# S1 2020 Earnings Call

## Company Participants

- Axel Andre, Executive Vice President and Chief Financial Officer
- James Turner, Group Chief Rick Officer and Compliance Officer
- Mark FitzPatrick, Group Chief Financial Officer & Chief Operating Officer
- Michael Falcon, Chief Executive Officer
- Michael Wells, Group Chief Executive Officer
- Nicolaos Nicandrou, Chief Executive Officer
- Patrick Bowes, Head, Investor Relations
- Raghu Hariharan, Chief Financial Officer

## Other Participants

- Abid Hussain, Analyst
- Andrew Crean, Analyst
- Ashik Musaddi, Analyst
- Blair Stewart, Analyst
- David Motemaden, Analyst
- Greig Paterson, Analyst
- Jon Hocking, Analyst
- Kailash Mistry, Analyst

## Presentation

### Operator

Ladies and Gentleman, welcome to the Prudential 2020 Half Year Results Call. My name is Bethany, and I'll be coordinating your call today. (Operator Instructions)

I will now hand over to your host Mike Wells, Group Chief Executive, to begin. Mike, please go ahead.

### Michael Wells {BIO 4211236 <GO>}

Bethany, thank you. Hello, everybody.

Welcome to the Prudential plc 2020 interim results and strategy update. This year, we've recorded our full presentation in advance and it's up on our website with the transcript already. So today, we can use most of the call then to take your questions. And given the nature of our news this morning, we would expect that, that will take up the full hour at least. So to give you an idea who is with me, I'm joining you from Lansing, Michigan, the home of Jackson. Also in US, you've got Michael Falcon CEO of Jackson, Axel Andre, CFO of Jackson, and in London, we have Mark FitzPatrick, our Group CFO and COO and the IR team. In Hong Kong, we have Group Risk Director, James Turner; CEO of our Asian business, Nic Nicandrou and CEO of Asia, Raghu with us as well.

And I think, out of respect of time, instead of going through a summary of the comments we made on the video, I'm going to go straight to Q&A and just see where we are. And if need to, I'll bridge back to some of the key themes and key things we've accomplished in the first half of this year.

But Patrick, if you're okay, let's just go ahead and go straight to Q&A.

### Patrick Bowes {BIO 16444249 <GO>}

Sure. Okay. Bethany, can you bring the first question?

## Questions And Answers

### Operator

Our first question comes from David Motemaden from Evercore ISI. Apologies. David, please go ahead. Your line is open.

### Q - David Motemaden {BIO 18818634 <GO>}

Thanks. Good morning. Just wanted to maybe just get a little bit of background in terms of what made you think the full separation of Jackson is best achieved through an IPO. That's the first question.

Second, do you foresee the need to inject any additional capital into Jackson to facilitate this transaction?

And then third, if I may. If I look at the org chart, it looks like Jackson is stacked under PCA. So, I'm wondering if the Hong Kong RBC ratio currently benefits at all on a local basis from having Jackson as a wholly owned subsidiary. And if so, is there anything that needs to be put into Hong Kong to help replace that? Thank you.

### A - Michael Wells {BIO 4211236 <GO>}

Thanks, David. So, Mark, I'm going to let you take the last one. David, on the -- so if you think of this journey to Asia, it started with the demerger of M&G Pru. And I think there is a sell-down obviously to Athene of 11.1% to now the announcement today. So what we've said all along is we maintain optionality and how we execute and the statements, we talked about the fact we still could do a demerger if we thought markets require debt. That said, what you've seen us do with the Athene transactions is you've got Jackson's capital levels to a range that we think is appropriate for a standalone entity versus an entity that's part of a group.

We don't anticipate the need to put capital in Jackson. Actually, you'll have, if you look at the M&G transaction, there would be some debt activity, some movement back and forth with capital to reduce leverage in the group. All those things coming in the next months to get Jackson ready to be standalone. So the answer to your second question is it's not anticipated.

Mark? The IPO -- the advantage to an IPO is that you get more capital for reinvestment in Asia over time. The advantage of the demerger, obviously, would be less of that but faster. So again, we maintain that option. But the IPO is the route we're pursuing at pace now.

Mark, you want to talk about the regulatory structure?

## A - Mark FitzPatrick {BIO 20178326 <GO>}

Yeah. David, so the LCSM for Asia is 308% that is not affected in any way by the US piece. It's effectively is standalone tranche, if you will. So a separation of that would not change the Asia LCSM number. So that would continue if we were to do it at 30th of June, that would still be at 308% number for Asia.

## Q - David Motemaden {BIO 18818634 <GO>}

Got it. Thanks. And if I could just follow up with Mike and maybe for Axel as well. Just the RBC, the 425% -- in the 425% to 475% range, how should I think about any sort of changes to your hedge strategy within Jackson maybe from more of an option-based approach to more of a futures-based approach that would help reduce the upfront costs and improve capital generation?

## A - Michael Wells {BIO 4211236 <GO>}

Well, David, Jackson's bias is a futures-based approach and that was done at the time, not so much cost focused as it was counterparty risk-focused, so to concentrate the counterparty risk on upmarket and equity, not on downmarket and equity. One of the learnings from a previous crisis was the fact that we look back at some of the bank counterparties and realize that some of the risks that an insures has, they are highly correlated to the same one. So, we wanted to separate that. So the organization uses both. And at higher capital levels, you have more options on hedge strategy. So, there is a trade-off there of return on equity, capital intensity, hedge intensity, but it's across that range.

Axel, do you want to add any color to that?

## A - Axel Andre {BIO 19072099 <GO>}

I think you're right on, Mike. So essentially, when we are in a more benign environment, we would be hedging more with options and as we -- as the first quarter unraveled the options, essentially the put options that came in the money, we gradually rebalanced more into futures. The profile of the liability was more linear, so the futures were better match and as now we're tracing back, we're using a mix of futures and options.

## Q - David Motemaden {BIO 18818634 <GO>}

Thank you.



## Operator

Thank you. Our next question comes from Kailash Mistry from HSBC. Kailash, please go ahead.

## Q - Kailash Mistry

Hi. Good morning, afternoon, everyone. Thank you for taking my question. Few on Asia. First one is on Hong Kong. What's your base case for the border reopening? Is it fourth quarter or 2021? On the domestic business, thank you for the information on Slide 64. It seems to indicate a slowdown in the run rate between the first quarter and the second quarter. Is that COVID related? Or is that just the high base because of the launch of QDAP and VHIS this time last year? And specifically, what was the momentum like in July because, obviously, the insurance authority approved the sale of par online. Has there been a strong pickup? And also, has there been pent-up demand there?

Second question is just on agency. Obviously, you flagged that there is 7% growth in the agency force excluding India. Can you provide a little bit more color, especially what was the growth in Hong Kong, China and Indonesia?

And then on Pulse, seems to be some very strong progress there with 70% of customers being new and younger than your existing customer set. Can you talk a little bit about average case size, business mix compared with traditional business or your historic business and any impact that's had on the IRR that you're writing? Thank you.



## A - Michael Wells {BIO 4211236 <GO>}

So just a couple of general comments and Nic, I'll ask you and Raghu to comment as well. So as you've seen consumer interest in health and protection by both in action, buying policies and also in just in general interest, so there has been increased interest in joining firms that supply those products. And we're clearly an attractive player in that space. I'll let Nic tell you some of the more specifics around the growth. To scale the growth just from my point of view, adding 70,000 plus agents in this period is most of our top 10 competitors agents in the region, it's larger than their agency force, right? And not to say, all these agents will be successful or productive.

We're getting better and better at agency management. It's all virtual now. There's some great tools to improve the likelihood of success. But I just -- I want to add some scale to that. I think it's an incredible effort by the team. But Nic, do you want to comment on some of the specific questions, case size on Hong Kong, domestic run rate? You know the -- I would say on the other question, we don't have a forecast now given how fluid governments opening and closing borders and travel on COVID. I think it's pretty hard for anybody to credibly predict.

What I can tell you, I think in all markets with COVID globally, we are much faster at responding to whatever the opportunity set is. So for example, we didn't have all of our products, as you mentioned, prior approved until well into the second quarter virtually. We now have agency up and running with that. We have the leads coming off of Pulse. So in a lockdown, we're much more effective week by week than we were previously and therefore, less affected by a lockdown and we're much faster at coming back up to speed when a market opens. And we're assuming that this is the environment we work in for foreseeable few quarters at least.

And Nic, do you want to answer the question specifically, please?

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

Okay. Thanks, Mike. Thanks, Kailash. We stand ready when the border opens in relation to Mainland China. The -- it's possible that it may not, but once if it was to open, then we stand ready to go. And we know when we've seen opening up in other parts of the region, there is a rush to buy. So the minute the border opens, we think there'll be a rush to buy. We included a slide in the deck on 65. So that shows the information around our latest survey on purchasing intentions and why Mainland Chinese customers prefer Hong Kong and really it reinforces all the structural advantages that Chinese consumers see when they buy product in Hong Kong. So, I'm not going to predict when it will open, but we stand ready to take advantage of that.

In relation to the domestic, we had a good first quarter. First quarter, and these are published stats [ph], we were down, down 8%, and we did better than the rest of the market that was down 25%. It was on the back of us. So, we're doing really well in connection with the Qualifying Deferred Annuity Plan. Having added up all the information, we secured 17% share of that market. that speaks to the businesses ability to leverage an opportunity to innovate, move fast, use distribution channels, both agency and banca to deliver growth.

VHIS was smaller around the sector in terms of APE, clearly important in terms of case count and we've got a fair share there as well. In Q2, to your question, there was a slowdown. There was more social distancing than we saw in the first quarter, particularly as students came back in March and place -- yeah, the containment measures tightened up, as you know, Kailash, you are in this market. So that slow things down a little. Branches, SCB branches and generally banks reduced their capacity as we went into the second quarter. In fact, it didn't -- capacity wasn't fully restored until the back end of June. So, that was another factor.

And to your point, yes, queued up having been outside its first year also had, if you like, the uplift that was given to Q1 and the first full quarters of this product reduced. So queued up made up around 28% of our sales in Q1 and only 14% of our sales in Q2. The ability to sell virtually really only came in, in earnest towards the back end of June. It has been utilized in July.

Sales in July were kind of roughly at the same level as those in June in terms of comparison with prior year, roughly a third down because we have momentum with new products and a new push on a number of areas, but we have effectively a surge in infection rate here. So now in Hong Kong, we are experiencing the tighter of all the constraints that we've seen.

Nevertheless, there are -- there remain important opportunities for us. Domestic, we've got a sizable agency force. To your question on agency numbers, Hong Kong agency force at 24.5k is up 7% compared to what it was a year ago. Most of that uplift and a lot of the recruitment this year was domestically focused. We are celebrating our 20th year with SCB, so an important relationship. And we've launched Pulse, linking that to your last question. Not only have -- we've got 400,000 members now, users of Pulse and the business has done a really good job in using that membership as a lead referral, if you like, to agency and have managed to. We haven't yet farmed the full amount, but we've managed to convert since the April around 12,500 at full premium, full margin. So, that's where we are in Hong Kong.

On agency, the increase in the account, it's coming from Hong Kong. We said 7% increase in count relative to a year ago is coming in Hong Kong. I referenced that. Indonesia was up 13%, agency count year-on-year, Philippines was another area. China was also up. And in most other places, we've kind of held, notwithstanding the fact that for large parts of the second quarter because licensing is done by government authorities, a lot of licensing was shut. But nevertheless, we -- 72,000 new recruits, mostly from those markets.

On Pulse, the -- okay, there are -- we've done 1.7 million policies. Again, there is a slide in the appendix. 1.5 million of those were kind of offers, very short term, whether it's personal accident, some short-term life. There were freemium, if you like, some COVID-related covers. So that's that. About 165,000 takers of small micro insurance, so mini insurance, if you can call it that. Case sizes are around $12 a year, so $1 a month. So that gives you a sense now. We're able to effectively make money.

These are protection policies and the margins are fine, but literally, very small. But we can make profits on a dollar a month now, which is something that we couldn't do two years or three years ago. And the plans to do much more across all 11 markets where we've launched Pulse, we'll do at least three digital products in the market by the end of the year. And then we've had around 28,000 of referrals. This is nurtured leads that were passed on to agents that were followed up face-to-face or some of them were done virtually. And they translated, as you can see in the slide, around $60 million of APE.

That's the average case size, where it was done in Hong Kong, was of the order of $3,000, where it was done elsewhere was $1,000. And these are the full loaded, if you like, policies that an agent would sell, had the referral not come through Pulse, had it come through another channel. So the margins on those are the same as we do through other channels. So high-margin products. So, we can do the introductory offers to get a second point of engagement. We can do micro or mini products to act as a second point of engagement. And then once these are nurtured, they can be passed on to agents using new sophisticated lead management systems and converted into fully fledged products.

## Q - Kailash Mistry

Thank you. If I may just follow-up on that Pulse thing. Your offering is pretty advanced versus some of your competitors across the region. Are there other functions that you feel you need to add to this? Or are you kind of done with that and now it's about acquisition and then cost referral and the rest of model that you've highlighted?

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

No, we are only just starting. We are only just starting the -- we're going to add. There is a lot -- look, there is a lot more we can do. The next phase of this is, we said earlier that 90% of our products across the region can be sold virtually. This is done through a combination of technologies at the moment, as we've joined it up together two or three different platforms. By the end of the year, that virtual sale will be able to be done via Pulse with video, with being able to attach document. That's already up and light in the Philippines. It's just up and light now in Malaysia. So the 38% to the extent that we have another 38% in the future quarter will be done through Pulse. So it's becoming a fulfillment to -- for the agency, as well as a referral to -- as well as to where people can buy directly.

We're going to be adding a lot more mini projects -- products across the piece. And also, we are trying to bring more aspects of the value chain onto this. So Indonesia alongside the launch of Pulse, which attracted three million downloads earlier in the year, at the same time, we incorporated a minor claims processing functionality. So, we've integrated Pulse with the hospital portals, so that -- and issued kind of e-medical cards, which can admit someone onto the hospital. The bill can be submitted electronically by the hospital through Pulse to ourselves. We've connected to 570 of the 1,700 hospitals in our medical network and we can process a claim in less than a day. We're also using it for reservicing again in Indonesia, in Hong Kong. In-force customers can use it to go in and do inquiries and small servicing on their policy.

Now from here, we will have more services. We'll look at mental health. We'll look at diabetes. We will broadened the direct offering. We'll be tuning up the online-to-online everywhere. We will integrate PRUworks, which is our SME employer benefit into this. In fact, we will rebrand that to Pulse Prudential -- oh, I'm sorry, business at Pulse. We will be attaching it to other ecosystem. We've done that with OVO. We'll be doing that with UOB. We made another announcement with one of the biggest e-commerce platforms in Thailand today, Central. Again, we will be integrating it with that. And we'll look to see if we can broaden the geographical reach beyond 11 markets that we're in. So a lot of development and thought is going into this, both offering another route-to-market for us, but also integrating it with our end-to-end, if you like, with our traditional business model and through that gaining efficiencies. Sorry, long-winded answer but it's a big and a long answer, but it's an important differentiator for us. I mean, look, the other thing it gives us and what we've learned through the crisis is that people are now asking for services to be bundled with protection. So the fact that we can offer protection across the piece and now with services to go with this, again, puts us in a unique position.

## A - Michael Wells {BIO 4211236 <GO>}

Thanks, Nick.

## Q - Kailash Mistry

Thank you.

## Operator

Thank you. Our next question comes from Jon Hocking from Morgan Stanley. Jon, please go ahead.

## Q - Jon Hocking {BIO 2163183 <GO>}

Thank you. Good morning, everybody. I've got three questions, please. Firstly, on Asia, on your business strain, can you comment on why that was down at a much lower rate than sales? I think it was down 7% year-on-year. Is it purely the mix shift away from Hong Kong? But it doesn't seems to be something else going on there. So how should we think about that going forward? This is first question.

And second question, when are we likely to get some more visibility on the Hong Kong group-wide supervisory regime? And do you still expect that by year-end?

And then final question. Just looking at Slide 20, where you've got the phasing of the move restrictions, et cetera, it does seem that a lot of markets have actually gone into a more restrictive phase either in June or subsequent to the quarter end. You mentioned, obviously, the ability to transact online in Hong Kong, but that seems to be one market. Could you comment a little bit about how we should think about the sort of sales temper 3Q versus 2Q? Thank you.



## A - Michael Wells {BIO 4211236 <GO>}

Yeah. So let me give a general comment on the third one and then, James, I'm going to have you comment on group-wide Supervision and Raghu, how about you discuss new business strain in Asia. I'm trying to get everybody involved in the call today. So, we have 11 markets now, Jon, that we can transact virtually as we finished the second quarter. So basically, all of our product sets in those markets. And it's a -- and Nic referred to, one of the other pieces that's gone on is development of technology and tools for the agency force to be able to transact virtually and best practice virtually and things. So again, we're much better at that than we were. And those learnings are shared real time.

I mean, one of the -- our pace at being able to develop now and to be able to share something that's working across the region is historic for PRU. One of the agent lead -- one of the pieces in technology that helps an agent work with the Pulse lead to a full -- one of the full client relationships that Nic referenced, for example, was developed in a hot-house over three days virtually. People -- not just tech people, people all over the region and our digital team, they finished on a Sunday night. Again, none of these people could be in the same room. And Wednesday, the app was up in the iStore and Google store, et cetera.

So, there is a pace now that's unique. So when I say we're getting better weekly, that means improvements in the tools as well as sharing what's working. But you have 11 markets now across Asia. And the US is virtualized, its sales processes, its statements. It's always been an industry leader in its technology platform. That's -- it's clearly using that to its advantage in this environment as well. So, this is not just an Asian story for us.

But Raghu, you want talk about new business strain and James, you want to talk about group-wide supervision, please, both briefly. We've got to keep the pace going, guys.

## A - Raghu Hariharan {BIO 20434535 <GO>}

Yeah. Sure. Good afternoon, morning as it might apply. I think, Jon, it just reflects two things. One is it reflects a higher product, better product mix. So, we have more non-par and protection sales and par sales, as the proportion of sales are lower. That's one. And the second one is just the effect of lower rates. So that explains the strain levels, which have gone from 13% of APE to 18%.

## A - James Turner {BIO 21226013 <GO>}

Okay. And on the GWS, the primary legislation enabling the new GWS framework was passed by the LegCo before the end of last season -- the last session in July. The subsidiary legislation is required. And with the announcements today to extend the LegCo, it remains our expectation. So the GWS Framework will come into force in Q1 2021.

## Q - Jon Hocking {BIO 2163183 <GO>}

Thank you. Can I just come back on the -- on the sales point, Mike. You mentioned 11 markets have got the ability to transact virtually. What proportion of the product range? Would it be fair to say that you've got most of your best-selling products with virtual execution capability?

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

Shall I take that, Mike? So the -- the only -- the reason it's not 100 is Taiwan hasn't -- hasn't approved the use of virtual. It didn't need to because the impact in Taiwan of the pandemic wasn't that severe. So that was one. And the other one that hasn't been -- that hasn't virtualized is the use of linked products in Thailand. Vast majority of what we sell is linked. So that's the reason it's not -- it's not 100. So it's one market and one product type in another market. So -- and the other one is linked products also in Hong Kong. But that's less than 1% share of the industry and less than 1% share of our numbers.

To your question on some markets, our increasing restrictions in terms of impact on Q3, I referenced Hong Kong, we're now having the tighter set of restriction here. In Indonesia, Indonesia is struggling to contain this. So the number of cases now is increasing as is India. So that situation is live at the moment. In Vietnam, actually part of the reason Vietnam shut and opened up very quickly because they were decisive at the beginning. If they got a few cases, they shutdown. So having gone three months with almost no infections, when they've had a few, they immediately introduced social distancing. So look, if the situation is live and it's volatile like everywhere else in the world at the moment, and -- but we have -- we have more strengths. We referenced a few in the call so far in our presentation and therefore, we should be able to mitigate better than we did immediately at the outset.

## Q - Jon Hocking {BIO 2163183 <GO>}

Okay. Excellent. Thank you.

## Operator

The next question comes from Andrew Crean from Autonomous. Andrew, please go ahead.

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

Thank you. Good morning, all.

## A - Michael Wells {BIO 4211236 <GO>}

Hey, Andrew.

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

Two questions, if I can. Firstly, you were talking about debt capacity of Jackson being between 20% and 25%. And you were saying that Jackson doesn't need capital put into it. By my math and it may well be wrong that suggests debt raisings of between $2 billion and $2.7 billion to get to the 20%, 25%. Is it fair to say that, that money is earmarked for a pre -- that level of money is earmarked for a pre-IPO dividend?

And the second question, it's to do with where you set the dividend going forward. It's really difficult for us to judge the capital position of the company because we just don't have any ideas on our LCSM and that sort of thing. But I think you said that you've invested a $1 billion a year over the last decade. Do you require to invest more than the $1 billion a year organically going forward? And also do you need to reduce your group debt beyond that bit, which will be repaid as a result of the pre-closed dividend on Jackson?

## A - Michael Wells {BIO 4211236 <GO>}

Okay. Thanks, Andrew. Good questions. Let me -- let me start generally and Mark Fitzpatrick, I'm going to ask you to comment on the various debt pieces. So on the ability to deploy capital organically, Andrew, if you look at even just the last six months, you've now got a scale position in Thailand. You've got an increase as we've been talking in Pulse and the ability to do business through a digital channel and we've grown agency again. You're moving further from par product as Raghu mentioned, I think in his comment. So the breadth of products we're selling are incrementally more capital intensive.

Now, this is not suggesting we're going to a heavy spread-based sort of strategy across the region. That's not the message I want to land at all. But these are products that are non-pared disproportionately. So, they are more capital intensive. We published the IRRs. You see where -- it is very profitable, well received by the consumers, et cetera. So, we believe we can deploy more capital organically in Asia. And we don't want -- the dividend policy doesn't want to constrain the organic growth.

The inorganic stuff is, as we've talked before is opportunistic. We have two places or three places. We look there. Its increase in -- we're in the markets we want to be in. We have a great footprint. It's things that are related to earnings to something improve the actual operating earnings of the firm. That's the variety of lenses there. Improved distribution, first, so banca deal, for example, improves capability, which you've seen us do with the Pulse platform and those sorts of options are outside of our business plans and we view them -- as they approach us one at a time and so we don't -- we couldn't forecast them because we pursue a lot of that all the time, but we don't know what's going to land, when, it's counterparty dependent basically.

But, Mark FitzPatrick, would you comment please on the questions on debt, pre-IPO dividend, those pieces?

## A - Mark FitzPatrick {BIO 20178326 <GO>}

Yeah. Good afternoon. So in terms of the debt numbers that you spoke about, I think, kind of the 20%, 25% leverage based on the Jackson half year IFRS equity and also if you add in the additional $0.5 billion from Athene that closed last month in terms of its equity investment, that would get you somewhere in the $1.8 billion to kind of $2.5 billion debt type range. And effectively, we would expect that, that would be -- that, that would come up to plc or to the shareholders during the course of, kind of the pre-IPO dividend. So, that would be then used by group to effectively repay, as we mentioned, repay some of our debt at the center. We have quite a lot of debt that we can redeem that is kind of 2020-2021 call date. So we have the option. And we're looking to be able to do that, to be able to repay some of our debt, to be able to ensure that our leverage ratio stays at a good and sensible level.



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

Great. Thanks for answering.

## Operator

The next question comes from Blair Stewart from Bank of America. Blair, please go ahead.

## Q - Blair Stewart {BIO 4191309 <GO>}

Thanks very much, and good afternoon. Just a couple of follow-ups. I was also interested in Andrew's questions. Can you tell us what the level of organic RBC build is at Jackson now that, that it's not paying a dividend back to group? That's the first question. Give us an idea of where the RBC might land or everything else being equal.

The second question just relates to the equity story, I guess, for Jackson as we stand today. We've gone from various levels of appetite on sales and new business and also on objective. I think from Michael to improve the stock capital and cash generation, I just wonder where we are in all that? I think those two things are linked to my first question.

And my final question is just an observation on Indonesia. It was definitely a stand out. In terms of IFRS profits, growth across the region was very strong in all countries except for

Indonesia. I'm sure there are some obvious reasons for that. But perhaps you could just comment on that. Thank you very much.

## A - Michael Wells {BIO 4211236 <GO>}

So Blair, remember, where we are with the SEC in a pending S-1. So forecasting RBC would fall into that over-the-line category. But I've got Mark FitzPatrick first, then Michael on -- Mark, on, what we can say on again on capital generation. Let's call it that.

Michael will add [ph] just a little bit on equity story and then Nic will come back to you on Indonesia, please, on IFRS.

## A - Mark FitzPatrick {BIO 20178326 <GO>}

Okay. Blair, good afternoon. So in terms of organic RBC build, effectively, you've heard us say and you've heard say for a while in terms of approximately about the $1 billion -- $1.1 billion in terms of organic capital creation. And effectively, post the Athene reinsurance transaction, we've indicated that, that would probably take about $150 million of that level. So the guidance would probably be kind of somewhere between the $850-ish million kind of element. So that's on an -- on kind of the half. So, that's 425%. So that's about 20% to 25% kind of RBC points in terms of the half that we would ordinarily kind of look at on that particular patch.

So can't guide in terms of a forward piece, other than that component. But when you look at the element of the RBC role and you look at the capital generation during the component to the first half, you see that that's a strong number. And that's a strong contributor in the first half and very much in line with levels that was spoken about in the past.

## Q - Blair Stewart {BIO 4191309 <GO>}

Sorry, Mark, can you just clarify? Did you say 20% to 25% RBC points, is that in the half year?

## A - Mark FitzPatrick {BIO 20178326 <GO>}

Correct. That's in the half year. Yeah. So the ordinarily, we would operate at about, I'd said about $1 billion in terms of operating capital generation pre-Athene. Post-Athene, we're guiding that -- that's effectively closer to the 850 mark per annum. So that's where you get the $425 million for the half year and at the half year, that circa kind of 20% to 25% RBC points

## Q - Blair Stewart {BIO 4191309 <GO>}

Yeah. Thank you.

## A - Michael Falcon {BIO 17026942 <GO>}

Yeah. So Blair, good morning or good afternoon there. Michael Falcon here. And thanks for the question. So, I'm going to stay away, as Mike said, given the announcement that we've made and SEC rules. I'm going to stay away from forward-looking statements or a projection or a indication of what that equity story might be. But I can talk to where we are now and build on what we've said in the past, which is consistent with our view, which is that there is a big demand for protection products around retirement in the US, particularly around income and replacement income guarantee, as well as principal protection. Those are markets that we're in. We're the leading player in variable, and we've demonstrated our ability to quickly lead in other categories.

So, we don't see any change in terms of the market demand. In fact, in many indications that, that can increase with demographics and certainly volatility reminds people of why they want and need and use our products to begin with. I think we have excellent capabilities around distribution in that place and a low-cost platform that allows us to effectively and profitably write business and a proven historic ability to price and manage the risks associated with those. So, I can't go forward, obviously, as we go through the process, that appropriate times, there'll be more information about the nuance of the go-forward strategy as we can get into that detail. But I think the fundamentals that we rely on today are still there and they're consistent with what's built the company to this point.

## A - Michael Wells {BIO 4211236 <GO>}

And Indonesia, Nic? Thanks, Michael.

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

Thanks. Thanks, Mike. Blair, it's -- what you're seeing is the lag effect from past years, where we were seeing a decline in sales. So as we picked up last year, then that should change. I guess the other factor is, we are investing heavily in that business in terms of automation with tooling, the agency force, in terms of some of the developments, we're doing with Pulse. Indonesia is a little ahead of other markets. So, they are doing, they are developing a lot of things on behalf of the region as we look to developing once and standardize and use it elsewhere. And we've done a lot of work in the last year to launch, to refresh the entire product set and launch new ones.

We have 17 new product launches and all that requires investment in technology to pull through. Indonesia, now all our recruitment is done virtually. So again, that's more investment that we're making in that business. It's a shame on a number of levels. But certainly, for individual sales on COVID, but the underlying improvement in that business over the last year, a year and a bit has been phenomenal. But as soon as things normalize, we see a lot of demand coming back into a business that is much better placed now to fulfill that demand on a number of damage.

## A - Michael Wells {BIO 4211236 <GO>}

Thanks, Nic.

## Operator

I'll now hand back to Patrick for web questions if there are any.

## A - Patrick Bowes {BIO 16444249 <GO>}

Thanks. Thank you, Bethany. I've got two different questions. One from Thomas Wang in Goldman's in Asia. The first part of it is, are you providing any financial support to agents that used to sell to Mainland customers? And do you think you can continue to provide financial support if Mainland customers don't turn in any meaningful way until H2 2021?

And secondly, what's the impact of expense overruns on operating profit and new business profit in H1? That's Thomas Wang's question. So, I'll pose there probably to Nic.

## A - Michael Wells {BIO 4211236 <GO>}

Yeah, agreed. Nic?

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

We are -- yes, we're allowing Mainland customers to deferred payments. Our normal periods are 60 days to 90 days. Some of them are availing of that but nothing that impacts our overall figures. You saw the profits grow in Hong Kong strongly. The other -- the thing though that we've seen is and we've always knew that and known that, a lot of Mainland customers that transact with us have other business interest and other sources of income in Hong Kong. So, we've seen a switch away or rather a switch up in the electronic payment. So, it was around -- 65% of payments were received electronically. Now it's in the high 80s. So, yes, it's there to provide relief, but it's -- that's on the customer side.

Now on agents, the -- there are a number of initiatives that we have in place. Clearly, a lot of them are benefiting from trail commission from sales that they've done in the past. We do have financial support schemes available. They are available to all agents. They need to be, though, underwritten by leaders. We haven't seen a big take up in those in the last -- in the last six months. And if -- as I said, they are there for people to use. And on expenses, it's not impacted. I mean, clearly, some -- not all our sales costs are direct, but it's not giving us any cause for concern or indeed impacting the financials as you see them.

## A - Michael Wells {BIO 4211236 <GO>}

Thank you, Nic.

## A - Patrick Bowes {BIO 16444249 <GO>}

Thanks, Nic. I've got one more. And it's one for -- actually for Nic again and then the second one for Mark FitzPatrick from (inaudible) investments. The first one is, as business is increasingly done -- increasingly done online, has this reduced barriers to entry in your view for the market? And for Mark, which is, could you just run through the difference that existing investors should think about between a minority IPO and the demerger?

So, Nic, first?

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

I mean, a lot of -- a lot of the business that we've -- is human support at the moment. All the virtualization still requires a trained agent, albeit via video to engage -- to prospect engage with a customer. Yes, there is more research that is now done online. There are simple products that are made available and can be made available. And we're doing that as well. It's producing a lot of number of cases, but not necessarily a lot of premium at the moment until such time as a -- as further engagement is made. So, no, I don't -- I mean I don't think it's reducing -- it's reducing the barriers to entry, not for the fuller policies, the fuller sized policies.

## A - Patrick Bowes {BIO 16444249 <GO>}

Thank you. Then over to Mark.

## A - Mark FitzPatrick {BIO 20178326 <GO>}

So, minority IPO and demerger, ultimately, this is going to be driven by our desire to maximize shareholder value in terms of where we're at. Clearly, the element of an IPO, there is an aspect of sell-down proceeds to be able to fund future growth in Asia and that's a very important consideration. And also the aspect of an IPO would actually target Jackson's natural owners for the future on that particular piece. So, I can't really go into anything much more than that particular patch. But hopefully, that gives you a sense of how we're looking at it in our primary lens, which is ensuring we maximize shareholder value.

## A - Patrick Bowes {BIO 16444249 <GO>}

Thank you, Mark. Now, Bethany, that's all from the online. So back to you really [ph].

## Operator

Okay. The next question comes from Greig Paterson from KBW. Greig, please go ahead. Your line is open.

## Q - Greig Paterson

Good Morning, everybody. Can you hear me?

## A - Michael Wells {BIO 4211236 <GO>}

We can, Greig. Good morning.

## Q - Greig Paterson

I actually went -- lost the call when Andrew asked the question about the group debt. So, I don't know to what degree that was answered. But if it wasn't, I wonder if you could talk through the mechanics of the journey, how one would -- one should think about how much of the group debt will reduce considering money coming up from Jackson organic -- inorganic growth, et cetera, and Moody's leverage ratios, fixed charge coverage, et cetera? And that's question one.

The second -- two questions. One is, wonder if you could provide us the sensitivity of the RBC ratio to changes in interest rates. And the second one is you did provided the first quarter an RBC ratio for downgrades but subsequently, you've obviously transferred $28 billion of assets over to Athene. So, I was wondering how that sensitivity would have changed post the reinsurance contract? Thank you.

## A - Michael Wells {BIO 4211236 <GO>}

So, Greig, thanks for the questions. We did answer the debt piece. I'll let Mark address that again in a moment, give you a summary. The -- you have -- following in rates in RBC, and we did not give -- we gave a greater than number at the half year, just given everything we are announcing. We wanted to make sure you knew it. It's in the target range. And, again, we want to see that continue to move up.

So, I don't think -- Mark, why don't you do the debt first and then Axel will do a [ph] quick overview about where rates are in the US for us and how that affects RBC in general? That's not, again, two specifics on Jackson. But I think -- I think there is a clear mechanical piece, Greig, that's important in that.

Mark?

## A - Mark FitzPatrick {BIO 20178326 <GO>}

Okay. Greig, hey. So in terms of the debt, Greig, first and foremost, there aren't any -- we don't have any concerns with the ratings agencies or the ratings headroom. And we have been in conversations with the rating agencies in the run-up to today as you would expect and would expect to hear something from the rating agencies in terms of them providing some update on today's news imminently to the market.

So, I think in terms of the pre-IPO deck that would cut or that Jackson would raise and then dividend up to the -- to the group. It's in kind of the area of kind of the $1.8 billion to $2.5 billion debt. It's in that kind of -- in that kind of range to the 20% to 25% leverage. And that would be predominantly used to an element of debt repayment. We've got lots of flexibility and that's in terms of the debt that we have, and a lot of debt that is available in terms of the call dates that is there and that is available. So, no issues in terms of the debt and no issue in terms of rating agencies from a debt perspective as well, whether that be Moody's or any of the lot.

## A - Michael Wells {BIO 4211236 <GO>}

So actual impact of the de-risking of their credit portfolio with Athene and then the (inaudible) a little bit on the flooring rates in this RBC model.

## A - Axel Andre {BIO 19072099 <GO>}

Sure. Yeah. Let's start with the easy ones on credits. So, we disclosed at the end of the first quarter that if we did a hypothetical, that if 20% of the debt portfolio was downgraded by one whole debtor rating, the RBC ratio impact of that would be 16 points of RBC that was at the end of Q1. So post the transfer of a significant amount of assets as part of the reinsurance contract, that sensitivity has decreased now to 12 points versus the 16 points.

On the rate piece, as Mike said, the RBC methodology has an inherent flooring of interest rates. So the reality is given where rates are today, they are essentially below that floor that's embedded in those scenarios. So from a liability perspective, the reserves and capital requirements have relatively little sensitivity to interest rates at this point in time, whereas on the hedge and asset side, derivative hedges would be mark-to-markets and interest rate derivatives would be mark-to-market. And to the extent that we have some great protection embedded in fixed-income assets such as long duration US treasuries as we've mentioned in the past, those are carried on the -- on the stat [ph] balance sheet at a group level [ph].

## A - Michael Wells {BIO 4211236 <GO>}

Thanks, Axel.

## Operator

The next question comes from Ashik Musaddi from J.P. Morgan. Please go ahead.

## Q - Ashik Musaddi {BIO 15847584 <GO>}

Thank you. And good morning, everyone. Just I had a couple of questions, if you can help me. The first one is, if I look at the embedded value report, I mean there is a bit of economic assumption changes in Hong Kong business and that has resulted in $3.5 billion reduction in embedded value. I'm a bit surprised with that big numbers, because if I look at the embedded value of Asia, it's about $35 billion. So even if we say that Hong Kong is about a third, let's say $10 billion, okay, so it feels like the interest rate drop has wiped out the third of Hong Kong's embedded value. Can you get some clarity on that? What sort of assumptions were used in past and what has changed? I mean it looks like a massive drop.

The second question is on the demerger. I mean you mentioned that if the IPO is not successful for market reasons, then you would demerge the US business. What does that mean for capital for Asia? Because on one hand, you're suggesting that you might need that capital that comes from US to help the growth, to accelerate the growth in Asia. But at the same time, if you demerge, then you're not going to get back. So how should we get that?

And lastly, can we get some sensitivities on RBC for equity market as well? I think you gave, like clear answers on interest rates, but anything on the equity market would be helpful as well. Thank you.

## A - Michael Wells {BIO 4211236 <GO>}

Okay. Raghu, do you want to explain the shift -- the embedded value changes in the half year, Hong Kong?

## A - Raghu Hariharan {BIO 20434535 <GO>}

Sure. Thanks. Hi, Ashik. So first thing, I would do is consider both the -- as you know, the short-term flux and the effect of the economic assumption changes together to gauge the total impact. So that's point one.

Second, as you know, we updated options on an active basis. So here what's essentially happened is that the risk discount rates have undershot the fall in risk-free rates. As you know, the US 10-year is down 126 bps. Risk free -- risk discount rates have only come down 100 bps. So, we are holding some for market risk. And while the SCR has actually overshot the fall in risk-free rates. So the earned rates are lower. To give you a sense, it's about one and a half times, the 126 bps fall in risk-free rates.

And this is because of two reasons. One, we do not assume a mean reversion. And this is an important point. And the second -- so we assume June levels stay forever. And clearly, we also do not assume a dynamic rebalancing of the assets. So as bond values go up, proportionately you have more bonds and therefore, your earned rates are lower. So, it's purely a mechanical impact of the assumptions coming through our EV.

## A - Michael Wells {BIO 4211236 <GO>}

And then on demerger. So, I think we've been pretty clear on the advantages and disadvantages of both. I don't think we're looking at a scenario whether we have failed IPO. I would disagree with your choice of language there. I think if we looked at a market and thought if we can create more shareholder value by a demerger, you still have the debt that's been discussed on the call, that transference of an internal dividend, if you will, up to group. And it would be a decision by the Board and Management that, that was more accretive to value than an IPO given the unique market sickness [ph]. I think we're pretty clear that we think we can do a market -- an IPO in the first half of next year and we have the work streams, Ashik, that are consistent with an IPO, are consistent with the demerger on timing and on effort.

And so we don't anticipate any issues with an IPO, but we're just making sure everyone knows we're maintaining the option and we have a backup plan, if we don't think the market. So, I think like March of last year -- of this year, that was difficult environment, we still got off a -- we were the largest reinsurance transactions ever done and we got off in equity sale in that climate. So, I think we're confident we can do this. But we're also maintaining optionality, which I think is appropriate given the importance of the transaction.

On RBC, Axel, do you want to comment? I'm not sure I'll ask public comment is on RBC sensitivity. So, I want to -- let's keep to what we've said publicly, please. Just given the SEC --



## A - Axel Andre {BIO 19072099 <GO>}

Yeah. So, I think on RBC, I would simply say that we've -- as we've indicated in the past, we are essentially in capital preservation mode. So really, we're on any one day, you need to have us look at interest rates -- at equity sensitivities and putting on hedges to reduce, to minimize that sensitivity as much as possible on any one day. We may be more exposed to the up than to the down, but essentially we're attempting to stabilize that.

## A - Michael Wells {BIO 4211236 <GO>}

Okay. We've got just time -- Thanks, Ashik. Any last questions? I know we're coming up on the full hour here.

## Operator

The next question comes from Abid Hussain from Credit Suisse. Abid, please go ahead.

## Q - Abid Hussain {BIO 20229932 <GO>}

Hi. Morning [ph]. Thank you for taking my question. I think I've got three questions left. Firstly, just coming back to the capital construction -- on the debt leverage within the interaction between the US and UK. You said, you will take out around $2 billion of debt from the US. I mean you're looking to use those proceeds to retire debt, I think at the group. And I'm just wondering what is the right level of debt leverage that you are thinking at the group? I know there's a sort of separate conversation that's going with the rating agencies. But just in terms of group debt leverage, where are you sort of aiming for -- on that? And just sort of linked to that, can you just confirm that any debt raise you do with Jackson will count available capital? So that's just the first question.

And then the second question is on the RBC ratio. Just wondering why you feel 425% to 475% is the right level and how does that compare to peers? So what sort of metrics are you sort of thinking when you set that [ph] at that level?

And then the final question is on China. It's more of a broader question really. I was just wondering if you could perhaps talk through some of the growth initiatives in China and in particular, how China might reduce the reliance on Hong Kong?

## A - Michael Wells {BIO 4211236 <GO>}

Okay. Thanks, Abid. Mark, I'm going to have you handle the first one and Nic, I will have you some of the initiatives in China. I think on RBC, let me just make a general statement. And Michael, if you think it's that. So the range comes from a number of things. It's relative to market and what we see going on there. It's discussion with key stakeholders. So think of rating agencies and others that would opine on this and the financial strength in commercial rating of the entity. And it's a -- I think we've discussed.

So, you're into a new RBC regime, which Jackson adopted early. I've said before, I think it's personally a better regime than the old one. And I think it's more conservative than the old one. So, we think that creates a well-capitalized, still high return on equity business, still generating capital at again at very attractive returns and allows Jackson to operate as a standalone entity without the group. So, that was the lens at which we looked at what capital level we wanted for Jackson as a standalone listed entity.

Michael, did you want to add anything to that? Is that --

## A - Michael Falcon {BIO 17026942 <GO>}

Mike, I think you captured it right in terms of the mechanics and the direction and how the range was set and come to. I mean, our focus -- our principal focus is on economic and economic value creation, economic risk management. We obviously have accounting earnings and statutory capital that are really important measures and we need to focus on them as well. But there is a number of things that go into it, and the RBC is only -- is only one component.

## A - Michael Wells {BIO 4211236 <GO>}

Okay. So let's go to Mark, please, on debt US group leverage.

## A - Mark FitzPatrick {BIO 20178326 <GO>}

So in terms of debt, we are looking at and we plan on holding on to our current AA rating. We think we've got lots of headroom today. Ideally look to use some of the proceeds that come up to reduce the debtors, as I've said. That will be the essence of how we're looking to use that kind of the proceeds from the Jackson debtors as it comes up. So the AA rating for us, financial strength rating is an important piece. We've got that today and we plan on holding on to that. And as I've said, we've got plenty of scope for that. In terms of the debt raise for Jackson, (inaudible) is available capital? Yes, it does on that particular piece. And as regards to leverage target, I haven't commented or I haven't set necessarily a particular target. But I think it's fair to say that we will be aiming to make sure that in the medium, long term that we are comfortably within the leverage range that Moody set for that type of rating

## A - Michael Wells {BIO 4211236 <GO>}

Thank you, Mark. And Nic, do you want to give a little color on the growth that we're seeing in China and maybe a little bit on sequential as well, if you don't mind. Just giving a feel for a recovering market.

## A - Nicolaos Nicandrou {BIO 15589153 <GO>}

Okay. Thanks, Mike. But before I do that, let me just correct the point, it's not Hong Kong or China or Hong Kong or China instead of Hong Kong. Hong Kong will compound strongly. The needs are real. On the medical side, we see them now, on the retirement side and the savings. And the same is true in China, but on a much small -- a much bigger scale with $1.3 billion APE.

So a few comments on progress in China. And to Mike's point, China has been a highlight for us so far in 2020. Actually showcasing the power of our franchise, not only in that market but the potential everywhere else. Now the resilience in the depths of the crisis, if you like, at the start of the year and our recovery since is really underpinned by three things. The first is the broad geographic reach. We're in 20 provinces. So not all were affected in the same way at the same time. The second is the balanced channel strategy. With 36,000 agents and now 40 bank relationships, giving us access to 4,000 outlets.

And the third one is the diverse product strategy. So, we saw sales rebound strongly in the second quarter as restrictions were eased. We grew by 20%. Agency grew by 15% in the second quarter. Three drivers. The first was boosted by the recruitment that we did in the first part of the year. In the first four months, we upped our recruitment by 32% through January and April. The higher agency productivity that came from the use of virtual tools, 67% of our sales were virtual and a higher focus on H&P. H&P mix in agency increased from 40% to 60%, fulfilling demand that was kind of obviously there.

On the banker side, we built on the -- on the first quarter growth to deliver a 25% increase in the second quarter, as we made further inroads in not only the existing amount of new relationship. So that's what drove that. Looking at how we fared versus competitors, we had a better March through June than the rest of the market. And when we look at how we've done in each of our provinces, we grew market share in the first half of the year in 17 out of the 20 provinces.

NBP fared better, so to a minus 5 overall in APE, we were plus 4 NBP. Agency margins, because of the higher health and protection mix are now north of 80%. Just to give you a sense of how well our agency is now doing with increased productivity, more focus on H&P. In the banca channel, as I've said before, we managed that on an IRR basis given that it's selling mostly investment products and IRR stayed healthy in the 20s with a very short payback period.

So overall in China, our IRRs are 30% plus and payback period three years to four years. We are growing the platform. We're looking to enter our 21st province. We've expanded the number of cities by three. We've expanded the number of sales offices. So it's product initiatives, it's channeled initiatives, it's footprint initiatives and it's depth initiatives. And all these things has made for a very strong progression in all the financial and business indicators of that markets.

## A - Michael Wells {BIO 4211236 <GO>}

Great. Thanks, Nic. And, Abid, thanks for the question. Patrick, back to you.

## A - Patrick Bowes {BIO 16444249 <GO>}

Yeah. Thank you very much, everyone, on the call. For those who still got questions, you know how to get hold of us at Prudential. And we look forward to speaking to you in due course with the -- as we come forward with the next stages. Thank you very much, everyone, and good afternoon.

## Operator

This concludes today's call. Ladies and gentlemen, thank you for joining us. You may now disconnect.