Prudential plc - 2009 Half Year Financial Results

Transcript of Presentation to Analyst and Investors

13 August 2009

PRESENTATION

Mark Tucker (Group Chief Executive)

Good morning and welcome to Prudential's 2009 Interim Results presentation. As you will see today, we've got a slightly broader agenda than normal. What I want to do is kick off this morning with a short introduction before handing over to Tidjane, who will be taking you through a detailed financial review. We will then have updates from Clark and Barry, so that you can have a more hands-on view of what has happened in the US and in Asia in 2009 so far; and I'll finish with my views for the outlook for the rest of the year. As always, we will be happy to take your questions at the end and for that I am joined by my colleagues from the Executive Team over the front couple of rows.

Let me first go to the results. You can see that we've continued our very solid performance in what, as we all know, have been exceptionally challenging circumstances. Bear in mind that prior year comparisons are being made with the period before the collapse of Lehman & AIG, before the credit crunch and before the onset of the most serious worldwide recession since the 1930s – quite a different world altogether.

We said coming into 2009, with the prevailing economic uncertainty in mind, we would take a very conservative approach to new business generation, balancing new business volumes with cash generation. We also said it was our top priority to make sure that our balance sheet and capital position remained robust, and indeed that's exactly what we focused on. Maintaining, or rather intensifying our disciplined approach, we've been focusing the Group's new business production on the highest shareholder value opportunities rather than on volume. As a result, whilst new business sales were down 8%, much more importantly to us new business profit is ahead 25%, and we've seen an increase in average margins at a Group level up from 38% to 52%. We've also seen very strong net inflows of superior investment performance in our asset management businesses – a truly exceptional combination. Overall EEV operating profit was down 8% at £1.2 billion, but importantly IFRS operating profit was up 6%.

If we now turn to the very important subject of capital and cash, you can see from the slide that the estimated IGD surplus at the end of June is £2.5 billion, rising to £3 billion as a result of the hybrid we raised in July. This is a very resilient and robust position and we believe it to be one of the strongest in the industry and certainly one of the strongest in Europe, with a solvency ratio of 262%.

As Tidjane will talk about just a little bit later, we also continued to prioritise free surplus generation. Overall there was an increase of around £900 million in that period and, once again, we're operating cash flow positive at a holding company level in the first half of 2009. As you've seen, we've increased the interim dividend by 5% and that reinforces our confidence in the underlying earnings and cash generation of our businesses.

Now what I'd like to do is just make a few comments about each of the businesses and the power of the franchise – let me start with Asia. Right across the Asian region we've seen a pretty dramatic shift in economic performance, especially in the more export-orientated economies. We know we outperformed across the region in 2008 as far as sales are concerned and, we estimate that this will also be the case in the first half of 2009.

The building blocks that we put in place over the last fifteen years or so have been very important in delivering this outperformance. We've made sure that we've got geographic spread, exceptionally advantaged distribution, and a flexible and complete product range. These factors, together with a highly trusted brand and excellent people, have all played a central role in our success over this period.

At the 2008 prelims we showed you the clear benefits of protection coming through in our IFRS results throughout the region, and more recently Barry and the team have been driving the development of this business to new levels. Looking forward, our strategic position gives us great flexibility and we remain absolutely confident about the long-term potential in Asia.

To the US: strategically the US remains a very important market for us; they have $2 trillion in assets currently generating retirement income. The combination of our strategy and our positioning means we are emerging from the 2008/2009 market dislocation as one of the clear winners. The backbone of our success has been to focus on advice-based distribution, product customisation and our excellent product development. These factors, together with operational flexibility, market leading efficiency and the strength of Clark and his first-rate team give us real competitive advantage. We've also been able to respond quickly and effectively to changing dynamics in consumer demand in annuity markets. The consistency of Jackson's strategy and product offering, and the difficulties experienced by many of our competitors in the VA market have clearly played in our favour.

Since the beginning of the year we've maintained a strong focus on capital preservation and we've only written highly profitable and capital efficient business. VA hedging has continued to perform well and, as a result, of our disciplined approach to capital, overall returns have been very strong.

To the UK: as you know, Nick Prettejohn has decided to move on from the Group in September and he'll be succeeded by Rob Devey, who joins us from the Lloyds Banking Group. Nick leaves a very strong business for Rob to take over, and I'd like to take this opportunity to thank Nick for the really excellent job he's done and the leading role he's played in successfully refocusing our business in the UK. It's a business that now is clearly based on its strength in annuities and with-profits, and is delivering market-leading margins of returns on new business.

At the same time we've taken head on the issue of a reducing policy count in the in-force book; there's also been a significant switch within our UK expense base with fixed-to-variable cost, which will of course prove very beneficial in the years ahead.

From a Group perspective the superior long-term investment performance of the With-Profits Fund and that Fund's inherent financial strength continued to provide strong shareholder cash flows. We remain on track for the shareholder business to break even in cash terms, in 2010.

Finally, but certainly not least, Asset Management: throughout the past 18 months M&G has shown the benefits of a business model that combines an emphasis on the development of a significant presence across all major asset classes, with a culture of delivering consistently

superior investment performance. Led by Michael, our strategy has paid dividends in both the retail and institutional markets in the UK and Europe.

In the retail market M&G improved its position during the first half of this year in terms of both net inflows and funds under management. Early indications are that we are number one in terms of both net inflows and fixed income funds under management at the end of June; a really impressive achievement.

In Asia our approach to Asset Management is to build a multi-asset, multi-country model which is scalable. PCA Asset Management now manages a total of £36 billion of funds across our insurance businesses and on behalf of external clients. During the first half of the year we maintained Top 5 positions in a number of the most important markets in Asia, and we've also been able to increase market share in the majority of those markets.

Our message coming into 2009 had two key elements: it was a message of caution and concern regarding the general economic and business climate, but it was also one of confidence in our strategy and our business model. We've got a number of strong franchises; franchises are primarily based on extracting value from the retirement opportunity in each of our chosen markets. Our operating principles have remained consistent.

We believe that the geographic spread within the Group gives us excellent profit and risk diversification, as well as profitable options for growth, and all of these factors have been in evidence during the market dislocation.

As I said earlier, and as you've heard me say on many occasions in the past, we've got a shareholder value-driven approach delivering growth.
In addition to the actions we've taken in the first six months of this year, we've strengthened our capital position very significantly and we've given ourselves additional flexibility from a capital perspective.

With that, let me hand over to Tidjane to take your through the detailed financials.

Tidjane Thiam (Chief Financial Officer)

Thank you Mark and good morning everyone.

Before I deliver my usual financial review, I would like to say a few words about some topics which I know are on your minds ahead of my change of role on 1st October. The first thing I would like address is our strategy. Mark has just reminded you of what we are aiming to achieve and why. I voted with my feet when I decided to June the Pru in September 2007 – almost two years ago – for what was a major career decision for me so I'm totally aligned with the strategic vision and I have no plans to change the Group's strategy. The second thing I would like to say is that my focus, as it has been since the day I joined the Pru, remains on execution and delivery. We have the right strategy; what we need to do is to continue to execute it successfully; that will then result in the delivery of sustained, superior performance.

Now back to the financial review. You are familiar with the way we have been presenting our performance with two key sections; first our performance on our key financial metrics and, second our approach to risk and capital management. As usual, all our prior year figures will be stated at actual exchange rates. In addition, following the completion of the transfer of the Taiwan agency business in June 2009 and to help comparisons, we have removed the results of this business from 2009 and from the 2008 comparatives throughout the presentation. After the financial review, I have asked Clark to cover with more granularity our US performance, focusing on the trading environment, the credit book and our hedging programme so I will not address those; I've also asked Barry to provide some more colour on Asia.

My first slide is similar to the one I used at the Prelims. I continue to believe that the best way to create value over the long-term in our business is to have a balanced approach and to keep an eye on EEV, IFRS and cash flow. Over time those three measures should track each other, so at a Group level IFRS operating profit has increased 6% with a truly remarkable performance in Asia, and I'll come back to that. EEV operating profit was down 8%; within that Life EEV operating profit was flat so most of the decrease was due to lower asset management profits and lower investment income, both as a result of market movements.

I have introduced a new item on this page - free surplus. As you know, we have been using since the prelims movements in Free Surplus as a proxy for cash generation; in the first half free surplus increased by £932 million to almost £1.8 billion, benefiting significantly from the Taiwan transaction. Finally, holding company cash flow remained positive at £22 million after paying an increased final dividend for 2008.

I'd like you to note that going forward I intend to use increasingly Free Surplus evolution to comment on cash flow generation, which I expect to increase over time.
Holding company cash flow is mostly used to cover our progressive dividend and should be expected to balance close to zero after payment of a dividend, considering the many opportunities we have to write business profitably. As the chart shows - and I had it done to scale - after dividend, holding company cash flow is a small balancing item. I will come back to this.

At the end of 2008, faced with a very uncertain outlook, we focused on cash generation and capital preservation. We developed our 2009 budget starting from the bottom with a cash and capital objective and treating sales like a residual, not an objective. In that context, we decided to deliberately concentrate our sales efforts on the products with the highest IRRs

and the shortest payback periods across our businesses. In a volatile environment, this approach has served us well and has had a major impact on our new business profitability. For the Group, new business profit has increased by 25% to £691 million and average margins, as Mark said, improved from 38% to 52%.

Taking it by region: in Asia we achieved a strong increase in margins from 45% to 50%, thanks to our focus on protection and health; in the period, protection and health increased from 22% to 30% of APE. That increase in margins partially offset a 15% fall in volume so that new business profit was down only 4% to £277 million. Our payback period is four years; a very strong performance in a challenging environment.

In the US, new business profit has more than doubled. I believe we made as much profit in the first half as in the whole of last year, save £2 million. Focusing on preserving capital, we have not written any capital intensive institutional business in the first half and we don't anticipate writing any in the second half either. We have achieved an IRR in excess of 20% and a payback period of just two years. We have benefited from the organic consolidation under way in variable annuities (Clark will talk about that) and done really well in fixed annuities as well with lower volumes but higher market share.

In the UK, margins increased from 29% to 32% with new business profits down 5% due to lower volumes. The payback period of new business in the UK was five years and returns in excess of 15% are market leading. In total, the average group IRR was comfortably above 20%, one of the highest in the industry and well above our cost of capital, with attractive payback periods.

Let's now look at how much we have had to invest to generate those new business profits I just described. We have two main rules when deciding where and how much to invest in new business acquisitions. First, we manage the total strain; not strain as a percentage of APE; it is the total strain that we control and that has a direct impact on our cash flows and our long-term value creation potential. Second, in normal market conditions we would allocate marginal capital primarily to Asia, as that is where we believe our highest returns and our highest growth opportunities are and will remain in the long-term.

Let's look now at the evolution for each half year over the last eighteen months. I said at the Interims that to preserve capital and cash I would manage our new business strain closer to levels seen in prior years as it had exceptionally reached £806 million in 2008, significantly higher than £500 million in 2007. There was effectively a significant increase in the second half of 2008, driven by our investment in the UK and mainly related to a Cable & Wireless book which had a premium of just over £1 billion and a strain of £94 million.

Our decision not to write bulk business in the first half of 2009 in the UK, together with the beneficial impacts of increased With-Profit profit sales and our disciplined approach to pricing annuities, has reduced strain significantly, as you can see. In Asia, our new business sales were lower than planned this year. There was less demand from capital than we expected. Therefore, we decided deliberately to allow our investment in the US to increase temporarily above our initial plans in order to take advantage of IRRs in excess of 20% with a 2-year payback period, available at a point in the business cycle where our competition had decreased markedly. Overall in the first half, we have managed to control, very effectively, our new business strain whilst at the same time shifting to a higher margin product mix and generating higher new business profits.

That's all I wanted to say about new business. Let's now look at EEV operating profit. EEV operating profit for the Group is down 8% and before we look at the detail of this evolution

it is important to note that for our Group this half year there were no major assumption changes or large operating variances. They represented in total 0.5% of the opening value of in-force. Looking at it more closely, you can see that the overall operating profit from the Life businesses, as shown on the right-hand of the slide, was flat. Our very strong new business performance allowed us to offset the decrease we did experience in in-force profits. Experience variances and assumption changes had a negative impact of £64 million; a good performance in the context of an in-force value of £9.58 billion, almost £10 million at the start of the year. This resulted from a combination of positive experience variances of £13 million and of negative operating assumption changes of £77 million. As you know, in-force performance is crucial in our business; it is an area of intense focus for me and this will continue.

Overall, losses in Asia were partially offset by gains in the US and in the UK. In that context, it is important to note that Asia has grown from 20% of our embedded value in 2004 to 38% at this half year, a major evolution.

In the first half (of 2009), embedded values have held up well in most of our Asian territories, in spite of significant financial and economic disruptions. However, we had a specific issue in Korea related to premium holidays and we have deliberately taken a cautious approach to the issue and changed our operating assumptions to a very conservative level and Barry will give you more detail on that, when he talks about Asia.

Turning now to the profit from asset management and other operations of £152 million; M&G and our asset management business in Asia have continued to attract significant net flows. Profits, unsurprisingly, have declined, compared to the first half of 2008, when equity markets were at much higher average levels. Depressed conditions in the commercial property market and lower investment income have also had a negative effect on M&G. On the positive side, you can see that the GI Commissions in the UK increased to £27 million.

The third and last factor in the evolution of the EV operating profit is what we call OIE - other income and expenses. Here we have experienced a £63 million deterioration over the first half of 2008, mainly due to lower investment income on centrally held funds, as short term interest rates fell within the first half of this year. To summarise: in a changing environment we have demonstrated the resilience of our EV operating profit.

Turning now to the balance sheet and shareholder funds; they decreased by 8% in the period to £13.7 billion. Operating profits added £1.246 million; so it is good to remember that operating profit is a good source of capital. Below the operating line, short term investment fluctuations were negative £491 million, mainly due to losses and impairments related to US debt securities and to the effect of the negative 1% return on the UK With Profit Fund, compared to our long term assumption of 3.3% for the half year; 6.6% for the full year if you annualise. Reporting within short term fluctuations, we also incurred one-off IGD hedging costs of £216 million – I will come back to this in the capital section later.

Economic assumption changes were negative £384 million; two-thirds of this was in the UK; and on an EEV basis as previously indicated, we made a profit on the sale of the Taiwan agency business, reported here as £91 million. Finally, during the period, Sterling strengthened considerably against almost all currencies, generating this time negative FX movements of £1,104 million, bringing us down to the £13.7 billion I mentioned at the beginning.

So much for EEV, let's now talk about IFRS. This slide sets out the evolution of a major component of IFRS operating profit, which increased by 6% to £688 million. Within that, the operating profit for the life businesses increased by 26% to £732 million.

The movements in asset management, other businesses and Group related items are similar to what I've just described under EEV, so I will not repeat here my earlier comments. Let's focus on the life business operating profit on the next chart.

Starting from the bottom of the chart with Asia in red, profit has almost trebled with an underlying increase of 99% - or simply a doubling - if we exclude the £63 million one-off gain due to the implementation of a risk-based capital regime in Malaysia. Given the emphasis we have put on ensuring that our IFRS earnings in Asia track our EEV earnings more closely, this is a particularly pleasing result.

What explains this Asian performance? At the Prelims I highlighted the importance of insurance margin in Asia versus fee and spread. We have continued to benefit strongly from our profitable growth in health and protection. We have also benefited from the slowdown in sales, which led to a £24 million decrease in new business trend on an IFRS basis and you will see an appendix describing that; it went from £71 to £47 million.

In the US profits were down 6% compared to the first half of 2008 due to a number of factors, including lower fee income from our separate account, the VA account business, reflecting lower account balances; the non recurrence of hedging gains we achieved in H1 '08 and the increased cost of hedging in H1 '09; also on the positive side improvements in mortality profit reflecting positive experience in the period.

Finally in the UK, profit was up 11% on H1 '08, due to two main factors: one our shareholder backed IBT business contributed an additional £55 million in the period, as a result of a disciplined approach to pricing of annuities; and because there were also more shareholder assets earning an investment return.

The second factor is the shareholder transfer from the With-Profits Fund, which as you can see fell by £51 million in the period, reflecting the impact of the bullish rate reductions already announced earlier in the year. On this metric again the key message is that we have been able to deliver a strong and resilient performance throughout the market dislocations of 2008/2009.

Let us now look at IFRS shareholders funds. The opening shareholders funds were £5.1 billion; we added again £688 million of operating profit as I've described. Short term fluctuations were a positive £136 million (the break out box shows the composition by region). As in EEV there is a one-off charge for exceptional IGD hedge costs of £216 million.

The sale of the Taiwan business generated a loss of £621 million; and moving onto changes for equity, the unrealised loss position has improved, leading to a gain of £423 million (net of DAC and tax) and I will come back to this later also. Dividends net of scrip were £226 billion. Foreign exchange movements were negative 298 to give closing shareholders funds of £4.7 billion.

I have talked about the growth in Asian IFRS profits, very important; we gave you reserve movement information in the 2008 pack, but I did not include it in the main presentation. This time I would like to illustrate it and use a slide on this topic. The slide shows you reserve development for the shareholder business in Asia in the first six months of the year.

This is an alternative way of looking at the development of in-force and at the potential for growth in cash flows and earnings.

Reversing out for Taiwan agency business from opening reserves and normalising for exchange rates to see the underlying trend, you can see that the Asian shareholder business had net inflows of £972 million or 12.3% of opening reserves in one 6-month period or 26% annualised. This is driven by strong business sales and importantly also by the growing book of regular premiums from existing customers, a true strength of our Asian business.

During '08 as a whole, we had net inflows of 20% of opening reserves in Asia. This is more evidence, if needed, of the quality of the growth and of the earnings power of our Asian platform.

Moving on now to cash – cash and capital: as you know, I have been emphasising free surplus, which I feel is a useful proxy for underlying cash for generation. You probably remember this slide, it's just a reminder of the colour coding in the following slides: the fact that the sources of free surplus are in red, uses are in blue and stocks are in grey.

The next slide shows you the movement in free surplus for all of our operating businesses - that's life and asset management - in the first half of the year. At the beginning of '09, the opening free surplus was £859 million on the left here. During the first half our operations generated £912 million of underlying free surplus and that's a number I invite you to take away from this presentation, half year £912 million of free surplus generated; with £241 million of other movements.

If we move now to the blue, the uses of free surplus, starting with an item largely under our control, new business strain. We decided to invest £331 million to write new business and you'll recognise the £331 million we talked about earlier and it was £220 million of capital and £111 million of expenses. It is actually key to understanding how we navigated for the first half of 2009. Back in the fourth quarter of 2008, we decided that we would contain our new business trend and flex it, depending on the evolution of the economic environment, which at that point was very hard to predict.

Containing this new business strain is going to remain an important feature of how we manage the Group. In the same period, market-related items, including FX, reduced free surplus by £502 million, leaving us with a free surplus of £1,179 million. Therefore, free surplus generated by the operations, after investment in new business and after market movements, increased by £320 million.

You can then see we isolated that for the benefit of the transfer of the Taiwan agency business at £987 million; and the next item is to upstream, £375 million of cash to the holding company to meet corporate needs - and that's where you go back to the holding company cash flow.

The net impact of all these movements is to leave us with a free surplus of £1,791 million at 30th June on the right of the slide. Just to put this in perspective, that £1,791 million represents a £300 million increase of our June weight and it is useful to remember what happened in the meantime; we have absorbed £1.5 billion of adverse market movements and created reserves strengthening. We have used £787 million to write new business and up-streamed £556 million to the Group. We believe that having stayed at the same level net is quite an achievement and demonstrates the strength of our operations and their ability to generate significant amounts of free surplus, even for one of the worst markets in decades.

I would like now to show the evolution of our holding company cash flow over four years and how the Group uses the cash remitted from the Life and asset management free surplus as described in the previous slide.

A few comments here: dividend to Group from the businesses is at £375 million - it's in blue here; the holding company cash flow pre dividend, the red bar, has grown from 2006 to 2008 and is roughly flat over 2009 and 2008. The cash cost of the dividend net of scrip has increased to £226 million and hence there is a lower residue of £22 million compared to £86 million in 2008.

A key point to take away here, holding company cash flow is useful to think about our ability to meet corporate needs and particularly to pay for dividend, whereas free surplus is relevant to analyse the cash flow generation ability of the Group. Therefore we do not need to upstream cash from the operating businesses to the Group, over and above that required to meet corporate needs. One should not expect the holding company cash flow to increase beyond what is needed to pay a progressive dividend, as the Group has significant scope to invest capital at very strong returns - I said 20% overall for the Group, significantly above 20% - due to our unique strategic position.

This is probably a good place to say a little more on the dividend paying capacity of the Group. First, let me say that we look at the dividend and its progression across the economic cycle, which leads to very large impact - positive or negative - as we've been seeing now for two years.

We're showing here the underlying free surplus generation before market impacts, which are cyclical by nature and can obscure the underlying picture. Set against that are the uses of free surplus that are under our control; how much we invest in new business; how much we spend at the corporate level; and how much we pay in dividend. This slide shows that we have set our dividend at a level that is such that the net position in all periods is positive. We have also included this information in the appendix for the full year, as this is only half year. Given the underlying capacity to generate free surplus, the strength of the capital position we have built, the absolute quantum of our dividend and the very strong liquidity we have centrally, we remain confident that we can support a progressive dividend through the economic cycle on reasonable assumptions.

To summarise on performance: as we said we would, we have focused on capital and cash preservation. As a direct consequence we have seen all our metrics for new business profitability, absolute profits, margin, IRR and pay-back improve. The performance of a bad book; of course the Group has remained robust; IFRS profits have held up well, with a particularly pleasing increase in Asia and the ability of our business to generate free surplus remains and has allowed us to absorb significant adverse market movements in 2008 and 2009.

Let's move now to the second section, capital and risk, starting with solvency. The key considerations on solvency, as ever, are of the absolute level of the surplus; our ability to generate capital; and its resilience, or if you prefer, its sensitivity. In absolute terms, it's good to put this in perspective. Our IGD surplus is up £1 billion from £1.5 billion as of 31st December 2008 to £2.5 billion as of 30th June 2009. Pro forma and including the hybrid raised in July, our IGD surplus has doubled over the past six months to three billion, with an IGC cover of 262%. In addition, the UK credit reserve remains at £1.4 billion; this has already been expensed as you know and acts as an additional IGD capital buffer.

The free surplus analysis I showed you, but our underlying capital generation is strong, a key source of IGD capital. In terms of sensitivity, we set our risk appetite - i.e. the level of volatility in the surplus that we are willing to accept - so as to optimise the trade-off between the cost of raising additional capital and the cost of hedging various risks. We have generally built our strategy and hedging programmes to optimise economic outcomes, confident that in the long run across the cycle they are more important than short term accounting impacts.

I said earlier that I would come back to the specific IGD hedge. In the first quarter, you will recall that equity market levels had fallen significantly and volatilities were at historically high levels of between 50 basis points and 80 basis points - equity volatilities. At that point our sensitivity to extreme tail events - such as an immediate one-day fall in the markets of 40%, with no recovery - had become very high on an IGD basis, at a time when we had an IGD surplus of £1.5 billion. I do remember those days.

Therefore we took a decision to put in place a one-off hedge in addition to our continuous operational hedges, to protect the IGD surplus against tail events, due to the market dislocation, until such time that we would have strengthened our IGD position. Having significantly increased the IGD surplus for management action, such as the sale of the Taiwan agency and the issuance of hybrid debt in May and July, we are now comfortable that we will not need to renew this exceptional IGD hedge. The residual sensitivities that we have presented here, sit comfortably within our risk appetite.

The final topic I would like to address in this financial review is the asset side of our balance sheet. We have, as you know, £180 billion of invested assets, of which £53 billion are shareholder backed. Overall, we have seen our £41 billion debt portfolio perform well in the first half of the year across our businesses. Defaults totalled £11 million and losses on sale were £42 million i.e. just 13 basis points of the total credit portfolio. In addition, we have taken IFRS impairments of £324 million in the US, giving a total credit charge of £377 million for the period.

On the right hand side, and as I referred to earlier, our net unrealised loss position has improved significantly, starting from £2.9 billion at the end of 2008 - it had moved out to £3.2 billion, as you remember at Q1- and has now moved back to £1.8 billion at 30th June 2009. They're not on this slide, so I just got the numbers yesterday, but the unrealised losses position at the end of July was estimated at £1.1 billion from the £1.8 billion that you see here, strengthening our net asset value. Within this, corporates are now net positive; from the end of July corporates are now net positive, no unrealised losses on the corporate portfolio; I believe a remarkable moment in this credit cycle.

I would like to say a few words now here about the UK, where we have a significant portion of our exposure to credit risk. The UK credit portfolio remains of high quality with 78% invested in assets A rated or above and 96% investment grade. Defaults on the portfolio were £11 million, as I said earlier, and there were no net realised losses. The credit spread on the portfolio has reduced from 323 basis points at the end of 2008 to 275 at 30th June 2009. However, we have not reduced our reserves to reflect this statement.

Instead, we have retained the existing provision, plus the positive experience that emerged in the period and not taken it as profit. The Pillar 1 and EEV assumption is now 85 basis points per annum, which is equivalent to 31% of the 30th June 2009 spread; remember that our previous position was 80 basis points on 25% of the spread (at end 2008); our position has strengthened and the credit reserve remains intact at £1.4 billion.

We continue to set our IFRS credit assumptions at prudent levels and again the positive experience in the period has been retained. Clark will give you a detailed update on the US credit portfolio and there is more information in the appendix. We have provided you with a number of schedules, aligned with the ones I presented at the Prelims.

In summary: my key message is that we have continued to deliver a strong operating performance. We have executed well our strategy of cash generation and capital preservation. We have maintained our prudent and proactive approach to risk and capital management, achieving a very strong IGD position. Mark has built around him an exceptionally strong team and I have every confidence that we are well equipped to continue to out-perform our competition. I think that Mark has been a great CEO for this company, we've been through interesting times together and those are times when you learn to know a person when we were looking at IGDs around £700-800 million and share prices going down 29% on the day. I know Mark well, I believe; he's been a great CEO; he's a great person; he's been a great boss for me and I just wanted to say Mark really well done, thank you and good luck in whatever you do next. So thank you very much and I'll let Clark continue.

Clark Manning (President and Chief Executive Officer, Jackson National Life Insurance Company)

Thank you Tidjane. It's been an interesting half year in the US markets: starting with the baby boomer story, only two things have changed. Their homes are worth 30-45% less than two years ago and their retirement plan assets are down about 40%. Meanwhile retirement gets closer by the day and there's a clear need to replenish and increase savings. At the same time, we've seen a number of providers pull back from the US VA market in one way or another.

These trends clearly benefit Jackson, as we have long standing relationships across the independent advisor channel, that allow us to promote the importance and value of guarantees and hence of variable annuities, our core product.

We're benefiting from a substantial flight to quality in the VA market, as advisors and investors seek out the most disciplined carriers. As a result, we achieved the highest VA sales in company history in the first half, up 40% in Sterling or 6% in Dollars over first half 2008. We estimate that market share was over 7.5% in the second quarter and over 8% in June. Far from behaving aggressively, we were able to achieve these record results, while also increasing margins from 49% in 2008 to 71% in 2009. The increase was a result of a number of factors, including revised pricing of the benefits and increased spread in the fixed account options. From a risk management perspective, there is a stark contrast between those who say VAs are an unprofitable, un-hedgeable business and our risk management philosophy, which has led to the hedging gains we've reported since the beginning of this cycle. It has not been our strategy to compete on price, nor get involved in the feature fest and we were willing to lose market share during 2007 and 2008, as you see from the chart. Our current market share gains demonstrate that we are now reaping the benefits of our conservatism, as Jackson is increasingly seen by distributors as a must-have writer.

Moving to fixed annuities: our focus in the first half was value over volume; unlike the growth in VA sales, FA sales have been managed down 17% in Dollar terms, compared to the first half of 2008, as we looked to conserve capital. The margins, IRR and pay-back at which the business was written in the first half of the year were extremely attractive; our APE margin on the fixed line increased by 40 percentage points from the end of 2008. We recognise that this unusually high level is unsustainable, but we're taking and booking profitable sales that will generate strong IFRS earnings and cash flows going forward.

The increase in margins was partly a result of a slightly higher achieved yield on new assets, with the average quality of 2009 asset purchases at Single-A, which is consistent with the first half of 2008. Margins were more significantly positively impacted as a result of us reducing the credited rate on new sales to well below the current industry average, as you see from this chart.

It should be noted that we protect the value in-force and decrease vulnerability to surrenders, by selling products with a 6% to a 9% surrender charge in the first year. Further, market value adjustment provisions on many of the products insulate Jackson from changes in interest rates and help us protect future persistency.

While we're on the subject of fixed annuities, I'll say a few words about our credit portfolio. As you know, we have a £21 billion portfolio of debt securities in the US. Impairments on an IFRS basis are significantly lower in the first half of 2009 compared to the second half of 2008. This is in part due to the spike in corporate defaults and impairments, mainly relating to financials around the time of the Lehman collapse last September.

In addition, as Tidjane mentioned, unrealised losses reduced significantly in the second quarter. One thing you'll notice, though, is the increase in the impairments of the RMBS securities; and so I thought I would give you a little more colour on that. We have £3.4 billion of RMBS, of which £2.2 billion is agency guaranteed and £155 million is sub-prime. In the first half, £17.5 million in impairments was taken on the sub-prime portfolio. The remaining exposure is Alt A and prime, of which £750 million is senior and £314 million is non-senior.

We're seeing some contagion into the 2005 issues from the 2006/2007, due to the length of the economic downturn, which is now about 19 months in duration. Whereas the 2006/07 vintages were characterised by poor underwriting, with unemployment at a 25-year high of 9.4%, we're now seeing an increase in delinquency from borrowers who previously could afford their homes, but have now come under more difficult personal economic times. The duration of the downturn in the length of time, for which unemployment remains at these levels, will determine the ultimate extent of the contagion to prior year RMBS.

The split of senior and non-senior is an important point, although 70% of the prime in Alt A portfolio is in senior tranches. The importance of this is that although we may see some losses in these bonds, the losses will be contained. In a typical RMBS structure, the non Triple-A tranches are relatively thin, so that as collateral losses increase non Triple-A tranches can be hit very hard. The senior Triple-A tranche on the other hand is very wide and thus the actual economic loss is much more contained and much lower than the current price declines that are driving reported accounting values. There is a chart in the appendix that sets this out.

I'll now say a few words about hedging VA guarantees, which I know is a topic of interest to many of you. First of all, we do our hedging on a macro basis; that is we hedge residual economic exposures after taking into account all the substantial natural offsets within our book. As an example, with the current make-up of our liabilities, the offsets from the fixed indexed annuity portfolio is approximately one-third of our VA equity exposure. Jackson is typically fully hedged for a 10-20% instantaneous market move using options. Dynamic hedging is employed to fine tune our exposure around the 10-20% range, or when option based instruments are not economically viable. Frequent rebalancing mitigates the impact of larger moves that occur over time.

We pre-hedged a portion of our 2008 sales when options were historically inexpensive in late 2007. When implied volatility increased in 2008, a larger component of dynamic hedging was employed to complement the core option-based programme to manage through a period of severe market instability. We anticipate moving back to a traditional option-based approach once volatility reduces, so dynamic hedging can result in accounting losses in the interim.

Finally, our hedging programme covers all embedded VA guarantees, as well as the fees related to them. Few, if any of our competitors take such a conservative approach. Having described how we approach hedging, I now want to cover the performance over the last 18 months. It's been a very volatile environment and our hedging has held up very well. The right hand side of this chart shows the VA hedging performance over the last 18 months and note that I will briefly switch into Dollars. In 2008, we had $177 million IFRS gain; in part due to our pre-funded hedge position. In the first half of 2009 we posted a $52 million loss, which nets to $125 million IFRS profit over the past 18 months. On a statutory basis, which determines our regulatory capital, we made a profit of $28 million on hedging in the first half of 2009. Over the 18-month period, the statutory results were positive $177 million.

Unlike many of our competitors, basis risk has been a moderate positive over this period, as our funds in aggregate performed slightly better than the S&P 500.

In summary, we believe these results reflect Jackson's well-defined risk management programme and validate the economic based hedging programme that we've discussed at these meetings over the last several years. It is a combination of outstanding distribution and prudent risk management that's allowed Jackson to grow the variable annuity book, while less disciplined competitors are retrenching.

To sum up, I'd like to give you an idea of Jackson's priorities over the next few periods. Our first priority is to continue to grow the VA book profitably. The value to customers of the guarantees that we provide, has never been more apparent, nor has our customers need to repair their own balance sheets. We're already seeing a major shift in customer demand from fixed back to variable annuities and we expect this to continue. We will be increasing our distribution footprint and will continue to hedge our own balance sheet conservatively.

Our second priority is to manage fixed and fixed indexed annuities for value. These products have higher new business strain than VAs and with our limited capital appetite at present, we'll seek to maximise IRRs and minimise pay-back periods, rather than simply chasing volumes.

Lastly, market turmoil will create opportunities for inorganic growth and in Jackson's case we view this as an opportunity to diversify our sources of income beyond spread and fee business. While some larger deals may seem attractive at face value, we remain committed to our bolt-on strategy which takes advantage of our low cost scaleable single platform and was most recently demonstrated by the Life of Georgia deal. While nothing is imminent, we consistently explore our options, but will not deviate from the efficient bolt-on acquisition model that's served us well in the past.

We believe that financial turmoil has changed the US Life market in a way that plays to Jackson's strengths and I look forward to telling you more about it in the months ahead.

With that, I would like to hand you over to Barry, who will give you more colour on the performance in Asia over the last six months. Thank you.

Barry Stowe (Chief Executive, Prudential Corporation Asia)

Tidjane and Mark have shared with you this morning, the details of our first half performance in Asia. It is a strong performance in a challenging economic environment. I'd like to take a few moments to share with you some additional context around this performance.

Not surprisingly, given the severity of the economic disruption in Asia, absolute sales levels are below those of 2008, by 15%. However, they are 16% above 2007, which was as you will recall, a transformational year for Prudential in Asia. It is worth noting that sales of recurring premium products are down only 7% on 2008 and that sales of protection products are up more than 17%.

You will be sufficiently familiar with the results of our regional competitors to appreciate that this is consistent with our track record of out-performance. We continue to hold top three positions in most markets where we operate and we're the market leader in India, Indonesia, Singapore, Vietnam and in Malaysia, including our Takaful business. We are clearly better positioned than any of our competitors in the region.

In those rare instances where we have given up share, it is based upon our unwillingness to engage in pricing or distribution techniques that make no sense for our shareholders. We have not and will not manufacture loss leader products. We have not and will not pay excessive compensation to distributors or work with distributors who do not write quality business. This naturally leads us to a discussion of how we have done, what we have done in Asia.

It's very important to understand how different organisations have responded to the economic crisis. Some have made it clear that their priority is short term market share gains and they've done whatever they've had to do in an effort, often a futile effort, to boost absolute sales levels. In contrast, Prudential's first task performance was achieved by focusing on high margin, recurring premium products and by continuing to aggressively drive the protection element of our product mix, just as we have repeatedly told you that we would. This resulted in an improvement in new business margin, from 45.5% to 50.3%.

We've spent a great deal of time over the last few years talking about our value over volume proposition. If you ever had any doubts about how serious we are about this, about how disciplined we are as an organisation, then our first half results should put those doubts to rest. I think it's also very important to note that our sales volumes and our margins are driving results, not just for Prudential's shareholders, but also for over 400,000 Prudential agents who are weathering this storm and who are uniquely well-positioned to take advantage of improvements in consumer sentiment in Asia.

You've heard me say before that organisations that are serious about Asia must be serious about agency. We remain committed to agency distribution; it is the largest element of our unparalleled multi channel distribution platform; a platform that represents a greater competitive advantage for us today, than at any time in our history.

Moving on, I'd like to spend a moment on our EEV operating profit, where we have reported some adverse assumption changes and experience variances. Relative to the total embedded value in the region, these adjustments are small and movements of this type are not surprising, given the scale and diversity of our business.

You see from the chart, that persistency is the main component of the £124 million in adverse impact and that the principle driver of this is Korea. While Korea represents only 6% of our embedded value in the region, it represents over one-third of the variances and assumption changes. We've seen an up-tick in cases where linked policyholders in Korea have elected a premium holiday. These policies have not lapsed; instead, policyholder's funds are used to pay the insurance charges related to these policies. While the premium holiday feature is designed to allow for a temporary suspension of premium payments, we've taken a very prudent approach and have assumed that none of these policies will generate any further premium. Of course, if our actual experience proves better than this, positive adjustments will be made in future reporting periods. While Korea is contributing disproportionately to the EEV changes, it should be noted that we have seen some increases in premium holidays, in Hong Kong and Singapore as well as some partial fund withdrawals in India.

EEV operating profit is a key priority for us and management takes aggressive action to deal with variances such as these we've described today, when they arise. For example, in Korea we've undertaken a coordinated campaign using our call centre capabilities and our agency force to reach out to customers and encourage them to resume payments of premiums. Already, we are seeing signs of improvement as a result of these activities.

Let's move on now to the outlook for the future. No one is ready to suggest that the economic crisis is over, but neither is anyone suggesting that Asia's medium to long term prospects are anything other than positive. In fact the latest status suggests that Asia is recovering more quickly than the rest, with stronger GDP growth forecasts. Equally significant, is the recent out-performance of Asian equity markets and the positive impact this is having on consumer sentiment. The fundamentals of Asia remain unchanged: strong economic growth; demographic and social changes that work to our advantage; a growing mass affluent class; positive consumer disposition towards savings and protection products. Prudential's position and prospects in Asia are unchanged as well.

This slide is familiar to you; you've seen it many times before and it tells a compelling story. We remain uniquely well-placed in terms of our presence, our trusted brand, our scale, our core product and distribution competencies and our disciplined focus on value for shareholders. As I said, no one is ready to suggest the crisis has run its course, but I would like to close by calling to your attention some encouraging trends.

Our second quarter sales levels were well ahead of the first quarter in many key markets including Hong Kong, which was up 15%; Indonesia, which is up 21%; Malaysia which is up 33% and Singapore which is up 45%. Collectively these four markets generate about half of our APE and an even higher proportion of our new business profit, and these trends are continuing. Our distribution platform is also growing. In the second quarter we recruited over 40,000 new agents in Asia ex-India, representing a 50% increase over recruitment levels in the fourth quarter of 2008.

Let me finish my saying that times like these tend to punish mediocrity and reward excellence. There can be little doubt that Prudential is being rewarded for our discipline and that we are building upon our position of undisputed regional leadership and with that I'll turn it back over to Mark.

Mark Tucker (Group Chief Executive)

Let me move on now just to a single page summary and outlook before we go into Q&As. Whilst the business environment is expected to remain difficult in 2009, we are very confident that we will continue to deliver against our consistent and compelling strategy. We have a business model that is both advantaged and flexible, and that has proven its resilience. We are well-positioned to take advantage of any market upturn and we remain focused on the most profitable opportunities. We have a management team that has made, and will continue to make, a series of clear sighted decisions and proactive moves to improve the positioning of the Group.

Finally, and on a personal note, I'd like to say that it has been an honour, a privilege and a pleasure to lead the Group over the last four and a half years. I take great pride in what we as a team have achieved and I have every confidence that Prudential, under Tidjane's strong leadership, will continue to go from strength to strength. Thank you and we'll be happy to take any questions.

Q&A

Jon Hocking (Morgan Stanley):
- Firstly, could you comment a little bit about how you're managing the distributor relationship? You seem to be being far more dynamic in how you're managing the sales mix in all the territories really and how you're managing that relationship?
- Second, what is your appetite for bulk annuity business in the UK going forward?
- Finally, on the US. could you comment on the statutory capital metrics, in terms of where the statutory capital was at the end of the first half and if you could give an RBC ratio?

Mark Tucker:
Clark, can I ask you do that in reverse and talk about the statutory capital and also talk about distributor relationships?

Clark Manning:
Starting with statutory capital, we have not disclosed an RBC number, RBC is a year-end calculation and there are a lot of rules that are up in the air and being implemented this year. If I talk about development of statutory capital though, and things that might impact RBC ratio as we move into year-end, if you look at total adjusted capital in the US it is down $300 million since the beginning of the year. $200 million of that traces back directly to the IGD hedge and a $100 million to just the normal development of the book. If you look at the second quarter rather, it's about flat, so it had stopped declining. The underlying earnings on the business were offsetting any damage coming through from impairments in the second quarter.

Downgrades have impacted the denominator of the ratio; it will continue to. Our C1 factor in our denominator has increased by about $160 million and then you reduce that by about 20% for a co-variance factor and that's still out there. You have AG 43 out there; the impact of AG 43 at current market levels would be essentially nothing - that's not true at all market levels - and there's a disconnect between AG 43 and C3 Phase II that has to be worked through, but all of that appears to be manageable. You've got some things going on in the denominator that we're working on; the numerator is absolute capital; ratios are holding up pretty well.

SAP 98 would come into effect for the RMBS portfolio at the end of the third quarter; and what that would effectively do is bring fair value impairments to RMBS. Us, a lot of the industry and now increasingly the regulators are thinking that didn't make much sense, as opposed to going to what would be more of a yield maintenance standard, approximately rough and ready explanation marking these things to something approximating the yield at which you bought them, if there's an impairment as opposed to marking them all the way to fair value. That is SAP43 R; that seems to have a lot of support developing that would clearly be very beneficial for RMBS security impairments for us and for the industry.

Distribution relationships in the US, we think we've been in the right place through this. The advice-based advisors are going to come out of this stronger than ever because people are going to be looking for advice more than ever. There has been a lot of disruption of the product providers servicing that channel. For the first time in my career there are more distributors than there is product, where normally that relationship has been inverted. If you look at the top ten providers of VAs, five of them are clearly badly disrupted and other

ones are somewhat, let's say, disorganised in their ability to execute, so we've gained from that.

We also have gained from disruptions in other independent broker dealer networks owned by product providers, who now are wondering why they were providing the product that they were providing through those channels. The reps have become available and as a result we've increased the rep count in NPH from about 3,000 a year ago to about 3,500 now, so very good recruiting there at good economics for us. At the same time we've seen our percentage of house brand sales through NPH increase dramatically, similarly to what we've seen for our overall market share. I'd say that the other trend to watch is that other distribution channels that we were not interested in before have become more available to us. We are looking at possibilities of relationships in the wire houses where heretofore we've not tried to play, but they don't really have house brand product that they can push any more and they're becoming more planning orientated and their overall, let's say, tariffs and persistency behaviour has improved. As well as, because of the product shelf space inversion, large banks may now be available to us where, heretofore we were not willing to pay the economics required to get our products on those shelves. We have a lot of interesting things going on, on the distribution side right now.

Barry Stowe:
I wouldn't characterise what's going on in Asia with respect to distribution as being any sort of significant change. We're still focused on building, in most markets, the scale of agency distribution with an intense focus on improving the productivity in agency distribution. There's a lot of work going on in training new agents as well as existing agents on total needs selling. That's what drives them towards doing a total needs analysis with customers; that ends up generally in not just an investment sale, but very often a pretty beefy protection sale and that's why you're seeing some of the numbers that we've already shown to you today.

The efforts on distribution aren't limited just to agency. We're still very much focused on bank and that's doing very well also. There are markets where bank distribution was uniquely disrupted by what happened during the course of the third and fourth quarters of last year. We're starting to see that come back and we've done a lot of work in building bank assurance, particularly in China and in Taiwan over the last several months and that's coming through very, very strongly in the results.

Nick Prettejohn:
As far as UK distribution is concerned I think we have had a very strong story over the course of the last year. We have actually increased the number of our regional sales units. We had 44 new panel wins last year and we have actually had 39 new panel wins in the first half of this year. I think there is a lot of good evidence that our service levels to the advisor community have improved and as far as our fitness for the new RDR world is concerned, then I think with our early move towards factory gate pricing across a number of our products then I think we are well based in that new environment.

Tidjane Thiam:
It is also about retail and wholesale and what we have done; it is not just that we have shifted things in the distribution, it is about diversification, the fact that we have been both a retail and wholesale player in the two key markets, the US and the UK, has allowed us flexibility and you can turn the tap off much more easily on bulks, than you could when you have a brand and a retail presence and we need to also support the sales force, so I think that has given us flexibility that we have used. Back to your question on bulks, our appetite for bulks is actually healthy in normal market conditions. The point is that when you are

capital constrained you have to go as we have done, for the highest return; you fill your bucket from the highest profitability of your very shortest payback down. In more favourable times we write all the value creating business we can and in such times things like bulks properly fit within the strategy which shows at this point in the cycle we made a tactical decision.

Andrew Crean (Autonomous Research):
A couple of questions, on capital allocation:

- If there is so much pricing power that you have and the capacity to write good retail business, will you always constrain yourselves to the cash generation, or will you at some stage allow yourself to write more business than the cash generated in that period would allow?
- Second question, this whole debate on Solvency II over liquidity premiums - if the UK were to lose that debate and we have to be bound by Government bond yields, what would the capital impact of that be on you, and do you perceive that you could absorb that internally?

Tidjane Thiam:
Yes, I will take the first one; I think it is a fantastic question really, so the problem of how much business to write and how much cash to generate. I think fundamentally it is about giving you visibility and confidence in what we are doing and that is the path we are on through the disclosures on free surplus to gain on the right to write more business, more profitable business as long as we are delivering what we are promising for the embedded value and the evolution of the profit. I think at this point in the cycle we would rather stay relatively cautious and we would rather continue to drive the cash up, but there may come a point, a period where you may not be cash positive in every single period because you see how good it is out there and if that happens then we will explain it and show it, but for the time being maintaining the cash flow discipline, I think, is useful and is a good to drive the Group forward.

On Solvency II: we have been supportive of a risk-based, call it capital-based solvency regime, we think that is a good thing for the industry; diversification benefits will be significant for us and there are other benefits. Clearly there is a debate on the liquidity premium, it is encouraging that the debate with MCEV has moved towards recognition of the premium, there seems to be an agreement on that, and really all I can say is that the discussions are continuing. The consequences of a lack of agreement on that point would be so wide-ranging because they would go way beyond just the capital of insurance companies which have very deep consequences on the functioning of the bond market itself, even the size that we have as investors, but I think that that would have to be discussed at a higher level, in the UK Government, et cetera, but at this stage we cannot speculate on numbers. We are lobbying to get to a reasonable outcome and we have every reason to believe that that would be the case.

Mark Tucker:
I would say, that you should also add to that the effect on the consumers themselves (i.e. the annuitants) and again that becomes a major political issue.

Tidjane Thiam:
Yes, this could be seen as a national issue.

Andrew Crean (Autonomous Research):
I am presuming that you have done internal modelling on this, you did internal modelling on a 40% fall in equity markets earlier in the year so you would have done internal modelling

on this falling on the wrong side of the line; I just wanted to get an understanding as to whether that modelling would lead you to have to raise external capital?

Mark Tucker:
I think we do external modelling on all different scenarios, which we clearly keep to ourselves; I think we have no intention of disclosing those figures at this point, there is so much uncertainty there, it doesn't help to add to the debate.

Tidjane Thiam:
It wouldn't be helpful, with millions of people involved, to put numbers out there without the context; we just won't do it at this point.

Greig Patterson (KBW):
- I just want to understand the degree to which the fact that AIA is still paying double commission is creating inertia in terms of agent recruiting, or are you starting to get over that hurdle in Asia?
- The second one is in terms of the UK, would you consider selling the UK operation to a company like Resolution? I wonder if you would just make some comments around that.
- And, in terms of acquisition and acquisition capital, understanding within the context of your fixed charge cover to what extent you can issue hybrid debt - could you give me a number (i.e. can you say £1/2/3 billion) to give some idea of the capacity that you have?

Barry Stowe:
Our understanding is that the double commission payments which were occurring in certain markets, certain AIA markets have stopped now as of the last couple of months. The focus in terms of stabilising distribution has focused to talking to the agents about an upcoming IPO and all the benefits that they will get from the IPO and the manufacturer of some products that we have sort of autopsied. We can't figure out how in the world they put them together, but there is a two-year pay / five-year endowment (i.e. pay two year's premium and get covered for 5 years) that has just come out in Hong Kong that we are scratching our heads over; it looks like a negative embedded value, but in terms specifically on the double commissions, we think that has slowed down and they have shifted to other techniques to try to stabilise distribution. I think as to whether or not there are opportunities, I think there is some disruption and it would also be interesting to see how quickly these agents move and where they go, but there will no doubt be flight to quality on the part of some of them.

Tidjane Thiam:
On the UK: I think we are very happy with our UK business. We found a new strategy that Nick has implemented very successfully to focus business on key products generating good margins – you've seen the margins increase again, we are very comfortable with our position. That is all we have to say on the topic.
On acquisition capital: Tier 1, Tier 2 we have technically basically exhausted our Tier 1 capacity, we still have a lot of Tier 2 capacity, we are very far from the limit there. We are talking billions, we could issue billions more (in Tier 2) at this point in time.

Greig Patterson (KBW):
What is your capacity in relation to the fixed charge cover?

Tidjane Thiam:
We don't disclose that information because it is really important for our dialogue with our rating agencies. If it gives you any comfort I met every one of the rating agencies before transactions we did and they didn't object at all and, were very supportive of what we did, there is capacity for Tier 3.

Blair Stewart (Bank of America Merrill Lynch):
Two questions on cash flow:

- Firstly, on the free surplus, particularly the top line which is expected cash flow from the value of inforce; can you talk about the drivers there? I think it is up something like 10% or 15% year-on-year despite the fact the VIF has actually dropped off, so what is going on there?
- The second question is specifically on Asia with the higher profits even allowing for the one-off and cash flow coming through. Could you just talk a bit more detail there given that you are selling more capital intensive protection products and the asset base has been under some pressure?

Tidjane Thiam:
It is an interesting question on what happens in Asia, I am giving you this from memory, so don't quote me too precisely on this: we have basically added a billion to the embedded value from 2008/09 and what is going on is that you grow the difference, the discount rate and the net worth and the investment return rate and when you do those calculations you realise that this is actually quite a good progression in the generation of free surplus; so that is really driven by the volumes of business we have written and the stickiness of that business basically.

If you go from one year to another year it has allowed us to continue to progress and we don't see any reason why that would stop. If you go back to the IFRS chart that I showed on the reserve development you will see the contribution in Asia coming through and it is feeding through, so Asia is playing a significant role in that, and so does the UK and so does the US, but the developments in Asia are very positive. Clearly the health and protection products are more capital intensive, but also they have shorter payback periods and they may come back more quickly, but that is Barry's domain.

Barry Stowe:
The J-curve on the protection products, it does go deeper below the line, but when it comes out it looks like a shuttle shot, and it doesn't stay under water very long. We have been at this now for a couple of years; the volumes are coming through in a material way, so we are going to quickly get to a point where we are seeing real cash coming out of those products, material scale.

James Pearce (Cazenove):

- Could Clark talk about the VA margin expansion and specifically the consumer behaviour that was referenced in the press release and, talk about sustainability of the new high level of VA margins? I think the comments were about the fixed annuity margin in the presentation.
- Second, on Free Surplus in Asia you have gone from negative c£200 million to positive £900 million; what do you plan to do with that money? Is that earmarked for shareholder dividends or, for the US or, M&A or what have you got planned?

Clark Manning:
On the US margin, on the VAs we have split the margin increase into roughly three pieces. One is going to be re-pricings that we have done - we have been doing re-pricings late last year, early this year and there is some more stuff teed up for this Autumn, that is about a third of the increase that is sustainable and, if anything, might get a little better as we continue to re-price stuff. Another third you can think of as coming from the allocation of the money to the fixed accounts; allocation of new money to the fixed accounts has been running higher than historical, been running at about 30% (rather than 20%) – that is

monies being credited 2%, so the margin on that is pretty good. As money shifts back to the unit linked accounts then that margin will start to decline.

Then the other piece - policyholder behaviour - late last year, we reviewed policyholder behaviour versus assumptions and, our assumptions going in to the downturn. The guaranteed benefits on policyholder behaviour has always been very conservative because what we said is we don't have experience in the tails and therefore we are going to be very conservative on our approach in the tails. We have experience in the tails now, lots of it, so we were able to make some adjustments to policyholder behaviour assumptions there. That was about the other third, as long as policyholder behaviour remains good and there are no changes there that indicate anything differently that should hang around.

Tidjane Thiam:
On free surplus the point about Taiwan is that it has been a fantastic transaction really that Barry and the team have developed; it puts us in a much better position. It is not always visible, but what it has done is reduce the volatility of our balance sheet and our capital position; we are in a much more comfortable position now. It is not about giving that money back immediately; we're just in a more comfortable, more stable position which allows us to really manage for the long term. Again, on the dividend my view is it is difficult to have a dividend that would be both low and volatile, so we have set it at an absolute level that is compatible with our growth ambitions and as I said we intend to continue to have a progressive policy throughout the cycle and the level allows us to do that.

Colin Simpson (Goldman Sachs)
Can you talk a little bit about Prudential India, it seems the IRDA has introduced some price caps on both existing and new business, is that going to have a material impact? Also, there seems to be some talk about a potential IPO should the FDI limits increase, what is your appetite for that sort of activity?

Barry Stowe:
The regulator has introduced some caps that could have impact on the unit-linked products. The industry right now is in discussion with IRDA in an attempt to make certain that we are talking about the fees involved in actually managing the underlying funds in these unit linked products as opposed to the insurance charges and hopefully we will get that all sorted out in a proper way. Obviously it was going to require us to go back on new products in particular and take another look at the pricing and make sure that we generate acceptable margins from those products. It gives us even more impetus to do, in some respects, what we were already doing, which was also shifting the focus of the India agency force from purer and transparent investment products towards health products and we have had a lot of success in doing that. Unit premiums are still quite a bit smaller than for the investment products, but the actual number of sales being made of health products in India is skyrocketing.

There is a lot of discussion of IPO; there is a lot of discussion of increasing foreign investor share from 26% to 49%. It seems to be a more positive environment given the election results, the political results in India, but the reality is the proposal has not come out; it is not part of the budget package for the Government this year. There is speculation it could happen in the calendar first quarter, but when it happens we will see and also we will see if it makes shareholder sense when it happens, we will always view it through that lens.

Robert Haim (JP Morgan Asset Management)

I have just noticed in the reports today that your US namesake was actually selling its business in Korea. I was just wondering, given the issues that you have had there, whether this is something you would consider?

Mark Tucker:
Just be very clear; they were selling their brokerage unit on the unit trust side, it has nothing to do with the life insurance side, so I think it is not something that we would consider, in a sense it is a different business altogether. It was their asset management side, not their life side. That is the announcement this morning Rob, yes?

Robert Haim (JP Morgan Asset Management)
Yes.

Mark Tucker:
Yes, it is the asset management side, it is their brokerage side.

Bob Gullett (Newton Investment Management)
Mark, let me just say that on behalf of (I think) the investment community how sorry I and many of us are to see you go; I know you inherited the Company at a very difficult time and you saw off an unworthy bid from the person who is taking over from you!

Mark Tucker:
He caught me in the end!

Bob Gullett (Newton Investment Management)
You avoided all the pitfalls that your neighbours suffered, you have done a really great job, you have build a great management team and I think it gives us a lot of confidence in the Company going forward. So thanks very much and welcome to Tidjane and also thanks to Nick for a very great restructuring you did on the UK side, sorry to see you go.

Mark Tucker:
Thank you Bob - on that happy note, thank you very much and good morning.