	**3,616**	**913**	3,088	903	17	1	3,221	942	12	(3)

IFRS Profit[2,3]

	Actual Exchange Rate			Constant Exchange Rate	
	2017 £m	2016 £m	Change %	2016 £m	Change %
Operating profit before tax based on longer-term investment returns					
Asia					
Long-term business	**1,799**	1,503	20	1,571	15
Asset management	**176**	141	25	149	18
Total	**1,975**	1,644	20	1,720	15
US					
Long-term business	**2,214**	2,052	8	2,156	3
Asset management	**10**	(4)	350	(4)	350
Total	**2,224**	2,048	9	2,152	3
UK and Europe					
Long-term business	**861**	799	8	799	8
General insurance commission	**17**	29	(41)	29	(41)
Total insurance operations	**878**	828	6	828	6
Asset management	**500**	425	18	425	18
Total	**1,378**	1,253	10	1,253	10
Other income and expenditure	**(775)**	(694)	(12)	(700)	(11)
Total operating profit based on longer-term investment returns before tax, restructuring costs and interest received from tax settlement	**4,802**	4,251	13	4,425	9
Restructuring costs[4]	**(103)**	(38)	(171)	(39)	(164)
Interest received from tax settlement	**-**	43	n/a	43	n/a
Total operating profit based on longer-term investment returns before tax	**4,699**	4,256	10	4,429	6
Non-operating items:					
Short-term fluctuations in investment returns on shareholder-backed business	**(1,563)**	(1,678)	7	(1,764)	11
Amortisation of acquisition accounting adjustments	**(63)**	(76)	17	(79)	20
Profit (loss) attaching to disposal of businesses	**223**	(227)	n/a	(244)	n/a
Profit before tax	**3,296**	2,275	45	2,342	41
Tax charge attributable to shareholders' returns	**(906)**	(354)	(156)	(360)	(152)
Profit for the year	**2,390**	1,921	24	1,982	21

***Post-tax profit - EEV*[3,5]**

	Actual Exchange Rate			Constant Exchange Rate	
	2017 £m	**2016 £m**	**Change %**	**2016 £m**	**Change %**
Post-tax operating profit based on longer-term investment returns					
Asia operations					
Long-term business	**3,705**	3,074	21	3,220	15
Asset management	**155**	125	24	132	17
Total	**3,860**	3,199	21	3,352	15
US operations					
Long-term business	**2,143**	1,971	9	2,071	3
Asset management	**7**	(3)	333	(4)	275
Total	**2,150**	1,968	9	2,067	4
UK and Europe operations					
Long-term business	**1,015**	643	58	643	58
General insurance commission	**13**	23	(43)	23	(43)
Total insurance operations	**1,028**	666	54	666	54
Asset management	**403**	341	18	341	18
Total	**1,431**	1,007	42	1,007	42
Other income and expenditure	**(746)**	(682)	(9)	(688)	(8)
Post-tax operating profit based on longer-term investment returns before restructuring costs and interest received from tax settlement	**6,695**	5,492	22	5,738	17
Restructuring costs[4]	**(97)**	(32)	(203)	(32)	(203)
Interest received from tax settlement	**-**	37	n/a	37	n/a
Post-tax operating profit based on longer-term investment returns	**6,598**	5,497	20	5,743	15
Non-operating items:					
Short-term fluctuations in investment returns	**2,111**	(507)	516	(567)	472
Effect of changes in economic assumptions	**(102)**	(60)	(70)	(54)	(89)
Mark to market value on core structural borrowings	**(326)**	(4)	(8,050)	(4)	(8,050)
Impact of US tax reform	**390**	-	n/a	-	n/a
Profit (loss) attaching to disposal of businesses	**80**	(410)	n/a	(445)	n/a
Post-tax profit for the year	**8,751**	4,516	94	4,673	87

Basic earnings per share - based on operating profit after tax

	Actual Exchange Rate			Constant Exchange Rate	
	2017 pence	**2016 pence**	**Change %**	**2016 pence**	**Change %**
IFRS	**145.2**	131.3	11	136.8	6
EEV	**257.0**	214.7	20	224.3	15

Underlying free surplus generated [3,6]

	Actual Exchange Rate						Constant Exchange Rate			
	2017 £m		**2016 £m**		**Change %**		**2016 £m**		**Change %**	
	Long-term	**Total**	**Long-term**	**Total**	**Long-term**	**Total**	**Long-term**	**Total**	**Long-term**	**Total**
Asia	**923**	**1,078**	734	859	26	25	773	905	19	19
US	**1,321**	**1,328**	1,568	1,565	(16)	(15)	1,648	1,644	(20)	(19)
UK and Europe	**895**	**1,311**	794	1,158	13	13	794	1,158	13	13
Total Group before restructuring costs	**3,139**	**3,717**	3,096	3,582	1	4	3,215	3,707	(2)	-
Restructuring costs[4]	**(38)**	**(77)**	(16)	(16)	(138)	(381)	(16)	(16)	(138)	(381)
Total Group	**3,101**	**3,640**	3,080	3,566	1	2	3,199	3,691	(3)	(1)

***Cash remitted by the business units to the Group*[3,7]**

	2017 £m	**2016 £m**	**Change %**
Asia	**645**	516	25
US	**475**	420	13
UK and Europe	**643**	590	9
Other UK (including Prudential Capital)	**25**	192	(87)
Total Group	**1,788**	1,718	4

Cash and capital

	2017	2016	Change %
Dividend per share relating to the reporting year	**47.0p**	43.5p	8
Holding company cash and short-term investments	**£2,264m**	£2,626m	(14)
Group Solvency II capital surplus[8,9]	**£13.3bn**	£12.5bn	6
Group Solvency II capital ratio[8,9]	**202%**	201%	+1pp

Group shareholders' funds (including goodwill attributable to shareholders)

	2017	2016	Change %
IFRS	**£16.1bn**	£14.7bn	10
EEV	**£44.7bn**	£39.0bn	15

	2017 %	2016 %
Return on IFRS shareholders' funds[10]	**25**	26
Return on embedded value[10]	**17**	17

	2017	2016	Change %
EEV shareholders' funds[11] per share (including goodwill attributable to shareholders)	**1,728p**	1,510p	14
EEV shareholders' funds[12] per share (excluding goodwill attributable to shareholders)	**1,671p**	1,453p	15

2017 Financial objectives[13]

Asia Objectives	**2012 £m**	**2017 £m**	**CAGR[13] (since 2012) %**	**Objectives 2017[13]**
Asia life and asset management IFRS operating profit				
Full year				
Actuals	909	1,975		>£1,826 million
Constant exchange rate[14]	884	1,855	16	>15% CAGR
Asia Underlying Free Surplus Generation				
Full year				
Actuals	468	1,078		£0.9 - £1.1 billion
Constant exchange rate[14]	454	1,029		

Group Objective for cumulative period 1 January 2014 to 31 December 2017	**Actual 1 Jan 2014 to 31 Dec 2017**	**Objective 1 Jan 2014 to 31 Dec 2017**
Cumulative Group Underlying Free Surplus Generation[6,15] from 2014 onwards	£12.8 billion	> £10 billion

Notes

1 APE sales is a measure of new business activity that is calculated as the sum of annualised regular premiums from new business plus 10 per cent of single premiums on new business written during the period for all insurance products, including premiums for contracts designated as investment contracts under IFRS 4. It is not representative of premium income recorded in the IFRS financial statements. Further explanation of the differences is included in note E of the Additional EEV financial information.

2 IFRS operating profit is management's primary measure of profitability and provides an underlying operating result based on longer-term investment returns and excludes non-operating items. Further information on its definition and reconciliation to profit for the period is set out in note B1 of the IFRS financial statements.

3 The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3 of the IFRS financial statements. On re-presentation, Prudential Capital is excluded from total segment profit and underlying free surplus generated.

4 Restructuring costs include business transformation and integration costs.

5 Embedded value reporting provides investors with a measure of the future profit streams of the Group. The EEV basis results have been prepared in accordance with EEV principles discussed in note 1 of the EEV basis results. A reconciliation between IFRS and the EEV shareholder funds is included in note D of the Additional EEV financial information.

6 Underlying free surplus generated comprises underlying free surplus generated from the Group's long-term business (net of investment in new business) and that generated from asset management operations. Further information is set out in note 11 of the EEV basis results.

7 Cash remitted to the Group form part of the net cash flows of the holding company. A full holding company cash flow is set out in note II (a) of the Additional unaudited IFRS financial information. This differs from the IFRS Consolidated Statement of Cash Flows which includes all cash flows relating to both policyholders and shareholders' fund. The holding company cash flow is therefore a more meaningful indicator of the Group's central liquidity.

8 The Group shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds and staff pension schemes in surplus. The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.

9 Estimated before allowing for second interim ordinary dividend.

10 Operating profit after tax and non-controlling interests, as a percentage of opening shareholders' funds, as set out in note II(c) of the Additional unaudited IFRS financial information and note F of the Additional EEV financial information.

11 Closing EEV shareholders' funds divided by issued shares, as set out in note G of the Additional EEV financial information.

12 Closing EEV shareholders' funds less goodwill attributable to shareholders divided by issued shares, as set out in note G of the Additional EEV financial information.

13 The current year and all comparative amounts for the Asia objectives exclude contributions from the Korea life business which was sold in 2017. The 2017 Asia IFRS operating profit objective was adjusted accordingly. 2012 comparative amounts include the one-off gain on sale of the stake in China Life of Taiwan of £51 million.

14 Constant exchange rates results translated using exchange rates at December 2013.

15 For the purpose of the Group Objective, cumulative underlying free surplus generation includes the free surplus relating to Prudential Capital.

Group Chief Executive's report

I am pleased to report that over 2017 our clear, consistent strategy, high-quality products and improving capabilities have enabled us to meet the needs of customers around the world better than ever before.

Our purpose is to help remove uncertainty from life's big events. Whether that's starting a family, saving for a child's education or planning for retirement, we provide our customers with financial peace of mind, enabling them to face the future with greater confidence. We also invest our customers' money actively in the real economy, helping not only to improve the lives of individuals and families, but also to build stronger communities and drive the cycle of growth.

Our strategy is aligned to structural trends: the savings and protection needs of the fast-growing middle class in Asia, the retirement income needs of the approximately 75 million baby boomers in the United States[1] and the growing demand for managed savings solutions among the ageing populations of the United Kingdom and Europe. These trends are sustained, and we remain focused on the opportunities they present.

We have continued to develop our products and our capabilities in order to improve the way we meet customers' needs. We are creating new, better and more personalised products, and we have a flexible, collaborative approach to incorporating the best digital technologies into our operations, while also leveraging our global scale to share new insights across our businesses at pace. The result is constant improvement in the way we serve our customers, providing value both to them and to our shareholders.

In March 2018 the Group announced its intention to demerge its UK and Europe businesses ('M&G Prudential') from Prudential plc, resulting in two separately-listed companies, with different investment characteristics and opportunities. Our businesses share common heritage, values and purpose. Looking forward, we believe we will be better able to focus on meeting our customers' rapidly evolving needs and to deliver long-term value to investors as two separate businesses. On completion of the demerger, shareholders will hold interests in both Prudential plc and M&G Prudential.

In line with its strategy to transition towards a more capital efficient, de-risked business model, M&G Prudential agreed in March 2018 to the sale of £12.0 billion[20] of its shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, M&G Prudential has reinsured £12.0 billion[20] of liabilities to Rothesay Life, which is expected to be followed by a Part VII transfer of the portfolio by the end of 2019. The capital benefit of this transaction will be retained within the Group to support the UK demerger process.

In preparation for the UK demerger process, and to align the ownership of the Group's businesses with their operating structures, Prudential plc intends to transfer the legal ownership of its Hong Kong insurance subsidiaries from The Prudential Assurance Company Limited (M&G Prudential's UK regulated insurance entity) to Prudential Corporation Asia Limited, which is expected to complete by the end of 2019.

Our financial performance

We have built on our good start to 2017 through disciplined execution of our strategy, again led by our businesses in Asia.

We announce today the achievement of our remaining 2017 objectives, which were set in December 2013. During the first half of 2017, we exceeded the Group objective of underlying free surplus generation of at least £10 billion from the beginning of 2014 to the end of 2017. By the end of 2017 we had generated £12.8 billion over this four year period. Our Asia businesses delivered growth in IFRS operating profit based on longer-term investment returns[2] ('IFRS operating profit') at a compound average rate of 16 per cent[3] over the period 2012 to 2017, and underlying free surplus generation of £1,078 million[3] for the full year 2017. This is testament to the strength, scale and diversity of our Asia platform, validates our focus on recurring premium health and protection business and demonstrates the strength of our operational execution. It also marks the third set of objectives that we have successfully achieved within the last 10 years.

During 2017 we combined our UK and European life and asset management businesses to form M&G Prudential, which delivered record levels of external asset management net inflows of £17.3 billion in 2017. This contributed to combined assets under management[4] of £351 billion at 31 December 2017.

As in previous years, we comment on our performance in local currency terms (expressed on a constant exchange rate basis) to show the underlying business trends in a period of currency movement.

Group IFRS operating profit was 6 per cent[5] higher at £4,699 million (up 10 per cent on an actual exchange rate basis). IFRS operating profit from our Asia life insurance and asset management businesses grew by 15 per cent[5], reflecting continued broad-based business momentum across the region, with double-digit[5] growth in eight out of 12 life insurance markets. In the US, Jackson's total IFRS operating profit increased by 3 per cent[5], due mainly to growth in fee income on higher asset balances, which outweighed the anticipated reduction in spread earnings. In the UK and Europe, M&G Prudential's total IFRS operating profit was 10 per cent higher than the prior year, reflecting 6 per cent growth in the IFRS operating profit generated from insurance business and 18 per cent growth in that generated from asset management.

The Group's capital generation is underpinned by our large and growing in-force business portfolio, and focus on profitable, short-payback business. Overall underlying free surplus generation[6] decreased by 1 per cent[5] to £3,640 million, with higher contributions in Asia and the UK and Europe, offset by higher restructuring costs and a lower contribution from our US business. 2016 benefited from the impact of a US transaction to enhance local capital efficiency that was not repeated in 2017. Cash remittances to the Group increased to £1,788 million, with Asia the largest contributor[7] at £645 million. The Group's overall performance supported an 8 per cent increase in the 2017 full year ordinary dividend to 47 pence per share.

The Group remains robustly capitalised, with a 2017 year-end Solvency II cover ratio[8,9] of 202 per cent. Over the period, IFRS shareholders' funds increased by 10 per cent to £16.1 billion, reflecting profit after tax of £2,390 million (2016: £1,921 million on an actual exchange rate basis) net of other movements that included dividend payments to shareholders of £1,159 million and adverse foreign exchange movements of £470 million. EEV shareholders' funds increased by 15 per cent to £44.7 billion, equivalent to 1,728 pence per share[10,11].

New business profit[11] increased by 12 per cent[5] to £3,616 million (up 17 per cent on an actual exchange rate basis), driven by improved business mix in Asia, higher UK volumes and the favourable effect of tax reform in the US.

In Asia, we continue to develop our capabilities and reach, which build scale and enhance quality. Our strategic emphasis on increasing sales from health and protection business has contributed to a 12 per cent[5] increase in new business profit in Asia. Our asset management business, Eastspring Investments, has again seen growth, with its total assets under management up 18 per cent[12] to £138.9 billion and IFRS operating profit also up 18 per cent[5] to £176 million.

In the US we remain focused on meeting the retirement income needs of the growing generation of baby boomer retirees and expanding our operations into the large asset pools of the fee-based advisory market. Although the evolving regulatory environment continues to cause industry sales disruption, in 2017 Jackson delivered positive separate account net inflows of £3.5 billion, with separate account assets reaching £130.5 billion, an increase of 19 per cent[5]. In December 2017 the US enacted a major tax reform package, including a reduction in the corporate income tax rate from 35 per cent to 21 per cent effective from 1 January 2018. While this led to a £445 million charge in the income statement from re-measuring deferred tax balances on the IFRS balance sheet, we expect the tax changes to be positive in the long term. The US effective tax rate is expected to fall from the current rate of circa 28 per cent to circa 18 per cent in the future.

In the UK, both our UK life and asset management businesses performed well in 2017. PruFund new business APE sales increased 36 per cent to £1.2 billion, while M&G saw record net inflows of £17.3 billion from external clients. Overall M&G Prudential assets under management[4] reached £351 billion, up from £311 billion at 31 December 2016.

Our financial KPIs continue to reflect the outcome of the Group's strategy. Our Asia life businesses are driven by growth in our recurring premium base and focus on health and protection business, and elsewhere we are benefiting from our prioritisation of fee-generating products across our Asia asset management, US variable annuity and UK and European asset management activities.

A successful strategy

Our performance is based on our clear, consistent and successful strategy, which is focused on long-term opportunities arising from structural trends in our markets around the world.

In Asia, the growth of the middle class is creating significant and long-term demand for the products we offer. The working-age population in the region is growing by a million people a month, and by 2030 is expected to reach 2.5 billion[13], while 65 per cent of Asian private financial wealth is held in cash[14] and at the same time, that wealth is growing by US$4 trillion a year[14].

The growing and increasingly wealthy middle classes of the region are under-protected. In Asia, out-of-pocket healthcare spend makes up 42 per cent of total health expenditure[15], compared with just 12 per cent in the US and 9 per cent in the UK. While in a more developed market such as the UK insurance penetration is equivalent to 7.5 per cent[16] of GDP, in Asia that figure is just 2.4 per cent[16], giving an idea of the scale of the growth opportunity that remains in our Asian markets. The gap between the insurance cover of people in the region and what they need in order to maintain the living standards of their families has been estimated at circa £35 trillion[17]. We help to bridge that gap with a broad range of solutions across 14 markets in the region. We are in the top three in nine of our markets in Asia[18], and we have 15 million life customers, with access to total markets of more than 3.3 billion people.

The United States is the world's largest retirement market, with approximately 40 million Americans reaching retirement age over the next decade alone, and these consumers have a need for investment options through which they can grow their savings while at the same time protecting their income. This is creating demand for our variable annuity products, which are designed to help this cohort of Americans avoid running out of money and provide them with a reliable cushion against volatile markets. In the US, over US$15 trillion is invested in adviser-distributed financial assets net of existing annuities, while penetration of variable annuity sales into the retirement market remains low, demonstrating the scale of the opportunity for us.

In the UK and Europe there is growing demand among customers for managed solutions, savings products that provide better long-term returns than cash, while smoothing out the ups and downs of the market. We meet that need through our PruFund propositions and our comprehensive range of actively managed funds. M&G Prudential is well positioned to target this growing customer demand for comprehensive financial solutions and the demerger will enable this business to play an even greater role in these markets.

Doing more for our customers

We deliver on our clear strategy and our long-term opportunities by paying close attention to the needs of our customers, by responding to those needs with products that fit their changing requirements, and by improving our capabilities continually in order to deliver the best products in the most effective way.

In Asia, our broad-based portfolio of businesses continues to drive the growth of the Group. We are constantly improving the range and quality of the products we offer in the region, developing our multi-channel distribution platform to ensure that those products reach as many customers as possible and improving our capabilities throughout our operations, not least by accessing new innovations in digital technology.

We develop products that meet the needs of our customers, whether that is for more personalised features or products aimed at new areas of the market and in 2017 we launched a number of new health and protection products in Indonesia, Vietnam, Singapore, Malaysia and Hong Kong. We are also continuing to improve both our agency platform and our bancassurance partnerships in Asia to ensure that we reach as many customers as possible. Nowhere is this clearer than in China, where, through our joint venture CITIC-Prudential, we now have a presence in 77 cities, with access to 940 million people, or about 70 per cent of the population of the world's most populous country. We have over 44,000 agents in China and access to more than 4,000 bank branches. Across the region during 2017 we increased our total agents to over 600,000 and we ended the year with over 15 million life insurance customers. Recent announcements of new agreements in the Philippines, Thailand, Indonesia and Vietnam have also increased the reach of our bancassurance partnerships.

Continuous improvement of our capabilities is also a key part of our approach, and in Asia we introduced a number of digital initiatives that will benefit both our customers and our shareholders, including apps and chatbots, that, among other services, can provide rapid claims payment, constant customer support, answer queries, help schedule appointments and transfer feedback from customers to our businesses. Building on its success in Hong Kong, our myDNA service, which provides diet and exercise advice based on genetic profiles, has been launched in Vietnam, Malaysia and Singapore. In Singapore we also launched PRU Fintegrate, a new initiative enabling us to collaborate with fintech startups to co-develop digital solutions for customers.

Eastspring is well placed for the anticipated growth in Asia's retail mutual fund market. To prepare further, we have strengthened our in-house investment teams, entered into new strategic partnerships and made significant progress in systems and operating model upgrades. In addition, Eastspring recognises that environmental, social and governance (ESG) factors can be material to investment returns, particularly in the long term, and has become a signatory to the United Nations-supported Principles for Responsible Investment (PRI), joining M&G Prudential asset management.

In the United States, we are continuing to develop our business to ensure we capture the opportunity presented by the millions of Americans moving into retirement now and over the coming years. Regulatory and industry changes are creating new areas of growth potential and we are adapting our offering to meet those opportunities. During 2017, in response to evolving conditions in the hybrid adviser segment of the market, Jackson launched Perspective Advisory II, an advisory version of our flagship product, Perspective II. We also announced the formation in November of our Private Wealth & Trust group, a specialised team focused on complex planning, investment management and tax mitigation strategies for high-net-worth clients. At the same time, we are improving communication for customers, and our initiatives in this area last year included the launch of a new website, the Financial Freedom Studio, where consumers can learn about financial planning for retirement, aimed at simplifying the language and focusing on planning for lifetime income.

In the UK and Europe, the combination of our life and asset management businesses into M&G Prudential has enabled us to meet the needs of our customers better than ever before. The business manages £351 billion of assets[4] for more than seven million customers, both in the UK and internationally, and we are leveraging our scale, financial strength and complementary product and distribution capabilities to enhance the development of capital-efficient, customer-focused solutions. Bringing these businesses together has given us the opportunity to deliver better collaboration across business segments and more innovative and differentiated propositions. It also provides better access to customers and channels, merger cost synergies and transformation benefits, including the chance to invest to create a digital, data-led business with low marginal cost of growth. M&G Prudential is in the top five in UK retail funds[19], with an active management offering, and provides a range of consumer-focused retirement and savings wrappers. The performance of its products continues to make them very popular among customers. The flagship PruFund Growth Life Fund, for example, has grown by 36 per cent since the start of 2013, compared with benchmark growth of 30 per cent, and this performance has driven growth in PruFund assets under management from £7.5 billion in 2012 to £35.9 billion at the end of 2017. To improve the offering to customers, in 2017 the business rolled out myM&G, its direct-to-consumer platform.

We took another step forward in our Africa business in 2017 when we entered Nigeria, Africa's largest economy and our fifth market in the region. Following the launch of our businesses in Ghana, Kenya, Uganda and Zambia, this further demonstrates our commitment to Africa and our determination to bring the benefits of our products to customers across the region.

We continue to invest in our capabilities and our people across the organisation. In July we welcomed Mark FitzPatrick to our executive team as Chief Financial Officer, succeeding Nic Nicandrou, who took over from Tony Wilkey as Chief Executive of Prudential Corporation Asia. Mark brings with him significant experience and knowledge of the sector, and I am confident that Nic will lead our Asian business to further success. In March 2018 James Turner was appointed Group Chief Risk Officer, bringing fresh perspective and additional leadership capacity to our executive team.

A positive outlook

With our clear strategy focused on long-term trends around the world and continued improvements in our execution capabilities, we are delivering value to our customers, our shareholders and the communities in which we operate. This is supported by our ongoing focus on risk management and the strength of our balance sheet. We believe the demerger of M&G Prudential from the international group will leave both businesses better able to focus on meeting our customers' rapidly evolving needs and to deliver long-term value to investors as two separate companies. I have no doubt that the strength of our underlying opportunities and our proven ability to innovate and improve the way we do things, will ensure that both businesses are well positioned to continue to serve our customers well and grow profitably into the future.

Notes

1 Source: US Census Bureau, Population Division, 2017 estimate of population.
2 IFRS operating profit is management's primary measure of profitability and provides an underlying operating result based on longer-term investment returns and excludes non-operating items. Further information on its definition and reconciliation to profit for the period is set out in note B1 of the IFRS financial statements.
3 The current year and all comparative amounts for the Asia objectives exclude contributions from the Korea life business which was sold in 2017. The 2017 Asia IFRS operating profit objective was adjusted accordingly. 2012 comparative amounts include the one-off gain on sale of the stake in China Life of Taiwan of £51 million.
4 Represents M&G Prudential asset management external funds under management and internal funds included on the M&G Prudential long-term insurance business balance sheet.
5 Year-on-year percentage increases are stated on a constant exchange rate basis unless otherwise stated.
6 Underlying free surplus generated comprises underlying free surplus generated from the Group's long-term business (net of investment in new business) and that generated from asset management operations. Further information is set out in note 11 of the EEV basis results.
7 Based on the 2017 operating segments.
8 The Group shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds and staff pension schemes in surplus. The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.
9 Estimated before allowing for second interim dividend.
10 Closing EEV shareholders' funds divided by issued shares, as set out in note G of the Additional EEV financial information.
11 Embedded value reporting provides investors with a measure of the future profit streams of the Group. The EEV basis results have been prepared in accordance with EEV principles discussed in note 1 of EEV basis results. A reconciliation between IFRS and the EEV shareholder funds is included in note D of the Additional EEV financial information.
12 Growth rate on an actual exchange rate basis.
13 Working age population 15 - 64 years. Source: United Nations, Department of Economic and Social Affairs, Population Division (2015). World Population Prospects: The 2015 Revision, DVD Edition.
14 Source: BCG Global Wealth 2016. Navigating the New Client Landscape.
15 Source: World health Organisation - Global Health Observatory data repository (2013). Out of pocket as percentage of total health expenditure.
16 Source: Swiss Re Sigma 2015. Insurance penetration calculated as premiums as percentage of GDP. Asia penetration calculated on a weighted population basis.
17 Source: Swiss Re, Mortality Protection Gap: Asia-Pacific, 2015.
18 Source: Based on formal (Competitors' results release, local regulators and insurance associations) and informal (industry exchange) market share data. Ranking based on new business (APE or weighted FYP depending on the availability of data).
19 Source: The Investment Association, September 2017.
20 Relates to £12.0 billion of IFRS shareholder annuity liabilities, valued as at 31 December 2017.

Chief Financial Officer's report on the 2017 financial performance

I am pleased to report that Prudential's financial performance in 2017 has resulted in all of our 2017 financial objectives being met. Our progress across our KPIs reflects the benefits of our focus on driving growth in high-quality, recurring health and protection and fee business across our geographies, products and distribution channels.

Performance was broad-based across our business units led by our Asia businesses which delivered double digit growth in new business profit (up 12 per cent[1]), IFRS operating profit based on longer-term investment returns ('IFRS operating profit') (up 15 per cent[1]) and underlying free surplus generation[3] (up 19 per cent[1]). Asia achieved its 2017 financial objectives, demonstrating successful execution of its strategy, focusing on diversified recurring premium business, at scale. In the US, we saw good growth in fee income, driven by positive net inflows and favourable equity market conditions, which outweighed the expected reduction in the contribution from spread income.

During 2017 we combined M&G and our UK and Europe life business to form M&G Prudential. I am pleased to report that M&G Prudential asset management delivered record external net inflows of £17.3 billion, with overall assets under management[4] at a new high of £351 billion at the end of 2017. We are making good progress in delivering our merger and transformation programme, and remain on track to deliver our previously announced savings by the end of 2022.

Sterling continued to strengthen against most of the currencies in our major international markets over 2017. However, on an average basis, sterling exchange rates remain lower than 2016, contributing to a positive effect on the translation of results from our non-sterling operations in 2017. If sterling exchange rates remain at or above end 2017 levels over the remainder of 2018, this will act to depress our results on translation of our non-sterling operations in 2018 compared with 2017. To aid comparison of underlying progress, we continue to express and comment on the performance trends in our Asia and US operations on a constant currency basis.

Our performance in 2017 was also supported by favourable equity markets, which lifted average investment balances on which we earn fees. During the year the S&P 500 index increased 19 per cent, the FTSE 100 index 8 per cent and the MSCI Asia excluding Japan index 39 per cent. Long-term yields showed little movement in 2017 and therefore have had no material impact on 2017 performance versus 2016.

The key financial highlights in 2017 were as follows:

- **New business profit** was 12 per cent higher at £3,616 million (17 per cent on an actual exchange rate basis), underpinned by higher volumes with **APE sales** up 6 per cent (10 per cent on an actual exchange rate basis). In Asia, new business profit increased 12 per cent primarily as a result of prioritisation of health and protection products and positive pricing actions. Jackson's new business profit increased by 9 per cent, including the benefit of US tax reform. UK life new business profit grew by 28 per cent, driven by a 29 per cent increase in APE sales, supported by consumer demand for products offering access to our PruFund investment option.
- **Asset management net inflows** reached record levels, with M&G Prudential asset management reporting external net inflows of £17.3 billion (2016: net outflows of £8.1 billion) reflecting growth across its wholesale/direct and institutional businesses, and Eastspring delivering external net inflows of £3.1 billion (excluding money market funds) (2016: £1.8 billion on an actual exchange rate basis).
- **IFRS operating profit based on longer-term investment returns** was 6 per cent higher at £4,699 million (10 per cent higher on an actual exchange rate basis). IFRS operating profit from our Asia business grew by 15 per cent to £1,975 million, reflecting continued business momentum. In the US, IFRS operating profit increased by 3 per cent, reflecting mainly growth in fee income on higher asset balances, which outweighed the anticipated reduction in spread earnings. In the UK, M&G Prudential's total IFRS operating profit was 10 per cent higher than the prior year reflecting 6 per cent growth in the insurance business, with core[5] life operating profit stable at £597 million, and record asset management profit of £500 million resulting from the positive impact on earnings of net fund inflows, supportive markets and higher performance fees.
- **Total IFRS post-tax profit** was up 21 per cent at £2,390 million (24 per cent on an actual exchange rate basis) and total EEV after-tax profit was 87 per cent higher at £8,751 million (94 per cent on an actual exchange rate basis). Total profit includes the impact of short-term fluctuations in financial assets held to back the commitments that we have made to our customers, and the related liabilities, and are reported outside the operating result which is based on longer-term investment return assumptions. In 2017 these principally arose within Jackson as discussed later in my report. Total profit after tax includes the impact of the US tax reform, which generated an IFRS charge of £445 million from the re-measurement of US net deferred tax balances following the reduction in the corporate income tax rate and an EEV gain of £390 million which additionally includes the benefit of future profits being taxed at a lower rate. Reflecting this post-tax profit, **Group IFRS shareholders' equity** was 10 per cent higher at £16.1 billion. Similarly, EEV basis shareholders' equity was up 15 per cent at £44.7 billion.
- **Underlying free surplus generation**[2,3], our preferred measure of cash generation, from our life and asset management businesses, decreased by 1 per cent to £3,640 million (up 2 per cent on an actual exchange rate basis), after financing new business growth. Increased contributions from our Asia and UK businesses were balanced by a lower contribution from our US business primarily as a result of non-recurrence of a transaction undertaken in 2016 to enhance local capital efficiency. We continue to focus on high-return new business with fast payback periods.
- **Group shareholders' Solvency II capital surplus**[6] was estimated at £13.3 billion at 31 December 2017, equivalent to a cover ratio of 202 per cent[7] (1 January 2017: £12.5 billion, 201 per cent). The improvement in the period reflects the continuing strength of the Group's operating capital generation in excess of growing dividend payments to shareholders.
- **Full year ordinary dividend** increased by 8 per cent to 47 pence per share, reflecting our 2017 performance and our confidence in the future prospects of our Group.

***IFRS Profit*[2]**

	Actual exchange rate			Constant exchange rate	
	2017 £m	**2016 £m**	**Change %**	**2016 £m**	**Change %**
Operating profit before tax based on longer-term investment returns					
Asia					
Long-term business	**1,799**	1,503	20	1,571	15
Asset management	**176**	141	25	149	18
Total	**1,975**	1,644	20	1,720	15
US					
Long-term business	**2,214**	2,052	8	2,156	3
Asset management	**10**	(4)	350	(4)	350
Total	**2,224**	2,048	9	2,152	3
UK and Europe					
Long-term business	**861**	799	8	799	8
General insurance commission	**17**	29	(41)	29	(41)
Total insurance operations	**878**	828	6	828	6
Asset management	**500**	425	18	425	18
Total	**1,378**	1,253	10	1,253	10
Other income and expenditure[8]	**(775)**	(694)	(12)	(700)	(11)
Total operating profit based on longer-term investment returns before tax, restructuring costs and interest received from tax settlement	**4,802**	4,251	13	4,425	9
Restructuring costs	**(103)**	(38)	(171)	(39)	(164)
Interest received from tax settlement	**-**	43	n/a	43	n/a
Total operating profit based on longer-term investment returns before tax	**4,699**	4,256	10	4,429	6
Non-operating items:					
Short-term fluctuations in investment returns on shareholder-backed business	**(1,563)**	(1,678)	7	(1,764)	11
Amortisation of acquisition accounting adjustments	**(63)**	(76)	17	(79)	20
Profit (loss) attaching to disposal of businesses	**223**	(227)	n/a	(244)	n/a
Profit before tax	**3,296**	2,275	45	2,342	41
Tax charge attributable to shareholders' returns	**(906)**	(354)	(156)	(360)	(152)
Profit for the year	**2,390**	1,921	24	1,982	21

IFRS earnings per share

	Actual exchange rate			Constant exchange rate	
	2017 pence	**2016 pence**	**Change %**	**2016 pence**	**Change %**
Basic earnings per share based on operating profit after tax	**145.2**	131.3	11	136.8	6
Basic earnings per share based on total profit after tax	**93.1**	75.0	24	77.4	20

IFRS operating profit based on longer-term investment returns

2017 total IFRS operating profit increased by 6 per cent (10 per cent on an actual exchange rate basis) to £4,699 million, with increased contributions from all of our core business units.

Asia total operating profit of £1,975 million was 15 per cent higher than the previous year (20 per cent on an actual exchange rate basis). IFRS operating profit from life insurance operations increased 15 per cent to £1,799 million (20 per cent on an actual exchange rate basis), reflecting the continued growth of our in-force book of recurring premium business, with renewal insurance premiums[9] reaching £11.6 billion (2016: £9.5 billion on a constant exchange rate basis). Insurance margin was up 21 per cent, reflecting our continued focus on health and protection business. At a country level, we have seen improvement in all of our markets, with double-digit growth in IFRS operating profit in eight out of 12, led by Hong Kong and China (both increasing 38 per cent). Including money market funds and the assets managed for internal life operations, Eastspring's total assets under management increased to £138.9 billion (2016: £117.9 billion on an actual exchange rate basis), while the cost-income ratio was stable at 56 per cent (2016: 56 per cent), driving an 18 per cent increase in IFRS operating profit to £176 million (2016: £149 million).

US total operating profit at £2,224 million increased by 3 per cent (9 per cent increase on an actual exchange rate basis), reflecting increased profit from our variable annuity business. US equity markets have continued to rise in 2017, which together with separate account net asset inflows of £3.5 billion, has led to separate account balances that were on average 17 per cent higher than the prior period. As a result, fee income increased 15 per cent to £2,343 million. Spread-based income decreased 10 per cent, as anticipated, reflecting the impact of lower yields on our fixed annuity portfolio and a reduced contribution from asset duration swaps. We expect these effects to continue to compress spread margins, although continued upwards movements in US yields may help to reduce the speed of the decline.

UK and Europe total operating profit was 10 per cent[2] higher at £1,378 million. Life insurance IFRS operating profit increased by 8 per cent to £861 million (2016: £799 million). Within this total, the contribution from our core[5] with-profits and in-force annuity business was £597 million (2016: £601 million), including an increased transfer to shareholders from the with-profits funds of £288 million (2016: £269 million) of which 15 per cent was from PruFund business (2016: 10 per cent). The balance of the life insurance result reflects the contribution from other activities which are not expected to recur to the same extent going forward. This includes, as anticipated, lower IFRS operating profit from the sale of annuities of £9 million (2016: £41 million) and a number of other items discussed below. Asset management IFRS operating profit increased 18 per cent to £500 million, driven by higher average assets under management and improved performance fees, together with a lower cost-income ratio of 58 per cent (2016: 59 per cent).

We took a number of actions during the year to optimise our asset portfolios and capital position, which generated profit of £276 million (2016: £332 million). Of this amount £31 million related to profit from longevity risk transactions (2016: £197 million) and £245 million from the effect of repositioning the fixed income asset portfolio (2016: £135 million). Favourable longevity assumption changes, reflecting updated actuarial mortality tables, contributed a further £204 million. This was offset partly by an increase of £225 million (2016: £175 million) in the provision related to the potential costs and related potential redress of reviewing internally vesting annuities sold without advice after 1 July 2008. The provision does not include potential insurance recoveries of up to £175 million.

Life insurance profit drivers

The increase in our IFRS operating profit levels reflects the growth in the scale of our operations, driven primarily by positive business flows. We track the progress that we make in growing our life insurance 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 increase as we write new business and collect regular premiums from existing customers and decrease as we pay claims and policies mature. The overall scale of these policyholder liabilities is relevant in the evaluation of our profit potential in that it reflects, for example, our ability to earn fees on the unit-linked element and indicates the scale of the insurance element, another key source of profitability for the Group.

Shareholder-backed policyholder liabilities and net liability flows[10]

	2017 £m				2016 £m			
	Actual exchange rate				Actual exchange rate			
	At 1 January	Net liability flows[11]	Market and other movements	At 31 December	At 1 January	Net liability flows[11]	Market and other movements	At 31 December
Asia	**32,851**	**2,301**	**2,250**	**37,402**	25,032	2,086	5,733	32,851
US	**177,626**	**3,137**	**(39)**	**180,724**	138,913	5,198	33,515	177,626
UK and Europe	**56,158**	**(2,721)**	**2,930**	**56,367**	52,824	(3,646)	6,980	56,158
Total Group	**266,635**	**2,717**	**5,141**	**274,493**	216,769	3,638	46,228	266,635

Focusing on business supported by shareholder capital, which generates the majority of the life profit, in 2017 net flows into our businesses were overall positive at £2.7 billion driven by our US and Asian operations, as we continue to focus on both retaining our existing customers and attracting new business to drive long-term value creation. In the UK our shareholder liabilities includes the run-off of the in-force annuity portfolio following our effective withdrawal from selling new annuity business. This has been more than offset by inflows into the with-profits funds of £3.5 billion. Positive investment markets, offset partly by currency effects as sterling has strengthened over the period, increased liabilities by £5.1 billion. In total, business flows and market movements have increased shareholder-backed policyholder liabilities from £266.6 billion to £274.5 billion.

Policyholder liabilities and net liability flows in with-profits business[10,12]

	2017 £m				2016 £m			
	Actual exchange rate				Actual exchange rate			
	At 1 January	Net liability flows[11]	Market and other movements	At 31 December	At 1 January	Net liability flows[11]	Market and other movements	At 31 December
Asia	**29,933**	**4,574**	**1,930**	**36,437**	20,934	3,696	5,303	29,933
UK and Europe	**113,146**	**3,457**	**8,096**	**124,699**	100,069	1,119	11,958	113,146
Total Group	**143,079**	**8,031**	**10,026**	**161,136**	121,003	4,815	17,261	143,079

Policyholder liabilities in our with-profits business have increased by 13 per cent to £161.1 billion reflecting the growing popularity of our participating funds in Asia and PruFund in the UK, as consumers seek protection from some of the short-term ups and downs of direct stock market investments by using an established smoothing process. Across our Asia and UK operations, net liability flows increased to £8.0 billion. As returns from these funds are smoothed and shared with customers, the emergence of shareholder profit is more gradual. This business, nevertheless, remains an important source of future shareholder value.

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

	Actual exchange rate						Constant exchange rate		
	2017 £m			2016 £m			2016 £m		
	Operating profit	Average liability	Margin bps	Operating profit	Average liability	Margin bps	Operating profit	Average liability	Margin bps
Spread income	**1,108**	**88,908**	**125**	1,171	83,054	141	1,215	85,266	142
Fee income	**2,603**	**166,839**	**156**	2,175	139,451	156	2,280	145,826	156
With-profits	**347**	**136,474**	**25**	317	118,334	27	319	119,170	27
Insurance margin	**2,271**			1,991			2,083		
Margin on revenues	**2,286**			2,126			2,211		
Expenses:									
Acquisition costs	**(2,433)**	**6,958**	**(35)%**	(2,251)	6,320	(36)%	(2,353)	6,574	(36)%
Administration expenses*	**(2,297)**	**261,114**	**(88)**	(1,943)	229,477	(85)	(2,025)	238,392	(85)
DAC adjustments	**505**			390			411		
Expected return on shareholder assets	**229**			221			227		
	4,619			4,197			4,368		
Longevity reinsurance and other management actions to improve solvency	**276**			332			332		
Changes in longevity assumption basis	**204**			-			-		
Provision for review of past annuity sales	**(225)**			(175)			(175)		
Operating profit based on longer-term investment returns	**4,874**			4,354			4,525		

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

We continue to maintain our preference for high-quality sources of income such as insurance margin from life and health and protection business, and fee income. We favour insurance margin because it is relatively insensitive to the equity and interest rate cycle and prefer fee income to spread income because it is more capital-efficient. In line with this approach, on a constant exchange rate basis, insurance margin has increased by 9 per cent (up 14 per cent on an actual exchange rate basis) and fee income by 14 per cent (up 20 per cent on an actual exchange rate basis), while spread income decreased by 9 per cent (down 5 per cent on an actual exchange rate basis). Administration expenses increased to £2,297 million (2016: £2,025 million) as the business continues to expand. The expense margin has grown from 85 basis points to 88 basis points reflecting the continued increase in US producers selecting asset-based commissions which are treated as an administrative expense in this analysis.

Asset management profit drivers

Movements in asset management operating profit are also influenced primarily by changes in the scale of these businesses, as measured by funds managed on behalf of external institutional and retail customers and our internal life insurance operations.

Asset management external funds under management[13,14]

	2017 £m				2016 £m			
	Actual exchange rate				Actual exchange rate			
	At 1 January	Net flows	Market and other movements	At 31 December	At 1 January	Net flows	Market and other movements	At 31 December
UK and Europe	**136,763**	**17,337**	**9,755**	**163,855**	126,405	(8,090)	18,448	136,763
Asia[15]	**38,042**	**3,141**	**5,385**	**46,568**	30,281	1,835	5,926	38,042
Total asset management	**174,805**	**20,478**	**15,140**	**210,423**	156,686	(6,255)	24,374	174,805
Total asset management (including MMF)	**182,519**	**21,973**	**15,248**	**219,740**	162,692	(5,852)	25,679	182,519

In 2017, average assets under management in our asset management businesses in the UK and Asia benefited from positive net inflows of assets and favourable markets, driving higher fee revenues. Reflecting this, IFRS operating profit derived from asset management activities in M&G Prudential increased by 18 per cent to £500 million and in Eastspring by 18 per cent (up 25 per cent on an actual exchange rate basis) to £176 million.

M&G Prudential's external assets under management have benefited from a record level of net inflows, reflecting improvement in investment performance and supportive markets. External asset management net inflows totalled £17.3 billion (2016: net outflows of £8.1 billion), with significant contributions from European investors in the Optimal Income Fund, Global Floating Rate High Yield Fund and multi-asset range, and from institutional clients, notably within our public debt, illiquid credit strategies and infrastructure equity funds. External assets under management increased 20 per cent to £163.9 billion during the year. Internal assets benefiting from PruFund sales and favourable markets increased 7 per cent, taking total M&G Prudential assets under management to £350.7 billion (2016: £310.8 billion).

Eastspring also attracted good levels of external net inflows during the year across its equity, fixed income and balanced fund range, totalling £3.1 billion, excluding money market funds (2016: £1.8 billion on an actual exchange rate basis). Overall external assets under management increased by 22 per cent to £46.6 billion. Combined with higher internal assets under management and money market funds lifted Eastspring's total assets under management to £138.9 billion.

Other income and expenditure and restructuring costs[8]
Higher interest costs following the debt issued in 2016 and 2017, and restructuring costs of £103 million, as the business invests for the future, including UK and Europe infrastructure, contributed to an increase in net central expenditure of £139 million to £878 million (2016: £732 million on an actual exchange rate basis).

IFRS non-operating items[8]
IFRS non-operating items consist of short-term fluctuations in investment returns on shareholder-backed business of negative £1,563 million (2016: negative £1,764 million), the results attaching to disposal of businesses of £223 million (2016: negative £244 million), and the amortisation of acquisition accounting adjustments of negative £63 million (2016: negative £79 million) arising mainly from the REALIC business acquired by Jackson in 2012. The profit attributable to disposal of businesses relates to amounts in respect of the Korea life business sold in 2017 and the disposal of the US broker-dealer network in August 2017.

Short-term fluctuations in investment returns on shareholder-backed business represent the most significant component of non-operating items and are discussed further below.

IFRS short-term fluctuations in investment returns on shareholder-backed business
IFRS operating profit is based on longer-term investment return assumptions. The difference between actual investment returns recorded in the income statement and the assumed longer-term returns is reported within short-term fluctuations in investment returns. In 2017, the total short-term fluctuations in investment returns on shareholder-backed business were negative £1,563 million and comprised negative £1 million for Asia, negative £1,568 million in the US, negative £14 million in the UK and positive £20 million in other operations.

In the US, Jackson provides certain guarantees on its annuity products, the value of which would rise typically when equity markets fall and long-term interest rates decline. Jackson includes the expected cost of hedging when pricing its products and charges fees for these guarantees which are used, as necessary, to purchase downside protection in the form of options and futures to mitigate the effect of equity market falls, and swaps and swaptions to cushion the impact of declines in long-term interest rates. Under IFRS, accounting for the movement in the valuation of these derivatives, which are all fair valued, is asymmetrical to the movement in guarantee liabilities, which are not fair valued in all cases. Jackson designs its hedge programme to protect the capital and economics of the business from large movements in investment markets and accepts the variability in accounting results. The negative short-term fluctuations in investment returns on shareholder-backed business of £1,568 million in the year are attributable mainly to the net value movement in the period of the hedge instruments held to manage market exposures and reflect the positive equity market performance in the US during the period.

IFRS effective tax rates
In 2017, the effective tax rate on IFRS operating profit based on longer-term investment returns was 21 per cent, which is unchanged from 2016 (21 per cent).

The 2017 effective tax rate on the total IFRS profit was 27 per cent (2016: 16 per cent), reflecting the inclusion of a £445 million one-off charge on the re-measurement of US deferred tax balances using a rate of 21 per cent (previously 35 per cent) following the enactment in December 2017 of a comprehensive US tax reform package. Excluding this one-off charge, the 2017 effective tax rate would have been 14 per cent.

In addition to the impact on the IFRS profit, the re-measurement of US deferred tax balances also resulted in a separate benefit of £134 million recognised in other comprehensive income, in relation to changes to deferred tax on cumulative unrealised gains (net of DAC) on bonds which are taken directly through other comprehensive income.

The main driver of the Group's effective tax rate is the relative mix of the profits between jurisdictions with higher tax rates (such as Indonesia and Malaysia), jurisdictions with lower tax rates (such as Hong Kong and Singapore), and jurisdictions with rates in between (such as the UK, and now from 2018, the US).

Once the US tax changes are fully reflected, we would expect a favourable impact on the Group's effective tax rate. The US operating profit effective tax rate is expected to be circa 18 per cent (previously 28 per cent), and the overall Group operating profit effective tax rate is likely to settle in the range of 16 per cent to 18 per cent.

Total tax contribution
The Group continues to make significant tax contributions in the jurisdictions in which it operates, with £2,903 million remitted to tax authorities in 2017. This was similar to the equivalent amount of £2,887 million in 2016.

Tax strategy
In May 2017 the Group published its tax strategy, which in addition to complying with the mandatory UK (Finance Act 2016) requirements, also included a number of additional disclosures, including a breakdown of revenues, profits and taxes for all jurisdictions where more than £5 million tax was paid. This disclosure was included as a way of demonstrating that our tax footprint (ie where we pay taxes) is consistent with our business footprint. An updated version of the tax strategy, including 2017 data, will be available on the Group's website before 31 May 2018.

New business performance

Life EEV new business profit and APE new business sales (APE sales)

	Actual exchange rate						Constant exchange rate			
	2017 £m		2016 £m		Change %		2016 £m		Change %	
	APE sales	New business profit	APE sales	New business profit	APE sales	New business profit	APE sales	New business profit	APE sales	New business profit
Asia	**3,805**	**2,368**	3,599	2,030	6	17	3,773	2,123	1	12
US	**1,662**	**906**	1,561	790	6	15	1,641	830	1	9
UK and Europe	**1,491**	**342**	1,160	268	29	28	1,160	268	29	28
Total Group	**6,958**	**3,616**	6,320	3,088	10	17	6,574	3,221	6	12

Life insurance new business profit was up 12 per cent (17 per cent on an actual exchange rate basis) to £3,616 million, and **Life insurance new business APE sales** increased by 6 per cent (10 per cent on an actual exchange rate basis) to £6,958 million.

In **Asia**, new business profit was 12 per cent higher at £2,368 million (17 per cent on an actual exchange rate basis), primarily reflecting the beneficial impact of our strategic emphasis on increasing sales from health and protection business and pricing actions.

Our focus on quality is undiminished with regular premium contracts accounting for 94 per cent of APE sales and supporting a 26 per cent increase in health and protection new business profit. This favourable mix provides a high level of recurring income and an earnings profile that is significantly less correlated to investment markets.

In Hong Kong new business profit has increased by 8 per cent as we continue to focus on driving growth in health and protection business. This targeted shift to higher margin but lower case size protection business, aligned with the de-emphasis of broker sales and the expected moderation in the level of sales from Mainland China has, as we reported previously, resulted in a 14 per cent reduction in Hong Kong APE sales.

Outside Hong Kong, new business profit increased by 20 per cent, in line with APE sales which were up 17 per cent. Our performance remains broad-based, with double digit growth in new business profit across both agency and bancassurance channels. In China, new business profit more than doubled, driven by higher sales and a significant uplift in regular premium health and protection business from our increased scale and productivity in the agency channel, together with a positive contribution from our bancassurance partners. In Singapore, new business profit increased by 22 per cent supported by APE sales growth of 21 per cent, reflecting growth across both agency and bancassurance channels. Indonesia's APE sales grew 2 per cent while new business profit declined 5 per cent due to product mix.

In **the US**, new business profit increased by 9 per cent to £906 million (up 15 per cent on an actual exchange rate basis) reflecting a modest increase in APE sales, up 1 per cent (6 per cent on an actual exchange rate basis) and the positive impact on future profit from a reduction in corporate income tax rates. Uncertainty regarding the application and implementation of the US Department of Labor Fiduciary Duty Rule has led to continued pressure on industry sales in 2017 which were down 11 per cent over the first nine months of the year. Despite this, Jackson's variable annuity sales increased by 1 per cent, with the economics on new business in variable annuities remaining extremely attractive, with high internal rates of return and short payback periods. Net inflows into Jackson's separate account asset balances, which drive fee-based earnings on variable annuity business, remained positive at £3.5 billion. More favourable market conditions relating to the institutional product market also provided Jackson with the opportunity to write APE sales of £232 million (2016: £193 million).

In our **UK life business**, our strategy of extending customer access to PruFund's with-profits investment option via additional product wrappers continues to drive growth in new business profit, which increased to £342 million, up 28 per cent. APE sales increased 29 per cent to £1,491 million. We have seen notable success with the build out of PruFund, which has contributed significantly towards an APE sales increase in individual pensions (up 110 per cent), income drawdown (up 35 per cent) and ISAs (up 7 per cent). Reflecting this performance, total PruFund assets under management of £35.9 billion as at 31 December 2017 were 46 per cent higher than at the start of the year.

Free surplus generation[2,3]

	Actual exchange rate			Constant exchange rate	
	2017 £m	2016 £m	Change %	2016 £m	Change %
Free surplus generation					
Asia	**1,562**	1,335	17	1,405	11
US	**1,582**	1,863	(15)	1,957	(19)
UK and Europe	**1,486**	1,287	15	1,287	15
Underlying free surplus generated from in-force life business and asset management before restructuring costs	**4,630**	4,485	3	4,649	-
Restructuring costs	**(77)**	(16)	(381)	(16)	(381)
Underlying free surplus generated from in-force life business and asset management	**4,553**	4,469	2	4,633	(2)
Investment in new business	**(913)**	(903)	(1)	(942)	3
Underlying free surplus generated	**3,640**	3,566	2	3,691	(1)
Market related movements, timing differences and other non-operating movements	**(1,012)**	(432)			
Profit (loss) attaching to disposal of businesses	**172**	(86)			
Net cash remitted by business units	**(1,788)**	(1,718)			
Total movement in free surplus	**1,012**	1,330			
Free surplus at end of year	**7,578**	6,566			

Free surplus generation is the financial metric we use to measure the internal cash generation of our business operations and is based on the capital regimes which apply locally in the various jurisdictions in which our life businesses operate. For life insurance operations it represents amounts maturing from the in-force business during the year, net of amounts reinvested in writing new business. For asset management it equates to post-tax IFRS operating profit for the period.

We drive free surplus generation by targeting markets and products that have low capital strain, high-return and fast payback profiles and by delivering both good service and value to improve customer retention. Our ability to generate both growth and cash is a distinctive feature of Prudential.

In 2017, underlying free surplus generation from our life insurance and asset management business decreased by 1 per cent to £3,640 million (increased 2 per cent on an actual exchange rate basis), reflecting increased contributions from our Asia and UK businesses, a non-recurrence of a one-off prior year gain from our US business, and higher restructuring costs. In Asia, growth in the in-force life portfolio, combined with post-tax asset management profit from Eastspring, contributed to free surplus generation of £1,562 million, up 11 per cent. In the US, in-force free surplus generation decreased by 19 per cent reflecting the non-recurrence of a £247 million benefit from contingent financing actions taken in 2016, together with lower favourable experience variances. In the UK, in-force free surplus generation increased by 15 per cent to £1,486 million, attributable to growth in asset management earnings, the adoption of the CMI 2015 assumption basis and portfolio and capital management actions including longevity reinsurance to improve the solvency position of our UK life business of £400 million (2016: £351 million). The result includes an increase in the provision for the costs of the UK review of past non-advised annuity sales practices and related potential redress, which has a post-tax impact of £187 million in 2017 (2016: £145 million).

Although new business profit increased by 12 per cent, the amount of free surplus invested in writing new life business in the period was lower at £913 million (2016: £942 million) reflecting a greater proportion of sales in Asia and the UK where strain is lower, and a higher proportion of variable annuity premium being allocated to the separate account in the US.

After funding cash remittances from the business units to the Group, recognition of the profit attaching to the disposal of businesses, and other movements, which includes adverse currency effects and the impact of US tax reform, the closing value of free surplus in our life and asset management operations was £7.6 billion at 31 December 2017.

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 capital in business opportunities.

Business unit remittance[2,16]

	Actual exchange rate	
	2017 £m	**2016 £m**
Net cash remitted by business units:		
Asia	**645**	516
US	**475**	420
UK and Europe	**643**	590
Other UK (including Prudential Capital)	**25**	192
Net cash remitted by business units	**1,788**	1,718
Holding company cash at 31 December	**2,264**	2,626

Cash remitted to the corporate centre in 2017 amounted to £1,788 million, driven by higher remittances from Asia. For the first time, our Asia business unit is the largest contributor[17] to cash in the Group, demonstrating the quality and scale of its growth. Jackson made sizeable remittances of £475 million. The remittance from M&G Prudential of £643 million was 9 per cent higher than the combined remittance in 2016. Prudential Capital contributed a further £25 million.

Cash remitted to the Group in 2017 was used to meet central costs of £470 million (2016: £416 million) and pay the 2016 second interim and 2017 first interim dividends respectively. These movements and other corporate cash flows, including a net reduction in core structural borrowings and the impact of currency movements, led to holding company cash decreasing from £2,626 million to £2,264 million over 2017.

***Post-tax profit - EEV*[2]**

	Actual exchange rate			Constant exchange rate	
	2017 £m	**2016 £m**	**Change %**	**2016 £m**	**Change %**
Post-tax operating profit based on longer-term investment returns					
Asia operations					
Long-term business	**3,705**	3,074	21	3,220	15
Asset management	**155**	125	24	132	17
Total	**3,860**	3,199	21	3,352	15
US operations					
Long-term business	**2,143**	1,971	9	2,071	3
Asset management	**7**	(3)	333	(4)	275
Total	**2,150**	1,968	9	2,067	4
UK and Europe operations					
Long-term business	**1,015**	643	58	643	58
General insurance commission	**13**	23	(43)	23	(43)
Total insurance operations	**1,028**	666	54	666	54
Asset management	**403**	341	18	341	18
Total	**1,431**	1,007	42	1,007	42
Other income and expenditure[18]	**(746)**	(682)	(9)	(688)	(8)
Post-tax operating profit based on longer-term investment returns before restructuring costs and interest received from tax settlement	**6,695**	5,492	22	5,738	17
Restructuring costs[18]	**(97)**	(32)	(203)	(32)	(203)
Interest received from tax settlement	**-**	37	n/a	37	n/a
Post-tax operating profit based on longer-term investment returns	**6,598**	5,497	20	5,743	15
Non-operating items:					
Short-term fluctuations on investment returns	**2,111**	(507)	516	(567)	472
Effect of changes in economic assumptions	**(102)**	(60)	(70)	(54)	(89)
Mark to market value movements on core structural borrowings	**(326)**	(4)	(8,050)	(4)	(8,050)
Impact of US tax reform	**390**	-	n/a	-	n/a
Profit (loss) attaching to disposal of businesses	**80**	(410)	120	(445)	118
Post-tax profit for the year	**8,751**	4,516	94	4,673	87

Earnings per share

	Actual exchange rate			Constant exchange rate	
	2017 pence	**2016 pence**	**Change %**	**2016 pence**	**Change %**
Basic earnings per share based on post-tax operating profit	**257.0**	214.7	20	224.3	15
Basic earnings per share based on post-tax total profit	**340.9**	176.4	93	182.5	87

EEV operating profit

On an EEV basis, Group post-tax operating profit based on longer-term investment return increased by 15 per cent (up 20 per cent on an actual exchange rate basis) to £6,598 million in 2017.

EEV operating profit includes new business profit from the Group's life business, which increased by 12 per cent (up 17 per cent on an actual exchange rate basis) to £3,616 million. It also includes in-force life business profit of £3,247 million, which was 20 per cent higher than prior year (up 25 per cent on an actual exchange rate basis), primarily reflecting the growth in our in-force business. This is most evident in the profit from the unwind of the in-force business, which was 10 per cent higher at £2,166 million (2016: £1,962 million). Experience and assumption changes were positive at £1,081 million (2016: £751 million), reflecting our ongoing focus on managing the in-force book for value.

In **Asia**, EEV life operating profit was up 15 per cent to £3,705 million, reflecting growth in new business profit of 12 per cent at £2,368 million. In-force profit was 22 per cent higher at £1,337 million reflecting the increased value of in-force business and positive assumption changes and experience as the business continues to grow with discipline.

Jackson's EEV life operating profit was up 3 per cent to £2,143 million, reflecting a 9 per cent increase in new business profit to £906 million and a stable contribution from in-force profit of £1,237 million, which included favourable operating assumption changes and experience variances of £543 million (2016: £628 million), related largely to persistency and mortality effects. The increase in our US EEV new business profit reflects the positive impact on future profits from lower tax rates.

In the **UK and Europe**, EEV life operating profit increased by 58 per cent to £1,015 million (2016: £643 million). The increase was driven by a 28 per cent increase in new business profit, and higher in-force profit including a £195 million benefit from revisions to longevity assumptions following adoption of updated actuarial mortality projections under CMI 2015[19]. Profits arising from actions undertaken to improve solvency were more than offset by an increase in the provision related to the potential costs and related potential redress of reviewing internally vesting annuities sold without advice after 1 July 2008.

Capital position, financing and liquidity
Capital position

Analysis of movement in Group shareholder Solvency II surplus[20]

	2017 £bn	2016 £bn
Solvency II surplus at 1 January	**12.5**	9.7
Operating experience	**3.6**	2.7
Non-operating experience (including market movements)*	**(0.6)**	(1.1)
Other capital movements:		
Subordinated debt (redemption) / issuance	**(0.2)**	1.2
Foreign currency translation impacts	**(0.7)**	1.6
Dividends paid	**(1.2)**	(1.3)
Model changes	**(0.1)**	(0.3)
Estimated Solvency II surplus at 31 December	**13.3**	12.5

* 2017 includes a £(0.6) billion reduction in deferred tax assets following US tax reform.

The high quality and recurring nature of our operating capital generation and our disciplined approach to managing balance sheet risk has resulted in an increase in the Group's shareholders' Solvency II capital surplus which is estimated at £13.3 billion[6,7] at 31 December 2017 (equivalent to a solvency ratio of 202 per cent), compared with £12.5 billion (201 per cent) at 31 December 2016. In 2017 we generated £3.6 billion of operating capital. This was offset by dividends to shareholders, net repayment of subordinated debt, adverse foreign currency effects and the £0.6 billion reduction in statutory deferred tax assets following US tax reform.

Prudential has been designated as a Global Systemically Important Insurer (G-SII) and is monitoring and engaging with the PRA on the development and potential impact of the policy measures associated with such a designation.

Local statutory capital

All of our subsidiaries continue to hold appropriate capital levels on a local regulatory basis. In the UK, at 31 December 2017 The Prudential Assurance Company Limited and its subsidiaries[21] had an estimated Solvency II shareholder surplus[22] of £6.1 billion (equivalent to a cover ratio of 178 per cent) and a with-profits surplus[23] of £4.8 billion (equivalent to a cover ratio of 201 per cent). In the US, following the enactment in December 2017 of a comprehensive reform package, a £628 million reduction in the level of the statutory net admitted deferred tax asset more than offset operational capital formation, resulting in a risk based capital ratio of 409 per cent (2016: 485 per cent).

Debt portfolio

The Group continues to maintain a high-quality defensively positioned debt portfolio. Shareholders' exposure to credit is concentrated in the UK annuity portfolio and the US general account, mainly attributable to Jackson's fixed annuity portfolio. The credit exposure is well diversified and 98 per cent of our UK portfolio and 97 per cent of our US portfolio are investment grade[29]. During 2017, default losses were minimal and reported impairments across the UK and US portfolios were £2 million (2016: £35 million).

Financing and liquidity

Shareholders' net core structural borrowings and ratings

	2017 £m			2016 £m		
	IFRS basis	Mark to market value	EEV basis	IFRS basis	Mark to market value	EEV basis
Total borrowings of shareholder-financed operations	**6,280**	**743**	**7,023**	6,798	422	7,220
Less: Holding company cash and short-term investments	**(2,264)**	**-**	**(2,264)**	(2,626)	-	(2,626)
Net core structural borrowings of shareholder-financed operations	**4,016**	**743**	**4,759**	4,172	422	4,594
Gearing ratio*	**20%**			22%		

* Net core structural borrowings as proportion of IFRS shareholders' funds plus net debt, as set out in note II(d) of the Additional unaudited IFRS financial information.

The Group had central cash resources of £2.3 billion at 31 December 2017 (31 December 2016: £2.6 billion). Total core structural borrowings reduced by £0.5 billion, from £6.8 billion to £6.3 billion, with the issue of US$750 million (£547 million at 31 December 2017) 4.875 per cent tier 2 perpetual subordinated debt in October 2017 being more than offset by the redemption of US$1 billion (£741 million at 31 December 2017) 6.5 per cent tier 2 perpetual subordinated debt in December 2017.

In addition to its net core structural borrowings of shareholder-financed operations set out above, the Group also has access to funding via the money markets and has in place an unlimited global commercial paper programme. As at 31 December 2017, we had issued commercial paper under this programme totalling US$650 million, to finance non-core borrowings.

Prudential's holding company currently has access to £2.6 billion of syndicated and bilateral committed revolving credit facilities provided by 19 major international banks, expiring in 2022. Apart from small drawdowns to test the process, these facilities have never been drawn, and there were no amounts outstanding at 31 December 2017. The medium-term note programme, the US shelf programme (platform for issuance of SEC registered public bonds in the US market), 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 flexible funding capacity.

Shareholders' funds

	IFRS		EEV	
	2017 £m	**2016 £m**	**2017 £m**	**2016 £m**
Profit after tax for the year[24]	**2,389**	1,921	**8,750**	4,516
Exchange movements, net of related tax	**(409)**	1,161	**(2,045)**	4,211
Cumulative exchange gain of Korea life business recycled to profit and loss account	**(61)**	-	**-**	-
Unrealised gains and losses on Jackson fixed income securities classified as available for sale[25]	**486**	31	**-**	-
Dividends	**(1,159)**	(1,267)	**(1,159)**	(1,267)
Market to market value movements on Jackson assets backing surplus and required capital	**-**	-	**40**	(11)
Other	**175**	(135)	**144**	(367)
Net increase in shareholders' funds	**1,421**	1,711	**5,730**	7,082
Shareholders' funds at 1 January	**14,666**	12,955	**38,968**	31,886
Shareholders' funds at 31 December	**16,087**	14,666	**44,698**	38,968
Shareholders' value per share [26]	**622p**	568p	**1,728p**	1,510p
Return on shareholders' funds[27]	**25%**	26%	**17%**	17%

Group IFRS shareholders' funds at 31 December 2017 increased by 10 per cent to £16.1 billion (31 December 2016: £14.7 billion on an actual exchange rate basis), driven by the strength of the operating result, offset by dividend payments of £1,159 million. During the period, UK sterling has strengthened relative to the US dollar and various Asian currencies. With approximately 50 per cent of the Group's IFRS net assets (71 per cent of the Group's EEV net assets) denominated in non-sterling currencies, this generated a negative exchange rate movement on the net assets in the period. In addition, the moderate decline in US long-term interest rates between the start and the end of the reporting period produced unrealised gains on fixed income securities held by Jackson accounted through other comprehensive income.

The Group's EEV basis shareholders' funds also increased by 15 per cent to £44.7 billion (31 December 2016: £39.0 billion on an actual exchange rate basis), On a per share basis the Group's embedded value at 31 December 2017 equated to 1,728 pence, up from 1,510 pence at 31 December 2016.

Corporate transactions

Intention to demerge the Group's UK businesses and sale of £12.0 billion[30] UK annuity portfolio

In March 2018, the Group announced its intention to demerge its UK and Europe businesses ('M&G Prudential') from Prudential plc, resulting in two separately-listed companies. On completion of the demerger, shareholders will hold interests in both Prudential plc and M&G Prudential.

In preparation for the UK demerger process, and to align the ownership of the Group's businesses with their operating structures, Prudential plc intends to transfer the legal ownership of its Hong Kong insurance subsidiaries from The Prudential Assurance Company Limited (M&G Prudential's UK regulated insurance entity) to Prudential Corporation Asia Limited, which is expected to complete by the end of 2019.

M&G Prudential agreed in March 2018 to the sale of £12.0 billion[30] of its shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, M&G Prudential has reinsured £12.0 billion[30] of liabilities to Rothesay Life, which is expected to be followed by a Part VII transfer of the portfolio by the end of 2019. The capital benefit of this transaction will be retained within the Group to support the demerger process.

The IFRS liabilities relating to M&G Prudential's total UK shareholder annuity portfolio as at 31 December 2017 were £32.6 billion. The UK annuity business being sold contributed around £140 million towards UK life insurance core[5] IFRS operating profit before tax of £597 million in 2017. Total M&G Prudential IFRS operating profit before tax was £1,378 million in 2017.

Based on asset and liability values as at 31 December 2017, the transaction is estimated to give rise to a pre-tax IFRS loss of around £500 million in the first half of 2018, alongside the de-risking being achieved.

Prudential plc's Hong Kong subsidiaries which are subject to legal transfer from The Prudential Assurance Company Limited to Prudential Corporation Asia Limited comprise its life business, Prudential Hong Kong Limited, and its general insurance business, Prudential General Insurance Hong Kong Limited. Hong Kong will continue to be included in the segmental reporting of Asia's IFRS and embedded value results. The transfers will be subject to regulatory approval.

The sale of the UK annuity portfolio and the transfer of Prudential plc's Hong Kong subsidiaries to Asia are expected to complete by the end of 2019. Assuming that these actions had both been completed as at 31 December 2017, the Group's embedded value of £44.7 billion is estimated to reduce by approximately £300 million, reflecting the loss of future profits on the portion of annuity liabilities being sold.

The estimated pro-forma impact on the Group shareholder Solvency II capital position, assuming that these actions had both been completed as at 31 December 2017, is an increase in surplus of £0.3 billion and an increase in the shareholder solvency ratio of 6 percentage points.

Pro-forma estimated Group shareholder Solvency II capital position

	Own Funds	Solvency Capital Requirement	Surplus	Ratio
	£bn	£bn	£bn	%
31 December 2016 as reported	24.8	12.3	12.5	201
31 December 2017 as reported	26.4	13.1	13.3	202
31 December 2017 pro-forma estimate*	26.2	12.6	13.6	208

* The pro-forma estimate assumes that the partial sale of the UK annuity portfolio and the transfer of Prudential plc's Hong Kong subsidiaries to Asia had both been completed as at 31 December 2017.

On the same basis, the estimated pro-forma impact on the shareholder Solvency II capital position of the UK regulated insurance entity, The Prudential Assurance Company Limited, is provided in the table below. This pro-forma solvency position reflects the reduced risk exposures in the UK insurance entity after the partial annuity sale and Hong Kong transfer.

Pro-forma estimated The Prudential Assurance Company Limited shareholder Solvency II capital position

	Own Funds	Solvency Capital Requirement	Surplus	Ratio
	£bn	£bn	£bn	%
31 December 2016 as reported	12.0	7.4	4.6	163
31 December 2017 as reported	14.0	7.9	6.1	178
31 December 2017 pro-forma estimate*	8.5	5.7	2.8	150

* The pro-forma estimate assumes that the partial sale of the UK annuity portfolio and the transfer of Prudential plc's Hong Kong subsidiaries to Asia had both been completed as at 31 December 2017. In relation to the sale of the UK annuity portfolio, this estimate includes a £1.3 billion reduction in the Solvency Capital Requirement (SCR) and a £0.2 billion decrease in Own Funds, resulting in an increase in capital surplus of £1.1 billion, of which £0.6 billion is expected to be recognised in the UK capital position as at 30 June 2018 under the reinsurance agreement. In relation to the Hong Kong transfer, the impact on the SCR allows for the release of the Hong Kong business standalone SCR of £2.0 billion, partially offset by the removal of diversification benefits between UK and Hong Kong of £1.1 billion.

Entrance into Nigeria

In July 2017 the Group acquired a majority stake in Zenith Life of Nigeria and formed exclusive bancassurance partnerships with Zenith Bank in Nigeria and Ghana. The acquisition and bancassurance partnerships will see Prudential enter the market in Nigeria, Africa's largest economy, with a population of over 180 million. This expands Prudential's regional platform in Africa following the launch of businesses in Ghana and Kenya in 2014, in Uganda in 2015 and Zambia in 2016.

Disposal of Korea life

In May 2017, the Group completed the sale of the Group's life insurance subsidiary in Korea, PCA Life Insurance Co. Ltd to Mirae Asset Life Insurance Co. Ltd. for KRW170 billion (equivalent to £117 million at 17 May 2017 closing rate).

Disposal of broker-dealer network in the US

In August 2017, the Group, through its subsidiary National Planning Holdings, Inc. ('NPH') sold its US independent broker-dealer network to LPL Financial LLC for an initial purchase price of US$325 million (equivalent to £252 million at 15 August 2017).

Dividend

The Board has decided to increase the full-year ordinary dividend by 8 per cent to 47 pence per share, reflecting our 2017 financial performance and our confidence in the future prospects of the Group. In line with this, the directors have approved a second interim ordinary dividend of 32.5 pence per share (2016: 30.57 pence per share).

The Group's dividend policy remains unchanged. The Board will maintain focus on delivering a growing ordinary dividend. In line with this policy, Prudential aims to grow the ordinary dividend by 5 per cent per annum. The potential for additional distributions will continue to be determined after taking into account the Group's financial flexibility across a broad range of financial metrics and an assessment of opportunities to generate attractive returns by investing in specific areas of the business[28].

Notes

1 Increase stated on a constant exchange rate basis.
2 The 2016 comparative results have been re-presented from those published previously, following reassessment of the Group's operating segments as described in note B1.3 of the IFRS financial statements.
3 Underlying free surplus generated comprises underlying free surplus generated from the Group's long-term business (net of investment in new business) and that generated from asset management operations. Further information is set out in notes 11 of the EEV basis results. Free surplus represents 'underlying free surplus' based on operating movements and excludes market movements, foreign exchange, capital movements, shareholders' other income and expenditure and restructuring and Solvency II implementation costs arising centrally.
4 Represents M&G Prudential asset management external funds under management and internal funds included on the M&G Prudential long-term insurance business balance sheet.
5 Core refers to the underlying profit of the UK and Europe insurance business excluding the effect of, for example, management actions to improve solvency and material assumption changes. Details of these are set out in note I(d) of the Additional unaudited IFRS financial information.
6 The Group shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds and staff pension schemes in surplus. The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.
7 Before allowing for second interim ordinary dividend.
8 Refer to note B1.1 in IFRS financial statements for the breakdown of other income and expenditure and other non-operating items.
9 Gross earned premiums for contracts in second and subsequent years, comprising Asia segment IFRS gross earned premium of £15.7 billion less gross earned premiums relating to new regular and single premiums of £5.7 billion, plus renewal premiums from joint ventures of £1.6 billion, and excluding any amounts relating to the sold Korea life business.
10 Includes Group's proportionate share of the liabilities and associated flows of the insurance joint ventures and associates in Asia.
11 Defined as movements in shareholder-backed policyholder liabilities arising from premiums (net of charges), surrenders/withdrawals, maturities and deaths.
12 Includes Unallocated surplus of with-profits business.
13 Includes Group's proportionate share in PPM South Africa and the Asia asset management joint ventures.
14 For our asset management business the level of funds managed on behalf of third parties, which are not therefore recorded on the balance sheet, is a driver of profitability. We therefore analyse the movement in the funds under management each period, focusing between those which are external to the Group and those held by the insurance business and included on the Group balance sheet. This is analysed in note II(b) of the Additional unaudited IFRS financial information.
15 Net inflows exclude Asia Money Market Fund (MMF) inflows of £1,495 million (2016: net inflows £403 million). External funds under management exclude Asia MMF balances of £9,317 million (2016: £7,714 million).
16 Net cash remitted by business units are included in the Holding company cash flow, which is disclosed in detail in note II(a) of the Additional unaudited IFRS financial information.
17 Based on the 2017 operating segments.
18 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 further detail on other income and restructuring costs.
19 Continuous Mortality Investigation 2015 mortality improvements model.
20 The methodology and assumptions used in calculating the Solvency II capital results are set out in note II(f) of the Additional unaudited IFRS financial information.
21 The insurance subsidiaries of The Prudential Assurance Company Limited are Prudential General Insurance Hong Kong Limited, Prudential Hong Kong Limited, Prudential International Assurance plc and Prudential Pensions Limited.
22 The UK shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds and staff pension schemes in surplus. The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.
23 The estimated solvency position includes management's calculation of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.
24 Excluding profit for the year attributable to non-controlling interests.
25 Net of related charges to deferred acquisition costs and tax.
26 Closing IFRS shareholders' funds divided by issued shares, as set out in note II(e) of the Additional unaudited IFRS financial information. Closing EEV shareholders' funds divided by issued shares, as set out in note G of the Additional EEV financial information.
27 Operating profit after tax and non-controlling interests as percentage of opening shareholders' funds, as set out in note II(c) of the Additional unaudited IFRS financial information and note F of the Additional EEV financial information.
28 Refer to note 11 on the parent company financial statements for further detail on the distributable profits of Prudential plc.
29 Based on hierarchy of Standard and Poor's Moody's and Fitch, where available and if unavailable, internal ratings have been used.
30 Relates to £12.0 billion of IFRS shareholder annuity liabilities, valued as at 31 December 2017.

Report of the risks facing our business and how these are managed

1. Introduction

2017 was, in many respects, a year of global geopolitical transition. Popular discontent was one of the driving factors, shifting the political landscape in many countries, in particular in the US and across Western Europe. The nature of technology risks evolved during the year, with high profile and untargeted attacks affecting companies around the world. Despite all this, financial markets appeared largely unperturbed during 2017 with low volatility and steady and broad global economic growth, and the first steps were taken toward monetary policy tightening in key economies.

As in previous years, we continue to maintain a sustained focus on managing prevailing market conditions and macroeconomic uncertainty arising from the global environment. Looking internally, in August 2017 we announced our intention to combine M&G and our UK life business to form M&G Prudential, allowing us better to leverage our scale and capabilities. Change inherently carries risk, but we will manage and minimise this appropriately in order to provide better outcomes for our customers.

Our results show that, even in times of unpredictability, we can generate value for our shareholders by taking selective exposure to risks that are rewarded commensurately and that can be quantified appropriately and managed. We retain risks within a clearly defined risk appetite, where we believe doing so contributes to value creation and the Group is able to withstand the impact of an adverse outcome. For our retained risks, we ensure that we have the necessary capabilities, expertise, processes and controls to manage the exposure appropriately.

Our Group Risk Framework and risk appetite have allowed us to control our risk exposure successfully throughout the year. Our governance, processes and controls enable us to deal with the uncertainty ahead in order to continue helping our customers achieve their long-term financial goals.

This section explains the main risks inherent in our business and how we manage those risks, with the aim of ensuring we maintain an appropriate risk profile.

2. Risk governance, culture and our risk management cycle

Prudential defines 'risk' as the uncertainty that we face in implementing our strategies and objectives successfully. This includes all internal or external events, acts or omissions that have the potential to threaten the success and survival of the Group. Accordingly, material risks will be retained selectively when we think there is value to do so, and where it is consistent with the Group's risk appetite and philosophy towards risk-taking.

The following section provides more detail on our risk governance, risk culture and risk management process.

a. Risk governance

Our risk governance comprises the Board, organisational structures, reporting relationships, delegation of authority, roles and responsibilities, and risk policies that the Group Head Office and our business units establish to make decisions and control their activities on risk-related matters. This encompasses individuals, Group-wide functions and committees involved in overseeing and managing risk.

i. Risk committees and governance structure

Our risk governance structure is led by the Group Risk Committee, supported by independent non-executives on risk committees of major subsidiaries. These committees monitor the development of the Group Risk Framework, which includes risk appetite, limits, and policies, as well as risk culture.

In addition to our risk committees, there are various executive risk forums to ensure risk issues are shared and considered across the Group. These are led by the Group Executive Risk Committee, an advisory committee to the Group Chief Risk Officer which is supported by a number of sub-committees, including security and information security where specialist skills and knowledge are required.

ii. Group Risk Framework

The Group Risk Framework has been developed to monitor and manage the risks to our business and is owned by the Board. The aggregate Group exposure to our key risk drivers is monitored and managed by the Group Risk function which is responsible for reviewing, assessing and reporting on the Group's risk exposure and solvency position from the Group economic, regulatory and ratings perspectives.

The Framework requires all our businesses and functions to establish processes for identifying, evaluating, managing and reporting of the key risks faced by the Group – the 'Risk Management Cycle' (see below) is based on the concept of the 'three lines of defence', comprising risk taking and management, risk control and oversight, and independent assurance.

A major part of the Risk Management Cycle is the annual assessment of the Group's most material risks. These risks range from those associated with the economic, market, political and regulatory environment; those that we assume when writing our insurance products and by virtue of the investments we hold; and those that are inherent in our business model and its operations. This is used to inform risk reporting to the risk committees and the Board for the year.

The Group Risk Committee reviews the Group Risk Framework and recommends changes to our Board to ensure that it remains effective in identifying and managing the risks faced by the Group. A number of core risk policies and standards support the Framework to ensure that risks to the Group are identified, assessed, managed and reported.
During 2017 we made a number of enhancements to our policies and processes. These included changes to our processes around new product approvals, management of our critical outsourcing arrangements and increased oversight

of model risk across the Group. A new framework was developed to support the monitoring and reporting of risks associated with material transformation programmes, and work continued over the year on the Group's risk culture.

iii. Risk appetite, limits and triggers

The extent to which we are willing to take risk in the pursuit of our business strategy and objective to create shareholder value is defined by a number of qualitative and quantitative expressions of risk appetite, operationalised through measures such as limits, triggers, thresholds and indicators. The Group Risk function is responsible for reviewing the scope and operation of these risk appetite measures at least annually to determine that they remain relevant. The Board approves all changes made to the Group's aggregate risk appetite, and has delegated authority to the Group Risk Committee to approve changes to the system of limits, triggers and indicators.

Group risk appetite is set with reference to economic and regulatory capital, liquidity and earnings volatility, as well as for our major risks, and is aimed at ensuring that we take an appropriate level of aggregate risk. It covers risks to shareholders, including those from participating and third-party business.

We have some appetite to take market and credit risk where it arises from profit-generating insurance activities, to the extent that it remains part of a balanced portfolio of sources of income for shareholders and is compatible with a robust solvency position. We also have some appetite for retaining insurance risks in areas where we believe we have expertise and operational controls, and where we judge it to create more value to retain rather than transfer the risk. The extent of insurance risk that we are willing to hold is conditional on a balanced portfolio of income to shareholders and compatibility with a robust solvency position.

We have no appetite for material losses (direct or indirect) suffered as a result of failing to develop, implement or monitor appropriate controls to manage operational risks. Similarly, we have no appetite for liquidity risk, ie for any business to have insufficient resources to cover its outgoing cash flows, or for the Group as a whole to not meet cash flow requirements from its debt obligations under any plausible scenario.

Group limits operate within these expressions of risk appetite to constrain material risks, while triggers and indicators provide further constraint and ensure escalation. The Group Chief Risk Officer determines the action to be taken upon all breaches of Group limits which may include escalation to the Group Risk Committee or Board. Any decision on action taken by the Group Chief Risk Officer is reviewed at the subsequent Group Risk Committee meeting.

Earnings volatility:

The objectives of the aggregate risk limits seek to ensure that:

- The volatility of earnings is consistent with the expectations of stakeholders;
- The Group has adequate earnings (and cash flows) to service debt, expected dividends and to withstand unexpected shocks; and
- 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 IFRS operating profit and EEV operating profit, although IFRS and EEV 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. Risk appetite with respect to liquidity risk is measured using a Liquidity Coverage Ratio which considers the sources of liquidity against liquidity requirements under stress scenarios.

Capital requirements:

The limits aim to ensure that:

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

The two measures used at the Group level are Solvency II capital requirements and internal economic capital (ECap) requirements. In addition, capital requirements are monitored on local statutory bases.

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 from our local business units to calculate the Group's aggregated position (allowing for diversification effects between local business units) relative to the aggregate risk limits.

iv. Risk policies

These set out the specific requirements which cover the fundamental principles for risk management within the Group Risk Framework. Policies are designed to give some flexibility so that business users can determine how best to comply with policies based on their local expertise.

There are core risk policies for credit, market, insurance, liquidity and operational risks and a number of internal control policies covering internal model risk, underwriting, dealing controls and tax risk management. 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 maintain in line with the UK Corporate Governance Code and the Hong Kong Code on Corporate Governance Practices. Group Head Office and business units must confirm on an annual basis that they have implemented the necessary controls to evidence compliance with the Group Governance Manual.

v. **Risk standards**

The Group-wide Operating Standards provide supporting detail to the higher level risk policies. In many cases they define the minimum requirements for compliance with Solvency II regulations which in some areas are highly prescriptive. The standards are more detailed than policies.

b. Our risk culture

Culture is a strategic priority of the Board who recognise the importance of good culture in the way that we do business. Risk culture is a subset of broader organisational culture, which shapes the organisation-wide values that we use to prioritise risk management behaviours and practices.

An evaluation of risk culture forms part of the Group Risk Framework and in particular seeks to identify evidence that:

- Senior management in business units articulate the need for good risk management as a way to realise long-term value and continuously support this through their actions;
- Employees understand and care about their role in managing risk – they are aware of and discuss risk openly as part of the way they perform their role; and
- Employees invite open discussion on the approach to the management of risk.

During 2017 a risk culture assessment was performed across the Group. The assessment allowed us to compare the Group's risk culture against best practice behaviours, identify any areas which need improvement and provide high-level industry benchmarking and peer comparison. The Group Risk Committee also has a key role in providing advice to the Remuneration Committee on risk management considerations to be applied in respect of executive remuneration.

Our Code of Conduct and our Group Governance Manual include a series of guiding principles that govern the day-to-day conduct of all our people and any organisations acting on our behalf. This is supported by specific risk policies which require that we act in a responsible manner. This includes, but is not limited to, policies on anti-money laundering, financial crime and anti-bribery and corruption. Our Group outsourcing and third-party supply policy ensures that human rights and modern slavery considerations are embedded within all of our supplier and supply chain arrangements. We also have embedded procedures to allow individuals to speak out safely and anonymously against unethical behaviour and conduct.

c. The risk management cycle

The risk management cycle comprises processes to identify, measure and assess, manage and control, and monitor and report on our risks.

i. **Risk identification**

Group-wide risk identification takes place throughout the year and includes processes such as our Own Risk and Solvency Assessment (ORSA) and the horizon-scanning performed as part of our emerging risk management process.

On an annual basis, a top-down identification of the Group's key risks is performed, which considers those risks that have the greatest potential to impact the Group's operating results and financial condition. A bottom-up process of risk identification is performed by the business units who identify, assess and document risks, with appropriate coordination and challenge from the risk functions.

The Group ORSA report pulls together the analysis performed by a number of risk and capital management processes, which are embedded across the Group, and provides quantitative and qualitative assessments of the Group's risk profile, risk management and solvency needs on a forward-looking basis. The scope of the report covers the full known risk universe of the Group.

In accordance with provision C.2.1 of the UK Code, the Directors perform a robust assessment of the principal risks facing the Company through the Group-wide risk identification process, Group ORSA report, and the risk assessments done as part of the business planning review, including how they are managed and mitigated.

Reverse stress testing, which requires us to ascertain the point of business model failure, is another tool that helps us to identify the key risks and scenarios that may have a material impact on the Group.

Our emerging risk management process identifies potentially material risks which have a high degree of uncertainty around timing, magnitude and propensity to evolve. In 2017 we enhanced our Emerging Risk Framework to bring it closer to the Group's risk management activity. This included a redefinition of the relationship between emerging and emerged risks, enabling a consistent framework for evaluating and escalating sufficiently developed emerging risks for risk management activity. The Group holds emerging risk sessions over the year to identify emerging risks which includes input from local subject matter and industry experts. We maintain contacts with thought leaders and peers to benchmark and refine our process.

The risk profile is a key output from the risk identification and risk measurement processes, and is used as a basis for setting Group-wide limits, management information, assessment of solvency needs, and determining appropriate stress and scenario testing. The risk identification processes support the creation of our annual set of key risks, which are then given enhanced management and reporting focus.

ii. **Risk measurement and assessment**

All identified risks are assessed based on an appropriate methodology for that risk. All quantifiable risks which are material and mitigated by holding capital are modelled in the Group's internal model, which is used to determine capital requirements under Solvency II and our own economic capital basis. Governance arrangements are in place to support the internal model, including independent validation and process and controls around model changes and limitations.

iii. Risk management and control

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

The management and control of risks are set out in the Group risk policies, and form part of the holistic risk management approach under the Group's ORSA. These risk policies define:

- The Group's risk appetite in respect of material risks, and the framework under which the Group's exposure to those risks is limited;
- The processes to enable Group senior management to effect the measurement and management of the Group material risk profile in a consistent and coherent way; and
- The flows of management information required to support the measurement and management of the Group material risk profile and to meet the needs of external stakeholders.

The methods and risk management tools we employ to mitigate each of our major categories of risks are detailed in section 4 below.

iv. Risk monitoring and reporting

The identification of the Group's key risks informs the management information received by the Group risk committees and the Board. Risk reporting of key exposures against appetite is also included, as well as ongoing developments in other key and emerging risks.

3. Summary risks

The components of our business model give rise to risks of varying nature across the Group which can broadly be categorised as those which arise as a result of our business operations; those risks arising from our investments; those which arise from the nature of our products; and those broad risks which apply to us because of the global environment in which we operate. These risks, where they materialise, may have a financial impact on the Group, and could also impact on the performance of our products or the services we provide our customers and distributors, which gives rise to potential risks to our brand, reputation and have conduct risk implications. These risks are summarised below. We have indicated whether these risks are considered material at the level of the Group or our business units. Our disclosures covering risk factors can be found at the end of this document.

'Macro' – risks

Some of the risks that we are exposed to are necessarily broad given the external influences which may impact on the Group. These risks include:

- **Global economic conditions.** Changes in global economic conditions can impact us directly; for example by leading to poor returns on our investments and increasing the cost of promises (guarantees) we have made to our customers. Our fund investment performance may also be impacted, which is a fundamental part of our business in providing appropriate returns for our customers and shareholders. Changes in economic conditions can also have an indirect impact on us; for example economic pressures could lead to decreased savings, reducing the propensity for people to buy our products. Global economic conditions may also impact on regulatory risk for the Group by changing prevailing political attitudes towards regulation. We consider this to be a risk which is material at the level of the Group.

- **Geopolitical risk.** The geopolitical environment has produced varying levels of volatility in recent years as seen by political developments in the UK, the US and the Eurozone. Uncertainty in these regions, combined with conflict in the Middle East and elevated tensions in east Asia and the Korean peninsula underline that geopolitical risks are truly global and their potential impacts are wide-ranging; for example through increased regulatory and operational risks. The geopolitical and economic environments are increasingly closely linked, and changes in the political arena may have direct or indirect impacts on our Group.

- **Digital disruption.** The emergence of advanced technologies such as artificial intelligence and block chain is providing an impetus for companies to rethink their existing operating models and how they interact with their customers. We consider digital disruption from both an external and internal view. The external view considers the rise of new technologies and how this may impact on our industry and our competitiveness within it, while the internal view considers the risks associated with our own internal developments in meeting digital change challenges and opportunities. While we are embracing such opportunities, we are also closely monitoring any risks which arise.

Risks from our investments	Risks from our products	Risks from our business operations

Risks from our investments

Credit risk
Is the potential for reduced value of our investments due to the uncertainty around investment returns arising from the potential for defaults of our investment counterparties. Invested credit risk arises from our asset portfolio. We increase sector focus where necessary.

The assets backing the M&G Prudential and Jackson annuity businesses means credit risk is considered a material risk for these business units in particular.

Market risk
Is the potential for reduced value of our investments resulting from the volatility of asset prices as driven by fluctuations in equity prices, interest rates, foreign exchange rates and property prices. Certain market risks are considered more material for specific business units.

In our Asia business, our main market risks arise from the value of fees from our fee-earning products. In the US, Jackson's fixed and variable annuity books are exposed to a variety of market risks due to the assets backing these policies.

In the UK, exposure arises from the valuation of the proportion of the with-profits fund's future profits which is transferred to the shareholders (future transfers), which is dependent on equity, property and bond values. M&G Prudential invests in a broad range of asset classes and its income is subject to the price volatility of global financial and currency markets.

Liquidity risk
Is the risk of not having sufficient liquid assets to meet our obligations as they fall due, and incorporates the risk arising from funds composed of illiquid assets. It results from a mismatch between the liquidity profile of assets and liabilities. We consider this a risk which is material at the level of the Group.

Risks from our products

Insurance risks
The nature of the products offered by the Group exposes it to insurance risks, which we consider to form a significant part of our overall Group risk profile.

The insurance risks that we are exposed to by virtue of our products include **longevity risk** (policyholders living longer than expected); **mortality risk** (policyholders with life protection dying); **morbidity risk** (policyholders with health protection becoming ill) and **persistency risk** (customers lapsing their policies, and a type of policyholder behaviour risk).

From our health protection products, increases in the costs of claims (including the level of medical expenses) increasing over and above price inflation (claim inflation) is another risk.

The processes that determine the price of our products and reporting the results of our long-term business operations require us to make a number of assumptions. Where experience deviates from these assumptions our profitability may be impacted.

Across our business units, some insurance risks are more material than others.

Persistency and morbidity risks are among the most material insurance risks for our Asia business given our focus on health protection products in the region.

For M&G Prudential the most material insurance risk is longevity risk driven by legacy annuity business.

At Jackson, the most material insurance risk is policyholder behaviour risk, including persistency. This impacts the profitability of the variable annuity business and influenced by market performance and the value of policy guarantees.

Risks from our business operations

Operational risks
The complexity of our Group and activities means we face a challenging operating environment. This results from the high volume of transactions we process; product and investment portfolios; our people, processes and IT systems; and the extensive regulations under which we operate.

We also face operational risks through business transformation; introducing new products; new technologies; engaging in third party relationships; and entering into new markets and geographies. Implementing our business strategy requires interconnected change initiatives across the Group. The pace of change further adds to the complexity of our operational risk profile.

Without an effective operational risk framework, such risks could cause significant disruption our systems and operations, resulting in financial loss and/or reputational damage. We consider operational risk to be material at the level of the Group.

Information security risk is a significant consideration within operational risk, including both the continuously evolving risk of malicious attack on our systems as well as risks relating to data security and integrity and network disruption. The size of Prudential's IT infrastructure and network, our move toward digitalisation and the increasing number of high profile cyber security incidents across industries means that this risk will continue to be an area of high focus and is one considered to be material to the Group.

Regulatory risk
We also operate under the ever-evolving requirements set out by diverse regulatory and legal and tax regimes, as well as utilising a significant number of third parties to distribute products and to support business operations; all of which adds to the complexity of our operations.

The number of regulatory changes under way across Asia, in particular those focusing on consumer protection means that regulatory change in the region is considered a key risk.

Both Jackson and M&G Prudential operate in highly regulated markets. Regulatory reforms can have a material impact on our businesses, and regulatory focus continues to be high.

4. Further risk information

In reading the sections below, it is useful to understand that there are some risks that our policyholders assume by virtue of the nature of their products, and some risks that the Company and its shareholders assume. Examples of the latter include those risks arising from assets held directly by and for the Company or the risk that policyholder funds are exhausted. This report is focused mainly on risks to the shareholder, but will include those which arise indirectly through our policyholder exposures.

4.1 Risks from our investments

a. Market risk

The main drivers of market risk in the Group are:

- Investment risk (including equity and property risk);
- Interest rate risk; and
- Given the geographical diversity of our business, foreign exchange risk.

With respect to investment risk, equity and property risk arises from our holdings of equity and property investments, the prices of which can change depending on market conditions.

The valuation of our assets (particularly the bonds that we invest in) and liabilities are also dependent on market interest rates and exposes us to the risk of those moving in a way that is detrimental for us.

Given our global business, we earn our profits and have assets and liabilities in various currencies. The translation of those into our reporting currency exposes us to movements in foreign exchange rates.

Our main investment risk exposure arises from the portion of the profits from the M&G Prudential with-profits fund to which we are entitled to receive; the value of the future fees from our fee-earning products in our Asia business; and from the asset returns backing Jackson's variable annuities business.

Our interest rate risk is driven in the UK business by our need to match the duration of our assets and liabilities; from the guarantees of some non unit-linked investment products in Asia; and the cost of guarantees in Jackson's fixed, fixed index and variable annuity business.

The methods that we use to manage and mitigate our market risks include the following:

- Our market risk policy;
- Risk appetite statements, limits and triggers that we have in place;
- The monitoring and oversight of market risks through the regular reporting of management information;
- Our asset and liability management programmes;
- Use of derivative programmes, including, for example, interest rate swaps, options and hybrid options for interest rate risk;
- Regular deep dive assessments; and
- Use of currency hedging.

<u>Investment risk</u>

In the UK business, our main investment risk arises from the assets held in the with-profits funds. Although this is mainly held by our policyholders, a proportion of the funds' declared bonuses and policyholder net investment gains is shared with shareholders and so our investment exposure relates to the future performance of that proportion (future transfers).

This investment risk is driven mainly by equities in the funds, although there is some risk associated with other investments such as property and bonds. Some hedging to protect against a reduction in the value of these future transfers against falls in equity prices is performed outside the funds using derivatives. The with-profits funds' large Solvency II own funds – estimated at £9.6 billion as at 31 December 2017 (31 December 2016: £8.4 billion) – helps to protect against market fluctuations and helps the funds to maintain appropriate solvency levels. The with-profits funds' Solvency II own funds are protected partially against falls in equity markets through an active hedging programme within the fund.

In Asia, our shareholder exposure to equity price movements results from unit-linked products, where our fee income is linked to the market value of the funds under management. Further exposure arises from with-profits businesses where bonuses declared are based broadly on historical and current rates of return from our investment portfolios which include equities.

In Jackson, investment risk arises from the assets backing customer policies. In the case of spread-based business, including fixed annuities, these assets are generally bonds, and shareholder exposure comes from the minimum returns needed to meet the guaranteed rates that we offer to policyholders. For our variable annuity business, these assets include both equities and bonds. In this case, the main risk to the shareholder comes from the guaranteed benefits that can be included as part of these products. Our exposure to this is reduced by using a derivative hedging programme, as well as through the use of reinsurance to pass on the risk to third-party reinsurers.

<u>Interest rate risk</u>

While long-term interest rates in advanced economies have increased broadly since mid-2016 and indications are for further gradual tightening of monetary policy and the start of balance sheet normalisation by central banks, they remain close to historical lows. Some products that we offer are sensitive to movements in interest rates. We have already taken a number of actions to reduce the risk to the in-force business, as well as re-pricing and restructuring new business offerings in response to these historically low interest rates. Nevertheless, we still retain some sensitivity to interest rate movements.

Interest rate risk arises in M&G Prudential's insurance business from the need to match cash payments to meet annuity obligations with the cash we receive from our investments. To minimise the impact on our profit, we aim to match the duration (a measure of interest rate sensitivity) of assets and liabilities as closely as possible and the position is monitored regularly. Under the Solvency II regulatory regime, additional interest rate risk results from the way the balance sheet is constructed, such as the requirement for us to include a risk margin. The UK business assesses on a continual basis the need for any derivatives in managing its interest rate sensitivity. The with-profits business is exposed to interest rate risk because of underlying guarantees in some of its products. Such risk is borne largely by the with-profits fund itself but shareholder support may be required in extreme circumstances where the fund has insufficient resources to support the risk.

In Asia, our exposure to interest rate risk arises from the guarantees of some non unit-linked investment products. This exposure exists because it may not be possible to hold assets which will provide cash payments to us which match exactly those payments we in turn need to make to policyholders – this is known as an asset and liability mismatch and although it is small and managed appropriately, 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 impact on the cost of guarantees in these products; in particular the cost of guarantees to us may increase when interest rates fall. We monitor the level of sales of variable annuity products with guaranteed living benefits actively, and together with the risk limits we have in place this helps us to ensure that we are comfortable with the interest rate and market risks we incur as a result. The Jackson hedging programme includes hybrid derivatives to provide some protection from a combined fall in interest rates and equity markets since Jackson is exposed to the combination of these market movements.

Foreign exchange risk

The geographical diversity of our businesses means that we have some exposure to the risk of exchange rate fluctuations. Our operations in the US and Asia, which represent a large proportion of our operating profit and shareholders' funds, generally write policies and invest in assets in local currencies. Although this limits the effect of exchange rate movements on local operating results, it can lead to fluctuations in our Group financial statements when results are reported 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. We accept the foreign exchange risk this can produce when reporting our Group balance sheet and income statement. In cases where a surplus arises in an overseas operation which is to be used to support Group capital, or where a significant cash payment is due from an overseas subsidiary to the Group, this foreign exchange exposure is hedged where we believe it is favourable economically to do so. Generally, we do not have appetite for significant direct shareholder exposure to foreign exchange risks in currencies outside of the countries in which we operate, but we do have some appetite for this on fee income and on non-sterling investments within the with-profits fund. Where foreign exchange risk arises outside our appetite, currency borrowings, swaps and other derivatives are used to manage our exposure.

b. Credit risk

We invest in bonds that provide a regular, fixed amount of interest income (fixed income assets) in order to match the payments we need to make to policyholders. We also enter into reinsurance and derivative contracts with third parties to mitigate various types of risk, as well as holding cash deposits at certain banks. As a result, we are exposed to credit risk and counterparty risk across our business.

Credit risk is the potential for reduction in the value of our investments which results from the perceived level of risk of an investment issuer being unable to meet its obligations (defaulting). Counterparty risk is a type of credit risk and relates to the risk that the counterparty to any contract we enter into being unable to meet their obligations causing us to suffer loss.

We use a number of risk management tools to manage and mitigate this credit risk, including the following:

- Our credit risk policy;
- Risk appetite statements and limits that we have defined on issuers, and counterparties;
- Collateral arrangements we have in place for derivative, secured lending reverse repo and reinsurance transactions;
- The Group Credit Risk Committee's oversight of credit and counterparty credit risk and sector and/or name-specific reviews. In 2017 it has conducted sector reviews in the Asia sovereign sector, the UK banking sector, the US retail property sector, and continues to review the developments around central clearing;
- Regular deep dive assessments; and
- Close monitoring or restrictions on investments that may be of concern.

Debt and loan portfolio

Our UK business is exposed mainly to credit risk on fixed income assets in the shareholder-backed portfolio. At 31 December 2017, this portfolio contained fixed income assets worth £35.3 billion. Credit risk arising from a further £57.4 billion of fixed income assets is borne largely by the with-profits fund, to which the shareholder is not exposed directly although under extreme circumstances shareholder support may be required if the fund is unable to meet payments as they fall due.

Credit risk also arises from the debt portfolio in our Asia business, the value of which was £41.0 billion at 31 December 2017. The majority (68 per cent) of the portfolio is in unit-linked and with-profits funds and so exposure of the shareholder to this component is minimal. The remaining 32 per cent of the debt portfolio is held to back the shareholder business.

Credit risk also arises in the general account of the Jackson business, where £35.4 billion of fixed income assets are held to support shareholder liabilities including those from our fixed annuities, fixed index annuities and life insurance products.

The shareholder-owned debt and loan portfolio of the Group's other operations was £2.3 billion as at 31 December 2017.

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

<u>Group sovereign debt</u>
We also invest in bonds issued by national governments. This sovereign debt represented 19 per cent or £16.5 billion of the shareholder debt portfolio as at 31 December 2017 (31 December 2016: 19 per cent or £17.1 billion). 5 per cent of this was rated AAA and 90 per cent was considered investment grade (31 December 2016: 92 per cent investment grade).

The particular risks associated with holding sovereign debt are detailed further in our disclosures on risk factors.

The exposures held by the shareholder-backed business and with-profits funds in sovereign debt securities at 31 December 2017 are given in Note C3.2(f) of the Group's IFRS financial statements.

<u>Bank debt exposure and counterparty credit risk</u>
Our exposure to banks is a key part of our core investment business, as well as being important for the hedging and other activities we undertake to manage our various financial risks. Given the importance of our relationship with our banks, exposure to the sector is considered a material risk for the Group with an appropriate level 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 bank debt securities at 31 December 2017 are given in Note C3.2(f) of the Group's IFRS financial statements.

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, buy credit protection or use additional collateral arrangements to manage our levels of counterparty credit risk.

At 31 December 2017, shareholder exposures by rating[1] and sector are shown below:
- 95 per cent of the shareholder portfolio is investment grade rated. In particular, 69 per cent of the portfolio is rated A and above; and
- The Group's shareholder portfolio is well diversified: no individual sector makes up more than 10 per cent of the total portfolio (excluding the financial and sovereign sectors).

c. Liquidity risk
Our liquidity risk arises from the need to have sufficient liquid assets to meet policyholder and third-party payments as they fall due. This incorporates the risk arising from funds composed of illiquid assets and results from a mismatch between the liquidity profile of assets and liabilities. Liquidity risk may impact on market conditions and valuation of assets in a more uncertain way than for other risks like interest rate or credit risk. It may arise, for example, where external capital is unavailable at sustainable cost, increased liquid assets are required to be held as collateral under derivative transactions or redemption requests are made against Prudential external funds.

We have significant internal sources of liquidity, which are sufficient to meet all of our expected cash requirements for at least 12 months from the date the financial statements are approved, without having to resort to external sources of funding. In total, the Group has £2.6 billion of undrawn committed facilities that we can make use of, expiring in 2022. We have access to further liquidity by way of the debt capital markets, and also have in place an extensive commercial paper programme and have maintained a consistent presence as an issuer in this market for the last decade.

Liquidity uses and sources are assessed at a Group and business unit level under both base case and stressed assumptions. We calculate a Liquidity Coverage Ratio (LCR) under stress scenarios as one measure of our liquidity risk, and this ratio and the liquidity resources available to us are monitored regularly and are assessed to be sufficient.

Our risk management and mitigation of liquidity risk include:
- Our liquidity risk policy;
- The risk appetite statements, limits and triggers that we have in place;
- The monitoring of liquidity risk we perform through regular management information to committees and the Board;
- Our Liquidity Risk Management Plan, which includes details of the Group Liquidity Risk Framework as well as gap analysis of our liquidity risks and the adequacy of our available liquidity resources under normal and stressed conditions;
- Regular stress testing;
- Our established contingency plans and identified sources of liquidity;
- Our ability to access the money and debt capital markets;
- Regular deep dive assessments; and
- The access we have to external sources of finance through committed credit facilities.

4.2 Risks from our products

a. Insurance risk
Insurance risk makes up a significant proportion of our overall risk exposure. The profitability of our businesses depends on a mix of factors including levels of, and trends in, mortality (policyholders dying), morbidity (policyholders becoming ill) and policyholder behaviour (variability in how customers interact with their policies, including utilisation of withdrawals, take-up of options and guarantees and persistency, ie lapsing of policies), and increases in the costs of claims, including the level of medical expenses increases over and above price inflation (claim inflation).

The principal drivers of the Group's insurance risks are persistency and morbidity risk in the Asia business; longevity risk in the UK legacy business of M&G Prudential; and policyholder behaviour risks in Jackson.

We manage and mitigate our insurance risk using the following:

- Our insurance and underwriting risk policies;
- The risk appetite statements, limits and triggers we have in place;
- Using longevity, morbidity and persistency assumptions that reflect recent experience and expectation of future trends, and industry data and expert judgement where appropriate;
- Using reinsurance to mitigate longevity and morbidity risks;
- Ensuring appropriate medical underwriting when policies are issued and appropriate claims management practices when claims are received in order to mitigate morbidity risk;
- Maintaining the quality of our sales processes and using initiatives to increase customer retention in order to mitigate persistency risk;
- Using product re-pricing and other claims management initiatives in order to mitigate medical expense inflation risk; and
- Regular deep dive assessments.

Longevity risk is an important element of our insurance risks for which we need to hold a large amount of capital under Solvency II regulations. Longevity reinsurance is a key tool for us in managing our risk. The enhanced pensions freedoms introduced in the UK during 2015 reduced the demand for retail annuities greatly and further liberalisation is anticipated. Although we have withdrawn from selling new annuity business, given our significant annuity portfolio the assumptions we make about future rates of improvement in mortality rates remain key to the measurement of our insurance liabilities and to our assessment of any reinsurance transactions.

We continue to conduct research into longevity risk using both experience from our annuity portfolio and industry data. Although the general consensus in recent years is that people are living longer, there is considerable volatility in year-on-year longevity experience, which is why we need expert judgement in setting our longevity basis.

Our morbidity risk is mitigated by appropriate underwriting when policies are issued and claims are received. Our morbidity assumptions reflect our recent experience and expectation of future trends for each relevant line of business.

In Asia, we write significant volumes of health protection business, and so a key assumption for us is the rate of medical inflation, which is often in excess of general price inflation. There is a risk that the expenses of medical treatment increase more than we expect, so the medical claim cost passed on to us is higher than anticipated. Medical expense inflation risk is best mitigated by retaining the right to re-price our products each year and by having suitable overall claim limits within our policies, either limits per type of claim or in total across a policy.

Our persistency assumptions reflect similarly a combination of recent past experience for each relevant line of business and expert judgement, especially where a lack of relevant and credible experience data exists. Any expected change in future persistency is also reflected in the assumption. Persistency risk is mitigated by appropriate training and sales processes and managed locally post-sale through regular experience monitoring and the identification of common characteristics of business with high lapse rates. Where appropriate, we make allowance for the relationship (either assumed or observed historically) between persistency and investment returns and account for the resulting additional risk. Modelling this dynamic policyholder behaviour is particularly important when assessing the likely take-up rate of options embedded within certain products. The effect of persistency on our financial results can vary but depends mostly on the value of the product features and market conditions.

4.3 Risks from our business operations

a. Non-financial risks

In the course of doing business, the Group is exposed to non-financial risks arising from our operations, the business environment and our strategy. Our main risks across these areas are detailed below.

We define operational risk as the risk of loss (or unintended gain or profit) arising from inadequate or failed internal processes, personnel or systems, or from external events. This includes employee error, model error, system failures, fraud or some other event which disrupts business processes. Processes are established for activities across the scope of our business, including operational activity, regulatory compliance, and those supporting environmental, social and governance (ESG) activities among others, any of which can expose us to operational risks.

We process a large volume of complex transactions across a number of diverse products, and are subject to a high number of varying legal, regulatory and tax regimes. We also have a number of important third-party relationships that provide the distribution and processing of our products, both as market counterparties and as outsourcing partners. M&G Prudential outsources several operations, including a significant part of its back office, customer-facing functions and a number of IT functions. These third party arrangements help us to provide a high level and cost-effective service to our customers, but they also make us reliant on the operational performance of our outsourcing partners.

The performance of our core business activities places reliance on the IT infrastructure that supports day-to-day transaction processing. Our IT environment must also be secure and we address an increasing cyber risk threat as our digital footprint increases – see separate Cyber risk section below. The risk that our IT infrastructure does not meet these requirements is a key area of focus for us, particularly the risk that legacy infrastructure supporting core activities/processes affects business continuity or impacts on business growth.

Operational challenges also exist in keeping pace with regulatory changes. This requires implementing processes to ensure we are, and remain, compliant on an ongoing basis, including regular monitoring and reporting. The high rate of global regulatory change, in an already complex regulatory landscape, increases the risk of non-compliance due to a failure to identify, interpret correctly, implement and/or monitor regulatory compliance. See Global regulatory and political risk section below. Legislative developments over recent years, together with enhanced regulatory oversight and increased capability to issue sanctions, have resulted in a complex regulatory environment that may lead to breaches of varying magnitude if the Group's business-as-usual operations are not compliant. As well as prudential regulation, we focus on conduct regulation, including those related to sales practice and anti-money laundering, bribery and corruption. We have a particular focus on regulations related to the latter in newer/emerging markets.

The business environment we operate in has become increasingly complex over the years. The political, environmental, societal, legal and economic landscape is highly dynamic and uncertain. Changes and developments on the horizon may result in emerging risks to us which are monitored under our Emerging Risk Framework.

The Group maintains active engagement with our shareholders, governments, policymakers and regulators in our key markets, as well as with international institutions. This introduces expectations for the Group to act and respond to environmental, social and governance (ESG) matters in a certain manner. The perception that our key stakeholders have of us and our businesses is crucial in forming and maintaining a robust brand and reputation. As such, the Group's operational risk framework explicitly incorporates ESG as a component of our social and environmental responsibility, brand management and external communications within our framework. This is further strengthened by factoring considerations for reputational impacts when the materiality of operational risks are assessed.

The climate risk landscape continues to evolve and is moving up the agenda of many regulators, governments, non-governmental organisations and investors. Examples of this include the US Department of Labor's decision to change its guidance to pension fund fiduciaries to allow them to factor ESG issues into investment decisions; Hong Kong Stock Exchange listing rules requiring listed companies to provide a high-level discussion of ESG approaches and activities in external disclosures, and the Financial Stability Board (FSB's) Task Force for Climate-related Financial Disclosures.

The increased regulatory focus on environmental issues not only reflects existing commitments, for example in the UK under the 2008 Climate Change Act, but also a heightened societal awareness of climate change as a pressing global concern. Regulatory and stakeholder interest in environmental matters is expected to increase as climate change moves higher up governmental agendas. This increase in focus creates a number of potential near term risks. These include:

- Investment risk in the form of 'transition risk'. This is the risk that an abrupt, unexpected tightening of carbon emission policies lead to a disorderly re-pricing of carbon-intensive assets;
- Liability risk, if the Group is unable to demonstrate sufficiently that we have acted to mitigate our exposure to climate change risk; and
- Reputational risks, where the Group's actions could affect external perceptions of our brand and corporate citizenship.

The Group has established a Group-wide Responsible Investment Advisory Committee with designated responsibility to oversee Prudential's responsible investment activities as both asset owners and asset managers.

Physical impacts of climate change could also arise, driven by specific climate-related events such as natural disasters. These impacts are mitigated through our crisis management and disaster recovery plans.

Strategic risk requires a forward-looking approach to risk management. A key part of our approach are the risk assessments performed as part of the Group's annual strategic planning process, which supports the identification of potential future threats and the initiatives needed to address them, as well as competitive opportunities. We also assess the impact on the Group's businesses and our risk profile to ensure that strategic initiatives are within the Group's overall risk appetite.

Implementation of the Group's strategy and the need to comply with emerging regulation has resulted in a significant portfolio of transformation and change initiatives, which may further increase in the future. In particular the intention to demerge the UK and Europe business from the rest of the Group will result in a substantial change programme which will need to be managed at the same time that other material transformation programmes are being delivered. The scale and the complexity of the transformation programmes could impact business operations and customers, and has the potential for reputational damage if these programmes fail to deliver their objectives. Implementing further strategic initiatives may amplify these risks.

Other significant change initiatives are occurring across the Group. The volume, scale and complexity of these programmes increases the likelihood and potential impact of risks associated with:

- Dependencies between multiple projects;
- The organisational ability to absorb change being exceeded;
- Unrealised business objectives/benefits; and
- Failures in project design and execution.

The risks detailed above form key elements of the Group's operational risk profile. In order to effectively identify, assess, manage, control and report on all operational risks across the business, a Group-wide operational risk framework is in place. The key components of the framework are:

- Application of a risk and control assessment (RCA) process, where operational risk exposures are identified and assessed as part of a periodical cycle. The RCA process takes into account a range of internal and external factors, including an assessment of the control environment, to determine the business's most significant risk exposures on a prospective basis;
- An internal incident capture process, which identifies, quantifies and monitors remediation conducted through application of action plans for risk events that have occurred across the business;
- A scenario analysis process for the quantification of extreme, yet plausible manifestations of key operational risks across the business on a forward looking basis. This is carried out at least annually and supports external and internal capital requirements as well as informing risk activity across the business; and
- An operational risk appetite framework that articulates the level of operational risk exposure the business is willing to tolerate and sets out escalation processes for breaches of appetite.

Outputs from these processes and activities performed individual business units are monitored by the Group Risk function, who provide an aggregated view of risk profile across the business to the Group Risk Committee and Board.

These core framework components are embedded across the Group via the Group Operational Risk Policy and Standards documents, which sets out the key principles and minimum standards for the management of operational risk across the Group.

The Group operational risk policy, standards and operational risk appetite framework sit alongside other risk policies and standards that individually engage with key operational risks, including outsourcing and third-party supply, business continuity, technology and data, and operations processes.

These policies and standards include subject matter expert-led processes that are designed to identify, assess, manage and control operational risks, including the application of:

- A transformation risk framework that assesses, manages and reports on the end-to-end transformation lifecycle, project prioritisation and the risks, interdependencies and possible conflicts arising from a large portfolio of transformation activities;
- Internal and external review of cyber security capability;
- Regular updating and testing of elements of disaster-recovery plans and the Critical Incident Procedure process;
- Group and business unit-level compliance oversight and testing in respect of adherence with in-force regulations;
- Regulatory change teams in place assist the business in proactively adapting and complying with regulatory developments;
- A framework in place for emerging risk identification and analysis in order to capture, monitor and allow us to prepare for operational risks that may crystallise beyond the short-term horizon;
- Corporate insurance programmes to limit the financial impact of operational risks; and
- Reviews of key operational risks and challenges within Group and business unit business plans.

These activities are fundamental in maintaining an effective system of internal control, and as such outputs from these also inform core RCA, incident capture and scenario analysis processes and reporting on operational risk. Furthermore, they also ensure that operational risk considerations are embedded in key business decision-making, including material business approvals and in setting and challenging the Group's strategy.

b. Global regulatory and political risk

Our risk management and mitigation of regulatory and political risk includes the following:

- Risk Assessment of the Business Plan which includes consideration of current strategies;
- Close monitoring and assessment of our business environment and strategic risks;
- The consideration of risk themes in strategic decisions; and
- Ongoing engagement with national regulators, government policy teams and international standard setters.

Recent shifts in the focus of some governments toward more protectionist or restrictive economic and trade policies could impact on the degree and nature of regulatory changes and Prudential's competitive position in some geographic markets. This could take effect, for example, through increased friction in cross-border trade, capital controls or measures favouring local enterprises such as changes to the maximum level of non-domestic ownership by foreign companies. We continue to monitor these developments at a national and global level and these considerations form part of our ongoing engagement with government policy teams and regulators.

On 29 March 2017 the UK submitted formal notification of its intention to withdraw from the EU. In December 2017, agreement was reached between the UK and EU to progress negotiations onto transitional arrangements and the future trading relationship. The outcome of negotiations remains highly uncertain. If no formal withdrawal agreement is reached then it is expected the UK's membership of the EU will terminate automatically two years after the submission of the notification.

The ongoing uncertainty during the remainder of the negotiation period and the potential for a disorderly exit from the EU by the UK without a negotiated agreement may increase volatility in the markets where we operate, creating the potential for a general downturn in economic activity and for falls in interest rates in some jurisdictions due to easing of monetary policy and investor sentiment.

As a Group, our diversification by geography, currency, product and distribution should reduce some of the potential impact. We have UK-domiciled operations including M&G Prudential, and due to the geographical location of both its businesses and its customers, its insurance and the fund management operations have most potential to be affected by the UK's exit. The extent of the impact will depend in part on the nature of the arrangements that are put in place between the UK and the EU. Contingency plans were developed ahead of the referendum by business units and operations that may be impacted immediately by a vote to withdraw the UK from the EU, and these plans have been enacted since the referendum result. We have since also undertaken significant work to ensure that our business, and in particular our customer base, is not unduly affected by the decision of the UK to exit from the EU.

The UK's decision to leave the EU has introduced uncertainty to the extent of future applicability of the Solvency II regime in the UK. In October 2017, the Treasury Committee published its report on the Solvency II Directive and the UK Insurance Industry, which highlighted the need for a strategy, post-UK exit, to foster innovation, competition and competitiveness for the benefit of UK consumers. In late 2016 the European Commission began a review of some aspects of the Solvency II legislation, with a particular focus on the Solvency Capital Requirement calculated using the standard formula, which is expected to run until 2021.

National and regional efforts to curb systemic risk and promote financial stability are also underway in certain jurisdictions in which Prudential operates, including the Dodd-Frank Wall Street Reform and Consumer Protection Act in the US, the work of the Financial Stability Board (FSB) on Global Systemically Important Insurers (G-SIIs) and the Insurance Capital Standard being developed by the International Association of Insurance Supervisors (IAIS). There are also a number of ongoing policy initiatives and regulatory developments that are having, and will continue to have, an impact on the way Prudential is supervised. These include addressing Financial Conduct Authority (FCA) reviews, ongoing engagement with the Prudential Regulation Authority (PRA), and the work of the Financial Stability Board (FSB) and standard-setting institutions such as the IAIS. Decisions taken by regulators, including those related to solvency requirements, corporate or governance structures, capital allocation and risk management may have an impact on our business.

The IAIS's G-SII regime forms additional compliance considerations for us. Groups designated as G-SIIs are subject to additional regulatory requirements, including enhanced group-wide supervision, effective resolution planning, development of a Systemic Risk Management Plan, a Recovery Plan and a Liquidity Risk Management Plan. The FSB did not publish a new list of G-SIIs in 2017, however the policy measures set out in the FSB's 2016 communication on G-SIIs continue to apply to the Group. Prudential is monitoring the development and potential impact of the policy measures and is continuing to engage with the PRA on the implications of such measures and Prudential's designation as a G-SII. The IAIS has launched a public interim consultation on an activities-based approach to systemic risk. Following the feedback from this, a second consultation with proposals for policy measures is due to be launched in 2018. Any changes to the designation methodology are expected to be implemented in 2019.

We continue to engage with the IAIS on developments in capital requirements for groups with G-SII designation. The regime introduces capital requirements in the form of a Higher Loss Absorption (HLA) requirement. This requirement was initially intended to come into force in 2019 but has been postponed until 2022. The HLA is also now intended to be based on the Insurance Capital Standard, which is being developed by the IAIS as the capital requirements under its Common Framework (ComFrame). This framework is focused on the supervision of Internationally Active Insurance Groups (IAIGs) and will establish a set of common principles and standards designed to assist regulators in addressing risks that arise from insurance groups with operations in multiple jurisdictions. As part of this, work is underway to develop a global Insurance Capital Standard (ICS) that is intended to apply to Internationally Active Insurance Groups.

The IAIS has announced that the implementation of ICS will be conducted in two phases – a five-year monitoring phase followed by an implementation phase. During the monitoring phase, IAIGs will be required to report on ICS to the group-wide supervisor on a confidential basis, although these results will not be used as a basis to trigger supervisory action.

The IAIS's Insurance Core Principles, which provide a globally-accepted framework for the supervision of the insurance sector and ComFrame evolution, are expected to create continued development in both prudential and conduct regulations over the next two to three years.

In the US, some parts of the Department of Labor (DoL) rule introducing fiduciary obligations for distributors of investment products, which may reshape dramatically the distribution of retirement products, became effective on 9 June 2017. This included those provisions on impartial conduct standards, although other provisions of the rule have now been delayed until 1 July 2019. Jackson has introduced fee-based variable annuity products in response to the introduction of the rule, and we anticipate that the business's strong relationships with distributors, history of product innovation and efficient operations should further mitigate any impacts.

The US National Association of Insurance Commissioners (NAIC) is continuing its industry consultation with the aim of reducing the non-economic volatility in the variable annuity statutory balance sheet and risk management. Following two industry quantitative impact studies, proposed changes to the current framework have been released by the NAIC for comment from industry and other interested parties. Jackson continues to be engaged in the consultation and testing process. The proposed changes are expected to be effective from 2019 at the earliest. In December 2017, the Tax Cuts and Jobs Act was signed into law in the US. Some uncertainty exists on the implications of the tax reforms on the NAIC's proposals.

A degree of uncertainty as to the timing, status and final scope of these key US reforms exists. Our preparations to manage the impact of these reforms will continue while we await further clarification.

In May 2017, the International Accounting Standards Board (IASB) published IFRS 17 which will introduce fundamental changes to the statutory reporting of insurance entities that prepare accounts according to IFRS from 2021. The Group is reviewing the complex requirements of the standard and is considering its potential impact. This is expected to, among other things, include altering the timing of IFRS profit recognition, and the implementation of the standard is likely to require changes to the Group's IT, actuarial and finance systems.

In Asia, regulatory regimes are developing at different speeds, driven by a combination of global factors and local considerations. New local capital rules and requirements could be introduced in these and other regulatory regimes that challenge legal or ownership structures, current sales practices, or could be applied to sales made prior to their introduction retrospectively, which could have a negative impact on Prudential's business or reported results.

c. Cyber risk

Cyber risk remains an area of heightened focus after a number of recent high profile attacks and data losses. The growing maturity and industrialisation of cyber-criminal capability, together with an increasing level of understanding of complex financial transactions by criminal groups, are two reasons why risks to the financial services industry are increasing. Disruption to the availability, confidentiality and integrity of our IT systems could make it difficult to recover critical services, result in damage to assets and compromise the integrity and security of data. This could result in significant impacts to business continuity, our customer relationship and our brand reputation. Developments in data protection worldwide (such as the EU General Data Protection Regulation that comes into force in May 2018) may increase the financial and reputational implications for Prudential of a breach of its (or third-party suppliers') IT systems.

Given this, cyber security is seen as a key risk for the Group and is an area of increased scrutiny by global regulators. The threat landscape is continuously evolving, and our assessment is that the systemic risk from untargeted but sophisticated and automated attacks has increased. Cyber risks are also increasingly stemming from geopolitical tensions.

The core objectives of our Cyber Risk Management Strategy are: to develop a comprehensive situational awareness of our business in cyberspace; to pro-actively engage cyber attackers to minimise harm to our business; and to enable the business to grow and safely in cyberspace confidently.

Our Cyber Defence Plan consists of a number of work-streams, including developing our ability to deal with incidents; alignment with our digital transformation strategy; and increasing cyber oversight and assurance to the Board. We have made progress in all of these across 2017. Protecting our customers remains core to our business, and the successful delivery of the Cyber Defence Plan will reinforce our capabilities to continue doing so in cyberspace as we transition to a digital business.

The Board receives periodic updates on cyber risk management throughout the year, which includes assessments against the core objectives under our Group-wide Cyber Risk Management Strategy and progress updates on the associated Group-wide Coordinated Cyber Defence Plan.

Group functions work with each of the business units to address cyber risks locally within the national and regional context of each business, following the strategic direction laid out in the Cyber Risk Management Strategy and managed through the execution of the Cyber Defence Plan.

The Group Information Security Committee, which consists of senior executives from each of the businesses and meets on a regular basis, governs the execution of the Cyber Defence Plan and reports on delivery and cyber risks to the Group Executive Risk Committee. Both committees also receive regular operational management information on the performance of controls.

Note

1 Based on hierarchy of Standard and Poor's Moody's and Fitch, where available and if unavailable, internal ratings have been used.

Corporate governance

The Board confirms that it has complied with all the principles and provisions set out in the Hong Kong Code on Corporate Governance Practices (the HK Code) throughout the accounting period with the following exception. With respect to 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 Code, fees for 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 year.

IFRS Disclosure and Additional Unaudited Financial Information
Prudential plc 2017 results
International Financial Reporting Standards (IFRS) basis results

Notes

Additional unaudited IFRS financial information

International Financial Reporting Standards (IFRS) Basis Results

Consolidated income statement

Year ended 31 December	Note	2017 £m	2016 £m
Gross premiums earned		**44,005**	38,981
Outward reinsurance premiums		**(2,062)**	(2,020)
Earned premiums, net of reinsurance		**41,943**	36,961
Investment return		**42,189**	32,511
Other income		**2,430**	2,370
Total revenue, net of reinsurance		**86,562**	71,842
Benefits and claims		**(71,854)**	(60,948)
Outward reinsurers' share of benefit and claims		**2,193**	2,412
Movement in unallocated surplus of with-profits funds		**(2,871)**	(830)
Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance		**(72,532)**	(59,366)
Acquisition costs and other expenditure	B2	**(10,165)**	(8,848)
Finance costs: interest on core structural borrowings of shareholder-financed operations		**(425)**	(360)
Disposal of Korea life business:	D1		
Cumulative exchange gain recycled from other comprehensive income		**61**	-
Remeasurement adjustments		**5**	(238)
Gain on disposal of other businesses	D1	**162**	-
Total charges, net of reinsurance and gain (loss) on disposal of businesses		**(82,894)**	(68,812)
Share of profits from joint ventures and associates, net of related tax		**302**	182
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)**		**3,970**	3,212
Less tax charge attributable to policyholders' returns		**(674)**	(937)
Profit before tax attributable to shareholders	B1.1	**3,296**	2,275
Total tax charge attributable to policyholders and shareholders	B4	**(1,580)**	(1,291)
Adjustment to remove tax charge attributable to policyholders' returns		**674**	937
Tax charge attributable to shareholders' returns	B4	**(906)**	(354)
Profit for the year		**2,390**	1,921
Attributable to:			
Equity holders of the Company		**2,389**	1,921
Non-controlling interests		**1**	-
Profit for the year		**2,390**	1,921

Earnings per share (in pence)		2017	2016
Based on profit attributable to the equity holders of the Company:	B5		
Basic		**93.1p**	75.0p
Diluted		**93.0p**	75.0p

Dividends per share (in pence)		2017	2016
Dividends relating to reporting year:	B6		
First interim ordinary dividend		**14.50p**	12.93p
Second interim ordinary dividend		**32.50p**	30.57p
Total		**47.00p**	43.50p
Dividends paid in reporting year:	B6		
Current year first interim dividend		**14.50p**	12.93p
Second interim ordinary dividend for prior year		**30.57p**	26.47p
Special dividend		**-**	10.00p
Total		**45.07p**	49.40p

* 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 is not representative of pre-tax profits attributable to shareholders. Profit before all taxes 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.

International Financial Reporting Standards (IFRS) Basis Results

Consolidated statement of comprehensive income

Year ended 31 December	Note	2017 £m	2016 £m
Profit for the year		**2,390**	1,921
Other comprehensive income:			
Items that may be reclassified subsequently to profit or loss			
Exchange movements on foreign operations and net investment hedges:			
Exchange movements arising during the year		**(404)**	1,148
Cumulative exchange gain of sold Korea life business recycled through profit or loss		**(61)**	-
Related tax		**(5)**	13
		(470)	1,161
Net unrealised valuation movements on securities of US insurance operations classified as available-for-sale:			
Net unrealised holding gains arising during the year		**591**	241
Net gains (losses) included in the income statement on disposal and impairment		**26**	(269)
Total	C3.2(c)	**617**	(28)
Related change in amortisation of deferred acquisition costs	C5 (b)	**(76)**	76
Related tax	C8	**(55)**	(17)
		486	31
Total		**16**	1,192
Items that will not be reclassified to profit or loss			
Shareholders' share of actuarial gains and losses on defined benefit pension schemes:			
Gross		**104**	(107)
Related tax		**(15)**	14
		89	(93)
Other comprehensive income for the year, net of related tax		**105**	1,099
Total comprehensive income for the year		**2,495**	3,020
Attributable to:			
Equity holders of the Company		**2,494**	3,020
Non-controlling interests		**1**	-
Total comprehensive income for the year		**2,495**	3,020

International Financial Reporting Standards (IFRS) Basis Results

Consolidated statement of changes in equity

		Year ended 31 December 2017 £m							
	Note	Share capital note C10	Share premium note C10	Retained earnings	Translation reserve	Available -for-sale securities reserves	Shareholders' equity	Non-controlling interests	Total equity
Reserves									
Profit for the year		-	-	2,389	-	-	2,389	1	2,390
Other comprehensive income:									
Exchange movements on foreign operations and net investment hedges, net of related tax		-	-	-	(470)	-	(470)	-	(470)
Net unrealised valuation movements, net of related change in amortisation of deferred acquisition costs and related tax		-	-	-	-	486	486	-	486
Shareholders' share of actuarial gains and losses on defined benefit pension schemes, net of tax		-	-	89	-	-	89	-	89
Total other comprehensive income (loss)		-	-	89	(470)	486	105	-	105
Total comprehensive income for the year		-	-	2,478	(470)	486	2,494	1	2,495
Dividends	B6	-	-	(1,159)	-	-	(1,159)	-	(1,159)
Reserve movements in respect of share-based payments		-	-	89	-	-	89	-	89
Change in non-controlling interests*							-	5	5
Share capital and share premium									
New share capital subscribed	C10	-	21	-	-	-	21	-	21
Treasury shares									
Movement in own shares in respect of share-based payment plans		-	-	(15)	-	-	(15)	-	(15)
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS				(9)		-	(9)	-	(9)
Net increase (decrease) in equity		-	21	1,384	(470)	486	1,421	6	1,427
At beginning of year		129	1,927	10,942	1,310	358	14,666	1	14,667
At end of year		129	1,948	12,326	840	844	16,087	7	16,094

*Arising from the acquisition of the majority stake in Zenith Life of Nigeria in 2017.

International Financial Reporting Standards (IFRS) Basis Results

Consolidated statement of changes in equity

		Year ended 31 December 2016 £m							
	Note	**Share capital** note C10	**Share premium** note C10	**Retained earnings**	**Translation reserve**	**Available -for-sale securities reserves**	**Shareholders' equity**	**Non-controlling interests**	**Total equity**
Reserves									
Profit for the year		-	-	1,921	-	-	1,921	-	1,921
Other comprehensive income:									
Exchange movements on foreign operations and net investment hedges, net of related tax		-	-	-	1,161	-	1,161	-	1,161
Net unrealised valuation movements, net of related change in amortisation of deferred acquisition costs and related tax		-	-	-	-	31	31	-	31
Shareholders' share of actuarial gains and losses on defined benefit pension schemes, net of tax		-	-	(93)	-	-	(93)	-	(93)
Total other comprehensive income (loss)		-	-	(93)	1,161	31	1,099	-	1,099
Total comprehensive income for the year		-	-	1,828	1,161	31	3,020	-	3,020
Dividends	B6	-	-	(1,267)	-	-	(1,267)	-	(1,267)
Reserve movements in respect of share-based payments		-	-	(51)	-	-	(51)	-	(51)
Share capital and share premium									
New share capital subscribed	C10	1	12	-	-	-	13	-	13
Treasury shares									
Movement in own shares in respect of share-based payment plans		-	-	2	-	-	2	-	2
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS		-	-	(6)	-	-	(6)	-	(6)
Net increase in equity		1	12	506	1,161	31	1,711	-	1,711
At beginning of year		128	1,915	10,436	149	327	12,955	1	12,956
At end of year		129	1,927	10,942	1,310	358	14,666	1	14,667

International Financial Reporting Standards (IFRS) Basis Results

Consolidated statement of financial position

31 December	Note	2017 £m	2016 £m
Assets			
Goodwill	C5(a)	**1,482**	1,628
Deferred acquisition costs and other intangible assets	C5(b)	**11,011**	10,807
Property, plant and equipment		**789**	743
Reinsurers' share of insurance contract liabilities		**9,673**	10,051
Deferred tax assets	C8	**2,627**	4,315
Current tax recoverable		**613**	440
Accrued investment income		**2,676**	3,153
Other debtors		**2,963**	3,019
Investment properties		**16,497**	14,646
Investment in joint ventures and associates accounted for using the equity method		**1,416**	1,273
Loans	C3.3	**17,042**	15,173
Equity securities and portfolio holdings in unit trusts		**223,391**	198,552
Debt securities	C3.2	**171,374**	170,458
Derivative assets		**4,801**	3,936
Other investments		**5,622**	5,465
Deposits		**11,236**	12,185
Assets held for sale		**38**	4,589
Cash and cash equivalents		**10,690**	10,065
Total assets	C1	**493,941**	470,498
Equity			
Shareholders' equity		**16,087**	14,666
Non-controlling interests		**7**	1
Total equity		**16,094**	14,667
Liabilities			
Insurance contract liabilities	C4.1	**328,172**	316,436
Investment contract liabilities with discretionary participation features	C4.1	**62,677**	52,837
Investment contract liabilities without discretionary participation features	C4.1	**20,394**	19,723
Unallocated surplus of with-profits funds	C4.1	**16,951**	14,317
Core structural borrowings of shareholder-financed operations	C6.1	**6,280**	6,798
Operational borrowings attributable to shareholder-financed operations	C6.2	**1,791**	2,317
Borrowings attributable to with-profits operations	C6.2	**3,716**	1,349
Obligations under funding, securities lending and sale and repurchase agreements		**5,662**	5,031
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		**8,889**	8,687
Deferred tax liabilities	C8	**4,715**	5,370
Current tax liabilities		**537**	649
Accruals, deferred income and other liabilities		**14,185**	13,825
Provisions		**1,123**	947
Derivative liabilities		**2,755**	3,252
Liabilities held for sale		**-**	4,293
Total liabilities	C1	**477,847**	455,831
Total equity and liabilities		**493,941**	470,498

Included within equity securities and portfolio holdings in unit trusts, debt securities and other investments are £8,232 million (2016: £8,545 million) of lent securities and assets subject to repurchase agreements.

International Financial Reporting Standards (IFRS) Basis Results

Consolidated statement of cash flows

Year ended 31 December	Note	2017 £m	2016 £m
Cash flows from operating activities			
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)*note (i)		**3,970**	3,212
Non-cash movements in operating assets and liabilities reflected in profit before tax:			
Investments		**(49,771)**	(37,824)
Other non-investment and non-cash assets		**(968)**	(2,490)
Policyholder liabilities (including unallocated surplus)		**44,877**	31,135
Other liabilities (including operational borrowings)		**3,360**	7,861
Interest income and expense and dividend income included in result before tax		**(8,994)**	(9,749)
Other non-cash items		**549**	834
Operating cash items:			
Interest receipts		**6,900**	7,886
Dividend receipts		**2,612**	2,286
Tax paidnote (iv)		**(915)**	(950)
Net cash flows from operating activities		**1,620**	2,201
Cash flows from investing activities			
Purchases of property, plant and equipment		**(134)**	(348)
Proceeds from disposal of property, plant and equipment		**-**	102
Acquisition of subsidiaries and intangiblesnote (v)		**(351)**	(303)
Sale of businessesnote (v)		**1,301**	-
Net cash flows from investing activities		**816**	(549)
Cash flows from financing activities			
Structural borrowings of the Group:			
Shareholder-financed operations:note (ii)	C6.1		
Issue of subordinated debt, net of costs		**565**	1,227
Redemption of subordinated debt		**(751)**	-
Interest paid		**(369)**	(335)
With-profits operations:note (iii)	C6.2		
Interest paid		**(9)**	(9)
Equity capital:			
Issues of ordinary share capital		**21**	13
Dividends paid		**(1,159)**	(1,267)
Net cash flows from financing activities		**(1,702)**	(371)
Net increase in cash and cash equivalents		**734**	1,281
Cash and cash equivalents at beginning of year		**10,065**	7,782
Effect of exchange rate changes on cash and cash equivalents		**(109)**	1,002
Cash and cash equivalents at end of year		**10,690**	10,065

Notes

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

(ii) 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.
The changes in the carrying value of the structural borrowings of shareholder-financed operations during 2017 are analysed as follows:

		Cash movements £m		Non-cash movements £m		
	Balance at 1 Jan 2017	Issue of debt	Redemption of debt	Foreign exchange movement	Other movements	Balance at 31 Dec 2017
Structural borrowings of shareholder-financed operations	**6,798**	**565**	**(751)**	**(341)**	**9**	**6,280**

(iii) 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. There is no change in respect of the carrying value of the £100 million structural borrowings of the with-profits operations during 2017. 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.

(iv) Tax paid includes £298 million (2016: £226 million) paid on profits taxable at policyholder rather than shareholder rates.

(v) Net cash flows for corporate transactions are for distribution rights and acquisition and disposal of businesses (including private equity and other subsidiaries acquired by with-profits funds for investment purposes).

International Financial Reporting Standards (IFRS) Basis Results

Notes

A Background
A1 Basis of preparation and exchange rates

These statements have been prepared in accordance with IFRS Standards as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU) as required by EU law (IAS Regulation EC1606/2032). EU-endorsed IFRS Standards may differ from IFRS Standards issued by the IASB if, at any point in time, new or amended IFRS Standards have not been endorsed by the EU. At 31 December 2017, there were no unendorsed standards effective for the two years ended 31 December 2017 which impact the consolidated financial information of the Group. There were no differences between IFRS Standards endorsed by the EU and IFRS Standards issued by the IASB in terms of their application to the Group.

The Group IFRS accounting policies are the same as those applied for the year ended 31 December 2016 with the exception of the adoption of the new and amended accounting standards as described in note A2.

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

	Closing rate at 31 Dec 2017	Average rate for 2017	Closing rate at 31 Dec 2016	Average rate for 2016
Local currency: £				
Hong Kong	**10.57**	**10.04**	9.58	10.52
Indonesia	**18,353.44**	**17,249.38**	16,647.30	18,026.11
Malaysia	**5.47**	**5.54**	5.54	5.61
Singapore	**1.81**	**1.78**	1.79	1.87
China	**8.81**	**8.71**	8.59	8.99
India	**86.34**	**83.90**	83.86	91.02
Vietnam	**30,719.60**	**29,279.71**	28,136.99	30,292.79
Thailand	**44.09**	**43.71**	44.25	47.80
US	**1.35**	**1.29**	1.24	1.35

Certain notes to the financial statements present 2016 comparative information at Constant Exchange Rates (CER), in addition to the reporting at Actual Exchange Rates (AER) used throughout the 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 financial information set out in this announcement does not constitute the Company's statutory accounts for the years ended 31 December 2017 or 2016 but is derived from those accounts. The auditors have reported on the 2017 statutory accounts. Statutory accounts for 2016 have been delivered to the registrar of companies, and those for 2017 will be delivered following the Company’s Annual General Meeting. Their 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.

A2 New accounting pronouncements in 2017

The IASB has issued the following new accounting pronouncements to be effective for 1 January 2017:

- Disclosure Initiative (Amendments to IAS 7, ‘Statement of Cash Flows’);
- Recognition of deferred tax assets for unrealised losses (Amendments to IAS 12, ‘Income Taxes’); and
- Annual improvements to IFRSs 2014 – 2016 cycle.

Other than the additional disclosure of the changes in structural borrowings during the year in the statement of cash flows, these pronouncements have no effect on these financial statements.

B Earnings performance

B1 Analysis of performance by segment

B1.1 Segment results – profit before tax

	Note	2017 £m	2016* £m AER note (v)	2016* £m CER note (v)	% 2017 vs 2016 AER note (v)	% 2017 vs 2016 CER note (v)
Asia						
Insurance operations	B3(a)	**1,799**	1,503	1,571	20%	15%
Asset management		**176**	141	149	25%	18%
Total Asia		**1,975**	1,644	1,720	20%	15%
US						
Jackson (US insurance operations)	B3(b)	**2,214**	2,052	2,156	8%	3%
Asset management		**10**	(4)	(4)	350%	350%
Total US		**2,224**	2,048	2,152	9%	3%
UK and Europe						
UK and Europe insurance operations:	B3(c)					
Long-term business		**861**	799	799	8%	8%
General insurance commission[note (i)]		**17**	29	29	(41)%	(41)%
Total UK and Europe insurance operations		**878**	828	828	6%	6%
UK and Europe asset management[note (vi)]	B2	**500**	425	425	18%	18%
Total UK and Europe		**1,378**	1,253	1,253	10%	10%
Total segment profit		**5,577**	4,945	5,125	13%	9%
Restructuring costs [note (iii)]		**(103)**	(38)	(39)	(171)%	(164)%
Other income and expenditure:						
Investment return and other income		**11**	28	28	(61)%	(61)%
Interest payable on core structural borrowings		**(425)**	(360)	(360)	(18)%	(18)%
Corporate expenditure[note (ii)]		**(361)**	(334)	(340)	(8)%	(6)%
Solvency II implementation costs		**-**	(28)	(28)	n/a	n/a
Total other income and expenditure		**(775)**	(694)	(700)	(12)%	(11)%
Interest received from tax settlement		**-**	43	43	n/a	n/a
Operating profit based on longer-term investment returns		**4,699**	4,256	4,429	10%	6%
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	**(1,563)**	(1,678)	(1,764)	7%	11%
Amortisation of acquisition accounting adjustments[note (iv)]		**(63)**	(76)	(79)	17%	20%
Profit (loss) attaching to disposal of businesses	D1	**162**	(227)	(244)	n/a	n/a
Cumulative exchange gain on the sold Korea life business recycled from other comprehensive income	D1	**61**	-	-	n/a	n/a
Profit before tax		**3,296**	2,275	2,342	45%	41%
Tax charge attributable to shareholders' returns	B4	**(906)**	(354)	(360)	(156)%	(152)%
Profit for the year		**2,390**	1,921	1,982	24%	21%
Attributable to:						
Equity holders of the Company		**2,389**	1,921	1,982	24%	21%
Non-controlling interests		**1**	-	-	N/A	N/A

		2017	2016 AER note (v)	2016 CER note (v)	% 2017 vs 2016 AER note (v)	% 2017 vs 2016 CER note (v)
Basic earnings per share (in pence)	B5					
Based on operating profit based on longer-term investment returns[note (vii)]		**145.2p**	131.3p	136.8p	11%	6%
Based on profit for the year		**93.1p**	75.0p	77.4p	24%	20%

* The 2016 comparative results have been re-presented from those previously published following the reassessment of the Group's operating segments as described in note B1.3.

Notes

(i) General insurance commission represents the commission receivable net of expenses for Prudential-branded general insurance products in connection with the arrangement to transfer the UK general insurance business to Churchill in 2002.
(ii) Corporate expenditure as shown above is primarily for Group Head Office and Asia Regional Head Office.
(iii) Restructuring costs are incurred primarily in UK and Europe and Asia and represent business transformation and integration costs.
(iv) Amortisation of acquisition accounting adjustments principally relate to the REALIC business of Jackson which was acquired in 2012.
(v) For definitions of AER and CER refer to note A1. The difference between 'Profit for the year attributable to shareholders' in the prior year on an AER basis and a CER basis is £61 million, arising from the retranslation of the prior year results of the Group's foreign subsidiaries into GBP using the exchange rates applied to the equivalent current year results.
(vi) UK and Europe asset management operating profit based on longer-term investment returns:

	2017 £m	2016 £m
Asset management fee income	**1,027**	900
Other income	**7**	23
Staff costs	**(400)**	(332)
Other costs	**(202)**	(212)
Underlying profit before performance-related fees	**432**	379
Share of associate results	**15**	13
Performance-related fees	**53**	33
Total UK and Europe asset management operating profit based on longer-term investment returns	**500**	425

(vii) Tax charges have been reflected as operating and non-operating in the same way as for the pre-tax items. In 2017 a significant US tax reform package was enacted, and the effects of which in the income statement have been treated as non-operating. Further details are provided in note B4.

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

	2017 £m	2016 £m
Asia	**(1)**	(225)
US[note (i)]	**(1,568)**	(1,455)
UK and Europe[note (ii)]	**(14)**	206
Other operations[note (iii)]	**20**	(204)
Total	**(1,563)**	(1,678)

Notes

(i) *US operations*

The short-term fluctuations in investment returns for US insurance operations are reported net of related credit for amortisation of deferred acquisition costs, of £462 million as shown in note C5(b) (2016: £565 million) and comprise amounts in respect of the following items:

	2017 £m	2016 £m
Net equity hedge result[note (a)]	**(1,490)**	(1,587)
Other than equity-related derivatives[note (b)]	**(36)**	(126)
Debt securities [note (c)]	**(73)**	201
Equity-type investments: actual less longer-term return	**12**	35
Other items	**19**	22
Total	**(1,568)**	(1,455)

Notes

(a) Net equity hedge result

The purpose of the inclusion of this item in short-term fluctuations in investment returns is to segregate the amount included in pre-tax profit that relates to the accounting effect of market movements on both the measured value of guarantees in Jackson's variable annuity and fixed index annuity products and on the related derivatives used to manage the exposures inherent in these guarantees. As the Group applies US GAAP for the measured value of the product guarantees this item also includes asymmetric impacts where the measurement bases of the liabilities and associated derivatives used to manage the Jackson annuity business differ as described in note B1.3(c) below.

The net equity hedge result therefore includes significant accounting mismatches and other factors that detract from the presentation of an economic result. These other factors include:

- The variable annuity guarantees and fixed index annuity embedded options being only partially fair valued under 'grandfathered' US GAAP as described in note B1.3 (c);
- The interest rate exposure being managed through the other than equity-related derivative programme explained in note (b) below; and
- Jackson's management of its economic exposures for a number of other factors that are treated differently in the accounting frameworks such as future fees and assumed volatility levels.

The net equity hedge result (net of related DAC) can be summarised as follows:

	2017 £m	2016 £m
Fair value movements on equity hedge instruments[1]	**(1,871)**	(1,786)
Accounting value movements on the variable and fixed index annuity guarantee liabilities[2]	**(99)**	(188)
Fee assessments net of claim payments	**480**	387
Total	**(1,490)**	(1,587)

1. Held to manage equity exposures of the variable annuity guarantees and fixed index annuity options.
2. The accounting value movements on the variable and fixed index annuity guarantee liabilities reflect the impact of market movements and changes in economic and actuarial assumptions. These actuarial assumptions changes include, amongst other items, a charge (net of related DAC) of £359 million for strengthening policyholder utilisation and persistency rates offset by a benefit (net of related DAC) of £382 million from modelling refinements in the period, principally enhancements to how Jackson's own credit risk is incorporated in the fair valuation of these long-term liabilities.

(b) Other than equity-related derivatives

The fluctuations for this item comprise the net effect of:

- Fair value movements on free-standing, other than equity-related derivatives;
- Fair value movements on the Guaranteed Minimum Income Benefit (GMIB) reinsurance asset that are not matched by movements in the underlying GMIB liability, which is not fair valued as explained in note B1.3; and
- Related amortisation of DAC.

The free-standing, other than equity-related derivatives, are held to manage interest rate exposures and durations within the general account and the variable annuity guarantees and fixed index annuity embedded options described in note (a) above. Accounting mismatches arise because of differences between the measurement basis and presentation of the derivatives, which are fair valued with movements recorded in the income statement, and the exposures they are intended to manage.

(c) Short-term fluctuations related to debt securities

	2017 £m	2016 £m
Short-term fluctuations relating to debt securities		
(Charges) credits in the year:		
Losses on sales of impaired and deteriorating bonds	**(3)**	(94)
Defaults	**-**	(4)
Bond write-downs	**(2)**	(35)
Recoveries / reversals	**10**	15
Total credits (charges) in the year	**5**	(118)
Less: Risk margin allowance deducted from operating profit based on longer-term investment returns[note]	**86**	89
	91	(29)
Interest-related realised (losses) gains:		
(Losses) gains arising in the year	**(43)**	376
Less: Amortisation of gains and losses arising in current and prior years to operating profit based on longer-term investment returns	**(140)**	(135)
	(183)	241
Related amortisation of deferred acquisition costs	**19**	(11)
Total short-term fluctuations related to debt securities	**(73)**	201

Note

The debt securities of Jackson are held in the general account of the business. Realised gains and losses are recorded in the income statement with normalised returns included in operating profit with variations from year to year included in the short-term fluctuations category. The risk margin reserve charge for longer-term credit-related losses included in operating profit based on longer-term investment returns of Jackson for 2017 is based on an average annual risk margin reserve of 21 basis points (2016: 21 basis points) on average book values of US$55.3 billion (2016: US$56.4 billion) as shown below:

Moody's rating category (or equivalent under NAIC ratings of mortgage-backed securities)	2017 Average book value	2017 RMR	2017 Annual expected loss		2016 Average book value	2016 RMR	2016 Annual expected loss	
	US$m	%	US$m	£m	US$m	%	US$m	£m
A3 or higher	**27,277**	**0.12**	**(33)**	**(25)**	29,051	0.12	(36)	(27)
Baa1, 2 or 3	**26,626**	**0.22**	**(58)**	**(45)**	25,964	0.24	(62)	(46)
Ba1, 2 or 3	**1,046**	**1.03**	**(11)**	**(8)**	1,051	1.07	(11)	(8)
B1, 2 or 3	**318**	**2.70**	**(9)**	**(7)**	312	2.95	(9)	(7)
Below B3	**23**	**3.78**	**(1)**	**(1)**	40	3.81	(2)	(1)
Total	**55,290**	**0.21**	**(112)**	**(86)**	56,418	0.21	(120)	(89)
Related amortisation of deferred acquisition costs (see below)			**21**	**15**			23	17
Risk margin reserve charge to operating profit for longer-term credit-related losses			**(91)**	**(71)**			(97)	(72)

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.

In addition to the accounting for realised gains and losses described above for Jackson general account debt securities, included within the statement of other comprehensive income is a pre-tax credit of £541 million for net unrealised gains on debt securities classified as available-for-sale net of related amortisation of deferred acquisition costs (2016: credit of £48 million). Temporary market value movements do not reflect defaults or impairments. Additional details of the movement in the value of the Jackson portfolio are included in note C3.2(b).

(ii) *UK and Europe operations*

The negative short-term fluctuations in investment returns for UK and Europe operations of £(14) million (2016: positive £206 million) include net unrealised movements on fixed income assets supporting the capital of the shareholder-backed annuity business.

(iii) *Other operations*

The positive short-term fluctuations in investment returns for other operations of £20 million (2016: negative £(204) million) include unrealised value movements on financial instruments.

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

Operating segments

The Group's operating segments for financial reporting are defined and presented in accordance with IFRS 8, 'Operating Segments' on the basis of the management reporting structure and its financial management information. Following the combination during the year of the Group's UK insurance business and M&G to form M&G Prudential. The Group has reassessed its operating segments.

Under the Group's management and reporting structure its chief operating decision maker is the Group Executive Committee (GEC). In the revised management structure, responsibility is delegated to the Chief Executive Officers of Prudential Corporation Asia, the North American Business Unit and M&G Prudential for the day-to-day management of their business units (within the framework set out in the Group Governance Manual). Financial management information used by the GEC has been revised to align with these three business segments. These operating segments derive revenue from both long-term insurance and asset management activities.

In the prior year, the operating segments of the Group were each of the insurance operations in Asia, US and UK, and the asset management operations of Asia, US, M&G and Prudential Capital.

Operations which do not form part of any business unit are reported as 'Unallocated to a segment'. These include Group Head Office and Asia Regional Head Office costs. Following the formation of M&G Prudential certain minor operations which were previously reported as 'Unallocated to a segment' are now included in the UK and Europe segment, reflecting the revised structure. Prudential Capital and Africa operations do not form part of any operating segment under the revised structure, and their assets and liabilities and loss before tax are not material to the overall financial position of the Group. Prudential Capital and Africa operations are therefore reported as 'Unallocated to a segment'.

Comparative segmental information for prior periods has been presented on a basis consistent with the current year.

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 on shareholder-backed business. This includes the impact of short-term market effects on the carrying value of Jackson's guarantee liabilities and related derivatives as explained below.
– 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; and
– Profit / loss attaching to businesses that have been sold in the year including, where relevant, the recycling of the cumulative translation gain or loss in respect of sold businesses.

Determination of operating profit based on longer-term investment returns for investment and liability movements:

(a) General principles

(i) UK style with-profits business

The operating profit based on longer-term returns reflects the statutory transfer gross of attributable tax. Value movements in the underlying assets of the with-profits funds do not affect directly the determination of operating profit.

(ii) Unit-linked business

The policyholder unit liabilities are directly reflective of the underlying asset value movements. Accordingly, the operating results based on longer-term investment returns reflect the current period value movements in both the unit liabilities and the backing assets.

(iii) US variable annuity and fixed index annuity business

This business has guarantee liabilities which are measured on a combination of fair value and other US GAAP derived principles. These liabilities are subject to an extensive derivative programme to manage equity and interest rate exposures. The principles for determination of the operating profit and short-term fluctuations are necessarily bespoke, as discussed in section (c) below.

(iv) Business where policyholder liabilities are sensitive to market conditions

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

Examples of where such bifurcation is necessary are in Hong Kong and for UK shareholder-backed annuity business, as explained in sections b(i) and d(i), respectively. For other types of Asia's non-participating business, expected longer-term investment returns are used to determine the movement in policyholder liabilities for determining operating results.

(v) 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.

Except in the case of assets backing liabilities which are directly matched (such as unit-linked business) or closely correlated with value movements (as discussed below) operating profit based on longer-term investment returns for shareholder-financed business is determined on the basis of expected longer-term investment returns. 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.

Debt securities and loans
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.

At 31 December 2017, the level of unamortised interest-related realised gains and losses related to previously sold bonds for the Group was a net gain of £855 million (2016: £969 million).

Equity-type securities
For equity-type securities, the longer-term rates of return are estimates of the long-term trend investment returns 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 separate accounts are principally relevant for the US and Asia insurance operations. Different rates apply to different categories of equity-type securities.

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 derivatives whose value movements are excluded from operating profit arises in Jackson, as discussed below in section (c).

(b) Asia insurance operations
(i) Business where policyholder liabilities are sensitive to market conditions
For certain Asia non-participating business, for example in Hong Kong, 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 certain other types of non-participating business expected longer-term investment returns are used to determine the movement in policyholder liabilities for determining operating results.

(ii) Other Asia shareholder-financed business
Debt securities
For this business, 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.

Equity-type securities
For Asia insurance operations, investments in equity securities held for non-linked shareholder-backed operations amounted to £1,759 million as at 31 December 2017 (2016: £1,405 million). The rates of return applied in 2017 ranged from 4.3 per cent to 17.2 per cent (2016: 3.2 per cent to 13.9 per cent) with the rates applied varying by business unit. These rates are broadly stable from period to period but may be different between countries reflecting, for example, differing expectations of inflation in each business unit. The assumptions are for the 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 using the equity method are determined on a similar basis as the other Asia insurance operations described above.

(c) US insurance operations
(i) Separate account business
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.

(ii) 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. See note B1.2 note (i):

– Fair value movements for equity-based derivatives;
– Fair value movements for embedded derivatives for the 'not for life' portion of Guaranteed Minimum Withdrawal Benefit ('GMWB') and fixed index annuity business, and Guaranteed Minimum Income Benefit ('GMIB') reinsurance (see below);
– Movements in the accounts carrying value of Guaranteed Minimum Death Benefit ('GMDB'), GMIB and the 'for life' portion of GMWB liabilities, (see below) 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 (ie they are relatively insensitive to the effect of current period equity market and interest rate changes);
– A portion of the fee assessments as well as claim payments, in respect of guarantee liabilities; and
– Related amortisation of deferred acquisition costs for each of the above items.

Embedded derivatives for the 'not for life' portion of GMWB and fixed index annuity business
The 'not for life' portion of GMWB embedded derivative liabilities is measured under the US GAAP basis applied for IFRS in a manner consistent with IAS 39 under which the projected future growth rate of the account balance is based on current swap rates (rather than expected rates of return) with only a portion of the expected future guarantee fees included. Reserve value movements on these liabilities are sensitive to changes to levels of equity markets, implied volatility and interest rates.

Embedded derivatives for variable annuity guarantee minimum income benefit
The GMIB liability, which is substantially 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. This accounting basis substantially does not recognise the effects of market movements. 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 GMIB is economically reinsured, the mark to market element of the reinsurance asset is included as a component of short-term fluctuations in investment returns.

(iii) Other derivative value movements
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 other 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.

(iv) Other US shareholder-financed business
Debt securities
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 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.

Equity-type securities
As at 31 December 2017, the equity-type securities for US insurance non-separate account operations amounted to £946 million (2016: £1,323 million). For these operations, the longer-term rates of return for income and capital applied in the years indicated, which reflect the combination of the average risk-free rates over the year and appropriate risk premiums are as follows:

	2017	**2016**
Equity-type securities such as common and preferred stock and portfolio holdings in mutual funds	**6.1% to 6.5%**	5.5% to 6.5%
Other equity-type securities such as investments in limited partnerships and private equity funds	**8.1% to 8.5%**	7.5% to 8.5%

(d) UK and Europe insurance operations
(i) Shareholder-backed annuity business
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.

The operating result based on longer-term investment returns reflects the impact of value movements on policyholder liabilities for shareholder-backed annuity business within The Prudential Assurance Company Limited (PAC) 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 with 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 with 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.

(ii) Non-linked shareholder-financed business
For debt securities backing non-linked shareholder-financed business of the UK and Europe insurance operations (other than the annuity business) 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.

(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 in the operating result with temporary unrealised gains and losses being included in short-term fluctuations. 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.

B2 Acquisition costs and other expenditure

	2017 £m	**2016 £m**
Acquisition costs incurred for insurance policies	**(3,712)**	(3,687)
Acquisition costs deferred less amortisation of acquisition costs	**911**	923
Administration costs and other expenditure	**(6,380)**	(5,522)
Movements in amounts attributable to external unit holders of consolidated investment funds	**(984)**	(562)
Total acquisition costs and other expenditure	**(10,165)**	(8,848)

B3 Effect of changes and other accounting matters on insurance assets and liabilities

The following matters are relevant to the determination of the 2017 results:

(a) Asia insurance operations

In 2017, the IFRS operating profit based on longer-term investment returns for Asia insurance operations included a net credit of £75 million (2016: £67 million) representing a small number of individually minor items.

(b) US insurance operations

Changes in the policyholder liabilities held for variable and fixed index annuity guarantees are reported as part of non-operating profit and are as described in note B1.2.

(c) UK and Europe 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. The credit risk allowance comprises an amount for long-term best estimate defaults and additional provisions for credit risk premium, the cost of downgrades and short-term defaults.

The IFRS credit risk allowance made for the UK shareholder-backed fixed and linked annuity business equated to 42 basis points at 31 December 2017 (2016: 43 basis points). The allowance represented 28 per cent of the bond spread over swap rates (2016: 26 per cent).

The reserves for credit risk allowance at 31 December 2017 for the UK shareholder-backed business were £1.6 billion (2016: £1.7 billion).

Other assumption changes

For the shareholder-backed business, in addition to the movement in the credit risk allowance discussed above, the net effect of routine changes to assumptions in 2017, was a credit of £173 million (2016: credit of £16 million).This included, amongst other items, a benefit to IFRS operating profit based on longer-term investment returns of £204 million, relating to changes to annuitant mortality assumptions primarily reflecting the adoption of the Continuous Mortality Investigation (CMI) 2015 model.

Longevity reinsurance and other management actions

A number of management actions were taken in 2017 to improve the solvency position of the UK and Europe insurance operations and further mitigate market risk, which have generated combined profits of £276 million. Similar actions were also taken in 2016 and 2015.

Of this amount £31 million related to profit from an additional longevity reinsurance transactions covering £0.5 billion of annuity liabilities on an IFRS basis, with the balance of £245 million reflecting the effect of repositioning the fixed income portfolio and other actions. The contribution to profit from similar longevity reinsurance and other management actions in 2016 was £332 million (of which £197 million related to longevity reinsurance transactions covering £5.4 billion of IFRS annuity liabilities).

At 31 December 2017, longevity reinsurance covered £14.4 billion of IFRS annuity liabilities equivalent to 44 per cent of total annuity liabilities (2016: £14.4 billion, 42 per cent).

Review of past annuity sales

Prudential has agreed with the Financial Conduct Authority (FCA) to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. The review will examine whether customers were given sufficient information about their potential eligibility to purchase an enhanced annuity, either from Prudential or another pension provider. The FCA formally released its redress calculation methodology in early 2018 and accordingly Prudential reassessed the provision held to cover the costs of undertaking the review and any potential redress. At 31 December 2017, following this reassessment, the gross provision was increased to £400 million (2016: £175 million), excluding any utilisation during the year. The ultimate amount that will be expended by the Group on the review, which is currently expected to be completed in 2019, remains uncertain. Although the Group's professional indemnity insurance is expected to mitigate the overall financial impact of this review, with potential insurance recoveries of up to £175 million, no such recovery has been factored in the provision, in accordance with the requirements of IAS 37 'Provisions, Contingent Liabilities and Contingent Assets'.

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B4 Tax charge

On 22 December 2017, a significant US tax reform package, The Tax Cuts and Jobs Act, was enacted into law effective from 1 January 2018. The tax reform package as a whole, which includes a reduction in the corporate income tax rate from 35 per cent to 21 per cent, and a number of specific measures affecting US life insurers, is expected to be beneficial in the longer term. However in 2017 the changes have had an adverse impact on the tax charge attributable to shareholders in the Group's US operations and a benefit to policyholders in the with-profits fund of the UK and Europe operations, due to the requirement to remeasure deferred tax balances at the new 21 per cent rate. The 2017 impacts on the Group's income statement and on other comprehensive income of the US tax changes are set out below and the impact on the balance sheet are set out in note C8.

(a) Total tax charge by nature of expense

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

	2017 £m			2016 £m
Tax charge	**Current tax**	**Deferred tax**	**Total**	**Total**
Attributable to shareholders:				
Asia operations	**(164)**	**(89)**	**(253)**	(256)
US operations	**56**	**(564)**	**(508)**	66
UK and Europe	**(302)**	**35**	**(267)**	(275)
Other operations	**122**	**-**	**122**	111
Tax charge attributable to shareholders' returns	**(288)**	**(618)**	**(906)**	(354)
Attributable to policyholders:				
Asia operations	**(92)**	**(157)**	**(249)**	(155)
UK and Europe	**(316)**	**(109)**	**(425)**	(782)
Tax charge attributable to policyholders' returns	**(408)**	**(266)**	**(674)**	(937)
Total tax charge	**(696)**	**(884)**	**(1,580)**	(1,291)

The principal reason for the increase in the tax charge attributable to shareholders' returns is a £445 million deferred tax charge arising on the remeasurement of the US net deferred tax assets from 35 per cent to 21 per cent. The principal reason for the decrease in the tax charge attributable to policyholders' returns is a smaller increase in deferred tax liabilities on unrealised gains on investments in the with-profits fund of UK and Europe compared to 2016, combined with a £92 million credit following the remeasurement of US net deferred tax liabilities in the same with-profits fund.

The reconciliation of the expected to actual tax charge attributable to shareholders is provided in (b) below. The tax charge attributable to policyholders of £674 million above is equal to the profit before tax attributable to policyholders of £674 million. This is the result of accounting for policyholder income after the deduction of expenses and movement on unallocated surpluses and on an after tax basis.

In 2017, a tax charge of £75 million (2016: credit of £10 million) attributable to shareholders has been taken through other comprehensive income. The 2017 charge includes a £190 million deferred tax charge primarily on unrealised gains on bonds held in the US operations partly offset by £134 million benefit relating to the remeasurement of US net deferred tax liabilities on the bonds

(b) Reconciliation of shareholder effective tax rate

In the reconciliation below, the expected tax rates reflect the corporation tax rates that are expected to apply to the taxable profit of the relevant business. Where there are profits of more than one jurisdiction the expected tax rates reflect the corporation tax rates weighted by reference to the amount of profit contributing to the aggregate business result.

	2017 £m					
	Asia operations	US operations	UK and Europe	Other* operations	Total attributable to shareholders	Percentage impact on ETR
Operating profit (loss) based on longer-term investment returns	**1,975**	**2,224**	**1,378**	**(878)**	**4,699**	
Non-operating profit (loss)	**53**	**(1,462)**	**(14)**	**20**	**(1,403)**	
Profit (loss) before tax	**2,028**	**762**	**1,364**	**(858)**	**3,296**	
Expected tax rate	**21%**	**35%**	**19%**	**19%**	**24%**	
Tax at the expected rate	**426**	**267**	**259**	**(163)**	**789**	**23.9%**
Effects of recurring tax reconciliation items:						
Income not taxable or taxable at concessionary rates	**(64)**	**(11)**	**(2)**	**(14)**	**(91)**	**(2.8%)**
Deductions not allowable for tax purposes	**26**	**6**	**13**	**10**	**55**	**1.7%**
Items related to taxation of life insurance businesses	**(92)**	**(238)**	**(2)**	**-**	**(332)**	**(10.1%)**
Deferred tax adjustments	**11**	**17**	**(1)**	**(5)**	**22**	**0.7%**
Effect of results of joint ventures and associates	**(52)**	**-**	**(3)**	**-**	**(55)**	**(1.7%)**
Irrecoverable withholding taxes	**-**	**-**	**-**	**54**	**54**	**1.6%**
Other	**(10)**	**-**	**6**	**(1)**	**(5)**	**(0.1%)**
Total	**(181)**	**(226)**	**11**	**44**	**(352)**	**(10.7%)**
Effects of non-recurring tax reconciliation items:						
Adjustments to tax charge in relation to prior years	**(3)**	**(15)**	**(3)**	**(3)**	**(24)**	**(0.7%)**
Movements in provisions for open tax matters	**19**	**25**	**-**	**-**	**44**	**1.3%**
Impact of US tax reform	**-**	**445**	**-**	**-**	**445**	**13.5%**
Adjustments in relation to business disposals	**(8)**	**12**	**-**	**-**	**4**	**0.1%**
Total	**8**	**467**	**(3)**	**(3)**	**469**	**14.2%**
Total actual tax charge (credit)	**253**	**508**	**267**	**(122)**	**906**	**27.4%**
Analysed into:						
Tax on operating profit based on longer-term investment returns	**276**	**548**	**268**	**(121)**	**971**	
Tax on non-operating profit	**(23)**	**(40)**	**(1)**	**(1)**	**(65)**	
Actual tax rate:						
Operating profit based on longer-term investment returns:						
Including non-recurring tax reconciling items	**14%**	**25%**	**19%**	**14%**	**21%**	
Excluding non-recurring tax reconciling items	**13%**	**24%**	**20%**	**13%**	**20%**	
Total profit	**12%**	**67%**	**20%**	**14%**	**27%**	

* Other operations include restructuring costs.

The more significant reconciling items are explained below:

Income not taxable or taxable at concessionary rates

£26 million of the £64 million reconciling item in Asia operations is due to non-taxable gains on domestic securities in Taiwan (no equivalent amount in 2016) with the balance principally relating to income taxable at rates lower than the expected rates in Malaysia and Singapore.

Items related to taxation of life insurance businesses

The £92 million reconciling item in Asia operations reflects where the basis of tax is not the accounting profits, primarily in:
- Hong Kong where the taxable profit is based on the net insurance premiums; and
- Indonesia and Philippines where investment income is subject to withholding tax at source and no further corporation tax.

It is higher than the 2016 adjustment of £20 million due to a larger proportion of profits attributable to Hong Kong.

The £238 million (full year 2016: £159 million) reconciling item in US operations reflects the impact of the dividend received deduction on the taxation of profits from variable annuity business. US tax reform changes effective from 1 January 2018 are expected to reduce the level of this deduction from 2018 onwards.

Effects of results of joint ventures and associates

The £55 million reconciling item arises from the accounting requirement for inclusion in the profit before tax of Prudential's share of the profits after tax from the joint ventures and associates, with no equivalent item included in Prudential's tax charge.

Irrecoverable withholding taxes

The £54 million adverse reconciling items reflects withholding taxes on dividends paid by certain non-UK subsidiaries, principally Indonesia, to the UK. The dividends are exempt from UK tax and consequently the withholding tax cannot be offset against UK tax payments.

Movements in provisions for open tax matters

The complexity of the tax laws and regulations that relate to our businesses means that from time to time we may disagree with tax authorities on the technical interpretation of a particular area of tax law. This uncertainty means that in the normal course of business the Group will have matters where upon ultimate resolution of the uncertainty, the amount of profit subject to tax may be greater than the amounts reflected in the Group's submitted tax returns. The statement of financial position contains the following provisions in relation to open tax matters:

	£m
At 1 January 2017	**(89)**
Movements in the current period included in:	
Tax charge attributable to shareholders	**(44)**
Other movements*	**(6)**
At 31 December 2017	**(139)**

* Other movements include interest arising on open tax matters and amounts included in the Group's share of profits from joint ventures and associates, net of related tax.

Impact of US tax reform

As noted earlier, the reduction in the US corporate income tax rate from 35 per cent to 21 per cent from 1 January 2018 was substantively enacted on 22 December 2017, giving rise to a £445 million unfavourable reconciling item in US operations relating to the remeasurement of the net deferred tax asset attributable to shareholders. Separately a £134 million benefit has been recognised in other comprehensive income. Further detail on the impact of US tax reform is provided in note C8.

	2016** £m					
	Asia operations	**US operations**	**UK and Europe**	**Other* operations**	**Total attributable to shareholders**	**Percentage impact on ETR**
Operating profit (loss) based on longer-term investment returns	1,644	2,048	1,253	(689)	4,256	
Non-operating (loss) profit	(460)	(1,523)	206	(204)	(1,981)	
Profit (loss) before tax	1,184	525	1,459	(893)	2,275	
Expected tax rate	22%	35%	20%	20%	24%	
Tax at the expected rate	260	184	292	(179)	557	24.4%
Effects of recurring tax reconciliation items:						
Income not taxable or taxable at concessionary rates	(31)	(18)	(13)	(5)	(67)	(2.9%)
Deductions not allowable for tax purposes	20	8	10	22	60	2.6%
Items related to taxation of life insurance businesses	(20)	(159)	(1)	-	(180)	(7.9%)
Deferred tax adjustments	(11)	-	2	(14)	(23)	(1.0%)
Effect of results of joint ventures and associates	(44)	-	(2)	-	(46)	(2.0%)
Irrecoverable withholding taxes	-	-	-	36	36	1.6%
Other	3	-	-	(7)	(4)	(0.1%)
Total	(83)	(169)	(4)	32	(224)	(9.7%)
Effects of non-recurring tax reconciliation items:						
Adjustments to tax charge in relation to prior years	1	(81)	(7)	5	(82)	(3.6%)
Movements in provisions for open tax matters	20	-	-	31	51	2.2%
Impact of changes in local statutory tax rates	-	-	(6)	-	(6)	(0.2%)
Write-down of Korea life business	58	-	-	-	58	2.5%
Total	79	(81)	(13)	36	21	0.9%
Total actual tax charge (credit)	256	(66)	275	(111)	354	15.6%
Analysed into:						
Tax on operating profit based on longer-term investment returns	271	467	244	(88)	894	
Tax on non-operating profit	(15)	(533)	31	(23)	(540)	
Actual tax rate:						
Operating profit based on longer-term investment returns:						
Including non-recurring tax reconciling items	16%	23%	19%	13%	21%	
Excluding non-recurring tax reconciling items	15%	27%	21%	18%	22%	
Total profit	22%	(13)%	19%	12%	16%	

* Other operations include restructuring costs.

**The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3.

The 2016 expected and actual tax rates as shown include the impact of the re-measurement loss on the held for sale Korea life business. The 2016 tax rates for Asia operations and Group, excluding the impact of the held for sale Korea life business are as follows:

	Asia operations	**Attributable to shareholders**
Expected tax rate on total profit	22%	24%
Actual tax rate:		
Operating profit based on longer-term investment returns	16%	21%
Total profit	18%	14%

B5 Earnings per share

		2017					
	Note	Before tax B1.1 £m	Tax B4 £m	Non-controlling interests £m	Net of tax and non-controlling interests £m	Basic earnings per share Pence	Diluted earnings per share Pence
Based on operating profit based on longer-term investment returns		**4,699**	**(971)**	**(1)**	**3,727**	**145.2p**	**145.1p**
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	**(1,563)**	**572**	**-**	**(991)**	**(38.6)p**	**(38.6)p**
Amortisation of acquisition accounting adjustments		**(63)**	**20**	**-**	**(43)**	**(1.7)p**	**(1.7)p**
Cumulative exchange gain on the sold Korea life business recycled from other comprehensive income	D1	**61**	**-**	**-**	**61**	**2.4p**	**2.4p**
Profit attaching to disposal of businesses	D1	**162**	**(82)**	**-**	**80**	**3.1p**	**3.1p**
Impact of US Tax Reform	B4	**-**	**(445)**	**-**	**(445)**	**(17.3)p**	**(17.3)p**
Based on profit for the year		**3,296**	**(906)**	**(1)**	**2,389**	**93.1p**	**93.0p**

		2016					
	Note	Before tax B1.1 £m	Tax B4 £m	Non-controlling interests £m	Net of tax and non-controlling interests £m	Basic earnings per share Pence	Diluted earnings per share Pence
Based on operating profit based on longer-term investment returns		4,256	(894)	-	3,362	131.3p	131.2p
Short-term fluctuations in investment returns on shareholder-backed business	B1.2	(1,678)	519	-	(1,159)	(45.3)p	(45.2)p
Loss attaching to held for sale Korea life business	D1	(227)	(4)	-	(231)	(9.0)p	(9.0)p
Amortisation of acquisition accounting adjustments		(76)	25	-	(51)	(2.0)p	(2.0)p
Based on profit for the year		2,275	(354)	-	1,921	75.0p	75.0p

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, which excludes those held in employee share trusts and consolidated unit trusts and OEICs, is set out as below:

Weighted average number of shares for calculation of:	2017 (millions)	2016 (millions)
Basic earnings per share	**2,567**	2,560
Shares under option at end of year	**6**	7
Number of shares that would have been issued at fair value on assumed option price	**(5)**	(5)
Diluted earnings per share	**2,568**	2,562

B6 Dividends

	2017		2016	
	Pence per share	**£m**	**Pence per share**	**£m**
Dividends relating to reporting year:				
First interim ordinary dividend	**14.50p**	**375**	12.93p	333
Second interim ordinary dividend	**32.50p**	**841**	30.57p	789
Total	**47.00p**	**1,216**	43.50p	1,122
Dividends paid in reporting year:				
Current year first interim ordinary dividend	**14.50p**	**373**	12.93p	332
Second interim ordinary dividend for prior year	**30.57p**	**786**	26.47p	679
Special dividend	**-**	**-**	10.00p	256
Total	**45.07p**	**1,159**	49.40p	1,267

Dividend per share

For the year ended 31 December 2016 the second interim ordinary dividend of 30.57 pence per ordinary share was paid to eligible shareholders on 19 May 2017. The 2017 first interim ordinary dividend of 14.50 pence per ordinary share was paid to eligible shareholders on 28 September 2017.

The second interim ordinary dividend for the year ended 31 December 2017 of 32.50 pence per ordinary share will be paid on 18 May 2018 in sterling to shareholders on the principal register and the Irish branch register at 6.00pm BST on 3 April 2018 (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 25 May 2018. The second interim ordinary dividend will be paid on or about 25 May 2018 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 13 March 2018. The exchange rate at which the dividend payable to the SG Shareholders will be translated into Singapore dollars, 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 statement of financial position by segment

(a) Position as at 31 December 2017

By operating segment	Note	2017 £m Asia C2.1	US C2.2	UK and Europe C2.3	Unallocated to a segment (other operations) note (i)	Elimination of intra-group debtors and creditors	Group Total	2016 £m Group Total
Assets								
Goodwill	C5(a)	**305**	**-**	**1,177**	**-**	**-**	**1,482**	1,628
Deferred acquisition costs and other intangible assets	C5(b)	**2,540**	**8,219**	**210**	**42**	**-**	**11,011**	10,807
Property, plant and equipment		**125**	**214**	**447**	**3**	**-**	**789**	743
Reinsurers' share of insurance contract liabilities		**1,960**	**6,424**	**2,521**	**3**	**(1,235)**	**9,673**	10,051
Deferred tax assets	C8	**112**	**2,300**	**157**	**58**	**-**	**2,627**	4,315
Current tax recoverable		**58**	**298**	**244**	**93**	**(80)**	**613**	440
Accrued investment income		**595**	**492**	**1,558**	**31**	**-**	**2,676**	3,153
Other debtors		**2,675**	**248**	**3,118**	**2,121**	**(5,199)**	**2,963**	3,019
Investment properties		**5**	**5**	**16,487**	**-**	**-**	**16,497**	14,646
Investment in joint ventures and associates accounted for using the equity method		**912**	**-**	**504**	**-**	**-**	**1,416**	1,273
Loans	C3.3	**1,317**	**9,630**	**5,986**	**109**	**-**	**17,042**	15,173
Equity securities and portfolio holdings in unit trusts		**29,976**	**130,630**	**62,670**	**115**	**-**	**223,391**	198,552
Debt securities	C3.2	**40,982**	**35,378**	**92,707**	**2,307**	**-**	**171,374**	170,458
Derivative assets		**113**	**1,611**	**2,954**	**123**	**-**	**4,801**	3,936
Other investments		**-**	**848**	**4,774**	**-**	**-**	**5,622**	5,465
Deposits		**1,291**	**43**	**9,540**	**362**	**-**	**11,236**	12,185
Assets held for sale		**-**	**-**	**38**	**-**	**-**	**38**	4,589
Cash and cash equivalents		**1,934**	**1,658**	**5,808**	**1,290**	**-**	**10,690**	10,065
Total assets	C1	**84,900**	**197,998**	**210,900**	**6,657**	**(6,514)**	**493,941**	470,498
Total equity		**5,926**	**5,248**	**8,245**	**(3,325)**	**-**	**16,094**	14,667
Liabilities								
Insurance contract liabilities	C4.1	**63,468**	**177,728**	**88,180**	**31**	**(1,235)**	**328,172**	316,436
Investment contract liabilities with discretionary participation features	C4.1	**337**	**-**	**62,340**	**-**	**-**	**62,677**	52,837
Investment contract liabilities without discretionary participation features	C4.1	**328**	**2,996**	**17,069**	**1**	**-**	**20,394**	19,723
Unallocated surplus of with-profits funds	C4.1	**3,474**	**-**	**13,477**	**-**	**-**	**16,951**	14,317
Core structural borrowings of shareholder-financed operations	C6.1	**-**	**184**	**-**	**6,096**	**-**	**6,280**	6,798
Operational borrowings attributable to shareholder-financed operations	C6.2	**50**	**508**	**148**	**1,085**	**-**	**1,791**	2,317
Borrowings attributable to with-profits operations	C6.2	**10**	**-**	**3,706**	**-**	**-**	**3,716**	1,349
Obligations under funding, securities lending and sale and repurchase agreements		**-**	**4,304**	**1,358**	**-**	**-**	**5,662**	5,031
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		**3,631**	**-**	**5,243**	**15**	**-**	**8,889**	8,687
Deferred tax liabilities	C8	**1,152**	**1,845**	**1,703**	**15**	**-**	**4,715**	5,370
Current tax liabilities		**122**	**47**	**377**	**71**	**(80)**	**537**	649
Accruals deferred income and other liabilities		**6,069**	**5,109**	**6,609**	**1,597**	**(5,199)**	**14,185**	13,825
Provisions		**254**	**24**	**784**	**61**	**-**	**1,123**	947
Derivative liabilities		**79**	**5**	**1,661**	**1,010**	**-**	**2,755**	3,252
Liabilities held for sale	D1	**-**	**-**	**-**	**-**	**-**	**-**	4,293
Total liabilities	C1	**78,974**	**192,750**	**202,655**	**9,982**	**(6,514)**	**477,847**	455,831
Total equity and liabilities		**84,900**	**197,998**	**210,900**	**6,657**	**(6,514)**	**493,941**	470,498

Note

(i) Unallocated to a segment includes central operations, Prudential Capital and Africa operations as per note B1.3.

C2 Analysis of segment statement of financial position by business type

C2.1 Asia

		31 Dec 2017 £m							31 Dec 2016* £m
		Insurance							
	Note	With-profits business	Unit-linked assets and liabilities	Other business	Total	Asset management	Eliminations	Total	Total
Assets									
Goodwill		**-**	**-**	**244**	**244**	**61**	**-**	**305**	306
Deferred acquisition costs and other intangible assets		**45**	**-**	**2,490**	**2,535**	**5**	**-**	**2,540**	2,319
Property, plant and equipment		**86**	**-**	**36**	**122**	**3**	**-**	**125**	124
Reinsurers' share of insurance contract liabilities		**76**	**-**	**1,884**	**1,960**	**-**	**-**	**1,960**	1,539
Deferred tax assets		**-**	**-**	**102**	**102**	**10**	**-**	**112**	107
Current tax recoverable		**1**	**2**	**55**	**58**	**-**	**-**	**58**	29
Accrued investment income		**230**	**53**	**277**	**560**	**35**	**-**	**595**	549
Other debtors		**1,823**	**169**	**648**	**2,640**	**67**	**(32)**	**2,675**	2,662
Investment properties		**-**	**-**	**5**	**5**	**-**	**-**	**5**	5
Investment in joint ventures and associates accounted for using the equity method		**-**	**-**	**768**	**768**	**144**	**-**	**912**	825
Loans	C3.3	**725**	**-**	**592**	**1,317**	**-**	**-**	**1,317**	1,303
Equity securities and portfolio holdings in unit trusts		**14,995**	**13,199**	**1,759**	**29,953**	**23**	**-**	**29,976**	23,599
Debt securities	C3.2	**24,432**	**3,507**	**13,043**	**40,982**	**-**	**-**	**40,982**	36,546
Derivative assets		**82**	**5**	**26**	**113**	**-**	**-**	**113**	47
Deposits		**246**	**511**	**499**	**1,256**	**35**	**-**	**1,291**	1,425
Assets held for sale	D1	**-**	**-**	**-**	**-**	**-**	**-**	**-**	3,863
Cash and cash equivalents		**632**	**287**	**822**	**1,741**	**193**	**-**	**1,934**	2,157
Total assets		**43,373**	**17,733**	**23,250**	**84,356**	**576**	**(32)**	**84,900**	77,405
Total equity		**-**	**-**	**5,525**	**5,525**	**401**	**-**	**5,926**	5,376
Liabilities									
Insurance contract liabilities		**33,861**	**15,935**	**13,672**	**63,468**	**-**	**-**	**63,468**	54,417
Investment contract liabilities with discretionary participation features	C4.1	**337**	**-**	**-**	**337**	**-**	**-**	**337**	347
Investment contract liabilities without discretionary participation features	C4.1	**-**	**328**	**-**	**328**	**-**	**-**	**328**	254
Unallocated surplus of with-profits funds		**3,474**	**-**	**-**	**3,474**	**-**	**-**	**3,474**	2,667
Operational borrowings attributable to shareholder-financed operations		**-**	**7**	**43**	**50**	**-**	**-**	**50**	19
Borrowings attributable to with-profits operations		**10**	**-**	**-**	**10**	**-**	**-**	**10**	4
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		**2,152**	**1,219**	**260**	**3,631**	**-**	**-**	**3,631**	3,093
Deferred tax liabilities		**774**	**38**	**340**	**1,152**	**-**	**-**	**1,152**	935
Current tax liabilities		**24**	**-**	**81**	**105**	**17**	**-**	**122**	125
Accruals, deferred income and other liabilities		**2,620**	**206**	**3,207**	**6,033**	**68**	**(32)**	**6,069**	5,916
Provisions		**62**	**-**	**102**	**164**	**90**	**-**	**254**	229
Derivative liabilities		**59**	**-**	**20**	**79**	**-**	**-**	**79**	265
Liabilities held for sale	D1	**-**	**-**	**-**	**-**	**-**	**-**	**-**	3,758
Total liabilities		**43,373**	**17,733**	**17,725**	**78,831**	**175**	**(32)**	**78,974**	72,029
Total equity and liabilities		**43,373**	**17,733**	**23,250**	**84,356**	**576**	**(32)**	**84,900**	77,405

* The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3.

Note

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'.

C2.2 US

	Note	31 Dec 2017 £m						31 Dec 2016* £m
		Insurance						
		Variable annuity separate account assets and liabilities	Fixed annuity, GIC and other business	Total	Asset management	Eliminations	Total	Total
Assets								
Goodwill		**-**	**-**	**-**	**-**	**-**	**-**	16
Deferred acquisition costs and other intangible assets		**-**	**8,216**	**8,216**	**3**	**-**	**8,219**	8,327
Property, plant and equipment		**-**	**209**	**209**	**5**	**-**	**214**	247
Reinsurers' share of insurance contract liabilities		**-**	**6,424**	**6,424**	**-**	**-**	**6,424**	7,224
Deferred tax assets		**-**	**2,218**	**2,218**	**82**	**-**	**2,300**	3,979
Current tax recoverable		**-**	**284**	**284**	**14**	**-**	**298**	101
Accrued investment income		**-**	**444**	**444**	**48**	**-**	**492**	628
Other debtors		**-**	**247**	**247**	**77**	**(76)**	**248**	304
Investment properties		**-**	**5**	**5**	**-**	**-**	**5**	6
Loans	C3.3	**-**	**9,630**	**9,630**	**-**	**-**	**9,630**	9,735
Equity securities and portfolio holdings in unit trusts		**130,528**	**102**	**130,630**	**-**	**-**	**130,630**	120,747
Debt securities	C3.2	**-**	**35,378**	**35,378**	**-**	**-**	**35,378**	40,745
Derivative assets		**-**	**1,611**	**1,611**	**-**	**-**	**1,611**	834
Other investments		**-**	**844**	**844**	**4**	**-**	**848**	992
Deposits		**-**	**-**	**-**	**43**	**-**	**43**	49
Cash and cash equivalents		**-**	**1,224**	**1,224**	**434**	**-**	**1,658**	1,135
Total assets		**130,528**	**66,836**	**197,364**	**710**	**(76)**	**197,998**	195,069
Total equity		**-**	**5,013**	**5,013**	**235**	**-**	**5,248**	5,408
Liabilities								
Insurance contract liabilities		**130,528**	**47,200**	**177,728**	**-**	**-**	**177,728**	174,328
Investment contract liabilities without discretionary participation features	C4.1	**-**	**2,996**	**2,996**	**-**	**-**	**2,996**	3,298
Core structural borrowings of shareholder-financed operations		**-**	**184**	**184**	**-**	**-**	**184**	202
Operational borrowings attributable to shareholder-financed operations		**-**	**508**	**508**	**-**	**-**	**508**	480
Obligations under funding, securities lending and sale and repurchase agreements		**-**	**4,304**	**4,304**	**-**	**-**	**4,304**	3,534
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		**-**	**-**	**-**	**-**	**-**	**-**	-
Deferred tax liabilities		**-**	**1,844**	**1,844**	**1**	**-**	**1,845**	2,832
Current tax liabilities		**-**	**46**	**46**	**1**	**-**	**47**	-
Accruals, deferred income and other liabilities		**-**	**4,728**	**4,728**	**457**	**(76)**	**5,109**	4,920
Provisions		**-**	**8**	**8**	**16**	**-**	**24**	3
Derivative liabilities		**-**	**5**	**5**	**-**	**-**	**5**	64
Total liabilities		**130,528**	**61,823**	**192,351**	**475**	**(76)**	**192,750**	189,661
Total equity and liabilities		**130,528**	**66,836**	**197,364**	**710**	**(76)**	**197,998**	195,069

* The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3.

C2.3 UK and Europe

		31 Dec 2017 £m							31 Dec 2016* £m
		Insurance							
			Other funds and subsidiaries						
By operating segment	Note	With-profits sub-funds note (i)	Unit-linked assets and liabilities	Annuity and other long-term business	Total	Asset management	Eliminations	Total	Total
Assets									
Goodwill		**24**	**-**	**-**	**24**	**1,153**	**-**	**1,177**	1,306
Deferred acquisition costs and other intangible assets		**100**	**-**	**103**	**203**	**7**	**-**	**210**	132
Property, plant and equipment		**406**	**-**	**37**	**443**	**4**	**-**	**447**	369
Reinsurers' share of insurance contract liabilities		**1,269**	**133**	**1,119**	**2,521**	**-**	**-**	**2,521**	2,590
Deferred tax assets		**70**	**-**	**64**	**134**	**23**	**-**	**157**	174
Current tax recoverable		**63**	**-**	**181**	**244**	**-**	**-**	**244**	308
Accrued investment income		**892**	**107**	**553**	**1,552**	**6**	**-**	**1,558**	1,939
Other debtors		**1,553**	**76**	**624**	**2,253**	**941**	**(76)**	**3,118**	3,233
Investment properties		**14,153**	**682**	**1,652**	**16,487**	**-**	**-**	**16,487**	14,635
Investment in joint ventures and associates accounted for using the equity method		**464**	**-**	**-**	**464**	**40**	**-**	**504**	448
Loans	C3.3	**4,268**	**-**	**1,718**	**5,986**	**-**	**-**	**5,986**	3,572
Equity securities and portfolio holdings in unit trusts		**47,173**	**15,369**	**9**	**62,551**	**119**	**-**	**62,670**	54,177
Debt securities	C3.2	**50,661**	**6,711**	**35,335**	**92,707**	**-**	**-**	**92,707**	90,796
Derivative assets		**2,420**	**8**	**526**	**2,954**	**-**	**-**	**2,954**	2,927
Other investments		**4,744**	**11**	**1**	**4,756**	**18**	**-**	**4,774**	4,473
Deposits		**7,167**	**1,139**	**1,234**	**9,540**	**-**	**-**	**9,540**	10,705
Assets held for sale note (ii)		**38**	**-**	**-**	**38**	**-**	**-**	**38**	726
Cash and cash equivalents		**4,096**	**693**	**576**	**5,365**	**443**	**-**	**5,808**	5,064
Total assets		**139,561**	**24,929**	**43,732**	**208,222**	**2,754**	**(76)**	**210,900**	197,574
Total equity		**-**	**-**	**6,344**	**6,344**	**1,901**	**-**	**8,245**	7,832
Liabilities									
Insurance contract liabilities	C4.1	**48,894**	**6,097**	**33,189**	**88,180**	**-**	**-**	**88,180**	88,993
Investment contract liabilities with discretionary participation features	C4.1	**62,323**	**-**	**17**	**62,340**	**-**	**-**	**62,340**	52,490
Investment contract liabilities without discretionary participation features	C4.1	**5**	**17,048**	**16**	**17,069**	**-**	**-**	**17,069**	16,171
Unallocated surplus of with-profits funds	C4.1	**13,477**	**-**	**-**	**13,477**	**-**	**-**	**13,477**	11,650
Operational borrowings attributable to shareholder-financed operations		**-**	**4**	**123**	**127**	**21**	**-**	**148**	167
Borrowings attributable to with-profits operations		**3,706**	**-**	**-**	**3,706**	**-**	**-**	**3,706**	1,345
Obligations under funding, securities lending and sale and repurchase agreements		**748**	**-**	**610**	**1,358**	**-**	**-**	**1,358**	1,497
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		**3,409**	**1,667**	**167**	**5,243**	**-**	**-**	**5,243**	5,594
Deferred tax liabilities		**1,410**	**-**	**274**	**1,684**	**19**	**-**	**1,703**	1,592
Current tax liabilities		**119**	**76**	**138**	**333**	**44**	**-**	**377**	513
Accruals deferred income and other liabilities		**4,791**	**36**	**1,293**	**6,120**	**565**	**(76)**	**6,609**	6,688
Provisions		**55**	**-**	**525**	**580**	**204**	**-**	**784**	647
Derivative liabilities		**624**	**1**	**1,036**	**1,661**	**-**	**-**	**1,661**	1,860
Liabilities held for sale note (ii)		**-**	**-**	**-**	**-**	**-**	**-**	**-**	535
Total liabilities		**139,561**	**24,929**	**37,388**	**201,878**	**853**	**(76)**	**202,655**	189,742
Total equity and liabilities		**139,561**	**24,929**	**43,732**	**208,222**	**2,754**	**(76)**	**210,900**	197,574

* The 2016 comparative results have been re-presented from those previously published following reassessment of the Group's operating segments as described in note B1.3.

Note

(i) Includes the Scottish Amicable Insurance Fund which, at 31 December 2017 have total assets and liabilities of £5,768 million (2016: £6,101 million). 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). The PAC with-profits fund includes £10.6 billion (2016: £11.2 billion) of non-profits annuities liabilities.

(ii) The assets and liabilities held for sale for the UK and Europe insurance operations comprise the investment properties and consolidated venture investments of the PAC with-profits fund, for which the sales had been agreed but not yet completed at the year end.

C3 Assets and liabilities

C3.1 Group assets and liabilities – measurement

(a) Determination of fair value

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.

Other than the loans which have been designated at fair value through profit or loss, the loans and receivables have been shown net of provisions for impairment. The fair value of loans have been estimated from discounted cash flows expected to be received. The discount rate is updated for 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 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 measurement hierarchy of Group assets and liabilities

Assets and liabilities carried at fair value on the statement of financial position

The table below shows the assets and liabilities 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.

Financial instruments at fair value

	31 Dec 2017 £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				
Loans	**-**	**-**	**2,023**	**2,023**
Equity securities and portfolio holdings in unit trusts	**57,347**	**4,470**	**351**	**62,168**
Debt securities	**29,143**	**45,602**	**348**	**75,093**
Other investments (including derivative assets)	**68**	**3,638**	**3,540**	**7,246**
Derivative liabilities	**(68)**	**(615)**	**-**	**(683)**
Total financial investments, net of derivative liabilities	**86,490**	**53,095**	**6,262**	**145,847**
Percentage of total	**60%**	**36%**	**4%**	**100%**
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	**158,631**	**457**	**10**	**159,098**
Debt securities	**4,993**	**5,226**	**-**	**10,219**
Other investments (including derivative assets)	**12**	**4**	**8**	**24**
Derivative liabilities	**-**	**(1)**	**-**	**(1)**
Total financial investments, net of derivative liabilities	**163,636**	**5,686**	**18**	**169,340**
Percentage of total	**97%**	**3%**	**0%**	**100%**
Non-linked shareholder-backed				
Loans	**-**	**-**	**2,814**	**2,814**
Equity securities and portfolio holdings in unit trusts	**2,105**	**10**	**10**	**2,125**
Debt securities	**21,443**	**64,313**	**306**	**86,062**
Other investments (including derivative assets)	**7**	**2,270**	**876**	**3,153**
Derivative liabilities	**-**	**(1,559)**	**(512)**	**(2,071)**
Total financial investments, net of derivative liabilities	**23,555**	**65,034**	**3,494**	**92,083**
Percentage of total	**25%**	**71%**	**4%**	**100%**
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans	**-**	**-**	**4,837**	**4,837**
Equity securities and portfolio holdings in unit trusts	**218,083**	**4,937**	**371**	**223,391**
Debt securities	**55,579**	**115,141**	**654**	**171,374**
Other investments (including derivative assets)	**87**	**5,912**	**4,424**	**10,423**
Derivative liabilities	**(68)**	**(2,175)**	**(512)**	**(2,755)**
Total financial investments, net of derivative liabilities	**273,681**	**123,815**	**9,774**	**407,270**
Investment contract liabilities without discretionary participation features held at fair value	**-**	**(17,397)**	**-**	**(17,397)**
Borrowings attributable to with-profits operations	**-**	**-**	**(1,887)**	**(1,887)**
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	**(4,836)**	**(3,640)**	**(413)**	**(8,889)**
Other financial liabilities held at fair value	**-**	**-**	**(3,031)**	**(3,031)**
Total financial instruments at fair value	**268,845**	**102,778**	**4,443**	**376,066**
Percentage of total	**72%**	**27%**	**1%**	**100%**

	31 Dec 2016 £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				
Loans	-	-	27	27
Equity securities and portfolio holdings in unit trusts	45,181	3,669	690	49,540
Debt securities	26,227	43,880	690	70,797
Other investments (including derivative assets)	58	3,357	3,443	6,858
Derivative liabilities	(51)	(1,025)	-	(1,076)
Total financial investments, net of derivative liabilities	71,415	49,881	4,850	126,146
Percentage of total	56%	40%	4%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	146,637	374	22	147,033
Debt securities	5,136	4,462	-	9,598
Other investments (including derivative assets)	6	8	5	19
Derivative liabilities	(4)	(24)	-	(28)
Total financial investments, net of derivative liabilities	151,775	4,820	27	156,622
Percentage of total	97%	3%	0%	100%
Non-linked shareholder-backed				
Loans	-	276	2,672	2,948
Equity securities and portfolio holdings in unit trusts	1,966	3	10	1,979
Debt securities	21,896	67,915	252	90,063
Other investments (including derivative assets)	-	1,492	1,032	2,524
Derivative liabilities	(9)	(1,623)	(516)	(2,148)
Total financial investments, net of derivative liabilities	23,853	68,063	3,450	95,366
Percentage of total	25%	71%	4%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans	-	276	2,699	2,975
Equity securities and portfolio holdings in unit trusts	193,784	4,046	722	198,552
Debt securities	53,259	116,257	942	170,458
Other investments (including derivative assets)	64	4,857	4,480	9,401
Derivative liabilities	(64)	(2,672)	(516)	(3,252)
Total financial investments, net of derivative liabilities	247,043	122,764	8,327	378,134
Investment contract liabilities without discretionary participation features held at fair value	-	(16,425)	-	(16,425)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(4,217)	(3,587)	(883)	(8,687)
Other financial liabilities held at fair value	-	(385)	(2,851)	(3,236)
Total financial instruments at fair value	242,826	102,367	4,593	349,786
Percentage of total	70%	29%	1%	100%

All assets and liabilities held at fair value are classified as fair value through profit or loss, except for £35,293 million (2016: £40,645 million) of debt securities classified as available-for-sale.

The Korea life business was classified as held for sale in 2016, with the sale completed in May 2017. The assets and liabilities held for sale on the consolidated statement of financial position at 31 December 2016 in respect of Korea life business included a net financial instruments balance of £3,200 million, primarily for equity securities and debt securities. Of this amount, £2,763 million was classified as level 1 and £437 million as level 2.

Investment properties at fair value

	31 December £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	
2017	**-**	**-**	**16,497**	**16,497**
2016	-	-	14,646	14,646

(c) Valuation approach for level 2 fair valued assets and liabilities

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 service 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 below in this note with the objective of arriving at a fair value measurement that 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 £115,141 million at 31 December 2017 (2016: £116,257 million), £13,910 million are valued internally (2016: £12,708 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 assets and liabilities

Valuation approach for level 3 fair valued assets and liabilities
Financial instruments at fair value
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 that 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 a significant volume 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 31 December 2017, the Group held £4,443 million (2016: £4,593 million) of net financial instruments at fair value within level 3. This represents 1 per cent (2016: 1 per cent) of the total fair valued financial assets net of fair valued financial liabilities.

The net financial instruments at fair value within level 3 at 31 December 2017 include £1,983 million of loans and a corresponding £1,887 million of borrowings held by a subsidiary of the Group's UK with-profits fund, attaching to a portfolio of buy-to-let mortgages and other loans financed largely by external third-party (non-recourse) borrowings (see note C3.3(c) for further details). The Group's exposure is limited to the investment held by the UK with-profits fund, rather than to the individual loans and borrowings themselves. The fair value movements of these loans and borrowings have no effect on shareholders' profit and equity. The most significant non observable inputs to the mortgage fair value are the level of future defaults and prepayments by the mortgage holders.

Also included within these amounts are loans of £2,512 million at 31 December 2017 (2016: £2,672 million), measured as the loan outstanding balance, plus accrued investment income, attached to REALIC and held to back the liabilities for funds withheld under reinsurance arrangements. The funds withheld liability of £2,664 million at 31 December 2017 (2016: £2,851 million) is 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 £(152) million (2016: £(179) million), the level 3 fair valued financial assets net of financial liabilities are £4,595 million (2016: £4,772 million). Of this amount, a net asset of £117 million (2016: net asset of £72 million) is internally valued, representing less than 0.1 per cent of the total fair valued financial assets net of financial liabilities (2016: less than 0.1

per cent). Internal valuations are inherently more subjective than external valuations. Included within these internally valued net asset/liability are:

(a) Debt securities of £500 million (2016: £422 million), which are 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).
(b) Private equity and venture investments in both debt and equity securities of £217 million (2016: £956 million) which are valued internally using discounted cash flows based on management information available for these investments. The significant unobservable inputs include the determination of expected future cash flows on the investments being valued, determination of the probability of counterparty default and prepayments and the selection of appropriate discount rates. The valuation is performed in accordance with International Private Equity and Venture Capital Association Valuation guidelines. These investments were principally held by consolidated investment funds that are managed on behalf of third parties.
(c) Equity release mortgage loans of £366 million (2016: £276 million classified as level 2) which are valued internally using the discounted cash flow models. The inputs that are significant to the valuation of these investments are primarily the economic assumptions, being the discount rate (risk-free rate plus a liquidity premium) and property values. See below for the explanation of the transfer of these investments from level 2 into level 3 during the year.
(d) Liabilities of £(403) million (2016: £(883) 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.
(e) Derivative liabilities of £(512) million (2016: £(516) million) which are valued internally using the discounted cash flow method in line with standard market practices but are subject to independent assessment against external counterparties' valuations.
(f) Other sundry individual financial investments of £81 million (2016: £93 million).

Of the internally valued net asset referred to above of £117 million (2016: net asset of £72 million):

(a) A net asset of £67 million (2016: £315 million) is 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.
(b) A net liability of £(184) million (2016: £(243) million) is 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 decreased by 10 per cent, the change in valuation would be £18 million (2016: £24 million), which would reduce shareholders' equity by this amount before tax. All this amount passes through the income statement substantially as part of short-term fluctuations in investment returns outside of operating profit.

Other assets at fair value – investment properties

The investment properties of the Group are principally held by the UK and Europe insurance operations that are externally valued by professionally qualified external valuers using the Royal Institution of Chartered Surveyors (RICS) valuation standards. An 'income capitalisation' technique is predominantly applied for these properties. This technique calculates the value through the yield and rental value depending on factors such as the lease length, building quality, covenant and location. The variables used are compared to recent transactions with similar features to those of the Group's investment properties. As the comparisons are not with properties that are virtually identical to the Group's investment properties, adjustments are made by the valuers where appropriate to the variables used. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of the properties.

(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 the year, the transfers between levels within the Group's portfolio were primarily transfers from level 1 to level 2 of £1,389 million and transfers from level 2 to level 1 of £411 million. These transfers which relate to equity securities and debt securities arose to reflect the change in the observed valuation inputs and in certain cases, the change in the level of trading activities of the securities.

In addition, in 2017, the transfers into level 3 were a net liability of £80 million and the transfers out of level 3 were £92 million. The transfers into level 3 include a transfer from level 2 of a net liability of £83 million relating to the equity release mortgage loans of £302 million and a corresponding liability of £385 million held by the UK insurance operations that are carried at fair value through profit or loss. During 2017, the assumptions used within the discounted cash flow model used to value these loans were refined to reflect developing market practice, including consideration of the Prudential Regulation Authority's industry-wide review in this area and resulting guidance. This refinement incorporates inputs relevant to determining the discount rate that are not market observable. As a result, the loans were reclassified as level 3. There was no material difference in the fair value of these loans recognised in 2017, arising from this change in the valuation model.

(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. In addition the Group has minimum standards for independent price verification to ensure valuation accuracy is regularly independently verified. Adherence to this policy is monitored across the business units.

C3.2 Debt securities

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

With the exception of certain debt securities for US insurance operations classified as 'available-for-sale' under IAS 39 as disclosed in notes C3.2 (b) to (d) below, the Group's debt securities are carried at fair value through profit or loss.

(a) Credit rating

Debt securities are analysed below according to external credit ratings issued, with equivalent ratings issued by different ratings agencies grouped together. Standard and Poor's ratings have been used where available, if this isn't the case Moody's and then Fitch have been used as alternatives. In the table below, AAA is the highest possible rating. Investment grade financial assets are classified within the range of AAA to BBB- ratings. Financial assets which fall outside this range are classified as below BBB-. Debt securities with no external credit rating are classified as 'Other'.

	2017 £m						
	AAA	**AA+ to AA-**	**A+ to A-**	**BBB+ to BBB-**	**Below BBB-**	**Other**	**Total**
Asia							
With-profits	**2,504**	**10,641**	**3,846**	**3,234**	**1,810**	**2,397**	**24,432**
Unit-linked	**528**	**103**	**510**	**1,429**	**372**	**565**	**3,507**
Non-linked shareholder-backed	**990**	**2,925**	**3,226**	**2,970**	**1,879**	**1,053**	**13,043**
US							
Non-linked shareholder-backed	**368**	**6,352**	**9,578**	**12,311**	**1,000**	**5,769**	**35,378**
UK and Europe							
With-profits	**6,492**	**9,378**	**11,666**	**12,856**	**2,877**	**7,392**	**50,661**
Unit-linked	**670**	**2,732**	**1,308**	**1,793**	**91**	**117**	**6,711**
Non-linked shareholder-backed	**5,118**	**11,005**	**9,625**	**3,267**	**258**	**6,062**	**35,335**
Other operations	**742**	**1,264**	**182**	**67**	**36**	**16**	**2,307**
Total debt securities	**17,412**	**44,400**	**39,941**	**37,927**	**8,323**	**23,371**	**171,374**

	2016 £m						
	AAA	**AA+ to AA-**	**A+ to A-**	**BBB+ to BBB-**	**Below BBB-**	**Other**	**Total**
Asia							
With-profits	3,183	8,522	3,560	2,996	1,887	1,713	21,861
Unit-linked	448	112	525	1,321	494	421	3,321
Non-linked shareholder-backed	1,082	2,435	2,864	2,388	1,680	915	11,364
US							
Non-linked shareholder-backed	445	7,932	10,609	13,950	1,009	6,800	40,745
UK and Europe							
With-profits	5,740	9,746	10,679	12,798	3,289	6,684	48,936
Unit-linked	461	2,660	1,158	1,699	212	87	6,277
Non-linked shareholder-backed	4,238	10,371	10,558	4,515	397	5,504	35,583
Other operations	830	1,190	242	97	10	2	2,371
Total debt securities	16,427	42,968	40,195	39,764	8,978	22,126	170,458

Securities with credit ratings classified as 'Other' can be further analysed as follows:

	2017 £m	**2016 £m**
Asia - non-linked shareholder-backed		
Internally rated		
Government bonds	**25**	63
Corporate bonds – rated as investment grade by local external ratings agencies	**959**	757
Other	**69**	95
Total Asia non-linked shareholder-backed	**1,053**	915

	£m			
US	**Mortgage -backed securities**	**Other securities**	**2017 Total**	**2016 Total**
Implicit ratings of other US debt securities based on NAIC* valuations (see below)				
NAIC 1	**1,843**	**2,075**	**3,918**	4,759
NAIC 2	**22**	**1,772**	**1,794**	1,909
NAIC 3-6	**3**	**54**	**57**	132
Total US	**1,868**	**3,901**	**5,769**	6,800

* 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.

	2017 £m	2016 £m
UK and Europe		
Internal ratings or unrated		
AAA to A-	**7,994**	6,939
BBB to B-	**3,141**	3,257
Below B- or unrated	**2,436**	2,079
Total UK and Europe	**13,571**	12,275

In addition to the debt securities shown above, the assets held for sale on the consolidated statement of financial position at 31 December 2016 in respect of Korea life business included a debt securities balance of £652 million.

(b) Additional analysis of US insurance operations debt securities

	2017 £m	2016 £m
Corporate and government security and commercial loans:		
Government	**4,835**	5,856
Publicly traded and SEC Rule 144A securities*	**22,849**	25,992
Non-SEC Rule 144A securities	**4,468**	4,576
Asset backed securities (see note (e))	**3,226**	4,321
Total US debt securities†	**35,378**	40,745

* 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:

	2017 £m	2016 £m
Available-for-sale	**35,293**	40,645
Fair value through profit or loss:		
Securities held to back liabilities for funds withheld under reinsurance arrangement	**85**	100
	35,378	40,745

Realised gains and losses, including impairments, recorded in the income statement are as shown in note B1.2 of this report.

(c) Movements in unrealised gains and losses on Jackson available-for-sale securities

The movement in the statement of financial position value for debt securities classified as available-for-sale was from a net unrealised gain of £676 million to a net unrealised gain of £1,205 million as analysed in the table below.

	2017	Foreign exchange translation	Changes in unrealised appreciation**	2016
		Reflected as part of movement in other comprehensive income		
	£m	£m	£m	£m
Assets fair valued at below book value				
Book value*	**6,325**			14,617
Unrealised gain (loss)	**(106)**	**33**	**536**	(675)
Fair value (as included in statement of financial position)	**6,219**			13,942
Assets fair valued at or above book value				
Book value*	**27,763**			25,352
Unrealised gain (loss)	**1,311**	**(121)**	**81**	1,351
Fair value (as included in statement of financial position)	**29,074**			26,703
Total				
Book value*	**34,088**			39,969
Net unrealised gain (loss)	**1,205**	**(88)**	**617**	676
Fair value (as included in the footnote above in the overview table and the statement of financial position)	**35,293**			40,645

* Book value represents cost/amortised cost of the debt securities.

**Translated at the average rate of US$1.2889: £1.00.

(d) US debt securities classified as available-for-sale in an unrealised loss position

(i) 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:

	2017 £m		2016 £m	
	Fair value	**Unrealised loss**	**Fair value**	**Unrealised loss**
Between 90% and 100%	**6,170**	**(95)**	12,326	(405)
Between 80% and 90%	**36**	**(6)**	1,598	(259)
Below 80%:				
Residential mortgage-backed securities - sub-prime	**-**	**-**	-	-
Commercial mortgage-backed securities	**-**	**-**	8	(3)
Other asset-backed securities	**10**	**(4)**	9	(8)
Government bonds	**-**	**-**	-	-
Corporates	**3**	**(1)**	1	
	13	**(5)**	18	(11)
Total	**6,219**	**(106)**	13,942	(675)

(ii) Unrealised losses by maturity of security

	2017 £m	2016 £m
1 year to 5 years	**(7)**	(7)
5 years to 10 years	**(41)**	(118)
More than 10 years	**(39)**	(510)
Mortgage-backed and other debt securities	**(19)**	(40)
Total	**(106)**	(675)

(iii) 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:

	2017 £m			2016 £m		
	Non-investment grade	**Investment grade**	**Total**	**Non-investment grade**	**Investment grade**	**Total**
Less than 6 months	**(4)**	**(31)**	**(35)**	(3)	(599)	(602)
6 months to 1 year	**(1)**	**(4)**	**(5)**	-	(2)	(2)
1 year to 2 years	**-**	**(49)**	**(49)**	(4)	(27)	(31)
2 years to 3 years	**(1)**	**(6)**	**(7)**	(2)	(1)	(3)
More than 3 years	**-**	**(10)**	**(10)**	(2)	(35)	(37)
Total	**(6)**	**(100)**	**(106)**	(11)	(664)	(675)

Further, the following table shows the age analysis as at 31 December, of the securities whose fair values were below 80 per cent of the book value:

	2017 £m		2016 £m	
Age analysis	Fair value	Unrealised loss	Fair value	Unrealised loss
Less than 3 months	**2**	**-**	1	-
3 months to 6 months	**1**	**(1)**	-	-
More than 6 months	**10**	**(4)**	17	(11)
	13	**(5)**	18	(11)

(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 31 December are as follows:

	2017 £m	2016 £m
Shareholder-backed operations:		
Asia operations note (i)	**118**	130
US operations note (ii)	**3,226**	4,321
UK and Europe operations (2017: 34% AAA, 16% AA) note (iii)	**1,070**	1,464
Other operations note (iv)	**589**	771
	5,003	6,686
With-profits operations:		
Asia operations note (i)	**233**	357
UK and Europe operations (2017: 58% AAA, 10% AA) note (iii)	**5,658**	5,177
	5,891	5,534
Total	**10,894**	12,220

Notes

(i) Asia operations

The Asia operations' exposure to asset-backed securities is primarily held by the with-profits operations. Of the £233 million, 98 per cent (2016: 99 per cent) are investment grade.

(ii) US operations

US operations' exposure to asset-backed securities at 31 December comprises:

	2017 £m	2016 £m
RMBS		
Sub-prime (2017: 2% AAA, 4% AA, 3% A)	**112**	180
Alt-A (2017: 3% AAA, 3% A)	**126**	177
Prime including agency (2017: 70% AA, 4% A)	**440**	675
CMBS (2017: 82% AAA, 15% AA, 1% A)	**1,579**	2,234
CDO funds (2017: 49% AA, 31% A), including £nil exposure to sub-prime	**28**	50
Other ABS (2017: 21% AAA, 14% AA, 50% A), including £96 million exposure to sub-prime	**941**	1,005
Total	**3,226**	4,321

(iii) UK and Europe operations

The majority of holdings of the shareholder-backed business are UK securities and relate to PAC's annuity business. Of the holdings of the with-profits operations, £1,913 million (2016: £1,623 million) relates to exposure to the US markets with the remaining exposure being primarily to the UK market.

(iv) Other operations

Other operations' exposure to asset-backed securities is held by Prudential Capital with no sub-prime exposure. Of the £589 million, 96 per cent (2016: 95 per cent) are graded AAA.

(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 31 December are analysed as follows:

Exposure to sovereign debts

	2017 £m		2016 £m	
	Shareholder-backed business	**With-profits funds**	**Shareholder-backed business**	**With-profits funds**
Italy	**58**	**63**	56	61
Spain	**34**	**18**	33	18
France	**23**	**38**	22	-
Germany*	**693**	**301**	573	329
Other Eurozone	**82**	**31**	83	33
Total Eurozone	**890**	**451**	767	441
United Kingdom	**5,918**	**3,287**	5,510	2,868
United States**	**5,078**	**10,156**	6,861	9,008
Other, predominantly Asia	**4,638**	**2,143**	3,979	2,079
Total	**16,524**	**16,037**	17,117	14,396

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

Exposure to bank debt securities

	2017 £m							
	Senior debt			Subordinated debt				
Shareholder-backed business	**Covered**	**Senior**	**Total senior debt**	**Tier 1**	**Tier 2**	**Total subordinated debt**	**2017 Total £m**	**2016 Total £m**
Italy	**-**	**-**	**-**	**-**	**-**	**-**	**-**	32
Spain	**42**	**26**	**68**	**-**	**-**	**-**	**68**	170
France	**28**	**41**	**69**	**10**	**7**	**17**	**86**	166
Germany	**30**	**-**	**30**	**-**	**87**	**87**	**117**	124
Netherlands	**-**	**65**	**65**	**-**	**6**	**6**	**71**	50
Other Eurozone	**15**	**-**	**15**	**-**	**-**	**-**	**15**	19
Total Eurozone	**115**	**132**	**247**	**10**	**100**	**110**	**357**	561
United Kingdom	**695**	**374**	**1,069**	**5**	**308**	**313**	**1,382**	1,174
United States	**-**	**2,457**	**2,457**	**1**	**161**	**162**	**2,619**	2,684
Other, including Asia	**17**	**652**	**669**	**93**	**401**	**494**	**1,163**	1,018
Total	**827**	**3,615**	**4,442**	**109**	**970**	**1,079**	**5,521**	5,437
With-profits funds								
Italy	**-**	**31**	**31**	**-**	**-**	**-**	**31**	62
Spain	**-**	**16**	**16**	**-**	**-**	**-**	**16**	213
France	**9**	**213**	**222**	**-**	**64**	**64**	**286**	213
Germany	**120**	**24**	**144**	**-**	**36**	**36**	**180**	114
Netherlands	**-**	**188**	**188**	**5**	**6**	**11**	**199**	202
Other Eurozone	**-**	**27**	**27**	**-**	**-**	**-**	**27**	31
Total Eurozone	**129**	**499**	**628**	**5**	**106**	**111**	**739**	835
United Kingdom	**859**	**592**	**1,451**	**3**	**484**	**487**	**1,938**	1,396
United States	**-**	**2,205**	**2,205**	**17**	**296**	**313**	**2,518**	2,229
Other, including Asia	**532**	**1,256**	**1,788**	**290**	**453**	**743**	**2,531**	1,992
Total	**1,520**	**4,552**	**6,072**	**315**	**1,339**	**1,654**	**7,726**	6,452

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

C3.3 Loans portfolio

(a) Overview of 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 or loss of the UK and Europe insurance operations as this loan portfolio is managed and evaluated on a fair value basis; and
- Certain policy loans of the US insurance operations that are held to back liabilities for funds withheld under reinsurance arrangements and are also accounted on a fair value basis.

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

	2017 £m				2016 £m			
	Mortgage loans*	Policy loans**	Other loans†	Total	Mortgage loans*	Policy loans**	Other loans†	Total
Asia								
With-profits	**-**	**613**	**112**	**725**	-	577	113	690
Non-linked shareholder-backed	**177**	**216**	**199**	**592**	179	226	208	613
US								
Non-linked shareholder-backed	**6,236**	**3,394**	**-**	**9,630**	6,055	3,680	-	9,735
UK and Europe								
With-profits	**2,441**	**4**	**1,823**	**4,268**	668	6	1,218	1,892
Non-linked shareholder-backed	**1,681**	**-**	**37**	**1,718**	1,642	-	38	1,680
Other operations	**-**	**-**	**109**	**109**	-	-	563	563
Total loans securities	**10,535**	**4,227**	**2,280**	**17,042**	8,544	4,489	2,140	15,173

* All mortgage loans are secured by properties.

** In the US £2,512 million (2016: £2,672 million) policy loans are backing liabilities for funds withheld under reinsurance arrangements and are accounted for at fair value through profit or loss. All other policy loans are accounted for at amortised cost, less any impairment.

† Other loans held in UK with-profits funds are commercial loans and comprise mainly syndicated loans. The majority of other loans in shareholder-backed business in Asia are commercial loans held by the Malaysia operation and which are all investment graded by two local rating agencies.

(b) Additional information on US mortgage loans

In the US, mortgage loans are all commercial mortgage loans that are secured by the following property types: industrial, multi-family residential, suburban office, retail or hotel. The US insurance operations' commercial mortgage loan portfolio does not include any single-family residential mortgage loans and is therefore not exposed to the same risk of defaults associated with residential sub-prime mortgage loans. The average loan size is £12.6 million (2016: £12.4 million). The portfolio has a current estimated average loan to value of 55 per cent (2016: 59 per cent).

At 31 December 2017, Jackson had no mortgage loans where the contractual terms of the agreements had been restructured (2016: none).

(c) Additional information on UK mortgage loans

During 2017, the UK with-profits fund invested in an entity that holds a portfolio of buy-to-let mortgage loans. The vehicle financed its acquisitions through the issue of debt instruments, largely to external parties, securitised upon the loans acquired. These third-party borrowings have no recourse to any other assets of the Group and the Group's exposure is limited to the amount invested by the UK with-profits fund.

By carrying value, 99.98 per cent of the £1,681 million (31 December 2016: 96.29 per cent of £1,642 million) mortgage loans held by the UK shareholder-backed business relates to lifetime (equity release) mortgage business which has an average loan to property value of 31 per cent (31 December 2016: 30 per cent).

(d) Loans held by other operations

These 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:

	2017 £m	2016 £m
Loans and receivables internal ratings:		
AA+ to AA-	**14**	29
A+ to A-	**-**	100
BBB+ to BBB-	**-**	248
BB+ to BB-	**95**	185
B and other	**-**	1
Total	**109**	563

C4 Policyholder liabilities and unallocated surplus

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 and duration of liabilities

C4.1(a) Group overview

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

	Insurance operations £m			
	Asia note C4.1(b)	**US** note C4.1(c)	**UK and Europe** note C4.1(d)	**Total**
At 1 January 2016	48,778	138,913	152,893	340,584
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position	41,255	138,913	142,350	322,518
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	2,553	-	10,543	13,096
- Group's share of policyholder liabilities of joint ventures and associate[§]	4,970	-	-	4,970
Reclassification of Korea life business as held for sale*	(2,812)	-	-	(2,812)
Net flows:				
Premiums	9,639	14,766	11,129	35,534
Surrenders	(2,299)	(7,872)	(6,821)	(16,992)
Maturities/deaths	(1,558)	(1,696)	(6,835)	(10,089)
Net flows	5,782	5,198	(2,527)	8,453
Shareholders' transfers post-tax	(44)	-	(215)	(259)
Investment-related items and other movements	2,005	5,690	18,626	26,321
Foreign exchange translation differences	9,075	27,825	527	37,427
As at 31 December 2016/1 January 2017	**62,784**	**177,626**	**169,304**	**409,714**
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position[¶]	**53,716**	**177,626**	**157,654**	**388,996**
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	**2,667**	**-**	**11,650**	**14,317**
- Group's share of policyholder liabilities of joint ventures and associate[§]	**6,401**	**-**	**-**	**6,401**
Net flows:				
Premiums	**11,863**	**15,219**	**14,810**	**41,892**
Surrenders	**(3,079)**	**(10,017)**	**(6,939)**	**(20,035)**
Maturities/deaths	**(1,909)**	**(2,065)**	**(7,135)**	**(11,109)**
Net flows	**6,875**	**3,137**	**736**	**10,748**
Shareholders' transfers post-tax	**(54)**	**-**	**(233)**	**(287)**
Investment-related items and other movements	**8,182**	**16,251**	**11,146**	**35,579**
Foreign exchange translation differences	**(3,948)**	**(16,290)**	**113**	**(20,125)**
At 31 December 2017	**73,839**	**180,724**	**181,066**	**435,629**
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position[¶] *(excludes £32 million classified as unallocated to a segment)*	**62,898**	**180,724**	**167,589**	**411,211**
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	**3,474**	**-**	**13,477**	**16,951**
- Group's share of policyholder liabilities of joint ventures and associate[§]	**7,467**	**-**	**-**	**7,467**
Average policyholder liability balances[†]				
2017	**65,241**	**179,175**	**162,622**	**407,038**
2016	51,765	158,270	150,003	360,038

* The reclassification of Korea life business as held for sale reflects the value of policyholder liabilities held at 1 January 2016. No other amounts are shown within the 2016 analysis above in respect of Korea.

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

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

¶ The policyholder liabilities of the Asia insurance operations of £62,898 million (2016: £53,716 million), shown in the table above, is after deducting the intra-group reinsurance liabilities ceded by the UK and Europe insurance operations of £1,235 million (2016: £1,302 million) to the Hong Kong with-profits business. Including this amount total Asia policyholder liabilities are £64,133 million (2016: £55,018 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 year but exclude liabilities that have not been allocated to a reporting segment. 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 will exclude any deductions for fees/charges. Claims (surrenders, maturities and deaths) represent the policyholder liabilities provision released rather than the claim amount paid to the policyholder.

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

	Shareholder-backed business £m			
	Asia	**US**	**UK and Europe**	**Total**
At 1 January 2016	27,844	138,913	52,824	219,581
Reclassification of Korea life business as held for sale*	(2,812)	-	-	(2,812)
Net flows:				
Premiums	4,749	14,766	1,842	21,357
Surrenders	(1,931)	(7,872)	(2,967)	(12,770)
Maturities/deaths	(732)	(1,696)	(2,521)	(4,949)
Net flows[note (a)]	2,086	5,198	(3,646)	3,638
Investment-related items and other movements	1,116	5,690	6,980	13,786
Foreign exchange translation differences	4,617	27,825	-	32,442
At 31 December 2016/1 January 2017	32,851	177,626	56,158	266,635
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position	26,450	177,626	56,158	260,234
- Group's share of policyholder liabilities relating to joint ventures and associate	6,401	-	-	6,401
Net flows:				
Premiums	**6,064**	**15,219**	**2,283**	**23,566**
Surrenders	**(2,755)**	**(10,017)**	**(2,433)**	**(15,205)**
Maturities/deaths	**(1,008)**	**(2,065)**	**(2,571)**	**(5,644)**
Net flows[note (a)]	**2,301**	**3,137**	**(2,721)**	**2,717**
Investment-related items and other movements	**3,797**	**16,251**	**2,930**	**22,978**
Foreign exchange translation differences	**(1,547)**	**(16,290)**	**-**	**(17,837)**
At 31 December 2017	**37,402**	**180,724**	**56,367**	**274,493**
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position (excludes £32 million classified as unallocated to a segment)	**29,935**	**180,724**	**56,367**	**267,026**
- Group's share of policyholder liabilities relating to joint ventures and associate	**7,467**	**-**	**-**	**7,467**

* The reclassification of Korea life business as held for sale reflects the value of policyholder liabilities held at 1 January 2016. No other amounts are shown within the 2016 analysis above in respect of Korea.

Note

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

C4.1(b) Asia 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 Asia insurance operations from the beginning of the year to the end of the year is as follows:

	With-profits business £m	Unit-linked liabilities £m	Other business £m	Total £m
At 1 January 2016	20,934	15,966	11,878	48,778
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position	18,381	13,355	9,519	41,255
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	2,553	-	-	2,553
- Group's share of policyholder liabilities relating to joint ventures and associate‡	-	2,611	2,359	4,970
Reclassification of Korea life business as held for sale*	-	(2,187)	(625)	(2,812)
Premiums				
New business	1,701	921	767	3,389
In-force	3,189	1,447	1,614	6,250
	4,890	2,368	2,381	9,639
Surrenders note (c)	(368)	(1,641)	(290)	(2,299)
Maturities/deaths	(826)	(78)	(654)	(1,558)
Net flows note (b)	3,696	649	1,437	5,782
Shareholders' transfers post-tax	(44)	-	-	(44)
Investment-related items and other movements	889	621	495	2,005
Foreign exchange translation differences note (a)	4,458	2,458	2,159	9,075
At 31 December 2016/1 January 2017	**29,933**	**17,507**	**15,344**	**62,784**
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position	**27,266**	**14,289**	**12,161**	**53,716**
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	**2,667**	**-**	**-**	**2,667**
- Group's share of policyholder liabilities relating to joint ventures and associate‡	**-**	**3,218**	**3,183**	**6,401**
Premiums				
New business	**1,143**	**1,298**	**999**	**3,440**
In-force	**4,656**	**1,637**	**2,130**	**8,423**
	5,799	**2,935**	**3,129**	**11,863**
Surrenders note (c)	**(324)**	**(2,288)**	**(467)**	**(3,079)**
Maturities/deaths	**(901)**	**(150)**	**(858)**	**(1,909)**
Net flows note (b)	**4,574**	**497**	**1,804**	**6,875**
Shareholders' transfers post-tax	**(54)**	**-**	**-**	**(54)**
Investment-related items and other movements note (d)	**4,385**	**2,830**	**967**	**8,182**
Foreign exchange translation differences note (a)	**(2,401)**	**(807)**	**(740)**	**(3,948)**
At 31 December 2017 note (b)	**36,437**	**20,027**	**17,375**	**73,839**
Comprising:				
- Policyholder liabilities on the consolidated statement of financial position§	**32,963**	**16,263**	**13,672**	**62,898**
- Unallocated surplus of with-profits funds on the consolidated statement of financial position	**3,474**	**-**	**-**	**3,474**
- Group's share of policyholder liabilities relating to joint ventures and associate‡	**-**	**3,764**	**3,703**	**7,467**
Average policyholder liability balances†				
2017	**30,115**	**18,767**	**16,359**	**65,241**
2016	22,823	15,643	13,299	51,765

* The reclassification of Korea life business as held for sale reflects the value of policyholder liabilities held at 1 January 2016. No other amounts are shown within the 2016 analysis above in respect of Korea.

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

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

§ The policyholder liabilities of the with-profits business of £32,963 million, shown in the table above, is after deducting the intra-group reinsurance liabilities ceded by UK and Europe insurance operations of £1,235 million to the Hong Kong with-profits business (2016: £1,302 million). Including this amount the Asia with-profits policyholder liabilities are £34,198 million.

Notes

(a) Movements in the year have been translated at the average exchange rates for the year. The closing balance has been translated at the closing spot rates as at the end of the year. Differences upon retranslation are included in foreign exchange translation differences.

(b) Net flows have increased by £1,093 million to £6,875 million in 2017 predominantly reflecting continued growth of the in-force book and increased flows from new business.

(c) Investment-related items and other movements for 2017 principally represent equity market gains and falls in bond yields during the year, in a number of business units with the greatest impact being on with-profits and unit-linked business.

(ii) Duration of liabilities

The table below shows the carrying value of policyholder liabilities and the maturity profile of the cash flows on a discounted basis for 2017 and 2016, taking account of expected future premiums and investment returns:

	2017 £m	**2016 £m**
Policyholder liabilities	**62,898**	53,716
Expected maturity:	**%**	%
0 to 5 years	**21**	23
5 to 10 years	**19**	20
10 to 15 years	**16**	16
15 to 20 years	**12**	11
20 to 25 years	**10**	9
Over 25 years	**22**	21

C4.1(c) US insurance operations

(i) Analysis of movements in policyholder liabilities

A reconciliation of the total policyholder liabilities of US insurance operations from the beginning of the year to the end of the year is as follows:

US insurance operations

	Variable annuity separate account liabilities £m	Fixed annuity, GIC and other business £m	Total £m
At 1 January 2016	91,022	47,891	138,913
Premiums	10,232	4,534	14,766
Surrenders	(5,036)	(2,836)	(7,872)
Maturities/deaths	(803)	(893)	(1,696)
Net flows note (b)	4,393	805	5,198
Transfers from general to separate account	1,164	(1,164)	-
Investment-related items and other movements	5,246	444	5,690
Foreign exchange translation differences note (a)	18,586	9,239	27,825
At 31 December 2016/1 January 2017	**120,411**	**57,215**	**177,626**
Premiums	**11,529**	**3,690**	**15,219**
Surrenders	**(6,997)**	**(3,020)**	**(10,017)**
Maturities/deaths	**(1,026)**	**(1,039)**	**(2,065)**
Net flows note (b)	**3,506**	**(369)**	**3,137**
Transfers from general to separate account	**2,096**	**(2,096)**	**-**
Investment-related items and other movements note (c)	**15,956**	**295**	**16,251**
Foreign exchange translation differences note (a)	**(11,441)**	**(4,849)**	**(16,290)**
At 31 December 2017	**130,528**	**50,196**	**180,724**
Average policyholder liability balances*			
2017	**125,469**	**53,706**	**179,175**
2016	105,717	52,553	158,270

* Averages have been based on opening and closing balances.

Notes

(a) Movements in the year have been translated at an average rate of US$1.29/£1.00 (2016: US$1.35/£1.00). The closing balances have been translated at closing rate of US$1.35/£1.00 (2016: US$1.24/£1.00). Differences upon retranslation are included in foreign exchange translation differences.

(b) Net flows were £3,137 million in 2017, reflecting continued strong inflows into the variable annuity business.

(c) Positive investment-related items and other movements in variable annuity separate account liabilities of £15,956 million for 2017 primarily reflects the increases in equities and bond values during the year. Fixed annuity, GIC and other business investment and other movements of £295 million primarily reflect the increase in guarantee reserve in the year.

(ii) Duration of liabilities

The table below shows the carrying value of policyholder liabilities and maturity profile of the cash flows on a discounted basis for 2017 and 2016:

	2017			2016		
	Fixed annuity and other business (including GICs and similar contracts) £m	Variable annuity separate account liabilities £m	Total £m	Fixed annuity and other business (including GICs and similar contracts) £m	Variable annuity separate account liabilities £m	Total £m
Policyholder liabilities	**50,196**	**130,528**	**180,724**	57,215	120,411	177,626
	%	%	%	%	%	%
Expected maturity:						
0 to 5 years	**50**	**42**	**44**	49	43	45
5 to 10 years	**25**	**29**	**28**	26	29	28
10 to 15 years	**12**	**15**	**14**	11	14	14
15 to 20 years	**7**	**8**	**8**	7	8	7
20 to 25 years	**3**	**4**	**4**	3	4	3
Over 25 years	**3**	**2**	**2**	4	2	3

C4.1(d) UK and Europe 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 and Europe insurance operations from the beginning of the year to the end of the year is as follows:

		Shareholder-backed funds and subsidiaries		
	With-profits sub-funds** £m	Unit-linked liabilities £m	Annuity and other long-term business £m	Total £m
At 1 January 2016	100,069	21,442	31,382	152,893
Comprising:				
- Policyholder liabilities	89,526	21,442	31,382	142,350
- Unallocated surplus of with-profits funds	10,543	-	-	10,543
Premiums	9,287	1,227	615	11,129
Surrenders	(3,854)	(2,889)	(78)	(6,821)
Maturities/deaths	(4,314)	(583)	(1,938)	(6,835)
Net flows note (a)	1,119	(2,245)	(1,401)	(2,527)
Shareholders' transfers post-tax	(215)	-	-	(215)
Switches	(152)	152	-	-
Investment-related items and other movements	11,798	2,770	4,058	18,626
Foreign exchange translation differences	527	-	-	527
At 31 December 2016/1 January 2017	**113,146**	**22,119**	**34,039**	**169,304**
Comprising:				
- Policyholder liabilities	**101,496**	**22,119**	**34,039**	**157,654**
- Unallocated surplus of with-profits funds	**11,650**	**-**	**-**	**11,650**
Premiums	**12,527**	**1,923**	**360**	**14,810**
Surrenders	**(4,506)**	**(2,342)**	**(91)**	**(6,939)**
Maturities/deaths	**(4,564)**	**(612)**	**(1,959)**	**(7,135)**
Net flows note (a)	**3,457**	**(1,031)**	**(1,690)**	**736**
Shareholders' transfers post-tax	**(233)**	**-**	**-**	**(233)**
Switches	**(192)**	**192**	**-**	**-**
Investment-related items and other movements note (b)	**8,408**	**1,865**	**873**	**11,146**
Foreign exchange translation differences	**113**	**-**	**-**	**113**
At 31 December 2017	**124,699**	**23,145**	**33,222**	**181,066**
Comprising:				
- Policyholder liabilities	**111,222**	**23,145**	**33,222**	**167,589**
- Unallocated surplus of with-profits funds	**13,477**	**-**	**-**	**13,477**
Average policyholder liability balances*				
2017	**106,359**	**22,632**	**33,631**	**162,622**
2016	95,511	21,781	32,711	150,003

*Averages have been based on opening and closing balances and exclude unallocated surplus of with-profits funds.
**Includes the Scottish Amicable Insurance Fund.

Notes

(a) Net flows improved from negative £(2,527) million in 2016 to positive £736 million in 2017, due primarily to higher premium flows into our with-profits funds following increased sales into with-profits savings and retirement products. This has been offset by lower premiums into our annuity business following our withdrawal from this market in the UK. The level 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 a small number of schemes influencing the level of flows in the period.

(b) Investment-related items and other movements of £11,146, million principally comprise investment return attributable to policyholders earned in the period reflecting favourable equity market movements.

(ii) Duration of liabilities

The following tables show the carrying value of the policyholder liabilities and the maturity profile of the cash flows, on a discounted basis for 2017 and 2016:

	With-profits business			Annuity business (Insurance contracts)			Other			Total
	Insurance contracts	Investment contracts	Total	Non-profit annuities within WPSF	Shareholder-backed annuity	Total	Insurance contracts	Investments contracts	Total	
2017 £m										
Policyholder liabilities	**38,285**	**62,328**	**100,613**	**10,609**	**32,572**	**43,181**	**6,714**	**17,081**	**23,795**	**167,589**
2017 %										
Expected maturity:										
0 to 5 years	**33%**	**37%**	**36%**	**31%**	**26%**	**27%**	**41%**	**31%**	**34%**	**34%**
5 to 10 years	**23%**	**27%**	**25%**	**24%**	**23%**	**23%**	**26%**	**22%**	**23%**	**25%**
10 to 15 years	**16%**	**17%**	**17%**	**17%**	**18%**	**18%**	**15%**	**18%**	**17%**	**17%**
15 to 20 years	**11%**	**10%**	**10%**	**11%**	**13%**	**13%**	**9%**	**13%**	**12%**	**11%**
20 to 25 years	**7%**	**4%**	**5%**	**7%**	**9%**	**9%**	**5%**	**8%**	**7%**	**6%**
over 25 years	**10%**	**5%**	**7%**	**10%**	**11%**	**10%**	**4%**	**8%**	**7%**	**7%**
2016 £m										
Policyholder liabilities	37,848	52,495	90,343	11,153	33,881	45,034	6,111	16,166	22,277	157,654
2016 %										
Expected maturity:										
0 to 5 years	37%	37%	37%	29%	25%	26%	40%	34%	37%	34%
5 to 10 years	23%	29%	26%	24%	22%	23%	23%	23%	23%	25%
10 to 15 years	15%	16%	16%	18%	18%	18%	12%	17%	15%	17%
15 to 20 years	9%	10%	10%	12%	14%	13%	7%	12%	10%	11%
20 to 25 years	7%	4%	5%	7%	9%	9%	4%	7%	6%	6%
over 25 years	9%	4%	6%	10%	12%	11%	14%	7%	9%	7%

– The cash flow projections of expected benefit payments used in the maturity profile table above are from value of in-force business and exclude the value of future new business, including future vesting of internal pension contracts.
– Benefit payments do not reflect the pattern of bonuses and shareholder transfers in respect of the with-profits business.
– Shareholder-backed annuity business includes the ex-PRIL and the legacy PAC shareholder annuity business.
– Investment contracts under 'Other' comprise certain unit-linked and similar contracts accounted for under IAS 39 and IAS 18.
– For business with no maturity term included within the contracts; for example, with-profits investment bonds such as Prudence Bonds, an assumption is made as to likely duration based on prior experience.

C5 Intangible assets

C5(a) Goodwill

	Attributable to: Shareholders	With-profits	2017 £m	2016 £m
Cost				
At beginning of year	**1,475**	**153**	**1,628**	1,648
Disposals/reclassifications to held for sale	**(16)**	**(139)**	**(155)**	(56)
Additional consideration paid on previously acquired business	**-**	**9**	**9**	7
Exchange differences	**(1)**	**1**	**-**	29
Net book amount at end of year	**1,458**	**24**	**1,482**	1,628

Goodwill comprises:

	2017 £m	2016 £m
M&G	**1,153**	1,153
Other – attributable to shareholders	**305**	322
Goodwill – attributable to shareholders	**1,458**	1,475
Venture fund investments – attributable to with-profits funds	**24**	153
	1,482	1,628

Other goodwill attributable to shareholders represents amounts allocated to entities in Asia and until August 2017 the US operations. These goodwill amounts are not individually material.

C5(b) Deferred acquisition costs and other intangible assets

	2017 £m	2016 £m
Deferred acquisition costs and other intangible assets attributable to shareholder	**10,866**	10,755
Deferred acquisition costs and other intangible assets attributable to with-profits funds	**145**	52
Total of deferred acquisition costs and other intangible assets	**11,011**	10,807

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

	2017 £m	2016 £m
Deferred acquisition costs related to insurance contracts as classified under IFRS 4	**9,170**	9,114
Deferred acquisition costs related to investment management contracts, including life assurance contracts classified as financial instruments and investment management contracts under IFRS 4	**63**	64
	9,233	9,178
Present value of acquired in-force policies for insurance contracts as classified under IFRS 4 (PVIF)	**36**	43
Distribution rights and other intangibles	**1,597**	1,534
	1,633	1,577
Total of deferred acquisition costs and other intangible assets	**10,866**	10,755

	2017 £m						2016 £m
	Deferred acquisition costs						
	Asia insurance	US insurance	UK and Europe insurance	All asset management	PVIF and other intangibles[1]	Total	Total
Balance at 1 January	**788**	**8,303**	**79**	**8**	**1,577**	**10,755**	8,422
Additions	**331**	**663**	**14**	**3**	**229**	**1,240**	1,179
Amortisation to the income statement:[2]							
Operating profit	**(133)**	**(403)**	**(10)**	**(5)**	**(158)**	**(709)**	(686)
Non-operating profit	**-**	**462**	**-**	**-**	**(7)**	**455**	557
	(133)	**59**	**(10)**	**(5)**	**(165)**	**(254)**	(129)
Disposals and transfers	**-**	**-**	**-**	**-**	**-**	**-**	(268)
Exchange differences and other movements	**(40)**	**(752)**	**1**	**-**	**(8)**	**(799)**	1,475
Amortisation of DAC related to net unrealised valuation movements on the US insurance operation's available-for-sale securities recognised within other comprehensive income[2]	**-**	**(76)**	**-**	**-**	**-**	**(76)**	76
Balance at 31 December	**946**	**8,197**	**84**	**6**	**1,633**	**10,866**	10,755

[1] PVIF and other intangibles includes amounts in relation to software rights with additions of £38 million, amortisation of £32 million, foreign exchange losses of £5 million and a balance at 31 December 2017 of £67 million.

[2] Under the Group's application of IFRS 4, US GAAP is used for measuring the insurance assets and liabilities of its US and certain Asia operations. Under US GAAP, most of the US insurance operation's products are accounted for under Accounting Standard no. 97 of the Financial Accounting Standards Board (FAS 97) whereby deferred acquisition costs are amortised in line with the emergence of actual and expected gross profits which are determined using an assumption for long-term investment returns for the separate account of 7.4 per cent (2016: 7.4 per cent) (gross of asset management fees and other charges to policyholders, but net of external fund management fees). The amounts included in the income statement and other comprehensive income affect the pattern of profit emergence and thus the DAC amortisation attaching. DAC amortisation is allocated to the operating and non-operating components of the Group's supplementary analysis of profit and other comprehensive income by reference to the underlying items (see note C7.3(iv)).

Note
PVIF and other intangibles comprise PVIF, distribution rights and other intangibles such as software rights. Distribution rights relate to amounts that have been paid or have become unconditionally due for payment as a result of past events in respect of bancassurance partnership arrangements in Asia. These agreements allow for bank distribution of Prudential's insurance products for a fixed period of time.

US insurance operations

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

	2017 £m	2016 £m
Variable annuity business	**8,208**	7,844
Other business	**278**	696
Cumulative shadow DAC (for unrealised gains booked in other comprehensive income)*	**(289)**	(237)
Total DAC for US operations	**8,197**	8,303

* Consequent upon the positive unrealised valuation movement in 2017 of £617 million (2016: negative unrealised valuation movement of £28 million), there is a loss of £76 million (2016: a gain of £76 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 occurred 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 31 December 2017, the cumulative shadow DAC balance as shown in the table above was negative £289 million (2016: negative £237 million).

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 (which is used for moderating the effect of short-term volatility in investment returns) 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 2017, the DAC amortisation charge for operating profit was determined after including a credit for decelerated amortisation of £86 million (2016: credit for decelerated amortisation of £93 million). The 2017 amount primarily reflects the impact of the positive separate account performance, which is higher than the assumed level for the year.

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. In 2018, it would take approximate movements in separate account values of more than either negative 32 per cent or positive 37 per cent for the mean reversion assumption to move outside the corridor.

C6 Borrowings

C6.1 Core structural borrowings of shareholder-financed operations

	2017 £m	2016 £m
Holding company operations: note (i)		
Perpetual Subordinated Capital Securities (Tier 1) note (i)	**814**	890
Perpetual Subordinated Capital Securities (Tier 2) note (i),(iv),(v)	**2,326**	2,754
Subordinated Notes (Tier 2) note (i)	**2,132**	2,128
Subordinated debt total	**5,272**	5,772
Senior debt: note (ii)		
£300m 6.875% Bonds 2023	**300**	300
£250m 5.875% Bonds 2029	**249**	249
Holding company total	**5,821**	6,321
Prudential Capital bank loan note (iii)	**275**	275
Jackson US$250m 8.15% Surplus Notes 2027	**184**	202
Total (per consolidated statement of financial position)	**6,280**	6,798

Notes
(i) These debt tier classifications are consistent with the treatment of capital for regulatory purposes under the Solvency II regime. The Group has designated all US$4,275 million (2016: US$4,525 million) of its US dollar denominated subordinated debt as a net investment hedge under IAS 39 to hedge the currency risks related to the net 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 is drawn at a cost of 12 month GBP LIBOR plus 0.33 per cent. The loan was renewed in December 2017 maturing on 20 December 2022 with an option to repay annually.
(iv) In October 2017, the Company issued core structural borrowings of US$750 million 4.875 per cent Tier 2 perpetual subordinated notes. The proceeds, net of costs, were £565 million.
(v) In December 2017, the Company repaid its US$1,000 million 6.5 per cent Tier 2 perpetual subordinated notes.

Prudential plc has debt ratings from Standard & Poor's, Moody's and Fitch. Prudential plc'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.

The financial strength of The Prudential Assurance Company Limited is rated AA by Standard & Poor's, Aa3 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, AA by Fitch and A+ by AM Best.

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

All ratings on Prudential and its subsidiaries have been reaffirmed on stable outlook. All ratings stated as at 13 March 2018.

C6.2 Other borrowings

(a) Operational borrowings attributable to shareholder-financed operations

	2017 £m	**2016 £m**
Borrowings in respect of short-term fixed income securities programmes	**1,085**	1,651
Other borrowings[note]	**706**	666
Total	**1,791**	2,317

Note

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

	2017 £m	**2016 £m**
Non-recourse borrowings of consolidated investment funds*	**3,570**	1,189
£100m 8.5% undated subordinated guaranteed bonds of Scottish Amicable Finance plc†	**100**	100
Other borrowings (predominantly obligations under finance leases)	**46**	60
Total	**3,716**	1,349

* In all instances the holders of the debt instruments issued by these subsidiaries and funds do not have recourse beyond the assets of these subsidiaries and funds. The increase since 31 December 2016 primarily relates to the debt instruments issued by new consolidated securitisation entities backed by a portfolio of mortgage loans (see note C3.3(c) for further details).

† The interests of the holders of the bonds issued by Scottish Amicable Finance plc, a subsidiary of the Scottish Amicable Insurance Fund, are subordinated to the entitlements of the policyholders of that fund.

C7 Risk and sensitivity analysis

C7.1 Group overview

The Group's risk framework and the management of the risk, including those attached to the Group's financial statements including financial assets, financial liabilities and insurance liabilities, together with the inter-relationship with the management of capital have been included in the 'Report on the risks facing our business and how these are managed'.

The financial and insurance assets and liabilities on the Group's balance sheet are, to varying degrees, subject to market and insurance risk and other changes of experience assumptions that may have a material effect on IFRS basis profit or loss and shareholders' equity. The market and insurance risks, including how they affect Group's operations and how these are managed are discussed in the Risk report referred to above.

The most significant items that the IFRS shareholders' profit or loss and shareholders' equity for the Group's life assurance business are sensitive to, are shown in the following tables. The distinction between direct and indirect exposure is not intended to indicate the relative size of the sensitivity.

Type of business	Market and credit risk			Insurance and lapse risk
	Investments/derivatives	Liabilities / unallocated surplus	Other exposure	
Asia insurance operations (see also section C7.2)				
All business	Currency risk			Mortality and morbidity risk Persistency risk
With-profits business	Net neutral direct exposure (indirect exposure only)		Investment performance subject to smoothing through declared bonuses	
Unit-linked business	Net neutral direct exposure (indirect exposure only)		Investment performance through asset management fees	
Non-participating business	Asset/liability mismatch risk			
	Credit risk	Interest rates for those operations where the basis of insurance liabilities is sensitive to current market movements		
	Interest rate and price risk			
US insurance operations (see also section C7.3)				
All business	Currency risk			Persistency risk
Variable annuity business	Net effect of market risk arising from incidence of guarantee features and variability of asset management fees offset by derivative hedging programme			Risk that utilisation of withdrawal benefits or lapse levels differ from those assumed in pricing
Fixed index annuity business	Derivative hedge programme to the extent not fully hedged against liability	Incidence of equity participation features		
Fixed index annuities, Fixed annuities and GIC business	Credit risk Interest rate risk Profit and loss and shareholders' equity are volatile for these risks as they affect the values of derivatives and embedded derivatives and impairment losses. In addition, shareholders' equity is volatile for the incidence of these risks on unrealised appreciation of fixed income securities classified as available-for-sale under IAS 39		Spread difference between earned rate and rate credited to policyholders	Lapse risk, but the effects of extreme events may be mitigated by the application of market value adjustments
UK and Europe insurance operations (see also section C7.4)				
With-profits business	Net neutral direct exposure (indirect exposure only)		Investment performance subject to smoothing through declared bonuses	Persistency risk to future shareholder transfers
SAIF sub-fund	Net neutral direct exposure (indirect exposure only)		Asset management fees earned	
Unit-linked business	Net neutral direct exposure (indirect exposure only)		Investment performance through asset management fees	Persistency risk
	Asset/liability mismatch risk			
Shareholder-backed annuity business	Credit risk for assets covering liabilities and shareholder capital Interest rate risk for assets in excess of liabilities ie assets representing shareholder capital			Mortality experience and assumptions for longevity

Detailed analyses of sensitivity of IFRS basis profit or loss and shareholders' equity to key market and other risks by business unit are provided in notes C7.2, C7.3, C7.4 and C7.5. The sensitivity analyses provided show the effect on profit or loss and shareholders' equity to changes in the relevant risk variables, all of which are reasonably possible at the relevant balance sheet date. In the equity risk sensitivity analysis shown below, the Group has considered the impact of an instantaneous 20 per cent fall in equity markets. If equity markets were to fall by more than 20 per cent, the Group believes that this would not be an instantaneous fall but rather would be expected to occur over a period of time during which the Group would be able to put mitigating management actions in place. In addition, the equity risk sensitivity analysis provided assumed that all equity indices fall by the same percentage.

Impact of diversification on risk exposure
The Group benefits from diversification benefits achieved through the geographical spread of the Group's operations and, within those operations, through a broad mix of product types. Relevant correlation factors include:

Correlation across geographic regions:
- Financial risk factors; and
- Non-financial risk factors.

Correlation across risk factors:
- Longevity risk;
- Expenses;
- Persistency; and
- Other risks.

The sensitivities below do not reflect that assets and liabilities are actively managed and may vary at the time any actual market movement occurs. There are strategies in place to minimise the exposure to market fluctuations. For example, as market indices fluctuate, Prudential would take certain actions including selling investments, changing investment portfolio allocation and adjusting bonuses credited to policyholders. In addition, these analyses do not consider the effect of market changes on new business generated in the future.

Other limitations on the sensitivities include: the use of hypothetical market movements to demonstrate potential risk that only represent Prudential's view of reasonably possible near-term market changes and that cannot be predicted with any certainty; the assumption that interest rates in all countries move identically; the assumption that all global currencies move in tandem with the US dollar against pound sterling; and the lack of consideration of the inter- relation of interest rates, equity markets and foreign currency exchange rates.

C7.2 Asia insurance operations

Exposure and sensitivity of IFRS basis profit and shareholders' equity to market and other risks
The Asia operations sell with-profits and unit-linked policies, and the investment portfolio of the with-profits funds contains a proportion of equities. Non-participating business is largely backed by debt securities or deposits. The Group's exposure to market risk arising from its Asia operations is therefore at modest levels. This reflects the fact that the Asia operations have a balanced portfolio of with-profits, unit-linked and other types of business.

In Asia, adverse persistency experience can impact the IFRS profitability of certain types of business written in the region. This risk is managed at a business unit level through regular monitoring of experience and the implementation of management actions as necessary. These actions could include product enhancements, increased management focus on premium collection, as well as other customer retention efforts. The potential financial impact of lapses is often mitigated through the specific features of the products, eg surrender charges, or through the availability of premium holiday or partial withdrawal policy features.

In summary, for Asia operations, the operating profit based on longer-term investment returns is mainly affected by the impact of market levels on unit-linked persistency, and other insurance risks. At the total IFRS profit level the Asia result is affected by short-term value movements on the asset portfolio for non-linked shareholder-backed business.

i Sensitivity to risks other than foreign exchange risk
Interest rate risk
Excluding its with-profits and unit-linked businesses, the results of the Asia business are sensitive to the movements in interest rates.

For the purposes of analysing sensitivity to variations in interest rates, reference has been made to the movements in the 10-year government bond rates of the territories. At 31 December 2017, 10-year government bond rates vary from territory to territory and range from 1.0 per cent to 7.5 per cent (2016: 1.2 per cent to 8.1 per cent).

For the sensitivity analysis as shown in the table below, the reasonably possible interest rate movement used is 1 per cent for all territories.

The estimated sensitivity to the decrease and increase in interest rates at 31 December 2017 and 2016 is as follows:

	2017 £m		2016 £m	
	Decrease of 1%	**Increase of 1%**	**Decrease of 1%**	**Increase of 1%**
Profit before tax attributable to shareholders	**2**	**(443)**	213	(509)
Related deferred tax (where applicable)	**(7)**	**20**	(41)	62
Net effect on profit and shareholders' equity	**(5)**	**(423)**	172	(447)

The pre-tax impacts, if they arose, would mostly be recorded within the category short-term fluctuations in investments returns in the Group's segmental analysis of profit before tax.

The degree of sensitivity of the results of the non-linked shareholder-backed business of the Asia operations to movements in interest rates depends upon the degree to which the liabilities under the 'grandfathered' IFRS 4 measurement basis reflects market interest rates from period-to-period. For example for those countries, such as those applying US GAAP, the results can be more sensitive as the effect of interest rate movements on the backing investments may not be offset by liability movements.

In addition, the degree of sensitivity of the results shown in the table above is dependent on the interest rate level at that point of time. The low interest rates in certain countries have had an adverse impact on the degree of sensitivity to a decrease in interest rates.

An additional factor to the direction of the sensitivity of the Asia operations as a whole is movement in the country mix.

Equity price risk
The non-linked shareholder-backed business has limited exposure to equity and property investment (31 December 2017: £1,764 million). Generally changes in equity and property investment values are not directly offset by movements in non-linked policyholder liabilities.

The estimated sensitivity to a 10 per cent and 20 per cent change in equity and property prices for shareholder-backed Asia other business (including those held by the Group's joint venture and associate businesses), which would be reflected in the short-term fluctuation component of the Group's segmental analysis of profit before tax, at 31 December 2017 and 2016 is as follows:

	2017 £m		2016 £m	
	Decrease		**Decrease**	
	of 20%	**of 10%**	**of 20%**	**of 10%**
Profit before tax attributable to shareholders	**(478)**	**(239)**	(386)	(192)
Related deferred tax (where applicable)	**7**	**4**	4	2
Net effect on profit and shareholders' equity	**(471)**	**(235)**	(382)	(190)

A 10 or 20 per cent increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above.

Insurance risk
Many of the business units in Asia are exposed to mortality/morbidity risk and provision is made within policyholder liabilities on a prudent regulatory basis to cover the potential exposure. If these prudent assumptions were strengthened by 5 per cent then it is estimated that post-tax profit and shareholders' equity would be decreased by approximately £66 million (2016: £61 million). Mortality and morbidity has a symmetrical effect on the portfolio and any weakening of these assumptions would have a similar equal and opposite impact.

ii Sensitivity to foreign exchange risk
Consistent with the Group's accounting policies, the profits of the Asia insurance operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2017, the rates for the most significant operations are given in note A1.

A 10 per cent increase (strengthening of the pound sterling) or decrease (weakening of the pound sterling) in these rates would have reduced or increased profit before tax attributable to shareholders, profit for the year and shareholders' equity, excluding goodwill attributable to Asia insurance operations respectively as follows:

	A 10% increase in local currency to £ exchange rates		A 10% decrease in local currency to £ exchange rates	
	2017 £m	**2016 £m**	**2017 £m**	**2016 £m**
Profit before tax attributable to shareholders	**(155)**	(97)	**189**	118
Profit for the year	**(135)**	(77)	**165**	94
Shareholders' equity, excluding goodwill, attributable to Asia operations	**(492)**	(442)	**601**	540

C7.3 US insurance operations

Exposure and sensitivity of IFRS basis profit and shareholders' equity to market and other risks
Jackson's reported operating profit based on longer-term investment returns is sensitive to market conditions, both with respect to income earned on spread-based products and indirectly with respect to income earned on variable annuity asset management fees. Jackson's main exposures to market risk are to interest rate risk and equity risk.

Jackson is exposed primarily to the following risks:

Risks	Risk of loss
Equity risk	• related to the incidence of benefits related to guarantees issued in connection with its variable annuity contracts; and • related to meeting contractual accumulation requirements in fixed index annuity contracts.
Interest rate risk	• related to meeting guaranteed rates of accumulation on fixed annuity products following a sustained fall in interest rates; • related to increases in the present value of projected benefits related to guarantees issued in connection with its variable annuity contracts following a sustained fall in interest rates especially if in conjunction with a fall in equity markets; • related to the surrender value guarantee features attached to the Company's fixed annuity products and to policyholder withdrawals following a sharp and sustained increase in interest rates; and • the risk of mismatch between the expected duration of certain annuity liabilities and prepayment risk and extension risk inherent in mortgage-backed securities.

Jackson's derivative programme is used to manage interest rate risk associated with a broad range of products and equity market risk attaching to its equity-based products. Movements in equity markets, equity volatility, interest rates and credit spreads materially affect the carrying value of derivatives that are used to manage the liabilities to policyholders and backing investment assets. Movements in the carrying value of derivatives combined with the use of US GAAP measurement (as 'grandfathered' under IFRS 4) for the insurance contracts assets and liabilities, which is largely insensitive to current period market movements mean that the Jackson total profit (ie including short-term fluctuations in investment returns) is sensitive to market movements. In addition to these effects the Jackson shareholders' equity is sensitive to the impact of interest rate and credit spread movements on the value of fixed income securities. Movements in unrealised appreciation on these securities are included as movement in shareholders' equity (ie outside the income statement).

Jackson enters into financial derivative transactions, including those noted below to reduce and manage business risks. These transactions manage the risk of a change in the value, yield, price, cash flows or quantity of, or a degree of exposure with respect to assets, liabilities or future cash flows, which Jackson has acquired or incurred.

Jackson uses free-standing derivative instruments for hedging purposes. Additionally, certain liabilities, primarily trust instruments supported by funding agreements, fixed index annuities, certain variable annuity guaranteed benefit features and reinsured Guaranteed Minimum Income Benefit variable annuity features are similar to derivatives. Jackson does not account for such items as either fair value or cash flow hedges as might be permitted if the specific hedge documentation requirements of IAS 39 were followed. Financial derivatives, including derivatives embedded in certain host liabilities that have been separated for accounting and financial reporting purposes are carried at fair value.

The principal types of derivatives used by Jackson and their purpose are as follows:

Derivative	Purpose
Interest rate swaps	These generally involve the exchange of fixed and floating payments over the period for which Jackson holds the instrument without an exchange of the underlying principal amount. These agreements are used to hedge Jackson's exposure to movements in interest rates.
Swaption contracts	These contracts provide the purchaser with the right, but not the obligation, to require the writer to pay the present value of a long-duration interest rate swap at future exercise dates. Jackson both purchases and writes swaptions in order to hedge against significant movements in interest rates.
Treasury futures contracts	These derivatives are used to hedge Jackson's exposure to movements in interest rates.
Equity index futures contracts and equity index options	These derivatives (including various call and put options and options contingent on interest rates and currency exchange rates) are used to hedge Jackson's obligations associated with its issuance of certain VA guarantees. Some of these annuities and guarantees contain embedded options that are fair valued for financial reporting purposes.
Cross-currency swaps	Cross-currency swaps, which embody spot and forward currency swaps and additionally, in some cases, interest rate swaps and equity index swaps, are entered into for the purpose of hedging Jackson's foreign currency denominated funding agreements supporting trust instrument obligations.
Credit default swaps	These swaps represent agreements under which Jackson has purchased default protection on certain underlying corporate bonds held in its portfolio. These contracts allow Jackson to sell the protected bonds at par value to the counterparty if a default event occurs in exchange for periodic payments made by Jackson for the life of the agreement. Jackson does not write default protection using credit derivatives.

The estimated sensitivity of Jackson's profit and shareholders' equity to equity and interest rate risks provided below is net of the related changes in amortisation of DAC. The effect on the related changes in amortisation of DAC provided is based on the current 'grandfathered' US GAAP DAC basis but does not include any effect from an acceleration or deceleration of amortisation of DAC.

i Sensitivity to equity risk

At 31 December 2017 and 2016, Jackson had variable annuity contracts with guarantees, for which the net amount at risk (NAR) is defined as the amount of guaranteed benefit in excess of current account value, as follows:

31 December 2017	**Minimum return**	**Account value £m**	**Net amount at risk £m**	**Weighted average attained age**	**Period until expected annuitisation**
Return of net deposits plus a minimum return					
GMDB	**0-6%**	**100,451**	**1,665**	**66.0 years**	
GMWB - premium only	**0%**	**2,133**	**20**		
GMWB*	**0-5%****	**235**	**13**		
GMAB - premium only	**0%**	**38**	**-**		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		**9,099**	**96**	**66.5 years**	
GMWB - highest anniversary only		**2,447**	**51**		
GMWB*		**667**	**47**		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	**0-6%**	**5,694**	**426**	**69.0 years**	
GMIB†	**0-6%**	**1,484**	**436**		**0.4 years**
GMWB*	**0-8%****	**93,227**	**4,393**		

31 December 2016	**Minimum return**	**Account value £m**	**Net amount at risk £m**	**Weighted average attained age**	**Period until expected annuitisation**
Return of net deposits plus a minimum return					
GMDB	0-6%	93,512	2,483	65.6 years	
GMWB - premium only	0%	2,217	39		
GMWB*	0-5%**	256	22		
GMAB - premium only	0%	44	-		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		8,798	346	66.0 years	
GMWB - highest anniversary only		2,479	125		
GMWB*		747	83		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0-6%	5,309	699	68.7 years	
GMIB†	0-6%	1,595	595		0.5 years
GMWB*	0-8%**	85,402	9,293		

* Amounts shown for GMWB comprise sums for the 'not for life' portion (where the guaranteed withdrawal base less the account value equals to the net amount at risk (NAR)), and a 'for life' portion (where the NAR has been estimated as the present value of future expected benefit payment remaining after the amount of the 'not for life' guaranteed benefits is zero).

** Ranges shown based on simple interest. The upper limits of 5 per cent or 8 per cent simple interest are approximately equal to 4.1 per cent and 6 per cent respectively, on a compound interest basis over a typical 10-year bonus period. For example 1 + 10 x 0.05 is similar to 1.04 growing at a compound rate of 4 per cent for a further nine years.

† The GMIB guarantees are essentially fully reinsured.

Account balances of contracts with guarantees were invested in variable separate accounts as follows:

	2017 £m	**2016 £m**
Mutual fund type:		
Equity	**80,843**	73,430
Bond	**13,976**	15,044
Balanced	**19,852**	17,441
Money market	**681**	994
Total	**115,352**	106,909

As noted above, Jackson is exposed to equity risk through the options embedded in the fixed index annuity liabilities and guarantees included in certain variable annuity benefits as illustrated above. This risk is managed using an equity hedging programme to minimise the risk of a significant economic impact as a result of increases or decreases in equity market levels while taking advantage of naturally offsetting exposures in Jackson's operations. Jackson purchases futures and options that hedge the risks inherent in these products, while also considering the impact of rising and falling guaranteed benefit fees.

Due to the nature and the valuation under IFRS of the free-standing derivatives and the Variable annuity guarantee features, this hedge, while highly effective on an economic basis, would not be completely mute in the financial reporting as the immediate impact of equity market movements reset the free-standing derivatives immediately while the hedged liabilities reset more slowly and fees are recognised prospectively in the period in which they are earned.

In addition to the exposure explained above, Jackson is also exposed to equity risk from its holding of equity securities, partnerships in investment pools and other financial derivatives.

At 31 December 2017, the estimated sensitivity of Jackson's profit and shareholders' equity to immediate increases and decreases in equity markets is shown below. The sensitivities are shown net of related changes in DAC amortisation.

	2017 £m				2016 £m			
	Decrease		Increase		Decrease		Increase	
	of 20%	of 10%	of 20%	of 10%	of 20%	of 10%	of 20%	of 10%
Pre-tax profit, net of related changes in amortisation of DAC	**1,107**	**336**	**619**	**262**	1,061	488	370	59
Related deferred tax effects	**(233)**	**(71)**	**(130)**	**(55)**	(371)	(171)	(129)	(21)
Net sensitivity of profit after tax and shareholders' equity	**874**	**265**	**489**	**207**	690	317	241	38

Note

The table above has been prepared to exclude the impact of the instantaneous equity movements on the separate account fees. In addition, the sensitivity movements shown include those relating to the fixed index annuity and the reinsurance of GMIB guarantees.

The above table provides sensitivity movements as at a point in time while the actual impact on financial results would vary contingent upon the volume of new product sales and lapses, changes to the derivative portfolio, correlation of market returns and various other factors including volatility, interest rates and elapsed time.

The directional movements in the sensitivities reflect the hedging programme in place at 31 December 2017 and 2016.

ii Sensitivity to interest rate risk

Except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of fixed annuity liabilities of Jackson’s products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement. The GMWB features attached to variable annuity business (other than ‘for life’ components) are accounted for under US GAAP as embedded derivatives which are fair valued and, therefore, will be sensitive to changes in interest rates.

Debt securities and related derivatives are marked to fair value. Value movements on derivatives, again net of related changes to amortisation of DAC and deferred tax, are recorded within the income statement. Fair value movements on debt securities, net of related changes to amortisation of DAC and deferred tax, are recorded within other comprehensive income. The estimated sensitivity of these items and policyholder liabilities to a 1 per cent and 2 per cent decrease and increase in interest rates at 31 December 2017 and 2016 is as follows:

	2017 £m				2016 £m			
	Decrease		Increase		Decrease		Increase	
	of 2%	of 1%	of 1%	of 2%	of 2%	of 1%	of 1%	of 2%
Profit and loss:								
Pre-tax profit effect (net of related changes in amortisation of DAC)	**(4,079)**	**(1,911)**	**1,373**	**2,533**	(2,899)	(1,394)	1,065	2,004
Related effect on charge for deferred tax	**857**	**401**	**(288)**	**(532)**	1,015	488	(373)	(701)
Net profit effect	**(3,222)**	**(1,510)**	**1,085**	**2,001**	(1,884)	(906)	692	1,303
Other comprehensive income:								
Direct effect on carrying value of debt securities (net of related changes in amortisation of DAC)	**3,063**	**1,700**	**(1,700)**	**(3,063)**	3,364	1,883	(1,883)	(3,364)
Related effect on movement in deferred tax	**(643)**	**(357)**	**357**	**643**	(1,177)	(659)	659	1,177
Net effect	**2,420**	**1,343**	**(1,343)**	**(2,420)**	2,187	1,224	(1,224)	(2,187)
Total net effect on shareholders' equity	**(802)**	**(167)**	**(258)**	**(419)**	303	318	(532)	(884)

These sensitivities are shown only for interest rates in isolation and do not include other movements in credit risk that may affect credit spreads and valuations of debt securities. Similar to sensitivity to equity risk, the sensitivity movements provided in the table above are at a point in time and reflect the hedging programme in place on the balance sheet date, while the actual impact on financial results would vary contingent upon a number of factors.

iii Sensitivity to foreign exchange risk

Consistent with the Group's accounting policies, the profits of the Group's US operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2017, the average and closing rates were US$1.29 (2016: US$1.35) and US$1.35 (2016: US$1.24) to £1.00 sterling, respectively. A 10 per cent increase (weakening of the dollar) or decrease (strengthening of the dollar) in these rates would reduce or increase profit before tax attributable to shareholders, profit for the year and shareholders' equity attributable to US insurance operations respectively as follows:

	A 10% increase in US$:£ exchange rates		A 10% decrease in US$:£ exchange rates	
	2017 £m	**2016 £m**	**2017 £m**	**2016 £m**
Profit before tax attributable to shareholders	**(54)**	(48)	**66**	59
Profit for the year	**(20)**	(54)	**24**	66
Shareholders' equity attributable to US insurance operations	**(456)**	(473)	**557**	578

iv Other sensitivities

The total profit of Jackson is sensitive to market risk on the assets covering liabilities other than variable annuity business segregated in the separate accounts.

For term business, acquisition costs are deferred and amortised in line with expected premiums. For annuity and interest-sensitive life business, acquisition costs are deferred and amortised in line with expected gross profits on the relevant contracts. For interest-sensitive business, the key assumption is the expected long-term spread between the earned rate and the rate credited to policyholders. In addition, expected gross profits 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 experience is measured by internally developed expense, mortality and persistency studies.

For variable annuity business, an assumption made is the expected long-term level of separate account returns, which for 2017 was 7.4 per cent (2016: 7.4 per cent). The impact of using this return is reflected in two principal ways, namely:

– Through the projected expected gross profits that are used to determine the amortisation of deferred acquisition costs. This is applied through the use of a mean reversion technique; and
– The required level of provision for claims for guaranteed minimum death, 'for life' withdrawal, and income benefits.

Jackson is sensitive to mortality risk, lapse risk and other types of policyholder behaviour, such as the utilisation of its GMWB product features. Jackson's persistency assumptions reflect a combination of recent experience for each relevant line of business and expert judgement, especially where a lack of relevant and credible experience data exists. These assumptions vary by relevant factors, such as product, policy duration, attained age and for variable annuity lapse assumptions, the extent to which guaranteed benefits are 'in the money' relative to policy account values. Changes in these assumptions, which are assessed on an annual basis after considering recent experience, could have a material impact on policyholder liabilities and therefore on profit before tax. See further information in note B1.2.

In addition, in the absence of hedging, equity and interest rate movements can both cause a loss directly or an increased future sensitivity to policyholder behaviour. Jackson has an extensive derivative programme that seeks to manage the exposure to such altered equity markets and interest rates.

C7.4 UK and Europe insurance operations

Exposure and sensitivity of IFRS basis profit and shareholders' equity to market and other risks

The IFRS basis results of the UK and Europe insurance operations are most sensitive to the following factors:

- Asset/liability matching;
- Default rate experience;
- Mortality;
- Longevity assumptions; and
- The difference between the return on corporate bond and risk-free rate for shareholder-backed annuity business of The Prudential Assurance Company Limited.

Further details are described below.

The IFRS operating profit based on longer-term investment returns for UK and Europe insurance operations is sensitive to changes in longevity assumptions affecting the carrying value of liabilities to policyholders for UK shareholder-backed annuity business. At the total IFRS profit level, the result is particularly sensitive to temporary value movements on assets backing the capital of the shareholder-backed annuity business.

With-profits business

With-profits sub-fund business

The shareholder results of the UK with-profits business (including non-participating annuity business of the with-profits sub-fund) are only sensitive to market risk through the indirect effect of investment performance on declared policyholder bonuses.

The investment assets of PAC with-profits funds are subject to market risk. Changes in their carrying value, net of related changes to asset-share liabilities of with-profits contracts, affect the level of unallocated surplus of the fund. Therefore, the level of unallocated surplus is particularly sensitive to the level of investment returns on the portion of the assets that represents surplus. However, as unallocated surplus is accounted for as a liability under IFRS, movements in its value do not affect shareholders' profit and equity.

The shareholder results of the UK with-profits fund are currently one-ninth of the cost of bonuses declared to with-profits policyholders. For certain unitised with-profits products, such as the PruFund range of funds, the bonuses represent the policyholders' net return based on the smoothed unit price of the selected investment fund. Investment performance is a key driver of bonuses declared, and hence the shareholder results. Due to the 'smoothed' basis of bonus declaration, the sensitivity to short-term investment performance is relatively low. However, long-term investment performance and persistency trends may affect future shareholder transfers.

Shareholder-backed annuity business

Profits from shareholder-backed annuity business are most sensitive to:

- The extent to which the duration of the assets held closely matches the expected duration of the liabilities under the contracts;
- Actual versus expected default rates on assets held;
- The difference between long-term rates of return on corporate bonds and risk-free rates;
- The variance between actual and expected mortality experience;
- The extent to which changes to the assumed rate of improvements in mortality give rise to changes in the measurement of liabilities; and
- Changes in renewal expense levels.

In addition the level of profit is affected by change in the level of reinsurance cover.

A decrease in assumed mortality rates of 1 per cent would decrease pre-tax profit by approximately £66 million (2016: £67 million). A decrease in credit default assumptions of five basis points would increase pre-tax profit by £198 million (2016: £200 million). A decrease in renewal expenses (excluding asset management expenses) of 5 per cent would increase pre-tax profit by £40 million (2016: £41 million). The effect on profit would be approximately symmetrical for changes in assumptions that are directionally opposite to those explained above. The net effect on profit after tax and shareholders' equity from all the changes in assumptions as described above would be an increase of approximately £143 million (2016: £144 million). See C4.1(d)(iii) for further details on mortality assumptions.

Unit-linked and other business

Unit-linked and other business represents a comparatively small proportion of the in-force business of the UK and Europe insurance operations.

Due to the matching of policyholder liabilities to attaching asset value movements, the UK unit-linked business is not directly affected by market or credit risk. The liabilities of the other business are also broadly insensitive to market risk. Profits from unit-linked and similar contracts primarily arise from the excess of charges to policyholders for management of assets, over expenses incurred. The former is most sensitive to the net accretion of funds under management as a function of new business and lapse and timing of death. The accounting impact of the latter is dependent upon the amortisation of acquisition costs in line with the emergence of margins (for insurance contracts) and amortisation in line with service provision (for the investment management component of investment contracts). By virtue of the design features of most of the contracts which provide low levels of mortality cover, the profits are relatively insensitive to changes in mortality experience.

Sensitivity to interest rate risk and other market risk

By virtue of the fund structure, product features and basis of accounting, the policyholder liabilities of the UK and Europe insurance operations are, except annuity business, not generally exposed to interest rate risk. At 31 December 2017 annuity liabilities accounted for 98 per cent (2016: 98 per cent) of UK shareholder-backed business liabilities. For annuity business, liabilities are exposed to interest rate risk. However, the net exposure substantially ameliorated by virtue of the close matching of assets with appropriate duration. The level of matching from period to period can vary depending on management actions and economic factors so it is possible for a degree of mis-matching profits or losses to arise.

The close matching by the Group of assets of appropriate duration to annuity liabilities is based on maintaining economic and regulatory capital. Liabilities are measured differently under Solvency II reporting requirements than under IFRS resulting in an alteration to the assets used to measure the IFRS annuity liabilities. As a result, IFRS has a different sensitivity to interest rate and credit risk than under Solvency II.

The estimated sensitivity of the UK non-linked shareholder-backed business (principally annuities business) to a movement in interest rates is as follows:

	2017 £m				**2016 £m**			
	A decrease of 2%	**A decrease of 1%**	**An increase of 1%**	**An increase of 2%**	**A decrease of 2%**	**A decrease of 1%**	**An increase of 1%**	**An increase of 2%**
Carrying value of debt securities and derivatives	**13,497**	**5,805**	**(4,659)**	**(8,541)**	12,353	5,508	(4,527)	(8,313)
Policyholder liabilities	**(9,426)**	**(4,210)**	**3,443**	**6,295**	(10,023)	(4,466)	3,636	6,635
Related deferred tax effects	**(658)**	**(254)**	**190**	**348**	(396)	(177)	151	285
Net sensitivity of profit after tax and shareholders' equity	**3,413**	**1,341**	**(1,026)**	**(1,898)**	1,934	865	(740)	(1,393)

In addition the shareholder-backed portfolio of UK non-linked insurance operations (covering policyholder liabilities and shareholders' equity) includes equity securities and investment properties. Excluding any offsetting effects on the measurement of policyholder liabilities, a fall in their value would have given rise to the following effects on pre-tax profit, profit after tax and shareholders' equity.

	2017 £m		2016 £m	
	A decrease of 20%	**A decrease of 10%**	**A decrease of 20%**	**A decrease of 10%**
Pre-tax profit	**(332)**	**(166)**	(326)	(163)
Related deferred tax effects	**57**	**28**	66	33
Net sensitivity of profit after tax and shareholders' equity	**(275)**	**(138)**	(260)	(130)

A 10 or 20 per cent increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above. The market risk sensitivities shown above reflect the impact of temporary market movements, and, therefore the primary effect of such movements would, in the Group's segmental analysis of profits, be included within the short-term fluctuations in investment returns.

C7.5 Asset management and other operations

a Asset management

i Sensitivities to foreign exchange risk

Consistent with the Group's accounting policies, the profits of Eastspring Investments and US asset management operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. The rates for the functional currencies of most significant operations are shown in note A1.

A 10 per cent increase in the relevant exchange rates (strengthening of the pound sterling) would have reduced reported profit before tax attributable to shareholders, and shareholders' equity excluding goodwill attributable to Eastspring Investments and US asset management operations, by £30 million and £53 million respectively (2016: £12 million and £47 million, respectively).

ii Sensitivities to other financial risks for asset management operations

The profits of asset management businesses are sensitive to the level of assets under management, as this significantly affects the value of management fees earned by the business in the current and future periods. The Group's asset management operations do not hold significant investments in property or equities.

b Other operations

The Group holds certain derivatives that are used to manage foreign currency movements and macroeconomic exposures. The fair value of these derivatives is sensitive to the combined effect of movements in exchange rates, interest rates and inflation rates. The possible permutations cover a wide range of scenarios. For indicative purposes, a reasonably possible range of fair value movements could be plus or minus £150 million.

Other operations are sensitive to credit risk on the bridging loan portfolio of the Prudential Capital operation. Total debt securities held at 31 December 2017 by Prudential Capital were £2,238 million (2016: £2,359 million). Debt securities held by Prudential Capital are in general variable rate bonds and so market value is limited in sensitivity to interest rate movements and consequently any change in interest rates would not have a material impact on profit or shareholders' equity.

C8 Tax assets and liabilities

Deferred tax

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

	2017 £m				
	At 1 Jan	**Movement in income statement**	**Movement through other comprehensive income and equity**	**Other movements including foreign currency movements**	**At 31 Dec**
Deferred tax assets					
Unrealised losses or gains on investments	**23**	**(8)**	**-**	**(1)**	**14**
Balances relating to investment and insurance contracts	**1**	**-**	**-**	**-**	**1**
Short-term temporary differences	**4,196**	**(1,396)**	**(1)**	**(267)**	**2,532**
Capital allowances	**16**	**(2)**	**-**	**-**	**14**
Unused tax losses	**79**	**(12)**	**-**	**(1)**	**66**
Total	**4,315**	**(1,418)**	**(1)**	**(269)**	**2,627**
Deferred tax liabilities					
Unrealised losses or gains on investments	**(1,534)**	**(177)**	**(55)**	**18**	**(1,748)**
Balances relating to investment and insurance contracts	**(730)**	**(156)**	**-**	**14**	**(872)**
Short-term temporary differences	**(3,071)**	**870**	**(26)**	**186**	**(2,041)**
Capital allowances	**(35)**	**(3)**	**-**	**(16)**	**(54)**
Total	**(5,370)**	**534**	**(81)**	**202**	**(4,715)**

The reduction in the US corporate income tax rate to 21 per cent from 1 January 2018 was substantively enacted on 22 December 2017. The remeasurement to 21 per cent reduced deferred tax assets subject to US taxation by £1,587 million and deferred tax liabilities by £1,368 million. The £219 million net reduction was reflected partly in the income statement (£445 million charge attributable to shareholders and £92 million benefit to policyholders) and partly through reserves in other comprehensive income (£134 million benefit).

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 period.

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.

C9 Defined benefit pension schemes

(a) Background and summary economic and IAS 19 financial positions

The Group's businesses operate a number of pension schemes. The specific features of these schemes 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 82 per cent (2016: 82 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 (SASPS) and M&G (M&GGPS). In addition, there are two small defined benefit schemes in Taiwan which have negligible deficits.

Under IAS 19 'Employee Benefits' and IFRIC 14 'IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction', the Group is only able to recognise a surplus to the extent that it is able to access the surplus either through an unconditional right of refund or through reduced future contributions relating to on-going service of active members. The Group has no unconditional right of refund to any surplus in PSPS. Accordingly, the PSPS surplus recognised is restricted to the present value of the economic benefit to the Group from the difference between the estimated future on-going contributions and the full future cost of service for the active members. In contrast, the group is able to access the surplus of SASPS and M&GGPS. Therefore, the amounts recognised for these schemes are the IAS 19 valuation amount (either a surplus or deficit).

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

	2017 £m					2016 £m				
	PSPS note (i)	**SASPS** note (ii)	**M&GGPS**	**Other schemes**	**Total**	**PSPS** note (i)	**SASPS** note (ii)	**M&GGPS**	**Other schemes**	**Total**
Underlying economic surplus (deficit)	**721**	**(137)**	**109**	**(1)**	**692**	717	(237)	84	(1)	563
Less: unrecognised surplus	**(485)**	**-**	**-**	**-**	**(485)**	(558)	-	-	-	(558)
Economic surplus (deficit) (including investment in Prudential insurance policies)[note (iii)]	**236**	**(137)**	**109**	**(1)**	**207**	159	(237)	84	(1)	5
Attributable to:										
PAC with-profits fund	**165**	**(55)**	**-**	**-**	**110**	111	(95)	-	-	16
Shareholder-backed operations	**71**	**(82)**	**109**	**(1)**	**97**	48	(142)	84	(1)	(11)
Consolidation adjustment against policyholder liabilities for investment in Prudential insurance policies	**-**	**-**	**(151)**	**-**	**(151)**	-	-	(134)	-	(134)
IAS 19 pension asset (liability) on the Group statement of financial position[note (iv)]	**236**	**(137)**	**(42)**	**(1)**	**56**	159	(237)	(50)	(1)	(129)

Notes

(i) No deficit or other funding is required for PSPS. Deficit funding, where applicable, is apportioned in the ratio of 70/30 between the PAC with-profits fund and shareholder-backed operations following detailed considerations 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.

(ii) The deficit of SASPS has been allocated 40 per cent to the PAC with-profits fund and 60 per cent to the shareholders' fund as at 31 December 2017 and 2016.

(iii) 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.

(iv) At 31 December 2017, the PSPS pension asset of £236 million (2016: £159 million) and the other schemes' pension liabilities of £180 million (2016: £288 million) are included within 'Other debtors' and 'Provisions' respectively on the consolidated statement of financial position.

Triennial actuarial valuations
Defined benefit pension 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 actuarial valuation differs from the IAS 19 accounting basis valuation in a number of respects, including the discount rate assumption where IAS 19 prescribes a rate based on high quality corporate bonds while a more 'prudent' assumption is used for the actuarial valuation.

The information on the latest completed actuarial valuation for the UK schemes is shown in the table below:

	PSPS	SASPS	M&GGPS
Last completed actuarial valuation date	5 April 2014*	31 March 2017	31 December 2014*
Valuation actuary, all Fellows of the Institute and Faculty of Actuaries	C G Singer Towers Watson Limited	Jonathan Seed Xafinity Consulting	Paul Belok AON Hewitt Limited
Funding level at the last valuation	107 per cent	75 per cent	99 per cent
Deficit funding arrangement agreed with the Trustees based on the last completed valuation	No deficit or other funding required. Ongoing contributions for active members are at the minimum level required under the scheme rules (approximately £6 million per annum excluding expenses)	Deficit funding of £26 million per annum from 1 April 2017 until 31 March 2027, or earlier if the scheme's funding level reaches 100 per cent before this date. The deficit funding will be reviewed every three years at subsequent valuations	No deficit funding required from 1 January 2016

*The triennial valuations for PSPS and M&GGPS as at 5 April 2017 and 31 December 2017 respectively are currently in progress.

(b) Assumptions
The actuarial assumptions used in determining benefit obligations and the net periodic benefit costs for the years ended 31 December were as follows:

	2017 %	2016 %
Discount rate*	**2.5**	2.6
Rate of increase in salaries	**3.1**	3.2
Rate of inflation**		
Retail prices index (RPI)	**3.1**	3.2
Consumer prices index (CPI)	**2.1**	2.2
Rate of increase of pensions in payment for inflation:		
PSPS:		
Guaranteed (maximum 5%)	**2.5**	2.5
Guaranteed (maximum 2.5%)	**2.5**	2.5
Discretionary	**2.5**	2.5
Other schemes	**3.1**	3.2

* 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 UK RPI or CPI depending on the tranche of the schemes.

The calculations are based on current mortality estimates with an allowance made for future improvements in mortality. This allowance reflected the CMI's 2014 mortality improvements model, with scheme-specific calibrations. For immediate annuities in payment, in 2017 and 2016, a long-term mortality improvement rate of 1.75 per cent per annum and 1.25 per cent per annum was applied for males and females, respectively.

(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 31 December 2017, M&GGPS held investments in Prudential insurance policies of £151 million (2016: £134 million).

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

	2017 £m				
	Surplus (deficit) in schemes at 1 Jan 2017	**(Charge) credit to income statement**	**Actuarial gains and losses in other comprehensive income**	**Contributions paid**	**Surplus (deficit) in schemes at 31 Dec 2017**
All schemes					
Underlying position (without the effect of IFRIC 14)					
Surplus (deficit)	**563**	**(40)**	**119**	**50**	**692**
Less: amount attributable to PAC with-profits fund	**(425)**	**10**	**(39)**	**(19)**	**(473)**
Shareholders' share:					
Gross of tax surplus (deficit)	**138**	**(30)**	**80**	**31**	**219**
Related tax	**(27)**	**6**	**(15)**	**(6)**	**(42)**
Net of shareholders' tax	**111**	**(24)**	**65**	**25**	**177**
Application of IFRIC 14 for the derecognition of PSPS surplus					
Derecognition of surplus	**(558)**	**(14)**	**87**	**-**	**(485)**
Less: amount attributable to PAC with-profits fund	**409**	**10**	**(56)**	**-**	**363**
Shareholders' share:					
Gross of tax	**(149)**	**(4)**	**31**	**-**	**(122)**
Related tax	**29**	**-**	**(6)**	**-**	**23**
Net of shareholders' tax	**(120)**	**(4)**	**25**	**-**	**(99)**
With the effect of IFRIC 14					
Surplus (deficit)	**5**	**(54)**	**206**	**50**	**207**
Less: amount attributable to PAC with-profits fund	**(16)**	**20**	**(95)**	**(19)**	**(110)**
Shareholders' share:					
Gross of tax surplus (deficit)	**(11)**	**(34)**	**111**	**31**	**97**
Related tax	**2**	**6**	**(21)**	**(6)**	**(19)**
Net of shareholders' tax	**(9)**	**(28)**	**90**	**25**	**78**

Underlying investments 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’ assets at 31 December comprise the following investments:

	2017				**2016**			
	PSPS £m	**Other schemes £m**	**Total £m**	**%**	**PSPS £m**	**Other schemes £m**	**Total £m**	**%**
Equities								
UK	**9**	**67**	**76**	**1**	18	85	103	1
Overseas	**226**	**272**	**498**	**6**	293	368	661	7
Bonds*								
Government	**5,040**	**655**	**5,695**	**63**	5,411	550	5,961	66
Corporate	**1,491**	**248**	**1,739**	**20**	1,169	196	1,365	15
Asset-backed securities	**164**	**-**	**164**	**2**	144	6	150	2
Derivatives	**188**	**(6)**	**182**	**2**	252	(2)	250	3
Properties	**140**	**130**	**270**	**3**	71	109	180	2
Other assets	**216**	**77**	**293**	**3**	269	67	336	4
Total value of assets	**7,474**	**1,443**	**8,917**	**100**	7,627	1,379	9,006	100

(d)Sensitivity of the pension scheme liabilities to key variables

The sensitivity information below is based on the core scheme liabilities and assumptions at the balance sheet date. The sensitivities are calculated based on a change in one assumption with all other assumptions being held constant. As such, interdependencies between the assumptions are excluded. The impact of the rate of inflation assumption sensitivity includes the impact of inflation on the rate of increase in salaries and rate of increase of pensions in payment.

The sensitivities of the underlying pension scheme liabilities as shown below do not directly equate to the impact on the profit or loss attributable to shareholders or shareholders' equity due to the effect of the application of IFRIC 14 on PSPS and the allocation of a share of the interest in the financial position of PSPS and SASPS to the PAC with-profits fund as described above.

	Assumption applied		**Sensitivity change in assumption**	**Impact of sensitivity on scheme liabilities on IAS 19 basis**		
	2017	**2016**			**2017**	**2016**
Discount rate	**2.5%**	2.6%	**Decrease by 0.2%**	**Increase in scheme liabilities by:**		
				PSPS	**3.5%**	3.5%
				Other schemes	**5.4%**	5.3%
Discount rate	**2.5%**	2.6%	**Increase by 0.2%**	**Decrease in scheme liabilities by:**		
				PSPS	**3.4%**	3.5%
				Other schemes	**4.9%**	5.0%
Rate of inflation	**3.1%**	3.2%	**RPI: Decrease by 0.2%**	**Decrease in scheme liabilities by:**		
	2.1%	2.2%	**CPI: Decrease by 0.2% with consequent reduction in salary increases**	**PSPS**	**0.6%**	0.6%
				Other schemes	**3.9%**	4.1%
Mortality rate			**Increase life expectancy by 1 year**	**Increase in scheme liabilities by:**		
				PSPS	**4.0%**	3.5%
				Other schemes	**3.8%**	3.7%

C10 Share capital, share premium and own shares

Issued shares of 5p each fully paid	2017 Number of ordinary shares	2017 Share capital £m	2017 Share premium £m	2016 Number of ordinary shares	2016 Share capital £m	2016 Share premium £m
At 1 January	**2,581,061,573**	**129**	**1,927**	2,572,454,958	128	1,915
Shares issued under share-based schemes	**6,113,872**	**-**	**21**	8,606,615	1	12
At 31 December	**2,587,175,445**	**129**	**1,948**	2,581,061,573	129	1,927

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 31 December 2017, 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
31 December 2017	**6,448,853**	**629p**	**1,455p**	**2023**
31 December 2016	7,068,884	466p	1,155p	2022

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 £250 million as at 31 December 2017 (2016: £226 million) is deducted from retained earnings. The Company has established trusts to facilitate the delivery of shares under employee incentive plans. At 31 December 2017, 11.4 million (2016: 10.7 million) Prudential plc shares with a market value of £218 million (2016: £175 million) were held in such trusts all of which are for employee incentive plans. The maximum number of shares held during 2017 was 15.1 million which was in March 2017.

The Company purchased the following number of shares in respect of employee incentive plans. The shares purchased each month are as follows:

	2017 Number of shares	2017 Share price Low £	2017 Share price High £	2017 Cost £	2016 Number of shares	2016 Share price Low £	2016 Share price High £	2016 Cost £
January	**62,388**	**15.83**	**16.02**	**989,583**	67,625	13.73	14.00	932,711
February	**65,706**	**15.70**	**16.09**	**1,052,657**	79,077	11.96	12.01	947,993
March	**70,139**	**16.40**	**16.54**	**1,159,950**	735,361	13.09	13.72	9,686,101
April	**3,090,167**	**16.58**	**16.80**	**51,369,760**	84,848	12.91	13.31	1,115,919
May	**55,744**	**17.50**	**17.62**	**979,645**	2,272,344	13.17	13.31	30,238,832
June	**182,780**	**17.52**	**18.00**	**3,269,447**	576,386	11.28	13.09	6,604,231
July	**51,984**	**17.72**	**17.93**	**927,452**	84,883	11.96	12.32	1,040,732
August	**55,857**	**18.30**	**18.73**	**1,025,802**	73,602	14.01	14.25	1,040,528
September	**51,226**	**17.45**	**17.97**	**912,151**	173,166	13.69	14.14	2,372,037
October	**136,563**	**17.99**	**18.22**	**2,483,879**	71,253	14.37	14.50	1,026,260
November	**53,951**	**18.38**	**18.40**	**992,123**	69,976	13.49	15.40	1,044,194
December	**53,519**	**18.26**	**18.47**	**986,000**	71,626	15.76	16.37	1,134,181
Total	**3,930,024**			**66,148,449**	4,360,147			57,183,719

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 31 December 2017 was 6.4 million (2016: 6.0 million) and the cost of acquiring these shares of £71 million (2016: £61 million) is included in the cost of own shares. The market value of these shares as at 31 December 2017 was £121 million (2016: £97 million). During 2017, these funds made net acquisitions of 372,029 Prudential shares (2016: net disposals of 77,423) for a net increase of £9.4 million to book cost (2016: net increase of £7.9 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 2017 or 2016.

D Other notes

D1 Disposal of businesses

On 18 May 2017, the Group announced that it had completed the sale of its life insurance subsidiary in Korea, PCA Life Insurance Co. Ltd. to Mirae Asset Life Insurance Co. Ltd., following regulatory approvals. The transaction, announced on 10 November 2016, was for a consideration of KRW170 billion (equivalent to £117 million at 17 May 2017 closing rate).The proceeds, net of £9 million of related expenses, were £108 million.

On completion of the sale the cumulative foreign exchange translation gain of the Korea life business of £61 million, that had arisen from 2004 (the year of the Group's conversion to IFRS) to disposal was recycled from other comprehensive income through the profit and loss account in 2017 as required by IAS 21. The adjustment has no net effect on shareholders' equity. The net contribution from the Korea life business to the 2017 profit after tax is the £61 million gain arising from the recycling of foreign exchange translation gains previously recognised in other comprehensive income and other elements in various line items of £5 million.

The 2016 income statement recorded a charge for remeasurement of Korea life business classified as held for sale of £(238) million. For 2016 the result for the year, including short-term fluctuations in investment returns, together with the adjustment to the carrying value gave rise to an aggregate loss of £(227) million. To facilitate comparisons of businesses retained by the Group, the supplementary analysis of profit shown in note B1.1 shows separately the results of the Korea life business.

On 15 August 2017, the Group, through its subsidiary National Planning Holdings, Inc. (NPH) sold its US independent broker-dealer network to LPL Financial LLC. The initial consideration received was £252 million (US$325 million) resulting in a profit on disposal of £162 million (US$209 million) before tax and after costs and net losses that have been incurred in the year.

D2 Contingencies and related obligations

Litigation and regulatory matters

In addition to the matters set out in note B3(c) in relation to the Financial Conduct Authority review of past annuity sales, the Group is involved in various litigation and regulatory issues. These may from time to time include class actions involving Jackson. While the outcome of such litigation and regulatory issues cannot be predicted with certainty, the Company believes that their ultimate outcome will not have a material adverse effect on the Group's financial condition, results of operations, or cash flows.

D3 Post balance sheet events

Dividends

The second interim ordinary dividend for the year ended 31 December 2017, that was approved by the Board of Directors after 31 December 2017 is described in note B6.

Intention to demerge the Group's UK businesses

In March 2018, the Group announced its intention to demerge its UK & Europe business ('M&G Prudential') from Prudential plc, resulting in two separately-listed companies. In preparation for the UK demerger process, Prudential plc intends to transfer the legal ownership of its Hong Kong insurance subsidiaries from The Prudential Assurance Company Limited (M&G Prudential's UK regulated insurance entity) to Prudential Corporation Asia Limited, which is expected to complete by the end of 2019.

Sale of £12.0 billion* UK annuity portfolio

In March 2018, M&G Prudential also announced the sale of £12.0 billion* of its shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, M&G Prudential has reinsured £12.0 billion* of liabilities to Rothesay Life, which is expected to be followed by a Part VII transfer of the portfolio by the end of 2019. Further details are set out in the CFO Report.

* Relates to £12.0 billion of IFRS shareholder annuity liabilities, valued as at 31 December 2017.

Additional Unaudited Financial Information

I(a) 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:

– **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.

– **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.

– **With-profits** business represents the gross of tax shareholders' transfer from the with-profits fund for the year.

– **Insurance margin** primarily represents profits derived from the insurance risks of mortality and morbidity.

– **Margin on revenues** primarily represents amounts deducted from premiums to cover acquisition costs and administration expenses.

– **Acquisition costs and administration expenses** represent expenses incurred in the year 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 sources of earnings lines (eg investment expenses are netted against investment income as part of spread income or fee income as appropriate).

– **DAC adjustments** comprise DAC amortisation for the year, 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 and margin analysis of Group long-term insurance business

The following analysis expresses certain of the Group's sources of operating profit as a margin of policyholder liabilities or other relevant drivers. Details on the calculation of the Group's average policyholder liability balances are given in note (iv) at the end of this section.

	2017 £m					
	Asia	**US**	**UK and Europe**	**Total**	**Average liability** note (iv)	**Total bps** note (ii)
Spread income	**220**	**751**	**137**	**1,108**	**88,908**	**125**
Fee income	**199**	**2,343**	**61**	**2,603**	**166,839**	**156**
With-profits	**59**	**-**	**288**	**347**	**136,474**	**25**
Insurance margin	**1,310**	**906**	**55**	**2,271**		
Margin on revenues	**2,097**	**-**	**189**	**2,286**		
Expenses:						
Acquisition costs[note (i)]	**(1,489)**	**(876)**	**(68)**	**(2,433)**	**6,958**	**(35)%**
Administration expenses	**(959)**	**(1,174)**	**(164)**	**(2,297)**	**261,114**	**(88)**
DAC adjustments[note (v)]	**241**	**260**	**4**	**505**		
Expected return on shareholder assets	**121**	**4**	**104**	**229**		
	1,799	**2,214**	**606**	**4,619**		
Longevity reinsurance and other management actions to improve solvency			**276**	**276**		
Changes in longevity assumption basis			**204**	**204**		
Provision for review of past annuity sales			**(225)**	**(225)**		
Long-term business operating profit based on longer-term investment returns	**1,799**	**2,214**	**861**	**4,874**		

See notes at the end of this section.

	2016 AER £m					
	Asia	**US**	**UK and Europe**	**Total**	**Average liability** note (iv)	**Total bps** note(ii)
Spread income	192	802	177	1,171	83,054	141
Fee income	174	1,942	59	2,175	139,451	156
With-profits	48	-	269	317	118,334	27
Insurance margin	1,040	888	63	1,991		
Margin on revenues	1,919	-	207	2,126		
Expenses:						
Acquisition costs[note (i)]	(1,285)	(877)	(89)	(2,251)	6,320	(36)%
Administration expenses	(832)	(959)	(152)	(1,943)	229,477	(85)
DAC adjustments[note (v)]	148	244	(2)	390		
Expected return on shareholder assets	99	12	110	221		
	1,503	2,052	642	4,197		
Longevity reinsurance and other management actions to improve solvency			332	332		
Provision for review of past annuity sales			(175)	(175)		
Long-term business operating profit based on longer-term investment returns	1,503	2,052	799	4,354		

See notes at the end of this section.

	2016 CER £m note (iii)					
	Asia	**US**	**UK and Europe**	**Total**	**Average liability** note (iv)	**Total bps** note (ii)
Spread income	201	837	177	1,215	85,266	142
Fee income	181	2,040	59	2,280	145,826	156
With-profits	50	-	269	319	119,170	27
Insurance margin	1,087	933	63	2,083		
Margin on revenues	2,004	-	207	2,211		
Expenses:						
Acquisition costs[note (i)]	(1,343)	(921)	(89)	(2,353)	6,574	(36)%
Administration expenses	(866)	(1,007)	(152)	(2,025)	238,392	(85)
DAC adjustments[note (v)]	153	260	(2)	411		
Expected return on shareholder assets	104	13	110	227		
	1,571	2,155	642	4,368		
Longevity reinsurance and other management actions to improve solvency			332	332		
Provision for review of past annuity sales			(175)	(175)		
Long-term business operating profit based on longer-term investment returns	1,571	2,155	799	4,525		

See notes at the end of this section.

Margin analysis of long-term insurance business – Asia

	Asia								
	2017			**2016 AER**			**2016 CER** note (iii)		
	Profit	**Average liability** note (iv)	**Margin** note (ii)	**Profit**	**Average liability** note (iv)	**Margin** note (ii)	**Profit**	**Average liability** note (iv)	**Margin** note (ii)
Long-term business	**£m**	**£m**	**bps**	**£m**	**£m**	**bps**	**£m**	**£m**	**bps**
Spread income	**220**	**16,359**	**134**	192	13,299	144	201	13,980	144
Fee income	**199**	**18,767**	**106**	174	15,643	111	181	16,475	110
With-profits	**59**	**30,115**	**20**	48	22,823	21	50	23,659	21
Insurance margin	**1,310**			1,040			1,087		
Margin on revenues	**2,097**			1,919			2,004		
Expenses:									
Acquisition costs[note (i)]	**(1,489)**	**3,805**	**(39)%**	(1,285)	3,599	(36)%	(1,343)	3,773	(36)%
Administration expenses	**(959)**	**35,126**	**(273)**	(832)	28,942	(287)	(866)	30,455	(284)
DAC adjustments[note (v)]	**241**			148			153		
Expected return on shareholder assets	**121**			99			104		
Operating profit based on longer-term investment return	**1,799**			1,503			1,571		

See notes at the end of this section.

Analysis of Asia operating profit drivers:

– Spread income has increased on a constant exchange rate basis by 9 per cent (AER: 15 per cent) to £220 million in 2017, predominantly reflecting the growth of the Asia non-linked policyholder liabilities.
– Fee income has increased by 10 per cent at constant exchange rates (AER: 14 per cent) to £199 million in 2017, broadly in line with the increase in movement in average unit-linked liabilities.
– Insurance margin has increased by 21 per cent to £1,310 million in 2017 on a constant exchange rate basis (AER: 26 per cent), primarily reflecting the continued growth of the in-force book, which contains a relatively high proportion of risk-based products.
– Margin on revenues has increased by £93 million on a constant exchange rate basis from £2,004 million in 2016 to £2,097 million in 2017, primarily reflecting growth of the in-force book and higher regular premium income recognised in the year.
– Acquisition costs have increased by 11 per cent at constant exchange rates (AER: 16 per cent) to £1,489 million, compared to the 1 per cent increase in APE sales, resulting in an increase 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 66 per cent (2016: 70 per cent at CER), the decrease being the result of product and country mix.
– Administration expenses including renewal commissions have increased by 11 per cent at a constant exchange rate basis (AER: 15 per cent increase) in 2017 as the business continues to expand. On a constant exchange rate basis, the administration expense ratio has decreased from 284 basis points in 2016 to 273 basis points in 2017, the result of changes in country and product mix.

Margin analysis of long-term insurance business – US

	US								
	2017			2016 AER			2016 CER note (iii)		
	Profit	Average liability note (iv)	Margin note (ii)	Profit	Average liability note (iv)	Margin note (ii)	Profit	Average liability note (iv)	Margin note (ii)
Long-term business	£m	£m	bps	£m	£m	bps	£m	£m	bps
Spread income	**751**	**38,918**	**193**	802	37,044	217	837	38,575	217
Fee income	**2,343**	**125,440**	**187**	1,942	102,027	190	2,040	107,570	190
Insurance margin	**906**			888			933		
Expenses									
Acquisition costs[note (i)]	**(876)**	**1,662**	**(53)%**	(877)	1,561	(56)%	(921)	1,641	(56)%
Administration expenses	**(1,174)**	**169,725**	**(69)**	(959)	146,043	(66)	(1,007)	153,445	(66)
DAC adjustments	**260**			244			260		
Expected return on shareholder assets	**4**			12			13		
Operating profit based on longer-term investment returns	**2,214**			2,052			2,155		

See notes at the end of this section.

***Analysis of US operating profit drivers*:**

– Spread income has decreased by 10 per cent at constant exchange rates (AER: decreased by 6 per cent) to £751 million during 2017. The reported spread margin decreased to 193 basis points from 217 basis points in 2016, due to lower yields in the investment portfolio. Spread income benefited from swap transactions previously entered into so that asset and liability duration can be more closely matched. Excluding this effect, the spread margin would have been 144 basis points (2016 CER: 152 basis points and AER: 153 basis points).

– Fee income has increased by 15 per cent at constant exchange rates (AER: increased by 21 per cent) to £2,343 million during 2017, primarily due to higher average separate account balances due to positive net flows from variable annuity business and market appreciation during the year.

– Insurance margin represents operating profits from insurance risks, including variable annuity guarantees and other sundry items. Insurance margin decreased to £906 million in 2017 from £933 million in 2016 on a constant exchange rate basis, with higher income from the variable annuity guarantees being more than offset by a decline in the contribution from the closed books of business.

– Acquisition costs, which are commissions and expenses incurred to acquire new business, including those that are not deferrable, have decreased by 5 per cent at a constant exchange rate basis, largely due to the continued increase in producers selecting asset based commissions, which are paid upon policy anniversary dates and are treated as an administration expense in this analysis, rather than front end commissions.

– Administration expenses increased to £1,174 million during 2017, compared to £1,007 million for 2016 at a constant exchange rate (AER: £959 million), primarily as a result of higher asset based commissions. Excluding these asset based commissions, the resulting administration expense ratio was relatively flat at 35 basis points (2016: 34 basis points at CER and AER).

Analysis of pre-tax operating profit before and after acquisition costs and DAC adjustments

	2017 £m				2016 AER £m				2016 CER £m note (iii)			
		Acquisition costs				Acquisition costs				Acquisition costs		
	Other operating profits	Incurred	Deferred	Total	Other operating profits	Incurred	Deferred	Total	Other operating profits	Incurred	Deferred	Total
Total operating profit before acquisition costs and DAC adjustments	**2,830**			**2,830**	2,685			2,685	2,816			2,816
Less new business strain		**(876)**	**663**	**(213)**		(877)	678	(199)		(921)	716	(205)
Other DAC adjustments - amortisation of previously deferred acquisition costs:												
Normal			**(489)**	**(489)**			(527)	(527)			(554)	(554)
(Accelerated)/Decelerated			**86**	**86**			93	93			98	98
Total	**2,830**	**(876)**	**260**	**2,214**	2,685	(877)	244	2,052	2,816	(921)	260	2,155

Analysis of operating profit based on longer-term investment returns for US operations by product

	2017 £m	2016 £m		%	
		AER	CER	2017 vs 2016 AER	2017 vs 2016 CER
Spread business[note (a)]	**317**	323	339	(2)%	(6)%
Fee business[note (b)]	**1,788**	1,523	1,601	17%	12%
Life and other business[note (c)]	**109**	206	216	(47)%	(50)%
Total insurance operations	**2,214**	2,052	2,156	8%	3%
US asset management and broker-dealer	**10**	(4)	(4)	350%	350%
Total US operations	**2,224**	2,048	2,152	9%	3%

The analysis of operating profit based on longer-term investment returns for US operations by product represents the net profit generated by each line of business after allocation of costs. Broadly:

a) Spread business is the net operating profit for fixed annuity, fixed indexed annuity and guaranteed investment contracts and largely comprises spread income less costs.

b) Fee business represents profits from variable annuity products. As well as fee income, revenue for this product line includes spread income from investments directed to the general account and other variable annuity fees included in insurance margin.

c) Life and other business includes the profits from the REALIC business and other closed life books. Revenue allocated to this product line includes spread income and premiums and policy charges for life protection, which are included in insurance margin after claim costs. Insurance margin forms the vast majority of revenue.

Margin analysis of long-term insurance business – UK and Europe

	UK and Europe					
	2017			2016		
Long-term business	Profit £m	Average liability note (iv) £m	Margin note (ii) bps	Profit £m	Average liability note (iv) £m	Margin note (ii) bps
Spread income	**137**	**33,631**	**41**	177	32,711	54
Fee income	**61**	**22,632**	**27**	59	21,781	27
With-profits	**288**	**106,359**	**27**	269	95,511	28
Insurance margin	**55**			63		
Margin on revenues	**189**			207		
Expenses:						
Acquisition costs[note (i)]	**(68)**	**1,491**	**(5)%**	(89)	1,160	(8)%
Administration expenses	**(164)**	**56,263**	**(29)**	(152)	54,492	(28)
DAC adjustments	**4**			(2)		
Expected return on shareholder assets	**104**			110		
	606			642		
Longevity reinsurance and other management actions to improve solvency	**276**			332		
Changes in longevity assumption basis	**204**			-		
Provision for review of past annuity sales	**(225)**			(175)		
Operating profit based on longer-term investment returns	**861**			799		

See notes at the end of this section.

***Analysis of UK and Europe operating profit drivers*:**

– Spread income reduced from £177 million in 2016 to £137 million in 2017, mainly due to lower annuity sales. Spread income has two components:
  - A contribution from new annuity business which was lower at £9 million in 2017 compared to £41 million in 2016, reflecting our effective withdrawal from this market.
  - A contribution from in-force annuity and other business, which was broadly in line with last year at £128 million (2016: £136 million), equivalent to 38 basis points of average reserves (2016: 42 basis points).

– Fee income principally represents asset management fees from unit-linked business, including direct investment only business to group pension schemes, where liability flows are driven by a small number of large single mandate transactions and fee income mostly arises within our UK asset management business. Excluding these schemes, the fee margin on the remaining balances was 39 bps (2016: 40 bps).

– Margin on revenues represents premium charges for expenses of shareholder-backed business and other sundry net income.

– Acquisition costs decreased from £89 million in 2016 to £68 million in 2017, equivalent to 5 per cent of total APE sales in 2017 (2016: 8 per cent). 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-profits business in the year. Acquisition costs expressed as a percentage of shareholder-backed APE sales remained broadly consistent at 38 per cent (2016: 37 per cent).

– The contribution from longevity reinsurance and other management actions to improve solvency during 2017 was £276 million (2016: £332 million). Further explanation and analysis is provided in Additional Unaudited IFRS Financial Information section I(d).

- The £204 million favourable longevity assumption changes reflect the adoption of the Continuous Mortality Investigation 2015 model. Further information on changes to mortality assumptions is given in C4.1 (d).
- The 2017 increase in the provision for the cost of undertaking a review of past non-advised annuity sales and related potential redress of £225 million (2016: £175 million) is explained in note B4(b).

Notes to sources of earnings tables

(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 year as a proportion of the relevant class of policyholder liabilities excluding unallocated surplus.

(iii) The 2016 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 year results using the current year foreign exchange rates. All CER profit figures have been translated at current year average rates. For Asia CER average liability calculations, the policyholder liabilities have been translated using current year opening and closing exchange rates. For the US CER average liability calculations, the policyholder liabilities have been translated at the current year month end closing exchange rates. See also note A1.

(iv) For UK and Europe and Asia, opening and closing policyholder liabilities have been used to derive an average balance for the year, as a proxy for average balances throughout the year. The calculation of average liabilities for Jackson is generally derived from month end balances throughout the year, as opposed to opening and closing balances only. The average liabilities for fee income in Jackson have been calculated using daily balances instead of month end balances in order to provide a more meaningful analysis of the fee income, which is charged on the daily account balance. Average liabilities for spread income are based on the general account liabilities to which spread income attaches. Average liabilities used to calculate the administration expense margin exclude the REALIC liabilities reinsured to third parties prior to the acquisition by Jackson. Average liabilities are adjusted for business acquisitions and disposals in the year.

(v) The DAC adjustments contain a credit of £43 million in respect of joint ventures and an associate in 2017 (2016: AER credit of £28 million).

I(b) Asia operations – analysis of IFRS operating profit by business unit

Operating profit based on longer-term investment returns for Asia operations is analysed as follows:

	2017 £m	AER 2016 £m	CER 2016 £m	2016 AER vs 2017	2016 CER vs 2017
Hong Kong	**346**	238	250	45%	38%
Indonesia	**457**	428	447	7%	2%
Malaysia	**171**	147	149	16%	15%
Philippines	**41**	38	37	8%	11%
Singapore	**272**	235	247	16%	10%
Thailand	**107**	92	100	16%	7%
Vietnam	**135**	114	117	18%	15%
South-east Asia Operations including Hong Kong	**1,529**	1,292	1,347	18%	14%
China	**91**	64	66	42%	38%
Taiwan	**43**	35	39	23%	10%
Other	**64**	49	53	31%	21%
Non-recurrent items note (ii)	**75**	67	70	12%	7%
Total insurance operations note (i)	**1,802**	1,507	1,575	20%	14%
Development expenses	**(3)**	(4)	(4)	25%	25%
Total long-term business operating profit	**1,799**	1,503	1,571	20%	15%
Asset management (Eastspring Investments)	**176**	141	149	25%	18%
Total Asia operations note (iii)	**1,975**	1,644	1,720	20%	15%

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:

	2017 £m	2016 £m AER	2016 £m CER
New business*	**16**	(29)	(30)
Business in force	**1,711**	1,469	1,535
Non-recurrent items note (ii)	**75**	67	70
Total	**1,802**	1,507	1,575

* The IFRS new business result corresponds to approximately 0.4 per cent of new business APE premiums for 2017 (2016: approximately (0.8) per cent of new business APE).

The new business result reflects the aggregate of the pre-tax regulatory basis result to net worth after IFRS adjustments for deferral of acquisition costs and deferred income where appropriate.

(ii) In 2017, the IFRS operating profit based on longer-term investment returns for Asia insurance operations included a net credit of £75 million (2016: £67 million) representing a small number of individually minor items.

I(c) Analysis of asset management operating profit based on longer-term investment returns

	2017 £m	
	M&G Prudential asset management note (ii)	**Eastspring Investments** note (ii)
Operating income before performance-related fees	**1,034**	**421**
Performance-related fees	**53**	**17**
Operating income (net of commission)[note (i)]	**1,087**	**438**
Operating expense[note (i)]	**(602)**	**(238)**
Share of associate's results	**15**	**-**
Group's share of tax on joint ventures' operating profit	**-**	**(24)**
Operating profit based on longer-term investment returns	**500**	**176**
Average funds under management	**£275.9bn**	**£128.4bn**
Margin based on operating income*	**37bps**	**33bps**
Cost/income ratio**	**58%**	**56%**

	2016 £m	
	M&G Prudential asset management note (ii)	**Eastspring Investments** note (ii)
Operating income before performance-related fees	923	353
Performance-related fees	33	7
Operating income (net of commission)[note (i)]	956	360
Operating expense[note (i)]	(544)	(198)
Share of associate's results	13	-
Group's share of tax on joint ventures' operating profit	-	(21)
Operating profit based on longer-term investment returns	425	141
Average funds under management	£250.4bn	£109.0bn
Margin based on operating income*	37bps	32bps
Cost/income ratio**	59%	56%

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 the IFRS financial statements, these amounts are netted and tax deducted and shown as a single amount.

(ii) M&G Prudential asset management and Eastspring Investments can be further analysed as follows:

M&G Prudential asset management						
Operating income before performance related fees						
	Retail £m	**Margin of FUM* bps**	**Institu-tional† £m**	**Margin of FUM* bps**	**Total £m**	**Margin of FUM* bps**
2017	**604**	**85**	**430**	**21**	**1,034**	**37**
2016	504	86	419	22	923	37

Eastspring Investments						
Operating income before performance related fees						
	Retail £m	**Margin of FUM* bps**	**Institu-tional† £m**	**Margin of FUM* bps**	**Total £m**	**Margin of FUM* bps**
2017	**249**	**57**	**172**	**20**	**421**	**33**
2016	211	58	142	20	353	32

* Margin represents operating income before performance-related fees as a proportion of the related funds under management (FUM). 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 that are managed by third parties outside 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.

I(d) Contribution to UK life financial metrics from specific management actions undertaken to position the balance sheet more efficiently under the Solvency II regime

In 2017, further management actions were taken to improve the solvency of UK and Europe insurance operations and to mitigate market risks. These actions included extending the reinsurance of longevity risk to cover a further £0.5 billion of IFRS annuity liabilities. As at 31 December 2017, the total IFRS annuity liabilities subject to longevity reinsurance were £14.4 billion. Management actions also repositioned the fixed income asset portfolio to improve the trade-off between yield and credit risk.

The effect of these actions on the UK's long-term IFRS operating profit, underlying free surplus generation and EEV operating profit before restructuring costs is shown in the tables below.

IFRS operating profit of UK long-term business*

	2017 £m	2016 £m
Shareholder-backed annuity new business	**9**	41
In-force business:		
Longevity reinsurance transactions	**31**	197
Other management actions to improve solvency	**245**	135
Changes in longevity assumption basis	**204**	-
Provision for the review of past annuity sales	**(225)**	(175)
	255	157
With-profits and other in-force	**597**	601
Total	**861**	799

Underlying free surplus generation of UK long-term business*

	2017 £m	2016 £m
Expected in-force and return on net worth	**706**	693
Longevity reinsurance transactions	**15**	126
Other management actions to improve solvency	**385**	225
Changes in longevity assumption basis	**179**	-
Provision for the review of past annuity sales	**(187)**	(145)
	392	206
Changes in operating assumptions and experience variances	**(28)**	24
Underlying free surplus generated from in-force business	**1,070**	923
New business strain	**(175)**	(129)
Total	**895**	**794**

EEV post-tax operating profit of UK long-term business*

	2017 £m	2016 £m
Unwind of discount and other expected return	**465**	445
Longevity reinsurance transactions	**(6)**	(90)
Other management actions to improve solvency	**127**	110
Changes in longevity assumption basis	**195**	-
Provision for the review of past annuity sales	**(187)**	(145)
	129	(125)
Changes in operating assumptions and experience variances	**79**	55
Operating profit from in-force business	**673**	375
New business profit	**342**	268
Total	**1,015**	643

* Before restructuring costs.

II Other information

II(a) Holding company cash flow*

	2017 £m	2016 £m
Net cash remitted by business units:		
Total Asia net remittances to the Group	**645**	516
US remittances to the Group	**475**	420
UK and Europe net remittances to the Group		
With-profits remittance	**215**	215
Shareholder-backed insurance business remittance	**105**	85
Asset management remittance	**323**	290
	643	590
Other UK paid to the Group (including Prudential Capital)[4]	**25**	192
Total UK net remittances to the Group	**668**	782
Net remittances to the Group from business units[1]	**1,788**	1,718
Net interest paid	**(415)**	(333)
Tax received	**152**	132
Corporate activities	**(207)**	(215)
Total central outflows	**(470)**	(416)
Operating holding company cash flow before dividend	**1,318**	1,302
Dividend paid	**(1,159)**	(1,267)
Operating holding company cash flow after dividend*	**159**	35
Non-operating net cash flow[2]	**(511)**	335
Total holding company cash flow	**(352)**	370
Cash and short-term investments at beginning of year	**2,626**	2,173
Foreign exchange movements	**(10)**	83
Cash and short-term investments at end of year[3]	**2,264**	2,626

* The holding company cash flow differs from the IFRS cash flow statement, which includes all cash flows in the period including those relating to both policyholder and shareholder funds. The holding company cash flow is therefore a more meaningful indication of the Group's central liquidity.

1 Net cash remittances comprise dividends and other transfers from business units that are reflective of emerging earnings and capital generation.
2 Non-operating net cash flow principally relates to the repayment of subordinated debt net of the proceeds from that issued in the year, and payments for distribution rights and acquisition of subsidiaries.
3 Including central finance subsidiaries.
4 2016 remittance principally represents the outcome of actions completed in that year that facilitated access to central resources previously held at intermediary holding and other companies.

II(b) Funds under management

(a) Summary

For our asset management businesses, funds managed on behalf of third parties are not recorded on the balance sheet. They are, however, a driver of profitability. We therefore analyse the movement in the funds under management each period, focusing on those which are external to the Group and those primarily held by the insurance businesses. The table below analyses, by segment, the funds of the Group held in the statement of financial position and the external funds that are managed by Prudential's asset management operations.

	2017 £bn	2016 £bn
Business area:		
Asia operations:		
Internal funds	**81.4**	69.6
Eastspring Investments' external funds	**55.9**	45.7
	137.3	115.3
US operations - internal funds	**178.3**	173.3
M&G Prudential:		
Internal funds, including PruFund-backed products	**186.8**	174.0
External funds	**163.9**	136.8
	350.7	310.8
Other operations	**3.0**	2.9
Total funds under management[note]	**669.3**	602.3

Note

Total funds under management comprise:

	2017 £bn	2016 £bn
Total investments per the consolidated statement of financial position	**451.4**	421.7
External funds of M&G Prudential and Eastspring Investments (as analysed in note (b)1)	**219.8**	182.5
Internally managed funds held in joint ventures and other adjustments	**(1.9)**	(1.9)
Prudential Group funds under management	**669.3**	602.3

(b) Investment products – external funds under management

	2017 £m					2016 £m				
	At 1 Jan 2017	Market gross inflows	Redemptions	Market and other movements	At 31 Dec 2017	At 1 Jan 2016	Market gross inflows	Redemptions	Market and other movements	At 31 Dec 2016
M&G Prudential Wholesale/Direct	**64,209**	**30,949**	**(19,906)**	**4,445**	**79,697**	60,801	15,785	(22,038)	9,661	64,209
M&G Prudential Institutional	**72,554**	**15,220**	**(8,926)**	**5,310**	**84,158**	65,604	7,056	(8,893)	8,787	72,554
Total M&G Prudential[1]	**136,763**	**46,169**	**(28,832)**	**9,755**	**163,855**	126,405	22,841	(30,931)	18,448	136,763
Eastspring Investments	**45,756**	**215,907**	**(211,271)**	**5,493**	**55,885**	36,287	164,004	(161,766)	7,231	45,756
Total[2]	**182,519**	**262,076**	**(240,103)**	**15,248**	**219,740**	162,692	186,845	(192,697)	25,679	182,519

Notes

1 The results exclude contribution from PruFund products (net inflows of £9.0 billion in 2017; funds under management of £35.9 billion as at 31 December 2017, £24.7 billion as at 31 December 2016).

2 The £219.7 billion (2016: £182.5 billion) investment products comprise £210.4 billion (2016: £174.8 billion) plus Asia Money Market Funds of £9.3 billion (2016: £7.7 billion).

(c) M&G and Eastspring Investments – total funds under management

M&G, the asset management business of M&G Prudential and Eastspring Investments, the Group's asset management business in Asia, manage funds from external parties and also funds for the Group's insurance operations. The table below analyses the total funds under management managed by M&G and Eastspring Investments respectively.

	M&G		Eastspring Investments	
	2017 £bn	2016 £bn	2017 £bn note	2016 £bn note
External funds under management	**163.9**	136.8	**55.9**	45.7
Internal funds under management	**134.6**	128.1	**83.0**	72.2
Total funds under management	**298.5**	264.9	**138.9**	117.9

Note

The external funds under management for Eastspring Investments include Asia Money Market Funds at 31 December 2017 of £9.3 billion (2016: £7.7 billion).

II(c) Return on IFRS shareholders' funds

Return on IFRS shareholders' funds is calculated as operating profit based on longer-term investment returns net of tax and non-controlling interests divided by opening shareholders' funds. Operating profit based on longer-term investment returns is reconciled to IFRS profit before tax in note B1 to the IFRS financial statements.

	Note	**2017 £m**	**2016 £m**
Operating profit based on longer-term investment returns, net of tax and non-controlling interests	B5	**3,727**	3,362
Opening shareholders' funds		**14,666**	12,955
Return on shareholders' funds		**25%**	26%

II(d) IFRS Gearing ratio

Gearing ratio is calculated as net core structural borrowings of shareholder-financed operations divided by closing IFRS shareholders' funds plus net core structural borrowings.

	Note	**2017 £m**	**2016 £m**
Core structural borrowings of shareholder-financed operations	C6.1	**6,280**	6,798
Less holding company cash and short-term investments	II(a)	**(2,264)**	(2,626)
Net core structural borrowings of shareholder-financed operations		**4,016**	4,172
Closing shareholders' funds		**16,087**	14,666
Shareholders' funds plus net core structural borrowings		**20,103**	18,838
Gearing ratio		**20%**	22%

II(e) IFRS shareholders' funds per share

IFRS shareholders' funds per share is calculated as closing IFRS shareholders' funds divided by the number of issued shares at the balance sheet date.

	2017	**2016**
Closing shareholders' funds (£ million)	**16,087**	14,666
Number of issued shares at year end (millions)	**2,587**	2,581
Shareholders' funds per share (pence)	**622**	568

II(f) Solvency II capital position at 31 December 2017

The estimated Group shareholder Solvency II surplus at 31 December 2017 was £13.3 billion, before allowing for payment of the 2017 second interim ordinary dividend and reflects approved regulatory transitional measures as at 31 December 2017.

Estimated Group shareholder Solvency II capital position*	**31 Dec 2017 £bn**	**31 Dec 2016 £bn**
Own funds	26.4	24.8
Solvency capital requirement	13.1	12.3
Surplus	**13.3**	**12.5**
Solvency ratio	202%	201%

* The Group shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring fenced With-Profit Funds and staff pension schemes in surplus. The solvency positions include management's estimates of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.

In accordance with Solvency II requirements, these results allow for:

- Capital in Jackson in excess of 250 per cent of the US local Risk Based Capital requirement. As agreed with the Prudential Regulation Authority, this is incorporated in the result above as follows:

  - Own funds: represents Jackson's local US Risk Based available capital less 100 per cent of the US Risk Based Capital requirement (Company Action Level);
  - Solvency Capital Requirement: represents 150 per cent of Jackson's local US Risk Based Capital requirement (Company Action Level); and
  - No diversification benefits are taken into account between Jackson and the rest of the Group.

- Matching adjustment for UK annuities and volatility adjustment for US dollar denominated Hong Kong with-profits business, based on approvals from the Prudential Regulation Authority and calibrations published by the European Insurance and Occupational Pensions Authority; and

- UK transitional measures, which have been recalculated using management's estimate of the impact of operating and market conditions at the valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority and this recalculation will therefore be reflected in the formal regulatory Quantitative Reporting Templates as at 31 December 2017.

The Group shareholder Solvency II capital position excludes:

- A portion of Solvency II surplus capital (£1.7 billion at 31 December 2017) relating to the Group's Asian life operations, including due to the Solvency II definition of 'contract boundaries' which prevents some expected future cashflows from being recognised;
- The contribution to Own Funds and the Solvency Capital Requirement from ring-fenced with-profits funds in surplus (representing £4.8 billion of surplus capital from UK with-profits funds at 31 December 2017) and from the shareholders' share of the estate of with-profits funds; and
- The contribution to Own Funds and the Solvency Capital Requirement from pension funds in surplus.

It also excludes unrealised gains on certain derivative instruments taken out to protect Jackson against declines in long-term interest rates. At Jackson's request, the Department of Insurance Financial Services renewed its approval to carry these instruments at book value in the local statutory returns for the period 31 December 2017 to 1 October 2018. At 31 December 2017, this approval had the effect of decreasing local statutory capital and surplus (and by extension Solvency II Own Funds and Solvency II surplus) by £0.4 billion, net of tax. This arrangement reflects an elective longstanding practice first put in place in 2009, which can be unwound at Jackson's discretion.

The 31 December 2017 Solvency II results above allow for the completion of the sale of the Korea life business and sale of the US broker-dealer network in 2017, which contributes £0.1 billion to the Group Solvency II surplus. The results also allow for the impact of US tax reforms enacted in December 2017, which reduce the Group Solvency II surplus by £0.6 billion.

Further information on the Solvency II capital position for the Group and The Prudential Assurance Company Limited is published annually in the Solvency and Financial Condition Reports. These were last published on the Group's website on 18 May 2017.

Analysis of movement in Group capital position

A summary of the estimated movement in Group Solvency II surplus from £12.5 billion at year end 2016 to £13.3 billion at year end 2017 is set out in the table below. The movement from the Group Solvency II surplus at 31 December 2015 to the Solvency II surplus at 31 December 2016 is included for comparison.

Analysis of movement in Group shareholder surplus	**Full year 2017 £bn**	**Full year 2016 £bn**
	Surplus	**Surplus**
Estimated Solvency II surplus at beginning of period	**12.5**	**9.7**
Underlying operating experience	3.2	2.3
Management actions	0.4	0.4
Operating experience	3.6	2.7
Non-operating experience (including market movements)	(0.6)	(1.1)
Other capital movements		
Subordinated debt issuance / redemption	(0.2)	1.2
Foreign currency translation impacts	(0.7)	1.6
Dividends paid	(1.2)	(1.3)
Model changes	(0.1)	(0.3)
Estimated Solvency II surplus at end of period	**13.3**	**12.5**

The estimated movement in Group Solvency II surplus over 2017 is driven by:

- *Operating experience of £3.6 billion:* generated by in-force business and new business written in 2017, after allowing for amortisation of the UK transitional and the impact of one-off management optimisations implemented over the period;
- *Non-operating experience* of £(0.6) billion: resulting mainly from the impact of US tax reform and market movements during 2017, after allowing for the recalculation of the UK transitional at the valuation date;
- *Other capital movements:* comprising a loss from foreign currency translation, the net impact of debt raised offset by debt redeemed during 2017 and a reduction in surplus from payment of dividends; and
- *Model changes:* reflecting minor calibration changes made to the internal model during 2017.

Analysis of Group Solvency Capital Requirements

The split of the Group's estimated Solvency Capital Requirement by risk type including the capital requirements in respect of Jackson's risk exposures based on 150 per cent of US Risk Based Capital requirements (Company Action Level) but with no diversification between Jackson and the rest of the Group, is as follows:

	31 Dec 2017		**31 Dec 2016**	
Split of the Group's estimated Solvency Capital Requirements	**% of undiversified Solvency Capital Requirements**	**% of diversified Solvency Capital Requirements**	**% of undiversified Solvency Capital Requirements**	**% of diversified Solvency Capital Requirements**
Market	**57%**	**71%**	**55%**	**68%**
Equity	14%	23%	12%	19%
Credit	24%	38%	25%	41%
Yields (interest rates)	13%	7%	13%	7%
Other	6%	3%	5%	1%
Insurance	**26%**	**21%**	**28%**	**23%**
Mortality/morbidity	5%	2%	5%	2%
Lapse	14%	17%	16%	19%
Longevity	7%	2%	7%	2%
Operational/expense	**11%**	**7%**	**11%**	**7%**
FX translation	**6%**	**1%**	**6%**	**2%**

Reconciliation of IFRS equity to Group Solvency II Shareholder Own Funds

Reconciliation of IFRS equity to Group Solvency II Shareholder Own Funds	31 Dec 2017 £bn	31 Dec 2016 £bn
IFRS shareholders' equity	**16.1**	**14.7**
Restate US insurance entities from IFRS onto local US statutory basis	(3.0)	(2.2)
Remove DAC, goodwill and intangibles	(4.0)	(3.8)
Add subordinated debt	5.8	6.3
Impact of risk margin (net of transitionals)	(3.9)	(3.4)
Add value of shareholder transfers	5.3	4.0
Liability valuation differences	12.1	10.5
Increase in net deferred tax liabilities resulting from liability valuation differences above	(1.6)	(1.3)
Other	(0.4)	0.0
Estimated Solvency II Shareholder Own Funds	26.4	24.8

The key items of the reconciliation as at 31 December 2017 are:

- £3.0 billion represents the adjustment required to the Group's shareholders' funds in order to convert Jackson's contribution from an IFRS basis to the local statutory valuation basis. This item also reflects a derecognition of Own Funds of £0.8 billion, equivalent to the value of 100 per cent of Risk Based Capital requirements (Company Action Level), as agreed with the Prudential Regulation Authority;
- £4.0 billion due to the removal of DAC, goodwill and intangibles from the IFRS balance sheet;
- £5.8 billion due to the addition of subordinated debt which is treated as available capital under Solvency II but as a liability under IFRS;
- £3.9 billion due to the inclusion of a risk margin for UK and Asia non-hedgeable risks, net of £2.3 billion from transitional measures (after allowing for recalculation of the transitional measures as at 31 December 2017) which are not applicable under IFRS;
- £5.3 billion due to the inclusion of the value of future shareholder transfers from with-profits business (excluding the shareholders' share of the with-profits estate, for which no credit is given under Solvency II), which is excluded from the determination of the Group's IFRS shareholders' funds;
- £12.1 billion due to differences in insurance valuation requirements between Solvency II and IFRS, with Solvency II Own Funds partially capturing the value of in-force business which is excluded from IFRS;
- £1.6 billion due to the impact on the valuation of net deferred tax liabilities resulting from the liability valuation differences noted above; and
- £0.4 billion due to other items, including the impact of revaluing loans, borrowings and debt from IFRS to Solvency II.

Sensitivity analysis

The estimated sensitivity of the Group shareholder Solvency II capital position to significant changes in market conditions is as follows:

Impact of market sensitivities	31 Dec 2017		31 Dec 2016	
	Surplus £bn	**Ratio**	**Surplus £bn**	**Ratio**
Base position	**13.3**	**202%**	**12.5**	**201%**
Impact of:				
20% instantaneous fall in equity markets	0.7	9%	0.0	3%
40% fall in equity markets[1]	(2.1)	(11)%	(1.5)	(7)%
50 basis points reduction in interest rates[2,3]	(1.0)	(14)%	(0.6)	(9)%
100 basis points increase in interest rates[3]	1.2	21%	1.0	13%
100 basis points increase in credit spreads [4]	(1.4)	(6)%	(1.1)	(3)%

1 Where hedges are dynamic, rebalancing is allowed for by assuming an instantaneous 20 per cent fall followed by a further 20 per cent fall over a four-week period.
2 Subject to a floor of zero.
3 Allowing for further transitional recalculation after the interest rate stress.
4 US Risk Based Capital solvency position included using a stress of 10 times expected credit defaults.

The Group believes it is positioned to withstand significant deteriorations in market conditions and we continue to use market hedges to manage some of this exposure across the Group, where we believe the benefit of the protection outweighs the cost. The sensitivity analysis above allows for predetermined management actions and those taken to date, but does not reflect all possible management actions which could be taken in the future.

UK Solvency II capital position[1, 2]

On the same basis as above, the estimated shareholder Solvency II surplus for The Prudential Assurance Company Limited ('PAC') and its subsidaries[2] at 31 December 2017 was £6.1 billion, after allowing for recalculation of transitional measures as at 31 December 2017. This relates to shareholder-backed business including future with-profits shareholder transfers, but excludes the shareholders' share of the estate in line with Solvency II requirements.

Estimated UK shareholder Solvency II capital position*	**31 Dec 2017 £bn**	**31 Dec 2016 £bn**
Own funds	14.0	12.0
Solvency capital requirement	7.9	7.4
Surplus	**6.1**	**4.6**
Solvency ratio	178%	163%

* The UK shareholder capital position excludes the contribution to Own Funds and the Solvency Capital Requirement from ring-fenced With-Profit Funds and staff pension schemes in surplus. The solvency positions include management's estimate of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.

While there is a large surplus in the UK with-profits funds, this is ring-fenced from the shareholder balance sheet and is therefore excluded from both the Group and the UK shareholder Solvency II surplus results. The estimated UK with-profits funds Solvency II surplus at 31 December 2017 was £4.8 billion, after allowing for recalculation of transitional measures as at 31 December 2017.

Estimated UK with-profits Solvency II capital position*	**31 Dec 2017 £bn**	**31 Dec 2016 £bn**
Own funds	9.6	8.4
Solvency capital requirement	4.8	4.7
Surplus	**4.8**	**3.7**
Solvency ratio	201%	179%

* The solvency positions include management's estimate of UK transitional measures reflecting operating and market conditions at each valuation date. An application to recalculate the transitional measures as at 31 December 2017 has been approved by the Prudential Regulation Authority.

Reconciliation of UK with-profits IFRS unallocated surplus to Solvency II Own Funds[1]

A reconciliation between the IFRS unallocated surplus and Solvency II Own Funds for UK with-profits business is as follows:

Reconciliation of UK with-profits funds	**31 Dec 2017 £bn**	**31 Dec 2016 £bn**
IFRS unallocated surplus of UK with-profits funds	13.5	11.7
Adjustments from IFRS basis to Solvency II		
Value of shareholder transfers	(2.7)	(2.3)
Risk margin (net of transitional)	(0.7)	(0.7)
Other valuation differences	(0.5)	(0.3)
Estimated Solvency II Own Funds	**9.6**	**8.4**

Annual regulatory reporting

The group will publish its Solvency and Financial Condition Report and related quantitative templates no later than 17 June 2018. The templates will require us to combine the Group shareholder solvency position with those of all other ring-fenced funds across the Group. In combining these solvency positions, the contribution to own funds from these ring-fenced funds will be set equal to their aggregate solvency capital requirements, estimated at £6.6 billion (ie the solvency surplus in these ring-fenced funds will not be captured in the templates). There will be no impact on the reported Group Solvency II surplus.

Statement of independent review in respect of Solvency II Capital Position at 31 December 2017

The methodology, assumptions and overall result have been subject to examination by KPMG LLP.

Notes

1 The UK with-profits capital position includes the PAC with-profits sub-fund, the Scottish Amicable Insurance Fund and the Defined Charge Participating Sub-Fund.

2 The insurance subsidiaries of PAC are Prudential General Insurance Hong Kong Limited, Prudential Hong Kong Limited, Prudential International Assurance plc and Prudential Pensions Limited.

European Embedded Value (EEV) basis results

Notes on the EEV basis results

Additional EEV financial information*

<u>Description of EEV basis reporting</u>

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

The EEV basis results have been prepared in accordance with the EEV Principles dated April 2016, issued by the European Insurance CFO Forum. The EEV 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, taking into account recent experience in assessing likely future persistency, mortality, morbidity and expenses. Further details are explained in notes 14 and 15.

* The additional financial information is not covered by the KPMG LLP independent audit opinion.

European Embedded Value (EEV) Basis Results

POST-TAX OPERATING PROFIT BASED ON LONGER-TERM INVESTMENT RETURNS

	Note	**2017 £m**	2016 £m note (iii)
Asia operations			
New business	3	**2,368**	2,030
Business in force	4	**1,337**	1,044
Long-term business		**3,705**	3,074
Asset management		**155**	125
Total		**3,860**	3,199
US operations			
New business	3	**906**	790
Business in force	4	**1,237**	1,181
Long-term business		**2,143**	1,971
Asset management		**7**	(3)
Total		**2,150**	1,968
UK and Europe operations			
New business	3	**342**	268
Business in force	4	**673**	375
Long-term business		**1,015**	643
General insurance commission		**13**	23
Total insurance operations		**1,028**	666
Asset management		**403**	341
Total		**1,431**	1,007
Other income and expenditure note (i)		**(746)**	(682)
Restructuring costs note (ii)		**(97)**	(32)
Interest received from tax settlement		**-**	37
Operating profit based on longer-term investment returns		**6,598**	5,497
Analysed as profit (loss) from:			
New business	3	**3,616**	3,088
Business in force	4	**3,247**	2,600
Long-term business		**6,863**	5,688
Asset management and general insurance commission		**578**	486
Other results		**(843)**	(677)
		6,598	5,497

Notes

(i) EEV basis other income and expenditure represents the post-tax IFRS basis results for other operations (including Group and Asia Regional Head Office, holding company borrowings, Africa operations and Prudential Capital) less the unwind of expected margins on the internal management of the assets of the covered business (as explained in note 14(a)(vii)).

(ii) Restructuring costs comprise the post-tax charge recognised on an IFRS basis and the additional amount recognised on an EEV basis for the shareholders' share incurred by the PAC with-profits fund. The costs are primarily incurred in UK and Europe and Asia and represent business transformation and integration costs.

(iii) The comparative results have been prepared using previously reported average exchange rates for the year. The 2016 comparative results have been re-presented from those previously published following the reassessment of the Group's operating segments as described in note B1.3 of the IFRS financial statements. This approach has been adopted consistently throughout this supplementary information.

POST-TAX SUMMARISED CONSOLIDATED INCOME STATEMENT

	Note	**2017 £m**	2016 £m
Asia operations		**3,860**	3,199
US operations		**2,150**	1,968
UK and Europe operations		**1,431**	1,007
Other income and expenditure		**(746)**	(682)
Restructuring costs		**(97)**	(32)
Interest received from tax settlement		**-**	37
Operating profit based on longer-term investment returns		**6,598**	5,497
Short-term fluctuations in investment returns	5	**2,111**	(507)
Effect of changes in economic assumptions	6	**(102)**	(60)
Mark to market value movements on core structural borrowings		**(326)**	(4)
Impact of US tax reform	7	**390**	-
Profit (loss) attaching to disposal of businesses	17	**80**	(410)
Total non-operating profit (loss)		**2,153**	(981)
Profit for the year		**8,751**	4,516
Attributable to:			
Equity holders of the Company		**8,750**	4,516
Non-controlling interests		**1**	-
		8,751	4,516

Basic earnings per share

	2017	2016
Based on post-tax operating profit including longer-term investment returns after non-controlling interests (in pence)	**257.0p**	214.7p
Based on post-tax profit attributable to equity holders of the Company (in pence)	**340.9p**	176.4p
Weighted average number of shares (millions)	**2,567**	2,560

MOVEMENT IN SHAREHOLDERS' EQUITY

	Note	**2017 £m**	2016 £m
Profit for the year attributable to equity holders of the Company		**8,750**	4,516
Items taken directly to equity:			
Exchange movements on foreign operations and net investment hedges		**(2,045)**	4,211
External dividends		**(1,159)**	(1,267)
Mark to market value movements on Jackson assets backing surplus and required capital		**40**	(11)
Other reserve movements		**144**	(367)
Net increase in shareholders' equity	9	**5,730**	7,082
Shareholders' equity at beginning of year	9	**38,968**	31,886
Shareholders' equity at end of year	9	**44,698**	38,968

	31 Dec 2017 £m			31 Dec 2016 £m		
Comprising:	**Long-term business operations**	**Asset management and other operations**	**Group total**	Long-term business operations	Asset management and other operations	Group total
Asia operations	**21,191**	**401**	**21,592**	18,717	383	19,100
US operations	**13,257**	**235**	**13,492**	11,805	204	12,009
UK and Europe operations	**11,713**	**1,914**	**13,627**	10,320	1,845	12,165
Other operations	**-**	**(4,013)**	**(4,013)**	-	(4,306)	(4,306)
Shareholders' equity at end of year	**46,161**	**(1,463)**	**44,698**	40,842	(1,874)	38,968
Representing:						
Net assets attributable to equity holders of the Company excluding acquired goodwill, holding company net borrowings and non-controlling interests	**45,917**	**1,562**	**47,479**	40,597	948	41,545
Acquired goodwill	**244**	**1,214**	**1,458**	245	1,230	1,475
Holding company net borrowings at market value[note 8]	**-**	**(4,239)**	**(4,239)**	-	(4,052)	(4,052)
	46,161	**(1,463)**	**44,698**	40,842	(1,874)	38,968

SUMMARY STATEMENT OF FINANCIAL POSITION

	Note	**31 Dec 2017 £m**	31 Dec 2016 £m
Total assets less liabilities, before deduction for insurance funds*		**434,608**	407,928
Less insurance funds:			
Policyholder liabilities (net of reinsurers' share) and unallocated surplus of with-profits funds		**(418,521)**	(393,262)
Less shareholders' accrued interest in the long-term business	9	**28,611**	24,302
		(389,910)	(368,960)
Total net assets attributable to equity holders of the Company	9	**44,698**	38,968
Share capital		**129**	129
Share premium		**1,948**	1,927
IFRS basis shareholders' reserves		**14,010**	12,610
Total IFRS basis shareholders' equity	9	**16,087**	14,666
Additional EEV basis retained profit	9	**28,611**	24,302
Total EEV basis shareholders' equity	9	**44,698**	38,968

* Including liabilities in respect of insurance products classified as investment contracts under IFRS 4.

Net asset value per share

	31 Dec 2017	31 Dec 2016
Based on EEV basis shareholders' equity of £44,698 million (2016: £38,968 million) (in pence)	**1,728p**	1,510p
Number of issued shares at year end (millions)	**2,587**	2,581
Annualised return on embedded value*	**17%**	17%

* Annualised return on embedded value is based on EEV post-tax operating profit after non-controlling interests, as a percentage of opening EEV basis shareholders' equity.

NOTES ON THE EEV BASIS RESULTS

1 Basis of preparation

The EEV basis results have been prepared in accordance with the EEV Principles dated April 2016, issued by the European Insurance CFO Forum. Where appropriate, the EEV basis results include the effects of adoption of EU-endorsed IFRS.

The directors are responsible for the preparation of the supplementary information in accordance with the EEV Principles. The auditors have reported on the 2017 EEV basis results supplement to the Company's statutory accounts for 2017. Their report was (i) unqualified and (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report. Except for the reclassification of results to reflect the reassessment of the Group's operating segments as described in the note in B1.3 of the IFRS financial statements, the 2016 results have been derived from the EEV basis results supplement to the Company's statutory accounts for 2016. 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 2016 comparative results are shown below on both actual exchange rates (AER) and constant exchange rates (CER) bases. The 2016 CER comparative results are translated at 2017 average exchange rates.

Annual premium equivalents (APE)[note 16]

		2017 £m	2016 £m		% change	
	Note		AER	CER	AER	CER
Asia		**3,805**	3,599	3,773	6%	1%
US		**1,662**	1,561	1,641	6%	1%
UK and Europe		**1,491**	1,160	1,160	29%	29%
Group total	3	**6,958**	6,320	6,574	10%	6%

Post-tax operating profit

		2017 £m	2016 £m		% change	
	Note		AER	CER	AER	CER
Asia operations						
New business	3	**2,368**	2,030	2,123	17%	12%
Business in force	4	**1,337**	1,044	1,097	28%	22%
Long-term business		**3,705**	3,074	3,220	21%	15%
Asset management		**155**	125	132	24%	17%
Total		**3,860**	3,199	3,352	21%	15%
US operations						
New business	3	**906**	790	830	15%	9%
Business in force	4	**1,237**	1,181	1,241	5%	0%
Long-term business		**2,143**	1,971	2,071	9%	3%
Asset management		**7**	(3)	(4)	333%	275%
Total		**2,150**	1,968	2,067	9%	4%
UK and Europe operations						
New business	3	**342**	268	268	28%	28%
Business in force	4	**673**	375	375	79%	79%
Long-term business		**1,015**	643	643	58%	58%
General insurance commission		**13**	23	23	(43)%	(43)%
Total insurance operations		**1,028**	666	666	54%	54%
Asset management		**403**	341	341	18%	18%
Total		**1,431**	1,007	1,007	42%	42%
Other income and expenditure		**(746)**	(682)	(688)	(9)%	(8)%
Restructuring costs		**(97)**	(32)	(32)	(203)%	(203)%
Interest received from tax settlement		**-**	37	37	n/a	n/a
Operating profit based on longer-term investment returns		**6,598**	5,497	5,743	20%	15%
Analysed as profit (loss) from:						
New business	3	**3,616**	3,088	3,221	17%	12%
Business in force	4	**3,247**	2,600	2,713	25%	20%
Total long-term business		**6,863**	5,688	5,934	21%	16%
Asset management and general insurance commission		**578**	486	492	19%	17%
Other results		**(843)**	(677)	(683)	(25)%	(23)%
		6,598	5,497	5,743	20%	15%

Post-tax profit

	Note	2017 £m	2016 £m		% change	
			AER	CER	AER	CER
Operating profit based on longer-term investment returns		**6,598**	5,497	5,743	20%	15%
Short-term fluctuations in investment returns	5	**2,111**	(507)	(567)		
Effect of changes in economic assumptions	6	**(102)**	(60)	(54)		
Mark to market value movements on core structural borrowings		**(326)**	(4)	(4)		
Impact of US tax reform	7	**390**	-	-		
Profit (loss) attaching to disposal of businesses	17	**80**	(410)	(445)		
Total non-operating profit (loss)		**2,153**	(981)	(1,070)	319%	301%
Profit for the year		**8,751**	4,516	4,673	94%	87%

Basic earnings per share

	2017	2016		% change	
		AER	CER	AER	CER
Based on post-tax operating profit including longer-term investment returns after non-controlling interests (in pence)	**257.0p**	214.7p	224.3p	20%	15%
Based on post-tax profit attributable to equity holders of the Company (in pence)	**340.9p**	176.4p	182.5p	93%	87%

3 Analysis of new business contribution

(i) Group summary for long-term business operations

	2017				
	Annual premium equivalents (APE) £m note 16	**Present value of new business premiums (PVNBP) £m** note 16	**New business contribution £m**	**New business margin**	
				APE %	**PVNBP %**
Asia[note (ii)]	**3,805**	**20,405**	**2,368**	**62**	**11.6**
US	**1,662**	**16,622**	**906**	**55**	**5.5**
UK and Europe	**1,491**	**13,784**	**342**	**23**	**2.5**
Total	**6,958**	**50,811**	**3,616**	**52**	**7.1**

	2016				
	Annual premium equivalents (APE) £m note 16	Present value of new business premiums (PVNBP) £m note 16	New business contribution £m	New business margin	
				APE %	PVNBP %
Asia[note (ii)]	3,599	19,271	2,030	56	10.5
US	1,561	15,608	790	51	5.1
UK and Europe	1,160	10,513	268	23	2.5
Total	6,320	45,392	3,088	49	6.8

Note

After allowing for foreign exchange effects of £133 million, the new business contribution increased by £395 million on a CER basis. This increase is driven by higher sales volumes (a contribution of £188 million), a beneficial effect of changes in long-term interest rates (£48 million) and pricing, product mix and other actions of £159 million. The £159 million impact reflects the beneficial impact of our strategic emphasis on increasing sales from health and protection business in Asia, together with a positive £76 million effect arising in the US for the impact of US tax reform (see note 7).

(ii) Asia new business contribution by business unit

	2017 £m	2016 £m	
		AER	CER
China	**133**	63	65
Hong Kong	**1,535**	1,363	1,427
Indonesia	**174**	175	183
Taiwan	**57**	31	35
Other	**469**	398	413
Total Asia	**2,368**	2,030	2,123

4 Operating profit from business in force

(i) Group summary for long-term business operations

	2017 £m			
	Asia note (ii)	**US** note (iii)	**UK and Europe** note (iv)	**Group total**
Unwind of discount and other expected returns	**1,007**	**694**	**465**	**2,166**
Effect of changes in operating assumptions	**241**	**196**	**195**	**632**
Experience variances and other items	**89**	**347**	**13**	**449**
Group total	**1,337**	**1,237**	**673**	**3,247**

	2016 £m			
	Asia note (ii)	US note (iii)	UK and Europe note (iv)	Group total
Unwind of discount and other expected returns	866	583	445	1,894
Effect of changes in operating assumptions	54	170	25	249
Experience variances and other items	124	428	(95)	457
Group total	1,044	1,181	375	2,600

Note

The movement in operating profit from business in force of £647 million from £2,600 million for 2016 to £3,247 million for 2017 comprises:

		£m
Movement in unwind of discount and other expected returns:		
Effects of changes in:		
Growth in opening value	**251**	
Interest rates and other economic assumptions	**(47)**	
Foreign exchange	**68**	
		272
Movement in effect of changes in operating assumptions, experience variances and other items (including foreign exchange of £45 million)		**375**
Net movement in operating profit from business in force		**647**

(ii) Asia

	2017 £m	2016 £m
Unwind of discount and other expected returns[note (a)]	**1,007**	866
Effect of changes in operating assumptions[note (b)]	**241**	54
Experience variances and other items[note (c)]	**89**	124
Total	**1,337**	1,044

Notes

(a) The £141 million increase in unwind of discount and other expected returns to £1,007 million for 2017 is driven by the growth in the in-force book, with offsetting effects arising from foreign exchange (£38 million) and movements in long-term interest rates and changes in other economic assumptions (£(38) million).

(b) The effect of changes in operating assumptions of £241 million reflects the net benefit for EEV arising from the annual review of experience, together with the benefit of management actions reflecting our ongoing focus on managing the in-force book for value. It includes a £107 million benefit arising in China from adopting the principles for embedded value reporting under the China Risk Oriented Solvency System (C-ROSS) regime in 2017 (see note 14(a)(v)).

(c) The £89 million effect of experience variances and other items in 2017 is driven by positive mortality and morbidity experiences in a number of business units, together with positive persistency variances from participating and health and protection products, partially offset by unfavourable persistency variances on unit-linked products. Experience variances also include expense overruns where these are expected to be short-lived, including businesses that are growing rapidly or are sub-scale.

(iii) US

	2017 £m	2016 £m
Unwind of discount and other expected returns[note (a)]	**694**	583
Effect of changes in operating assumptions[note (b)]	**196**	170
Experience variances and other items:		
Spread experience variance	**71**	119
Amortisation of interest-related realised gains and losses	**91**	88
Other[note (c)]	**185**	221
	347	428
Total	**1,237**	1,181

Notes

(a) The £111 million increase in unwind of discount and other expected returns to £694 million for 2017 represents a positive £87 million effect for the growth in the in-force book (after allowing for the benefit of US tax reform) and a net £24 million effect for foreign exchange and interest rate movements.

(b) The effect of assumption changes of £196 million in 2017 mainly relates to assumption updates for persistency, mortality and policyholder utilisation.

(c) Other experience variances of £185 million in 2017 include the effects of positive mortality and persistency experience in the period, together with the benefit of tax credits relating to the dividend received deduction for variable annuity business.

(iv) UK and Europe

	2017 £m	2016 £m
Unwind of discount and other expected returns[note (a)]	**465**	445
Change in longevity assumptions basis[note (b)]	**195**	-
Reduction in corporate tax rate	**-**	25
Other items[note (c)]	**13**	(95)
Total	**673**	375

Notes

(a) The £20 million increase in unwind of discount and other expected returns to £465 million for 2017 is mainly driven by the underlying growth in the in-force book.

(b) The £195 million relates to changes to annuitant mortality assumptions primarily reflecting the adoption of the Continuous Mortality Investigation 2015 model as the basis for future mortality improvements.

(c) Other items comprise the following:

	2017 £m	2016 £m
Longevity reinsurance	**(6)**	(90)
Impact of specific management actions to improve solvency position	**127**	110
Provision for cost of undertaking past non-advised annuity sales review and potential redress[note (d)]	**(187)**	(145)
Other	**79**	30
	13	(95)

(d) In response to the findings of the FCA's Thematic Review of Annuities Sales Practices, the UK business has agreed to review all internally vesting annuities sold without advice after 1 July 2008. The FCA formally released its redress calculation methodology in early 2018 and Prudential reassessed the provision held. Reflecting this, the UK 2017 result includes a £(187) million (post-tax) increase in the provision held for the estimated cost of the review and any appropriate customer redress. The provision held continues to exclude any potential for insurance recoveries. For more information, see note B3 of the IFRS financial statements.

5 Short-term fluctuations in investment returns

Short-term fluctuations in investment returns included in profit for the year arise as follows:

(i) Group summary

	2017 £m	2016 £m
Asia operations[note (ii)]	**887**	(100)
US operations[note (iii)]	**582**	(1,102)
UK and Europe operations[note (iv)]	**621**	876
Other operations	**21**	(181)
Group total	**2,111**	(507)

(ii) Asia operations

The short-term fluctuations in investment returns for Asia operations comprise:

	2017 £m	2016 £m
Hong Kong	**531**	(105)
Singapore	**126**	52
Other	**230**	(47)
Total	**887**	(100)

Note

For 2017, the credit of £887 million mainly reflects unrealised gains on bonds driven by the decrease in bond yields across many of the business units (see note 15(i)), together with higher equity returns than assumed for Hong Kong with-profits business and higher investment returns than assumed in Singapore for with-profits and unit-linked businesses.

(iii) US operations

The short-term fluctuations in investment returns for US operations comprise:

	2017 £m	2016 £m
Investment return related experience on fixed income securities[note (a)]	**(46)**	(85)
Investment return related impact due to changed expectation of profits on in-force variable annuity business in future periods based on current year separate account return, net of related hedging activity and other items[note (b)]	**628**	(1,017)
Total	**582**	(1,102)

Notes

(a) The net result relating to fixed income securities reflects a number of offsetting items as follows:
- the impact on portfolio yields of changes in the asset portfolio in the year;
- the difference between actual realised gains and losses and the amortisation of interest-related realised gains and losses that is recorded within operating profit; and
- credit experience (versus the longer-term assumption).

(b) This item reflects the net impact of:
- changes in projected future fees and future benefit costs arising from the difference between the actual growth in separate account asset values of 17.5 per cent and that assumed of 5.9 per cent for the year (2016: actual growth of 8.9 per cent compared to assumed growth of 6.0 per cent); and
- related hedging activity arising from realised and unrealised gains and losses on equity-related hedges and interest rate options, and other items.

(iv) UK and Europe operations

The short-term fluctuations in investment returns for UK and Europe operations comprise:

	2017 £m	2016 £m
Insurance operations:		
Shareholder-backed annuity business[note (a)]	**387**	431
With-profits and other business[note (b)]	**229**	438
Asset management	**5**	7
Total	**621**	876

Notes

(a) Short-term fluctuations in investment returns for shareholder-backed annuity business include:
- gains on surplus assets compared to the expected long-term rate of return reflecting reductions in corporate bond and gilt yields; and
- the difference between actual and expected default experience.

(b) The positive £229 million fluctuation in 2017 for with-profits and other business represents the impact of achieving a 9 per cent pre-tax return on the with-profits fund (including unallocated surplus) compared to the assumed rate of return of 5 per cent for the year (2016: achieved return of 14 per cent compared to assumed rate of 5 per cent), partially offset by the effect of a partial hedge of future shareholder transfers expected to emerge from the UK's with-profits sub-fund entered into to protect future shareholder with-profit transfers from movements in the UK equity market.

6 Effect of changes in economic assumptions

The effects of changes in economic assumptions for in-force business included in the profit for the year arise as follows:

(i) Group summary for long-term business operations

	2017 £m	2016 £m
Asia[note (ii)]	**(95)**	70
US[note (iii)]	**(136)**	45
UK and Europe[note (iv)]	**129**	(175)
Group total	**(102)**	(60)

(ii) Asia

The effect of changes in economic assumptions for Asia comprises:

	2017 £m	2016 £m
Hong Kong	**(321)**	85
Indonesia	**81**	46
Malaysia	**59**	(20)
Singapore	**131**	(60)
Taiwan	**(12)**	12
Other	**(33)**	7
Total	**(95)**	70

Note

The negative effect in 2017 of £(95) million largely arises from movements in long-term interest rates, driven by lower assumed fund earned rates in Hong Kong, partially offset by profits arising from the beneficial impact of valuing future profits at lower discount rates in Indonesia, Malaysia and Singapore (see note 15(i)). In addition, various changes to the basis of setting economic assumptions were made with an overall impact of £5 million (see note 14(a)(viii), note 15(i) and note 15(iv)).

(iii) US

The effect of changes in economic assumptions for US comprises:

	2017 £m	2016 £m
Variable annuity business	**(101)**	86
Fixed annuity and other general account business	**(35)**	(41)
Total	**(136)**	45

Note

For 2017, the charge of £(136) million mainly reflects the decrease in the assumed separate account return and reinvestment rates, following the 10 basis points decrease in the US 10-year treasury yield in the year, resulting in lower projected fee income and an increase in projected benefit costs for variable annuity business. For fixed annuity and other general account business, the impact reflects the effect on the present value of future projected spread income from the combined movement in interest rates and credit spreads.

(iv) UK and Europe

The effect of changes in economic assumptions for UK and Europe comprises:

	2017 £m	2016 £m
Shareholder-backed annuity business	**28**	(113)
With-profits and other business	**101**	(62)
Total	**129**	(175)

Note

The credit of £129 million mainly reflects the movement in expected long-term rates of return and risk discount rates as shown in note 15 (iii).

7 Impact of US tax reform

On 22 December 2017, a significant US tax reform package, The Tax Cuts and Jobs Act, was enacted into law effective from 1 January 2018. The tax reform package as a whole, which includes a reduction in the corporate income tax rate from 35 per cent to 21 per cent, and a number of specific measures affecting US life insurers, results in a £390 million benefit in non-operating profit. The positive impact on an EEV basis represents the benefit of future profits being taxed at a lower rate, partially offset by a reduction in the net deferred tax asset held in the balance sheet to reflect remeasurement at the new lower tax rate, together with a reduction in the benefit from the dividend received deduction on taxable profits from variable annuity business.

In accordance with our usual methodology, the new business contribution and unwind of discount and other expected returns are determined by applying operating and economic assumptions as at the end of the year, including the effect of US tax reform. This led to an increase in new business profit of £76 million.

8 Net core structural borrowings of shareholder-financed operations

	31 Dec 2017 £m			31 Dec 2016 £m		
	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 (including central finance subsidiaries) cash and short-term investments	**(2,264)**	**-**	**(2,264)**	(2,626)	-	(2,626)
Central funds						
Subordinated debt	**5,272**	**515**	**5,787**	5,772	182	5,954
Senior debt	**549**	**167**	**716**	549	175	724
	5,821	**682**	**6,503**	6,321	357	6,678
Holding company net borrowings	**3,557**	**682**	**4,239**	3,695	357	4,052
Prudential Capital bank loan	**275**	**-**	**275**	275	-	275
Jackson surplus notes	**184**	**61**	**245**	202	65	267
Group total	**4,016**	**743**	**4,759**	4,172	422	4,594

Note

In October 2017, the Company issued core structural borrowings of US$750 million 4.875 per cent Tier 2 perpetual subordinated notes. The proceeds, net of costs, were £565 million. In December 2017, the Company repaid its US$1,000 million 6.5 per cent Tier 2 perpetual subordinated notes. The movement in IFRS basis core structural borrowings from 2016 to 2017 also includes foreign exchange effects.

9 Reconciliation of movement in shareholders' equity

	2017 £m				
	Asia operations note (i)	**US operations**	**UK and Europe operations**	**Other operations** note (i)	**Group total** note (iv)
Operating profit (based on longer-term investment returns)					
Long-term business:					
New business[note 3]	**2,368**	**906**	**342**	**-**	**3,616**
Business in force[note 4]	**1,337**	**1,237**	**673**	**-**	**3,247**
	3,705	**2,143**	**1,015**	**-**	**6,863**
Asset management and general insurance commission	**155**	**7**	**416**	**-**	**578**
Restructuring costs	**(14)**	**-**	**(73)**	**(10)**	**(97)**
Other results	**-**	**-**	**-**	**(746)**	**(746)**
Operating profit based on longer-term investment returns	**3,846**	**2,150**	**1,358**	**(756)**	**6,598**
Non-operating items	**792**	**917**	**750**	**(306)**	**2,153**
	4,638	**3,067**	**2,108**	**(1,062)**	**8,751**
Non-controlling interests	**-**	**-**	**-**	**(1)**	**(1)**
Profit for the year	**4,638**	**3,067**	**2,108**	**(1,063)**	**8,750**
Other items taken directly to equity:					
Exchange movements on foreign operations and net investment hedges	**(1,192)**	**(1,159)**	**6**	**300**	**(2,045)**
Intra-group dividends and investment in operations[note (ii)]	**(842)**	**(466)**	**(678)**	**1,986**	**-**
External dividends	**-**	**-**	**-**	**(1,159)**	**(1,159)**
Mark to market value movements on Jackson assets backing surplus and required capital	**-**	**40**	**-**	**-**	**40**
Other movements[note (iii)]	**(111)**	**1**	**26**	**228**	**144**
Net increase in shareholders' equity	**2,493**	**1,483**	**1,462**	**292**	**5,730**
Shareholders' equity at beginning of year	**18,855**	**12,009**	**12,165**	**(4,061)**	**38,968**
Shareholders' equity at end of year	**21,348**	**13,492**	**13,627**	**(3,769)**	**44,698**
Representing:					
IFRS basis shareholders' equity:					
Net assets (liabilities)	**5,620**	**5,248**	**7,092**	**(3,331)**	**14,629**
Goodwill	**61**	**-**	**1,153**	**244**	**1,458**
Total IFRS basis shareholders' equity	**5,681**	**5,248**	**8,245**	**(3,087)**	**16,087**
Additional retained profit (loss) on an EEV basis	**15,667**	**8,244**	**5,382**	**(682)**	**28,611**
EEV basis shareholders' equity	**21,348**	**13,492**	**13,627**	**(3,769)**	**44,698**
Balance at beginning of year:					
IFRS basis shareholders' equity:					
Net assets (liabilities)	5,069	5,392	6,679	(3,949)	13,191
Goodwill	61	16	1,153	245	1,475
Total IFRS basis shareholders' equity	5,130	5,408	7,832	(3,704)	14,666
Additional retained profit (loss) on an EEV basis	13,725	6,601	4,333	(357)	24,302
EEV basis shareholders' equity	18,855	12,009	12,165	(4,061)	38,968

Notes

(i) Other operations of £(3,769) million represents the shareholders' equity of £(4,013) million as shown in the movement in shareholders' equity and includes goodwill of £244 million (2016: £245 million) related to Asia long-term operations.

(ii) Intra-group dividends represent dividends that have been declared in the year and investment in operations reflect increases in share capital. The amounts included in note 11 for these items are as per the holding company cash flow at transaction rates. The difference primarily relates to intra-group loans, foreign exchange and other non-cash items.

(iii) Other movements include reserve movements in respect of the shareholders' share of actuarial gains and losses on defined benefit pension schemes, share capital subscribed, share-based payments and treasury shares and intra-group transfers between operations which have no overall effect on the Group's embedded value.

(iv) Group total EEV basis shareholders' equity can be further analysed as follows:

	31 Dec 2017 £m				31 Dec 2016 £m			
	Total long-term business operations note 10	**Asset management and general insurance commission**	**Other operations**	**Group total**	Total long-term business operations	Asset management and general insurance commission	Other operations	Group total
Total IFRS basis shareholders' equity	**16,624**	**2,550**	**(3,087)**	**16,087**	15,938	2,432	(3,704)	14,666
Additional retained profit (loss) on an EEV basis[note (v)]	**29,293**	**-**	**(682)**	**28,611**	24,659	-	(357)	24,302
Total EEV basis shareholders' equity	**45,917**	**2,550**	**(3,769)**	**44,698**	40,597	2,432	(4,061)	38,968

(v) The additional retained loss on an EEV basis for other operations represents the mark to market value adjustment for holding company net borrowings of a cumulative charge of £(682) million (2016: £(357) million), as shown in note 8.

10 Analysis of movement in net worth and value of in-force for long-term business

	2017 £m				
	Free surplus	Required capital	Total net worth	Value of in-force business	Total embedded value
Group					
Shareholders' equity at beginning of year	**5,364**	**10,296**	**15,660**	**24,937**	**40,597**
New business contribution	**(913)**	**700**	**(213)**	**3,829**	**3,616**
Existing business – transfer to net worth	**3,279**	**(742)**	**2,537**	**(2,537)**	**-**
Expected return on existing business[note 4]	**138**	**201**	**339**	**1,827**	**2,166**
Changes in operating assumptions and experience variances[note 4]	**635**	**(117)**	**518**	**563**	**1,081**
Restructuring costs	**(38)**	**-**	**(38)**	**(10)**	**(48)**
Operating profit based on longer-term investment returns	**3,101**	**42**	**3,143**	**3,672**	**6,815**
Sale of Korea life business[note 17]	**76**	**(76)**	**-**	**-**	**-**
Other non-operating items	**(426)**	**251**	**(175)**	**2,601**	**2,426**
Profit for the year	**2,751**	**217**	**2,968**	**6,273**	**9,241**
Exchange movements on foreign operations and net investment hedges	**(274)**	**(248)**	**(522)**	**(1,800)**	**(2,322)**
Intra-group dividends and investment in operations	**(1,535)**	**-**	**(1,535)**	**-**	**(1,535)**
Other movements	**(64)**	**-**	**(64)**	**-**	**(64)**
Shareholders' equity at end of year	**6,242**	**10,265**	**16,507**	**29,410**	**45,917**
Asia					
New business contribution	**(484)**	**152**	**(332)**	**2,700**	**2,368**
Existing business – transfer to net worth	**1,275**	**(146)**	**1,129**	**(1,129)**	**-**
Expected return on existing business[note 4]	**51**	**48**	**99**	**908**	**1,007**
Changes in operating assumptions and experience variances[note 4]	**81**	**151**	**232**	**98**	**330**
Operating profit based on longer-term investment returns	**923**	**205**	**1,128**	**2,577**	**3,705**
Sale of Korea life business[note 17]	**76**	**(76)**	**-**	**-**	**-**
Other non-operating items	**254**	**137**	**391**	**401**	**792**
Profit for the year	**1,253**	**266**	**1,519**	**2,978**	**4,497**
US					
New business contribution	**(254)**	**304**	**50**	**856**	**906**
Existing business – transfer to net worth	**1,329**	**(219)**	**1,110**	**(1,110)**	**-**
Expected return on existing business[note 4]	**56**	**53**	**109**	**585**	**694**
Changes in operating assumptions and experience variances[note 4]	**190**	**12**	**202**	**341**	**543**
Operating profit based on longer-term investment returns	**1,321**	**150**	**1,471**	**672**	**2,143**
Non-operating items	**(1,247)**	**(222)**	**(1,469)**	**2,358**	**889**
Profit for the year	**74**	**(72)**	**2**	**3,030**	**3,032**
UK and Europe					
New business contribution	**(175)**	**244**	**69**	**273**	**342**
Existing business – transfer to net worth	**675**	**(377)**	**298**	**(298)**	**-**
Expected return on existing business[note 4]	**31**	**100**	**131**	**334**	**465**
Changes in operating assumptions and experience variances[note 4]	**364**	**(280)**	**84**	**124**	**208**
Restructuring costs	**(38)**	**-**	**(38)**	**(10)**	**(48)**
Operating profit based on longer-term investment returns	**857**	**(313)**	**544**	**423**	**967**
Non-operating items	**567**	**336**	**903**	**(158)**	**745**
Profit for the year	**1,424**	**23**	**1,447**	**265**	**1,712**

Note

The net value of in-force business comprises the value of future margins from current in-force business less the cost of holding required capital for long-term business as shown below:

	31 Dec 2017 £m				31 Dec 2016 £m			
	Asia	**US**	**UK and Europe**	**Total**	Asia	US	UK and Europe	Total
Value of in-force business before deduction of cost of capital and time value of guarantees	**17,539**	**10,486**	**3,648**	**31,673**	15,371	8,584	3,468	27,423
Cost of capital	**(588)**	**(232)**	**(607)**	**(1,427)**	(477)	(319)	(692)	(1,488)
Cost of time value of guarantees	**(186)**	**(650)**	**-**	**(836)**	(87)	(911)	-	(998)
Net value of in-force business	**16,765**	**9,604**	**3,041**	**29,410**	14,807	7,354	2,776	24,937
Total net worth	**4,182**	**3,653**	**8,672**	**16,507**	3,665	4,451	7,544	15,660
Total embedded value[note 9(iv)]	**20,947**	**13,257**	**11,713**	**45,917**	18,472	11,805	10,320	40,597

11 Analysis of movement in free surplus

For EEV covered business, 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. In Asia and US operations, assets deemed to be inadmissible on local regulatory basis are included in net worth where considered fully recognisable on an EEV basis. Free surplus for asset management operations and the UK general insurance commission is taken to be IFRS basis post-tax earnings and shareholders' equity, net of goodwill. Free surplus for other operations (including Group and Asia Regional Head Office, holding company borrowings, Africa operations and Prudential Capital) is taken to be EEV basis post-tax earnings and shareholders' equity net of goodwill, with subordinated debt recorded as free surplus to the extent that it is classified as available capital under Solvency II.

Free surplus for insurance and asset management operations and Group total free surplus, including other operations, are shown in the tables below.

(i) Underlying free surplus generated – insurance and asset management operations

The 2016 comparative results are shown below on both actual exchange rates (AER) and constant exchange rates (CER) bases. The 2016 CER comparative results are translated at 2017 average exchange rates.

	2017 £m	2016 £m		% change	
		AER	CER	AER	CER
Asia operations					
Underlying free surplus generated from in-force life business	**1,407**	1,210	1,273	16%	11%
Investment in new business[note (iii)(a)]	**(484)**	(476)	(500)	(2)%	3%
Long-term business	**923**	734	773	26%	19%
Asset management	**155**	125	132	24%	17%
Total	**1,078**	859	905	25%	19%
US operations					
Underlying free surplus generated from in-force life business	**1,575**	1,866	1,961	(16)%	(20)%
Investment in new business[note (iii)(a)]	**(254)**	(298)	(313)	15%	19%
Long-term business	**1,321**	1,568	1,648	(16)%	(20)%
Asset management	**7**	(3)	(4)	333%	275%
Total	**1,328**	1,565	1,644	(15)%	(19)%
UK and Europe operations					
Underlying free surplus generated from in-force life business	**1,070**	923	923	16%	16%
Investment in new business[note (iii)(a)]	**(175)**	(129)	(129)	(36)%	(36)%
Long-term business	**895**	794	794	13%	13%
General insurance commission	**13**	23	23	(43)%	(43)%
Asset management	**403**	341	341	18%	18%
Total	**1,311**	1,158	1,158	13%	13%
Underlying free surplus generated from insurance and asset management operations before restructuring costs	**3,717**	3,582	3,707	4%	0%
Restructuring costs	**(77)**	(16)	(16)	(381)%	(381)%
Underlying free surplus generated from insurance and asset management operations	**3,640**	3,566	3,691	2%	(1)%
Representing:					
Long-term business:					
Expected in-force cash flows (including expected return on net assets)	**3,417**	3,159	3,278	8%	4%
Effects of changes in operating assumptions, operating experience variances and other items before restructuring costs	**635**	840	879	(24)%	(28)%
Underlying free surplus generated from in-force life business before restructuring costs	**4,052**	3,999	4,157	1%	(3)%
Investment in new business[note (iii)(a)]	**(913)**	(903)	(942)	(1)%	3%
Total long-term business	**3,139**	3,096	3,215	1%	(2)%
Asset management and general insurance commission	**578**	486	492	19%	17%
Restructuring costs	**(77)**	(16)	(16)	(381)%	(381)%
	3,640	3,566	3,691	2%	(1)%

(ii) Underlying free surplus generated – Group total

	2017 £m	2016 £m		% change	
		AER	CER	AER	CER
Underlying free surplus generated from insurance and asset management operations[note (i)]	**3,640**	3,566	3,691	2%	(1)%
Other income and expenditure	**(756)**	(681)	(687)	(11)%	(10)%
Interest received from tax settlement	**-**	37	37	n/a	n/a
Group total	**2,884**	2,922	3,041	(1)%	(5)%

(iii) Movement in free surplus

	2017 £m					
	Asia operations	**US operations**	**UK and Europe operations**	**Total insurance and asset management operations**	**Other operations**	**Group total**
Underlying free surplus generated before restructuring costs	**1,078**	**1,328**	**1,311**	**3,717**	**(746)**	**2,971**
Restructuring costs	**(14)**	**-**	**(63)**	**(77)**	**(10)**	**(87)**
Underlying free surplus generated[notes (i)(ii)]	**1,064**	**1,328**	**1,248**	**3,640**	**(756)**	**2,884**
Profit attaching to disposal of businesses[note 17]	**76**	**96**	**-**	**172**	**-**	**172**
Other non-operating items[note (b)]	**254**	**(1,299)**	**572**	**(473)**	**27**	**(446)**
	1,394	**125**	**1,820**	**3,339**	**(729)**	**2,610**
Net cash flows to parent company[note (c)]	**(645)**	**(475)**	**(668)**	**(1,788)**	**1,788**	**-**
External dividends	**-**	**-**	**-**	**-**	**(1,159)**	**(1,159)**
Exchange rate movements, timing differences and other items[note (d)]	**(421)**	**(140)**	**22**	**(539)**	**226**	**(313)**
Net movement in free surplus	**328**	**(490)**	**1,174**	**1,012**	**126**	**1,138**
Balance at beginning of year	**2,142**	**2,418**	**2,006**	**6,566**	**1,648**	**8,214**
Balance at end of year	**2,470**	**1,928**	**3,180**	**7,578**	**1,774**	**9,352**

	2016 £m					
	Asia operations	US operations	UK and Europe operations	Total insurance and asset management operations	Other operations	Group total
Underlying free surplus generated before restructuring costs	859	1,565	1,158	3,582	(628)	2,954
Restructuring costs	-	-	(16)	(16)	(16)	(32)
Underlying free surplus generated[notes (i)(ii)]	859	1,565	1,142	3,566	(644)	2,922
Loss attaching to the sold Korea life business	(86)	-	-	(86)	-	(86)
Other non-operating items[note (b)]	(91)	(770)	(64)	(925)	(214)	(1,139)
	682	795	1,078	2,555	(858)	1,697
Net cash flows to parent company[note (c)]	(516)	(420)	(782)	(1,718)	1,718	-
External dividends	-	-	-	-	(1,267)	(1,267)
Exchange rate movements, timing differences and other items[note (d)]	162	310	21	493	1,119	1,612
Net movement in free surplus	328	685	317	1,330	712	2,042
Balance at beginning of year	1,814	1,733	1,689	5,236	936	6,172
Balance at end of year	2,142	2,418	2,006	6,566	1,648	8,214

Notes

(a) Free surplus invested in new business primarily represents acquisition costs and amounts set aside for required capital.

(b) Non-operating items include short-term fluctuations in investment returns and the effect of changes in economic assumptions for long-term business operations and the effect of business disposals. In addition, for 2017 this includes the impact of US tax reform.

(c) 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.

(d) Exchange rate movements, timing differences and other items represent:

	2017 £m					
	Asia operations	**US operations**	**UK and Europe operations**	**Total insurance and asset management operations**	**Other operations**	**Group total**
Exchange rate movements	**(113)**	**(190)**	**6**	**(297)**	**(13)**	**(310)**
Mark to market value movements on Jackson assets backing surplus and required capital[note 9]	**-**	**40**	**-**	**40**	**-**	**40**
Other items[note (e)]	**(308)**	**10**	**16**	**(282)**	**239**	**(43)**
	(421)	**(140)**	**22**	**(539)**	**226**	**(313)**

	2016 £m					
	Asia operations	US operations	UK and Europe operations	Total insurance and asset management operations	Other operations	Group total
Exchange rate movements	338	368	10	716	48	764
Mark to market value movements on Jackson assets backing surplus and required capital	-	(11)	-	(11)	-	(11)
Other items[note (e)]	(176)	(47)	11	(212)	1,071	859
	162	310	21	493	1,119	1,612

(e) Other items include the effect of movements in subordinated debt for other operations, intra-group loans and other intra-group transfers between operations, non-cash items.

12 Expected transfer of value of in-force business and required capital to free surplus

The discounted value of in-force business and required capital for long-term business operations can be reconciled to the 2017 and 2016 totals for the emergence of free surplus as follows:

	2017 £m	2016 £m
Required capital[note 10]	**10,265**	10,296
Value of in-force business (VIF)[note 10]	**29,410**	24,937
Add back: deduction for cost of time value of guarantees[note 10]	**836**	998
Free surplus generation from the sale of Korea life business	**-**	(76)
Other items*	**(1,371)**	(1,430)
Total long-term business operations	**39,140**	34,725

* 'Other items' represent amounts incorporated into VIF where there is no definitive timeframe for when the payments will be made or receipts received. In particular, other items include the deduction of the shareholders' interest in the with-profits estate, the value of which is derived by increasing final bonus rates so as to exhaust the estate over the lifetime of the in-force with-profits business. This is an assumption to give an appropriate valuation. To be conservative this item is excluded from the expected free surplus generation profile below.

Cash flows are projected on a deterministic basis and are discounted at the appropriate risk discount rate. The modelled cash flows use the same methodology underpinning the Group's EEV reporting and so are subject to the same assumptions and sensitivities.

The table below shows how the VIF generated by the in-force business and the associated required capital for long-term business operations is modelled as emerging into free surplus over future years.

		2017 £m					
		Expected period of conversion of future post-tax distributable earnings and required capital flows to free surplus					
	2017 total as shown above	**1-5 years**	**6-10 years**	**11-15 years**	**16-20 years**	**21-40 years**	**40+ years**
Asia	**18,692**	**5,583**	**3,638**	**2,418**	**1,655**	**3,845**	**1,553**
US	**12,455**	**6,247**	**3,993**	**1,697**	**401**	**117**	**-**
UK and Europe	**7,993**	**3,012**	**2,066**	**1,289**	**899**	**704**	**23**
Total	**39,140**	**14,842**	**9,697**	**5,404**	**2,955**	**4,666**	**1,576**
	100%	**38%**	**25%**	**14%**	**7%**	**12%**	**4%**

		2016 £m					
		Expected period of conversion of future post-tax distributable earnings and required capital flows to free surplus					
	2016 total as shown above	1-5 years	6-10 years	11-15 years	16-20 years	21-40 years	40+ years
Asia	16,393	5,141	3,331	2,209	1,515	3,118	1,079
US	10,556	5,542	3,203	1,240	372	199	-
UK and Europe	7,776	2,890	1,931	1,119	901	899	36
Total	34,725	13,573	8,465	4,568	2,788	4,216	1,115
	100%	39%	25%	13%	8%	12%	3%

13 Sensitivity of results to alternative assumptions

(a) Sensitivity analysis – economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2017 and 31 December 2016 and the new business contribution after the effect of required capital for 2017 and 2016 for long-term business operations to:

- 1 per cent increase in the discount rates;
- 1 per cent increase in interest rates and risk discount rates, including consequential changes (assumed investment returns for all asset classes, market values of fixed interest assets);
- 0.5 per cent decrease in interest rates and risk discount rates, including consequential changes (assumed investment returns for all asset classes, market values of fixed interest assets);
- 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 in contrast to EEV basis required capital (for embedded value only); and
- 5 basis points increase in UK long-term expected defaults.

In each sensitivity calculation, all other assumptions remain unchanged except where they are directly affected by the revised economic conditions.

New business contribution from long-term business operations

	2017 £m				2016 £m			
	Asia	**US**	**UK and Europe**	**Total**	Asia	US	UK and Europe	Total
New business contribution[note 3]	**2,368**	**906**	**342**	**3,616**	2,030	790	268	3,088
Discount rates – 1% increase	**(477)**	**(34)**	**(48)**	**(559)**	(375)	(43)	(32)	(450)
Interest rates – 1% increase	**(103)**	**124**	**44**	**65**	51	64	27	142
Interest rates – 0.5% decrease	**(59)**	**(85)**	**(23)**	**(167)**	(30)	(49)	(15)	(94)
Equity/property yields – 1% rise	**130**	**130**	**52**	**312**	129	91	28	248
Long-term expected defaults – 5 bps increase	**-**	**-**	**(1)**	**(1)**	-	-	(2)	(2)

Embedded value of long-term business operations

	31 Dec 2017 £m				31 Dec 2016 £m			
	Asia	**US**	**UK and Europe**	**Total**	Asia	US	UK and Europe	Total
Shareholders' equity[note 10]	**20,947**	**13,257**	**11,713**	**45,917**	18,472	11,805	10,320	40,597
Discount rates – 1% increase	**(2,560)**	**(440)**	**(774)**	**(3,774)**	(2,078)	(379)	(809)	(3,266)
Interest rates – 1% increase	**(944)**	**26**	**(635)**	**(1,553)**	(701)	(241)	(638)	(1,580)
Interest rates – 0.5% decrease	**121**	**(166)**	**384**	**339**	248	25	369	642
Equity/property yields – 1% rise	**873**	**896**	**425**	**2,194**	771	653	314	1,738
Equity/property market values – 10% fall	**(429)**	**(209)**	**(479)**	**(1,117)**	(361)	(11)	(399)	(771)
Statutory minimum capital	**169**	**158**	**-**	**327**	150	223	-	373
Long-term expected defaults – 5 bps increase	**-**	**-**	**(135)**	**(135)**	-	-	(138)	(138)

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 assumptions 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, namely the effect of economic assumption changes and short-term fluctuations in investment returns. In addition to the sensitivity effects shown above, the other components of the profit for the following year 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 changes in interest rates, the effect shown above for Jackson would also be recorded within the fair value movements on assets backing surplus and required capital, which are taken directly to shareholders' equity.

(b) Sensitivity analysis – non-economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2017 and 31 December 2016 and the new business contribution after the effect of required capital for 2017 and 2016 for long-term business operations to:

- 10 per cent proportionate decrease in maintenance expenses (a 10 per cent sensitivity on a base assumption of £10 per annum would represent an expense assumption of £9 per annum);
- 10 per cent proportionate decrease in lapse rates (a 10 per cent sensitivity on a base assumption of 5 per cent would represent a lapse rate of 4.5 per cent per annum); and
- 5 per cent proportionate decrease in base mortality and morbidity rates (ie increased longevity).

New business contribution from long-term business operations

	2017 £m				2016 £m			
	Asia	**US**	**UK and Europe**	**Total**	Asia	US	UK and Europe	Total
New business contribution[note 3]	**2,368**	**906**	**342**	**3,616**	2,030	790	268	3,088
Maintenance expenses – 10% decrease	**38**	**14**	**3**	**55**	33	10	3	46
Lapse rates – 10% decrease	**133**	**24**	**20**	**177**	132	26	11	169
Mortality and morbidity – 5% decrease	**69**	**4**	**(2)**	**71**	57	4	(4)	57
Change representing effect on:								
Life business	**69**	**4**	**1**	**74**	57	4	-	61
UK annuities	**-**	**-**	**(3)**	**(3)**	-	-	(4)	(4)

Embedded value of long-term business operations

	31 Dec 2017 £m				31 Dec 2016 £m			
	Asia	**US**	**UK and Europe**	**Total**	Asia	US	UK and Europe	Total
Shareholders' equity[note 10]	**20,947**	**13,257**	**11,713**	**45,917**	18,472	11,805	10,320	40,597
Maintenance expenses – 10% decrease	**213**	**169**	**64**	**446**	187	104	91	382
Lapse rates – 10% decrease	**753**	**659**	**64**	**1,476**	659	533	79	1,271
Mortality and morbidity – 5% decrease	**668**	**214**	**(442)**	**440**	554	192	(302)	444
Change representing effect on:								
Life business	**668**	**214**	**13**	**895**	554	192	12	758
UK annuities	**-**	**-**	**(455)**	**(455)**	-	-	(314)	(314)

14 Methodology and accounting presentation

(a) Methodology

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(b)(iii), 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(b)(i).

(i) 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, including the Group's investments in joint venture and associate insurance operations, 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 asset management and other operations (including Group and Asia Regional Head Office, holding company borrowings, Africa operations and Prudential Capital). Under the EEV Principles, the results for covered business incorporate the projected margins of attaching internal asset management, as described in note 14(a)(vii).

The definition of long-term business operations 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 Limited (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.
- 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.

A small amount of UK group pensions business is also not modelled for EEV reporting purposes.

(ii) 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, mortality and morbidity, as described in note 15(vii). 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.

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 and economic assumptions as at the end of the year. 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 premiums and one-tenth of single premiums. PVNBP is calculated as equalling single premiums plus the present value of expected premiums of regular premium new 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 year (to the extent that changes in capital values do not directly match changes in liabilities) are included directly in the profit for the year 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 an IFRS basis.

However, in determining the movements on the additional shareholders' interest, the basis for calculating the EEV result for Jackson 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/depreciation on these securities are accounted for in equity rather than in the income statement, as shown in the movement in shareholders' equity.

(iii) Cost of capital

A charge is deducted from the embedded value for the cost of locked-in required capital supporting the Group's long-term business. 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 post-tax investment earnings 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.

(iv) Financial options and guarantees

Nature of financial options and guarantees in Prudential's long-term business

Asia

Subject to local market circumstances and regulatory requirements, the guarantee features described below in respect of UK and Europe business broadly apply to similar types of participating contracts which are principally written in 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 (Jackson)

The principal financial options and guarantees in Jackson are associated with the fixed annuity (FA) 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 both years, depending on the particular product, jurisdiction where issued, and date of issue. For both years, 87 per cent of the account values on fixed annuities are for policies with guarantees of 3 per cent or less, and the average guarantee rate is 2.6 per cent.

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 for which it contractually guarantees to the contract holder, subject to specific conditions, 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 upon depletion of funds (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 policyholders' value in the event of poor equity market performance. Jackson hedges the GMWB and GMDB guarantees through the use of equity options and futures contracts, and essentially fully reinsures the GMIB guarantees.

Jackson also issues fixed index annuities (FIA) that enable policyholders to obtain a portion of an equity-linked return while providing a guaranteed minimum return. The guaranteed minimum returns are of a similar nature to those described above for fixed annuities.

UK and Europe (M&G Prudential)

For covered business the only significant financial options and guarantees in M&G Prudential 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 PAC with-profits fund also held a provision of £53 million at 31 December 2017 (31 December 2016: £62 million) to honour guarantees on a small number of guaranteed annuity option products.

The Group's main exposure to guaranteed annuity options in M&G Prudential is through the non-covered business of SAIF. A provision of £503 million was held in SAIF at 31 December 2017 (31 December 2016: £571 million) to honour the guarantees. As described in note 14(a)(i), 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' funds.

Time value
The value of financial options and guarantees comprises two parts:
— The first part arises from a deterministic valuation on best estimate assumptions (the intrinsic value).
— The second 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.

(v) 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 M&G Prudential, a portion of future shareholder transfers expected from the with-profits fund is recognised within net worth, together with the associated capital requirements.

For shareholder-backed business, the following capital requirements for long-term business operations apply:
— Asia: 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. For China operations, the level of required capital as at 31 December 2017 follows the approach for embedded value reporting issued by the China Association of Actuaries (CAA), reflecting the C-ROSS regime;
— US: the level of required capital has been set at 250 per cent of the risk-based capital (RBC) required by the National Association of Insurance Commissioners (NAIC) at the Company Action Level (CAL); and
— UK and Europe: the capital requirements are set at the Solvency II Solvency Capital Requirement (SCR) for shareholder-backed business as a whole.

(vi) 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.

(vii) Internal asset management
The in-force and new business 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 year 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 year as included in 'Other operations'. 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 assets for covered business.

(viii) 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.

For Asia and the US, the risk-free rates are based on 10-year local government bond yields.

For UK and Europe, the EEV risk-free rate is based on the full term structure of interest rates, ie a yield curve, which is used to determine the embedded value at the end of the reporting period.

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. In order to better reflect differences in relative market risk volatility inherent in each product group, Prudential sets the risk discount rates to reflect the expected volatility associated with the cash flows for each product category in the embedded value model, rather than at a Group level.

Since financial options and guarantees are explicitly valued under the EEV methodology, risk 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 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.

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 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
For Asia, 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 (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 (0.2 per cent for variable annuity business and 1.0 per cent for non-variable annuity business for both years), 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 short-term 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 returns 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 and Europe (M&G Prudential)
(1) Shareholder-backed annuity business
For 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 liabilities, the future cash flows are discounted using the swap yield curve plus an allowance for liquidity premium based on the Solvency II allowance for credit risk. The Solvency II allowance is set by European Insurance and Occupational Pensions Authority (EIOPA) using a prudent assumption that all future downgrades will be replaced annually, and allowing for the credit spread floor.

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 a best estimate credit risk allowance. The remaining elements of prudence within the Solvency II allowance are incorporated into the risk margin included in the discount rate, shown in note 15(iii).

(2) With-profits fund non-profit annuity business
For non-profit annuity business attributable to the PAC with-profits fund, 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 for this business is taken into account in determining the projected cash flows from the with-profits fund, which are in turn discounted at the risk discount rate applicable to all of the projected cash flows from the fund.

(3) With-profits fund holdings of debt securities
The 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 risk free, 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. An allowance for non-diversifiable non-market risks is estimated as set out below:

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 Asia operations in China, Indonesia, the Philippines, Taiwan, Thailand and Vietnam, additional allowances are applied for emerging market risk ranging from 100 to 250 basis points. The level of these allowances are reviewed and updated based on an assessment of a range of pre-defined emerging market risk indicators, as well as the Group's exposure and experience in the business units. During 2017, the China allowance for non-market risk was reduced reflecting the growth in the size of the business, increasing management exposure and experience in the country and an improvement in our risk assessment of the market. For the Group's US business and UK and Europe business, no additional allowance is necessary.

(ix) Foreign currency translation
Foreign currency profits and losses have been translated at average exchange rates for the year. Foreign currency assets and liabilities have been translated at year-end exchange rates. The principal exchange rates are shown in note A1 of the IFRS financial statements.

(x) Taxation
In determining the post-tax profit for the year 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.

(xi) Inter-company arrangements
The EEV results for covered business incorporate annuities established in the PAC non-profit sub-fund from vesting pension policies 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 the PAC non-profit sub-fund.

(b) Accounting presentation

(i) Analysis of post-tax profit
To the extent applicable, the presentation of the EEV post-tax profit for the year 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(b)(ii)) and incorporate the following:

- new business contribution, as defined in note 14(a)(ii);
- unwind of discount on the value of in-force business and other expected returns, as described in note 14(b)(iii);
- the impact of routine changes of estimates relating to operating assumptions, as described in note 14(b)(iv); and
- operating experience variances, as described in note 14(b)(v).

Non-operating results comprise the recurrent items of:

- short-term fluctuations in investment returns;
- the mark to market value movements on core structural borrowings; and
- the effect of changes in economic assumptions.

In addition, non-operating results include the effect of the disposal of businesses (see note 17) and in 2017, the impact of US tax reform (see note 7).

Total profit attributable to shareholders and basic earnings per share include these items, together with actual investment returns. The Group believes that operating profit, as adjusted for these items, better reflects underlying performance.

(ii) Investment returns included in 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 M&G Prudential, 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(b)(iii).

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 reserve 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 business 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 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 operating result for the year.

(iii) Unwind of discount and other expected returns

The Group's methodology in determining the unwind of discount and other expected returns is by reference to:

- the value of in-force business at the beginning of the year (adjusted for the effect of current year 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 M&G Prudential is described below.

M&G Prudential

The unwind is determined by reference to an implied single risk discount rate. The EEV risk-free rate is based on a yield curve (as set out in note 14(a)(viii)), which is used to derive a single implied discount rate which, if this rate had been used, would reproduce the same embedded value as that calculated by reference to the yield curve. The difference between the operating profit determined using the single implied discount rate and that derived using the yield curve is included within non-operating profit.

For with-profits business, the opening value of in-force is adjusted for the effect 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 31 December 2017 the shareholders' interest in the smoothed surplus assets used for this purpose only were £57 million lower (31 December 2016: £77 million lower) than the surplus assets carried in the statement of financial position.

(iv) Effect of changes in operating assumptions

Operating profit includes the effect of changes to non-economic assumptions on the value of in-force at the end of the year. For presentational purposes the effect of changes is delineated to show the effect on the opening value of in-force as operating assumption changes, with the experience variances subsequently being determined by reference to the end-of-year assumptions (see note 14(b)(v)).

(v) Operating experience variances

Operating profit includes the effect of experience variances on non-economic assumptions, such as persistency, mortality and morbidity, expenses and other factors, which are calculated with reference to the end-of-year assumptions.

(vi) Effect of changes in economic assumptions

Movements in the value of in-force business at the beginning of the year caused by changes in economic assumptions, net of the related change in the time value of cost of options and guarantees, are recorded in non-operating results. For M&G Prudential, the embedded value incorporates Solvency II transitional measures, which are recalculated using management's estimate of the impact of operating and market conditions at the valuation date. The effect of changes in economic assumptions is after allowing for this recalculation.

15 Assumptions

Principal economic assumptions

The EEV basis results for the Group's operations have been determined using economic assumptions where the long-term expected rates of return on investments and risk discount rates are set by reference to year-end risk-free rates of return (defined below for each of the Group's insurance operations). 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 over time 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 profit with the efforts and risks of current management actions, particularly with regard to business sold during the year.

(i) Asianotes (b)(c)

The risk-free rates of return for Asia are defined as 10-year government bond yields at the end of the year.

In order to reflect Prudential's most recent assessment of the growth prospects of the region compared to other developed markets and the historically strong relationship between long-term economic growth and long-term equity returns, in a number of Asia business units, equity risk premiums were increased during 2017 by between 25 basis points and 75 basis points from those applied at 2016. The related expected return on equity and risk discount rates have also been increased by equivalent amounts. In addition, for a few Asia business units, expected long-term inflation assumptions were revised during 2017 to better reflect central bank inflation targets and to align with the currency of the underlying exposures.

	Risk discount rate %				10-year government bond yield %		Expected long-term Inflation %	
	New business		In-force business					
	31 Dec 2017	31 Dec 2016	**31 Dec 2017**	31 Dec 2016	**31 Dec 2017**	31 Dec 2016	**31 Dec 2017**	31 Dec 2016
China	**9.7**	9.6	**9.7**	9.6	**3.9**	3.1	**3.0**	2.5
Hong Kong notes (b)(d)	**4.1**	3.9	**4.1**	3.9	**2.4**	2.5	**2.5**	2.3
Indonesia	**10.6**	12.0	**10.6**	12.0	**6.4**	8.1	**4.5**	5.0
Malaysia note (d)	**6.4**	6.8	**6.5**	6.9	**3.9**	4.3	**2.5**	2.5
Philippines	**12.7**	11.6	**12.7**	11.6	**5.2**	4.8	**4.0**	4.0
Singapore note (d)	**3.5**	4.2	**4.4**	5.0	**2.0**	2.5	**2.0**	2.0
Taiwan	**4.3**	4.0	**3.9**	4.0	**0.9**	1.2	**1.5**	1.0
Thailand	**9.8**	9.4	**9.8**	9.4	**2.3**	2.7	**3.0**	3.0
Vietnam	**12.6**	13.0	**12.6**	13.0	**5.1**	6.3	**5.5**	5.5
Total weighted risk discount rate note (a)	**5.3**	5.3	**5.7**	6.1				

Notes

(a) The weighted risk discount rates for Asia operations shown above have been determined by weighting each market's risk discount rates by reference to the post-tax EEV basis new business contribution and the closing value of in-force business. The changes in the risk discount rates for individual Asia business units reflect:
- the movements in 10-year government bond yields;
- changes in product mix; and
- the effect of changes in the economic basis (see note 14(a)(viii) and above).

(b) For Hong Kong the assumptions shown are for US dollar denominated business. For other business units, the assumptions are for local currency denominated business.

(c) Equity risk premiums in Asia range from 4.0 per cent to 9.4 per cent (2016: from 3.5 per cent to 8.7 per cent).

(d) The mean equity return assumptions for the most significant equity holdings of the Asia operations are:

	31 Dec 2017 %	31 Dec 2016 %
Hong Kong	**6.4**	6.5
Malaysia	**10.4**	10.2
Singapore	**8.5**	8.5

(ii) US

The risk-free rates of return for the US are defined as 10-year treasury bond yield at the end of the year.

	31 Dec 2017 %	31 Dec 2016 %
Assumed new business spread margins:*		
Fixed annuity business:†		
January to June issues	**1.50**	1.25
July to December issues	**1.25**	1.25
Fixed index annuity business:		
January to June issues	**1.75**	1.50
July to December issues	**1.50**	1.50
Institutional business	**0.50**	0.50
Allowance for long-term defaults included in projected spread[note 14(a)(viii)]	**0.19**	0.21
Risk discount rate:		
Variable annuity:		
Risk discount rate	**6.8**	6.9
Additional allowance for credit risk included in risk discount rate[note 14(a)(viii)]	**0.2**	0.2
Non-variable annuity:		
Risk discount rate	**4.1**	4.1
Additional allowance for credit risk included in risk discount rate[note 14(a)(viii)]	**1.0**	1.0
Weighted average total:		
New business	**6.7**	6.8
In-force business	**6.5**	6.5
US 10-year treasury bond yield	**2.4**	2.5
Pre-tax expected long-term nominal rate of return for US equities	**6.4**	6.5
Expected long-term rate of inflation	**3.0**	3.0
Equity risk premium	**4.0**	4.0
S&P equity return volatility[note (v)]	**18.0**	18.0

* 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.

† Including the proportion of variable annuity business invested in the general account.

(iii) UK and Europe

The risk-free rate is based on the full term structure of interest rates, ie a yield curve, which is used to determine the embedded value at the end of the reporting period. These yield curves are used to derive pre-tax expected long-term nominal rates of investment return and risk discount rates. For the purpose of determining the unwind of discount in the analysis of operating profit, these yield curves are used to derive a single implied risk discount rate, as explained in note 14(a)(viii).

This single implied risk discount rate is shown, along with the 15-year nominal rate of investment return and 15-year rate of inflation based on the yield curve.

	31 Dec 2017 %	31 Dec 2016 %
Shareholder-backed annuity in-force business:[note (a)]		
Risk discount rate	**4.0**	4.5
Pre-tax expected 15-year nominal rates of investment return[note (c)]	**2.6**	2.8
With-profits and other business:		
Risk discount rate:[note (b)]		
New business	**4.7**	4.7
In-force business	**4.8**	4.9
Pre-tax expected 15-year nominal rates of investment return:[note (c)]		
Overseas equities	**6.2 to 10.1**	6.2 to 9.4
Property	**4.4**	4.5
15-year gilt yield	**1.6**	1.7
Corporate bonds	**3.4**	3.5
Expected 15-year rate of inflation	**3.5**	3.6
Equity risk premium	**4.0**	4.0

Notes

(a) For shareholder-backed annuity business, the movements in the pre-tax long-term nominal rates of return and risk discount rates reflect the effect of changes in asset yields.

(b) The risk discount rates for with-profits and other business shown above represents a weighted average total of the rates applied to determine the present value of future cash flows, including a portion of future with-profits business shareholders' transfers recognised in net worth.

(c) The table below shows the pattern of the UK risk-free Solvency II spot yield curve at the end of both years:

	1 year	**5 year**	**10 year**	**15 year**	**20 year**
31 Dec 2017	0.6%	0.9%	1.2%	1.3%	1.4%
31 Dec 2016	0.4%	0.7%	1.1%	1.3%	1.3%

Stochastic assumptions

Details are given below of the key characteristics of the models used to determine the time value of the financial options and guarantees as referred to in note 14(a)(iv).

(iv) Asia

- The stochastic cost of guarantees is primarily of significance for the Hong Kong, Malaysia, Singapore and Taiwan operations;
- The principal asset classes are government and corporate bonds;
- The asset return models are similar to the models as described for M&G Prudential below; and

— The volatility of equity returns ranges from 18 per cent to 35 per cent, and the volatility of government bond yields ranges from 1.1 per cent to 2.0 per cent (2016: from 0.9 per cent to 2.3 per cent) following a number of modelling changes at full year 2017 in respect of future bond returns.

(v) US (Jackson)

— Interest rates and equity returns are projected using a log-normal generator reflecting historical market data;
— Corporate bond returns are based on treasury yields plus a spread that reflects current market conditions; and
— The volatility of equity returns ranges from 18 per cent to 27 per cent for both years, and the standard deviation of interest rates ranges from 2.5 per cent to 2.8 per cent (2016: from 2.3 per cent to 2.6 per cent).

(vi) UK and Europe (M&G Prudential)

— Interest rates are projected using a stochastic interest rate model calibrated to the current market yields;
— Equity returns are assumed to follow a log-normal distribution;
— The corporate bond return is calculated based on a risk-free return plus a mean-reverting spread;
— Property returns are also modelled on a risk-free return plus a risk premium with a stochastic process reflecting total property returns; and
— The standard deviation of equities and property ranges from 14 per cent to 20 per cent (2016: from 15 per cent to 20 per cent).

Operating assumptions

(vii) 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 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 actions to achieve the savings have been delivered. Expense overruns are reported where these are expected to be short-lived, including businesses that are growing rapidly or are sub-scale.

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, comprises:

— expenditure for Group Head Office, to the extent not allocated to the PAC with-profits funds, together with restructuring costs; 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.

(viii) Tax rates

The assumed long-term effective tax rates for operations reflect the incidence of taxable profits and losses in the projected cash flows as explained in note 14(a)(x).

The local statutory corporate tax rates applicable for the most significant operations for 2016 and 2017 are as follows:

Statutory corporate tax rates	%
Asia operations:	
Hong Kong	16.5 per cent on 5 per cent of premium income
Indonesia	25.0
Malaysia	24.0
Singapore	17.0
US operations*	2016 and 2017: 35.0; from 1 January 2018: 21.0
UK operations	2016: 20.0; from 1 April 2017: 19.0; from 1 April 2020: 17.0

* The US tax reform changes included a reduction in the corporate income tax rate from 35 per cent to 21 per cent effective from 1 January 2018 (see note 7).

16 Insurance new business premiums[note (i)]

	Single premiums		Regular premiums		Annual premium equivalents (APE) note 14(a)(ii)		Present value of new business premiums (PVNBP) note 14(a)(ii)	
	2017 £m	2016 £m	**2017 £m**	2016 £m	**2017 £m**	2016 £m	**2017 £m**	2016 £m
Asia	**2,299**	2,397	**3,575**	3,359	**3,805**	3,599	**20,405**	19,271
US	**16,622**	15,608	**-**	-	**1,662**	1,561	**16,622**	15,608
UK and Europe	**13,044**	9,836	**187**	177	**1,491**	1,160	**13,784**	10,513
Group total	**31,965**	27,841	**3,762**	3,536	**6,958**	6,320	**50,811**	45,392
Asia								
Cambodia	**-**	-	**16**	14	**16**	14	**70**	66
Hong Kong	**582**	1,140	**1,667**	1,798	**1,725**	1,912	**10,027**	10,930
Indonesia	**288**	236	**268**	255	**297**	279	**1,183**	1,048
Malaysia	**73**	110	**271**	233	**278**	244	**1,398**	1,352
Philippines	**62**	91	**71**	61	**77**	70	**287**	278
Singapore	**859**	523	**361**	299	**447**	351	**3,463**	2,627
Thailand	**139**	80	**70**	81	**84**	89	**421**	404
Vietnam	**8**	6	**133**	115	**134**	116	**659**	519
SE Asia operations including Hong Kong	**2,011**	2,186	**2,857**	2,856	**3,058**	3,075	**17,508**	17,224
China[note (ii)]	**179**	124	**276**	187	**294**	199	**1,299**	880
Taiwan	**46**	36	**208**	146	**213**	150	**634**	499
India[note (iii)]	**63**	51	**234**	170	**240**	175	**964**	668
Total	**2,299**	2,397	**3,575**	3,359	**3,805**	3,599	**20,405**	19,271
US								
Variable annuities	**11,536**	10,653	**-**	-	**1,154**	1,065	**11,536**	10,653
Elite Access (variable annuity)	**2,013**	2,056	**-**	-	**201**	206	**2,013**	2,056
Fixed annuities	**454**	555	**-**	-	**45**	55	**454**	555
Fixed index annuities	**295**	508	**-**	-	**30**	51	**295**	508
Wholesale	**2,324**	1,836	**-**	-	**232**	184	**2,324**	1,836
Total	**16,622**	15,608	**-**	-	**1,662**	1,561	**16,622**	15,608
UK and Europe								
Bonds	**3,509**	3,834	**-**	-	**351**	384	**3,510**	3,835
Corporate pensions	**103**	110	**130**	121	**140**	132	**533**	479
Individual pensions	**5,747**	2,532	**32**	35	**607**	289	**5,897**	2,681
Income drawdown	**2,218**	1,649	**-**	-	**222**	165	**2,218**	1,649
Other products	**1,467**	1,711	**25**	21	**171**	190	**1,626**	1,869
Total	**13,044**	9,836	**187**	177	**1,491**	1,160	**13,784**	10,513
Group total	**31,965**	27,841	**3,762**	3,536	**6,958**	6,320	**50,811**	45,392

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. A reconciliation of APE and gross earned premiums on an IFRS basis is provided in Note E within the EEV unaudited financial information.

(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.

17 Disposal of businesses

On 18 May 2017, the Group announced it had completed the sale of its life insurance subsidiary in Korea, PCA Life Insurance, to Mirae Asset Life Insurance for KRW 170 billion (£117 million at 17 May 2017 closing exchange rate) following regulatory approval. The proceeds, net of £(9) million of related expenses, were £108 million. Upon disposal, £76 million of required capital was released and a corresponding increase in free surplus was recognised. There were no other impacts on the 2017 results.

On 15 August 2017, the Group through its subsidiary National Planning Holdings, Inc. (NPH) sold its US independent broker-dealer network to LPL Financial LLC. The initial consideration received was £252 million (US$ 325 million) resulting in a post-tax profit on disposal of £80 million (US$103 million) after costs and net losses that have been incurred in the year.

18 Post balance sheet events

Intention to demerge the Group's UK businesses

In March 2018, the Group announced its intention to demerge its UK & Europe business ('M&G Prudential') from Prudential plc, resulting in two separately-listed companies. In preparation for the UK demerger process, Prudential plc intends to transfer the legal ownership of its Hong Kong insurance subsidiaries from The Prudential Assurance Company Limited (M&G Prudential's UK regulated insurance entity) to Prudential Corporation Asia Limited, which is expected to complete by the end of 2019.

Sale of £12.0 billion* UK annuity portfolio

In March 2018, M&G Prudential also announced the sale of £12.0 billion* of its shareholder annuity portfolio to Rothesay Life. Under the terms of the agreement, M&G Prudential has reinsured £12.0 billion* of liabilities to Rothesay Life, which is expected to be followed by a Part VII transfer of the portfolio by the end of 2019. Further details are set out in the CFO Report.

* Relates to £12.0 billion of IFRS shareholder annuity liabilities, valued as at 31 December 2017.

Additional EEV financial information*

A New Business

BASIS OF PREPARATION

The format of the schedules 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 Prudential Regulation Authority regulations.

The details shown 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 and Europe Insurance Operations, and Guaranteed Investment Contracts and similar funding agreements written in US Insurance Operations.

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. New business premiums reflect those premiums attaching to covered business, including premiums for contracts designed as investment products for IFRS reporting.

Investment products referred to in the tables for funds under management are unit trusts, 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, as described in the preceding paragraph, although similar IFRS recognition and measurement principles apply to the acquisition costs and fees attaching to this type of business.

Post-tax New Business Profit has been determined using the European Embedded Value (EEV) methodology set out in our EEV basis results supplement.

In determining the EEV basis value of new business written in the period policies incept, 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.

Annual premium equivalent (APE) sales are subject to rounding.

* The additional financial information is not covered by the KPMG LLP independent audit opinion.

Notes to Schedules A(i) to A(v)

(1) Prudential plc reports its results using both actual exchange rates (AER) and constant exchange rates (CER) so as to eliminate the impact of exchange translation.

	Average rate*			Closing rate		
Local currency : £	**2017**	**2016**	**% appreciation (depreciation) of local currency against GBP**	**31 Dec 2017**	**31 Dec 2016**	**% appreciation (depreciation) of local currency against GBP**
China	**8.71**	8.99	3%	**8.81**	8.59	(2)%
Hong Kong	**10.04**	10.52	5%	**10.57**	9.58	(9)%
Indonesia	**17,249.38**	18,026.11	5%	**18,353.44**	16,647.30	(9)%
Malaysia	**5.54**	5.61	1%	**5.47**	5.54	1%
Singapore	**1.78**	1.87	5%	**1.81**	1.79	(1)%
Thailand	**43.71**	47.80	9%	**44.09**	44.25	0%
US	**1.29**	1.35	5%	**1.35**	1.24	(8)%
Vietnam	**29,279.71**	30,292.79	3%	**30,719.60**	28,136.99	(8)%

* Average rate is for the 12 month period to 31 December.

(2) Annual Premium Equivalents (APE), calculated as regular new business contributions plus 10 per cent of single new business contributions, are subject to rounding. Present value of new business premiums (PVNBP) are calculated as equalling single premiums plus the present value of expected premiums of new regular premium business. In determining the present value, allowance is made for lapses and other assumptions applied in determining the EEV new business profit.
(3) Balance includes segregated and pooled pension funds, private finance assets and other institutional clients.
(4) New business in India is included at Prudential's 26 per cent interest in the India life operation.
(5) Balance Sheet figures have been calculated at the closing exchange rates.
(6) New business in China is included at Prudential's 50 per cent interest in the China life operation.
(7) Mandatory Provident Fund (MPF) product sales in Hong Kong are included at Prudential's 36 per cent interest in Hong Kong MPF operation.
(8) Investment flows for the year exclude year-to-date Eastspring Money Market Funds (MMF) gross inflow of £192,662 million (2016: gross inflow of £146,711 million) and net inflow of £1,495 million (2016: net inflow of £403 million).
(9) Total Group Investment Operations funds under management exclude MMF funds under management of £9,317 million at 31 December 2017 (31 December 2016: £7,714 million).

Schedule A(i) New Business Insurance Operations (Actual Exchange Rates)

Note: The 2016 comparative results are shown below on actual exchange rates (AER) as previously reported.

	Single premiums			Regular premiums			APE[2]			PVNBP[2]		
	2017	2016	+/(-)	2017	2016	+/(-)	2017	2016	+/(-)	2017	2016	+/(-)
	£m	£m	%	£m	£m	%	£m	£m	%	£m	£m	%
Group insurance operations												
Asia	**2,299**	2,397	(4)%	**3,575**	3,359	6%	**3,805**	3,599	6%	**20,405**	19,271	6%
US	**16,622**	15,608	6%	**-**	-	-	**1,662**	1,561	6%	**16,622**	15,608	6%
UK and Europe	**13,044**	9,836	33%	**187**	177	6%	**1,491**	1,160	29%	**13,784**	10,513	31%
Group total	**31,965**	27,841	15%	**3,762**	3,536	6%	**6,958**	6,320	10%	**50,811**	45,392	12%
Asia insurance operations												
Cambodia	**-**	-	-	**16**	14	14%	**16**	14	14%	**70**	66	6%
Hong Kong	**582**	1,140	(49)%	**1,667**	1,798	(7)%	**1,725**	1,912	(10)%	**10,027**	10,930	(8)%
Indonesia	**288**	236	22%	**268**	255	5%	**297**	279	6%	**1,183**	1,048	13%
Malaysia	**73**	110	(34)%	**271**	233	16%	**278**	244	14%	**1,398**	1,352	3%
Philippines	**62**	91	(32)%	**71**	61	16%	**77**	70	10%	**287**	278	3%
Singapore	**859**	523	64%	**361**	299	21%	**447**	351	27%	**3,463**	2,627	32%
Thailand	**139**	80	74%	**70**	81	(14)%	**84**	89	(6)%	**421**	404	4%
Vietnam	**8**	6	33%	**133**	115	16%	**134**	116	16%	**659**	519	27%
SE Asia operations including Hong Kong	**2,011**	2,186	(8)%	**2,857**	2,856	0%	**3,058**	3,075	(1)%	**17,508**	17,224	2%
China[6]	**179**	124	44%	**276**	187	48%	**294**	199	48%	**1,299**	880	48%
Taiwan	**46**	36	28%	**208**	146	42%	**213**	150	42%	**634**	499	27%
India[4]	**63**	51	24%	**234**	170	38%	**240**	175	37%	**964**	668	44%
Total Asia insurance operations	**2,299**	2,397	(4)%	**3,575**	3,359	6%	**3,805**	3,599	6%	**20,405**	19,271	6%
US insurance operations												
Variable annuities	**11,536**	10,653	8%	**-**	-	-	**1,154**	1,065	8%	**11,536**	10,653	8%
Elite Access (variable annuity)	**2,013**	2,056	(2)%	**-**	-	-	**201**	206	(2)%	**2,013**	2,056	(2)%
Fixed annuities	**454**	555	(18)%	**-**	-	-	**45**	55	(18)%	**454**	555	(18)%
Fixed index annuities	**295**	508	(42)%	**-**	-	-	**30**	51	(41)%	**295**	508	(42)%
Wholesale	**2,324**	1,836	27%	**-**	-	-	**232**	184	26%	**2,324**	1,836	27%
Total US insurance operations	**16,622**	15,608	6%	**-**	-	-	**1,662**	1,561	6%	**16,622**	15,608	6%
UK and Europe insurance operations												
Bonds	**3,509**	3,834	(8)%	**-**	-	-	**351**	384	(9)%	**3,510**	3,835	(8)%
Corporate pensions	**103**	110	(6)%	**130**	121	7%	**140**	132	6%	**533**	479	11%
Individual pensions	**5,747**	2,532	127%	**32**	35	(9)%	**607**	289	110%	**5,897**	2,681	120%
Income drawdown	**2,218**	1,649	35%	**-**	-	-	**222**	165	35%	**2,218**	1,649	35%
Other products	**1,467**	1,711	(14)%	**25**	21	19%	**171**	190	(10)%	**1,626**	1,869	(13)%
Total UK and Europe insurance operations	**13,044**	9,836	33%	**187**	177	6%	**1,491**	1,160	29%	**13,784**	10,513	31%
Group total	**31,965**	27,841	15%	**3,762**	3,536	6%	**6,958**	6,320	10%	**50,811**	45,392	12%

Schedule A(ii) New Business Insurance Operations (Constant Exchange Rates)

Note: The 2016 comparative results are shown below on constant exchange rates (CER), ie translated at 2017 average exchange rates.

	Single premiums			Regular premiums			APE[2]			PVNBP[2]		
	2017 £m	2016 £m	+/(-) %	2017 £m	2016 £m	+/(-) %	2017 £m	2016 £m	+/(-) %	2017 £m	2016 £m	+/(-) %
Group insurance operations												
Asia	**2,299**	2,509	(8)%	**3,575**	3,522	2%	**3,805**	3,773	1%	**20,405**	20,180	1%
US	**16,622**	16,405	1%	**-**	-	-	**1,662**	1,641	1%	**16,622**	16,405	1%
UK and Europe	**13,044**	9,836	33%	**187**	177	6%	**1,491**	1,160	29%	**13,784**	10,513	31%
Group total	**31,965**	28,750	11%	**3,762**	3,699	2%	**6,958**	6,574	6%	**50,811**	47,098	8%
Asia insurance operations												
Cambodia	**-**	-	-	**16**	14	14%	**16**	14	14%	**70**	69	1%
Hong Kong	**582**	1,192	(51)%	**1,667**	1,884	(12)%	**1,725**	2,002	(14)%	**10,027**	11,442	(12)%
Indonesia	**288**	247	17%	**268**	267	0%	**297**	292	2%	**1,183**	1,096	8%
Malaysia	**73**	111	(34)%	**271**	235	15%	**278**	246	13%	**1,398**	1,368	2%
Philippines	**62**	90	(31)%	**71**	61	16%	**77**	70	10%	**287**	275	4%
Singapore	**859**	550	56%	**361**	314	15%	**447**	369	21%	**3,463**	2,761	25%
Thailand	**139**	88	58%	**70**	88	(20)%	**84**	97	(13)%	**421**	442	(5)%
Vietnam	**8**	6	33%	**133**	119	12%	**134**	120	12%	**659**	537	23%
SE Asia operations including Hong Kong	**2,011**	2,284	(12)%	**2,857**	2,982	(4)%	**3,058**	3,210	(5)%	**17,508**	17,990	(3)%
China[6]	**179**	129	39%	**276**	193	43%	**294**	206	43%	**1,299**	909	43%
Taiwan	**46**	40	15%	**208**	163	28%	**213**	167	28%	**634**	557	14%
India[4]	**63**	56	13%	**234**	184	27%	**240**	190	26%	**964**	724	33%
Total Asia insurance operations	**2,299**	2,509	(8)%	**3,575**	3,522	2%	**3,805**	3,773	1%	**20,405**	20,180	1%
US insurance operations												
Variable annuities	**11,536**	11,196	3%	**-**	**-**	-	**1,154**	1,120	3%	**11,536**	11,196	3%
Elite Access (variable annuity)	**2,013**	2,161	(7)%	**-**	-	-	**201**	216	(7)%	**2,013**	2,161	(7)%
Fixed annuities	**454**	584	(22)%	**-**	-	-	**45**	58	(22)%	**454**	584	(22)%
Fixed index annuities	**295**	534	(45)%	**-**	-	-	**30**	54	(44)%	**295**	534	(45)%
Wholesale	**2,324**	1,930	20%	**-**	-	-	**232**	193	20%	**2,324**	1,930	20%
Total US insurance operations	**16,622**	16,405	1%	**-**	-	-	**1,662**	1,641	1%	**16,622**	16,405	1%
UK and Europe insurance operations												
Bonds	**3,509**	3,834	(8)%	**-**	-	-	**351**	384	(9)%	**3,510**	3,835	(8)%
Corporate pensions	**103**	110	(6)%	**130**	121	7%	**140**	132	6%	**533**	479	11%
Individual pensions	**5,747**	2,532	127%	**32**	35	(9)%	**607**	289	110%	**5,897**	2,681	120%
Income drawdown	**2,218**	1,649	35%	**-**	-	-	**222**	165	35%	**2,218**	1,649	35%
Other products	**1,467**	1,711	(14)%	**25**	21	19%	**171**	190	(10)%	**1,626**	1,869	(13)%
Total UK and Europe insurance operations	**13,044**	9,836	33%	**187**	177	6%	**1,491**	1,160	29%	**13,784**	10,513	31%
Group total	**31,965**	28,750	11%	**3,762**	3,699	2%	**6,958**	6,574	6%	**50,811**	47,098	8%

Schedule A(iii) Total Insurance New Business APE (Actual and Constant Exchange Rates)

Note: Comparative results for the first half (H1) and second half (H2) of 2016 and H1 2017 are presented on both actual exchange rates (AER) and constant exchange rates (CER). The H2 2017 amounts are presented on actual exchange rates (including the effect of retranslating H1 results for movements in average exchange rates between H1 and H2).

	AER				**CER**			
	2016		**2017**		**2016**		**2017**	
	H1	**H2**	**H1**	**H2**	**H1**	**H2**	**H1**	**H2**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Group insurance operations								
Asia	1,605	1,994	1,943	1,862	1,779	1,994	1,908	1,897
US	782	779	960	702	869	772	939	723
UK and Europe	593	567	721	770	593	567	721	770
Group total	**2,980**	**3,340**	**3,624**	**3,334**	**3,241**	**3,333**	**3,568**	**3,390**
Asia insurance operations								
Cambodia	6	8	8	8	6	8	8	8
Hong Kong	868	1,044	914	811	962	1,040	891	834
Indonesia	125	154	144	153	139	153	140	157
Malaysia	109	135	128	150	116	130	127	151
Philippines	30	40	36	41	31	39	35	42
Singapore	142	209	195	252	158	211	194	253
Thailand	43	46	42	42	50	47	42	42
Vietnam	44	72	62	72	49	71	61	73
SE Asia operations including Hong Kong	**1,367**	**1,708**	**1,529**	**1,529**	**1,511**	**1,699**	**1,498**	**1,560**
China[6]	109	90	187	107	118	88	186	108
Taiwan	56	94	105	108	67	100	104	109
India[4]	73	102	122	118	83	107	120	120
Total Asia insurance operations	**1,605**	**1,994**	**1,943**	**1,862**	**1,779**	**1,994**	**1,908**	**1,897**
US insurance operations								
Variable annuities	500	565	604	550	556	564	591	563
Elite Access (variable annuity)	99	107	110	91	110	106	107	94
Fixed annuities	28	27	24	21	32	26	24	21
Fixed index annuities	28	23	16	14	30	24	16	14
Wholesale	127	57	206	26	141	52	201	31
Total US insurance operations	**782**	**779**	**960**	**702**	**869**	**772**	**939**	**723**
UK and Europe insurance operations								
Bonds	196	188	174	177	196	188	174	177
Corporate pensions	74	58	75	65	74	58	75	65
Individual pensions	134	155	279	328	134	155	279	328
Income drawdown	81	84	106	116	81	84	106	116
Other products	108	82	87	84	108	82	87	84
Total UK and Europe insurance operations	**593**	**567**	**721**	**770**	**593**	**567**	**721**	**770**
Group total	**2,980**	**3,340**	**3,624**	**3,334**	**3,241**	**3,333**	**3,568**	**3,390**

Schedule A(iv) Investment Operations (Actual Exchange Rates)

Note: The H1 and H2 of 2016 and H1 2017 comparative results are shown below on actual exchange rates (AER) as previously reported.

	2016		2017	
	H1 £m	H2 £m	H1 £m	H2 £m
Group investment operations				
Opening FUM	156,686	162,384	174,805	193,714
Net Flows:[8]	(7,378)	1,123	9,452	11,026
- Gross Inflows	15,894	24,239	34,213	35,201
- Redemptions	(23,272)	(23,116)	(24,761)	(24,175)
Other Movements	13,076	11,298	9,457	5,683
Group total[9]	**162,384**	**174,805**	**193,714**	**210,423**
M&G Prudential				
Retail				
Opening FUM	60,801	59,217	64,209	72,500
Net Flows:	(6,122)	(131)	5,515	5,528
- Gross Inflows	6,160	9,625	15,871	15,078
- Redemptions	(12,282)	(9,756)	(10,356)	(9,550)
Other Movements	4,538	5,123	2,776	1,669
Closing FUM	**59,217**	**64,209**	**72,500**	**79,697**
Comprising amounts for:				
UK	34,308	35,208	35,201	35,740
Europe (excluding UK)	23,020	26,905	35,192	42,321
South Africa	1,889	2,096	2,107	1,636
	59,217	**64,209**	**72,500**	**79,697**
Institutional[3]				
Opening FUM	65,604	70,439	72,554	76,618
Net Flows:	(844)	(993)	1,664	4,630
- Gross Inflows	3,571	3,485	6,806	8,414
- Redemptions	(4,415)	(4,478)	(5,142)	(3,784)
Other Movements	5,679	3,108	2,400	2,910
Closing FUM	**70,439**	**72,554**	**76,618**	**84,158**
Total M&G Prudential	**129,656**	**136,763**	**149,118**	**163,855**
PPM South Africa FUM included in total M&G Prudential	**5,354**	**6,047**	**5,427**	**5,963**
Eastspring - excluding MMF[8]				
Third party retail[7]				
Opening FUM	25,541	27,155	30,793	36,093
Net Flows:	(787)	1,237	2,186	1,567
- Gross Inflows	5,650	9,875	10,781	11,017
- Redemptions	(6,437)	(8,638)	(8,595)	(9,450)
Other Movements	2,401	2,401	3,114	1,016
Closing FUM[5]	**27,155**	**30,793**	**36,093**	**38,676**
Third party institutional				
Opening FUM	4,740	5,573	7,249	8,503
Net Flows:	375	1,010	87	(699)
- Gross Inflows	513	1,254	755	692
- Redemptions	(138)	(244)	(668)	(1,391)
Other Movements	458	666	1,167	88
Closing FUM[5]	**5,573**	**7,249**	**8,503**	**7,892**
Total Eastspring investment operations (excluding MMF)	**32,728**	**38,042**	**44,596**	**46,568**

Schedule A(v) Total Insurance New Business Profit (Actual and Constant Exchange Rates)

Note: Comparative results for half year (HY) and full year (FY) 2016 and half year 2017 are presented on both actual exchange rates (AER) and constant exchange rates (CER). The full year 2017 results are presented on actual exchange rates.

	AER				CER			
	2016		2017		2016		2017	
	HY £m	FY £m	HY £m	FY £m	HY £m	FY £m	HY £m	FY £m
New Business Profit								
Total Asia insurance operations	821	2,030	1,092	2,368	908	2,123	1,069	2,368
Total US insurance operations	311	790	436	906	346	830	426	906
Total UK and Europe insurance operations	125	268	161	342	125	268	161	342
Group total	**1,257**	**3,088**	**1,689**	**3,616**	**1,379**	**3,221**	**1,656**	**3,616**
APE[(2)]								
Total Asia insurance operations	1,605	3,599	1,943	3,805	1,779	3,773	1,908	3,805
Total US insurance operations	782	1,561	960	1,662	869	1,641	939	1,662
Total UK and Europe insurance operations	593	1,160	721	1,491	593	1,160	721	1,491
Group total	**2,980**	**6,320**	**3,624**	**6,958**	**3,241**	**6,574**	**3,568**	**6,958**
New Business Margin (NBP as % of APE)								
Total Asia insurance operations	51%	56%	56%	62%	51%	56%	56%	62%
Total US insurance operations	40%	51%	45%	55%	40%	51%	45%	55%
Total UK and Europe insurance operations	21%	23%	22%	23%	21%	23%	22%	23%
Group total	**42%**	**49%**	**47%**	**52%**	**43%**	**49%**	**46%**	**52%**
PVNBP[(2)]								
Total Asia insurance operations	8,679	19,271	10,095	20,405	9,609	20,180	9,914	20,405
Total US insurance operations	7,816	15,608	9,602	16,622	8,690	16,405	9,387	16,622
Total UK and Europe insurance operations	5,267	10,513	6,616	13,784	5,267	10,513	6,616	13,784
Group total	**21,762**	**45,392**	**26,313**	**50,811**	**23,566**	**47,098**	**25,917**	**50,811**
New Business Margin (NBP as % of PVNBP)								
Total Asia insurance operations	9.5%	10.5%	10.8%	11.6%	9.4%	10.5%	10.8%	11.6%
Total US insurance operations	4.0%	5.1%	4.5%	5.5%	4.0%	5.1%	4.5%	5.5%
Total UK and Europe insurance operations	2.4%	2.5%	2.4%	2.5%	2.4%	2.5%	2.4%	2.5%
Group total	**5.8%**	**6.8%**	**6.4%**	**7.1%**	**5.9%**	**6.8%**	**6.4%**	**7.1%**

B Reconciliation of expected transfer of value of in-force business and required capital to free surplus

The tables below show how the value of in-force business (VIF) generated by the in-force long-term business and the associated required capital is modelled as emerging into free surplus over the next 40 years. Although a small amount (less than 4 per cent) of the Group's embedded value emerges after this date, analysis of cash flows emerging in the years shown in the tables is considered most meaningful. The modelled cash flows use the same methodology underpinning the Group's embedded value reporting and so are subject to the same assumptions and sensitivities used to prepare our 2017 results.

In addition to showing the amounts, both discounted and undiscounted, expected to be generated from all in-force business at 31 December 2017, the tables also present the expected future free surplus to be generated from the investment made in new business during 2017 over the same 40-year period for long-term business operations.

(i) Expected transfer of value of in-force business (VIF) and required capital to free surplus

	31 Dec 2017 £m							
	Undiscounted expected generation from all in-force business*				Undiscounted expected generation from new business written*			
Expected period of emergence	Asia	US	UK and Europe	Total	Asia	US	UK and Europe	Total
2018	1,393	1,464	671	**3,528**	197	226	36	**459**
2019	1,352	1,425	685	**3,462**	182	113	38	**333**
2020	1,299	1,483	674	**3,456**	181	124	40	**345**
2021	1,256	1,551	660	**3,467**	162	155	43	**360**
2022	1,239	1,441	638	**3,318**	164	129	48	**341**
2023	1,202	1,433	618	**3,253**	139	65	44	**248**
2024	1,171	1,404	601	**3,176**	142	73	40	**255**
2025	1,149	1,277	580	**3,006**	136	179	39	**354**
2026	1,154	1,158	553	**2,865**	131	154	39	**324**
2027	1,109	1,051	526	**2,686**	141	138	38	**317**
2028	1,066	897	499	**2,462**	121	125	36	**282**
2029	1,032	840	473	**2,345**	125	114	32	**271**
2030	1,003	731	448	**2,182**	116	99	31	**246**
2031	980	612	422	**2,014**	117	89	30	**236**
2032	971	514	532	**2,017**	134	78	30	**242**
2033	919	325	498	**1,742**	112	51	28	**191**
2034	898	333	467	**1,698**	113	32	26	**171**
2035	885	189	434	**1,508**	112	29	25	**166**
2036	868	140	402	**1,410**	111	23	23	**157**
2037	854	90	370	**1,314**	120	21	22	**163**
2038-2042	4,252	286	1,401	**5,939**	581	-	83	**664**
2043-2047	4,280	-	972	**5,252**	719	-	76	**795**
2048-2052	3,948	-	385	**4,333**	737	-	9	**746**
2053-2057	3,490	-	197	**3,687**	714	-	5	**719**
Total free surplus expected to emerge in the next 40 years	37,770	18,644	13,706	**70,120**	5,507	2,017	861	**8,385**

* The analysis excludes amounts incorporated into VIF at 31 December 2017 where there is no definitive timeframe for when the payments will be made or receipts received. In particular, it excludes the value of the shareholders' interest in the with-profits estate. It also excludes any free surplus emerging after 2057.

The above amounts can be reconciled to the new business amounts as follows:

	2017 £m			
	Asia	US	UK and Europe	Total
Undiscounted expected free surplus generation for years 2018 to 2057	5,507	2,017	861	**8,385**
Less: discount effect	(3,153)	(689)	(339)	**(4,181)**
Discounted expected free surplus generation for years 2018 to 2057	2,354	1,328	522	**4,204**
Discounted expected free surplus generation for years after 2057	442	-	1	**443**
Less: Free surplus investment in new business	(484)	(254)	(175)	**(913)**
Other items**	56	(168)	(6)	**(118)**
Post-tax EEV new business profit for long-term business operations	2,368	906	342	**3,616**

** Other items represent the impact of the time value of options and guarantees on new business, foreign exchange effects and other non-modelled items. Foreign exchange effects arise as EEV new business profit amounts are translated at average exchange rates and the expected free surplus generation uses year end closing rates.

The undiscounted expected free surplus generation from all in-force business at 31 December 2017 shown below can be reconciled to the amount that was expected to be generated as at 31 December 2016 as follows:

Group	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	Other £m	Total £m
2016 expected free surplus generation for years 2017 to 2056	3,441	3,195	3,111	3,070	3,030	2,865	45,321	**64,033**
Less: Amounts expected to be realised in the current year	(3,441)	-	-	-	-	-	-	**(3,441)**
Add: Expected free surplus to be generated in year 2057*	-	-	-	-	-	-	578	**578**
Foreign exchange differences	-	(180)	(176)	(176)	(175)	(163)	(2,225)	**(3,095)**
New business	-	459	333	345	360	341	6,547	**8,385**
Operating movements	-	(130)	(96)	(63)	(34)	(5)		
Non-operating and other movements	-	184	290	280	286	280	2,668	**3,660**
2017 expected free surplus generation for years 2018 to 2057	-	3,528	3,462	3,456	3,467	3,318	52,889	**70,120**

Asia	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	Other £m	Total £m
2016 expected free surplus generation for years 2017 to 2056	1,320	1,247	1,202	1,167	1,142	1,122	27,080	**34,280**
Less: Amounts expected to be realised in the current year	(1,320)	-	-	-	-	-	-	**(1,320)**
Add: Expected free surplus to be generated in year 2057*	-	-	-	-	-	-	540	**540**
Foreign exchange differences	-	(69)	(66)	(65)	(64)	(63)	(1,511)	**(1,838)**
New business	-	197	182	181	162	164	4,621	**5,507**
Operating movements	-	11	15	-	(8)	(17)		
Non-operating and other movements	-	7	19	16	24	33	501	**601**
2017 expected free surplus generation for years 2018 to 2057	-	1,393	1,352	1,299	1,256	1,239	31,231	**37,770**

US	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	Other £m	Total £m
2016 expected free surplus generation for years 2017 to 2056	1,446	1,279	1,273	1,281	1,282	1,152	8,257	**15,970**
Less: Amounts expected to be realised in the current year	(1,446)	-	-	-	-	-	-	**(1,446)**
Foreign exchange differences	-	(111)	(110)	(111)	(111)	(100)	(714)	**(1,257)**
New business	-	226	113	124	155	129	1,270	**2,017**
Operating movements	-	(72)	(48)	(8)	24	57		
Non-operating and other movements	-	142	197	197	201	203	2,467	**3,360**
2017 expected free surplus generation for years 2018 to 2057	-	1,464	1,425	1,483	1,551	1,441	11,280	**18,644**

UK and Europe	2017 £m	2018 £m	2019 £m	2020 £m	2021 £m	2022 £m	Other £m	Total £m
2016 expected free surplus generation for years 2017 to 2056	675	669	636	622	606	591	9,984	**13,783**
Less: Amounts expected to be realised in the current year	(675)	-	-	-	-	-	-	**(675)**
Add: Expected free surplus to be generated in year 2057*	-	-	-	-	-	-	38	**38**
New business	-	36	38	40	43	48	656	**861**
Operating movements	-	(69)	(63)	(55)	(50)	(45)		
Non-operating and other movements	-	35	74	67	61	44	(300)	**(301)**
2017 expected free surplus generation for years 2018 to 2057	-	671	685	674	660	638	10,378	**13,706**

* Excluding 2017 new business.

At 31 December 2017, the total free surplus expected to be generated over the next five years (2018 to 2022 inclusive), using the same assumptions and methodology as those underpinning our 2017 embedded value reporting was £17.2 billion, an increase of £1.4 billion from the £15.8 billion expected over an equivalent period from the end of 2016.

This increase primarily reflects the new business written in 2017, which is expected to generate £1,838 million of free surplus over the next five years.

At 31 December 2017, the total free surplus expected to be generated on an undiscounted basis in the next 40 years is £70.1 billion, up from the £64.0 billion expected at the end of 2016, reflecting the effect of new business written across all three business operations of £8.4 billion, a negative foreign exchange translation effect of £(3.1) billion and a £3.7 billion net effect reflecting operating, market assumption changes and other items. In Asia, these include the effect of changes in operating assumptions reflecting the net benefit arising from annual review of experience, together with the benefit of management actions. In the US, these mainly reflect the positive effect from persistency assumption updates and increase in equity market returns, together with the benefits from US tax reform, partially offset by lower future separate account return due to the decrease in interest rates. In the UK and Europe, these reflect the impact of management actions which had the effect of accelerating the generation of future free surplus into 2017, partially offset by higher than assumed investment returns on with-profits funds. The overall growth in the Group's undiscounted value of free surplus reflects our ability to write both growing and profitable new business.

Actual underlying free surplus generated in 2017 from life business in force before restructuring costs at the end of 2017 was £4.1 billion including £0.6 billion of changes in operating assumptions and experience variances. This compares with the expected 2017 realisation at the end of 2016 of £3.4 billion. This can be analysed further as follows:

	Asia £m	US £m	UK and Europe £m	Total £m
Transfer to free surplus in 2017	**1,275**	**1,329**	**675**	**3,279**
Expected return on free assets	**51**	**56**	**31**	**138**
Changes in operating assumptions and experience variances	**81**	**190**	**364**	**635**
Underlying free surplus generated from in-force life business before restructuring costs in 2017	**1,407**	**1,575**	**1,070**	**4,052**
2017 free surplus expected to be generated at 31 December 2016	1,320	1,446	675	3,441

The equivalent discounted amounts of the undiscounted expected transfers from in-force business and required capital into free surplus shown previously are as follows:

	31 Dec 2017 £m							
	Discounted expected generation from all in-force business				Discounted expected generation from new business written			
Expected period of emergence	Asia	US	UK and Europe	Total	Asia	US	UK and Europe	Total
2018	1,337	1,400	655	**3,392**	188	220	35	**443**
2019	1,218	1,282	645	**3,145**	161	103	36	**300**
2020	1,102	1,254	610	**2,966**	150	107	38	**295**
2021	997	1,234	573	**2,804**	127	124	39	**290**
2022	929	1,077	529	**2,535**	121	99	41	**261**
2023	845	1,008	487	**2,340**	98	46	36	**180**
2024	777	930	452	**2,159**	96	51	32	**179**
2025	718	795	415	**1,928**	86	112	30	**228**
2026	679	680	375	**1,734**	78	89	28	**195**
2027	619	580	337	**1,536**	80	75	25	**180**
2028	561	467	303	**1,331**	64	64	22	**150**
2029	515	410	272	**1,197**	62	54	20	**136**
2030	477	337	241	**1,055**	55	44	18	**117**
2031	445	268	212	**925**	52	37	16	**105**
2032	420	215	261	**896**	56	31	15	**102**
2033	376	124	229	**729**	45	24	13	**82**
2034	350	123	202	**675**	44	16	12	**72**
2035	329	72	176	**577**	42	14	10	**66**
2036	309	52	156	**517**	39	10	9	**58**
2037	291	30	136	**457**	42	8	7	**57**
2038-2042	1,314	117	465	**1,896**	180	-	30	**210**
2043-2047	1,101	-	117	**1,218**	192	-	7	**199**
2048-2052	837	-	89	**926**	166	-	2	**168**
2053-2057	593	-	33	**626**	130	-	1	**131**
Total discounted free surplus expected to emerge in the next 40 years	17,139	12,455	7,970	**37,564**	2,354	1,328	522	**4,204**

The above amounts can be reconciled to the Group's EEV basis financial statements as follows:

	31 Dec 2017 £m
Discounted expected generation from all in-force business for years 2018 to 2057	**37,564**
Discounted expected generation from all in-force business for years after 2057	**1,576**
Discounted expected generation from all in-force business at 31 December 2017	**39,140**
Add: Free surplus of life operations held at 31 December 2017	**6,242**
Less: Time value of guarantees	**(836)**
Other non-modelled items	**1,371**
Total EEV for long-term business operations	**45,917**

C 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:

2017 Free surplus and Group IFRS results

	Underlying free surplus generated for total insurance and asset management operations %	Group IFRS pre-tax operating profit % notes (2)(3)	Group IFRS shareholders' funds % notes (2)(3)
US dollar linked[note (1)]	**13%**	**24%**	**21%**
Other Asia currencies	**17%**	**18%**	**16%**
Total Asia	**30%**	**42%**	**37%**
UK sterling[notes (2)(3)]	**34%**	**11%**	**50%**
US dollar[note (3)]	**36%**	**47%**	**13%**
Total	**100%**	**100%**	**100%**

2017 Group EEV post-tax results

	New business profits %	Operating profit % notes (2)(3)	Shareholders' funds % notes (2)(3)
US dollar linked[note (1)]	**54%**	**46%**	**37%**
Other Asia currencies	**12%**	**12%**	**11%**
Total Asia	**66%**	**58%**	**48%**
UK sterling[notes (2)(3)]	**9%**	**9%**	**29%**
US dollar[note (3)]	**25%**	**33%**	**23%**
Total	**100%**	**100%**	**100%**

Notes

(1) US dollar linked comprise 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) For operating profit and shareholders' funds, UK sterling includes amounts in respect of M&G Prudential and other operations (including central operations, Africa operations and Prudential Capital). Operating profit for central operations includes amounts for corporate expenditure for Group Head Office as well as Asia Regional Head Office which is incurred in HK dollars.

(3) For shareholders' funds, the US dollar grouping includes US dollar denominated core structural borrowings. Sterling operating profits include all interest payable as sterling denominated, reflecting interest rate currency swaps in place.

D Reconciliation between IFRS and EEV shareholders' funds

The table below shows the reconciliation of EEV shareholders' funds and IFRS shareholders' funds at the end of the year:

	31 Dec 2017 £m	31 Dec 2016 £m
EEV shareholders' funds	**44,698**	38,968
Less: Value of in-force business of long-term business[note (a)]	**(29,410)**	(24,937)
Deferred acquisition costs assigned zero value for EEV purposes	**9,227**	9,170
Other[note (b)]	**(8,428)**	(8,535)
IFRS shareholders' funds	**16,087**	14,666

Notes

(a) The EEV shareholders' funds comprises the present value of the shareholders' interest in the value of in-force business, net worth of long-term business operations and IFRS shareholders' funds of asset management and other operations. The value of in-force business reflects the present value of future shareholder cash flows from long-term in-force business which are not captured as shareholders' interest on an IFRS basis. Net worth represents the net assets for EEV reporting purposes that reflect the regulatory basis position, sometimes with adjustments to achieve consistency with the IFRS treatment of certain items.

(b) Other adjustments represent asset and liability valuation differences between IFRS and the local regulatory reporting basis used to value net worth for long-term insurance operations. For the UK, this would be the difference between IFRS and Solvency II.

It also includes the mark to market of the Group's core structural borrowings which are fair valued under EEV but not IFRS. The most significant valuation differences relate to changes in the valuation of insurance liabilities. For example, in Jackson where IFRS liabilities are higher than the local regulatory basis as they are principally based on policyholder account balances (with a deferred acquisition costs recognised as an asset) whereas the local regulatory basis used for EEV is based on future cash flows due to the policyholder on a prudent basis with consideration of an expense allowance as applicable, but with no separate deferred acquisition cost asset.

E Reconciliation of APE new business sales to earned premiums

The Group reports APE new business sales as a measure of the new policies sold in the year. This differs from the IFRS measure of premiums earned as shown below:

	2017 £m	2016 £m
Annual premium equivalents as published	**6,958**	6,320
Adjustment to include 100% of single premiums on new business sold in the year[note (a)]	**28,769**	25,057
Premiums from in-force business and other adjustments[note (b)]	**8,278**	7,604
Gross premiums earned	**44,005**	38,981
Outward reinsurance premiums	**(2,062)**	(2,020)
Earned premiums, net of reinsurance as shown in the IFRS financial statements	**41,943**	36,961

Notes

(a) APE new business sales only include one tenth of single premiums, recorded on policies sold in the year. Gross premiums earned include 100 per cent of such premiums.

(b) Other adjustments principally include amounts in respect of the following:

- Gross premiums earned include premiums from existing in-force business as well as new business. The most significant amount is recorded in Asia, where a significant portion of regular premium business is written. Asia in-force premiums form the vast majority of the other adjustment amount;
- APE includes new policies written in the year which are classified as investment contracts without discretionary participation features under IFRS 4, arising mainly in Jackson for guaranteed investment contracts and in M&G Prudential for certain unit-linked savings and similar contracts. These are excluded from gross premiums earned and recorded as deposits;
- APE new business sales are annualised while gross premiums earned are recorded only when revenues are due; and
- For the purpose of reporting APE new business sales, we include the Group's share of amounts sold by the Group's insurance joint ventures and associates. Under IFRS, joint ventures and associates are equity accounted and so no amounts are included within gross premiums earned.

F Calculation of return on embedded value

Return on embedded value is calculated as the EEV post-tax operating profit based on longer-term investment returns, as a percentage of opening EEV basis shareholders' funds.

	Note	2017	2016
Operating profit based on longer-term investment returns (£ million)	2	**6,598**	5,497
Opening EEV basis shareholders' funds (£ million)	9	**38,968**	31,886
Return on embedded value		**17%**	17%

G Calculation of EEV shareholders' funds per share

EEV shareholders' funds per share is calculated as closing EEV shareholders' funds divided by the number of issued shares at the balance sheet date. EEV shareholders' funds per share excluding goodwill attributable to shareholders is calculated in the same manner, except goodwill attributable to shareholders is deducted from closing EEV shareholders' funds.

	Note	31 Dec 2017	31 Dec 2016
Closing EEV shareholders' funds (£ million)	9	**44,698**	38,968
Less: Goodwill attributable to shareholders (£ million)	9	**(1,458)**	(1,475)
Closing EEV shareholders' funds excluding goodwill attributable to shareholders (£ million)		**43,240**	37,493
Number of issued shares at year end (millions)		**2,587**	2,581
Shareholders' funds per share (in pence)		**1,728p**	1,510p
Shareholders' funds per share excluding goodwill attributable to shareholders (in pence)		**1,671p**	1,453p

Risk Factors

A number of 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, 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 'Report on the risks facing our business and how these are managed' section of this document.

Risks relating to Prudential's business

Prudential's businesses are inherently subject to market fluctuations and general economic conditions

Uncertainty, fluctuations or negative trends in international economic and investment climates could have a material adverse effect on Prudential's business and profitability. Prudential operates in a macroeconomic and global financial market environment that presents significant uncertainties and potential challenges, For example, government interest rates remain low in the US, the UK and some Asian countries in which Prudential operates.

Global financial markets are subject to uncertainty and volatility created by a variety of factors. These factors include the reduction in accommodative monetary policies in the US, the UK and other jurisdictions together with its impact on the valuation of all asset classes, effects on interest rates and the risk of disorderly repricing of inflation expectations and global bond yields, concerns over sovereign debt, a general slowing in world growth, the increased level of geopolitical risk and policy-related uncertainty and potentially negative socio-political events.

The adverse effects of such factors could be felt principally through the following items:

- Reduced investment returns arising on the Group's portfolios including impairment of debt securities and loans, which could reduce Prudential's capital and impair its ability to write significant volumes of new business, increase the potential adverse impact of product guarantees, and/or 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 who have transactions with Prudential (eg banks and reinsurers) to meet commitments that could give rise to a negative impact on Prudential's financial position and on the accessibility or recoverability of amounts due or, for derivative transactions, adequate collateral not being in place;

- Estimates of the value of financial instruments becoming more 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, which also adds to uncertainty over the accessibility of financial resources and may reduce capital resources as valuations decline. This could occur where external capital is unavailable at sustainable cost, increased liquid assets are required to be held as collateral under derivative transactions or redemption restrictions are placed on Prudential's investments in illiquid funds. In addition, significant redemption requests could also be made on Prudential's issued funds and while this may not have a direct impact on the Group's liquidity, it could result in reputational damage to Prudential. The potential impact of increased illiquidity is more uncertain than for other risks such as interest rate or credit risk.

In general, upheavals in the financial markets may affect general levels of economic activity, employment and customer behaviour. As a result, 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. In addition, there may be a higher incidence of counterparty failures. 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 its balance sheet and profitability. For example, this could occur if the recoverable value of intangible assets for bancassurance agreements and deferred acquisition costs are reduced. 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 premium and claim 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 those used to calculate premium and claim values over a sustained period, this could have a material adverse effect on Prudential's reported profit.

In the US, Jackson writes a significant amount of variable annuities that offer capital or income protection guarantees. The value of these guarantees is affected by market factors (such as interest rates, equity values, bond spreads and realised volatility) and policyholder behaviour. Jackson uses a derivative hedging programme to reduce its exposure to market risks arising on these guarantees. There could be market circumstances where the derivatives that Jackson enters into to hedge its market risks may not cover its exposures under the guarantees. The cost of the guarantees that remain unhedged will also affect Prudential's results.

In addition, Jackson hedges the guarantees on its variable annuity book on an economic basis (with consideration of the local regulatory position) and, thus, accepts variability in its accounting results in the short term in order to achieve the appropriate result on these bases. 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 or local regulatory results that may be less significant under IFRS reporting.

Also, in the US, fluctuations in prevailing interest rates can affect results from Jackson which has a significant spread-based business, with the significant proportion 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 surrender levels arising from interest rate rises, could have a material impact on its businesses or results of operations.

On 29 March 2017 the UK submitted the formal notification of its intention to withdraw from the EU pursuant to Article 50 of the Treaty on the European Union, as amended. Following submission of this notification, the UK has a maximum period of two years to negotiate the terms of its withdrawal from the EU. If no formal withdrawal agreement is reached between the UK and the EU, then it is expected the UK's membership of the EU will automatically terminate two years after the submission of the notification of the UK's intention to withdraw from the EU. The UK's decision to leave the EU will have political, legal and economic ramifications for both the UK and the EU, although these are expected to be more pronounced for the UK. The Group has several UK domiciled operations, including M&G Prudential, and these may be impacted by a UK withdrawal from the EU. The outcome of the negotiations on the UK's withdrawal and any subsequent negotiations on trade and access to the country's major trading markets, including the single EU market, is currently unknown. As a result, there is ongoing uncertainty over the terms under which the UK will leave the EU, whether any transitional arrangements will be agreed between the UK and the EU, the possibility of a lengthy period before negotiations are concluded, and the potential for a disorderly exit by the UK without a negotiated agreement. This uncertainty may increase volatility in the markets where the Group operates and create the potential for a general downturn in economic activity and for further or prolonged interest rate reductions in some jurisdictions due to monetary easing and investor sentiment.

A significant part of the profit from M&G Prudential's 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

Investing in sovereign debt creates exposure to the direct or indirect consequences of political, social or economic changes (including changes in governments, heads of state 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 adversely affected, as might counterparty relationships between financial institutions. If a sovereign were to default on its obligations, or adopted policies that devalued or otherwise altered the currencies in which its obligations were 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 the 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 financial reporting ratios such as dividend cover, which is calculated as operating profit after tax on an IFRS basis, divided by the dividends relating to the reporting year. 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 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 with possible consequences for the degree of flexibility that Prudential has in managing its business.

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 and legislation (including in relation to tax), capital control measures on companies and individuals, regulation or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which Prudential operates, or decisions taken by regulators in connection with their supervision of members of the Group, which in some circumstances may be applied retrospectively may adversely affect Prudential. The adverse impact from these changes may affect Prudential's product range, distribution channels, competitiveness, profitability, capital requirements, risk management approaches, corporate or governance structure and, consequently, reported results and financing requirements. Also, regulators in jurisdictions in which Prudential operates may impose requirements affecting the allocation of capital and liquidity between different business units in the Group, whether on a geographic, legal entity, product line or other basis. Regulators 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 following recent financial and global economic conditions, there may continue to be changes in government regulation and supervision of the financial services industry, including the possibility of higher capital requirements, restrictions on certain types of transactions and enhanced supervisory powers.

Recent shifts in the focus of some national governments toward more protectionist or restrictive economic and trade policies could impact on the degree and nature of regulatory changes and Prudential's competitive position in some geographic markets. This could take effect, for example, through increased friction in cross-border trade or measures favouring local enterprises such as changes to the maximum level of non-domestic ownership by foreign companies.

The European Union's Solvency II Directive came into effect on 1 January 2016. This measure of regulatory capital is more volatile than under the previous Solvency I regime and regulatory policy may evolve under the new regime. The European Commission began a review in late 2016 of some aspects of the Solvency II legislation, which is expected to continue until 2021 and covers, among other things, a review of the Long Term Guarantee measures. Prudential applied for, and has been granted approval by the UK Prudential Regulation Authority to use the following measures when calculating its Solvency II capital requirements: the use of an internal model, the 'matching adjustment' for UK annuities, the 'volatility adjustment' for selected US Dollar-denominated business, and UK transitional measures. Prudential also has permission to use 'deduction and aggregation' as the method by which the contribution of the Group's US insurance entities to the Group's solvency is calculated, which in effect recognises surplus in US insurance entities in excess of 250 per cent of local US Risk Based Capital requirements. There is a risk that in the future changes are required to be made to the approved internal model and these related applications which could have a material impact on the Group Solvency II capital position. Where internal model changes are subject to regulatory approval, there is a risk that the approval is delayed or not given. In such circumstances, changes in our risk profile would not be able to be appropriately reflected in our internal model, which could have a material impact on the Group's Solvency II capital position.

The UK's decision to leave the EU could result in significant changes to the legal and regulatory regime under which the Group operates, the nature and extent of which are uncertain while the outcome of negotiations regarding the UK's withdrawal from the EU and the extent and terms of any future access to the single EU market remains unknown.

Currently there are also a number of other global regulatory developments which could impact Prudential's businesses 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), the Insurance Capital Standard (ICS) being developed by the International Association of Insurance Supervisors (IAIS), the Markets in Financial Instruments Directive (the "MiFID II Directive"), which recently came into force in the EU and the EU General Data Protection Regulation that comes into force in May 2018. In addition, regulators in a number of jurisdictions in which the Group operates are further developing local capital regimes; this includes potential future developments in Solvency II in the UK (as referred to above), National Association of Insurance Commissioners' reforms in the US including any implications from the recently enacted US tax reform legislation and amendments to certain local statutory regimes in some territories in Asia. There remains a high degree of uncertainty over the potential impact of these changes on the Group.

The Dodd-Frank Act provides for a comprehensive overhaul of the financial services industry within the US including reforms to financial services entities, products and markets. The full impact of the Dodd-Frank Act on Prudential's businesses remains unclear, as many of its provisions are primarily focused on the banking industry, have a delayed effectiveness and/or require rulemaking or other actions by various US regulators over the coming years. There is also potential uncertainty surrounding future changes to the Dodd-Frank Act under the current US administration.

Prudential's designation as a G-SII was reaffirmed on 21 November 2016. As a result of this designation, Prudential is subject to additional regulatory requirements, including a requirement to submit enhanced risk management plans (such as a Group-wide Recovery Plan, a Systemic Risk Management Plan and a Liquidity Risk Management Plan) to a Crisis Management Group (CMG) comprised of an international panel of regulators.

The G-SII regime also introduces capital requirements in the form of a Higher Loss Absorption (HLA) requirement. While this requirement was initially intended to come into force in 2019, this has now been postponed to 2022. The HLA is also now intended to be based on the ICS. The IAIS has announced that the implementation of ICS will be conducted in two phases – a five-year monitoring phase followed by an implementation phase. During the monitoring phase, Internationally Active Insurance Groups, for which Prudential satisfies the criteria, will be required to report on compliance with the ICS to the group-wide supervisor on a confidential basis, although these results will not be used as a basis to trigger supervisory action. The Common Framework (ComFrame) for the Supervision of Supervision of Internationally Active Insurance Groups will more generally establish a set of common principles and standards designed to assist regulators in addressing risks that arise from insurance groups with operations in multiple jurisdictions.

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 in which 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, under its standard IFRS 4 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 May 2017, the IASB published its replacement standard on insurance accounting (IFRS 17, 'Insurance Contracts'), which will have the effect of introducing fundamental changes to the statutory reporting of insurance entities that prepare accounts according to IFRS from 2021. The European Union will apply its usual process for assessing whether the standard meets the necessary criteria for endorsement. The Group is reviewing the complex requirements of this standard and considering its potential impact. The effect of changes required to the Group's accounting policies as a result of implementing the new standard is currently uncertain, but these changes can be expected to, amongst other things, alter the timing of IFRS profit recognition. The implementation of this standard is also likely to require significant enhancements to IT, actuarial and finance systems of the Group, and so will have an increase on the Group's expenses.

Any changes or modification of IFRS accounting policies may require a change in the way in which future results will be determined and/or a retrospective adjustment of reported results to ensure consistency.

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. Such actions may relate to the application of current regulations for example the Financial Conduct Authority's (FCA) principles and conduct of business rules or the failure to implement new regulations. 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 pensions 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. Current regulatory actions include the UK business's undertaking to the FCA to review annuities sold without advice after 1 July 2008 to its contract-based defined contribution pension customers. This will result in the UK business being required to provide redress to certain such customers, the ultimate amount of which remains uncertain.

Regulators may also focus on 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 attention on the different regulatory standards applied to investment advice delivered to retail customers by different sectors of the industry. As a result of reports relating to perceptions of industry abuses, there have been numerous regulatory inquiries and proposals for legislative and regulatory reforms. This includes focus on the suitability of sales of certain products, alternative investments and the widening of the circumstances under which a person or entity providing investment advice with respect to certain employee benefit and pension plans would be considered a fiduciary (subjecting the person or entity to certain regulatory requirements, such as those adopted by the US Department of Labor (DoL). Elements of the DoL fiduciary duty rules, including the impartial conduct standards, became effective on 9 June 2017 but applicability of the remaining components of the rules has been delayed until 1 July 2019. There is a risk that new regulations introduced may have a material adverse effect on the sales of the products by Prudential and increase Prudential's exposure to legal risks.

Litigation, disputes and regulatory investigations may adversely affect Prudential's profitability and financial condition

Prudential is, and may in the future be, 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 respects 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 imposed and the inherent unpredictability of litigation and disputes, it is possible that an adverse outcome could 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 upon 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, the ability to respond to developing demographic trends, customer appetite for certain savings products and technological advances. 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. 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 include global life insurers such as Allianz, AXA, and Manulife together with regional insurers such as AIA and Great Eastern, and multinational asset managers such as Franklin Templeton, HSBC Global Asset Management, J.P. Morgan Asset Management and Schroders. In most markets, there are also local companies that have a material market presence.

M&G Prudential's principal competitors include many of the major retail financial services companies and fund management companies including, in particular, Aviva, Janus Henderson, Jupiter, Legal & General, Schroders and Standard Life Aberdeen.

Jackson's competitors in the US include major stock and mutual insurance companies, mutual fund organisations, banks and other financial services companies such as Aegon, AIG, Allianz, AXA Financial Inc., Brighthouse, Lincoln Financial Group, MetLife and Prudential Financial.

Prudential believes competition will intensify across all regions in response to consumer demand, digital and other technological advances, the need for economies of scale and the consequential 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 plc's long-term senior debt is rated as A2 by Moody's, A+ by Standard & Poor's, and A by Fitch. These ratings are all on a stable outlook.

Prudential plc'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 Aa3 by Moody's, AA by Standard & Poor's, and AA by Fitch. These ratings are all on a stable outlook.

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 by Standard & Poor's. This rating is on a stable outlook.

All ratings above are stated as at 13 March 2018.

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 disrupt its business functions and have a negative impact on its results of operations

Operational risks are present in all of Prudential's businesses, including the risk (from both Prudential and its outsourcing partners) of direct or indirect loss resulting from inadequate or failed internal and external processes, systems or human error, the effects of natural or man-made catastrophic events (such as natural disasters, pandemics, cyber-attacks, acts of terrorism, civil unrest and other catastrophes) or from other external events. Exposure to such events could disrupt Prudential's systems and operations significantly, which may result in financial loss and reputational damage.

Prudential's business is dependent on processing a large number of transactions across numerous and diverse products, and it employs a large number of models, and user developed applications, some of which are complex, in its processes. The long-term nature of much of the Group's business also means that accurate records have to be maintained for significant periods. Further, Prudential operates in an extensive and evolving legal and regulated environment which adds to the operational complexity of its business processes and controls.

These factors, among others, result in significant reliance on and require significant investment in information technology (IT), compliance and other operational systems, personnel and processes.

As part of the implementation of its business strategies, Prudential has commenced a number of change initiatives to be established across the Group, some of which are interconnected and/or of large scale, that may have material financial and reputational implications if such initiatives fail (either wholly or in part) to meet their objectives and could place strain on the operational capacity of the Group. These initiatives include the combination of M&G and Prudential UK & Europe, the proposed demerger of M&G Prudential and the intended sale of part of the UK annuity portfolio. In addition, Prudential outsources several operations, including a significant part of its 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, models and processes incorporate controls designed to manage and mitigate the operational and model risks associated with its activities, there can be no assurance that such controls will always be effective. Due to human error among other reasons, operational and model risk incidents do happen periodically and no system or process can entirely prevent them although there have not been any material events to date. Prudential's legacy and other IT systems and processes, as with operational systems and processes generally, may be susceptible to failure or security 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 reputation and relationships with its customers and business partners. Similarly, any weakness in administration systems (such as those relating to policyholder records or meeting regulatory requirements) or actuarial reserving processes could have a material adverse effect on its results of operations during the effective period.

The proposed demerger of M&G Prudential carries with it execution risk and will require significant management attention

The proposed demerger of M&G Prudential (Prudential's UK business), is subject to a number of factors (including prevailing market conditions, transfer of the Hong Kong business from The Prudential Assurance Company Limited to Prudential Corporation Asia Limited and approvals from regulators and shareholders). Therefore there can be no certainty as to timing of the demerger, or that it will be completed as proposed (or at all). Further, if the proposed demerger is completed, there can be no assurance that either Prudential plc or M&G Prudential will realise the anticipated benefits of the transaction, or that the proposed demerger will not adversely affect the trading value or liquidity of the shares of either or both of the two businesses. In addition, preparing for and implementing the proposed demerger is expected to require significant time from management, which may divert management's attention from other aspects of Prudential's business.

Attempts by third parties to access or disrupt Prudential's IT systems could result in loss of trust from Prudential's customers, reputational damage and financial loss

Prudential and its business partners are increasingly exposed to the risk that third parties may attempt to disrupt the availability, confidentiality and integrity of its IT systems, which could result in disruption to key operations, make it difficult to recover critical services, damage assets and compromise the integrity and security of data (both corporate and customer). This could result in loss of trust from Prudential's customers, reputational damage and direct or indirect financial loss. The cyber-security threat continues to evolve globally in sophistication and potential significance. Prudential's increasing market profile, growing customer interest in interacting with their insurance providers and asset managers through the internet and social media, improved brand awareness and the classification of Prudential as a G-SII could also increase the likelihood of Prudential being considered a target by cyber criminals. Further, there have been recent changes to the threat landscape and the risk from untargeted but sophisticated and automated attacks has increased. Developments in data protection worldwide (such as the EU General Data Protection Regulation that comes into force in May 2018) may also increase the financial and reputational implications for Prudential following a significant breach of its (or its third party suppliers') IT systems. To date, Prudential has not identified a failure or breach which has had a material impact in relation to its legacy and other IT systems and processes. However, it has been, and likely will continue to be, subject to potential damage from computer viruses, attempts at unauthorised access and cyber-security attacks such as 'denial of service' attacks (which, for example, can cause temporary disruption to websites and IT networks), phishing and disruptive software campaigns.

Prudential is continually enhancing its IT environment to remain secure against emerging threats, together with increasing its ability to detect system compromise and recover should such an incident occur. However, there can be no assurance that such events will not take place which may have material adverse consequential effects on Prudential's business and financial position.

The failure to understand and respond effectively to the impacts of transitional and physical risks associated with climate change could adversely affect Prudential's results of operations and its long-term strategy

Climate change poses potentially significant risks to Prudential and its customers, not only from the physical impacts of climate change, driven by specific climate-related events such as natural disasters, but also from the transition risks, associated with the shift to a low carbon economy.

The climate risk landscape continues to evolve and is moving up the agenda of many regulators, governments, non-governmental organisations and investors. For example, the Financial Stability Board (FSB's) Task Force for Climate-related Disclosures recommendations were published in 2017 to provide a voluntary framework on corporate climate-related financial disclosures following the FSB's concern that there may be systemic risk in the financial system related to climate change.

Global commitments to limit climate change were recently agreed and governmental and corporate efforts to transition to a low carbon economy in the coming decades could have an adverse impact on global investment assets. In particular, there is a risk that this transition including the related changes to technology, policies and regulations and the speed of their implementation, could result in some sectors (such as but not limited to the fossil fuel industry) facing significantly higher costs and a disorderly adjustment to their asset values. This could lead to an adverse impact on the value and the future performance of the investment assets of the Group if climate considerations are not effectively integrated into investment decisions and fiduciary and stewardship duties. Where Prudential's investment horizons are long-term, the relevant assets are potentially more exposed to the long-term impact of climate change.

Adverse experience relative to the assumptions used in pricing products and reporting business results could significantly affect Prudential's results of operations

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 surrenders and take-up rates on guarantee features of products, investment performance and impairments, unit cost of administration and new business acquisition expenses.

Prudential needs to make assumptions about a number of factors in determining the pricing of its products, for setting reserves, and 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, where payments are guaranteed for at least as long as the policyholder is alive. Prudential conducts rigorous research into longevity risk, using industry data as well as its own substantial annuitant experience. 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 informed by models from the Continuous Mortality Investigation (CMI) as published by the Institute and Faculty of Actuaries. Assumptions about future expected levels of mortality are also of relevance to the Guaranteed Minimum Withdrawal Benefit (GMWB) of Jackson's variable annuity business. If mortality improvement rates significantly exceed the improvement assumed, Prudential's results of operations could be adversely affected.

A further factor is the assumption that Prudential makes about future expected levels of the rates of early termination of products by its customers (known as persistency). This is relevant to a number of lines of business in the Group, especially for Jackson's portfolio of variable annuities. Prudential's persistency assumptions reflect a combination of recent past experience for each relevant line of business and expert judgement, especially where a lack of relevant and credible experience data exists. Any expected change in future persistency is also reflected in the assumption. If actual levels of future persistency are significantly different than assumed, the Group's results of operations could be adversely affected. Furthermore, Jackson's variable annuity products are sensitive to other types of policyholder behaviour, such as the take-up of its GMWB product features.

In addition, Prudential's business may be adversely affected by epidemics and other effects that give rise to a large number of deaths or additional sickness claims. Significant influenza epidemics have occurred a number of times historically 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.

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, which are subject to the risks discussed elsewhere in this "Risk Factors" section.

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 Prudential's subsidiaries are restricted by applicable insurance, foreign exchange and tax laws, rules and regulations that can limit remittances. In some circumstances, this could limit Prudential's 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, 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 and other similar arrangements. For such Group operations, management control is exercised in conjunction with other participants. The level of control exercisable by the Group depends on the terms of the contractual agreements, in particular, the allocation of control among, and continued cooperation between, the participants. In addition, the level of control exercisable by the Group could also be subject to changes in the maximum level of non-domestic ownership imposed on foreign companies in certain jurisdictions. Prudential may face financial, reputational and other exposure (including regulatory censure) in the event that any of its partners fails to meet its obligations under the arrangements, encounters financial difficulty, or fails to comply with local or international regulation and standards such as those pertaining to 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 therefore dependent upon continuation of these relationships. A temporary or permanent disruption to these distribution arrangements, such as through significant deterioration in the reputation, financial position or other circumstances of the third party or material failure in controls (such as those pertaining to 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.

By order of the Board
Prudential plc
Alan F. Porter
Group General Counsel and Company Secretary

14 March 2018, London

As at the date of this announcement, the Board of Directors of Prudential plc comprises:

Chairman
Paul Victor Falzon Sant Manduca

Executive Directors
Michael Andrew Wells *(Group Chief Executive)*, Mark Thomas FitzPatrick CA, Stuart James Turner FCA, John William Foley, Nicolaos Andreas Nicandrou ACA, Anne Helen Richards and Barry Lee Stowe

Independent Non-executive Directors
Sir Howard John Davies, David John Alexander Law ACA, Kaikhushru Shiavax Nargolwala FCA, Anthony John Liddell Nightingale CMG SBS JP, The Hon. Philip John Remnant CBE FCA, Alice Davey Schroeder, Jonathan Adair Lord Turner FRS and Thomas Ros Watjen

* *For identification purposes*