S1 2020 Earnings Call

Company Participants

- Clare Jane Bousfield, CFO
- David Macmillan, Chief Customer & Distribution Officer
- John William Foley, CEO
- Jonathan Daniels, CIO
- Spencer Horgan, Director of IR

Other Participants

- Andrew Baker, Analyst
- Andrew John Crean, Analyst
- Andrew Sinclair, Analyst
- Ashik Musaddi, Analyst
- Dominic Alexander O'Mahony, Analyst
- Gordon Aitken, Analyst
- Kathryn Anne Fear, Analyst
- Louise S. Miles, Analyst
- Steven Haywood, Analyst

Presentation

Operator

Ladies and gentlemen, welcome to the M&G Half Year Q&A Conference Call. (Operator Instructions) Okay. Now I'll now hand over to your host, Spencer Horgan, to begin. Please go ahead, Spencer.

Spencer Horgan {BIO 4241901 <GO>}

Hello, everyone. Thank you for joining us for this Q&A call on M&G's first half 2020 results. With me this morning, I have John Foley, our Chief Executive; Clare Bousfield, our CFO; Jack Daniels, our CIO; and David Macmillan, our Customer and Distribution Officer. We've got about 45 minutes for your questions. Before we get into that, John, if I could pass it over to you for some opening remarks.

John William Foley {BIO 4239156 <GO>}

Sure. Thanks, Spencer. Good morning, everybody. Hope you're all well. Hopefully you've all had the opportunity to watch the video or read the transcript that we released this morning in relation to the half year results. Obviously the COVID-19 pandemic is not the backdrop that we would have wished for as a newly independent company. However these are really good and resilient set of results in very difficult times, and I think that demonstrates the value of our diversified business mix as asset manager and asset owner. Before we move into Q&A, I want to share some late news with you. Yesterday the FCA approved the change of control of Ascentric, which enables us to complete this transaction in September. As you know, the acquisition of Ascentric strengthens our position in the U.K. savings market and will help accelerate our move into high-value wealth management. So that was the update. With that, I'll take no more of your time and open it up for questions.

Questions And Answers

Operator

(Operator Instructions) We have one question from Louise Miles.

Q - Louise S. Miles {BIO 20765435 <GO>}

Just two questions for me, please, today. The first one on cash remittances from the subsidiaries. So we saw that, that was GBP 472 million in the first half of 2020. It'd be great to get an understanding of the split, which means what came up from M&G investment and what came up from PAC? And also, it'd just be good to understand that the favoring of the year because if you look at the full year 2019, what -- you can see that the cash remitted from subsidiaries, excluding specials, was fairly similar to that GBP 472 million as well. So it would just be good to understand what we should expect in the second half of 2020.

Then my second question is on the private asset capabilities. So you -- this was something you talked about a lot in the asset management business. But when we look at the shareholder annuity portfolio, we can see that only 10% of the portfolio is invested in private market fixed income at the moment. What are the plans to increase this proportion? Are there plans to increase there? Some of your competitors have a 40% in illiquid asset target. Are you thinking of doing anything similar? And obviously this is something that could improve your matching adjustment in ForEx and capital.

A - John William Foley {BIO 4239156 <GO>}

All right. Thank you, Louise. So I'll ask Clare, to just take the cash remittances question, I'll talk a little bit about where we're at with private assets and hand over to Jack for the detail. Is that all right, Clare?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

Yes. So Louise, on the cash remittances, you're right. We -- there was GBP 472 million that came up in the first half of 2020. It's fair to say that the split between M&G and PAC isn't particularly helpful at the moment just because we're going through a transitional period as we effectively go through the demerger process. Going forward, what we will look to do is basically pay up dividends from both PAC and M&G, effectively just before the announcement of the dividend from an M&G plc perspective.

We're just basically getting into that transition -- into that routine in terms of being a demerged entity. If you look at the actual cash remittances that come up from the subsidiaries, obviously from an M&G perspective, it's largely driven by the operating profit. And from PAC, it's driven by the Solvency II capital generation, and that's obviously predominantly from an insurance company perspective. But we would see that to be a very routine process. There's really no fungibility issues between the underlying capital generation and then what comes up as dividends.

A - John William Foley {BIO 4239156 <GO>}

Okay. Thanks. On your private assets question, we do talk a lot about it because it's a very key strength of this organization, but it's not necessarily in respect of our own balance sheet. So it's private assets business that we have built is largely off the back of the institutional business. And as you would have seen, the institutional business, is now the largest third-party component of our overall business. So rather than steal any of his thunder, I'll just pass it over to Jack to talk a bit about the private assets business. But he'll also mention the sort of capital queue that we have on that side of the business. Jack, can you pick that up?

A - Jonathan Daniels {BIO 20973577 <GO>}

Sure. Yes. Hopefully you can hear me okay. I mean the point you make about our strength in private assets is correct. We've been in this area of the market for a long period of time, over 20 years, so we have a lot of experience there. In terms of how we think about private assets, there is the internal requirement for the With-Profits Fund, for the PruFund. The annuity portfolio, where we have been growing the percentage of private assets and also for our third-party clients. It's managing those competing demands. It's an area of the market where it's quite hard to replicate the capabilities that we've built up over a long period of time. So we will continue to grow that part of the business. The allocation of private assets will continue to be shared between third-party clients and also our internal funds, both the -- both PruFund and the annuity portfolio.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

One follow-up from that -- on that, Louise. I don't know where you're getting your 10% of private assets from, but it's around -- 30% is the level of private assets in the annuity portfolio. So that might be one that you can follow-up with Spencer.

A - Jonathan Daniels {BIO 20973577 <GO>}

Yes. That's correct. That seems -- that 10%, I agree, seems a bit low. It's more like 30%. Yes. I'll give you a call back on that one, Louise.

Operator

We have another question from Andrew Sinclair from Bank of America.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Two from me as well, if that's okay. Firstly, was about the property trading loss on the annuity portfolio. I'm probably a little bit surprised by that. I'm just really looking for a bit more color. Is there anything else, property-wise, in the portfolio where there could be any potential risks of a loss crystallizing?

And secondly, was just on Ascentric. Just really wondered if you could put this in a bit more context, the acquisition for the wider savings plans. It's clearly good to get a bit more scale and more products, but I think there's still quite a distance behind some of the leading players in the platform market. And really, I kind of question, is it possible to be a winner nowadays in the platform market without your own financial advisers? Is there any interest in a reincarnation of demand from the Pru?

A - John William Foley {BIO 4239156 <GO>}

Thank you. Let's go straight to the Ascentric question. Without stealing any of his thunder, I'll pass that one to David. Then Clare will pick up the property trading question.

A - David Macmillan {BIO 16195004 <GO>}

Thanks, John. Andrew, with respect to Ascentric, I would absolutely agree with you that there have been open architecture platforms in the market for a considerable period of time. I think when we announced the acquisition in the first place, we're quite clear that in the context of our business, we see that acquisition is the opportunity to take our core capabilities into segments of the market, particularly wealth management, where we've not really played, as John said, a lot of high net worth business that we know is attractive, not just a PruFund but to a lot of our M&G capabilities.

We simply haven't passed that up and that is absolutely our intention. And when it comes to the question of advice, we never ever walked away from Man from the Pru entirely and have had their own in-house advice business since in 2011, 2012, which has consistently been there to look after our large existing Prudential customer base and continues to do that and has enjoyed good performance through the course of this year on the back of the fact that we've been able to integrate our new advice technology, in a digital sense, alongside our existing product capability and deliver a sustained service to our customers. So those two things are obviously to be built upon going forward.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

And it's fair to say that, that business is sort of -- around about, sort of 10th in size in the market in terms of advice, so it's a reasonably sized Advice business. On the property trading loss, this was one transaction where we have an offer, and we felt it was a credible offer but it resulted in a small loss in terms of just the way the accounting works for the annuity book. You can see on Slide 32 that we've got GBP 2 billion of real estate that backs the annuity book. So the portfolio is very small. We're not expecting to see any other small losses come through on that book. But as I said, the transaction was actually -- we felt economically was the right thing to do, but it did have a small accounting loss.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Sorry. Just to follow-up. Can you just confirm what was the size of the accounting loss on that transaction?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

It's small tens of millions, Andy.

Operator

We have another question from Andrew Baker from Citi.

Q - Andrew Baker {BIO 20402705 <GO>}

Great. First is on asset management expenses. So adjusting for one-offs, full year '19 expenses were about GBP 685 million. Obviously the first half run rate of GBP 306 million is materially below this. Is this -- is some of this just first half versus second half timing difference or are you expecting 2020 full years' expenses to be materially down year-on-year? And if so, what's driving that?

Then secondly, just on the regulatory Solvency II ratio. So this was 136% at the end of June. I know previously you said it doesn't -- this metric doesn't drive the dividend decision. But at some point, I'm sure, there has to be a constraint. So are you comfortable with the 136%? And how low can it go before there was any impact on that dividend decision?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

So on your first point on the asset management expenses, if you look back over history, what you see is that the second half of the year on the asset management side tends to be higher than the first half of the year. That's driven by just some of the incentive plans and some of the unwinds of accruals that happen through the period. Now we would hope to basically level that off more into the future, but there is potentially a bit of seasonality between first half and second half of the year. The expense savings in the first half of the year are driven by location and some of the changes in the properties that we've had. They're also driven by the reduction in travel, and they're also driven by the reduction in recruitment.

All of those, as we talked about in -- or as John talked about in his speech because of the changes that we're looking to make in terms of the way that we're working, the way that we're traveling, the use of mobile and digital technology, from our perspective, that is very much sustainable cost reduction in terms of how we see the business going forward.

A lot of those costs were already in our plan in terms of the GBP 145 million because fundamentally, we wanted to move from some of the higher-cost locations to some -- to lower cost and more flexible working in terms of that approach, together with the need to reduce the kind of travel footprint in the context of the environmental aspects around that. On the regulatory solvency ratio.

So the regulatory solvency ratio is low because the With-Profit Fund is so big and has a big, sizable capital requirement. The one thing to remember is that as the solvency ratio gets impacted by market volatility, that market volatility has, effectively, would get you to the same point in terms of 0 or 100%, whether it's the regulatory solvency ratio or the shareholder solvency ratio.

So for example, if you say that interest rates at 50 bps fall in interest rates has a 6percentage point impact on the shareholder solvency, it has around about a 3% impact on the regulatory solvency. So from that perspective, we do monitor the regulatory solvency ratio, but actually, it's just a functional calculation that effectively is a lot less volatile than the shareholder solvency because it's got a bigger denominator. So all our risk appetites are set based off the shareholder solvency, and we're very comfortable with 164%, well above our risk appetite and pretty much in line with the resilience of the balance sheet that we expected.

A - John William Foley {BIO 4239156 <GO>}

And just to -- I'm not wishing to belabor the cost question that you heard, Andrew. But we were contemplating going down this road before COVID hit. We had this -- as I suspect, many other companies were as well, the fundamental belief that you could actually operate your business on a different basis with much increased flexibility. Of course as with many other companies, we've had to respond to that. We found that we can do it, we can do it well. It has significantly reduced our carbon footprint. These are all cost savings that we are going to sort of try and include in the BAU, so that they are captured going forward.

Q - Andrew Baker {BIO 20402705 <GO>}

So maybe just one follow-up, if that's okay. So should this be thought of an acceleration of the GBP 145 million benefit on the cost side? Or is there any actual income considered? [ph]

A - John William Foley {BIO 4239156 <GO>}

No.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

No.

A - John William Foley {BIO 4239156 <GO>}

No. It's just a different way of thinking about it. I mean we wouldn't want to -- so we're not changing that. That remains the number that we've said all along. But I think what it does do is give us options around how we can deploy our resources and make them more efficient going forward [ph]. That doesn't necessarily mean cost reduction. It means we can probably do more. I don't know about your productivity levels, but ours have gone up actually since we've been working from home.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

Yes. The other thing to remember, Andy, is we announced at the year-end results that we would basically target a 10% reduction in our headcount, and we also announced a voluntary redundancy program. So we left the voluntary redundancy program open, but we stopped compulsory redundancy through this period just because of the social implications and the importance of giving our staff a degree of certainty through this crisis. So some of this kind of counterbalances some of that decision that we made at that point in time.

Operator

We have another question from Andrew Crean from Autonomous.

Q - Andrew John Crean {BIO 16513202 <GO>}

We have two questions, if I might. Firstly, could you give us a sense of your flow -- net flows in June and July, both in the retail -- well, retail, asset management retail savings business and the institutional. Just so we can get some concept of shaping up the second half? And secondly, could you talk -- you mentioned something about a cut in the retail charges in your retail asset management business, I think related to performance. Is that going to be a material thing that we should think about?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

So John, do you want me take those two?

A - John William Foley {BIO 4239156 <GO>}

Yes.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

So on the flows in terms of June and July, so on the retail asset management, other than March and April, where we saw a significant uptick in the outflows on the retail asset management. The flows post that have pretty much returned to the levels that we saw during 2019, and that has continued through June and July. On retail savings...

A - John William Foley {BIO 4239156 <GO>}

And net outflow.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

And net outflow. Yes. Then on retail savings, as I mentioned in my speech, what we saw during the sort of March, April period is we saw an uptick in terms of outflows. That pretty much reversed very quickly. But what we have seen is a dampening on new business flows, and that's basically driven by the advisers and their ability in terms of digital technology. So -- and what we've been doing is working with those advisers in terms of leveraging our technology. But fundamentally, it's out of our control in terms of how they can do the face-to-face advice. And because we're relatively high pensions, that is one of the higher advice-type transactions, and that's one of the drivers to why the Ascentric deal makes a lot of sense in terms of broadening our tax brackets [ph]. Now those levels of new business flows have stayed pretty much as the sort of dampened view through June and July. Obviously August is a month that you can't get much evidence from because it's a holiday month. So what we are looking to do is basically working with those intermediaries as we go through the sort of Fourth Quarter. Then on retail asset management. So we've guided around margins at every presentation. In line with the industry, we expect margins to reduce. We cut margins on the direct book and introduced a unified fee in August. Then we also offer the discount on the property fund when we gated it.

That, together with just the mix of the underlying funds as we've seen inflows on certain funds and outflows on others, has driven the drop in margin on the retail asset management side. We are continuing to basically focus on value for money, as you can see from the value assessment, but this is a journey and it's a journey that we've basically started over the last 18 months, and we'll continue to basically adopt. But remember that value for money is not purely about investment performance. It's about all aspects of the service that we actually provide. And certainly, there's no evidence to say that if you cut the fee and the investment performance is poor, that, that actually solves the problem. Investment performance is way more important than fee.

Operator

We have another question from Kathy Fear from Berenberg.

Q - Kathryn Anne Fear {BIO 21827368 <GO>}

So I just had a quick one. Just on the retail fund range strategic revenue that you've spoke about. I was just wondering when we might start seeing some results from that or when we might potentially get an impact. So when you think that could actually start having a positive impact on the business? Then secondly, just on Pru funds, are you still under launch in Europe? Were there any changes to the way that you might...

A - John William Foley {BIO 4239156 <GO>}

Wait. Kathy, you're really -- you're breaking up.

Q - Kathryn Anne Fear {BIO 21827368 <GO>}

Oh, sorry. So can you hear me right now? Or?

A - John William Foley {BIO 4239156 <GO>}

It's all right.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

I can hear her, John. She's not breaking --

A - John William Foley {BIO 4239156 <GO>}

Oh, okay. She was breaking up for me. Sorry. Press on, Kathy.

Operator

We have lost connection with that questioner. We have another question from Gordon Aitken for RBC.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

Maybe she was breaking up, John. Sorry.

A - John William Foley {BIO 4239156 <GO>}

Well I'm quite prepared to accept that it's my phone. Go on, Gordon.

Q - Gordon Aitken {BIO 3846728 <GO>}

Okay. So a couple of questions on the insurance business, please. First, I mean it looks like you may -- or you will need mortality releases to hit your GBP 2.2 billion capital generation targets. Can you just talk a bit about the different components of those releases? I mean first of all, you're currently still -- you're still yet to move the 18 table. I mean that was a 3-month reduction in life expectancy and then will you definitely move to that in this financial year? The smoothing factor. If you could just tell us what your smoothing factor currently is. I mean that was guidance from that to drop that from 7.5 to 7 also came along with CMI 18.And that's another 3 month drop in life expectancy. Then maybe just talk about the deaths you've seen this year-to-date and maybe how they compare with the population? And the second question is on the annuity book. I mean really aside from mortality, what else could you do on that annuity book to release capital, perhaps talk about reinsurance and change the asset allocation?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

So Gordon, on mortality. So you're absolutely right. We're currently on CMI 17. We will look to move to CMI 18 this year as part of the mortality or the assumption review that we do in the second half of every year. That review will look at not just mortality improvements, but it will also look at base mortality as well. We have historically, with both improvements and base mortality, been prudent in our approach. We've been one of the last insurance companies to adopt the latest tables. When we adopt -- when we adopted CMI 17 and the same will be for CMI 18, those tables are highly calibrated to our underlying book. So in effect, it's quite difficult to necessarily say that this is what the impact will be of CMI 18. We're not expecting it to have a significant impact in terms of mortality releases. And the other thing that we do need to do is look at CMI 19 in terms of what is the trend showing because it would be madness to basically release on 18 and then strengthen again when we implemented 19 a year later. That's obviously our whole kind of philosophy around the prudence that we operate.

In terms of the deaths that we have seen as a result of COVID, the amount is relatively small in terms of the impact on our numbers in Q1 and Q2. Definitely, in terms of the deaths being higher than expected, is absolutely the case. You can see that through a lot of the population data as well in terms of where it's at. But you've got to remember that in June, that over 40% of our book is reinsured, so there's a reasonable chunk of benefit that goes to the reinsurers. Then in terms of opportunities on the annuity book.

Obviously yes, longevity is one of the areas that we look at. Expenses is another one in terms of just optimizing the way that we administer the book, and we've done a lot of work around transforming those processes, and that can have a fairly sizable impact just because of the capitalization factor. You've then also got the optimization of the asset portfolio, the use of private assets that we talked about earlier on.

Then also interest rate hedging is the other place that we obviously manage and monitor through the period. We've got a strong track record of delivering a lot of management actions across the entire portfolio, not just the annuity portfolio. But a number of them are market-driven in terms of making sure that you've got the right conditions from a market perspective. So -- and that is something that we look to optimize on a regular basis. As you can see from these numbers, we've delivered

just under GBP 300 million in the first half year.

Q - Gordon Aitken {BIO 3846728 <GO>}

Can I just follow-up on -- and the point on the mortalities moving back so many. I mean are you currently using 7.5 is it -- got to [ph] drop that to 7?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

I haven't got the detail on how -- where we are on the smoothing factor. And as I said, it calibrates, I'm not sure you would just take that smoothing factor without taking into account other aspects around it.

Operator

We have a question from Kathryn Fear from Berenberg.

Q - Kathryn Anne Fear {BIO 21827368 <GO>}

Sorry about that. Hopefully, you can hear me. I got cut off.

A - John William Foley {BIO 4239156 <GO>}

A lot better now.

Q - Kathryn Anne Fear {BIO 21827368 <GO>}

I'm terribly sorry. The dog will probably stop barking now. Sorry. I've been at home working. And just on the -- so on the first question was just on the retail funds range in the strategic review. And just when we might start seeing some results from that or is there going to be a turnaround there on the retail asset management business? From there, what you think about come out of that? Then the second one was just on PruFund. I was just wondering, I think I was -- there was some talk maybe before about change to the structure going away from the 90-10 when you launched it internationally. I was just wondering if you've made any further -- or had any further thoughts on that or if it's going to remain a 90-10 product when you launch it in Europe?

A - John William Foley {BIO 4239156 <GO>}

So just to be clear, on your question, it's around retail fund performance?

Q - Kathryn Anne Fear {BIO 21827368 <GO>}

Sure.

A - John William Foley {BIO 4239156 <GO>}

I know we're doing about that on the first one. So as we said before, there are a number of things coming on there, which is being led by Jack, who's on this call, and he can give some more color on it. But it's around a couple of things.

First thing is that, as you have seen, the performance on PruFund has been stellar for very many years. And bringing the techniques of how we think about the investment thesis around PruFund to other parts of our business is a no-brainer in my -- from my point of view. That's a team-orientated approach. It's a more quant approach using digital capabilities. And those are things that are being embraced by the funds management team. So -- and that's already -- I mean that's been happening for some months. We're already starting to see the fruits of that. Jack, I don't know if you want to make any more comments around that.

A - Jonathan Daniels {BIO 20973577 <GO>}

Yes. I mean if it's a general question, both about the new potential propositions and performance. I think just on performance, we think about it in 3 ways. We think about funds which John has alluded to, with a strong track record; the institutional business, again consistently strong performance. Those two parts of the business have had a pretty good first half, came into the crisis with reduced risk positions and added risk in March and April. So pretty comfortable there. On the retail and wholesale side, they've been more challenging. The multi-asset and fixed income funds generally positioned for a positive economic outlook. And clearly, that wasn't the case. But they've rebounded quite strongly in the Second Quarter. And on the equity side, clearly, the value base of some of our funds hit us in that -- particularly in that First Quarter, but even during the recovery. So we're thinking about the retail funds in 2 ways: one, refreshing the range and taking a look at it.

So that will be looking at opportunities to consolidate the existing fund range, where appropriate, to identify new funds and strategies to launch and ESG and impact will be at the core of these new propositions. The integration of ESG and sustainable investing into the research and investment processes, which we've already undertaken, will help us and give us an edge there. And also within the equity strategies, a diversification away from value as a style with some thematic offerings to come out there.

So a number of things going on there, and you'll start that coming through towards the end of this year and beginning of next year, but will come through during the course of next year. And we're also taking some actions around how we work with the fund managers to improve the consistency of performance on our flagship funds. There are a number of initiatives that we've got running there which we've had in place for some time, and we're starting to see some positive outcomes as a result.

Operator

We have another question from Ashik Musaddi from JPMorgan.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes. I just have a couple of questions. So first of all, going back to -- so first of all, let's talk about the PruFunds and heritage With-Profit fund. Now if I look at the shareholder transfer of heritage with profit fund, it increased year-on-year, whereas the shareholder transfer from PruFunds decreased year-on-year quite a lot. That was a severe decrease because in past, I guess you used to get about 2% of the outflows as shareholder transfer improvement. But in first half this year, it was only 1%. So what is the mechanism that, on heritage, it is going up; on PruFunds, it is going down, even though if I understand correctly, the crediting rate is more or less same for both PruFunds and heritage. So that would be my first question.

And secondly, going back to Gordon's question on that confidence on GBP 2.2 billion capital generation, I mean you need to do -- based on that guidance, you still plan to do about GBP 2.4 billion capital generation over 2.5 years. So is it possible for you to split that into underlying management action and macro moves? So what are your expectation on these 3 buckets? Yes, these two questions would be great.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

Okay. Ashik, I'm actually just going to go back and answer Kathy's question on PruFunds in Europe because I don't think we've covered that in terms of -- we are looking at 100-0 in terms of PruFund in Europe rather than 90-10. So that is still our current working philosophy, we haven't finalized in terms of the underlying structure, but that's the current direction of where we're going.

On the shareholder transfers in terms of the PruFund versus the old star traditional with profits, the reason why there's a difference between what's going on there is on the PruFunds, you have this concept of the unit price adjustments. So when the unsmoothed price and the smooth price get out of line by plus or minus 5% on the higher-risk funds. What that does, is it triggers the unit price adjustment up or downwards depending on where we're at. Those funds basically had a unit price adjustment downwards at the end of March. A number of the cautious, more cautious funds have also had a price adjustment upwards that's happened in the last month or so.

Some of the higher-risk funds, when you look at where they're sitting in terms of smoothed and unsmoothed assuming markets behave, it looks like they may well have an upward adjustment as well. That -- and of course on the traditional With-Profits book.

What we haven't done is reset bonuses because effectively, what we've done is looked at the impact that happened in March and April, but then also the recovery and basically, we're pretty comfortable in terms of the level of terminal bonuses that we're paying at the moment in the context of where the market sits today. So that's the reason why you've got a slightly different dynamic going on between the underlying, too. But the core underlying asset call is exactly the same. The hedging process is exactly the same that it's just the mechanics of how the outcome customers changed in terms of the transactions.

Q - Ashik Musaddi {BIO 15847584 <GO>}

So just one -- go ahead. Yes.

A - Clare Jane Bousfield {BIO 16746072 <GO>}

No. Go ahead. Because I was going to move on to the capital generation, but if you've got a follow-up on With-Profits.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes. Just on PruFunds. So does it mean that the shareholder transfer will go back to the 2% level because that one-off hit has been taken, but going forward, like from second half onwards, it will go back to whatever the historical rate?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

And so we did have a small reduction in the expected growth rate at the last quarter end. So -- but it should return to that more normal level, yes, assuming market conditions behave. Then on capital generation, you're absolutely right. Our task is now GBP 2.4 billion over 2.5 years. And as I said in my speech, we do need normal market conditions in terms of returns over that 2.5 years. Then together with management actions in terms of delivering that GBP 2.4 billion. It is stretching. It is always an ambitious target. But also, if you look at the track record of what we've delivered historically in terms of management actions, it is achievable, but stretching is the way that I would articulate it.

If you look in terms of the split between management actions and the underlying generation, what you can do is use effectively what we've provided to you in terms of the analysis of the underlying capital generation because -- and also the guidance in terms of how we see the future outlook, that'll give you a sense in terms of what the underlying capital generation, we're expecting it to do during the period. But I'm not going to get into the detailed numbers, but I think it gives you a pretty good guide if you look at half 1 2020.

Operator

We have a question from Dom O'Mahony from Exane BNP.

Q - Dominic Alexander O'Mahony

Just two -- one quite specific. You mentioned that you booked the Asian asset management team. You've recaptured, I think GBP 6 billion of assets there and another

GBP 3 billion expected in H2. You're also building a U.S. team in Chicago. I'm just wondering, what's the potential recapture of assets currently managed outside of M&G itself? Is there a ceiling in terms of -- could it be 100% of all assets kind of managed externally? Or are there good reasons to leave more assets with other managers?

Second question, I think this may build on Ashik's question. Just coming back to the GBP 2.2 billion target, which it's clearly a stretch given what markets have done. It also sounds like you have true line of sight to quite a lot of capital management actions. Just really trying to understand the extent to which this is a change versus what you originally expected when you set the target. In particular, whether what you're anticipating is essentially bringing forward capital generation that might otherwise have been later, i.e. that better return on assets because it's earlier -- versus sort of the creation of new capital, which would obviously be quite a different -- have very different implications in terms of fair valuation.

A - John William Foley {BIO 4239156 <GO>}

So as a business, we obviously think that we should have the capability to manage all of our internal assets and have a very strong capability to do that. But that's not a given. And as a consequence, we have to compete with external providers and go through the appropriate governance to ensure that we merit the transfer of -- or the repatriation of money back to M&G from third-party managers. But this is an opportunity for us because clearly, we're already in those markets, and we know people, we manage those assets from a, if you like, a 10,000-feet perspective within the investment office.

So we know precisely what it is that we need to develop and grow, which is why we acquired the Asia team and why we've acquired the U.S. team. But there would still be governance to go through to ensure that we provide Boards of those related entities with the with the -- with all the information that they require to ensure that we're the right people or the company with the right people to manage those assets.

And yes. Is it -- I mean it's a philosophical point as to whether or not you think it's a good idea to leave some money with external providers. I mean traditionally, we haven't. We're not, to a significant extent anyway. Because we have develop the in-house capability and then proven over time that we've got the capability set, which is why we've grown an institutional business to the magnitude that we have because we are good at that part of the business. So I would expect -- my expectations are to see more money being repatriated both from Asia and North America. But as I say we've got to go through governments, and it's not a slam dunk. Clare, do you want to pick up the other question?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

Yes. So on capital management and the GBP 2.2 billion on the original plan. So I think one thing you have to remember is that one of the underlying reasons for bringing the business together and effectively operating as one business is that we get the diversification of the insurance and annuity book with the with profits and then with the asset management side. We always, as part of the business planning process, envisaged there was a cyclicality, particularly on the retail asset management, and also the margin pressure that we knew. So in terms of actually the number of management actions, we always believe there are levers that we needed to pull depending on the conditions in terms of where the market was.

That's exactly what happened in terms of the crisis. I don't think we envisaged that this size of the crisis was going to hit us so early in our life as a newly listed company. But fundamentally, that's how we see this business, as both elements of the business are able to basically support the other one, both in terms of the capabilities in terms of the investment proposition, but also financially in terms of enabling us to deliver something that's a very stable return.

So we didn't -- we always looked at ranges on this rather than necessarily saying, right, this was the number of management actions, and this was the underlying numbers. But you can see from the capital generation, at the operating capital generation has been very strong. Yes, supported by a number of management actions, but those management actions were all-natural things that we were doing as part of the kind of business as usual.

As I said in my speech, we're not interested in basically doing management actions that effectively destroy long-term value. There's no value in that whatsoever. We're all shareholders. That doesn't make any sense. But does some of this move profit from period to period? Absolutely, it does. In terms of -- but it's all about how do we manage the balance sheet and how do we manage the businesses, one, to get the stability in terms of the outcomes that we need as a listed company.

Operator

We have another question from Steven Haywood from HSBC.

Q - Steven Haywood {BIO 15743259 <GO>}

Two questions from me. On your credit risk allowance, you've given an increase of GBP 117 million. Could you explain what M&G's assumptions for defaults and downgrades are currently? And you said 4% of bonds have been downgraded by a whole letter. Could you say what is the amount downgraded to high yield?

Then secondly, just a quick question on your property fund. Is there any update on your gated property funds? And what are you expecting the outflows to be when they open?

A - Clare Jane Bousfield {BIO 16746072 <GO>}

So on the credit assumptions, I'm not going to get into the specific details in terms of where or what the underlying assumptions are. But basically, what we've done is we've strengthened the kind of short-term allowance that we put up as you go through any kind of crisis where we expect credit experience to deteriorate. We did that during the financial crisis. And you basically -- because effectively, a lot of this stuff takes quite a long time to come through.

So what we've done is we've reassessed the credit, the IFRS revision and effectively said we want to hold a short-term amount, which is GBP 117 million. Again it's effectively that experience that we expect to incur on a short-term basis. That will take quite a long time to run off, and it will run off in line with the actual experience in terms of the downgrade experience. I don't think we're going to get into the specifics of which bonds we actually hold and what's being downgraded. But as we've said, the portfolio is very conservatively positioned. What we've seen to date is not out of line with what we're expecting.

A - John William Foley {BIO 4239156 <GO>}

On the property fund, so we are keeping our customers very well appraised of what's going on in the fund. What's happening in terms of cash buffers, sales and so on. We have been surprised about -- we've sold 1 or 2 properties that have actually been completed at levels above pre-COVID pricing, which feels counterintuitive but nevertheless, that's what's happened. So that will continue. As you know, all other funds are being closed [ph] now on that from a valuation perspective.

So in terms of what we would expect as outflows, I'm not going to speculate on that. All I know is that we will try and sort of get a close read from our customers nearer time when the funds will open because the last thing we want is for the fund to reopen only to then be met with a lot of redemptions, and we have to close it again. So obviously we're all over it, but it feels like it's not something that's going to happen next year.

Operator

Ladies and gentlemen, this is the last question for today's call. I'll now hand you over to John Foley.

A - John William Foley {BIO 4239156 <GO>}

Hello?

Operator

Yes. John, you may begin.

A - John William Foley {BIO 4239156 <GO>}

So are we wrapping up now?

Operator

Yes, this is the last question.

A - John William Foley {BIO 4239156 <GO>}

Okay. Well so look. I just want to thank everybody -- not only in a COVID environment, but also in this heat. Because unless you have the luxury of air conditioning, you're stifling just like I am. So I'll just wrap up quickly and say that we have delivered a really good set of results in what has been a challenging market. I think that really demonstrates the value and resilience of our unique business mix. Given our continued financial strength and the resilient first half performance, we have declared a dividend of 6p per share, which is in line with our dividend policy. That is something that we're proud about. I also have to say that we are a crew that really want to deliver in respect of the things we've talked about and the business generally. We remain committed to the GBP 2.2 billion capital generation target by the end of 2022. We know that's more stretching, but we remain on track to deliver the annual cost savings of GBP 145 million by the end of that period. And despite the crisis, we have brought (inaudible) back to life as we expand business. We are increasingly well positioned to deliver long-term sustainable growth. That's my view. Thank you very much for your time. It's really appreciated. I hope to see you all in the not-too-distant future.

Operator

Ladies and gentlemen, this concludes today's call. Thank you for joining. You may now disconnect your lines.