Business Update Call

Company Participants

- Mark FitzPatrick, Chief Financial Officer and Chief Operating Officer
- Michael Falcon, Chief Executive Officer, Jackson Holdings LLC
- Mike Wells, Group Chief Executive
- Nic Nicandrou, Chief Executive Office, Asia
- Patrick Bowes, Director of Investor Relations

Other Participants

- Abid Hussain, Analyst
- Andrew Crean, Analyst
- Ashik Musaddi, Analyst
- David Motemaden, Analyst
- Johnny Vo, Analyst
- Jon Hocking, Analyst
- Nick Holmes, Analyst

Presentation

Operator

Ladies and gentlemen, thank you for joining us today for the Investor and Analyst Conference Call. We will now go live into the venue. (Operator Instructions) Thank you.

Mike Wells {BIO 4211236 <GO>}

Well, thank you for joining us everyone. I'm Mike Wells, I'm Group Chief Executive of Prudential. And today, I'm joined by Mark FitzPatrick, CFO and COO, and also here to take your questions are Nic Nicandrou, CEO of our Asian businesses, and Michael Falcon, who leads Jackson, our US business.

Yesterday, we were pleased to confirm the timetables for the demerger of the M&G business. Subject to shareholder approval, trading in M&G plc shares will begin on October 21, a little less than four weeks from now. Yesterday, we also published the M&G perspective and the circular for Prudential. You'll be able to hear John Foley and his team summarize the M&G story tomorrow. What we've done for you today is to bestow the Prudential circular and do a short presentation highlighting our particular strengths and clear-sighted strategy. Mark and I will talk to some of the key points and then we'll be happy to take your questions.

The demerger will benefit both the businesses in a variety of ways. To sum up the rationale, it's about two things. It's about alignment and it's about focus. The demerger will help both businesses become more closely aligned to the interest of our stakeholders, that's our customers, our regulators and of course, you, our shareholders, and the demerger will sharpen the focus of both businesses. Management will be able to focus more closely on improving operational outcomes. And as separate groups, I believe, we'll be able to allocate capital even more effectively.

There are four core principles that will drive the way we manage the Group. One, we will continue to grow Asia profitably. Two, we will enhance Jackson's ability to generate cash. Three, we will continue to be active managers of the Group's portfolio and to allocate capital with discipline. Four, we will build long-term shareholder value and pay progressive dividends.

We have a global portfolio of businesses, each of which is executing on meeting a large and growing consumer need. In Asia, the growing middle-class needs to save more to protect themselves from ill health. In the United States, the growing aging population needs more access to secure retirement income. And we are operating in markets in Africa, the total population of almost 400 million people.

Each of our businesses have leadership positions in their chosen segments or in the case of Africa, are expected to become leaders in the near future. While our portfolio is diversified across three continents, to be clear, this is an Asian-led group and over time it will become even more so. Over 60% of our embedded value be in Asia. And Asia has the largest portion of the world's population and almost all the new entrants in the global middle class. Asia is also where there is a largest unmet need for financial protection and long-term saving services we continually provide. And the penetration rates on the right side of the slide are a good proxy for this. Asia is where we see strong community support for what we do. There is recognition among policyholders who are an essential element of the broader social safety net and Asia is where we see the fastest technology innovation. This is aimed at improving efficiency and scalability as well as expanding the market, again by improving distribution and creating unique product categories, and unique customer experience. And this is where we see the most attractive investment opportunities for your money.

I've talked about the Asian opportunity. I want to say a few words about our capability. First, we have breadth. This is a portfolio of 14 different markets, all of which have structural growth. We have depth. We do protection, health, savings and asset management. And our customers range from high net worth individuals in affluent cities and marketplaces to people in emerging markets buying their first-ever financial product. In China, for example, we are now in 20 provinces and 89 cities, giving us access to regions with about 80% of the country's GDP. And we distribute these services through multiple channels.

We have scale. Three businesses produce over GBP300 million and five more generate in excess of GBP100 million. We are innovating at scale. Pulse, our new digital health app is not unique just in the diverse services it offers, but also in its pan regional size and its ambition. Our brand and our digital capabilities are making us an attractive partner, for example, with OVO, Indonesia's largest digital payment technology platform. And finally, we have a strong growth-oriented and disciplined management team.

In the United States, we have a very strong business. It's a leader in variable annuities, delivering a great return on equity and consistently producing large quantities of cash for the Group. As we've said, at the half year, we can further improve the cash generation power of Jackson and its remittances through diversifying our product mix. We look to do this both organically and inorganically. Organically, Jackson is creating new products to build its position in fixed index and fixed annuity markets. More than 30% of the sales in the first half of the year were from products other than variable annuities.

On the inorganic side, we had a strong record here in bolt-ons, most recently buying the book from John Hancock, and we've proven capability and advantages in this area. As we said last month, in funding this diversification, we are open to a third-party financing and reinsurance, and to be clear what this means, it's our intention that diversification in the US will be achieved without the Group investing additional capital. Jackson is a good business, which we can improve to drive greater shareholder value. We have clear objectives here and we're executing on.

Over the past few years, while growing profitability and investing for future growth, we've also exited countries, withdrawn from product lines, and sold businesses. This slide sets out just some of the highlights. We have always been active approaching the management of the full portfolio across the Group. To be clear, nothing is off limits. And the demerger of M&G is merely the largest transaction and a continuing craft to optimize the shape of the Group. The result has been an increasing focus on the most attractive opportunities in Asia.

The stats on the right-hand side of the slide show in Asia over the past decade, we've now invested GBP3.6 billion in running new business. This has supported delivery of GBP8.4 billion of high quality revenue. And this has contributed to an average operating return of just under 30% on IFRS equity. This active approach to the portfolio management and capital allocation will continue. Everything we do is geared toward creating long-term shareholder value. That means, aiming to deliver profitable growth throughout the cycle and I've spoken about the focus on structural growth opportunities, our investment in new capabilities and new distribution and again, our disciplined approach to portfolio management.

A final key element is the focus on resilient, high quality earnings. In Asia, more than 80% of the operating income comes from insurance margin and light fees. The proportion of our sales to this regular premium is 93% in Asia, and our customer retention rates in the region are well over 90%. What sits behind these impressive metrics is a unique mix of skills and distribution, customer service, risk management, and investment management. There's also about deep and trusted relationships with consumers, governments, regulators and business partners, some of which date back almost a century. These attributes combined to create a highly sustainable competitive advantage.

I'm extremely proud of this Group's track record. Compounded annual growth across all key metrics over the past decades are well into the teens. Few other businesses of our size can put up a chart like this. What drove our performance in these decades at a structural opportunity, quality income, disciplined capital allocation will continue to drive us through the next decade and beyond.

We have an opportunity to further accelerate our performance. We are now better than ever with innovation. We are better developing partnerships, including with the world's best technology players. We're better at applying best practices quickly across the Group. This allows us to scale up even faster the pace. We have a culture that's more passionate than ever about improving the customer experience and delivering positive growth. I'm confident that for Prudential the best is yet to come.

I'd now like to hand it over to Mark, who can talk about the metrics, dividends and our disciplined capital allocation. Mark.

Mark FitzPatrick {BIO 20178326 <GO>}

Thank you, Mike. Over the next few minutes, I want to cover off two main areas. Firstly, the key financial metrics of Prudential plc post demerger, covering Asia and the US, and secondly, our approach to capital management. And as part of this, I'll take you through our new dividend policy.

But before I get into those elements, for anyone who is new to us, a brief financial profile of Prudential plc post demerger. By any measure, we are a growing business with scale and strength. 2018 for the Asia and US businesses combined, our new sales were GBP5.3 billion and our new business profit GBP3.5 billion, with the lion's share of our new sales and new business profits driven by our Asia business.

In the first half of this year, our Asia businesses grew both new sales and new business profits by 10% on a constant currency basis. This geographic weighting is reflected in our EEV operating profit before central expenses, which in 2018 was GBP6.7 billion, of which GBP4.5 billion is in Asia. On a similar basis, 2018 IFRS pre-tax operating profit was GBP4.1 billion, of which Asia was GBP2.2 billion.

At the end of June, on a pro forma basis, our Group IFRS equity was GBP14.5 billion and on an EEV basis, GBP43 billion. Our pro forma core structural borrowings are GBP4.4 billion. And finally, we are strongly capitalized. On the basis of the LCSM measure that will apply post demerger, our cover ratio, again on a pro forma and June basis was 338% with a surplus of GBP7.6 billion. Although interest rates have fallen since June, our estimated LCSM ratio remains healthy and resilient. To help you better navigate LCSM, we will provide you with the sensitivities with our financial year '19 results.

So having given you that brief overview of our new financial profile, let's get started on our key financial metrics. For Asia, this is to continue to focus on generating high quality growth, driven particularly by regular premium health and protection business, which grows embedded value over the longer term. As you have heard from Mike, the objective for Jackson is clear; grow statutory capital, to grow remittances. At Group, we are focused on capital management. Allocating capital to create long-term value and overseeing an appropriate return on that capital, including disciplined focus on central expenses and managing central liquidity. And outworking at this is our new dividend policy, which I will run through shortly.

So how do we do this? Let's dive into this in a little more detail. As I think about our Asia business, I see that we are well positioned in growth markets. We have a track record of strong growth and continue to see a very significant opportunity ahead of us. We are focused on selling high quality business with over 80% of our operating income coming from insurance margins and life fee income, which are relatively less correlated to market conditions. 93% of our new business sales are regular premium business, and we have around a 95% retention rate, thereby compounding earnings and creating long-term value.

PCA's first half 2019 performance evidenced the strength of our strategic and operational delivery. Now, to bring this up-to-date, our year-to-date sales, excluding Hong Kong, to the end of August saw broad-based double-digit growth. Hong Kong's first half domestic sales growth momentum has continued, notwithstanding the sector wide slowdown of sales to Mainland China customers. Overall PCA new business sales continued to grow year-to-date.

I also want to point out the strong and growing profit contribution of our Eastspring asset management business, which you can see in the gray on the chart on the right-hand side. In the two-month period since the half year, Eastspring has maintained its positive momentum in both net inflows and fund. Eastspring is an important strategic asset as well as a source of differentiation compared with many of our competitors. Our high-quality new business creates long-term value as evidenced through our sustained growth and embedded value. Over the five-year period to 2018, new business profits increased by a CAGR of 19% and contributed to a combined increase in embedded value of GBP10.9 billion as at the end of June this year. This powers the nearly three-fold increase in embedded value for the life business since 2013 to GBP27.1 billion at the half year.

Our embedded value messaged us because it is a present value to shareholders of the future cash flows that would emerge from our in-force life businesses over time. This, combined with the release of capital requirements as the in-force business matures, creates free surplus. And it's this free surplus, which provides a capital to write new business, fund inorganic investments, and support remittances. As you can see on the right-hand chart, operating free surplus generation from our Asia asset management and in-force life business has been building steadily and remittances have increased broadly in line with this over time.

Moving on to Jackson, I'd simply like to emphasize its long track record of resilient capital generation. Since 2012, Jackson's cumulative remittance totaled $4.4 billion and you will have seen that it delivered $525 million to the Group in the first half of this year. Jackson's sales trends in the third quarter show a higher mix of FIA, continuing the trend seen in the first half of 2019. And for fixed annuities, sales have increased following new product introductions. The third quarter VA sales are exhibiting similar trends to those at the half year, reflecting the industry-wide slowdown with monthly sales continuing at broadly the same levels seen in the first half. So to sum up, the Group continues to focus on high quality Asia-led growth, measured through increasing embedded value and growing free surplus generation over the long term.

Now moving on to the second part of my session, one of the key strengths of this Group has been the disciplined approach to capital allocation, and this rigor will continue after the demerger, our capital management priority to drive profitable growth in Asia. So let me take you through the steps we used in the framework.

Firstly, capital is allocated to prioritize profitable organic growth. The key performance metrics we use to drive this are new business profit, i.e., shareholder value created by writing new business and investments in new business, i.e., the shareholder capital required to support this new business.

Secondly, inorganic growth. Given our size and scale, we get to see just about all the inorganic opportunities in our markets, but we're very disciplined about how we use our capital. These are assessed by reference to expected shareholder returns and payback periods relative to risk-adjusted hurdle rates, which is set centrally. The assessment also considers a range of other factors. These include a strategic rationale for the investment, the extent to diversification with existing risks and our experience in managing similar businesses. Assessment of these opportunities is also reviewed and approved centrally within the Prudential Group's governance framework in order to maintain a rigorous approach to capital allocation.

Thirdly, we want to retain a resilient balance sheet and associated local and Group capital and liquidity position. As we previously flagged, under the new Hong Kong Insurance Authority-led regime, our regulatory Pillar 1 capital will be the Local Capital Summation Method, rather than Solvency II.

And the final element is how we view dividend. Firstly, we have set out our expectations for the combined 2019 dividend across both Prudential plc and M&G plc, which subject to financial performance and market conditions are expected to total 51.82p per share. This represents a 5% increase on the 2018 dividend of 49.35p per share and is equivalent to a total cost of GBP1.345 billion across the two groups. Of this amount, around GBP425 million represents the first interim dividend already declared in August 2019. Around GBP510 million is expected to be paid from Prudential plc and GBP410 million from M&G plc in May 2020. Now please bear in mind that the GBP510 million expected Prudential plc's second interim dividend will be declared in US dollars and paid in May 2020. This will be translated into US dollars, using the 2019 year-end exchange rate. Of the GBP1.345 billion total 2019 dividends, GBP750 million represents the total 2019 contribution of the post-demerger Prudential Group to which our new dividend policy will apply going forward.

Secondly, we have set out the new progressive dividend policy for Prudential plc, which applies from this level, albeit future dividends for Prudential plc will be declared in US dollars. And applying this progressive dividend policy, the Board will consider a range of factors, looking to the medium term and beyond, including capital generation capacity, financial prospects and investment opportunities as well as market conditions.

Over the medium term, we would expect future central outflows to be covered by remittances from business units. These central outflows include dividend, debt interest costs and other central expenses, which encompasses central payments for bancassurance distribution agreements and restructuring costs, net of tax recoverables. So in calibrating your forecast, you should consider the scope of our Asia and US businesses to grow their capital generation, which over time will govern their respective remittance capacity. We discussed Asia's record of OFSG and remittance growth a moment ago and in respect of our US business, Jackson has paid the Group a 2019 remittance of $525 million and we expect over time a strategy of diversification to enhance cash generation.

Turning to central outflows, the table here follows our holding company cash flow disclosure. The central outflows reflect the Group's current pre-demerger structure. There were four key points to bear in mind going forward over the medium term. They are, one, net interest paid and at post-demerger our annual interest costs on our pro forma core structural debt is expected to be around GBP230 million. Two, on corporate activities, the historic numbers here reflect the Group's current structure. Post demerger, we expect these costs to reflect our new footprint with two major business units, not three.

Note that unlike IFRS reporting, our central corporate expenditure, the holding company cash flow does not include the cost of our Asia regional office. Those cash costs are really net off against the Asia remittance. You may also have seen from the circular that the M&G group expects head office and group function costs in the range of GBP80 million to GBP100 million per annum. In the short term, we expect to incur restructuring costs to align our corporate overhead with our new footprint. We will provide more details on this in due course.

Three, on tax received, after the demerger completes, we will no longer generate profits in the UK, but with the London head office, we will continue to incur some costs in the UK, including interest on Group debt. Post-demerger, the absolute level of holdco tax benefit is expected to materially reduce. Over time, this is expected to be partially mitigated by changes to the Group operating model.

And finally, four, other movements. This line includes a number of components, which vary from period to period. And if you double the half year '18 level you see here, that is more indicative of the annual run rate we would expect over the medium term for 2020 before one-off effects.

Summary to conclude the section, our capital management policy supports our approach of active capital allocation across the Group to create long-term value. So, to sum up, looking forward, post-demerger from a financial perspective, we have a proven powerful Asia life and asset management business, and our priority is to drive its growth, with embedded value development, a key measure of this. We have a successful and profitable US business in Jackson and a clear strategy. Growth in statutory capital generation and remittances is our priority. The capital management framework I outlined, which is very much a continuation of our long established and, I think, successful approach supports these objectives and our progressive dividend policy. And finally, to repeat Mike's message, we have a long record of -- as active allocators of our shareholders' capital. We aim to grow long-term value. The long successful record across measures of growth, earnings, and cash that you see here is powerful evidence of this.

I will now hand you back to Mike.

Mike Wells {BIO 4211236 <GO>}

Thank you, Mark. So again just to reiterate, Asia-led, focus on structural growth markets, look to Jackson to enhance its cash generation through participation in the world for its retirement market, stay an active manager of the portfolio and develop long-term shareholder value, underpinned by a progressive dividend policy. So again we think highly compelling.

I'm going to hand it over to Patrick now, our Head of Investor Relations to give you a quick briefing on the timeline for the demerger. If you would please, Patrick.

Patrick Bowes {BIO 16444249 <GO>}

Thank you, Mike. So on to the next steps in the demerger, with the circular on M&G perspective published yesterday, we have the M&G investor and analyst presentation tomorrow, Friday, at 10:00 a.m. UK time on 27th September. There is a detailed timetable in the circular with significant dates being the General Meeting on the 15th of October, 2019 and the listing of M&G expected on Monday the 21st of October, 2019. This is in line with our earlier guidance for Q4 completion. To remind you, the qualifying shareholders will be entitled to receive one M&G share for each Prudential share held by them at the applicable record time. Our tickers will remain unchanged and are shown on this slide. The demerger doesn't affect any of our listings. Going forward, we will report in US dollars. We retain our premium listing in London and membership of the FTSE 100 with continuing listings in Hong Kong and Singapore.

Thank you, Mike.

Mike Wells {BIO 4211236 <GO>}

Thank you, Patrick. And now I give it, please, back to the operator, and let's open it up for Q&A. I think it's appropriate.

Questions And Answers

Operator

(Operator Instructions) We now have a question from Jon Hocking from Morgan Stanley. Your line is now open.

Q - Jon Hocking {BIO 2163183 <GO>}

Good afternoon, everybody. I've got three questions, please. Firstly, starting with the dividend. I wonder if you could give some more color about what the anchor for the dividend is going forward. I think if you look at underlying dividend rebasing that's happened for the pre-plc Group, I just wondered, given we don't have a fully developed capital framework to look at for the Asia business, how is that dividend anchored and how did you decide that the starting level should be modestly lower? And should we think that we'll go back into the old pattern of periodic rebasing of the dividend upwards. That's the first question.

Second question, can you be more specific, please, in terms of the slowdown in Hong Kong in August? I think there has been a very sharp fall in the mainland tourists in all the key --give some quantification about the specific percentage fall in sales. And then just finally, on Jackson and the remittances, what impact would there be on future remittances if interest rates were to stay where they are now given the elevated level of hedge costs? Thank you.

A - Mike Wells {BIO 4211236 <GO>}

Okay, Jon. Thank you. I think we'll divide this into three parts as we could. Mark, if you please address the dividend issue, Nic a bit of a trading update or just impact on the resilience of the Hong Kong business, if you would, and Michael, a general comment please on interest rates at Jackson. So, Mark?

A - Mark FitzPatrick {BIO 20178326 <GO>}

Jon, hi, thanks for your question. In terms of the dividend, when we look at the element around the progressive dividend and the level of growth and how we think about the element of the dividend going forward, it's very much in terms of around the capital generation that we have and we will also then be having a good look at the financial prospects and investment opportunities we have as well as the market conditions. So those are the factors that we are going to be looking at in taking into account in terms of where we're at and how we go forward.

Overall, as you've heard me say before, we only bring up to the center, cash that we need from the business units in any one year and that takes into account the level of central cash stock and other potential investment opportunity or uses of central liquidity. And given where we are and given the starting point 750 [ph] was an entirely sensible and appropriate number for the business and in light of the capital generation we have in the report that we sent.

A - Mike Wells {BIO 4211236 <GO>}

And, Nic, on Hong Kong, just the general feel that (multiple speakers) business to sales.

A - Nic Nicandrou {BIO 15589153 <GO>}

I mean, as Mark said, so in Hong Kong, we have been impacted by the sector-wide slowdown in mainland China customers. The coming -- the disruptions that have been caused are impacting their ability to come across. Now everything that we see indicates no change in purchase intention and it's simply that the number of visits are being postponed. Now, conversely, the domestic demand and the activity to fulfill that demand remains robust. Our sales through July and August were actually up in the domestic market year-on-year, aided by the new annuity and the health offerings. Actually this lands weight. So I believe that structural purchases are much more resilient that more discretionary or transactional purchases. Therefore that Hong Kong picture taken together with the continuation of double-digit growth that we saw earlier in the year in the non-Hong Kong part of our portfolio, these are through July and August -- our overall sales were up.

The activity, as you can imagine, the -- there is no letting up -- no let up in the focus of Derek and his team to push forward. We continue to launch new products. We launched the new juvenile education product only a few days ago. We've launched a number of promotional activities on some of the very bespoke offerings that we have on Evergreen's favor, and some of the protection products. We're rolling out Pulse in Hong Kong in the course of the fourth quarter. And actually even though despite the disruption, we're stepping up on agent recruitment. So through July and August, our recruitment was 20% up on the equivalent period last year. So the businesses remains in good health and keeps on focusing on capturing an opportunity that is structural as we move forward.

A - Mike Wells {BIO 4211236 <GO>}

And Nic, percentage of recurring premium retention just real quick again, that market...

A - Nic Nicandrou {BIO 15589153 <GO>}

No, thank you for that, Mike. It's 98% recurring premium and the other fact that I think it may be relevant to mention is that the mix of business that we go through July and August is identical to what we saw earlier in the year indeed to what we see -- what we've seen historically, so which tells me that the needs that we are covering are structure and in real.

A - Mike Wells {BIO 4211236 <GO>}

Thank you.

Q - Jon Hocking {BIO 2163183 <GO>}

Thank you. So, can you remind me what the mix is, please, of mainland versus domestic?

A - Nic Nicandrou {BIO 15589153 <GO>}

So in the first half, it was 63 mainland, 37 domestic in APE terms and it's roughly similar...

A - Mike Wells {BIO 4211236 <GO>}

So Michael, range of interest rates could incur in Jackson.

A - Michael Falcon {BIO 17026942 <GO>}

So there is a couple of things. Clearly, and obviously through the first half results, the drop in rates have been a headwind and we saw that in August as well. So it's surfacing that -- we're within our -- despite that with the hedging portfolio being effective, we're within our risk limits on all of our capital and sensitivity measures. So that's important. Going forward, we do have the shift coming to the new regime, the new NAIC regime and that model is a lot less sensitive to rates.

I know, I think earlier and last year we had indicated based on where rates were at the time, which were obviously much higher that that shift to that regime was going to be a bit of a headwind. It's actually at a point -- we're in a point in the curve now where that shift is actually accretive as well which we disclosed in the first half year results, the permitted practice, which I'll talk about in a second is also right now a headwind where generally it had been a help.

We are not renewing that permitted practice going forward. And in fact, we'll leave that and I think in our published numbers, the capital drag on tax for the permitted practice at the mid-year was about $570 million. So that's a good lift. Again, it's not just that there isn't rate sensitivity in capital formation next year, but I think at this point, we're more susceptible to further declines, though at a much less sensitive level in the new regime than the old.

A - Mike Wells {BIO 4211236 <GO>}

Thank you, Michael.

Q - Jon Hocking {BIO 2163183 <GO>}

Thank you.

Operator

We now have a question from David Motemaden from Evercore ISI. Your line is now open.

Q - David Motemaden {BIO 18818634 <GO>}

Hi. Thanks for taking the question. Just a question on the target debt to capital levels post demerger, you're at. I think, 26% pro forma, including short-term securities. I guess where do you want debt to capital to get to and over what time period? Second, just on the holding company cash balance. Could you give us a sense for what the holdco cash balance will be post demerger and what the minimum level of holdco cash you intend to hold is? And finally, I was hoping to get a little bit more elaboration around the plans to reduce the corporate overhead going forward. Any sort of targets you may have and separately just on the TSAs that you have with M&GPrudential, I guess how faster are those going to be rolling off and how are you planning to offset the stranded overhead associated with those? Thank you.

A - Mike Wells {BIO 4211236 <GO>}

So, David, thanks for the questions. On the overhead, no, we're not going to give targets. We will rightsize their capabilities obviously to the size of the Group and the tasks at hand. And -- but we're not going to give a public target on that. On the TSAs, they are fairly minimal between the entities. And again, they have got a -- both sides have -- you have plans to in-house, if you will, various services that are currently shared. The decision on having TSAs as a function of us wanting to keep the pace of pull forward the timing of the demerger, not any capability development issue on either side. So that's more of a when do they fit on the project list of each of the two entities, it's not in our lens.

But do you want to go to target on where we are in debt to capital and holdco cash?

A - Mark FitzPatrick {BIO 20178326 <GO>}

So, it's Mark here. Thanks for your question. In terms of the debt leverage kind of the mid-2026 (inaudible) We're comfortable with that leverage. We think it works for us, and it's not one that causes us concern and conversations we've had with ratings and co, they are comfortable with that level as well. In terms of holdco cash balance at the year-end, as we said at the half year, the holding company cash is expected to reduce in the second half of 2019 and the level at the half year, but we haven't set out an exact number. And I'm not minded to set out an exact number at this stage.

Q - David Motemaden {BIO 18818634 <GO>}

Got it, thanks. And if I could just follow up on the -- around the $200 million or sorry GBP200 million of other movements that is expected to be sort of a run rate going forward in the medium term. There are few different items in there. What's really driving that going forward?

A - Mike Wells {BIO 4211236 <GO>}

So as I mentioned, I think there are a number of components in there and those do vary from period to period. And you can see the way those numbers have bounced around a bit. So one of the things I just wanted to give you a sense of is, what we think going forward will be helpful from an element of a run rate for your modeling before any one-off effects.

Q - David Motemaden {BIO 18818634 <GO>}

Thank you.

Operator

We now have a question from Ashik Musaddi from JPMorgan. Your line is now open.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Thank you. Hi, good afternoon, everyone. Just few questions. First of all, I mean, if I look at this cash plan, which is Slide Number 21, and if I apply some growth for US and Asia, I mean I kind of get the number of which kind of suggests me that there is no net cash accumulation after the payment of dividend based on the new figures. Now, I appreciate that you mentioned that you take out dividend, the amount that you want, but then, where is the dividend flexibility from subsidiaries, how much are we talking about in Asia because I'm not sure if there is a lot of flexibility in US at the moment. So, any thoughts on that would be great. Secondly, any progress on the US diversification plan? Where are we on that? Any progress? I know, we were just talking about this last month, so might be there is nothing at the moment, but any thoughts on that? And thirdly on this other movement, sorry, going back to that, again what is that GBP200 million? Is it like you're giving us some normal numbers for potential M&A or bancassurance payments or is there some cost that is a recurring cost. So these three questions would be good. Thank you.

A - Mike Wells {BIO 4211236 <GO>}

So let me just comment on the diversification. So, Ashik, we're not going to comment on any work in progress we have on strategic issues in the United States. So the answer to that one at this point would be no comment. Do you want to address the other two questions?

A - Mark FitzPatrick {BIO 20178326 <GO>}

Yeah, so in terms of the element of the cash build, if you look at Slide 17 of the deck, it shows the element of the OFSG level, for example, in Asia across life and the asset management business versus the net remittance, and therefore shows you that there is actually considerable capacity and capability that we want to be able to hold in the ground close to the businesses to be able to provide the maximum flexibility for the businesses to be able to pursue investments and growth opportunity on that particular piece. And as for the other element in terms of that GBP200 million, it is, as I've -- I've got the risk of repeating myself, it's a number of different components and they do bounce around quite a lot and what we've tried to do is, give an element of what we think that number could be on a go-forward basis, as I said, before any one-off effects.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah, sorry, what I was trying to understand on that is, is it a recurring number or is it something like you believe that on a normalized basis, some different items may come to this GBP200 million number? I'm just trying to understand that, is this a cost today that is there, like for example like corporate center costs? We understand it is there, it will remain unless you do the efficiency, et cetera. So what is that GBP200 million? Is it like just a normal view of what year in, year out, should be or -- yeah?

A - Mark FitzPatrick {BIO 20178326 <GO>}

So it is -- as the slide indicates, it's an element of things that include the element around bancassurance distribution includes things around restructuring costs and some of those things and some of those aspects as we know are going to shift and change depending upon our activity in any one year.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay, that's very clear. Thank you.

Operator

We now have a question from Johnny Vo from Goldman Sachs. Your line is now open.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah, hi. Thank you very much. Just could you give us the -- because the LCSM is so new, could you tell us what the LCSM has been over the past few years, so we have a track record? And also, can you remind us of what ratio you have included the US business in that LCSM and therefore, what it would be if the RBC ratio was closer to 400%? Also, in terms of the debt leverage capacity, do you have an upper range at which you wouldn't want to go above, so say 30% range? And the final question is just in regards to OFSG. Is that based on a minimum requirement of 100%? Thank you.

A - Mark FitzPatrick {BIO 20178326 <GO>}

So in terms of the LCSM, it is new and therefore we've looked at it for the half year. We haven't gone back. One of the things we're going to be spending time is looking at it from a go-forward perspective in terms of what it is. It is very, very new, but also we think it is potentially -- it's a bespoke arrangement that we have with the HKIA. And once the new group-wide supervisory standards come out, we'll get a better sense of what that's going to be in the future. And as we said at the half year, we expect that to happen sometime during the course of next year.

A - Mike Wells {BIO 4211236 <GO>}

But, Johnny, I think the way to think of it is, it's an extremely well aligned look at fungible capital from the local regulators point of view. It's cumulative look at our regulatory requirements across jurisdictions at reasonable capitalization. So again if -- it's sort of -- it's a good first look at a true fungibility of capital on a portfolio like ours. So we don't have audited historics on it. It's clearly a lens we've used in the past. You want to go debt to leverage?

A - Mark FitzPatrick {BIO 20178326 <GO>}

And then in terms of the elements around the US piece and how that's bought in, it's effectively a 100% of the RBC basis, it is how that's bought in terms of the calculation as we set out in the half-year account. And then from the elements around the debt to equity ratio or the debt lever element, one of the things that we keep a close eye on is the element around the leverage we have. 26% is where we are very comfortable with. We haven't indicated an upper limit in terms of we would or would not be prepared to go, it's something that we keep under close review and if that position was changed materially, we'd be able to -- we'd notify the market.

A - Mike Wells {BIO 4211236 <GO>}

And then just to go back to the cap ratio, we're continuing to use our economic capital and our cash flow stream models internally as they're obviously developed to incredibly high standards. The number of resumes you worked under that it's not a single lens look at how we deploy capital or how we define dividend level or fungibility of capital. And again we think we see convergence on the regulatory arising between US, European, and

Asian regulators of how they look at quality of capital, capital level strain, et cetera, and we think we're ready for that.

Q - Johnny Vo {BIO 5509843 <GO>}

Thank you.

Operator

We now have a question from Andrew Crean from Autonomous Research. Your line is now open.

Q - Andrew Crean {BIO 16513202 <GO>}

Good afternoon, all. Two questions, if I can. Firstly, on your plan to increase the cash remittances from the US, could you help us the tool with forecast and that will provide some targets because at the moment, the only information we get on statutory capital is one slide in the appendix once a year, which provides a statutory operating profit, which is reconcilable to nothing. It's impossible from the outside for us to be able to substantiate the increased cash remittances. Second, as I think you'll be aware from your shareholders feedback, the main issue on the stock appears to be whether to keep Asia and the US together or to separate and have the US. Could you say why you're not separating the US at this time? And what the synergistic benefits between the two companies, which you have talked about in the past, what are they and how powerful are they?

A - Mike Wells {BIO 4211236 <GO>}

So, Andrew, I might give you the same answer, I think at the half year on the targets. We're not going to provide targets on US. And I appreciate the challenge externally that creates, but the answer to that is, no, there won't be a target.

On the US synergy piece, there's quite a few. I mean, the international business has approximate 80% of its earnings in dollars with the combination that goes to the reporting currency, different risks to that. There's diversification benefit across the two. There's cash flow that goes to supporting our ratings, its capability. We don't have a market in Asia that is looking at for the most part retirement products and capability in that space. Recognize different issues in the US business, on that valuation, we have a very different business and some of those firms had in the US. And we'll continue to do things that allow shareholders to better understand the value of that business or -- but we're not going to get into specifics as I said earlier, what those are, but those would be just some of the synergies.

Q - Andrew Crean {BIO 16513202 <GO>}

Could we -- could I come back on the first question? If you're not going to give targets, can you please give us more disclosure so that we can actually forecast the dividend of the US business?

A - Mike Wells {BIO 4211236 <GO>}

Yeah, we can look at that. We appreciate the -- that in the absence of other information, cash and the ability to model cash is a key metric for the market. So we'll continue to increase disclosure. That's a fair challenge.

Q - Andrew Crean {BIO 16513202 <GO>}

Thank you.

Operator

We now have a question from Abid Hussain from Credit Suisse. Your line is now open.

Q - Abid Hussain {BIO 20229932 <GO>}

Hi. Just one question for me, please. Actually just coming back to some of the earlier questions on, I just wondered if you can clarify how much discretionary surplus capital that you have across the Group? I don't think the LCSM provides the true reflection of where you are. So I just wondered, can you give us an indication of where the discretion surplus capital is sitting and how much it is? And I guess the second part of that question is, what's your ability and what's your firepower for kind of growth within Asia?

A - Mike Wells {BIO 4211236 <GO>}

Yeah. So, I mean, let's start with where we are no longer which under Solvency II basis we're clearly one of the best capitalized firms under an ill fitting regime. So our intent to this is not a capital arbitrage, we release capital by shifting jurisdictions. As I said earlier, our view on risk capital allocation hasn't changed and a lot of our internal tools haven't changed. And this is true across a number of capital regimes that we manage the business over decades. So this is intended to be a very strong company financially.

Do you want to talk about the specific numbers to give him a word of it? [ph]

A - Mark FitzPatrick {BIO 20178326 <GO>}

So in terms of the surplus in terms of the half year that we have in terms of total insurance and asset management, if you look at the half year accounts in terms of the EEV section in Note 9, you'll see the continuing operations number GBP5.2 billion for personal insurance and asset management, and then you've got in other types of GBP3.1 billion and Asia makes up just GBP2.9 billion, just under GBP3 billion of that.

Q - Abid Hussain {BIO 20229932 <GO>}

Is that all? I mean, how much of that is actually fungible uncertainty available to use?

A - Mike Wells {BIO 4211236 <GO>}

The quality of capital is a good one, but that's under, I think, even in the most strict regimes, it's a multiple of sources. It's a multiple of measurements. I think it'd take us more than a couple of minutes there to give you a line by line on that, but if you think about it, it is by the most stringent Western Standards moving to a more regime -- not exactly sure I gave them, but I am doing a line by line comparison of the three capital regimes.

Operator

We now have a question from Nick Holmes from Societe Generale. Your line is now open.

Q - Nick Holmes {BIO 3387435 <GO>}

Hi, there. Thank you very much. Just one question. Can you tell us the net impact on RBC of the NAIC reform and giving up the permitted practice because you changed your view on both of these items, haven't you? And I wondered if you could give us a bit more detail on what the net impact of the two is. Thank you.

A - Mark FitzPatrick {BIO 20178326 <GO>}

Thanks, Nick. So we don't give RBC as you know for year, or until the full year. The permitted practice historically renews in October, first week of October. So with the new regime coming, being it's the only one of its type, I think it's much good housekeeping as it was anything else. And the intent was to give you directional, not the specific basis points on the impact of those because the calculation is not simply on the permitted practice. So the big change in the period of time since that historic discussions of this would be the movements in rates effectively.

A - Mike Wells {BIO 4211236 <GO>}

I would add that one, we haven't changed our view. Rates have changed in the market, so the impact relative to the calculation changes and we've given I think just in guidance that we expect to be in that range of 400 to 450 and we still expect that that guidance to hold from where we sit right now for the end of the year.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. So you're just looking at the year-end position. If you're guiding on the negative effect on the RBC ratio from NAIC reform next year, is that still the same? The changes in NAIC calculation?

A - Mark FitzPatrick {BIO 20178326 <GO>}

No, no, no, we're looking -- when I talk about 400 to 450 we're talking about in the new regime, which I think was the guidance that Chad gave last year in Singapore was that we're -- we were prepared to be in that range of planning for that. And certainly low rates has made that a bit more challenging, but we still expect to be within that range. And obviously where rates are will depend where we fall in that, but I think we're talking exactly about the new regime.

A - Mike Wells {BIO 4211236 <GO>}

So Nick the new information would be rate and equity movement and a better understanding of the models as everyone -- as we're moving forward with more information there. So we're trying to give you a current look, I don't think it's a contradiction of our -- and everything doesn't help [ph] the same we would have different information for you, be higher.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. I'm sorry to lay the point slightly, but just could you -- I mean, the influence of what you're saying seems to be net-net, there is no particular change. Is that your guidance?

A - Mike Wells {BIO 4211236 <GO>}

Again, not going to give you to a specific RBC target or number or indication of where we are today, we don't do that on intervals, what we're telling you is the combination of the new regime and the strength of the firm, we'll put it in the range that we forecasted even with the changes we've discussed. And that was the consistent with both -- even though things have changed. So it's a --

Q - Nick Holmes {BIO 3387435 <GO>}

And giving up the permitted practice?

A - Mike Wells {BIO 4211236 <GO>}

Yes. Giving up the permitted practice, which, again, as we said would've renewed in October and given it's the only one of its type in the states with as much hygiene as not -- that's a conversation with us (inaudible) And its impact on the new regime may or may not have been helpful and it wasn't a conversation...

A - Mark FitzPatrick {BIO 20178326 <GO>}

(inaudible) those permitted practices do with how the swaps are treated and it's a much lower portion of our book, our hedge book now than it was when it was put in place. And the new regime is much less sensitive to rates, particularly short-term fluctuations in rates. And so it's less of an impact whether it's favorable or negative based on any particular rate or market environment, it's just less impactful. So we are going forward without it and in the new regime.

Q - Nick Holmes {BIO 3387435 <GO>}

And the number of GBP570 million that you gave is the permitted practice contribution. Is that correct?

A - Mark FitzPatrick {BIO 20178326 <GO>}

Yeah. That's getting into...

A - Mike Wells {BIO 4211236 <GO>}

That was a mid-year. That was at mid-year.

A - Mark FitzPatrick {BIO 20178326 <GO>}

That was mid-year. We're not going to do an update on that.

Q - Nick Holmes {BIO 3387435 <GO>}

That was mid-year. Okay. But it's going to come down, yes, because of the market movement. Okay.

A - Mark FitzPatrick {BIO 20178326 <GO>}

No, no, no, Nick. Nick. we're going to come down.

A - Mike Wells {BIO 4211236 <GO>}

The impact would've gone up with market. With rate drops, that impact would have gone up.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. But you don't want to give us any further guidance?

A - Mark FitzPatrick {BIO 20178326 <GO>}

No, no.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay.

A - Mark FitzPatrick {BIO 20178326 <GO>}

Thank, Nick.

Q - Nick Holmes {BIO 3387435 <GO>}

Thank you very much. Thank you.

Operator

We have currently no further questions. Back to you, Patrick.

A - Patrick Bowes {BIO 16444249 <GO>}

So I've just got one on the online. That's from Jackie (inaudible) Comparing the value of Pru Asia's AIA, is the market giving you limited value for Jackson? What is the right answer to shareholders?

A - Mike Wells {BIO 4211236 <GO>}

Well, again, I think, it's better for management to drive earnings, new business profit, embedded value, dividend, capability, all the things we're doing. I think the market prices in its view of the businesses. On the US business, I think, a fair way to look at it is, it is unique in its space. Everything about the business is done what it was priced and built to do. Its outcome for its consumers has been excellent. Its pricing integrity is there. This is not a business that's come back to you with assumption change after assumption change, the original pricing and the original integrity and its -- of its model is held. And it's in an environment in the States over the last 36 months with regulatory turmoil and competitors who've had some challenges.

So I think the right thing for us to do is to try and give investors a clear view on the value of that business, clear view on the cash generation of the business, so that it appeals to a broader set of investors and makes it easy for the value, but the actual reaction to the stock and its value and I don't want to comment on it.

A - Patrick Bowes {BIO 16444249 <GO>}

Perfect.

A - Mike Wells {BIO 4211236 <GO>}

Okay. All right guys. I want to just thank everybody for your time today. Obviously, thank you everyone for the support. We made a conscious decision in this journey to go as fast as we could and give you information when it was printed and true versus forecasting when we might know something or might have something, I appreciate that's created some uncertainty. Thank you for your patience. And in doing that, I think, we've created two very successful very good companies. They are both -- I've not seen in my years here either side of this transaction of these firms anymore tuned up, anymore focused on what their objectives are. And I think they're both going to be extremely successful in their space. And I just want to thank you for your support and your time today.

Shelly, back to you, I think we're done.

Operator

Ladies and gentlemen, this concludes today's call. Thank you for joining.