Q2 2016 Earnings Call

Company Participants

- Anne Helen Richards
- Barry Lee Stowe
- Guy Robert Strapp
- Michael Andrew Wells
- Nicolaos Andreas Nicandrou
- Paul Chad Myers
- Raghu Hariharan
- Tony Wilkey

Other Participants

- Alan G. Devlin
- Andy Hughes
- Arjan van Veen
- Blair Stewart
- Jon M. Hocking
- Lance M. Burbidge
- Nick Holmes
- Oliver George Nigel Steel

MANAGEMENT DISCUSSION SECTION

Michael Andrew Wells {BIO 4211236 <GO>}

All right, everybody. If you don't mind, we'll go ahead and get started. Good morning. I'm Mike Wells, Nic and everybody in the room. We're going to follow the same format as the last presentation where you're going to have me go through some high-level comments, Nic do a very detailed drilldown on the financials. I'm going to come back up and give you some comments on outlook in general, and then we'll bring a variety of the senior management team up here to answer Q&A for you, and we have some other of our key associates in the audience as well, so we'll get to any level of detail you'd like in the conversation.

So that said, let's go ahead with delivery. I think we are commenting with our colleagues beforehand, it was an interesting first half of the year. I mean, no questions, lots of different challenges globally. I'm very pleased with our success in delivering both cash and growth. IFRS, up 6%. Free surplus generation, up 10%. The dividend, as you know, is mechanical but up 5%. Solvency ratio, 175%, which, again, as we've said – I think it's a good number. We've never considered it as a particularly good fit for us given about a quarter of our business or less is actually in the regional target of Solvency structure, and our local regulators use their own capital regimes.

But again, I think from a headline point of view, until this number matures in the industry, it's important we have a strong number, and we think that's a strong number. So we thought that was good, clear, results in a fairly tumultuous period.

And what I wanted to focus on in the opening today is what I think there are going to be three of your key questions. One is the resilience and the relevance of our growth, the second being the positioning for us in markets whether volatility of interest rates or equities and just competitively in general. And then, the third and final piece that comes up a lot is Brexit and its impact on the group or little impact on the group as the case may be. And then I'll get to more general comments on the business.

But I think what you saw in the first half on growth, the structural model we have, the strategic decision of going with the uninsured middle class that's still seeing two-thirds of our Asian clients not having owned a product before, that's detached from markets. So you don't have a high correlation between those transactions and their view on interest or equity, right. So that's turning out to be a very, very good piece of our business.

In the U.S. and the UK, more and more it is about our ability to gather assets effectively, perform well for the clients, right, and price and distribute effectively. Again, so those are slightly more opportunistic, but given the general demographics in those markets as you saw from the first half results, even in a climate like this, consumers are looking to derisk. They're more and more responsible for solutions. So again, it's giving us a very predictable and robust growth.

And then the last piece, which I'll get into a little more detail later, is we're continuing to invest for scale. One of the questions I think that's fair is that our continuing size, each year we get bigger and bigger and bigger. Can we continue to grow? And I'm not sure we spend enough time in all the things we're doing to invest for that growth, but we think we've got plenty going to continue to grow at the rates we've seen historically.

So moving to markets, again 16% of the business is now, the revenue is now coming from spread-based products. We moved away from these 10 years ago. With the start, it's taken time. This can be anything from de-emphasizing fixed in the U.S., moving away from bulks in the UK, and moving away from UL and (03:42) the Asian markets. There is an implication of top line. So, our competitor can hold up a graph now and say, aha, we have them beating this part of this market. I would ask you to consider when you see those sorts of comments, just prove out the ability to manufacture that product, and the answer is usually yes, and we probably already had it, systems-wise and capability-wise. And second, do we have the ability to distribute it, and the answer again I think is generally resounding yes.

So it's a conscious decision for us to participate, and in the case of interest sensitive products, not participate in markets because we have better uses of the capital. If they can or can't make money depends on the company, and in my role is not to tell you which of them can or can't make money, but I can tell you for us, we have higher uses of capital and I'll show you some of those returns as we see them in the lenses we're using now. But I want to challenge that thesis, if someone has it, that we can't capture that market share if we chose to.

If we gave the U.S. and the UK and Tony, the highest priced product in each market, we would be out of capital in about two hours of the distribution firepower we have, and we're clearly not going to do that. But I think that's a key element in this discussion. As we choose the growth we want, we choose the markets it's in, and we choose the value of those earnings over the volume.

The balance sheet itself, extremely defensive. We have not stretched for yield. We are not into aggressive asset classes. We've been talking for the last four years, if you will, about going up in asset class, managing duration carefully, up in quality, Nic will get you in some detail on this, but disproportionately, what we own is investment grade.

You'll see that in the shocks on spread and we don't think this is what our core business proposition is and nor do we think it is the right time in the cycle for taking tremendous investment risks. So we have an extremely conservative portfolio, an actively managed balance sheet. You saw that in the first half of the year, and I think, again, we'll let Nic get into some of the details there, but very pleased with the quality credit portfolio, quality of the hedging in the U.S. and quality of underlying assets on the balance sheet in the group. A proactive approach to value across the cycle.

An interesting thing we're talking before about Solvency II, so that's a pro-cyclical regime. We're arguably a countercyclical player. If you look at what we do best, certainly some of the results you see here, and that is a byproduct of our conservatism at different points in a cycle. So I think that's – these sorts of times, these stresses show what we can do, we certainly can do more than this. Again, I'll come back to that in the second half, but I think it shows the nature of the business on what we want to do.

But our intent at this size, we have a great growing stable earnings base. 90% of our IFRS earnings now come from existing clients, and if you think about those terms for stability, okay. So the incremental things we will do from here, we should be more countercyclical. You should expect that, we should get paid more for that, we should get better pricing. We should be able to create more unique solutions for consumers from that.

And finally on Brexit. Our UK participation has been selective. I think that's the key takeaway there, 10% of the M&G's team's assets roughly are in Europe. Poland if you remember is a rep office for our UK business. So we are not a European facing insurer by any means and we're certainly not the asset management business.

We will see what solutions come for those clients to be serviced effectively and transact effectively with M&G. It's a little early in that, but obviously M&G had contingency plans in place and continues to work those. We want to maintain a seamless relationship with those consumers, and it's clear as Brexit evolves, at least in my view, you will see clients as you did when we saw a real run up in our bond fund sales. They want to own pound denominated products, they want to – London is successful, continues as a financial center because the rule of law, currency, all the various things that have succeeded over a very long period of time. So we will make sure it's available to clients as they need in the jurisdictions they want to buy them, in the forms they want to buy them. But that's an evolving process as the rules evolve and we're fully capable of managing that. So the Brexit in general for us, minimal strategic and certainly minimal financial impact to the group.

Let's go to Asia. So where does the confidence come from in the growth? It's the quality of the growth. Again, I'm going to bring it back to the recurring premium versus single premium. The quality of it sold, the health and protection focus, and then absolutely critically, the pan-regional model. And I understand there's been a few questions about this. So let me go through a couple of these. So the long-term – and the blue shadow box on your far right of the screen shows, as it should, that the first half of the year regardless of what was going on, looks a lot like history of this business, okay. There's no material change in the shape of the business. A continued focus on health and protection, continued long-term focus on relationships with the clients as it should be, right.

Why does the pan-regional model matter? Well, 7 of the 11 markets were up double digits in terms of earnings, right. We can't predict which markets in a portfolio that big will have political turmoil, will have rate movement, we'll have other options, we'll have an irrational competitor. All those things are the nature of – including our Western markets, but certainly, our Asian markets. So the footprint we have gives us the ability to be disciplined. It allows us to back off on a product segment, a market, a country if we needed to, right, and to accelerate if we see the opportunity there being unique.

So I think you see that in this half's results. It was an interesting period of time, lots going on, pretty broad Asian results, and getting to the clients we want with the products we want, with the earnings we want, again value over volume because we have choices, right.

We're not defined by our limited licenses, limited distribution options, limited product or systems capability. And that's where I think you'll see us continue to succeed across a broad set of economic environments in Asia. We have tremendous optionality there and again it's an attribute scale. Should translate to earnings for you. It does.

Again, the earnings base, strongly driven by existing clients, not the new business profits and the sales, so new clients are an important, we want to keep adding cohorts of profitable clients to the business year-after-year-after-year, right, as we do in the U.S. business, as we do in the UK business, as we do in M&G, right.

That is the long-term stability of the earnings of the group, comes from that. But again, not a particularly unique shape in the first half of the year with the historic shape of the business and good year-over-year numbers in an interesting period of time. So very, very pleased with the execution of the team an extension of what they've been doing for a long time.

Reasonable expectation and that should turn into both growth and cash. So cash and free surplus generation, if you will, both up - excuse me - our earnings and free surplus generation both up 15%, good number. Again I mentioned, 7 of 11 countries in double-digit earnings including Indonesia, right, and markets where we're seeing irrational competition. We're accelerating other parts of the business, getting good earnings growth out of it and good profitability out of it.

So again, you see the breadth of the portfolio producing very, very good outcomes for our investors.

When time in the region, which you also see is the footprint allows us to recruit very talented people. Rinaldi, we brought a new CEO into Indonesia. He's an incredible add to the staff, people in the business units can move from one country to another as both their interest and ambitions and skills evolve. So it allows us to recruit talent. It allows regulators to look across the region and say, how do they behave for consumers, are they a good partner for the social solutions that we bring to the market? There's tremendous leverage in our footprint in a region, and it's not simply earnings based, right.

The learnings we have for one market we apply to another. I thought the most interesting one of these, personally it's not material in your models yet, will be someday, we're spending some time with the Cambodia team, right. You see our learnings from multiple markets in that effectively startup. I think it's important to firm our size can still do startups. You see us doing it in Africa, Laos, Cambodia, other markets, but what you also see is a very familiar business plan, some familiar faces, and very, very good execution very early on in the life of those business plans.

The other place you see it is on the bank relationships. As I mentioned to some of you before, you see the bank relationships are not linear. There's a learning curve. There's a relationship development phase. There is a product development phase and we're pretty good at accelerating that just given the share experience we have and Standard Chartered is still being the standout bank relationship with I think any insurer in that region. And the others we have are maturing nicely.

So what does this produce? Pretty consistent delivery. 2017 targets, the objectives we put out, double earnings still look in line and on target. And then, of course, if you back into that, that implies a tenfold increase in 11 years. So again these are strong growth rates.

Other subjective comment and, again, I know a number of you've been there. The businesses feel materially different than they did a year ago, three years ago, five years ago, ten years ago. I mean these are maturing - these are companies, these are portfolio of standalone companies run with similar sense of purpose, similar sense of value, similar risk managements. They're maturing very, very evenly and very effectively. And it's quite impressive to spend time with these teams.

Okay. Jumping to the West. Let's go to the U.S. So, the main event in the U.S., so we're talking about the last year's DOL. So you have the rules out, you have an April next year implementation. We said to you at the time, this was going to be a sales event, not an earnings event. As you see, VA earnings are up 9%. It's actually pretty much captured all of the net flows in the U.S. VA industry in the first half of the year. That's mostly going to the respective two products, their flagship products.

As you can imagine, Elite Access without a guarantee in this sort of climate is not as popular with clients as a product with the guarantee. So I think that's – and you're also still seeing some of the broker dealers looking at, if it should be on there, qualified plan platforms.

Jackson has put a number of products and processes in place for these distributors. Going into DOL, fee-based products based as it turns out the final interpretation of that is a little broader and a little better for the broker dealers. So most of them are looking that as a – they can, in fact, charge commissions. So we'll have a two-tier approach to this, a traditional product approach and a fee-based product approach. There's a part of the industry that believes that the rules will get better. That's upside. We're fine with the rules as they are. If they get better, we're more fine with that. And certainly, it could be a little clearer. But that said, we can function with them as written. And the value of the consumer, we'll see if that plays out over time, but we think we can build good product for consumers both on a fee-based structure, and we know we have good product for consumers in the traditional structure of our VA products.

We also, in the U.S., are continuing to look opportunistically at bolt-ons. And hopefully, at this point of the cycle, there is something we can do, but again, nothing to report at this time. I mentioned net flows are excellent. Hedges are holding up well. At this point, as the rules in DOL stabilize, Jackson should see more opportunity.

The UK is probably one of the most interesting stories, I think for us. So this I think defines our group's versatility at this point. So sales now in the life company post-RDR, post-pension reform, post-Solvency II, post-annuity review are now higher than they've ever been, right. Not surprising with profit product and its various forms is – the distribution team has done a great job of getting this in front of consumers who are now responsible for funding their own pension. I'm living here for – coming into my second year.

Lots and lots of conversations with people all around the city about what they're doing with their money, where they're putting in their ISS (17:28) things. And I'm shocked that a number of them that are cash candidly. Hope they look more at an investments, but a lot of the banks sold stuff seems to be cash centric, and we're getting a lot of it. And that's a great thing. So I think this is – this product provides good asset diversification, good smoothing for the client, it's a good long-term hold, really appropriate product for a long-term retirement savings. And the more volatility we see the more demand we see for the product.

So the team is shifted nicely to a capital light model as requested and as market driven. John continues to staff out his team. We'll show you more of that in November given a few folks aren't officially onboard with us yet, but I think you'll be pleased that the level of talent is brought to bear on that business. And again, this is a good example of our ability to pivot.

M&G, controlling cost, the earnings again at the guidance levels, I gave you at the full year. Clearly, there's been some challenges in outflows for U.S. equity managers in general - sorry, UK fund managers in general. But M&G continues to work on not only the current climate we're in as second half is better than first half, but also what they need to be the next 10 years.

And again, I'm going to ask your indulgence let Anne and the team, they've been working on it since January but we'll let Anne and the team, since she's joined, have a good portion of the November investor meeting and show you where they're going at that point in time. So obviously answer direct questions for you today on where they are at this point in time.

But again, very pleased with what they're doing, good combination. The two entities give us great capability in market.

We talked about this before and I think it's been a bit more important in this first half. Diversification by types of earnings, diversification by currency, right, diversification by the types of exposures we have and then of course the earnings and profits following that model. So we like the footprint, we continue to deemphasize spread. This gives us resilience, it gives us good cushion against some of the rate movement and we think positions the group extremely well for this climate.

So I'm going to stop there. Last comment, I guess, before I turn over to Nic. We think having watched what's been going on in the industry, these are good results both on a relative basis and on an absolute basis. I think you guys know my bias is to compare them to ourselves. I think they're consistent with what we've been able to do in the past as far as client acquisition, profitability, flexibility of the firm, its ability to adjust to challenges.

So, I'll come back up after Nic and I'll give you some comments on outlook. But I could ask Nic to come up, please.

Nicolaos Andreas Nicandrou {BIO 15589153 <GO>}

Okay. Thank you, Mike, and good morning, everyone. So, in my presentation, I will take you through the half year results, highlighting the key drivers of our performance in the period. And then I'll cover the group's capital position.

So, starting with the financial headlines, Prudential has delivered another strong performance across our main growth and cash measures despite the effect of lower rates and the expected reductions from U.S. spread, UK annuities and M&G retail, which I flagged to you back in March. Our progress in the face of these headwinds was achieved by making the most out of our structural advantages in the countries that we operate, and by executing with discipline and focus.

On a constant currency basis, IFRS operating profit increased by 6% to £2,059 million. New business profit was up 8% at £1,260 million, and free surplus generation was 10% higher at £1,609 million. Currency effects were positive, adding between three points and five points to our underlying performance. This performance is entirely driven by the outcome of commercial transactions and does not benefit from any changes to our reserve in Prudent (21:44). Furthermore, no aggressive actions were taken in any of our businesses to stimulate short-term sales as we continue to prioritize long-term value creation over volume.

These results demonstrate the benefit of our earnings diversity by geography, currency and source, and the power of our Asian platform, which continues to compound strongly, supported by largely uncorrelated structural drivers. Our ability to deliver growing levels of profit and cash also provides meaningful protection at times of extreme market volatility. Therefore, even though interest rates fell to unprecedented levels, our Solvency II capital at June 30 was trimmed back by only £0.6 billion at £9.1 billion. In contrast our embedded value, which is a fairer measure of economic value as it has no artificial restrictions and is not subject to excessive regulatory prudence, was up 9% in the first half to £13.56 per share.

The first-half performance takes us another step closer to the 2017 objectives. Our Asia IFRS operating profit and free surplus generation continued to compound nicely towards the 2017 target levels, demonstrating the ability of the PCA team to successfully execute against the secular opportunity in the region. The market cyclicality that we have experienced so far in 2016 confirms why targets for our other businesses are not sensible. Here the focus is on remaining disciplined and on balancing the trade-offs between risk, value and capital. Cash generation is the best way of measuring how effective we are at doing this, which is why we have a cumulative free surplus generation target. As you can see, we're also on track to deliver this goal.

The actions we have taken over the years to improve the quality of our earnings and to manage risk provide us with meaningful protection, as Mike has already said, against low rates. Therefore, before turning to the results, I would like to take a few minutes to remind you what underpins our resilience with the current market environment. So, starting with earnings on this slide, we have spoken many times of our strategic focus on insurance and fee income, as these sources are less sensitive to the interest rate cycle. In today's environment, this is a significant strength.

Compared to 2011, which was the last time that we saw a material drop in rates, we have more than doubled the size of insurance and fee income, and increased its share of the total to 76%. We can also draw more comfort now from the greater diversity in our earnings, with the amount of profit coming from our overseas markets being 2.3 times higher than in 2011, representing nearly 70% of the total. At the same time, our business growth has not detracted from our careful management of cost, which have grown at a slower rate than revenues. In most of our operations, our flexible and scalable platforms will continue to generate unit efficiencies, which will in turn help absorb the impact of natural business cyclicality.

Moving to capital, our ability to generate sizable Solvency II operational capital and a healthy start to the year position (25:25), have enabled us to absorb the effect of markets on this metric, and report a surplus of £9.1 billion at June 30. Our financial resources remain strong and provide ample buffers to absorb further downward moves from here.

By taking actions, we have also significantly reduced the sensitivity of our capital ratio. The sensitivity shown here reflect protection currently in place and incorporate the effect of action, which have already been taken or are within our control. More can be done if required.

As I have said before, given our predominant non-EU business footprint, Solvency II is an imperfect fit for Prudential. It, therefore, underplays the strength of the group as it excludes sources of real economic value such as the shareholder share of estate surplus of £0.4 billion. The further surplus in the ring-fenced UK With-Profit Funds of £3.1 billion. The unrealized gains on Jackson's interest rate swaps of £0.8 billion. The deduction of £1.6 billion of Asian surplus due to regulatory prudence, and the £2 billion of economic diversification benefits between Jackson and the rest of the group. If we were to incorporate all these items, then our Solvency would materially improve to a level that more closely reflects the true capital strength of the group.

We continue to manage our balance sheet cautiously. At June 30, the proportion of investment grade holdings in both our U.S. and UK credit portfolios was at 98%. These portfolios are well diversified and subject to strict concentration limit. We continue to prioritize quality of the yield, an approach that has been in place for many years and is consistent with our overall philosophy on risk. The fact that both portfolios are higher quality, more diversified and with smaller individual exposures, means that we are in a better position now than at any point in our recent history to weather credit events. The balance sheet exposure to product risk is also well managed. In variable annuities, we protect our downside risk with extensive hedges, which continue to perform well.

We have updated the charts that show the unhedged VA cash flows at June 30, and have included them in the appendix slide. These charts compare the net present values of future guarantee fees with the value of future policyholder benefit, which we then stretch under a down rate and a down equity scenario. The output which is summarized on the right, shows that the base position is unaffected by the fall in rates seen so far this year. The down rate scenario from here does not alter this picture. The down equity scenario produces an overall negative value, but again, this is not markedly different to the position at the start of the year.

In this scenario, of course, gains on existing hedges would turn the number into a positive. These cash flow projections confirm the ongoing health of Jackson's VA back book, in-the-moneyness has remained broadly unchanged in CRN (29:04) at around 9%. So in summary, our confidence in our ability to successfully navigate the current market environment reflects the fact that our earnings are high quality and resilient to market cycles. Our capital and economic financial resources remain healthy, and our approach to risk management continues to be robust. So, returning to our half year results, IFRS operating profit was up 6% to £2.059 billion, equivalent to an annualized return on equity of 24%.

I flagged in March that our 2016 earnings would be adversely impacted in the UK, reflecting our reduced appetite for annuities. In the U.S., from the impact of lower yields on spread margin and in M&G as a result of net outflows. These effects have come through as expected, reducing IFRS profit by a combined £112 million and will continue to be a feature in the second half. Our profit improvement in the period was predominantly led by Asia where earnings were 15% higher, reflecting increased income from insurance business, and by Jackson's fee business, which benefited from stable margins and growth in the large-base or variable annuity asset.

The half-year results also benefited from an extra contribution to profit of £74 million, reflecting the effect of actions taken to improve the UK Solvency, which I will come back to shortly. While there are a number of moving parts, this first-half picture highlights that our business has the scale, positioning and flexibility to successfully manage through the current cyclical challenges. I now want to turn to each business in turn. Asia has delivered another excellent set of results, improving all of its growth and cash measures by 15% or more. Our focus on quality delivered a 21% increase in regular premium new business, representing 94% of APE. The result was underpinned by another strong performance from agency where sales were up 22%, driven by improved productivity.

The strong growth in Hong Kong, Vietnam, Malaysia and China continues to afford us the flexibility to make strategic decisions on a country level. We strike the right balance between protecting our overall long-term economics and short-term sales headline. New business profit increased at a faster rate of 20%, boosted by favorable changes in country and product mix. The NBP improvement is supported by a 26% increase in the contribution from Health & Protection business, which accounts for two-thirds of Asia's NBP. IFRS operating profit and free surplus generation were both up 15% driven by ongoing growth in the scale of the business and the strong bias towards insurance. At a country level, as Mike have said, we have seen double-digit earnings growth in seven markets led by Hong Kong, Indonesia and Malaysia.

Eastspring increased asset managed. However, a shift in asset mix meant that revenues were broadly unchanged. Cost control improved margin by 2 points to deliver operating profit of £61 million, just ahead of last year. Finally, underlying cash remittances were higher at £258 million, tracking the growth of the book of business.

Now, as Mike said, all of the quality drivers which underpin Asia's momentum are intact, which bodes well for our future earnings prospect in the region. Our strategic preference for new regular premium business with a high protection content provides an in-force premium base that is both large and growing. Together with our focus on customer retention, this produces a higher liability base, up 22% compared to a year ago, which includes a sizeable insurance risk component. This forms a stable and highly valuable source of predictable income both in good times and bad, underpinning the positive performance outlook for our business in the region.

Jackson's results continue to reflect its disciplined value-based approach to managing the business. Sales in the first half were impacted by volatile markets and by the uncertainty, which surrounded the Department of Labor ruling. As a result, total VA sales were down 27%, broadly in line with observed market trend. Elite Access sales were similarly impacted, but were also affected by lower demand from qualified accounts. This product remains a leading investment on the VA in the market and drives the 28% nonliving benefit mix of our sales. New business profit fell due to lower sales and the decline in rates. Nevertheless, the overall margins remain very attractive.

Despite these cyclical headwinds, Jackson maintained its IFRS operating profit of £215 million levels. The contribution from fee business proved resilient but was offset by the anticipated effect of lower yields on spread business. Spread margin fell by 27 points to 217 basis points. And if rates remain at current levels, we expect this margin to now drift towards the 150 basis point level by 2020.

Jackson remitted another sizable dividend to the group at £339 million. This was lower than 2015 when capital formation was stronger, reflecting the more benign market condition at the time. Fee income on variable annuity business remains the dominant component of Jackson's earnings. This is driven by separate account asset values, which have continued to benefit from net inflows despite the reduction in gross sales in the period. Combined with a small gain from market movement, the separate account balance increased to £138.9 billion, having traded below the start-of-year value for most of the first quarter. As a result, fee income was flat compared to last year.

We have extended our analysis of Jackson's sources of earnings to now show the profit contribution for each product. These show that after deducting direct and allocated costs, profits from fee business increased by 9%, benefiting from lower strength. The increase also confirms what we have previously said that DOL is a gross sales, not an earnings event. At the time when asset yields are declining and consumers are becoming more self-reliant, our UK proposition in retail risk-managed products is becoming more popular. Retail sales were 51% higher with PruFund attracting the lion's share of these sales.

As a result of the onerous Solvency II capital requirement, we have stopped writing bulk annuity business. Indeed, in the current rate environment, the highest Solvency II trade has reduced the attractiveness of retail annuities, and we have taken steps starting in July to scale down our presence in this market. Our core with profits and in-force annuity business has delivered stable profits of £306 million in line with 2015. During the first half of the year, we took actions to support the solvency position of the UK. These actions delivered a £66 million profit from longevity reinsurance transactions and a £74 million profit reflecting the effect of repositioning the asset portfolio.

Our longevity reinsurance program now covers £10.7 billion of annuity liabilities, which is about a third of the book. While the value trade-off is appropriate in our minds, these actions will reduce further – will reduce future annual earnings by between £10 million and £15 million on top of the previous guidance of £25 million. Finally, in line with our normal practice, remittances from the UK in the first half reflected the 2015 reported transfer.

The effect of a market-wide retrenchment from equities in the first half combined with continued withdrawals from optimal income led to a £6.1 billion retail net outflows from M&G in the first half. I indicated in March that retail business accounted for two-thirds of M&G's total revenue. So, the 14% decline in retail AUM was the main driver of the 10% drop in fee income to £440 million. Actions on costs mitigated the overall impact on margin to deliver operating profit of £225 million, down 10%. Absent the meaningful recovery in net flows, the first half revenue trends will persist for the rest of the year, which together with the usual seasonality on cost, we'll see the cost/income ratio move to around 60% for the full year.

Moving on to cash generation. Free surplus after investment in the new business increased by 10% to £1,609 million. The life in-force result grew by 14% and was underpinned by the sizable expected return of £1,437 million augmented by positive experience of £374 million. The former was dampened by the effect of rates, whilst the latter benefited from UK management actions that I covered earlier. As you can see in the top right, Asia's in-force momentum provides important support to this metric and acts as a buffer to the cyclical impact elsewhere. New business strain is higher at £502 million. In Asia, strain has grown at a slower rate than sales due to changes in business mix.

The U.S. increase is also mix-related driven by higher (39:30) and lower Elite Access sales. It also reflects the higher proportion of new VA premiums directed to the fixed accounts, which was up 4 points to 22%. In both Asia and the U.S., the investment in new growth opportunity remains highly capital efficient with returns well in excess of 20% and short payback period. The new business strain in the UK for 2016 is on the more onerous Solvency II basis. The increase here is driven by retail annuities, which despite the modest sales levels consumed £69 million of free surplus, equivalent to 24% of single premium.

Mindful of the many moving parts this time around, this next slide provides you with some additional details on the movements of the free surplus generation between the two periods. And I'll leave you to (40:18) at you leisure, but I will draw out a few points.

As you move from left to right, you can see the negative £128 million interest rate effect on this metric, which mostly relates to Jackson, about £70 million relates to Jackson. You can also see the positive £138 million offset provided by the UK actions and the additional £147 million from our ongoing focus to grow and manage the business for value, which represents the underlying growth driver of free surplus.

You can also see the effect of Solvency II on UK free surplus generation. We're in line with our guidance. The expected return from in-force after amortizing the transitionals were £22 million higher in the top row and where our shift in focus to capital-light products contained the more onerous strain effects of this regime to only £31 million. The negative interest rate effect does not detract from our ability to continue to grow this measure. And as I said at the start, we'll remain on track to exceed the £10 billion cumulative free surplus target for 2017.

The next slide shows how the annual free surplus generation has impacted stock on the left and cash on the right. I would remind you that form this year, the UK insurance contribution to free surplus stock and flow is based on Solvency II. For the rest of the group, free surplus continues to be based on local measures as these remain the biting constraint.

Stock has increased overall, driven by the resilient operating performance. Market effects were more adverse this time, reflecting, for the most part, higher negatives in the UK given the more market sensitive nature of the new regime. After remittances, free surplus stock finished higher, as I mentioned. Central cash was also up at £2.5 billion.

Completing the overall earnings picture for the period, items outside the operating results have made an overall net positive contribution on EEV and have largely affect on (42:35) IFRS. In the IFRS table, the negative investment variance of £0.9 billion was primarily driven by the asset and liability accounting asymmetry in the U.S. This is further accentuated this year as Jackson opted to achieve economic protection against fold-in rates by increasing allocation to long-dated treasuries instead of buying more traditional instruments.

Unrealized gains on these treasuries are included within the £1.1 billion positive shown on the next line alongside the gains on other fixed income security. Otherwise, there was no change to Jackson's hedging approach, which remains economically effective. The net negative investment variance under EEV, which coincidentally is also £0.9 billion, mostly reflects the effect of the lower assumed future investment returns on VA's M&E fees, as under our methodology, these future returns are actively set.

Given the group's sizeable non-sterling assets, currency movements contributed positively in the first half under both reporting basis. The effect of adopting Solvency II trims £473 million off our UK life EEV, reflecting the extra cost of holding higher capital. The fact that both IFRS and EEV shareholders fund increased in the period by 13% and 9%, respectively, is testament to the consistency of our operational delivery and the natural offsets which exist across our business.

I'll summarize on this slide the movement in the Solvency II surplus during the first half of 2016. Our operating performance remains an important and reliable source of capital, contributing £1.2 billion of the surplus in the first half. Market effects were negative £2.4 billion. Around a third of this total relates to Asia, reflecting the highest Solvency II risk margin at lower rate.

Now, unlike UK and European domiciled businesses, transitional release is not available to us to cushion this effect. Just over a third of the market effect relates to Jackson, where the instruments we use to hedge against falls in rates are brought in at book value, which means that the sizeable gains of around £0.8 billion made this year have been excluded. And finally, about a quarter arises in the UK, where lower rates increased the annuity SCR and reduced the contribution from with-profit transfers.

At £0.9 billion, currency also provided a meaningful positive on the Solvency measure. As I have already mentioned, we took action in the course of the year to mitigate the adverse effect of lower rates and to improve the sensitivity of our surplus to further market shocks. These included longevity and other liability actions, asset switches, asset duration lengthening, and additional hedging within businesses in a group.

So, in summary, we remain comfortable with the overall capital level. We have the operational and financial growth to mitigate negative market effects, and we're better protected than six months ago against the shocks from here.

I have provided on this next slide, a capital update for our main businesses. The contribution of our Asia operations to the group's Solvency II surplus has been maintained at £5.1 billion, as operating capital generation and currency positives have offset the higher risk margin effect. However, it is the locally-driven free surplus of £1.8 billion that remains a relevant measure for cash and capital, which is extremely stable.

The U.S. local TAC (46:39) basis capital has been impacted by the falling rates. The permitted practice currently in place means that the offsetting gains on the hedge instruments that we use to protect against falls in rates are not brought into account. Here, unwinding the permitted practice, which is up for renewal next month, would recapture $1 billion of post-tax hedge gains and restore Jackson's capital to near start of year levels.

In the UK, shareholder Solvency II surplus of £2.9 billion has benefited from the actions that we have taken. With a ratio of 138%, Solvency remains within our target range. The UK with-profit Solvency surplus has improved to £3.5 billion, equivalent to a ratio of 176%.

I will conclude my presentation by reiterating two key points. The first is our belief that the most important source of capital is the consistent delivery of a growing level of high-quality earnings. This is precisely what we have achieved so far this year, delivering higher IFRS operating profit and improving operating free surplus and Solvency II capital generation.

The second point is the resilience that comes from having a large economically effective and well-diversified balance sheet, which is both secure and growing in scale. While we're not immune to the economic and market cycles, we are in a strong position to trade profitably through any environment.

And with this, I will hand you back to Mike.

Michael Andrew Wells {BIO 4211236 <GO>}

Thanks, Nic. Appreciate that. Just a little bit on outlook. We obviously feel pretty good about where the group is and its ability to capitalize on the market and what's going on in this next phase of the cycle, a couple of fundamental reasons; one being strategic. The behavior of the growing Asian middle class, the behavior of what someone referred to as the graying middle class in the western markets. As one getting gray hair, I took that slightly personally, but that's a – there is a consistency in their behavior which is this de-risking of their financial assets of various concerns and directly towards products and services that we provide.

So, the footprint we have, the capabilities we have, the services we have seemed to be fitting the major demographic trends. And the more volatility we're getting, the more investors foresee rates harder to live on or asset returns at lower levels and more concerning the more valuable our solutions consistently seem to be for clients across the globe.

There's been a lot of discussion in the industry about cutting and I want to address this very clearly. This has two issues for us. One, we manage expenses very tightly all the time, right? Can we get better? Always. Is that challenge to the team up here? Always. Right? But we're actually investing pretty heavily in this company.

And we do investing in sort of three levels. Things we do that improve the relationship we have with existing clients, be it service, technology, their access to other products we have, just anything that grows and develops that relationships, get them more likely to buy something to stay with us longer, again, to protect the long-term operating (50:31).

The second area is on scalability. We invest in things that we see improve our marginal costs, improve our capabilities, allow us to do things competitors can't do. That could be on risks, that can be on our asset management platforms, in the life businesses. It's a key element to it, because as we get bigger, we should produce a higher return for our shareholders and we should produce a better product for our consumers. And we're doing both of those, again, at scale in multiple countries.

And the last piece is things we do for innovation, for new opportunities, for new relationships, and that can be anything from a bank relationship to entering a new market in Africa or Asia to recruiting a portfolio team for one of the asset managers, be it Eastspring or M&G, all those sorts of things that take us into businesses that we didn't have or capabilities we didn't have quickly. M&A in the U.S. and bolt-ons, all those sorts of things are in that category.

And then when we look at what money we put behind - what capital is being deployed (51:40) behind the products, the lens is as it's always been, it's on cash payback, its IFRS centric. It's on the cash flow signatures. It's on the strain. It's on the interest rate sensitivity.

I want to be very clear. We can get more efficient as a group and we will continue to work on that. But our earnings growth isn't based on us coming up with a material reduction in what we already have in cutting our way profitability. It's based on growing from here. And again, I want to reiterate, we have more options for capital than we have capital. We could invest more, do more, grow more if we chose to. We understand the balance required with our shareholders on those metrics. So, what does that look like? How are you using that? What's the discipline of that?

Well, we know there's an expectation on the growth, as you do this investment to do it, from an ongoing basis, not one-offs, not - we're going to stop and do this for a while and then come back to profitability. We're trying to give you a very high rate of return of growth, trying to do that at very attractive returns. The bottom gray box is the return on embedded value.

I'm going to be defensive on the half year, because it bugs me, at 14% (52:50). 1% of that is interest rates and 1% of that, just to remind you, is front-end loading of expenses in our business model. So, it's a little stronger than it looks. But we think these are competitive returns in this market, given where our risk-free rates are and alternatives. And again, we think they give us - they demonstrate a bit of our scale and our ability to grow at scale.

The other thing I want to hit on just for a minute is a lot of questions in the meetings after full year results on dividend. Why do we think it's sustainable? Why is it a better dividend if we're not growing at a 5% plus the incremental as we did? Where's the confidence coming from that? Well, first off, it comes from the fact that, in our view, dividend should be aligned with earnings growth.

Post crisis, you've seen a lot of our competitors not grow earnings per share and grow dividend per share. And that is not what this management team is going to do, to be very clear. This is a long-term growth business growing earnings first and dividends second. And we're doing both as we're growing the value of the company. So, all three of those metrics are moving at pretty effective rates, but the other model, guys, I don't believe is sustainable.

If you're growing dividend faster than you're growing earnings, there's only a couple of ways that can end. You either have an awful a lot of capital to start with or you need an event later to recapitalize that. We don't believe either of those are necessary for us. We're growing earnings in a very strong predictable manner. And I come back to one of my favorite slides from Jackson days and certainly from this role.

Our earnings in the first half looked like they have for the last decade. This is how you should hold us up. We have the responsibility to deliver a few quarter-after-quarter, but the context of that should be against our own performance and the context of that should be how does that growth look, how does that profitability look, how does that cash generation look over the cycle. The relationships we have with consumers are decades long if we do them correctly. You should get the benefit of that as the shareholder.

So, I think this is one of the most effective ways to look at it. There's a lot of good slides in the deck, a lot of good slides in the appendix, but if I got one then this would be the one I'd use. He's smiling. I also like the cash flow testing in the U.S. That's my second favorite slide. But there's a – I do think this is a business where short-term things we can do can increase one of these lines, and that's not our objective; grow growth, grow value, grow dividend.

All right, so, let me just finish with a couple of final comments. So, all this is what we've been doing. All this is the team that's been doing it. All this is the markets we've been in, all the things that you knew before coming in. And again, I think the results in an absolute and a relative level are pretty good.

Is there upside? What else could happen? Well, given the Asian numbers and the pace at which they're doubling, any more normalcy in Asia is clearly upside for them. In the western markets, given our success at gathering assets and managing them, any improvement in market performance, any lighter version of DOL, if that in fact comes to play, is better. A broader capture of assets under that, more RIA assets coming to Jackson on that side, they're not factored into how we're looking at the business, but clearly part of its capabilities.

The improvements we're making to our UK businesses, scalability, capital-light, positioning them for where that market is going. We see upside there. And again, the general climate for consumers, the blend between the new expectations of what returns are and what expertise they need is driving them towards the things we're good at and the markets we're good at. So, this is a challenging time, we're not suggesting it's not, but we think we're very well positioned to succeed in, what for a lot of firms, seems to be a very difficult time and we're growing cash, growing earnings and growing dividend.

So, I'm going to stop there and then open up for questions. And if I could ask some of my colleagues to join us. And we've got a few more in the audience. This is the biggest stage we could find. So, we hand them a microphone if you need a specific question.

Raghu, I'll leave you to the honors of hosting this piece.

Q&A

A - Raghu Hariharan {BIO 15133573 <GO>}

We're just going to wait for the team to settle down. But before you ask a question, please do state the name of your firm and your name before firing away. Could I start with Jon there, please?

Q - Jon M. Hocking {BIO 2163183 <GO>}

Good afternoon, everybody. Jon Hocking from Morgan Stanley. I've got three questions, please; two on the U.S. and then one on the group capital sensitivities. So, first question on the U.S., just in terms of the (58:11) you've seen in the VA product in the first half, I appreciate we didn't get the rules DOL until sort of, I guess, beginning of the second quarter. And you're going to re-launch, I guess, in 3Q. How should we think about the sort of outlook for flows for the second half of the year? Because we don't really have a sort of normal run rate here and also we didn't get a Q1 update. That's the first question.

Second question, the GICs, I'm slightly surprised you're writing GICs again in size in the U.S. What are the sort of return on capital of that product? And is this just an expense play? Are you worried about the general accounts just depleting? The second question.

And then just finally, on the Solvency II rate stand sensitivities, just the £2.4 billion that Nic ran through, it sounded like a lot of that was rates and risk margin. But the rate sensitivity, you get the 50 bps down on the right hand side of that slide, looks reasonably small. Just wondered if you could sort of talk, Barry, how much of that is sort of assets versus liabilities and how much of it is sort of risk margin related? Thank you.

A - Raghu Hariharan {BIO 15133573 <GO>}

So, Barry, do you want to take the two U.S. comments, and Nic, the Solvency II?

A - Barry Lee Stowe {BIO 15021253 <GO>}

Yeah. Sure. So, the slowdown, it's correct that we did not actually get the rule change until April, but it was highly anticipated. And because there was uncertainty around grandfathering, and when we ultimately ended up with an element of grandfathering which is helpful, it's not full grandfathering, but because there was uncertainty around grandfathering, the slowdown in production of new business actually started much earlier back in the second half of 2015. So, that's the reason for the flows. In terms of the GIC, we feel it was opportunistic. It's just something we do periodically. Chad, you want to talk about the specific details or...

A - Paul Chad Myers {BIO 2234559 <GO>}

Sure. So, (01:00:06) returns, generally speaking, we target about 12% un-levered on those types of products. So, I think that's, generally speaking, what we saw. Keep in mind that this used to be a material portion of our overall balance sheet. The ability to actually earn a spread has not been there for a while because financial paper has been relatively pricy post-crisis, and that's finally started to go away. So, we're actually seeing good opportunity now to lever off of our AA rating and actually build and invest well against that during a good spread.

Q - Jon M. Hocking {BIO 2163183 <GO>}

Okay. Now, just coming back on the GIC question, on the GICs, because historically, I think, you said that you sort of reinvest to make it sort of greater than 20% IRR across new business. Is that 12% unlevered return? Is that a return on capital rather IRR metric? Was it - the two aren't same number.

A - Paul Chad Myers {BIO 2234559 <GO>}

Return on capital, on AA statutory capital.

A - Raghu Hariharan {BIO 15133573 <GO>}

So Nic, your comments on Solvency.

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

Sure. There are other advantages. But, as you say, maintaining a stable general account level has a lot of benefits across the business. Certainly helps with liquidity as well. So, we take everything into consideration.

Okay. On the sensitivity, look, we - you have to appreciate that Solvency II is only very new. The sensitivities we gave you reflected the balance sheet that we had at the time. The balance sheet was not optimized at that time to withstand those sensitivities. We have taken both liability and assets side actions. I've referenced one of the liability actions in relation to the longevity, which we started doing that in any event in the course of last year.

On the asset side, there's a key thing here that across our UK business, but also across certainly some of the Asian countries, which contribute to the overall Solvency II surplus. We match our assets for the best estimate flows. We don't match the assets for the one in 200 cash flows. So, when interest rates fall as they did immediately in the aftermath of January 1 and then again, you have a mismatch effectively that comes from having shorter assets than the liabilities on the SCR.

So, what we've done in the course of the year as we look to optimize the position as I said both in the UK and elsewhere, we traded a lot of our excess assets, if you like, and increased the duration. So where did we do that? We did that with some of the excess assets that we have backing our excess capital in the UK, so we switched £2 billion of extended the duration by something like 15 years.

Opportunistically, there was another £2.8 billion that we did elsewhere in the group across the piece, which also gives us economic protection for that. Other area is the matching adjustment was quite efficient. We entered the year with 95% efficiency at the end of - so there was some ineligible assets.

Now, you get to the law of diminishing returns, but we effectively sold £400 million of ineligible asset, which gave us some further protection against that. We did some general asset trading within the matching adjustment constraint to improve, if you like, the risk and liability, the risk versus yield position. There was another £1.2 billion of that. And of course, we did some more equity hedging, as I said, elsewhere in the group.

So, there's a whole host of actions that in effect by June 30 have shifted our matching to not just be on the (01:04:05) liabilities plus. Not all the way to the one in 200 cash flows. We don't think that's sensible, but enough to bring the sensitivities down.

A - Raghu Hariharan {BIO 15133573 <GO>}

Andy?

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. Andy Hughes from Macquarie. First question, 24% strain of the single premium for individual annuities?

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

Yeah.

Q - Andy Hughes {BIO 15036395 <GO>}

But that's presuming the bulk annuities, it would be even bigger and presumably - and I know you're outsourcing some of the annuity team to Mumbai, I suggest you probably outsource them to (01:04:41) instead. That's a huge trend. Is there something too specific about that? Is the expenses the right number or is that...

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

No, there's no expense, Andy. The people that we're transferring is to administer the sizeable back book. So, it's what the numbers show. It is what the numbers show. That 17%

or so is SCR, the rest is risk margin. The 18% to 20% depending on where you were – where the interest rates were in the quarter, the rest is risk margin. We dialed up prices as we entered the year. So you come to a point where you run against the constraint or value for money from a customer perspective.

So, we've moved the pricing as much as we can without giving ourselves problems with the FCA. Of course, it's without the benefit of any reinsurance. The numbers that we've given you are without that. But even if we rerun the numbers, if you assume you reinsure 80% of that and you – at a 4% or so fee which is a typical fee for these type of reinsurance, you save a little on the strain, you remove the risk margin component, but it still leaves you in the teens, right?

And you save some capital, but you give away enough of the returns. It gives you a small IRR pick up, but it's still at or just above the cost of capital, which is why we said we will – we have taken action to withdraw. We wrote around £27 million of APEs, £270 million of single premium, about a quarter of that comes from open market sales and sales with partnerships. We announced in June that we're stopping selling to the open market and we've given notice to our partners effective on July that we will not take any annuity.

About half of it comes from the with-profit fund, people vesting was effectively – which was reinsured under the shareholder account. We stopped doing that again on July 1, and that leaves us with the guaranteed annuity which we're trying to find a solution for. So, it is onerous and that's why we stopped bulk, and this is why, in this interest rate environment, you'll see us pull back on retail annuity as well.

Q - Andy Hughes {BIO 15036395 <GO>}

Okay. And my second question was about U.S. VAs. Mike, I know you personally love dollar-for-dollar withdrawals and GMIB. And I see so many competitors had lots of problems in those products. So, is that going to impact the competitive landscape for second half of the year? Are you going to see products on the GMIB side being pulled? And also on lapse rates, obviously, MetLife brought forward the investigation of (01:07:17), so if lapse rates in your U.S. business come down, it looks like that's probably positive based on your cash flow disclosures. So, if DOL drops lapse rates, is that positive? Thanks.

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

Yeah. I think on – just a general comment and you got a number of experts here in the room on it. So, lapse rates – one U.S. competitor wrote off (01:07:33) £2.1 billion, added £1 billion, so there's an element of – we look at our assumptions at year end. We don't have – I'm glad we don't have the GMIB exposures, the structures you're talking about. For a lot of years, we stood up here and said that was a wrong product. Wouldn't waste that problem on anybody, but some firms have it.

I think the thing that's – the bigger issue in the market was DOL. The firms need – so you go from a regulatory standard historically that was suitability of product. Are you selling a product suitable for the client? That would be a good reason for a sell. That's a clearly good reason for a buy that had all to be justified in the U.S. market, pretty prudent model.

It's been up now to what's basically the same as the reasons (01:08:25) the best product. It's a difficult business, you're signing off, but this is basically the right product, much more specific, much more liability. If you're wrong, it's got a different recourse to it.

We think the quality of the VA product that the advisers sell gets even more important. So, the performance matters, the flexibility matters. One of the other topics that Andy didn't bring up that we didn't like was the bulk control, and this has been around – I'll leave you to your own homework or go back and look at those funds versus the funds we have for our consumers. Just never been a fan of that model. And again, if you're paying for that and paying for a guarantee, it's always been a question on our mind.

So, I think Jackson's got a very good product set of where the market is going. And I think the – just knowing what some of the broker dealers think, if they see that, you're likely to see more concentrations at broker dealers because there's more technical support, more IT support to go on these RIA platforms and things. So, it's a good question for you in your travels for the heads of the broker dealers, which products are they willing invest in to have on their platforms, and I think quality will be a major cut. I think we're in good shape on that.

A - Raghu Hariharan {BIO 15133573 <GO>}

Let's go to Lance, please.

Q - Lance M. Burbidge {BIO 3978332 <GO>}

Good morning. It's Lance Burbidge from Autonomous. I've got a couple of questions on Jackson as well. So, in terms of launching of the fee-based version of the product, I wondered, Barry, if you could talk about, presumably, this is attractive for a sales person to sell because they get a recurring fee which is higher than their commission if the product lasts long enough. But how does that play with the consumers that presumably would be worth of, which is not what DOL was trying to do in the first place?

And going back to something sort of Mike has talked about in the past, which is as interest rates fall, is there a point where this product from a guarantee perspective becomes unattractive from either your perspective or from the customer's perspective? So, maybe you can talk about that as well. And then just on the sensitivity for Solvency II, you like other companies don't put negative rates into your sensitivity. I just wondered, Nic, if you've looked at what that does or if there's nothing in there.

A - Barry Lee Stowe {BIO 15021253 <GO>}

The fee-based product will be introduced. The Perspective II

version would be introduced in September. What it really does, I think, as much as anything else is it does – it gives an alternative to the broker, to the advisor that it does not want to deal with (01:11:21) whatever people call it. It doesn't want to deal with the regulatory complexity of operating under that. So, it gives him an alternative that I think from a compliance perspective is a little easier.

For a sale that's made that has long duration, there is the prospect that the agent gets paid more. The customer – typically, what companies like ours do in order to fund, if you will, the upfront commissions is you build about 100 basis points in for distribution. So, if you accept that the standard fee is going to be about 100 basis points, the customer is really not going to see a material difference, because we talked before this session, there is the prospect that as you move towards more fee-based than it's, let's say, 100 basis points gets locked in, it's the typical fee level that, over time, there'd be pressure on that to get it pushed down to 75 basis points or 50 basis points, and that could certainly happen.

But I don't think that it's going to disadvantage the consumer in any way, but what it is going to do is give a choice to the financial advisor, which is really important. In talking with broker dealers and talking with the wirehouses, what we're hearing, overwhelmingly, is that they will operate under the (01:12:49). They accept that, they've gotten their heads around that. Some of them view it as a long-term proposition; others view it as a bridge. And maybe within three years to five years, they plan to have transitioned completely off of commission-based sales and be totally on fee-based.

So, there's no doubt that there's going to be an evolution around distribution in the industry. And that, in fact, is what I think regulators are trying to get at, because we spend a lot of time also talking to political leaders, regulatory leaders, people within Department of Labor, SEC, and what comes through overwhelmingly is they think the product is complicated for consumers. The reality of the industry has complicated it. It's really not a terribly complicated product for a consumer to understand, but we need to change the way we talk about it and use different simpler language, which the regulators, they welcome that.

But they love the product itself. They love the idea of a product that provides upside that only equity markets are going to be able to get for the foreseeable future combined with some levels, some modest level, but some level of guaranteed income for life around which someone approaching retirement or entering retirement and plan. So they really like the product. So, there's cause for real optimism for organizations who have a track record of being flexible, adaptable and sort of get on the cutting edge of things, and that's where I think Jackson is. Did I answer your question?

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

(01:14:27). I think on the interest rate piece, we've got a couple of issues. We have the ability to adjust guarantees down, as you have seen us do. The systems have the flexibility to do that. And then the accounting point of view, IFRS has sort of a market (01:14:42) consistent element in the drift rate. The discount rate is defined by the current rate and the discount – the drift rate of the equity assumed performance is defined by rate. So, you can get quite a ways – the accounting, as rates get lower, gets quite a ways from what's a reasonable economic set of assumptions. So, that's one of the challenges and that's the discussion as a management team and with you guys as our investors, how we view that.

But, at the lower levels, the drift rate assumptions feel kind of ridiculous that a portfolio with every asset class available basically on the globe can't produce 100 basis point return sort of thing is a bit of a – over 20 years is a bit of a stretch. If you actually believe that, you probably would offer a different product. So, that's where I think you'll see the noise. But, again, we're looking at it. And we do have the flexibility if we believe the fact that the true economics of lowering the guarantees and we have done that on the withdrawal rates.

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

Okay. Can I, Mike? Can I answer the question on the flows? So, you're referring to our internal model which flows interest rates pull shocks at zero.

Q - Lance M. Burbidge {BIO 3978332 <GO>}

Oh, I'm sorry. I forgot to...

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

Yeah. That's okay. So, when you – so, we start – just to be clear, so, we start with the swap curves in the various markets that we operate. We then apply the one-in-200 shock. In all cases, that stays above zero. And then we apply the 50 basis points in there.

The only place where that drops to below zero is in year one in Singapore. And our cash flows in Asia are pretty much across the piece. The others are 10 years plus out, so immaterial impact. The other place where it drops to below zero is in the UK between years not – today in year five, that's in the minus 50. Our cash flows in the UK are even longer. So, they go out 20 years plus. So, that in fact is immaterial.

A - Raghu Hariharan {BIO 15133573 <GO>}

Arjan?

Q - Arjan van Veen {BIO 5197778 <GO>}

Thank you. Arjan van Veen, UBS. Two questions, if I may, first one on Solvency II capital movements. So, firstly, thank you for your detailed disclosure on page 76 on the movements there. The £1 billion of underlying organic capital generation represents about 10% of your opening SCR, which annualize at 20% which is the top end of your peer range. It's also relatively stable compared to the £2 billion in 2015. So, just looking for a comment on can we use that as a starting point to build forward there's nothing sort of untoward in that number?

Second question is on Asia in two parts. Firstly, on Hong Kong, so obviously the strong growth has continued there. And there's obviously concern around both sustainability of growth and also some regulatory tail risk. So, Tony, if you can give us some comments around the growth side and also and particularly on the tail risk, the initiatives from the Hong Kong regulator, which I think will help manage out of it.

On the non-Hong Kong side, we saw obviously some negative growth in this half. That's partly driven - you've obviously a strong switch towards regular premium, there's some management initiatives in Indonesia, you stopped selling universal life in Singapore. So I'm just curious, all these different actions, where do you think - or are we close to - and obviously, underlying economic growth headwinds there? Are we seeing some light in terms of where you see that stabilizing and then picking up again, given all that different moving part?

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

Well, Nic, do you want to take the Solvency II piece, and Tony the...

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

Thank you, and I think your analysis is correct. I mean clearly, there are some management actions in there, the benefit which you've accounted for them. Look, we have a business that generates capital. When you consider that effectively the U.S. comes in on a local basis and you've seen a very strong capital formation from the U.S. that we've reported year-after-year as the business has grown. There's no reason to believe that its contribution to that number is going to do anything other than what it's done in the past plus (01:18:52)

Of course, the UK is under Solvency II and we gave you the Solvency II risk monetization profiles at the year-end. On an underlying level, you saw £300 million or so come through, it's £600 million for the year, okay, we have to trim a little off that.

But as we withdraw from - what works against that is the new business strength which will eliminate as we go into the second half and beyond. And of course, we have a positive experience that contribute. So, no, we're confident in the same way as we are against all the metrics, but we ask you to judge us again, we're confident that we can continue to have a positive slope.

A - Tony Wilkey {BIO 19184129 <GO>}

Asia. Yeah. Hong Kong growth continues strong up 58% at the half. Again continued driven by Mainland Chinese and correlated quite well in with the growth in the agency force, which I think is now close to 16,000. In the first half, in Hong Kong, we've recruited about 700 to 800 new agents every month. And so that feed into nicely.

In terms of the actions from regulators like - and there's a lot of activity in the first half, I think the most interesting ones are declaration put out by the China regulator CIRC, I think towards the end of Q1, early Q2. That they actually put out I guess to the Chinese citizens on their websites that was state. And if you're going to buy product in Hong Kong, these are a couple of things you need to be aware of.

I view this as good news. Honestly, in part codification of the process that it's okay for the business that continue under certain controls. And we did as we've always done. We immediately took those CIRC statements and put them in an additional disclosure at point of sale that the agents and customers have to sign.

Now, what the Hong Kong regulator, OCI has done is taking those standards and created the formal form, disclosure form that effective September 1, all Mainland customers purchasing in Hong Kong will have to execute. So, based on everything we've seen, so far, not materially concerned about the impact, and again and as usual, we're ahead of the curve in terms of implementing those standards.

In terms of the rest of Asia, I think you might have answered the question. Yeah, there have been some economic headwinds, probably most notably in Indonesia where GDP has struggled for an extended period of time. And that, for us – I think we talked about this in the past, that has flown through into on the call phase, the consumer sentiment index which has been depressive. And remember, in Indonesia, we sell to the middle market, the mass market, not the mass affluent. So, household disposable income, a little bit more sensitive than it might be in some of the upper segments which is typically the people who are actually buying product to bancassurance, not agency.

So, yeah, we have felt some impacts. But we continue to grow the business. I mean, if you look at the – even though the comparable is not great, if you look at the business, we averaged about IDR 370 billion per month of new businesses in the first half. That's £21 million of new business. Margins staying in line, and almost £200 million of IFRS profit coming through. We also added on average 7,000 new agents every month in the first half, and I think we acquired 160,000 plus new customers. So, 800 new customers a day, and we're a little disappointed that that's not per hour, but we'll get there.

Probably the most – if you look at the leading indicators or drivers for direction, Q2 over Q1 grew by 11%. That's great news. If you look at Q2 over Q1 last year, it was flat. And the growth coming through APE per active. So, agents were actually starting to have a lot more success at point of sales. So I think if one add on the final macro of Jokowi's new cabinet especially with his new Minister of Finance, I think we feel pretty good about maybe the economies -you probably know the economy in Indo better than I do, but it feels like it might have bottomed out. Currency is stable, JCI is up 20% year-to-date, looks a little bit better. As the economy recovers, our business will recover.

A - Raghu Hariharan {BIO 15133573 <GO>}

So, Oliver, please.

Q - Oliver George Nigel Steel {BIO 6068696 <GO>}

Oliver Steel, Deutsche Bank. Three questions. First, I'm going to refer (1:24:03) back to the U.S. Are you able to give us a some sort of indication of how much sales from qualifying accounts actually fell in the first half and ramification (01:24:13) what happened on the non-qualifying accounts? And how you see particularly on the qualifying accounts, how that will develop over the next one, two, three years, if you can?

Secondly, the flows both with M&G and Eastspring were a bit low my expectations. So, Eastspring, can you tell us what's happening there because they were remarkably good this year, but they weren't too good – they were remarkably good last year, but lesser than the first half M&G, perhaps an update on particular funds and how much is left in each of these.

And then third question, perhaps a bit left field, is you talked about raising the dividend in line with earnings. But obviously, your earnings are benefiting quite a lot from sterling currency weakness, and your dividend is paid in sterling. So how are you thinking about sterling relative to your dividend decision?

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

Okay. So, Barry, do you want to comment on the qualified accounts first?

A - Barry Lee Stowe {BIO 15021253 <GO>}

What is the exact – I know Elite Access, you only talked to the sale side I think, Oliver. The Elite Access sales from qualified accounts have dropped to essentially zero almost. I mean they've fallen precipitously because, as Mike alluded to I think earlier or maybe Nic in the presentation. Most of the broker dealers are now not allowing advisers to sell EA in the qualified because they feel like the fee in return for the advantage that you get from the tax wrapper which, obviously, you don't get with the qualified, I mean it's not a new advantage. So that's been hit very hard. Overall sales, do we have that number at our fingertips? How much qualified is down versus non-qual?

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

We don't have the number at our fingertips in terms of percentage down, but what I would say is that the mix is about the same as it was last year. So you're looking at roughly 65%ish percent is qualified. But, in the EA...

A - Barry Lee Stowe {BIO 15021253 <GO>}

In the non-EA. So, EA has been hit very hard. In terms of how we expect it to develop, broadly, we think that if recovery's afoot, it's not like it's going to come roaring back in the third quarter or the fourth quarter. I think it's a gradual thing over a series of quarters to return to the historic levels of flows across the industry. But I do think that there is, based on some of the comments I made earlier about the way regulators actually are embracing, the product concept and just want to look at distribution, I think as we're successful in evolving distribution, I think there's a strong prospect that we'll see growth in flows, there need to be.

When you look at the number of baby boomers that are retiring, the assets that are going to be looking for a home, the fact that interest rates oriented, our parents and grandparents retired on CDs, which were paying 10% and 12% interest, but that's not an option. So there's really – there are a few alternatives for people other than going into equities. And the prospect of a guarantee with the equity upside just, I think, is becoming increasingly appealing. So, don't look for instantaneous change in sales levels, but over time, I think there's real cause for optimism.

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

Oliver, if you think of it, the problem we're solving for the consumer, it doesn't materially change with the new product structure. You're going to have some assets already in qualified plans rolling over. You're going to have supplemental savings for retirements. So they may go see, they may go commission, but the fundamental problem we're solving is the same regardless of DOL. I wouldn't just if I was guessing, I wouldn't think you'll see a material shift in qualified and non-qualified mix in the U.S.

The exception that might be in a fee-based Elite Access, you get into a different - no, even with that you're not going to - I'm just thinking all that. No, it should be the same problem you're solving with effectively the same tools, just different optionality and other (1:28:19) structure, but I think we get the same outcome.

Let's go - we just happened to have the CEO of Eastspring right here. Guy, you want comment on flows?

A - Guy Robert Strapp {BIO 15272859 <GO>}

So, if we just wind back slightly, second half of last year flows started to slow after China intervened in both currency and stock market. So, sentiment in Asia started to shift after a very strong 2014 and for us, very strong first half 2015. You translate it into 2016 and investor appetite for equity product has evaporated largely. Its money market, pockets of high yield. All countries that we look - all 10 countries that we run money in Asia except two, who had positive flows for the first half. So it was confined to Japan where we saw outflow mainly through dividend distributions in Asia equity income product. And a very short duration product which is almost money market quasi product in China, which management decided to close down with the two recent - with the only two funds that we're in outflow in the first half. So, 8 out of 10 countries is positive flow.

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

Anne on M&G, please?

A - Anne Helen Richards {BIO 4145347 <GO>}

Yeah. So I think there's a couple of things to comment on. Two main reasons, I think, what flows have been under pressure over the last 18 months or so. First was very obviously related to performance and I think the second bigger driver was around Brexit, uncertainty on Brexit ahead of that. So, maybe touching on performance. Some challenges over the past 18 months or so. But if you look back over the last six months, over 60% of funds in the retail range and now above median. So there's a bit of work to do to repair some of the slightly longer-term relative performance, but you can see the direction of travel is right.

And in particular, Optimal Income, which is the single biggest funds there. There, we're now seeing, against the European sector, which is the most important sector for that fund to the European share class there. We're now first quartile year-to-date one year and five years, again, to really rebuild that record. And over three years, again, we're second quartile.

So direction of travel is very much right in the right direction there. And if you look at the broader context of flows, actually, what is quite encouraging is to see that we have got net inflows across quite a few different strategies, both on the retail side and importantly on the institutional side as well. And quite a range of different things. Real estates, some of the private debt markets and so forth, global macro, multi-assets.

So there's a lot of work to do to turn net outflows into net inflows but we have some of the building blocks already in place there. I think the Brexit vote, obviously has relevance in particular to the £25 billion or so of asset under management that we manage for Continental European clients. And I think we still don't have perfect foresight in terms of how that's likely to progress going forward.

So, that's the area of where we're looking at focusing really on client service as we wait to hopefully get a little bit more unraveling and visibility on the extent to which, for example, we'll still have European passporting (1:31:45) as the Brexit negotiations would underline. But in the rounds, that's the picture on that.

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

And Nic, do you want to comment on dividend effects...

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

On dividend. Yes. Is it a factor? Yes, it's a factor. Is it more important when we stress test the dividend to the impact on shocks? No. Is it more important than when we weigh up the growth opportunities? No. And we take (01:32:12)

Now, that being said, we have always maintained that currency and the part of the world that we're exposed to is a tailwind for this business. At the end of the day, over the medium to longer term currency should follow growth in GDP and if you're operating in countries where GDP is growing faster than the currency in which you're reporting. Then over time, that will come through into additional earning. So, day-in, day-out, it's a fact that's not that significant, longer term, I think it's rightly a tailwind for us.

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

Oliver, we've historically hedged dividend payments, not hedged earnings, but – so there is some – we tried to dampen some of that a bit.

A - Raghu Hariharan {BIO 15133573 <GO>}

We've Blair.

Q - Blair Stewart {BIO 4191309 <GO>}

Thank you very much. It's Blair Stewart from BoA Merrill. Three questions, please. Nic, you talked about the implemented practice in the U.S., I just wonder if you can expand on that? Is that something you're looking to explore? And then could you give us what the RBC in the U.S. actually was? I don't think if that's a route to getting more capital or more cash out of the U.S. It wouldn't be a results presentation without me complaining about cash coming out of the U.S.

And second question on Indonesia, I noticed the profit growth has slowed to 12% growth. Is that simply a function to any of investing in the business during a period of a time where sales are coming down, I suspect it is.

And thirdly, on back to management actions, Nic, I was wondering what more can be done especially to capture some of that surpluses disallowed (1:33:58) I don't think particularly on the With-Profit (01:34:00) if there is anything smaller that could be done there? Thank you.

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

Nic, (01:34:07).

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

I mean, maybe I'll say one or two things and then I'll pass onto Chad. I mean, it was – permit to practice is something that we carried, put in place after the last Financial Crisis at the time. If you like the balance of the book, it was more on the general account where interest rates up was a predominant risk. The balance of the book is gradually shifting and clearly given where interest rates are. The point at which it becomes the permit to practice is a benefit to us, is further away. That being said, we've had strong capital formation, even with this in place over the years. But it's something that we're looking at. Chad, would you add anything to that?

A - Paul Chad Myers {BIO 2234559 <GO>}

Yeah. I think it's – the bulk of the answer is right there. So, with the permit to practice, we view that as something where interest rates are low enough, and we're deep enough with the money, if you will, that there's pretty good to offset up and down with reserves now. So, there's logical reason why you might take the permit to practice off, and that'll be part of the conversation we'll have with the state. The thing would be it's still – the reason we've had it on to begin with is, were you to have rates move up significantly, then there's going to be an asymmetry between the mark on the swap book and the reserves because the reserves will pour out under STAT (01:35:27).

So, there's still that kind of tail risk, if you will, if you had a big inflationary environment or something like that where rates started moving back up rapidly, we'd have a disconnect. I think it would be harder for us to get that back on, having taken it off. But we wouldn't do so lightly but it's certainly an active discussion just given the fact what we're seeing now kind of one-sided market against us even though that economic edge is in place.

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

The other thing I'd add, Blair, is you see the – the use more of treasuries as part of the hedging strategy, because it's more efficient plus volatile, plus they're also under STAT (01:36:03) graded book. So you're getting quite an understatement of the financial strength of Jackson. We haven't ever given RBC other than when we published year-end, but it's still a very acceptable range for us.

Q - Blair Stewart {BIO 4191309 <GO>}

Okay. So, the 12% growth in Indonesia?

A - Tony Wilkey {BIO 19184129 <GO>}

Yeah. I mean, Blair, you're absolutely right. We have been investing in the business. We've learned, and Mike often talks about countercyclical opportunities. We've continued to invest. We've expanded new branches. We've hired more agents. We've upgraded our people. And we've invested quite heavily in technology to make the whole process more efficient on the back end in the front end. So, obviously, that has some impact. I don't know Nic, if you want to expand on it any further?

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

Sorry. On the With-Profit side – sorry on the – yeah, we are extremely frustrated that I can't include the With-Profit that stayed into the ratio, not least because it seems we are the only business now that has a sizable amount. Nevertheless, we've had that debate. The rules have been interpreted in the way in which they've been interpreted, and we exclude it. How can we access it? We could distribute it, but that wouldn't be what we wanted to do. It's the thing that is underpinning, providing the working capital and the risk coverage to invest in the way that we do in the With-Profit Fund, which is now attracting the phenomenal flows that we're getting. We could – there's things you can do from this point, but to get more credit up front, you could monetize the shift, you could hedge the shift further, but you're giving up the upside that we would do if we needed to within reason. But on the With-Profit side, it's difficult to bring more credit through onto the ratio.

A - Raghu Hariharan {BIO 15133573 <GO>}

Nick here, please.

Q - Nick Holmes {BIO 21515144 <GO>}

Thank you very much. Nick Holmes of Soc Gen. Couple of questions on the variable annuity book again. Just wanted to follow up on the policyholder behavior assumptions. Wondered if you could – I know this is an incredibly difficult take area. But I wonder if you could try to give us a sense of your level of confidence about your assumptions, not just lapse but also guarantee utilization. Perhaps, looking backwards, what did the last review tell you and what were you pleased about, what are you worried about?

And then the second question is I've noticed that there was a very large unrealized loss below the operating line. Now, this, we all know, is a familiar feature of insurance accounting, but I think in your case, quite a lot of it is to do with the hedge program. And I just wondered kind of what is your thinking about communicating the performance of the hedging of your variable annuities? Are you at all inclined to start reporting an economic type of – I know that's subjective in itself, but there is one very large European company that does this and it puts it in its operating earnings. Now, is this something that you would be interested in doing in the future because my sense is that it would be very helpful for people to understand the true performance of the variable annuity guarantees and hedging. Thank you.

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

So, Nick, I'll take - start with both and I'll (01:39:48) to U.S. colleagues for help maybe. On the hedging, I think there's two elements. If you remember the New York meeting, a number of you were out and we sort of gave you 11.5 hours of everything you want to know about Jackson. One of the things that we did there was showed you some of the internal work we do on cash flow testing. Because of the industry's varying descriptions of metrics, the choices management teams have to define hedging, define risks. Part of the reason on those, we've always looked at, and if you remember, unhedged. And then, we can tell you what the hedge looks like and that shock in terms of value at a given point in time. But we're not getting in a debate of what type of hedge and how is it structured, and is that better than Met's or PRU's or Lincoln's, et cetera?

We intend to keep - at the various investments, we'll keep showing you those sorts of measures. I think personally, that's the single best way to look at a VA block and how it's going to perform. And if you remember back at that meeting, one of the things we said is, it is not just the PV, which, again, that's one of the - that's the easy one for us to summarize for you, but it's also how does a given year shock looked versus your capital (01:41:00) for cash at the end of the day.

So, those stresses are important and our intention is to keep showing you that. I think that gives you a better look at our hedging than anything else - our non-hedged liabilities. There was a question that came out in one of the meetings about like net amount at risk versus in the money. Net amount of risk is a shock event. That's not how our liabilities are structured. It's sort of everybody goes at once sort of model. (01:41:28) it's an incredibly inefficient way of looking at our liabilities. It may fit a life company with pure mortality (01:41:34) concentrated in one region. You start to get to say, is that viable. But for us, with the fact that the guarantees plays out over decades, shocking it to one day can't even structurally occur. They all can't collect.

So, that's kind of particularly good metric. So, I do think the cash flow metrics assuming very efficient utilization is the best way to say, do you like to look at what's there? The actual value the hedges we can mark-to-market any given day, you see some of that below, some of the (01:42:04) this time was interest rate as well, just the severity of the rate movement in the U.S.

And your other question on policyholder review, there's multiple levels in the U.S. on policyholder review. There's an ongoing intellectual challenge quarterly, that is a team that gets together and say, look for any inefficiency, look for any behavior that's changed, look for anything that would suggest that our models are wrong, look for new combinations. Anybody in that committee can bring up any combination of variables they want to be run and tested, and it's quite detailed. And then we have our formal processes that we follow as all U.S. carriers do to review our assumption setting, and we typically do those in the second half of the year.

The challenge you guys have - and I appreciate these as investors - is you have firms in the U.S. that have different structures of liabilities and a VA. They have different assumptions. There's a lot of assumptions to your earlier point inside our policyholder behavior. It's not just one number. And so, when you look at that, you got to say, do you agree with all the things you're seeing in the marketplace? We've got this discussion with external consultants (01:43:17) for Jackson is marketplace data that's GMIB-based or they've gone back and raised the fees or they've gone back and put force allocation or (01:43:25) control on versus our clients.

It is directionally of some value, but we wouldn't build pricing based on it. So, there's - I appreciate the - it's beyond - it's not just opaque, it's a confusing space that - but I think Jackson, you'll see us disclose sensitivities, what are we - we've shown before what we think of lapse rates, what we think of - what our stresses look like in the financial implications and we'll continue to give you those.

A - Barry Lee Stowe {BIO 15021253 <GO>}

Mike, can I comment on the reporting as well? Look, I'm aware of what other companies do in this regard. And we thought long and hard, look, you know our position on accounting disclosure. We thought long and hard about how we best project that. But you hit on two of the key points. The first challenge you run into is what is economic. Is it real world or is it market-consistent? And there can be different judgments that are applied in that regard or something in between.

Then you hit the other challenge which is to say that you then depart from U.S. GAAP. And bringing the entire guarantee seizes the calculation of the way you think of the reserves or the element that you brought in on day one which is when you lock them in that produces zero profit on day one. The more you depart - we took the view that the more you depart and make judgments from the base U.S. accounting, the less comparable your numbers are with the way that everyone else does it. And in the end, we decided that it's better to take that volatility and be more comparable and answer your question rather than make judgments that put us out of kilter with the way the rest of the industry is reporting.

So, yes, we will - so, what would you leave then? Refer you back to the cash flow on the one side and the other thing is the embedded value because ultimately that does capture all the fees. And that's factored in the way you move forward how your hedging program will react. And there are stochastic elements that are run within that to capture some of the variability of some of the assumption. So, no, we look at it, but we just thought if we moved, it would be just too artificial.

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

One other valid point that might be interesting for you, too, is around the policyholder behavior and the validity of the assumptions. And as Mike has said, we're constantly going through the process of reviewing, and we occasionally tweak as a result of that analysis. But historically, our assumptions have held very, very well. And I would argue that, given that we have provided, Mike alluded to this as well, probably the most stable consumer experience amidst any one at the industry around these products, and given the scale of our book, I would say the historical data that we produce on our book is probably the most credible data available in the industry.

A - Raghu Hariharan {BIO 15133573 <GO>}

Now, go, Alan, please?

Q - Alan G. Devlin {BIO 5936254 <GO>}

Thanks. Alan Devlin from Barclays. Just one question. You mentioned the bolt-on deals. I think, you referenced to the U.S. I was wondering if you could give some color and what kind of things you were considering? Was the Department of Labor forcing you to (01:46:42) potentially out of the market? Thanks.

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

No. The Department of Labor doesn't have anything to do, for us, with bolt-ons. We wouldn't buy - we're not looking for VA blocks, for example. We've been pretty clear that that's not something we have an appetite for. What we look for is life. So, life (01:46:59) technical revenue, further diversification, just get a nice (01:47:04) benefits. There's a lot of things we get.

The last 24 months you've had some interesting new players in the market, private equity, some of the Japanese firms and things that bid things up. Typically, what you see is, on this point, just like a little more rational pricing. But you've got some new players. We've got some pension funds, multiple Canadian pension funds and vehicles now. It's actually a very good liability for pension fund. You think about it, the cash flow signature of their lives look a lot like the cash flow signature of the underlying life (01:47:34) premiums.

So, there's competition still, but we're looking - we continue to look - for all the years I've stood up here, we're always looking. Oh, yeah, and that was my old role as well. But if we see something we like, we would do it and we're not in it. There's no obligation or capital allocated specifically to that. We'll just - it'll be opportunistic as it's always been. But you do own a very low cost platform in the U.S. They can integrate those and produce some return in addition to their return the existing owner is getting. So, there's value there.

A - Raghu Hariharan {BIO 15133573 <GO>}

And then one last one? Andy?

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

Andy.

Q - Andy Hughes {BIO 15036395 <GO>}

All right. Thanks so much. I've got a couple more questions. I think, Nic, will be disappointed if I didn't ask (01:48:13) Indonesia just to double check the persistency and lapses are okay because that would be my main concern. And I can see there's not much easy hit from lapses in the numbers, so obviously just double check that. And the second point, on Asia, obviously you're sticking with your growth targets. But obviously Indonesia adds a lot more to the IFRS earnings in the net than Hong Kong. So, is that kind of the mix can be a bit of the headwind in terms of growth going forward?

The third question is on VAs and regulatory change, so you actually hinted that you're holding back of some cash for potential changes in the U.S. VA rules, which may or may not happen. Obviously, they have a big captive and you don't. But they were sounding like – do you expect any VA rules to come more economic, which might lead to higher capital requirements? Can you comment on that? Thanks.

A - Barry Lee Stowe {BIO 15021253 <GO>}

Lapses, if you like, you can see the numbers come through. The persistency pretty much across actually the portfolio on the protection side is strong. From time to time, you will some spikes, if equity markets aren't performing. You see some offshore withdrawals, maybe people taking money out. But we see nothing different this time around to what we've seen before.

On the impact of Indonesia on the growth rates, I think the answer is that the strength of the platform, don't under estimate the growth in Hong Kong. Yes, a lot of it comes from the success with profits offering there, the (01:49:46). But the growth within that of health and protection, which as you know, has a very attractive IFRS signature is not to be underestimated, and which is – we're building some nice momentum in Hong Kong on the back of layering, if you like, more protection business to what was previously there. Hong Kong was underweight in our earnings before and it's now gradually drifting up to its appropriate weight. So, yeah, there's some (01:50:15).

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

(01:50:18) regulatory question, Andy, there's – I mean, there's always a prospect that regulations evolve over time. But we have always had and continue to enjoy a very positive and productive relationship with Jackson's lead regulator which is the State of Michigan. And I mean, there are literally weekly, multiple weekly meetings between Jackson and the state. And I think they are comfortable, A, with the existing regulatory regime under which Jackson operates, and even more so, happy with the manner in which we've complied with that regime. And so, I don't think – I don't see a huge risk such as you've described.

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

I just want to thank everybody for a very long session. I appreciate the time and the questions. And we'll maybe up for a few minutes if anybody want to do one-on-one. Thank you.

Operator

If you've missed any part of this call or would like to hear it again, replay will be available shortly. Thank you for joining today's call.