PRUDENTIAL PLC
Form 20-F
April 16, 2013

As filed with the Securities and Exchange Commission on 16 April 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OR (G) OF THE SECURITIES EXCHANGE ACT OF 1934
OR

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended 31 December 2012

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number: 1-15040

PRUDENTIAL PUBLIC LIMITED COMPANY

(Exact Name of Registrant as Specified in its Charter)

England and Wales
(Jurisdiction of Incorporation)

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London EC4R 9AQ, England
(Address of Principal Executive Offices)

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Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
American Depositary Shares, each representing 2 Ordinary Shares, 5 pence par value each	New York Stock Exchange

Ordinary Shares, 5 pence par value each	New York Stock Exchange*
6.75% Perpetual Subordinated Capital Securities Exchangeable at the Issuer's Option into Non-Cumulative Dollar Denominated Preference Shares	New York Stock Exchange
6.50% Perpetual Subordinated Capital Securities Exchangeable at the Issuer's Option into Non-Cumulative Dollar Denominated Preference Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

The number of outstanding shares of each of the issuer's classes of capital or common stock as of 31 December 2012 was:

2,557,242,352 Ordinary Shares, 5 pence par value each

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes X No ____

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes ____ No X

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes X No ____

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web sites, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ____ No ____

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer X Accelerated filer ____ Non-accelerated filer ____

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP ___ International Financial Reporting Standards as issued by the International Accounting Standards Board X Other ___

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 ____ Item 18 ____

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ____ No _X_

*

Not for trading, but only in connection with the registration of American Depositary Shares.

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As used in this document, unless the context otherwise requires, the terms 'Prudential', the 'Group', 'we', 'us' and 'our' each refer to Prudential plc, together with its subsidiaries, while the terms 'Prudential plc', the 'Company' or the 'parent company' each refer to 'Prudential plc'.

In the UK, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) replaced the Financial Services Authority (FSA) on 1 April 2013. The new regulatory environment in the UK is explained in Item 4 Supervision and Regulation. References made in this document to the FSA incorporate references to the PRA and FCA as appropriate.

Limitations on Enforcement of US Laws against Prudential, its Management and Others

Prudential is an English public limited company. Most of its directors and executive officers are resident outside the United States, and a substantial portion of its assets and the assets of such persons are located outside the United States. As a result, it may be difficult for you to effect service of process within the United States upon these persons or to enforce against them or Prudential in US courts judgments obtained in US courts predicated upon the civil liability provisions of the federal securities laws of the United States. We believe that there may be doubt as to the enforceability in England and Wales, in original actions or in actions for enforcement of judgments of US courts, of liabilities predicated solely upon the federal securities laws of the United States.

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Item 3. Key Information

SELECTED HISTORICAL FINANCIAL INFORMATION OF PRUDENTIAL

The following table sets forth selected consolidated financial data for Prudential for the periods indicated. Certain data is derived from Prudential's audited consolidated financial statements prepared in accordance with International Financial Reporting Standards ('IFRS') as issued by the International Accounting Standards Board ('IASB') and as endorsed by the European Union ('EU'). EU-endorsed IFRS may differ from IFRS as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. As at 31 December 2012, there were no unendorsed standards effective for the years presented below affecting the consolidated financial information of Prudential and there were no differences between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to Prudential. Accordingly, the selected consolidated financial data presented below that is derived from Prudential's audited consolidated financial statements is derived from audited consolidated financial statements prepared in accordance with IFRS as issued by the IASB. This table is only a summary and should be read in conjunction with Prudential's consolidated financial statements and the related notes included elsewhere in this document, together with Item 5, 'Operating and Financial Review and Prospects'.

Income statement data

Year Ended 31 December	**2012**	**2012**	**2011**	**2010**	**2009**	**2008**
	$m(1)	**£m(1)**	**£m(3)**	**£m(3)**	**£m(3)**	**£m(3)**
Gross premium earned	**48,640**	**29,910**	25,706	24,568	20,299	18,993
Outward reinsurance premiums	**(823)**	**(506)**	(429)	(357)	(323)	(204)
Earned premiums, net of reinsurance	**47,817**	**29,404**	25,277	24,211	19,976	18,789
Investment return	**39,112**	**24,051**	9,360	21,769	26,889	(30,202)
Other income	**3,287**	**2,021**	1,869	1,666	1,234	1,146
Total revenue, net of reinsurance	**90,215**	**55,476**	36,506	47,646	48,099	(10,267)
Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance	**(74,729)**	**(45,953)**	(29,289)	(40,518)	(41,195)	10,824
Acquisition costs and other expenditure	**(9,847)**	**(6,055)**	(5,120)	(4,989)	(4,756)	(2,457)
Finance costs: interest on core structural borrowings of shareholder financed operations	**(455)**	**(280)**	(286)	(257)	(209)	(172)
Loss on sale of Taiwan agency business					(559)	
Total charges, net of reinsurance	**(85,031)**	**(52,288)**	(34,695)	(45,764)	(46,719)	8,195
Profit (loss) before tax (*being tax attributable to shareholders' and policyholders' returns*)(2)	**5,184**	**3,188**	1,811	1,882	1,380	(2,072)
Tax credit (charge) attributable to policyholders' returns	**(615)**	**(378)**	17	(611)	(818)	1,624
Profit (loss) before tax attributable to shareholders	**4,570**	**2,810**	1,828	1,271	562	(448)
Tax (charge) credit attributable to shareholders' returns	**(997)**	**(613)**	(409)	40	10	58
Profit (loss) from continuing operations after tax	**3,573**	**2,197**	1,419	1,311	572	(390)
Discontinued operations (net of tax)					(14)	

Profit (loss) for the year	**3,573**	**2,197**	1,419	1,311	558	(390)

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	2012	2012	2011	2010	2009	2008
	(In $m, Except Share Information)(1)	(In £m, Except Share Information)(1)				
Statement of financial position						
Total assets	**504,533**	**310,253**	272,745	260,040	227,103	214,858
Total policyholder liabilities and unallocated surplus of with-profits funds	**441,291**	**271,363**	236,290	224,980	196,417	182,391
Core structural borrowings of shareholder financed operations	**5,780**	**3,554**	3,611	3,676	3,394	2,958
Total liabilities	**487,679**	**299,889**	264,138	252,475	221,230	210,193
Total equity	**16,854**	**10,364**	8,607	7,565	5,873	4,665
Other data						
Based on profit (loss) for the year attributable to the equity holders of the Company:						
Basic earnings per share (in pence)	**140.7¢**	**86.5p**	55.8p	51.8p	22.3p	(16.0)p
Diluted earnings per share (in pence)	**140.5¢**	**86.4p**	55.7p	51.7p	22.2p	(16.0)p
Dividend per share declared and paid in reporting period (in pence)(6)	**41.70¢**	**25.64p**	25.19p	20.17p	19.20p	18.29p
Equivalent cents per share(7)		**40.68¢**	40.39¢	30.15¢	30.62¢	35.36¢
Market price per share at end of period(9)	**1407.5¢**	**865.5p**	638.5p	668.0p	640.0p	416.5p
Weighted average number of shares (in millions)		**2,541**	2,533	2,524	2,501	2,472
New business:						
Single premium sales(5)(8)	**36,359**	**22,358**	18,889	18,177	14,438	15,071
New regular premium sales(4)(5)(8)	**3,186**	**1,959**	1,792	1,667	1,401	1,330
Gross investment product contributions(5)	**157,678**	**96,961**	89,707	106,969	96,057	63,147
Funds under management(5)	**658,611**	**405,000**	351,000	340,000	290,000	249,000

(1) Amounts stated in US dollars in the 2012 US dollar column have been translated from pounds sterling at the rate of $1.6262 per £1.00 (the noon buying rate in New York City on 31 December 2012).

(2) This measure is the formal profit (loss) before tax measure under IFRS but is not the result attributable to shareholders. See 'Presentation of results before tax' in note A3 to Prudential's consolidated financial statements in Item 18 for further explanation.

(3) The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2008-2011 comparative results have been adjusted from those previously published for the retrospective application of the change as if the

new accounting policy had always applied, as described in note A5 to Prudential's consolidated financial statements in Item 18.

(4)

New regular premium sales are reported on an annualised basis, which represents a full year of instalments in respect of regular premiums irrespective of the actual payments made during the year.

(5)

The new business premiums in the table shown above are provided as an indicative volume measure of transactions undertaken in the reporting period that have the potential to generate profits for shareholders. The amounts shown are not, and are not intended to be, reflective of premium income recorded in the IFRS income statement. Internal vesting business is classified as new business where the contracts include an open market option.

The details shown above for new business include contributions for contracts that are classified under IFRS 4 'Insurance Contracts' as not containing significant insurance risk. These products are described as investment contracts or other financial instruments under IFRS. Contracts included in this category are primarily certain unit-linked and similar contracts written in UK insurance operations and Guaranteed Investment Contracts and similar funding agreements written in US operations.

Investment products included in the table for funds under management above are unit trust, mutual funds and similar types of retail fund management arrangements. These are unrelated to insurance products that are classified as 'investment contracts' under IFRS 4, as described in the preceding paragraph, although similar IFRS recognition and measurement principles apply to the acquisition costs and fees attaching to this type of business.

(6)

Under IFRS, dividends declared after the balance sheet date in respect of the prior reporting period are treated as a non-adjusting event. The appropriation reflected in the statement of changes in equity, therefore, includes the final dividend in respect of the prior year. Parent company dividends relating to the reporting period were an interim dividend of 8.40p per share in 2012 (2011: 7.95p, 2010: 6.61p) and a final dividend of 20.79p per share in 2012 (2011: 17.24p, 2010: 17.24p).

(7)

The dividends have been translated into US dollars at the noon buying rate on the date each payment was made.

(8)

The new business premiums shown, for the 2008-2010 comparative figures, exclude the new business premiums from the Group's Japanese insurance subsidiary, which ceased selling new business with effect from 15 February 2010. Japan's new business premiums for the year ended 31 December 2010 are shown in Item 4 'Asian Business'.

(9)

Market prices presented are the closing prices of the shares on the London Stock Exchange on the last day of trading for each indicated period.

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Dividend Data

Under UK company law, Prudential may pay dividends only if 'distributable profits' of the holding company are available for that purpose. 'Distributable profits' are accumulated, realised profits not previously distributed or capitalised less accumulated, realised losses not previously written off, on the applicable GAAP basis. Even if distributable profits are available, under UK law Prudential may pay dividends only if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves (such as, for example, the share premium account) and the payment of the dividend does not reduce the amount of its net assets to less than that aggregate. For further information about the holding company refer to Schedule II. The financial information in Schedule II has been prepared under UK GAAP reflecting the legal basis of preparation of the Company's separate financial statements as distinct from the IFRS basis that applies to the Company's consolidated financial statements.

As a holding company, Prudential is dependent upon dividends and interest from its subsidiaries to pay cash dividends. Many of its insurance subsidiaries are subject to regulations that restrict the amount of dividends that they can pay to Prudential. These restrictions are discussed in more detail in Item 4, 'Information on the Company Supervision and Regulation of Prudential UK Supervision and Regulation Regulation of Insurance Business Distribution of Profits and With-profits Business' and Item 4, ' Information on the Company Supervision and Regulation of Prudential US Supervision and Regulation General'.

Historically, Prudential has declared an interim and a final dividend for each year (with the final dividend being paid in the year following the year to which it relates). Subject to the restrictions referred to above, Prudential's directors have the discretion to determine whether to pay a dividend and the amount of any such dividend but must take into account the Company's financial position.

The following table shows certain information regarding the dividends per share that Prudential declared for the periods indicated in pence sterling and converted into US dollars at the noon buying rate in effect on each payment date. Interim dividends for a specific year now generally have a record date in August and a payment date in September of that year, and final dividends now generally have a record date in the following March/April and a payment date in the following May.

Year	Interim Dividend (pence)	Interim Dividend (US Dollars)	Final/Second Interim* Dividend (pence)	Final/Second Interim* Dividend (US Dollars)
2008	5.99	0.1112	12.91	0.2052
2009	6.29	0.1011	13.56	0.1976
2010	6.61	0.1039	17.24	0.2818
2011	7.95	0.1221	17.24	0.2706
2012	8.40	0.1362	20.79	

*

The dividend of 13.56 pence for 2009 was paid as a second interim dividend. All other dividends shown in this column of the table are final dividends.

The Board has decided to rebase the full year dividend upwards by 4 pence, reflecting the strong progress made in both the earnings and free surplus[(1)] generation of the business and in the delivery of its financial objectives. In line with this, the directors recommend a final dividend of 20.79 pence per share (2011: 17.24 pence), which brings the total dividend for the year to 29.19 pence (2011: 25.19 pence), representing an increase of 15.9 per cent over 2011.

(1)

Group free surplus at the end of the period comprises free surplus for the insurance businesses, representing the excess of the net worth over the required capital included in the EEV results, and IFRS net assets for the asset management businesses excluding goodwill. The free surplus generated during the period comprises the movement in this balance excluding foreign exchange, capital movements, and other reserve movements. Specifically, it includes amounts maturing from the in-force operations during the period less the investment in new business, the effect of market movements and other one-off items.

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The Board will maintain its focus on delivering a growing dividend from this new higher base, which will continue to be determined after taking into account the Group's financial flexibility and their assessment of opportunities to generate attractive returns by investing in specific areas of the business. The Board believes that in the medium term a dividend cover of around two times is appropriate.

Exchange Rate Information

Prudential publishes its consolidated financial statements in pounds sterling. References in this document to 'US dollars', 'US$', '$' or '¢' are to US currency, references to 'pounds sterling', '£', 'pounds', 'pence' or 'p' are to UK currency (there are 100 pence to each pound) and references to 'euro' or '€' are to the single currency adopted by the participating members of the European Union. The following table sets forth for each year the average of the noon buying rates on the last business day of each month of that year, as certified for customs purposes by the Federal Reserve Bank of New York, for pounds sterling expressed in US dollars per pound sterling for each of the five most recent fiscal years. Prudential has not used these rates to prepare its consolidated financial statements.

Year ended 31 December	Average rate
2008	1.84
2009	1.62
2010	1.54
2011	1.61
2012	1.59

The following table sets forth the high and low noon buying rates for pounds sterling expressed in US dollars per pound sterling for each of the previous six months:

	High	Low
October 2012	1.62	1.59
November 2012	1.61	1.58
December 2012	1.63	1.60
January 2013	1.63	1.57
February 2013	1.58	1.51
March 2013	1.52	1.49

On 12 April 2013 the latest practicable date prior to this filing, the noon buying rate was £1.00 = $1.54.

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RISK FACTORS

A number of factors (risk factors) affect Prudential's operating results and financial condition and, accordingly, the trading price of its shares. The risk factors mentioned below should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. The information given is as of the date of this document, is not updated, and any forward-looking statements are made subject to the reservations specified below under 'Forward-Looking Statements'.

Risks relating to Prudential's business

Prudential's businesses are inherently subject to market fluctuations and general economic conditions

Prudential's businesses are inherently subject to market fluctuations and general economic conditions. Uncertainty or negative trends in international economic and investment climates could adversely affect Prudential's business and profitability. Since 2008 Prudential has had to operate against a challenging background of periods of significant volatility in global capital and equity markets, interest rates and liquidity, and widespread economic uncertainty. Government interest rates have also fallen to historic lows in the US and UK and some Asian countries in which Prudential operates. These factors have, at times during this period, had a material adverse effect on Prudential's business and profitability.

In the future, the adverse effects of such factors would be felt principally through the following items:

- investment impairments or reduced investment returns, which could impair Prudential's ability to write significant volumes of new business and would have a negative impact on its assets under management and profit;

- higher credit defaults and wider credit and liquidity spreads resulting in realised and unrealised credit losses;

- Prudential in the normal course of business enters into a variety of transactions with counterparties, including derivative transactions. Failure of any of these counterparties to discharge their obligations, or where adequate collateral is not in place, could have an adverse impact on Prudential's results; and

- estimates of the value of financial instruments being difficult because in certain illiquid or closed markets, determining the value at which financial instruments can be realised is highly subjective. Processes to ascertain value and estimates of value require substantial elements of judgment, assumptions and estimates (which may change over time). Increased illiquidity also adds to uncertainty over the accessibility of financial resources and may reduce capital resources as valuations decline.

Global financial markets have experienced, and continue to experience, significant uncertainty brought on, in particular, by concerns over European and US sovereign debt, as well as concerns about a general slowing of global demand reflecting an increasing lack of confidence among consumers, companies and governments. Upheavals in the financial markets may affect general levels of economic activity, employment and customer behaviour. For example, insurers may experience an elevated incidence of claims, lapses, or surrenders of policies, and some policyholders may choose to defer or stop paying insurance premiums. The demand for insurance products may also be adversely affected. If sustained, this environment is likely to have a negative impact on the insurance sector over time and may consequently have a negative impact on Prudential's business and profitability. New challenges related to market fluctuations and general economic conditions may continue to emerge.

For some non-unit-linked investment products, in particular those written in some of the Group's Asian operations, it may not be possible to hold assets which will provide cash flows to match exactly

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those relating to policyholder liabilities. This is particularly true in those countries where bond markets are not developed and in certain markets where regulated surrender values are set with reference to the interest rate environment prevailing at the time of policy issue. This results in a mismatch due to the duration and uncertainty of the liability cash flows and the lack of sufficient assets of a suitable duration. While this residual asset/liability mismatch risk can be managed, it cannot be eliminated. Where interest rates in these markets remain lower than interest rates used to calculate surrender values over a sustained period, this could have an adverse impact on Prudential's reported profit.

In the US, fluctuations in prevailing interest rates can affect results from Jackson National Life Insurance Company (Jackson) which has a significant spread-based business, with the majority of its assets invested in fixed income securities. In particular, fixed annuities and stable value products written by Jackson expose Prudential to the risk that changes in interest rates, which are not fully reflected in the interest rates credited to customers, will reduce spread. The spread is the difference between the rate of return Jackson is able to earn on the assets backing the policyholders' liabilities and the amounts that are credited to policyholders in the form of benefit increases, subject to minimum crediting rates.

Declines in spread from these products or other spread businesses that Jackson conducts could have a material impact on its businesses or results of operations. Jackson also writes a significant amount of variable annuities that offer capital or income protection guarantees. There could be market circumstances where the derivatives that it enters into to hedge its market risks may not fully offset its losses, and any cost of the guarantees that remain unhedged will also affect Prudential's results.

A significant part of the profit from Prudential's UK insurance operations is related to bonuses for policyholders declared on with-profits products, which are broadly based on historical and current rates of return on equity, real estate and fixed income securities, as well as Prudential's expectations of future investment returns. This profit could be lower in a sustained low interest rate environment.

Prudential is subject to the risk of potential sovereign debt credit deterioration owing to the amounts of sovereign debt obligations held in its investment portfolio

Prudential is subject to the risk of potential sovereign debt credit deterioration on the amounts of sovereign debt obligations, principally for UK, other European, US and Asian countries held in its investment portfolio. In recent years, rating agencies have downgraded the sovereign debt of some Continental European countries, the UK and the US. There is a risk of further downgrades for these countries. For some European countries the risk of default has also increased. Investing in such instruments creates exposure to the direct or indirect consequences of political, social or economic changes (including changes in governments, heads of states or monarchs) in the countries in which the issuers are located and the creditworthiness of the sovereign. Investment in sovereign debt obligations involves risks not present in debt obligations of corporate issuers. In addition, the issuer of the debt or the governmental authorities that control the repayment of the debt may be unable or unwilling to repay principal or pay interest when due in accordance with the terms of such debt, and Prudential may have limited recourse to compel payment in the event of a default. A sovereign debtor's willingness or ability to repay principal and to pay interest in a timely manner may be affected by, among other factors, its cash flow situation, its relations with its central bank, the extent of its foreign currency reserves, the availability of sufficient foreign exchange on the date a payment is due, the relative size of the debt service burden to the economy as a whole, the sovereign debtor's policy toward local and international lenders, and the political constraints to which the sovereign debtor may be subject. Periods of economic uncertainty may affect the volatility of market prices of sovereign debt to a greater extent than the volatility inherent in debt obligations of other types of issuers. If a sovereign were to default on its obligations, this could have a material adverse effect on Prudential's financial condition and results of operations.

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Prudential is subject to the risk of exchange rate fluctuations owing to the geographical diversity of its businesses

Due to the geographical diversity of Prudential's businesses, Prudential is subject to the risk of exchange rate fluctuations. Prudential's operations in the US and Asia, which represent a significant proportion of operating profit based on longer-term investment returns and shareholders' funds, generally write policies and invest in assets denominated in local currency. Although this practice limits the effect of exchange rate fluctuations on local operating results, it can lead to significant fluctuations in Prudential's consolidated financial statements upon translation of results into pounds sterling. The currency exposure relating to the translation of reported earnings is not currently separately managed. The impact of gains or losses on currency translations is recorded as a component of shareholders' funds within other comprehensive income. Consequently, this could impact on Prudential's gearing ratios (defined as debt over debt plus shareholders' funds).

Prudential conducts its businesses subject to regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies and interpretations and any accounting standards in the markets in which it operates

Changes in government policy, legislation (including tax) or regulatory interpretation applying to companies in the financial services and insurance industries in any of the markets in which Prudential operates, which in some circumstances may be applied retrospectively, may adversely affect Prudential's product range, distribution channels, profitability, capital requirements and, consequently, reported results and financing requirements. Also, regulators in jurisdictions in which Prudential operates may change the level of capital required to be held by individual businesses or could introduce possible changes in the regulatory framework for pension arrangements and policies, the regulation of selling practices and solvency requirements. Furthermore, as a result of the recent interventions by governments in response to global economic conditions, it is widely expected that there will be a substantial increase in government regulation and supervision of the financial services industry, including the possibility of higher capital requirements, restrictions on certain types of transaction structure and enhanced supervisory powers.

Current EU directives, including the EU Insurance Groups Directive ('IGD') require European financial services groups to demonstrate net aggregate surplus capital in excess of solvency requirements at the group level in respect of shareholder-owned entities. The test is a continuous requirement, so that Prudential needs to maintain a higher amount of regulatory capital at the group level than otherwise necessary in respect of some of its individual businesses to accommodate, for example, short-term movements in global foreign exchange rates, interest rates, deterioration in credit quality and equity markets. The EU is also developing a regulatory framework for insurance companies, referred to as 'Solvency II'. The approach is based on the concept of three pillars Pillar 1 consists of the quantitative requirements, for example, the amount of capital an insurer should hold. Pillar 2 sets out requirements for the governance and risk management of insurers, as well as for the effective supervision of insurers. Pillar 3 focuses on disclosure and transparency requirements.

The Solvency II Directive covers valuations, the treatment of insurance groups, the definition of capital and the overall level of capital requirements. A key aspect of Solvency II is that the assessment of risks and capital requirements are intended to be aligned more closely with economic capital methodologies, and may allow Prudential to make use of its internal economic capital models, if approved by the Financial Services Authority (FSA) or other relevant supervisory authority. The Solvency II Directive was formally approved by the Economic and Financial Affairs Council in November 2009. Representatives from the European Parliament, the European Commission and the Council of the European Union are currently discussing the Omnibus II Directive which, once approved, will amend certain aspects of the original Solvency II Directive. In addition, the European Commission is continuing to develop the detailed rules that will complement the high-level principles of the Directive, referred to

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as 'implementing measures'. The Omnibus II Directive is not currently scheduled to be finalised until late 2013, while the implementing measures cannot be finalised until after Omnibus II. There is a significant uncertainty regarding the final outcome of this process. In particular, the Solvency II rules relating to the determination of the liability discount rate and to the treatment of the US business remain unclear. As a result there is a risk that the effect of the measures finally adopted could be adverse for Prudential, including potentially a significant increase in capital required to support its business and that Prudential may be placed at a competitive disadvantage to other European and non-European financial services groups.

Currently there are also a number of other prospective global regulatory developments which could impact the way in which Prudential is supervised in its many jurisdictions. These include the Dodd-Frank Act in the US, the work of the Financial Stability Board (FSB) on Globally Systemically Important Financial Institutions (G-SIFIs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) being developed by the International Association of Insurance Supervisors (IAIS).

The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry within the United States that, among other reforms to financial services entities, products and markets, may subject financial institutions designated as systematically important to heightened prudential and other requirements intended to prevent or mitigate the impact of future disruptions in the US financial system, The full impact of the Dodd-Frank Act on Prudential's businesses is not currently clear, as many of its provisions have a delayed effectiveness and/or require rulemaking or other actions by various US regulators over the coming years.

As part of a global initiative to identify G-SIFIs, in May 2012, the IAIS published proposed assessment methodology for designating Globally Systemically Important Insurers (G-SIIs). For those groups that are designated by the FSB as G-SII, additional policy measures including enhanced supervision and higher loss absorbency requirements could be proposed. Further detail of the proposals is expected during 2013 and implementation is likely to be over a period of years. Furthermore, the FSA is considering the designation of a Domestically Systemically Important Insurer (D-SII) for those UK insurers that are significant in UK terms. It is not yet clear what the impact of this designation may be.

ComFrame is also being developed by the IAIS to provide common global requirements for the supervision of insurance groups. The framework is designed to develop common principles for supervision and so may increase the focus of regulators in some jurisdictions. It is also possible that some prescriptive requirements, including regarding group capital, could be proposed. Further clarity on ComFrame is expected during the second half of 2013.

Various jurisdictions in which Prudential operates have created investor compensation schemes that require mandatory contributions from market participants in some instances in the event of a failure of a market participant. As a major participant in the majority of its chosen markets, circumstances could arise where Prudential, along with other companies, may be required to make such contributions.

The Group's accounts are prepared in accordance with current International Financial Reporting Standards ('IFRS') applicable to the insurance industry. The International Accounting Standards Board ('IASB') introduced a framework that it described as Phase I, which permitted insurers to continue to use the statutory basis of accounting for insurance assets and liabilities that existed in their jurisdictions prior to January 2005. In July 2010, the IASB published an Exposure Draft for its Phase II on insurance accounting, which would introduce significant changes to the statutory reporting of insurance entities that prepare accounts according to IFRS. The IASB continues its deliberation on the exposure draft principles but it remains uncertain whether the proposals in the Exposure Draft will become the final IASB standard. The timing of the changes taking effect is uncertain but not expected to be before 2017.

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Any changes or modification of IFRS accounting policies may require a change in the future results or a restatement of reported results.

The resolution of several issues affecting the financial services industry could have a negative impact on Prudential's reported results or on its relations with current and potential customers

Prudential is, and in the future may be, subject to legal and regulatory actions in the ordinary course of its business, both in the UK and internationally. These actions could involve a review of business sold in the past under acceptable market practices at the time, such as the requirement in the UK to provide redress to certain past purchasers of pension and mortgage endowment policies, changes to the tax regime affecting products and regulatory reviews on products sold and industry practices, including, in the latter case, businesses it has closed.

Regulators are increasingly interested in the approach that product providers use to select third party distributors and to monitor the appropriateness of sales made by them. In some cases, product providers can be held responsible for the deficiencies of third-party distributors.

In the US, federal and state regulators have focused on, and continue to devote substantial attention to, the mutual fund, fixed index annuity and insurance product industries. This focus includes new regulations in respect of the suitability of sales of certain products. As a result of publicity relating to widespread perceptions of industry abuses, there have been numerous regulatory inquiries and proposals for legislative and regulatory reforms.

In Asia, regulatory regimes are developing at different speeds, driven by a combination of global factors and local considerations. There is a risk that new requirements are introduced that challenge current practices, or are retrospectively applied to sales made prior to their introduction.

Litigation, disputes and regulatory investigations may adversely affect Prudential's profitability and financial condition

Prudential is, and may be in the future, subject to legal actions, disputes and regulatory investigations in various contexts, including in the ordinary course of its insurance, investment management and other business operations. These legal actions, disputes and investigations may relate to aspects of Prudential's businesses and operations that are specific to Prudential, or that are common to companies that operate in Prudential's markets. Legal actions and disputes may arise under contracts, regulations (including tax) or from a course of conduct taken by Prudential, and may be class actions. Although Prudential believes that it has adequately provided in all material aspects for the costs of litigation and regulatory matters, no assurance can be provided that such provisions are sufficient. Given the large or indeterminate amounts of damages sometimes sought, other sanctions that might be applicable and the inherent unpredictability of litigation and disputes, it is possible that an adverse outcome could, from time to time, have an adverse effect on Prudential's reputation, results of operations or cash flows.

Prudential's businesses are conducted in highly competitive environments with developing demographic trends and continued profitability depends on management's ability to respond to these pressures and trends

The markets for financial services in the UK, US and Asia are highly competitive, with several factors affecting Prudential's ability to sell its products and continued profitability, including price and yields offered, financial strength and ratings, range of product lines and product quality, brand strength and name recognition, investment management performance, historical bonus levels, developing demographic trends and customer appetite for certain savings products. In some of its markets, Prudential faces competitors that are larger, have greater financial resources or a greater market share,

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offer a broader range of products or have higher bonus rates or claims-paying ratios. Further, heightened competition for talented and skilled employees and agents with local experience, particularly in Asia, may limit Prudential's potential to grow its business as quickly as planned.

In Asia, the Group's principal competitors in the region are international financial companies, including Allianz, AXA, ING, AIA and Manulife. In a number of markets, local companies have a very significant market presence.

Within the UK, Prudential's principal competitors in the life market include many of the major retail financial services companies including, in particular, Aviva, Legal & General, Lloyds Banking Group and Standard Life.

Jackson's competitors in the US include major stock and mutual insurance companies, mutual fund organisations, banks and other financial services companies such as AIG, AXA Financial Inc., Hartford Life Inc., Prudential Financial, Lincoln National, MetLife and TIAA-CREF.

Prudential believes competition will intensify across all regions in response to consumer demand, technological advances, the impact of consolidation, regulatory actions and other factors. Prudential's ability to generate an appropriate return depends significantly upon its capacity to anticipate and respond appropriately to these competitive pressures.

Downgrades in Prudential's financial strength and credit ratings could significantly impact its competitive position and hurt its relationships with creditors or trading counterparties

Prudential's financial strength and credit ratings, which are used by the market to measure its ability to meet policyholder obligations, are an important factor affecting public confidence in most of Prudential's products, and as a result its competitiveness. Downgrades in Prudential's ratings, as a result of, for example, decreased profitability, increased costs, increased indebtedness or other concerns, could have an adverse effect on its ability to market products; retain current policyholders; and on the Group's financial flexibility. In addition, the interest rates Prudential pays on its borrowings are affected by its debt credit ratings, which are in place to measure the Group's ability to meet its contractual obligations.

Prudential's long-term senior debt is rated as A2 by Moody's, A+ by Standard & Poor's and A by Fitch. The Moody's and Fitch ratings are on stable outlook and the Standard & Poor's rating is on negative outlook.

Prudential's short-term debt is rated as P-1 by Moody's, A-1 by Standard & Poor's and F1 by Fitch.

The Prudential Assurance Company Limited's financial strength is rated Aa2 by Moody's, AA by Standard & Poor's and AA by Fitch. The Moody's and Fitch ratings are on stable outlook and the Standard & Poor's rating is on negative outlook.

Jackson's financial strength is rated AA by Standard & Poor's and Fitch, A1 by Moody's, and A+ by AM Best. The Moody's, Fitch and AM Best ratings are on stable outlook and the Standard & Poor's rating is on negative outlook.

In addition, changes in methodologies and criteria used by rating agencies could result in downgrades that do not reflect changes in the general economic conditions or Prudential's financial condition.

Adverse experience in the operational risks inherent in Prudential's business could have a negative impact on its results of operations

Operational risks are present in all of Prudential's businesses, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, systems and human error or from external events. Prudential's business is dependent on processing a large number of complex

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transactions across numerous and diverse products, and is subject to a number of different legal and regulatory regimes. Further, because of the long-term nature of much of the Group's business, accurate records have to be maintained for significant periods. These factors, among others, result in significant reliance on and require significant investment in information technology, compliance and other systems, personnel and processes. In addition, Prudential outsources several operations, including a significant part of its UK back office and customer-facing functions as well as a number of IT functions, resulting in reliance upon the operational processing performance of its outsourcing partners.

Although Prudential's systems and processes incorporate controls designed to manage and mitigate the operational risks associated with its activities, there can be no assurance that such controls will always be effective. For example, although the business has not experienced a material failure or breach in relation to IT systems and processes to date, failures or breaches of this sort, including a cyber-security attack, could harm its ability to perform necessary business functions and hurt its relationships with its business partners and customers. Similarly, any weakness in the administration systems or actuarial reserving processes could have an impact on its results of operations during the effective period. Prudential has not experienced or identified any operational risks in its systems or processes during 2012, which have subsequently caused, or are expected to cause, a significant negative impact on its results of operations.

Adverse experience relative to the assumptions used in pricing products and reporting business results could significantly affect Prudential's results of operations

Prudential needs to make assumptions about a number of factors in determining the pricing of its products, setting reserves, for reporting its capital levels and the results of its long-term business operations. For example, the assumption that Prudential makes about future expected levels of mortality is particularly relevant for its UK annuity business. In exchange for a premium equal to the capital value of their accumulated pension fund, pension annuity policyholders receive a guaranteed payment, usually monthly, for as long as they are alive. Prudential conducts rigorous research into longevity risk, using data from its substantial annuitant portfolio. As part of its pension annuity pricing and reserving policy, Prudential's UK business assumes that current rates of mortality continuously improve over time at levels based on adjusted data and models from the Continuous Mortality Investigations (CMI) as published by the Institute and Faculty of Actuaries. If mortality improvement rates significantly exceed the improvement assumed, Prudential's results of operations could be adversely affected.

A further example is the assumption that Prudential makes about future expected levels of the rates of early termination of products by its customers (persistency). This is particularly relevant to its lines of business other than its UK annuity business. Prudential's persistency assumptions reflect recent past experience for each relevant line of business. Any expected deterioration in future persistency is also reflected in the assumption. If actual levels of future persistency are significantly lower than assumed (that is, policy termination rates are significantly higher than assumed), the Group's results of operations could be adversely affected.

Another example is the impact of epidemics and other effects that cause a large number of deaths. Significant influenza epidemics have occurred three times in the last century, but the likelihood, timing, or the severity of future epidemics cannot be predicted. The effectiveness of external parties, including governmental and non-governmental organisations, in combating the spread and severity of any epidemics could have a material impact on the Group's loss experience.

In common with other life insurers, the profitability of the Group's businesses depends on a mix of factors including mortality and morbidity trends, policy surrender rates, investment performance and impairments, unit cost of administration and new business acquisition expense.

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As a holding company, Prudential is dependent upon its subsidiaries to cover operating expenses and dividend payments

The Group's insurance and investment management operations are generally conducted through direct and indirect subsidiaries.

As a holding company, Prudential's principal sources of funds are remittances from subsidiaries, shareholder-backed funds, the shareholder transfer from long-term funds and any amounts that may be raised through the issuance of equity, debt and commercial paper. Certain of the subsidiaries are restricted by applicable insurance, foreign exchange and tax laws, rules and regulations that can limit the payment of dividends, which in some circumstances could limit the ability to pay dividends to shareholders or to make available funds held in certain subsidiaries to cover operating expenses of other members of the Group.

Prudential operates in a number of markets through joint ventures and other arrangements with third parties (including in China and India), involving certain risks that Prudential does not face with respect to its consolidated subsidiaries

Prudential operates, and in certain markets is required by local regulation to operate, through joint ventures (including in China and India). For the Group's joint venture operations, management control is exercised jointly with the venture participants. The level of control exercisable by the Group depends on the terms of the joint venture agreements, in particular, the allocation of control among, and continued co-operation between, the joint venture participants. Prudential may also face financial or other exposure in the event that any of its joint venture partners fails to meet its obligations under the joint venture or encounters financial difficulty. In addition, a significant proportion of the Group's product distribution is carried out through arrangements with third parties not controlled by Prudential and is dependent upon continuation of these relationships. A temporary or permanent disruption to these distribution arrangements could adversely affect the results of operations of Prudential.

Prudential's Articles of Association contain an exclusive jurisdiction provision

Under Prudential's Articles of Association, certain legal proceedings may only be brought in the courts of England and Wales. This applies to legal proceedings by a shareholder (in its capacity as such) against Prudential and/or its directors and/or its professional service providers. It also applies to legal proceedings between Prudential and its directors and/or Prudential and Prudential's professional service providers that arise in connection with legal proceedings between the shareholder and such professional service provider. This provision could make it difficult for US and other non-UK shareholders to enforce their shareholder rights.

Changes in tax legislation may result in adverse tax consequences

Tax rules, including those relating to the insurance industry, and their interpretation, may change, possibly with retrospective effect, in any of the jurisdictions in which Prudential operates. Significant tax disputes with tax authorities, and any change in the tax status of any member of the Group or in taxation legislation or its scope or interpretation could affect Prudential's financial condition and results of operations.

FORWARD-LOOKING STATEMENTS

This document may contain 'forward-looking statements' with respect to certain of Prudential's plans and its goals and expectations relating to its future financial condition, performance, results, strategy and objectives. Statements that are not historical facts, including statements about Prudential's beliefs and expectations and including, without limitation, statements containing the words "may", "will", "should", "continue", "aims", "estimates", "projects", "believes", "intends", "expects", "plans", "seeks" and

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"anticipates", and words of similar meaning, are forward-looking statements. These statements are based on plans, estimates and projections as at the time they are made, and therefore undue reliance should not be placed on them. By their nature, all forward-looking statements involve risk and uncertainty. A number of important factors could cause Prudential's actual future financial condition or performance or other indicated results to differ materially from those indicated in any forward-looking statement. Such factors include, but are not limited to, future market conditions, including fluctuations in interest rates and exchange rates and the potential for a sustained low-interest rate environment, and the performance of financial markets generally; the policies and actions of regulatory authorities, including, for example, new government initiatives related to the financial crisis and the effect of the European Union's 'Solvency II' requirements on Prudential's capital maintenance requirements; the impact of competition, economic growth, inflation, and deflation; experience in particular with regard to mortality and morbidity trends, lapse rates and policy renewal rates; the timing, impact and other uncertainties of future acquisitions or combinations within relevant industries; the impact of changes in capital, solvency standards, accounting standards or relevant regulatory frameworks, and tax and other legislation and regulations in the jurisdictions in which Prudential and its affiliates operate; and the impact of legal actions and disputes. These and other important factors may for example result in changes to assumptions used for determining results of operations or re-estimations of reserves for future policy benefits. Further discussion of these and other important factors that could cause Prudential's actual future financial condition or performance or other indicated results to differ, possibly materially, from those anticipated in Prudential's forward-looking statements can be found under the 'Risk Factors' heading of this annual report, as well as under the 'Risk Factors' heading of any subsequent Prudential Half Year Financial Report furnished to the US Securities and Exchange Commission on Form 6-K.

Any forward-looking statements contained in this document speak only as of the date on which they are made. Prudential may also make or disclose written and/or oral forward-looking statements in reports filed with or furnished to the US Securities and Exchange Commission, the UK Financial Services Authority or other regulatory authorities, as well as in its annual report and accounts to shareholders, proxy statements, offering circulars, registration statements, prospectuses and, prospectus supplements, press releases and other written materials and in oral statements made by directors, officers or employees of Prudential to third parties, including financial analysts. All such forward-looking statements are qualified in their entirety by reference to the factors discussed under the 'Risk Factors' heading of this document, as well as under the 'Risk Factors' heading of any subsequent Prudential Half-Year Financial Report furnished to the US Securities and Exchange Commission on Form 6-K. These factors are not exhaustive as Prudential operates in a continually changing business environment with new risks emerging from time to time that it may be unable to predict or that it currently does not expect to have a material adverse effect on its business. Prudential expressly disclaims any obligation to update any of the forward-looking statements contained in this document or any other forward-looking statements it may make, whether as a result of future events, new information or otherwise except as required pursuant to the UK Prospectus Rules, the UK Listing Rules, the UK Disclosure and Transparency Rules, the Hong Kong Listing Rules, the SGX-ST listing rules or other applicable laws and regulations.

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EEV BASIS AND NEW BUSINESS RESULTS

In addition to IFRS basis results, Prudential's filings with the UK Listing Authority, the Stock Exchange of Hong Kong, the Singapore Stock Exchange and Group Annual Reports include reporting by Key Performance Indicators ('KPIs'). These include results prepared in accordance with the European Embedded Value ('EEV') Principles and Guidance issued by the Chief Financial Officers' ('CFO') Forum of European Insurance Companies, and New Business measures.

The EEV basis is a value based method of reporting in that it reflects the change in the value of in-force long-term business over the accounting period. This value is called the shareholders' funds on the EEV basis which, at a given point in time, is the value of future cash flows expected to arise from the current book of long-term insurance business plus the net worth (based on statutory solvency capital or economic capital where higher and free surplus) of Prudential's life insurance operations. Prudential publishes its EEV results semi-annually in the UK, Hong Kong and Singapore markets.

New Business results are published quarterly and are provided as an indicative volume measure of transactions undertaken in the reporting period that have the potential to generate profits for shareholders. New business results are categorised as single premiums and annual regular premiums. New business results are also summarised by annual premium equivalents (APE) which are calculated as the aggregate of regular new business amounts and one-tenth of single new business amounts. The amounts are not, and are not intended to be, reflective of premium income recorded in the IFRS income statement. EEV basis new business profits and margins are also published quarterly.

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Item 4. Information on the Company

BUSINESS OF PRUDENTIAL

Overview and Summary of Strategy

Overview

Prudential is an international financial services group, with significant operations in Asia, the United States and the United Kingdom. It has been in existence for over 160 years, serves around 24 million insurance customers globally and has £405 billion in assets under management (as at 31 December 2012). Prudential is not affiliated with Prudential Financial, Inc. or its subsidiary, The Prudential Insurance Company of America.

Prudential is structured around four main business units: Prudential Corporation Asia (incorporating the asset management business, Eastspring Investments), Jackson, Prudential UK insurance operations and M&G. These are supported by central functions which are responsible for Prudential strategy, cash and capital management, leadership development and succession, reputation management and other core group functions.

Prudential Corporation Asia has operations in Hong Kong, Malaysia, Singapore, Indonesia and other Asian countries. Its core business is health, protection, either attached to a life policy or on a standalone basis, other life insurance (including participating business) and mutual funds. It also provides selected personal lines property and casualty insurance, group insurance, institutional fund management and consumer finance (Vietnam only). The product range offered is tailored to suit the individual country markets. Insurance products are distributed mainly through an agency sales force together with selected banks, while the majority of mutual funds are sold through banks and brokers. Joint venture partners are mandatory in some markets: for example, the life insurance operation in China is a 50 per cent equity joint venture with CITIC; in India Prudential has a 26 per cent equity stake in a joint venture with ICICI and in Malaysia its Takaful business is a 70 per cent equity joint venture with Bank Simpanan Nasional. In the fund management business in India, Prudential holds a 49 per cent equity stake in a joint venture with ICICI, in China it has a 49 per cent equity stake in a joint venture with CITIC and in Hong Kong it has a 36 per cent equity stake in a joint venture with Bank of China International.

As at 31 December 2012, Prudential Corporation Asia had:

- 13 million insurance customers with life and fund management operations in 12 markets;
- distribution relationships with over 77 institutions across Asia including Standard Chartered Bank (SCB), United Overseas Bank Limited (UOB) and joint venture partners ICICI in India and CITIC in China;
- one of the largest networks of tied agents in Asia; and
- consistently high brand recognition, outperforming many other financial services companies and had received multiple awards for its customer service. Prudential was in the top three for market share of new business in India, Indonesia, Malaysia, Singapore, the Philippines and Vietnam.

In the United States, Prudential offers a range of products through Jackson, including fixed annuities (fixed interest annuities, fixed index and immediate annuities), variable annuities and institutional products (including guaranteed investment contracts and funding agreements). Although Jackson historically also offered traditional life insurance products, it discontinued new sales of life insurance products effective 1 August 2012. Jackson distributes these products through independent insurance agents; independent broker-dealers; regional broker-dealers; wirehouses; registered investment advisers; and banks, credit unions and other financial institutions.

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Jackson also offers fee-based separately managed accounts and investment products through Curian Capital, LLC, which is Jackson's registered investment adviser.

As at 31 December 2012, in the United States, Jackson:

- was among the 20 largest life insurance companies in terms of general account assets[(2)];
- was a top two player in US variable annuities[(3)];
- was once again awarded the 'Highest Customer Satisfaction by Industry' award for the seventh successive year from Service Quality Measurement Group; and
- was once again rated as a 'World Class' service provider for the seventh successive year by Service Quality Measurement Group.

In the United Kingdom, Prudential is structured into Prudential UK(comprising the insurance operations) and M&G (the UK and European fund manager of the Group) and offers a range of retail financial products and services, including long-term insurance and asset accumulation and retirement income products (life insurance, pensions and pension annuities), retail investment and unit trust products, and fund management services. Prudential in the United Kingdom primarily distributes these products through financial advisers, partnership agreements with other financial institutions, and direct marketing, by telephone, mail, internet and face-to-face advisers.

As at 31 December 2012, Prudential UK:

- was one of the market leaders in the individual annuity market and the with-profits market[(4)]; and
- had total company assets of £158 billion on the balance sheet, comprising £93 billion within the with-profits sub fund, £57 billion within shareholder-backed business and £8 billion in the Scottish Amicable Insurance Fund.

As at 31 December 2012, M&G:

- had responsibility for £228 billion of investment on behalf of both internal and external clients; and
- M&G's retail business has been awarded the prestigious Outstanding Investment House of the Year 2012 Award for the third year running at the OBSR Awards. M&G's institutional business was recognised for its strength and expertise at the UK Pensions Awards, where it was named Fixed Income Manager of the Year 2012.

Group Strategy Overview

Prudential's strategy has remained consistent: to accelerate growth in Asia; to build on the strength of US operations; to focus the UK business and optimise asset management.

In a turbulent environment, the Group has continued to take proactive and decisive management action to deliver on strategy. In this industry, distribution is absolutely key. Therefore the Group has continued to strengthen its ability to reach its chosen customers in its chosen markets. For instance, Prudential has strengthened its distribution in Thailand by establishing an exclusive partnership with

(2)

Source: Third Quarter 2012 SNL Financial

(3)

Source: Morningstar Annuity Research Center (MARC) Third Quarter 2012 Sales Report©. © Morningstar, Inc. All Rights Reserved. The information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.

(4)

Source: Association of British Insurers (ABI)

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Thanachart Bank, a leading bank in this market, and through the acquisition of its life business, Thanachart Life. In the US, the Group has continued to invest in distribution as well, strengthening relationships with partners. Throughout the year, Prudential has ensured that it puts value ahead of volume, ensuring that it reached its return on capital and payback targets. To mention a few examples, in Malaysia the Group refocused the business on higher-value, lower-volume protection business. In Korea and in Taiwan, at times during the year, Prudential refused to write poor value business, sacrificing some sales and growth in the process.

Prudential has maintained its bias in favour of insurance income and fee income, which have grown as a proportion of profits, ahead of spread income. True to that logic, in the US Prudential acquired Reassure America Life Insurance Company (REALIC), which increased its insurance income. The Group also continues to drive its product mix to achieve the optimal balance between growth in sales, profit growth, cash generation and capital strength. Therefore, it has continued to emphasise and to grow protection products in Asia, which also provide excellent value to customers. In the US, the Group has seen growing demand for Elite Access, a variable annuity without guarantees, launched in March 2012. Elite Access allows the Group to meet the needs of a key customer segment and to grow profitably while staying within our quantitative risk appetite in the year. Prudential believes Elite Access has excellent prospects in the US market. More generally, The Group has continually and proactively re-priced products and modified their features to ensure they continued to generate adequate returns in the new interest rate environment.

The Group's strategy is supported by three key Group-wide operating principles.

First, it takes a balanced approach to performance management across the key measures of IFRS, EEV and cash, with a particular focus on IFRS and cash. Second, it focuses on allocating capital to the highest return and shortest payback opportunities across the Group taking strong action where necessary, such as deliberately reducing sales in geographies, products or channels where its return and payback criteria are not met. Third, the Group is proactive in managing risk across the cycle.

The Group continues to focus on promoting transparency by providing shareholders with relevant disclosures about its business and how they run it, to ensure that both its strategy and its operating principles are well understood. In addition to the disclosures that are provided with its quarterly financial results, since 2010 it has organised an annual seminar to provide investors and analysts with a further opportunity to discuss the business in detail with the Group's senior management.

The Group has organised three investor seminars in London (on 1 December 2010), Kuala Lumpur (on 15 November 2011), and New York (on 29 November 2012). These seminars consisted of presentations on different aspects of its business including: Group strategy; its operating principles; the 2013 'Growth and Cash' objectives; its Asian business, including country-by-country presentations; and Jackson, with further insights into its hedging strategy, capital position and sensitivity to market shocks. The Group intends to hold a fourth annual seminar in the last quarter of 2013 in London.

Company Address and Agent

Prudential plc is a public limited company incorporated on 1 November 1978, and organised under the laws of England and Wales. Refer to Item 10, 'Additional information Memorandum and Articles of Association' for further information on the constitution of the Company.

Prudential's registered office is Laurence Pountney Hill, London EC4R 0HH, England (telephone: +44 20 7220 7588) and its principal executive offices are at 12 Arthur Street, London EC4R 9AQ, England (telephone: +44 20 7220 7588). Prudential's agent in the United States for purposes of Item 4 of this annual report on Form 20-F is Jackson National Life Insurance Company, located at 1 Corporate Way, Lansing, Michigan 48951, United States of America.

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Significant Subsidiaries

The table below sets forth Prudential's significant subsidiaries.

Name of Company	Main activity	Percentage Owned(1)	Country of incorporation
The Prudential Assurance Company Limited	Insurance	100%	England and Wales
Prudential Annuities Limited(2)	Insurance	100%	England and Wales
Prudential Retirement Income Limited (PRIL)(2)	Insurance	100%	Scotland
M&G Investment Management Limited(2)	Asset management	100%	England and Wales
Jackson National Life Insurance Company(2)	Insurance	100%	US
Prudential Assurance Company Singapore (Pte) Limited(2)	Insurance	100%	Singapore

(1) Percentage of equity owned by Prudential directly or indirectly. The percentage of voting power held is the same as the percentage owned. Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for Prudential Retirement Income Limited which operates mainly in England and Wales.

(2) Owned by a subsidiary of Prudential.

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Asian Business

Life Insurance

Introduction

Asia's rapidly growing middle classes remain a key growth driver for the retail financial services sector, particularly life insurance with an emphasis on protection. Research has shown that as the middle class becomes more established the proportion of income they allocate to financial planning increases from 5 per cent to around 12 per cent[(5)]. The manifestation of this demand varies significantly across the region, reflecting the various stages of development in each individual market, together with their distinct regulatory and competitive environments, cultural differences and customer preferences. However, across all markets there is increasing recognition among governments and regulators of the social utility of a vibrant private sector life insurance market that provides financial security to families, efficiently channels long-term savings into financial markets and generates employment opportunities within the industry.

Our strategy in Asia is focused on meeting the needs of the emerging middle class in the region for savings and protection. The region's positive demographics, strong economic growth, sound public finances and favourable public policy environment with a clear preference for private provision of protection, have all led to a rapidly expanding middle class, with a strong and growing demand for our savings and protection products.

On 2 July 2012 we announced that Prudential has received in-principle approval from Cambodia's Ministry of Economy and Finance to establish a wholly foreign-owned life insurance operation in the country. Although the Cambodian economy is relatively small at present, it has delivered strong GDP growth over the past ten years and we see excellent opportunities to develop the life insurance industry in the coming years. The business sold its first policies in January 2013.

On 5 November 2012, Prudential plc , through its subsidiary Prudential Life Assurance (Thailand) Public Company Limited ('Prudential Thailand') entered into an agreement to acquire 100 per cent of Thanachart Life Assurance Company Limited ('Thanachart Life'), a wholly-owned life insurance subsidiary of Thanachart Bank Public Company limited ('Thanachart Bank'). The transaction was approved by the regulator in March 2013 and is expected to close in the second quarter of 2013. As part of the deal, Prudential Thailand and Thanachart Bank have entered into an agreement to establish an exclusive 15-year partnership to develop jointly their bancassurance business in Thailand. This transaction builds on Prudential's strategy of focusing on the highly attractive markets of South-East Asia and is in line with the group's multichannel distribution strategy.

Overall, our geographic footprint, combined with the exceptional quality of our distribution and of our products, has enabled us to deliver another year of very strong performance in Asia. Our 13 million insurance customers, whom we serve well and profitably, represent only a small proportion of the long-term potential of this part of the world for our company.

Distribution

Prudential's strategy in Asia is well established and continues to be highly effective. The customer is at the heart of our strategy and Asian customers find our offering of regular premium savings and protection products distributed principally through high quality face to face distribution channels particularly attractive. The quality of our brand, our products, and of our distribution allows us to translate our sales in to strong returns to our shareholders.

Building and strengthening Prudential's multichannel distribution capabilities is a constant objective for us. Tied-agency remains a highly effective and efficient distribution channel in Asia and Prudential

(5) HSBC Global Research

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has one of the region's largest agency forces. We focus both on the size and the productivity of our agency force.

Prudential has a diverse range of successful bank distribution partnerships across the region that includes regional relationships with international banks such as Standard Chartered and local ones such as E.Sun in Taiwan. Prudential is also successful in working with multiple partners in one market. Key drivers of this success are a long-term commitment to creating value for both partners, expertise in developing, training and motivating bank sales teams and committed marketing support. Bancassurance has been growing rapidly in the region in recent years and Prudential remains a regional leader in this channel, led by highly productive relationships including SCB and UOB. As described above, in November 2012, Prudential announced a new and strategically significant, exclusive long-term partnership with Thailand's Thanachart Bank as part of a deal that will see Thanachart Life merged with our existing life operation in the country immediately doubling our market share. The deal is expected to complete during the first half of 2013.

Products

The life insurance products offered by Prudential in Asia include with-profits (participating) and non-participating term, whole life and endowment and unit-linked policies often combined with protection riders and typically with regular premium payments. Prudential in Asia also offers health, disablement, critical illness and accident cover to supplement its core life products. Prudential's product mix is orientated around a core of regular premium policies with protection riders. The portfolio is regularly refreshed with new features and benefits that keep pace with evolving customer needs and also drive sales force activities.

It is part of our strategy to focus on regular premium products which allow our customers to invest over the long term. We aim to make most of our sales as regular premiums and the proportion of regular premium business has been consistently high, which ensures the profitability and resilience of our growing in-force book. Although single premium products can provide appropriate opportunities for customers with lump sums, we believe that regular premium policies with protection riders best meet the majority of our customers' needs.

Unit-linked products combine savings with protection, with the cash value of the policy depending on the value of the underlying unitised funds. Participating products provide savings with protection where the basic sum assured can be enhanced by a profit share (or bonus) from the underlying fund as determined at the discretion of the insurer. Non-participating products offer savings with protection where the benefits are guaranteed or determined by a set of defined market-related parameters. Accident and health products provide mortality or morbidity benefits and include health, disablement, critical illness and accident cover. These products are commonly offered as supplements to main life policies, but can also be sold separately.

Policyholder and insurer share the profits from participating policies (typically in a 90:10 ratio) in the same way as with-profits business in the UK. With unit-linked products, shareholders receive the profits arising from managing the policy, its investments and the insurance risk. Policyholders within the underlying unitised fund receive investment gains. The profits from accident and health and non-participating products come from any surplus remaining after paying policy benefits.

At the end of 2012, Prudential is offering unit-linked products in all markets except Thailand and Vietnam. However, given the recent volatility in the financial markets, we have seen a shift towards non linked products.

Critical factors in Prudential's success in health and protection include integrating the product initiatives with the distribution channels and tailoring sales support activities to the sales force. For example, health products have been incorporated into agency incentive programs and a standalone

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healthcare product was launched into the SCB channel with simplified underwriting and compelling media campaigns to capture direct business and provide leads for other channels.

In Malaysia and Indonesia, Prudential also offers life insurance policies that are constructed to comply with Islamic principles otherwise known as Takaful. The main principles are that policyholders co-operate amongst themselves for the common good, uncertainty is eliminated in respect of subscription and compensation and there is no investment in prohibited areas such as gambling or alcohol.

In addition to providing value directly to our customers through our products and services, we aim to provide wider benefits to the community where we operate. Therefore, Prudential supports a range of corporate social responsibility activities across Asia, with a focus on providing disaster relief, promoting financial literacy and benefiting children. During 2012, Prudential extended its highly successful children's financial literacy programme, 'Cha-Ching', for example this has now been adopted in the Philippines as part of the school curriculum.

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New Business Premiums

In 2012, total sales of insurance products, excluding Japan, were £3,308 million, up 11 per cent from 2011 (£2,970 million). Of this amount, regular premium insurance sales increased 15 per cent to £1,740 million and single premium insurance sales increased 8 per cent to £1,568 million.

The following table shows Prudential's Asian life insurance new business premiums by territory for the periods indicated. In this table, 'Other Countries' includes Thailand, the Philippines and Vietnam.

	2012	**2011**	**2010**
	£m	**£m**	**£m**
Single premiums			
Singapore	**399**	371	318
Hong Kong	**157**	180	107
Malaysia	**98**	79	58
Taiwan (excluding Taiwan agency)	**172**	217	146
Korea	**94**	71	66
China (Prudential's 50% interest in joint venture with CITIC)	**37**	46	103
Indonesia	**359**	250	141
India (Prudential's 26% interest in joint venture with ICICI)	**67**	135	85
Other countries	**185**	107	80
Total excluding Japan	**1,568**	1,456	1,104
Japan			13
Total including Japan	**1,568**	1,456	1,117
Regular premiums			
Singapore	**261**	198	143
Hong Kong	**380**	313	276
Malaysia	**208**	215	198
Taiwan (excluding Taiwan agency)	**138**	126	105
Korea	**86**	94	89
China (Prudential's 50% interest in joint venture with CITIC)	**53**	54	48
Indonesia	**410**	338	269
India (Prudential's 26% interest in joint venture with ICICI)	**96**	88	180
Other countries	**108**	88	83
Total excluding Japan	**1,740**	1,514	1,391
Japan			6
Total including Japan	**1,740**	1,514	1,397
Total			
Total excluding Japan	**3,308**	2,970	2,495
Japan*			19
Total including Japan	**3,308**	2,970	2,514

* The Group's Japanese insurance subsidiary ceased selling new business with effect from 15 February 2010.

Eastspring Investments

Prudential's asset management business in Asia manages investments for Asia's third-party retail and institutional clients in addition to investments of Prudential's Asia, UK and US life companies. It has operations in 11 markets, including Indonesia which was successfully opened during 2012, increasing our asset management footprint in the region.

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In November 2011, Prudential announced that its Asia Asset Management operations would be rebranded Eastspring Investments. The new brand, which was officially launched in February 2012, is enabling the business to establish a cohesive regional presence in Asia thereby penetrating the offshore segment more effectively. It also supports distribution to new markets outside Asia and we have recently opened a distribution office in the US.

Eastspring Investment's leading presence in Asia was acknowledged, when it was ranked the largest retail asset manager in Asia (based on assets sourced from Asia ex-Japan) as at 30 June 2012, in a survey conducted by Asia Asset Management magazine. Eastspring Investments also received multiple accolades for its investment capabilities, including four fund managers from Singapore, Malaysia and Indonesia being named '2012 Most Astute Investors in Asian currency bonds' by The Asset Benchmark Research and the joint venture business in India being recognised as the 'Best Debt Fund House of the year' in Morningstar Awards 2012.

Distribution

In order to capitalise on the sizeable opportunities in Asia's retail financial services market, Eastspring Investments maintained its focus on building a strong third-party customer retail franchise. The customer proposition is driven by Eastspring Investments' investment capabilities, which enable it to develop innovative product suites, and distribute them through diverse channels including regional banks, local banks, private banks, and securities houses and an internal sales force.

The mutual fund industry continues to diversify its investments, with expectations for a significant increase in net flows over the coming years. Bank distribution continues to be important in most markets in Asia, with Prudential having established strong relationships with both regional and local banks and placing significant emphasis on providing good service. Prudential's Asian asset management business is also growing its third party institutional and pension fund management business.

Products

Eastspring Investments offers mutual fund investment products in India, Taiwan, Japan, Singapore, Malaysia, Hong Kong, Korea, Vietnam, China and now Indonesia, thus enabling customers to participate in debt, equity and money market investments across the region.

Markets in Asia remained challenging in 2012. Equity funds struggled to gain traction due to poor investor sentiment in the face of weak macroeconomic signals. Fixed income and regular yield products remained in favour.

Net flows and funds under management

Eastspring Investments levies transaction charges (initial and surrender depending on the type of fund and the length of the investment) and also a service charge based on assets under management. The charges vary by country and fund, with money market style funds generally having the lowest charges and equity funds the highest.

Total funds under management (FUM) reached a record £58.1 billion at the end of 2012 (2011: £50.3 billion: 2010: £51.9 billion) representing a 16 per cent increase from a year ago on the back of strong net inflows and positive market movements, while net third party inflows (excluding MMF) of £1,626 million were driven by net inflows in India, Taiwan and China.

Specifically, strong fund raising was seen in India for our fixed maturity plan range and open-ended bond funds, while the Taiwan business saw a successful launch of the Emerging Asian Local Fixed Income Fund in the first half of the year and the Global Aggregate Strategy High Yield Bond Fund in the second half. In addition, Taiwan's existing range of onshore and offshore bond funds also generated significant net inflows in 2012. In China, both the CSI 500 Index Fund and the Tianjin Split Bond Fund

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launched in second half of the year attracted positive flows. The positive net flows were partially offset by redemptions from an institutional client in Singapore and another in Korea.

US Business

Prudential conducts its US insurance operations through Jackson National Life Insurance (Jackson) and its subsidiaries, including Curian Capital, a registered investment adviser. The US operations also include PPM America, Prudential's US internal and institutional fund manager, and Prudential's US broker dealer operations (National Planning Corporation, SII Investments, INVEST Financial Corporation and Investment Centers of America). As at 31 December 2012, Prudential's US operations had more than 4.7 million policies and contracts in effect (including those acquired through the purchase of REALIC as described below) and PPM America managed approximately £63.9 billion of assets. In 2012, new business premiums totalled £14,516 million.

Jackson

Jackson is a leading provider of retirement income and savings solutions in the mass and mass-affluent segments of the US market, primarily to those planning for retirement or in retirement already. It offers tools that help people plan for their retirement, and offers products with specialised features and guarantees to meet customers' needs. By seeking to add value to both the representatives who sell Jackson products, and to their customers, Jackson has built a strong position in the US retirement savings and income market with an almost ten-fold increase in variable annuity sales over the past decade. Over the same period, Jackson increased its total annuity market share from 2.3 per cent in 2001 to 10.4 per cent in 2012 and moved from 17th in total annuity sales to 1st[(6)].

Jackson's strategy remains focused on providing value to its customers and driving shareholder value while operating within a conservative risk management framework. This approach has enabled us to successfully navigate the significant macroeconomic and financial market challenges of the last five years and ensured a continuation of our strong performance in 2012.

In 2012, Jackson delivered a higher retail sales than 2011 and had a modest benefit from institutional sales. Retail annuity net flows continued to benefit from increased sales and low levels of surrender activity.

We believe that Jackson continues to be one of the most efficient operators within the US life insurance market. The ratio of statutory general expenses to average assets improved slightly to 41 basis points in 2012 versus 42 basis points in 2011. This efficiency has been delivered while maintaining world class standards of customer service for our contract holders. In 2012, Jackson was rated as a 'World Class' service provider by the Service Quality Measurement Group for the seventh consecutive year.

On 4 September 2012, Jackson completed the acquisition of SRLC America Holding Corp (SRLC) from Swiss Re for a consideration of £370 million which is subject to finalisation of completion procedures. SRLC was the US holding company of REALIC. The acquisition helps diversify Jackson's sources of earnings by increasing the amount of income generated from underwriting activities. The transaction is expected to add an additional £100 million to Jackson's IFRS pre-tax profits in the first year, representing stand-alone earnings from REALIC of approximately £115 million, less £15 million of income foregone on the assets sold to finance the transaction. In the four month period since completion, REALIC contributed £67 million to Jackson's IFRS operating profit based on longer-term investment returns while having only a modest impact on statutory capital. SRLC's primary subsidiary was REALIC, which was merged into Jackson on 31 December 2012. REALIC's primary business activity involved the acquisition of blocks of life insurance. In addition to REALIC, SRLC had other insignificant subsidiaries. Subsequent to the purchase SRLC was dissolved and its subsidiaries became direct subsidiaries of Jackson.

(6) Source: Third Quarter 2012 Life Insurance and Market Research Association.

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National Planning Holdings ('NPH') is Jackson's affiliated independent broker dealer network. The business is comprised of four broker dealer firms, including INVEST Financial Corporation, Investment Centers of America, Inc, National Planning Corporation and SII Investments, Inc. NPH continues to grow its business and revenue per representative. By utilising high-quality, state-of-the-art technology, NPH provides advisers the tools they need to operate their practices more efficiently. At the same time, through its relationship with NPH, Jackson continues to benefit from an important retail distribution outlet, in addition to receiving valuable insight into the needs of financial advisers and their clients.

Curian Capital, LLC ('Curian'), Jackson's registered investment adviser, provides innovative fee-based separately managed accounts and investment products to advisers through a sophisticated technology platform. Curian expands Jackson's access to advisers while also complementing Jackson's core annuity product lines with Curian's retail asset management products.

Products

The following table shows total new business premiums in the United States by product line and distribution channel for the periods indicated. Total new business premiums include Jackson's deposits for investment contracts with limited or no life contingencies.

	Year Ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
By Product			
Annuities			
Fixed annuities			
Interest sensitive	**550**	441	755
Fixed index	**1,094**	934	1,089
Immediate	**31**	31	81
Variable annuities	**12,445**	10,909	9,481
Total	**14,120**	12,315	11,406
Life insurance	**17**	29	33
Institutional products			
GICs, funding agreements and Federal Home Loan Bank of Indianapolis (FHLBI) advances	**379**	237	
Total	**14,516**	12,581	11,439
By Distribution Channel			
Independent broker dealer	**8,319**	7,471	6,503
Bank	**2,705**	2,135	2,285
Regional broker dealer	**2,421**	2,075	1,789
Independent agents	**682**	643	846
Institutional products department	**379**	237	
Captive agents	**10**	20	16
Total	**14,516**	12,581	11,439

Of the total new business premiums of £14,516 million in 2012 (2011: £12,581 million; 2010: £11,439 million), £14,125 million (2011: £12,325 million; 2010: £11,417 million) were single premiums, £12 million (2011: £19 million; 2010: £22 million) were regular premiums and £379 million (2011: £237; 2010: nil) were institutional product premiums.

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Annuities

Fixed Annuities

Interest-sensitive Annuities

In 2012, interest-sensitive fixed annuities accounted for 4 per cent (2011: 4 per cent) of total new business premiums and 13 per cent (2011: 16 per cent) of policy and contract liabilities of the US operations. Interest-sensitive fixed annuities are primarily deferred annuity products that are used for asset accumulation in retirement planning and for providing income in retirement. They permit tax-deferred accumulation of funds and flexible payout options.

The contract holder of an interest-sensitive fixed annuity pays Jackson a premium, which is credited to the contract holder's account. Periodically, interest is credited to the contract holder's account and in some cases administrative charges are deducted from the contract holder's account. Jackson makes benefit payments at a future date as specified in the policy based on the value of the contract holder's account at that date. On more than 83 per cent (2011: 90 per cent) of in-force business, Jackson may reset the interest rate on each contract anniversary, subject to a guaranteed minimum, in line with state regulations. When the annuity matures, Jackson either pays the contract holder the amount in the contract holder account or begins making payments to the contract holder in the form of an immediate annuity product. This latter product is similar to a UK annuity in payment.

At 31 December 2012, Jackson had fixed interest rate annuities totalling £11.7 billion (US$19.0 billion) (2011: £11.5 billion (US$17.8 billion) in account value with minimum guaranteed rates ranging from 1.0 per cent to 5.5 per cent and a 3.09 per cent average guaranteed rate (2011: 1.0 per cent to 5.5 per cent and a 3.08 per cent average guaranteed rate).

Fixed interest rate annuities are subject to early surrender charges for the first six to nine years of the contract. In addition, the contract may be subject to a market value adjustment at the time of surrender. During the surrender charge period, the contract holder may cancel the contract for the surrender value. Jackson's profits on fixed annuities arise primarily from the spread between the return it earns on investments and the interest credited to the contract holder's account, less expenses. The fixed annuity portfolio could be impacted by the continued low interest rate environment as lower crediting rates could result in increased surrenders and lower sales if customers seek alternative investment opportunities.

Approximately 50 per cent (2011: 48 per cent) of the interest sensitive fixed annuities Jackson wrote in 2012 provide for a market value adjustment that could be positive or negative, on surrenders in the surrender period of the policy. This formula-based adjustment approximates the change in value that assets supporting the product would realise as interest rates move up or down. The minimum guaranteed rate is not affected by this adjustment.

Fixed Indexed Annuities

Fixed indexed annuities (FIA) accounted for 7 per cent (2011: 7 per cent) of total new business premiums in 2012 and 8 per cent (2011: 9 per cent) of Jackson's policy and contract liabilities. Fixed indexed annuities vary in structure, but generally are deferred annuities that enable the contract holder to obtain a portion of an equity-linked return (based on participation rates and caps) but provide a guaranteed minimum return. These guaranteed minimum rates are generally set at 1.0 to 3.0 per cent on indexed funds. Jackson had fixed indexed annuities allocated to indexed funds totalling £5.6 billion (US$9.2 billion) (2011: £5.0 billion (US$7.8 billion)) in account value with minimum guaranteed rates on indexed accounts ranging from 1.0 per cent to 3.0 per cent and a 1.82 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 1.76 per cent average guarantee rate). Jackson also offers fixed interest accounts on some fixed indexed annuity products. Fixed interest accounts on fixed indexed annuities totalled £1.5 billion (US$2.3 billion) (2011: £1.4 billion (US$2.1 billion)) in account

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value with minimum guaranteed rates ranging from 1.0 per cent to 3.0 per cent and a 2.53 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 2.50 per cent average guarantee rate).

Jackson's profit arises from the investment income earned and the fees charged on the contract, less the expenses incurred, which include the costs of hedging the equity component of the interest credited to the contract. Fixed index annuities are subject to early surrender charges for the first five to 12 years of the contract. During the surrender charge period, the contract holder may cancel the contract for the surrender value.

Jackson hedges the equity risk return on fixed indexed products using futures and options linked to the relevant index as well as through offsetting equity exposure in the VA product. The cost of the hedges is taken into account in setting the index participation rates or caps. Jackson bears the investment and surrender risk on these products.

Immediate Annuities

In 2012, immediate annuities accounted for less than one per cent (2011: less than one per cent) of total new business premiums and one per cent (2011: one per cent) of Jackson's policy and contract liabilities. Immediate annuities guarantee a series of payments beginning within a year of purchase and continuing over either a fixed period of years and/or the life of the contract holder. If the term is for the life of the contract holder, then Jackson's primary risk is mortality risk. This product is generally used to provide a guaranteed amount of income for contract holders and is used both in planning for retirement and in retirement itself. The implicit interest rate on these products is based on the market conditions that exist at the time the policy is issued and is guaranteed for the term of the annuity.

Variable Annuities

In 2012, variable annuities accounted for 86 per cent (2011: 87 per cent) of total new business premiums and 60 per cent (2011: 63 per cent) of Jackson's policy and contract liabilities. Variable annuities are deferred annuities that have the same tax advantages and payout options as interest-sensitive and fixed indexed annuities. They are also used for asset accumulation in retirement planning and to provide income in retirement.

The contract holder can allocate the premiums between a variety of variable sub-accounts with a choice of fund managers and/or a guaranteed fixed interest rate option. The contract holder's premiums allocated to the variable accounts are held apart from Jackson's general account assets, in a separate account, which is analogous to a unit-linked fund. The value of the portion of the separate account allocated to variable sub-accounts fluctuates with the underlying investments. Variable annuities are subject to early surrender charges for the first four to nine years of the contract. During the surrender charge period, the contract holder may cancel the contract for the surrender value. Jackson also offers a variable annuity and an option on another variable annuity that has no surrender charge.

At 31 December 2012, Jackson had fixed interest rate accounts within variable annuities totalling £4.3 billion (US$7.0 billion) (2011: £4.3 billion (US$6.7 billion)) in account value with minimum guaranteed rates ranging from 1.0 per cent to 3.0 per cent and a 1.89 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 1.99 per cent average guaranteed rate).

Jackson offers a choice of guaranteed benefit options within its variable annuity product portfolio, which customers can elect and pay for. These include the guaranteed minimum death benefits ('GMDB'), which guarantee that, upon death of the owner, the beneficiary receives a minimum value regardless of past market performance. These guaranteed death benefits might be expressed as the return of original premium, the highest past anniversary value of the contract, or as the original premium accumulated at a fixed rate of interest. In addition, there are three other types of guarantees: guaranteed minimum

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withdrawal benefits ('GMWB'), guaranteed minimum accumulation benefits ('GMAB') and guaranteed minimum income benefits ('GMIB'). GMWBs provide a guaranteed return of the principal invested by allowing for periodic withdrawals that are limited to a maximum percentage of the initial premium. One version of the GMWBs provides for a minimum annual withdrawal amount that is guaranteed for the contract holder's life without annuitisation. GMABs generally provide a guarantee for a return of a certain amount of principal after a specified period. This benefit was eliminated from Jackson's product offerings in 2011. GMIBs provide for a minimum level of benefits upon annuitisation regardless of the value of the investments underlying the contract at the time of annuitisation. Jackson no longer offers GMIBs, with existing coverage being reinsured with an unaffiliated reinsurer.

As the investment return on the separate account assets is attributed directly to the contract holders, Jackson's profit arises from the fees charged on the contracts, less the expenses incurred, which include the costs of hedging and eventual payment of benefits guarantees. In addition to being a profitable book of business in its own right, the variable annuity book also provides an opportunity to utilise the offsetting equity risk among various lines of business to effectively manage Jackson's equity exposure. Jackson believes that the internal management of equity risk coupled with the utilisation of external derivative instruments where necessary, continues to provide a cost-effective method of managing equity exposure.

Profits in the variable annuity book of business will continue to be subject to the impact of market movements on both sales and allocations to the variable accounts and the effects of the economic hedging programme. Hedging is conducted based on an economic approach so, the nature and duration of the hedging instruments, which are recorded at fair value through the income statement, will fluctuate and produce some accounting volatility.

In March 2012, Jackson launched a new variable annuity product, Elite Access, which has no guaranteed benefits and provides tax efficient access to alternative investments. This product has received a positive reaction from distributors and Jackson is optimistic about the future of the Elite Access product and will continue to drive product innovation as a way of both meeting the needs of its customers and driving shareholder value.

Aggregate distribution of account values

The table below shows the distribution of account values for fixed annuities (interest-sensitive and fixed indexed) and variable annuities within the range of minimum guaranteed interest rates as described above as at 31 December 2012 and 2011:

	Account value	
	2012	**2011**
	£m	**£m**
Minimum guaranteed interest rate annuities		
1.0%	**2,534**	1,988
> 1.0% 2.0%	**8,374**	8,321
> 2.0% 3.0%	**9,174**	9,352
> 3.0% 4.0%	**1,236**	841
> 4.0% 5.0%	**1,518**	1,425
> 5.0% 5.5%	**209**	167
Total	**23,045**	22,094

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Life Insurance

Background

Reflecting the competitive life insurance market and the overall trend towards asset accumulation products, Jackson's life insurance products accounted for less than 1 per cent (2011: less than 1 per cent) of the total new business premiums and 15 per cent (2011: 7 per cent) of Jackson's policy and contract liabilities in 2012. The increase in policy and contract liabilities and the distribution of account values within a range of minimum guaranteed interest rates as shown below was a result of the acquisition of REALIC. Jackson discontinued new sales of life insurance products effective 1 August 2012. Previously, Jackson sold several types of life insurance, including term life, universal life and variable universal life. Term life provides protection for a defined period and a benefit that is payable to a designated beneficiary upon death of the insured. Universal life provides permanent individual life insurance for the life of the insured and includes a savings element. Variable universal life is a type of life insurance policy that combines death benefit protection with the ability for the contract holder account to be invested in separate account funds. Jackson's life insurance book has delivered consistent profitability, driven primarily by positive mortality and persistency experience.

Aggregate distribution of account values

At 31 December 2012, Jackson had interest sensitive life business in force with a total account value of £6.0 billion (US$9.7 billion) (2011: £3.3 billion (US$5.1 billion)), with minimum guaranteed interest rates ranging from 2.5 per cent to 6.0 per cent with a 4.67 per cent average guaranteed rate (2011: 3.0 per cent to 6.0 per cent with a 4.88 per cent average guaranteed rate). The table below shows the distribution of the interest-sensitive life business account values within this range of minimum guaranteed interest rates as at 31 December 2012 and 2011:

	Account value	
	2012	**2011**
	£m	**£m**
Minimum guaranteed interest rate interest sensitive life business		
> 2.0% 3.0%	**183**	130
> 3.0% 4.0%	**2,141**	1,145
> 4.0% 5.0%	**2,097**	686
> 5.0%	**1,550**	1,317
Total	**5,971**	3,278

Institutional Products

Institutional products consist of traditional guaranteed investment contracts ('GICs'), funding agreements (including agreements issued in conjunction with Jackson's participation in the US Federal Home Loan Bank of Indianapolis ('FHLBI') programme) and medium-term note funding agreements. In 2012, institutional products accounted for three per cent (2011: two per cent) of total new business premiums and three per cent (2011: 4 per cent) of Jackson's policy and contract liabilities. Jackson sold no institutional products during 2010, as available capital was directed to support higher margin variable annuity sales. In 2012 and 2011, Jackson re-entered the institutional market on a limited and selective basis, taking advantage of high returns available at particular times during the year. The GICs are marketed by the institutional products department to defined contribution pension and profit sharing retirement plans. Funding agreements are marketed to institutional investors, including corporate cash accounts and securities lending funds, as well as money market funds, and are issued to the FHLBI in connection with its programme.

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Traditional Guaranteed Investment Contracts

Under a traditional GIC, the contract holder makes a lump sum deposit. Interest is paid on the deposited funds, usually on a quarterly basis. The interest rate paid is fixed and is established when the contract is issued.

Traditional GICs have a specified term, usually two to three years, and typically provide for phased payouts. Jackson tailors the scheduled payouts to meet the liquidity needs of the particular retirement plan. If deposited funds are withdrawn earlier than scheduled, an adjustment is made that approximates a market value adjustment.

Jackson sells GICs to retirement plans, in particular 401(k) plans. The traditional GIC market is extremely competitive. This is due in part to competition from synthetic GICs, which Jackson does not sell.

Funding Agreements

Under a funding agreement, the contract holder either makes a lump sum deposit or makes specified periodic deposits. Jackson agrees to pay a rate of interest, which may be fixed but which is usually a floating short-term interest rate linked to an external index. Interest is paid quarterly to the contract holder. The average term for the funding agreements is one to two years. At the end of the specified term, contract holders may re-deposit the principal in another funding agreement. Jackson makes its profit on the spread between the yield on its investments and the interest rate credited to contract holders.

Typically, brokerage accounts and money market mutual funds are required to invest a portion of their funds in cash or cash equivalents to ensure sufficient liquidity to meet their customers' requirements. The funding agreements permit termination by the contract holder on seven to 90 days notice, and thus qualify as cash equivalents for the clients' purposes. In 2012 and 2011, there were no funding agreements terminable by the contract holder with less than 90 days notice.

Jackson is a member of the FHLBI. Membership allows Jackson access to advances from FHLBI that are collateralised by mortgage related assets in Jackson's investment portfolio. These advances are in the form of funding agreements issued to FHLBI.

Medium Term Note Funding Agreements

Jackson has also established European and global medium-term note programs. The notes offered may be denominated in any currency with a fixed or floating interest rate. Notes are issued to institutional investors by a special purpose vehicle and are secured by funding agreements issued by Jackson. Although Jackson has these programs in-force, there have been no new sales since 2008.

Distribution and Marketing

Jackson distributes products in all 50 states of the United States and in the District of Columbia, although not all products are available in all states. Operations in the state of New York are conducted through a New York insurance subsidiary. Jackson markets its retail products primarily through advice based distribution channels, including independent agents, independent broker-dealer firms, regional broker-dealers, and wirehouses, banks and registered investment advisors. Through August 2012, Jackson also marketed life insurance and fixed annuity products through its captive insurance agency.

Jackson focuses on independent distribution systems and supports its network of independent agents and advisers with education and training programs.

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Independent Agents and Broker Dealers

Jackson's subsidiary, Jackson National Life Distributors, LLC ('JNLD'), is the primary marketing and distribution organisation for Jackson's annuities. The annuity products are distributed through independent agents located throughout the United States. These approximately 20,000 appointed insurance agents or brokers at 31 December 2012, who also may represent other companies, are supported with marketing materials and multimedia presentations to help advisers choose the right solutions for their clients' individual financial situations. JNLD generally deals directly with writing agents and brokers thereby eliminating intermediaries, such as general agents. This distribution channel has enabled Jackson to generate significant volumes of business on a low, variable cost basis.

JNLD's wholesalers meet directly with independent broker dealers and financial planners and are supported by an extensive internal sales staff. At 31 December 2012, Jackson had active selling agreements with independent broker dealer organisations throughout the United States providing access to more than 58,900 appointed agents. Jackson provides training for its broker dealers and also provides them with product information and sales materials.

Regional Broker Dealers

JNLD's Regional Broker Dealer ('RBD') team provides dedicated service and support to regional brokerage firms and wirehouses. Regional broker dealers are a hybrid between independent broker dealers and wirehouses. Like representatives who work for wirehouses, financial representatives at regional broker dealers are actual employees of the firm. However, unlike wirehouses, RBD firms have limited institutional investment banking services. The RBD team develops relationships with regional firms throughout the US and provides customised materials and support to meet their specialised advisory needs.

Jackson's RBD team also provides support for the wirehouse channel, which produced £1.8 billion of premium in 2012.

Jackson's RBD team supports more than 33,800 representatives in regional broker dealers and wirehouses.

Banks, Credit Unions and Other Financial Institutions

Jackson's Institutional Marketing Group distributes annuity products through banks, credit unions and other financial institutions and through third party marketing organisations that serve these institutions. Jackson is a leading provider of annuities offered through banks and credit unions and at 31 December 2012 had access to more than 33,200 financial institution representatives through existing relationships with banks and credit unions. Jackson has established distribution relationships with medium sized regional banks, which it believes are unlikely to develop their own insurance product capability.

Independent Broker Dealers

Jackson's retail distribution is managed by Prudential's independent broker dealer network, NPH, which is described in more detail above. NPH had 3,540 registered representatives at the end of 2012.

Institutional Products Department

Jackson markets its institutional products through its institutional products department. It has direct contacts with banks, municipalities, asset management firms and direct plan sponsors. Institutional products are distributed and marketed through intermediaries to these groups.

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Captive Agency

In connection with the acquisition of Life of Georgia in 2005, Jackson established the JNL Southeast Agency ('JNLSA'), the company's first captive agency since 1970. JNLSA was formed to help retain the Life of Georgia book of business and to create a new distribution channel for Jackson's life insurance. In conjunction with Jackson's withdrawal from retail life insurance sales, this agency was terminated in 2012.

Registered Investment Adviser

As described above Curian Capital, LLC is Jackson's registered investment adviser channel.

The registered investment adviser industry began as a service offered to very high net worth investment clients, focusing on platforms rather than specific products, and providing institutional quality management, custom portfolios and tax services. The industry has evolved to offer personalised investment advice, high-quality money management, good returns and reasonable costs to a broader range of clients.

Curian's sales, not included in Jackson's premiums and deposits, totalled £1,550 million and £1,684 million in 2012 and 2011, respectively.

Factors Affecting Pricing of Products and Asset Liability Management

Jackson prices products based on assumptions about future mortality, investment yields, expenses and persistency. Pricing is influenced by its objectives for return on capital and by competition. Although Jackson includes a profit margin in the price of its products, the variation between the assumptions and actual experience can result in the products being more or less profitable than it was assumed they would be. This variation can be significant.

Jackson designs its interest sensitive products and conducts its investment operations to match closely the duration of the assets in its investment portfolio with the duration of the annuity, term life, whole life, universal life and guaranteed investment contract product obligations. Jackson seeks to achieve a target spread between what it earns on its assets and what it pays on its liabilities by investing principally in fixed-rate securities and in options and futures to hedge equity related movements in the value of its products.

Jackson segregates its investment portfolio for certain investment management purposes, and as part of its overall investment strategy, into four portfolios: life and fixed annuities without market value adjustment, fixed annuities with market value adjustment, fixed index annuities and institutional liabilities. The portfolios backing life and fixed annuities with and without market value adjustments and the fixed index annuities have similar characteristics and differ primarily in duration. The portfolio backing the institutional liabilities has its own mix of investments that meet more limited duration tolerances. Consequently, the institutional portfolio is managed to permit less interest rate sensitivity and has limited exposure to mortgage backed securities. At 31 December 2012, 4 per cent of the institutional portfolio was invested in residential mortgage backed securities.

The fixed-rate products may incorporate surrender charges, market value adjustments, two-tiered interest rate structures or other limitations relating to when policies can be surrendered for cash, in order to encourage persistency. As of 31 December 2012, 70 per cent of Jackson's fixed annuity reserves had surrender penalties or other withdrawal restrictions. Substantially all of the institutional portfolio had withdrawal restrictions or market value adjustment provisions.

Fixed index annuities issued by Jackson also include an equity component that is hedged using equity options and futures contracts issued on the corresponding exchange. The equity component of

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these annuities constitutes an embedded derivative under IAS 39 'Financial Instruments: Recognition and Measurement' that is carried at fair value, as are other derivative instruments.

Guaranteed benefits issued by Jackson in connection with the sales of variable annuity contracts expose Jackson to equity risk as the benefits generally become payable when equity markets decline and contract values fall below the guaranteed amount. As discussed previously, certain of these benefits are carried at fair value under IAS 39 with changes in fair value recorded in income. Jackson hedges the tail risk associated with the equity exposure using equity options and futures contracts, which are also carried at fair value under IAS 39. Jackson hedges the economic risk associated with these contracts and, therefore, has not explicitly hedged its fair value risk. In addition, certain benefits have mortality risk and are therefore precluded from being carried at fair value. As a result of these factors, the income statement may include a timing mismatch related to changes in fair value. However, as demonstrated during the economic crisis, subsequent rebound and recent volatility in the equity markets, Jackson's hedges have effectively operated as designed.

Reserves

Except for certain non-insurance deposit-type accounts and as allowed under IFRS, Jackson uses reserves established on a grandfathered US GAAP basis as the basis for consolidation into Prudential's IFRS accounts.

For the fixed and variable annuity contracts and institutional products, the reserve is the contract holder's account value. For the immediate annuities, reserves are determined as the present value of future policy benefits. Mortality assumptions are based on the 1983 Individual Annuitant Mortality Table and the Annuity 2000 Mortality Table for newer issues. Interest rate assumptions currently range from one per cent to five and a half per cent.

The IFRS accounting for guarantees on Jackson's variable annuity contracts has a mixed measurement approach. GMWB 'not for life' contract features are fair valued under IAS 39 and current US GAAP, with a capping feature to prevent early anticipation of expected fees for guarantees. However, the GMDB and GMWB 'for life' blocks of business are accounted for under grandfathered US GAAP which does not, and is not intended to, fair value the liabilities.

For the traditional term life contracts, reserves for future policy benefits are determined using assumptions as to mortality, interest, policy persistency and expenses. Mortality assumptions are generally from 25 per cent to 160 per cent of the 1975-1980 Basic Select and Ultimate tables, depending on underwriting classification and policy duration. Interest rate assumptions range from two and one half per cent to six per cent. Persistency and expense assumptions are based on Jackson's experience.

For the interest sensitive and single premium life contracts, reserves approximate the contract holder's account value.

Reinsurance

Jackson reinsures portions of the coverage provided by its life insurance products with other insurance companies under agreements of indemnity reinsurance. Indemnity reinsurance agreements are intended to limit a life insurer's maximum loss on a large or unusually hazardous risk or to obtain a greater diversification of risk for the life insurer. Indemnity reinsurance does not discharge the original insurer's primary liability to the insured. Jackson's reinsured business is ceded to numerous unaffiliated reinsurers and the amount of reserves ceded to any one reinsurer is not material to Jackson's overall financial position. Typically, the reinsurers have an AM Best Co rating of A or higher.

As a condition to the REALIC acquisition and after receipt of all required regulatory approvals, REALIC entered into three retrocession reinsurance agreements with Swiss Re. Pursuant to these

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reinsurance agreements, REALIC ceded to Swiss Re on a 100 per cent coinsurance basis certain blocks of business written or assumed by REALIC. The effective date of the three retrocession agreements was 1 July 2012. In addition and pursuant to these reinsurance agreements, Jackson holds certain assets, primarily in the form of policy loans and fixed maturities, as collateral. This collateral is reported as a funds held liability.

At 31 December 2012, Jackson's largest amount ceded to one reinsurer totalled £4.3 billion, which is primarily related to the retrocession reinsurance arrangements.

Jackson typically ceded 90 per cent of level premium term products. Jackson discontinued new sales of life insurance products effective 1 August 2012.

Jackson ceded the guaranteed minimum income benefit on variable annuities to an unaffiliated reinsurer.

Policy administration

Jackson provides a high level of administrative support for both new and existing contract holders. Jackson's ability to implement new products quickly and provide customer service is supported by integrated computer systems that issue and administer complex life insurance and annuity contracts. Jackson continues to develop its fixed and variable annuity administration systems to enhance the service capabilities for both new and existing policies. The REALIC business is currently administered by several third party administrators.

PPM America

PPM America (PPMA) is Prudential's US fund management operation, with offices in Chicago and New York. PPMA manages assets for Prudential's US, UK and Asian affiliates. PPMA also provides other affiliated and unaffiliated institutional clients with investment services including collateralised debt obligations (CDOs), private equity funds, institutional accounts, and mutual funds. PPMA's strategy is focused on managing existing assets effectively, maximising the benefits derived from synergies with our international asset management affiliates, and leveraging investment management capabilities across the Group. PPMA also pursues third-party mandates on an opportunistic basis.

UK Business

Introduction

As at 31 December 2012, Prudential's UK business was structured into two business units, each focusing on its respective target customer markets. The Prudential's UK business units are Prudential UK (being the insurance operations) and M&G (being the asset management business).

In 2012, Prudential's UK business generated new business insurance premiums of £6,495 million and gross investment inflows of £34,464 million. As at 31 December 2012, M&G had £228 billion of funds under management.

Prudential UK business overview

The Life & Pensions market in the UK is mature and highly regulated. Significant regulatory change occurred in 2012 with the implementation of the Retail Distribution Review, Gender Neutral Pricing and Auto-enrolment for company pension schemes.

The UK market is also characterised by an ageing population and a concentration of wealth in the 50+ age group, many of whom have built up substantial pension funds in employer-sponsored schemes. These customers require help to convert wealth into sustainable lifetime income. For the next generation of savers, the responsibility for retirement provision has shifted substantially away from government and

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employers towards the individual. These customers are typically under-funded for retirement and this creates a significant need for long term savings and retirement income products.

Prudential UK's longevity experience, multi-asset investment capabilities, strong brand and financial strength mean that we are strongly positioned to help consumers translate their accumulated wealth into the provision of dependable retirement income through our range of market leading with-profits and annuity products.

We do so by competing on a selective basis in the UK's retirement savings and income market, with a focus on writing profitable new business combined with sustainable cash generation and capital preservation, rather than pursuing top-line sales growth.

Prudential UK has a well-established individual annuity business, built on a robust pipeline of internal vestings from maturing pension policy customers. The internal vestings pipeline is supplemented by sales through intermediaries and strategic partnerships with third parties where Prudential is the offered annuity provider for customers vesting their pensions at retirement.

The combined financial strength and investment performance track record of Prudential's UK With-Profits Fund continues to provide a key source of non-price differentiation in a competitive market. Our with-profits customers benefit from the security of Prudential's large inherited estate, which was valued at £7 billion at the year-end, and provides a high degree of protection against adverse market movements. The Fund continues to provide customers with solid returns and to out-perform the FTSE All-Share Index over medium to long-term horizons. Over the last 15 years, the Fund has delivered a cumulative investment return of 184.3 per cent on investments covering policyholder liabilities. This compares favourably with other with-profits funds and the FTSE All-Share Index total return of 106.5 per cent over the same period, and, by offering customers a smoothed return, helps provide protection from the full impact of volatile market conditions. This performance shows that investing in a strong with-profits fund can produce good returns for cautious investors, in spite of the combined pressures of volatile market conditions and UK interest rates remaining at historically low levels.

Retention and management of our customer base of approximately 7 million remains a key focus for the business. We aim to maintain loyalty by continuing to improve our service year on year for both customers and intermediaries. Prudential UK's focus on continuing to deliver excellent customer service was recognised at the 2012 Financial Adviser Service Awards, where we retained our two 5-Star ratings in the Life & Pensions and Investment categories.

In 2010, Prudential UK met its cost savings target of £195 million per annum and announced further cost saving initiatives to reduce costs by £75 million per annum on a consistent basis by the end of 2013. By 31 December 2012, annual cost savings of £75 million per annum had been achieved, which was one year earlier than originally planned.

UK Products and profitability

In common with other UK long-term insurance companies, Prudential UK's products are structured as either with-profits (or participating) products, or non-participating products including annuities in payment and unit-linked products. Depending on the structure, the level of shareholders' interest in the value of policies and the related profit or loss varies.

With-profits policies are supported by a with-profits sub-fund and can be single premium (for example, Onshore Bonds) or regular premium (for example, certain pension products). Prudential UK's primary with-profits sub-fund is part of The Prudential Assurance Company Limited (PAC)'s long-term fund. The return to shareholders on virtually all Prudential UK's with-profits products is in the form of a statutory transfer to PAC shareholders' funds. This is analogous to a dividend from PAC's long-term fund, and is dependent upon the bonuses credited or declared on policies in that year. Prudential's with-profits policyholders currently receive 90 per cent of the distribution from the main with-profits

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sub-fund as bonus additions to their policies, while shareholders receive 10 per cent as a statutory transfer.

The Defined Charge Participating Sub-Fund (DCPSF) forms part of the PAC long-term fund. It comprises the accumulated investment content of premiums paid in respect of the defined charge participating with-profits business issued in France and the defined charge participating with-profits business reassured into PAC from Prudential International Assurance plc and Canada Life (Europe) Assurance Ltd. It also includes the portfolio of with-profits annuity policies acquired from Equitable Life in 2007. All profits in this fund accrue to policyholders in the DCPSF.

The profits from almost all of the new non-participating business accrue solely to shareholders. Such business is written in the non-profit sub-fund within PAC's long-term fund, or in various shareholder-owned direct or indirect subsidiaries. The most significant of these is Prudential Retirement Income Limited (PRIL), which writes conventional annuities including all new conventional annuities arising from vesting deferred annuity and personal pension policies in the with-profits sub-fund of PAC. There is also a substantial volume of in-force non-participating business in PAC's with-profits sub-fund and that fund's wholly owned subsidiary Prudential Annuities Limited (PAL), which is closed to new business. Profits from this business accrue to the with-profits sub-fund (WPSF). On 31 October 2012, we reinsured substantively all of the long-term insurance business of PAL to the WPSF.

The traditional life insurance product offered by UK life insurance companies was a long-term savings product with a life insurance component. The life insurance element conferred tax advantages that originally distinguished the traditional life insurance products offered in the United Kingdom from the savings products offered by banks, building societies and unit trust companies. The gradual reduction of these tax advantages and increasing sales of single premium life products has resulted in the distinction between life insurance and other long-term savings products becoming less important. Pension products remain tax-advantaged within certain limits.

Further information on the UK products is provided below under 'UK Business Units Long term products'.

Distribution

Retail financial services products are distributed face to face through independent financial advisers (IFAs) and restricted advisers, or directly by mail, telephone and over the internet. IFAs dominate the advice market and offer products from a range of insurance companies selected from the whole of the market. Restricted advisers do not need to select from the whole market and are typically tied to a single insurer or a small panel of insurers. Direct and e-commerce distribution methods are generally non-advised and therefore operate on a lower-cost basis than other distribution channels. Accordingly, products distributed directly are generally more straightforward and aimed at more simple financial planning needs.

The FSA's review of the retail distribution marketplace called the Retail Distribution Review ('RDR') came into force on 31 December 2012. One of the main aims of the RDR was to increase the level of professionalism within the financial advice market. Prudential supports this aim.

The changes implemented increase the clarity with which advisory firms describe their services and charges. They stipulate that the adviser must be paid by the customer. Providers are no longer permitted to pay commission on new sales of retail investment products. Comparable rules have been introduced for group pensions business. Sales of protection business and general insurance can still attract commission. The changes have also significantly increased the requirements for firms who seek to describe themselves as independent. Major advisory firms have launched restricted advice models and the popularity of this model is expected to grow.

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A significant feature of the UK retail marketplace over the past decade has been the growth of investment platforms. From an initial concept of providing easy access for consumers and advisers to open ended investment companies (OEICs) from a range of fund managers, many models have been developed into distribution-led propositions with the objective of capturing total business flows from adviser firms, across various products.

As a result, in parallel to the overall RDR, the FSA has been paying specific attention to the role of platforms and in June 2012 published a consultation paper proposing a ban on the payment of rebates from fund managers to platforms and reconfirming their intention to introduce a ban on the payment of cash rebates to customers. The FSA acknowledged that such proposals could not be implemented at the same time as the RDR and indicated the most likely date for the implementation of these new platform rules would be 31 December 2013. A policy statement confirming the outcome of the FSA's review on platforms and introducing corresponding rules is currently expected during the second quarter of 2013.

The full impact of the RDR remains uncertain. As expected, FSA figures confirm that some IFAs chose to exit the market on the introduction of the new rules. Increasingly, others are expected to seek partnership arrangements with product providers through restricted advice models. Prudential is well placed to participate in such arrangements with partnerships already in place with a number of major advice firms

A large proportion of Prudential UK's annuity sales are made direct on a non-advised basis and will be largely unaffected by the RDR.

Prudential UK is continuing to work with the regulator, industry bodies and distributors on ways to help advisers make the transition to the new environment as it believes that a strong adviser sector is beneficial for the market, and for Prudential.

In 2010-2012, Prudential UK's new business premiums by channels are as follows:

	Year Ended 31 December		
	2012	2011	2010
	£m	£m	£m
Individual Annuities:			
Direct & Partnerships	**297**	328	593
Intermediated	**653**	241	221
Internal Vesting*	**1,456**	1,223	1,235
Total Individual Annuities	**2,406**	1,792	2,049
Other Products:			
Direct & Partnerships	**642**	654	588
Intermediated	**2,922**	2,244	2,215
Wholesale	**408**	336	945
Total Other Products	**3,972**	3,234	3,748
DWP Rebates	**115**	104	113
Total New Business Premiums	**6,493**	5,130	5,910

* Internal vesting business is classified as new business where the contracts include an open market option.

Direct and Partnerships

The direct distribution channel is primarily charged with increasing revenue from existing Prudential UK customers and retention of our existing customer base. Direct distribution channels include the telephone, mail and internet, and focus on annuities, investments, protection and health products.

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In December 2011 Prudential UK launched a direct advice service, Prudential Financial Planning (PFP). PFP offers a complete financial planning service, focused primarily on existing customers who originally came to Prudential through its direct sales force. Starting with 25 advisers recruited at the end of 2011, Prudential has steadily increased the scale of the channel through 2012; and as at 31 December 2012 it had grown to 129 advisers.

In March 2013, the ABI code of conduct on retirement choices, to which Prudential has committed, came into force. The code is designed to help customers make the most appropriate choices at retirement. Prudential's direct channel will support the requirements of the code for its pension customers.

Partnerships are primarily arrangements with other insurers whereby we offer our annuity products to their vesting pension customers.

Intermediaries

In 2012 Prudential UK consolidated its position with major intermediary firms and significantly increased sales through this channel in a challenging market. Alongside this, Prudential UK worked closely with its distribution partners in the development of their business models for the post-RDR environment and is well placed to support the new emerging models which distributors have introduced to deal with the RDR requirements.

Wholesale

In the Wholesale market, Prudential UK's aim is to continue to participate selectively in bulk and back-book buyouts using its financial strength, superior investment track record, annuitant mortality risk assessment and servicing capabilities. In line with this opportunistic approach, two bulk annuity buy-in insurance agreements were signed in 2012 totalling £408 million of new business premiums. Prudential UK will continue to maintain a strict focus on value and only participate in capital-efficient transactions that meet its return on capital requirements.

UK Business Units

Long-term Products

Prudential's long-term products in the United Kingdom consist of life insurance, pension products and pensions annuities. The following table shows Prudential UK's new business insurance and investment premiums by product line for the periods indicated. New business premiums include deposits for policies with limited or no life contingencies. Prudential UK also distributes life insurance products, primarily investment bonds, in other European countries. The volume of such business is relatively small and is included in the table below.

	Year Ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Pension annuities	**2,406**	1,792	2,049
Corporate pensions	**459**	399	426
Onshore bonds	**2,276**	1,779	1,660
Other products	**946**	824	830
Wholesale	**408**	336	945
Total new business premiums	**6,495**	5,130	5,910

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Of the total new business premiums of £6,493 million (2011: £5,130 million; 2010: £5,910 million), £6,286 million (2011: £4,871 million; 2010: £5,656 million) were single premiums and £207 million (2011: £259 million; 2010: £254million) were regular premiums.

Pension Annuities

Prudential UK offers individual conventional immediate annuities that are either fixed or retail price indexed (referred to as 'RPI'), where annuity payments are guaranteed from the outset, or with-profits annuities, where annuity payments are variable dependent on the investment performance of underlying assets.

A total of £2,406 million of individual annuities were sold in 2012. Of this total, £1,456 million was sold through internal vesting, that is existing Prudential UK customers with maturing pension policies. The other £950 million were sold to new customers, typically individuals with a pension maturing with another provider who chose Prudential UK to provide their annuity. Prudential UK's immediate annuity products provide guaranteed income for a specified time, usually the life of the policyholder, in exchange for a lump sum capital payment. No surrender value is available under any of these products. The primary risks to Prudential UK from immediate annuity products, therefore, are mortality improvements and credit risk.

Conventional Annuities

Prudential UK's conventional annuities include level (non-increasing), fixed increase and RPI annuities. Prudential UK's fixed increase annuities incorporate automatic increases in annuity payments by fixed amounts over the policyholder's life. The RPI annuities provide for a regular annuity payment to which an additional amount is added periodically based on the increase in the UK Retail Prices Index. In 2012, sales of RPI annuities were £122 million (including £111 million of bulk annuities). In 2012, sales of level and fixed increase conventional annuities amounted to £1,782 million (including £297 million of bulk annuities).

With-profits Annuities

Prudential UK's with-profits annuities combine the income features of annuity products with the investment smoothing features of with-profits products and enable policyholders to obtain equity-type returns over time. In 2009, Prudential UK launched the Income Choice Annuity, which allows customers to choose an income between a defined maximum and minimum level, with the option of re-setting this every two years. It also provides an opportunity for pension income to grow based on the returns of the with-profits fund. Through this product, Prudential UK brings its product development strengths to bear while also capitalizing on people's need for protection from inflation through increasingly long periods of retirement.

Prudential is one of only a few companies in the United Kingdom which are active in the with-profits annuities market and has been operating in this market since 1991. In 2012, Prudential UK's premiums for this business were £910 million. Prudential UK has a new business market share of 76 per cent in the first nine months of 2012[(7)].

Pension Products

Prudential UK provides both corporate and individual pension products. Corporate pension products are discussed below whilst individual pension products are discussed under 'Other Products'. Pension products are tax-advantaged long-term savings products that comply with rules established by the HM Revenue and Customs ('HMRC') and are designed to supplement state-provided pensions. These

(7) Source: ABI

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products provide policyholders with a number of options at retirement. Policyholders may elect to use part or all of their maturity benefits to purchase a pension annuity, they may choose to draw down funds without purchasing an annuity (subject to a number of rules and restrictions on the amount able to be drawn down each year), they may delay taking any benefits, or take a combination of these options. They are also permitted to take a portion as a tax-free lump sum. For drawdown products, the investment risk remains with the policyholder, payments are not guaranteed, and tend to cost more to administer. This means that the option to enter drawdown will tend to apply mainly to more sophisticated policyholders and to larger retirement funds. This, combined with the individual's own need for a secured income in retirement, means that in practice most policyholders are likely to purchase an annuity.

Prior to retirement, these products typically have minimal mortality risk to Prudential UK and are primarily considered investment products. An exception is where a guaranteed annuity option ('GAO') has been offered on the product, with an element of risk to Prudential UK both in underlying mortality and investment assumptions. Prudential UK ceased marketing GAOs in 1987, but for a minority of corporate pension schemes GAOs still apply for new members. Current liabilities for this type of business make up less than one per cent of the with-profits sub-fund as at 31 December 2012.

Many of the pension products Prudential UK offers are with-profits products or offer the option to have all or part of the contributions allocated to a with-profits fund. Where funds invested in the with-profits fund are withdrawn prior to the pension date specified by the policyholder, Prudential UK may apply a market value adjustment to the amount paid out. The remaining pension products are non-participating products, which include unit-linked products.

Corporate Pensions

There are two categories of corporate pension products: defined benefit and defined contribution. Prudential UK has an established defined benefit plan client base covering the small to medium-sized employer market. Prudential UK's defined contribution client base ranges from small unlisted companies to some of the largest companies in the United Kingdom as well as a number of clients in the public sector (in particular where Prudential UK offers the Additional Voluntary Contribution ('AVC') facility). Additional Voluntary Contribution plans enable employees to make additional pension contributions, either regularly or as a lump sum, to supplement their occupational pension plans. Prudential UK administers corporate pensions for over 600,000 scheme members sponsored by some of the UK's largest employers and has also built a very strong position in the provision of with-profits AVC arrangements. Prudential UK provides AVCs to 68 of the 99 Local Government Authorities in England & Wales.

Defined benefit plans and products have previously dominated the corporate pensions market in terms of funds under management. In recent years, however, most new plans established have been defined contribution products. In addition, there is an increasing trend among companies to close defined benefit plans to new members or to convert existing schemes from defined benefit to defined contribution in order to stabilise or reduce potential pension liabilities.

Prudential UK offers group unit-linked policies and with-profits policies to the corporate pensions market. Prudential UK's defined contribution products are AVC plans, Group Money Purchase plans, Group Personal Pension plans, Group Stakeholder Pension plans and Executive Pension plans.

In addition, Prudential UK has a Company Pension Transfer Plan (or 'Bulk S32'), designed to accept benefits from both defined benefit and defined contribution pension schemes which are winding up (ceasing to exist or being replaced by a new type of scheme). Prudential UK also has the facility to accept enhanced transfers from deferred members of a corporate's defined benefit pensions scheme into Prudential UK Personal Pension plan where the member has received advice from an independent financial adviser (often called an enhanced transfer value exercise).

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Onshore Bonds

Prudential UK offers customers a range of investment funds to meet different risk and reward objectives. Prudential UK's main onshore bond product wrapper is the Prudential Investment Plan ('PIP'). Through this plan, based on a single premium with no fixed term, customers have the option to invest in the with-profits fund through PruFund or in a range of unit-linked investment funds.

PIP also gives financial advisers the opportunity to choose from different external fund management groups and the flexibility to make changes to portfolio and asset allocation over time. In 2012, sales of the unit-linked option within on-shore bond wrappers, including PIP were £127 million.

Prudential Dynamic Portfolios, launched in 2010, offer advisers a choice of portfolio options to match a client's risk/reward profile as an alternative to building an individual portfolio.

Prudential UK offers a unitised and smoothed with-profits investment bond entitled PruFund, which is designed to provide increased transparency and smoothed investment returns to the customer with a choice of Cautious or Growth funds. PruFund also offers clients an optional guarantee on the initial investment with a term from six to ten years depending on the client's requirements. PruFund is available across Prudential UK's range of tax wrappers including individual pensions, income drawdown and onshore and offshore bonds. In 2012, total new business premiums attributable to PruFund, including new business through PIP, was £1,601 million.

With-profits bonds aim to provide capital growth over the medium to long term, and access to a range of investment sectors without the costs and risks associated with direct investment into these sectors. Capital growth for the policyholder on with-profits bonds apart from PruFund is achieved by the addition of reversionary or annual bonuses, which are credited to the bond on a daily basis from investment returns achieved within PAC's long-term with-profits fund, offset by charges and expenses incurred in the fund. A final bonus may also be added when the bond is surrendered. PruFund delivers growth through a published expected growth rate, updated quarterly, and a transparent formulaic smoothing mechanism. In contrast the capital return on unit-linked bonds directly reflects the movement in the value of the assets underlying those funds. When funds invested in PAC's long-term with-profits fund are either fully or partially withdrawn, PAC may apply a market value adjustment to the amount paid out.

The sales growth across Prudential UK's with-profits range has been achieved on the back of sustained strong investment performance in its Life Fund over a number of years, reflecting the benefits of its diversified investment policy. Prudential believes that this market will continue to see further growth as investors turn to trusted and financially strong brands and products offering an element of capital protection.

Other Products

Other products comprise individual pensions, income drawdown, offshore bonds, healthcare, life insurance and equity release mortgages.

Individual Pensions

Prudential UK's individual pension range offers unit-linked and unitized with-profits products, including products that meet the criteria of the UK government's stakeholder pension program.

The stakeholder pension is intended for individuals earning enough to be able to afford to make contributions to a pension but who are not currently doing so. The introduction of stakeholder pensions has had implications for, among other things, how Prudential UK designs, administers and charges for and distributes pension products. The most significant requirements involve capped charges and a low minimum contribution which must be accepted by the provider. The UK government has capped charges

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at 1.5 per cent per annum of the policyholder account balance for stakeholder pensions for the first ten years, decreasing to 1 per cent thereafter, which is below the charges on personal pension products previously offered by the UK pensions industry.

As of 2012, individuals who are not already in a pension scheme, who are over 21 and below retirement age and whose earnings are over a minimum amount have had to be automatically enrolled in a pension scheme by their employer, who will be required to make contributions. These requirements were applied first to larger employers and will be rolled out gradually to medium-sized and smaller employers.

Prudential UK also provides individual personal pension products through the DWP Rebate arrangement. Under this arrangement, individuals may elect to contract out of the UK's State Second Pension (referred to as 'S2P') which was previously known as State Earnings Related Pension Scheme, administered by the UK Department of Work and Pensions. If an individual elects to contract out, then he or she will designate a pension provider, such as Prudential UK. Premiums on products sold in this manner are paid through 'rebates' from the Department of Work and Pensions, which represent the amount that would be otherwise paid into S2P. Rebate amounts are invested to provide benefits to the individual. Premiums from Department of Work and Pensions Rebates are typically reported in the first quarter of each year. The option to contract out was removed from April 2012 and no further contributions will be received, although Prudential will continue to administer in-force policies.

Income Drawdown

Given the UK's historic requirement for compulsory annuitisation by a maximum age (removed completely in April 2011), an increasingly sophisticated consumer population, and the rising incidence of second careers and semi-retirement as a result of increasing longevity, the market has seen good growth in the 'bridge' between pensions and annuities through income drawdown products. These products help customers manage their pensions through the various stages of retirement, and also offer flexibility while providing potential for capital growth. In 2012, Prudential UK sold £110 million of income drawdown products.

Offshore Bonds

Prudential UK's offshore bond products are the Prudential International Investment Bond and the Prudential International Investment Portfolio offering clients access to a wide range of quoted UK investments. Prudential UK's offshore bond sales grew by 17 per cent to £310 million in 2012.

Healthcare

PruHealth was launched in 2004 as a private medical insurance provider and is backed by Prudential and Discovery of South Africa. PruHealth uses the Prudential brand and Discovery's expertise to build branded distribution and innovative product offerings in the private healthcare and protection markets. In August 2010, PruHealth acquired Standard Life Healthcare and as part of the transaction, Prudential UK reduced its shareholding in the combined PruHealth and PruProtect businesses from its previous level of 50 per cent to 25 per cent of the enlarged business.

Life Insurance Products

Prudential's UK life insurance products are predominantly pure protection (term) products, and include the PruProtect product sold through the joint venture with Discovery. PruProtect's product is focused around a core philosophy of helping people become healthier while protecting and improving the quality of their lives.

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Equity Release Mortgage

In November 2009, Prudential UK announced the decision to close its equity release operation to new business. Existing customers may, however, still draw down additional funds, subject to their overall borrowing limits.

Wholesale

Wholesale business comprises bulk annuities. Prudential UK offers bulk annuities selectively, whereby it manages the assets and accepts the liabilities of a company pension scheme. The volume of Prudential UK's bulk annuity sales is unpredictable as the business maintains a very strict focus on value and only participates in capital-efficient transactions that meet its return on capital requirements.

Reinsurance

In view of the size and spread of PAC's long-term insurance fund, there is little need for reinsurance to protect this business. Some limited reinsurance is maintained and treaties relating to annuities, critical illness, permanent health insurance, term insurance and certain unit-linked products are in place.

Reserves

In the United Kingdom, a life insurance company's reserve and other requirements are determined by its Board, with advice from its Actuarial Function Holder, subject to minimum reserve requirements. These minimum reserve requirements are established by the rules and guidance of the FSA.

The reserves are published in annual returns to the FSA. In practice, similar provisions are included in the life insurance company's statutory accounts with limited adjustments. The Actuarial Function Holder must pay due regard to the fair treatment of policyholders in making recommendations to the company's board. The Actuarial Function Holder is required to report directly to the FSA any serious concerns regarding the company's ability to treat its customers fairly.

Prudential UK's regulatory reserving for with-profits products, as required by UK regulation, takes into account annual bonuses/annual interest credited to policyholders because these are 'attached' to the policies and are guaranteed. Realistic reserves are also calculated for with-profits products under UK regulation. These include an allowance for final bonuses based on the asset share or a prospective valuation of the policies and the cost of guarantees, smoothing and enhancements.

Prudential UK reserves for unit-linked products on the basis of the value of the unit fund and additional reserves are held for expenses and mortality where this is required by the contract design.

As well as the reserves, the company's assets must also cover other capital requirements set out in the FSA Prudential Sourcebook. These comprise a with-profits insurance capital component, which is a measure of the difference in the surplus assets on regulatory and realistic bases; a resilience capital requirement for entities other than PAC, which makes prudent allowance for potential future adverse movements in investment values; and the long-term insurance capital requirement, which must be held by all EU insurance companies. See 'Financial Strength of PAC's Long-term Fund' for further information on solvency and 'Realistic Financial Strength Reporting' for further information on realistic reporting.

Financial strength of PAC's with-profits fund

The PAC's with-profits fund is supported by a large inherited estate, with the free assets of the with-profits fund valued at approximately £7 billion (as at 31 December 2012), on a regulatory realistic basis. This provides the working capital required to support the fund for the long-term benefit of

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current and future policyholders. The strength of the with-profits fund offers strong policyholder protection and assists in generating positive returns for both policyholders and shareholders.

The table below shows the change in the investment mix of PAC's main with-profits fund:

	2012	**2011**	**2010**
	%	**%**	**%**
UK equities	**17**	24	26
International equities	**17**	10	13
Property	**12**	13	12
Fixed Interest	**44**	44	42
Cash and other asset classes	**10**	9	7
Total	**100**	100	100

Despite a low interest rate environment and continued volatile market conditions, the with-profits sub-fund earned a return of 10.5 per cent before tax in 2012 on investments covering policyholder liabilities. The with-profits sub-fund has delivered investment returns of 184.3 per cent over 15 years for policyholder asset shares in the fund, compared with the FTSE All-share index (total return) of 106.5 per cent over the same period (figures are to 31 December 2012, before tax and charges).

Realistic Financial Strength Reporting

In accordance with the FSA Prudential Sourcebook, PAC has to demonstrate solvency on a 'realistic' valuation basis as well as the regulatory basis. In the aggregate, the basis has the effect of placing a value on the liabilities of UK with-profits contracts that reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances.

This basis makes companies' financial health more transparent to policyholders, intermediaries and regulators alike, and enables more informed choices to be made by policyholders. The PAC long-term with-profits sub-fund is strong with the inherited estate (free assets) measured on a realistic basis, valued at approximately £7 billion at the end of 2012 before deduction for the risk capital margin.

In line with FSA requirements, PAC produces an Individual Capital Assessment ('Pillar II') which is an assessment of the economic capital required to ensure that there is a high likelihood that the company can meet its liabilities as they fall due.

Shareholders' Interests in Prudential UK's Long-term Insurance Business

In common with other UK long-term insurance companies, Prudential UK's products are structured as either with-profits products or non-participating (including unit-linked) products. With-profits policies are supported by a with-profits fund. Prudential UK's primary with-profits fund is part of PAC's long-term fund. For statutory and management purposes, PAC's long-term fund consists of a number of sub-funds in which shareholders and policyholders have varying interests.

With-profits Products

With-profits products provide an equity-type return to policyholders through bonuses that are 'smoothed'. There are two types of bonuses: 'annual' and 'final'. Annual bonuses, often referred to as reversionary bonuses, are declared once a year and, once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, final bonuses are only guaranteed until the next bonus declaration. Final bonuses are only credited on a product's maturity or surrender or on the death of the policyholder. Final bonuses can represent a substantial portion of the ultimate return to policyholders.

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With-profits products provide benefits that are generally either the value of the premiums paid, less charges and fees and with the addition of declared bonuses, or the guaranteed death benefit with the addition of declared bonuses. Smoothing of investment returns is an important feature of with-profits products. It is designed to reduce the impact of fluctuations in investment return from year to year and is accomplished predominantly through the level of final bonuses declared.

The return to Prudential's shareholders in respect of with-profits business Prudential UK writes is an amount equal to up to one-ninth of the value of the bonuses Prudential UK credits or declares to policyholders in that year. Prudential UK has a large block of in-force with-profits business with varying maturity dates that generates a relatively stable stream of shareholder profits from year to year.

PAC's board of directors, with the advice of its Actuarial Function Holder and its With-Profits Actuary, determines the amount of annual and final bonuses to be declared each year on each group of contracts.

When determining policy payouts, including final bonuses, PAC follows an actuarial practice of considering 'asset shares' for specimen policies. Asset shares broadly reflect the value of premiums paid in respect of a policy accumulated at the investment return on the assets PAC notionally attributes to the policy. In calculating asset shares, PAC takes into account the following items:

- the cost of mortality risk and other guarantees (where applicable),
- the effect of taxation,
- management expenses, charges and commissions,
- the proportion of the amount determined to be distributable to shareholders, and
- the surplus arising from surrenders, non-participating business included in the with-profits fund and other miscellaneous sources.

However, Prudential UK does not take into account the surplus assets of the long-term fund, or their investment return, in calculating asset shares. Asset shares are used in the determination of final bonuses together with treating customers fairly, the need to smooth claim values and payments from year to year and competitive considerations.

Prudential UK is required by UK law and regulation to consider the fair treatment of its customers in setting bonus levels. The concept of treating customers fairly is established by statute but is not defined. In practice, it provides one of the guiding principles for decision-making in respect of with-profits products.

The overall return to policyholders is an important competitive measure for attracting new business. The ability to declare competitive bonuses depends, in part, on the financial strength of PAC's long-term fund, enabling it to maintain high levels of investment in equities and real estate, if it wishes to do so. Equities and real estate have historically over the long-term provided a return in excess of fixed interest securities.

In 2012, PAC declared a total surplus of £2,210 million (2011: £2,293 million) from PAC's primary with-profits sub-fund, of which £1,990 million (2011: £2,064 million) was added to with-profits policies and £220 million (2011: £229 million) was distributed to shareholders. These amounts included annual bonus rates of 3.0 per cent for Prudence Bond and 3.0 per cent for personal pensions.

The closed Scottish Amicable Insurance Fund ('SAIF') declared total bonuses in 2012 of £541 million compared to £611 million in 2011. Shareholders have no interest in profits from the SAIF fund, although they are entitled to the investment management fees paid by this business. For greater detail on the SAIF fund, see 'The SAIF sub-fund and accounts' below.

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Surplus Assets in PAC's Long-term With-profits Fund

The assets of the main with-profits sub-fund within the long-term fund of PAC comprise the amounts that it expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the with-profits sub-fund is equal to the policyholders' accumulated asset shares plus any additional payments that may be required by way of smoothing or to meet guarantees. The balance of the assets of the with-profits sub-fund is called the 'inherited estate' and has accumulated over many years from various sources.

The inherited estate, as working capital, enables Prudential UK to support with-profits business by providing the benefits associated with smoothing and guarantees, by providing investment flexibility for the fund's assets, by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies. The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

Depletion of Surplus Assets and Shareholders' Contingencies

As a proprietary insurance company, PAC is liable to meet its obligations to policyholders even if the assets of the long-term funds are insufficient to do so. The assets, represented by the unallocated surplus of with-profits funds, in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers ('the excess assets') in the long-term funds could be materially depleted over time by, for example, a significant or sustained equity market downturn, costs of significant fundamental strategic change or a material increase in the pension mis-selling provision. In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the Group's ability to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

In 1998, Prudential UK stated that deducting personal pensions mis-selling costs from the inherited estate of the with-profits sub-fund would not impact Prudential UK's bonus or investment policy and it gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged. The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing.

The mis-selling review was completed on 30 June 2002 and the assurance has not applied to new business issued since 1 January 2004. New business in this context consists of new policies, new members to existing pension schemes plus regular and single premium top-ups, transfers and switches to existing arrangements. The maximum amount of capital support available under the terms of the assurance will reduce over time as claims are paid on the policies covered by it.

The bonus and investment policy for each type of with-profits policy is the same irrespective of whether or not the assurance applies. Hence removal of the assurance for new business has had no impact on policyholder returns and this is expected to continue for the foreseeable future.

During 2009, the FSA issued a policy statement confirming that certain payments of compensation and redress for events occurring after 31 July 2009 may only be paid from assets attributable to shareholders. As the pensions mis-selling review was concluded prior to this date, the requirements of the policy statement do not impact the provisions outlined above.

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The SAIF Sub-fund and Accounts

The SAIF sub-fund is a ring-fenced sub-fund of PAC's long-term fund and was formed following the acquisition of the mutual Scottish Amicable Life Assurance Society in 1997. No new business may be written in SAIF, although regular premiums are still being paid on policies in-force at the time of the acquisition and 'top-ups' are permitted on these policies.

This fund is solely for the benefit of those Scottish Amicable Life Assurance Society policyholders whose policies were transferred to SAIF. Shareholders have no interest in the profits of this fund, although they are entitled to the investment management fees paid on this business. The brand name and rights to profit on new business were transferred to a new Prudential UK subsidiary, Scottish Amicable Life plc, which operated for the benefit of shareholders.

SAIF with-profits policies contain minimum levels of guaranteed benefit to policyholders. In addition, as mentioned below, certain pensions products have guaranteed annuity rates at retirement. Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations of the policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency in the first instance. The directors believe that the probability of either the PAC long-term fund or the Group's shareholders' funds having to contribute to SAIF is remote.

Non-participating Business

The majority of Prudential-branded non-participating business is written in the non-profit sub-fund of PAC's long-term fund or in subsidiaries owned by Prudential UK. Since mid-2004, Prudential UK has written all of its new non-profit annuity business through Prudential Retirement Income limited ('PRIL'), from which the profits are attributed solely to shareholders. Prior to that time, certain non-profit annuity business was written through Prudential Annuities Limited ('PAL'), which is wholly owned by PAC's with-profits fund. The profits on this business are attributable to the fund and not to shareholders, although indirectly shareholders get one-ninth of additional amounts paid to policyholders through the declaration of bonuses.

The unit-linked business written by PAC and Prudential International Assurance is written with capital provided by shareholders.

Guaranteed Annuities

Prudential used to sell guaranteed annuity products in the United Kingdom and held a technical provision of £47 million as at 31 December 2012, within the main with-profits fund to honour guarantees on these products. PAC's main exposure to guaranteed annuities in the United Kingdom is through SAIF and a provision of £371 million was held in SAIF as at 31 December 2012, to honour the guarantees. As SAIF is a separate sub-fund of PAC's long-term business fund, wholly attributable to the policyholders of the fund, the movement in this provision has no impact on shareholders.

M&G

M&G is the UK and European fund manager of the Prudential Group with responsibility for investments on behalf of both internal and external clients. M&G is made up of two distinct businesses being Retail and Institutional. M&G's investment expertise covers all key asset classes, equities, fixed interest and commercial real estate, and includes a number of specialist fixed income and real estate strategies. M&G manages its own retail fund operations, funds for pensions, insurance companies and third-party entities.

It is an investment-led business with a clear focus on generating superior long-term returns for investors, whether they are third-party clients or the funds of Prudential's insurance operations. This is achieved by creating an environment that is attractive to talented investment professionals.

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Against a backdrop of continued political and macroeconomic uncertainty, M&G continues to deliver strong investment performance. Over the three years to 31 December 2012, 20 funds representing approximately 61 per cent of retail funds under management (FUM) produced first or second quartile investment returns. The performance of funds managed on behalf of institutional fixed income clients also remains extremely strong with all actively-managed mandates meeting or outperforming their benchmarks over this period.

Performance Overview

M&G has had a record-breaking year in terms of net sales, funds under management and profits.

Total net sales for the 12 months to the end of December 2012 were £16.9 billion, 25 per cent higher than the previous full year peak of £13.5 billion in 2009 and 285 per cent higher than net sales of £4.4 billion in 2011.

The strength of net flows, together with increases in equities and bond values in the year, have led to an increase of 13 per cent in total funds under management, to an all-time high of £228 billion. The FTSE All Share Index has increased by 8 per cent over the year and the sterling corporate bond index has increased by 15 per cent. Building on the strength of the net flows generated by the business over recent years, M&G was the largest retail fund manager in the UK[(8)], measured by funds under management. M&G's total UK retail FUM is £41.2 billion as noted by the Investment Management Association at the end of December 2012.

This caps a decade of extremely strong growth for M&G. Since 2003 net fund sales have increased at an annual compound rate of 32 per cent and external client assets have grown at an annual compound rate of 19 per cent. Over this period underlying profit has grown at an annual rate of 22 per cent.

Retail

In the retail market, M&G operates a single fund range from the UK which it distributes both locally and internationally through increasingly diverse channels. Assets sourced from investors outside the UK now account for 29 per cent of M&G's total retail FUM.

Its reputation for delivering superior long-term investment returns and a high standard of client service enabled M&G to attract a record level of net fund sales in the retail market in 2012. Excluding the results of our South African associate company, where our shareholding reduced from 75 per cent to 49.99 per cent during 2012, total net sales were £8.2 billion. This is 15 per cent higher than their previous high of £7.2 billion in 2010.

In the UK, M&G's core market, net sales totalled £3.1 billion, 30 per cent lower than the previous year but still sufficiently high to rank M&G as the top selling house for the year. M&G has ranked first for both net and gross fund sales in the UK for four consecutive calendar years, an unprecedented achievement. Fund sales slowed in the second half as a direct consequence of a decision in July to limit flows of new money into two of our best-selling sterling corporate bond funds to ensure continued flexibility in the management of the funds. We expect UK net sales to continue to slow in 2013.

By contrast, net fund sales in mainland Europe increased sharply. Following a minor net outflow in 2011, the business generated a record £5.2 billion of net sales representing 67 per cent of total retail net sales in 2012. Over the year M&G saw retail assets sourced from European clients grow by 75 per cent to £14.4 billion (2011: £8.2 billion). Today M&G has offices in 15 different countries and its retail funds are registered for sale in 20 jurisdictions.

(8) Source: Investment Management Association, data as at end-December 2012.

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A core pillar of M&G's retail business is to offer a diversified range of investment funds and so be well-placed for changes in investor trends. The demand for conservatively managed portfolios for most of 2012 saw strong inflows into the M&G Optimal Income Fund, a highly flexible international fixed income fund, and into the M&G Global Dividend Fund. In Europe, Optimal Income was the fourth best selling fund, while Global Dividend ranked ninth over the year to end of December 2012 and was the top selling cross border Equity fund in 2012[(9)].

No fewer than 10 of M&G's retail funds, across the major asset classes of fixed income, equities and real estate, each attracted net sales of at least £100 million during the 12 month period.

The £8.2 billion of net retail inflows in the UK and Europe were partially off-set by a £0.4 billion net outflow from funds managed by M&G's associate entity in South Africa. These redemptions were entirely from the PPM South Africa Dividend Income Fund which was closed on 31 March 2012 ahead of the implementation of new tax legislation on 1 April 2012 which would have had a materially adverse impact on the treatment of the distribution made by the fund to its investors. Fund flows into other retail funds of the South African business have been positive.

Institutional

In the institutional marketplace, M&G's approach is to leverage investment strategies developed primarily for Prudential's internal funds to create higher margin external business opportunities. M&G offers third-party clients, such as pension funds and sovereign wealth funds an innovative range of specialist fixed income and real estate strategies, including private debt opportunities and infrastructure investment.

The institutional business attracted a record level of net funds in 2012, predominantly into fixed income strategies on the strength of its outstanding record of outperformance. At £9.0 billion, net inflows were 50 per cent higher than the previous best of £6.0 billion in 2009. The 2012 inflows include a single £7.6 billion mandate which is expected to be partially or wholly redeemed within the next 24 months.

M&G continues to grow its business with external institutional clients, including the provision of alternatives to bank lending. The M&G UK Companies Financing Fund, a loan facility for medium-sized companies launched in the wake of the 2008 credit crisis, has increased its total commitments to £930 million across 11 individual loans. During the year, loans were made to three new clients, while a fourth advance went to an existing borrower.

Other innovations for third-party clients include a series of investment strategies to manage long-term inflation-linked liabilities. The business successfully launched the M&G Inflation Opportunities Fund and the M&G Debt Opportunities Fund, which complement the existing M&G Secured Property Income Fund, a portfolio of long-lease properties with inbuilt inflation-linked increases. This last fund, which has total investor commitments of £1.3 billion, has delivered an annualised return of 7 per cent above the retail prices index (RPI) over the past three years.

In infrastructure, Infracapital, M&G's unlisted infrastructure equity division, led a consortium (comprising Infracapital and other parties independent of Prudential) in the acquisition of a 90 per cent interest in Veolia Environnement S.A.'s ("Veolia") UK regulated water business (now renamed Affinity Water). Affinity Water is the largest regulated water-only company in the UK by turnover. The acquisition is the first investment for Infracapital Partners II LP, which has current commitments of £358 million.

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(9) Source: SimFund Global. Data as at December 2012 in EUR. Based on estimated net sales of funds classed as fund market 'International' (registered for sale in more than 5 countries). Excludes Money Market and Alternative funds.

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The following table shows funds managed by M&G at the dates indicated.

	At 31 December		
	2012	**2011**	**2010**
	£bn	**£bn**	**£bn**
Retail fund management	**55**	44	42
Institutional fund management	**57**	48	47
Internal fund management	**116**	109	109
Total	**228**	201	198

Prudential Capital

Prudential Capital manages the Group's balance sheet for profit by leveraging Prudential's market position. This business has three strategic objectives: (i) to provide professional treasury services to the Prudential Group; (ii) to operate a first-class wholesale and capital markets interface; and (iii) to realise profitable opportunities within a tightly controlled risk framework. Prudential Capital generates revenue by providing bridging finance, managing investments and operating a securities lending and cash management business for the Prudential Group and its clients.

Markets have remained difficult and volatile in 2012, and as a result the business remains focused on liquidity across the Prudential Group, management of the existing asset portfolio and conservative levels of new investment. Prudential Capital has continued to invest in developing its capabilities, by seeking to maintain the dynamism and flexibility necessary to ensure that the treasury and wholesale services remain robust in a period of increased regulatory change, and to identify and realise opportunities for profit within acceptable risk parameters. Prudential Capital is committed to working closely with other business units across the Prudential Group to exploit opportunities and increase value creation for Prudential as a whole.

Prudential Capital has a diversified earnings base derived from its portfolio of secured loans, debt investments and the provision of wholesale markets services.

Group Risk Framework

Risk Management

Introduction

As a provider of financial services, including insurance, the management of risk lies at the heart of Prudential's business. As a result, effective risk management capabilities represent a key source of competitive advantage for the Group.

The Group's risk framework includes the Group's appetite for risk exposures as well as its approach to risk management. Under this approach, Prudential continuously assesses the Group's top risks and monitors its risk profile against approved limits. Prudential's main strategies for managing and mitigating risk include asset liability management, using derivatives to hedge relevant market risks, and implementing reinsurance and corporate insurance programmes.

Risk Oversight

Group risk appetite

(Audited)

Prudential defines and monitors aggregate risk limits based on financial and non-financial stresses for its earnings volatility, liquidity and capital requirements.

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Earnings volatility: the objectives of the limits are to ensure that:

a. the volatility of earnings is consistent with the expectations of stakeholders;

b. the Group has adequate earnings (and cash flows) to service debt, expected dividends and to withstand unexpected shocks; and

c. earnings (and cash flows) are managed properly across geographies and are consistent with funding strategies.

The two measures used to monitor the volatility of earnings are European Embedded Value (EEV) operating profit and International Financial Reporting Standards (IFRS) operating profit, although EEV and IFRS total profits are also considered.

Liquidity: the objective is to ensure that the Group is able to generate sufficient cash resources to meet financial obligations as they fall due in business as usual and stressed scenarios.

Capital requirements: the limits aim to ensure that:

a. the Group meets its internal economic capital requirements;

b. the Group achieves its desired target rating to meet its business objectives; and

c. supervisory intervention is avoided.

The two measures used are the EU Insurance Groups Directive (IGD) capital requirements and internal economic capital requirements. In addition, capital requirements are monitored on both local statutory and future Solvency II regulatory bases.

Prudential's risk appetite framework forms an integral part of its annual business planning cycle. The Group Risk Committee is responsible for reviewing the risks inherent in the Group's business plan and for providing the Board with input on the risk/reward trade offs implicit therein. This review is supported by the Group Risk function, which uses submissions by business units to calculate the Group's aggregated position (allowing for diversification effects between business units) relative to the limits contained within the risk appetite statements.

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Risk exposures

(Audited)

The Group Risk Framework deploys a common risk language, allowing meaningful comparisons to be made between different business units. Risks are broadly categorised as shown below.

Category	Risk type	Definition
Financial risks	Market risk	The risk of loss for the Group's business, or of adverse change in the financial situation, resulting, directly or indirectly, from fluctuations in the level or volatility of market prices of assets and liabilities.
	Credit risk	The risk of loss for the Group's business or of adverse change in the financial position, resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors in the form of default or other significant credit event (eg downgrade or spread widening).
	Insurance risk	The risk of loss for the Group's business or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of a number of insurance risk drivers. This includes adverse mortality, longevity, morbidity, persistency and expense experience.
	Liquidity risk	The risk of the Group being unable to generate sufficient cash resources or to meet financial obligations as they fall due in business as usual and stress scenarios.
Non-financial risks	Operational risk	The risk of loss arising from inadequate or failed internal processes, or from personnel and systems, or from external events other than those covered by business environment risk.
	Business environment risk	Exposure to forces in the external environment that could significantly change the fundamentals that drive the business's overall strategy.
	Strategic risk	Ineffective, inefficient or inadequate senior management processes for the development and implementation of business strategy in relation to the business environment and the Group's capabilities.

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Financial risks

a Market risk

(i) Equity risk

(Audited)

In the UK business, most of Prudential's equity exposure is incurred in the with-profits fund, which includes a large inherited estate estimated at £7.0 billion as at 31 December 2012 (31 December 2011: £6.1 billion). This can absorb market fluctuations and protect the fund's solvency. The inherited estate itself is partially protected against falls in equity markets through an active hedging policy.

In Asia Prudential's shareholder exposure to equities relates to revenue from unit-linked products and, from a capital perspective, to the effect of falling equity markets on the with-profits businesses.

In the US, where we are a leading provider of variable annuities, there are risks associated with the guarantees embedded in our products. We provide guaranteed minimum death benefits (GMDB) on substantially all policies in this class, guaranteed minimum withdrawal benefits (GMWB) on a significant proportion of the book, and guaranteed minimum income benefits (GMIB) on only 3 per cent. To protect the shareholders against the volatility introduced by these embedded options, we use both a comprehensive hedging programme and reinsurance. The GMIB is no longer offered, with existing coverage being reinsured.

The Jackson IFRS shareholders' equity and US statutory capital are sensitive to the effects of policyholder behaviour on the valuation of GMWB guarantees, but to manageable levels.

In our variable annuity sales activities, we focus on meeting the needs of conservative and risk averse customers who are seeking reliable income in retirement, and who display little tendency to arbitrage their guarantees. These customers generally select conservative investment options. We are able to meet the needs of these customers because of the strength of our operational platform.

It is our philosophy not to compete on price; rather, we seek to sell at a price sufficient to fund the cost we incur to hedge or reinsure our risks and to achieve an acceptable return for our shareholders.

We use a macro approach to hedging that covers the risks inherent across the US business. Within this macro approach we make use of the natural offsets that exist between the variable annuity guarantees and the fixed index annuity book, and then use a combination of over-the-counter (OTC) options and exchange traded derivatives to hedge the remaining risk, considering significant market shocks and limiting the amount of capital we are putting at risk. Internal positions are generally netted before any external hedge positions are considered. The hedging programme also covers the fees on variable annuity guarantees.

Jackson hedges the economics of its products rather than the accounting result. This focus means that we accept a degree of variability in our accounting results in order to ensure we achieve the appropriate economic result. Accordingly, while Jackson's hedges are effective on an economic basis, due to different accounting treatment for the hedges and some of the underlying hedged items on an IFRS basis, the reported income effect is more variable.

(ii) Interest rate risk

(Audited)

Interest rate risk arises from Prudential's investments in long-term debt and fixed income securities, and also exists in policies that carry investment guarantees on early surrender or at maturity, where claim values can become higher than the value of backing assets as a result of rises or falls in interest rates.

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In Asia, the exposure to interest rate risk arises from the guarantees of some non-unit-linked investment products. This exposure arises because it may not be possible to hold assets which will provide cash flows to match exactly those relating to policyholder liabilities. This results in a mismatch due to the duration and uncertainty of the liability cash flows and the lack of sufficient assets of a suitable duration. While this residual asset/liability mismatch risk can be managed, it cannot be eliminated.

In the US, there is interest rate risk across the portfolio. The majority of Jackson's fixed annuity and life liabilities allow for an annual reset of the crediting rate, which provides for a greater level of discretion in determining the amount of interest rate risk to assume. The primary concerns with these liabilities relate to potential surrenders when rates increase and, in a low interest environment, the minimum guarantees required by state law. For variable annuities, interest rate changes will influence the level of reserves held for certain guaranteed benefits. With its large fixed annuity and fixed index annuity books, Jackson has natural offsets for its variable annuity interest-rate related risks. Jackson manages interest rate exposure through a combination of interest rate swaps and interest rate options.

In the UK, the investment policy for the shareholder-backed annuity business is to match the annuity payments with the cash flows from investments. As a result, assets and liabilities are closely matched by duration. The impact on profit of any residual cash flow mismatching can be adversely affected by changes in interest rates; therefore the mismatching position is regularly monitored. The guarantees of the with-profit business give rise to some interest rate discounting risk as falling rates may result in an increase in the cost of guarantees. Except for severe stress scenarios where shareholders' support may be required, this risk is borne by the with-profits fund.

(iii) Foreign exchange risk

(Audited)

Prudential principally operates in the UK, the US and in Asia. The geographical diversity of its businesses means that Prudential is inevitably subject to the risk of exchange rate fluctuations. Prudential's international operations in the US and Asia, which represent a significant proportion of its operating profit and shareholders' funds, generally write policies and invest in assets denominated in local currency. Although this practice limits the effect of exchange rate fluctuations on local operating results, it can lead to significant fluctuations in Prudential's consolidated financial statements when results are expressed in pounds sterling.

The Group retains revenues locally to support the growth of the Group's business and capital is held in the local currency of the business to meet local regulatory and market requirements, accepting the balance sheet translation risks this can produce. However, in cases where a surplus arising in an overseas operation supports Group capital or shareholders' interest (ie remittances), this exposure is hedged if it is economically optimal to do so. The Group does not have appetite for significant shareholder exposures to foreign exchange risks in currencies outside the local territory. Currency borrowings, swaps and other derivatives are used to manage exposures.

b Credit risk

(Audited)

In addition to business unit and Group-wide operational limits on credit risk, Prudential monitors closely its counterparty exposures at Group level, highlighting those that are large or of concern. Where appropriate, Prudential will reduce its exposure, purchase credit protection or make use of collateral arrangements to control its levels of credit risk.

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The Group's balance sheet held the following total investments at 31 December 2012.

	2012				2011
	Participating funds	Unit-linked and variable annuities	Shareholder-backed	Total Group	Total Group
	£bn	£bn	£bn	£bn	£bn
Debt securities	**62.0**	**9.5**	**68.6**	**140.1**	124.5
Equity	**25.1**	**73.9**	**1.0**	**100.0**	87.3
Property investments	**8.7**	**0.6**	**1.6**	**10.9**	10.8
Mortgage loans	**1.3**		**4.8**	**6.1**	5.7
Other loans	**1.4**		**4.3**	**5.7**	4.0
Deposits	**9.5**	**1.4**	**1.8**	**12.7**	10.7
Other investments	**4.7**		**3.2**	**7.9**	7.6
Total	**112.7**	**85.4**	**85.3**	**283.4**	250.6

The table below presents the balances of investments related to shareholder-backed operations at 31 December 2012.

	2012	2011
	£bn	£bn
Shareholder-backed investments:		
Asia life	**8.7**	7.1
UK life	**31.3**	28.5
US life	**42.0**	34.0
Other	**3.3**	3.8
Total	**85.3**	73.4

Shareholders are not directly exposed to value movements on assets backing participating or unit-linked operations, with sensitivity mainly related to shareholder-backed operations.

(i) Debt portfolio

(Audited)

The investments held by the shareholder-backed operations are predominantly debt securities, of which 95 per cent are rated, either externally or internally, as investment grade (31 December 2011: 95 per cent).

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The Group's total debt securities portfolio on an IFRS basis comprised the following at 31 December 2012:

	2012				2011
	Participating funds	Unit-linked and variable annuities*	Shareholder-backed	Total Group	Total Group
	£bn	£bn	£bn	£bn	£bn
Insurance operations:					
UK	**50.5**	**6.3**	**27.1**	**83.9**	78.0
Jackson National Life			**33.0**	**33.0**	27.0
Asia long-term business	**11.5**	**3.2**	**6.7**	**21.4**	17.7
Other operations			**1.8**	**1.8**	1.8
Total	**62.0**	**9.5**	**68.6**	**140.1**	124.5

* Jackson's variable annuity separate account assets comprise equity securities and portfolio holdings in unit trusts (including mutual funds), the majority of which are equity based.

UK

The UK's debt portfolio on an IFRS basis is £83.9 billion as at 31 December 2012, including £50.5 billion within the UK with-profits fund. Shareholders' risk exposure to the with-profits fund is limited as the solvency is protected by the large inherited estate. Outside the with-profits fund there is £6.3 billion in unit-linked funds where the shareholders' risk is limited, with the remaining £27.1 billion backing the shareholders' annuity business and other non-linked business (of which 75 per cent is rated AAA to A-, 23 per cent BBB and 2 per cent non-investment grade). The UK shareholder-backed portfolio did not experience any default losses in 2012.

US

At 31 December 2012 Jackson's fixed income debt securities portfolio consisted of:

Summary	**2012**	**2011**
	£bn	**£bn**
Corporate and government security and commercial loans:		
Government	**4,126**	2,163
Publicly traded and SEC Rule 144A securities[note]	**19,699**	16,281
Non-SEC Rule 144A securities	**3,542**	3,198
Total	**27,367**	21,642
Residential mortgage-backed securities	**2,400**	2,591
Commercial mortgage-backed securities	**2,639**	2,169
Other debt securities	**587**	620
Total US debt securities	**32,993**	27,022

Note

A 1990 SEC rule that facilitates the resale of privately placed securities that are without SEC registration to qualified institutional investors. The rule was designed to develop a more liquid and efficient institutional resale market for unregistered securities.

Of the £23.2 billion of corporate debt, 95 per cent is investment grade. Concentration risk within the corporate debt portfolio is low, with the top ten holdings accounting for approximately 8 per cent of the portfolio. Our largest sector exposures in the investment grade corporate debt portfolio are Energy

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and Utilities at 15 per cent and 13 per cent, respectively. We actively manage the portfolio and will sell exposures as events dictate.

Within the RMBS portfolio of £2.4 billion, the portion guaranteed by the US government sponsored agencies is 57 per cent. The CMBS portfolio of £2.6 billion is performing strongly, with 40 per cent of the portfolio rated AAA and less than 2 per cent rated below investment grade. The entire portfolio has an average credit enhancement level of 31 per cent. This level provides significant protection, since it means the underlying collateral has to incur a 31 per cent loss, net of recoveries, before our holding is at risk.

Jackson's debt securities experienced total credit-related losses in 2012 of £47 million (2011: £52 million). This includes a loss net of recoveries of £10 million (2011: gains of £10 million) on credit-related sales of impaired bonds. IFRS write-downs on debt securities were £37 million (2011: £62 million). Of this amount of write-downs, £8 million (2011: £21 million) was in respect to RMBS securities. In addition to the amounts for debt securities, there were £5 million (2011: £28 million) of write-downs on Jackson's commercial mortgage loan portfolio. In 2012 and 2011, Jackson did not experience any defaults on its debt securities.

The impairment process reflects a review of every bond and security in our portfolio. Our accounting policy requires us to book full mark to market losses on impaired securities through our balance sheet. However, we would expect only a proportion of these losses eventually to turn into defaults, and some of the impaired securities to recover in price over time.

Unrealised gains and losses on debt securities in the US

Jackson's net unrealised gains from debt securities were £2,807 million at 31 December 2012, compared to £2,057 million at 31 December 2011. The gross unrealised loss position was £178 million at 31 December 2012 (31 December 2011: £246 million). Gross unrealised losses on securities priced at less than 80 per cent of face value totalled £53 million at 31 December 2012 compared to £158 million at 31 December 2011.

Asia

Asia's debt portfolio totalled £21.4 billion at 31 December 2012. Of this, approximately 69 per cent was in unit-linked and with-profits funds with minimal shareholders' risk. The remaining 31 per cent is shareholder exposure and is invested predominantly (65 per cent) in investment grade bonds. The Asian portfolio has performed very well, and did not experience any default losses in 2012.

Asset management

The debt portfolio of the Group's asset management operations of £1.8 billion as at 31 December 2012 is principally related to Prudential Capital operations. Of this amount £1.5 billion were rated AAA to A- by S&P or Aaa by Moody's.

(ii) Group sovereign debt exposure

(Audited)

Sovereign debt represented 15 per cent or £10.4 billion of the debt portfolio backing shareholder business (excluding unit-linked business) at 31 December 2012 (2011: 16 per cent and £9.2 billion respectively). 38 per cent of this was rated AAA and 92 per cent investment grade (2011: 43 per cent and 94 per cent respectively). Of the Group's holdings in Continental Europe of £564 million, 79 per cent was AAA rated (2011: £690 million and 87 per cent respectively). Shareholder exposure to the Eurozone sovereigns of Portugal, Italy, Ireland, Greece and Spain (PIIGS) is £52 million

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(2011: £44 million). The Group does not have any sovereign debt exposure to Greece, Portugal or Ireland.

The exposure of the Group's shareholder and with-profits funds to sovereign debt (including credit default swaps that are referenced to sovereign debt) at 31 December 2012 is as follows.

	Shareholder sovereign debt	With-profits sovereign debt
	£m	£m
Continental Europe		
Italy	43	52
Spain	1	33
	44	85
Germany	598	602
Other Europe (principally Isle of Man and Belgium)	48	62
	690	749
United Kingdom	3,254	2,801
United States	2,448	2,615
Other, predominantly Asia	2,850	332
Total	**9,242**	**6,497**

(iii) Exposure to bank debt securities

(Audited)

Prudential expects that any second order sovereign credit exposures would most likely be concentrated in the banking sector. The Group's bank exposure is a function of its core investment business, as well as of the hedging and other activity undertaken to manage its various financial risks. Prudential relies on public information and credit research sources to identify banks with large concentrations of indirect exposure.

Prudential has a range of controls and processes to manage credit exposure. In addition to the control frameworks that cover shareholder and policyholder credit risk within each business unit, the Group Credit Risk Committee oversees shareholder credit risk across the Group. The Committee receives comprehensive management information, including details of counterparty and invested credit exposure (including structured credit and loans), secured and unsecured cash balances, top 30 credit exposures, and an analysis of shareholder exposure by industry/country and rating. The business units and the Group Risk function also continually monitor the portfolio for emerging credit risks through various tools and processes.

Prudential actively mitigates the level of Group-wide credit risk (invested credit and counterparty) through a comprehensive system of hard limits, collateralisation agreements and centrally managed 'watch lists'.

Of the £68.6 billion of debt securities backing shareholder business, excluding holdings attributable to external holders of consolidated unit trusts, 3 per cent or £2.2 billion was in Tier 1 and Tier 2 hybrid bank debt. A further £3.2 billion was in the form of senior debt.

In terms of shareholder exposures to the bank debt of PIIGS, Prudential held £260 million at 31 December 2012 (31 December 2011: £328 million). This comprised £130 million of covered bonds, £93 million senior debt, £3 million Tier 1 debt and £34 million Tier 2 debt. There was no direct exposure to Greek banks.

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The Group held the following direct exposures to banks' debt securities of shareholder-backed business at 31 December 2012.

	Bank debt securities shareholder-backed business						
	Senior debt			Subordinated debt			
	Covered	Senior	Total senior debt	Tier 2	Tier 1	Total subordinated debt	31 Dec 2011 Total
	£m	£m	£m	£m	£m	£m	£m
Portugal		24	24				24
Ireland		13	13				13
Italy		11	11	56	14	70	81
Greece							
Spain	107	11	118	90	2	92	210
	107	59	166	146	16	162	328
Austria				9		9	9
Belgium							
France	2	34	36	78	35	113	149
Germany		28	28	1		1	29
Luxembourg							
Netherlands		7	7	81	64	145	152
United Kingdom	228	145	373	615	95	710	1,083
Total Europe	337	273	610	930	210	1,140	1,750
United States		1,362	1,362	352	2	354	1,716
Other, predominantly Asia		246	246	562	33	595	841
Total	337	1,881	2,218	1,844	245	2,089	4,307

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In addition to the exposures held by the shareholder-backed business, the Group held the following banks' securities at 31 December 2012 within its with-profits funds.

	Bank debt securities participating funds						
	Senior debt			Subordinated debt			
	Covered	Senior	Total senior debt	Tier 2	Tier 1	Total subordinated debt	31 Dec 2011 Total
	£m	£m	£m	£m	£m	£m	£m
Portugal		7	7				7
Ireland							
Italy		45	45	49	2	51	96
Greece	5		5				5
Spain	137		137	1		1	138
	142	52	194	50	2	52	246
Austria							
Belgium							
France		80	80	47	17	64	144
Germany		7	7				7
Luxembourg		7	7				7
Netherlands		80	80	14	28	42	122
United Kingdom	319	385	704	772	74	846	1,550
Total Europe	461	611	1,072	883	121	1,004	2,076
United States		1,378	1,378	396	278	674	2,052
Other, predominantly Asia	1	384	385	341	20	361	746
Total	462	2,373	2,835	1,620	419	2,039	4,874

(iv) Other possible impacts of a Eurozone crisis

(Audited)

Other knock on impacts of a Eurozone crisis may represent some risk to the Group, both in terms of financial market impact and potential operational issues. These third order exposures are intrinsically more difficult to quantify. However, as well as the monitoring routines noted above, Prudential has also developed tools to identify the Group's exposure to counterparties at risk (including contingent credit exposures), and has in place Group-wide processes to facilitate the management of such risks should they materialise.

In respect of operational risks, Prudential has strong investment operations, counterparty risk and change management capabilities and Prudential is confident in its ability to manage the transition to a new Eurozone regime if events require it to do so.

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(v) Loans

(Audited)

Of the total Group loans of £11.8 billion at 31 December 2012, the following are held by shareholder-backed operations.

	2012 £bn			2011 £bn		
	Mortgage loans	**Other loans**	**Total**	**Mortgage loans**	**Other loans**	**Total**
Asia insurance operations[i]		**0.4**	**0.4**		0.4	0.4
US insurance operations[ii]	**3.5**	**2.7**	**6.2**	3.6	0.6	4.2
UK insurance operations[iii]	**1.3**		**1.3**	1.1		1.1
Asset management operations[iv]		**1.2**	**1.2**		1.3	1.3
Total loans held by shareholder-backed operations	**4.8**	**4.3**	**9.1**	4.7	2.3	7.0

Notes

(i) The majority of Asia insurance operations loans are commercial loans held by the Malaysian operation that are rated investment grade by two local rating agencies.

(ii) The US insurance operations held £6.2 billion of loans, comprising £3.5 billion of commercial mortgage loans and £2.7 billion of policy loans. Approximately £1.8 billion of the policy loans are held as collateral related to the three reinsurance treaties with Swiss Re, which are offset by a funds withheld liability. These loans are carried at fair value. All other loans are accounted for at amortised cost, less any impairment. All commercial mortgage loans held by US insurance operations are collateralised by properties. The US commercial mortgage loan portfolio does not include any single-family residential mortgage loans and therefore is not exposed to the risk of defaults associated with residential sub-prime mortgage loans. Jackson incurred write downs of £5 million on its commercial mortgage book (2011: write downs of £28 million).

(iii) The majority of mortgage loans held by UK insurance operations are mortgage loans collateralised by properties.

(iv) Relates to bridging loan finance managed by Prudential Capital.

(vi) Counterparty Credit Risk

(Audited)

The Group enters into a variety of exchange traded and over-the-counter derivative financial instruments, including futures, options, forward currency contracts and swaps such as interest rate swaps, cross-currency swaps, swaptions and credit default swaps.

All over-the-counter derivative transactions, with the exception of some Asian transactions, are conducted under standardised ISDA (International Swaps and Derivatives Association Inc) master agreements and the Group has collateral agreements between the individual Group

entities and relevant counterparties in place under each of these market master agreements.

The Group's exposure to derivative counterparty and reinsurance counterparty credit risk is subject to the same framework of Group-wide operational limits and monitoring as its invested credit risk. Where appropriate, Prudential will reduce its exposure, purchase credit protection or make use of additional collateral arrangements to control its levels of counterparty credit risk.

c Insurance risk

(Audited)

The processes of determining the price of Prudential's products and reporting the results of its long-term business operations require Prudential to make a number of assumptions. In common with

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other industry players, the profitability of Prudential's businesses depends on a mix of factors including mortality and morbidity levels and trends, persistency, investment performance, unit cost of administration and new business acquisition expenses.

Prudential continues to conduct research into longevity risk using data from its substantial annuity portfolio. The assumptions that Prudential makes about future expected levels of mortality are particularly relevant in its UK annuity business. The attractiveness of transferring longevity risk (via reinsurance and other external solutions) is regularly evaluated. These are used as risk management tools where it is appropriate and attractive to do so.

Prudential's morbidity risk is mitigated by appropriate underwriting and use of reinsurance and the morbidity assumptions reflect recent experience and expectation of future trends for each relevant line of business.

Prudential's persistency assumptions reflect recent experience for each relevant line of business, and any expectations of future persistency. Persistency risk is mitigated by appropriate training and sales processes and managed proactively post sale. Where appropriate, allowance is also made for the relationship either assumed or historically observed between persistency and investment returns, and for the resulting additional risk.

d Liquidity risk

(Audited)

The parent company has significant internal sources of liquidity which are sufficient to meet all of its expected requirements for the foreseeable future without having to make use of external funding. In aggregate the Group has £2.1 billion of undrawn committed facilities, expiring between 2013 and 2017. In addition, the Group has access to liquidity via the debt capital markets. Prudential also has in place an unlimited commercial paper programme and has maintained a consistent presence as an issuer in this market for the last decade. Liquidity uses and sources have been assessed at the Group and at a business unit level under base case and stressed assumptions. The liquidity resources available and the subsequent Liquidity Coverage Ratio are regularly monitored and have been assessed to be sufficient under both sets of assumptions.

Non-financial risk

(Unaudited)

Prudential is exposed to operational, business environment and strategic risk in the course of running its businesses.

Prudential is exposed to operational risk through the course of running its business. It is dependent on the successful processing of a large and complex number of transactions, utilising various IT applications and platforms, across numerous and diverse products. It also operates under the ever evolving requirements set out by different regulatory and legal regimes (including tax), as well as utilising a significant number of third parties to distribute products and to support business operations.

Prudential's systems and processes incorporate controls that are designed to manage and mitigate the operational risks associated with its activities. The Prudential Group Governance Manual was developed to make a key contribution to the sound system of internal control that the Group is expected to maintain under the UK Corporate Governance Code and the Hong Kong Code on Corporate Governance Practices. Group Head Office and business units confirm that they have implemented the necessary controls to evidence compliance with the Manual.

Prudential has an operational risk management framework in place that facilitates both the qualitative and quantitative analysis of operational risk exposures. The output of this framework, in

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particular management information on key operational risk and control assessments, scenario analysis, internal incidents and external incidents, is reported by the business units and presented to the Group Operational Risk Committee. This information also supports business decision-making and lessons-learned activities; the ongoing improvement of the control environment; and determination of the adequacy of Prudential's corporate insurance programme.

With regard to business environment risk, including the impacts of regulatory developments, the Group has a wide-ranging programme of active and constructive engagement with governments, policymakers and regulators in its key markets and with relevant international institutions. Such engagement is undertaken both directly and indirectly via trade associations. The Group has procedures in place to monitor and track political and regulatory developments and assess their potential impact on the Group. Where appropriate, the Group provides submissions and technical input to officials and others, either via submissions to formal consultations or through interactions with officials.

With regard to strategic risk, both business units and the Group Head Office are required to adopt a forward-looking approach to risk management by performing risk assessments as part of the annual strategic planning process. This supports the identification of potential threats and the initiatives needed to address them, as well as competitive opportunities. The impact on the underlying businesses and/or Group-wide risk profile is also considered to ensure that strategic initiatives are within risk appetite.

Solvency II represents a regulatory risk due to the uncertainty of what the rules will be when finalised, their potential impacts, and the timing of their introduction. The risks are that the Group may not be able to respond sufficiently quickly to the strategic implication of the change given levels of uncertainty around the content and timing; operational risk in terms of the scale and complexity of the delivery and uncertainty over timelines; and the additional capital that the Group may be required to hold. Solvency II is covered in more detail in the Capital Management section below.

Capital management

Regulatory capital (IGD)

(Audited)

Prudential is subject to the capital adequacy requirements of the European Union Insurance Groups Directive (IGD) as implemented by the Financial Services Authority (FSA) in the UK. The IGD capital adequacy requirements involve aggregating surplus capital calculated on a FSA consistent basis for regulated subsidiaries, from which Group borrowings, except those subordinated debt issues that qualify as capital, are deducted. No credit for the benefit of diversification is permitted under this approach.

Prudential's capital position remains strong. Prudential has continued to place emphasis on maintaining the Group's financial strength through optimising the balance between writing profitable new business, conserving capital and generating cash. Prudential estimates that its IGD capital surplus is £5.1 billion at 31 December 2012 (before taking into account the 2012 final dividend), with available capital covering its capital requirements 3.0 times. This compares to a capital surplus of £4.0 billion at the end of 2011 (before taking into account the 2011 final dividend).

The movements in 2012 mainly comprise:

Net capital generation mainly through operating earnings (in-force releases less investment in new business, net of tax) of £2.5 billion;

Offset by:

Negative impact arising from market movements estimated at £0.2 billion;

Final 2011 dividend of £0.5 billion and interim 2012 dividend of £0.2 billion;

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External financing costs and other central costs, net of tax, of £0.4 billion; and

Negative impact arising from foreign exchange movements of £0.1 billion.

IGD surplus represents the accumulation of surpluses across all of our operations based on local regulatory minimum capital requirements with some adjustments, pursuant to the requirements of Solvency I. The calculation does not fully adjust capital requirements for risk nor does it capture the true economic value of assets. Global regulatory developments, such as Solvency II and ComFrame, aim to ensure that the calculation of regulatory surplus continues to evolve over time into a more meaningful economic measure.

There is broad agreement that ultimately it would be beneficial to replace the IGD regime with a regime that would be more risk based. Solvency II was supposed to provide such a framework but we now know that it will not be implemented before 31 December 2015. The structure of the Group and the approach we have taken to managing our risks, with a sizeable credit reserve in the UK annuity book, a strong inherited estate in UK with profits and the relatively low risk nature of our asset management and Asian operations, together with a high level of IGD surplus means we have positioned ourselves well for future regulatory developments and stresses to our business.

(Unaudited)

In March 2013, we have agreed with the FSA to amend the calculation of the contribution Jackson makes to the Group's IGD surplus. Until now, the contribution of Jackson to the reported IGD was based on an intervention level set at 75 per cent of US Risk Based Capital Company Action Level (CAL). Going forward, the contribution of Jackson to IGD surplus will equal the surplus in excess of 250 per cent of CAL. This is more in line with the level at which we currently report free surplus, which we have set at 235 per cent of CAL. In the absence of an agreed Solvency II approach, we believe that this change makes the IGD surplus a more meaningful measure and one that is more closely aligned with economic reality. The revised IGD surplus calculation has no impact on the way that the US business is managed or regulated locally.

(Unaudited)

On this revised basis, the IGD surplus at 28 February 2013 is estimated at £4.4 billion[(10)] (equivalent to a capital cover of 2.5 times) which includes the £0.4 billion of subordinated debt raised in January 2013 and is after deducting £1.3 billion in respect of the Jackson change from 75 per cent to 250 per cent of CAL.

Prudential continues to have further options available to manage available and required capital. These could take the form of increasing available capital (for example, through financial reinsurance) or reducing required capital (for example, through the mix and level of new business) and the use of other risk mitigation measures such as hedging and reinsurance. A number of such options were utilised through the last financial crisis in 2008 and 2009 to enhance the Group's IGD surplus. One such arrangement allowed the Group to recognise a proportion of the shareholder's interest in future transfers from the UK's with-profits business and this remained in place, contributing £0.36 billion to the IGD at 31 December 2012. We will phase this out in two equal steps, reducing the credit taken to £0.18 billion from January 2013 and we expect to take zero credit from January 2014.

In addition to its strong capital position, on a statutory (Pillar 1) basis, the total credit reserve for the UK shareholder annuity funds also protects its capital position in excess of the IGD surplus. This

(10) The estimated position at 28 February 2013 allows for economic conditions and surplus generation since 31 December 2012 and is stated before the final dividend and the effect of the Thanachart acquisition and after allowing for a reduction in Jackson's contribution to IGD surplus of £1.3 billion.

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credit reserve as at 31 December 2012 was £2.1 billion. This credit risk allowance represents 40 per cent of the bond portfolio spread over swap rates, compared to 33 per cent as at 31 December 2011.

Stress testing

(Unaudited)

As at 31 December 2012, stress testing of our IGD capital position to various events has the following results:

An instantaneous 20 per cent fall in equity markets from 31 December 2012 levels would reduce the IGD surplus by £450 million;

A 40 per cent fall in equity markets (comprising an instantaneous 20 per cent fall followed by a further 20 per cent fall over a four-week period) would reduce the IGD surplus by £950 million;

A 100 basis points reduction (subject to a floor of zero) in interest rates would reduce the IGD surplus by £850 million*; and

Credit defaults of ten times the expected level would reduce IGD surplus by £700 million.

* The impact of the 100 basis points reduction in interest rates is exacerbated by the current regulatory permitted practice used by Jackson, which values all interest rate swaps at book value rather than fair value for regulatory purposes. At 31 December 2012, removing the permitted practice would have increased reported IGD surplus by £0.3 billion. As at 31 December 2012, it is estimated that a 100 basis point reduction in interest rates (subject to a floor of zero) would have resulted in an IGD surplus of £4.9 billion, excluding the permitted practice. The effect of the revised calculation of Jackson's contribution to IGD surplus as at 31 December 2012 would have been to increase the sensitivity to equity market falls by approximately £50 million.

Prudential believes that the results of these stress tests, together with the Group's strong underlying earnings capacity, its established hedging programmes and its additional areas of financial flexibility, demonstrate that it is in a position to withstand significant deterioration in market conditions.

Prudential also uses an economic capital assessment to monitor its capital requirements across the Group, allowing for realistic diversification benefits and continues to maintain a strong position. This assessment provides valuable insights into its risk profile.

Solvency II and other global regulatory developments

(Unaudited)

The European Union (EU) is developing a new solvency framework for insurance companies, referred to as 'Solvency II'. The Solvency II Directive, which sets out the new framework, was formally approved by the Economic and Financial Affairs Council in November 2009. The new approach is based on the concept of three pillars minimum capital requirements, supervisory review of firms' assessments of risk, and enhanced disclosure requirements.

Specifically, Pillar 1 covers the quantitative requirements around own funds, valuation rules for assets and liabilities and capital requirements. Pillar 2 provides the qualitative requirements for risk management, governance and controls, including the requirement for

insurers to submit an Own Risk and Solvency Assessment which will be used by the regulator as part of the supervisory review process. Pillar 3 deals with the enhanced requirements for supervisory reporting and public disclosure.

A key aspect of Solvency II is that the assessment of risks and capital requirements are intended to be aligned more closely with economic capital methodologies and may allow Prudential to make use of internal economic capital models if approved by the relevant supervisory authority.

Representatives from the European Parliament, the European Commission and the Council of the European Union are currently discussing the Omnibus II Directive which, once approved, will amend

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certain aspects of the original Solvency II Directive. In addition the European Commission is continuing to develop, in consultation with stakeholders including industry, the detailed rules that will complement the high-level principles of the Directive, referred to as 'implementing measures'. The Omnibus II Directive is not currently scheduled to be finalised until late 2013, while the implementing measures cannot be finalised until after Omnibus II.

There is a significant uncertainty regarding the final outcome from this process. In particular, the Solvency II rules relating to the determination of the liability discount rate and to the treatment of US business remain unclear and Prudential's capital position is sensitive to these outcomes. With reference to the liability discount rate, solutions to remove artificial volatility from the balance sheet have been suggested by policymakers as the regulations continue to evolve. These solutions, along with transitional arrangements for the treatment of the US business, are continuing to be considered by policymakers as part of the process to reach agreement on the Omnibus II Directive. There is a risk that the effect of the measures finally adopted could be adverse for Prudential, including potentially that a significant increase in capital may be required to support its business and that Prudential may be placed at a competitive disadvantage to other European and non-European financial services groups. Prudential is actively participating in shaping the outcome through our involvement in industry bodies and trade associations, including the Chief Risk Officer and Chief Financial Officer Forums, together with the Association of British Insurers and Insurance Europe (formerly known as the Comité Européen des Assurances).

The delays in finalising the Omnibus II Directive and implementing measures are expected to result in a deferral of the Solvency II implementation date for firms beyond the previously anticipated date of 1 January 2014. At this stage, it remains unclear exactly when Solvency II will come into force, although a deferral until 1 January 2016 or beyond appears likely.

Having assessed the requirements of Solvency II, an implementation programme was initiated with dedicated teams to manage the required work across the Group. The activity of the local Solvency II teams is being coordinated centrally to achieve consistency in the understanding and application of the requirements. Prudential is continuing its preparations to adopt the regime when it eventually comes into force and is undertaking in parallel an evaluation of the possible actions to mitigate its effects. Prudential regularly reviews its range of options to maximise the strategic flexibility of the Group. This includes consideration of optimising the Group's domicile as a possible response to an adverse outcome on Solvency II.

Over the coming months Prudential will remain in regular contact with the FSA as it continues to engage in the 'pre-application' stage of the approval process for the internal model. In addition, Prudential also expects to engage in the initial stage of the FSA's proposed 'Individual Capital Adequacy Standards Plus (ICAS+)' regime, which will ultimately enable its UK insurance entities to leverage the developments made in relation to the Solvency II internal model for the purpose of meeting existing ICAS regime.

Currently there are also a number of other prospective global regulatory developments which could impact the way in which Prudential is supervised in its many jurisdictions. These include the Dodd-Frank Act in the US, the work of the Financial Stability Board (FSB) on Globally Systemically Important Financial Institutions (G-SIFIs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) being developed by the International Association of Insurance Supervisors (IAIS).

The Dodd-Frank Act represents a comprehensive overhaul of the financial services industry within the United States that, among other reforms to financial services entities, products and markets, may subject financial institutions designated as systemically important to heightened prudential and other requirements intended to prevent or mitigate the impact of future disruptions in the US financial system, The full impact of the Dodd-Frank Act on Prudential's businesses is not currently clear, however, as

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many of its provisions have a delayed effectiveness and/or require rulemaking or other actions by various US regulators over the coming years.

As part of a global initiative to identify G-SIFIs, in May 2012, the IAIS published proposed assessment methodology for designating Globally Systemically Important Insurers (G-SIIs). For those groups that are designated by the FSB as G-SII then additional policy measures including enhanced supervision, introduction of recovery and resolution plans and higher loss absorbency requirements could be proposed. Further detail of the proposals is expected during 2013 and implementation is likely to be over a period of years. Furthermore, the FSA is considering the designation of Domestically Systemically Important Insurer (DSII) for those UK insurers that are significant in UK terms. It is not yet clear what the impact of this designation may be.

ComFrame is also being developed by the IAIS to provide common global requirements for supervision of insurance groups. The framework is designed to develop common principles for supervision and so may increase the focus of regulators in some jurisdictions. It is also possible that some prescriptive requirements, including group capital, could be proposed. Further clarity on ComFrame is expected during the second half of 2013.

Capital allocation

(Unaudited)

Prudential's approach to capital allocation is to attain a balance between risk and return, investing in those businesses that create shareholder value. In order to efficiently allocate capital, Prudential measures the use of, and the return on, capital.

Prudential uses a variety of metrics for measuring capital performance and profitability, including traditional accounting metrics and economic returns. Capital allocation decisions are supported by this quantitative analysis, as well as strategic considerations.

The economic framework measures risk adjusted returns on economic capital, a methodology that ensures meaningful comparison across the Group. Capital utilisation, return on capital and new business value creation are measured at the product level as part of the business planning process.

Risk mitigation and hedging

(Unaudited)

Prudential manages its actual risk profile against its tolerance of risk. To do this, Prudential maintains risk registers that include details of the risks Prudential has identified and of the controls and mitigating actions it employs in managing them. Any mitigation strategies involving large transactions such as a material derivative transaction involving shareholder business are subject to review at Group level before implementation.

Prudential uses a range of risk management and mitigation strategies. The most important of these include: adjusting asset portfolios to reduce investment risks (such as duration mismatches or overweight counterparty exposures); using derivatives to hedge market risks; implementing reinsurance programmes to manage insurance risk; implementing corporate insurance programmes to limit the impact of operational risks; and revising business plans where appropriate.

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RISK GOVERNANCE

Principles and objectives

Risk is defined as the uncertainty that Prudential faces in successfully implementing its strategies and objectives. This includes all internal or external events, acts or omissions that have the potential to threaten the success and survival of Prudential.

The control procedures and systems established within the Group are designed to manage rather than eliminate the risk of failure to meet business objectives. They can only provide reasonable and not absolute assurance against material misstatement or loss and focus on aligning the levels of risk-taking with the achievement of business objectives.

Material risks will only be retained where this is consistent with Prudential's risk appetite framework and its philosophy towards risk-taking. The Group's current approach is to retain such risks where doing so contributes to value creation and the Group is able to withstand the impact of an adverse outcome, and has the necessary capabilities, expertise, processes and controls to appropriately manage the risk.

In keeping with this philosophy, the Group has five objectives for risk and capital management which are as follows:

Framework to design, implement and maintain a capital management and risk oversight framework, which is consistent with the Group's risk appetite and philosophy towards risk taking;

Monitoring to establish a 'no surprises' risk management culture by identifying the risk landscape, assessing and monitoring risk exposures and understanding change drivers;

Control to implement suitable risk mitigation strategies and remedial actions where exposures are deemed inappropriate, and to manage the response to potentially extreme events;

Communication to effectively communicate the Group risk, capital and profitability position to both internal and external stakeholders; and

Culture to foster a risk management culture, providing quality assurance and facilitating the sharing of best practice.

Prudential's risk governance framework requires that all of the Group's businesses and functions establish processes for identifying, evaluating and managing the key risks faced by the Group. The framework is based on the concept of 'three lines of defence' comprising risk taking and management, risk control and oversight and independent assurance.

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The diagram above outlines the Group-level framework.

Primary responsibility for strategy, performance management and risk control lies with the Board, which has established the Risk Committee to assist in providing leadership, direction and oversight in respect of the Group's significant risks, and with the Group Chief Executive and the chief executives of each of the Group's business units.

Risk Management

Risk taking and the management thereof forms the first line of defence and is facilitated through both the Group Executive Committee ('GEC') and the Balance Sheet and Capital Management Committee ('BSCMC').

The GEC is comprised of the chief executives of each of the Group's major business units, as well as a number of functional specialists, and supports the Group Chief Executive in the executive management of the Group.

The BSCMC is comprised of functional specialists and supports the Chief Financial Officer in the management of the Group's balance sheet, as well as providing oversight to the activities of Prudential Capital, which undertakes the treasury function for the Group.

Risk Oversight

Risk control and oversight constitutes the second line of defence, and is achieved through the operation of a number of Group-level risk committees, chaired by either the Chief Financial Officer or

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the Group Chief Risk Officer, which monitor and keep risk exposures under regular review . These committees are as follows:

Group Executive Risk Committee
The committee meets monthly to oversee the Group's risk exposures, including market, credit, liquidity, insurance and operational risks, and also monitors the Group's capital position.

Group Credit Risk Committee
The committee reports directly to the Group Executive Risk Committee and meets monthly to review the Group's investment and counterparty credit risk positions.

Group Operational Risk Committee
The committee meets quarterly to oversee the Group's operational risk exposures. The committee reports directly to the Group Executive Risk Committee.

Solvency II Technical Oversight Committee
The committee normally meets ten times per year to provide ongoing technical oversight and advice to the Board and executive in respect of their duties with regard to the Group's Internal Model. The committee reports to the Group Executive Risk Committee.

Technical Actuarial Committee
The committee reports to the Group Executive Risk Committee and usually meets monthly to set the methodology for valuing Prudential's assets, liabilities and capital requirements under Solvency II and the Group's internal economic capital basis.

Group Compliance Committee
The committee reports to the Group Executive Risk Committee and meets every two months to oversee the effectiveness of risk and capital management for all financial and non-financial risks faced by Prudential Group and has responsibility to consider Group-wide regulatory compliance risks and controls.

The Group-level risk committees are supported by the Group Chief Risk Officer, with functional oversight provided by Group Security, Group Compliance and Group Risk. Group Security is responsible for developing and delivering appropriate security measures with a view to protecting the Group's staff, physical assets and intellectual property. Group Compliance provides verification of compliance with regulatory standards and informs the Board, as well as the Group's management, on key regulatory issues affecting the Group. Group Risk has responsibility for establishing and embedding a capital management and risk oversight framework and culture consistent with Prudential's risk appetite that protects and enhances the Group's embedded and franchise value.

Independent assurance

The third line of defence comprises the Group wide Internal Audit function, which provides independent and objective assurance to the Board, GEC, Audit and Risk committees on the overall effectiveness of risk management, control and governance processes across the Group.

Reporting

The Risk Committee is provided with regular reports on the activities of the Risk function and, where it affects the results of the assurances under the Turnbull compliance statement, the Audit Committee also receives appropriate reporting from the same function. Reports to the Risk Committee include information on the activities of the Group Executive Risk Committee, the Group Operational Risk Committee, the Group Credit Risk Committee, the Solvency II Technical Oversight Committee, the Technical Actuarial Committee and the Group Compliance Committee, as well as reports from Group-wide Internal Audit.

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The Group's capital position and overall position against risk limits are reviewed regularly by the Group Executive Risk Committee, the Group Risk Committee and the Board. Key economic capital metrics, as well as risk-adjusted profitability information, are included in the business plans which are reviewed by the Group Executive Risk Committee, the Group Risk Committee and the Board.

Routine internal reporting by the business units vary according to the nature of the business, with each business unit responsible for ensuring that its risk reporting framework meets both the needs of the respective business unit and the standards set by the Group Risk function. Clear escalation criteria and processes are in place for the timely reporting of risks and incidents by business units to the various Group-level risk committees and, where appropriate, the Board.

Each business unit reviews the risks inherent in their business operations as part of the annual preparation of their business plan, and subsequently, these opportunities and risks are regularly reviewed against business objectives with Group Risk. The impact of large transactions or divergences from the agreed business plan are also reviewed and reported by Group Risk.

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Investments

General

The overall financial strength of Prudential and the results, both current and future, of the insurance business are in part dependent upon the quality and performance of the various investment portfolios in the United Kingdom, the United States and Asia.

Prudential's Total Investments

The following table shows Prudential's insurance and non-insurance investments, net of derivative liabilities, at 31 December 2012. In addition, at 31 December 2012 Prudential had £121.4 billion of external funds under management. Assets held to cover linked liabilities relate to unit-linked and variable annuity products. In this table, investments are valued as set out in note A3 to the consolidated financial statements in Item 18.

	At 31 December 2012								
	UK Insurance	US Insurance	Asia Insurance	Total Insurance	Asset Management(a)	Other	Total	Less: assets to cover linked liabilities and external unit holders(b)	Group excluding assets to cover linked liabilities and external unit holders
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Investment properties	10,852	24	4	10,880			10,880	(1,095)	9,785
Investments accounted for using the equity method	72			72	41		113		113
Financial investments:									
Loans	3,373	6,235	1,014	10,622	1,199		11,821		11,821
Equity securities	36,027	49,551	14,310	99,888	70		99,958	(61,937)	38,021
Debt securities	83,862	32,993	21,402	138,257	1,846		140,103	(22,156)	117,947
Other investments	4,576	2,296	957	7,829	44	27	7,900	(58)	7,842
Deposits	11,131	211	1,227	12,569	84		12,653	(1,432)	11,221
Total financial investments	138,969	91,286	38,910	269,165	3,243	27	272,435	(85,583)	186,852
Total investments	149,893	91,310	38,914	280,117	3,284	27	283,428	(86,678)	196,750
Derivative liabilities	(1,007)	(645)	(837)	(2,489)	(150)	(190)	(2,829)	95	(2,734)
Total investments	148,886	90,665	38,077	277,628	3,134	(163)	280,599	(86,583)	194,016

(a)

Investments held by asset management operations are further split in note E2 to the consolidated financial statements in Item 18.

(b)

Prudential's Group statement of financial position includes the line by line investments of unit-linked and the consolidated unit-trusts and similar funds. In the table above, these amounts have been deducted in deriving the underlying investments in the right-hand column.

The disclosure below has been provided on the same basis as that included in previous Form 20-F submissions, with analysis focusing on the investments attributable to shareholders and consequently excluding those held to cover linked liabilities or attributable to unit holders of consolidated unit trusts and similar funds.

In addition to the detail provided below further analysis is included in the consolidated financial statements, in accordance with IFRS 7 'Financial Instruments: Disclosures'. The further analysis is included in notes D2, D3, D4, E2, G1 and G2 to Prudential's consolidated financial statements in Item 18.

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Prudential's Average Investment Return

The following table shows the income from the investments of Prudential's operations, net of derivative liabilities, by asset category for the periods indicated. This table does not include investment income from assets held to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds. Average investment return has been calculated using the average of opening and closing balances for the appropriate asset.

	Year Ended 31 December					
	2012		2011		2010	
	Average investment return	Amount	Average investment return	Amount	Average investment return	Amount
		£m		£m		£m
Investment properties						
Net investment income	**5.2%**	**512**	5.6%	557	5.6%	564
Net realised investment (losses) gains	**0.8%**	**81**	(1.0)%	(101)	0%	4
Net unrealised investment (losses) gains	**(0.6)%**	**(57)**	3.5%	354	5.2%	527
Ending assets		**9,785**		9,803		10,260
Investments accounted for using the equity method						
Net realised investment gains	**0.0%**		0%		78.5%	30
Ending assets		**113**		70		71
Loans						
Net investment income	**4.6%**	**500**	4.7%	442	5.2%	469
Net realised investment (losses) gains	**(0.3)%**	**(37)**	0%	1	(0.3)%	(26)
Net unrealised investment gains	**(0.6)%**	**(62)**	0.5%	46	(0.1)%	(10)
Ending assets		**11,821**		9,714		9,261
Equity securities						
Net investment income	**2.6%**	**841**	2.8%	995	2.6%	948
Net realised investment gains	**7.8%**	**2,570**	4.2%	1,505	4.2%	1,500
Net unrealised investment gains (losses)	**(0.3)%**	**(99)**	(11.0)%	(3,959)	6.6%	2,368
Ending assets		**38,021**		34,261		37,800
Debt securities						
Net investment income	**4.5%**	**5,213**	4.9%	5,168	5.1%	4,823
Net realised investment gains (losses)	**2.9%**	**3,396**	1.9%	2,038	1.5%	1,422
Net unrealised investment gains (losses)	**1.0%**	**1,189**	8.5%	2,776	2.3%	2,209
Ending assets		**117,947**		108,590		101,398

Other investments (including derivative liabilities)						
Net investment income	**10.9%**	**514**	9.7%	394	0.3%	13
Net realised investment (losses) gains	**(7.2)%**	**(340)**	0.6%	23	(11.0)%	(403)
Net unrealised investment (losses) gains	**13.1%**	**620**	8.5%	347	8.2%	299
Ending assets, net of derivative liabilities		**5,108**		4,444		3,693
Deposits						
Net investment income	**0.9%**	**90**	0.8%	78	0.5%	56
Ending assets		**11,221**		9,164		9,202
Total						
Net investment income	**4.1%**	**7,670**	4.4%	7,634	4.2%	6,874
Net realised investment gains (losses)	**3.1%**	**5,670**	2.0%	3,466	1.5%	2,526
Net unrealised investment gains (losses)	**0.9%**	**1,591**	(0.3)%	(436)	3.3%	5,394
Ending assets, net of derivative liabilities		**194,016**		176,046		171,685

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Prudential's Insurance Investment Strategy and Objectives

Prudential's insurance investments support a range of businesses operating in many geographic areas. Each of the operations formulates a strategy based on the nature of its underlying liabilities, its level of capital and its local regulatory requirements.

Internal funds under management

Prudential manages 77 per cent of its group funds principally through its fund management businesses, M&G in the United Kingdom, PPM America in the United States and Eastspring Investments in Asia. The remaining 23 per cent of the Group's funds mainly relate to assets held to back unit-linked, unit trust and variable annuity liabilities.

In each of the operations, local management analyses the liabilities and determines asset allocation, benchmarks and permitted deviations from these benchmarks appropriate for its operation. These benchmarks and permitted deviations are agreed with internal fund managers, who are responsible for implementing the specific investment strategy through their local fund management operations.

Investments Relating to UK Insurance Business

Strategy

In the United Kingdom, Prudential tailors its investment strategy for long-term business, other than unit-linked business, to match the type of product a portfolio supports. The primary distinction is between with-profits portfolios and non-participating portfolios, which include the majority of annuity portfolios. Generally, the objective is to maximise returns while maintaining investment quality and asset security and adhering to the appropriate government regulations.

Consistent with the product nature, in particular regarding guarantees, the with-profits fund's investment strategy emphasises a well-diversified equity portfolio (containing some international equities), real estate (predominantly in the United Kingdom), UK and international fixed income securities and cash.

For Prudential's UK pension annuities business and other non-participating business the objective is to maximise profits while ensuring stability by closely matching the cash flows of assets and liabilities. To achieve this matching, the strategy is to invest in fixed income securities of appropriate maturity dates.

For Prudential's unit-linked business, the primary objective is to maximise investment returns subject to following an investment policy consistent with the representations Prudential has made to its unit-linked product policyholders.

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Investments

The following table summarises the total investments, net of derivative liabilities, of the UK insurance business at 31 December 2012.

	At 31 December 2012					
	SAIF	**PAC**	**Other**	**Total**	**Less: assets to cover linked liabilities and external unit holders Less:(a)**	**Total excluding assets to cover linked liabilities and external unit holders**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Investment properties	**500**	**8,159**	**2,193**	**10,852**	**(1,096)**	**9,756**
Investment accounted for using the equity method			**72**	**72**		**72**
Financial investments:						
Loans	**116**	**1,993**	**1,264**	**3,373**		**3,373**
Equity securities	**2,070**	**19,875**	**14,082**	**36,027**	**(13,077)**	**22,950**
Debt securities	**3,864**	**46,643**	**33,355**	**83,862**	**(7,151)**	**76,711**
Other investments	**283**	**3,958**	**335**	**4,576**	**(11)**	**4,565**
Deposits	**910**	**8,395**	**1,826**	**11,131**	**(822)**	**10,309**
Total financial investments	**7,243**	**80,864**	**50,862**	**138,969**	**(21,061)**	**117,908**
Total investments	**7,743**	**89,023**	**53,127**	**149,893**	**(22,157)**	**127,736**
Derivative liabilities	**(36)**	**(652)**	**(319)**	**(1,007)**	**95**	**(912)**
Total investment, net of derivative liabilities	**7,707**	**88,371**	**52,808**	**148,886**	**(22,062)**	**126,824**

(a)

Please refer to the notes in the total Group investments table.

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The following table shows additional analysis of the investments relating to Prudential's UK insurance business, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, at 31 December 2012. The 'Other' column includes investments relating to solvency capital of unit-linked funds and investments relating to non-life long-term business.

	At 31 December 2012					
	With-Profits	PRIL	SAIF	Other	Total	Total
	£m	£m	£m	£m	£m	%
Investment properties	7,873	1,174	500	209	9,756	7.7
Investments accounted for using the equity method				72	72	0.1
Financial investments:						
Loans:						
Mortgage loans	1,289	150	22	1,108	2,569	
Policy loans	9		7		16	
Other loans	696	5	87		788	
Total loans and receivables	1,994	155	116	1,108	3,373	2.7
Equity securities:						
United Kingdom:						
Listed	9,363	2	1,066	82	10,513	
Unlisted	642		3	1	646	
Total United Kingdom	10,005	2	1,069	83	11,159	8.8
International:						
United States	1,073		97		1,170	
Europe (excluding the United Kingdom)	5,489		432		5,921	
Japan	1,035		116		1,151	
Pacific (excluding Japan)	1,592		173	6	1,771	
Other	1,594	1	183		1,778	
Total international	10,783	1	1,001	6	11,791	9.3
Total equity securities	20,788	3	2,070	89	22,950	18.1
Debt securities:						
UK government	2,182	2,141	120	604	5,047	
US government	966		187		1,153	
Other	42,653	21,597	3,557	2,704	70,511	
Total debt securities	45,801	23,738	3,864	3,308	76,711	60.5
Other investments:						
Other financial investments	3,004		214		3,218	
Derivative assets	953	324	69	1	1,347	
Total other investments	3,957	324	283	1	4,565	3.6
Deposits	8,395	669	910	335	10,309	8.0
Total investments	88,808	26,063	7,743	5,122	127,736	100.7

Derivative liabilities	**(619)**	**(256)**	**(36)**	**(1)**	**(912)**	**(0.7)**
Total investment, net of derivative liabilities	**88,189**	**25,807**	**7,707**	**5,121**	**126,824**	**100.0**

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Equity Securities

Prudential's UK insurance operations, had £22,950 million invested in equities at 31 December 2012 excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds. Most of these equities support Prudential Assurance's with-profits fund and the SAIF fund, both of which are managed using the same general investment strategy.

The following table shows the geographic spread of this equity portfolio by market value in accordance with the policies described in note A4 to the consolidated financial statements in Item 18.

At 31 December 2012
Market Value

	£m	%
United Kingdom	**11,159**	**48.6**
United States	**1,170**	**5.1**
Europe (excluding United Kingdom)	**5,921**	**25.8**
Japan	**1,151**	**5.0**
Pacific (excluding Japan)	**1,771**	**7.7**
Other	**1,778**	**7.8**
Total	**22,950**	**100.0**

The UK equity holdings are well diversified. Prudential held equities in 378 UK companies at 31 December 2012. The ten largest holdings in UK equities at 31 December 2012 amounted to £3,569 million, accounting for 15.5 per cent of the total UK equity holdings of £22,950 million supporting the UK insurance operations. The following table shows the market value of the ten largest holdings in UK equities at 31 December 2012.

At 31 December 2012

Market Value	Percentage of Total UK equities
£m	%
BP **511**	**2.2**
HSBC Holdings **441**	**1.9**
British American Tobacco **431**	**1.9**
Vodafone Group **425**	**1.9**
GlaxoSmithKline **414**	**1.8**
Royal Dutch Shell **353**	**1.5**
Rio Tinto **351**	**1.5**
Diageo **246**	**1.1**
Unilever **203**	**0.9**
Imperial Tobacco **194**	**0.8**
Total **3,569**	**15.5**

A wide variety of industry sectors are represented in Prudential's equity portfolio. At 31 December 2012, within the £11,159 million in UK equities supporting the UK insurance operations, Prudential had £9,802 million, or 87.8 per cent of the holdings, invested in ten industries. The following table shows

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the primary industry concentrations based on market value of the portfolio of UK equities relating to the UK insurance business at 31 December 2012.

	At 31 December 2012	
	Market Value	Percentage of Total UK equities
	£m	%
Banks	2,053	18.4
Oil & gas producers	1,694	15.2
Pharmaceuticals & biotechnology	1,197	10.7
Mining	1,032	9.2
Mobile telecommunications	726	6.5
Tobacco	662	5.9
Financial services	636	5.7
Travel & leisure	614	5.5
Support services	598	5.4
Media	590	5.3
Total	9,802	87.8

Debt Securities

At 31 December 2012, of the debt securities held by the UK insurance operations, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, 91.9 per cent were issued by corporations and overseas governments other than the US, 6.6 per cent were issued or guaranteed by the UK government and 1.5 per cent were issued or guaranteed by the US government. These guarantees relate only to payment and, accordingly, do not provide protection against fluctuations in market price that may occur during the term of the fixed income securities.

The following table shows the market value of the debt securities portfolio by maturity at 31 December 2012, in accordance with the policies described in note A4 to the consolidated financial statements in Item 18.

	At 31 December 2012 Market Value	
	£m	%
Securities maturing:		
Within one year	1,112	1.4
Over one year and up to five years	10,226	13.3
Over five years and up to ten years	17,733	23.1
Over ten years and up to fifteen years	11,255	14.7
Over fifteen years	36,385	47.5
Total debt securities	76,711	100.0

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The following table shows debt securities by rating:

At 31 December 2012
Market Value

	£m	%
S&P AAA	**8,596**	**11.2**
S&P AA+ to AA-	**8,754**	**11.4**
S&P A+ to A-	**21,002**	**27.4**
S&P BBB+ to BBB-	**16,213**	**21.1**
S&P Other	**2,867**	**3.7**
	57,432	**74.8**
Moody's Aaa	**7,177**	**9.4**
Moody's Aa1 to Aa3	**1,288**	**1.7**
Moody's A1 to A3	**858**	**1.1**
Moody's Baa1 to Baa3	**1,167**	**1.5**
Moody's Other	**227**	**0.3**
	10,717	**14.0**
Fitch	**501**	**0.7**
Other	**8,061**	**10.5**
Total debt securities	**76,711**	**100.0**

*

Further information is provided in note D2(c) to the consolidated financial statements in Item 18.

In the table above, Standard & Poor's (S&P) ratings have been used where available. For securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative. Where no external ratings are available, internal ratings produced by the Group's asset management operation, which are prepared on the Company's assessment of a comparable basis to external ratings, are used where possible. Further information is provided in note D2(c) to the consolidated financial statements in Item 18.

Real Estate

At 31 December 2012, Prudential's UK insurance operations, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, had £9,756 million of investments in real estate. The following table shows the real estate portfolio by type of investment. The real estate investments are shown at market value in accordance with the policies described in note A4 to the consolidated financial statements in Item 18.

At 31 December 2012
Market Value

	£m	%
Office buildings	**3,530**	**36.2**
Shopping centers/commercial	**4,111**	**42.1**
Retail warehouses/industrial	**1,500**	**15.4**
Development	**465**	**4.8**
Other	**150**	**1.5**
Total	**9,756**	**100**

Approximately 44.9 per cent of the UK held real estate investment is located in London and Southeast England with 36.3 per cent located throughout the rest of the UK and the remaining 18.8 per cent located overseas.

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Investments Relating to Prudential's US Insurance Business

Strategy

The investment strategy of the US insurance operations, for business other than the variable annuity business, is to maintain a diversified and largely investment grade debt securities portfolio that maintains a desired investment spread between the yield on the portfolio assets and the rate credited on policyholder liabilities. Interest rate scenario testing is continually used to monitor the effect of changes in interest yields on cash flows, the present value of future profits and interest rate spreads.

The investment portfolio of the US insurance operations consists primarily of debt securities, although the portfolio also contains investments in mortgage loans, policy loans, common and preferred stocks, derivative instruments, cash and short-term investments and miscellaneous other investments.

Investments

The following table shows total investments, net of derivative liabilities, relating to the US insurance operations at 31 December 2012.

	31 December 2012		
	Variable annuity separate account assets	Fixed annuity, GIC and other business	Total
	£m	£m	£m
Investment properties		24	24
Financial investments:			
Loans		6,235	6,235
Equity securities	49,298	253	49,551
Debt securities		32,993	32,993
Other investments		2,296	2,296
Deposits		211	211
Total financial investments	49,298	41,988	91,286
Total investments	49,298	42,012	91,310
Derivative liabilities		(645)	(645)
Total investment, net of derivative liabilities	49,298	41,367	90,665

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The following table further analyses the investments, net of derivative liabilities of the US insurance operations, excluding the separate account investments supporting the variable annuity business, at 31 December 2012.

31 December 2012

	£m	%
Non-institutional		
Investment properties	**24**	**0.1**
Loans	**5,941**	**14.4**
Equity securities	**196**	**0.5**
Debt Securities		
Corporate securities	**21,402**	**51.6**
Government securities	**4,113**	**10.0**
Residential mortgage-backed securities	**2,271**	**5.5**
Commercial mortgage-backed securities	**2,405**	**5.8**
Other debt securities	**497**	**1.2**
Total debt securities	**30,688**	**74.1**
Other investments	**2,092**	**5.1**
Deposits	**211**	**0.5**
Derivative liabilities	**(353)**	**(0.9)**
Total non-institutional	**38,799**	**93.8**
Institutional		
Investment properties		
Loans	**294**	**0.7**
Equity securities	**57**	**0.1**
Debt Securities		
Corporate securities	**1,839**	**4.5**
Government securities	**13**	
Residential mortgage-backed securities	**129**	**0.3**
Commercial mortgage-backed securities	**234**	**0.6**
Other debt securities	**90**	**0.2**
Total debt securities	**2,305**	**5.6**
Other investments	**204**	**0.5**
Deposits		
Derivative liabilities	**(292)**	**(0.7)**
Total institutional	**2,568**	**6.2**
Total		
Investment properties	**24**	**0.1**
Loans	**6,235**	**15.1**
Equity securities	**253**	**0.6**
Debt Securities		
Corporate securities	**23,241**	**56.1**
Government securities	**4,126**	**10.0**
Residential mortgage-backed securities	**2,400**	**5.8**
Commercial mortgage-backed securities	**2,639**	**6.4**
Other debt securities	**587**	**1.4**
Total debt securities	**32,993**	**79.7**

Other investments	**2,296**	**5.6**
Deposits	**211**	**0.5**
Derivative liabilities	**(645)**	**(1.6)**
Total	**41,367**	**100.0**

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Under IFRS, for the insurance operations, debt securities are shown at fair value and loans are at amortised cost with the exception of certain policy loans which are held to back liabilities for funds withheld under reinsurance arrangements, which are also accounted on a fair value basis. Equity securities and investment properties are shown at fair value. The fair value of unlisted securities is estimated by Jackson using independent pricing services or analytically determined values.

Debt Securities

Corporate Securities

At 31 December 2012, the US insurance operations had £23,241 million of corporate securities representing 56.2 per cent of the US insurance operations total investments excluding separate account investments. Of the £23,241 million, £19,699 million consisted of debt securities that are publicly traded or trade under Rule 144A under the Securities Act of 1933, as amended ('Rule 144A') and £3,542 million consisted of investments in non-Rule 144A privately placed fixed income securities. Rule 144A is a 1990 SEC rule that facilitates the resale of privately placed securities that are without SEC registration to qualified institutional investors. The rule was designed to develop a more liquid and efficient institutional resale market for unregistered securities.

For statutory reporting in the US, debt securities are classified into six quality categories specified by the Securities Valuation Office of the National Association of Insurance Commissioners (NAIC). The categories range from Class 1 (the highest) to Class 6 (the lowest). Performing securities are designated as Classes 1 to 5. Securities in or near default are designated Class 6. Securities designated as Class 3, 4, 5 and 6 are non-investment grade securities. Generally, securities rated AAA to A by nationally recognised statistical ratings organisations are reflected in Class 1, BBB in Class 2, BB in Class 3 and B and below in Classes 4 to 6. If a designation is not currently available from the NAIC, Jackson's investment adviser, PPM America, provides the designation for the purposes of disclosure below.

The following table shows the quality of the publicly traded and SEC Rule 144A debt securities by NAIC classifications:

	2012 Carrying value		**2011 Carrying value**	
	£m	**% of total**	**£m**	**% of total**
NAIC designation:				
1	**7,575**	**39**	6,338	39
2	**11,096**	**56**	9,002	55
3	**681**	**3**	723	5
4	**315**	**2**	204	1
5	**27**		10	
6	**5**		4	
	19,699	**100**	16,281	100

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The following table shows the quality of the non-SEC Rule 144A private placement portfolio by NAIC classifications:

	2012 Carrying value		2011 Carrying value	
	£m	% of total	£m	% of total
NAIC designation:				
1	**1,392**	**39**	1,262	39
2	**2,067**	**59**	1,835	58
3	**66**	**2**	81	3
4	**3**		8	
5	**14**		12	
6				
	3,542	**100**	3,198	100

Residential Mortgage-Backed Securities

At 31 December 2012, the US insurance operations had £2,400 million of residential mortgage-backed securities, representing 5.8 per cent of US insurance operations total investments, excluding separate account investments. At 31 December 2012, of the £2,400 million, 2.4 per cent of this total were rated AAA. (Standard & Poor's ratings have been used where available and for securities where Standard & Poor's ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative).

The primary investment risk associated with residential mortgage-backed securities is that a change in the interest rate environment or other economic conditions could cause payment of the underlying obligations to be made slower or quicker than was anticipated at the time of their purchase. If interest rates decline, then this risk is called 'pre-payment risk' and the underlying obligations will generally be repaid quicker when the yields on reinvestment alternatives are lower. Alternatively, if interest rates rise, the risk is called 'extension risk' and the underlying obligations will generally be repaid slower when reinvestment alternatives offer higher returns. Residential mortgage-backed securities offer additional yield to compensate for these risks. The US operations can manage pre-payment risk, in part, by reducing crediting rates on its products.

Commercial Mortgage-Backed Securities

At 31 December 2012, the US insurance operations had £2,639 million of commercial mortgage-backed securities, representing 6.4 per cent of US insurance operations total investments, excluding separate account investments. 39.7 per cent of this total were rated AAA (Standard & Poor's ratings have been used where available and for securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative). Due to the structures of the underlying commercial mortgages, these securities do not present the same pre-payment or extension risk as residential mortgage-backed securities.

Other Debt Securities

At 31 December 2012, the US insurance operations had £2,296 million of other debt securities, representing 5.6 per cent of US insurance operations total investments, excluding separate account investments.

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Loans

At 31 December 2012, loans totalled £6,235 million, representing 15.1 per cent of US insurance operations total investments, excluding separate account investments. Of the total, £3,543 million related to commercial mortgage loans and £2,692 million to policy loans. Of the £2,692 million policy loans, £1,842 million were held to back the liabilities for funds withheld under reinsurance arrangements attaching to the purchase of REALIC in 2012 (as explained further in note I1 to the Prudential's consolidated financial statements in Item 18).

Commercial Mortgage Loans

At 31 December 2012, commercial mortgage loans represented 8.6 per cent of US insurance operations total investments excluding separate account investments. The average loan size is £6.4 million, collaterised by properties located in the United States.

Jackson has addressed the risk of these investments by building a portfolio that is diverse both in geographic distribution and property type.

The property types are mainly industrial, multi-family residential, suburban office, retail and hotel. The breakdown of the market value by property type is as follows:

	31 December 2012
	%
Industrial mortgage loans	**29.3**
Multi-family residential mortgage loans	**24.8**
Retail mortgage loans	**18.5**
Suburban office mortgage loans	**16.8**
Hotel mortgage loans	**10.2**
Other loans	**0.4**
Total	**100.0**

The following table shows the geographic split of the collateral for these loans:

	31 December 2012
	%
California	**12.9**
Florida	**9.1**
Georgia	**6.5**
Illinois	**6.7**
Texas	**9.7**
Other (sum of all states < 5% each)	**55.1**
Total	**100.0**

Commercial mortgages generally involve more credit risk than residential mortgages due to several factors, including larger loan size, general and local economic conditions, local real estate conditions and the credit quality of the underlying tenants for the properties. Jackson's investment policy and strict underwriting standards are designed to reduce these risks while maintaining attractive yields. In contrast to residential mortgage loans, commercial mortgage loans have minimal or no pre-payment and extension risk.

Policy Loans

Policy loans represented 6.5 per cent of US insurance operations total investments, excluding separate account investments at 31 December 2012. Policy loans are fully secured by individual life insurance policies or annuity policies and are contractual arrangements made under the policy. As described above, £1,842 million out of the £2,692 million policy loans were held to back the liabilities for funds withheld under reinsurance arrangements attaching to the purchase of REALIC in 2012.

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Equity Securities

Equity securities supporting US insurance operations, excluding separate account investments, totaled £253 million at 31 December 2012.

Other

Other financial investments of £2,296 million, representing 5.6 per cent of US insurance operations total investments, excluding separate account investments at 31 December 2012 were made up of £769 million of limited partnership interests and derivative assets of £1,546 million. See also note D3 to the Prudential's consolidated financial statements in Item 18 for further details on the use of derivatives by the US insurance operations.

The largest investment in the limited partnerships category is a £109 million interest in the PPM America Private Equity Fund. The remainder of this category consists of diversified investments in 166 other partnerships managed by independent money managers that generally invest in various equity and fixed income loans and securities.

Investments Relating to Asian Insurance Business

Prudential's Asian insurance operations' investments, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, largely support the business of Prudential's Singapore, Hong Kong, Malaysia, and Japan operations.

The following table shows Asia's investments, net of derivative liabilities, at 31 December 2012. In this table, investments are valued in accordance with the policies described in note A4 to the consolidated financial statements in Item 18.

	31 December 2012						
	With-profits business	Unit-linked assets	Other	Total	Less: assets to cover linked liabilities and external unit holders(a)	Total excluding assets to cover linked liabilities and external unit holders	
	£m	£m	£m	£m	£m	£m	%
Investment properties			4	4		4	
Financial investments:							
Loans	600		414	1,014		1,014	4.4
Equity securities	3,160	10,491	659	14,310	(1,884)	12,426	54.5
Debt securities	11,495	3,194	6,713	21,402	(12,759)	8,643	37.9
Other investments	504	47	406	957	(47)	910	4.0
Deposits	165	574	488	1,227	(574)	653	2.9
Total financial investments	15,924	14,306	8,680	38,910	(15,264)	23,646	103.7
Total investments	15,924	14,306	8,684	38,914	(15,264)	23,650	103.7
Derivative liabilities	(446)		(392)	(838)		(838)	(3.7)
Total investment, net of derivative liabilities	15,478	14,306	8,292	38,076	(15,264)	22,812	100.0

(a)

Please refer to notes in the total Group investments table.

Prudential manages interest rate risk in Asia by matching liabilities with fixed interest assets of the same duration to the extent possible. Asian fixed interest markets however generally have a relatively

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short bond issue term, which makes complete matching challenging. A large proportion of the Hong Kong liabilities are denominated in US dollars and Prudential holds US fixed interest securities to back these liabilities.

Debt Securities

The following table shows rating categorisation of the debt security investments of Prudential Corporation Asia's long-term insurance fund, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, at 31 December 2012.

	31 December 2012 Market Value	
	£m	%
S&P AAA	210	2.4
S&P AA+ to AA-	1,931	22.3
S&P A+ to A-	1,150	13.3
S&P BBB+ to BBB-	492	5.7
S&P Other	849	9.8
	4,632	53.6
Moody's Aaa	1,050	12.1
Moody's Aa1 to Aa3	126	1.5
Moody's A1 to A3	100	1.2
Moody's Baa1 to Baa3	81	0.9
Moody's Other	1	
	1,358	15.7
Fitch	440	5.1
Other*	2,213	25.6
Total debt securities	8,643	100.0

*

Further information is provided in note D4(d) to the consolidated financial statements in item 18.

Equity Securities

The following table shows a geographic analysis of equity security investments of Asia's long-term insurance fund, excluding assets to cover linked liabilities and those attributable to external unit holders of consolidated unit trusts and similar funds, at 31 December 2012.

	31 December 2012 Market Value	
	£m	%
Hong Kong	7,784	62.6
Singapore	3,829	30.8
Taiwan	381	3.1

Malaysia	**235**	**1.9**
Other	**197**	**1.6**
Total	**12,426**	**100.0**

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Description of Property Corporate Property

As at 31 December 2012, Prudential's UK headquartered businesses occupied approximately 48 properties in the United Kingdom, Europe and India. These properties are primarily offices with some ancillary storage and warehouse facilities. Prudential's global headquarters are located in London. Of the remainder, the most significant are offices in London and Reading in England, Stirling in Scotland and Mumbai in India. The property in Stirling is held on a freehold basis, and is leased by the business from PAC's long-term fund. The rest of the properties occupied by Prudential's UK based businesses, in the UK and India, are held leasehold. In Europe, 15 of the properties are occupied leasehold and the rest (four) are short-term serviced offices. The leasehold properties range in size from 500 to 135,000 sq. ft. Overall, the UK, Europe and Mumbai occupied property portfolio totals approximately 780,000 sq. ft.

Prudential's UK headquartered businesses also hold one surplus owned property and approximately 46 surplus leasehold properties in the United Kingdom, spread geographically throughout the country. There are also three in Dublin, Ireland. This surplus accommodation (i.e. not occupied by the Group) totals approximately 365,000 sq. ft. There is also one surplus land holding in the United Kingdom, of 43 acres. A high proportion of the surplus estate has been sublet to third party occupiers generating income for the Group to cover this overhead. As at 31 December 2012 vacancy within the surplus estate stood at 59,000 sq ft.

In the United States, Prudential owns Jackson National Life's executive and principal administrative office located in Michigan. Prudential owns a total of seven facilities in Lansing, Michigan, which total 595,272 sq. ft. Prudential also leases premises in Michigan, Colorado, Tennessee, California, Illinois, New York, New Jersey, Georgia, Florida, Wisconsin, Massachusetts, Connecticut, New Hampshire, Pennsylvania, Indiana and North Dakota for certain of its operations. Prudential holds 29 operating leases with respect to office space, throughout the United States. The leasehold properties range in size from 500 180,000 sq. ft. In the United States, Prudential owns and leases a total of approximately 1,141,708 sq. ft. of property. In addition to the owned and leased properties, Prudential also owns a total of 238 acres of surplus land. This property is all located in Lansing, Michigan.

In Asia, Prudential owns or leases properties principally in Hong Kong, Singapore, Malaysia, Indonesia, Thailand, Philippines, China (JV), Taiwan, Japan, Vietnam, India (JV), Korea, United Arab Emirates and Cambodia.

Within these countries, Prudential owns 20 property assets, ranging from office space to land holdings. The break down of these owned assets by country is as follows:

Malaysia: six owned assets All office space totaling 12,315 sq. ft.

Philippines: two owned assets All office space totaling 4,278 sq. ft.

Singapore: one owned asset Office space totaling 11,883 sq. ft.

Thailand: eleven owned assets All surplus land holdings totaling 73,832 sq. ft.

Prudential has (excluding India), a total of 439 operating leases, (external and intercompany leases), totaling approximately 4.28 million square feet of property.

In India, Prudential holds a minority stake (26%) with ICICI in a joint venture which holds the property interests. The property is occupied by the ICICIPru Life and ICICIPru AMC businesses. The holding comprises approximately 700 leased properties, totaling approximately 1.3 million sq. ft. There is one owned and occupied asset comprising approximately 30,000 sq. ft. in Mumbai.

Prudential Corporation Asia's real estate strategy moving forward involves consolidation of its existing property portfolio to support its local business strategies throughout the region, to take advantage of opportunities in the regional markets in securing long term cost savings for the business while maintaining competitive advantage.

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There have been no property transactions subsequent to 31 December 2012 which would have a material impact on the financial position of Prudential.

Prudential believes that its facilities are suitable for the conduct of its businesses. We periodically review our space requirements and may acquire or lease new space as needed to accommodate any future needs of our businesses. Prudential's operating leases have no material commercial value.

In summary, Prudential owns 17 properties which it also occupies and which are accounted for as owner occupied. These properties are comprised of 9 in Asia, one in the UK and seven in the US. ICICIPru also owns and occupies one property in India. The total value of Prudential's owner occupied properties at 31 December 2012 was £216 million. This represents less than 0.1 per cent of Prudential's total assets.

Prudential is the lessee under 509 operating leases used as office accommodation, comprising 439 leases held by the Asian business, 29 leases held by the US business and 41 leases held by the UK businesses. For the UK based businesses, Prudential holds four short-term serviced offices.

Investment Interests

Prudential also holds interests in properties within its investment portfolios accounted for as investment property. At 31 December 2012 the total value of investment properties was £10,880 million and comprised 484 properties held by the UK, 3 held by the US and 21 held by the Asia business. In total they comprised 3.5 per cent of Prudential's total assets. The UK business' holdings account for over 99 per cent by value of the total investment properties.

Competition

General

There are other significant participants in each of the financial services markets in which Prudential operates. Its competitors include both mutual and stock financial companies. In addition, regulatory and other developments in many of Prudential's markets have blurred traditional financial service industry lines and opened the market to new competitors and increased competition. In some of the Prudential's markets, other companies may have greater financial resources, allowing them to benefit from economies of scale, and may have stronger brands than Prudential does in that market.

The principal competitive factors affecting the sale of Prudential's products in its chosen markets are:

- price and yields offered,
- financial strength and ratings,
- commission levels, charges and other expenses,
- range of product lines and product quality,
- brand strength, including reputation and quality of service,
- distribution channels,

investment management performance, and

historical bonus/contract enhancement and bonus interest levels.

An important competitive factor is the ratings Prudential receives in some of its target markets, most notably in the United States, from recognised rating organisations. The intermediaries with whom the Prudential works, including financial advisers, tied agents, brokers, wholesalers and financial institutions consider ratings as one factor in determining which provider to purchase financial products from.

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Prudential offers different products in its different markets in Asia, the United Kingdom and the United States and, accordingly, faces different competitors and different types of competition in these markets. In all of the markets in which Prudential operates, its products are not unique and, accordingly, it faces competition from market participants who manufacture a varying range of similar and identical products.

Asia

The competitive landscape across the Asia Pacific region differs widely by geographical market, reflecting differing levels of market maturity and regulation. Prudential's competitors include both the subsidiaries of global life insurers and local domestic (including state-owned) entities. Subsidiaries of global life insurance groups that operate in the Asia Pacific region tend to operate in multiple markets in the region, and some currently have top five market shares in a small number of markets. The majority of local domestic life insurers in the Asia Pacific region remain focused on their core home markets. The developed and liberalised markets of Hong Kong and Singapore are dominated by subsidiaries and branches of global life insurance groups. The developing markets in South East Asia such as Indonesia, Vietnam and the Philippines also see a high level of participation by global life insurance groups. The large and relatively mature markets of Korea and Taiwan are dominated by local domestic insurers. In certain countries with continued foreign ownership restrictions (such as China and India), the life insurance markets are dominated by local domestic insurers or by joint venture entities between global insurance groups and local companies.

The global life insurers that are Prudential's competitors in the Asia Pacific region include AIA, Allianz, Aviva, AXA, ING and Manulife. Other competitors relevant in some of Prudential's key markets include HSBC Life in Hong Kong, Hanwha Life (formerly Korea Life), Kyobo Life and Samsung Life in Korea, Thai Life in Thailand, Great Eastern in Singapore and Malaysia, and China Life, China Pacific and Ping An in China. Prudential's principal competitors in respect of its fund management operations across the region largely comprise multinational asset managers including Fidelity Fund Management, Deutsche Asset Management, Blackrock, UBS Global Asset Management, JP Morgan Asset Management and BNP Paribas IP.

United States

Prudential's insurance operations in the United States operate under the Jackson brand. Prudential is not affiliated with Prudential Financial, Inc. or its subsidiary, The Prudential Insurance Company of America.

Jackson's competitors in the United States include major stock and mutual insurance companies, mutual fund organisations, banks and other financial services companies. National banks, in particular, may become more significant competitors in the future for insurers who sell annuities, as a result of recent legislation, court decisions and regulatory actions. Jackson's principal life insurance company competitors in the United States include AIG, Hartford Life Inc., Prudential Financial, MetLife, Lincoln National, AXA Financial Inc., TIAA-CREF and Allianz.

Jackson does not have a career agency sales force to distribute its annuity products in the United States and, consequently, competes for distributors such as banks, broker-dealers and independent agents.

United Kingdom

Prudential's principal competitors include many of the major retail financial services and fund management companies operating in the United Kingdom. These companies include Aviva, Legal & General, Standard Life, Friends Life, Lloyds Banking Group, Aegon, AXA, Just Retirement, Zurich Financial Services, Fidelity, Invesco Perpetual, Jupiter, Threadneedle, Schroders and BlackRock. Prudential

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competes with other providers of financial products to be included on financial advisors' panels of preferred providers.

Intellectual Property

Prudential conducts business under the 'Prudential', 'Jackson', 'M&G' and 'Eastspring Investments' brand names and logos. It is also the registered owner of over 100 domain names, including 'www.prudential.co.uk', 'www.prudentialcorporation-asia.com','www.jackson.com','www.mandg.co.uk', 'www.eastspringinvestments.com' and 'www.pru.co.uk'.

Prudential does not operate in the United States under the Prudential name and there have been long-standing arrangements between it and Prudential Financial, Inc. and its subsidiary, the Prudential Insurance Company of America, relating to their respective uses of the Prudential name. Under these arrangements Prudential Financial Inc has the right to use the Prudential name in the Americas and certain parts of the Caribbean, Japan, Korea and Taiwan and Prudential has the right to use the name everywhere else in the world although third parties have rights to the name in certain countries.

Legal Proceedings

Prudential

Prudential and its subsidiaries are involved in various litigation matters. While an adverse ruling in any individual case may not in itself be material to Prudential, if applied across all similar cases, the potential liabilities may be more significant. Although the outcome of such matters cannot be predicted with certainty, management believes that the ultimate outcome of such litigation will not have a material adverse effect on the group's financial condition, results of operations or cash flows.

Jackson

Jackson is involved as a defendant in class action and other litigation substantially similar to class action and other litigation pending against many life insurance companies including a modal premium case and allegation of misconduct in the sale and administration of insurance products. Jackson generally accrues a liability for legal contingencies with respect to pending litigation once management determines that the contingency is probable and estimable. Accordingly, at 28 March 2013 Jackson had recorded an accrual of £8 million for class action litigation (31 December 2012: £18 million). Management, based on developments to date, believes that the ultimate disposition of the litigation is not likely to have a material impact on Jackson's financial condition or results of operations.

Sources

Throughout this annual report, Prudential describes the position and ranking of its overall business and individual business units in various industry and geographic markets. The sources for such descriptions come from a variety of conventional sources generally accepted as relevant business indicators by members of the financial services industry. These sources include information available from the Annuity Specs, Asia Asset Management Magazine, Asosiasi Asuransi Jiwa Indonesia, Association of British Insurers, Association of Vietnamese Insurers, Association of Unit Trusts and Investment Funds, Fitch, Hong Kong Federation of Insurers, Hong Kong Office of the Commissioner of Insurance, HSBC Global Research, Insurance Regulatory and Development Authority of India, Insurance Services Malaysia Berhad, Investment Management Association, Life Insurance Marketing and Research Association (LIMRA), Life Insurance Association of Malaysia, Life Insurance Association of Singapore, Life Insurance Association of Taiwan, Morningstar, Moody's, Neilsen Net Ratings, Propriety Research, Service Quality Management Group, SNL Financial, Standard & Poor's, Thai Life Assurance Association, The Asset Benchmark Research, The Advantage Group, Townsend and Schupp and UBS.

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SUPERVISION AND REGULATION OF PRUDENTIAL

Supervision and Regulation

Prudential's principal insurance and investment operations are in Asia, the United Kingdom (UK), and the United States (US). Accordingly, it is subject to applicable Asian, UK and US insurance and other financial services regulation which is discussed below.

Until 1 April 2013, the UK Financial Services Authority (the 'FSA'), as Prudential's 'lead supervisor' for the purposes of the EU's Insurance Groups Directive (the 'IGD'), played a principal role in assessing and ensuring the adequacy of Prudential's solvency and financial stability on a Group-wide basis. The FSA has now been replaced in this role by the Prudential Regulation Authority (the 'PRA') as part of reforms to the UK regulatory architecture and this role in supplementary Group-level supervision will also be enhanced under the new EU solvency framework, Solvency II. Both of these developments are discussed further below.

As well as co-ordinating EU-level local regulators in the context of the IGD, as both Prudential's parent company and a significant proportion of its global insurance operations are in the UK, the FSA also played an important co-ordinating role in regulatory initiatives at a global level. This role is less formal than within the EU and has depended principally on the various memoranda of understanding signed by the FSA with non-EU regulators, including in the US and Asia. In consequence, although the FSA's role as a lead supervisor has not restricted the role of individual local regulators or overridden the local insurance and other financial services regimes described in the following sections, the FSA's rules and its regulatory agenda have impacted (and it is expected that the PRA's rules and regulatory agenda will similarly impact) Prudential's operations globally.

Moreover, because the UK regulatory framework is considerably shaped and influenced by directives emanating from the EU, the significant Group-wide impact of such rules may, at times, result in legal and regulatory developments in the EU (including the evolving Solvency II framework discussed below) in turn having a significant impact on the business and operations of the Group as a whole.

In March 2013, Prudential plc and The Prudential Assurance Company Limited settled with the FSA over issues relating to Prudential's unsuccessful bid to acquire AIA, the Asian subsidiary of AIG, in early 2010. The companies agreed to pay fines totalling £30 million, in respect of a decision by the FSA that it and the UKLA should have been informed earlier about Prudential's contemplation of the potential transaction. The Group Chief Executive also agreed to be censured in respect of a decision by the FSA that it should have been informed earlier. Final Notices published on 27 March 2013 concerning these decisions accordingly represent the final resolution of the matter.

In a statement accompanying the Final Notices, the FSA stated that the investigation was into past events and did not concern the current conduct of the management of the Prudential Group. The FSA accepted that Prudential did consider their obligations in forming their assessment in respect of informing the regulator. Therefore, although the FSA considered that the circumstances of the breaches were serious, the FSA did not consider the breaches were reckless or intentional. Prudential has confirmed that the Group Chief Executive acted at all times in the interests of the Company and with the full knowledge and authority of the Board. Prudential works diligently to maintain close and positive relationships with its regulators, and the Group's relationship with its UK regulators continues to be good.

Global Regulatory Developments

Currently there are a number of regulatory developments globally which may impact the supervision of Prudential in the future, including the work of the Financial Stability Board (the 'FSB') (an international entity established to coordinate, develop and promote effective regulatory, supervisory and other financial sector policies in the interest of financial stability) on Globally Systemically Important

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Financial Institutions ('G-SIFIs') and the Common Framework for the Supervision of Internationally Active Insurance Groups ('ComFrame') being developed by the International Association of Insurance Supervisors ('IAIS').

As part of a global initiative to identify G-SIFIs, in May 2012, the IAIS published proposed assessment methodology for designating Globally Systemically Important Insurers (G-SIIs). For those groups that are designated by the FSB as G-SII then additional policy measures including enhanced supervision, introduction of recovery and resolution plans and higher loss absorbency requirements could be proposed. Further detail of the proposals is expected during 2013 and implementation is likely to be over a period of years. Furthermore, the FSA is considering the designation of Domestically Systemically Important Insurer (DSII) for those UK insurers that are significant in UK terms. It is not yet clear what the impact of this designation may be.

ComFrame is also being developed by the IAIS to provide common global requirements for supervision of insurance groups. The framework is designed to develop common principles for supervision and so may increase the focus of regulators in some jurisdictions. It is also possible that some prescriptive requirements, including group capital, could be proposed. Further clarity on ComFrame is expected during the second half of 2013.

UK Supervision and Regulation

The Financial Services and Markets Act 2000

Prudential's insurance and investment businesses in the UK are regulated under the Financial Services and Markets Act 2000 ('FSMA 2000'). In addition, those businesses are subject to various UK laws (for example, the Data Protection Act 1998 in relation to the processing of customer data and various Pension Acts) some of which require the relevant Prudential entity to be licensed or registered. There have been extensive amendments to the FSMA 2000 regime as a result of the Financial Services Act 2012 and the 'legal cutover' to a new regulatory regime on 1 April 2013, described below.

New regulatory regime

Until 1 April 2013, FSA was the single regulator for all authorised persons carrying on regulated activities in the financial services sector and was empowered to make rules and issue guidance in relation to a wide sphere of activity, encompassing the governance, conduct of business and the prudential supervision of firms. From 1 April 2013, the FSA itself ceased to exist and has been replaced by:

- The PRA, which oversees macro-prudential regulation of deposit-takers and insurers and some systemically important investment firms; and

- The Financial Conduct Authority ('FCA'), which has responsibility for conduct of business regulation for all authorised firms and the prudential regulation of firms not regulated by the PRA. The FCA has also inherited the majority of the FSA's market regulatory functions (excluding certain functions which sit with the Bank of England).

Transition to the new regulatory regime has principally involved the allocation of the FSA's functions and responsibilities between the PRA and FCA, although the PRA and FCA are also vested with some additional to those exercised previously by the FSA and their statutory objectives differ from those of the FSA.

The substantive content of the FSA's macro-prudential and conduct of business regulation prior to 1 April 2013, including that discussed below under 'Main features of regulation applicable to Prudential's insurance and investment business', has not been materially affected as a result of the legal cutover, although it is too early to predict whether or how the substantive content of such regulation (or its

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interpretation) might evolve differently under the altered statutory objectives and regulatory approaches of the PRA and the FCA.

The FSA's risk-based approach to regulation

The FSA employed a risk-based regulatory approach to supervision under the FSMA 2000 pursuant to which each regulated firm's risk was assessed by the FSA using a risk assessment methodology known as ARROW (Advanced Risk Response Operating Framework). This was a high-level review aimed at assessing the significance of a particular risk posing threats to the FSA's statutory objectives under the FSMA 2000.

Prudential was regarded by the FSA as a high impact firm in view of the nature and complexity of its business and, as such, has generally received ARROW assessments at least once in every two year regulatory period. Between ARROW visits, the FSA met regularly with members of senior management and persons holding controlled functions to understand developing strategy and challenges and the key issues arising, in particular any significant risks identified and how Prudential was mitigating these. This 'close and continuous' supervision was supported by focused (relating to a firm or group) and themed (relating to the industry or market as a whole) visits where appropriate. In advance of discussions, the FSA requested relevant mandatory management information at prescribed intervals, which helped to frame the agenda for these meetings.

The approach of the PRA and FCA

Close and regular contact between the PRA and FCA and senior management and those performing controlled functions is expected to continue to be a feature of the UK regulatory regime following 1 April 2013, but the ARROW process has not been adopted by either regulator. Both regulators will continue to focus on risk, but their approaches are informed by separate statutory objectives and will be pursued through distinct supervisory programmes.

The strategic objective of the FCA is to ensure that the relevant markets function well and its operational objectives are to secure an appropriate degree of protection for consumers, to protect and enhance the integrity of the UK financial system and to promote effective competition in the interests of consumers. To meet these objectives, the FCA's supervision model is based on three pillars: a 'Firm Systemic Framework' ('FSF'), involving preventative work through structured conduct assessment of firms; 'event-driven' work covering issues which occur outside a firm's assessment cycle; and thematic reviews focused on particular sectors of the market aimed at product issues which the FCA identifies as driving poor outcomes for consumers or endangering market integrity. The FSF will involve Prudential being subject to, amongst other initiatives, a business model and strategy analysis ('BMSA') to establish which assessment areas to prioritise over a two-year cycle.

The FCA divides the firms it supervises into one of four conduct classifications (C1-C4) based on a combination of a measure of a firm's potential impact on FCA objectives and the number of retail customers a firm has, with C1 being the highest risk. Prudential has been categorised as 'C2', the second highest risk category. Additionally, as a group also regulated by the PRA with subsidiaries that are prudentially regulated by the FCA, Prudential has been assigned one of four prudential classifications (P1-P4). Prudential's entities that the FCA prudentially regulates in the group have been categorised as 'P1' as they are considered prudentially critical.

The PRA's statutory obligation is to promote the safety and soundness of PRA-authorised persons but it also has an additional insurance-specific objective: to contribute to the securing of an appropriate degree of protection for those who are or may become policyholders. The PRA intends to weight its supervision towards those issues and those insurers that, in its judgment, pose the greatest risk to these objectives, conducting its assessment work on a continuous cycle.

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Compared with the approach adopted by the FSA, both the PRA and FCA intend to adopt a more judgment-led approach to supervision and to be more forward-looking in those judgments, i.e. assessing firms not just against current risks, but also against those which could plausibly arise in the future. The PRA has indicated that, for significant firms such as Prudential, it will, for example, conduct detailed analysis of their business model including forming its own projection of an insurer's ability to generate returns and the associated risks. In line with a more interventionist approach, the PRA has indicated that, if it believes that mitigating measures alone cannot adequately reduce material risks to safety and soundness and policyholder protection, it will require the insurer to change its business model.

Overview of FSMA 2000 regulatory regime

Principles for Businesses

An authorised firm is subject to a range of ongoing regulatory requirements of the FCA and, for dual-regulated firms, the PRA, including meeting at all times specified threshold conditions, including possession of adequate resources for the carrying on of its business and being fit and proper. A key feature of the FSA regime was the existence of 11 'Principles for Businesses', by which all authorised firms were expected to abide. These covered key areas such as the firm's relationship with the FSA and the need to act with integrity as well as to treat customers fairly. The Principles for Businesses will continue to be a feature of both PRA and FCA supervision although only certain of the Principles of Businesses have been adopted by the PRA. All have been adopted by the FCA.

Main features of regulation applicable to the Prudential's insurance and investment businesses

Supervision of management of authorised firms

Historically, the FSA closely supervised the management of authorised firms through the 'approved persons' regime, under which any appointment of persons who perform a 'controlled function', including functions that enable the exercise of significant influence over an authorised firm, must be pre-approved by the regulator. The approved persons regime continues to be administered by the PRA and the FCA, although certain additional controlled functions have been added under the new regime.

Intervention and enforcement

The FCA and PRA have extensive powers to investigate and intervene in the affairs of an authorised firm as well as extensive enforcement powers.

Certain of these intervention and enforcement powers are additional to those previously exercised by the FSA. For example, the FCA has powers to make temporary product intervention rules, allowing it block an imminent product launch or to stop an existing product, and is also able to require firms to withdraw or amend misleading financial promotions with immediate effect. Both the FCA and the PRA can also impose requirements on UK-incorporated unregulated parent undertakings that exert influence over authorised persons. The latter power is of particular potential relevance to the Group given that it is headed by a UK-incorporated unregulated parent undertaking but it remains to be seen how this new power will be used.

Conduct of Business Rules

The Conduct of Business Rules regulate the day-to-day conduct of business standards to be observed by authorised persons in carrying on regulated activities.

The scope and range of obligations imposed on an authorised firm under the Conduct of Business Rules varies according to the scope of its business and the range of its clients. Generally, however, the obligations imposed on an authorised firm by the Conduct of Business Rules will include the need to categorise its clients according to their level of sophistication, provide them with information about the

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firm, meet certain standards of product disclosure, ensure that promotional materials which it produces are clear, fair and not misleading, assess suitability when advising on certain products, manage conflicts of interest, report appropriately to its clients and provide certain protections in relation to client assets. Additional details of relevance to the insurance and investment businesses are discussed below.

Consumer Protection, the Financial Ombudsman Service ('FOS') and the Financial Services Compensation Scheme ('FSCS')

The consumer protection agenda in the UK is now within the remit of the FCA. The FCA's focus is on product scrutiny, sales practices and firms' culture, including assessment of how remuneration structures affect consumer outcomes. In addition, the FCA has a specific remit to promote competition within the financial services industry.

Authorised firms must have appropriate complaints handling procedures and the principles of complaints handling are defined in the FCA Handbook. However, once these procedures have been exhausted, qualifying complainants may turn to the FOS. The Ombudsman is empowered to order firms to pay fair compensation for loss and damage and may order a firm to take such steps as the Ombudsman determines to be just and appropriate in order to remedy a complaint.

The FSCS is intended to compensate individuals and other groups of 'eligible claimants', including certain trustees for claims against an authorised firm where the authorised firm is unable or unlikely to be able to meet those claims (generally, when it is insolvent or has gone out of business).

During 2012, the FSA undertook a comprehensive review of the FSCS funding model and made changes designed to ensure faster and more efficient payments by the FSCS to claimants. Further changes to the FSCS's comprehensive model were the subject of an FSA consultation (CP 12/16) which closed at the end of October 2012.

Following 1 April 2013, both the PRA and the FCA have rule-making powers for the FSCS and the FSCS is now accountable to both regulators.

Regulation of insurance business

Most of Prudential's subsidiaries that carry on insurance business in the UK, including PAC, Prudential Annuities Limited, Prudential Retirement Income Limited, Prudential Pensions Limited and Prudential Holborn Life Limited have become 'dual-regulated' following 1 April 2013, meaning that they are regulated by the PRA for prudential purposes and by the FCA for conduct purposes. The exceptions are Prudential Distribution Limited, Prudential Financial Planning Limited and Scottish Amicable ISA Managers Limited, which are regulated by the FCA only due to their business model.

Conduct of business requirements for insurance business

Authorised firms which advise and sell to retail customers packaged products such as life insurance policies are subject to detailed conduct of business obligations relating to product disclosure, assessment of suitability, the range and scope of the advice which the firm provides, and fee and remuneration arrangements.

The FSA launched the Retail Distribution Review ('RDR') in 2006 with the specific aim of addressing shortcomings in the retail investment market. On 31 December 2012, new rules took effect which, *inter alia*:

- required changes in how firms offering advice to retail customers present and describe the adviser services that they offer, including limiting the extent to which advisers can hold themselves out as 'independent';

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banned the payment of commission when a personal recommendation is made and required the adoption of 'adviser charging', whereby a firm must set and clearly disclose its tariff of charges and where these are to be facilitated by a product provider, the amount must not be determined by the provider and there must be clear distinction from any product charges;

imposed higher qualification requirements as well as continuing professional development and professional standards on advisers; and

introduced increased reporting requirements on firms in respect of their retail investment advisers.

The changes introduced by the RDR are having a broad-ranging impact on Prudential, including necessitating significant system changes, affecting decisions as to which products Prudential offers and the pricing of those products, as well as expanding UK regulatory reporting requirements. For further information on RDR, see 'UK Business Distribution' and Item 5, 'Operating and Financial Review and Prospects Introduction and Overview'.

Capital requirements for insurers

As noted above, in order to maintain authorised status under the FSMA 2000, firms must continue to satisfy certain threshold conditions, which, among other things, require firms to have adequate resources for the carrying on of their business. The rules which govern the prudential regulation of insurers are currently found in the General Prudential Sourcebook ('GENPRU'), Prudential Sourcebook for Insurers ('INSPRU') and the Interim Prudential Sourcebook for Insurers ('IPRU (INS)') in the PRA Handbook. Solvency II, described further below, is the European Commission's project to reform prudential regulation of European Union insurers.

The rules require an insurer to prepare and submit to the PRA its own assessment of its capital requirements, known as an individual capital assessment ('ICA'), based on the risks it faces. Where the PRA disagrees with a firm's capital requirement assessment, it will issue individual capital guidance ('ICG'), including at times as a requirement.

Insurance companies must maintain assets sufficient to meet the relevant capital requirement at all times in respect of both long-term insurance and general insurance business undertaken by the company. The calculation of such capital requirements is dependent on the type and amount of insurance business a company writes. Under the rules in GENPRU, an insurer must hold capital resources equal at least to the Minimum Capital Requirement (the 'MCR'). Insurers with with-profits liabilities of £500 million or more must hold capital equal to the higher of MCR and the Enhanced Capital Requirement (the 'ECR'). The ECR is intended to provide a more risk responsive and 'realistic' measure of a with-profits insurer's capital requirements, whereas the MCR is broadly speaking equivalent to the previously required minimum margin under the IPRU (INS) and satisfies the current minimum EU standards.

The ECR is determined as the higher of two separate measurements of the firm's financial resources requirements, reflecting capital as determined by reference to two bases for calculating liabilities (regulatory and realistic), which is referred to as the 'twin peaks' approach. The regulatory basis reflects strict contractual liabilities whereas the realistic basis includes more discretionary but expected benefits, including those required to treat customers fairly.

Long-term business assets and liabilities those assets and liabilities relating to, broadly, life and health insurance policies must be segregated from the assets and liabilities attributable to non-life insurance business or to shareholders. Separate accounting and other records must be maintained and a separate fund must be established to hold all receipts of long-term business.

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The extent to which long-term fund assets may be used for purposes other than long-term business is restricted by the rules in INSPRU. Only the 'established surplus' the excess of assets over liabilities in the long-term fund, as determined by an actuarial investigation may be transferred so as to be available for other purposes. Restrictions also apply to the payment of dividends by the insurance company, as described below. The rules in INSPRU require, in addition to the capital requirements referred to above, the maintenance of sufficient assets in the separate long-term insurance fund to cover the actuarially determined value of the insurance liabilities.

The rules also require banks, building societies, insurers and investment firms to undertake reverse stress testing. Reverse stress testing requires firms to work backwards from an assumed point of business model failure, to identify the stress scenarios that could result in such adverse outcomes. Each firm must then consider whether the likelihood of these scenarios, taking into account likely management actions, is consistent with its risk appetite and, if not, must initiate actions to address any inconsistencies.

Actuarial functions

The PRA's rules require every insurance company that carries on long-term business to appoint one or more actuaries to perform the 'actuarial function' in respect of all classes of its long-term insurance business and, the 'with-profits actuary function' in respect of all classes of that with-profits business (if any).

The actuary performing the 'actuarial function' must prepare at least annually, a report for the company's directors quantifying the company's long-term liabilities attributable to the insurance company's long-term insurance business, determining the value of any excess over those liabilities of the assets representing the long-term insurance fund and, where any rights of long-term policyholders to participate in profits relate to particular parts of such a fund, a valuation of any excess of assets over liabilities in respect of each of those parts.

The actuary performing the 'with-profits actuary function' must, amongst other responsibilities, advise the firm's management on key aspects of the discretion to be exercised affecting these classes of the with-profits business of the firm, and, at least once a year report to the firm's governing body on key aspects (including those aspects of the firm's application of its Principles and Practices of Financial Management ('PPFM') on which the advice described above has been given) of the discretion exercised in respect of the period covered by his report. All firms that carry on with-profits business are required to publish the PPFM that are applied in the management of their with-profits funds.

Distribution of profits and with-profits business

Under IPRU (INS), once an allocation of surplus in a with-profits fund has been made to policyholders, no transfer of assets representing any part of a subsequent surplus can be made, to shareholders or otherwise, unless either a defined 'relevant minimum' of the surplus has been allocated to policyholders or a statutory notification procedure has been followed.

There has been considerable public debate about the rights and legitimate expectations of with-profits policyholders to assets forming part of an insurance company's surplus. The FSA confirmed in July 2009 that proprietary life insurance companies will not be able to meet future compensation and redress payments from their with-profits funds, and the FSA confirmed a rule change, meaning that liabilities arising from operational failures (including mis-selling) after the rule came into effect from 31 July 2009 should be met by shareholder funds rather than policyholder funds.

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With-profits business

The with-profits business was an area of focus for the FSA, including specifically: the costs charged to a with-profits fund by the firm managing the fund; penalties and charges levied on policyholders who surrender their policies early; the need for funds to be managed with the objective of ensuring that maturity payouts fall within a target range set for the fund; and the provision of information to with-profits policyholders or potential policyholders in a format that they can more readily understand.

On 1 April 2012, the FSA introduced further changes to its rules and guidance in a number of areas relevant to the operation of with-profits funds, including in relation to: conflicts of interest with the potential to prejudice with-profits policyholders; the fair treatment of with-profits policyholders in mutually-owned funds; the terms on which new business may be written by with-profits insurers; communications and planning surrounding material reductions in new business; the application of market value reductions; the use of with-profits funds to make strategic investments; the removal of the ability of firms to reattribute excess surplus; rules surrounding reattribution of inherited estates; and changes to the rules surrounding corporate governance.

The PRA and FCA now share responsibility for protecting policyholders' reasonable expectations in relation to with-profits business. The PRA seeks to ensure that any discretionary benefit allocations or other changes with financial implications that the insurer has proposed are compatible with its continued safety and soundness, whereas the FCA has responsibility for monitoring whether the proposed changes are consistent with the insurer's previous communications, the FCA's conduct rules and the overriding obligation to treat customers fairly. The PRA has the power to prevent allocations being made if they would materially impair the firm's safety and soundness.

Gender discrimination in contracts of insurance

In a 2011 decision, the European Court of Justice ('the ECJ') ruled that gender-related factors could not be used in determining premiums and benefits under insurance policies. The ECJ granted a transitional period of relief for implementation until 21 December 2012 and the UK Government amended the Equality Act 2010 during 2012 to give effect to the judgment. Although the full effect of the ruling in the UK and other EU member states remains uncertain to date, the scale of the judgment is contributing to a period of uncertainty. In particular, it is unclear how insurance contracts that were entered into prior to the ruling but which have continued in force after 21 December 2012, will be treated. In practice, the requirement for unisex premiums has been seen to affect the cost of some types of insurance for both men and women, notably car insurance, life insurance, health insurance, and the cost of an annuity a financial product that provides a regular pension income.

Auto enrolment

From October 2012, auto enrolment into a workplace pension was introduced, opting in millions of workers to a workplace pension, with contributions from the employers and the government in most cases, as well as a percentage of pay automatically being taken. Individuals can choose to opt out, but the aim is to tackle reliance on the state pension in retirement.

EU Directives on groups

Prudential is subject to the capital adequacy requirements of the IGD, as implemented in the PRA rules. The IGD pertains to groups whose activities are primarily concentrated in the insurance sector.

Historically, the FSA, as lead supervisor of Prudential under the IGD, supervised Prudential on a group basis in addition to supervising the UK insurance companies within Prudential individually. This is referred to in the IGD as supplementary supervision and encompasses such matters as general supervision over intra-group transactions (including, *inter alia*, loans, guarantees and off-balance sheet

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transactions, investments, reinsurance, retrocession and cost sharing agreements), group risk management processes and internal control mechanisms, and reporting and accounting procedures. In accordance with the IGD, the FSA required the calculation of group capital resources on a consolidated basis and required that such group capital resources are equal to or in excess of Prudential's group capital resources requirement (each as calculated in accordance with INSPRU).

The FSA also played a coordinating role amongst EU regulators under the IGD. Due to the geographically diverse nature of Prudential's operations, the application of these requirements to Prudential is complex. In particular, for the purposes of calculating the group capital requirement and actual group capital resources under INSPRU, for many of the Asian operations, the assets, liabilities and capital requirements have to be recalculated based on UK regulations as if the companies were directly subject to such regulation.

As noted above, the FSA has been replaced in its lead supervisory role by the PRA following the legal cutover on 1 April 2013.

New EU solvency framework

The European Commission is continuing to develop a new prudential framework for insurance companies, 'Solvency II', which will repeal and replace the existing Life, Non-life, Re-insurance and IGD directives. The main aim of this framework is to ensure the financial stability of the insurance industry and protect policyholders through solvency requirements better matched to the true risks of the business.

Solvency II adopts a three-pillar approach to prudential regulation, which is similar to the 'Basel II' approach that has already been adopted in the banking sector in Europe.

Although the Solvency II Directive has similarities to the current UK regime set out in GENPRU and INSPRU in terms of its risk-based approach to the calculation of capital requirements and use of capital tiering, there are also many differences both in terms of substance and terminology. For example, while both regimes share the principle of a market consistent valuation of assets and liabilities, there are differences in the detailed valuation methodologies.

A key aspect of Solvency II is the focus on a supervisory review at the level of the individual legal entity. Insurers will be encouraged to improve their risk management processes and will be allowed to make use of internal economic capital models to calculate capital requirements, subject to approval by the PRA. In addition, Solvency II requires firms to develop and embed an effective risk management system as a fundamental part of running the firm.

The new regime will require firms to disclose a considerably greater level of qualitative and quantitative information than under current rules, both to their own supervisor through Regular Supervisory Reporting ('RSR') and to the market through the publication of a Solvency and Financial Condition Report ('SFCR'). This is intended to increase transparency, allowing easier comparison across the industry and enabling supervisors to identify sooner if firms are heading for financial difficulty. In turn, increased transparency is intended to drive market discipline, arising from the reaction of ratings agencies and the capital markets to firms' performance.

Further details on Solvency II and its implication for the Group are set out in Item 4 Group Risk Framework. As described in that section, the previously anticipated implementation date for Solvency II of 1 January 2014 is now expected to be delayed. At this stage, it remains unclear exactly when Solvency II will come into force, although a deferral until 1 January 2016 or beyond appears likely.

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ICAS+

It is now widely acknowledged that full implementation of Solvency II by 1 January 2014 is unrealistic. Regulators across Europe are now considering how they can ensure that the momentum built towards better risk management gained over the last few years is not lost. Insurers are also keen to leverage improved governance, risk management, and capital models developed as part of Solvency II implementation rather than see this effort being wasted or sidelined.

The FSA has already confirmed that within the UK the existing ICAS regime will continue to operate and it is anticipated this will have a renewed focus from the PRA. Many companies (in particular those in the Internal Model approval process) are planning to review their ICA in 2013 both to ensure it remains fit for purpose and to investigate areas where they can incorporate elements of their Solvency II developments.

In October 2012, the FSA announced its initial thoughts on how Internal Model companies could transition from the ICAS regime to Solvency II. It confirmed its thinking in a letter to companies on 29 January 2013. The FSA proposed to allow companies to use the Solvency II Internal Model (or elements of it), subject to it being of an appropriate standard, to calculate their ICAS under what is being called 'ICAS+'. In addition, it is likely that companies will need to submit an in-development ORSA as part of their ICAS+ submission. More detail is expected in the second quarter of this year.

Regulation of investment business

Certain of Prudential's subsidiaries were authorised by the FSA to carry on investment business. These entities were subject to regulation and supervision by the FSA and had to comply with the FSA Conduct of Business and Prudential Rules made under the FSMA 2000. After 1 April 2013, these subsidiaries have been regulated by the PRA and FCA. Not all subsidiaries are dual regulated, some are regulated by the FCA only for both conduct and prudential matters, such as the M&G subsidiaries.

One of the Prudential's UK subsidiaries, M&G Investment Management Limited, is also regulated by the United States' Securities and Exchange Commission (the "SEC") so that it can act as investment adviser to a number of US mutual funds.

Conduct of business requirements for investment businesses and the Markets in Financial Instruments Directive ('MiFID')

MiFID sets out detailed and specific organisational and conduct of business requirements for investment firms and regulated markets. In October 2011, the European Commission published proposals to amend MiFID and introduce a new Markets in Financial Instruments Regulation ('MiFID 2'). Among other things, the proposals were designed to expand the scope of MiFID, both in terms of the types of firms and instruments (e.g. structured deposits and emissions allowances) its requirements encompass. The impact on our M&G investment management business will be mainly around fixed income and derivatives.

MiFID 2 is still being negotiated through the European legislative process and areas of uncertainty remain. The pre-trade transparency would also apply to a wider range of instruments: bonds and derivatives in addition to shares. If the threshold is set at too low a level, asset managers like M&G could potentially have to publish quotes received within three minutes. It is also possible that MiFID 2 could impose a partial or full ban on inducements to advisers, similar to that introduced by the RDR in the UK (as described above). This could require M&G to modify its European adviser charging model. MiFID 2 is expected to be agreed during 2013 at the earliest, with its changes taking effect in 2014 or 2015.

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Capital requirements for investment businesses

The capital requirements for investment businesses are contained in the Prudential Standards section of the PRA Handbook. These rules implement the requirements of the EU's Recast Capital Adequacy Directive (Directive 2006/49/EC), which together with the EU's Banking Consolidation Directive (Directive 2006/49/EC) constitute the Capital Requirements Directive ('CRD'). CRD has been amended a number of times and the European Commission has proposed a legislative package known as 'CRD IV' which will replace CRD in order, amongst other ends, to implement the rules proposed by the Basel Committee on Banking Supervision, known as 'Basel III'. This is likely to slightly increase the capital requirements for M&G. CRD IV is currently expected to be finalised in 2013, although this may be delayed.

Alternative Investment Fund Managers Directive (AIFMD)

The AIFMD, a Directive designed to regulate the managers, management and marketing of alternative investment funds including private equity and hedge funds entered into force on 21 July 2011. EU Member States must implement it by 22 July 2013, and a key element in implementing the Directive will be the adoption of a European Commission regulation ('the Level 2 Regulation') specifying much of the detail with which affected firms will have to comply. The FSA published the first part of its consultation on the implementation of the AIFMD in November 2012 and the second consultation in the first quarter of 2013. HM Treasury also published a consultation paper in January 2013 covering the Government's proposed approach to a number of key policy decisions in relation to the transposition of the Directive into UK law and is to issue a second paper in due course. M&G is running a comprehensive project to ensure that all of its alternative investment fund managers meet the requirements of the AIFMD, which are similar to the existing requirements for retail mutual fund managers.

European Market Infrastructure Regulation ('EMIR')

The Regulation of the European Parliament and of the Council on OTC derivative transactions, central counterparties (CCPs) and trade repositories, widely known as European Market Infrastructure Regulation, or 'EMIR', came into force on 16 August 2012. Its key provisions, however, are taking effect on a phased basis from the beginning of 2013 following the provision of guidance and standards on the implementation of EMIR by European Securities and Markets Authority ('ESMA') and the European Commission. EMIR's rules are intended to lessen risk and increase transparency within the OTC derivative markets by introducing for most counterparties: (i) a reporting obligation for OTC derivatives; (ii) a clearing obligation for eligible OTC derivatives; (iii) measures to reduce counterparty credit risk and operational risk for bilaterally cleared OTC derivatives, including through collateral requirements; (iv) common rules for CCPs and for trade repositories; and (v) rules on the establishment of interoperability between CCPs. M&G is running a comprehensive project to implement necessary changes, by the relevant deadlines.

Asian Supervision and Regulation

1. Regulation of insurance business

Prudential's businesses in Asia are subject to all relevant local regulatory and supervisory schemes. These laws and regulations vary from country to country, but the regulators typically grant (or revoke) licenses and therefore control the ability to operate a business.

Industry regulations are usually widely drawn and include provisions governing both financial matters and the way business is conducted in general. In general, regulatory regimes will include features governing the registration of agents, the approval of products, asset allocation, minimum capital and the basis for calculating the company's solvency and reserves and the valuation of policyholder

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liabilities, conditions for outsourcing non-core functions, policyholder and investor protection and regulation of product features, as well as anti-money laundering and 'know your client' requirements and data protection requirements. Regulatory authorities may also regulate affiliations with other financial institutions, shareholder structures and the injection of capital and payment of dividends. Financial statements and other returns are filed with the regulators. The regulators may also conduct physical inspections of the operations from time to time. A number of jurisdictions across Asia require insurance companies to participate in policyholder protection schemes (ie contribute to a fund to support policyholders in the event of an insurance company failing).

Regulatory standards are generally being raised, and insurance companies operating in Asia are finding themselves subject to increasing regulatory supervision and scrutiny. In general, the pace of regulatory developments has increased since 2008 in most markets, particularly in relation to risk capital, consumer protection and governance requirements. For example, greater regulatory emphasis is being placed on ensuring that products are fit for purpose and that customers fully appreciate the features of their policies, as well as on data privacy. Also whereas the need for compliance with relevant regulations was always implicit in the way insurers ran their businesses, there is a trend towards a more explicit demonstration of this through documentation, audits and more formal management structures. This increased regulatory pressure will continue as Asian regulators begin to take on board the new International Association of Insurance Supervisors (IAIS) standards, which is expected to translate into an accelerating trend around a sharper focus on risk management systems and a requirement to hold more capital to manage asset and liability positions.

The increasingly extraterritorial approach of certain regulators outside Asia, aimed among other things at protecting financial systems from systemic risks and curbing tax avoidance, could have wider consquences on financial groups in the Asia-Pacific region. For example, firms based outside the US are increasingly being required to comply with certain US originated rules like FATCA (see 'US Supervision and Regulation Implementation of US Foreign Account Tax Compliance Act ('FATCA') provisions' below), which will impact on the bancassurance business channel as banks will have to set up separate systems to deal with US customers. The effects of UK anti-bribery legislation have become increasingly significant outside the UK, and Prudential Corporation Asia's ('PCA's') business units will be required to adhere to Prudential's group-wide policy designed to comply with the EU Solvency II requirements (although they will not each be required to be compliant on a solo entity basis). Asian regulators are monitoring closely how Solvency II is developed and implemented but are not currently requiring regulated insurance entities to comply.

Certain additional details of the regulatory regimes to which PCA's insurance operations are subject are discussed below:

Hong Kong The Prudential Assurance Company Limited

Overview

The Hong Kong branch of The Prudential Assurance Company Limited is authorised to carry on both long-term business and general business in Hong Kong under a composite license. By virtue of its branch status, the lead regulator on capital requirements of the Hong Kong business is the UK PRA. Further details on the PRA approach to capital requirements are explained in the UK Supervision and Regulation section above.

The Office of the Commissioner of Insurance (the 'OCI') is currently the regulatory body that administers the Insurance Companies Ordinance (the 'ICO'). The Office is headed by the Commissioner of Insurance who has been appointed as the Insurance Authority (the 'IA') for administering the ICO. The principal functions of the IA are to ensure that the interests of policyholders or potential policyholders are protected and to promote the general stability of the insurance industry, including by authorising insurers to carry on insurance business in Hong Kong, regulating insurers' conduct primarily

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through the examination of the annual audited financial statements and business returns insurers submit, and development of legislation and guidelines on insurance supervision. A key supervisory responsibility relates to solvency margin requirements contemplated by the ICO, as further discussed below.

The Financial Services and Treasury Bureau has issued a public consultation on its proposed plans for an Independent Insurance Regulator (IIR) in Hong Kong. Legislation is expected in 2013, with the IIR on track to be established in 2015.

The branch is also subject to the codes and guidance developed by a self-regulatory body the Hong Kong Federation of Insurers (the 'HKFI'). HKFI actively promotes its self-regulatory regime with respect to areas like conduct of insurers and insurance intermediaries, cooling off initiatives, policy replacement and initiative on needs analysis, etc. The Insurance Agents Registration Board of the HKFI is responsible for administering the registration and approval of insurance intermediaries of insurance agents, their responsible officers and technical representatives; and handling complaints against them and providing enquiry services to and handling complaints from the public relating to insurance agents.

In addition, the sale of mandatory pension products by agents is regulated by the Mandatory Provident Fund Authority (the 'MPFA'), which licenses and supervises the conduct of MPF intermediaries and the supervision of the conduct of MPF intermediaries.

The branch is also regulated by the Hong Kong Securities and Futures Commission (the 'SFC') for its offering of Investment Linked products.

Capital requirements

Under the ICO, an insurer is required to maintain at all times an excess of assets over liabilities of not less than a required solvency margin. The objective is to provide a reasonable safeguard against the risk that the insurer's assets may be inadequate to meet its liabilities arising from unpredictable events, such as adverse fluctuations in its operating results or the value of its assets and liabilities.

For general business insurers, the ICO stipulates an absolute minimum solvency margin of HK$10 million, or HK$20 million in the case of a composite insurer (i.e. carrying on both general and long term business) or for an insurer wishing to carry on statutory classes of insurance business. Above these minimum levels, solvency margins are calculated on the basis of the greater of an insurer's relevant premium income (defined as the greater of gross premium income after deduction of reinsurance premium payments or 50 per cent of gross premium income) or relevant outstanding claims (defined as the sum of unexpired risks plus the greater of 50 per cent of claims outstanding before deduction of sums recoverable from reinsurers or the amount of claims outstanding after deduction of sums recoverable from reinsurers).

For long-term business insurers, the ICO stipulates an absolute minimum solvency margin of HK$2 million. Above this minimum level, solvency margins are determined in accordance with the Insurance Companies (Margin of Solvency) Regulation (Chapter 41 F of the Laws of Hong Kong), which sets out a series of calculations to be used depending on the particular class of long-term business involved.

For composite insurers, the ICO stipulates a minimum solvency margin based on the aggregate of the solvency margin required in respect of an insurer's general business and its long-term business, both calculated as described above.

Taiwan PCA Life Assurance Company Limited

Overview

PCA Life Assurance Company Limited is licensed to conduct life insurance business in Taiwan.

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The Financial Supervisory Commission ('FSC') is responsible for regulating the entire financial services industry, including the banking, securities and insurance sectors. The FSC's responsibilities include supervision, examination and investigation. The Insurance Bureau ('IB') under the FSC is responsible for the insurance sector. The Financial Examination Bureau (the 'FEB') under the FSC acts as the executive supervisory authority for the FSC and principally carries out examinations and on-site visits of insurance companies, generally every two years. The Investigation Bureau under the Ministry of Justice is responsible for supervision of anti-money laundering and counter-terrorism financing efforts.

Capital Requirements

The Insurance Act requires all insurance companies to maintain a risk-based capital (RBC) ratio of not less than 200 per cent. The ratio is determined as the adjusted net capital compared against the risk-based capital. This measurement takes into consideration asset, insurance, interest and other relevant risks as requires in calculating the capital on a risk adjusted basis. Any company failing the threshold may be subjected to measures ranging from restrictions in business operations to the withdrawal of business license.

Korea PCA Life Insurance Company Limited

Overview

PCA Life Insurance Company Limited is authorised to carry on life insurance business in Korea including but not limited to casualty insurance, illness insurance, nursing insurance and incidental business and services related thereto.

Korea's financial supervision structure is composed of the Financial Services Commission (the 'FSC') and the Financial Supervisory Service (the 'FSS'). As Korea's principal supervisory authority, the FSC is given a broad statutory mandate to carry out three key functions: financial policy formulation, financial institution and market oversight, and anti-money laundering. It also issues regulatory licenses to financial institutions. The Financial Supervisory Service (the 'FSS') acts as the executive supervisory authority for the FSC and principally carries out examination of financial institutions along with enforcement and other oversight activities as directed or charged by the FSC.

In respect of anti-money laundering, the Korea Financial Intelligence Unit ('KoFIU'), a part of the FSC leads the government's anti-money laundering and counter terrorism financing efforts.

Korean laws permit an insurer to operate only one license (life or non-life) at any one time. In the past, the FSC has been highly interventionist in setting and enforcing rules on the insurance industry. In recent years the FSC has moved away from its interventionist approach, in response to the evolving and liberalised landscape. The most prominent change has been a deregulation in asset management and product design activities. However, in connection with deregulation, the FSC has also sought to strengthen supervision. Additions and amendments to Korean law and regulation aimed at protecting consumers have, amongst other things, resulted in expansion of the scope of concurrent/ancillary businesses which can be conducted by insurance companies, new reporting requirements for foreign insurers' Korean offices, new regulations governing asset management by insurance companies, and updated processes for development of insurance products, prohibitions on corporate insurance agents and corporate insurance brokers from engaging in other business, new additions to the list of acts prohibited when entering into insurance contracts or soliciting consumers and additional and more specific requirements in respect of data protection.

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Capital requirements

A risk-based supervision framework applies to insurers, encompassing the risk-based capital solvency requirement, the risk assessment and application system (RAAS), which assesses insurers' various risks and relevant internal controls, and risk disclosure.

Under RBC solvency, the ratio of an insurer's available capital to required capital is calculated, and the analysis of equity capital used to determine capital adequacy must take into account market, credit, operational, insurance and interest rate risks, which are not taken into consideration under the solvency margin requirement.

In the event an insurer fails to satisfy the applicable capital adequacy requirement and this poses a threat to the financial soundness of that insurer in Korea, the FSC may take corrective action, ranging from issuing a recommendation to an insurer to increase its capital reserves or to restrict its investments in high-risk securities and other assets to issuing an order to an insurer to suspend its business or transfer it to a third party.

Singapore Prudential Assurance Company Singapore (Pte.) Limited

Overview

Prudential Assurance Company Singapore (Pte.) Limited is registered by the Monetary Authority of Singapore (the 'MAS') to design and sell both life and general insurance business pursuant to the Singapore Insurance Act.

Under the Singapore Insurance Act, the MAS is responsible for insurance regulation and supervision of insurance companies. MAS regulation covers, among other things, the appointment and training of representatives, maximum tier structure, loans and advances, disciplinary action, product disclosure, sales processes and replacement (switching) of life policies. The MAS also has responsibility for supervising compliance with anti-money laundering ('AML') provisions, though suspicious transactions must be notified to the Commercial Affairs Department, an enforcement agency of the Singapore Police Force.

Another relevant regulatory authority for the business is the Central Provident Fund (the 'CPF') Board, which acts as a trustee of social security savings schemes jointly supported by employees, employers and the government. The CPF Board regulates insurers in the operation of various CPF schemes including the CPF Investment Scheme where CPF monies are used by policyholders to purchase insurance policies such as annuities and investment linked policies.

The MAS and CPF Board have very detailed regulatory frameworks to govern insurance companies and the distribution of insurance products in Singapore.

Capital requirements

Registered insurers in Singapore are subject to a risk based capital ('RBC') framework. The framework sets out the valuation methodology for assets and liabilities, rules relating to the operations of life insurance funds, capital requirement rules, the role of actuaries, and a set of statutory reporting standards. An insurer has to notify the MAS when it has failed or is likely to fail to comply with the mandated RBC indicators or when a financial resources warning event has occurred or is likely to occur.

A registered insurer is required at all times to maintain a minimum level of paid-up ordinary share capital and to ensure that its financial resources are not less than the greater of the sum of the aggregate of the total risk requirement of all insurance funds established and maintained by the insurer under the Singapore Insurance Act; and where the insurer is incorporated in Singapore, the total risk requirement arising from the assets and liabilities of the insurer that do not belong to any insurance fund established and maintained under the Singapore Insurance Act (including assets and liabilities of

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any of the insurer's branches located outside Singapore); or a minimum amount of 5 million Singapore Dollars.

The MAS also has the authority to direct that the insurer satisfy capital adequacy requirements other than those that the insurer is required to maintain under the Singapore Insurance Act if the MAS considers it appropriate.

Malaysia Prudential Assurance Malaysia Berhad

Overview

Prudential Assurance Malaysia Berhad has composite licenses to carry on both life and general insurance business in Malaysia pursuant to the Insurance Act 1996.

In Malaysia, Bank Negara Malaysia ('BNM') is the regulatory body responsible for supervising and regulating the conduct of insurance business. BNM places considerable emphasis on fair market conduct by the insurance industry and protection of consumers' interests.

In addition, the company is a member of the Life Insurance Association of Malaysia and the General Insurance Association of Malaysia, which are both self-regulated bodies. Resolutions and circulars issued by these associations are binding on the member insurance companies.

Capital requirements

BNM has introduced an RBC framework aimed at improving the risk management practices of insurers. Under the RBC framework, insurers are required to maintain a capital adequacy level that is commensurate with their risk profiles. Each insurer is required to determine the adequacy of the capital available in its insurance and shareholders' fund to support the total capital it requires. This serves as a key indicator of the insurer's financial resilience and is used by BNM to determine the need for supervisory interventions.

Under the RBC framework guidelines, the Board of Directors and senior management of an insurer are also expected to identify, monitor and control risks which are not adequately addressed under the framework. An insurer is also expected to manage actively its capital adequacy by taking into account the potential impact of its business strategies on its risk profile and overall financial resilience.

BNM implemented the internal capital adequacy assessment process (ICAAP) regime for the insurance sector in September 2012. This set out the framework for meeting risk-based capital requirements. The ICAAP is a comprehensive and forward looking assessment which requires insurance companies to consider material risks to demonstrate how they will be linked to their capital management program.

Malaysia (Takaful business) Prudential BSN Takaful Berhad

Overview

Prudential BSN Takaful Berhad ('Prudential Takaful') (a Prudential joint venture with Bank Simpanan Nasional) was the first overseas insurer to be granted a domestic Takaful License in Malaysia.

The Takaful business in Malaysia, like the insurance business discussed above, is also regulated by BNM. In addition, Prudential Takaful is required to be a member of the Malaysian Takaful Association ('MTA'), an association for Takaful operators that seeks to improve industry self-regulation through uniformity in market practice and to promote a higher level of co-operation.

Takaful in Malaysia is considered to be part of mainstream mercantile law, and is subject to the civil court structure. It is not regulated by Shariah law in Shariah courts. However, the operations of a Takaful operator must conform to the rules and requirements of Shariah as regulated in the Takaful Act

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1984, which elevates the BNM's Shariah Advisory Council to the position of sole authority on Shariah matters. A Takaful operator is required to establish a Shariah advisory body approved by BNM to which BNM's Shariah Advisory Council will give guidance and advice on operations and business activities. Since 2004, BNM has issued a series of guidelines aimed at fostering the Takaful industry and promoting its orderly growth, including capital adequacy, financial reporting, stress testing and conduct of business rules around product disclosure, suitability and anti-money laundering.

Capital requirements

BNM issued the Takaful Operational Framework which came into force on 2 January 2012. The regulations further strengthen the operational and valuation requirements of Shariah law, such that the paid-up capital requirement is RM100 million. The regulator also published a new Risk Based Capital framework for Takaful on 30 October 2012. The framework aims to facilitate sound management of capital, aligned to the Takaful operator's risk profile. Full implementation is scheduled for January 2014 but Takaful operators have been required to submit quarterly and annual reports on a parallel basis from March 2013.

China CITIC-Prudential Life Insurance Company Limited

Overview

CITIC-Prudential Life Insurance Company Limited (Prudential's joint venture with CITIC) is authorised to conduct life insurance business in China. To date, CITIC-Prudential Life had business across China including the key markets of Guangdong, Beijing, Shanghai, Hubei, Shandong, Shejiang, Jiangsu, Tianjin, Guangxi, Fujian and Hebei.

The body responsible for regulation of the insurance sector is the Chinese Insurance Regulatory Commission ('CIRC'). CIRC reports directly to the State Council.

CIRC is authorised to conduct the administration, supervision and regulation of the Chinese insurance market, and to ensure that the insurance industry operates in a stable manner in compliance with the law. CIRC also has local offices in all 31 of the provinces and selected direct administrative cities and regions across the country which set and administer implementation rules and guidelines in the application of the regulations introduced by CIRC, and which regulate many aspects of the insurance companies' activities within the locations for which they are responsible, including conduct and licensing matters.

CIRC has focused specific attention on the area of risk prevention, with five identified lines of defense against risks, namely internal management and control systems, supervision of solvency adequacy, on-site inspection, fund management regulation and insurance security fund. In response to the global financial crisis, more importance has been attached to the supervision of internal control systems, corporate governance, and market conduct and information disclosure by insurance companies. A classification system has also been developed by the regulator to monitor risks in the industry. Under the system, insurance companies are classified into four groups based on the risk indicators relating to solvency margins, corporate governance, capital management, financial status and market conduct. Different administrative measures may be imposed on different groups.

The new Chairman of the CIRC has re-emphasised the importance of preventing sales malpractices and embarked on a major exercise of industry self-assessment and regulatory inspection aimed at evaluating and improving the effectiveness of controls over such activities. Further action is expected in this area both in the near future and over the coming years.

The People's Bank of China ('PBOC') is entrusted with responsibility and authority to regulate all anti-money laundering activities in China and has actively been developing rules and guidance, requiring insurance companies to abide by the PRC's main AML law and regulations in connection with capital

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investment, transfers and set-up of new branches, and specify senior management's responsibilities on AML.

Capital requirements

The minimum registered paid-up capital of a foreign invested insurance company is RMB200 million. A similar requirement is imposed on a Chinese branch of a foreign insurance company. Both foreign invested insurance companies and Chinese branches of foreign insurance companies are required to maintain a solvency ratio that is not lower than 100 per cent. Under relevant PRC regulations, the solvency ratio is the ratio of actual capital to the minimum capital requirement applicable to the insurer pursuant to relevant regulations. The actual capital is the difference between the admitted assets and admitted liabilities. The CIRC requires solvency reports to be submitted quarterly, annually or *ad hoc* as required by the CIRC. Where an insurer is not able to meet its solvency requirement, it is required to immediately report to the CIRC.

In March 2012, the CIRC released its plan for the second generation of its solvency framework, to bring it closer to international norms within the next three to five years. Solvency and risk management requirements are expected to be enhanced, but it is too early to assess the impact on insurance companies.

Thailand Prudential Life Assurance (Thailand) Public Company Limited

Overview

Prudential Life Assurance (Thailand) Public Company Limited (PLT) holds a life insurance license and is authorised to offer life and general insurance products. This also includes an authorisation to offer products with an investment linked feature.

PLT is regulated and supervised by the Office of Insurance Commission ('OIC'),the independent regulatory organisation handling day-to-day insurance business affairs and reporting to the Ministry of Finance. The OIC has the power to manage and supervise insurance companies, protect insured persons and the general public, implement policies with respect to insurance funds, and regulate the professional conduct, qualifications and licensing of insurance brokers, agents and actuaries.

In respect of AML, all life insurance businesses are also regulated by the Anti-Money Laundering Office 'AMLO.' All suspicious reporting is to be made to Thailand's Financial Intelligence Unit ('FIU').

In the private sector, the Thai Life Assurance Association and the General Insurance Association play an active development role for their membership and support the insurance business as its representative bodies.

The OIC has a five-year insurance development plan in place covering 2010-2014 that aims to strengthen the Thai insurance system by enhancing standards to meet international norms and to prepare for greater liberalisation in the future. Consultations on proposed regulation focused on how banks and insurance companies sell insurance and investment-related products to their customers occurred in 2012. When implemented, such regulations are expected to require insurance firms to enhance internal systems and controls in firms. The Bank of Thailand regulations on bancasssurance came into effect in January 2013. Under these regulations banks are required to ensure that staff distributing insurance products possess the relevant competence around product knowledge, enhanced disclosure of product yields and the prohibition of bundling insurance products with bank products. It is anticipated that similar regulation for insurance companies will be issued during 2013.

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Capital requirements

Life insurers are required by law to maintain capital funds at the greater of two per cent of their insurance reserve or 50 million Thai Baht, but the OIC requires insurers to maintain capital funds of at least 150 per cent of this amount. An insurer that fails to maintain capital funds in line with OIC guidelines and does not take corrective action to address the deficiency will be subject to sanctions through restrictions on its investment and other business activities.

The 2008 amendments to the Life Insurance Act required the implementation of risk-based capital adequacy tests by 2011. Relating to this the OIC issued guidelines in 2011 requiring audited quarterly RBC returns to be filed with them.

Philippines Pru Life Insurance Corporation of UK

Overview

Pru Life Insurance Corporation of UK is licensed in the Philippines as a life insurance company and also permitted to offer health, accident and disability insurance.

The Insurance Code of the Philippines, as amended, ('Insurance Code') gives the power to supervise and regulate the operations and business of insurance companies to the Insurance Commission ('IC'). The IC is a government agency under the Department of Finance, and is headed by the Insurance Commissioner. IC regulation and supervision seeks, amongst other things, to ensure that adequate insurance protection is available to the public at a fair and reasonable cost and to ensure the financial stability of the insurance industry so that all legitimate claims of the insured public are met promptly and equitably, and to safeguard the rights and interests of the insured.

Capital Requirements

Any life insurance company existing, operating, or otherwise doing business in the Philippines with at least sixty percent (60%) foreign equity must meet a minimum capital requirement and also adopt an RBC Framework.

To strengthen the RBC regulatory framework, a new directive was also issued in 2012 requiring increased capitalization for both life and non-life insurance providers, with a minimum paid-up capital of Php250m (increasing to Php1bn by the end of 2020).

India ICICI Prudential Life Insurance Company Limited

Overview

ICICI Prudential Life Insurance Company Limited (Prudential's joint venture with ICICI in which Prudential has a 26 per cent share) is authorised to carry on long-term insurance business in India.

Insurance is subject to federal regulation in India. The Insurance Regulatory & Development Authority (the 'IRDA') is the key regulator for ICICI Prudential Life Insurance operations. The IRDA's duties include issuing certificates of registration to insurance companies, protecting the interests of policyholders, and regulating, promoting and ensuring the orderly growth of the insurance industry. Regulatory direction is currently focused on corporate governance and disclosures to stakeholders. The IRDA's regulations also encourage the sale of insurance to customers in rural parts of India.

There has been a significant volume of regulatory developments in India since 2010 designed to shift the emphasis of the industry away from products which are mostly investment oriented and encourage more traditional savings and protection. The most significant changes relate to product regulation of investment-linked policies known as unit-linked insurance policies (ULIPS) with initiatives to rationalise ULIP product features, including through increased minimum lock-in periods and terms and

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requirements of minimum guaranteed rates of return and payouts. Regulatory initiatives or changes have also included streamlining of the product approval process and product rules for traditional products.

In late 2011, the Finance Ministry formed four committees to prepare a roadmap for the insurance industry, tasked to look into issues relating to insurance penetration, product development and the regulatory framework, these committees engage with industry bodies, ratings agencies and the Finance Ministry.

A number of developments aimed at fostering the growth of the insurance industry are underway. The IRDA is currently exploring tax incentives for life insurance and the Finance ministry is currently engaged in discussion with the industry. In October 2012, the cabinet approved an amendment to the Insurance Bill 2008 to raise the FDI from 26 per cent to 49 per cent, with the increase now pending approval by the Indian Parliament. In the same month, the IRDA also issued draft regulations on the Bancassurance business to help foster the growth of the insurance industry that would permit a bank to act as a corporate agent or a broker (the latter requiring the bank to terminate existing partnerships), and to also tie up with life, non-life and health insurers up to a maximum of 20 locations across India. This limits the outreach of ICICI Prudential Life's products and may hamper servicing of customers in provinces where the banks have no permissions to distribute these products.

The Reserve Bank of India and the IRDA recently initiated probes into allegations by an online Indian investigative media outlet that sales practices at certain Indian banks (including ICICI Bank) and insurance companies (including ICICI Prudential Life Insurance Company Limited) would have permitted or facilitated money-laundering transactions in violation of local law. It is too early to predict whether such allegations, some of which involve offers to sell insurance products (including those of ICICI Prudential Life Insurance Company Limited), might lead to additional regulatory actions against the implicated Indian insurance companies whose products were allegedly offered.

Capital Requirements

There are proposals to develop a risk based capital regime in India. Every insurer must maintain an excess of assets over liabilities and the Required Solvency Margin for an insurer is the higher of Rs.500 million or formulaic calculation of net premium or formulaic calculation of net claims.

Indonesia PT. Prudential Life Assurance

Overview

PT. Prudential Life Assurance is authorised to carry on long-term (for an indefinite period) insurance business in Indonesia. Prudential's operations in Indonesia are authorised to distribute life insurance products based on either conventional or Shariah principles, through agency and bancassurance (including direct marketing) channels. While the regulations for life products based on conventional principles are fully developed (in accordance with current market conditions), the government has promulgated new regulations in relation to life products with Shariah principles.

The insurance industry is regulated by the Insurance Bureau under the Capital Market and Financial Institution Supervisory Board ('Bapepam-LK') of the Ministry of Finance ('MoF'). Currently, Bapepam-LK is in the transitional period to becoming Otoritas Jasa Keuangan (OJK). OJK is the newly established financial sector regulator that is going to replace all Bapepam-LK functions, including Investment Management Bureau, insurance, pension funds, financing companies and banking industry supervision by Bank Indonesia (the Indonesian central bank). OJK became partially operational in January 2013, since taking over supervision of Non-Bank Financial Institutions (NBFIs). The transition of supervision of the banking sector is expected to be completed by end 2013.

The MoF issues decrees on, among other things, licensing of insurance companies, business conduct, auditing, solvency, fit and proper test for directors and commissioners of insurance companies,

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Shariah insurance and Know Your Customer (KYC) principles. These decrees are usually supplemented by implementing regulations issued by the Bapepam LK.

The local Life Insurance Association ('AAJI') continues to act as a conduit between insurers and the MoF and Bapepam LK in terms of the development of new regulations and guidelines. Insurance sales forces are licensed by the AAJI.

The implementation of anti-money laundering controls in the insurance industry is monitored by the Indonesian Financial Transaction Reports and Analysis Center (the 'PPATK').

In January 2012, the MoF issued draft regulations governing product development and distribution which were implemented in the first quarter of 2013. Insurers are now required to develop and implement strategic product plans, including relevant risks to be integrated in the organisational risk management framework and adhere to detailed disclosure requirements relating to product sales and marketing materials.

Capital Requirements

The minimum capital requirement for insurers who operate in Indonesia was Rp 40 billion, which was increased to Rp 70 billion at the end of 2012 and will increase again to Rp 100 billion by 2014 to 'encourage tighter market consolidation.'

Japan PCA Life Insurance Company Limited ('PCA Life Japan')

Overview

The Financial Services Agency of Japan (the 'JFSA') regulates insurance companies and other financial institutions. In particular, the Insurance Business Division of the JFSA specifically undertakes the supervision of insurance companies. PCA Life Japan is licensed by the Prime Minister of Japan (who delegates most of the supervisory functions to the JFSA) as a life insurance company. PCA Life Japan ceased underwriting new policyholder contracts from 15 February 2010.

Capital Requirements

The Insurance Business Law requires insurance companies to demonstrate financial soundness by maintaining a solvency margin ratio of greater than 200% and a positive adjusted net capital balance. Any insurance companies failing to comply will be subject to administrative actions including business suspension.

The JFSA has recently revised and enhanced its inspection criteria regarding reinsurers' financial strength and its integrated risk management schemes.

Vietnam Prudential Vietnam Assurance Private Limited

Overview

Prudential Vietnam Assurance Private Limited is licensed and regulated by the Ministry of Finance of Vietnam (the 'MoF') as a life insurance company. An insurance company is not permitted to operate both life and non-life insurance at the same time, except in the case of a life insurance company that offers personal health and protection care insurance as a supplement to life insurance.

The Insurance Division of the MoF specifically undertakes the supervision of insurance companies. The fundamental principles of the operation of insurance companies are set out in the Insurance Business Law.

Generally, the Insurance Business Law and its guiding regulations focus on administrative supervision of insurance operations. In practice, the Insurance Business Law reserves most of its items

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for insurance contracts (that is, for the terms and conditions of policies) in order to protect policyholders' interests. Furthermore, the MoF has issued the new regulation on bankruptcy procedures for insurers, securities and financial institutions in late 2008 to allow it to take timely intervention to control the solvency of insurance companies.

Anti-money laundering controls in the insurance industry are monitored by the Anti-Money Laundering Department under the Banking Inspection, State Bank of Vietnam.

Capital Requirements

10 out of the 11 Life insurance companies in Vietnam are foreign-owned, and influenced by the need to have funds of at least 600 billion dong (US $31 million) in capital a requirement beyond the reach of most Vietnamese owned companies.

Cambodia Prudential Cambodia

Prudential Cambodia was granted in-principle approval from Cambodia's Ministry of Economy and Finance in June 2012 to establish life insurance operations in that country. A representative office has been established in Phnom Penh and started selling life insurance policies in January 2013.

2. Regulation of investment and funds businesses and other regulated operations

Prudential conducts investment and fund businesses through subsidiaries or joint ventures in the following countries in Asia: Hong, Kong, Japan, Korea, Taiwan, The People's Republic of China, India, Singapore, Malaysia, Dubai, Vietnam and Indonesia. All operations are authorised and licensed by the relevant authorities, or exempted from licensing under the relevant regulations.

On 14 February 2012, the Asia Fund Management operations (except joint venture companies) was rebranded Eastspring Investments, and the new brand replaced a number of different business names that the asset management business had operated under across Asia.

All of the relevant authorities generally have broad supervisory and disciplinary powers, including, among others, the power to set minimum capital requirements, to temporarily or permanently revoke the authorization to carry on regulated business, to suspend registered employees/licensed representatives, and to invoke censures and fines for both the regulated business and its registered employees/licensed representatives. Although the detail of regulation varies, common features of the regulatory regimes in each jurisdiction tend to include investment restrictions, advertising codes, disclosure requirements in prospectuses and/or marketing materials, and requirements to seek unit holders' approvals in certain instances, provision of financial statements and other periodic disclosures to regulators, audits by regulators and so on.

Hong Kong

Products and services offered by Prudential in Hong Kong are regulated under separate statutory regimes by different regulatory bodies, including the Hong Kong Securities and Futures Commission ('HKSFC'), the Hong Kong Monetary Authority and the Mandatory Provident Fund Schemes Authority ('MPFA').

The MPFA regulates the compulsory Mandatory Provident Fund ('MPF'). In addition, the selling of MPF products by agents is regulated by the MPFA. The MPFA is responsible for the licensing and supervision of trustees who wish to administer MPF schemes and MPF intermediaries.

The Securities and Futures Ordinance ('SFO') and other subsidiary legislation govern the key regulatory requirements in Hong Kong relating to licensing requirements for persons carrying out regulated activities, including dealing in securities, advising on securities, fund management, market

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conduct, disclosure of interests, offering document requirements for securities and products including mutual funds and unit trusts, as well as investment-linked assurance products. The HKSFC is the statutory body responsible for the administration of the SFO and the related subsidiary legislations and rules.

The Hong Kong branch of PAC is regulated by the HKSFC for its operations relating to investment linked products. It is also registered with the MPFA as a MPF corporate intermediary.

Eastspring Investments (Hong Kong) Limited, incorporated in Hong Kong, is a wholly owned subsidiary of Prudential Plc. It is licensed with the HKSFC and authorised to deal in and advise on securities and undertake asset management activities in Hong Kong. It also holds a QFII (Qualified Foreign Institutional Investors) license issued by the China Securities Regulatory Commission ('CSRC'). The company is also registered with the Korea Financial Supervisory Service (KFFS) as an offshore investment advisor for investment advisory business and investment discretionary management business. The funds registered in Hong Kong by Eastspring Investments (Hong Kong) are also registered in Macau with the Monetary Authority of Macau.

BOCI-Prudential Asset Management Limited ('BOCIP'), incorporated in Hong Kong, is a joint venture between Prudential Corporation Holdings Limited (36 per cent) and BOCI Asset Management Limited (64 per cent). BOCIP is licensed by the HKSFC and is authorised to deal in and advise on securities, advise on corporate finance, advise on futures contracts and undertake asset management activities. It is also registered with the MPFA as an MPF corporate intermediary. It also holds a QFII license issued by the CSRC. The investment funds registered in Hong Kong by BOCIP are also registered in Macau with the Monetary Authority of Macau.

BOCI-Prudential Trustee Limited is a joint venture between Prudential Corporation Holdings Limited (36 per cent) and BOC Group Trustee Company Limited (64 per cent). The company is incorporated in Hong Kong and is an approved trustee under the Mandatory Provident Fund Schemes Ordinance and an associated entity to the BOCIP under the SFO.

Japan

Eastspring Investment Limited (known until February 2012 as PCA Asset Management Limited) is registered with the Kanto Local Finance Bureau under the Financial Services Agency ('JFSA') to engage in (a) second financial instruments business, (b) investment management business, (c) investment advisory & agency business and (d) ancillary business under the Financial Instruments and Exchange Act ('FIEA')

The company is also a member of the Investment Trusts Association, Japan and the Japan Investment Advisers Association. Both associations are self-regulatory bodies under FIEA. Eastspring Investment Limited is required to comply with the policies and regulations issued by these associations, which are authorised to conduct on and off-site inspection in addition to the inspection conducted by the Securities and Exchange Surveillance Commission which is part of FSA.

Under its registration in respect of the second financial instruments business, the company is permitted to explain products being sold but cannot effect actual sales of Eastspring Investments Limited's funds directly to investors. It does not therefore set up or maintain customer accounts for purposes of investment in Prudential's funds or their settlement, which may only be opened at relevant distributors such as registered financial institutions and type one financial instruments business operators like securities companies.

Korea

Prudential conducts a fund business in Korea through an indirect, wholly-owned subsidiary, Eastspring Asset Management Korea Co. Ltd. The bodies responsible for the regulation of asset

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management companies, investment advisers and discretionary management companies are the Financial Services Commission ('FSC') and its executive arm, the Financial Supervisory Service ('FSS').

Traditionally, the FSC in Korea has operated in a prescriptive manner with a significant amount of detailed regulation that asset management companies must comply with. In recent years, the style of regulation of the indirect investment industry has been changing in line with a more general trend towards liberalisation of financial services. In particular, the FSC has focused on deregulation in asset management and product design activities and shifted increasingly towards a principles-based regulatory regime.

Taiwan

The body responsible for regulation of securities investment trust enterprises ('SITE'), securities investment consulting enterprises ('SICE') and discretionary investment businesses is the Securities and Futures Bureau ('SFB') under the Financial Supervisory Commission ('FSC'). The SFB is responsible for promulgating laws, regulations and policies in relation to these business areas.

Eastspring Investment Trust Co. Ltd is registered as a SITE with the FSC. It is compulsory that all SITEs are members of the Securities Investment Trust and Consulting Association ('SITCA'), a self-regulatory organisation ('SRO'). SITCA supports the regulatory and administrative operations entrusted to the SFB by adopting self-regulatory rules and overseeing self-regulation by its members, establishing a membership disciplinary framework and carrying out matters that the SFB has authorised it to handle, such as previewing product filing documents before submission for the SFB's final review. SITCA also acts as liaison between the SFB and its members for matters of business development.

China

CITIC-Prudential Fund Management Company Limited, a joint venture between Prudential and CITIC Group (China International Trust and Investment Corporation), is regulated by the China Securities Regulatory Commission ('CSRC'). The CSRC supervises the establishment of fund management companies ('FMCs') and the launch of securities investment funds.

The legislative framework of China's fund industry comprises the China Securities Investment Funds Law (the 'Fund Law') and a set of ancillary regulations (the 'Fund Regulations'). While the Fund Law and Fund Regulations articulate the rules and requirements which must be adhered to by all FMCs, the supervisory approach of CSRC, to a certain extent, is also principles- based. The Chinese authorities aim to protect the legitimate rights and interests of investors and other relevant parties, and thereby to promote the healthy development of securities investment funds and securities markets. The CSRC has slowly started a process of deregulation. One major deregulation measure in 2010 was to lift the control over product approvals, which enables FMCs to launch more fund products.

The National People's Congress ('NPC'), China's top legislator, has approved the revised Fund Law to take effect in June 2013. The key proposed changes include registration of hedge funds, which will for the first time provide hedge funds opportunity to register with the regulator, as well as having a regulatory framework in place. The changes will also allow individual ownership of fund management companies, which will help to diversify the shareholding structure of EMCs and makes ESOP(s) possible as incentive schemes. Lastly, the changes will lift personal trading and investment restrictions. The changes to the investment restrictions will provide funds with more flexibility in investment activities and offer more opportunity for product innovation.

India

ICICI Prudential Asset Management Company Limited ('AMC'), a joint venture between Prudential and ICICI Bank Ltd., is approved by the Securities and Exchange Board of India ('SEBI') to act as

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Investment Manager of ICICI Prudential Mutual Fund (the 'Fund'). The Fund was set up as a Trust sponsored by Prudential (through its wholly owned subsidiary Prudential Corporation Holdings Ltd) and ICICI Bank Ltd. ICICI Prudential Trust Limited (the 'Trust Company'), is the Trustee to the Fund.

Mutual funds in India are comprehensively regulated by the guidelines and statutes promulgated under the SEBI (Mutual Funds) Regulations, 1996, the Indian Trusts Act, 1882, relevant provisions of the Companies Act 1956 and other applicable laws.

All mutual funds are required to be in the form of trusts. The trustee functions are carried out by separately established trust companies or boards of trustees. In all cases, the trust deed must be approved by the SEBI. AMC has obtained registration from the SEBI to act as a Portfolio Manager under SEBI (Portfolio Managers) Regulations 1993. AMC under its portfolio management license has also been appointed as the investment manager by the Trust for managing the scheme launched under the ICICI Prudential Venture Capital Fund.

In 2005, SEBI confirmed it had no objection to AMC undertaking Advisory Services to Offshore Funds. AMC has commenced the provision of Advisory Services and has also applied to set up a venture capital fund ('VCF') in India.

A key regulatory developments in 2012 was to permit mutual funds/asset management companies to charge service tax on investment and advisory fees to the scheme in addition to the maximum limit of TER, with service tax on other than investment and advisory fees, if any, borne by the scheme within the maximum limit of TER.

Singapore

Eastspring Investments (Singapore) Limited ('Eastspring Singapore'), an indirect wholly owned subsidiary of Prudential plc, has been issued a Capital Markets Services ('CMS') license, to conduct the regulated activities of fund management and dealing in securities by the MAS. In addition, Eastspring Singapore is admitted by the Central Provident Board ('CPF') as a Fund Management Company ('FMC') under the CPF Investment Scheme ('CPFIS') and may manage unit trusts included under the CPFIS. It is also registered with the U.S. Securities and Exchange Commission as a registered investment adviser under the Investment Advisers Act of 1940; the Financial Services Commission of South Korea, as a Cross border Investment Advisor under the Capital Market Consolidation Act and SEBI, under the SEBI (Foreign Institutional Investors) Regulations, 1995. Eastspring Singapore is also registered as a Qualified Institutional Investor with Japan's Financial Supervisory Authority, and is relying on the Class Order Exemption CO 03/1102 from the Australian Securities and Investments Commission for exemption from the need to hold an Australian financial services license for provision of services to wholesale clients in Australia.

Prudential Property Investment Management (Singapore) Pte. Ltd. ('Prupim SGP') is an indirect wholly-owned subsidiary of Prudential plc. It is a real estate fund management company, and operates in Singapore as an exempt fund manager and exempt financial adviser under the Securities and Futures Act and the Financial Advisers Act respectively. As an exempt fund manager and exempt financial adviser, Prupim SGP provides services to not more than 30 qualified investors (for fund management services) and accredited investors (for financial advisory services).

Key regulatory developments in 2012 included the following:

A new regime on disclosure of interests in entities listed on the Singapore Exchange Securities Trading Limited ('SGX') came into effect, streamlining and enhancing the disclosure of interests in SGX-listed entities;

An enhanced regulatory regime for FMCs took effect under which all FMCs have to meet enhanced business conduct and capital requirements; and

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MAS introduced a regulatory framework for credit rating agencies, under which they will be regulated under the Securities and Futures Act.

New requirements for mandatory reporting of certain OTC derivative transactions were also introduced. MAS has proposed requiring central clearing for two initial types of instruments, US dollar interest rate swaps ('IRS'), Singapore dollar IRS and non-deliverable forwards ('NDF') in selected Asian currencies (if one leg of the contract is booked in Singapore) with approved central clearing party and mandatory reporting of such transactions to trade repositories if it exceeds a certain clearing/reporting threshold.

Malaysia

Eastspring Investments Berhad (formerly known as Prudential Fund Management Berhad) was incorporated in November 2000 and is a wholly owned subsidiary of a Malaysian incorporated company, Nova Sepadu Sdn Bhd, which is in turn a subsidiary of Prudential.

Eastspring Al Wara' Investments Berhad (formerly known as Prudential Al-Wara' Asset Management Berhad)was incorporated in June 2009 and is a wholly owned subsidiary of Prudential Corporation Holdings Ltd. Eastspring Al Wara' Investments Berhad is an Islamic Shariah compliance asset management company.

Eastspring Investments Berhad and Eastspring Al Wara' Investments Berhad are both regulated by the Securities Commission (the 'SC'), a statutory body formed under the Securities Commission Act 1993 (SCA) and Capital Markets Services Act 2007 (CMSA), which reports to the Minister of Finance. The SC pursues an intensive and comprehensive approach to the oversight of firms and markets.

The SC has recognised the Federation of Investment Managers Malaysia (FIMM) as a self-regulatory organisation (SRO) for the unit trust industry. As an SRO, FIMM will regulate its own members while also ensuring that investors are protected and public interests are upheld. This complements the SC's efforts to ensure a more efficient and effective regulatory regime without compromising investor protection.

In addition, under a notable 2011 reform, the key Guidelines on Compliance Function for Fund Managers were revised to enhance client asset protection and raise compliance standards to safeguard the interests of investors. This included obligations on fund management companies to make adequate arrangements to safeguard clients' ownership rights on all clients' assets, ensure that the client assets are properly accounted for at all times and perform an annual evaluation of custodians.

Dubai

Eastspring Investments Limited ('Eastspring Investments Dubai') was incorporated in the Dubai International Financial Centre ('DIFC') in September 2006. Eastspring Investments Dubai is an ultimately wholly-owned subsidiary of Prudential Plc. Eastspring Investments Dubai is regulated by the Dubai Financial Services Authority ('DFSA'), which is the independent regulator for DIFC. Eastspring Investments Dubai holds a license for arranging credit or deals in investments, advising on financial products or credit and has a retail endorsement on its license. The supervisory approach of DFSA, to a large extent, is risk-based.

In June 2012, DFSA announced the enactment of two new laws which, among other things, brought about a number of significant changes to prospectus disclosure, what activities constitute an offer, market misconduct provisions and corporate governance. The new laws are designed to promote investor protection in a manner that better aligns the DIFC to international standards.

New regulations for mutual funds came into effect on 26 August 2012. All marketing of foreign funds will need to occur through a local promoter and all such funds will need to be approved by the

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Emirates Securities and Commodities Authority ('ESCA'). There is a grace period of one year for firms currently servicing the market. Eastspring Investments Dubai markets funds through platforms operated by local distributors. These distributors are in the process of having all funds on their platforms approved. We will need to monitor this process and maintain contact with trade bodies to ensure we fully understand how this regulation is being implemented in practice.

Vietnam

Eastspring Investments Fund Management Limited Liability Company ('Eastspring Investments Vietnam') was established and operates under a business registration for securities investment fund management and securities portfolio management.

Prudential Vietnam Assurance Private Limited is the sole owner of Eastspring Investments Vietnam.

Eastspring Investments Vietnam is regulated by the State Securities Commission of Vietnam ('SSC'), which is overseen by the Ministry of Finance ('MoF'). In keeping with its mandate to establish and develop the securities markets, the SSC supervises the organisation, and operation of securities investment funds and fund management companies.

Indonesia

PT. Eastspring Investments Indonesia ('Eastspring Investments Indonesia') was established on 24 March 2011, owned 99% by Eastspring Investments (Hong Kong) Limited and 1% by PT. Prudential Life Assurance. Eastspring Investments Indonesia received its Asset Management Company license on 25 April 2012, which was granted Bapepam-LK. Eastspring Investments Indonesia is currently exclusively regulated and supervised by the Investment Management Bureau of Bapepam-LK. (As discussed above under 'Regulation of insurance business *Indonesia PT Prudential Life Assurance*', Bapepam-LK is in the transitional period to becoming OJK.) This operating license authorised Eastspring Investments Indonesia to perform fund management of collective investment portfolios and discretionary fund portfolios. In addition, Eastspring Investments Indonesia is also allowed to provide investment advisory services regarding the purchase and sale of securities by its clients but without receiving any financial compensation. This condition of non-compensation for the investment advisory service shall apply as long as Eastspring Investments Indonesia has no investment advisory license.

United States

Eastspring Investments Incorporated ('Eastspring Investments USA') was incorporated in the State of Delaware in April 2012 and the business was launched in August 2012. Eastspring Investments USA is an indirect wholly owned subsidiary of Prudential plc.

Eastspring Investments USA is not engaged in providing investment management services or in broker-dealer activity. On behalf of its affiliate, Eastspring Investments (Singapore) Ltd. ('Eastspring Investments Singapore'), Eastspring Investments USA serves as a 'solicitor' as that term is defined under the provisions of the Investment Adviser Act of 1940 and the rules thereunder. Eastspring Investments Singapore is registered with the U.S. Securities and Exchange Commission as a registered investment adviser, and, although its solicitation activity is regulated under the Investment Adviser Act of 1940, Eastspring Investments USA is not required to be separately registered with the U.S. Securities and Exchange Commission.

Certain US states and local governmental bodies may require that individuals engaged in solicitation activity be either registered or otherwise qualify for an exemption to be soliciting in that jurisdiction. Based on its solicitation activity on behalf of Eastspring Investments Singapore, Eastspring Investments USA is subject to the solicitation restrictions and filings of those individual states, as applicable.

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US Supervision and Regulation

Overview

Prudential conducts its US insurance activities through Jackson, a life insurance company licensed to transact its insurance business in, and subject to regulation and supervision by, the District of Columbia, the Cayman Islands and 49 of the 50 states. Jackson operates a subsidiary, Jackson National Life Insurance Company of New York, in the state of New York. The extent of such regulation varies, but most jurisdictions have laws and regulations governing the financial aspects of insurance companies, including standards of solvency, reserves, reinsurance and capital adequacy and the business conduct of insurance companies. In addition, statutes and regulations usually require the licensing of insurers and their agents and the approval of policy forms and related materials. These statutes and regulations in a US insurance company's state of domicile (Michigan in the case of Jackson) also regulate the investment activities of insurers.

Insurance regulatory authorities in the jurisdictions in which Jackson does business require it to file detailed quarterly and annual financial statements, and these authorities have the right to examine its operations and accounts. In addition, Jackson is generally subject to federal and state laws and regulations that affect the conduct of its business. New York and Michigan require their state insurance authorities to conduct an examination of an insurer under their jurisdiction at least once every five years.

In 2012, the New York insurance authorities commenced a triennial examination of Jackson National Life of New York for the examination period of 1 January 2009 through 31 December 2011. Michigan insurance authorities commenced an examination of Jackson in 2012 for the period 1 January 2009 through 31 December 2011. There have been no material findings to date in the examinations by the Michigan and New York authorities.

Jackson's ability to pay shareholder dividends is limited under Michigan insurance law. The Commissioner of the Michigan Office of Financial and Insurance Regulation (the 'Michigan Insurance Commissioner') may limit, or not permit, the payment of shareholder dividends if the Michigan Insurance Commissioner determines that an insurer's surplus, as regards policyholders, is not reasonable in relation to its outstanding liabilities and is not adequate to meet its financial needs as required by Michigan insurance law. Jackson must report any shareholder dividends to the Michigan Insurance Commissioner before they can be paid. In the case of an extraordinary shareholder dividend or distribution, an insurer may not pay the dividend or distribution until 30 days after the Michigan Insurance Commissioner has received notice of the declaration and has not disapproved, or has approved, the payment within that period. For this purpose, an extraordinary dividend or distribution means any dividend or distribution of cash or other property where the fair market value, together with that of other dividends or distributions that an insurer made within the preceding twelve months, exceeds the greater of 10 per cent of the insurer's surplus, as regards policyholders as of 31 December of the immediately preceding year, or the net gain from operations of the insurer, not including realised capital gains, for the prior year. In 2010, 2011 and 2012, Jackson paid shareholder dividends to Prudential plc of US$275.0 million, US$530.0 million, and US$400.0 million respectively.

State regulators also require prior notice or regulatory approval of changes in control of an insurer or its holding company and of certain material transactions with affiliates. Under New York and Michigan insurance laws and regulations, no person, corporation or other entity may acquire control of an insurance company or a controlling interest in any parent company of an insurance company, unless that person, corporation or entity has obtained the prior approval of the regulator. For the purpose of each of New York and Michigan law, any person acquiring, directly or indirectly, 10 per cent or more of the voting securities of an insurance company is presumed to have acquired 'control' of the company. To obtain approval of any change in control, the proposed acquirer must file an application with the New York Superintendent of Insurance or the Michigan Insurance Commissioner, as appropriate. This

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application requires the proposed acquirer to disclose, among other information, its background, financial condition, the financial condition of its affiliates, the source and amount of funds by which it will effect the acquisition, the criteria used in determining the nature and amount of consideration to be paid for the acquisition, proposed changes in the management and operations of the insurance company and other related matters. The Michigan Insurance Commissioner can grant an exemption from filing an application if an acquisition does not have the effect of changing or influencing control.

On 4 September 2012, with applicable regulatory approvals, Jackson completed the purchase of SRLC America Holding Corp ('SRLC') from Swiss Re Life Capital Ltd. ('Swiss Re') for a consideration of US$587 million which is subject to finalisation of completion procedures. Reassure America Life Insurance company (REALIC), an Indiana domiciled life insurer, was a wholly owned subsidiary of SRLC and the primary business entity under SRLC prior to the transaction. Certain REALIC business was excluded from the purchase through 100 per cent coinsurance transactions executed prior to the sale between REALIC and Swiss Re and its affiliates. Under the Michigan insurance law, value of business acquired ("VOBA") is reported as an admitted asset if certain criteria are met. In relation to the acquisition of REALIC and pursuant to Michigan insurance law at 31 December 2012, Jackson reported approximately US$470.1 million of statutory basis VOBA, which is fully admissible. Accordingly, the acquisition had no impact on Jackson's statutory basis capital and surplus at the acquisition date. On 31 December 2012, with applicable regulatory approvals, REALIC was merged with and into Jackson.

Guaranty associations and similar arrangements

Each of the 50 states of the United States, the District of Columbia and the Commonwealth of Puerto Rico has laws requiring insurance companies doing business within their jurisdictions to participate in various types of guaranty associations or other similar arrangements. These associations and arrangements provide certain levels of protection to policyholders from losses under insurance policies issued by insurance companies that become impaired or insolvent. Typically, these associations levy assessments, up to prescribed limits, on member insurers on a basis that is related to the member insurer's proportionate share of the business in the relevant jurisdiction of all member insurers in the lines of business in which the impaired or insolvent insurer is engaged. Some jurisdictions permit member insurers to recover assessments that they paid through full or partial premium tax offsets, usually over a period of years. In 2012, Jackson increased its reserve for future guarantee fund assessments by $20.1 million as a result of the announced liquidation of the Executive Life Insurance Company of New York. Prudential Group estimated its reserve for future guarantee fund assessments for Jackson to be US$23 million at 31 December 2011. Prudential estimated its reserve for future guarantee fund assessments for Jackson to be US$39.6 million at 31 December 2012. Prudential believes this reserve to be adequate for all anticipated payments for known insolvencies.

Asset valuation reserve

State regulators generally require that insurers establish an asset valuation reserve that consists of two components: a 'default component' to provide for future credit-related losses on fixed income investments and an 'equity component' to provide for losses on all types of equity investments. The asset valuation reserve establishes statutory reserves for fixed maturity securities, equity securities, mortgage loans, real estate, derivative instruments and other invested assets. The reserve is designed to provide for a normalised level of future losses based on the credit rating of each individual investment. The level of reserves is based on both the type of investment and its rating. Contributions to the reserve may result in a reduction in Jackson's unassigned surplus, which, in turn, may reduce funds available for shareholder distributions. The extent of the impact of the asset valuation reserve on Jackson's statutory surplus depends in part on the future composition of the investment portfolio.

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Interest maintenance reserve

State regulators generally require that insurers establish an interest maintenance reserve to defer non-credit-related realised capital gains and losses, net of taxes, on fixed income investments (primarily bonds, derivative instruments and mortgage loans) which are amortised into net income over the estimated remaining periods to maturity of the investments sold and to defer material gains or losses, net of taxes, resulting from market value adjustments on policies and contracts backed by assets carried at book value. The extent of the impact of the interest maintenance reserve on earnings and surplus depends on the amount of future interest rate-related realised capital gains and losses on fixed maturity investments, derivatives and mortgage loans and deferred gains or losses resulting from market value adjustments on policies and contracts backed by assets that are valued at book value.

The National Association of Insurance Commissioners ratios

On the basis of statutory financial statements that insurers file with state insurance regulators, the National Association of Insurance Commissioners annually calculates 12 financial ratios to assist state regulators in monitoring the financial condition of insurance companies. A usual range of results for each ratio is used as a benchmark and departure from the usual range on four or more of the ratios can lead to inquiries from individual state insurance departments. In 2012, none of Jackson's ratios fall outside the usual range.

Policy and contract reserve sufficiency analysis

State insurance laws require life insurance companies to conduct annually an analysis of the sufficiency of its life and annuity reserves. A qualified actuary must submit an opinion that states that the reserves, when considered in the light of the assets that an insurance company holds with respect to such reserves, make good and sufficient provision for the associated contractual obligations and related expenses of the insurance company. If a qualified actuary cannot provide such an opinion, then the insurance company must set up additional reserves by moving funds from surplus. The 2011 opinion has been submitted to the Michigan Office of Financial and Insurance Regulation without any qualifications.

Jackson's capital and surplus

Michigan insurance law requires Jackson, as a domestic life insurance company, to maintain at least US$7,500,000 in unimpaired capital and surplus. In addition, insurance companies are required to have sufficient capital and surplus to be safe, reliable and entitled to public confidence.

As a licensed insurer in the District of Columbia and every state but New York, where it operates through a subsidiary, Jackson is subject to the supervision of the regulators of each jurisdiction. In connection with the continual licensing of Jackson, regulators have discretionary authority to limit or prohibit the new issuance of business to policyholders when, in their judgment, the regulators determine that such insurer is not maintaining minimum surplus or capital or if the further transaction of business will be hazardous to policyholders.

As a Michigan domiciled insurer, Jackson is subject to a prescribed accounting practice that, under certain circumstances, allows an insurer to include the 'value of business acquired' as an admitted asset in excess of the amount allowed under NAIC guidance. At 31 December 2012, as a result of the acquisition of REALIC, Jackson has admitted US$242 million of value of business acquired in excess of the amount allowed under NAIC guidance.

Jackson has received approval from the Michigan Office of Financial and Insurance Regulation regarding the use of a permitted accounting practice. This permitted practice allows Jackson to carry certain interest rate swaps at book value as if statutory hedge accounting were in place instead of at fair value as would have been otherwise required. The permitted practice is effective 31 December 2012

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and expires with the period ending 30 September 2013 unless extended by the Michigan Insurance Commissioner. The effects of this permitted practice may not be considered by the company when determining the surplus available for dividends, nor the nature of dividends as ordinary or extraordinary.

Risk-based capital

The National Association of Insurance Commissioners has developed risk-based capital standards for life insurance companies as well as a model act for state legislatures to enact. The model act requires that life insurance companies report on a risk-based capital formula standard that they calculate by applying factors to various asset, premium and reserve items and separate model based calculations of risk associated primarily with variable annuity products. The risk-based capital formula takes into account the risk characteristics of a company, including asset risk, insurance risk, interest rate risk, market risk and business risk. The National Association of Insurance Commissioners designed the formula as an early warning tool to identify potentially inadequately capitalised companies for purposes of initiating regulatory action.

Any state adopting the model act gives the state insurance commissioner explicit regulatory authority to require various actions by, or take various actions against, insurance companies whose adjusted capital does not meet minimum risk-based capital standards. The Michigan Office of Financial and Insurance Regulation takes into account the National Association of Insurance Commissioners' risk-based capital standards to determine compliance with Michigan insurance law.

At 31 December 2012 the Company's total adjusted capital under the National Association of Insurance Commissioners' definition substantially exceeded Michigan standards.

Regulation of investments

Jackson is subject to state laws and regulations that require diversification of its investment portfolio, limit the amount of investments in certain investment categories such as below investment grade fixed income securities, common stock, real estate and foreign securities and forbid certain other types of investments altogether. Jackson's failure to comply with these laws and regulations would cause investments exceeding regulatory limitations to be treated by the Michigan Insurance Commissioner as non-admitted assets for purposes of measuring surplus and, in some instances, the Michigan Insurance Commissioner could require divestiture of non-qualifying investments.

Implementation of US Foreign Account Tax Compliance Act ('FATCA') provisions

Although the insurance business is regulated on a State level, US federal tax legislation and rules, including those relating to the insurance industry or insurance products, can have a significant impact on Prudential's business. Tax legislation and rules, and their interpretation, may change, possibly with retrospective effect, and proposals that would affect such changes are debated periodically by the US Congress.

Legislation incorporating provisions referred to as FATCA was passed in the US on 18 March 2010. The legislation and subsequent final regulations released in January 2013, requires Foreign Financial Institutions (FFIs) (such as Prudential plc and many of its subsidiaries) to enter into an FFI agreement, which requires the FFI to undertake due diligence procedures to identify and provide information on accounts held by US persons and US-owned foreign entities, or otherwise face a 30 per cent withholding tax on certain payments made to the FFI. In addition, FFIs that have entered into an FFI agreement may be required to withhold on certain payments made to FFIs that have not entered into an FFI Agreement, account holders who fail to provide sufficient information to classify an account as a US or non-US account, and US account holders who do not agree to the FFI reporting certain account related information to the IRS.

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Since 2012, the US Treasury has been negotiating intergovernmental agreements (IGA) with a number of countries which will result in those countries embedding the FATCA provisions into their domestic law. This development should have the added benefit of significantly reducing any withholding obligations on payments by US companies or FFIs to other companies or customers in these IGA countries. On 12 September 2012, the United Kingdom and the United States entered into an IGA which is expected to be implemented into UK law as part of the Finance Bill 2013 and related regulations. Prudential plc will be subject to the information collection and sharing required under this IGA, although non-UK branches of Prudential plc and non-UK subsidiaries of Prudential plc that are FFIs will not be subject to the UK-US IGA. These non-UK branches and subsidiaries will instead be required to either comply with an IGA in their home jurisdictions (if any), or comply with the FATCA provisions and final regulations. Any applicable IGA may require compliance with the FATCA provisions and final regulations, as modified by the relevant IGA.

FATCA will have an impact on many of Prudential's non-US businesses in the UK and Asia, and will require a review and enhancement of existing practices to ensure FATCA compliance. A Group-wide project has been set up by Prudential to manage the implementation of the new practices. All of Prudential's businesses have established formal project structures to deliver the requirements within the timescales.

The start date for implementation of the FATCA regime, including withholding on certain US source payments and the implementation of certain account diligence procedures, was recently changed from 1 January 2013 to 1 January 2014 and certain provisions may be further delayed. Complying with the required identification, withholding and reporting obligations is expected to require significant review and focus in an FFI's compliance and reporting framework. We are following developments regarding FATCA closely, and are coordinating with all relevant authorities.

USA Patriot Act

The USA Patriot Act, enacted in 2001, includes numerous provisions designed to fight international money laundering and to block terrorist access to the US financial system. The US Treasury Department has issued a number of regulations implementing the Patriot Act that apply certain of its requirements to financial institutions including broker dealers and insurance companies. Among other things, the regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Jackson and, to the extent applicable, certain of its affiliates, have established policies and procedures to ensure compliance with the Patriot Act's provisions and the Treasury Department regulations.

Securities laws

Jackson, certain of its affiliates and certain policies and contracts that Jackson issues are subject to regulation under the federal securities laws administered by the US Securities and Exchange Commission (the 'SEC'). The primary intent of these laws and regulations is to protect investors in the securities markets and generally grant supervisory agencies broad administrative powers, including the power to limit or restrict the conduct of business for failure to comply with such laws and regulations and (in the case of broker dealers) to impose capital and related requirements. Jackson may also be subject to similar laws and regulations in the states in which it provides investment advisory services, offers the products described above or conducts other securities-related activities.

Jackson National Asset Management, LLC ('JNAM') is registered with the SEC as an investment adviser pursuant to the Investment Advisers Act of 1940, as amended (the 'Investment Advisers Act'). JNAM is registered as a transfer agent pursuant to the Securities Exchange Act of 1934, as amended (the 'Securities Exchange Act'). The investment companies (mutual funds) for which JNAM serves as an investment adviser are subject to SEC registration and regulation pursuant to the Securities Act of 1933,

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as amended (the 'Securities Act'), and the Investment Company Act of 1940, as amended (the 'Investment Company Act'). Certain of the mutual funds advised by JNAM underlie variable products offered by Jackson. In addition, each variable annuity and variable life product sponsored by Jackson is subject to SEC registration and regulation pursuant to the Securities Act and the Investment Company Act, and applicable state insurance and securities laws. Each variable annuity and variable life product is organised as a separate account that is a unit investment trust.

Effective 31 December 2012, the U.S. Commodity Futures Trading Commission ('CFTC') eliminated an exclusion previously available to the mutual funds from the definition of a 'commodity pool' under the Commodity Exchange Act ('CEA'). Consequently, certain of the mutual funds became a commodity pool and became subject to the requirements of the CEA and the rules of the CFTC promulgated thereunder. As of 1 January 2013, JNAM is registered with the CFTC and the National Futures Association ('NFA') as a 'commodity pool operator' and is acting as a 'commodity pool operator' with respect to the operation of certain of the mutual funds as 'commodity pools' under and pursuant to the CEA, as applicable. The full impact of these new requirements on JNAM and the mutual funds is uncertain at this time. However, the new requirements will cause JNAM and the mutual funds to incur additional regulatory compliance and reporting expenses. The effects of these regulatory changes could reduce investment returns or harm the mutual fund's ability to implement its investment strategy.

Curian Capital, LLC ('Curian Capital') is registered with the SEC pursuant to the Investment Advisers Act and is also registered or notice filed in all applicable states. Curian serves as an investment adviser to certain investment companies. The investment companies (mutual funds) for which JNAM serves as an investment adviser are subject to SEC registration and regulation pursuant to the Securities Act and Investment Company Act. Certain of the mutual funds advised by Curian Capital underlie variable products offered by Jackson. In addition, each variable annuity and variable life product sponsored by Jackson is subject to SEC registration and regulation pursuant to the Securities Act and the Investment Company Act, and applicable state insurance and securities laws. Each variable annuity and variable life product is organised as a separate account that is a unit investment trust.

As of 1 January 1, 2013, Curian Capital is registered with the CFTC and the NFA as a 'commodity pool operator' and is acting as a 'commodity pool operator' with respect to the operation of certain of the mutual funds as 'commodity pools' under and pursuant to the CEA, as applicable. The full impact of these new requirements on Curian Capital and the mutual funds is uncertain at this time. However, the new requirements will cause Curian Capital and the mutual funds to incur additional regulatory compliance and reporting expenses. The effects of these regulatory changes could reduce investment returns or harm the mutual fund's ability to implement its investment strategy.

Curian Clearing, LLC is registered as a broker-dealer with the SEC pursuant to the Securities Exchange Act, and is registered as a broker-dealer in all applicable states. In addition, Curian Clearing, LLC is a member firm of the Financial Industry Regulatory Authority (the 'FINRA'), subject to its supervisory and regulatory requirements.

Jackson National Life Distributors LLC is registered as a broker-dealer with the SEC pursuant to the Securities Exchange Act, and is registered as a broker-dealer in all applicable states. In addition, Jackson National Life Distributors LLC is a member firm of the FINRA, subject to its supervisory and regulatory requirements.

National Planning Holdings, Inc. ('NPH') owns four retail broker dealers, being IFC Holdings, Inc. (doing business as INVEST Financial Corporation), ('IFC'), Investment Centers of America, Inc ('ICA'), National Planning Corporation ('NPC') and SII Investments, Inc. ('SII'). These entities conduct business as securities broker-dealers, investment advisers, and insurance agencies (or affiliated with insurance agencies), and are licensed and qualified to transact business pursuant to their respective registration on licensure with the SEC, state securities and insurance authorities, and membership with FINRA and the

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Municipal Securities Rulemaking Board. NPC, SII, and ICA are also registered with the CFTC, and are members of the NFA for purposes of commodities and futures trading.

Prudential also conducts certain of its US institutional investment management activities through PPM America, Inc., which is registered with the SEC as an investment adviser under the Investment Advisers Act. PPM America serves as the investment adviser to Jackson and as the primary institutional investment adviser for certain Prudential subsidiaries, including The Prudential Assurance Company Limited. PPM America also acts as sub-adviser to certain US and foreign advisers affiliated with Prudential with respect to certain US portfolios of accounts or products sponsored or managed by such affiliates, including US mutual funds, UK-based pooled investment vehicles, a Luxembourg-based SICAV, Japanese investment trusts, and other similar vehicles. PPM America also serves as an investment adviser to other affiliated and unaffiliated institutional clients such as CDOs or similar structured vehicles and private investment funds (in which PPM America affiliates such as Prudential UK entities and Jackson are generally investors), and a limited number of other unaffiliated accounts. The US mutual funds for which PPM America serves as sub-adviser are subject to regulation under the Securities Act and the Investment Company Act, and other similar vehicles organised outside of the US may also be subject to regulation under applicable local law.

PPM America and certain of its subsidiaries are subject to various levels of regulation under the federal securities laws that the SEC administers as well as state securities laws. In connection with providing investment advisory services to certain of its clients, PPM America may also be subject to regulation under applicable foreign laws.

To the extent that PPM America or the NPH broker-dealers manage accounts with assets of employee benefit plans subject to the Employee Retirement Income Security Act of 1974 ('ERISA'), or the Internal Revenue Code, they may be subject to certain restrictions imposed by ERISA or the Internal Revenue Code. Such restrictions are summarised in 'Employee Benefit Plan Compliance' in the Section below. The US Department of Labor (the 'Department of Labor') and the US Internal Revenue Service have interpretive and enforcement authority over the applicable provisions of ERISA and the Internal Revenue Code.

Disclosure obligations under the US Securities Exchange Act and in particular under Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012

Under Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012, which added Section 13(r) of the US Securities and Exchange Act of 1934, we are required to disclose certain of our activities and those of our affiliates related to Iran and to persons sanctioned by the United States under programs relating to terrorism and proliferation of weapons of mass destruction that occurred in the twelve-month period covered by this report.

Two of our non-US affiliates have engaged in transactions with persons sanctioned by the United States under Executive Order 13224, relating to terrorism. These transactions were entered into in compliance with laws and regulations applicable to the relevant affiliates. The first individual took out a one-off takaful certificate (a Shariah compliant life policy) with our Malaysian insurance subsidiary in October 2011. It was discovered in March 2012 through automated checking that his name matched various sanctions lists. The policy was for RM600 per month and RM 7,200 was paid for the year in 2012 (equivalent to around US$193 and US$2,316 respectively). The matter was reported to the Malaysian governmental sanctions authority, the Bank Negara Malaysia Financial Intelligence Unit, in March 2012.

The second individual is a beneficiary to three life insurance policies in his wife's name, the first taken out in December 2010 and two others taken out in November 2011 with our Indonesian insurance subsidiary. The first policy has a monthly premium of Rp 500,000 (around US$51) with premiums paid of Rp 6,000,000 paid for the year in 2012 (approximately US$612), the second and third are also for

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Rp 500,000 per month each with Rp 6,000,000 paid into each policy in 2012. The person was identified as a sanctioned individual in July 2012, and the matter was notified to the Indonesian governmental sanctions authority, the Indonesia FIU (PPATK), in August 2012. All 3 policies remain in force, but payments out will only be made in accordance with applicable law.

As the provisioning of insurance liabilities is undertaken on a portfolio as a whole basis, it is not practical to estimate the 2012 net profits on the contracts referred to above. We do not intend to engage in further new business dealings with these individuals.

In the UK, the Prudential Assurance Company Ltd operates a pension scheme for employees of the UK branch of government-owned Iranian bank. A total of 58 scheme members are receiving benefits, with 49 deferred members. All members are inactive in that no member or scheme contributions are being made or were made in 2012. The scheme is closed to new members. Due to the long term nature of a pension scheme it is not practical to advise the net profit, but the fund value at 31 December 2012 stood at £5,510,527.00. In return for administering the scheme there are standard Prudential scheme charges: an annual fee of £692, plus £11 per member, £56 per quote and a Trustee Accounts charge (£1,849.50 currently), all subject to 20 per cent Value Added Tax and an annual review. The annual invoice submitted for the annual period to 31 July 2012 was for £4,675.80 (including VAT). In addition to this an Annual Management Charge of 1.25 per cent is reflected in the fund value. The UK governmental sanctions authority, HM Treasury, has been informed of this arrangement and in 2008 advised us that following an analysis of the deeds, the fund is not owned, held or controlled by the bank. Payments out of the fund have been approved by HM Treasury through a licence. There are no plans to discontinue with this contract in light of this licence.

Employee benefit plan compliance

Jackson issues certain types of general account stable value products, such as GICs and funding agreements, to employee benefit plans and to investment vehicles that pool the investments of such plans. Many of these plans are retirement plans that are subject to the fiduciary standards of ERISA and that are tax-qualified under the Internal Revenue Code. As such, Jackson may be subject to certain restrictions imposed by ERISA and taxes imposed by the Internal Revenue Code. These restrictions include:

- the requirement under ERISA that fiduciaries must perform their duties solely in the interests of ERISA plan participants and beneficiaries,
- the requirements under ERISA that fiduciaries may not engage in 'conflict of interest' transactions, and
- the requirements under ERISA that a fiduciary may not cause a covered plan to engage in certain 'prohibited transactions' with certain persons who provide services to the plan or are affiliated with the plan sponsor or a plan service provider.

In general, the Internal Revenue Code imposes taxes on persons involved in certain of the transactions described above.

The Department of Labor and the Internal Revenue Service have interpretive and enforcement authority over the applicable provisions of ERISA and the Internal Revenue Code.

In the instance where an insurer issues a guaranteed benefit policy to a plan, ERISA provides that the insurer need not become a fiduciary with respect to the plan solely as a result of the issuance of the policy. Under Section 401 of ERISA, a guaranteed benefit policy means an insurance policy to the extent such policy provides for benefits the amount of which the insurer guarantees.

In 1993, in John Hancock Mutual Life Insurance Company v. Harris Trust & Savings Bank, the US Supreme Court held that a portion of the funds held under a certain type of general account annuity

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contract did not constitute a 'guaranteed benefit policy' within the meaning of ERISA, a holding which potentially exposes insurers with similar types of contracts to the application of ERISA's fiduciary and prohibited transaction provisions in connection with the management of assets in their general accounts.

Although no assurances can be given, Jackson believes that none of its contracts are of the type to which the holding in Harris Trust would be applicable. Moreover, the Department of Labor has issued PTE 95-60, which generally exempts external, unaffiliated investment transactions from ERISA's prohibited transaction provisions. If the Harris Trust holding is applied to its contracts, Jackson would be subject to ERISA's fiduciary and prohibited transaction provisions described above.

Financial services regulatory and legislative issues

In the US, the Dodd Frank Wall Street Reform and Consumer Protection Act of 2010 ('The Dodd Frank Act') which represents a comprehensive overhaul of the financial services industry within the United States, was enacted in July 2010. The full impact of the Dodd Frank Act on Prudential's businesses is not currently clear, however, as many of its provisions have a delayed effectiveness and/or require rulemaking by various US regulators over the coming years.

The Dodd Frank Act vests a newly created Financial Stability Oversight Council ('the Council') with the power to designate systemically important institutions which will be subject to special regulatory supervision and other provisions intended to prevent or mitigate the impact of future disruptions in the US financial system. If Prudential is designated as a systemically important institution, its US operations may be subject to heightened prudential standards to be administered by the US Federal Reserve Board, including, amongst other things, heightened capital, leverage and liquidity standards, risk management requirements, concentration limits, resolution plans and stress tests, and potential discretionary requirements relating to contingent capital, enhanced public disclosure and short term debt limits. This same analysis may also be applied to Jackson.

Rules and guidance outlining the manner in which the Council will determine which companies should be so designated were adopted in April 2012. The rules set forth a three-stage process of increasingly in-depth evaluation and analysis, drawing on both qualitative and quantitative information (but preserving significant Council discretion). The rules do not, however, permit a definitive view as to whether Prudential (or Jackson) would or would not be designated as systemically important.

Other changes in the Dodd Frank Act include the creation of a new 'Federal Insurance Office' within the Treasury Department that will, amongst other things, monitor (but not regulate) the insurance industry and, conduct a study of how to improve insurance regulation in the United States; discretionary authority for the SEC to impose a harmonised standard of care for investment advisers and broker dealers which provide personalised advice about securities to retail customers; and requiring that certain derivatives be traded on registered exchanges and cleared through registered central counterparties.

Prudential and Jackson have determined that they are not swap dealers/security-based swap dealers or major swap participants/major security-based swap participants. However, it is not yet clear how and to what extent other swaps regulation might apply to non-US institutions. With the passage of the Dodd Frank Act, certain derivatives instruments, including, but not limited to, futures contracts, interest rate swaps, and credit default swaps, may be required to trade on an exchange. While the transition to exchange-traded derivative instruments may limit counterparty risk, it could increase costs associated with such investments, including transaction and exchange fees. The standardization of exchange-traded derivative instruments may also limit the ability of Jackson and the mutual funds to customise certain derivative instruments with the counterparties. Exchange-trade derivative instruments may also require the Jackson and the mutual funds to post additional collateral or limit the types of collateral that may be used for such transactions, and this may limit the ability of the Jackson and the mutual funds to effectively deploy assets in a timely manner.

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The timing and the ultimate impact on the management and operations of Prudential and the regulations promulgated, or to be promulgated, pursuant to these statutory provisions, cannot yet be definitively determined.

Proposals to change the laws and regulations governing the financial services industry are frequently introduced in the US Congress, in the state legislatures and before the various regulatory agencies. The likelihood and timing of any proposals or legislation, and the impact they might have on Jackson, its subsidiaries, or other Prudential subsidiaries doing business in the US, cannot be determined at this time.

State legislatures and/or state insurance regulatory authorities frequently enact laws and/or regulations that significantly affect insurers supervised by such authorities. Although the US federal government does not directly regulate the insurance business, federal initiatives may also have an impact on the insurance industry.

A coalition of national insurance and banking organisations has supported the introduction of US federal legislation that would allow insurance companies to obtain a federal charter as a regulatory alternative to a state charter. A coalition of insurers has been formed that is opposed to the so-called optional federal charter. Prudential cannot predict whether any federal charter or any other federal (or state) legislative initiative to change the nature or scope of the regulation of the insurance industry will be enacted into law.

Federal and state regulators have focused on the mutual fund and variable annuity and insurance product industries including the broker-dealer system. As a result of publicity relating to widespread perceptions of industry abuses, including fraudulent and anti-competitive practices among insurance brokers and mutual funds, there have been numerous regulatory inquiries and proposals for legislative and regulatory actions that could affect the operations and management of market participants. It is difficult to predict at this time whether changes resulting from industry investigations and/or new laws and regulations will affect the Group's insurance or investment management businesses, and, if so, to what degree.

Capital Expenditures and Divestures

Please refer to Item 5 'Operating and Financial Review' Liquidity and Capital Resources Changes to Group holdings during the period' for a discussion of the principal capital expenditures and divestures during the period under review.

Item 4A. Unresolved Staff Comments

None

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Item 5. Operating and Financial Review and Prospects

The following discussion and analysis should be read in conjunction with Prudential's consolidated financial statements and the related notes to Prudential's consolidated financial statements included in this document.

A summary of the critical accounting policies which have been applied to these statements is set forth in the section below entitled 'IFRS Critical Accounting Policies'.

The results discussed below are not necessarily indicative of the results to be expected in any future periods. This discussion contains forward-looking statements based on current expectations, which involve risks and uncertainties. Actual results and the timing of certain events may differ significantly from those projected in these forward-looking statements due to a number of factors, including those set forth in the section below entitled ' Principal Factors Affecting Results of Operations' and in Item 3, 'Key Information Risk Factors' and elsewhere in this document.

Introduction and Overview

Prudential is an international retail financial services group with significant operations in Asia, the US and the UK. Prudential serves around 24 million insurance customers globally and has £405 billion of assets under management. Prudential is listed on stock exchanges in London, Hong Kong, Singapore and New York. Prudential is structured around four main business units: Prudential Corporation Asia, (incorporating the asset management business, Eastspring Investments), Jackson, Prudential UK and M&G.

Prudential is a leading life insurer in Asia operating in 13 markets (including Cambodia, where operations were launched in 2013). Prudential has built a high performing platform with effective, multi-channel distribution, a product portfolio centred on regular savings and protection, award winning customer services and a well respected brand. Prudential's Asian based asset management division, Eastspring Investments, is one of the region's leading fund managers and the largest retail asset manager.

Jackson is one of the largest life insurance companies in the US, providing retirement savings and income solutions to approximately 4 million customers. Jackson is also one of the top two providers of variable annuities in the US. Founded 50 years ago, Jackson has a long and successful record of providing advisers with the products, tools and support to design effective retirement solutions for their clients.

Prudential UK is a leading life and pensions provider to approximately 7 million customers in the United Kingdom. Prudential believes that its expertise in areas such as longevity, risk management and multi-asset investment, together with its financial strength and highly respected brand, means that the business is strongly positioned to continue pursuing a value-driven strategy built around our core strengths in with-profits and annuities.

M&G is Prudential's UK and European fund management business with total company and external assets under management of £228 billion (at 31 December 2012). M&G has been investing money for individual and institutional clients for over 80 years. It is one of Europe's largest active investment managers.

Summary of Performance

The Group reported a strong performance in 2012. Our focus on our customers in each of our geographies combined with the strength of our distribution, franchise and brands, has allowed us to continue to provide distinctive value to our customers. Thanks to this, the Group has continued to deliver on the three key financial metrics we have focused on since 2009: IFRS operating profit, new

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business profit and net cash remittances. In 2012 in Asia, we have achieved two of the 2013 'Growth and Cash' objectives and have continued to make progress towards achieving the others, despite a global macroeconomic environment which remains challenging and historically low long-term interest rates.

Prudential Corporation Asia (insurance operations)

Asia has delivered excellent results in 2012. Our business, Prudential Corporation Asia, which is already one of the largest in the region, has nevertheless been able to more than double its IFRS operating profit based on longer-term investment returns in three years to almost £1 billion, delivering £988 million in 2012. That growth in IFRS operating profit based on longer-term investment returns was not achieved at the expense of cash generation or by slowing down sales growth. It also delivered a net cash remittance of £341 million, exceeding its 2013 objective of £300 million. For the first time in our history, Asia was the largest contributor of cash to the Group, an exceptional performance when you consider that in 2009 Asia's net cash remittance was £40 million. This performance was largely driven by the clear progress we have made in some of our 'sweet-spot' markets particularly Indonesia, Singapore, Malaysia, the Philippines and Thailand.

Our strategy in Asia is focused on meeting the needs of the emerging middle class in the region for savings and protection. The region's positive demographics, strong economic growth, sound public finances and favourable public policy environment with a clear preference for private provision of protection, have all led to a rapidly expanding middle class, with a strong and growing demand for our savings and protection products.

Geographically, Asia is a vast and diverse region. Our primary area of focus is on what we call our 'sweet-spot' Indonesia, Hong Kong, Singapore, Malaysia, the Philippines, Thailand and Vietnam all these markets have attractive long term characteristics. We are in a strong position to capture profitably the growing demand for our products and services in these selected markets. We continuously invest in these markets to grow our distribution and to ensure we are well positioned in terms of people, systems and capabilities. We will continue to innovate to meet the evolving needs of our customers and maintain our focus on regular premium savings and protection products.

We have delivered healthy and sustainable quality growth in Asia. While under-penetration of insurance in markets across the region offers significant long-term growth opportunities, we retain our focus on value not volume. We refocused our businesses in Taiwan, Korea and Malaysia, deliberately reducing sales of lower margin products to ensure a consistent focus on higher value lines.

Our life business in Asia, with its focus on capital-efficient products and fast payback periods, continues to deliver profitable, cash generative growth. IFRS long-term operating profit based on longer-term investment returns in Asia increased by 30 per cent in the period to £920 million (2011: £709 million)[(11)] and net cash remittances increased by 66 per cent to £341 million (2011: £206 million).

Our four largest markets Indonesia, Hong Kong, Singapore and Malaysia have made the most material contribution to the region's growth in recent years. In addition to our well known strength in these four markets, we are building our presence and distribution in other markets that have the potential to become material drivers of growth over the medium and long term. Two such markets are Thailand and the Philippines. In Thailand, a market with considerable and attractive growth potential, where we were historically underweight, our recently announced exclusive long-term bancassurance partnership with Thanachart, and the acquisition of Thanachart Life, fulfils our longstanding ambition to significantly increase our footprint in that country. In the Philippines, where we are a market leader, our business is now making good progress delivering strong and profitable growth. We believe this market has promising prospects due to its large population and the improved quality of its macroeconomic

(11) Comparatives adjusted for retrospective application of the accounting policy change for deferred acquisition costs as discussed in note A5 to the Prudential's consolidated financial statements in Item 18.

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management, with its renewed emphasis on attracting foreign direct investment as well as the upgrading of the country's infrastructure. In January 2013, we started life insurance operations in Cambodia, our thirteenth market and entered into a partnership with ACLEDA Bank PLC, the largest retail and commercial bank in the country. This is the first deal of its kind in Cambodia, where we believe there are significant opportunities for growth as the market develops.

Overall, our geographic footprint, combined with the exceptional quality of our distribution and of our products, has enabled us to deliver another year of very strong performance in Asia. Our 13 million insurance customers, whom we serve well and profitably, represent only a small proportion of the long-term potential of this part of the world for our company.

Jackson

There was strong growth in the US, with total IFRS operating profit based on longer-term investment returns exceeding £1 billion for the first time, demonstrating the strength of Jackson's operations in a competitive marketplace. The US is the world's largest retirement savings market, with large cohorts of the 78 million baby-boomers[(12)] reaching retirement age each year, creating significant demand for retirement income products. Our strategy in the US is to take advantage of this profitable growth opportunity. We approach this with a long-term perspective, proactively managing sales through the economic cycle as our experience has shown us how important it is to put value ahead of volume in the variable annuity market. We take at all times a conservative approach to pricing, even when that means losing market share to other players, while hedging our financial risks and managing our balance sheet.

In 2012, Jackson delivered IFRS long-term operating profit based on longer-term investment returns of £964 million, up 48 per cent on the prior year (2011: £651 million[(13)]). This increase in profits is in part due to increased fee income from the significant net flows captured in the last few years, and in part due to the non-recurring in 2012 of an accelerated deferred acquisition cost amortisation charge of £190 million in 2011.

There is always a degree of tactical management in the variable annuity market as sales are impacted by a number of factors, including but not limited to, equity market levels, interest rates and the actions of Jackson's competitors. During the second half of 2012, as equity markets recovered, we saw stronger sales growth in variable annuities despite pricing actions taken earlier in the year to mitigate the impact of lower investment returns as bond yields remained low. Therefore, in November and December, Jackson worked closely with distributors to proactively manage volumes and to ensure that the level of sales for 2012 would remain within the Group's quantitative risk appetite. We will continue to proactively balance value, volume, capital and balance sheet strength in this market.

In March 2012 we launched Elite Access, a variable annuity without guarantees, which offers access to alternative investments. It taps into an unmet demand from customers and has been particularly well received by distributors. The launch of Elite Access helps Jackson to continue growing within the Group's risk appetite for products with guarantees. The acquisition of REALIC, a traditional US life business, has helped to diversify Jackson's earnings and make the business more resilient.

In the context of industry debates about the advantages and disadvantages of various accounting methods, we believe that cash generation is ultimately a very tangible metric of the quality and value of a strategy. Therefore we set Jackson a net cash remittance objective for 2013 (as described further below) which, following the acquisition of REALIC, was increased from £200 million to £260 million. In

(12) Source: US Census Bureau.

(13) Comparatives adjusted for retrospective application of the accounting policy change for deferred acquisition costs as discussed in note A5 to the Prudential's consolidated financial statements in Item 18.

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2012, Jackson delivered net cash remittances of £249 million in the year (2011: £322 million including an exceptional release of surplus) and is on track to meet this objective.

Prudential UK & Europe (insurance operations)

The UK remains focused on with-profits products and individual annuities, seeing strong sales of both in a difficult market. In the UK, Prudential has adopted a focused strategy and competes selectively to help Britain's ageing population convert their accumulated wealth into retirement income. We have a clear focus on writing profitable new business while generating cash sustainably and preserving our capital. We concentrate on areas in which we have a clear competitive advantage, namely individual annuities and with-profits products, where we continue to be market leaders.

Over the last decade, Prudential has been widely recognised as the UK's leading with-profits manager. Our long-term approach to the management of the with-profits fund has continued to benefit customers during 2012 as it helps to provide protection from the full impact of volatile market conditions. The fund has consistently out performed the FTSE All-Share Index. Over the last 15 years, the fund has delivered a cumulative investment return of 184.3 per cent on investments covering policyholder liabilities. This compares favourably with the FTSE All-Share Index total return of 106.5 per cent over the same period. Total bonus payments are expected to top £2 billion in 2013 and our policyholders will typically see year-on-year increases of between 3.5 per cent and 6.5 per cent in accumulating with-profits policy values. Since 2003 an estimated £22 billion has been added to policy values. Our UK business is also one of the largest providers of annuities in the UK and in 2012 paid out £2.9 billion in income to UK annuitants.

Our performance in 2012 has been strong in a difficult market, which has been impacted by significant UK and EU regulatory change. This includes the implementation of the Retail Distribution Review (RDR), auto-enrolment for company pension schemes and Gender Neutral Pricing.

Our UK business has demonstrated resilience as it continues to benefit from its focus on its core products, with-profits and individual annuities, with increased sales for both. Where we see opportunities for future profitable growth we will seek to capitalise on them but only if they meet our payback criteria. In 2013 we have commenced sales operations in Poland, one of Europe's fastest-growing economies, which has an expanding middle class and high savings rates.

We continue to assess the impact of the RDR, which was implemented on 31 December 2012 and the resulting changes to distributors' business models. This is likely to lead to some short-term dislocation in the market as consumers and distributors adjust to the new sales environment. We expect this transition phase to dampen our sales of investment bonds in 2013, compared to the high sales in 2012. We are confident that the strength of our brand combined with our investment capabilities, financial strength and experience will ensure that we remain well placed to provide customers with dependable retirement income. We believe that with-profits products will continue to be popular with customers seeking competitive long-term real investment returns.

Net cash remittances were £313 million, up 5 per cent (2011: £297 million). Our inherited estate, which is estimated at £7.0 billion (31 December 2011: £6.1 billion), is a key source of capital strength.

Asset Management

Our asset management business, M&G has seen record net flows, at £16.9 billion, IFRS operating profit and funds under management, all driven by its investment performance and customer proposition.

M&G, has continued to focus on delivering superior investment performance for our customers while maximising the strength of its distribution capabilities. It has pursued business diversification across both geographies and asset classes. Its retail funds are now registered for sale in 20 jurisdictions, with offices in 15 countries. During 2012, the business has seen record net sales, funds under

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management and IFRS operating profit. The growth in sales has been driven by M&G's business in Continental Europe as investor risk appetite returned.

M&G continued to attract significant new asset flows during the recent years of global market volatility, testament to the strength of its reputation and focus on investment performance. It has seen record total retail and institutional net inflows of £16.9 billion in 2012, significantly higher than 2011 and the previous high of £13.5 billion in 2009.

Total net sales in the UK were lower than 2011, reflecting the maturity of the UK business and management decisions to slow the inflow of new money into two market-leading UK corporate bond funds to safeguard investment performance. We expect these trends to persist in 2013. Despite the deliberate slowing of sales in the UK, M&G was the UK's top-selling investment management house in 2012 and has ranked number one for both net and gross fund sales for an unprecedented four consecutive calendar years. Net fund sales in Continental Europe have increased, generating a record £5.2 billion of net sales in 2012. Assets sourced from outside the UK account for 29 per cent of total retail funds under management, up from 25 per cent in 2011.

Underlying profits for the full year rose by 14 per cent to a new record level of £298 million. Following the addition of performance-related fees and profit from our associate investment in South Africa, total operating profit based on longer-term investment returns for 2012 was £320 million. M&G's funds under management also grew to a record £228 billion (2011: £201 billion).

Looking ahead, the diversification of our business by asset class and geography positions us well to manage the expected shifts in consumer asset allocation going forward.

Eastspring Investments, our rebranded Asia asset management business, increased funds under management to £58.1 billion, up 16 per cent (2011: £50.3 billion). IFRS operating profit based on longer-term investment returns was marginally lower, reflecting a change in product mix towards bond funds that attract lower fees. Also costs were higher as we continued to invest in people and infrastructure, as we build out our offshore capabilities following the launch of the new brand. This included opening a US distribution office, starting an operation in Indonesia and launching new funds in Taiwan, China and India.

2013 'Growth and Cash' Financial Objectives

As with other aspects of this annual report the following discussion contains forward-looking statements that involve inherent risks and uncertainties. Prudential's actual future financial condition or performance or other indicated results may differ materially from those indicated in any such forward-looking statement due to a number of important factors (including those discussed under Item 3 'Risk factors' in this filing). See the discussion under the heading 'Forward-looking statements' in Item 3. The objectives assume current exchange rates and a normalised economic environment consistent with the economic assumptions made by Prudential in calculating the EEV basis supplementary information for the full year 2010. They have been prepared using current solvency rules and do not pre-judge the outcome of Solvency II (as described in the Risk and Capital Management section of this filing), which remains uncertain.

At its 2010 investor conference entitled 'Growth and Cash' Prudential announced new financial objectives demonstrating our confidence in continued rapid growth in Asia, and increasing levels of cash remittances from all of our businesses. These objectives have been defined as follows:

(i)

Asia growth and profitability objectives:

To double the 2009 value of IFRS life and asset management pre-tax operating profit in 2013 (2009: £465 million); and

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To double the 2009 value of new business profits[14] in 2013 (2009: £713 million).

(ii) Business unit cash remittance objectives:

Asia to deliver £300 million of net cash remittance to the Group in 2013 (2009: £40 million);

Jackson to deliver £260 million[15] of net cash remittance to the Group in 2013 (2009: £39 million); and

UK to deliver £350 million of net cash remittance to the Group in 2013 (2009: £284 million[16]).

(iii) Cumulative net cash remittances:

All business units in aggregate to deliver cumulative net cash remittances of at least £3.8 billion over the period 2010 to end-2013. These net remittances are to be underpinned by a targeted level of cumulative underlying free surplus[17] generation of £6.5 billion over the same period.

The Group remains focused on these objectives and has continued to make progress towards them. Prudential has delivered its IFRS operating profit and net remittance objectives for Asia one year early and is on track to achieve those that remain outstanding.

Summary of Capital and Risk Management

We take a disciplined approach to capital management and continue to take action to ensure our capital works efficiently and effectively for the Group. Using the regulatory measure of the Insurance Groups Directive, our Group capital surplus position at 31 December 2012 was estimated at £5.1 billion (31 December 2011: £4.0 billion), before allowing for the final dividend. The Group's required capital cover was 3 times. The structure of the Group and the approach we have taken to managing our risks, with a sizeable credit reserve in the UK annuity book, a strong inherited estate in UK with-profits and the relatively low risk nature of our asset management and Asian operations, together with a high level of IGD surplus means we have positioned ourselves well for future regulatory developments and stresses to our business.

There is broad agreement that ultimately it would be beneficial to replace the IGD regime with a regime that is more risk based. Solvency II may provide such a framework but we now know that it will not be implemented before 31 December 2015. In common with other insurers we have been working with regulators to ensure that the current capital regime remains robust while we wait for the implementation of Solvency II.

In early March 2013, we agreed with the FSA to revise the calculation of the contribution Jackson makes to the Group's IGD surplus. We consider the revised basis to be an improvement as it is more closely aligned to the one we use to assess and report free surplus. In the absence of an agreed Solvency II approach, we believe that this change makes the IGD surplus a more meaningful measure and one that is more closely aligned with economic reality. The revised IGD surplus calculation has no impact on the way that the US business is managed or regulated locally. On this revised basis, the IGD

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(14) New business profits are the profits, calculated in accordance with EEV Principles (as defined further under the section "EEV Basis and New Business Results" in Item 3), from business sold in the financial reporting period under consideration.

(15) The net remittance objective for Jackson was increased from £200 million to £260 million to reflect the positive impact of the acquisition of REALIC.

(16)

Representing the underlying remittances excluding the £150 million impact of proactive financing techniques used to bring forward cash emergence of the in-force book during the financial crisis.

(17)

Group free surplus at the end of the period comprises free surplus for the insurance businesses, representing the excess of the net worth over the required capital included in the EEV results, and IFRS net assets for the asset management businesses excluding goodwill. The free surplus generated during the period comprises the movement in this balance excluding foreign exchange, capital movements, and other reserve movements. Specifically, it includes amounts maturing from the in-force operations during the period less the investment in new business, the effect of market movements and other one-off items.

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surplus at 28 February 2013 is estimated at £4.4 billion[18], before allowing for the final dividend, equivalent to a capital cover of 2.5 times.

Uncertainty about the final Solvency II outcome remains. We will continue to evaluate our options, including consideration of the Group's domicile, in the event that the final outcome is negative and potentially impacts our ability to deliver value to our customers and shareholders. We welcome the decision by the UK Financial Services Authority to strengthen the existing Individual Capital Adequacy Standards (ICAS) regime in the absence of the implementation of Solvency II.

Outlook

In 2012, Prudential delivered a strong performance. In spite of tough macroeconomic conditions and the negative effect of persistently low long-term interest rates, the Group has achieved significant and profitable growth and produced increased levels of cash, which allowed the Group to provide their shareholders with a growing dividend.

Prudential's strategy and operating principles remain clear and unchanged. Asia is the key driver of sustainable and profitable growth, building on the significant opportunity that the emergence of the growing and increasingly wealthy middle class in this region represents. The Group's best opportunities lie in South-east Asia, where the depth and breadth of Prudential's franchise is a source of strength. Prudential's business units in the US and in the UK will continue to focus on delivering strong earnings and cash. The Group will achieve this by continuing to execute with discipline, by maintaining a robust balance sheet and with proactive risk management.

Prudential is set to continue to provide a distinctive combination of profitable growth and cash by meeting the needs of their customers across the world. The Group's confidence is reflected in the decision to rebase the dividend upwards, the second time in three years, as they remain focused on creating long-term, sustainable value for their shareholders.

Principal factors affecting Prudential's results of operations

Prudential's results of operations are affected, to a greater or lesser degree, by a variety of factors, including demographics, general economic and market conditions, government policy and regulation and exchange rate fluctuations, as discussed in greater detail below. In addition, changes in interest rates and returns from equity, real estate and other investments as well as volatility in these items may affect Prudential's profitability.

Please refer to "Introduction and Overview", Item 3. "Key Information Risk Factors" and Item 4. "Information on the Company Business of Prudential" for additional discussion of factors that may impact Prudential's results of operations.

General economic and market conditions

Prudential's results of operations are impacted by general economic and market conditions and are sensitive to the pace of and extent of changes in equity markets and interest rates, as well as the changes in behaviour of individuals and institutions that these changes in economic and market

(18) The estimated position at 28 February 2013 allows for economic conditions and surplus generation since 31 December 2012 and is stated before the final dividend and the effect of the Thanachart acquisition and after allowing for a reduction in Jackson's contribution to IGD surplus of £1.3 billion.

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conditions may cause. Particular features of relevance to the Prudential's geographic areas of operations are shown below:

Asia

Asia's rapidly growing middle classes remain a key growth driver for the retail financial services sector, particularly life insurance with an emphasis on protection. Research has shown that as the middle class becomes more established the proportion of income they allocate to financial planning increases from 5 per cent to around 15 per cent . The manifestation of this demand varies significantly across the region, reflecting the various stages of development in each individual market, together with their distinct regulatory and competitive environments, cultural differences and customer preferences. However, across all markets there is increasing recognition among governments and regulators of the social utility of a vibrant private sector life insurance market that provides financial security to families, efficiently channels long-term savings into financial markets and generates employment opportunities within the industry.

During 2012 Asia's average economic growth rates, although they remained well above the global average, continued to moderate following the post crisis high seen in 2010. This is to some degree a consequence of the ongoing weakness of the economies of North America and Europe. While domestic factors were a significant influence in India and China as policymakers grapple with sensitive political situations and economic imbalances, the resilience of many other economies in the region, particularly in South-east Asia, was highlighted by upward revisions to IMF growth forecasts in the second half of the year. Hong Kong's economic growth accelerated during the fourth quarter last year and looks set to have an improved year in 2013 and Singapore has said that the outlook for its economy is cautiously positive as it also had a better than expected fourth quarter. However, the strongest performing regional economies were led by Indonesia, Malaysia, the Philippines and Thailand where growth is increasingly driven by the expansion of domestic demand and is less reliant on exports.

United States

The United States is the world's largest retirement savings market. Each year, many of the 78 million 'baby boomers' reach retirement age, which will trigger a shift from savings accumulation to retirement income generation for more than US$10 trillion of accumulated wealth over the next decade[(19)]. This demographic transition provides a significant opportunity for those companies that are able to provide long-term retirement solutions. Jackson takes a selective approach to this opportunity by leveraging its distribution capabilities and asset liability management expertise to offer prudently priced annuity products.

Despite the ongoing challenges faced by the global economy, US equity markets delivered strong gains in 2012. The S&P 500 index increased by 13.4 per cent over the course of the year and market volatility declined notably from the levels experienced in 2011. Interest rates remained historically low with the 10-year treasury rate ending below 180 bps at year end, while corporate spreads tightened considerably from 2011 year end levels.

The competitive environment continues to favour companies with good financial strength ratings and a track record of financial discipline. Companies that were hardest hit by the market disruptions over the last few years still have to work to regain market share as customers and distributors seek product providers that offer consistency, stability and financial strength. Jackson continues to benefit from this flight to quality and heightened risk aversion.

Jackson's strategy remains focused on driving shareholder value while operating within a conservative risk management framework. This approach has enabled Jackson to successfully navigate

(19) Source: US Census Bureau.

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the significant macroeconomic and financial market challenges of the last five years and ensured a continuation of the strong performance in 2012.

Jackson was predominantly a spread-based business until recently, with the majority of its assets invested in fixed income securities. Recently its fee-based business has become more prominent and now represents a significant part of Jackson's business mix.

Spread-based products written by Jackson are principally for fixed interest rate annuities. Sales of life business, including interest sensitive life products, were discontinued in the second half of 2012. Jackson also writes fixed index annuities and institutional business that are spread-based products. The spread is the difference between the rate of return Jackson is able to earn on the assets backing the contract holder liabilities and the amounts that are credited to contract holders in the form of benefit increases, subject to minimum crediting rates.

In general, Jackson's results are significantly affected by fluctuations in economic and market conditions, especially interest rates, credit conditions and equity markets. The profitability of Jackson's spread-based business depends in large part on its ability to manage interest rate exposure, as well as the credit and other risks inherent in its investment portfolio. Jackson designs its US products and manages the investments and liabilities to reduce overall interest rate sensitivity. This has the effect of moderating the impact on Prudential's results of changes in prevailing interest rates.

Jackson's exposure to interest rate risk relates primarily to the market price and cash flow variability associated with changes in interest rates. Changes in interest rates, either upward or downward, including changes in the difference between the levels of prevailing short-term and long-term rates, can expose Jackson to the risk of not earning anticipated spreads. For example, if interest rates increase and/or competitors offer higher crediting rates, withdrawals on annuity contracts may increase as contract holders seek higher investment returns elsewhere. In response, Jackson could (i) raise its crediting rates to stem withdrawals, decreasing its spread; (ii) sell assets which may have depressed values in a high interest rate environment to fund policyholder payments, creating realised investment losses; or (iii) pay out from existing cash which would otherwise have been invested and earned interest at the higher interest rates.

Conversely, if interest rates decrease, withdrawals from annuity contracts may decrease relative to original expectations, creating more cash than expected to be invested at lower rates. Jackson may have the ability to lower the rates it credits to contract holders as a result, but may be forced to maintain crediting rates for competitive reasons or because there are minimum interest rate guarantees in certain contracts. In either case, the spread earned by Jackson would be compressed.

The majority of assets backing the spread-based business are invested in fixed income securities. Jackson actively manages its investment and derivative portfolio, considering a variety of factors, including the relationship between the expected duration of its assets and its liabilities.

Recent periods have been characterised by low interest rates. The current low interest rate environment is likely to be prolonged. A prolonged low interest rate environment may result in a lengthening of maturities of the contract holder liabilities from initial estimates, primarily due to lower policy lapses. As interest rates remain at low levels, Jackson may also have to reinvest the cash it receives as interest or proceeds from investments that have matured or that have been sold at lower yields, reducing its investment margins. Moreover, borrowers may prepay or redeem the securities in its investment portfolio with greater frequency in order to borrow at lower market rates, which exacerbates this risk.

The majority of Jackson's fixed interest rate annuities and life products were designed with contractual provisions that allow crediting rates to be re-set annually subject to minimum crediting rate guarantees. Therefore, on new business written, as well as on in-force business above minimum guarantees, Jackson has adjusted, and will continue to adjust, crediting rates in order to maintain

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targeted interest rate spreads. Lowering crediting rates helps to mitigate the effect of spread compression but the spreads could still decline as Jackson is typically only entitled to reset the crediting rates at limited pre-established intervals and the re-setting is subject to the guaranteed minimum rates. As at 31 December 2012, approximately 87 per cent of Jackson's fixed interest rate annuities and interest-sensitive life business account values correspond to crediting rates that are at the minimum guaranteed interest rates (2011: 84 per cent). Tabular disclosures are provided in Item 4. 'Information on the Company Business of Prudential US Business Products' and note D3(d) to the consolidated financial statements in Item 18 on the distribution of the account values of these businesses within the range of their contractual minimum guaranteed interest rates. The tables demonstrate that approximately 70 per cent (2011: 78 per cent) of Jackson's combined fixed interest rate annuities and interest sensitive life business account values of £20 billion (US$33 billion (2011: £20 billion (US$31billion)) have contractual minimum rates of 3 per cent or less.

Jackson's expectation for future spreads is also an important component in the amortisation of deferred acquisition costs. Significantly lower spreads may cause it to accelerate amortisation, thereby reducing total IFRS profit in the affected reporting period. Low market interest rates could also reduce Jackson's return on investments that are held to support the company's capital. In addition, changes in interest rates will affect the net unrealised gain or loss position of Jackson's available-for-sale fixed income securities which is reported as a component of other comprehensive income. Further information on the factors affecting the pricing of products and asset liability management of Jackson is provided in Item 4. 'Information on the Company Business of Prudential US Business'.

In addition to the impact on Jackson's spread product profitability, a prolonged period during which interest rates remain at levels lower than those anticipated in its pricing may also result in greater costs associated with certain of Jackson's product features which guarantee benefits and higher costs for derivative instruments used to hedge certain of its product risks. Reflecting these impacts in recoverability and loss recognition testing under U.S. GAAP as 'grandfathered' under IFRS may require Jackson to accelerate the amortisation of DAC as noted above, as well as to increase required reserves for future contract holder benefits. In addition, certain statutory capital and reserve requirements are based on formulas or models that consider interest rates, and a prolonged period of low interest rates may increase the statutory capital Jackson is required to hold as well as the amount of assets it must maintain to support statutory reserves.

Accordingly, without active management, a prolonged low interest rate environment may materially affect Jackson's financial position, results of operations and cash flows. However, Jackson has and continues to proactively adapt its asset-liability management, hedging programme, product design and pricing and crediting rate strategies to mitigate the downward pressures created by the prolonged low interest rate environment.

The sensitivity of Jackson's IFRS basis profit or loss and shareholders' equity to changes in interest rates is provided in note D3(h) to the consolidated financial statements in Item 18.

The profitability of Jackson's fee-based business depends in large part on its ability to manage equity market risk. As the investment return on the separate account assets is attributed directly to the contract holders, Jackson's profit arises from the fees charged on the contracts, less the expenses incurred, which include the costs of guarantees. In addition to being a profitable book of business in its own right, the variable annuity book also provides an opportunity to utilise the offsetting equity risk among various lines of business to manage Jackson's equity exposure in a cost-effective fashion. Jackson believes that the internal management of equity risk coupled with the utilisation of external derivative instruments where necessary, continues to provide a cost-effective method of managing equity exposure. Profits in the variable annuity book of business will continue to be subject to the impact of market movements both on sales and allocations to the variable accounts and the effects of the economic hedging program. While Jackson hedges its risk on an economic basis, the nature and

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duration of the hedging instruments, which are recorded at fair value through the income statement, will fluctuate and produce some accounting volatility.

Jackson continues to believe that, on a long-term economic basis, its equity exposure remains well managed.

United Kingdom

The life and pensions market in the UK is mature and highly regulated. Significant regulatory change occurred in 2012 with the implementation of the conclusions of the Retail Distribution Review (RDR), auto-enrolment for company pension schemes and Gender Neutral Pricing. These new regulations represent major changes to the way business is conducted in a number of areas of the markets in which we operate in the UK, and impact not only insurance and investments providers, but also distributors and consumers. It is inevitable that regulatory change of this scale and scope creates a period of uncertainty before the shape of the new long-term competitive landscape becomes evident.

The UK market is also characterised by an ageing population and a concentration of wealth in the 50+ age group, many of whom have built up substantial pension funds in employer-sponsored schemes. These customers require help to convert their wealth into sustainable lifetime income. For the next generation of savers, the responsibility for retirement provision has shifted substantially away from Government and employers towards the individual. These customers are typically under-funded for retirement and helping them accumulate saving constitutes a significant opportunity for long-term savings and retirement income providers, at a time when the ability of the state to intervene is significantly diminished.

Prudential UK's longevity experience, multi-asset investment capabilities, long-standing trusted brand and financial strength mean that we are favourably positioned to help consumers translate their accumulated wealth into dependable retirement income through our range of market leading with-profits and annuity products.

In the United Kingdom, where Prudential's with-profits fund invests in debt and other fixed income securities, equity securities and real estate, shareholders' profits under IFRS are strongly related to the bonuses it declares. The most important influences on the bonus rates are the overall rate of return earned on investments and Prudential's expectation of future investment returns. Further information on with-profits products is provided in Item 5 'Basis of Profits', ' With-Profits Products' and ' Bonus Rates' below. In addition, shareholders' profits under IFRS are significantly influenced by the contribution from the growing shareholder backed annuity business. The key factors affecting the profitability of this business are described in note D2 to the consolidated financial statements in Item 18.

Government policy and regulation

Changes in government policy or regulation applying to companies in the financial services and insurance industries in any of the jurisdictions in which Prudential operates, particularly in Asia, the United Kingdom and the United States, may adversely affect the result of its operations. These include possible changes in the tax treatment of financial products and services, government pension arrangements and policies, the regulation of selling practices and solvency standards.

These changes may affect Prudential's existing and future business by, for example, causing customers to cancel existing policies, requiring Prudential to change its range of products and services, redesign its technology or other systems, retrain staff, pay increased tax or incur other costs.

In recent years, the insurance sectors in the markets in which Prudential operates have seen considerable regulatory change. In Asia, more generally as the life insurance industry continues to grow, so the regulatory environment continues to evolve. Regulators are encouraging insurers to strengthen their risk and solvency management processes and to improve their sales processes to ensure that

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customers receive good quality advice and buy products suitable to their needs. Most international insurers operating in the region are supportive of these trends and generally aim to operate above current local regulatory standards. The recent recommendations of the Monetary Authority of Singapore's FAIR Panel are indicative of the kind of regulatory efforts under way in the region to improve the overall standard of agency distribution in insurance. In the UK, significant regulatory change occurred in 2012 with the implementation of the conclusions of the Retail Distribution Review (RDR), auto-enrolment for company pension schemes and Gender Neutral Pricing as described above. Further details on the regulatory supervision which Prudential is subject to in the UK and internationally are provided in Item 4 'Information on the Company Supervision and Regulation'.

Exchange rates

Due to the geographical diversity of Prudential's businesses, it is subject to the risk of exchange rate fluctuations. Prudential's international operations in Asia, the United States and Europe, which represent a significant proportion of total group income and expenses, generally write policies and invest in the same local currency, which although limiting the effect of exchange rate fluctuations on local operating results, can lead to fluctuations in Prudential's consolidated financial information upon translation of results into pounds sterling. Please refer to Item 4 'Information on the Company Business of Prudential Group Risk Framework Financial Risks Foreign Exchange Risk' and notes D2, D3 and D4 for additional information on the impact of foreign currency fluctuations on the Group.

IFRS Critical Accounting Policies

Prudential's discussion and analysis of its financial condition and results of operations are based upon Prudential's consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB and as endorsed by the EU. EU-endorsed IFRS may differ from IFRS as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. As at 31 December 2012, there were no unendorsed standards effective for the three years ended 31 December 2012 affecting the consolidated financial information of Prudential and there were no differences between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to Prudential. Accordingly, Prudential's financial information for the three years ended 31 December 2012 is prepared in accordance with IFRS as issued by the IASB. Prudential adopts mandatory requirements of new or altered EU-adopted IFRS standards when required, and may consider earlier adoption where permitted and appropriate in the circumstances.

The preparation of these financial statements requires Prudential to make estimates and judgements that affect the reported amounts of assets, liabilities, and revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, Prudential evaluates its estimates, including those related to long-term business provisioning and the fair value of assets.

Critical accounting policies are defined as those that are reflective of significant judgements and uncertainties, and potentially give rise to different results under different assumptions and conditions. Prudential believes that its critical accounting policies are limited to those described below.

The critical accounting policies in respect of the items discussed below are critical for those that relate to the Group's shareholder-financed business. In particular this applies for Jackson which is the largest shareholder-backed business in the Group. The policies are not critical in respect of the Group's with-profits business. This distinction reflects the basis of recognition of profit and accounting treatment of unallocated surplus of with-profits funds as a liability, as described elsewhere in these financial statements.

In determining the measurement of the Group's assets and liabilities estimates and judgements are required.

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The critical aspects are described below.

Investments

Determining the fair value of financial investments when the markets are not active

The Group holds certain financial investments for which the markets are not active. These can include financial investments which are not quoted on active markets and financial investments for which markets are no longer active as a result of market conditions e.g. market illiquidity. When the markets are not active, there is generally no or limited observable market data to account for financial investments at fair value. The determination of whether an active market exists for a financial investment requires management's judgement.

If the market for a financial investment of the Group is not active, the fair value is determined by using valuation techniques. The Group establishes fair value for these financial investments by using quotations from independent third-parties, such as brokers or pricing services or by using internally developed pricing models. Priority is given to publicly available prices from independent sources when available, but overall the source of pricing and/or the valuation technique is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The valuation techniques include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these financial investments.

The financial investments measured at fair value are classified into the following three level hierarchy on the basis of the lowest level of inputs that is significant to the fair value measurement of the financial investment concerned:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Level 2: Inputs other than quoted prices included within level 1 that are observable either directly or indirectly (i.e. derived from prices).

Level 3: Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At 31 December 2012, £6,660 million (2011: £4,565 million) of the financial investments (net of derivative liabilities) valued at fair value were classified as level 3. Of these £861 million (2011: £800 million) are held to back shareholder non-linked business and so changes to these valuations will directly impact shareholders' equity. Further details of the level 3 investments and the classification of financial instruments are given in note G1 to the consolidated financial statements in Item 18.

Determining impairments relating to financial assets

i Available-for-sale securities

The majority of Jackson's debt securities portfolio are accounted for on available-for-sale basis. The consideration of evidence of impairment requires management's judgement. In making this determination the factors considered include, for example:

Whether the decline of the financial investment's fair value is substantial;

A substantial decline in fair value might be indicative of a credit loss event that would lead to a measurable decrease in the estimated future cash flows;

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The impact of the duration of the security on the calculation of the revised estimated cash flows;

The duration of a security to maturity helps to inform whether assessments of estimated future cash flows that are higher than market value are reasonable;

The duration and extent to which the amortised cost exceeds fair value;
This factor provides an indication of how the contractual cash flows and effective interest rate of a financial asset compares with the implicit market estimate of cash flows and the risk attaching to a 'fair value' measurement. The length of time for which that level of difference has been in place may also provide further evidence as to whether the market assessment implies an impairment loss has arisen; and

The financial condition and prospects of the issuer or other observable conditions that indicate the investment may be impaired.
If a loss event that will have a detrimental effect on cash flows is identified an impairment loss in the income statement is recognised. The loss recognised is determined as the difference between the book cost and the fair value of the relevant impaired securities. This loss comprises the effect of the expected loss of contractual cash flows and any additional market-price-driven temporary reductions in values.

For Jackson's residential mortgage-backed and other asset-backed securities, all of which are classified as available-for-sale, the model used to analyse cash flows, begins with the current delinquency experience of the underlying collateral pool for the structure, by applying assumptions about how much of the currently delinquent loans will eventually default, and multiplying this by an assumed loss severity. Additional factors are applied to anticipate ageing effects. After applying a cash flow simulation an indication is obtained as to whether or not the security has suffered, or is anticipated to suffer, contractual principal or interest payment shortfalls. If a shortfall applies an impairment charge is recorded. The difference between the fair value and book cost for unimpaired securities designated as available-for-sale, is accounted for as unrealised gains or losses, with the movements in the accounting period being included in other comprehensive income.

The Group's review of fair value involves several criteria, including economic conditions, credit loss experience, other issuer-specific developments and future cash flows. These assessments are based on the best available information at the time. Factors such as market liquidity, the widening of bid/ask spreads and a change in cash flow assumptions can contribute to future price volatility. If actual experience differs negatively from the assumptions and other considerations used in the consolidated financial statements, unrealised losses currently in equity may be recognised in the income statement in future periods. Additional details on the impairments of the available-for-sale securities of Jackson are described in notes D3 and G5 to the consolidated financial statements in Item 18.

Impairment losses recognised on available-for-sale securities amounted to £37 million (2011: £62 million; 2010: £124 million). Of this amount, 22 per cent (2011: 34 per cent; 2010: 90 per cent) has been recorded on structured asset-backed securities, primarily due to reduced cash flow expectations on such securities that are collateralised by diversified pools of primarily below investment grade securities. Of the losses related to the impairment of fixed maturity securities, the top five individual corporate issuers made up 74 per cent (2011: 75 per cent; 2010: 32 per cent), reflecting a deteriorating business outlook of the companies concerned. The impairment losses have been recorded in 'investment return' in the income statement.

In 2012, the Group realised gross losses on sales of available-for-sale securities of £44 million (2011: £43 million; 2010: £160 million) with 64 per cent (2011: 64 per cent; 2010: 45 per cent) of these losses related to the disposal of fixed maturity securities of 10 (2011: 10; 2010: 15) individual issuers, which were disposed of as part of risk reduction programmes intended to limit future credit loss

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exposure. Of the £44 million (2011: £ 43 million; 2010: £160 million), £23 million (2011: £32 million; 2010: £99 million) relates to losses on sales of impaired and deteriorating securities.

The effect of those reasonably likely changes in the key assumptions that underpin the assessment of whether impairment has taken place depends on the factors described above. A key indicator of whether such impairment may arise in future, and the potential amounts at risk, is the profile of gross unrealised losses for fixed maturity securities accounted for on an available-for-sale basis by reference to the time periods by which the securities have been held continuously in an unrealised loss position and by reference to the maturity date of the securities concerned.

In 2012, there was a movement in the statement of financial position value for debt securities classified as available-for-sale from a net unrealised gain of £2,057 million to a net unrealised gain of £2,807 million. The gross unrealised gain in the statement of financial position increased from £2,303 million at 31 December 2011 to £2,985 million at 31 December 2012 (31 December 2010: £1,580 million), while the gross unrealised loss decreased from £246 million at 31 December 2011 to £178 million at 31 December 2012 (31 December 2010: £370 million).

Available for sale securities

The following table shows the fair value of those securities that are in a gross unrealised loss position for various percentages of book value at 31 December:

	2012		2011	
	Fair value £m	Unrealised loss £m	Fair value £m	Unrealised loss £m
Between 90% and 100%	**4,214**	**(112)**	1,829	(60)
Between 80% and 90%	**85**	**(13)**	172	(28)
Below 80%*	**74**	**(53)**	208	(158)
Total	**4,373**	**(178)**	2,209	(246)

* The unrealised losses as at 31 December 2012 include £77 million (2011: £183 million) relating to mortgage-backed and other debt securities. The unrealised losses in the portfolio by reference to the length of time 3 years or more as at 31 December 2012 are £36 million (2011: £105 million) in the investment grade and £31 million (2011: £61 million) in non-investment grade.

ii Assets held at amortised cost

Except for certain loans of the UK insurance operations and Jackson National Life, which are accounted for on a fair value through profit and loss basis, and as described below, financial assets classified as loans and receivables under IAS 39 are carried at amortised cost using the effective interest rate method. The loans and receivables include loans collateralised by mortgages, deposits and loans to policyholders. In estimating future cash flows, the Group looks at the expected cash flows of the assets and applies historical loss experience of assets with similar credit risks that has been adjusted for conditions in the historical loss experience which no longer exist or for conditions that are expected to arise. The estimated future cash flows are discounted using the financial asset's original or variable effective interest rate and exclude credit losses that have not yet been incurred.

The risks inherent in reviewing the impairment of any investment include: the risk that market results may differ from expectations, facts and circumstances may change in the future and differ from estimates and assumptions, or the Group may later decide to sell the asset as a result of changed circumstances.

Certain mortgage loans of the UK insurance operations and, consequent upon the purchase of REALIC in 2012, policy loans held to back funds withheld under reinsurance arrangements have been

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designated at fair value through profit and loss as these loan portfolios are managed and evaluated on a fair value basis.

Insurance contracts

Product classification

IFRS 4 requires contracts written by insurers to be classified as either 'insurance contracts' or 'investment contracts' depending on the level of insurance risk transferred. Insurance risk is a pre-existing risk, other than financial risk, transferred from the contract holder to the contract issuer. If significant insurance risk is transferred by the contract then it is classified as an insurance contract. Contracts that transfer financial risk but not significant insurance risk are termed investment contracts. Furthermore, some contracts, both insurance and investment, contain discretionary participating features representing the contractual right to receive additional benefits as a supplement to guaranteed benefits:

a that are likely to be a significant portion of the total contract benefits,

b whose amount or timing is contractually at the discretion of the insurer, and

c that are contractually based on asset or fund performance, as discussed in IFRS 4.

IFRS 4 permits the continued usage of previously applied GAAP for insurance contracts and investment contracts with discretionary participating features. Except for UK regulated with-profits funds, as described subsequently in section A4(b), this basis has been applied by the Group.

For investment contracts that do not contain discretionary participating features, IAS 39 and, where the contract includes an investment management element, IAS 18,'Revenue', apply measurement principles to assets and liabilities attaching to the contract.

Valuation assumptions

i Contracts of with-profits funds

For UK regulated with-profits funds, the contract liabilities are valued by reference to the UK Financial Services Authority's (FSA) realistic basis as described in section A4(b). This basis has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances. An explanation of the basis of liability measurement is contained in note D2(g)(ii) to the consolidated financial statements in Item 18.

The Group's other with-profits contracts are written in with-profits funds that operate in some of the Group's Asia subsidiaries. The liabilities for these contracts and those of Prudential Annuities Limited, which is a subsidiary company of the PAC with-profits fund, are determined differently. For these contracts the liabilities are estimated using actuarial methods based on assumptions relating to premiums, interest rates, investment returns, expenses, mortality and surrenders. The assumptions to which the estimation of these reserves is particularly sensitive are the interest rate used to discount the provision and the assumed future mortality experience of policyholders.

ii Other contracts

Contracts, other than those of with-profits funds, are written by shareholder-backed operations of the Group. The significant shareholder-backed product groupings and the factors that may significantly affect IFRS results due to experience against assumptions or changes of assumptions vary significantly between business units. For some types of business the effect of changes in assumptions may be significant, whilst for others, due to the nature of the product, assumption setting may be of less

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significance. The nature of the products and the significance of assumptions are discussed in notes D2, D3 and D4 in the consolidated financial statements in Item 18.

UK insurance operations

From the perspective of shareholder results the key sensitivity for UK insurance operations are the assumptions for allowance for credit risk and mortality for UK annuity business.

Jackson

With the exception of institutional products and an incidental amount of business for annuity certain contracts, which are accounted for as investment contracts under IAS 39, all of Jackson's contracts are accounted for under IFRS 4 as insurance contracts by applying US GAAP, the previous GAAP used before IFRS adoption. The accounting requirements under these standards and the effect of changes in valuation assumptions are considered below for fixed annuity, variable annuity and traditional life insurance contracts.

Fixed annuity contracts, which are investment contracts under US GAAP terminology, are accounted for by applying in the first instance a retrospective deposit method to determine the liability for policyholder benefits. This is then augmented by potentially three additional amounts, namely deferred income, any amounts previously assessed against policyholders that are refundable on termination of the contract, and any premium deficiency, ie any probable future loss on the contract. These types of contracts contain considerable interest rate guarantee features. Notwithstanding the accompanying market risk exposure, except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of Jackson's fixed annuity products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement.

Variable annuity contracts written by Jackson may provide for guaranteed minimum death, income, or withdrawal benefit features. In general terms, liabilities for these benefits are accounted for under US GAAP by using estimates of future benefits and fees under best estimate assumptions.

For traditional life insurance contracts, provisions for future policy benefits are determined using assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviation.

Except to the extent of mortality experience, which primarily affects profits through variations in claim payments and the guaranteed minimum death benefit reserves, the profits of Jackson are relatively insensitive to changes in insurance risk. This reflects the principally spread and fee-based nature of Jackson's business.

Asia operations

The insurance products written in the Group's Asia operations principally cover with-profits business, unit-linked business, and other non-participating business. The results of with-profits business are relatively insensitive to changes in estimates and assumptions that affect the measurement of policyholder liabilities. As for the UK business, this feature arises because unallocated surplus is accounted for by the Group as a liability. The results of Asia unit-linked business are also relatively insensitive to changes in estimates or assumptions due to the matching of asset value and liability movements. For other Asia non-participating business the degree of sensitivity of results to changes in interest rates depends upon the degree to which the liabilities under the 'grandfathered' IFRS 4 measurement basis reflects market interest rates from period to period for example, for those countries, such as those applying US GAAP, the results can be more sensitive as the effect of interest rate

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movements on the backing investments may not be offset by liability movements due to the US GAAP basis of measurement of insurance contracts.

Deferred acquisition costs for insurance contracts

Except for acquisition costs of with-profits contracts of the UK regulated with-profits funds, which are accounted for under the realistic FSA regime to the consolidated financial statements in Item 18, costs of acquiring new insurance business are accounted for in a way that is consistent with the principles of the ABI SORP with deferral and amortisation against margins in future revenues on the related insurance policies. Costs of acquiring new insurance business, principally commissions, marketing and advertising and certain other costs associated with policy insurance and underwriting that are not reimbursed by policy charges, are specifically identified and capitalised as part of deferred acquisition costs (DAC). In general, this deferral is presentationally shown by an explicit carrying value for DAC in the balance sheet. However, in some Asia operations the deferral is implicit through the reserving methodology. The recoverability of the explicitly and implicitly deferred acquisition costs is measured and are deemed impaired if the projected margins are less than the carrying value. To the extent that the future margins differ from those anticipated, then an adjustment to the carrying value will be necessary.

For UK regulated with-profits funds where the realistic FSA regime is applied, the basis of setting liabilities is such that it would be inappropriate for acquisition costs to be deferred, therefore these costs are expensed as incurred. The majority of the UK shareholder-backed business is individual and group annuity business where the incidence of acquisition costs is negligible.

The deferral and amortisation of acquisition costs is of most relevance to the Group's results for Jackson and Asia operations. The DAC for Jackson and some Asia operations is determined with reference to US GAAP principles.

Jackson

Under IFRS 4, the Group applies grandfathered US GAAP for measuring the insurance assets and liabilities of Jackson. In the case of Jackson term business, acquisition costs are deferred and amortised in line with expected profits. For interest-sensitive business, the key assumption is the long-term spread between the earned rate on investments and the rate credited to policyholders, which is based on an annual spread analysis. In addition, expected gross profits depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges), all of which are based on a combination of Jackson's actual industry experience and future expectations. A detailed analysis of actual mortality, lapse and expenses experience is performed using internally developed experience studies.

For US variable annuity business the key assumption is the investment return from the separate accounts, which for 2012 and 2011 was 8.4 per cent per annum (after deduction of external fund management fees) determined using a mean reversion methodology. Under the mean reversion methodology, projected returns over the next five years are flexed (subject to capping) so that, combined with the actual rates of return for the current and the previous two years the 8.4 per cent rate is maintained. The projected rates of return are capped at no more than 15 per cent for each of the next five years Further details are explained in note D3(g) in the consolidated financial statements in Item 18. These returns affect the level of future expected profits through their effects on the fee income with consequential impact on the amortisation of DAC.

The level of acquisition costs carried in the statement of financial position is also sensitive to unrealised valuation movements on debt securities held to back the liabilities and solvency capital. Further details are explained in notes D3(g) and H1 to the consolidated financial statements in Item 18.

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As explained in note A5 to the consolidated financial statements in Item 18, the Group has adopted the US Financial Accounting Standards Board measurement and recognition requirements in Accounting Standards Update No 2010-26 on 'Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts' from 1 January 2012 into its IFRS reporting for the results of Jackson and those Asia operations whose IFRS insurance assets and liabilities are measured principally by reference to US GAAP principles. Under the Update insurers are required to capitalise only those incremental costs directly relating to acquiring a contract from 1 January 2012. For Group IFRS reporting Prudential has chosen to apply this new basis retrospectively for the results of these operations.

On adoption of the new DAC policy for Jackson the deferred costs balance for business in force at 31 December 2011 was retrospectively reduced from £3,880 million to £3,095 million (31 December 2010: DAC balance reduced from £3,543 million to £2,829 million).

Asia operations

For those territories applying US GAAP to insurance assets and liabilities, as permitted by the ABI SORP, principles similar to those set out in the Jackson paragraph above are applied to the deferral and amortisation of acquisition costs. For other territories in Asia, the general principles of the ABI SORP are applied with, as described above, deferral of acquisition costs being either explicit or implicit through the reserving basis.

Other features of IFRS accounting that are of particular significance to an understanding of Prudential's results

The other features that are of particular significance relate to: the timing of adoption of certain IFRS standards and their consequential impact upon the financial statements; the accounting for UK with-profits funds; and the presentation of certain items in the financial statements.

Insurance contract accounting

With the exception of certain contracts described in note D1 to the consolidated financial statements in Item 18, the contracts issued by the Group's life assurance business are classified as insurance contracts and investment contracts with discretionary participating features. As permitted by IFRS 4, assets and liabilities of these contracts are accounted for under previously applied GAAP. Accordingly, except as described below, the modified statutory basis (MSB) of reporting as set out in the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers (ABI) in 2003 has been applied.

With-profits funds

With-profits funds are those in which the policyholder have a contractual right to receive at the discretion of the insurer, additional benefits based on factors such as the performance of a pool of assets held within the fund as a supplement to any guaranteed benefits.

UK regulated with-profits funds

For Group IFRS reporting, UK regulated with-profits funds are accounted for by the voluntary application of the UK accounting standard FRS 27, 'Life Assurance'. Under this standard, for such funds, policyholder liabilities are measured on a 'realistic basis' as discussed in section 2(a) of this note.

Unallocated surplus of with-profits funds:

Unallocated surplus represents the excess of assets over policyholder liabilities for the Group's with-profits funds that have yet to be appropriated between policyholders and shareholders. The Group

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has elected to account for unallocated surplus wholly as a liability with no allocation to equity. This treatment reflects the fact that shareholders' participation in the cost of bonuses arises only on distribution. The unallocated surplus is shown separately in the statement of financial position.

Overseas operations:

For Jackson, applying the MSB as applicable to overseas operations, which permits the application of local GAAP in some circumstances, the assets and liabilities of insurance contracts are accounted for under insurance accounting prescribed by US GAAP. For the assets and liabilities of insurance contracts of Asian operations, the local GAAP is applied with adjustments, where necessary, to comply with UK GAAP. For the operations in India, Japan, Taiwan and, until 2012, Vietnam, (as discussed in note A5 to the consolidated financial statements in Item 18) the local GAAP is not appropriate in the context of the previously applied MSB. For these countries the insurance assets and liabilities are measured principally by reference to US GAAP. For participating business the liabilities include provisions for the policyholders' interest in investment gains and other surpluses that have yet to be declared as bonuses.

The usage of these bases of accounting has varying effects on the way in which product options and guarantees are measured. For UK regulated with-profits funds, options and guarantees are valued on a market consistent basis. The basis is described in note A3(2) to the consolidated financial statements in Item 18. For other operations a market consistent basis is not applied under the accounting basis described in note A3(2)(a) to the consolidated financial statements in Item 18. Details of the guarantees, basis of setting assumptions, and sensitivity to altered assumptions are described in notes D3 and D4 to the consolidated financial statements in Item 18.

Additional details on the Group's accounting policies for insurance assets and liabilities are shown in note A3(2) to the consolidated financial statements in Item 18.

Valuation and accounting presentation of fair value movements of derivatives and debt securities of Jackson

These policies are critical because of their significance to the volatility of the income statement result and shareholders' equity. Under IAS 39, derivatives are required to be carried at fair value. Unless net investment hedge accounting is applied, value movements on derivatives are recognised in the income statement.

For derivative instruments of Jackson, the Group has considered whether it is appropriate to undertake the necessary operational changes to qualify for hedge accounting so as to achieve matching of value movements in hedging instruments and hedged items in the performance statements. In reaching the decision a number of factors were particularly relevant. These were:

IAS 39 hedging criteria have been designed primarily in the context of hedging and hedging instruments that are assessable as financial instruments that are either stand-alone or separable from host contracts, rather than, for example, duration characteristics of insurance contracts;

the high hurdle levels under IAS 39 of ensuring hedge effectiveness at the level of individual hedge transactions;

the difficulties in applying the macro hedge provisions under IAS 39 (which are more suited to banking arrangements) to Jackson's derivative book;

the complexity of asset and liability matching of US life insurers such as those with Jackson's product range; and finally

whether it is possible or desirable, without an unacceptable level of costs and constraint on commercial activity, to achieve the accounting hedge effectiveness required under IAS 39.

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Taking account of these considerations the Group has decided that, except for occasional circumstances, it is not appropriate to seek to achieve hedge accounting under IAS 39. As a result of this decision the total income statement results are more volatile as the movements in the value of Jackson's derivatives are reflected within it. This volatility is reflected in the level of short-term fluctuations in investment returns, as shown in note B1 to the consolidated financial statements in Item 18.

Under IAS 39, unless carried at amortised cost (subject to impairment provisions where appropriate) under the held-to-maturity category, debt securities are also carried at fair value. The Group has chosen not to classify any financial assets as held-to-maturity. Debt securities of Jackson are designated as available-for-sale with value movements, unless impaired, being recorded as movements within other comprehensive income. Impairments are recorded in the income statement.

Presentation of results before tax

The total tax charge for the Group reflects tax that in addition to relating to shareholders' profits is also attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. This is explained in more detail in note F5 to the consolidated financial statements in Item 18. Reported profit before the total tax charge is not representative of pre-tax profits attributable to shareholders. Accordingly, in order to provide a measure of pre-tax profits attributable to shareholders the Group has chosen to adopt an income statement presentation of the tax charge and pre-tax results that distinguishes between policyholder and shareholder components.

Segmental analysis of results and earnings attributable to shareholders

The Group uses operating profit based on longer-term investment returns as the segmental measure of its results. The basis of calculation is disclosed in the section of this Item 5 'Results of Operations and Financial Condition' entitled 'Analysis of IFRS basis operating profit based on longer-term investment returns and IFRS total profit in note A3(2)(d) to the consolidated financial statements in Item 18.

For shareholder-backed business, with the exception of debt securities held by Jackson and assets classified as loans and receivables at amortised cost, all financial investments and investment property are designated as assets at fair value through profit and loss. The short-term fluctuations affect the result for the year and the Group provides additional analysis of results before and after short-term fluctuations in investment returns, together with other items that are of a short-term volatile or one-off nature. Short-term fluctuations in investment returns on such assets held by with-profits funds, do not affect directly reported shareholder results. This is because (i) the unallocated surplus of with-profits funds is accounted for as a liability and (ii) excess or deficits of income and expenditure of the funds over the required surplus for distribution are transferred to or from unallocated surplus.

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Summary Consolidated Results and Basis of Preparation of Analysis

The following table shows Prudential's consolidated total profit for the years indicated.

	Year Ended 31 December		
	2012	**2011***	**2010***
	£m	**£m**	**£m**
Total revenue, net of reinsurance	**55,476**	36,506	47,646
Total charges, net of reinsurance	**(52,288)**	(34,695)	(45,764)
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)***	**3,188**	1,811	1,882
Tax attributable to policyholders' returns	**(378)**	17	(611)
Profit before tax attributable to shareholders	**2,810**	1,828	1,271
Tax charge	**(991)**	(392)	(571)
Less: tax attributable to policyholders' returns	**378**	(17)	611
Tax charge attributable to shareholders' returns	**(613)**	(409)	40
Profit for the year	**2,197**	1,419	1,311

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

** This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders. This is principally because the corporate taxes of the Group include those on the income of consolidated with-profits and unit-linked funds that, through adjustments to benefits, are borne by policyholders. These amounts are required to be included in the tax charge of the Company under IAS 12. Consequently, the profit before all taxes measure (which is determined after deducting the cost of policyholder benefits and movements in the liability for unallocated surplus of the PAC with-profits fund after adjusting for taxes borne by policyholders) is not representative of pre-tax profits attributable to shareholders. See 'Presentation of results before tax' under IFRS Critical Accounting Policies section above for further explanation.

Under IFRS, the pre-tax GAAP measure of profits is profit before policyholder and shareholder taxes. This measure is not relevant for reflecting pre-tax results attributable to shareholders for two reasons. Firstly, this profit measure represents the aggregate of pre-tax results attributable to shareholders and a pre-tax amount attributable to policyholders. Secondly, the amount is determined after charging the transfer to the liability for unallocated surplus, which in turn is determined in part by policyholder taxes borne by the ring-fenced with-profits funds. It is noted that this circular feature is specific to with-profits funds in the UK, and other similarly structured overseas funds, and should be distinguished from other products, which are referred to as 'with-profits' and the general accounting treatment of premium or other policy taxes.

Accordingly, Prudential has chosen to explain its consolidated results by reference to profits for the year, reflecting profit after tax. In explaining movements in profit for the year, reference is made to trends in profit before shareholder tax and the shareholder tax charge. The explanations of movement in profit before shareholder tax are shown below by reference to the profit analysis applied for segmental disclosure as shown in note B1 of the consolidated financial statements in Item 18. This basis is used by management and reported externally to

Prudential's UK, Hong Kong and Singapore shareholders and to the UK, Hong Kong and Singapore financial markets. Separately, in this section, analysis of movements in profits before shareholder tax is provided by nature of revenue and charges.

Explanation of Movements in Profits After Tax and Profits Before Shareholder Tax by Reference to the Basis Applied for Segmental Disclosure

(a) Group overview

Profit for the year after tax for 2012 was £2,197 million compared to £1,419 million for 2011. The increase of £778 million reflects the movement in total profit before tax attributable to shareholders,

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which improved from a profit of £1,828 million in 2011 to £2,810 million in 2012, partially offset by an increase in tax charge attributable to shareholders from £409 million in 2011 to £613 million in 2012. The improvement in total profit before tax attributable to shareholders reflects the increase in operating profit based on longer-term investment returns and the positive investment market returns earned in the year.

The effective rate of tax at the total profit level was 22 per cent in 2012 which is the same as 2011. In both 2012 and 2011, Prudential has benefited from the favourable impact of certain income in some Asian jurisdictions either not being taxable or being taxable at reduced rates. In addition, Prudential has benefitted from ongoing reductions in the main UK corporate tax rate from 28 per cent in 2010 to 26 per cent in 2011 to 24 per cent in 2012. Further details are provided in note F5 to the consolidated financial statements in Item 18.

The total profit before tax attributable to shareholders was £1,828 million in 2011, compared with £1,271 million in 2010. The improvement reflects the increase in operating profit based on longer-term investment returns, and the fact that in 2010 the profit was reduced by the terminated AIA transaction costs of £377 million.

The effective rate of tax at the total profit level was 22 per cent in 2011, compared to negative 3 per cent in 2010. In 2010 tax charge attributable to shareholders' profit included a credit of £158 million which primarily relates to the impact of a settlement agreed with the UK authorities. Adjusting the rate in 2010 to exclude the exceptional tax credit of £158 million gives an underlying tax rate at the total profit level for 2010 of 9 per cent. In both 2011 and 2010, Prudential has benefited from a reduction in the main UK corporate tax rate from 28 per cent to 26 per cent offset by an increase in the Asia tax rate following the resolution of outstanding issues. Further details are provided in note F5 to the consolidated financial statements in Item 18.

(b) Summary by business segment and geographical region

The Group's operating segments as determined under IFRS 8 are insurance operations split by territories in which the Group conducts business, which are Asia, the United States and the United Kingdom, and asset management operations split into M&G, which is the Group's UK and European asset management business, Eastspring Investments, which is the Asian asset management business and the US broker-dealer and asset management business (including Curian).

The following table shows Prudential's IFRS consolidated total profit/(loss) for the years indicated presented by summary business segment and geographic region. The accounting policies applied to the segments below are the same as those used in the Group's consolidated accounts.

	Year ended 31 December 2012				
	Asia	US	UK	Unallocated corporate	Total
	£m	£m	£m	£m	£m
Insurance operations	**831**	**621**	**697**		**2,149**
Asset management**	**58**	**18**	**411**		**487**
Total profit attributable to the segments	**889**	**639**	**1,108**		**2,636**
Unallocated corporate				**(439)**	**(439)**
Total profit (loss) for the year	**889**	**639**	**1,108**	**(439)**	**2,197**

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	Year ended 31 December 2011*				
	Asia	US	UK	Unallocated corporate	Total
	£m	£m	£m	£m	£m
Insurance operations	488	357	671		1,516
Asset management**	62	16	235		313
Total profit attributable to the segments	550	373	906		1,829
Unallocated corporate				(410)	(410)
Total profit (loss) for the year	550	373	906	(410)	1,419

	Year ended 31 December 2010*				
	Asia	US	UK	Unallocated corporate	Total
	£m	£m	£m	£m	£m
Insurance operations	572	221	646		1,439
Asset management**	57	13	237		307
Total profit attributable to the segments	629	234	883		1,746
Unallocated corporate***				(435)	(435)
Total profit (loss) for the year	629	234	883	(435)	1,311

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

**

For the US, including the broker dealer business and Curian.

***

The results for the unallocated corporate for the year ended 31 December 2010 included the impact of the costs of the terminated AIA transaction.

Profit from insurance operations

Total profit from insurance operations in 2012 was £2,149 million compared to £1,516 million in 2011 and £1,439 million in 2010. All of the profits from insurance operations in 2012, 2011 and 2010 were from continuing operations. The movement in profits for insurance operations can be summarised as follows:

	Year Ended 31 December		
	2012	**2011***	**2010***
	£m	**£m**	**£m**
Profit before shareholder tax	**2,702**	1,996	1,771
Shareholder tax	**(553)**	(480)	(332)
Profit after tax	**2,149**	1,516	1,439

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

The increase of £706 million in profit before tax attributable to shareholders in 2012 compared to 2011 reflects an increase in operating profits based on longer term investment returns combined with the favourable change in the short-term fluctuations in investment returns for the insurance operations.

The effective shareholder tax rate on profits from insurance operations decreased from 24 per cent in 2011 to 20 per cent in 2012. The decrease primarily relates to an increase in income that is non-taxable or taxable at concessionary rates in Asia, routine revisions to prior period tax returns and

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the reduction in tax rate in the UK, partially offset by adverse revisions to prior period tax returns in the US.

The increase of £225 million in profit before tax attributable to shareholders in 2011 compared to 2010 reflects an increase in operating profits based on longer term investment returns combined with a reduction in the overall negative short-term fluctuations in investment returns for the insurance operations.

The effective shareholder tax rate on profits from insurance operations increased from 19 per cent in 2010 to 24 per cent in 2011. The increase primarily relates to increased profits in the US and the recent fiscal developments in Indonesia affecting the life assurance industry offset by the reduction in the UK tax rate.

In order to understand how Prudential's results are derived it is necessary to understand how profit emerges from its business. This varies from region to region, primarily due to differences in the nature of the products and regulatory environments in which Prudential operates.

Asia

Basis of profits

The assets and liabilities of contracts classified as insurance under IFRS 4 are determined in accordance with methods prescribed by local GAAP and adjusted to comply, where necessary, with UK GAAP. Under IFRS 4, subject to the conditions of that standard, the continued application of UK GAAP in this respect is permitted.

For Asia operations in countries where local GAAP is not well established and in which the business is primarily non-participating and linked business, the measurement of the insurance assets and liabilities is determined substantially by reference to US GAAP principles. This basis is applied in India, Japan, Taiwan and until 2012 Vietnam. For with-profits business in Hong Kong, Singapore and Malaysia, the basis of profit recognition is bonus driven as described under 'United Kingdom Basis of Profits' below.

Comparison of total profit arising from Asia insurance operations

The following table shows the movement in profit arising from Asia insurance operations for 2012, 2011 and 2010:

	Year Ended 31 December		
	2012	**2011***	**2010**
	£m	**£m**	**£m**
Profit before shareholder tax	**989**	612	636
Shareholder tax	**(158)**	(124)	(64)
Profit after tax	**831**	488	572

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

The 2012 profit before tax attributable to shareholders of £989 million represented an increase of £377 million over 2011 of £612 million. This primarily reflects an increase of £209 million in operating profit based on longer-term investment returns, combined with an improvement in the short-term fluctuations in investment returns for shareholder-backed business of £168 million.

The effective shareholder tax rate changed from 20 per cent in 2011 to 16 per cent in 2012, with the movement principally due to an increase in income that is non-taxable or taxable at concessionary rates.

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The 2011 profit before tax attributable to shareholders of £612 million represented a decrease of £24 million as against the comparable 2010 figure of £636 million which primarily reflects an increase of £182 million in operating profit based on longer-term investment returns offset by an adverse change of £206 million in short-term fluctuations in investment returns for shareholder-backed business.

The effective shareholder tax rate changed from 10 per cent in 2010 to 20 per cent in 2011, with the movement principally due to the recent fiscal developments in Indonesia affecting the life assurance industry.

United States

Basis of profits

The underlying profit on Jackson's business predominantly arises from spread income from interest-sensitive products, such as fixed annuities and institutional products and fee income on variable annuity business with the insurance assets and liabilities of the business measured on a US GAAP basis. In addition, the results in any period include the incidence of gains and losses on assets classified as available-for-sale, and fair value movements on derivatives and securities classified as fair valued through profit and loss.

Comparison of total profit arising from US insurance operations

The following table shows the movement in profit arising from US insurance operations for 2012, 2011 and 2010:

	Year Ended 31 December		
	2012	**2011***	**2010**
	£m	**£m**	**£m**
Profit before shareholder tax	**855**	484	275
Shareholder tax	**(234)**	(127)	(54)
Profit after tax	**621**	357	221

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

The increase in profit before shareholder tax of £371 million in 2012 compared to 2011 was due primarily to an increase of £313 million in operating profit based on longer-term investment returns, combined with a favourable change in the short-term fluctuations in investment returns for shareholder backed business. The profit before shareholder tax in 2012 includes a £61 million contribution from REALIC which was acquired in September 2012, of which the operating profit based on longer-term investment returns was £67 million. Excluding this contribution from REALIC, the remaining year on year increase of £246 million in operating profit based on longer-term investment returns primarily reflects higher fee income generated by growth in the separate account assets, as well as the expected non-recurring impact of accelerated deferred acquisition cost (DAC) amortisation of £190 million in 2011. This has been partially offset by the adverse effect on spread income of lower bond yields.

The effective tax rate on profit from the US insurance operations changed from 26 per cent in 2011 to 27 per cent in 2012 due to adverse revisions to prior period tax returns.

The increase in profit before tax attributable to shareholders of £209 million in 2011 compared to 2010 reflected a decrease of £77 million in operating profit based on longer-term investment returns which was more than offset by a favourable change of £286 million in short-term fluctuations in investment returns reflected in the income statement. The decrease in the operating profit based on longer-term investment returns was due to the accounting impact of accelerated amortization of deferred acquisition costs (DAC) of £190 million in the year. Excluding the impact of accelerated DAC amortisation, the US insurance operations' earnings continued to grow during 2011. The favourable

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change of £286 million in the short-term fluctuations in investment returns was primarily due to lower negative fluctuations from the US operations' derivative hedging programmes in 2011 compared to 2010.

The effective tax rate on profit from the US insurance operations changed from 20 per cent in 2010 to 26 per cent in 2011. The 2010 effective tax rate is comparatively low as there is a larger proportion of non-taxable income.

United Kingdom

Basis of profits

Prudential's results comprise an annual profit distribution to shareholders from its UK long-term with-profits fund, hereafter referred to as the with-profits fund, as well as profits from its other businesses. For most of Prudential's operations, other than its UK long-term insurance businesses, the IFRS basis of accounting matches items of income and related expenditure within the same accounting period. This is achieved through the deferral of acquisition costs and application of the accruals concept.

With-profits products

For Prudential's UK insurance operations, the primary annual contribution to shareholders' profit comes from its with-profits products. With-profits products are designed to provide policyholders with smoothed investment returns through a mix of regular and final bonuses.

Shareholders' profit in respect of bonuses from with-profits products represents an amount of up to one-ninth of the value of that year's bonus declaration to policyholders. The Board of directors of the subsidiary companies that have with-profits operations, using actuarial advice, determine the amount of regular and final bonuses to be declared each year on each group of contracts. The smoothing inherent in the bonus declarations provides for relatively stable annual shareholders' profit from this business.

Bonus rates

Bonus rates are applied to with-profits policies in the UK and similar products in Singapore, Hong Kong and Malaysia. The most significant with-profits fund is in the UK where, as at 31 December 2012, liabilities to with-profits policyholders were in aggregate of £71 billion. Liabilities to with-profits policyholders in Asia as at 31 December 2012 were £13.4 billion. The details that follow are in respect of the UK with-profits business. The method by which bonuses for Prudential's Asia with-profits business are determined is substantially similar to the method by which bonuses for Prudential's UK with-profits business are determined.

The main factors that influence the determination of bonus rates are the return on the investments of the with-profits fund, the effect of inflation, taxation, the expenses of the fund chargeable to policyholders and the degree to which investment returns are smoothed. The overall rate of return earned on investments and the expectation of future investment returns are the most important influences on bonus rates. A high proportion of the assets backing the with-profits business are invested in equities and real estate. If the financial strength of the with-profits fund were adversely affected, then a higher proportion of fixed interest or similar assets might be held by the fund.

Further details on the determination of the two types of bonus ('regular' and 'final'), the application of significant judgment, key assumptions and the degree of smoothing of investment returns in determining the bonus rates are provided below.

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Regular bonus rates

For regular bonuses, the bonus rates are determined for each type of policy primarily by targeting the bonus level at a prudent proportion of the long-term expected future investment return on underlying assets. The expected future investment return is reduced as appropriate for each type of policy to allow for items such as expenses, charges, tax and shareholders' transfers. However, the rates declared may differ by product type, or by the date of payment of the premium, or date of issue of the policy, or if the accumulated annual bonuses are particularly high or low, relative to a prudent proportion of the achieved investment return.

When target bonus levels change the PAC board of directors (PAC Board) has regard to the overall strength of the long-term fund when determining the length of time over which it will seek to achieve the amended prudent target bonus level.

In normal investment conditions, PAC expects changes in regular bonus rates to be gradual over time. However, the PAC Directors retain the discretion whether or not to declare a regular bonus each year, and there is no limit on the amount by which regular bonus rates can change.

Final bonus rates

A final bonus which is normally declared yearly, may be added when a claim is paid or when units of a unitised product are realised.

The rates of final bonus usually vary by type of policy and by reference to the period, usually a year, in which the policy commences or each premium is paid. These rates are determined by reference to the asset shares for the sample policies but subject to the smoothing approach as explained below.

In general, the same final bonus scale applies to maturity, death and surrender claims except that:

- The total surrender value may be impacted by the application of a Market Value Reduction for accumulating with-profits policies and is the surrender bases for conventional with-profits business; and

- For the SAIF and Scottish Amicable, the final bonus rates applicable on surrender may be adjusted to reflect expected future bonus rates.

Application of significant judgement

The application of the above method for determining bonuses requires the PAC Board to apply significant judgement in many respects, including in particular the following:

- Determining what constitutes fair treatment of customers: Prudential is required by UK law and regulation to consider the fair treatment of its customers in setting bonus levels. The concept of determining what constitutes fair treatment, while established by statute, is not defined;

- Smoothing of investment returns: This is an important feature of with-profits products. Determining when particular circumstances, such as a significant rise or fall in market values, warrant variations in the standard bonus smoothing limits that apply in normal circumstances requires the PAC Board to exercise significant judgement; and

- Determining at what level to set bonuses to ensure that they are competitive: The overall return to policyholders is an important competitive measure for attracting new business.

Key assumptions

As noted above, the overall rate of return on investments and the expectation of future investment returns are the most important influences in bonus rates, subject to the smoothing described below. Prudential determines the assumptions to apply in respect of these factors, including the effects of

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reasonably likely changes in key assumptions, in the context of the overarching discretionary and smoothing framework that applies to its with-profits business as described above. As such, it is not possible to specifically quantify the effects of each of these assumptions, or of reasonably likely changes in these assumptions.

Prudential's approach, in applying significant judgement and discretion in relation to determining bonus rates, is consistent conceptually with the approach adopted by other firms that manage a with-profits business. It is also consistent with the requirements of UK law, which require all UK firms that carry out a with-profits business to define, and make publicly available, the Principles and Practices of Financial Management (PPFM) that are applied in the management of their with-profits funds.

Accordingly, Prudential's PPFM contains an explanation of how it determines regular and final bonus rates within the discretionary framework that applies to all with-profits policies, subject to the general legislative requirements applicable. The purpose of Prudential's PPFM is therefore to:

- explain the nature and extent of the discretion available,
- show how competing or conflicting interests or expectations of different groups and generations of policyholders, and policyholders and shareholders are managed so that all policyholders and shareholders are treated fairly, and
- provide a knowledgeable observer (eg a financial adviser) with an understanding of the material risks and rewards from starting and continuing to invest in a with-profits policy with Prudential.

Furthermore, in accordance with industry-wide regulatory requirements, the PAC Board has appointed:

- an Actuarial Function Holder who provides the PAC Board with all actuarial advice;
- a With-Profits Actuary whose specific duty is to advise the PAC Board on the reasonableness and proportionality of the manner in which its discretion has been exercised in applying the PPFM and the manner in which any conflicting interests have been addressed; and
- a With-Profits Committee of independent individuals, which assesses the degree of compliance with the PPFM and the manner in which conflicting rights have been addressed.

Smoothing of investment return

In determining bonus rates for the UK with-profits policies, smoothing is applied to the allocation of the overall earnings of the UK with-profits fund of which the investment return is a significant element. The smoothing approach differs between accumulating and conventional with-profits policies to reflect the different contract features. In normal circumstances, Prudential does not expect most payout values on policies of the same duration to change by more than 10 per cent up or down from one year to the next, although some larger changes may occur to balance payout values between different policies. Greater flexibility may be required in certain circumstances, for example following a significant rise or fall in market values, and in such situations the PAC Board may decide to vary the standard bonus smoothing limits in order to protect the overall interests of policyholders.

The degree of smoothing is illustrated numerically by comparing in the following table the relatively 'smoothed' level of policyholder bonuses declared as part of the surplus for distribution, with the more

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volatile movement in investment return and other items of income and expenditure of the UK component of the PAC with-profits fund for each year presented.

	2012	2011	2010
	£m	£m	£m
Net income of the fund:			
Investment return	**8,350**	4,094	8,815
Claims incurred	**(6,857)**	(6,411)	(6,390)
Movement in policyholder liabilities	**(3,989)**	(614)	(4,301)
Add back policyholder bonuses for the year (as shown below)	**1,865**	1,945	2,019
Claims incurred and movement in policyholder liabilities (including charge for provision for asset shares and excluding policyholder bonuses)	**(8,981)**	(5,080)	(8,672)
Earned premiums, net of reinsurance	**4,558**	3,404	3,148
Other income	**39**	17	9
Acquisition costs and other expenditure	**(740)**	(696)	(600)
Tax charge	**(292)**	(63)	(528)
Net income of the fund before movement in unallocated surplus	**2,934**	1,676	2,172
Movement in unallocated surplus	**(863)**	485	70
Surplus for distribution	**2,071**	2,161	2,242
Surplus for distribution allocated as follows:			
90% policyholders' bonus (as shown above)	**1,865**	1,945	2,019
10% shareholders' transfers	**206**	216	223
	2,071	2,161	2,242

Unallocated surplus

The unallocated surplus represents the excess of assets over policyholder liabilities for the Group's with-profits funds. As allowed under IFRS 4, the Group has opted to continue to record unallocated surplus of with-profits funds wholly as a liability. The annual excess (shortfall) of income over expenditure of the with-profits funds, after declaration and attribution of the cost of bonuses to policyholders and shareholders, is transferred to (from) the unallocated surplus each year through a charge (credit) to the income statement. The balance retained in the unallocated surplus represents cumulative income arising on the with-profits business that has not been allocated to policyholders or shareholders. The balance of the unallocated surplus is determined after full provision for deferred tax on unrealised appreciation on investments.

Changes to the level of the unallocated surplus do not directly impact shareholders' results or funds. After allowing for differences in the basis of preparation of the financial information and UK regulatory returns, movements in the level of the unallocated surplus are broadly indicative of movements in the excess of regulatory basis assets over liabilities of the fund. Differences in the basis of preparation of financial statements and UK regulatory returns arise principally from the treatment of certain regulatory basis liabilities, such as mismatching reserves (that are accounted for as reserves within the unallocated surplus), and asset valuation differences and admissibility deductions reflected in the regulatory returns. Except to the extent of any second order effects on other elements of the regulatory returns, such changes can be expected to have a consequent effect on the excess of assets over liabilities of the fund for the purposes of solvency calculations, and the related free asset ratio which is an indicator of the overall financial strength of the fund. Similar principles apply to Prudential's Asian with-profits business.

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Surplus assets and their use

The liability for unallocated surplus comprises amounts Prudential expects to pay to policyholders in the future, the related shareholder transfers and surplus assets. These surplus assets have accumulated over many years from a variety of sources and provide the with-profits fund with working capital. This working capital permits Prudential to invest a substantial portion of the assets of the with-profits fund in equity securities and real estate, smooth investment returns to with-profits policyholders, keep its products competitive, write new business without being constrained as to cash flows in the early policy years and demonstrate solvency.

In addition, Prudential can use surplus assets to absorb the costs of significant events, such as fundamental strategic change in its long-term business and, with the consent of the UK regulator, the cost of its historical pensions mis-selling, without affecting the level of distributions to policyholders and shareholders. The costs of fundamental strategic change may include investment in new technology, redundancy and restructuring costs, cost overruns on new business and the funding of other appropriate long-term insurance related activities, including acquisitions.

The 'SAIF' and 'PAL' funds

Prudential's with-profits fund also includes the SAIF and the wholly-owned subsidiary, PAL. All assets of the SAIF business are solely attributable to former policyholders of Scottish Amicable Life Assurance Society (predating the acquisition of Scottish Amicable by Prudential in October 1997). Since PAL is a wholly-owned subsidiary of the with-profits fund, profits from this business affect shareholders' profits only to the extent that they affect the annual with-profits bonus declaration and resultant transfer to shareholders.

Accounting for with-profits business

For with-profits business (including non-participating business of Prudential Annuities Limited which is owned by the PAC with-profits fund), adjustments to liabilities and any related tax effects are recognised in the income statement. However, except for any impact on the annual declaration of bonuses, shareholder profit for with-profits business is unaffected. This is because IFRS basis profits for the with-profits business, which are determined on the same basis as on preceding UK GAAP, solely reflect one-ninth of the cost of bonuses declared for the year.

Fair value of assets

Changes in the fair value of assets of Prudential's long-term with-profits funds will primarily be reflected in the excess of assets over liabilities recorded as the unallocated surplus. Shareholders' profits from with-profits business and shareholders' funds are not directly impacted by movements in the fair values of the assets. However, current investment performance is a factor that is taken into account in the setting of the annual declaration of bonuses which, in turn, affects UK shareholder profits to the extent of one-ninth of the cost of bonus.

Investment returns

For with-profits business, investment returns together with other income and expenditure are recorded within the income statement. However, the difference between net income of the fund and the cost of bonuses and related statutory transfers is reflected in an amount transferred to, or from, the unallocated surplus within the income statement. Except to the extent of current investment returns being taken into account in the setting of a bonus policy, the investment returns of a with-profits fund in a particular year do not affect shareholder profits or with-profits funds.

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UK shareholder-backed annuity business

The results for this type of business are prepared in accordance with the UK Modified Statutory Basis. The results reflect the inclusion of investment return including realised and unrealised gains. The charge for benefits reflects the valuation rate of interest applied to discount future anticipated payments to policyholders. This rate in turn reflects current market yields adjusted for factors including default risks on the assets backing the liabilities. The level of allowance for default risk is a key assumption. Details are included in note D2 of the consolidated financial statements in Item 18.

Comparison of total profit arising from UK insurance operations

The following table shows the movement in profit arising from UK insurance operations for 2012, 2011 and 2010:

	Year Ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Profit before shareholder tax	**858**	900	860
Shareholder tax	**(161)**	(229)	(214)
Profit after tax	**697**	671	646

Profit after tax from UK insurance operations of £697 million in 2012 is £26 million higher than the £671 million in 2011.

The decrease in profit before tax attributable to shareholders of £42 million to £858 million in 2012 was primarily due to an adverse change in the value of short-term fluctuations in investment returns of the shareholder-backed business of £23 million which reflects asset value movements principally on the shareholder-backed annuity business and a decrease of £32 million in the actuarial and other gains on defined benefit pension schemes from a gain of £18 million in 2011 to a loss of £14 million in 2012. These decreases were partially offset by an increase in operating profit based on longer-term investments returns of £13 million in 2012. Operating profit based on longer-term investment returns of £736 million included general insurance commissions which decreased by £7 million to £33 million in 2012 compared with £40 million for 2011.

The effective shareholder tax rate on profits from UK insurance operations for 2012 of 19 per cent compares with an effective tax rate of 25 per cent in 2011, with the movement principally due to routine revisions to prior period tax returns and the reduction in the UK rate of tax.

The increase in profit before tax attributable to shareholders of £40 million from £860 million in 2010 to £900 million in 2011 reflected an increase of £4 million in operating profit based on longer-term investment returns, a favourable change of £43 million in the value of short-term fluctuations in investment returns of the shareholder-backed business and a favourable change of £23 million in the shareholders' share of actuarial gains/losses in defined benefit pension schemes. These increases were partially offset by a non-recurring £30 million gain recorded in 2010 upon the dilution of the UK insurance operations' holding in PruHealth, as described further below under section (c) "Explanation of Movements in Profits After Tax and Profits Before Shareholder Tax by Reference to the Basis Applied for Segmental Disclosure".

The effective shareholder tax rate on profits from UK insurance operations for 2011 of 25 per cent is consistent with an effective tax rate of 25 per cent in 2010. The rate in 2011 remained the same as 2010 primarily due to adverse routine reversions to prior period tax returns being offset by the reduction in the UK tax rate.

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Profit from asset management

The following table shows the movement in profits from asset management for 2012, 2011 and 2010:

	Year Ended 31 December		
	2012	2011	2010
	£m	£m	£m
Profit before shareholder tax	**635**	436	420
Shareholder tax	**(148)**	(123)	(113)
Profit after tax	**487**	313	307

Total profit from asset management increased from £313 million in 2011 to £487 million in 2012. The £199 million increase in profit before tax attributable to shareholders resulted mainly from an increase in profit generated by M&G, which increased profit before tax of £332 million in 2011 to £521 million in 2012. The profit before tax attributable to shareholders for Eastspring Investments reduced by £5 million from £80 million in 2011 to £75 million in 2012. Profits generated by the US broker dealer and asset management operations increased by £15 million from £24 million in 2011 to £39 million in 2012.

The £189 million increase in profit before tax attributable to M&G was the result of a favourable change in short term fluctuations in investment returns of £122 million compared with 2011, an increase in operating profit based on longer-term investment returns of £14 million, an improvement in the actuarial gains on defined benefit schemes of £11 million and a one-off gain of £42 million arising on the dilution of M&G's investment holding in PPM South Africa. Further detail on the change in investment holdings in PPM South Africa is given in note I2 to the consolidated financial statements in Item 18.

The effective tax rate on profits from asset management operations changed from 28 per cent in 2011 to 23 per cent in 2012 principally due to the gain arising on the dilution of M&G's investment holding in PPM South Africa being non taxable.

Profit before tax attributable to shareholders from asset management increased from £420 million in 2010 to £436 million in 2011. The £16 million increase in profit before tax attributable to shareholders from 2010 to 2011 reflects improvements experienced across M&G of £6 million, Eastspring Investments of £8 million and the US broker-dealer and asset management operations of £2 million.

The £6 million increase in profit before tax attributable to M&G reflected an increase of £73 million in operating profit based on longer-term investment returns from £284 million in 2010 to £357 million in 2011, which was due to rising revenues and a fall in the cost-income ratio. Further, the increase also reflected a favourable change in actuarial gains/losses on defined benefit pension scheme of £9 million. These increases were partially offset by a negative year on year change in the short-term fluctuations of £76 million.

The effective tax rate on profits from asset management operations increased slightly from 27 per cent in 2010 to 28 per cent in 2011.

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Unallocated corporate result

The following table shows the movement in the unallocated corporate result for 2012, 2011 and 2010.

	Year Ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Loss before shareholder tax	**(527)**	(604)	(920)
Shareholder tax	**88**	194	485
Loss after tax	**(439)**	(410)	(435)

Total net charges for unallocated corporate activity increased by £29 million from £410 million in 2011 to £439 million in 2012 and reduced by £25 million from £435 million in 2010 to £410 million in 2011.

The loss before shareholder tax reduced by £77 million from £604 million at 2011 to £527 million at 2012. Net other expenditure (including restructuring and Solvency II implementation costs) increased by £53 million from a charge of £512 million in 2011 to a charge of £565 million in 2012. This was more than offset by a favourable change of £80 million in short-term fluctuations in investment returns from £91 million loss in 2011 to £11 million loss in 2012 and a favourable change in actuarial and other gains on defined benefit pension schemes of £50 million, from a loss of £1 million in 2011 to a gain of £49 million in 2012. The gain of £49 million on defined benefit pension schemes in 2012 reflected the partial recognition of actuarial surplus of PSPS following the results of its triennial valuation.

The 2011 net other expenditure included a credit of £42 million resulting from the Prudential's alteration of its inflation measure basis for future statutory increases to pension payments for certain tranches of Prudential's UK defined benefit schemes. This reflected the UK Government's decision to replace the RPI basis of indexation with the CPI.

The effective tax rate on unallocated corporate result (being a tax credit on a loss) changed from 32 per cent in 2011 to 17 per cent in 2012, principally due to an increase in provisions for open tax matters and by the reduction in the UK rate of tax.

The loss before shareholder tax in 2010 of £920 million included costs of £377 million incurred in relation to the terminated transaction to purchase AIA Group Limited. Further details of these costs are presented in note B1 of consolidated financial statements in Item 18 of this annual report. Excluding these termination costs, the loss before shareholder tax increased by £61 million from 2010 to 2011. The year-on-year movement resulted from a favourable movement of £9 million in other income and expenditure (including restructuring and Solvency II implementation costs) from £521 million in 2010 to £512 million in 2011 which was more than offset by a negative change in short-term fluctuations in investment returns of £69 million and small negative change of £1 million in the actuarial gains and losses of Prudential's defined benefit pension scheme.

The favourable movement of £9 million in net other expenditure includes a credit of £42 million resulting from Prudential's alteration of its inflation measure basis for future statutory increases to pension payments for certain tranches of Prudential's UK defined benefit schemes. This reflects the UK Government's decision to replace the Retail Prices Index (RPI) basis of indexation with the Consumer Prices Index (CPI).

The effective tax rate on unallocated corporate result (being a tax credit on a loss) decreased from 53 per cent in 2010 to 32 per cent in 2011. This was primarily due to 2010 containing both an exceptional UK tax credit primarily relating to the impact of the settlement agreed with the UK tax authorities and the ability to recognise a deferred tax credit on various tax losses which Prudential was previously unable to recognise.

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(c) Additional explanation of performance measures and analysis of consolidated results by business segment and geographical region

Prudential uses a performance measure of operating profit based on longer-term investment returns. The directors believe that this performance measure better reflects underlying performance. It is the basis used by management for the reasons outlined below. It is also the basis on which analysis of the Group's results has been provided to UK shareholders and the UK financial market for some years under long standing conventions for reporting by proprietary UK life assurers.

Prudential determines and presents operating segments based on the information that is internally provided to the Group Executive Committee ('GEC'), which is Prudential's chief operating decision maker.

An operating segment is a component of Prudential that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of Prudential's other components. An operating segment's operating results are reviewed regularly by the GEC to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

The operating segments identified by Prudential reflect its organisational structure, which is by both geography (Asia, US and UK) and by product line (insurance operations and asset management).

The Group's operating segments determined in accordance with IFRS 8, 'Operating Segments', are as follows:

Insurance operations

- Asia
- US (Jackson)
- UK

Asset management operations

- M&G (including Prudential Capital)
- Eastspring Investments
- US broker-dealer and asset management (including Curian)

The Group's operating segments are also its reportable segments with the exception of Prudential Capital (PruCap) which has been incorporated into the M&G operating segment for the purposes of segment reporting.

The performance measure of operating segments utilised by the Company is IFRS operating profit attributable to shareholders based on longer-term investment returns, as described below. This measure excludes the recurrent items of short-term fluctuations in investment returns and the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes. In addition for 2012 this measure excluded a gain arising upon the dilution of the Group's holding in PPM South Africa and the amortisation of the acquisition accounting adjustments arising on the purchase of REALIC as described further in note I1 to the Prudential's consolidated financial statements in Item 18. Further for 2010, this measure excluded costs associated with terminated AIA transaction and gain arising upon the dilution of the Group's holding in PruHealth. Operating earnings per share is based on operating profit based on longer-term investment returns, after tax and non-controlling interests. Further details on the determination of the performance measure of operating profit based on longer-term investment returns is provided below and in note A3(d) to the consolidated financial statements in Item 18.

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Segment results that are reported to the Group Executive Committee include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items are mainly in relation to the Group Head Office and the Asia Regional Head Office.

Except in the case of the assets backing the UK annuity business, unit-linked and US variable annuity separate account liabilities, operating profit based on longer-term investment returns for shareholder-financed business is determined on the basis of expected longer-term investment returns. In the case of assets backing the UK annuity business, unit-linked and US variable annuity separate account liabilities, the basis of determining operating profit based on longer-term investment returns is as follows:

Assets backing UK annuity business liabilities. For UK annuity business, policyholder liabilities are determined by reference to current interest rates. The value movements of the assets covering liabilities are closely correlated with the related change in liabilities. Accordingly, asset value movements are recorded within the 'operating results based on longer-term investment returns'. Policyholder liabilities include a margin for credit risk. Variations between actual and best estimate expected impairments are recorded as a component of short-term fluctuations in investment returns.

Assets backing unit-linked and US variable annuity business separate account liabilities. For such business, the policyholder unit liabilities are directly reflective of the asset value movements. Accordingly, the operating results based on longer-term investment returns reflect the current period value movements in unit liabilities and the backing assets.

In the case of other shareholder-financed business, the measurement of operating profit based on longer-term investment returns reflects the particular features of long-term insurance business where assets and liabilities are held for the long-term and for which the accounting basis for insurance liabilities under current IFRS is not generally conducive to demonstrating trends in underlying performance of life businesses exclusive of the effects of short-term fluctuations in market conditions. In determining the profit on this basis, the following key elements are applied to the results of the Group's shareholder-financed operations as reflected in the segment results shown in note B1.

i Debt, equity-type securities and loans

Longer-term investment returns for both debt, equity-type securities and loans comprise longer-term actual income receivable for the period (interest/dividend income) and longer-term capital returns.

In principle, for debt securities and loans, the longer-term capital returns comprise two elements. The first element is a risk margin reserve (RMR) based charge for the expected level of defaults for the period, which is determined by reference to the credit quality of the portfolio. The difference between impairment losses in the reporting period and the RMR charge to the operating result is reflected in short-term fluctuations in investment returns. The second element is for the amortisation of interest-related realised gains and losses to operating results based on longer-term investment returns to the date when sold bonds would have otherwise matured.

Jackson is the shareholder-backed operation for which the distinction between impairment losses and interest-related realised gains and losses is in practice relevant to a significant extent. Jackson has used the ratings by Nationally Recognised Statistical Ratings Organisations (NRSRO) or ratings resulting from the regulatory ratings detail issued by the National Association of Insurance Commissioners (NAIC) developed by external third parties such as PIMCO or BlackRock Solutions to determine the average annual RMR to apply to debt securities held to back general account business. Debt securities held to back separate account and reinsurance funds withheld are not subject to RMR charge. Further details of the RMR charge, as well as the amortisation of interest-related realised gains and losses, for Jackson are shown in note B1(iv) to the consolidated financial statements in Item 18.

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For debt securities backing non-linked shareholder-financed business of the UK insurance operations (other than the annuity business) and of the Asia insurance operations, the realised gains and losses are principally interest related. Accordingly, all realised gains and losses to date for these operations are being amortised over the period to the date those securities would otherwise have matured, with no explicit RMR charge.

At 31 December 2012, the level of unamortised interest-related realised gains and losses related to previously sold bonds for the Group was a net gain of £498 million (31 December 2011: net gain of £462 million;31 December 2010: net gain of £373 million).

For equity-type securities, the longer-term rates of return are estimates of the long-term trend investment return for income and capital having regard to past performance, current trends and future expectations. Equity-type securities held for shareholder-financed operations other than the UK annuity business, unit-linked and US variable annuity are of significance for the US and Asia insurance operations. Different rates apply to different categories of equity-type securities.

As at 31 December 2012, the equity-type securities for US insurance non-separate account operations amounted to £1,004 million (31 December 2011: £902 million; 2010: £852 million). For these operations, the longer-term rates of return for income and capital applied in 2012, 2011 and 2010, which reflect the combination of risk free rates and appropriate risk premiums are as follows:

	2012	2011	2010
Equity-type securities such as common and preferred stock and portfolio holdings in mutual funds	**5.5% to 6.2%**	5.9% to 7.5%	6.5% to 7.9%
Other equity-type securities such as investments in limited partnerships and private equity funds	**7.5% to 8.2%**	7.9% to 9.5%	8.5% to 9.9%

For Asia insurance operations, investments in equity securities held for non-linked shareholder-financed operations amounted to £659 million as at 31 December 2012 (31 December 2011: £590 million; 31 December 2010: £506 million). The rates of return applied in the years 2012 , 2011 and 2010 ranged from 1.0 per cent to 13.8 per cent with the rates applied varying by territory. The investment amounts for 2011 and 2010 of £590 million and £506 million, respectively included the Group's investment in China Life Insurance Company of Taiwan (China Life (Taiwan)) of £88 million and £101 million, respectively which was sold in 2012, as described in note B1to the consolidated financial statements in Item 18.

The longer-term rates of return discussed above for equity-type securities are determined after consideration by the Group's in-house economists of long-term expected real government bond returns, equity risk premium and long-term inflation. These rates are broadly stable from period to period but may be different between countries reflecting, for example, differing expectations of inflation in each territory. The assumptions are for returns expected to apply in equilibrium conditions. The assumed rates of return do not reflect any cyclical variability in economic performance and are not set by reference to prevailing asset valuations.

ii US variable and fixed index annuity business

The following value movements for Jackson's variable and fixed index annuity business are excluded from operating profit based on longer-term investment returns:

Fair value movements for equity-based derivatives;

Fair value movements for embedded derivatives for Guaranteed Minimum Withdrawal Benefit (GMWB) 'not for life' and fixed index annuity business, and Guaranteed Minimum Income Benefit (GMIB) reinsurance (see note);

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Movements in accounts carrying value of Guaranteed Minimum Death Benefit (GMDB) and GMWB 'for life' liabilities, for which, under the 'grandfathered' US GAAP applied under IFRS for Jackson's insurance assets and liabilities, the measurement basis gives rise to a muted impact of current period market movements;

Fee assessments and claim payments, in respect of guarantee liabilities; and

Related changes to amortisation of deferred acquisition costs for each of the above items.

Note: US operations Embedded derivatives for variable annuity guarantee features

The GMIB liability, which is fully reinsured, subject to a deductible and annual claim limits, is accounted for in accordance with FASB ASC Subtopic 944-80 Financial Services Insurance Separate Accounts (formerly SOP 03-1) under IFRS using 'grandfathered' US GAAP. As the corresponding reinsurance asset is net settled, it is considered to be a derivative under IAS 39, 'Financial Instruments: Recognition and Measurement', and the asset is therefore recognised at fair value. As the GMIB benefit is economically reinsured the mark to market element of the reinsurance asset is included as a component of short-term fluctuations in investment returns.

iii Other derivative value movements

Generally, derivative value movements are excluded from operating results based on longer-term investment returns (unless those derivative value movements broadly offset changes in the accounting value of other assets and liabilities included in operating profit). The principal example of non-equity based derivatives (for example interest rate swaps and swaptions) whose value movements are excluded from operating profit arises in Jackson. Non-equity based derivatives are primarily held by Jackson as part of a broadly-based hedging programme for features of Jackson's bond portfolio (for which value movements are booked in the statement of comprehensive income rather than the income statement), product liabilities (for which US GAAP accounting as 'grandfathered' under IFRS 4 does not fully reflect the economic features being hedged), and the interest rate exposure attaching to equity-based embedded derivatives.

iv Other liabilities to policyholders and embedded derivatives for product guarantees

Under IFRS, the degree to which the carrying values of liabilities to policyholders are sensitive to current market conditions varies between territories depending upon the nature of the 'grandfathered' measurement basis. In general, in those instances where the liabilities are particularly sensitive to routine changes in market conditions, the accounting basis is such that the impact of market movements on the assets and liabilities is broadly equivalent in the income statement, and operating profit based on longer-term investments returns is not distorted. In these circumstances, there is no need for the movement in the liability to be bifurcated between the elements that relate to longer-term market conditions and short-term effects.

However, some types of business movements in liabilities do require bifurcation to ensure that at the net level (ie after allocated investment return and change for policyholder benefits) the operating result reflects longer-term market returns.

Examples where such bifurcation is necessary are:

i Hong Kong

For certain non-participating business, the economic features are more akin to asset management products with policyholder liabilities reflecting asset shares over the contract term. For these products, the charge for policyholder benefits in the operating results should reflect the asset share feature rather

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than volatile movements that would otherwise be reflected if the local regulatory basis (which is applied for IFRS balance sheet purposes) was used.

For other Hong Kong non-participating business, longer term interest rates are used to determine the movement in policyholder liabilities for determining operating results. Similar principles apply for other Asia operations.

ii Japan Guaranteed Minimum Death Benefit (GMDB) product features

For unhedged GMDB liabilities accounted for under IFRS using 'grandfathered' US GAAP, such as in the Japanese business, the change in carrying value is determined under FASB ASC subtopic 944-80, Financial Services Insurance Separate Accounts (formerly SOP 03-1), which partially reflects changes in market conditions. Under the company's segmental basis of reporting the operating profit reflects the change in liability based on longer-term market conditions with the difference between the charge to the operating result and the movement reflected in the total result included in short-term fluctuations in investment returns.

UK shareholder-backed annuity business

The operating result based on longer-term investment returns reflects the impact of value movements on policyholder liabilities for annuity business in PRIL and the PAC non-profit sub-fund after adjustments to allocate the following elements of the movement to the category of 'short-term fluctuations in investment returns' in the Group's supplementary analysis of profit:

The impact on credit risk provisioning of actual upgrades and downgrades during the period;

Credit experience compared to assumptions

Short-term value movements on assets backing the capital of the business.

Credit experience reflects the impact of defaults and other similar experience, such as asset exchanges arising from debt restructuring by issuers that include effectively an element of permanent impairment of the security held. Negative experience compared to assumptions is included within short-term fluctuations in investment returns without further adjustment. This is to be contrasted with positive experience where surpluses are retained in short-term allowances for credit risk for IFRS reporting purposes. The effects of other changes to credit risk provisioning are included in the operating result, as is the net effect of changes to the valuation rate of interest due to portfolio rebalancing to align more closely with management benchmark.

v Fund management and other non-insurance businesses

For these businesses, the particular features applicable for life assurance noted above do not apply. For these businesses it is inappropriate to include returns in the operating result on the basis described above. Instead, it is appropriate to generally include realised gains and losses (including impairments) in the operating result with unrealised gains and losses being included in short-term fluctuations. For this purpose impairments are calculated as the credit loss determined by comparing the projected cash flows discounted at the original effective interest rate to the carrying value. In some instances it may also be appropriate to amortise realised gains and losses on derivatives and other financial instruments to operating results over a time period that reflects the underlying economic substance of the arrangements.

Actuarial and other gains and losses on defined benefit pension schemes

Actuarial and other gains and losses on defined benefit pension schemes principally reflect short-term value movements on scheme assets and the effects of changes in actuarial assumptions. Under Prudential's accounting policies these items are recorded within the income statement, rather than through other comprehensive income, solely due to the interaction of Prudential's approach to adoption of IFRS 4 for with-profits funds and the requirements of IAS 19.

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Reconciliation of total profit (loss) by business segment and geography to IFRS operating profit based on longer-term investment returns

Analysis of IFRS operating profit based on longer-term investment returns and IFRS total profit

A reconciliation of profit (loss) before tax (including tax attributable to policyholders' returns) to profit (loss) before tax attributable to shareholders and loss for the period is shown below.

	2012	2011*	2010*
	£m	£m	£m
Insurance business			
Long-term business[ii]			
Asia	**920**	709	526
US	**964**	651	728
UK	**703**	683	673
Development expenses	**(7)**	(5)	(4)
Long-term business operating profit	**2,580**	2,038	1,923
UK general insurance commission[iii]	**33**	40	46
Asset management business			
M&G	**371**	357	284
Eastspring Investments	**75**	80	72
US broker-dealer and asset management	**39**	24	22
	3,098	2,539	2,347
Other income and expenditure	**(498)**	(483)	(450)
RPI to CPI inflation measure change on defined benefit pension schemes[iv]		42	
Solvency II implementation costs	**(48)**	(55)	(45)
Restructuring costs[v]	**(19)**	(16)	(26)
Total IFRS operating profit based on longer-term investment returns[i]	**2,533**	2,027	1,826
Short-term fluctuations in investment returns[vi]			
Insurance operations	**122**	(100)	(223)
Other operations	**82**	(120)	25
Total short-term fluctuations in investment returns	**204**	(220)	(198)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes[vii]	**50**	21	(10)
Costs of terminated AIA transaction[viii]			(377)
Gain on dilution of Group's holdings	**42**		30
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC[ix]	**(19)**		
Profit before tax from continuing operations attributable to shareholders	**2,810**	1,828	1,271
Tax (charge) credit attributable to shareholders' returns	**(613)**	(409)	40
Profit for the year	**2,197**	1,419	1,311
Non-controlling interests		(4)	(5)
Total profit for the year attributable to equity holders of Prudential	**2,197**	1,415	1,306

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the

retrospective application of the changes in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

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Notes

(i)

Operating profit based on longer-term investment returns

The Group provides supplementary analysis of IFRS profit before tax attributable to shareholders so as to distinguish operating profit based on longer-term investment returns from other elements of total profit. Operating profit based on longer-term investment returns is the basis on which management regularly reviews the performance of Prudential's segments as defined by IFRS 8. Further discussion on the determination of operating profit based on longer-term investment returns is provided in A3(2)(d) of the consolidated financial statements in Item 18 and section c "Additional explanation of performance measures and analysis of consolidated results by business segment and geographical region" above.

(ii)

Effect of changes to assumptions, estimates and bases of determining life assurance liabilities

The results of the Group's long-term business operations are affected by changes to assumptions, estimates and bases of preparation.

These are described in notes D2(g), D3(g) and D4(g) of the consolidated financial statements in Item 18.

(iii)

UK operations transferred its general insurance business to Churchill in 2002, with general insurance commission representing the commission received net of expenses for Prudential-branded general insurance products as part of this arrangement.

(iv)

During 2011 the Group altered its inflation measure basis for future statutory increases to pension payments for certain tranches of its UK defined benefit pension schemes. This reflects the UK Government's decision to replace the basis of indexation from Retail Prices Index (RPI) to the Consumer Prices Index (CPI). This resulted in a credit to operating profit before tax in 2011 of £42 million.

(v)

Restructuring costs are incurred in the UK and represent one-off expenses incurred in securing expense savings.

(vi)

Short-term fluctuations in investment returns on shareholder-backed business comprise:

	2012	**2011***	**2010***
	£m	**£m**	**£m**
Insurance operations:			
Asia	**76**	(92)	114
US	**(90)**	(167)	(453)
UK	**136**	159	116
Other operations			
Economic hedge value movement	**(32)**		
Other	**114**	(120)	25
Total	**204**	(220)	(198)

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

Further details on the short-term fluctuations in investment returns are provided below under 'Charge for short-term fluctuations in investment returns' and also in note B1 in the consolidated financial statements in Item 18.

(vii)

For the 2011 comparatives, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes comprises the aggregate effect of actual less expected returns on scheme assets, experience gains and losses, the effect of changes in assumptions and altered provisions for deficit funding, where relevant. For 2012, these items also apply. However, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes also includes £49 million for the effect of partial recognition of surplus of the main Prudential Staff Pension Scheme (PSPS). This credit arises from altered funding arrangement following the 5 April 2011 triennial valuation. Further details on the Group's defined benefit pension schemes are shown in note I3 to the consolidated financial statements in Item 18.

(viii)

The costs were incurred in the first six months of 2010 in relation to the proposed, and subsequently terminated transaction, to purchase AIA Group Limited and related rights issue. Further details are provided in note B1(x) to the Consolidated financial statements in Item 18.

(ix)

These costs were incurred as a result of the acquisition of Reassure America Life Insurance Company (REALIC) on 4 September 2012.

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Reconciliation of IFRS operating profit based on longer-term investment returns to IFRS total profit

The following tables reconcile Prudential's operating profit based on longer-term investment returns to Prudential's total profit after tax for 2012, 2011 and 2010.

	Year ended 31 December 2012								
	Insurance operations			Asset management					
	UK	US	Asia	M&G	Eastspring UK	Eastspring US Investments	Total segment	Unallocated corporate	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	**736**	**964**	**913**	**371**	**39**	**75**	**3,098**	**(565)**	**2,533**
Short-term fluctuations in investment returns on shareholder-backed business	**136**	**(90)**	**76**	**93**			**215**	**(11)**	**204**
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	**(14)**			**15**			**1**	**49**	**50**
Gain on dilution of Group holdings				**42**			**42**		**42**
Amortisation of acquisition accounting adjustments arising on purchase of REALIC		**(19)**					**(19)**		**(19)**
Profit (loss) from continuing operations before tax attributable to shareholders	**858**	**855**	**989**	**521**	**39**	**75**	**3,337**	**(527)**	**2,810**
Tax attributable to shareholders									**(613)**
Profit for the year									**2,197**

	Year ended 31 December 2011*								
	Insurance operations			Asset management					
	UK	US	Asia	M&G	Eastspring UK	Eastspring US Investments	Total segment	Unallocated corporate	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	723	651	704	357	24	80	2,539	(512)	2,027
Short-term fluctuations in investment returns on shareholder backed business	159	(167)	(92)	(29)			(129)	(91)	(220)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	18			4			22	(1)	21
Profit (loss) from continuing operations before tax attributable to shareholders	900	484	612	332	24	80	2,432	(604)	1,828
Tax attributable to shareholders									(409)
Profit for the year									1,419

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	Year ended 31 December 2010*								
	Insurance operations		Asset management						
	UK	US	Asia	M&G	Eastspring Investments	US	Total segment	Unallocated corporate	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	719	728	522	284	22	72	2,347	(521)	1,826
Short-term fluctuations in investment returns on shareholder-backed business	116	(453)	114	47			(176)	(22)	(198)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(5)			(5)			(10)		(10)
Cost of terminated AIA transaction								(377)	(377)
Gain on dilution of holding in PruHealth	30						30		30
Profit (loss) from continuing operations before tax attributable to shareholders	860	275	636	326	22	72	2,191	(920)	1,271
Tax attributable to shareholders									40
Profit for the year									1,311

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

IFRS operating profit based on longer-term investment returns

In 2012, the Group's IFRS operating profit based on longer-term investment returns was £2,533 million, an increase of 25 per cent from 2011.

Insurance Operations

2012 compared to 2011

In Asia, IFRS operating profit based on longer-term investment returns for long-term business increased by £209 million from £704 million[20] in 2011 to £913 million in 2012. Included within this result is a £51 million one-off profit on sale of the Group's interest in China Life Insurance Company of Taiwan, which was originally acquired in 2008 when Prudential sold its Taiwanese agency business to the company. Excluding this amount, Asia's long-term business operating profit based on longer-term investment return increased by 22 per cent to £862 million, primarily reflecting strong growth in the size of our business in the region, particularly health and protection.

The contribution to profits from Indonesia, Hong Kong, Singapore and Malaysia, Prudential's largest markets in Asia, continues to rise, with operating profits based on longer-term investment return from these businesses[21] up 22 per cent from £552 million in 2011 to £674 million in 2012. High consumer demand for savings and protection in Indonesia continues to drive growth in premiums and earnings, with operating profit[21] based on longer-term investment returns up 23 per cent from £212 million to

(20)

Comparatives adjusted for retrospective application of the accounting policy change for deferred acquisition costs as discussed in Note A5 to the Prudential's consolidated financial statements in Item 18.

(21)

Before non-recurring items.

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£260 million. Hong Kong's operating profit[21] based on longer-term investment returns increased by 28 per cent to £88 million (2011: £69 million), as business mix has shifted towards higher return products. Singapore increased by 23 per cent to £206 million (2011: £167 million) and Malaysia's operating profit[21] based on longer-term investment returns at £120 million (2011: £104 million) increased by 15 per cent. Operating profits based on longer-term investment returns from our other long-term insurance operations in the region also increased by 24 per cent to £147 million (2011: £119 million), as these businesses increase in size.

The US long-term business operating profit based on longer-term investment return increased by 48 per cent from £651 million in 2011 to £964 million in 2012. The 2011 result included an accelerated deferred acquisition cost (DAC) amortisation of £190 million that did not recur. Excluding this item the underlying increase reflects the continued growth in fee income on the separate account business offset by lower earnings from fixed annuities in line with the compression in corporate spreads experienced in the course of the year. The result also includes a £67 million contribution from REALIC which was acquired in September 2012 and is performing in line with our expectations.

Prudential's UK business has sustained its performance at similar levels to the previous year, with total IFRS operating profit based on longer-term investment returns of £736 million (2011: £723 million). Long-term business generated £703 million (2011: £683 million) driven by an increase in profits from individual annuities and bulk annuity transactions, the latter contributing £31 million (2011: £23 million) to the total. Shareholders' with-profits business transfers amounted to £272 million, compared with £293 million in 2011, in line with reductions in policy bonus rates. Profit from UK general insurance commission continued to decline as expected to £33 million (2011: £40 million) as the business matures and in-force policy numbers fall.

Insurance Operations

2011 compared to 2010

In Asia, IFRS operating profit based on longer-term investment returns for long-term business increased by 35 per cent from £522 million in 2010 to £704 million in 2011. Profits from in-force business grew by 29 per cent between the two periods from £603 million to £779 million, reflecting the continued growth of the business in the region. New business strain of £70 million (2010: £76 million)[22] was lower despite higher sales due to favourable product and country mix.

Hong Kong, Indonesia, Singapore and Malaysia, Prudential's largest markets in Asia, continued to see profits grow strongly, with operating profits based on longer-term investment returns from long-term business[21] up 27 per cent from £434 million in 2010 to £552 million in 2011. The growth in Indonesia operating[21] profit based on longer-term investment returns was particularly strong, up 35 per cent from £157 million to £212 million, reflecting the organic growth of that business over recent years. Hong Kong's operating profit[21] based on longer-term investment returns increased 35 per cent to £69 million (2010: £51 million), reflecting the continued growth of the portfolio. Singapore increased by 29 per cent to £167 million[21] (2010: £129 million) and Malaysia increased by 7 per cent from £97 million to £104 million[21]. Other territories contributed operating profits based on longer-term investment returns of £114 million before non-recurring items (2010: £79 million) an increase of 43 per cent and all made positive contributions to this metric for the first time.

The US long-term business operating profit based on longer-term investment returns decreased by 11 per cent from £728 million in 2010 to £651 million in 2011, after charging £190 million (2010: £9 million) of accelerated DAC amortisation as anticipated. This charge, which is described further under 'Explanation of Movements in Profits before Shareholder Tax by Nature of Revenue and Charges Acquisition costs and other expenditure United States' below, arises as a result of market movements

(22) Excludes Japan which ceased writing new business in 2010. New business strain was in 2010 £1 million.

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and their interaction with the mean reversion methodology. It has the effect of masking an underlying improvement in the earnings of the US business, reflecting higher fees from variable annuity business following the growth of separate account balances in recent years. The benefit of higher fees is partially offset by administration expenses which have also increased broadly in line with the scale of business.

In Prudential's UK business, total IFRS operating profit based on longer-term investment returns was slightly higher than the prior year at £723 million (2010: £719 million), with long-term business generating £683 million (2010: £673 million). The year on year comparisons are distorted by the effect of bulk annuity transactions which are infrequent and vary in size between financial periods. Prudential's approach to these is very selective and Prudential will only write this business when it meets its strict profitability criteria. Two such transactions were completed in 2011 contributing £23 million to IFRS profits, compared to one transaction in 2010 with an IFRS profit contribution of £63 million.

Life business in the UK (excluding the impact of the bulk annuity transactions), contributed operating profits based on longer-term investment returns of £660 million in 2011, 8 per cent higher than the £610 million generated in 2010. The contribution from with-profits business was lower at £293 million (2010: £310 million). Operating profit based on longer-term investment returns from non-profit annuity and other life business was £67 million higher at £367 million, reflecting higher annuity profits. Profit from UK general insurance commission were lower at £40 million (2010: £46 million) following the expected decline of the in-force policy numbers as the business matures.

Asset management business

2012 compared to 2011

Total operating profit based on longer-term investment return for 2012 from M&G and Prudential Capital increased by 4 per cent, from £357 million in 2011 to £371 million in 2012, primarily reflecting positive net inflows into M&G during 2011 and 2012.

Eastspring Investments reported operating profit based on longer-term investment return of £75 million, down by £5 million from the £80 million recognised in 2011. This reflects a broadly unchanged level of fee income with the effect of higher fund values offset by a shift in business mix towards bond mandates, together with increased costs as the business develops the Eastspring Investments platform and expands into new markets.

2011 compared to 2010

Total operating profit based on longer-term investment returns for 2011 from M&G (including Prudential Capital) was £357 million, an increase of 26 per cent from £284 million in 2010. This performance was driven by improved revenues reflecting the strong net inflows received in recent periods, with funds under management of £201 billion at 31 December 2011, compared with £198 billion at 31 December 2010, together with a continued focus on cost discipline which saw a 3 percentage point reduction in the cost/income ratio.

Eastspring Investments reported operating profits based on longer-term investment returns of £80 million, an increase of 11 per cent from the £72 million recognised in 2010. This improvement was driven both by increased operating revenues from higher average funds under management during 2011 and continued cost discipline resulting in a 2 percentage point improvement in the cost/income ratio.

Unallocated corporate result

Operating loss based on longer-term investment returns for 2012 of £565 million comprised of a charge for other income and expenditure of £498 million, Solvency II implementation costs of £48 million and restructuring costs of £19 million.

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Operating loss based on longer-term investment returns for 2011 of £512 million comprised a charge for other income and expenditure of £483 million, Solvency II implementation costs of £55 million, restructuring costs of £16 million and a £42 million one-off credit, which was based on the UK Government's decision in 2011 to change the basis of indexation from RPI to CPI and as a result of which the Group altered its assumptions for future statutory increases to pension payments for its UK defined benefit pension schemes.

Operating loss based on longer-term investment returns for 2010 of £521 million comprised a charge for other income and expenditure of £450 million, Solvency II implementation costs of £45 million and restructuring costs of £26 million.

Analysis of long-term insurance business pre-tax IFRS operating profit based on longer-term investment returns by driver

This information classifies the Group's pre-tax operating earnings from long-term insurance operations into the underlying drivers of those profits, using the following categories:

i

Spread income represents the difference between net investment income (or premium income in the case of the UK annuities new business) and amounts credited to policyholder accounts. It excludes the operating investment return on shareholder net assets, which has been separately disclosed as **expected return on shareholder assets**.

ii

Fee income represents profits driven by net investment performance, being asset management fees that vary with the size of the underlying policyholder funds net of investment management expenses.

iii

With-profits results represents the shareholders' transfer from the with-profits fund in the period.

iv

Insurance margin primarily represents profits derived from the insurance risks of mortality, morbidity and persistency.

v

Margin on revenues primarily represents amounts deducted from premiums to cover acquisition costs and administration expenses.

vi

Acquisition costs and administration expenses represent expenses incurred in the period attributable to shareholders. It excludes items such as restructuring costs and Solvency II costs which are not included in the segment profit for insurance as well as items that are more appropriately included in other source of earnings lines (eg investment expenses are netted against investment income as part of spread income or fee income as appropriate).

vii

DAC adjustments comprises DAC amortisation for the period, excluding amounts related to short-term fluctuations, net of costs deferred in respect of new business.

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Analysis of pre-tax IFRS operating profit by source

	2012				
	Asia	**US**	**UK**	**Unallocated**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Spread income	**106**	**702**	**266**		**1,074**
Fee income	**141**	**875**	**61**		**1,077**
With-profits result	**39**		**272**		**311**
Insurance margin	**594**	**399**	**39**		**1,032**
Margin on revenues	**1,453**		**216**		**1,669**
Expenses:					
Acquisition costs	**(903)**	**(972)**	**(122)**		**(1,997)**
Administration expenses	**(583)**	**(537)**	**(128)**		**(1,248)**
DAC adjustments	**(28)**	**442**	**(8)**		**406**
Expected return on shareholder assets	**43**	**55**	**107**		**205**
Gain on China Life (Taiwan) shares	**51**				**51**
Long-term business operating profit	**913**	**964**	**703**		**2,580**
Asset management operating profit	**75**	**39**	**371**		**485**
GI commission			**33**		**33**
Other income and expenditure[ii]				**(565)**	**(565)**
Total operating profit based on longer-term investment returns	**988**	**1,003**	**1,107**	**(565)**	**2,533**

	2011				
	Asia	**US**	**UK**	**Unallocated**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Spread income	88	730	247		1,065
Fee income	131	680	59		870
With-profits result	38		293		331
Insurance margin	477	232	27		736
Margin on revenues	1,199		226		1,425
Expenses:					
Acquisition costs	(766)	(890)	(127)		(1,783)
Administration expenses	(503)	(412)	(128)		(1,043)
DAC adjustments[i]	14	228	(5)		237
Expected return on shareholder assets	26	83	91		200
Long-term business operating profit	704	651	683		2,038
Asset management operating profit	80	24	357		461
GI commission			40		40
RPI to CPI inflation measure change on defined benefit schemes				42	42
Other income and expenditure[ii]				(554)	(554)
Total operating profit based on longer-term investment returns	784	675	1,080	(512)	2,027

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	2010				
	Asia	US	UK	Unallocated	Total
	£m	£m	£m	£m	£m
Spread income	70	692	251		1,013
Fee income	122	506	60		688
With-profits result	32		310		342
Insurance margin	392	188	12		592
Margin on revenues	1,018		194		1,212
Expenses:					
Acquisition costs	(656)	(851)	(138)		(1,645)
Administration expenses	(467)	(344)	(113)		(924)
DAC adjustments[(i)]	(8)	412	(1)		403
Expected return on shareholder assets	19	125	98		242
Long-term business operating profit	522	728	673		1,923
Asset management operating profit	72	22	284		378
GI commission			46		46
Other income and expenditure[(ii)]				(521)	(521)
Total operating profit based on longer-term investment returns	594	750	1,003	(521)	1,826

Notes

(i) DAC adjustments have been adjusted for the retrospective application of the accounting policy improvement described in note A5 to the consolidated financial statements in Item 18.

(ii) Including restructuring and Solvency II implementation costs.

Margin analysis of long-term insurance business

The following analysis expresses certain of the Group's sources of operating profit as a margin of policyholder liabilities or other suitable driver. Details of the Group's average policyholder liability balances are given in notes D2(b), D3(b) and D4(b) in the consolidated financial statements in Item 18.

	2012			2011			2010		
Long-term business	**Profit**	**Average Liability**	**Margin**	**Profit**	**Average Liability**	**Margin**	**Profit**	**Average Liability**	**Margin**
	£m	**£m note (iv)**	**bps note (iii)**	**£m**	**£m note (iv)**	**bps note (iii)**	**£m**	**£m note (iv)**	**bps note (iii)**
Spread income	**1,074**	**62,174**	**173**	1,065	57,417	185	1,013	53,894	188
Fee income	**1,077**	**78,807**	**137**	870	68,298	127	688	56,822	121

With-profits result	**311**	**95,681**	**33**	331	93,056	36	342	89,693	38
Insurance margin	**1,032**			736			592		
Margin on revenues	**1,669**			1,425			1,212		
Expenses:									
Acquisition costs(i)	**(1,997)**	**4,195**	**(48)%**	(1,783)	3,681	(48)%	(1,645)	3,492	(47)%
Administration expenses	**(1,248)**	**143,321**	**(87)**	(1,043)	125,715	(83)	(924)	110,716	(83)
DAC adjustments(ii)	**406**			237			403		
Expected return on shareholder assets	**205**			200			242		
Gain on China Life (Taiwan) shares	**51**								
Operating profit	**2,580**			2,038			1,923		

Notes

(i) The ratio for acquisition costs is calculated as a percentage of APE including with-profits sales. Acquisition costs include only those relating to shareholders. APE is defined under the section 'EEV Basis and New Business Results' in Item 3 of this annual report.

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(ii)

DAC adjustments have been adjusted for the retrospective application of the accounting policy improvement described in note A5 to the consolidated financial statements in Item 18.

(iii)

Margin represents the operating return earned in the year as a proportion of the relevant class of policyholder liabilities excluding unallocated surplus.

(iv)

For UK and Asia, opening and closing policyholder liabilities have been used to derive an average balance for the year, as this is seen as a good proxy for average balances throughout the year. The calculation of average liabilities for Jackson is derived from month-end balances throughout the year as opposed to opening and closing balances only. Liabilities held in the general account for variable annuity living and death guaranteed benefits together with other amounts on which no spread income is earned (eg REALIC liabilities) are excluded from the calculation of the average. In addition for REALIC, which are included in the average liability to calculate the administration expense margin, the calculation excludes the liabilities reinsured to (and in essence retained by) Swiss Re immediately prior to the acquisition by Jackson.

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Long-term business	Asia 2012 Average Profit	Average Liability	Margin	2011 Average Profit	Average Liability	Margin	2010 Average Profit	Average Liability	Margin
	£m	£m	bps note (iii)	£m	£m	bps note (iii)	£m	£m	bps note (iii)
Spread income	**106**	**6,720**	**158**	88	5,623	157	70	4,393	159
Fee income	**141**	**13,022**	**108**	131	12,370	106	122	11,222	109
With-profits result	**39**	**12,990**	**30**	38	11,775	32	32	10,135	32
Insurance margin	**594**			477			392		
Margin on revenues	**1,453**			1,199			1,018		
Expenses:									
Acquisition costs(i)	**(903)**	**1,897**	**(48)%**	(766)	1,660	(46)%	(656)	1,508	(44)%
Administration expenses	**(583)**	**19,742**	**(295)**	(503)	17,993	(280)	(467)	15,615	(299)
DAC adjustments(ii)	**(28)**			14			(8)		
Expected return on shareholder assets	**43**			26			19		
Gain on China Life (Taiwan) shares	**51**								
Operating profit	**913**			704			522		

Notes

(i) The ratio for acquisition costs is calculated as a percentage of APE including with-profits sales. Acquisition costs include only those relating to shareholders. APE is defined under the section 'EEV Basis and New Business Results' in Item 3 of this annual report.

(ii) DAC adjustments have been adjusted for the retrospective application of the accounting policy change described in note A5 to the consolidated financial statements in Item 18.

(iii) Margin represents the operating return earned in the year as a proportion of the relevant class of policyholder liabilities excluding unallocated surplus.

Analysis of Asia IFRS operating profit drivers

Spread income has increased by £18 million from £88 million in 2011 to £106 million in 2012, an increase of 20 per cent that predominantly reflects the growth of the Asian non-linked policyholder liabilities. In 2011, Spread income increased by 26 per cent when compared to the £70 million earned in 2010, also driven by the increase in policyholder liabilities.

Fee income has increased from £122 million in 2010 to £131 million in 2011 and further to £141 million in 2012, broadly in line with the increase in movement in average unit-linked liabilities over the period.

Insurance margin has increased from £392 million in 2010 to £477 million in 2011and further to £594 million in 2012, predominantly reflecting the continued growth of the in-force book, which contains a relatively high proportion of risk-based products. Insurance margin includes non-recurring items of £48 million (2011 :£38 million; 2010: £19 million), reflecting assumption changes and other items that are not expected to reoccur in the future.

Margin on revenues has increased by £254 million from £1,199 million in 2011 to £1,453 million in 2012 primarily reflecting the on-going growth in the size of the portfolio and higher premium income recognised in the year. In 2011 income was £181 million higher than the £1,018 million earned in 2010. As well as growth in the portfolio there was also a change in business mix towards those countries that levy higher premium charges (eg Indonesia) during 2011.

Acquisition costs have increased by 18 per cent from £766 million in 2011 to £903 million in 2012, compared to the 14 per cent increase in sales, resulting in a marginal increase in the acquisition cost ratio. Acquisition costs in 2011 increased by 17 per cent when compared to the £656 million paid in 2010, ahead of the 10 per cent increase in sales in that year. This latter trend was distorted by changes in country mix, partially by the reduction of sales in India. The

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analysis above has been prepared applying shareholder acquisition costs as a proportion of total APE. If with-profits sales were excluded from the denominator the acquisition cost ratio would become 63 per cent (2011: 59 per cent; 2010: 53 per cent) reflecting changes to product and country mix.

Administration expenses have increased from £503 million in 2011 to £583 million in 2012 as the business continues to expand. Expressed as a ratio of policyholder liabilities, administration costs have increased from 280 basis points to 295 basis points due to changes in business mix. 2010 had an administration expense ratio of 299 basis points.

Expected return on shareholder assets has increased from £26 million in 2011 to £43 million in 2012 primarily due to higher income from increased shareholder assets. 2011 was £7 million higher than the £19 million earned in 2010, principally reflecting higher shareholder assets and lower investment expenses in 2011 as compared to 2010.

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Long-term business	US 2012 Average			2011 Average			2010 Average		
	Profit	Liability	Margin	Profit	Liability	Margin	Profit	Liability	Margin
	£m	£m note (iii)	bps	£m	£m note (iii)	bps	£m	£m note (iii)	bps
Spread income	**702**	**29,416**	**239**	730	28,274	258	692	28,532	243
Fee income	**875**	**44,046**	**199**	680	34,452	197	506	25,247	200
Insurance margin	**399**			232			188		
Expenses:									
Acquisition costs(i)	**(972)**	**1,462**	**(66)%**	(890)	1,275	(70)%	(851)	1,164	(73)%
Administration expenses	**(537)**	**75,802**	**(71)**	(412)	62,726	(66)	(344)	53,779	(64)
DAC adjustments(ii)	**442**			228			412		
Expected return on shareholder assets	**55**			83			125		
Operating profit	**964**			651			728		

Notes

(i) The ratio for acquisition costs is calculated as a percentage of APE. APE is defined under the section 'EEV Basis and New Business Results in Item 3 of this annual report.

(ii) DAC adjustments have been adjusted for the retrospective application of the accounting policy change described in note A5 to the consolidated financial statements in Item 18.

(iii) The calculation of average liabilities for Jackson is derived from month-end balances throughout the year as opposed to opening and closing balances only. Liabilities held in the general account for variable annuity living and death guaranteed benefits together with other amounts on which no spread income is earned (eg REALIC liabilities) are excluded from the calculation of the average. In addition for REALIC, which is included in the average liability to calculate the administration expense margin, the calculation excludes the liabilities reinsured to (and in essence retained by) Swiss Re immediately prior to the acquisition by Jackson.

Analysis of US operating profit drivers:

Spread income was £702 million in 2012, down £28 million from the £730 million earned in 2011. 2012 benefited by £156 million from the effect of transactions entered into during 2011 and 2010 to more closely match the overall asset and liability duration (2011: £113 million; 2010: £108 million). Excluding this effect, the spread margin would have been 186 basis points (2011: 218 basis points; 2010: 205 basis points). The reported spread margin decreased in 2012 as a result of downward pressure on yields caused by the low interest rate environment, the effect of which was only partly mitigated by reductions in crediting rates.

Fee income has increased by 29 per cent to £875 million in 2012, compared to £680 million in 2011 and £506 million in 2010, in each case as a result of the growth in separate account balances primarily due to positive net flows from variable annuity business. Fee income margin has increased slightly to 199 basis points (2011: 197 basis points) primarily reflecting changes to business mix. 2010 saw a fee income margin of 200 basis points.

Insurance margin represents operating profits from insurance risks, including variable annuity guarantees and other sundry items. Positive net flows into variable annuity business with life contingent and other guarantee fees over the last two years have increased the insurance margin from £188 million in 2010 to £232 million in 2011 and further to £399 million in 2012. 2012 also includes four months profits, amounting to £87 million, from the life business of REALIC, following its acquisition by Jackson in September 2012 as well as the benefit of repricing actions undertaken in the year.

Acquisition costs, which are commissions and general expenses incurred to acquire new business, have increased in absolute terms compared to 2011 due largely to an increase in sales volumes. However, acquisition costs as a percentage of APE have decreased to 66 per cent for 2012, compared to 70 per cent in 2011, due to the continued increase in producers selecting

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asset based commission which is treated as an administrative expense in this analysis, rather than front end commissions. 2010 saw an acquisition cost ratio of 73 per cent. 2011 was lower following a reduced rate of marketing costs and lower average commissions compared to 2010.

Administration expenses increased to £537 million in 2012 compared to £412 million in 2011, primarily as a result of higher asset based commissions paid on the larger 2012 separate account balance. Asset based commissions are paid upon policy anniversary dates and are treated as an administration expense in this analysis as opposed to a cost of acquisition and are offset by higher fee income. The administration expense margin was higher at 71 basis points (2011: 66 basis points; 2010: 66 basis points). Excluding these trail commission amounts, the resulting administration expense margin would be 48 basis points (2011: 46 basis points; 2010: 48 basis points). The increase in 2012 compared to 2011 arises as a result of the effect of the REALIC acquisition on the administration expense margin together with impact in 2012 of non-recurring expenditures.

DAC adjustments increased to £442 million in 2012 compared to £228 million in 2011 and £412 million in 2010. 2011 was lowered by £190 million of accelerated DAC amortisation as a result of the reversal of the benefit received in 2008 from the mean reversion formula. Market movements in 2012 resulted in deceleration of DAC amortisation of £56 million which was offset by higher amortisation when compared to 2011 as a result of higher gross profits. Following the adoption of the updated US GAAP principles for deferred acquisition costs, as described in note A5 to the consolidated financial statements in Item 18, certain acquisition costs are no longer fully deferrable resulting in new business strain of £174 million for 2012 (2011: £156 million; 2010: £159 million).

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Analysis of pre-tax operating profit before and after acquisition costs and DAC adjustments

	2012				2011				2010			
	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total	Other operating profits	Acquisition costs Incurred	Acquisition costs Deferred	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Total operating profit before acquisition costs and DAC adjustments	**1,494**			**1,494**	1,313			1,313	1,167			1,167
Less new business strain		**(972)**	**798**	**(174)**		(890)	734	(156)		(851)	692	(159)
Other DAC adjustments amortisation of previously deferred acquisition costs												
Normal(i)			**(412)**	**(412)**			(316)	(316)			(271)	(271)
Decelerated/(accelerated)			**56**	**56**			(190)	(190)			(9)	(9)
Total	**1,494**	**(972)**	**442**	**964**	1,313	(890)	228	651	1,167	(851)	412	728

Long-term business	UK 2012 Average Profit	Liability	Margin	UK 2011 Average Profit	Liability	Margin	UK 2010* Average Profit	Liability	Margin
	£m	£m	bps	£m	£m	bps	£m	£m	bps
Spread income	**266**	**26,038**	**102**	247	23,520	105	251	20,969	120
Fee income	**61**	**21,739**	**28**	59	21,476	27	60	20,353	29
With-profits result	**272**	**82,691**	**33**	293	81,281	36	310	79,558	39
Insurance margin	**39**			27			12		
Margin on revenues	**216**			226			194		
Expenses:									
Acquisition costs[(i)]	**(122)**	**836**	**(15)%**	(127)	746	(17)%	(138)	820	(17)%
Administration expenses	**(128)**	**47,777**	**(27)**	(128)	44,996	(28)	(113)	41,322	(27)
DAC adjustments	**(8)**			(5)			(1)		
Expected return on shareholder assets	**107**			91			98		
Operating profit	**703**			683			673		

Note

(i)

The ratio for acquisition costs is calculated as a percentage of APE including with-profits sales. Acquisition costs include only those relating to shareholders. APE is defined under the section 'EEV Basis and New Business Results' in Item 3 of this annual report.

Analysis of UK IFRS operating profit drivers

Spread income has increased from £247 million in 2011 to £266 million in 2012 principally due to increased new business profits from higher annuity sales. The margin has fallen slightly from 105 basis points to 102 basis points. The spread margin in 2011 of 105 basis points was lower than the 120 basis points seen in 2010, principally due to 2010 benefiting from higher bulk annuity sales, partly offset by the benefit of portfolio restructuring undertaken in 2011, and higher yields being achieved on new individual annuity business.

Fee income has increased in line with the growth in unit-linked liabilities. Expressed as an asset management charge it is equivalent to 28 basis points (2011: 27 basis points; 2010: 29 basis points).

With-profits income has decreased by £21 million from £293 million in 2011 to £272 million in 2012 principally due to a 50 basis point reduction in annual bonus rates. This has contributed to the reduction in the with-profits margin from 36 basis points in 2011 to 33 basis points in 2012.

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Insurance margin has increased from £12 million in 2010 to £27 million in 2011 and further to £39 million in 2012, mainly due to increased profits from our protection business.

Margin on revenues represents premiums charges for expenses and other sundry net income received by the UK. 2012 income was £216 million (2011: £226 million; 2010: £194 million). 2011 was higher than 2010 principally due to higher sundry income and an increase in premiums from shareholder-backed retail business in 2011 as compared to 2010.

Acquisition costs as a percentage of new business sales have improved from 17 per cent in 2010 and 2011 to 15 per cent in 2012.

The ratio above expresses the percentage of shareholder acquisition costs as a percentage of total APE sales. It is therefore impacted by the level of with-profit sales in the year. Acquisition costs as a percentage of shareholder-backed new business sales were 33 per cent for 2012 (2011: 33 per cent; 2010: 30 per cent). 2010 had a lower acquisition cost ratio as it benefited from a higher level of bulk annuity transactions, which had a relatively modest level of acquisition costs.

Expected return on shareholder assets has increased from £91 million in 2011 to £107 million in 2012 principally due to higher IFRS shareholders' funds.

Asia operations analysis of operating profit by territory

Operating profit based on longer-term investment returns for Asia operations are analysed as follows:

	2012	2011*	2010*
	£m	£m	£m
China	**19**	11	5
Hong Kong	**88**	69	51
India	**54**	47	25
Indonesia	**260**	212	157
Japan	**(2)**	2	(6)
Korea	**16**	17	12
Malaysia	**120**	104	97
Philippines	**15**	5	2
Singapore	**206**	167	129
Taiwan bancassurance business	**18**	2	(7)
Thailand	**7**	4	2
Vietnam	**25**	30	35
Other	**(5)**	1	5
Non-recurrent items:[(ii)]			
Gain on China Life (Taiwan) shares	**51**		
Other non-recurrent items	**48**	38	19
Total insurance operations[(i)]	**920**	709	526
Development expenses	**(7)**	(5)	(4)
Total long-term business operating profit	**913**	704	522
Eastspring Investments	**75**	80	72
Total Asia operations	**988**	784	594

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

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Notes

(i)

Analysis of operating profit between new and in-force business

The result for insurance operations comprises amounts in respect of new business and business in-force as follows:

	2012	2011*	2010*
	£m	£m	£m
New business strain	**(51)**	**(70)**	(77)
Business in force	**872**	**741**	584
Non-recurrent items:(ii)			
Gain on China Life (Taiwan) shares	**51**		
Other non-recurrent items	**48**	**38**	19
Total	**920**	**709**	526

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

The IFRS new business strain corresponds to approximately 3 per cent of new business APE premiums for 2012 (2011: approximately 4 per cent of new business APE). The improvement is driven by a shift in overall sales mix to lower strain products and countries.
The strain reflects the aggregate of the pre-tax regulatory basis strain to net worth after IFRS adjustments for deferral of acquisition costs and deferred income where appropriate.

(ii)

During 2012, the Group sold its 7.74 per cent stake in China Life (Taiwan) for £97 million crystallising a gain of £51 million.

Other non-recurrent items of £48 million in 2012 (2011: £38 million; 2010: £19 million) represent a small number of items that are not anticipated to re-occur in subsequent periods.

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Analysis of asset management operating profit based on longer-term investment returns

	2012				
	M&G(i),(ii)	Eastspring Investments(ii)	PruCap	US	Total
	£m	£m	£m	£m	£m
Operating income before performance-related fees	734	201	120	296	1,351
Performance-related fees	9	2			11
Operating income*	743	203	120	296	1,362
Operating expense	(436)	(128)	(69)	(257)	(890)
Share of associate's results	13				13
Operating profit based on longer-term investment returns	320	75	51	39	485
Average funds under management (FUM), including 49.99% proportional share of PPM South Africa**	£209.0 bn				
Average funds under management (FUM), excluding PPM South Africa**	£205.1 bn	£55.0 bn			
Margin based on operating income**	36 bps	37 bps			
Cost/income ratio***	59%	64%			

	2011				
	M&G(i),(ii)	Eastspring Investments(ii)	PruCap	US	Total
	£m	£m	£m	£m	£m
Operating income before performance-related fees	666	196	122	249	1,233
Performance-related fees	13	6			19
Operating income*	679	202	122	249	1,252
Operating expense	(404)	(122)	(66)	(225)	(817)
Share of associate's results	26				26
Operating profit based on longer-term investment returns	301	80	56	24	461
Average funds under management (FUM), including 49.99% proportional share of PPM South Africa**	£195.1 bn				
Average funds under management (FUM), excluding PPM South Africa**	£190.9 bn	£51.4 bn			
Margin based on operating income**	35 bps	38 bps			
Cost/income ratio***	61%	62%			

	2010				
	M&G(i)	Eastspring Investments(i)	PruCap	US	Total
	£m	£m	£m	£m	£m
Operating income before performance-related fees	578	185	88	229	1,080
Performance-related fees	14	6			20
Operating income*	592	191	88	229	1,100
Operating expense	(366)	(119)	(50)	(207)	(742)
Share of associate's results	20				20
Operating profit based on longer-term investment returns	246	72	38	22	378
Average funds under management (FUM) including 49.99% proportional share of PPM South Africa**	£179.6 bn				
Average funds under management (FUM), excluding PPM South Africa**	£175.5 bn	£47.6 bn			
Margin based on operating income**	33 bps	39 bps			
Cost/income ratio***	63%	64%			

(i) Following the divestment in the first half of 2012 of M&G's holding in PPM South Africa from 75 per cent to 49.99 per cent and its treatment from 2012 as an associate, M&G's operating income and expense no longer includes any element from PPM South Africa. In order to avoid period on period distortion, in the table above the 2011 and 2010 operating income, margin and cost/income ratio reflect the retrospective application of this basis of presentation for the 2011 and 2010 results.

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(ii)

M&G and Eastspring Investments can be further analysed as follows:

	M&G Operating income*						Eastspring Investments Operating income*					
	Retail	Margin of FUM**	Institutional	Margin of FUM**	Total	Margin of FUM**	Retail	Margin of FUM**	Institutional	Margin of FUM**	Total	Margin of FUM**
	£m	bps	£m	bps	£m	bps	£m	bps	£m	bps	£m	bps
2012	**438**	**91**	**297**	**19**	**734**	**36**	**118**	**64**	**83**	**24**	**201**	**37**
2011	396	97	270	18	666	35	120	62	76	24	196	38
2010	327	101	251	18	578	33	119	61	66	23	185	39

*

Operating income is net of commissions. M&G's operating income excludes any contribution from M&G's associate, PPM South Africa.

**

Margin represents operating income before performance related fees as a proportion of the related funds under management (FUM), excluding PPM South Africa. 2011and 2010 comparatives have been amended to be on a comparable basis. Monthly funds managed by the respective entity have been used to derive the average. Any funds held by the Group's insurance operations which are managed by third parties outside of the Prudential Group are excluded from these amounts.

***

Cost/income ratio represents cost as a percentage of operating income before performance related fees. In order to avoid period on period distortion, M&G's operating income and expense excludes any contribution from M&G's associate, PPM South Africa.

Institutional includes internal funds.

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Charge for short-term fluctuations in investment returns

As discussed above, in calculating the operating profit based on longer-term investment returns, longer-term investment return assumptions are used rather than actual investment returns arising in the year. The difference between actual investment returns recorded in the income statement and longer-term returns is shown in the analysis of profits as short-term fluctuations in investment returns.

In 2012 short-term fluctuations in investment returns for our insurance operations of positive £122 million comprised of positive £76 million for Asia, negative £90 million in the US and positive £136 million in the UK.

The positive short-term fluctuations of £76 million for our Asia operations in 2012 relates to unrealised gains on bond assets held across the region following the fall in long-term yields in the period.

The combination of higher equity markets and lower market volatility in the US has reduced the technical reserves held for the variable annuity guarantees. This favourable effect was more than offset by the net unrealised value movement on derivative instruments held to manage the Group's exposure to these guarantees, producing a net £90 million negative fluctuation in our US operation.

The positive short-term fluctuations of £136 million for our UK operations primarily reflect net valuation gains on fixed income assets supporting the capital of the shareholder-backed annuity business.

Short-term fluctuations for other operations were positive £82 million. This primarily represents appreciation on Prudential Capital's bond portfolio partially offset by net realised and unrealised losses in the year on derivatives held centrally to manage market risks.

In 2011, short-term fluctuations in investment returns for the Group's insurance operations comprised negative £92 million for Asia, negative £167 million for US operations and positive £159 million in the UK.

The negative short-term fluctuations of £92 million for Prudential's Asia operations in part reflected equity market falls in Taiwan and a partial reversal of unrealised gains recognised in prior years on the Group's investment in China Life Insurance Company in Taiwan.

Negative fluctuations of £167 million arising in Prudential's US operation comprised negative £255 million from short-term fluctuations offset by positive £88 million relating to Jackson's debt securities portfolio. These gains arose as a result of a high level of realised investment gains in 2011, following management's credit risk reduction programme.

The positive short-term fluctuations of £159 million for Prudential's UK operations principally reflected net valuation gains arising in the period on fixed income assets backing the capital of the shareholder-backed annuity business.

Short-term fluctuations for other operations were negative £120 million representing unrealised losses on investments, principally on centrally held swaps to manage foreign exchange and certain macro-economic exposures of the Group.

In 2010, short-term fluctuations in investment returns of negative £198 million comprised positive £114 million for Asia, negative £453 million for US operations, positive £116 million in the UK and positive £25 million for other operations.

The positive short-term fluctuations of £114 million in 2010 for Prudential's Asia operations primarily reflected unrealised gains on the shareholder debt portfolio, as well as a £30 million unrealised gain on the Group's 8.66 per cent stake in China Life Insurance Company of Taiwan.

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The negative short-term fluctuations of £453 million in 2010 for Prudential's US operations principally arose on derivative and embedded derivative value movements. They included the negative net equity hedge accounting effect (net of related DAC amortisation)[23] of £443 million. The strong rise in the S&P Index in the last quarter of 2010 resulted in fair value reductions in the free-standing derivatives backing the guarantees embedded in Jackson's variable and fixed index annuity products. As a substantial proportion of these guarantees are not fair valued for accounting purposes, there is insufficient accounting offset to these value movements. Other US short-term fluctuations were negative £10 million.

The positive short-term fluctuations of £116 million in 2010 for Prudential's UK operations reflected principally value movements on fixed income assets backing the capital of the shareholder-backed annuity business, brought about by the falls in yields during 2010.

Short-term fluctuations in investment returns for other operations in 2010 were positive £25 million and mainly represented unrealised appreciation on Prudential Capital's debt securities portfolio offset by unrealised value movements on centrally held derivatives.

Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes

The shareholders' share of actuarial and other gains and losses on defined benefit pension schemes of positive £50 million (2011: positive £21 million) mainly reflects the partial recognition of actuarial surplus in the Prudential Staff Pension Scheme following the results of the triennial valuation, further details of which are given in note I3 to the consolidated financial statements in Item 18.

Gain on dilution of Group holdings

2012

On 22 February 2012, M&G completed transactions to reduce its majority holding in PPM South Africa from 75 per cent to 49.99 per cent. Under IFRS the transactions give rise to a gain on dilution of £42 million, which has been excluded from the Group's IFRS operating profit.

2010

On 1 August 2010, Discovery Holdings of South Africa, the Group's joint venture partner in its investment in PruHealth, completed the acquisition of the entire share capital of Standard Life Healthcare, a wholly-owned subsidiary of the Standard Life Group, for £138 million. Discovery funded the purchase of the Standard Life Healthcare transaction, and contributed Standard Life Healthcare to PruHealth as a capital investment on completion. As a result of the transaction, Discovery increased their shareholding in PruHealth from the previous level of 50 per cent to 75 per cent, and Prudential's shareholding reduced from 50 per cent of the previous joint venture structure to 25 per cent of the new structure of the much enlarged business.

As a result of this dilution in holding and the consequential loss of control, PruHealth was reclassified from a joint venture to an associate and the entity was no longer proportionally consolidated from the date of the transaction. In accordance with IAS 31 'Interests in joint ventures' a gain of £30 million arose in 2010 upon the dilution, representing the difference between the fair value of the enlarged 25 per cent investment still held and the IFRS book value of the original 50 per cent investment holding.

(23) Based on longer-term equity volatility and interest rate assumptions.

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Amortisation of acquisition accounting adjustments arising on the purchase of REALIC

On 4 September 2012, Jackson completed the acquisition of 100 per cent of the issued share capital of SRLC America Holding Corp. (SRLC), and its primary operating subsidiary, REALIC for a total cash consideration of £370 million. The amortisation primarily comprises the difference between the yield on the acquired investments based on market values at acquisition and historic investment income on book yields recognised in IFRS operating profit. Movement in the fair value acquisition adjustments on the value of business acquired and policyholder liabilities is also included. Further details are given in note I1 to the consolidated financial statements in Item 18.

Costs of terminated AIA transaction in 2010

During 2010, Prudential incurred pre-tax costs in relation to the AIA transaction of £377 million. This comprised the termination break fee of £153 million, the costs associated with foreign exchange hedging of £100 million, underwriting fees of £58 million and adviser and other fees totalling £66 million. After expected tax relief, the post-tax cost was £284 million.

Effective tax rates

The effective rate of tax on operating profit based on longer-term investment returns was 23 per cent (2011: 21 per cent; 2010: 10 per cent). Comparing 2012 and 2011, the 2011 effective rate had benefited from utilising carried forward tax losses for which no deferred tax asset had been recognised. For 2010, adjusting the tax rate to exclude the exceptional tax credit of £158 million which primarily related to the impact of a settlement agreed with the UK tax authorities, the underlying tax rate operating profit was 18 per cent. The 2010 effective tax rate benefited from revisions to prior period tax returns in the UK and an increase in the proportion of income in Asia which attracts lower tax.

The effective rate of tax on the total IFRS profit was 22 per cent (2011: 22 per cent; 2010: negative 3 per cent). We have benefitted from reductions in the main UK corporation tax rate 28 per cent to 26 per cent in 2011 and 26 per cent to 24 per cent in 2012. Adjusting the negative 3 per cent rate in 2010 to exclude the exceptional tax credit of £158 million gave an underlying tax rate at the total IFRS total profit level of 9 per cent. In 2010, and to a lesser extent in 2011 and 2012, we have also benefited from utilising carried forward tax losses for which no deferred tax asset was previously established.

Earnings per share

	2012	2011(i)	2010 Excluding exceptional tax credit(ii)	2010 Including exceptional tax credit(ii)
	pence	pence	pence	pence
Basic EPS based on operating profit based on longer-term investment returns after tax and non-controlling interests	**76.8**	62.8	59.0	65.3
Basic EPS based on total profit after tax and non-controlling interests	**86.5**	55.8		51.7

Notes

(i) Comparatives adjusted for retrospective application of the accounting policy change for deferred acquisition

costs as discussed in note A5 to consolidated financial statements in Item 18.

(ii)

The exceptional tax credit in 2010 relates to a £158 million credit which primarily relates to the impact of a settlement agreed with the UK tax authorities.

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Explanation of Movements in Profits Before Shareholder Tax by Nature of Revenue and Charges

The following table shows Prudential's consolidated total revenue and consolidated total charges for the periods presented:

	2012	2011*	2010*
	£m	£m	£m
Gross premiums earned[a]	**29,910**	25,706	24,568
Outward reinsurance premiums	**(506)**	(429)	(357)
Earned premiums, net of reinsurance	**29,404**	25,277	24,211
Investment return[b]	**24,051**	9,360	21,769
Other income	**2,021**	1,869	1,666
Total revenue, net of reinsurance	**55,476**	36,506	47,646
Benefits and claims	**(44,831)**	(31,060)	(40,608)
Outward reinsurers' share of benefit and claims	**259**	746	335
Movement in unallocated surplus of with-profits funds	**(1,381)**	1,025	(245)
Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance[c]	**(45,953)**	(29,289)	(40,518)
Acquisition costs and other expenditure[d]	**(6,055)**	(5,120)	(4,989)
Finance costs: interest on core structural borrowings of shareholder-financed operations	**(280)**	(286)	(257)
Total charges, net of reinsurance	**(52,288)**	(34,695)	(45,764)
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)***	**3,188**	1,811	1,882
(Less) add tax (charge) credit attributable to policyholders' returns	**(378)**	17	(611)
Profit before tax attributable to shareholders	**2,810**	1,828	1,271
Total tax (charge) attributable to policyholders and shareholders	**(991)**	(392)	(571)
Adjustment to remove tax credit (charge) attributable to policyholders' returns	**378**	(17)	611
Tax charge attributable to shareholders' returns	**(613)**	(409)	40
Profit for the year	**2,197**	1,419	1,311
Attributable to:			
Equity holders of the Company	**2,197**	1,415	1,306
Non-controlling interests		4	5
Profit for the year	**2,197**	1,419	1,311

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to

its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5 to Prudential's consolidated financial statements in Item 18.

**

This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders.

This is principally because the corporate taxes of the Group include those on the income of consolidated with-profits and unit-linked funds that, through adjustments to benefits, are borne by policyholders. These amounts are required to be included in the tax charge of the Company under IAS 12. Consequently, the profit before all taxes measure (which is determined after deducting the cost of policyholder benefits and movements in the liability for unallocated surplus of the

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PAC with-profits fund after adjusting for taxes borne by policyholders) is not representative of pre-tax profits attributable to shareholders.

The 2010 tax charge attributable to shareholders' return included an exceptional tax credit of £158 million which primarily related to the impact of a settlement agreed with the UK tax authorities. In addition the 2010 profit before tax is stated after £377 million of pre-tax costs of the terminated AIA transaction.

(a) Gross earned premiums

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Asian operations	**8,230**	7,378	6,380
US operations	**14,660**	12,650	11,817
UK operations	**7,020**	5,678	6,371
Total	**29,910**	25,706	24,568

Gross earned premiums for insurance operations totalled £29,910 million in 2012, up 16 per cent from £25,706 million in 2011. The increase of £4,204 million was driven by growth of £852 million in the Asian operations; £2,010 million in the US operations and £1,342 million in the UK operations.

Gross earned premiums for insurance operations totalled £25,706 million in 2011, up 5 per cent from £24,568 million in 2010. The increase of £1,138 million was driven by growth of £998 million in the Asian operations and £833 million in the US operations which were partially offset by a decrease of £693 million in the UK operations.

Asia

Gross earned premiums increased by 12 per cent from £7,378 million in 2011 to £8,230 million in 2012 and by 16 per cent from £6,380 million in 2010 to £7,378 million in 2011. The premiums reflect the aggregate of single and recurrent premiums of new business sold in the year and premiums on annual business sold in previous years. The growth in earned premiums reflects increases for both factors.

Asia's rapidly growing middle classes remain a key growth driver for the retail financial services sector, particularly life insurance with an emphasis on protection. Our four largest markets Hong Kong, Indonesia, Singapore and Malaysia have made the most material contribution to the region's growth in recent years. In addition to our well known strength in these four markets, we are building our presence and distribution in other markets that have the potential to become material drivers of growth over the medium and long term. Two such markets are Thailand and the Philippines.

During 2012 Asia's average economic growth rates, although they remained well above the global average, continued to moderate following the post crisis high seen in 2010. This is to some degree a consequence of the ongoing weakness of the economies of North America and Europe. While domestic factors were a significant influence in India and China as policymakers grapple with sensitive political situations and economic imbalances, the resilience of many other economies in the region, particularly in South-east Asia, was highlighted by upward revisions to IMF growth forecasts in the second half of the year. During the second half of 2012 the reported growth rates on sales did moderate as the economic climate was generally more challenging and specifically in Malaysia, Korea and Taiwan we deliberately and proactively slowed sales of lower margin products.

Our multi-channel distribution model is at the heart of our success and we have continued to grow and strengthen our distribution further in 2012. In both the agency and the bank channels banacassurance the returns comfortably cover the cost of capital, so we have a strong appetite for growth in both. Agency is the largest channel and we continue to increase both the scale and,

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importantly the quality and productivity of our agency force. In the bank channel, where we are the regional leader, our partnerships with Standard Chartered Bank (SCB) and United Overseas Bank (UOB), have seen considerable sales growth. Regular premium products make up the bulk of our new business.

United States

Gross earned premiums increased by 16 per cent from £12,650 million in 2011 to £14,660 million in 2012. Approximately 2 per cent of this increase was due to the contribution from REALIC following its acquisition in September 2012. Excluding REALIC's contribution, the increase was driven principally by the increase in sales of new single premium variable annuity business, including primarily the sale of our Elite Access product launched in March 2012, and by modest institutional sales. Elite Access is a new variable annuity product which has no guaranteed benefits and provides tax efficient access to alternative investments. Although we do not target volume or market share, our ranking climbed to second in variable annuity sales in the US through the third quarter of 2012 (latest information available), while market share increased to 14.0 per cent from 11.4 per cent for the full year 2011[(24)].

Gross earned premiums increased by 7 per cent from £11,817 million in 2010 to £12,650 million in 2011, driven principally by the increase in sales of new single variable annuity business and an addition of modest institutional sales partially offset by decreases in fixed annuity and fixed index annuity sales. For the variable annuity sales, Jackson continued to benefit from its customers' and distributors' flight to quality.

Jackson's strategy remains focused on providing value to its customers and driving shareholder value while operating within a conservative risk management framework. In the course of 2012 and particularly in the second half of the year, Jackson implemented various product initiatives to continue to balance value, volume, capital and balance sheet strength.

United Kingdom

Gross earned premiums for UK operations increased from £5,678 million in 2011 to £7,020 million in 2012 primarily reflecting benefit from the focus on its core products, with-profits and individual annuities, which was partially offset by a reduction in sales of corporate pensions business, after exceptionally high volumes in 2011. The PruFund range, reintroduced in 2011 as described below comprised 75 per cent of with-profits bond sales, with 35 per cent higher sales than in 2011. Two bulk annuity buy-in insurance agreements were signed in 2012 totalling total new business premiums of £408 million (2011: single deal £336 million).

In the UK, Prudential has adopted a focused strategy and competes selectively to help Britain's ageing population convert their accumulated wealth into retirement income. We have a clear focus on writing profitable new business while generating cash sustainably and preserving our capital. We concentrate on areas in which we have a clear competitive advantage, namely individual annuities and with-profits products, where we continue to be market leaders. Our performance in 2012 has been strong in a difficult market, which has been impacted by significant UK and EU regulatory change. This includes the implementation of the Retail Distribution Review (RDR), auto-enrolment for company pension schemes and Gender Neutral Pricing.

Gross earned premiums for UK operations decreased from £6,371 million in 2010 to £5,678 million in 2011 primarily reflecting lower bulk annuities in 2011 with total new business premiums of £336 million compared to a total of £945 million in 2010, reductions in the sales of individual annuities

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as Prudential UK continues proactively to manage the flow of external conventional new business to control capital consumption and reductions in premiums for annual business sold in prior years. These decreases are partially offset by increase in sales of with-profits bonds. During 2011, Prudential UK reintroduced PruFund Protected Growth Fund, with a range of guarantees added to both the Growth and Cautious funds. The PruFund range comprised 74 per cent of with-profits bond sales.

(b) Investment return

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Asia operations	**3,120**	285	2,747
US operations	**6,199**	1,448	4,577
UK operations	**14,746**	7,732	14,560
Unallocated corporate and intragroup elimination	**(14)**	(105)	(115)
Total	**24,051**	9,360	21,769

Investment return principally comprises interest income, dividends, investment appreciation/depreciation (realised and unrealised gains and losses) on investments designated as fair value through profit and loss and realised gains and losses, including impairment losses, on Jackson's debt securities designated as available-for-sale. Movements in unrealised appreciation/depreciation of Jackson's debt securities designated as available for-sale are not reflected in investment return but are recorded in other comprehensive income.

Allocation of investment return between policyholders and shareholders

Investment return is attributable to policyholders and shareholders. A key feature of the accounting policies under IFRS is that the investment return included in the income statement relates to all investment assets of the Group, irrespective of whether the return is attributable to shareholders, or to policyholders or the unallocated surplus of with-profits funds, the latter two of which have no net impact on shareholders' profit. The table below provides a breakdown of the investment return for each regional operation attributable to each type of business.

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	2012	2011	2010
	£m	£m	£m
Asia operations			
Policyholder returns			
Assets backing unit-linked liabilities	**1,262**	(812)	1,279
With-profits business	**1,208**	756	1,039
	2,470	(56)	2,318
Shareholder returns	**650**	341	429
Total	**3,120**	285	2,747
US operations			
Policyholder returns			
Assets held to back (separate account) unit-linked liabilities	**5,217**	(869)	3,520
Shareholder returns			
Realised gains and losses (including impairment losses on available-for-sale bonds)	**(876)**	(238)	21
Value movements on derivative hedging programme for general account business	**197**	841	20
Interest/dividend income and value movements on other financial instruments for which fair value movements are booked in the income statement	**1,661**	1,714	1,016
	982	2,317	1,057
Total	**6,199**	1,448	4,577
UK operations			
Policyholder returns			
Scottish Amicable Insurance Fund (SAIF)	**791**	321	1,075
Assets held to back unit-linked liabilities	**2,320**	208	2,119
With-profits fund (excluding SAIF)	**8,350**	4,094	8,815
	11,461	4,623	12,009
Shareholder returns			
Prudential Retirement Income Limited (PRIL)	**2,196**	2,153	1,717
Other business	**1,089**	956	834
	3,285	3,109	2,551
Total	**14,746**	7,732	14,560
Unallocated corporate			
Shareholder returns	**(14)**	(105)	(115)
Group Total			
Policyholder returns	**19,148**	3,698	17,847
Shareholder returns	**4,903**	5,662	3,922
Total	**24,051**	9,360	21,769

Policyholder returns

The returns as shown in the table above, are delineated between those returns allocated to policyholders and those allocated to shareholders. In making this distinction, returns allocated to

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policyholders are those from investments in which shareholders have no direct economic interest, namely:

- unit-linked business in the UK, Asia and SAIF in the UK, for which the investment return is wholly attributable to policyholders;

- separate account business of US operations, the investment return of which is also wholly attributable to policyholders; and

- with-profits business (excluding SAIF) in the UK and Asia (in which the shareholders' economic interest, and the basis of recognising IFRS basis profits, is restricted to a share of the actuarially determined surplus for distribution (in the UK 10 per cent)). Except for this surplus the investment return of the with-profits funds is attributable to policyholders (through the asset-share liabilities) or the unallocated surplus, which is accounted for as a liability under IFRS 4.

The investment return related to the types of business above does not impact shareholders' profits directly. However, there is an indirect impact, for example, investment-related fees or the effect of investment return on the shareholders' share of the cost of bonuses of with-profits funds.

Investment returns for unit-linked and similar products have reciprocal impact on benefits and claims, with a decrease in market returns on the attached pool of assets affecting policyholder benefits on these products. Similarly for with-profits funds there is a close correlation between increases or decreases in investment returns and the level of combined charge for policyholder benefits and movement on unallocated surplus that arises from such returns.

Shareholder returns

For shareholder-backed non-participating business of the UK (comprising PRIL and other non-linked non-participating business) and of the Asian operations, the investment return is not directly attributable to policyholders and therefore does impact shareholders' profit directly. However, it should be noted that for UK shareholder-backed annuity business, principally PRIL, where the durations of asset and liability cash flows are closely matched, the discount rate applied to measure liabilities to policyholders (under 'grandfathered' UK GAAP and under IFRS 4) reflects movements in asset yields (after allowances for the future defaults) of the backing portfolios. Therefore, the net impact on the shareholders' profits of the investment return of the assets backing liabilities of the UK shareholder-backed annuity business is after taking into account the consequential effect on the movement in policyholder liabilities.

Changes in shareholder investment returns for US operations reflect primarily movements in the investment income, movements in the value of derivative instruments and realised gains and losses. The derivatives are held to manage general account assets and liabilities, and variable annuity guarantees under a dynamic hedging programme. Separately reflecting Jackson's types of business an allocation is made to policyholders through the application of crediting rates.

The majority of the investments held to back the US general account business are debt securities for which the available-for-sale designation is applied for IFRS basis reporting. Under this designation the return included in the income statement reflects the aggregate of investment income and realised gains and losses (including impairment losses). However, movements in unrealised appreciation or depreciation are recognised in other comprehensive income. The return on these assets is attributable to shareholders.

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Reasons for year-on-year changes in investment returns

With two exceptions, all Prudential investments are carried at fair value in the statement of financial position with fair value movements, which are volatile from year to year, recorded in the income statement. The exceptions are for:

(i) debt securities of the US operations, which are accounted for on an IAS 39 available-for-sale basis, in respect of which realised gains and losses (including impairment losses) are recorded in the income statement, while movements in unrealised appreciation (depreciation) are booked as other comprehensive income. As a result, the changes in fair value of these debt securities are not reflected in Prudential's investment return in the income statement. The unrealised gains and losses in the income statement of US operations primarily arise on the assets of the US separate account business; and

(ii) loans and receivables, which are carried at amortised cost.

Subject to the effect of these two exceptions, the year-on-year changes in investment return primarily reflect the generality of overall market movements for equities, debt securities and, in the UK, for investment property. In addition, for Asian and US separate account business, foreign exchange rates affect the sterling value of the translated income. Consistent with the treatment applied for other items of income and expenditure, investment returns for overseas operations are translated at average exchange rates.

Asia

The table below provides an analysis of investment return attributable to Asia operations for the years presented:

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Interest/dividend income (including foreign exchange gains and losses)	**670**	502	607
Investment appreciation (depreciation)	**2,450**	(217)	2,140
Total	**3,120**	285	2,747

In Prudential's Asia operations, debt securities accounted for 55 per cent, 54 per cent and 46 per cent of the total investment portfolio as at 31 December 2012, 2011 and 2010, respectively, with equities comprising 37 per cent; 37 per cent and 47 per cent respectively. The remaining 8 per cent, 9 per cent and 7 per cent of the total investment portfolio, respectively, primarily comprised loans and deposits with credit institutions. In Asia, investment return increased from £285 million in 2011 to £3,120 million in 2012. This increase was due to an increase of £168 million in interest and dividend income (including foreign exchange gains and losses) and an increase of £2,667 million in investment appreciation. The increase of £2,667 million in investment appreciation was driven primarily by favourable market movements in the Asia equity markets and also the appreciation in the debt securities held across the region following the fall in long-term yields in the period.

Investment return decreased from £2,747 million in 2010 to £285 million in 2011. The decrease was due to a decrease of £105 million in interest and dividend income (including foreign exchange gains and losses) and a decrease of £2,357 million in investment appreciation. The decrease of £2,357 million in investment appreciation was driven primarily by adverse market movements in the Asia equity markets in 2011.

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United States

The table below provides an analysis of investment return attributable to US operations for the periods presented:

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Realised gains (losses) (including impairment losses on available-for-sale bonds)	**(876)**	(238)	21
Investment return of investments backing US separate account liabilities	**5,217**	(869)	3,520
Other investment return	**1,858**	2,555	1,036
Total	**6,199**	1,448	4,577

In the US, investment return increased from £1,448 million in 2011 to £6,199 million in 2012. This £4,751 million favourable change resulted despite a £638 million increase in realised losses and a decrease of £697 million in other investment return, as these were more than offset by an increase of £6,086 million in the investment return on investments backing variable separate account liabilities from a loss of £(869) million in 2011 to £5,217 million in 2012. Realised losses of £876 million in 2012 were principally due to freestanding derivatives held to manage exposure to equity risk as explained further in note B1 to the consolidated financial statements in Item 18. The primary driver for the increase in investment return on investments backing variable annuity separate account liabilities as compared to 2011 was favourable movements in the US equity markets in 2012 on a larger separate account asset balance. The decrease of £697 million in other investment return was mainly accounted for by the movements in the fair value of derivatives held to manage the general account business and of the equity related derivatives.

In the US, investment return decreased from £4,577 million in 2010 to £1,448 million in 2011. This £3,129 million adverse change was due to a £259 million decrease in realised gains including gains on debt securities classified as available-for-sale, as well as a decrease in investment return of the investments backing the US variable separate account liabilities of £4,389 million offset by an increase of £1,519 million in other investment return. Realised losses were £238 million in 2011 compared with realised gains of £21 million in 2010. The primary driver for the decrease in US investment return was a decrease in the returns on investments backing the US variable annuity separate account liabilities as a result of adverse movements in the US equity markets in 2011 as compared to the favourable movements in 2010. The investment return of investment assets backing US separate account liabilities decreased from a gain of £3,520 million in 2010 to a loss of £869 million in 2011. The increase of £1,519 million in other investment return was mainly accounted for by the movements in the fair value of derivatives held to manage the general account business and of the equity-related derivatives.

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United Kingdom

The table below provides an analysis of investment return attributable to UK operations for the periods presented:

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Interest/dividend income	**6,367**	6,135	6,149
Foreign exchange gains and losses[(i)]	**835**	67	(48)
Investment appreciation[(ii)]	**7,544**	1,530	8,459
Total	**14,746**	7,732	14,560

Notes

(i) Foreign exchange gains and losses on retranslation of non-sterling based assets, including foreign currency forwards, principally of the UK with-profits fund.

(ii) Investment appreciation (depreciation) comprises realised and unrealised gains and losses on the investments.

In Prudential's UK operations, equities accounted for 23 per cent, 28 per cent and 28 per cent of the total investment portfolio as at 31 December 2012, 2011 and 2010, respectively. Debt securities comprised 56 per cent, 52 per cent and 52 per cent, respectively, with investment properties accounting for 7 per cent, 8 per cent and 8 per cent of the total investment portfolio in each respective year. The remaining 14 per cent, 12 per cent and 12 per cent of the total investment portfolio as at 31 December 2012 , 2011 and 2010, respectively, related to loans, deposits with credit institutions, investments in partnerships in investment pools and derivative assets. Within debt securities of £86 billion (2011: £80 billion; 2010: £76 billion) as at 31 December 2012, 73 per cent (2011: 70 per cent; 2010: 82 per cent) was comprised of corporate debt securities. In the UK, the investment return increased by £7,014 million, from £7,732 million in 2011 to £14,746 million in 2012. This increase was primarily driven by an increase of £6,014 million in investment appreciation, favourable movements in foreign exchange gains and losses of £768 million, from a positive of £67 million in 2011 to a positive £835 million in 2012 and increase in interest/dividend income of £232 million. The foreign exchange movement in 2012 related mainly to gains in foreign currency forwards of the UK with-profits fund as the pound sterling appreciated above its level in 2011. The investment appreciation of £7,544 million in 2012 primarily reflected the favourable UK financial markets' performance during the year. The investment appreciation mainly reflected movements on equities and debt securities.

In Prudential's UK operations, equities accounted for 28 per cent of the total investment portfolio as at each of 31 December 2011 and 2010. Debt securities comprised 52 per cent and investment properties accounted for 8 per cent of the total investment portfolio in each respective year. The remaining 12 per cent of the total investment portfolio as at 31 December 2011 and 2010 related, at each such date, to loans, deposits with credit institutions, investment in partnerships in investment pools and derivative assets. Within debt securities of £76 billion (2010: £76 billion) as at 31 December 2011, 74 per cent (2010: 82 per cent) was comprised of corporate debt securities. In the UK, the investment return declined by £6,828 million, from £14,560 million in 2010 to £7,732 million in 2011. This decline was primarily driven by a decrease of £6,929 million in investment appreciation, partly offset by favourable movements in foreign exchange gains and losses of £115 million, from a negative of £48 million in 2010 to a positive £67 million in 2011. The foreign exchange movement in 2011 related mainly to gains in foreign currency forwards of the UK with-profits fund. Interest and dividend income of £6,135 million in 2011 was in line with the £6,149 million in 2010.

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Unallocated corporate and intragroup elimination

Investment return for unallocated corporate and intragroup elimination in 2012 of negative £14 million compared to the negative £105 million in 2011 and negative £115 million in 2010.

(c) Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Asia operations	**(8,285)**	(5,365)	(6,734)
US operations	**(18,711)**	(12,651)	(15,423)
UK operations	**(18,957)**	(11,273)	(18,361)
Total	**(45,953)**	(29,289)	(40,518)

Benefits and claims represent payments, including final bonuses, to policyholders in respect of maturities, surrenders and deaths plus changes in technical provisions (which primarily represents the movement in amounts owed to policyholders). Benefits and claims are amounts attributable to policyholders. The movement in unallocated surplus of with-profits funds represents the transfer to (from) the unallocated surplus each year through a charge (credit) to the income statement of the annual excess (shortfall) of income over expenditure of the with-profits funds, after declaration and attribution of the cost of bonuses to policyholders and shareholders.

The underlying reasons for the year-on-year changes in benefits and claims and movement in unallocated surplus in each of Prudential's regional operations are changes in the incidence of claims incurred, increases or decreases in policyholders' liabilities, and movements in unallocated surplus of with-profits funds.

Total benefit and claims and movements in unallocated surplus of with-profits funds increased by £16,664 million in 2012 to a charge of £45,953 million compared to a charge of £29,289 million in 2011 and a charge of £40,518 in 2010. The amounts of this year on year charge attributable to each of the underlying reasons as stated above are shown below.

Benefits and claims and movements in unallocated surplus of with-profits funds net of reinsurance can be further analysed as follows.

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Claims incurred	**(19,329)**	(17,736)	(16,884)
Increase in policyholder liabilities	**(25,243)**	(12,578)	(23,389)
Movement in unallocated surplus of with-profits funds	**(1,381)**	1,025	(245)
Benefits and claims and movement in unallocated surplus	**(45,953)**	(29,289)	(40,518)

The charge for benefits and claims and movements in unallocated surplus, net of reinsurance of £45,953 million (2011: £29,289 million; 2010: £40,518 million) shown in the table above includes the effect of accounting for investment contracts without discretionary participation features (as defined by IFRS 4) in accordance with IAS 39 to reflect the deposit nature of the arrangement.

Additionally the movement in policyholder liabilities and unallocated surplus of with-profits funds represents the amount recognised in the income statement and therefore excludes the effect of foreign

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exchange translation differences on the policyholder liabilities of foreign subsidiaries and the movement in liabilities arising on acquisition and disposals of subsidiaries in the year.

The principal driver for variations in amounts allocated to policyholders is changes to investment return reflected in the statement of financial position measurement of liabilities for Prudential's with-profits, SAIF and unit-linked policies (including US separate account business). In addition, for those liabilities under IFRS, in particular, liabilities relating to the UK annuity business (principally PRIL), where the measurement reflects the yields on assets backing the liabilities, the year to year changes in investment yields also contribute significantly to variations in the measurement of policyholder liabilities. The principal driver for variations in the change in unallocated surplus of with-profits funds is the value movements on the investment assets of the with-profits funds to the extent not reflected in policyholder liabilities.

The principal variations are for the increases or decreases in policyholder liabilities and movements in unallocated surplus of with-profits funds for each regional operation are discussed below.

Asia

In 2012, benefits and claims and movements in unallocated surplus of with-profits funds totalled £8,284 million, representing an increase of £2,919 million compared to the charge totalled £5,365 million in 2011. In 2011, benefits and claims and movements in unallocated surplus of with-profits funds totalled £5,365 million, representing a decrease of £1,369 million compared to the charge of £6,734 million in 2010.

The amounts of the year-on-year change attributable to each of the underlying reasons are shown below:

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Claims incurred	**(3,229)**	(2,955)	(2,595)
Increase in policyholder liabilities	**(4,537)**	(2,950)	(3,824)
Movement in unallocated surplus of with-profits funds	**(518)**	540	(315)
Benefits and claims and movement in unallocated surplus	**(8,284)**	(5,365)	(6,734)

The growth in the policyholder liabilities in Asia over the three-year period partially reflected the increase due to the strong growth in new business in the region. The variations in the increases or decreases in policyholder liabilities in individual years were, however, primarily due to movement in investment returns. This was as a result of asset value movements that are reflected in the unit value of the unit-linked policies, which represent a significant proportion of the Asian operations' business. In addition, the policyholder liabilities of the Asia operations' with-profits policies also fluctuated with the investment performance of the funds.

Accordingly, due to the positive market returns in 2012, there was a related increase in the charge for benefits and claims. Conversely, due to the fall in market returns in 2011 compared to 2010, there was a year-on-year related decrease in the charge for benefits and claims.

United States

Except for institutional products and certain term annuities which are classified as investment products under IAS 39 for the purposes of IFRS reporting, deposits into the US operations' products are recorded as premiums, withdrawals and surrenders and are included in benefits and claims, and the resulting net movement is recorded under other reserve movements within benefits and claims.

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Benefits and claims also include interest credited to policyholders in respect of deposit products less fees charged on these policies.

In 2012, the accounting charge for benefits and claims increased by £6,060 million to £18,711 million compared to £12,651 million in 2011. In 2011, the accounting charge for benefits and claims decreased by £2,772 million to £12,651 million compared to £15,423 million in 2010.

The amounts of the year-on-year change attributable to each of the underlying reasons are shown below:

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Claims incurred	**(5,459)**	(4,678)	(4,348)
Increase in policyholder liabilities	**(13,252)**	(7,973)	(11,075)
Benefits and claims	**(18,711)**	(12,651)	(15,423)

The movements year-on-year in the claims incurred for the US operations as shown in the table above also included the effects of translating the US dollar results into pounds sterling at the average exchange rates for the relevant years.

The charges in each year comprise amounts in respect of variable annuity and other business. For variable annuity business, there are two principal factors that contribute to the variations in the charge, and for which the fluctuations in the years presented broadly offset each other. First, the investment return on the assets backing the variable annuity separate account liabilities changed to a £5,217 million credit in 2012 from a £869 million credit in 2011 and a £3,520 million credit in 2010 as shown in the section 'Investment return (b) United States' above. The second principal effect is the growth of the variable annuity business in force. This can be illustrated by the net cash flows of the US insurance operations' variable annuity separate account liabilities in note D3 (c) 'Reconciliation of movement in policyholder liabilities' to the consolidated financial statements in Item 18 of this annual report. The net flows of the variable annuity separate account liabilities shown in that note for 2012 were £7,808 million as compared with £6,978 million for 2011.

United Kingdom

Overall, benefits and claims and the movement in unallocated surplus recorded in the income statement was a charge of £18,958 million in 2012 compared to a £11,273 million charge in 2011 and a £18,361 million charge in 2010. The year-on-year changes attributable to each of the underlying reasons

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are shown below, together with a further analysis of the amounts included in respect of the movements in policyholder liabilities by type of business:

	Year ended 31 December		
	2012	2011	2010
	£m	£m	£m
Claims incurred	**(10,642)**	(10,103)	(9,941)
Decrease/(increase) in policyholder liabilities			
SAIF	**665**	1,198	212
PRIL	**(1,867)**	(1,788)	(2,142)
Unit-linked and other non-participating business	**(2,262)**	(451)	(2,258)
With-profits (excluding SAIF)	**(3,989)**	(614)	(4,301)
	(7,453)	(1,655)	(8,490)
Movement in unallocated surplus of with-profits funds	**(863)**	485	70
Benefits and claims and movement in unallocated surplus	**(18,958)**	(11,273)	(18,361)

Claims incurred in the UK operations in 2012 were £10,642 million, compared to £10,103 million in 2011 and £9,941 million in 2010.

As has been explained above, the principal driver for variations in amounts allocated to the policyholders is changes to investment returns.

In aggregate, as a result of the more positive market returns in 2012 compared to 2011 there has been a corresponding impact on benefits and claims and movements in unallocated surplus of with-profits funds in the year, moving from a net charge of £11,273 million in 2011 to a net charge of £18,958 million in 2012.The market returns in 2010 were also more positive than in 2011, which for similar reasons resulted in a higher net charge of £18,361 million.

SAIF is a ring-fenced fund with no new business written. The decrease in policyholder liabilities in SAIF reflects the underlying decreasing policyholder liabilities as the liabilities run off. The variations from year to year are, however, affected by the market valuation movement of the investments held by SAIF, which are wholly attributable to policyholders.

For PRIL, the increases in policyholder liabilities reflect the effect of altered investment yield reflected in the discount rate applied in the measurement of the liabilities, together with other factors such as changes in premium income for new business and altered assumptions.

For unit-linked business, the variations in the increases in the policyholder liabilities were primarily due to the movement in the market value of the unit-linked assets as reflected in the unit value of the unit-linked policies.

The part of Prudential where variations in amounts attributed to policyholder liabilities and unallocated surplus are most significant is the UK with-profits business (excluding SAIF). As explained in note D2 to the consolidated financial statements in Item 18, the liabilities for UK with-profits policyholders are determined on an asset-share basis that incorporates the accumulation of investment returns and all other items of income and outgo that are relevant to each policy type. Accordingly, the movement in policyholder liabilities in the income statement will fluctuate with the investment return of the fund. Separately, the excess of assets over liabilities of the fund represents the unallocated surplus. This surplus will also fluctuate on a similar basis to the market value movement on the investment assets of the fund with the movement reflected in the income statement. In addition, other items of income and expenditure affect the level of movement in policyholder liabilities (to the extent reflected in assets shares) and unallocated surplus.

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The correlation between total net income (loss) before benefits and claims and movement in unallocated surplus, on the one hand, and the (charge) credit for benefits and claims and movement in unallocated surplus, on the other, for the UK component of the PAC with-profits fund (excluding SAIF) is illustrated numerically by the table below for each of the years presented. In summary, the correlation principally arises due to the following factors:

(a) Investment return is included in full in the income statement and is attributable either to contracts or unallocated surplus.

(b) Investment return, to the extent attributable to contracts, directly affects asset-share liabilities, which are reflected in the income statement through changes in policyholder liabilities.

(c) Investment return, to the extent attributable to unallocated surplus, forms the majority part of the movement in such surplus in the income statement.

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Earned premiums, net of reinsurance[(i)]	**4,558**	3,404	3,148
Investment return	**8,350**	4,094	8,815
Other income	**39**	17	9
Acquisition costs and other expenditure	**(740)**	(696)	(600)
Tax charge	**(292)**	(63)	(528)
Total net income before benefit and claims and movement in unallocated surplus, net of reinsurance	**11,915**	6,756	10,844
Charges of:			
Claims incurred	**(6,857)**	(6,411)	(6,390)
(Increase)/decrease in policyholder liabilities[(i)]	**(3,989)**	(614)	(4,301)
Movement in unallocated surplus of with-profits funds	**(863)**	485	70
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	**(11,709)**	(6,540)	(10,621)
Shareholders' profit after tax	**206**	216	223

Note

(i) For the purposes of presentation in Prudential's consolidated financial information, references to the UK with-profits fund also include, for convenience, the amounts attaching to Prudential's UK Defined Charge Participating Sub-fund which includes the with-profits annuity business transferred to Prudential from the Equitable Life Assurance Society on 31 December 2007. Profits to shareholders emerge on a 'charges less expenses' basis and policyholders are entitled to 100 per cent of the investment earnings.

Separately, the cost of current year bonuses which is attributable to policyholders is booked within the movement in policyholder liabilities. One-ninth of the declared cost of policyholders' bonus is attributable to shareholders and represents the shareholders' profit. Both of these amounts, by comparison with the investment return, movement in other constituent elements of the change in policyholder liabilities and the change in unallocated surplus, are relatively stable from period to period.

In 2012, the income statement of the UK component of the PAC with-profits funds was charged with a transfer of £863 million from the unallocated surplus. This transfer, together with a corresponding transfer in the unallocated surplus of the Asia with-profits funds and the effect of exchange rate movements, resulted in an increase in Prudential's unallocated surplus from £9.2 billion in 2011 to £10.6 billion in 2012. This movement reflected the net effect of changes in the value of assets, liabilities (incorporating policyholder bonuses and other elements of asset shares attributable to policyholders), and the shareholders' share of the cost of bonuses for 2012.

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In 2011, the income statement of the UK component of the PAC with-profits funds was credited with a transfer of £485 million from the unallocated surplus. This transfer, together with a corresponding transfer in the unallocated surplus of the Asia with-profits funds and the effect of exchange rate movements, resulted in an increase in Prudential's unallocated surplus from £10.3 billion in 2010 to £9.2 billion in 2011. This movement reflected the net effect of changes in the value of assets, liabilities (incorporating policyholder bonuses and other elements of asset shares attributable to policyholders), and the shareholders' share of the cost of bonuses for 2011.

The surplus for distribution in future years will reflect the aggregate of policyholder bonuses and the cost of bonuses attributable to shareholders, which is currently set at 10 per cent. The policyholder bonuses comprise the aggregate of regular and final bonuses. When determining policy payouts, including final bonuses, Prudential considers asset shares of specimen policies.

Prudential does not take into account the surplus assets of the long-term fund, or the investment return, in calculating asset shares. Asset-shares are used in the determination of final bonuses, together with treating customers fairly, the need to smooth claim values and payments from year to year and competitive considerations.

In the unlikely circumstance that the depletion of excess assets within the long-term fund was such that Prudential's ability to treat its customers fairly was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

The factors that the PAC Board considers in setting bonus rates are described in more detail in the section headed 'With-profits products' in Item 4, in the section headed 'United Kingdom Basis of profits Bonus Rates' in Item 5 and are summarised in note D2 to the consolidated financial statements in Item 18.

(d) Acquisition costs and other expenditure

	Year ended 31 December		
	2012	**2011**	**2010**
	£m	**£m**	**£m**
Asia operations	**(2,172)**	(1,774)	(1,851)
US operations	**(1,771)**	(1,445)	(1,151)
UK operations	**(2,164)**	(1,943)	(1,721)
Unallocated corporate and intra-group elimination	**52**	42	(266)
Total	**(6,055)**	(5,120)	(4,989)

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

Total acquisition costs and other expenditure of £(6,055) million in 2012 were 18 per cent higher than the £(5,120) million incurred in 2011. Total acquisition costs and other expenditure of £(5,120) million in 2011 were 3 per cent higher than the £(4,989) million incurred in 2010.

Asia

Total acquisition costs and other expenditure for Asia in 2012 were £(2,172) million, an increase of £398 million or 22 per cent over 2011. This increase was primarily due to increased acquisition costs, net of change in deferred acquisition costs and increases in other operating expenses and in the charge for investment gains attributable to external unit-holders relating to investment funds managed on behalf of third parties which are consolidated but have no recourse to Prudential.

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Total acquisition costs and other expenditure for Asia in 2011 were £(1,774) million, a decrease of £77 million or 4 per cent as against 2010. This decrease was primarily due to increased acquisition costs, net of change in deferred acquisition costs being more than offset by decreased other operating expenses and a decrease in the charge for investment gains attributable to external unit-holders relating to investment funds managed on behalf of third parties which are consolidated but have no recourse to Prudential.

United States

Total acquisition costs and other expenditure for the US of £(1,771) million in 2012 represented an increase of £326 million over the amount of £(1,445) million in 2011. The £(1,445) million in 2011 in turn represented an increase of £294 million from the £(1,151) million in 2010. The year on year movements reflected increases in acquisition costs, net of change in deferred acquisition costs and in operating expenses.

Acquisition costs increased in absolute terms year on year over the three year period due largely to increases in sales volume. The DAC amortisation charge to the operating profit based on longer term investment returns for the US decreased in 2012 to £(356) million from £(506) million in 2011. From 2010 to 2011, the DAC amortisation charge for the US increased to £(506) million from £(280) million. The 2012 DAC amortisation comprises a core charge of £(412) million (2011: £(316) million; 2010: £(271) million) and a decelerated charge of £56 million (2011: accelerated charge of £(190) million; 2010: accelerated charge of £(9) million). The higher core charge year on year is in line with the increase in fee income and spread profits. The £(190) million accelerated charge in 2011 represented the reversal of the benefit received in 2008 from the use of the mean reversion formula.

Other operating expenses increased primarily due to higher asset based commissions paid on the growing separate account balance.

United Kingdom

Total UK acquisition costs and other expenditure were £(2,164) million compared to £(1,943) million in 2011. The increase of £221 million primarily reflects increased operating expenses which were partially offset by the positive impact of the partial recognition of the defined benefit pension scheme actuarial surplus of PSPS in 2012 of £164 million of which £115 million was allocated to the PAC with-profits fund included within the UK operations. Further detail is provided in note I3 to the consolidated financial statements in Item 18.

Total UK acquisition costs and other expenditure were £(1,943) million in 2011 compared to £(1,721) million in 2010. This increase arose primarily from the increase in acquisition costs, net of change in deferred acquisition costs and underlying increases in expenditure of M&G.

Unallocated corporate and intra-group elimination

Other net expenditure of a credit of £52 million in 2012, a credit of £42 million in 2011 and a charge of £(266) million in 2010 comprises both the other expenditure of the unallocated corporate and elimination of intragroup income and expenses. The principal reason for the year on year movement as shown above was that the amount in 2010 included the costs incurred in relation to the terminated AIA transaction. Of the £377 million total costs before tax of the terminated AIA transaction in 2010, £277 million was recorded as 'Other expenditure' within 'Acquisition costs and other expenditure' in the consolidated income statement. The remaining £100 million associated with foreign exchange hedging was recorded within 'Investment return'.

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IFRS Shareholders' Funds and Summary Balance Sheet

The following table sets forth a summary of the movement in Prudential's IFRS shareholders' funds for 2012, 2011 and 2010:

	IFRS		
	2012	**2011***	**2010***
	£m	**£m**	**£m**
Operating profit based on longer-term investment returns	**2,533**	2,027	1,826
Items excluded from operating profit	**277**	(199)	(555)
Total profit before tax	**2,810**	1,828	1,271
Exceptional Tax Credit			158
Tax and non-controlling interests	**(613)**	(413)	(123)
Profit for the year	**2,197**	1,415	1,306
Exchange movements, net of related tax	**(216)**	(105)	237
Unrealised gains and losses on Jackson securities classified as available for sale, net of related changes to deferred acquisition costs and tax	**387**	349	533
Dividends	**(655)**	(642)	(511)
New share capital subscribed	**17**	17	75
Other	**65**	9	36
Net increase in shareholders' funds	**1,795**	1,043	1,676
Shareholders' funds at beginning of the year	**8,564**	7,521	5,845
Shareholders' funds at end of the year	**10,359**	8,564	7,521

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

Summary Balance Sheet

	31 December	
	2012	**2011***
	£m	**£m**
Goodwill attributable to shareholders	**1,469**	1,465
Investments	**283,428**	250,605
Holding company cash and short-term investments	**1,380**	1,200
Other	**23,976**	19,475
Total assets	**310,253**	272,745
Less: Liabilities		
Policyholder liabilities	**260,774**	227,075
Unallocated surplus of with-profits funds	**10,589**	9,215

	271,363	236,290
Core structural borrowings of shareholders' financed operations	**3,554**	3,611
Other liabilities including non-controlling interest	**24,977**	24,280
Total liabilities and non-controlling interest	**287,810**	253,108
Share capital and premium	**2,017**	2,000
IFRS basis shareholders' reserves	**8,342**	6,564
IFRS basis shareholders' equity	**10,359**	8,564

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5 to Prudential's consolidated financial statements in Item 18.

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Policyholder liabilities and unallocated surplus of with-profits fund

Shareholder-backed business	Asia	US	UK	2012 Total	2011 Total
	£m	£m	£m	£m	£m
At 1 January	18,269	69,189	46,048	**133,506**	122,183
Premiums	4,141	14,907	3,801	**22,849**	20,296
Surrenders	(1,933)	(4,356)	(2,585)	**(8,874)**	(7,975)
Maturities/Deaths	(226)	(954)	(2,345)	**(3,525)**	(3,315)
Net cash flows	1,982	9,597	(1,129)	**10,450**	9,006
Investment related-items and other movements	1,539	4,241	4,586	**10,366**	1,988
Acquisition of REALIC		12,912		**12,912**	
Foreign exchange translation differences	(577)	(3,678)		**(4,255)**	329
At 31 December	21,213	92,261	49,505	**162,979**	133,506
With-profits funds					
Policyholder liabilities				**97,795**	93,569
Unallocated surplus				**10,589**	9,215
Total at 31 December				**108,384**	102,784
Total policyholder liabilities including unallocated surplus at 31 December				**271,363**	236,290

Policyholder liabilities relating to shareholder-backed business grew by £29.5 billion from £133.5 billion at 31 December 2011 to £163.0 billion at 31 December 2012.

The increase reflects positive net flows (premiums net of upfront charges less surrenders, maturities and deaths) of £10.5 billion in 2012 (2011: £9.0 billion), driven by strong inflows in the US £9.6 billion and Asia £2.0 billion. The negative net flows in UK of £1.1 billion are distorted by the fluctuating nature of unit-linked corporate pension scheme transfers. Net flows in Asia have increased by 8 per cent to £2.0 billion in 2012 (2011: £1.8 billion) while the overall rate of surrenders in the region (expressed as a percentage of opening liabilities) was 10.6 per cent in 2012 (2011: 9.8 per cent). Excluding India, where the market has been going through a significant period of change following regulatory changes in 2010, the surrender rate in 2012 was 9.7 per cent (2011: 9.6 per cent).

Other movements include negative foreign exchange effects of £4.3 billion (2011: positive £0.3 billion) together with investment-related and other items of £10.4 billion. Investment-related and other items increased from £2.0 billion in 2011 to £10.4 billion in 2012 principally following improvements in the bond and equity markets. The acquisition of REALIC reflects the liabilities acquired at the date of acquisition.

During 2012, the unallocated surplus, which represents the excess of assets over policyholder liabilities for the Group's with-profits funds on an IFRS basis, increased by 15 per cent from £9.2 billion at 31 December 2011 to £10.6 billion at 31 December 2012.

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Other results based information

Funds under Management

(a) Summary

	2012	2011
	£bn	£bn
Business area:		
Asia operations	**38.9**	32.6
US operations	**91.4**	71.9
UK operations	**153.3**	146.3
Internal funds under management	**283.6**	250.8
External funds[(i)]	**121.4**	99.8
Total funds under management	**405.0**	350.6

Note

(i) External funds shown above for 2012 of £121.4 billion (2011: £99.8 billion) comprise £133.5 billion (2011: £111.2 billion) of funds managed by Eastspring Investments and M&G (as shown in note (c) below) less £12.1 billion (2011: £11.4 billion) that are classified within internal funds.

(b) Internal funds under management analysis by business area

	Asian operations		US operations		UK operations		Total	
	2012	2011	2012	2011	2012	2011	2012	2011
	£bn	£bn	£bn	£bn	£bn	£bn	£bn	£bn
Investment properties[(i)]			**0.1**	0.1	**11.0**	10.9	**11.1**	11.0
Equity securities	**14.3**	12.0	**49.6**	38.1	**36.1**	37.3	**100.0**	87.4
Debt securities	**21.4**	17.7	**33.0**	27.0	**85.7**	79.8	**140.1**	124.5
Loans and receivables	**1.0**	1.2	**6.2**	4.1	**4.6**	4.4	**11.8**	9.7
Other investments and deposits	**2.2**	1.7	**2.5**	2.6	**15.9**	13.9	**20.6**	18.2
Total	**38.9**	32.6	**91.4**	71.9	**153.3**	146.3	**283.6**	250.8

Note

(i)

As included in the investments section of the consolidated statement of financial position at 31 December 2012 except for £0.2 billion (2011: £0.2 billion) investment properties which are held for sale or occupied by the Group and, accordingly under IFRS, are included in other statement of financial position captions.

(c) Investment products funds under management

	2012				
	1 Jan 2012	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2012
	£m	£m	£m	£m	£m
Eastspring Investments	19,221	60,498	(59,098)	1,013	21,634
M&G	91,948	36,463	(19,582)	3,039	111,868
Group total	111,169	96,961	(78,680)	4,052	133,502

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	2011				
	1 Jan 2011	Market gross inflows	Redemptions	Market exchange translation and other movements	31 Dec 2011
	£m	£m	£m	£m	£m
Eastspring Investments	22,048	63,726	(63,605)	(2,948)	19,221
M&G	89,326	25,981	(21,596)	(1,763)	91,948
Group total	111,374	89,707	(85,201)	(4,711)	111,169

Liquidity and Capital Resources

Prudential Capital operates a central treasury function for Prudential, which has overall responsibility for managing Prudential's capital funding program as well as its central cash and liquidity positions. Prudential arranges the financing of each of its subsidiaries primarily by raising external finance either at the parent company level (including through finance subsidiaries whose obligations the parent company guarantees) or at the operating company level.

After making enquiries the directors of Prudential have a reasonable expectation that the Company and the Group have adequate resources to continue their operations for the foreseeable future.

Group and holding company cash flow

Prudential's consolidated cash flow includes the movement in cash included within both policyholders' and shareholders' funds, such as cash in the with-profits fund. Prudential therefore believes that it is more relevant to consider individual components of the movement in holding company cash flow which relate solely to the shareholders.

Prudential continues to manage cash flows across the Group with a view to achieving a balance between ensuring sufficient net remittances from the businesses to cover the progressive dividend (after corporate costs) and maximising value for shareholders through the retention of the free surplus generated at business unit level, so that it can be reinvested in the profitable opportunities available to the Group. On this basis, the holding company cash flow statement at an operating level should ordinarily balance close to zero before exceptional cash flows, but from time to time additional remittances from business operations will be made to provide the Group with greater financial flexibility at the corporate centre.

Operating holding company cash flow for 2012 before the shareholder dividend was £911 million, £102 million higher than 2011. After deducting the shareholder dividend the operating holding company cash flow was £256 million (2011: £167 million).

Cash remittances to the Group from business units

The holding company received £1,200 million of net cash remittances from the business units in 2012, an increase of 9 per cent over the £1,105 million received in 2011.

Asia became the largest contributor of cash, with net cash remittances to the Group in 2012 of £341 million (2011: £206 million) exceeding its 2013 cash objective. This includes non-recurring items of £27 million representing cash received from the sale of the Group's holdings in China Life Insurance Company in Taiwan of £97 million offset by repayments of funding contingent on future profits of the Hong Kong Life

insurance operations of £70 million. This financing was taken out in 2009 and 2010 in order to increase the financial flexibility of the Group during the investment market crisis and has now been repaid.

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Cash received from Jackson of £249 million for 2012 is lower than the £322 million remitted in 2011 as annual remittances return to a more sustainable level. This follows the exceptional release of excess surplus made in the prior year.

The UK insurance operations remitted £313 million in 2012 (2011: £297 million). Cash from the annual with-profits transfer to shareholders contributed £216 million (2011: £223 million). During 2012, surpluses in the UK's shareholder-backed business were utilised to repay £60 million of funding contingent on future profits that was taken out in 2009 and 2010 and to remit a net £97 million (2011: £74 million) to Group. The UK's objective remains £350 million of net cash remittances in 2013.

M&G and PruCap collectively remitted £297 million in 2012, as the asset management businesses continue to remit significant portions of their annual post-tax earnings to the Group.

Net central outflows and other movements

Net central outflows improved to £289 million in 2012 (2011: £296 million) with higher corporate costs offset by lower net interest payments, lower Solvency II costs, and higher tax receipts.

After central costs, there was a net cash inflow before dividend of £911 million in 2012 compared to £809 million in 2011. The dividend paid was £655 million in 2012 compared to £642 million in the same period in 2011.

Outside of the normal recurring central cash flow items and in light of the heightened risks surrounding the Eurozone, we incurred a net cash flow of £32 million for short dated hedges to provide downside protection against severe equity market falls. We also incurred £43 million of other net cash payments in 2012, representing payments of £68 million to the UK tax authorities following the settlement reached in 2010 on historic tax issues offset by a receipt of £25 million from an increased bank loan in the year. A final instalment on the agreed settlement will be paid in 2013 to the UK tax authorities at a level similar to 2012.

The overall holding company cash and short-term investment balances at 31 December 2012 was £180 million higher than the balance held at the end of 2011 at £1.4 billion. The company seeks to maintain a central cash balance in excess of £1 billion.

Dividend payments

The total cost of dividends settled by Prudential were £655 million and £642 million for the years ended 31 December 2012 and 2011, respectively.

The Board has decided to rebase the full year dividend upwards by 4 pence, reflecting the strong progress made in both the earnings and free surplus generation of the business and in the delivery of its financial objectives. In line with this, the directors recommend a final dividend of 20.79 pence per share (2011: 17.24 pence), which brings the total dividend for the year to 29.19 pence (2011: 25.19 pence), representing an increase of 15.9 per cent over 2011.

Debt service costs

Debt service costs charged to profit in respect of core borrowings paid by Prudential in 2012 were £280 million compared with £286 million in 2011. Of total consolidated borrowings of £6,832 million as at 31 December 2012, the parent company had core borrowings of £3,126 million outstanding, all of which have contractual maturity dates of more than five years.

Liquidity sources

The holding company held cash and short-term investments of £1,380 million, £1,200 million and £1,232 million as at 31 December 2012, 2011 and 2010, respectively. The sources of cash in 2012

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included dividends, loans and interest received from operating subsidiaries. Prudential received £1,414 million in cash remittances from business units in 2012, compared to £1,285 million received in 2011 and £1,122 million received in 2010. These remittances primarily comprise dividends from business units and the shareholders' statutory transfer from the PAC long-term with-profits fund (UK Life Fund) relating to earlier bonus declarations. Offset against these cash remittances were £214 million, £180 million and £187 million of capital invested in 2012, 2011 and 2010 respectively. Overall net remittances from business units had increased from £1,105 million in 2011 to £1,200 million in 2012.

Shareholders' statutory transfer

In 2012, PAC declared a total surplus of £2,210 million from PAC's primary with-profits sub-fund, of which £1,990 million was added to with-profits policies and £220 million was distributed to shareholders. In 2011, PAC declared a total surplus of £2,293 million from PAC's primary with-profits sub-fund, of which £2,064 million was added to with-profits policies and £229 million was distributed to shareholders. In 2010, PAC declared a total surplus of £2,367 million from PAC's primary with-profits sub-fund, of which £2,131 million was added to with-profits policies and £236 million was distributed to shareholders.

Dividends, loans and interest received from subsidiaries

Under UK company law, dividends can only be paid if a company has distributable reserves sufficient to cover the dividend. In PAC, Prudential's largest operating subsidiary, distributable reserves are created mainly by the statutory long-term business profit transfer to shareholders that occurs upon the declaration of bonuses to policyholders of with profit products. See 'Shareholders' statutory transfer' above. Prudential's insurance and fund management subsidiaries' ability to pay dividends and loans to the parent company is restricted by various laws and regulations. Jackson is subject to state laws that limit the dividends payable to its parent company. Dividends in excess of these limitations generally require approval of the state insurance commissioner. The table below shows the dividends, loans and other amounts received by Prudential from the principal operating subsidiaries for 2012 and 2011:

	Dividends, loan and interest received in:	
	2012	**2011**
	£m	**£m**
Asia operations	**551**	344
US operations	**249**	322
UK Insurance operations (mainly PAC)	**317**	339
M&G (including Prudential Capital)	**297**	280
Total	**1,414**	1,285

Each of Prudential's main operations generates sufficient profits to pay dividends to the parent. The amount of dividends paid by the operations is determined after considering the development, growth and investment requirements of the operating businesses. Prudential does not believe that the legal and regulatory restrictions on the ability of any one of its businesses to pay dividends to the parent, constitutes a material limitation on the ability of Prudential plc to meet its cash obligations.

Changes to Group's holdings during the period

On 5 November 2012, Prudential plc , through its subsidiary Prudential Life Assurance (Thailand) Public Company Limited ('Prudential Thailand') entered into an agreement to acquire 100 per cent of Thanachart Life Assurance Company Limited ('Thanachart Life'), a wholly-owned life insurance subsidiary of Thanachart Bank Public Company limited ('Thanachart Bank'). The transaction was approved by the regulator in March 2013 and is expected to close in the second quarter of 2013.

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On 4 September 2012, the Group through its indirect wholly-owned subsidiary, Jackson National Life Insurance Company (JNLI) completed the acquisition of 100 per cent issued share capital of SRLC America Holding Corp. (SRLC), and its primary operating subsidiary, Reassure America Life Insurance Company (REALIC) for purchase consideration estimated at that time of £417 million (US$663 million). Subsequent adjustments have reduced the purchase price to £370 million (US$587 million), which remain subject to final agreement under the terms of the transaction with Swiss Re. The acquisition increases the scale of the Group's life business in the US, helping Jackson to diversify earnings by increasing the amount of income from underwriting activities thereby enhancing the quality of earnings in a capital efficient manner.

On 22 February 2012, M&G completed transactions to (i) exchange bonus share rights for equity holdings with the employees of PPM South Africa and (ii) the sale of a 10 per cent holding in the majority of the business to Thesele Group, a minority shareholder, for cash. Following these transactions M&G's majority holding in the business reduced from 75 per cent to 49.99 per cent. Under IFRS requirements, the divestment is accounted for as the disposal of the 75 per cent holding and an acquisition of a 49.99 per cent holding at fair value resulting in a reclassification of PPM South Africa from a subsidiary to an associate.

During 2010 Prudential completed the acquisition of UOB Life for total cash consideration, of SGD 495 million (£220 million), giving rise to goodwill of £141 million. This acquisition accompanied a long-term strategic partnership with UOB facilitating distribution of Prudential's life insurance products through UOB's bank branches in Singapore, Indonesia and Thailand.

In 2010, Prudential also announced the acquisition of Standard Life Healthcare by its PruHealth joint venture partner Discovery and its combination with the existing PruHealth business. This led to a reduction in its shareholding in the enlarged combined businesses from 50 per cent to 25 per cent effective from 1 August, the date of the acquisition.

Shareholders' net borrowings

	31 December	
	2012	**2011**
	£m	**£m**
Perpetual subordinated Capital securities (Innovative Tier 1)	**1,746**	1,823
Subordinated notes (Lower Tier 2)	**831**	829
	2,577	2,652
Senior debt:		
2023	**300**	300
2029	**249**	249
Holding company total	**3,126**	3,201
Prudential Capital	**275**	250
Jackson surplus notes (Lower Tier 2)	**153**	160
Total	**3,554**	3,611
Less: Holding company cash and short-term investments	**(1,380)**	(1,200)
Net core structural borrowings of shareholder-financed operations	**2,174**	2,411

On an IFRS basis, the Group's core structural borrowings at 31 December 2012 were broadly unchanged at £3.6 billion.

After adjusting for holding company cash and short-term investments of £1,380 million, net core structural borrowings at 31 December 2012 were £2,174 million compared with £2,411 million at 31 December 2011. The decrease of £237 million represents the net fall in borrowings of £57 million,

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mainly reflecting the foreign exchange movements in the year, together with a £180 million rise in holding company cash and short-term investments.

In addition to its core structural borrowings set out above, Prudential also has in place an unlimited global commercial paper programme. As at 31 December 2012, commercial paper issued under this programme totalled £183 million, US$1,512 million, €493 million, CHF20 million and AU$12 million. The central treasury function also manages our £5 billion medium-term note (MTN) programme, covering both core and non-core borrowings. In November 2012 Prudential issued a £300 million 3-year senior note to pre-finance a £250 million senior note maturing in January 2013 for operational funding. Also in January 2013 Prudential issued a new US$700 million 5.25 per cent perpetual Innovative Tier 1 hybrid under this programme, primarily to Asian retail investors. Under the MTN programme at 31 December 2012 the outstanding subordinated debt was £835 million, US$1,300 million and €20 million and the senior debt outstanding was £550 million. In addition, Prudential's holding company has access to £2.1 billion of syndicated and bilateral committed revolving credit facilities, provided by 17 major international banks, expiring between 2013 and 2017. Apart from small draw downs to test the process, these facilities have never been drawn, and there were no amounts outstanding at 31 December 2012. The commercial paper programme, the MTN programme and the committed revolving credit facilities are all available for general corporate purposes and to support the liquidity needs of Prudential's holding company and are intended to maintain a strong and flexible funding capacity.

Prudential manages the Group's core debt within a target level consistent with its current debt ratings. At 31 December 2012, the gearing ratio (debt, net of cash and short-term investments, as a proportion of EEV shareholders' funds plus net debt) was 8.8 per cent, compared with 10.9 per cent at 31 December 2011. Prudential plc has strong debt ratings from Standard & Poor's, Moody's and Fitch. Prudential's long-term senior debt is rated A+, A2 and A from Standard & Poor's, Moody's and Fitch, while short-term ratings are A-1, P-1 and F1 respectively. All long-term ratings from Fitch and Moody's are on stable outlook, and all long-term ratings from S&P are on negative outlook.

The financial strength of PAC is rated AA by Standard & Poor's, Aa2 by Moody's and AA by Fitch.

Jackson National Life Insurance Company's financial strength is rated AA by Standard & Poor's, A1 by Moody's and AA by Fitch.

Operating businesses

UK life insurance

The liquidity sources for Prudential's UK life insurance businesses comprise premiums, deposits and charges on policies, investment income, proceeds from the sale and maturity of investments, external borrowings and capital contributions from the parent company. The liquidity requirements comprise benefits and claims, operating expenses, interest on debt, purchases of investments and dividends to the parent company.

The liquidity requirements of Prudential's UK life insurance businesses are regularly monitored to match anticipated cash inflows with cash requirements. Cash needs are forecast and projected sources and uses of funds, as well as the asset, liability, investment and cash flow assumptions underlying these projections are reviewed periodically. Adjustments are made periodically to the investment policies with respect to, among other things, the maturity and risk characteristics of the investment assets to reflect changes in the business' cash needs and also to reflect the changing competitive and economic environment.

The liquidity of Prudential's UK insurance operations is affected by the payment of guaranteed benefits and terminal bonuses on maturing and surrendering policies by the UK insurance operations. In addition, the non-cash bonus declaration to policyholders results in a cash transfer to shareholders'

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funds. A large proportion of Prudential's liabilities contains discretionary surrender values or surrender charges. In addition, pension annuity policies cannot be surrendered by the policyholder.

As at 31 December 2012, 2011 and 2010, PAC's long-term fund assets in excess of its minimum capital requirements were £17,936 million, £16,674 million and £17,406 million, respectively. The 'with-profits insurance capital component' of the enhanced capital requirement, as at 31 December 2012, 2011 and 2010 amounted to £9,249 million, £9,674 million and £9,089 million respectively.

M&G

The principal liquidity source for M&G is fee income for managing retail, institutional and the internal investment funds of Prudential's UK operations. The principal liquidity requirements are for operating expenses. Amounts are distributed to the parent company after considering capital requirements. Capital requirements are driven by fixed operating expenses and various risks faced by the company. As at 31 December 2012, M&G met the relevant regulatory requirements.

US life insurance

The liquidity sources for Jackson are its cash, short-term investments and publicly traded bonds, premium income deposits received on certain annuity and institutional products, investment income, reverse repurchase agreements, utilisation of a short-term borrowing facility with the Federal Home Loan Bank of Indianapolis and capital contributions from the parent company.

Liquidity requirements are principally for purchases of new investments and businesses, repayment of principal and interest on debt, payments of interest on surplus notes, funding of insurance product liabilities including payments for policy benefits, surrenders, maturities and new policy loans, and funding of expenses including payment of commissions operating expenses and taxes. As at 31 December 2012, Jackson's outstanding notes and bank debt included:

US$30 million of collateralised loans maturing through 2016,

US$3 million of non-investment grade debt issued by variable interest entities maturing in 2016,

US$10 million of mortgage loans collaterised by real estate from the Federal Home Loan Bank of Indianapolis,

US$250 million of surplus notes maturing in 2027.

Significant increases in interest rates and disintermediation can create sudden increases in surrender and withdrawal requests by policyholders and contract holders. Other factors that are not directly related to interest rates can also give rise to disintermediation risk, including but not limited to changes in ratings from rating agencies, general policyholder concerns relating to the life insurance industry (eg the unexpected default of a large, unrelated life insurer) and competition from other products, including non-insurance products such as mutual funds, certificates of deposit and newly developed investment products. Most of the life insurance, annuity and institutional products Jackson offers permit the policyholder or contract holder to withdraw or borrow funds or surrender cash values. At 31 December 2012, a majority of Jackson's fixed annuity reserves include policy restrictions such as surrender charges and market value adjustments to discourage early withdrawal of policy and contract funds.

Jackson uses a variety of asset-liability management techniques to provide for the orderly provision of cash flow from investments and other sources as policies and contracts mature in accordance with their normal terms. Jackson's principal sources of liquidity to meet unexpected cash outflows associated with sudden and severe increases in surrenders and withdrawals are its portfolio of liquid assets and its net operating cash flows. As at 31 December 2012, the portfolio of cash, short-term investments and

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publicly traded bonds and equities amounted to US$46 billion. Operating net cash inflows for Jackson in 2012 were US$2.0 billion.

As at 31 December 2012, the statutory capital and surplus of Jackson was US$4.3 billion, which was in excess of the requirements set out under Michigan insurance law. Jackson is also subject to risk-based capital guidelines that provide a method to measure the adjusted capital that a life insurance company should have for regulatory purposes, taking into account the risk characteristics of Jackson's investments and products. As at 31 December 2012, Jackson's total risk based capital ratio under the National Association of Insurance Commissioners' definition exceeded the Michigan standards.

Asia life insurance

The liquidity sources for Prudential's Asia life insurance businesses comprise premiums, deposits and charges on policies, investment income, proceeds from the sale and maturity of investments, external borrowings and capital contributions from the parent company. The liquidity requirements comprise benefits and claims, operating expenses, interest on debt, purchases of investments and dividends to the parent company.

The liquidity requirements of Prudential's Asia life insurance businesses are regularly monitored to match anticipated cash inflows with cash requirements. Cash needs are forecast and projected sources and uses of funds, as well as the asset, liability, investment and cash flow assumptions underlying these projections are reviewed periodically. Adjustments are made periodically to the investment policies with respect to, among other things, the maturity and risk characteristics of the investment assets to reflect changes in the business cash needs and also to reflect the changing competitive and economic environment.

Derivative financial instruments and commitments

The Group enters into a variety of exchange traded and over-the-counter derivative financial instruments, including futures, options, forward currency contracts and swaps such as interest rate swaps, cross-currency swaps, swaptions and credit default swaps.

All over-the-counter derivative transactions, with the exception of some Asia transactions, are conducted under standardised ISDA (International Swaps and Derivatives Association Inc) master agreements and the Group has collateral agreements between the individual Group entities and relevant counterparties in place under each of these market master agreements.

These derivatives are used for efficient portfolio management to obtain cost effective and efficient exposure to various markets in accordance with the Group's investment strategies and to manage exposure to interest rate, currency, credit and other business risks.

The Group uses various interest rate derivative instruments such as interest rate swaps to reduce exposure to interest rate volatility.

The UK with-profits funds use derivatives for the purposes of efficient portfolio management or reduction in investment risks. For UK annuity business derivatives are used to assist with asset and liability cash flow matching.

Some of the Group's products, especially those sold in the US, have certain guarantee features linked to equity indexes. A mismatch between guaranteed product liabilities and the performance of the underlying assets backing them, exposes the Group to equity index risk. In order to mitigate this risk, the relevant business units purchase swaptions, equity options and futures to match asset performance with liabilities under equity-indexed products.

The US operations and some of the UK operations hold large amounts of interest-rate sensitive investments that contain credit risks on which a certain level of defaults is expected. These entities have

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purchased some swaptions in order to manage the default risk on certain underlying assets and hence reduce the amount of regulatory capital held to support the assets.

The types of derivatives used by Jackson and their purpose are as follows:

- Interest rate swaps generally involve the exchange of fixed and floating payments over the period for which Jackson holds the instrument without an exchange of the underlying principal amount. These agreements are used for hedging purposes;

- Put-swaption contracts provide the purchaser with the right, but not the obligation, to require the writer to pay the present value of a long-duration interest rate swap at future exercise dates. Jackson purchases and writes put-swaptions with maturities up to 10 years. Put-swaptions hedge against significant movements in interest rates;

- Equity index futures contracts and equity index options (including various call, put options and put spreads) are used to hedge Jackson's obligations associated with its issuance of fixed indexed immediate and deferred annuities and certain VA guarantees. These annuities and guarantees contain embedded options which are fair valued for financial reporting purposes;

- Total return swaps in which Jackson receives equity returns or returns based on reference pools of assets in exchange for short-term floating rate payments based on notional amounts, are held for both hedging and investment purposes;

- Cross-currency swaps, which embody spot and forward currency swaps and additionally, in some cases, interest rate swaps and equity index swaps, are entered into for the purpose of hedging Jackson's foreign currency denominated funding agreements supporting trust instrument obligations; and

- Credit default swaps, represent agreements under which Jackson has purchased default protection on certain underlying corporate bonds held in its portfolio. These contracts allow Jackson to sell the protected bonds at par value to the counterparty if a default event occurs in exchange for periodic payments made by Jackson for the life of the agreement. Jackson does not write default protection using credit derivatives.

The Group has provided, from time to time, certain guarantees and commitments to third-parties including funding the purchase or development of land and buildings and other related matters. The contractual obligations to purchase or develop investment properties at 31 December 2012 were £5 million (2011: £9 million; 2010: £28 million).

At 31 December 2012, Jackson has unfunded commitments of £325 million (2011: £341 million) related to its investments in limited partnerships and of £86 million (2011: £77 million) related to commercial mortgage loans. These commitments were entered into in the normal course of business and the directors do not expect a material adverse impact on the operations to arise from them.

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Contractual obligations

Contractual obligations with specified payment dates as at 31 December 2012 were as follows:

	Total	Less than 1 year	1 3 years	3 5 years	More than 5 years
	£m	£m	£m	£m	£m
Policyholder liabilities[(i)]	**398,186**	**23,375**	**47,404**	**44,884**	**282,523**
Long-term debt[(ii)]	**3,654**	**160**	**115**		**3,379**
Other borrowings[(ii)]	**3,178**	**2,208**	**521**	**117**	**332**
Capital lease obligations	**111**	**6**	**10**	**9**	**86**
Operating lease obligations	**389**	**74**	**100**	**99**	**116**
Purchase obligations[(iii)]	**416**	**416**			
Obligations under funding, securities lending and sale and repurchase agreements	**2,436**	**2,436**			
Other long-term liabilities[(iv)]	**4,865**	**4,571**	**209**	**43**	**42**
Total	**413,235**	**33,246**	**48,359**	**45,152**	**286,478**

	£m	£m
Reconciliation to consolidated statement of financial position:		
Total contractual obligations per above		413,235
Difference between policyholder liabilities per above (based on undiscounted cash flows) and total policyholder liabilities and unallocated surplus of with-profits funds per balance sheet:		
Total policyholder liabilities and unallocated surplus of with-profits funds per the consolidated statement of financial position	271,363	
Policyholder liabilities (undiscounted) per above	(398,186)	(126,823)
Other short-term/non-contractual obligations:		
Current tax liabilities	445	
Deferred tax liabilities	3,970	
Accruals and deferred income	833	
Other creditors (excluding capital and operating lease obligations and purchase obligations)	1,865	
Derivative liabilities	2,829	
Other liabilities	3,454	13,396
Other items		81
Total liabilities per consolidated statement of financial position		299,889

Notes

(i) Amounts shown in respect of policyholder liabilities represent estimated undiscounted cash flows for Prudential's life assurance contracts. In determining the projected payments, account has been taken of the contract features, in particular that the amount and timing of policyholder benefit payments reflect either surrender, death, or contract maturity. In addition, the undiscounted amounts shown include the expected payments based on assumed future investment returns on assets backing policyholder liabilities. The projected

cash flows exclude the unallocated surplus of with-profits funds. As at 31 December 2012, on the IFRS basis of reporting, the unallocated surplus was £10,589 million. The unallocated surplus represents the excess of assets over liabilities, including policyholder 'asset share' liabilities, which reflect the amount payable under the realistic Peak 2 reporting regime of the FSA. Although accounted for as a liability, as permitted by IFRS 4, there is currently no expected payment date for the unallocated surplus.

(ii)

The amounts represent the contractual maturity of amounts of borrowings included in the consolidated statement of financial position (i.e. excludes future interest payments) as shown in note H13 to Prudential's consolidated financial statements in

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Item 18. Long-term debt comprises the core structural borrowings of shareholder-financed operations and the £100 million 8.5 per cent undated subordinated guaranteed bonds of Scottish Amicable Finance plc. Other borrowings comprise operational borrowings attributable to shareholder-financed operations and borrowings attributable to with-profits operations but excluding the £100 million 8.5 per cent undated subordinated guaranteed bonds of Scottish Amicable Finance plc.

(iii)

Comprising unfunded commitments for investments in limited partnerships of £325 million (2011: £341 million) and unfunded commitments related to mortgage loans of £86 million (2011: £77 million) and commitments to purchase or develop investment properties of £5 million (2011: £9).

(iv)

Amounts due in less than one year include amounts attributable to unit holders of consolidated unit trusts and similar funds of £4,345 million.

Group Consolidated Cash Flows

The discussion that follows is based on the consolidated statement of cash flows prepared under IFRS and presented in Item 18 of this Form 20-F.

Net cash outflows in 2012 were £772 million. This amount comprised inflows of £446 million from operating activities less outflows of £326 million from investing activities less outflows of £892 million from financing activities.

Net cash inflows in 2011 were £658 million. This comprised inflows of £1,738 million from operating activities less outflows of £167 million from investing activities and £913 million from financing activities.

Net cash inflows in 2010 were £1,268 million. This comprised inflows of £1,948 million from operating activities less outflows of £234 million from investing activities and £446 million from financing activities.

The Group held cash and cash equivalents of £6,384 million at 31 December 2012 compared with £7,257 million and £6,631 million at 31 December 2011 and 2010, respectively.

Item 6. Directors, Senior Management and Employees

The Prudential Board consists of 16 directors as at 16 April 2013.

On 1 January 2012, Kai Nargolwala and Alistair Johnston joined the Board as non-executive directors. Kathleen O'Donovan retired as a non-executive director on 31 March 2012. Harvey McGrath retired as a director on 2 July 2012 and was succeeded as Chairman by Paul Manduca. Philip Remnant was appointed as the Senior Independent Director with effect from 1 January 2013. On 13 March, Prudential announced that Keki Dadiseth would retire from the Board with effect from 1 May 2013 and be replaced by Anthony Nightingale from 1 June 2013.

Set forth below are the names, ages, positions, business experience and principal business activities performed by the current directors of Prudential, as well as the dates of their initial appointment as directors. Ages given are as at 16 April 2013.

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Paul Manduca
Chairman

Appointments:
Board: October 2010
Chairman of the Board: July 2012
Chairman of the Nomination Committee: July 2012

Paul Manduca was the Senior Independent Director prior to his appointment as Chairman. He was also a member of the Audit and Remuneration Committees from October 2010 to June 2012 and a member of the Nomination Committee from January 2011.

Paul was a non-executive director of Wm Morrison Supermarkets Plc (Morrisons) from September 2005 until March 2011. During that time, he was the Senior Independent Director, a member of the Nomination Committee and Chairman of the Remuneration Committee of Morrisons, and prior to that he chaired the Audit Committee of Morrisons. Paul retired as Chairman of JPM European Smaller Companies Investment Trust Plc in December 2012 and was the Chairman of Aon UK Limited until September 2012. He was also a non-executive director and Chairman of the Audit Committee of KazmunaiGas Exploration & Production until the end of September 2012. Paul was the Senior Independent Director and Chairman of the Audit Committee of Development Securities plc until March 2010, Chairman of Bridgewell Group plc until 2007 and a director of Henderson Smaller Companies Investment Trust plc until 2006. Prior to that, he was European CEO of Deutsche Asset Management from 2002 to 2005, global CEO of Rothschild Asset Management from 1999 to 2002 and founding CEO of Threadneedle Asset Management Limited from 1994 to 1999 when he was also a director of Eagle Star and Allied Dunbar. Paul is a member of the Securities Institute, a former Chairman of the Association of Investment Companies from 1991 to 1993, and former member of the Takeover Panel. He is also the Chairman of Henderson Diversified Income Limited. Age 61.

Tidjane Thiam
Group Chief Executive

Appointments:
Board: March 2008
Group Chief Executive: October 2009

Tidjane was the Chief Financial Officer from March 2008 until his appointment as Group Chief Executive in 2009.

Tidjane spent the first part of his professional career with McKinsey & Company in Paris and New York, serving insurance companies and banks. He then spent a number of years in Africa where he was Chief Executive and later Chairman of the National Bureau for Technical Studies and Development in Cote d'Ivoire and a cabinet member as Secretary of Planning and Development. Tidjane returned to France to become a partner with McKinsey & Company and one of the leaders of their Financial Institutions practice before joining Aviva in 2002. He worked at Aviva until 2008, holding successively the positions of Group Strategy and Development Director, Managing Director of Aviva International, Group Executive Director and Chief Executive Officer, Europe.

Tidjane was a non-executive director of Arkema in France until November 2009. He is a member of the Board of the Association of British Insurers (ABI) and he was appointed as Chairman in July 2012. He is a member of the Council of the Overseas Development Institute (ODI) in London, a member of

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the Africa Progress Panel chaired by Kofi Annan and a sponsor of Opportunity International. Tidjane is a member of the UK-ASEAN Business Council and of the Strategic Advisory Group on UK Trade and Investment. In January 2012, Tidjane was appointed to the Prime Minister's Business Advisory Group and has been a member of the European Financial Round Table (EFR) since January 2013. Tidjane was awarded the Légion d'Honneur by the French President in July 2011. Age 50.

Nicolaos Nicandrou ACA
Chief Financial Officer

Appointments:
Board: October 2009

Before joining Prudential, Nic Nicandrou worked at Aviva, where he held a number of senior finance roles, including Norwich Union Life Finance Director and Board Member, Aviva Group Financial Control Director, Aviva Group Financial Management and Reporting Director and CGNU Group Financial Reporting Director. Nic started his career at PriceWaterhouse Coopers where he worked in both London and Paris. Age 47.

John Foley
Group Chief Risk Officer

Appointments:
Board: January 2011

John Foley has been Group Chief Risk Officer since January 2011. He joined Prudential as Deputy Group Treasurer in 2000 before being appointed Managing Director, Prudential Capital (formerly Prudential Finance (UK)) and Group Treasurer in 2001. He was appointed Chief Executive of Prudential Capital and to the Group Executive Committee in 2007. Prior to joining Prudential, John spent three years with National Australia Bank as General Manager, Global Capital Markets. John began his career at Hill Samuel & Co Limited where, over a 20 year period, he worked in every division of the bank, culminating in senior roles in risk, capital markets and treasury of the combined TSB and Hill Samuel Bank. Age 56.

Robert Devey
Executive Director

Appointments:
Board: November 2009

Rob Devey has been the Chief Executive of Prudential UK and Europe since 2009. Before joining Prudential, Rob worked at Lloyds Banking Group from 2002, where he held a number of senior leadership roles across insurance and retail banking. Prior to joining Lloyds Banking Group Rob was a consultant with the Boston Consulting Group (BCG) in the UK, US and Europe.

Rob chairs the London Leadership Team of Business in The Community and is also a trustee of the LloydsTSB Foundation for England and Wales. Age 44.

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Michael McLintock
Executive Director

Appointments:
Board: September 2000

Michael McLintock is the Chief Executive of M&G, a position he held at the time of M&G's acquisition by Prudential in 1999, having joined M&G in 1992. Michael has been a Trustee of the Grosvenor Estate since October 2008 and was appointed as a non-executive director of Grosvenor Group Limited in March 2012. He previously served on the board of Close Brothers Group plc as a non-executive director from 2001 to 2008 and has been a member of the Finance Committee of the MCC since October 2005. Age 52.

Barry Stowe
Executive Director

Appointments:
Board: November 2006

Barry Stowe is the Chief Executive of Prudential Corporation Asia, a position he has held since October 2006. Before joining Prudential, he was President, Accident & Health Worldwide for AIG Life Companies. He joined AIG in 1995, and prior to that was President and CEO of Nisus, a subsidiary of Pan-American Life, from 1992 to 1995. Before joining Nisus, Barry spent 12 years at Willis Corroon in the US.

Barry is a member of the Board of Directors of the International Insurance Society and was a director of the Life Insurance Marketing Research Association (LIMRA) and the Life Office Management Association (LOMA) from October 2008 to October 2011. He is also a member of the Board of Visitors of Lipscomb University, a member of the Board of Managers of the Hong Kong International School and Chairman of Save the Children (HK) Ltd. Age 55.

Michael Wells
Executive Director

Appointments:
Board: January 2011

Mike Wells is President and CEO of Jackson National Life Insurance Company ("Jackson"). Mike has served in a variety of senior and strategic positions at Jackson over the last 15 years, including President of Jackson National Life Distributors. Mike has been Vice Chairman and Chief Operating Officer of Jackson for the last nine years. During this period he has led the development of Jackson's variable annuity business and been responsible for IT, strategy, operations, communications, distributions, Curian and the retail broker dealers. Age 53.

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NON-EXECUTIVE DIRECTORS

Keki Dadiseth FCA
Non-executive director

Appointments:
Board: April 2005
Remuneration Committee: April 2005

Keki was a member of the Audit Committee from 2005 to 2007 and was appointed as a member of the Prudential Corporation Asia Audit Committee in July 2012. During 2006, he was appointed as a non-executive director of ICICI Prudential Life Insurance Company Limited and ICICI Prudential Trust Limited.

Keki is also a director of Britannia Industries Limited, JM Financial Limited, JM Financial Services Limited, Piramal Enterprises Limited, Siemens Limited, The Indian Hotels Company Limited and Godrej Properties Limited, all of which are quoted on the Bombay Stock Exchange. In addition, he acts as adviser to Fleishman-Hillard Inc and is Chairman of Marsh & McLennan Companies Group, India. He is Chairman of the Breach Candy Hospital Trust and a trustee for a number of Indian charities. Keki is the non-executive Chairman of Omnicom India Marketing Advisory Services Private Limited, an unquoted Indian company, and is also a board member of various other unquoted Indian companies. He serves as Chairman of Sony India Pvt Ltd and Senior Advisor to Sony Group in India.

Before he retired from Unilever in 2005, Keki was Director, Home and Personal Care, responsible for the HPC business of Unilever worldwide, a Board member of Unilever PLC and Unilever N.V., and a member of Unilever's Executive Committee. He joined Hindustan Lever Ltd in India in 1973 and in 1987, he joined the Board of Hindustan Lever and became Chairman in 1996. Age 67.

Sir Howard Davies
Non-executive director

Appointments:
Board: October 2010
Chairman of the Risk Committee: October 2010
Audit Committee: November 2010
Nomination Committee: July 2012

Sir Howard is chairman of the Phoenix Group, and a Professor at Institut d'Etudes Politiques (Sciences Po). He is also Chairman of the UK Government's Airports Commission. He chairs the International Advisory Board of the China Securities Regulatory Commission and is a member of the International Advisory Board of the China Banking Regulatory Commission. He is also an independent director of Morgan Stanley Inc and a Director of the National Theatre. Age 62.

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Michael Garrett
Non-executive director

Appointments:
Board: September 2004
Remuneration Committee: September 2004

Michael Garrett worked for Nestlé from 1961, becoming Head of Japan from 1990 to 1993, and then Zone Director and Member of the Executive Board, responsible for Asia and Oceania. In 1996 his responsibilities were expanded to include Africa and the Middle East. Michael retired as Executive Vice President of Nestlé in 2005. He served the Government of Australia as Chairman of the Food Industry Council and as a Member of the Industry Council of Australia, and was also a member of the Advisory Committee for an APEC (Asia-Pacific Economic Cooperation) Food System, a Member of The Turkish Prime Minister's Advisory Group and the WTO (World Trade Organization) Business Advisory Council in Switzerland.

Michael remains a director of Nestlé in India, and was appointed Chairman of the Evian Group, a think tank and forum for dialogue promoting free trade, from 2001 to 2011. He also serves as a non-executive director on the Boards of the Bobst Group in Switzerland, Hasbro Inc. in the USA, and Gottex Fund Management Holdings Limited in Guernsey. In addition, he is a Member of the Swaziland International Business Advisory Panel under the auspices of the Global Leadership Foundation (GLF) London, as well as being a member of the Development Committee of the International Business Leaders Forum (IBLF) until stepping down in 2011. Age 70.

Ann Godbehere FCGA
Non-executive director

Appointments:
Board: August 2007
Chairman of the Audit Committee: October 2009
Risk Committee: November 2010
Nomination Committee: July 2012

Ann was a member of the Audit Committee from 2007.

Ann began her career in 1976 with Sun Life of Canada, joining Mercantile & General Reinsurance Group in 1981, where she held a number of management roles rising to Senior Vice President and Controller for life and health and property/casualty businesses in North America in 1995. In 1996 Swiss Re acquired Mercantile & General Reinsurance Group and Ann became Chief Financial Officer of Swiss Re Life & Health, North America. In 1997 she was made Chief Executive Officer of Swiss Re Life & Health, Canada. She moved to London as Chief Financial Officer of Swiss Re Life & Health Division in 1998 and joined the Property & Casualty Business Group, based out of Zurich, as Chief Financial Officer on its establishment in 2001. From 2003 until February 2007, Ann was Chief Financial Officer of the Swiss Re Group.

Ann is also a non-executive director of British American Tobacco p.l.c., Rio Tinto plc, Rio Tinto Limited, UBS AG, Arden Holdings Limited, Atrium Underwriting Group Limited and Atrium Underwriters Limited. From its nationalisation in 2008 until January 2009, Ann was Interim Chief Financial Officer and Executive Director of Northern Rock. Age 58.

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Alexander Johnston (Alistair) CMG FCA
Non-executive director

Appointments:
Board: January 2012
Audit Committee: January 2012

Alistair was a partner of KPMG from 1986 to 2010. He joined KPMG (then Peat Marwick Mitchell) in 1973 and held a number of senior leadership positions. These included Vice Chairman of UK Financial Services and Head of UK Insurance Practice, International Managing Partner Global Markets and UK Vice Chairman. Latterly he served as a Global Vice Chairman of KPMG from 2007 to 2010.

Alistair acted as a non-executive director of the Foreign & Commonwealth Office from 2005 to 2010 and chaired the audit committee until 2009. He was an Association Member of BUPA until January 2012. Alistair is a member of the Strategy and Development Board and a Visiting Professor at Cass Business School. In February 2012 Alistair was appointed as a Trustee of the Design Museum in London. Age 60.

Kaikhushru Nargolwala FCA
Non-executive director

Appointments:
Board: January 2012
Remuneration and Risk Committees: January 2012

Kai Nargolwala was the non-executive Chairman of Credit Suisse Asia Pacific until December 2011, having joined Credit Suisse in 2008 as a member of the Executive Board and CEO of the Asia Pacific region.

From 1998 to 2007, Kai worked for Standard Chartered PLC where he was a Group Executive Director responsible for Asia Governance and Risk. His responsibilities included developing strategy and business performance across Asia, as well as strategic merger and acquisition activity. Prior to that, he spent 19 years at Bank of America and from 1990 was based in Asia as Group Executive Vice President and Head of the Asia Wholesale Banking Group. From 2004 to 2007, he was a non-executive director at Tate & Lyle plc and at Visa International, where he served on the Asia Pacific Board.

Kai is currently a non-executive director and lead independent director of Singapore Telecommunications Limited, a member of the Board of the Casino Regulatory Authority of Singapore, a non-executive director of PSA International Pte. Limited, Chairman of the Governing Board of the Duke-NUS Graduate Medical School and a director and Chairman of Clifford Capital Pte. Limited. Age 62.

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Philip Remnant CBE ACA
Senior Independent Director

Appointments:
Board: January 2013
Remuneration, Audit, Nomination Committees: January 2013

Philip Remnant is a senior adviser at Credit Suisse, a Deputy Chairman of the Takeover Panel, a non-executive director of UK Financial Investments Limited (since 2009) and Chairman of City of London Investment Trust plc (since 2011). He was previously a Vice Chairman of Credit Suisse First Boston (CSFB) Europe and Head of the UK Investment Banking Department. Philip was seconded to the role of Director General of the Takeover Panel, which administers the UK's code on takeovers and mergers, from 2001 to 2003 and again in 2010. He served on the Board of Northern Rock plc from 2008 to 2010 and from 2007 to 2012 was Chairman of the Shareholder Executive, which manages the relationships between the UK Government and the businesses in which it is a shareholder. Age 58.

Lord Turnbull KCB CVO
Non-executive director

Appointments:
Board: May 2006
Chairman of the Remuneration Committee: June 2011
Risk Committee: November 2010
Nomination Committee: June 2011

Lord Turnbull was a member of the Remuneration Committee from November 2010, and a member of the Audit Committee from January 2007 to November 2010.

Lord Turnbull entered the House of Lords as a Life Peer in 2005. In 2002 he became Secretary of the Cabinet and Head of the Home Civil Service until he retired in 2005. Prior to that he held a number of positions in the Civil Service, including Permanent Secretary at HM Treasury; Permanent Secretary at the Department of the Environment (later Environment, Transport and the Regions); Private Secretary (Economics) to the Prime Minister; and Principal Private Secretary to Margaret Thatcher and then John Major. He joined HM Treasury in 1970.

Lord Turnbull is a non-executive director of Frontier Economics Limited and The British Land Company PLC. He was formerly Chairman of BH Global Limited until January 2013 and a non-executive director of the Arup Group from 2006 to 2007. He also worked part-time as a Senior Adviser to the London partners of Booz and Co (UK) until February 2011. Age 68.

Other Executive Officers

The heads of Prudential's business units, Prudential UK and Europe, M&G, Jackson National Life Insurance Company and Prudential Corporation Asia, are also directors of Prudential as set forth above. For information relating to the compensation paid or accrued to all Prudential directors see Item 6, 'Compensation'.

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Compensation

Summary of main elements of remuneration

Element	Purpose	Policy in 2012	2012 Opportunity	2012 Performance metrics	Changes To Policy for 2013
Base salary	To provide executives with a guaranteed level of remuneration. Paying salaries at an appropriate level ensures that Prudential continues to be competitive when recruiting and retaining key executives. Salary is intended to reward executives for the performance of their role.	The Committee reviews salaries annually. Changes in base salaries are generally effective from 1 January. In determining base salaries for each executive the Committee considers: The performance and experience of the executive; Internal relativities; Company financial performance; Salary increases for all employees; and	2012 base salaries are set out on page 232.		

		Benchmark information from appropriate markets.			
Annual bonus	To incentivise and reward the achievement of stretching annual business plans which are: Determined in line with the Group's long-term commitments to shareholders. Consistent with the Group's risk appetite.	Executive directors participate in annual bonus plans based on the achievement of Group and business unit financial performance measures including profitability, cash flow and capital adequacy, and personal objectives. Executive directors are required to defer between 30 per cent and 50 per cent of annual bonus (for the Chief Executive of M&G, 50 per cent of bonus over £500,000 is deferred) into Prudential shares for three years. Bonuses are not pensionable.	The maximum annual bonus opportunity available to the majority of executive directors is between 160 per cent and 200 per cent of salary. Based on relevant market practice, the Chief Executive of M&G and the President & CEO, JNL have bonus opportunities which are not capped as a percentage of their salaries. the Chief Executive of M&G has an overriding cap on total remuneration of 3 per cent of M&G's IFRS profit. Details of executive directors' 2012 bonus opportunities are provided on page 231.	Awards for the majority of executive directors are subject to the achievement of: Net free surplus generated IFRS operating profit EEV operating profit Holding company cash flow; and Insurance Groups Directive (IGD) Capital Surplus. Personal objectives.	As part of the review of remuneration architecture which took place during 2012, the clawback provisions applied to the deferred portion of bonuses for 2013 onwards have been strengthened. The percentage of annual bonus awards which executives are required to defer has been made consistent across our senior executive team at 40 per cent. The annual bonus opportunity for the Chief Executive of M&G will be capped at the lower of 0.75 per cent of M&G's IFRS profit or six times salary.

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Element	Purpose	Policy in 2012	2012 Opportunity	2012 Performance metrics	Changes To Policy for 2013
Long-term incentives	To incentivise and reward the achievement of: Longer-term commitments to shareholders. Sustainable long-term returns for shareholders. Adherence to the Group's risk appetite.	All executive directors participate in the Group Performance Share Plan (GPSP). GPSP awards vest based on relative TSR. Business unit Chief Executives also participate in business unit performance plans (BUPPs or the M&G Executive LTIP) which focus on those financial measures which contribute to the long-term success of the business unit and, therefore, the Group.	The maximum combined award under the GPSP and BUPP is 550 per cent of salary, although the actual awards made in 2012 were below this level. The Chief Executive of M&G's long-term incentive opportunity was not capped as a percentage of salary in 2012. Michael has an overriding cap on total remuneration of 3 per cent of M&G's IFRS profit. A breakdown of the long-term incentive opportunities available to executive directors is set out on page 228.	GPSP awards vest based on relative TSR (Total Shareholder Return, a combination of share price growth and dividends paid) performance relative to an index of international insurers. The performance measures for the BUPPs and the M&G Executive LTIP vary according to the business plan and strategy of the business unit. These are outlined on pages 232 to 237.	As part of the review of remuneration architecture, the Remuneration Committee has proposed a new long-term incentive (the Prudential Long Term Incentive Plan) for approval at the 2013 AGM. Subject to shareholder approval, the first awards will be made under this plan in May 2013.
Share ownership guidelines	To create a community of interest between the executives and shareholders.	The Group Chief Executive and Chief Executive of M&G are required to build up and hold shares equal to 200 per cent of base salary. Other executive			As part of the review of remuneration architecture, the executive director shareholding guidelines have been enhanced. The revised

		directors are required to build up and hold shares equal to 100 per cent of base salary. Executives have five years to build up their shareholding. Full details of the current shareholdings of the directors are provided on page 242.	guidelines are: 350 per cent of salary for the Group Chief Executive 200 per cent of salary for all other executive directors.
Benefits	To provide executives with items and allowances that assist them in carrying out their duties efficiently.	All executive directors received core health and security benefits (for example medical insurance and life assurance). Other benefits may be offered to executives, dependent on: Local market practice. The benefits offered to other employees within the business unit.	

Applicable expatriate and relocation benefits and allowances.	
No benefits are pensionable. Details of the costs of providing the benefits to each executive director are outlined in the remuneration table on page 243.	

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Element	Purpose	Policy in 2012	2012 Opportunity	2012 Performance metrics	Changes To Policy for 2013
Pension	To provide executives with an opportunity to save for an income in retirement.	The pension provision for executive directors depends on the arrangements in place for other employees in their business unit when they joined the Group. Executives who joined after June 2003 have the option to: Receive payments into a defined contribution scheme, or Take a cash supplement in lieu of contributions. Executives who joined the Group before June 2003 were entitled to join the defined benefit plans available at that time. At the end of 2012, no executive director was an active member of a Group defined benefit scheme.	Executive directors based in the UK and Asia are entitled to receive pension contributions or a cash supplement (or combination of the two) of 25 per cent of base salary. The President & CEO, JNL participates in Jackson's Defined Contribution Retirement Plan on the same basis as other JNL employees. Full details of the amounts paid by the Company with regards to pension provision are outlined in the remuneration table on page 243 and the pensions table on page 239.	Jackson's Defined Contribution Retirement Plan has a guaranteed element and additional contributions based on the profitability of JNL. No other Group pension schemes have performance conditions.	

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The Operation of the Reward Policy in 2012

In 2012, executive directors were rewarded on the basis set out below:

Director	Role	Base Salary at 1 January 2012	Annual Bonus Maximum percentage of salary	Long-term incentives (2012 award as a percentage of salary) Group Performance Share Plan (GPSP)	Business Unit Performance Plan (BUPP)	Total
Rob Devey	Chief Executive, UK & Europe	£600,000	160%	112.50%	112.50%	225.00%
John Foley	Group Chief Risk Officer	£610,000	160%	250.00%		250.00%
Michael McLintock	Chief Executive, M&G	£360,000	note 1	100.00%	344.10%	444.10%
Nic Nicandrou	Chief Financial Officer	£630,000	175%	225.00%		225.00%
Barry Stowe	Chief Executive, PCA	HK$8,000,000	160%	112.50%	112.50%	225.00%
Tidjane Thiam	Group Chief Executive	£1,000,000	200%	400.00%		400.00%
Mike Wells	President & CEO, JNL	US$1,050,000	note 2	230.00%	230.00%	460.00%

Notes

(1)

Michael McLintock's annual bonus and long-term incentive opportunity under the M&G Executive LTIP (rather than the BUPP) are based on M&G's performance both in absolute terms and relative to its peers. In line with practice in the asset management sector, there is no specified maximum incentive award. Michael's total remuneration is subject to an overriding cap such that his total remuneration should not be greater than three per cent of M&G's annual IFRS profits. The figure shown for his 2012 M&G Executive LTIP award is the expected value of this grant.

(2)

Mike Wells' maximum annual bonus figure is comprised of 160 per cent of salary and a 10 per cent share of the Jackson senior management bonus pool based on the target performance of Jackson.

(3)

All long-term incentives have a three year performance period. For the awards detailed above the performance period will end on 31 December 2014.

(4)

Where awards are made in shares, the final number of shares awarded is calculated in line with the respective plan rules. Details on the shares granted under these plans are outlined in the Directors' outstanding long-term incentive awards tables in the Supplementary Information section.

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The package for 2012 offered the following proportions of fixed and variable short and long-term reward to executive directors (average of executive directors):

As illustrated above 'Good' performance results in the payment of 2012 annual bonus at the target level and 2012 long-term incentive awards vesting at the threshold level. 'Superior' performance generates maximum payment of 2012 annual bonuses and 2012 long-term incentive awards vest in full.

The single figure

Although the UK Government's proposed reporting requirements have not been finalised, we have anticipated the requirement to present a single figure for executives' total remuneration. This is included in the main remuneration table for 2012 on page [243]. The single figure has been calculated including the following elements:

The salary and the cost of providing benefits in 2012.

The bonus awarded for performance in 2012 (including the value at award of the deferred element which will be released in 2016).

The value of long-term incentive awards with a performance period ending in 2012 which will be released in 2013, using the average share price over the period 1 October 2012 31 December 2012

The value of any salary supplement for pension, employer contributions to a defined contribution pension plan or the increase in transfer value of final salary pension benefits in 2012 (less contributions made by the director during 2012).

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Base salary

Executive directors' salaries were reviewed in 2012 with changes effective from 1 January 2013. In determining 2013 salaries, the Committee considered the performance, experience and internal relativities of each director, as well as the performance of the Group and the salary increases awarded to other employees. To provide context for this review, information was drawn from the following market reference points:

Director	Role	Benchmark(s) used to assess remuneration
Rob Devey	Chief Executive, UK & Europe	FTSE 40 International Insurance Companies
John Foley	Chief Risk Officer	FTSE 40
Michael McLintock	Chief Executive, M&G	McLagan UK Investment Management Survey
Nic Nicandrou	Chief Financial Officer	FTSE 40 International Insurance Companies
Barry Stowe	Chief Executive, PCA	Towers Watson Asian Insurance Survey
Tidjane Thiam	Chief Executive	FTSE 40 International Insurance Companies
Mike Wells	President & CEO, JNL	Towers Watson US Financial Services Survey LOMA US Insurance Survey

After careful consideration the Committee decided to increase salaries by three per cent as set out below. Salary increases for the wider workforce vary across our business units, based on local market conditions. It is anticipated that 2013 salary budgets will increase between three per cent and five per cent, for the wider workforce.

Executive	2012 salary	2013 salary (+3%)
Rob Devey	£600,000	£618,000
John Foley	£610,000	£628,300
Michael McLintock	£360,000	£370,800
Nic Nicandrou	£630,000	£648,900
Barry Stowe	HK$8,000,000	HK$8,240,000
Tidjane Thiam	£1,000,000	£1,030,000
Mike Wells	US$1,050,000	US$1,081,500

Annual bonus

Performance measures

The financial measures used to assess performance for the 2012 AIP are set out below. These remain unchanged for 2013. Executive directors who have business unit responsibilities are assessed on both Group and business unit performance.

A portion of the annual bonus for each executive director is based on the achievement of personal objectives. These objectives include the executive's contribution to Group strategy as a member of the Board and specific goals related to their functional and/or business unit role (for instance, project measures relating to the implementation of Solvency II requirements). In addition, all employees are required to comply with the regulatory, governance and risk management practices and policies as these

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relate to their role and business area. Specifically, all business units must act within the Group's risk appetite and framework, and all individuals must act within the Group's Code of Business Conduct.

A proportion of each executive director's annual bonus is not paid in cash and must be deferred. This portion is deferred for three years in the form of the Company's shares. This deferral aligns the interests of our executive directors with our shareholders and helps to ensure a focus on the sustainable success of the Company.

Annual bonus opportunities

Executive directors' bonus opportunities, the weighting of performance measures for 2012 and the proportion of annual bonuses deferred are set out below.

	Maximum bonus opportunity (% of salary)	Deferral requirement	Weighting of measures		
			Group	Business Unit	Personal objectives
Rob Devey	160%	40% of total bonus	20%	60%	20%
John Foley	160%	40% of total bonus	50%		50%
Michael McLintock	Note 1	50% of bonus above £500,000	10%	60%	30%
Nic Nicandrou	175%	40% of total bonus	80%		20%
Barry Stowe	160%	40% of total bonus	20%	60%	20%
Tidjane Thiam	200%	50% of total bonus	80%		20%
Mike Wells[(note 2)]	c.400%	30% of total bonus	30%	60%	10%

Notes

(1) Michael McLintock's annual bonus and long-term incentive opportunities in 2012 were based on M&G's performance both in absolute terms and relative to its peers. In line with practice in the asset management sector, there is no specified maximum incentive award. Michael's total remuneration (including long-term incentives) is subject to an overriding cap which requires that his total remuneration must not be greater than 3 per cent of M&G's annual IFRS profit.

(2) Mike Wells' annual bonus figure comprises an AIP opportunity of 160 per cent of salary and a 10 per cent share of the Jackson senior management bonus pool. The figure above is based on the target performance of Jackson.

Rewarding performance in 2012

As set out in the Remuneration Committee Chairman's letter, during 2012 the Group delivered further increases in its key financial measures, specifically new business profitability, IFRS profitability and cash generation. The outstanding performance delivered in 2012 against these measures exceeded both the Group's 2011 performance and the stretching targets set by the Committee at the start of the year. The Group Chief Risk Office was invited to attend the Remuneration Committee meeting held in February 2013 and advised the Committee on the Groups' adherence to its risk appetite and framework during 2012.

2012 financial performance, relative to the targets set by the Committee, is summarised below:

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On the basis of this outstanding performance, the Committee approved the following 2012 AIP payments:

Executive	2012 salary	Maximum 2012 AIP	2012 outcome (as a percentage of max)	2011 outcome (as a percentage of max)	Total 2012 AIP payment
Rob Devey	£600,000	160%	73.9%	90.7%	£709,200
John Foley	£610,000	160%	100.0%	98.1%	£976,000
Michael McLintock	£360,000	n/a	n/a	n/a	£1,307,275
Nic Nicandrou	£630,000	175%	99.0%	95.9%	£1,091,475
Barry Stowe	HK$8,000,000	160%	98.1%	94.1%	HK$12,560,000
Tidjane Thiam	£1,000,000	200%	100.0%	96.9%	£2,000,000
Mike Wells[(1)]	US$1,050,000	160%	99.0%	95.4%	US$1,663,200

Note

(1) In addition to the AIP Mike Wells also received 10 per cent of the JNL senior management bonus pool. His total 2012 bonus, including his AIP and JNL senior management award is US$4,599,500.

Long-term incentives

Details of the awards made under these plans in 2012 can be found on pages 247 and 248. Additional discussion on the Group's share award and share option plans may be found in note I4 to the consolidated financial statements in Item 18.

Group Performance Share Plan (GPSP)

All executive directors receive GPSP awards. GPSP awards vest on the basis of the Group's Total Shareholder Return (TSR) performance over a three year period. Total Shareholder Return is the combination of the share price growth and the dividends paid. Prudential's TSR achievement over the performance period is compared with the TSR of an index composed of 10 international insurers (see box below). This performance measure was selected because it focuses on the value delivered to shareholders. TSR is measured on a local currency basis since this has the benefits of simplicity and directness of comparison.

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The vesting schedule for outstanding GPSP awards is set out below:

Peer Companies used within the Index for all outstanding GPSP awards

Aegon, Allianz, Aviva, Axa, Generali, ING, Legal & General, Manulife, Old Mutual and Standard Life.

For any GPSP award to vest, the Committee must be satisfied that the quality of the Company's underlying financial performance justifies the level of reward delivered at the end of the performance period. To ensure close alignment with our shareholders' long-term interests, participants receive the value of reinvested dividends over the performance period for those shares which ultimately vest. If performance measures are not achieved in full, the unvested portion of any award lapses and performance cannot be retested.

On 31 December 2012, the performance period for 2010 GPSP awards (which began on 1 January 2010) came to an end. Over the performance period the Group has delivered superior returns for shareholders through share price growth and dividends paid. This resulted in Prudential achieving excellent TSR performance of 156.4 per cent.

The peer group's TSR index was 100 at the start of the 2010-2012 performance period and was 111.8 at the end of the period (as illustrated overleaf). In order for the 2010 GPSP awards to vest in full, Prudential's TSR index over the period had to outperform the peer index by 20 per cent, i.e. increase from 100 to at least 134.2 (111.8 × 120 per cent). The TSR performance achieved by Prudential of 156.4 per cent equals an outperformance of the peer index of 139.9 per cent.

The Committee, having satisfied itself about the quality of the Company's underlying financial performance, confirmed vesting of 100 per cent of the 2010-2012 GPSP award (for reference, 100 per cent of the 2009-2011 GPSP award vested).

The Committee believes that the GPSP performance condition is a stretching requirement that requires exceptional performance, relative to other international insurance companies, for awards to be released in full.

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The line chart below compares Prudential's TSR during the three years from 1 January 2010 to 31 December 2012 with that of the peer group against which TSR is measured for the purposes of the GPSP.

Prudential TSR v peer group index total returns index % over 3 years to December 2012

Business Unit Performance Plans (BUPP)

Asia BUPP

The Chief Executive, PCA receives awards under the Asia BUPP. These awards are dependent on the achievement of PCA's new business profit, IFRS profit and cash remittance targets over the three year performance period. Each of these measures will determine vesting of one third of each award. Threshold performance results in 30 per cent of the award vesting increasing to 100 per cent for stretch performance.

On 31 December 2012, the performance period for the 2010 Asia BUPP award (which began on 1 January 2010) came to an end. Over the period, the new business profit, IFRS profit and cash remittance achieved by the PCA business unit meant that the Committee, having satisfied itself as to the quality of the business units' underlying financial performance, confirmed vesting of 95.2 per cent of Barry Stowe's 2010-12 Asia BUPP award (for reference, 86.50 per cent of Barry Stowe's 2009 2011 Asia BUPP award vested).

Jackson BUPP

The President and CEO, JNL receives an award under the Jackson BUPP. Vesting of awards made under this plan is dependent on Shareholder Capital Value (SCV) growth over the performance period.

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The SCV growth required is outlined in the table below. Vesting occurs between these performance levels on a straight line basis.

Percentage of BUPP award which vests	Compound annual growth in SCV over three years
0%	<8%
30%	8%
75%	10%
100%	12%

On 31 December 2012, the performance period for the 2010 Jackson BUPP came to an end. Although no current executive director had a 2010 award under this plan the vesting level for other participants was 100 per cent (for reference 93.75 per cent of the 2009 2011 awards vested).

UK BUPP

The Chief Executive, UK & Europe receives awards under the UK BUPP. Given the cash-generative priorities of the UK Business Unit, UK BUPP awards are assessed using the same relative TSR measure applied to GPSP awards.

On 31 December 2012, the performance period for the 2010 UK BUPP (which began on 1 January 2010) came to an end. As detailed above, Prudential's TSR over this period was equal to 139.9 per cent of the peer index. The Committee, having satisfied itself as to the quality of the business unit's underlying financial performance, confirmed vesting of 100 per cent of Rob Devey's 2010 2012 UK BUPP award (for reference 100 per cent of Rob Devey's 2009 2011 UK BUPP award vested).

For any BUPP award to vest, the Committee must be satisfied that the quality of underlying financial performance of the relevant business unit justifies the level of reward delivered at the end of the performance period. To ensure close alignment with our shareholders' long-term interests, participants receive the value of reinvested dividends over the performance period for those shares which ultimately vest. If the performance conditions are not achieved in full, the unvested portion of any award lapses and cannot be retested

Limits on award sizes

The rules of the GPSP and BUPP set a limit on the value of shares which may be awarded to an executive in a financial year. The combined value of shares awarded under the two plans may not exceed a maximum of 550 per cent of salary although the awards made in a particular year are often significantly below this limit. On a change in control of Prudential, vesting of awards made under these arrangements would be prorated for performance and to reflect the elapsed portion of the performance period.

M&G Executive Long-Term Incentive Plan

The Chief Executive, M&G receives awards under the M&G Executive Long-Term Incentive Plan. Under this plan an annual award of phantom shares is made with a notional starting share price of £1. The phantom share price at vesting is determined by the increase or decrease in M&G's profitability over the three-year performance period with profit and investment performance adjustments also applied:

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Profit growth

The value of phantom shares vesting will be adjusted by a profit measure as follows:

No adjustment will be made if profits in the third year of the performance period are at least equal to the average annual profit generated over the performance period;

A loss or zero profit will result in the value of the award being reduced to zero, irrespective of investment performance;

Between these points, the value of phantom shares will be reduced on a straight line basis from no reduction to the complete elimination of the value of the award.

Investment performance

The value of phantom shares vesting will be adjusted by an investment performance measure as follows:

Where the investment performance of M&G's funds is in the top two quartiles during the three-year performance period, the value of phantom shares vesting will be enhanced. The value of phantom shares may be doubled if performance is in the top quartile;

Investment performance in the third quartile will not change the value of phantom shares vesting;

Investment performance in the bottom quartile will result in awards being forfeited, irrespective of any profit growth.

The value of the vested phantom shares will be paid in cash after the end of the three-year performance period.

On 31 December 2012, the performance period for the 2010 award under the M&G Executive Long-Term Incentive Plan (which began on 1 January 2010) came to an end. M&G's profit at the end of the performance period was 204 per cent of that at the start and M&G's investment performance was in the second quartile. The Committee, having satisfied itself about the quality of M&G's underlying financial performance, confirmed vesting of Michael McLintock's 2010 award with a value of £2.65 per share. This will result in a payment of £2,616,024 to Michael McLintock in 2013 (for reference, the 2009 2011 award vested with a value of £2.96 per share which resulted in a payment of £5,417,359 to Michael McLintock during 2012.). Based on 2011 performance, an award of 952,960 phantom shares with an expected value of £1,238,849 was made to Michael McLintock in 2012.

As described in the remuneration architecture review section of this report, the method used to determine the number of phantom shares awarded to Michael McLintock under the M&G Executive Long-Term Incentive Plan has been revised. With effect from 2013, Michael McLintock will receive an annual award with a face value of three times his salary. The ultimate value of the 2013 award will be determined with reference to the profitability and investment performance of M&G over the three years from 1 January 2013 to 31 December 2015 using the measures set out above.

Jackson Long-Term Incentive Plans

Prior to his appointment as an executive director, Mike Wells participated in the two long-term incentive plans offered to senior staff within Jackson. Mike Wells was awarded ADRs under the JNL US Performance Share Plan and cash-based awards under the JNL Long-Term Incentive Plan. Awards made under both plans have a performance period of four years and vesting is dependent on the achievement of shareholder value targets. Up to 150 per cent of the original number of ADRs awarded under the JNL Performance Share Plan may be released if stretch performance targets are achieved.

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Outstanding awards made to Mike Wells before his appointment as an executive director remain subject to the original performance conditions and vesting schedule. No further awards will be made to Mike Wells under these plans.

On 31 December 2012, the performance periods for the 2009 awards under the JNL long-term incentive plans (which began on 1 January 2009) came to an end. Over the period the shareholder value of the US business grew by 22.68 per cent per annum (on a compound basis) and by 126.51 per cent over the performance period. This resulted in vesting of 150 per cent of Mike Wells' 2009 JNL US Performance Share Plan award and of 126.51 per cent of his 2009 cash-settled JNL Long-Term Incentive Plan award (for reference 150 per cent of Mike Wells' 2008 2011 JNL US Performance Share Plan award and 95 per cent of his 2008 2011 cash-settled JNL Long-Term Incentive Plan award vested).

Share ownership guidelines

As a condition of serving, all directors are required to have beneficial ownership of a minimum of 2,500 ordinary shares in the Company. This interest in shares must be acquired within 12 months of appointment to the Board if the director does not have such an interest upon appointment.

Executive directors should have a substantial shareholding to maximise the community of interest between them and other shareholders. This may be built up over a period of five years following their appointment.

The level of the requirements which applied to executive directors in 2012 and the current holdings of directors are shown below. The shareholding guidelines have been increased as part of the review of remuneration architecture and full details of the revised guidelines are outlined on page [226]. Shares earned and deferred under the Annual Incentive Plan are included in calculating the executive director's shareholding for these purposes.

	2012 Shareholding guideline as a percentage of base salary	Shareholding at 31 December 2012 as a percentage of base salary (1)	Shareholding guideline as a percentage of base salary
Rob Devey	100%	397%	200%
John Foley	100%	459%	200%
Michael McLintock	200%	1,641%	200%
Nic Nicandrou	100%	482%	200%
Barry Stowe	100%	680%	200%
Tidjane Thiam	200%	800%	350%
Mike Wells	100%	773%	200%

Note

(1) Beneficial interest, based on the share price as at 31 December 2012 (£8.655). Calculated using base salaries on 31 December 2012.

Benefits

All executive directors receive core health and security benefits for example medical insurance and life assurance.

Other benefits may be offered to executives, dependent on:

Local market practice.

The benefits offered to other employees within the business unit.

Applicable expatriate and relocation benefits and allowances.

The 2012 remuneration table on page [243] sets out the cost of providing benefits in 2012.

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All-employee share plans

It is important that all employees are offered the opportunity to own shares in Prudential, connecting them both to the success of the Company and to the interests of other shareholders. Executive directors are invited to participate in these plans on the same basis as other staff in their location.

Save As You Earn (SAYE) schemes

UK based executive directors are eligible to participate in the HM Revenue and Customs (HMRC) approved Prudential Savings-Related Share Option Scheme and Barry Stowe is invited to participate in the similar International Share Ownership Scheme. These schemes allow all eligible employees to save towards the exercise of options over Prudential plc shares with the option price set at the beginning of the savings period at a discount of up to 20 per cent of the market price.

Participants elect to enter into savings contracts of up to £250 per month for a period of three or five years. At the end of this term, participants may exercise their options within six months and purchase shares. If an option is not exercised within six months, participants are entitled to a refund of their cash savings plus interest if applicable under the rules. Shares are issued to satisfy those options which are exercised. No options may be granted under the schemes if the grant would cause the number of shares which have been issued, or which remain issuable pursuant to options granted in the preceding 10 years under the scheme and any other option schemes operated by the Company, or which have been issued under any other share incentive scheme of the Company, to exceed 10 per cent of the Company's ordinary share capital at the proposed date of grant.

Share Incentive Plan (SIP)

UK based executive directors are also eligible to participate in the Company's HMRC approved Share Incentive Plan (SIP). This allows all UK based employees to purchase Prudential plc shares up to a value of £125 per month from their gross salary (partnership shares). For every four partnership shares bought, an additional matching share is awarded which is purchased by Prudential on the open market. Dividend shares accumulate while the employee participates in the plan. Partnership shares may be withdrawn from the scheme at any time. If the employee withdraws from the plan within five years, matching shares are forfeited.

No directors or other employees are provided with loans to enable them to buy shares.

Pension benefits

Michael McLintock elected to become a deferred member of a contributory defined benefit scheme (described below) on 5 April 2012. Michael McLintock now receives a salary supplement of 25 per cent of salary. John Foley elects to receive a combination of contributions into the money purchase scheme and a cash supplement with a total value of 25 per cent of salary. All other executive directors based in the UK have chosen to receive their pension benefits in the form of a cash supplement of 25 per cent of salary throughout 2012. These executives are provided with life assurance cover of up to four times salary plus a dependants' pension.

Barry Stowe receives a cash supplement of 25 per cent of salary and a payment to the Hong Kong Mandatory Provident Fund. He is provided with life assurance cover of up to four times salary. Mike Wells participates in Jackson's Defined Contribution Retirement Plan, a qualified 401(k) retirement plan, on the same basis as all other US based employees. The Company provides matching contributions of 6 per cent of base salary (Mike Wells' salary for pension purposes is limited to US$250,000). He also participates in the profit sharing element of the plan which provides eligible participants with an annual profit sharing contribution, depending on the financial results of Jackson for the plan year, to a maximum of an additional 6 per cent of pensionable salary. An annual profit sharing contribution equivalent to 6 per cent of pensionable salary was made in 2012 (in 2011, the profit share contribution

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was 5 per cent of pensionable salary). Mike Wells is provided with life assurance cover of two times salary.

Those executives who joined the Group before June 2003 were entitled to maintain their membership of the defined benefit plans available at that time. However, at the end of 2012, no executive director was an active member of a Group defined benefit scheme. Until 5 April 2012, Michael McLintock participated in a contributory defined benefit scheme that provides a target pension of two thirds of final pensionable earnings on retirement at age 60 for an employee with 30 years or more potential service, his contribution was four per cent of base salary. Michael McLintock participated on the same basis as other employees who joined M&G at the same date. Benefits under the plan are subject to a notional scheme earnings cap (set at £129,600 for the 2011 to 2012 tax year) which replicates the HMRC earnings cap in force before A-Day (6 April 2006). Michael McLintock was also entitled to supplements based on his salary above the notional earnings cap.

Details of directors' pension entitlements under HMRC approved defined benefit schemes and supplements in the form of contributions to pension arrangements paid by the Company are set out in the following table:

			Additional pension earned during year ended 31 December 2012			Transfer value of accrued benefit at 31 December(3)			
	Age at 31 December 2012	Years of pensionable service at 31 December 2012	Accrued benefit at 31 December 2012 (Ignoring inflation on pension earned to 31 December 2011(1) £000	Allowing for inflation on pension earned to 31 December 2011(2) £000	2012 £000	2011 £000	Increase in transfer value less contributions made by directors during 2012 £000	Contributions to defined contribution pension schemes(4)
Rob Devey	44							
John Foley	56							50
Michael McLintock(5)	51	20	56	1	-1	1323	1102	218	
Nic Nicandrou	47							
Barry Stowe	55							2
Tidjane Thiam	50							
Mike Wells	52							19

Notes

(1) As required by the Companies Act remuneration regulations.

(2) As required by Stock Exchange Listing rules.

(3) The transfer value equivalent has been calculated in accordance with the M&G Group Pension Scheme's transfer basis.

(4)

This table includes employer contributions to defined contribution plans totalling £71,124 (2011: £56,224). Supplements in the form of cash are included in the table on page [243].

(5) Michael McLintock became a deferred member of the M&G defined benefit scheme on 5 April 2012. The amounts shown above as at 31 December 2012 are calculated as at this date.

No enhancements to retirement benefits were paid to or receivable by directors or former directors other than the discretionary pension increases awarded to all pensioners which have been made during the year.

Executive directors' service contracts

The normal notice of termination that the Company is required to give executive directors is 12 months. Accordingly, in normal circumstances, a director whose contract is terminated would be entitled to one year's salary and benefits in respect of their notice period. Additionally, outstanding awards under annual and long-term incentive plans may vest depending on the circumstances and according to the rules of the plans. When considering the termination of any service contract, the Remuneration Committee will have regard to the specific circumstances of each case, including the director's obligation to mitigate his loss. Payments are phased over the notice period.

Executive directors' service contracts provide details of the broad types of remuneration to which they are entitled, and about the kinds of plans in which they may be invited to participate. The service contracts offer no certainty as to the value of performance-related reward and confirms that any variable payment will be at the discretion of the company.

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Details of the service contracts of the executive directors are outlined below:

Executive director	Date of contract	Notice period to the Company	Notice period from the Company
Rob Devey	1 July 2009	12 months	12 months
John Foley	8 December 2010	12 months	12 months
Michael McLintock	21 November 2001	6 months	12 months
Nic Nicandrou	26 April 2009	12 months	12 months
Barry Stowe	18 October 2006	12 months	12 months
Tidjane Thiam	20 September 2007	12 months	12 months
Mike Wells[1]	15 October 2010	12 months	12 months

Note

(1) The contract for Mike Wells is a renewable one year fixed term contract. The contract is renewable automatically upon the same terms and conditions unless the Company or the director gives at least 90 days' notice prior to the end of the relevant term.

Policy on external appointments

Subject to the Group Chief Executive's or the Chairman's approval, executive directors are able to accept external appointments as non-executive directors of other organisations. Any fees paid may be retained by the executive director. During 2012, Michael McLintock received £47,500 as a trustee of another organisation (for reference, Michael McLintock received £45,000 for this role in 2011). Other directors served on the boards of educational, development, charitable and cultural organisations without receiving a fee for such services.

Chairman and Non-Executive Directors' letters of appointment and fees

Non-executive directors' letters of appointment

Non-executive directors do not have service contracts but are appointed pursuant to letters of appointment with notice periods of six months without liability for compensation.

Under the terms of their letters of appointment, continuation of the non-executive directors' appointment is contingent on satisfactory performance and re-election by shareholders. Non-executive directors are typically expected to serve two three year terms from the date of their election by shareholders. Thereafter, the Board may invite the Director to serve for an additional period.

Details of the letters of appointment for the non-executive directors are outlined below:

Non-executive director	Appointment by the Board	Initial election by shareholders at AGM	Notice period	Expiration of current term of appointment
Keki Dadiseth[1]	1 April 2005	AGM 2005	6 months	AGM 2013
Howard Davies	15 October 2010	AGM 2011	6 months	AGM 2014

Michael Garrett[2]	1 September 2004	AGM 2005	6 months	AGM 2013
Ann Godbehere	2 August 2007	AGM 2008	6 months	AGM 2014
Alistair Johnston	1 January 2012	AGM 2012	6 months	AGM 2015
Paul Manduca[3]	15 October 2010	AGM 2011	6 months	AGM 2014
Kaikhushru Nargolwala	1 January 2012	AGM 2012	6 months	AGM 2015
Kathleen O'Donovan[4]	8 May 2003	AGM 2004	6 months	n/a
Philip Remnant[5]	1 January 2013	AGM 2013	6 months	AGM 2016
Lord Turnbull	18 May 2006	AGM 2006	6 months	AGM 2015

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Notes

(1) Keki Dadiseth will retire from the Board on 1 May 2013.

(2) Michael Garrett was reappointed in 2012 for one year. The Board will consider a further renewal term in May 2013.

(3) Paul Manduca was appointed as Chairman of the Board on 2 July 2012.

(4) Kathleen O'Donovan retired from the Board on 31 March 2012.

(5) For Philip Remnant the table assumes initial election by shareholders at the 2013 AGM.

Chairman's letter of appointment, fees and benefits

Paul Manduca was appointed as a non-executive director on 15 October 2010 and became Senior Independent Director on 1 January 2011. On 2 July 2012 he was appointed Chairman. He is paid an annual fee of £600,000. A contractual notice period of 12 months by either party applies. Paul Manduca is provided with life assurance cover of four times his annual fees plus an additional sum to buy a dependants' annuity, private medical insurance and the use of a car and driver. No pension allowance is paid and he is not a member of any Group pension scheme.

Non-executive directors' fees

Non-executive directors are not eligible to participate in annual bonus plans, long-term incentive plans or pension arrangements. Their fees are determined by the Board and reflect their individual responsibilities, including chairmanship and membership of committees where appropriate. The Board reviews fees annually.

An increase of just under 3 per cent was made to the basic non-executive fee with effect from 1 July 2012. No increases were made to the additional fees paid to committee chairmen or members. The revised fees are shown below:

Annual Fees	**From 1 July 2012**
	(£)
Basic fee	87,500
Audit Committee Chairman additional fee	70,000
Audit Committee member additional fee	25,000
Remuneration Committee Chairman additional fee	50,000
Remuneration Committee member additional fee	25,000
Risk Committee Chairman additional fee	60,000
Risk Committee member additional fee	25,000
Senior Independent Director additional fee	50,000

Notes

(1) No fee is payable for chairmanship or membership of the Nomination Committee.

(2) The Company may determine that additional fees should be paid if, in a particular year, the number of meetings is materially greater than usual.

Please see the table on page 243 for details of the fees received by individual non-executive directors during 2012.

Non-executive directors' share ownership requirements

In July 2011, a share ownership requirement for non-executive directors was introduced. Non-executive directors are required to hold shares with a value equivalent to one times the annual basic fee (excluding additional fees for chairmanship and membership of any committees). Non-executive directors will be expected to attain this level of share ownership within three years of the

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implementation of this requirement (or within three years of their date of appointment, if later). The Chairman is required to hold shares with a value equivalent to one times his annual fee and is expected to attain this level of share ownership within five years of the date of his appointment.

Directors' shareholdings

The interests of directors in ordinary shares of the Company are set out below. 'Shares subject to deferral' includes shares acquired under the Share Incentive Plan (detailed in the table on page 251), deferred annual incentive awards and interests in shares awarded on appointment (detailed in the 'Other Share Awards' table on page 250).

	01 January 2012	31 December 2012				2 April 2013	Approximate Percentage of Ordinary Shares as of 2 April 2013
	Beneficial interest (number of shares)	Number of shares owned outright	Number of shares subject to deferral	Total beneficial interest (number of shares)	Number of shares subject to performance conditions	Beneficial interest (number of shares)	
Keki Dadiseth	32,196	32,196		32,196		32,196	0.002
Howard Davies	3,083	3,192		3,192		3,192	0.0002
Rob Devey	126,006	154,746	120,697	275,443	537,208	410,086	0.02
John Foley	364,378	277,178	46,057	323,235	351,917	357,962	0.02
Michael Garrett	39,233	39,233		39,233		39,233	0.002
Ann Godbehere	15,914	15,914		15,914		15,914	0.0007
Alistair Johnston[1]		5,000		5,000		5,000	0.0002
Paul Manduca	2,500	2,500		2,500		22,500	0.0009
Harvey McGrath[2]	300,636						
Michael McLintock	595,363	487,203	195,530	682,733	161,834	749,847	0.03
Kaikhushru Nargolwala[3]		16,000		16,000		16,000	0.0007
Nic Nicandrou[4]	167,655	227,791	123,067	350,858	546,037	499,286	0.02
Kathleen O'Donovan[5]	24,425						
Philip Remnant[6]						2,100	0.00009
Barry Stowe[7]	274,575	359,997	151,234	511,231	625,976	668,869	0.03
Tidjane Thiam	650,116	524,123	399,716	923,839	1,408,368	1,281,753	0.06
Lord Turnbull	16,624	16,624		16,624		16,624	0.0007
Mike Wells[8]	438,718	369,142	222,666	591,808	1,152,908	798,778	0.04

Notes

(1) Alistair Johnston was appointed to the Board on 1 January 2012.

(2) Harvey McGrath retired from the Board on 2 July 2012.

(3) Kaikhushru Nargolwala was appointed to the Board on 1 January 2012.

(4)

Nic Nicandrou's interest in shares on 2 April 2013 includes his monthly purchases made under the SIP plan in January, February and March 2013.

(5)

Kathleen O'Donovan retired from the Board on 31 March 2012.

(6)

Philip Remnant was appointed to the Board on 1 January 2013.

(7)

For the 31 December 2012 figure part of Barry Stowe's beneficial interest in shares is made up of 207,963 ADRs (representing 415,926 ordinary shares) and 95,305 ordinary shares. 8,513.73 of these ADRs are held within an investment account which secures premium financing for a life assurance policy). For the 2 April 2013 figure part of the beneficial interest in shares is made up of 286,782 ADRs (representing 573,564 ordinary shares) and 95,305 ordinary shares.

(8)

For the 31 December 2012 figure Mike Wells' beneficial interest in shares is made up of 295,904 ADRs (representing 591,808 ordinary shares). For the 2 April 2013 figure his beneficial interest in shares is made up of 399,389 (representing 798,778 ordinary shares). In the table above, the figure for shares subject to performance conditions reflects the maximum number of shares (150 per cent of the original number awarded) which may be released to Mike Wells under the JNL Performance Share Plan. This maximum number of shares may be released if stretch performance targets are achieved.

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Directors' remuneration for 2012

£000	Salary/ fees	2012 Cash bonus	2012 Deferred bonus	Total 2012 bonus	Benefits*	Cash supplements for pension purposes	Total emoluments 2012**	2012 employer pension contributions	Value of anticipated releases from LTIPs in respect of performance periods ending 31 December 2012	Total 2012 remuneration "The Single Figure"§
Chairman										
Paul Manduca[1]	393				71		464			464
Harvey McGrath[2]	252				50		302			302
Executive directors										
Rob Devey	600	426	284	710	114	150	1,574		1,804	3,378
John Foley	610	586	390	976	156	103	1,845	50		1,895
Michael McLintock[3]	360	904	404	1,308	124	93	1,885	218	3,190	5,293
Nic Nicandrou	630	655	437	1,092	99	158	1,979		1,804	3,783
Barry Stowe[4]	651	613	409	1,022	608	163	2,444	2	2,183	4,629
Tidjane Thiam	1,000	1,000	1,000	2,000	123	250	3,373		4,428	7,801
Mike Wells[5]	663	2,031	871	2,902	55		3,620	19	3,008	6,647
Total executive directors	**4,514**	**6,215**	**3,795**	**10,010**	**1,279**	**917**	**16,720**	**289**	**16,417**	**33,426**
Non-executive directors										
Keki Dadiseth[6]	120						120			120
Howard Davies	171						171			171
Michael Garrett	111						111			111
Ann Godbehere	181						181			181
Alistair Johnston	111						111			111
Kaikhushru Nargolwala	136						136			136
Kathleen O'Donovan[7]	28						28			28
Lord Turnbull	161						161			161
Total non-executive directors	**1,019**						**1,019**			**1,019**
Overall total	**6,178**	**6,215**	**3,795**	**10,010**	**1,400**	**917**	**18,505**	**289**	**16,417**	**35,211**

*

The value of benefits is the cost to the Company of providing core and additional benefits.

**

Each remuneration element is rounded to the nearest £1,000 and totals are the sum of these rounded figures.

Pension benefits are described in the section on 'Pension benefits' on page 238.

Value of anticipated long-term incentive plan releases is the total of cash paid plus, for shares released, the value of the released shares based on the average closing share price over the period 1 October 2012 to 31 December 2012. All executive directors participate in long-term incentive plans and the details of share releases from awards with a performance period ending 31 December 2012 are provided in the footnote to the tables on share awards on pages 247 and 248. This figure does not include releases from other share plans (detailed on page 250) or all-employee share plans, (set out on page 251). Dividend equivalents will be released on these vested shares.

§

"The Single Figure" is based on the methodology outlined on page 229.

Notes

(1)

Paul Manduca was appointed as Chairman on 2 July 2012. The figures above include the fees he received as senior independent non-executive director prior to his appointment as Chairman.

(2)

Harvey McGrath retired from the Board on 2 July 2012.

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(3)

"The Single Figure" for Michael McLintock includes the increase in transfer value of his defined benefit pension. This is outlined on page 239.

(4)

Barry Stowe's benefits relate primarily to his expatriate status, including costs of £217,567 for housing, £32,104 for children's education, £69,289 for home leave and a £248,894 Executive Director Location Allowance.

(5)

Mike Wells' bonus figure excludes a contribution of US$15,000 from a profit sharing plan which has been made into a 401(k) retirement plan. This is included under employers pension contribution.

(6)

Keki Dadiseth was paid allowances totalling £8,997 in respect of his accommodation expenses in London whilst on the Company's business.

(7)

Kathleen O'Donovan retired from the Board on 31 March 2012.

Directors' remuneration for 2011

	Salary/ fees	2011 Cash bonus	2011 Deferred bonus	Total 2011 bonus	Benefits*	Cash supple-ments for pension purposes	Total emoluments 2011	Value of anticipated releases from LTIPs in respect of perform-ance periods ending 31 December 2011
£000								
Chairman								
Harvey McGrath	500				82		582	
Executive directors								
Rob Devey	550	479	319	798	111	138	1,597	1,544
John Foley[note 1]	550	518	345	863	139	100	1,652	
Michael McLintock	350	779	279	1,058	93	96	1,597	6,005
Nic Nicandrou	550	507	338	845	84	138	1,617	2,020
Barry Stowe[note 2]	641	579	386	965	544	160	2,310	2,341
Tidjane Thiam	900	785	785	1,570	116	225	2,811	1,910
Mike Wells[notes 1 and 3]	624	1,660	711	2,371	64		3,059	1,369
Total executive directors	4,165	5,307	3,163	8,470	1,151	857	14,643	15,189

Non-executive directors								
Keki Dadiseth[(note 4)]	102						102	
Howard Davies	153						153	
Michael Garrett	93						93	
Ann Godbehere	158						158	
Bridget Macaskill[(note 5)]	65						65	
Paul Manduca	156						156	
Kathleen O'Donovan	98						98	
James Ross[(note 6)]	33						33	
Lord Turnbull	129						129	
Total non-executive directors	987						987	
Overall total	5,652	5,307	3,163	8,470	1,233	857	16,212	15,189

*

Benefits include (where provided) the cost of providing the use of a car and driver, medical insurance, security arrangements and expatriate benefits.

Pension benefits are described in the section on 'Pensions and long-term savings' in the Item 6 of the 2011 20F.

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Value of anticipated long-term incentive plan releases is the total of cash paid plus, for shares released, the value of the released shares based on the share price at 31 December 2011. This figure does not include releases from other share plans or all-employee share plans. Dividend equivalents will be released on these vested shares.

Notes

(1) John Foley and Mike Wells were appointed to the board on 1 January 2011.

(2) Barry Stowe's benefits relate primarily to his expatriate status, including costs of £184,489 for housing, £32,077 for children's education, £35,093 for home leave and a £245,114 Executive Director Location Allowance.

(3) Mike Wells' bonus figure excludes a contribution of $12,250 from a profit sharing plan which has been made into a 401(k) retirement plan. This is included in the table on pension contributions.

(4) Keki Dadiseth was paid allowances totalling £8,997 in respect of his accommodation expenses in London whilst on the Company's business as is the usual practice for directors who are not resident in the UK.

(5) Bridget Macaskill retired from the Board on 30 September 2011.

(6) James Ross retired from the Board on 19 May 2011.

Payments and share releases in 2012 to past executive directors

Nick Prettejohn

The 2009 Directors' Remuneration Report provided details of the remuneration arrangements that would apply to Nick Prettejohn after he resigned from the position of Chief Executive UK & Europe. These arrangements were implemented as intended by the Committee.

The performance periods of Nick Prettejohn's GPSP and UK BUPP awards for 2009 ended on 31 December 2011. Vesting was prorated based on service (i.e. 9/36ths). Vesting remained dependent on performance achieved over the performance period and shares were released at the same time as for other participants in these plans.

The performance condition attached to the 2009 GPSP award was met in full and 100 per cent of the proportion of the award which was outstanding was released during 2012. Achievement against the shareholder capital value performance measure attached to the 2009 UK BUPP award was 12.5 per cent per annum (on a compound basis), so 87.5 per cent of the outstanding portion of this award was released during 2012. This award was the last that Nick Prettejohn had outstanding under a Prudential long-term incentive plan.

Clark Manning

Clark Manning stepped down from his role as President and Chief Executive of Jackson and as an executive director on 31 December 2010. Clark Manning remained Chairman of Jackson until 30 April 2011 and acted in an advisory role until 31 December 2011. The 2010 Directors' Remuneration Report provided details of the remuneration arrangements that would apply to Clark Manning after his resignation. These arrangements were implemented as intended by the Committee.

During 2012, Clark Manning received the following payments:

Clark Manning had a prorated 2011 annual bonus opportunity (4/12ths) based on his length of service as Chairman of Jackson during 2011. On this basis, a cash payment of £725,389 was made to him in 2012.

The deferred portion of the bonuses awarded to Clark Manning in respect of performance in 2009 and 2010 were released to Clark Manning in July 2012.

The performance condition attached to the 2009 GPSP award was met in full and 100 per cent of the award was released in 2012.

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Achievement against the shareholder capital value performance measure attached to the 2009 JNL BUPP award was 11.5 per cent per annum (on a compound basis) so 93.75 per cent of the outstanding portion of this award was released in 2012.

The performance condition attached to the 2010 GPSP award was met in full and 100 per cent of the award will be released during 2013. Achievement of the SCV performance measure attached to the 2010 Jackson BUPP award was 22.68 per cent per annum (on a compound basis), so 100 per cent of the outstanding portion of this award will be released during 2013.

Outstanding 2010 awards made to Clark Manning under the GPSP and BUPP will vest (subject to the achievement of performance conditions) on the same schedule as awards made to other executive directors. These awards will be prorated to reflect the portion of the performance periods which had elapsed on 31 December 2011 (ie 24/36ths).

No awards were made to Clark Manning under any long-term incentive plan during 2011 or 2012 and none will be made in any subsequent year.

Payments and share releases in 2012 to newly appointed executive directors

Share awards made to Nic Nicandrou and Rob Devey in connection with their appointment were released, as scheduled, during 2012. Details of these awards were originally set out in the Directors' remuneration report for 2009. Please see the Other share awards table for details.

No other amounts were paid during the financial year or were receivable by directors (or past directors) in connection with leaving the organisation.

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Directors' outstanding long-term incentive awards

Share-based long-term incentive awards

The section below sets out the outstanding share awards under the Group Performance Share Plan and the awards made under additional long-term plans (Business Unit Performance Plan and JNL Performance Share Plan) for the executive directors with regional responsibilities.

	Plan name	Year of award	Conditional share awards outstanding at 1 Jan 2012 (Number of shares)	Conditional awards in 2012 (Number of shares)	Market price at date of award (pence)	Dividend equivalents on vested shares (Number of shares released) (note 2)	Rights exercised in 2012	Rights lapsed in 2012	Conditional share awards outstanding at 31 December 2012 (Number of shares)	Date of end of performance period
Rob Devey										
	GPSP	2009	120,898		639	15,361	136,259			31-Dec-11
	BUPP	2009	120,897		639	15,361	136,258			31-Dec-11
	GPSP	2010	104,089		568.5				104,089	31-Dec-12
	BUPP	2010	104,089		568.5				104,089	31-Dec-12
	GPSP	2011	76,242		733.5				76,242	31-Dec-13
	BUPP	2011	76,242		733.5				76,242	31-Dec-13
	GPSP	2012		88,273	678				88,273	31-Dec-14
	BUPP	2012		88,273	678				88,273	31-Dec-14
			602,457	**176,546**		**30,722**	**272,517**		**537,208**	
John Foley										
	GPSP	2011	152,484		733.5				152,484	31-Dec-13
	GPSP	2012		199,433	678				199,433	31-Dec-14
			152,484	**199,433**					**351,917**	
Michael McLintock										
	GPSP	2009	92,022		455.5	11,691	103,713			31-Dec-11
	GPSP	2010	66,238		568.5				66,238	31-Dec-12
	GPSP	2011	48,517		733.5				48,517	31-Dec-13
	GPSP	2012		47,079	678				47,079	31-Dec-14
			206,777	**47,079**		**11,691**	**103,713**		**161,834**	
Nic Nicandrou										
	GPSP	2009	316,328		639	40,197	356,525			31-Dec-11

	GPSP	2010	208,179		568.5			208,179	31-Dec-12
	GPSP	2011	152,484		733.5			152,484	31-Dec-13
	GPSP	2012		185,374	678			185,374	31-Dec-14
			676,991	**185,374**		**40,197**	**356,525**	**546,037**	
Barry Stowe (note 1)									
	GPSP	2009	196,596		455.5	22,868	219,464		31-Dec-11
	BUPP	2009	196,596		455.5	19,780	189,834	26,542	31-Dec-11
	GPSP	2010	129,076		568.5			129,076	31-Dec-12
	BUPP	2010	129,076		568.5			129,076	31-Dec-12
	GPSP	2011	88,270		733.5			88,270	31-Dec-13
	BUPP	2011	88,270		733.5			88,270	31-Dec-13
	GPSP	2012		95,642	678			95,642	31-Dec-14
	BUPP	2012		95,642	678			95,642	31-Dec-14
			827,884	**191,284**		**42,648**	**409,298**	**26,542**	**625,976**	
Tidjane Thiam									
	GPSP	2009	299,074		455.5	38,004	337,078		31-Dec-11
	GPSP	2010	510,986		568.5			510,986	31-Dec-12
	GPSP	2011	374,279		733.5			374,279	31-Dec-13
	GPSP	2012		523,103	678			523,103	31-Dec-14
			1,184,339	**523,103**		**38,004**	**337,078**	**1,408,368**	
Mike Wells (note 1 & 5)									
	JNL PSP	2008	84,900		546		84,900		31-Dec-11
	JNL PSP	2009	218,100		455.5			218,100	31-Dec-12
	JNL PSP	2010	141,000		568.5			141,000	31-Dec-13
	GPSP	2011	197,648		733.5			197,648	31-Dec-13
	BUPP	2011	197,648		733.5			197,648	31-Dec-13
	GPSP	2012		199,256	678			199,256	31-Dec-14
	BUPP	2012		199,256	678			199,256	31-Dec-14
			839,296	**398,512**			**84,900**	**1,152,908**	

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Notes

(1) The awards for Barry Stowe and Mike Wells were made in ADRs (1 ADR = 2 Prudential plc shares). The figures in the table are represented in terms of Prudential shares.

(2) In 2009 and 2010 a scrip dividend equivalent and in 2011 and 2012 a DRIP dividend equivalent were accumulated on these awards.

(3) On 31 December 2012 the performance period of the 2010 GPSP awards came to an end. Prudential's TSR performance was 139.9 per cent of the TSR performance of the peer index. On this basis, it is anticipated that awards granted under this plan in 2010 will vest in full. This will result in 104,089 shares vesting for Rob Devey, 66,238 shares for Michael McLintock, 208,179 shares for Nic Nicandrou, 129,076 shares for Barry Stowe and 510,986 shares for Tidjane Thiam under this plan. Dividend equivalents will be released on these vested shares.

(4) At 31 December 2012, the performance period of the 2010 BUPP awards came to an end. Over the performance period the new business profit, IFRS profit and cash remittance achieved by the Asian business meant that it is anticipated that 95.2 per cent of the award will vest. This will result in 122,880 shares being released to Barry Stowe under this plan. Since the UK BUPP uses the same TSR performance measure as the GPSP, it is anticipated that 104,089 shares will be released to Rob Devey under this plan. No current executive director participated in the 2010 JNL BUPP. Dividend equivalents will be released on these vested shares.

(5) The table above reflects the maximum number of shares (150 per cent of the original number awarded) which may be released to Mike Wells under the JNL Performance Share Plan. This maximum number of shares may be released if stretch performance targets are achieved. On 31 December 2012, the performance period of the 2009 JNL Performance Share Plan award came to an end. On the basis of the shareholder value being achieved by the Jackson business over the performance period, it is anticipated that 150 per cent of awards will vest, resulting in 218,100 shares being released to Mike Wells under this plan in 2013.

Business-specific cash-based long-term incentive plans

Details of all outstanding awards under cash-based long-term incentive plans are set out in the table below. The performance period for all M&G Executive LTIP awards is three years while the performance period for all JNL LTIP awards is four years:

Year of initial award	Face value of conditional share awards outstanding at	Conditionally awarded in 2012	Payments made in 2012	Face value of conditional share awards outstanding at	Date of end of performance period

		1 January 2012		31 December 2012	
		£000			
Michael McLintock					
M&G Executive LTIP	2009	1,830	5,417		31-Dec-11
M&G Executive LTIP	2010	987		987	31-Dec-12
M&G Executive LTIP	2011	1,318		1,318	31-Dec-13
M&G Executive LTIP	2012		953	953	31-Dec-14
Total cash payments made in 2012			5,417		
Mike Wells					
JNL LTIP	2008	756	827		31-Dec-11
JNL LTIP	2009	894		894	31-Dec-12
JNL LTIP	2010	906		906	31-Dec-13
Total cash payments made in 2012			827		

Note

Under the M&G Executive LTIP, the value of each unit at award is £1. The value of units changes based on M&G's profit growth and investment performance over the performance period. For the 2009 award of 1,830,189 units, the unit price at the end of the performance period was £2.96 which resulted in a payment of £5,417,359 to Michael McLintock during 2012.For the

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2010 award of 987,179 units, the unit price at the end of the performance period was £2.65. This will result in payment of £2,616,024 to Michael McLintock in 2013.

See page 236 for a description of the JNL LTIP. Performance over the period from 2008 to 2011 resulted in a payment of £826,975 to Mike Wells during 2012. Performance over the period from 2009 to 2012 will result in a payment of £1,117,509 being paid to Mike Wells in 2013. The awards above were made before Mike Wells became an executive director and it is anticipated that no further awards will be made to him under this Plan.

The sterling face value of Mike Wells' JNL LTIP awards have been calculated using the average exchange rate for the year in which the grant was made. The dollar face value of conditional share awards outstanding on 1 January 2012 and 31 December 2012 was US$4,200,000 and US$2,800,000 respectively.

Other share awards

The table below sets out the share awards that have been made to executive directors under their appointment terms and those deferred from annual incentive plan payments. The number of shares is calculated using the average share price over the three business days commencing on the day of the announcement of the Group's annual financial results for the relevant year. For the awards from the 2011 annual incentives, made in 2012, the average share price was 776 pence. Please see the table on page 251 for details of shares acquired under the Share Incentive Plan.

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	Year of grant	Conditional share awards outstanding at 1 Jan 2012 (Number of shares)	Conditional awarded in 2012 (Number of shares)	Dividends accumulated in 2012 (note 2) (Number of shares)	Shares released in 2012 (Number of shares)	Conditional share awards outstanding at 31 December 2012 (Number of shares)	Date of end of restricted period	Date of release	Market price at date of award (pence)	Market price at date of vesting or release (pence)
Rob Devey										
Awards under appointment terms	2009	**50,575**			**50,575**		31-Mar-12	29-Mar-12	639	750
Deferred 2009 annual incentive award	2010	**28,737**		**1,018**		**29,755**	31-Dec-12		552.5	
Deferred 2010 annual incentive award	2011	**46,694**		**1,655**		**48,349**	31-Dec-13		721.5	
Deferred 2011 annual incentive award	2012		**41,136**	**1,457**		**42,593**	31-Dec-14		750	
		126,006	**41,136**	**4,130**	**50,575**	**120,697**				
John Foley										
Deferred 2009 deferred PruCap award	2010	**172,993**		**6,133**	**179,126**		14-Dec-12	14-Dec-12	612	881
Deferred 2011 annual incentive award	2012		**44,481**	**1,576**		**46,057**	31-Dec-14		750	
		172,993	**44,481**	**7,709**	**179,126**	**46,057**				
Michael McLintock										
Deferred 2008 annual incentive award	2010	**137,700**			**137,700**		31-Dec-11	15-Mar-12	519.5	780
Deferred 2009 annual incentive award	2010	**74,840**		**2,653**		**77,493**	31-Dec-12		552.5	
Deferred 2010 annual incentive award	2011	**77,988**		**2,765**		**80,753**	31-Dec-13		721.5	
	2012		**36,008**	**1,276**		**37,284**	31-Dec-14		750	

Deferred 2011 annual incentive award									
		290,528	**36,008**	**6,694**	**137,700**	**195,530**			
Nic Nicandrou									
Awards under appointment terms	2009	**68,191**			**68,191**		31-Mar-12	29-Mar-12	639	750
Deferred 2009 annual incentive award	2010	**26,342**		**934**		**27,276**	31-Dec-12		552.5	
Deferred 2010 annual incentive award	2011	**48,155**		**1,707**		**49,862**	31-Dec-13		721.5	
Deferred 2011 annual incentive award	2012		**43,518**	**1,542**		**45,060**	31-Dec-14		750	
		142,688	**43,518**	**4,183**	**68,191**	**122,198**				
Barry Stowe (note 1)									
Deferred 2008 annual incentive award	2009	**22,643**			**22,643**		31-Dec-11	15-Mar-12	349.5	780
Deferred 2009 annual incentive award	2010	**39,088**		**1,386**		**40,474**	31-Dec-12		552.5	
Deferred 2010 annual incentive award	2011	**56,316**		**1,998**		**58,314**	31-Dec-13		721.5	
Deferred 2011 annual incentive award	2012		**50,648**	**1,798**		**52,446**	31-Dec-14		750	
		118,047	**50,648**	**5,182**	**22,643**	**151,234**				
Tidjane Thiam									
Deferred 2008 annual incentive award	2010	**69,924**			**69,924**		31-Dec-11	15-Mar-12	552.5	780
Deferred 2009 annual incentive award	2010	**63,240**		**2,242**		**65,482**	31-Dec-12		552.5	
Deferred 2010 annual incentive award	2011	**221,657**		**7,858**		**229,515**	31-Dec-13		721.5	
Deferred 2011 annual incentive	2012		**101,134**	**3,585**		**104,719**	31-Dec-14		750	

award							
		354,821	**101,134**	**13,685**	**69,924**	**399,716**		
Mike Wells (note 1)							
2009 After Tax Deferral Program award (note 3)	2010	**32,250**			**32,250**	15-Mar-13	520
Deferred 2010 Group Defered Bonus Plan award	2011	**90,854**		**3,226**	**94,080**	31-Dec-13	721.5
Deferred 2011 annual incentive award	2012		**93,034**	**3,302**	**96,336**	31-Dec-14	750
		123,104	**93,034**	**6,528**	**222,666**		

Notes

(1) The Deferred Share Awards in 2010, 2011 and 2012 for Barry Stowe and Mike Wells were made in ADRs (1 ADR = 2 Prudential plc shares). The figures in the table are represented in terms of Prudential shares.

(2) In 2009 and 2010 a scrip dividend equivalent and in 2011 and 2012 a DRIP dividend equivalent were accumulated on these awards.

(3) This award attracts dividends in the form of cash rather than shares.

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Shares acquired under the Share Incentive Plan

	Year of initial grant	Share Incentive Plan awards held in Trust at 1 January 2012 (Number of shares)	Partnership shares accumulated in 2012 (Number of shares)	Matching shares accumulated in 2012 (Number of shares)	Dividend shares accumulated in 2012 (Number of shares)	Share Incentive Plan awards held in Trust at 31 December 2012 (Number of shares)
Nic Nicandrou						
Shares held in Trust	2010	596	199	50	24	869

Note

The table above provides information about shares purchased under the SIP together with Matching shares (awarded on a 1:4 basis) and Dividend shares. The total number of shares will only be released if Nic Nicandrou remains in employment for five years.

Outstanding share options

The following table sets out the share options held by the directors in the UK Savings-Related Share Option Scheme (SAYE) as at the end of the period. No other directors held shares in any other option scheme.

	Date of grant	Exercise price	Market price at 31 Dec 2012	Exercise period		Number of options				
				Beginning	End	Beginning of period	Granted	Exercised	Lapsed	End of period
John Foley	25 Apr 08	551	865.5	01 Jun 13	29 Nov 13	2,953				2,953
Tidjane Thiam	16 Sep 11	465.8666	865.5	01 Dec 14	29 May 15	965				965
Nic Nicandrou	16 Sep 11	465.8666	865.5	01 Dec 16	31 May 17	3,268				3,268
Rob Devey	16 Sep 11	465.8666	865.5	01 Dec 16	31 May 17	3,268				3,268

Notes

(1) No gains were made by directors in 2012 on the exercise of SAYE options (2011: £665).

(2) No price was paid for the award of any option.

(3) The highest and lowest closing share prices during 2012 were 911.5 pence and 633.5 pence respectively.

Dilution

Releases from Prudential's GPSP and BUPP are satisfied using new issue shares rather than by purchasing shares in the open market. Shares relating to options granted under all-employee share plans are also satisfied by new issue shares. The combined dilution from all outstanding shares and options at 31 December 2012 was 0.1 per cent of the total share capital at the time. Deferred shares will continue to be satisfied by the purchase of shares in the open market.

Company TSR performance (unaudited information)

As required by the Companies Act, the line chart below compares Prudential's Total Shareholder Return (TSR) during the five years from 1 January 2008 to 31 December 2012, with that of the peer group against which TSR is measured for the purposes of the Group Performance Share Plan. Our

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performance is also shown relative to the FTSE 100 since Prudential is a major company within this index. This chart is prepared using the methodology stipulated in the current remuneration regulations:

Prudential TSR v FTSE 100 and peer group index total returns % over 5 years to December 2012

Share Ownership

Directors shareholdings

The current shareholding policy and the interests of directors in ordinary shares of Prudential are shown under the sections 'Compensation Shareholding guidelines' and 'Compensation Directors' Shareholdings' above.

Prudential is not owned or controlled directly or indirectly by another corporation or by any government or by any other natural or legal person severally or jointly and Prudential does not know of any arrangements that might result in a change in Prudential's control.

In addition, Prudential's directors held, as at 2 April 2013, options to purchase 10,454 shares, all of which were issued under Prudential's Savings-Related Share Option Scheme (SAYE). These options and plans are described in more detail below under 'Options to purchase securities from Prudential' in this section.

Outstanding options of directors and other executive officers

The SAYE is open to all UK and certain overseas employees. Options under this scheme up to HM Revenue & Customs (HMRC) limits are granted at a 20 per cent discount and cannot normally be exercised until a minimum of three years has elapsed. No payment is made for the grant of any options.

The share options held by the directors and other executive officers as at the end of period are shown under the section 'Compensation Outstanding share options' above.

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Options to purchase and discretionary awards of securities from Prudential

As of 2 April 2013, 9,272,286 options were outstanding, which Prudential issued under the SAYE schemes. As of 2 April 2013 directors and other executive officers held 10,454 of such outstanding options. Except as described above in 'Outstanding options of directors and other executive officers', each option represents the right of the bearer to subscribe for one share at a particular pre-determined exercise price at a pre-set exercise date.

As of 2 April 2013, 2,574 options were outstanding under the RSP. Such outstanding options held by directors or other executive officers at 31 December 2012 are included in the shares set forth under 'Long-term incentive plans' in the 'Compensation' section above.

As of 2 April 2013, 1,751,674 shares were outstanding under the Prudential Jackson National Life US Performance Share Plan. Such outstanding awards held by directors or other executive officers at 31 December 2012, are included in the shares set forth under 'Long-term incentive plans' in the 'Compensation' section above.

As of 2 April 2013, 16,223,175 shares were outstanding under other awards. Of those, 1,341,789 shares were outstanding under the Annual Incentive Plan, 848,334 shares were outstanding under the PruCap Deferred Bonus Plan, 392,835 shares were outstanding under the Momentum Retention Plan, 763,646 shares were outstanding under the One Off Awards, 5,009,393 shares were outstanding under the GPSP, 1,151.365 shares were outstanding under the BUPP, 2,327,972 shares were outstanding under the Deferred Share Plans, 3,805,841 shares were outstanding under the PCA LTIP and 582,000 were outstanding under the Prudential Agency Long Term Incentive Plan. Such outstanding awards held by directors or other executive officers at 31 December 2012 are included under 'Long-term incentive plans' in the 'Compensation' section above.

The aggregate proceeds that would arise if all outstanding options under the SAYE schemes were exercised is £42 million. The latest expiration dates for exercise or release of the securities underlying the options or awards and the number of options or shares are set out in the table below.

Year of Expiration	Shares Outstanding Under the Prudential Jackson National Life US Performance Share Plan	Options Outstanding Under Restricted Share Plan	Options Outstanding Under Savings Related Share Option Scheme	Shares Outstanding Under Other Awards	Total
			(In Millions)		
2012			0.124		0.124
2013			0.095	0.672	0.767
2014	1.25		4.019	7.207	12.476
2015	0.502	0.003	1.512	7.27	9.287
2016			2.779	0.938	3.717
2017			0.469	0.07	0.539
2018			0.274	0.05	0.324
2019				0.016	0.016
Total	1.752	0.003	9.272	16.223	27.25

Information concerning the Group's share award and share option plans for its employees is provided in 'Compensation' above as well as in Note I4 to the consolidated financial statements in Item 18.

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Board Practices

In accordance with Prudential's Articles of Association the Board, or the members in a general meeting, may appoint up to 20 directors. In line with UK corporate governance guidelines, all directors submit themselves for annual re-election by shareholders at the Annual General Meeting and any director appointed by the Board will retire at the first Annual General Meeting following his or her appointment and offer himself or herself for election by shareholders.

Non-executive directors of Prudential are usually appointed for an initial three-year term, commencing with their election by shareholders at the first Annual General Meeting following their appointment. Each appointment is reviewed towards the end of the three-year term against performance and the requirements of the Group's businesses. Non-executive directors are typically expected to serve for two terms of three years from their initial election by shareholders, although the Board may invite them to serve for an additional period. Their appointment is subject to continued performance evaluation and re-election by shareholders.

The Group Company Secretary supports the Chairman in providing tailored induction programs for new directors and on-going development for all directors. On appointment, all directors embark upon a wide-ranging induction program covering, amongst other things, the principal bases of accounting for the Group's results, the role of the Board and its key committees, and the ambit of the internal audit and risk management functions. In addition, they receive detailed briefings on the Group's principal businesses, its product range, the markets in which it operates and the overall competitive environment. Other areas addressed include the directors' obligations under the different listing regimes to which Prudential is subject, legal issues affecting directors of financial services companies, the Group's governance arrangements, its investor relations program, as well as its remuneration policies.

Directors have a statutory duty to avoid conflicts of interest with the Company. The Company's Articles of Association allow the directors to authorise conflicts of interest, and the Board has adopted a policy and effective procedures on managing and, where appropriate, approving conflicts or potential conflicts of interest. Under these procedures directors are required to declare all directorships or other appointments to companies which are not part of the Group as well as other situations which could result in conflicts or could give rise to a potential conflict. The Nomination Committee, or the Board where appropriate, evaluates and approves each such situation individually where applicable.

Directors' indemnities and protections

Suitable insurance cover is in place in respect of legal action against directors and senior managers of companies within the Prudential Group. Protection for directors, and certain senior managers, of companies within the Group, against personal financial exposure which may be incurred in their capacity as such, is also provided. These include qualifying third party indemnity provisions (as defined by the Companies Act 2006) for the benefit of directors of Prudential plc and other such persons including, where applicable, in their capacity as directors of other companies within the Group. These indemnities were in force during 2012 and remain in force.

In addition, the Articles of Association of the Company permit the directors and officers of the Company to be indemnified in respect of liabilities incurred as a result of their office.

External appointments

Directors may hold directorships or other significant interests in companies outside the Group which may have business relationships with the Group.

Non-executive directors may serve on a number of other boards provided that they are able to demonstrate satisfactory time commitment to their role at Prudential and that they discuss any new appointment with the Chairman prior to accepting. This ensures that they do not compromise their

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independence and that any potential conflicts of interest and any possible issues arising out of the time commitments required by the new role can be identified and addressed appropriately. The major commitments of our non-executive directors are detailed in their biographies set out on page 218 to 224.

Executive directors may accept external directorships and retain any fees earned from those directorships subject to prior discussion with the Group Chief Executive and always provided this does not lead to any conflicts of interest. In line with the UK Code, executive directors would be expected to hold no more than one non-executive directorship, nor the chairmanship, of a FTSE 100 company. Some of our executive directors hold directorships or trustee positions of unquoted companies or institutions. Details of any fees retained are included in Item 6 Compensation-Policy on external appointments.

Audit Committee Report

The Committee's responsibilities consist of oversight over financial reporting, the effectiveness of the internal control systems and monitoring auditor independence. Its duties include gaining assurance on the control over financial processes and the integrity of the Group's financial reports, monitoring the performance, objectivity and independence of the external auditor, reviewing the work of the internal auditor and providing oversight to the Group Compliance function.

During 2012, the Audit Committee continued to focus on ensuring the Group's financial reporting remained clear, robust and informative, and continued to work closely with the Risk Committee to ensure an integrated approach to risk assurance and risk management was achieved. The Committee met regularly with the Group-wide Internal Audit Director and the Audit Partner from the external auditor.

The principal responsibilities of the Committee are to:

- monitor the integrity of the financial statements, including the review of half and full-year results, the annual report and accounts and other significant financial announcements and review the critical accounting policies and key judgmental areas contained therein;
- monitor the framework and effectiveness of the Group's systems of internal control, including the Turnbull compliance statement and Sarbanes-Oxley procedures;
- monitor auditor independence and the external auditor's plans and audit strategy, the effectiveness of the external audit process, the external auditor's qualifications, expertise and resources, and make recommendations for the re-appointment of the external auditor;
- review the internal audit plan and resources, and monitor the audit framework and effectiveness of the internal audit function;
- monitor the effectiveness of compliance processes and controls, and performance against the Group Compliance Plan;
- review the anti-money laundering procedures in place, as well as the review of procedures operated for handling allegations from whistleblowers; and
- review the effectiveness of the business unit audit committees.

The Audit Committee has received balanced and timely information over the course of the year which has enabled it to provide effective oversight of the Group's key financial reporting risks and internal controls.

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Membership

The Audit Committee (the Committee) is comprised of the non-executive directors as set out below:

Ann Godbehere *(Chairman)*
Howard Davies
Alistair Johnston
Paul Manduca (to 2 July 2012)
Kathleen O'Donovan (to 31 March 2012)
Philip Remnant (from 1 January 2013)

The membership is selected to provide a broad range of financial, commercial and other experience relevant to meet the Committee's objectives.

In performing its duties, the Committee has access to employees and their financial or other relevant expertise across the Group and to the services of the Group-wide Internal Audit Director and the Group Company Secretary. The Committee may also seek external professional advice at the Company's expense.

Full biographical details of the members of the Committee are set out on pages 218 to 224.

Meetings

The Committee meets at least five times a year and gives consideration to the financial statements of the Group and the Group's system of internal control, as well as its internal and external audit providers. The Chairman of the Committee is a member of the Risk Committee and works closely with that committee in fulfilling the Audit Committee's responsibilities.

By invitation, the Chairman of the Board, the Group Chief Executive, the Chief Financial Officer, the Group Chief Risk Officer and the Group General Counsel, as well as other senior staff from the group finance, internal audit, risk, compliance and security functions attended the meetings to contribute to the discussions relating to their respective areas of expertise. The lead and other partners of the external auditor also attended the meetings.

During 2012, the Committee held twelve scheduled meetings.

A detailed forward agenda has been in operation for a number of years and is reviewed and updated regularly to ensure all matters for which the Committee is responsible are addressed at the appropriate time of year.

The Committee also received in-depth presentations on a range of topics and received the minutes of both the Disclosure Committee and the Assumptions Approval Committee. Further information on risk governance appears on pages 68 and 71 respectively.

The Committee Chairman reported to the Board on matters of particular significance after each meeting and the minutes were circulated to all Board members. The terms of reference for the Committee are kept under regular review and are updated where required. A copy of these can be found on the Company's website.

The Committee recognises the need to meet without the presence of executive management. Such sessions were held with the external auditor in July and October 2012, and with the internal auditor in July 2012. At all other times management and auditors had open access to the Chairman and the Committee.

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Financial reporting

The Committee is regularly briefed by management on developments in International Financial Reporting Standards and focussed on the critical accounting policies and practices as part of its review of financial statements prior to recommending their publication to the Board. The Committee also reviewed any changes or decisions requiring a major element of judgement, unusual transactions, clarity of disclosures, significant audit adjustments (of which there were none in 2012), the going concern assumption, compliance with accounting standards, and compliance with obligations under applicable laws, regulations and governance codes.

Confidential reporting

A standing agenda item of the Committee is to review a report on the use of the confidential reporting procedures, which are available to employees to enable them to communicate confidentially, and anonymously if they so wish, on matters of concern and actions taken in response to these communications.

No material control implications were raised through these procedures during the year.

Business unit audit committees

Every business unit has its own audit committee which provides oversight to the respective business unit and reports any relevant matters to the Committee. The members and chairmen are comprised primarily of senior management who are independent of the respective business unit. The minutes of these committees are reported regularly to the Committee and their meetings are attended by senior management of the respective business unit, including the business units' heads of finance, risk, compliance and Group-wide internal audit.

Business unit audit committees have adopted standard terms of reference across the Group with minor variations to address local requirements or particular requirements of the business. The terms of reference of those committees were reviewed during the year and all include escalation of significant matters to the Committee, recommendations for approval of the business unit internal audit plans and overseeing the adequacy of internal audit resources. During the year the business unit audit committees reviewed their respective internal audit plans, resources and the results of internal audit work, and both external and internal auditors were able to discuss any relevant matters with the Chairman and members of the Committee as required.

Effectiveness of business unit audit committees

Group-wide Internal Audit has reviewed the effectiveness of each business unit audit committee using an established evaluation tool. The evaluation comprises an annual review questionnaire which is divided into specific areas for appraisal and a walk through of each committee's terms of reference, assessing whether these are appropriate for the business unit and if the committee has fulfilled its responsibilities under the terms. A memorandum summarising the findings of the review, as well as any action points, is compiled for each business unit audit committee.

The findings were reviewed by the Group-wide Internal Audit business unit audit director in conjunction with the Chairman and discussed by the respective business unit audit committees. In addition, the Chairman of each business unit audit committee has confirmed that, in their opinion, the current members have the appropriate balance of skills, knowledge and expertise to oversee the relevant business unit.

On completion of the review, Group-wide Internal Audit concluded that the overall arrangements for the business unit audit committees remained appropriate for the nature and purpose of each

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business unit and that each business unit audit committee continued to meet the responsibilities as set out in their respective terms of reference.

Internal control and risk management

The Committee reviewed the Group's statement on internal control systems prior to its endorsement by the Board.

Pursuant to the requirements of Section 404 of the Sarbanes-Oxley Act, the Group undertakes an annual assessment of the effectiveness of internal control over financial reporting. Further details are provided below.

Group-wide Internal Audit

The Committee regards its relationship with the internal audit function as pivotal to the effectiveness of its own activities. Group-wide Internal Audit plays an important role in supporting the Committee to fulfil its responsibilities under the UK and HK Codes, as well as the Sarbanes-Oxley Act, and provides independent assurance on the Group's processes of identification and control of risk. Each of the Group's business units has an internal audit team, the heads of which report to the Group-wide Internal Audit Director. Internal audit resources, plans and work are overseen by the Committee and by the business unit audit committees. Total approved internal audit headcount across the Group was 148 at 31 December 2012. The Group-wide Internal Audit Director reports functionally to the Committee and for management purposes to the Chief Financial Officer.

The Committee assesses the effectiveness of the internal audit function by means of regular reviews, some of which are carried out by external advisers, and through ongoing dialogue with the Group-wide Internal Audit Director. A further external effectiveness review of Group-wide Internal Audit was undertaken in quarter four 2012, the findings of which were reported to the Committee in detail in February 2013. The purpose of the review was to ensure that the activities and resources of internal audit continue to be effectively organised to support the oversight responsibilities of the Committee. The review, performed by PwC, confirmed that Group-wide Internal Audit continued to remain in general conformance with the Institute of Internal Auditors (IIA) International Standards with no material exceptions and demonstrated a noted enhancement of GwIA processes and practices, since the last review in 2011.

The Committee approved the Group-wide Internal Audit annual audit plan of assurance work to be undertaken during 2013.

Group Compliance

The Committee receives regular reports from Group Compliance, who are responsible for assessing the risks posed to the Group as a result of non-compliance with relevant regulations, including those in respect of anti-money laundering and sanctions. Each business unit has its own compliance function, and the role of Group Compliance is to assess the effectiveness of these functions, as well as to provide oversight and support in the identification, mitigation and reporting of regulatory risks arising from both current business activities and from changes in the regulatory environment.

During 2012, the Committee reviewed and approved the target operating model, as well as the plan of work to be undertaken by Group Compliance during 2013.

Remuneration Committee Report

The Remuneration Committee determines the remuneration packages of the Chairman and executive directors. It also monitors the level and structure of remuneration for a defined population of management and for individuals with the opportunity to earn over £1,000,000 per annum.

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The principal responsibilities of the Committee are to:

- determine the remuneration policy for the Chairman and approve the remuneration of the executive directors of the Company; and
- oversee the remuneration of a defined leadership population and for individuals with the opportunity to earn over £1 million per annum.

Each business unit also has its own remuneration committee, with similar terms of reference, to ensure effective remuneration governance in all our businesses.

Membership

The Remuneration Committee (the Committee) is comprised exclusively of non-executive directors, as set out below:

Lord Turnbull KCB CVO (Chairman)
Keki Dadiseth (to 1 May 2013)
Michael Garrett
Paul Manduca (to 2 July 2012)
Kai Nargolwala

Philip Remnant joined the Committee on 1 January 2013 and Anthony Nightingale will join the Committee from 1 June 2013.

Meetings

The Committee meets at least three times a year and more often if required. In 2012, the Committee met five times and held one meeting in January 2012 to conclude issues arising from the December 2012 meeting.

During the year, the Committee considered the Directors' Remuneration Report 2012 and approved the 2012 long-term incentive awards and performance measures, giving consideration to the annual bonus measures and targets to be used in 2013. The Committee also considered proposed changes to the remuneration architecture and reviewed the remuneration of the Group Leadership Team, senior risk staff and other employees with a remuneration opportunity in excess of £1m per annum. The annual bonuses for 2011 and the vesting of long-term incentive awards with a performance period ending on 31 December 2011, were approved by the Committee, as were the executive directors remuneration and incentive opportunities for 2013.

The Chairman reported to the Board on matters of significance after each meeting. The terms of reference for the Committee are kept under regular review and are updated where required. A copy of these can be found on the Company's website.

Nomination Committee Report

The Nomination Committee plays a leading role in assessing the balance of skills and experience on the Board and the Group's principal committees. The Committee identifies the roles and capabilities required to meet the demands of the business and, with due regard to diversity, ensures that suitable succession planning is in place. Candidates continue to be considered on merit against specific criteria determined by the Committee.

The Committee also reviews conflicts of interest or potential conflicts of interest raised by directors between Board meetings and for prospective Board members. In cases where there might be an actual or potential conflict of interest the Committee has powers to authorise any such actual or potential conflict situation on behalf of the Board, imposing any terms and conditions it deems appropriate, or to

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make recommendations to the Board as to whether the conflict or potential conflict should be authorised and if any specific terms should be included in the authorisation.

During 2012, the Committee, under the leadership of Lord Turnbull, led the search for the new Chairman and, once the Chairman had been appointed, embarked on the search for a Senior Independent Director led by the Chairman.

The principal responsibilities of the Committee are to:

- review the size, structure and composition of the Board, including the skills, knowledge, experience and diversity of Board members, and make recommendations to the Board with regard to changes;
- identify and nominate candidates for appointment to the Board, based on merit and against objective criteria;
- make recommendations to the membership of the audit, risk, remuneration and nomination committees in consultation with the Chairmen of those Committees; and
- consider and, where necessary, authorise any actual or potential situational conflicts, upon such terms and conditions as the Committee considers appropriate, arising out of a proposed new appointment, the changed circumstances of an existing appointment or that of a director's connected person.

The Committee will continue to review the time commitment required from each of our non-executive directors and, going into 2013, the Committee will continue to review and refresh the skills required to pursue our strategic objectives successfully.

Membership

The Nomination Committee (the Committee) is comprised of the Chairman and the non-executive directors as set out below:

Paul Manduca (Chairman from 2 July 2012)
Harvey McGrath (Chairman to 2 July 2012)
Howard Davies (from 2 July 2012)
Ann Godbehere (from 2 July 2012)
Kathleen O'Donovan (to 31 March 2012)
Philip Remnant (from 1 January 2013)
Lord Turnbull

In performing its duties, the Committee has access to employees and their relevant expertise across the Group and to the services of the Group Company Secretary. The Committee may also seek external professional advice at the Company's expense.

Full biographical details of the members of the Committee are set out on pages 218 to 224.

Meetings

The Committee meets at least twice a year to consider the Board composition and membership of the principal Committees and to consider the suitability of all directors standing for re-election at the AGM. In addition, the Committee meets to consider candidates for appointment to the Board. The Group Chief Executive is closely involved in the work of the Committee and is invited to attend and contribute to meetings. By invitation, the Group HR Director also attends the meetings.

The Committee met on nine occasions during 2012.

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As part of the process for appointing any new director, the Committee gives consideration to the balance of skills, experience and knowledge on the Board and, in light of this evaluation, prepares a description of the role and capabilities required for a particular appointment, as well as the expected time commitment. Appointments are made based on merit, against objective criteria which are established by the Committee.

The focus of the Committee during the year was the search for a new Chairman and a replacement for the role of the Senior Independent Director. Harvey McGrath, the retiring Chairman, was not involved in the selection or appointment of the new Chairman, a process which was led by Lord Turnbull. Once this appointment had been made, the Committee, led by Paul Manduca, initiated the process for finding a Senior Independent Director. The Committee used the services of Spencer Stuart, Korn Ferry International and Ridgeway Partners, executive search agencies to facilitate both of these searches. None of these firms undertook any other significant projects for the Group.

The Chairman reported to the Board on matters of particular significance after each meeting. The terms of reference for the Committee are kept under regular review and are updated where required. A copy of these can be found on the Group's website.

Risk Committee Report

The Risk Committee continued its work during 2012 with the specific objectives of furthering the in depth understanding of the risks facing the business and enhancing the risk reporting framework with a view to ensuring that the various stakeholders received both timely and suitable information around risk exposures.

The Committee provides leadership, direction and oversight in relation to the Group's overall risk appetite and tolerance and the risk management framework. Oversight of the framework includes reviewing the Group's risk policies and standards, supporting risk limits, methodologies adopted and the processes and controls in place for assessing the Group's risks. During the year the Committee carried out an in depth review of a number of policies and other components forming part of the overall Group Risk Framework and recommended improvements to the Board, providing effective oversight with regard to the Group's risk appetite, tolerance and risk management framework. The Committee also provides oversight in respect of the Group Chief Risk Officer's responsibilities.

The principal responsibilities of the Committee are to:

- review the Group risk, capital and liquidity management framework, as well as the Group's risk appetite, its risk policies and standards, including the parameters used and methodologies and processes adopted for identifying and assessing risks;
- review the material and emerging risk exposures of the Group, including market, credit, insurance, operational, liquidity and economic and regulatory capital risks as well as regulatory and compliance matters;
- oversee the Group's processes and policies for determining risk tolerance and reviewing management's measurement and effectiveness of the Group's risk tolerance levels;
- receive and review Group-wide Internal Audit Reports on the risk management function;
- assist the Board in reviewing the risks inherent in the business plans; and
- provide qualitative and quantitative advice to the Remuneration Committee on risk weightings applied to performance objectives incorporated in executive remuneration and evaluate whether the remuneration approach for senior executives was positioned within the Group's overall risk appetite framework.

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The Committee also continued to build synergies with the Audit Committee, to ensure that areas of overlap were managed appropriately.

Membership

The Risk Committee (the Committee) is comprised of the non-executive directors as set out below:

Howard Davies *(Chairman)*
Ann Godbehere
Kai Nargolwala
Lord Turnbull

In performing its duties, the Committee has access to the Group Chief Risk Officer, as well as other employees and their relevant expertise across the Group. The Committee also has access to the services of the Group Company Secretary and may seek external professional advice at the Company's expense.

Full biographical details of the members of the Committee are set out on pages 218 to 224.

Meetings

The Committee meets at least four times a year to consider the Group's risk appetite and provide oversight to the management of risk within the Group. The Chairman of the Committee is a member of the Audit Committee and works closely with that committee in fulfilling the Risk Committee's responsibilities.

The Chairman of the Board, the Group Chief Executive, the Chief Financial Officer, the Group Chief Risk Officer, Group-wide Internal Audit Director, the Group General Counsel and the Group Risk Directors are also invited to attend.

During 2012, the Committee held five scheduled meetings.

The Committee undertook the identification and comprehensive analysis of the Group's key risks and approved the enhancements to the management information provided to the Group risk committees and the Board. The Committee further received presentations from certain of the business units on the particular risks inherent in those businesses, as well as the systems and controls in place to monitor and manage those risks. The Committee approved and subsequently reviewed the process for approving large credit risk exposures; it also approved a framework which provides separate limits for global counterparties in respect of counterparty risk exposures. The Committee also reviewed the Group-wide risk appetite framework, including risk appetite statements and limits by risk type. The Committee worked closely with the Audit Committee to ensure any risk assurance relevant to financial reporting was referred to the Audit Committee and with the Remuneration Committee on providing input in respect of risk adjustment measures for the executive remuneration policy. In addition, the role of the Committee includes responding to the needs of the business and carrying out reviews of specific areas of risk as they arise. The Committee worked closely with management and the Group-wide Internal Audit Director during the year and assisted the Board by providing oversight over requests for specific risk assessments.

The Chairman reviewed the work of the Committee and the Group's risk framework as part of the ongoing dialogue with the regulator.

The Committee Chairman reported to the Board on matters of significance after each meeting and the minutes were circulated to all Board members. The terms of reference for the Committee are kept under regular review and are updated where required. A copy of these can be found on the Group's website.

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NYSE Corporate Governance Rules compared to Prudential plc's Corporate Governance Practice

Pursuant to NYSE rule 303A Prudential has disclosed the differences between the NYSE Corporate Governance Rules and its Corporate Governance Practice on its website at www.prudential.co.uk/prudential-plc/aboutpru/nyse_corpgov. See also Item 16G, 'Corporate Governance' on page 292.

Employees

The average numbers of staff employed by the Prudential group, excluding employees of the venture investment subsidiaries of the PAC with-profits fund, for the following periods were:

	2012	2011	2010
Asian operations	**18,584**	16,666	17,988
US operations	**4,000**	3,785	3,545
UK operations	**5,035**	4,963	4,459
Total	**27,619**	25,414	25,992

At 31 December 2012, Prudential employed 26,057 representing an increase in the year from 24,358 persons as at 31 December 2011. Most of the increase relates to Asia due to regular business growth, supporting growth in operations along with branch expansions in certain countries. Of the 26,057 employees, approximately 18 per cent were located in the United Kingdom, 66 per cent in Asia and 16 per cent in the United States. In the United Kingdom at 31 December 2012, Prudential had 483 employees paying union subscriptions through the payroll. At 31 December 2012, Prudential had 436 temporary employees in the United Kingdom, 2,580 in Asia and 128 in the United States. At 31 December 2012, Prudential had 153 fixed term contractors in the United Kingdom, 108 in the United States and 821 in Asia.

Item 7. Major Shareholders and Related Party Transactions

Major Shareholders

The Disclosure and Transparency Rules issued by the Financial Services Authority provide that a person or corporate entity that acquires an interest of 3 per cent or more in Prudential ordinary shares is required to notify Prudential of that interest. If such interest subsequently reaches, exceeds or falls below a whole percentage point, this must also be notified. Similarly, a notification is required once the interest falls below 3 per cent. At 15 April 2013 Prudential had received the following notifications:

Significant Changes in Ownership

2010

In January 2010, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that its holdings had increased to 127,270,971 or 5.02 per cent of the ordinary share capital.

Later in January, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that its holdings had fallen to below 5 per cent of the ordinary share capital.

In March 2010, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that its holdings had decreased to 101,114,567 shares or 3.98 per cent of the ordinary share capital.

Also in March 2010, Capital Research and Management Company notified Prudential that it had an interest of 280,291,176 ordinary shares, or 11.07 per cent of the ordinary share capital.

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In April 2010, Capital Research and Management Company notified Prudential that it had an interest of 305,167,458 ordinary shares or 12.04 per cent of the ordinary share capital.

In May 2010, Legal and General Group plc notified Prudential that it had an interest of 101,114,567 ordinary shares or 4.03 per cent of the ordinary share capital.

Also in May 2010, Capital Research and Management Company notified Prudential that it had an interest of 329,934,111 shares, which represented 13.02 per cent of the ordinary share capital.

In June 2010, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that it had an interest of 98,291,088 shares, which represented 3.87 per cent of the ordinary share capital.

In July 2010, Capital Research and Management Company notified Prudential that it had an interest of 329,847,111 shares, which represented 12.99 per cent of the ordinary share capital and later in the same month, they increased their interest to 330,456,135 shares, which represented 13.01 per cent of the ordinary share capital.

In August 2010, BlackRock Inc notified Prudential that it had an interest of 126,912,539 shares, which represented 4.99 per cent of the ordinary share capital and the following day, notified that it had increased its interest to 126,965,629 shares, which represented 5.0 per cent of the ordinary share capital.

Also in August 2010, Janus Capital Management LLC notified Prudential that it had an interest of 76,770,894 shares, which represented 3.02 per cent of the ordinary share capital.

In September 2010, BlackRock Inc notified Prudential that it had decreased its interest to 125,634,073 shares, which represented 4.95 per cent of the ordinary share capital.

Later in September, BlackRock Inc notified Prudential that their holding increased to 127,010,669 shares representing 5.0 per cent of the ordinary capital.

In September 2010, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that it had an interest of 102,426,001 shares, which represented 4.03 per cent of the ordinary share capital. In September 2010, Capital Research and Management Company notified Prudential that it had an interest of 330,673,911 shares, which represented 12.99 per cent of the ordinary share capital.

In October 2010, BlackRock Inc notified Prudential that it had an interest of 124,987,739 shares, which represented 4.91 per cent of the ordinary share capital.

In November 2010, Capital Research and Management Company notified Prudential of a decrease in its interest to 296,189,505 shares, which represented 11.64 per cent of the ordinary share capital.

Also in November 2010, Norges Bank notified Prudential that it had an interest of 102,495,000 shares, which represented 4.03 per cent of the ordinary share capital. In December 2010, Legal and General Assurance (Pensions Management) Limited (PMC) notified Prudential that it had an interest of 101,803,187 shares, which represented 3.99 per cent of the ordinary share capital.

2011

In January 2011, BlackRock Inc notified Prudential that it had an interest of 127,614,906 shares, which represented 5.01 per cent of the ordinary share capital.

In March 2011, Capital Research and Management Company notified Prudential of a decrease in its interest to 281,048,317 shares representing 11.04 per cent of the ordinary share capital.

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Also in March 2011, BlackRock Inc notified Prudential of a decrease in their interest of 126,093,582 shares representing 4.95 per cent of ordinary share capital and then in a further notification, of an increase in their interest to 127,414,496 shares representing 5.0 per cent of the ordinary share capital.

BlackRock Inc made two notifications up to 15 April 2011; the first notification was of a decrease in their interest to 126,974,810 shares representing 4.98 per cent of the ordinary share capital and the second was of an increase in their interest to 128,470,662 shares representing 5.04 per cent of the ordinary share capital.

In April 2011, BlackRock Inc notified a decrease in their interest in Prudential shares of 126,930,350, representing 4.98 per cent of the ordinary share capital.

In May 2011 BlackRock Inc notified an increase in shares to 127,401,807, representing 5 per cent of the ordinary share capital and later in May, notified a decrease in their interest to 126,991,833 representing 4.95 per cent of the ordinary share capital.

Also in May 2011, Capital Research and Management Company notified a decrease in their interest to 279,316,829 shares, representing 10.96 per cent of the ordinary share capital.

In June 2011, BlackRock Inc notified an increase to 127,695,916 shares representing 5.01 per cent of the ordinary share capital.

In July 2011, Capital Research and Management Company notified a decrease to 252,448,407 shares, representing 9.91 per cent of the ordinary share capital.

In August 2011, BlackRock Inc notified a decrease in interest to 125,132,015 shares, representing 4.91 per cent of the ordinary share capital and in November 2011, notified an increase to 127,422,766 shares, representing 5 per cent of the ordinary share capital.

Later in November 2011, BlackRock Inc notified a decrease to 127,201,756 shares representing 4.99 per cent of the ordinary share capital.

2012

In April 2012, BlackRock Inc. notified an increase in interest to 129,499,098 shares, representing 5.8 per cent of the issued share capital.

In September 2012, Capital Group International Inc. (formerly interests notified by Capital Research and Management Company) notified an increase in interest to 256,652,047, representing 10.39 percent of the issued share capital.

Table: Notifications received from major shareholders as at 15 April 2013

Shareholder	Date advised	Percentage of share capital	Shareholding

Capital Group International Inc.	05/09/2012	10.39%	256,652,047
BlackRock Inc	10/04/2012	5.08%	129,499,098
Norges Bank	26/11/2010	4.03%	102,495,000
Legal and General Group plc	30/12/2010	3.99%	101,803,187

Major shareholders of Prudential have the same voting rights per share as other shareholders. See Item 10, 'Additional Information Memorandum and Articles of Association Voting Rights'.

As at 15 April 2013, there were 129 shareholders with a US address on Prudential's register of shareholders. These shares represented approximately 0.01 per cent of Prudential's issued ordinary share capital. As at 16 April 2013 there were 44 registered Prudential ADR holders. The shares

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represented by these ADRs amounted to approximately 1.77 per cent of Prudential's issued ordinary share capital.

Prudential does not know of any arrangements which may at a subsequent date result in a change of control of Prudential.

Related Party Transactions

Transactions between the Company and its subsidiaries are eliminated on consolidation.

In addition, the Company has transactions and outstanding balances with certain unit trusts, collateralised debt obligations and similar entities which are not consolidated and where a Group company acts as manager. These entities are regarded as related parties for the purposes of IAS 24. The balances are included in the Group's statement of financial position sheet at fair value or amortised cost in accordance with their IAS 39 classifications. The transactions are included in the income statement and include amounts paid on issue of shares or units, amounts received on cancellation of shares or units and paid in respect of the periodic charge and administration fee. Further details of the aggregate assets, liabilities, revenues, profits or losses and reporting dates of entities considered to be associates under IFRS are disclosed in note H8 to the consolidated financial statements in Item 18.

Executive officers and directors of the Company may from time to time purchase insurance, asset management or annuity products marketed by Group companies in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with other persons.

In 2012 and 2011 and 2010, other transactions with directors were not deemed to be significant both by virtue of their size and in the context of the directors' financial positions. As indicated above, all of these transactions are on terms broadly equivalent to those that prevail in arm's length transactions.

Apart from these transactions with directors, no director had interests in shares, transactions or arrangements that require disclosure, other than those given in Item 6 'Directors, Senior management and Employees'. Key management remuneration is disclosed in note I5 to the consolidated financial statements in Item 18.

Item 8. Financial Information

See Item 18, 'Financial Statements'.

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Item 9. The Offer and Listing

Comparative Market Price Data

The tables below set forth the highest and lowest closing middle-market quotations for Prudential shares, as derived from the Daily Official List of the London Stock Exchange, the actual ADRs high and low closing sale prices for the periods indicated on the New York Stock Exchange and the highest and lowest closing prices on the Hong Kong Stock Exchange and Singapore Stock Exchange.

	Prudential Ordinary Shares		Prudential ADRs		Prudential Ordinary Shares (Hong Kong)*		Prudential Ordinary Shares (Singapore)*	
Year	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**
	(pence)		**(US Dollars)**		**(HK Dollars)**		**(US Dollars)**	
2008	726.0	245.0	28.8	7.4				
2009	650.5	207.0	21.8	5.6				
2010	681.0	487.5	21.3	14.5	81.1	57.2	10.5	7.4
2011	777.0	509.0	25.8	16.2	100.0	62.4	12.6	8.0
2012	**911.5**	**628.5**	**29.4**	**19.6**	**113.8**	**74.0**	**12.3**	**9.9**

	Prudential Ordinary Shares		Prudential ADRs		Prudential Ordinary Shares (Hong Kong)*		Prudential Ordinary Shares (Singapore)*	
Quarter	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**
	(pence)		**(US Dollars)**		**(HK Dollars)**		**(US Dollars)**	
2011								
First quarter	749.0	654.5	24.3	21.0	98.0	80.5	11.9	10.6
Second quarter	777.0	683.0	25.8	21.9	100.0	84.9	12.6	11.5
Third quarter	614.5	546.5	19.6	16.8	78.6	64.0	10.1	8.5
Fourth quarter	681.0	509.0	22.3	16.2	84.8	62.4	10.6	8.0
2012								
First quarter	**797.5**	**633.5**	**25.6**	**19.6**	**98.7**	**74.0**	**12.0**	**9.9**
Second quarter	**764.0**	**660.0**	**24.7**	**20.3**	**96.0**	**78.2**	**12.0**	**12.0**
Third quarter	**854.0**	**729.5**	**27.6**	**22.7**	**107.0**	**87.4**	**12.0**	**10.0**
Fourth quarter	**911.5**	**820.0**	**29.4**	**26.3**	**113.8**	**101.7**	**12.3**	**10.0**

	Prudential Ordinary Shares (UK)		Prudential ADRs		Prudential Ordinary Shares (Hong Kong)		Prudential Ordinary Shares (Singapore)	
Month	**High**	**Low**	**High**	**Low**	**High**	**Low**	**High**	**Low**

	(pence)		(US Dollars)		(HK Dollars)		(US Dollars)	
October 2012	870.0	820.0	28.1	26.3	107.5	101.7	10.0	10.0
November 2012	905.0	839.5	29.2	26.9	111.8	102.5	12.1	10.0
December 2012	911.5	865.0	29.6	27.9	113.8	109.5	12.3	12.1
January 2013	973.0	901.5	30.8	29.3	116.5	111.0	13.1	12.3
February 2013	981.5	916.0	30.5	28.6	118.0	111.5	13.7	13.1
March 2013	1,155.0	986.5	35.0	29.8	134.0	114.6	15.4	13.7

*

Prudential listed on these stock exchanges on 25 May 2010. Accordingly, the market price data shown above for these stock exchanges is only from this date.

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Market Data

Prudential ordinary shares are listed on the Premium Listing segment of the Official List of the UK Listing Authority and traded on the London Stock Exchange under the symbol 'PRU'. On 25 May 2010, Prudential ordinary shares were admitted to listing on the Main Board of the Hong Kong Stock Exchange and are traded in board lots of 500 shares with the short name 'PRU' and stock code 2378; and as a secondary listing on the Singapore Stock Exchange, also traded in board lots of 500 shares, with the abbreviated name 'PRU 500'.

Prudential American Depositary Shares (ADSs) have been listed for trading on the New York Stock Exchange since 28 June 2000 under the symbol 'PUK'.

Item 10. Additional Information

Memorandum and Articles of Association

Prudential plc is incorporated and registered in England and Wales, under registered number 1397169. Under the provisions of the Companies Act 2006 a UK company's objects are unrestricted unless a company's Articles of Association provide otherwise. To avail the Company of this flexibility, the shareholders passed a resolution at the Annual General Meeting on 14 May 2009 (which became effective on 1 October 2009) removing the objects clause from the Company's Memorandum and Articles of Association.

The following is a summary of both the rights of Prudential shareholders and certain provisions of Prudential's Memorandum and Articles of Association. Rights of Prudential shareholders are set out in Prudential's Articles of Association or are provided for by English law. This document is a summary and, therefore, does not contain full details of Prudential's Memorandum and Articles of Association. A complete copy of Prudential's Memorandum and Articles of Association, adopted at the Annual General Meeting on 14 May 2009 and effective on 1 October 2009, was filed as an exhibit to Form 20-F for the year ended 31 December 2008. In addition, both the Memorandum and Articles of Association may be viewed on Prudential's website.

Share capital

The Company's issued share capital as at 31 December 2012, which is set out in Note H11 on page F-221, consisted of 2,557,242,352 (2011:2,548,039,330) ordinary shares of 5 pence each, all fully paid up and listed on the London Stock Exchange and the Hong Kong Stock Exchange. Subject to applicable local securities law, the Company's shares may be registered on the main register in the UK or the Company's branch registers in Ireland or Hong Kong. The number of accounts on the share registers at 31 December 2012 was 60,522 (2011:63,338).

The Company also maintains secondary listings on the New York Stock Exchange in the form of American Depositary Receipts which are referenced to ordinary shares on the main UK register, under a depositary agreement with J.P. Morgan, and on the Singapore Stock Exchange in the form of interests in shares, which are referenced to the shares on the Hong Kong register under a depository agreement with the Central Depository (Pte) Limited (the "CDP").

The Company has maintained a sufficiency of public float throughout the reporting period as required by the Hong Kong Listing Rules.

A number of dividend waivers are in place and these relate to shares issued but not allocated under the Group's employee share plans. These shares are held by the Trustees and will, in due course, be used to satisfy requirements under the Group's employee share plans.

The issued share capital of Prudential is not currently divided into different classes of shares. The Companies Act 2006 abolished the requirement for a company to have an authorised share capital.

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As at 16 April 2013, the directors retained authority granted at the Annual General Meeting on 17 May 2012 to allot before the earlier of 30 June 2013 and the Annual General Meeting of the Company to be held in 2013, ordinary shares of up to an aggregate nominal value of £42,527,821 subject to limitations and reductions in certain circumstances. Of those shares, directors would retain authority to allot equity securities for cash up to a maximum nominal value of £6,379,173 without first being required to offer such securities to shareholders in proportion with their existing holding. In the case of a rights issue, directors retained authority to allot equity securities in favor of ordinary shareholders up to an aggregate nominal amount equal to £85,055,642 subject to reduction in certain circumstances.

At the Annual General Meeting scheduled to be held on 16 May 2013, the shareholders are to vote on granting the directors similar authorities to allot ordinary shares, before the earlier of 30 June 2014 and the Annual General Meeting of the Company to be held in 2014.

In addition the directors have authority to allot Sterling preference shares up to a maximum nominal amount of £20 million, Dollar preference shares up to a maximum nominal amount of US$20 million, and Euro preference shares up to a maximum nominal value of €20 million, the terms of which will be determined by the Board on allotment.

The Board shall determine whether the preference shares are to be redeemable, their dividend rights, their rights to a return of capital or to share in the assets of the Company on a winding up or liquidation and their rights to attend and vote at general meetings of the Company prior to the date on which the preference shares are allotted. Under the Company's Articles of Association the Board has discretion to determine the terms and manner of redemption of redeemable shares when the shares are allotted.

The Board may only capitalise any amounts available for distribution in respect of any series or class of preference shares if to do so would mean that the aggregate of the amounts so capitalised would be less than the multiple, if any, determined by the Board of the aggregate amount of the dividends payable in the 12 month period following the capitalisation on the series or class of preference shares and on any other preference shares in issue which rank *pari passu* in relation to participation in profits. This restriction may be overturned with either: (i) the written consent of the holders of at least three-quarters in nominal value; or (ii) a special resolution passed at a general meeting of the holders of the class or series of preference shares.

Dividends and other distributions

Under English law, Prudential may pay dividends only if distributable profits are available for that purpose. Distributable profits are accumulated, realised profits not previously distributed or capitalised, less accumulated, realised losses not previously written off in a reduction or reorganisation of capital. Even if distributable profits are available, Prudential may only pay dividends if the amount of its net assets is not less than the aggregate of its called-up share capital and undistributable reserves, including, for example, the share premium account, and the payment of the dividend does not reduce the amount of the net assets to less than that aggregate. Subject to these restrictions, Prudential's directors may recommend to ordinary shareholders that a final dividend be declared, recommend the amount of any such dividend, determine whether to pay a distribution by way of an interim dividend, and the amount of any such interim dividend out of the profits of the Company, but must take into account Prudential's financial position. Final dividends become a legal liability of a company upon the later of the date they are declared by shareholders and the date the shareholder approval expresses them to be payable. Interim dividends only become a legal liability of a Company at the moment they are paid, unless a company's Articles of Association provide for declaration of interim dividends by directors. The Company's Articles do not provide for declaration of interim dividends.

The Company or its directors determine the date on which Prudential pays dividends. Prudential pays dividends to the shareholders on its share registers on the record date in proportion to the number

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of shares held by each shareholder. There are no fixed dates on which entitlements to dividends arise. Interest is not payable on dividends or other amounts payable in respect of shares.

If a shareholder does not claim a dividend within 12 years of such dividend becoming due for payment, such shareholder forfeits their right to receive it. Such unclaimed amounts may be invested or otherwise used for Prudential's benefit.

Shareholder meetings

English law provides for shareholders to exercise their power to decide on corporate matters at general meetings. In accordance with English law, the Company is required to call and hold annual general meetings. At annual general meetings, shareholders receive and consider the statutory accounts and the reports by the Company's auditor and its directors, approve the directors' remuneration report, elect and re-elect directors, declare final dividends, approve the appointment of the Company's auditor, authorise the directors to determine the auditor's remuneration, and transact any other business which ought to be transacted at a general meeting, either pursuant to the Articles of Association or English law. General meetings to consider specific matters may be held at the discretion of Prudential's directors and must be convened, in accordance with English law, following the written request of shareholders representing at least five per cent of the voting rights of the issued and paid-up share capital. The quorum required under Prudential's Articles of Association for a general meeting is two shareholders present in person or by proxy and entitled to vote on the business to be transacted.

Under the Companies (Shareholders' Rights) Regulations 2009, notice periods for all general meetings have to be 21 days, except for a meeting (i) which is not an Annual General Meeting, (ii) for which an electronic facility for voting and appointing proxies is available to all members, and (iii) in respect of which a company obtains shareholder approval annually to retain the shorter 14-day notice period. Prudential has been able to call general meetings (other than annual general meetings) on 14-days' notice and obtained shareholder approval at the Annual General Meeting on 17 May 2012 to enable it to continue to do so after the implementation of the Regulations. The approval will be effective until the Company's Annual General Meeting in 2013 when a similar resolution will be proposed.

Voting rights

Voting at any meeting of shareholders is by show of hands unless the Company's intention to call a poll on the resolution is stated in the notice to the general meeting or, before or on the declaration of the result of a vote on the show of hands or on the withdrawal of any other demand for a poll, a poll is duly demanded. A poll may be demanded as described below. On a show of hands every shareholder holding ordinary shares who is present in person, or a duly appointed proxy or in the case of a corporation, its duly authorised corporate representative, has one vote. On a poll, every shareholder who is present in person or by proxy and every duly authorised corporate representative has one vote for every share held. Only the holders of fully paid shares are allowed to attend, be counted in the quorum at meetings and vote. If more than one joint shareholder votes, only the vote of the shareholder whose name appears first in the register is counted. A shareholder whose shareholding is registered in the name of a nominee may only attend and vote at a general meeting if appointed by his or her nominee as a proxy or a corporate representative.

Resolutions of Prudential's shareholders generally require the approval of a majority of the shareholders to be passed. Such resolutions, referred to as ordinary resolutions, require:

- on a show of hands, a majority in number of the shareholders present and voting in person or by duly appointed proxies or (in the case of corporate shareholders) by authorised corporate representatives to vote in favor, or
- on a poll, more than 50 per cent of the votes cast to be in favor.

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Some resolutions, referred to as special resolutions, such as a resolution to amend the Articles of Association, require a 75 per cent majority. Such special resolutions require:

- on a show of hands, at least 75 per cent of the shareholders present and voting in person or by duly appointed proxies or (in the case of corporate shareholders) by authorised corporate representative to vote in favor, or
- on a poll, at least 75 per cent of the votes cast to be in favor.

Any shareholder who is entitled to attend and vote at a general meeting may appoint one or more proxies to attend and vote at the meeting on his or her behalf.

The following persons may demand a poll:

- the chairman of the meeting,
- at least five shareholders present in person, by corporate representative or by proxy having the right to vote on the resolution,
- any shareholder or shareholders present in person, by corporate representative or by proxy and representing at least 10 per cent of the total voting rights of all shareholders having the right to vote on the resolution, or
- any shareholder or shareholders present in person, by corporate representative or by proxy and holding shares conferring a right to vote on the resolution on which an aggregate sum has been paid up equal to at least 10 per cent of the total sum paid up on all shares conferring that right.

Transfer of shares

Transfers of shares may be made by an instrument of transfer. An instrument of transfer must be signed by or on behalf of the transferor and, unless the share is fully paid, by or on behalf of the transferee. The transferor remains the holder of the relevant shares until the name of the transferee is entered in the share register. Transfers of shares may also be made by a computer-based system and transferred without a written instrument in accordance with English law. The directors may in certain circumstances refuse to register transfers of shares, but only if such refusal does not prevent dealings in the shares from taking place on an open and proper basis. If the directors refuse to register a transfer they must send the transferee notice of the refusal within two months stating the reason(s) for such refusal.

Changes in share capital

Directors require authority to allot from shareholders before issuing new shares. The class and other rights attaching to new classes of shares may be determined by resolution of the shareholders or may be delegated by the shareholders to the directors. The following changes in share capital may only take place after approval by an ordinary resolution of the shareholders:

- share consolidations, and
- subdivisions of shares.

Reductions in Prudential's issued share capital and share premium account must be approved by a special resolution of the shareholders and must be confirmed by an order of the court.

Variation of rights

If the share capital is divided into different classes of shares, the rights of any class of shares may be changed or taken away only if such measure is approved by a special resolution passed at a separate meeting of the members of that class, or with the written consent of at least three quarters of the members of that class. Two persons holding or representing by proxy at least one-third in nominal

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amount of the issued shares of the class must be present at such a meeting in person or by proxy to constitute a quorum.

The Board may not authorise, create or increase the amount of, any shares of any class or any security convertible into shares of any class or any security which is convertible into shares of any class ranking, as regards rights to participate in the profits or assets in the company, in priority to a series or class of preference shares without the consent in writing of at least three- quarters in nominal value of, or the sanction of a special resolution of, the holders of such series or class of preference shares.

Lien

Prudential has a lien on every share that is not a fully paid share.

Accidental omission to give notice

Accidental omission to send notice of a meeting to any person entitled to receive it, or the non-receipt for any reason of any such notice, shall not invalidate the proceedings of that meeting.

Shareholders resident abroad

There are no limitations on non-resident or foreign shareholders' rights to own Prudential securities or exercise voting rights where such rights are given under English company law.

Winding-up

Prudential is subject to the general insolvency law applicable to UK companies.

Board of directors

Prudential's Board of directors manages the Company business. However, the Company's shareholders must approve certain matters, such as changes to the share capital and the election and re-election of directors. Directors are appointed subject to Prudential's Articles of Association. The Board may appoint directors to fill vacancies and appoint additional directors who hold office until the next Annual General Meeting. The Articles of Association require that each director must have beneficial ownership of a given number of ordinary shares. The number of shares is determined by ordinary resolution at a general meeting and is currently 2,500. The minimum number of directors is eight and the maximum number is twenty. Shareholders may vary the limits on the number of directors by ordinary resolution. There are currently sixteen directors on Prudential's Board.

At every Annual General Meeting, any director who has been appointed by the Board since the last Annual General Meeting; or who held office at the time of the two preceding Annual General Meetings and who did not retire at either of them; or who has held office with the Company, other than employment or executive office, for a continuous period of nine years or more at the date of the meeting, shall retire from office and may offer himself or herself for re-election by shareholders. Shareholders may remove any director before the end of his or her term of office by ordinary resolution and may appoint another person in his or her place by ordinary resolution. The UK Corporate Governance Code, contains a provision recommending that directors stand for annual re-election at the Annual General Meeting. In line with these provisions, all directors are expected to stand for re-election at each Annual General Meeting of the Company.

The directors may exercise all the powers of Prudential to borrow money and to mortgage or charge any of its assets provided that the total amount borrowed does not, when aggregated with the total borrowing (which excludes, amongst other things, intra-group borrowings and amounts secured by policies, guarantees, bonds or contracts issued or given by Prudential or its subsidiaries in the course of its business) of all of Prudential's subsidiaries, exceed the aggregate of the share capital and consolidated reserves and of one-tenth of the insurance funds of Prudential and each of its subsidiaries

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as shown in the most recent audited consolidated balance sheet of the Group prepared in accordance with the English law.

There is no age restriction applicable to directors in Prudential's Articles of Association.

Disclosure of interests

There are no provisions in Prudential's Articles of Association that require persons acquiring, holding or disposing of a certain percentage of Prudential's shares to make disclosure of their ownership percentage. The basic disclosure requirement under Part 6 of the Financial Services and Markets Act 2000 and Rule 5 of the Disclosure and Transparency Rules of the Financial Services Authority imposes a statutory obligation on a person to notify Prudential and the Financial Services Authority of the percentage of the voting rights in Prudential he or she directly or indirectly holds or controls, or has rights over, through his direct or indirect holding of certain financial instruments, if the percentage of those voting rights:

- reaches, exceeds or falls below 3 per cent and/or any subsequent whole percentage figure as a result of an acquisition or disposal of shares or financial instruments; or

- reaches, exceeds or falls below any such threshold as a result of any change in the number of voting rights attached to shares in Prudential.

The Disclosure and Transparency Rules set out in detail the circumstances in which an obligation of disclosure will arise, as well as certain exemptions from those obligations for specified persons. Under section 793 of the UK Companies Act 2006, Prudential may, by notice in writing, require a person that Prudential knows or has reasonable cause to believe is or was during the three years preceding the date of notice interested in Prudential's shares, to indicate whether or not that is the case and, if that person does or did hold an interest in Prudential's shares, to provide certain information as set out in that Act.

Where a company serves notice under the provisions described above on a person who is or was interested in shares of the company and that person fails to give the company the information required by the notice within the time specified in the notice, the company may apply to an English court for an order directing that the shares in question be subject to restrictions prohibiting, among other things, any transfer of those shares, the exercise of voting rights in respect of those shares and, other than in liquidation, payments in respect of those shares.

In addition, under Prudential's Articles of Association, a shareholder may lose the right to vote his shares if he or any other person appearing to be interested in those shares fails to comply within a prescribed period of time with such a request to give the required information with respect to past or present ownership or interests in those shares, or makes a statement in response to such a request which is in the opinion of the directors false or misleading in any material manner. In the case of holders of 0.25 per cent or more of the issued share capital of Prudential (or any class of the share capital), in addition to disenfranchisement, the sanctions that may be applied by Prudential under its Articles of Association include withholding the right to receive payment of dividends on those shares, and restrictions on transfers of those shares. In the case of holders of less than 0.25 per cent of the issued share capital of Prudential, the sanction is disenfranchisement alone.

The Disclosure and Transparency Rules further deal with the disclosure by certain persons, including directors, of interests in shares of the listed companies of which they are directors, and in derivatives or other financial instruments relating to those shares. The City Code on Takeovers and Mergers also imposes strict disclosure requirements with regard to dealings in the securities of an offeror or offeree company on all parties to a takeover and also on their respective associates during the course of an offer period.

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Directors' interests in contracts

A director may hold positions with or be interested in other companies and, subject to applicable legislation, contract with the Company or any other company in which Prudential has an interest.

A director may not vote or be counted in the quorum in relation to any resolution of the Board in respect of any contract in which he or she has an interest. This prohibition does not, however, apply to any resolution where that interest cannot reasonably be regarded as likely to give rise to a conflict of interest or where that interest arises only from certain matters specified in the Articles of Association (filed as an exhibit to Form 20-F), including the following:

- certain matters that benefit the Group (such as a guarantee, indemnity or security in respect of money lent or obligations undertaken by the director at the request of or for the benefit of Prudential or one of its subsidiaries);
- certain matters that are available to all other directors and/or employees (such as the provision to the director of an indemnity where all other directors are being offered indemnities on substantially the same terms or in respect of any contract for the benefit of Group employees under which the director benefits in a similar manner to the employees); and
- certain matters that arise solely from the director's interest in shares or debentures of the Company (such as where Prudential or one of its subsidiaries is offering securities in which offer the director is entitled to participate as a holder of securities or in respect of any contract in which a director is interested by virtue of his interest in securities in the Company).

The Company may by ordinary resolution suspend or relax these provisions to any extent or ratify any contract not properly authorised by reason of a contravention of these provisions contained in its Articles of Association.

In accordance with English company law, the Articles of Association allow the Board to authorise any matter which would otherwise involve a director breaching his duty under the Companies Act 2006 to avoid conflicts of interest or potential conflicts of interest and the relevant director is obliged to conduct himself or herself in accordance with any terms imposed by the Board in relation to such authorisation.

Directors' power to vote on own terms of appointment

A director shall not vote on or be counted in the quorum in relation to any resolution of the Board concerning his own appointment, or the settlement or variation of the terms or the termination of his own appointment, as the holder of any office or place of profit with the Company or any other company in which the Company is interested.

Directors' remuneration

The remuneration of the executive directors and the Chairman is determined by the Remuneration Committee, which consists of non-executive directors. The remuneration of the non-executive directors is determined by the Board. For further details see Item 6, 'Directors, Senior Management and Employees Compensation'.

Transactions with Directors

Prudential may only grant a loan or quasi-loan, or provide security or financial accommodation, to its directors and their connected persons if approval has been obtained from shareholders at a general meeting.

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Payments to Directors for loss of office

In accordance with English law, Prudential must obtain the approval of members in general meeting before making a payment in cash or non-cash benefits to a director or past director or any connected person as compensation for loss of any office (including as a director) or employment with Prudential or any of its subsidiary undertakings, and before making any payment in connection with his retirement. However, approval is not required for a payment made in good faith in discharge of an existing legal obligation, such as under an employment contract which has no connection with the event giving rise to the payment for loss of office.

Change of control

There is no specific provision in Prudential's Articles of Association that would have an effect of delaying, deferring or preventing a change in control of Prudential and that would operate only with respect to a merger, acquisition or corporate restructuring involving Prudential, or any of its subsidiaries.

Exclusive jurisdiction

Under Prudential's Articles of Association, any proceeding, suit or action between a shareholder and Prudential and/or its directors arising out of or in connection with the Articles of Association or otherwise, between Prudential and any of its directors (to the fullest extent permitted by law), between a shareholder and Prudential's professional service providers and/or between Prudential and Prudential's professional service providers (to the extent such proceeding, suit or action arises in connection with a proceeding, suit or action between a shareholder and such professional service provider) may only be brought in the courts of England and Wales.

Material Contracts

Not applicable.

Exchange Controls

Other than the requirement to report certain events and transactions to HM Revenue and Customs, there are currently no UK laws, decrees or regulations that restrict the export or import of capital, including, but not limited to, foreign exchange controls, or that affect the remittance of dividends or other payments to non-UK residents or to US holders of Prudential's securities, except as otherwise set forth under ' Taxation' in this section.

Taxation

The following is a summary, under current law and practice, of the principal UK tax, US federal income tax, Hong Kong and Singapore tax considerations relating to an investment by a US taxpayer in Prudential ordinary shares or ADSs. This summary applies to you only if:

- you are an individual US citizen or resident, a US corporation, or otherwise subject to US federal income tax on a net income basis in respect of your holding of Prudential ordinary shares or ADSs;
- you hold Prudential ordinary shares or ADSs or shares held or traded in Singapore through CDP as a capital asset for tax purposes;
- if you are an individual, you are neither resident nor ordinarily resident in the United Kingdom for UK tax purposes, and do not hold Prudential ordinary shares or ADSs for the purposes of a trade, profession, or vocation that you carry on in the

United Kingdom through a branch or agency or if you are a corporation, you are not resident in the UK for UK tax purposes and do

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not hold the securities for the purpose of a trade carried on in the United Kingdom through a permanent establishment in the United Kingdom; and

you are not domiciled in the UK for inheritance tax purposes.

This summary does not address any tax consideration other than certain UK tax, US federal income tax, Hong Kong tax and Singapore tax considerations and does not purport to be a comprehensive description of all of the tax considerations that may be relevant to any particular investor, and does not address the tax treatment of investors that are subject to special rules. Prudential has assumed that you are familiar with the tax rules applicable to investments in securities generally and with any special rules to which you may be subject. You should consult your own tax advisers regarding the tax consequences of the ownership of Prudential ordinary shares or ADSs in the context of your own particular circumstances.

The discussion is based on laws, treaties, judicial decisions, and regulatory interpretations in effect on the date hereof, all of which are subject to change possibly retrospectively.

Beneficial owners of ADSs will be treated as owners of the underlying Prudential ordinary shares for US federal income tax purposes and for purposes of the 24 July 2001 Treaty between the United States and the United Kingdom. Deposits and withdrawals of Prudential ordinary shares in exchange for ADSs generally will not result in the realisation of gain or loss for US federal income tax purposes.

UK Taxation of Dividends

UK tax is not required to be withheld in the United Kingdom at source from cash dividends paid to US resident holders.

UK Taxation of Capital Gains

A holder of Prudential ordinary shares or ADSs who for UK tax purposes is a US corporation that is not resident in the United Kingdom will not be liable for UK taxation on capital gains realised on the disposal of Prudential ordinary shares or ADSs unless at the time of disposal:

the holder carries on a trade in the United Kingdom through a permanent establishment in the United Kingdom, and

the Prudential ordinary shares or ADSs are or have been used, held or acquired for use by or for the purposes of such trade or permanent establishment.

Subject to the comments in the following paragraph, a holder of Prudential ordinary shares or ADSs who, for UK tax purposes, is an individual who is neither resident nor ordinarily resident in the United Kingdom will not be liable for UK taxation on capital gains realised on the disposal of Prudential ordinary shares or ADSs unless at the time of the disposal:

the holder carries on a trade, profession or vocation in the United Kingdom through a branch or agency, and

the Prudential ordinary shares or ADSs are or have been used, held, or acquired for use by or for the purposes of such trade, profession, or vocation, or for the purposes of such branch or agency.

A holder of Prudential ordinary shares or ADSs who (1) is an individual who has ceased to be both resident and ordinarily resident for UK tax purposes in the United Kingdom, (2) was resident or ordinarily resident for UK tax purposes in the United Kingdom for at least four out of the seven UK tax years immediately preceding the year in which he or she ceased to be both resident and ordinarily resident in the United Kingdom, (3) continues to be neither resident nor ordinarily resident in the United Kingdom for a period of less than five tax years and (4) disposes of their Prudential ordinary

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shares or ADSs during that period of non-residence may also be liable, upon becoming resident or ordinarily resident in the United Kingdom again for UK tax on capital gains, subject to any available exemption or relief, even though he or she was not resident or ordinarily resident in the United Kingdom at the time of the disposal.

UK Inheritance Tax

Prudential ordinary shares which are registered on the main Prudential share register are assets situated in the United Kingdom for the purposes of UK inheritance tax (the equivalent of US estate and gift tax). Prudential ADSs are likely to be treated in the same manner as the underlying Prudential ordinary shares and situated in the United Kingdom. Subject to the discussion of the UK-US estate tax treaty in the next paragraph, UK inheritance tax may apply if an individual who holds Prudential ordinary shares which are registered on the main Prudential share register or ADSs gifts them or dies even if he or she is neither domiciled in the United Kingdom nor deemed to be domiciled there under UK law. For inheritance tax purposes, a transfer of Prudential ordinary shares or ADSs at less than full market value may be treated as a gift for these purposes. Special inheritance tax rules apply (1) to gifts if the donor retains some benefit, (2) to close companies and (3) to trustees of settlements. Prudential ordinary shares which are registered on the Hong Kong or Irish branch register should not be treated as situated in the United Kingdom for the purpose of UK inheritance tax.

However, as a result of the UK-US estate tax treaty, Prudential ordinary shares which are registered on the main Prudential share register or ADSs held by an individual who is domiciled in the United States for the purposes of the UK-US estate tax treaty and who is not a UK national will, subject to special rules relating to trusts and settlements, not be subject to UK inheritance tax on that individual's death or on a gift of the Prudential ordinary shares or ADSs unless the Prudential ordinary shares or ADSs:

are part of the business property of a permanent establishment of an enterprise in the United Kingdom, or

pertain to a fixed base in the UK used for the performance of independent personal services.

The UK-US estate tax treaty provides a credit mechanism if the Prudential ordinary shares or ADSs are subject to both UK inheritance tax and to US estate and gift tax.

UK Stamp Duty and Stamp Duty Reserve Tax

Relevant legislation provides that, subject to certain exemptions, UK stamp duty would be payable on a transfer of, and UK stamp duty reserve tax ('SDRT') would be payable upon a transfer or issue of, Prudential ordinary shares to the depositary of Prudential ordinary shares that is responsible for issuing ADSs (the 'ADS Depository'), or a nominee or agent of the ADS depositary, in exchange for American Depository Receipts ('ADRs') representing ADSs. For this purpose, the current rate of stamp duty and stamp duty reserve tax is 1.5 per cent (rounded up, in the case of stamp duty, to the nearest £5).

However, as a result of recent case law, HMRC have stated that they will not seek to levy a 1.5 per cent SDRT charge on an issue of UK shares to a person providing clearance services or issuing depositary receipts, wherever located. HMRC do not, however, agree that the recent case law extends to transfers of shares to a person providing clearance services or issuing depositary receipts, wherever located, where that transfer is not an integral part of an issue of share capital. It is recommended that, should this charge arise, independent professional tax advice be sought without delay.

Provided that the instrument of transfer is not executed in the United Kingdom no UK stamp duty should be required to be paid on any transfer of Prudential ADRs representing ADSs. Based on Prudential's understanding of HMRC's application of the exemption from SDRT for depository receipts a

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transfer of Prudential ADRs representing ADSs should not, in practice, give rise to a liability to stamp duty reserve tax.

Subject to the special rules relating to clearance systems and issuers of depository receipts, a transfer for value of Prudential ordinary shares (but excluding Prudential ordinary shares registered on the Hong Kong or Irish branch register unless the instruments of transfer is executed in the UK), as opposed to ADSs, will generally give rise to a charge to UK stamp duty or stamp duty reserve tax, other than where the amount or value of the consideration for the transfer is £1,000 or under and the transfer instrument is certified at £1,000 (a 'Low Value Transaction'), at the rate of 0.5 per cent (rounded up, in the case of stamp duty, to the nearest £5). The rate is applied to the price payable for the relevant Prudential ordinary shares. To the extent that UK stamp duty is paid on a transfer of Prudential ordinary shares, no stamp duty reserve tax should generally be payable on the agreement for that transfer. Subject to certain special rules relating to clearance services, a transfer of ordinary shares from a nominee to their beneficial owner (other than on sale), including a transfer of underlying Prudential ordinary shares from the ADS depositary or its nominee to an ADS holder, is not subject to UK stamp duty. No UK stamp duty reserve tax should be payable on an agreement to transfer Prudential ordinary shares registered on the Hong Kong or Irish branch registers, subject to the special rule relating to clearance systems and issuers of depository receipts.

UK stamp duty is usually paid by the purchaser. Although stamp duty reserve tax is generally the liability of the purchaser, any such tax payable on the transfer or issue of Prudential ordinary shares to the ADS depositary or its nominee will (subject to the change referred to above) be payable by the ADS depositary as the issuer of the ADSs. In accordance with the terms of the Deposit Agreement, the ADS depositary will recover an amount in respect of such tax from the initial holders of the ADS.

US Federal Income Tax Treatment of Distributions on Prudential Ordinary Shares or ADSs

If Prudential pays dividends, you must include those dividends in your income when you receive them. The dividends will be treated as foreign source income. You should determine the amount of your dividend income by converting pounds sterling into US dollars at the exchange rate in effect on the date of your (or the depositary's, in the case of ADSs) receipt of the dividend. Subject to certain exceptions for short-term and hedged positions, the US dollar amount of dividends received by an individual will be subject to taxation at a lower rate than ordinary income if the dividends are 'qualified dividends.' Dividends received with respect to the ordinary shares or ADSs will be qualified dividends if Prudential was not, in the year prior to the year in which the dividend was paid, and is not, in the year in which the dividend is paid, a passive foreign investment company ('PFIC'). Based on the nature of its business activities and its expectations regarding such activities in the future, Prudential believes that it was not treated as a PFIC within the meaning of the Code with respect to its 2012 taxable year and does not anticipate becoming a PFIC for its 2013 taxable year.

US Federal Income Tax Treatment of Capital Gains

If you sell your Prudential ordinary shares or ADSs, you will recognise a US source capital gain or loss equal to the difference between the US dollar value of the amount realised on the disposition and the US dollar basis in the ordinary shares of the ADSs. A gain on the sale of Prudential ordinary shares or ADSs held for more than one year will be treated as a long-term capital gain. The net long-term capital gain is generally is subject to taxation at a lower rate than ordinary income. Your ability to offset capital losses against ordinary income is subject to limitations.

US Federal Medicare Tax on Net Investment Income

A 3.8% surtax will generally apply to the net investment income of individuals whose modified adjusted gross income exceeds certain threshold amounts. For 2013, these amounts are $200,000 in the

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case of single taxpayers, $250,000 in the case of married taxpayers filing joint returns, and $125,000 in the case of married taxpayers filing separately. Net investment income includes, among other items, dividends, interest, and net gain from the disposition of property (other than certain property held in a trade or business).

US Information Reporting and Backup Withholding

Under the US tax code, a US resident holder of Prudential ordinary shares or ADSs may be subject, under certain circumstances, to information reporting and possibly backup withholding with respect to dividends and proceeds from the sale or other disposition of Prudential ordinary shares or ADSs, unless the US resident holder provides proof of an applicable exemption or correct taxpayer identification number and otherwise complies with applicable requirements of the backup withholding rules. Any amount withheld under the backup withholding rules is not additional tax and may be refunded or credited against the US resident holder's federal income tax liability, so long as the required information is furnished to the IRS.

Hong Kong Taxation of Dividends

No tax will be payable in Hong Kong in respect of dividends Prudential pays to its US resident holders. Dividends distributed to Prudential's US resident holders will be free of withholding taxes in Hong Kong.

Hong Kong Taxation on gains of sale

No tax is imposed in Hong Kong in respect of capital gains. However, trading gains from the sale of property by persons carrying on a trade, profession or business in Hong Kong where the trading gains are derived from or arise in Hong Kong will be chargeable to Hong Kong profits tax. Hong Kong profits tax is currently charged at the rate of 16.5 per cent on corporations and at a maximum rate of 15 per cent on individuals. Certain categories of taxpayers whose business consists of buying and selling shares are likely to be regarded as deriving trading gains rather than capital gains (e.g. financial institutions, insurance companies and securities dealers) unless these taxpayers can prove that the investment securities are held for long-term investment purposes.

Trading gains from the sale of the Prudential Shares by US resident holders effected on the Hong Kong Stock Exchange will be considered to be derived from Hong Kong. A liability for Hong Kong profits tax would thus arise in respect of trading gains derived by US resident holders from the sale of Prudential Shares effected on the Hong Kong Stock Exchange where such trading gains are realised by US resident holders from a business carried on in Hong Kong.

Hong Kong Stamp duty

Hong Kong stamp duty, currently charged at the ad valorem rate of 0.1 per cent on the higher of the consideration for or the value of the Prudential Shares, will be payable by the purchaser on a purchase and by the seller on a sale of Prudential Shares where the transfer is required to be registered in Hong Kong (i.e. a total of 0.2 per cent is ordinarily payable on a sale and purchase transaction involving ordinary shares). In addition, a fixed duty of HK$5.00 is currently payable on any instrument of transfer of ordinary shares.

Hong Kong Estate duty

Hong Kong estate duty has been abolished with effect to all deaths occurring on or after 11 February 2006.

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Singapore Taxation on gains of sale

Disposal of the Prudential Shares

Singapore does not impose tax on capital gains. There are no specific laws or regulations which deal with the characterisation of whether a gain is income or capital in nature. Gains arising from the disposal of the Prudential Shares by US resident holders may be construed to be of an income nature and subject to Singapore income tax, especially if they arise from activities which are regarded as the carrying on of a trade or business and the gains are sourced in Singapore.

Adoption of FRS 39 for Singapore Tax Purposes

Any US resident holders who apply, or who are required to apply, the Singapore Financial Reporting Standard 39 Financial Instruments Recognition and Measurement ('FRS 39') for the purposes of Singapore income tax may be required to recognise gains or losses (not being gains or losses in the nature of capital) in accordance with the provisions of FRS 39 (as modified by the applicable provisions of Singapore income tax law) even though no sale or disposal is made. Taxpayers who may be subject to such tax treatment should consult their own accounting and tax advisers regarding the Singapore income tax consequences of their acquisition, holding and disposal of the Prudential Shares.

Singapore Taxation of Dividend distributions

As Prudential is incorporated in England and Wales and is not tax resident in Singapore for Singapore tax purposes, dividends paid by Prudential will be considered as sourced outside Singapore (unless the Prudential Shares are held as part of a trade or business carried out in Singapore in which event the US resident holders of such shares may be taxed on the dividends as they are derived).

Foreign-sourced dividends received or deemed received in Singapore by an US resident individual not resident in Singapore is exempt from Singapore income tax. This exemption will also apply in the case of a Singapore tax resident individual who receives his foreign-sourced income in Singapore on or after 1 January 2004 (except where such income is received through a partnership in Singapore).

Foreign-sourced dividends received or deemed received by corporate investors in Singapore (including US investors) will ordinarily be liable to Singapore tax. However, foreign-sourced income in the form of dividends, branch profits and service income received or deemed to be received in Singapore by Singapore tax resident companies on or after 1 June 2003 can be exempt from tax if certain prescribed conditions are met, including the following:

(i) such income is subject to tax of a similar character to income tax under the law of the jurisdiction from which such income is received; and

(ii) at the time the income is received in Singapore, the highest rate of tax of a similar character to income tax (by whatever name called) levied under the law of the territory from which the income is received on any gains or profits from any trade or business carried on by any company in that territory at that time is not less than 15 per cent.

Certain concessions and clarifications have also been announced by the Inland Revenue Authority of Singapore with respect to such conditions.

Singapore Stamp duty

As Prudential is incorporated in England and Wales and the Prudential Shares are not registered on any register kept in Singapore, no stamp duty is payable in Singapore:

(i) on the issuance of the Prudential Shares; and

(ii)

on any transfer of the Prudential Shares.

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Prudential Shares held or traded in Singapore through CDP will be registered on the HK Register. As such, Hong Kong stamp duty will be payable on a transfer of Prudential Shares held or traded in Singapore through CDP. Please refer to the description under the Hong Kong stamp duty section above.

All persons, including US resident holders, who hold or transact in Prudential Shares in Singapore through the SGX-ST and/or CDP should expect that they will have to bear Hong Kong stamp duty in respect of transactions in Prudential Shares effected in Singapore through the SGX-ST and/or CDP. Such persons should consult their brokers, or custodians for information regarding what procedures may be instituted for collection of Hong Kong stamp duty from them.

Singapore Estate duty

Singapore estate duty has been abolished with respect to all deaths occurring on or after 15 February 2008.

Singapore Goods and Services Tax

There is no Goods and Services Tax ('GST') payable in Singapore on the subscription or issuance of the Prudential Shares. The clearing fees, instruments of transfer deposit fees and share withdrawal fees are subject to GST at the prevailing standard-rate (currently 7per cent) if the services are provided by a person belonging to Singapore to a holder of the Prudential Shares. However, such fees could be zero-rated when provided to a US resident holder of the Prudential Shares belonging outside Singapore provided certain conditions are met. For a holder of the Prudential Shares belonging in Singapore who is registered for GST, the GST incurred is generally not recoverable as input tax credit from the Inland Revenue Authority of Singapore unless certain conditions are satisfied. These GST-registered holders of the Prudential Shares should seek the advice of their tax advisors on these conditions.

Documents on Display

Prudential is subject to the informational requirements of the Securities Exchange Act of 1934 applicable to foreign private issuers. In accordance with these requirements, Prudential files its Annual Report on Form 20-F and other documents with the Securities and Exchange Commission. You may read and copy this information at the following location:

Public Reference Room
100 F Street, N.E.
Room 1580
Washington, D.C. 20549

Please call the SEC at (202) 551 8090 for further information on the public reference room. Copies of these materials can also be obtained by fax (202) 777 1027, by email to PublicInfo@sec.gov or mail at prescribed rates from the Public Reference Section of the Securities and Exchange Commission, 100 F Street, N.E., Room 1580, Washington, D.C. 20549-0213. In addition, some of Prudential's filings with the Securities and Exchange Commission, including all those filed on or after 4 November 2002, are available on the websites of the Securities and Exchange Commission's and the New York Stock Exchange

Prudential also files reports and other documents with the London, Hong Kong and Singapore stock exchanges. This information may be viewed on the websites of each of those exchanges as well as via the National Storage Mechanism. All reports and other documents filed with the each of the exchanges are also published on Prudential's website.

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Item 11. Quantitative and Qualitative Disclosures about Market Risk

Overview

As a provider of financial services, including insurance, the management of risk lies at the heart of the Group's business. The control procedures and systems established within the Group are designed to manage, rather than eliminate, the risk of failure to meet business objectives. They can only provide reasonable and not absolute assurance against material misstatement or loss, and focus on aligning the levels of risk-taking with the achievement of business objectives.

The Group's internal control processes are detailed in the Group Governance Manual. This is supported by the Group Risk Framework, which provides an overview of the Group-wide philosophy and approach to risk management. Where appropriate, more detailed policies and procedures have been developed at Group and/or business unit levels. These include Group-wide mandatory policies on certain operational risks, including: health, safety, fraud, money laundering, bribery, business continuity, information security and operational security, and policies on certain financial risks. Additional guidelines are provided for some aspects of actuarial and financial activity.

Prudential's Group Risk Framework requires that all of the Group's businesses and functions establish processes for identifying, evaluating and managing the key risks faced by the Group. The Group Risk Framework is based on the concept of 'three lines of defence': Risk management; risk oversight and independent assurance. Primary responsibility for strategy, performance management and risk control lies with the Board, which has established the Group Risk Committee to assist in providing leadership, direction and oversight, and with the Group Chief Executive and the chief executive of each business unit. Risk oversight is provided by Group-level risk committees, chaired by the Group Chief Risk Officer or the Chief Financial Officer. Independent assurance on the Group's internal control and risk management systems is provided by the Audit Committee, supported by the Group-wide Internal Audit.

The Group's risk reporting framework forms an important part of the Group's business processes and planning. Business units review their risks as well as opportunities as part of their business plans, and risks against business objectives are regularly discussed with Group executive management.

Additional information on the Group's risk framework is included in the risk and capital management section under 'Group Risk Framework in Item 4 Information on the Company'.

The management of the risk attached to the Group's financial instruments and insurance liabilities, together with the inter-relationship with the management of capital is summarised in the following sections.

Major Risks

Specific business environmental and operational risks are discussed under Item 3, 'Key Information Risk Factors' and Item 5, 'Operating and Financial Review and Prospects Internal control and risk management' and 'Operating and Financial Review and Prospects Principal Factors Affecting Prudential Results of Operations'. Risks discussed under Item 4, 'Information on the Company Business of Prudential' include 'Business of Prudential UK Business' and 'Business of Prudential Legal Proceedings'.

Market and financial risks

A detailed analysis of market and financial risks is provided in Item 4 'Group Risk Framework' and notes D1(e), D2(h), D3(h) and D4(h) to the consolidated financial statements in Item 18.

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Currency of Investments

Prudential's investments are generally held in the same currency as its liabilities and, accordingly, pound sterling liabilities will generally be supported by pound sterling assets and US dollar liabilities will generally be supported by US dollar assets. However, where Prudential believes it is appropriate, it holds some non-domestic equities in the equity portfolios in the belief that this diversifies the overall portfolio risk.

As at 31 December 2012, the Group held 19 per cent (2011: 21 per cent) and 7 per cent (2011: 9 per cent) of its financial assets and financial liabilities respectively, in currencies, mainly US dollar and Euro, other than the functional currency of the relevant business unit.

Financial assets, of which 56 per cent (2011: 55 per cent) are held by the PAC with-profits fund, allow the PAC with-profits fund to obtain exposure to foreign equity markets.

Financial liabilities, of which 28 per cent (2011: 28 per cent) are held by the PAC with-profits fund, mainly relate to foreign currency borrowings.

The exchange risks inherent in these exposures are mitigated through the use of derivatives, mainly forward currency contracts (note G3 to the consolidated financial statements in Item 18).

The amount of exchange loss recognised in the income statement in 2012, except for those arising on financial instruments measured at fair value through profit and loss, is £213 million (2011: £1 million gain; 2010: £82 million loss). This constitutes £1 million loss (2011: £11 million loss; 2010: £16 million loss) on Medium Term Notes (MTN) liabilities and £212 million of net loss (2011: £12 million net gain;2010: £98 million loss), mainly arising on investments of the PAC with-profits fund. The gains/losses on MTN liabilities are fully offset by value movements on cross-currency swaps, which are measured at fair value through profit and loss.

Currency of Core Borrowings

Prudential is subject to certain interest rate risk and foreign exchange risk on its core borrowings. At 31 December 2012, Prudential held £1,639 million of pounds sterling debt, £1,899 million, or approximately $3,086 million, of US dollar debt and £16 million, or approximately €20 million of Euro debt. £3,263 million of the core debt was at fixed rates of interest and £291 million was at or has been swapped into floating rates of interest.

The profit and loss accounts of foreign subsidiaries are translated at average exchange rates for the year. Assets and liabilities of foreign subsidiaries are translated at closing exchange rates. Foreign currency borrowings that have been used to provide a hedge against Group equity investments in overseas subsidiaries are also translated at closing exchange rates. The impact of these translations is recorded as a component of the movement in shareholders' equity.

Sensitivity Analysis

Prudential is sensitive to interest rate movements, movements in the values of equities and real estate and foreign exchange fluctuations.

Sensitivity analysis with regard to the Group's investments in debt securities, equities and real estate, to insurance contracts and to foreign exchange fluctuations, is provided in notes D2(h), D3(h), D4(h) and E4 to the consolidated financial statements in Item 18.

Additional sensitivity analysis of the Group's long-term debt and interests in derivatives contracts has been provided below.

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Interest Rate Risk Long-term Debt

The table below quantifies the estimated increase in fair value of long-term borrowings at 31 December 2012 and 2011, resulting from a 100 basis point reduction in interest rates at those dates. The carrying value of short-term borrowings, which approximates their fair value, would not be materially increased by a 100 basis point reduction in interest rates. Prudential believes this to be a reasonably possible near-term market change for interest rates.

	31 December 2012			31 December 2011		
	Carrying Value	Fair Value	Estimated Increase in Fair Value	Carrying Value	Fair Value	Estimated Increase in Fair Value
	£m	£m	£m	£m	£m	£m
Long-term borrowings						
Bonds, £300 million aggregate principal amount, 6.875 per cent due 2023	**300**	**394**	**40**	300	356	34
Bonds, £250 million aggregate principal amount, 5.875 per cent due 2029	**249**	**313**	**44**	249	270	32
Bonds, £435 million aggregate principal amount, 6.125 per cent, due 2031	**429**	**518**	**73**	428	423	46
Bonds, £400 million aggregate principal amount, 11.375 per cent, due 2039	**386**	**555**	**38**	384	509	35
Capital securities, $1,000 million aggregate principal amount, 6.5 per cent perpetual	**615**	**631**	**92**	644	560	68
Capital securities, $250 million aggregate principal amount, 6.75 per cent perpetual[ii]	**154**	**154**		161	164	1
Capital securities, $300 million aggregate principal amount 6.5 per cent perpetual[ii]	**185**	**187**		193	196	
Capital securities, $750 million aggregate principal amount, 11.75 per cent perpetual	**458**	**536**	**11**	477	550	16
Capital securities, $550 million aggregate principal amount, 7.75 per cent perpetual[ii]	**334**	**358**	**48**	348	343	40
Medium Term Subordinated Notes, €20 million, 2023[i]	**16**	**16**		17	17	
Total central companies	**3,126**	**3,662**	**346**	3,201	3,388	272
Insurance operations						
Guaranteed bonds, £100 million, principal amount, 8.5 per cent undated subordinated	**100**	**107**	**5**	100	106	6
Surplus notes, $250 million principal amount, 8.15 per cent due 2027[iv]	**153**	**196**	**16**	160	178	15
Total long-term business	**253**	**303**	**21**	260	284	21
Other operations						
Bank Loans[iii]	**275**	**275**		250	250	
Total	**3,654**	**4,240**	**367**	3,711	3,922	293

Notes

(i)

The €20 million borrowings were issued at 20-year Euro Constant Maturity Swap (capped at 6.5 per cent). These have been swapped into borrowings of £14 million with interest payable at three month £LIBOR plus 1.2 per cent.

(ii)

The US$250 million 6.75 per cent borrowings, the US$300 million 6.5 per cent borrowings and the US$550 million 7.75 per cent borrowings can be converted, in whole or in part, at the Company's option and subject to certain conditions, on any interest payment date, into one or more series of Prudential preference shares.

(iii)

The PruCap bank loan was increased from £250 million to £275 million on 20 December 2012. The loan has been made in two tranches: a £160 million loan maturing in June 2014, currently drawn at a cost of 12 month £LIBOR plus 0.6 per cent and a £115 million loan maturing on 20 December 2017 and currently drawn at a cost of 12 month £LIBOR plus 0.79 per cent.

(iv)

The Jackson borrowings are unsecured and subordinated to all present and future indebtedness, policy claims and other creditor claims of Jackson.

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There is no impact on profit at 31 December 2012 and 2011 as a result of these reductions in interest rates because the liabilities are recognised in the financial statements at carrying value, which is equal to their amortised cost.

Derivative Contracts

As at 31 December 2012 the net market value exposure of derivatives was an asset of £1,033 million of which the largest exposures were held by the UK and US insurance operations. Excluding derivative contracts within assets held to cover linked liabilities and those attributable to unit holders of consolidated unit trusts and similar funds, as at 31 December 2012 the market value exposure of derivatives of the UK and US insurance operations was an asset of £1,336 million. The tables below show the sensitivity of the UK and US insurance operations derivatives, measured in terms of fair value, to equity and real estate market increases and decreases of 10 per cent and to interest rate increases and decreases of 100 basis points. Prudential believes these increases and decreases to be reasonably possible near-term market changes. These exposures will change as a result of ongoing portfolio and risk management activities.

	31 December 2012			**31 December 2011**		
	10 per cent Equity & Real Estate Increase		**10 per cent Equity & Real Estate Decrease**	**10 per cent Equity & Real Estate Increase**		**10 per cent Equity & Real Estate Decrease**
	Increase/(decrease) in Fair Value	**Fair Value**	**Increase/(decrease) in Fair Value**	**Increase/(decrease) in Fair Value**	**Fair Value**	**Increase/(decrease) in Fair Value**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
United Kingdom insurance operations						
With-profits fund (including PAL)	**124**	**334**	**(103)**	(13)	134	47
Shareholder-backed annuities		**68**			114	
SAIF	**19**	**33**	**(19)**	8	(11)	(7)
United States insurance operations	**(456)**	**901**	**626**	(657)	790	666
Total	**(313)**	**1,336**	**504**	(662)	1,027	706

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	31 December 2012			31 December 2011		
	100 bp Interest Rate Increase Increase/(decrease) in Fair Value	Fair Value	100 bp Interest Rate Decrease Increase/(decrease) in Fair Value	100 bp Interest Rate Increase Increase/(decrease) in Fair Value	Fair Value	100 bp Interest Rate Decrease Increase/(decrease) in Fair Value
	£m	£m	£m	£m	£m	£m
United Kingdom insurance operations						
With-profits fund (including PAL)	**(170)**	**334**	**229**	7	134	13
Shareholder-backed annuities	**(90)**	**68**	**113**	(102)	114	129
SAIF	**9**	**33**	**(10)**	18	(11)	(20)
United States insurance operations	**(625)**	**901**	**778**	(592)	790	735
Total	**(876)**	**1,336**	**1,110**	(669)	1,027	857

Limitations

The above sensitivities do not consider that assets and liabilities are actively managed and may vary at the time any actual market movement occurs. There are strategies in place to minimise the exposure to market fluctuations. For example, as market indices fluctuate, Prudential would take certain actions including selling investments, changing investment portfolio allocation, and adjusting bonuses credited to policyholders. In addition, these analyses do not consider the effect of market changes on new business generated in the future.

Other limitations on the sensitivities include: the use of hypothetical market movements to demonstrate potential risk that only represent Prudential's view of reasonably possible near-term market changes and that cannot be predicted with any certainty; the assumption that interest rates in all countries move identically; the assumption that all global currencies move in tandem with the US dollar against pounds sterling; and the lack of consideration of the inter-relation of interest rates, equity markets and foreign currency exchange rates.

Item 12. Description of Securities other than Equity Securities

Payments received from the ADR Depositary

Direct payments

J.P. Morgan Chase Bank, N.A. is the depositary ('ADR Depositary') of Prudential's ADR program. The ADR Depositary has agreed to reimburse Prudential for certain reasonable expenses related to Prudential's ADR program and incurred by Prudential in connection with the ADR program. Pursuant to this agreement, Prudential can claim up to US$75,000 for each incremental increase of 4,000,000 American Depositary Shares (ADS) issued and outstanding above the prior year's balance. The reimbursements shall be used by Prudential for actual expenses incurred in connection with the program during the contract year (year ending 19 May in each year), including but not limited to, expenses related to US investor relations servicing, US investor presentations, financial advertising and public relations.

No reimbursements were made by the ADR Depositary to Prudential in 2012 and 2011.

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Indirect payments

As part of its service to Prudential, the ADR Depositary has agreed to waive the following fees for the standard costs associated with the maintenance of the ADR program:

Category	Limit
General services, AGM services, report mailing services	up to US$5,000 per contract year

The amount of fees waived in each of the 2011 and 2012 contract years was US$5,000.

Fees or charges payable by ADR holders

The ADR holders of Prudential are required to pay the following fees to the ADR Depositary for general depositary services:

Category	ADR Depositary actions	Associated fee or charge
Depositing or surrendering the underlying shares	Each person to whom ADRs are delivered against deposits of shares, and each person surrendering ADRs for withdrawal of deposited securities	Up to US$5.00 for each 100 ADSs (or portion thereof) evidenced by the ADRs delivered or surrendered
Cable fee	Cable fee for delivery of underlying shares in the home market on the back of a cancellation	US$25 for each delivery
Currency charges	Charges incurred by the ADR Depositary in the conversion of foreign currency into US Dollars.	Amount paid by the ADR Depositary, and such charges are reimbursable out of such foreign currency.

Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

Item 14. Material Modifications to the Rights of Security Holders

None.

Item 15. Controls and Procedures

Management has evaluated, with the participation of Prudential plc's Group Chief Executive and Chief Financial Officer, the effectiveness of Prudential plc's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended ('Exchange Act')) as of 31 December 2012. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon Prudential plc's evaluation, Prudential plc's Group Chief Executive and Chief Financial Officer have concluded that as of 31 December 2012 Prudential plc's disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by Prudential plc in the reports Prudential plc files and submits under the Exchange Act is recorded,

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processed, summarised and reported, within the time periods specified in the applicable rules and forms and that it is accumulated and communicated to Prudential plc's management, including Prudential plc's Group Chief Executive and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Prudential plc is required to undertake an annual assessment of the effectiveness of internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act 2002 ('Section 404'). In accordance with the requirements of Section 404 the following report is provided by management in respect of Prudential plc's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act).

Management's Annual Report on Internal Control over Financial Reporting

Management acknowledges its responsibility for establishing and maintaining adequate internal control over financial reporting for Prudential plc. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Management has conducted, with the participation of Prudential plc's Group Chief Executive and Chief Financial Officer, an evaluation of the effectiveness of internal control over financial reporting based on the criteria set forth in 'Internal Control Integrated Framework' issued by the Committee of Sponsoring Organizations of the Treadway Commission ('COSO'). Based on the assessment under these criteria, management has concluded that, as of 31 December 2012, Prudential plc's internal control over financial reporting was effective.

On 4 September 2012, Prudential plc acquired Reassure America Life Insurance Company ('REALIC') and its subsidiaries. As allowed under the U.S. Securities and Exchange Commission ('the SEC') guidance, in conducting Prudential plc's assessment of internal control over financial reporting, management has excluded the internal control over financial reporting relating to REALIC, which, as mentioned above, was acquired in the third quarter of 2012. REALIC represents 5 per cent of the consolidated total assets of Prudential plc as at 31 December 2012, and 2 per cent of the consolidated profit before tax attributable to shareholders of Prudential plc for the year ended 31 December 2012. Management expects to complete the process of integrating REALIC's internal control over financial reporting in the course of 2013 and will include such controls in its assessment of internal control over financial reporting as of and for the year ended 31 December 2013.

In addition, there have been no changes in Prudential plc's internal control over financial reporting during 2012 that have materially affected, or are reasonably likely to affect materially, Prudential plc's internal control over financial reporting.

KPMG Audit Plc, which has audited the consolidated financial statements of Prudential plc for the year ended 31 December 2012, has also audited the effectiveness of Prudential plc's internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). KPMG Audit Plc's report on internal control over financial reporting is shown below.

Item 16A. Audit Committee Financial Expert

The Board has determined that Ann Godbehere, Chairman of the Audit Committee, qualifies as an audit committee financial expert within the meaning of Item 16A of Form 20-F, and that Ms Godbehere is independent within the meaning of Rule 10A-3 under the Exchange Act.

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Item 16B. Code of Ethics

Prudential has a code of ethics, as defined in Item 16B of Form 20-F under the Exchange Act, (which Prudential calls its Group Code of Business Conduct) which applies to the Group Chief Executive, Group Chief Financial Officer, the Group Chief Risk Officer and persons performing similar functions as well as to all other employees. Prudential's Code of Business Conduct is available on its website at www.prudential.co.uk. If Prudential amends the provisions of the Code of Business Conduct, as it applies to the Group Chief Executive, Group Chief Financial Officer and the Group Chief Risk Officer or if Prudential grants any waiver of such provisions, the Company will disclose such amendment or waiver on the Prudential website.

Item 16C. Principal Accountant Fees and Services

The Audit Committee (the 'Committee') has a key oversight role in relation to the external auditor, KPMG Audit Plc, whose primary relationship is with the Committee. The Group has established an Auditor Independence Policy which ensures that the independence and objectivity of the external auditor is not impaired. The four key principles of the policy underpin the provision of non-audit services by the external auditor, namely that the auditor should not audit its own firm's work, make management decisions for the Group, have a mutuality of financial interest with the Group or be put in the role of advocate for the Group.

All services provided by the auditor under this policy are provided in accordance with a pre-approved budget and are reviewed by the Committee and approved where necessary. The Committee regularly reviews and updates the policy to ensure alignment with the latest standards and best practice in establishing, maintaining and monitoring auditor independence and objectivity.

Fees payable to the auditor

For the year ended 31 December 2012 the Committee approved fees payable of £14.3 million to its auditor, KPMG Audit Plc. Within this total, the Committee approved fees payable of £2.6 million to KPMG for services not related to audit work which accounted for 18 per cent of total fees payable to the external auditor in the year. In accordance with the Group's Auditor Independence Policy, all services were approved prior to work commencing and each of the non-audit services was confirmed to be permissible for the external auditor to undertake as defined by the Sarbanes-Oxley Act. The Committee reviewed the non-audit services provided to the Group by KPMG at regular intervals during 2012. These included tax services, due diligence services, attestation reports on internal controls not required by legislation, agreed-upon procedures, other reports, certifications and examinations required by regulators, risk and compliance work, advising on accounting standards and regulatory rules and provision of comfort letters.

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Total fees payable to KPMG for the fiscal years ended 31 December are set out below:

	2012	2011
	£m	£m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	**2.0**	2.1
Fees payable to the Company's auditor and its associates for other services:		
Audit of subsidiaries pursuant to legislation	**6.5**	6.1
Audit related assurance services	**3.2**	2.6
Tax compliance services	**0.5**	0.6
Other assurance services	**0.5**	0.5
Services relating to corporate finance transactions	**0.4**	0.5
All other services	**1.2**	0.3
Total	**14.3**	12.7

In addition, there were fees of £0.1 million (2011: £0.1 million) for the audit of pension schemes.

2012

Fees of £2.0 million for the audit of Prudential's annual accounts comprised statutory audit fees of £0.8 million, US reporting audit fees of £0.5 million and EEV reporting audit fees of £0.7 million. Fees of £6.5 million for audit of subsidiaries and associates pursuant to legislation mainly related to the audit of local and statutory accounts and to statutory audit work in connection with the submission of results to be consolidated in Prudential's annual accounts.

Fees of £3.2 million for audit related assurance services supplied pursuant to legislation comprised of Sarbanes-Oxley reporting of £0.7 million and interim and regulatory reporting of £2.5 million.

Fees of £0.5 million for services relating to taxation related to tax compliance throughout the Group.

Fees of £0.5 million for all other assurance services comprised services in respect of accounting and regulatory requirements of £0.1 million services, in respect of attestation letters of £0.3 million, and services in respect of compliance of legislation of £0.1 million.

Fees of £1.2 million for all other services comprised model validation services of £1.1 million and other services of £0.1 million.

2011

Fees of £2.1 million for the audit of Prudential's annual accounts comprised statutory audit fees of £0.9 million, US reporting audit fees of £0.5 million and EEV reporting audit fees of £0.7 million. Fees of £6.1 million for audit of subsidiaries and associates pursuant to legislation mainly related to the audit of local and statutory accounts and to statutory audit work in connection with the submission of results to be consolidated in Prudential's annual accounts.

Fees of £2.6 million for audit related assurance services supplied pursuant to legislation comprised of Sarbanes-Oxley reporting of £0.7 million, interim and regulatory reporting of £1.8 million and fees of £0.1 relating to valuation services.

Fees of £0.6 million for services relating to taxation related to tax compliance throughout the Group.

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Fees of £0.5 million for all other assurance services comprised services in respect of accounting and regulatory requirements of £0.1 million services, in respect of attestation letters of £0.3 million, and services in respect of compliance of legislation of £0.1 million.

Auditor performance and independence

The Committee assessed the performance, as well as the independence and objectivity of the external auditor, and the effectiveness of the audit process. The review of the effectiveness of the external audit process was conducted through a questionnaire-based exercise administered by Group Finance.

The Committee also reviewed the external audit strategy and received reports from the auditor on its own policies and procedures regarding independence and quality control, including an annual confirmation of its independence in line with industry standards.

Re-appointment of auditor

The Group operates a policy under which at least once every five years a formal review is undertaken by the Committee to assess whether the external audit should be re-tendered. The external audit was last put out to competitive tender in 1999 when the present auditor was appointed. Since 2005 the Committee has annually considered the need to re-tender the external audit service and it again considered this in February 2012, concluding that there was nothing in the performance of the auditor which required a change.

In line with the Auditing Practices Board Ethical Statements and the Sarbanes-Oxley Act, the lead audit partner who was appointed by KPMG Audit Plc in 2007, was replaced by a new lead audit partner in respect of the 2012 financial year.

Following its review of the external auditor's effectiveness and independence, the Committee has recommended to the Board that KPMG Audit Plc be re-appointed as auditor of the Company and a resolution for the re-appointment of KPMG Audit Plc as auditor of the Company will be put to a shareholder vote at the Annual General Meeting on 16 May 2013.

Item 16D. Exemptions from the Listing Standards for Audit Committees

Not applicable

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Item 16E. Purchases of Equity Securities by Prudential plc and Affiliated Purchasers

The following table sets forth information with respect to purchases made by or on behalf of Prudential or any 'affiliated purchasers' (as that term is defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended) of Prudential's ordinary shares or American depositary shares for the year ended 31 December 2012.

Period	Total Number of Shares Purchased(1)	Average Price Paid Per Share	Total Number of Shares Purchased at Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under Plans or Programs
		(£)		
1 January 31 January	15,573	6.40	N/A	N/A
1 February 28 February	12,678	7.33		
1 March 31 March	4,022,002	7.97		
1 April 30 April	368,901	7.35		
1 May 31 May	939,541	6.82		
1 June 30 June	482,377	6.65		
1 July 31 July	15,047	7.26		
1 August 31 August	28,488	8.01		
1 September 30 September	712,649	8.18		
1 October 31 October	12,549	8.39		
1 November 30 November	492,993	9.13		
1 December 31 December	2,277,012	9.09		

Note

(1)

The shares listed in this column were acquired by employee benefit trusts during the year to satisfy future obligations to deliver shares under the Company's employee incentive plans, the savings related share option scheme and the share participation plan.

This table excludes Prudential plc shares purchased by investment funds managed by M&G in accordance with investment strategies that are established by M&G acting independently of Prudential plc.

In addition, 178,314 shares were allotted to the employee benefit trusts in lieu of receiving cash dividends as part of Prudential's dividend re-investment program in May and September 2012.

Item 16G. Corporate Governance

On 4 November 2003, the New York Stock Exchange (the 'NYSE') established new corporate governance rules. The application of the NYSE's rules is restricted for foreign companies, recognising that they have to comply with domestic requirements. As a foreign private issuer, Prudential must comply with the following NYSE rules:

1. The Company must satisfy the audit committee requirements of the SEC;

2. The Group Chief Executive must promptly notify the NYSE in writing after any executive officer of the Company becomes aware of any non-compliance with any applicable provisions of Section 303(A) of the NYSE's Listed Company Manual;

3. The Company must submit an executed written affirmation annually to the NYSE affirming the Company's compliance with applicable NYSE Corporate Governance Standards and submit an interim written affirmation notifying it of specified changes to its audit committee or a change to the Company's status as a foreign private issuer; and

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4. The Company must provide a brief description of any significant difference between its corporate governance practices and those followed by US companies under the NYSE listing standards.

As a company listed on the London Stock Exchange, Prudential is required to comply with the Listing Rules, Disclosure and Transparency Rules and Prospectus Rules issued by the Financial Services Authority, and to report and explain non-compliance with the UK Corporate Governance Code which is issued by the Financial Reporting Council. As a company listed on the Hong Kong Stock Exchange, Prudential is also required to comply with certain continuing obligations set forth in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the 'HK Listing Rules') and is expected to comply with or explain any deviation from the provisions of the Code on Corporate Governance Practices contained in Appendix 14 to the HK Listing Rules (the 'HK Code'). Any deviation from compliance with either corporate governance code is set out fully in the Governance Report in the Annual Report 2012.

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The table below discloses differences between Prudential's corporate governance practices and the NYSE rules on corporate governance. Unless specifically indicated otherwise, compliance with the provisions of the UK Corporate Governance Code in the table below also includes compliance with the HK Code.

	NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
	Director independence	
1	Listed companies must have a majority of independent directors.	Prudential complies with the equivalent requirements contained in the UK Corporate Governance Code (the UK Code). The UK Code requires that the Board should include a balance of executive and non-executive directors such that no individual or small group of individuals can dominate the Board's decision taking. At least half the Board, excluding the Chairman, should comprise non-executive directors determined by the Board to be independent. The Board considers that Keki Dadiseth, Howard Davies, Michael Garrett, Ann Godbehere, Alistair Johnston, Kai Nargolwala, Philip Remnant and Lord Turnbull are 'independent' under the UK Code. The Board is therefore compliant with the composition requirement under the UK Code.
2	In order to tighten the definition of 'independent director' for purposes of these standards: a) No director qualifies as 'independent' unless the Board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organisation that has a relationship with the company). The listed company must comply with the disclosure requirements set forth in Item 407(a) of Regulation S-K. b) In addition, a director is not independent if: i) The director is, or has been within the last three years, an employee of the listed company, or an immediate family member is, or has been within the last three years, an executive officer of the listed company.	The Board is required to determine whether directors are independent in character and judgment and whether there are relationships or circumstances which are likely to affect, or could affect, the directors' judgment. If the Board determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination it shall state its reasons. In undertaking this process the Board is required, amongst other factors, to consider if the director: Has been an employee of Prudential plc or the Group within the last five years; Has, or has had within the last three years, a material business relationship with Prudential either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with Prudential;

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NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
ii) The director has received, or has an immediate family member who has received, during any twelve-month period within the last three years, more than $120,000 in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service). Prudential complies with the corresponding domestic requirements contained in the Code, which sets out the principles for the Company to determine whether a director is 'independent'.	Has received or receives additional remuneration from Prudential apart from a director's fee, participates in Prudential's share option or a performance-related pay scheme, or is a member of Prudential's pension scheme; Has close family ties with any of Prudential's advisers, directors or senior employees; Holds cross-directorships or has significant links with other directors through involvement in other companies or bodies; Represents a significant shareholder; or Has served on the Board for more than nine years from the date of their first election. In addition, in assessing whether its directors are 'independent', the Board considers a further list of factors set forth in the HK Listing Rules that the Hong Kong Stock Exchange takes into account in assessing the independence of non executive directors (without treating any such factor as necessarily conclusive). These include, among others, whether a director: is a director, partner or principal of a professional adviser which currently provides, or has within one year immediately prior to the date of his proposed appointment provided, services, or is an employee of such professional adviser who is or has been involved in providing such services during the same period to, among others, Prudential or any of its subsidiaries; is, or has at any time during the two years immediately prior to the date of proposed appointment been, an executive or director (other than an independent non-executive director) of, among others, Prudential or any of its subsidiaries. Keki Dadiseth and Barry Stowe also serve as non-executive directors of ICICI Prudential Life Insurance Company Limited, an Indian company which is owned 26 per cent by Prudential, and in addition Mr Dadiseth serves at Prudential's request as a non-executive director of ICICI Prudential Trust Limited, an Indian company which is owned 49 per cent by Prudential. The Board does not consider that these appointments in any way affect Mr Dadiseth's status as an independent director of Prudential. Alistair Johnston was a partner in Prudential's auditor, KPMG, from 1986 to 2010. However, he did not audit the Group and he no longer has any financial or other interest in KPMG. The Board does not consider that this former relationship with KPMG affected Mr Johnston's status as an independent director of Prudential.
iii) (A) The director is a current partner or employee of a firm that is the listed company's internal or external auditor; (B) the director has an immediate family member who is a current partner of such a firm; (C) the director has an immediate family member who is a current employee of such a firm and personally works on the listed company's audit; or (D) the director or an immediate family member was within the last three years a partner or employee of such a firm and personally worked on the listed company's audit within that time.	
iv) The director or an immediate family member is, or has been within the last three years, employed as an executive officer of another company where any of the listed company's present executive officers at the same time serves or served on that company's compensation committee.	
v) The director is a current employee, or an immediate family member is a current executive officer, of a company that has made payments to, or received payments from, the listed company for property or services in an amount which, in any of the last three fiscal years, exceeds the greater of $1 million, or 2 per cent of such other company's consolidated gross revenues.	

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NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
	The non-executive Directors considered by the Board to be independent are identified in the Company's Annual Reports in accordance with the UK Code and on Prudential's website. Throughout the year 2012 all non-executive directors were considered by the Board to be independent in character and judgment and met the provisions for independence set out in the UK and HK Codes. Prudential has received confirmation of independence from each of the independent non-executive directors as required by the HK Listing Rules.
Executive Sessions	
3 To empower non-management directors to serve as a more effective check on management, the non-management directors of each listed company must meet at regularly scheduled executive sessions without management.	Prudential complies with the equivalent provisions set out in the UK Code, which requires that the Chairman of Prudential should hold meetings with the non-executive directors without executives present. The Chairman of Prudential usually meets formally, at least annually, with the non-executive directors without the executive directors being present. During 2012, the Chairman met with the non-executive directors without the presence of the executive directors on four occasions.
Nominating/Corporate Governance Committee	
4 a) Listed companies must have a nominating/ corporate governance committee composed entirely of independent directors. b) The nominating/corporate governance committee must have a written charter that addresses: i) the committee's purpose and responsibilities which, at minimum, must be to: identify individuals qualified to become board members, consistent with criteria approved by the Board, and to select, or to recommend that the Board select, the director nominees for the next annual meeting of shareholders; develop and recommend to the Board a set of corporate governance guidelines applicable to the corporation; and oversee the evaluation of the Board and management; and ii) an annual performance evaluation of the committee.	Prudential complies with the corresponding provisions set out in the UK Code, which requires that Prudential has a Nomination Committee, which should comprise a majority of independent non-executive directors. Prudential's Nomination Committee has written terms of reference in accordance with the UK Code. The terms of reference are available on Prudential's website, and explain the Nomination Committee's role and the authority delegated to it by the Board. The Board is responsible for regularly reviewing its corporate governance standards and practices. Requirements of the UK code to which Prudential is subject, do not mandate it to establish a corporate governance committee. Under the UK Code, the Board should state in the annual report how performance evaluation of the Board, its committees and its individual directors has been conducted. Prudential includes such description in its Annual Report, which is available on its website.

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	NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
Compensation Committee		
5	a) Listed companies must have a compensation committee composed entirely of independent directors. b) The compensation committee must have a written charter that addresses: i) the committee's purpose and responsibilities which, at minimum, must be to have direct responsibility to: a) review and approve corporate goals and objectives relevant to CEO compensation, evaluate the CEO's performance in light of those goals and objectives, and, either as a committee or together with the other independent directors (as directed by the Board), determine and approve the CEO's compensation level based on this evaluation; and b) make recommendations to the Board with respect to non-CEO executive officer compensation, and incentive-compensation and equity-based plans that are subject to Board approval; and c) prepare the disclosure required by Item 407(e)(5) of Regulation S-K; ii) an annual performance evaluation of the compensation committee.	Prudential complies with the equivalent provisions set out in the UK Code, which require that Prudential must have a Remuneration Committee that is comprised of at least three independent non-executive directors. Prudential's Remuneration Committee has written terms of reference in accordance with the UK Code. The terms of reference are available on Prudential's website. Prudential complies with the equivalent requirement set out in the UK Code, which provides that the Remuneration Committee: a) should have delegated responsibility for setting remuneration for all executive directors and the chairman, including pension rights and any compensation payments; b) should recommend and monitor the level and structure of remuneration for senior management; c) should carefully consider what compensation commitments (including pension contributions and all other elements) their directors' terms of appointment would entail in the event of early termination; and d) that the annual report should include a description of the work of the Remuneration Committee. Under the UK Code, the Board should state in the annual report how performance evaluation of the Board, its committees and its individual directors has been conducted. Prudential includes such description in its Annual Report which is available on its website.

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	NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
Audit Committee		
6	Listed companies must have an audit committee that satisfies the requirements of Rule 10A-3 under the Securities Exchange Act. In general: Rule 10A-3(1) requires that each member of the audit committee be a member of the board of directors of the listed issuer, and be independent within the meaning of the Rule, subject to certain exemptions; Rule 10A-3(2) requires the audit committee to be directly responsible for the appointment, compensation, retention and oversight of the work of the independent auditor engaged for the purpose of preparing or issuing an audit report or performing other audit, review or attest services for the issuer, and the independent auditor must report directly to the audit committee; Rule 10A-3(3) requires that an audit committee establish procedures for the receipt, retention and treatment of complaints received by the issuer regarding accounting, internal accounting controls or auditing matters and for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters; Rule 10A-3(4) requires that an audit committee have the authority to engage outside advisors, including counsel, as it determines necessary to carry out its duties. The Rule also requires the issuer to provide appropriate funding, as determined by the audit committee, for payment of compensation to the issuer's independent auditor and to any advisors employed by the audit committee; Rule 10A-3(5) requires that the audit committee be directly responsible for the appointment, compensation, retention and oversight of the work of the independent auditor engaged for the purpose of preparing an audit report or performing other audit, review or attest services for the issuer, and the independent auditor must report directly to the audit committee.	Prudential complies with equivalent requirements set out in the UK Code, which requires that Prudential has an Audit Committee that is comprised entirely of at least three independent non-executive directors. Prudential's Audit Committee has written terms of reference prepared in accordance with the requirements of the UK Code and related guidance. The terms of reference are available on Prudential's website and explain the Audit Committee's role and the authority delegated to it by the Board. The terms of reference, amongst other items, set out the Committee's role and responsibilities in respect of the external audit. The Committee reviews management's and the external and internal auditors' reports on the effectiveness of systems for internal control, financial reporting and risk management. It also reviews the effectiveness of the Group Governance Framework. The Audit Committee makes recommendations, through the Board, to be put to shareholders for approval at the Annual General Meeting, in relation to the appointment, re-appointment or removal of the external auditor. The Audit Committee has established a procedure for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls or auditing matters. The Audit Committee has the authority to engage independent counsel and other advisers as it determines necessary to carry out its duties. Prudential must provide appropriate funding for the Audit Committee.

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	NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
7	a) The audit committee must have a minimum of three members. All audit committee members must satisfy the requirements for independence set out in Section 303A.02 and, in the absence of an applicable exemption Rule I0A-3(b)(1).	Prudential complies with the equivalent provisions set out in the UK Code which requires that the Audit Committee should comprise a minimum of three 'independent' non-executive directors. Prudential has determined that each member of its Audit Committee is 'independent' for the purposes of Rule 10A-3(6)(1) under the Securities Exchange Act and UK Code. Prudential complies with the equivalent provisions set out in the UK Code which requires that the Board should satisfy itself that at least one member of the Audit Committee has recent and relevant financial experience. The Board of Prudential has designated that Ann Godbehere, Chairman of the Audit Committee, qualifies as an audit committee financial expert.
	b) The audit committee must have a written charter that addresses:	Prudential's Audit Committee has written terms of reference in accordance with the UK Code. The terms of reference are available on Prudential's website.
	i) the committee's purpose which, at minimum, must be to:	The UK Code requires that the main role and responsibilities of the Audit Committee should include:
	(A) assist board oversight of (1) the integrity of the listed company's financial statements, (2) the listed company's compliance with legal and regulatory requirements, (3) the independent auditor's qualifications and independence, and (4) the performance of the listed company's internal audit function and independent auditors; and	To monitor the integrity of the financial statements of the Company; To review the Company's internal financial controls and risk management systems as they relate to financial reporting; To monitor and review the effectiveness of the Company's internal audit function; To make recommendations to the Board, for it to put to the shareholders for their approval in general meeting, in relation to the appointment, re-appointment and removal of the external auditor and to authorise the Board to set the remuneration and terms of engagement of the external auditor. To review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; To develop and implement policy on the engagement of the external auditor to supply non-audit services, taking into account relevant guidance regarding the provision of non-audit services by the external audit firm, and to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken; and To report to the Board on how it has discharged its

responsibilities.

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NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
(B) prepare the disclosure required by Item 407(d)(3)(i) of Regulation S-K;	The UK Code requires that there is a separate section in a Company's Annual Report which describes the work of the Committee in discharging its duties.
ii) an annual performance evaluation of the audit committee; and	A description of the Committee's evaluation is included in the Annual Report.
iii) the duties and responsibilities of the audit committee which, at a minimum, must include those set out in Rule 10A-3(b)(2), (3), (4) and (5) of the Exchange Act, as well as to:	
(A) at least annually, obtain and review a report by the independent auditor describing: the firm's internal quality-control procedures; any material issues raised by the most recent internal quality-control review, or peer review, of the firm, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, respecting one or more independent audits carried out by the firm, and any steps taken to deal with any such issues; and (to assess the auditor's independence) all relationships between the independent auditor and the listed company;	Prudential's Audit Committee monitors and reviews the effectiveness of the Company's internal audit function.
(B) Meet to review and discuss the listed company's annual audited financial statements and quarterly financial statements with management and the independent auditor, including reviewing the listed company's specific disclosures under 'Management's Discussion and Analysis of Financial Condition and Results of Operations';	Prudential's Audit Committee monitors the integrity of the financial statements of the Company, and any formal announcements relating to the Company's financial performance, reviewing significant financial reporting judgments contained in them.
(C) Discuss the listed company's earnings press releases, as well as financial information and earnings guidance provided to analysts and rating agencies;	Prudential's Audit Committee reviews the Company's interim management statements and press releases associated with key financial results prior to their publication.
(D) Discuss policies with respect to risk assessment and risk management;	Prudential's Audit Committee reviews the Company's internal financial controls and, unless expressly addressed by the Board itself, reviews the Company's internal control and risk management systems in relation to financial reporting. The Group Risk Committee has responsibility for the oversight of risk management.

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NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
(E) Meet separately, periodically, with management, with internal auditors (or other personnel responsible for the internal audit function) and with independent auditors;	Committee members meet separately with management throughout the year and at least annually meet alone with the internal and external auditors.
(F) review with the independent auditor any audit problems or difficulties and management's response;	The terms of reference of Prudential's Audit Committee require it to consider management's responses to any major external audit recommendations, and to resolve disagreements between management and the external auditor regarding financial reporting.
(G) set clear hiring policies for employees or former employees of the independent auditors; and	The terms of reference of Prudential's Audit Committee require it to set clear hiring policies for employees or former employees of the external auditor.
(H) report regularly to the Board of directors.	Prudential's Audit Committee reports regularly to the Board of directors.
c) Each listed company must have an internal audit function.	Where there is no internal audit function, the audit committee should consider annually, under the requirements of the UK Code, whether there is a need for an internal audit function and make a recommendation to the Board, and the reasons for the absence of such a function should be explained in the relevant section of the annual report.

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	NYSE Corporate Governance Rules	Description of differences between Prudential's governance practice and the NYSE Corporate Governance Rules
Shareholder Approval of Equity Compensation Plans		
8	Shareholders must be given the opportunity to vote on all equity-compensation plans and material revisions thereto, except for employment inducement awards, certain grants, plans and amendments in the context of mergers and acquisitions, and certain specific types of plans.	Prudential complies with corresponding domestic requirements in the Listing Rules issued by the Financial Services Authority which mandate that the Company must seek shareholder approval for employee share plans.
Corporate Governance Guidelines		
9	Listed companies must adopt and disclose corporate governance guidelines.	Prudential complies with the corresponding provisions set out in the Listing Rules issued by the Financial Services Authority and the UK Code, which require that Prudential include an explanation in its Annual Report of how it complies with the principles of the UK Code and require confirmation that it complies with the UK Code's provisions or, where it does not, to provide an explanation of why it does not comply.
Code of Business Conduct and Ethics		
10	Listed companies must adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers.	Prudential's Code of Business Conduct is available on Prudential's website. Although not required by the Sarbanes-Oxley Act, Prudential has extended the applicability of its Code of Business Conduct to all employees.
Description of Significant Differences		
11	Listed foreign private issuers must disclose any significant ways in which their corporate governance practices differ from those followed by domestic companies under NYSE listing standards.	Prudential conforms by publishing this document to fulfill the requirement.
12	A foreign private issuer that is required to file an annual report on Form 20-F with the SEC must include the statement of significant differences in that annual report. All other foreign private issuers may either (i) include the statement of significant differences in an annual report filed with the SEC or (ii) make the statement of significant differences available on or through the listed company's website. If the statement of significant differences is made available on or through the listed company's website, the listed company must disclose that fact in its annual report filed with the SEC and provide the website address.	Prudential conforms by publishing this document in its annual report on Form 20-F and on its website to fulfill the requirement. The address of the website is also published in Prudential's Form 20-F.
13	Listed companies must have and maintain a publicly accessible website.	Prudential conforms by maintaining a publicly accessible website, on which a printable version of the terms of reference of its Remuneration Committee, Nomination Committee, Risk Committee and Audit Committee, its corporate governance practice, its Code of Business Conduct and document disclosing any significant ways in which its corporate governance practices differ from those followed by companies under NYSE listing standards are posted in the English language.

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Item 18. Financial Statements

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Prudential plc

We have audited the accompanying consolidated statements of financial position as at 31 December 2012, 2011, and 2010, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for each of the years in the three-year period ended 31 December 2012, including the disclosures marked 'audited' within the Risk Management section on pages 50 to 64 of Item 4 of the 2012 Form 20-F of Prudential plc (the Company) and its subsidiaries (collectively, the Group), and the related condensed financial statement Schedule II of the Company. We also have audited the Group's internal control over financial reporting as of 31 December 2012 based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Group's management is responsible for these consolidated financial statements and condensed financial statement schedule, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying 'Controls and Procedures'. Our responsibility is to express an opinion on the accompanying consolidated financial statements and condensed financial statement schedule and an opinion on the Group's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorisations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Group as of 31 December 2012, 2011, and 2010, and the results of its operations and its cash flows for each of the years in the three-year period ended 31 December 2012, in conformity with International Financial Reporting Standards (IFRS) as issued by the International

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Accounting Standards Board (IASB). Also, in our opinion, the related condensed financial statement schedule of the Company, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein in conformity with UK generally accepted accounting practice (UK GAAP). Accounting principles under UK GAAP vary in certain significant respects from IFRS as issued by the IASB. Information relating to the nature and effect of such differences is presented in note 3 to the condensed financial statement schedule of the Company.

As discussed in note A5 to the consolidated financial statements, the Group changed its accounting policy for deferring acquisition costs for certain operations of the Group in 2012.

Also in our opinion, the Group maintained, in all material respects, effective internal control over financial reporting as of 31 December 2012, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

The scope of management's assessment of internal control over financial reporting as of 31 December 2012 includes all of the subsidiaries of Prudential plc, except for Reassure America Life Insurance Company (REALIC) which was acquired on 4 September 2012. The consolidated profit before tax attributable to shareholders of Prudential plc and subsidiaries for the year ended 31 December 2012 was £2,810 million of which REALIC represented £61 million. The consolidated total assets of Prudential plc and its subsidiaries as of 31 December 2012 were £310,253 million of which REALIC represented £15,141 million. Our audit of internal control over financial reporting of Prudential plc also excluded an evaluation of the internal control over financial reporting of REALIC.

16 April 2013

/s/ KPMG AUDIT PLC

KPMG Audit Plc
London, England

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Prudential plc and subsidiaries

Consolidated Income Statements

Years ended 31 December

	Note	2012	2011*	2010*
		£m	£m	£m
Gross premiums earned		**29,910**	25,706	24,568
Outward reinsurance premiums		**(506)**	(429)	(357)
Earned premiums, net of reinsurance	**F2**	**29,404**	25,277	24,211
Investment return	**F2**	**24,051**	9,360	21,769
Other income	**F2**	**2,021**	1,869	1,666
Total revenue, net of reinsurance	**F1,F2**	**55,476**	36,506	47,646
Benefits and claims		**(44,831)**	(31,060)	(40,608)
Outward reinsurers' share of benefit and claims	**F1**	**259**	746	335
Movement in unallocated surplus of with-profits funds	**H12**	**(1,381)**	1,025	(245)
Benefits and claims and movement in unallocated surplus of with-profits funds, net of reinsurance		**(45,953)**	(29,289)	(40,518)
Acquisition costs and other expenditure	**F3**	**(6,055)**	(5,120)	(4,989)
Finance costs: interest on core structural borrowings of shareholder-financed operations	**F4**	**(280)**	(286)	(257)
Total charges, net of reinsurance	**F1**	**(52,288)**	(34,695)	(45,764)
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)***		**3,188**	1,811	1,882
(Less) add tax (charge) credit attributable to policyholders' returns		**(378)**	17	(611)
Profit before tax attributable to shareholders	**B1**	**2,810**	1,828	1,271
Total tax (charge) attributable to policyholders and shareholders	**F5**	**(991)**	(392)	(571)
Adjustment to remove tax credit (charge) attributable to policyholders' returns		**378**	(17)	611
Tax charge attributable to shareholders' returns	**F5**	**(613)**	(409)	40
Profit for the year		**2,197**	1,419	1,311
Attributable to:				
Equity holders of the Company		**2,197**	1,415	1,306

Non-controlling interests			4	5
Profit for the year		**2,197**	1,419	1,311
Earnings per share (in pence)				
Basic:				
Based on profit from continuing operations attributable to the equity holders of the Company	**B2**	**86.5 p**	55.8 p	51.8 p
Diluted:				
Based on profit from continuing operations attributable to the equity holders of the Company	**B2**	**86.4 p**	55.7 p	51.7 p

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

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This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders. This is principally because the corporate taxes of the Group include those on the income of consolidated with-profits and unit-linked funds that, through adjustments to benefits, are borne by policyholders. These amounts are required to be included in the tax charge of the Company under IAS 12. Consequently, the profit before all taxes measure (which is determined after deducting the cost of policyholder benefits and movements in the liability for unallocated surplus of the PAC with-profits fund after adjusting for taxes borne by policyholders) is not representative of pre-tax profits attributable to shareholders.

The 2010 tax charge attributable to shareholders' return included an exceptional tax credit of £158 million which primarily related to the impact of a settlement agreed with the UK tax authorities. In addition the 2010 profit before tax is stated after £377 million of pre-tax costs of the terminated AIA transaction.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries
Consolidated Statements of Comprehensive Income
Years ended 31 December

	Note	2012	2011*	2010*
		£m	£m	£m
Profit for the year		**2,197**	1,419	1,311
Other comprehensive income:				
Exchange movements on foreign operations and net investment hedges:				
Exchange movements arising during the year	**B4**	**(214)**	(37)	203
Related tax		**(2)**	(68)	34
		(216)	(105)	237
Unrealised valuation movements on securities of US insurance operations classified as available-for-sale:	**D3(a)**			
Unrealised holding gains arising during the year		**930**	912	1,170
Deduct net (gains)/add back net losses included in the income statement on disposal and impairment		**(68)**	(101)	51
Total		**862**	811	1,221
Related change in amortisation of deferred acquisition costs	**H1(b)**	**(270)**	(275)	(410)
Related tax		**(205)**	(187)	(278)
		387	349	533
Other comprehensive income for the year, net of related tax		**171**	244	770
Total comprehensive income for the year		**2,368**	1,663	2,081
Attributable to:				
Equity holders of the Company		**2,368**	1,659	2,076
Non-controlling interests			4	5
Total comprehensive income for the year		**2,368**	1,663	2,081

* The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Changes in Equity

Year ended 31 December

		Year ended 31 December 2012							
	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Shareholders' equity	Non-controlling interests	Total equity
		£m	£m	£m	£m	£m	£m	£m	£m
Reserves									
Profit for the year				**2,197**			**2,197**		**2,197**
Other comprehensive income									
Exchange movements on foreign operations and net investment hedges, net of related tax					**(216)**		**(216)**		**(216)**
Unrealised valuation movements, net of related change in amortisation of deferred acquisition costs and related tax						**387**	**387**		**387**
Total other comprehensive income					**(216)**	**387**	**171**		**171**
Total comprehensive income for the year				**2,197**	**(216)**	**387**	**2,368**		**2,368**
Dividends	**B3**			**(655)**			**(655)**		**(655)**
Reserve movements in respect of share-based payments				**42**			**42**		**42**
Change in non-controlling interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and other consolidated investment funds								**(38)**	**(38)**
Share capital and share premium									
New share capital subscribed	**H11**	**1**	**16**				**17**		**17**
Treasury shares									
Movement in own shares in respect of share-based payment plans				**(13)**			**(13)**		**(13)**
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS				**36**			**36**		**36**

Net increase (decrease) in equity		**1**	**16**	**1,607**	**(216)**	**387**	**1,795**	**(38)**	**1,757**
At beginning of year:									
As previously reported		**127**	**1,873**	**5,839**	**354**	**924**	**9,117**	**43**	**9,160**
Effect of change in accounting policy for deferred acquisition costs	**A5**			**(595)**	**(72)**	**114**	**(553)**		**(553)**
After effect of change		**127**	**1,873**	**5,244**	**282**	**1,038**	**8,564**	**43**	**8,607**
At end of year	**H11**	**128**	**1,889**	**6,851**	**66**	**1,425**	**10,359**	**5**	**10,364**

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Changes in Equity (Continued)

Year ended 31 December

		Year ended 31 December 2011*							
	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Shareholders' equity	Non-controlling interests	Total equity
		£m	£m	£m	£m	£m	£m	£m	£m
Reserves									
Profit for the year				1,415			1,415	4	1,419
Other comprehensive income									
Exchange movements on foreign operations and net investment hedges, net of related tax					(105)		(105)		(105)
Unrealised valuation movements, net of related change in amortisation of deferred acquisition costs and related tax						349	349		349
Total other comprehensive income					(105)	349	244		244
Total comprehensive income for the year				1,415	(105)	349	1,659	4	1,663
Dividends	B3			(642)			(642)		(642)
Reserve movements in respect of share-based payments				44			44		44
Change in non-controlling interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and other consolidated investment funds								(5)	(5)
Share capital and share premium									
New share capital subscribed	H11		17				17		17
Treasury shares									
Movement in own shares in respect of share-based payment plans				(30)			(30)		(30)
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS				(5)			(5)		(5)
Net increase (decrease) in equity			17	782	(105)	349	1,043	(1)	1,042
At beginning of year:									

As previously reported		127	1,856	4,982	454	612	8,031	44	8,075
Effect of change in accounting policy for deferred acquisition costs				(520)	(67)	77	(510)		(510)
After effect of change		127	1,856	4,462	387	689	7,521	44	7,565
At end of year	H11	127	1,873	5,244	282	1,038	8,564	43	8,607

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Changes in Equity (Continued)

Year ended 31 December

		Year ended 31 December 2010*							
	Note	Share capital	Share premium	Retained earnings	Translation reserve	Available-for-sale securities reserve	Shareholders' equity	Non-controlling interests	Total equity
		£m	£m	£m	£m	£m	£m	£m	£m
Reserves									
Profit for the year				1,306			1,306	5	1,311
Other comprehensive income									
Exchange movements on foreign operations and net investment hedges, net of related tax					237		237		237
Unrealised valuation movements, net of related change in amortisation of deferred income and acquisition costs and related tax						533	533		533
Total other comprehensive income					237	533	770		770
Total comprehensive income for the year				1,306	237	533	2,076	5	2,081
Dividends	B3			(511)			(511)		(511)
Reserve movements in respect of share-based payments				37			37		37
Change in non-controlling interests arising principally from purchase and sale of property partnerships of the PAC with-profits fund and other consolidated investment funds								7	7
Share capital and share premium									
New share capital subscribed (including shares issued in lieu of cash dividends)	H11		75				75		75
Reserve movements in respect of shares issued in lieu of cash dividends	H11		(62)	62					
Treasury shares									
Movement in own shares in respect of share-based payment plans				(4)			(4)		(4)
Movement in Prudential plc shares purchased by unit trusts consolidated under IFRS				3			3		3

Net increase in equity			13	893	237	533	1,676	12	1,688
At beginning of period									
As previously reported		127	1,843	3,964	203	134	6,271	32	6,303
Effect of improvement in accounting policy for deferred acquisition costs				(395)	(53)	22	(426)		(426)
After effect of improvement		127	1,843	3,569	150	156	5,845	32	5,877
At end of year	H11	127	1,856	4,462	387	689	7,521	44	7,565

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Financial Position

31 December

	Note	2012	2011*	2010*
		£m	£m	£m
Assets				
Intangible assets attributable to shareholders:				
Goodwill	H1(a)	**1,469**	1,465	1,466
Deferred acquisition costs and other intangible assets	H1(b)	**4,267**	4,234	3,901
Total		**5,736**	5,699	5,367
Intangible assets attributable to with-profits funds:				
In respect of acquired subsidiaries for venture fund and other investment purposes	H2(a)	**178**	178	166
Deferred acquisition costs and other intangible assets	H2(b)	**78**	89	110
Total		**256**	267	276
Total intangible assets		**5,992**	5,966	5,643
Other non-investment and non-cash assets:				
Property, plant and equipment	H6	**765**	748	554
Reinsurers' share of insurance contract liabilities§	H3	**6,859**	1,647	1,344
Deferred tax assets	H4	**2,314**	2,276	2,188
Current tax recoverable	H4	**254**	546	555
Accrued investment income	G1,H5	**2,798**	2,710	2,668
Other debtors	G1,H5	**1,361**	987	903
Total		**14,351**	8,914	8,212
Investments of long-term business and other operations:				
Investment properties	H7	**10,880**	10,757	11,247
Associate investments accounted for using the equity method	H8	**113**	70	71
Financial investments :	G1			
Loans		**11,821**	9,714	9,261
Equity securities and portfolio holdings in unit trusts		**99,958**	87,349	86,635
Debt securities		**140,103**	124,498	116,352
Other investments		**7,900**	7,509	5,779
Deposits		**12,653**	10,708	9,952
Total		**283,428**	250,605	239,297

Properties held for sale	**H9**	**98**	3	257
Cash and cash equivalents	**G1,H10**	**6,384**	7,257	6,631
Total assets	**B5**	**310,253**	272,745	260,040

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

As a result of the adoption of the altered US GAAP requirements as noted above, the 2010 balance sheet has been presented in accordance with IAS 1. The 2010 comparatives for the relevant balance sheet notes which have been affected by this change have been retrospectively adjusted accordingly.

Included within financial investments are £3,015 million (2011: £7,843 million) of lent securities and £2,012 million of loans and debt securities covering liabilities for funds withheld under reinsurance arrangements of the Group's US operations from the purchase of REALIC, as discussed in note I1.

§

The increase in reinsurers' share of insurance contract liabilities and other liabilities from 2011 to 2012 is attributed to amounts due to the reinsurance arrangements attaching to the purchase by Jackson of REALIC in September 2012, as discussed in note I1.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Financial Position (Continued)

31 December

	Note	2012	2011*	2010*
		£m	£m	£m
Equity and liabilities				
Equity				
Shareholders' equity	H11	**10,359**	8,564	7,521
Non-controlling interests		**5**	43	44
Total equity		**10,364**	8,607	7,565
Liabilities				
Policyholder liabilities and unallocated surplus of with-profits funds:				
Insurance contract liabilities	H12	**208,584**	180,363	171,291
Investment contract liabilities with discretionary participation features	G1	**33,812**	29,745	25,732
Investment contract liabilities without discretionary participation features	G1	**18,378**	16,967	17,704
Unallocated surplus of with-profits funds	H12	**10,589**	9,215	10,253
Total		**271,363**	236,290	224,980
Core structural borrowings of shareholder-financed operations:				
Subordinated debt	H13	**2,577**	2,652	2,718
Other	H13	**977**	959	958
Total	G1,H13	**3,554**	3,611	3,676
Other borrowings:				
Operational borrowings attributable to shareholder-financed operations	G1,H13	**2,245**	3,340	3,004
Borrowings attributable to with-profits operations	G1,H13	**1,033**	972	1,522
Other non-insurance liabilities:				
Obligations under funding, securities lending and sale and repurchase agreements	G1	**2,436**	3,114	4,199
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	G1	**4,345**	3,840	3,372
Deferred tax liabilities	H4	**3,970**	3,929	3,968
Current tax liabilities	H4	**445**	930	831
Accruals and deferred income		**833**	736	707
Other creditors	G1	**2,781**	2,544	2,321
Provisions	H14	**601**	529	729

Derivative liabilities	**G1,G3**	**2,829**	3,054	2,037
Other liabilities	**G1,H15**	**3,454**	1,249	1,129
Total		**21,694**	19,925	19,293
Total liabilities	**B5**	**299,889**	264,138	252,475
Total equity and liabilities		**310,253**	272,745	260,040

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS 4 for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

As a result of the adoption of the altered US GAAP requirements as noted above, the 2010 balance sheet has been presented in accordance with IAS 1. The 2010 comparatives for the relevant balance sheet notes which have been affected by this change have been retrospectively adjusted accordingly.

The increase in reinsurers' share of insurance contract liabilities and other liabilities from 2011 to 2012 is attributed to amounts due to the reinsurance arrangements attaching to the purchase by Jackson of REALIC in September 2012, as discussed in note I1.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Cash Flows

Years ended 31 December

	Note	2012	2011*	2010*
		£m	£m	£m
Cash flows from operating activities				
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)*[note(i)]		**3,188**	1,811	1,882
Total profit before tax		**3,188**	1,811	1,882
Non-cash movements in operating assets and liabilities reflected in profit before tax:				
Investments		**(27,126)**	(8,854)	(24,594)
Other non-investment and non-cash assets		**(801)**	(999)	(1,146)
Policyholder liabilities (including unallocated surplus)		**26,710**	10,874	24,287
Other liabilities (including operational borrowings)		**(969)**	(859)	1,301
Interest income and expense and dividend income included in result before tax		**(7,772)**	(7,449)	(7,514)
Other non-cash items[note(ii)]		**128**	108	345
Operating cash items:				
Interest receipts		**6,483**	6,365	6,277
Dividend receipts		**1,530**	1,302	1,412
Tax paid		**(925)**	(561)	(302)
Net cash flows from operating activities		**446**	1,738	1,948
Cash flows from investing activities				
Purchases of property, plant and equipment	**H6**	**(139)**	(124)	(93)
Proceeds from disposal of property, plant and equipment		**14**	10	4
Acquisition of subsidiaries, net of cash balance[note(iii)]	**I1**	**(224)**	(53)	(145)
Change to Group's holdings, net of cash balance	**I2**	**23**		
Net cash flows from investing activities		**(326)**	(167)	(234)
Cash flows from financing activities				
Structural borrowings of the Group:	**I10**			
Shareholder-financed operations:[note(iv)]				
Issue of subordinated debt, net of costs			340	
Redemption of senior debt			(333)	
Bank loan		**25**		250
Interest paid		**(270)**	(286)	(251)
With-profits operations:[note(v)]				
Interest paid		**(9)**	(9)	(9)
Equity capital:[note(vi)]				
Issues of ordinary share capital	**H11**	**17**	17	13
Dividends paid	**B3**	**(655)**	(642)	(449)
Net cash flows from financing activities		**(892)**	(913)	(446)
Net (decrease) increase in cash and cash equivalents		**(772)**	658	1,268
Cash and cash equivalents at beginning of year		**7,257**	6,631	5,307

Effect of exchange rate changes on cash and cash equivalents		**(101)**	(32)	56
Cash and cash equivalents at end of year	**H10**	**6,384**	7,257	6,631

*

The Group has adopted updated US GAAP requirements for deferred acquisition costs as an improvement to its accounting policy under IFRS4, for those operations of the Group which measure insurance assets and liabilities substantially by reference to US GAAP principles. Accordingly, the 2011 and 2010 comparative results and related notes have been adjusted from those previously published for the retrospective application of the change as if the new accounting policy had always applied, as described in note A5.

The accompanying notes are an integral part of these financial statements

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Prudential plc and subsidiaries

Consolidated Statements of Cash Flows (Continued)

Years ended 31 December

Notes

(i)

This measure is the formal profit before tax measure under IFRS but it is not the result attributable to shareholders.

(ii)

Other non-cash items consist of the adjustment of non-cash items to profit before tax together with other net items, net purchases of treasury shares and other net movements in equity.

(iii)

The acquisition of REALIC in 2012, as explained further in note I1, resulted in a net cash outflow of £224 million. The acquisition of subsidiaries in 2011 related to the PAC with-profits fund's purchase of Earth and Wind, and Alticom venture investments with an outflow of £53 million. In 2010 the acquisition of United Overseas Bank Life Assurance Limited (UOB) resulted in an outflow of cash of £133 million with the remaining outflow of £12 million relating to the PAC with-profits fund purchase of Meterserve.

(iv)

Structural borrowings of shareholder-financed operations comprise the core debt of the parent company, a PruCap bank loan and Jackson surplus notes. Core debt excludes borrowings to support short-term fixed income securities programmes, non-recourse borrowings of investment subsidiaries of shareholder-financed operations and other borrowings of shareholder-financed operations. Cash flows in respect of these borrowings are included within cash flows from operating activities.

(v)

Interest paid on structural borrowings of with-profits operations relate solely to the £100 million 8.5 per cent undated subordinated guaranteed bonds, which contribute to the solvency base of the Scottish Amicable Insurance Fund (SAIF), a ring-fenced sub-fund of the PAC with-profits fund. Cash flows in respect of other borrowings of with-profits funds, which principally relate to consolidated investment funds, are included within cash flows from operating activities.

(vi)

Cash movements in respect of equity capital in 2010 exclude scrip dividends. The scrip dividend alternative has been replaced by the Dividend Re-investment Plan (DRIP) from the 2010 final dividend.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies

A1: Nature of operations

Prudential plc (the Company) together with its subsidiaries (collectively, the Group or Prudential) is an international financial services group with its principal operations in Asia, the US and the UK. Prudential offers a wide range of retail financial products and services and asset management services throughout these territories. The retail financial products and services principally include life insurance, pensions and annuities as well as collective investment schemes.

In Asia, the Group has operations in Hong Kong, Malaysia, Singapore, Indonesia and other Asian countries. The life insurance products offered by the Group's operations in Asia include with-profits (participating) and non-participating term, whole life and endowment and unit-linked policies. In Asia, unit-linked policies are usually sold with insurance riders such as health covers.

In the US, the Group's principal subsidiary is Jackson National Life Insurance Company (Jackson). The principal products written by Jackson are fixed annuities (interest-sensitive, fixed indexed and immediate annuities), variable annuities (VA), life insurance and institutional products.

The Group operates in the UK through its subsidiaries, primarily The Prudential Assurance Company Limited (PAC), Prudential Annuities Limited (PAL), Prudential Retirement Income Limited (PRIL) and M&G Investment Management Limited. Long-term business products written in the UK are principally with-profits deposit administration, other conventional and unitised with-profits policies and non-participating pension annuities in the course of payment. Long-term business written in the UK also includes unit-linked products.

Prudential plc is a public limited company incorporated and registered in England and Wales. The registered office is:

Laurence Pountney Hill
London
EC4R 0HH
UK Companies House registered number: 1397169

A2: Basis of preparation

The consolidated financial statements consolidate the Group and the Group's interest in associates and jointly-controlled entities. The parent company financial statements present information about the Company as a separate entity and not about the Group.

The consolidated financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU) as required by EU law (IAS regulation EC 1606/2032).

The Group has applied all IFRS standards and interpretations adopted by the EU that are effective for financial years commencing on or before 1 January 2012. The Group has applied the same accounting policies in preparing the 2012 results as for 2011 except for the adoption of altered US GAAP reporting requirements for Group IFRS reporting, which is described in note A5.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

The consolidated financial statements do not represent Prudential's statutory accounts for the purposes of the UK Companies Act. These financial statements are based on the prescribed formats. The Groups external auditors have reported on the 2012, 2011 and 2010 statutory accounts. Statutory accounts for 2011 and 2010 have been delivered to the UK Registrar of Companies and those for 2012 will be delivered following the Company's Annual General Meeting. The auditors reports were (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not contain a statement under Section 498(2) or (3) of the UK Companies Act 2006.

A3: Accounting policies

1. Critical accounting policies

Prudential's discussion and analysis of its financial condition and results of operations are based upon Prudential's consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB and as endorsed by the EU. EU-endorsed IFRS may differ from IFRS as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. As at 31 December 2012, there were no unendorsed standards effective for the three years ended 31 December 2012 affecting the consolidated financial information of Prudential and there were no differences between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to Prudential. Accordingly, Prudential's financial information for the three years ended 31 December 2012 is prepared in accordance with IFRS as issued by the IASB. Prudential adopts mandatory requirements of new or altered EU-adopted IFRS standards when required, and may consider earlier adoption where permitted and appropriate in the circumstances.

The preparation of these financial statements requires Prudential to make estimates and judgements that affect the reported amounts of assets, liabilities, and revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, Prudential evaluates its estimates, including those related to long-term business provisioning and the fair value of assets.

Critical accounting policies are defined as those that are reflective of significant judgements and uncertainties, and potentially give rise to different results under different assumptions and conditions. Prudential believes that its critical accounting policies are limited to those described below.

The critical accounting policies in respect of the items discussed below are critical for those that relate to the Group's shareholder-financed business. In particular this applies for Jackson which is the largest shareholder-backed business in the Group. The policies are not critical in respect of the Group's with-profits business. This distinction reflects the basis of recognition of profit and accounting treatment of unallocated surplus of with-profits funds as a liability, as described elsewhere in these financial statements.

Insurance contract accounting

With the exception of certain contracts described in note D1, the contracts issued by the Group's life assurance business are classified as insurance contracts and investment contracts with discretionary participating features. As permitted by IFRS 4, assets and liabilities of these contracts are accounted for under previously applied GAAP. Accordingly, except as described below, the modified statutory basis

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

(MSB) of reporting as set out in the revised Statement of Recommended Practice (SORP) issued by the Association of British Insurers (ABI) in 2003 has been applied.

With-profits funds

With-profits funds are those in which the policyholder have a contractual right to receive at the discretion of the insurer, additional benefits based on factors such as the performance of a pool of assets held within the fund as a supplement to any guaranteed benefits.

UK regulated with-profits funds

For Group IFRS reporting, UK regulated with-profits funds are accounted for by the voluntary application of the UK accounting standard FRS 27, 'Life Assurance'. Under this standard, for such funds, policyholder liabilities are measured on a 'realistic basis' as discussed in section 2(a) of this note.

Unallocated surplus of with-profits funds:

Unallocated surplus represents the excess of assets over policyholder liabilities for the Group's with-profits funds that have yet to be appropriated between policyholders and shareholders. The Group has elected to account for unallocated surplus wholly as a liability with no allocation to equity. This treatment reflects the fact that shareholders' participation in the cost of bonuses arises only on distribution. The unallocated surplus is shown separately in the statement of financial position.

Overseas operations:

For Jackson, applying the MSB as applicable to overseas operations, which permits the application of local GAAP in some circumstances, the assets and liabilities of insurance contracts are accounted for under insurance accounting prescribed by US GAAP. For the assets and liabilities of insurance contracts of Asia operations, the local GAAP is applied with adjustments, where necessary, to comply with UK GAAP. For the operations in India, Japan, Taiwan and, until 2012, Vietnam, (as discussed in note A5) the local GAAP is not appropriate in the context of the previously applied MSB. For these countries the insurance assets and liabilities are measured principally by reference to US GAAP. For participating business the liabilities include provisions for the policyholders' interest in investment gains and other surpluses that have yet to be declared as bonuses.

The usage of these bases of accounting has varying effects on the way in which product options and guarantees are measured. For UK regulated with-profits funds, options and guarantees are valued on a market consistent basis. The basis is described in section 2(a) below. For other operations a market consistent basis is not applied under the accounting basis described in section 2(a) below. Details of the guarantees, basis of setting assumptions, and sensitivity to altered assumptions are described in notes D3 and D4.

Additional details on the Group's accounting policies for insurance assets and liabilities are shown in section 2 below.

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Valuation and accounting presentation of fair value movements of derivatives and debt securities of Jackson

These policies are critical because of their significance to the volatility of the income statement result and shareholders' equity. Under IAS 39, derivatives are required to be carried at fair value. Unless net investment hedge accounting is applied, value movements on derivatives are recognised in the income statement

For derivative instruments of Jackson, the Group has considered whether it is appropriate to undertake the necessary operational changes to qualify for hedge accounting so as to achieve matching of value movements in hedging instruments and hedged items in the performance statements. In reaching the decision a number of factors were particularly relevant. These were:

IAS 39 hedging criteria have been designed primarily in the context of hedging and hedging instruments that are assessable as financial instruments that are either stand-alone or separable from host contracts, rather than, for example, duration characteristics of insurance contracts;

the high hurdle levels under IAS 39 of ensuring hedge effectiveness at the level of individual hedge transactions;

the difficulties in applying the macro hedge provisions under IAS 39 (which are more suited to banking arrangements) to Jackson's derivative book;

the complexity of asset and liability matching of US life insurers such as those with Jackson's product range; and finally

whether it is possible or desirable, without an unacceptable level of costs and constraint on commercial activity, to achieve the accounting hedge effectiveness required under IAS 39.

Taking account of these considerations the Group has decided that, except for occasional circumstances, it is not appropriate to seek to achieve hedge accounting under IAS 39. As a result of this decision the total income statement results are more volatile as the movements in the value of Jackson's derivatives are reflected within it. This volatility is reflected in the level of short-term fluctuations in investment returns, as shown in note B1.

Under IAS 39, unless carried at amortised cost (subject to impairment provisions where appropriate) under the held-to-maturity category, debt securities are also carried at fair value. The Group has chosen not to classify any financial assets as held-to-maturity. Debt securities of Jackson are designated as available-for-sale with value movements, unless impaired, being recorded as movements within other comprehensive income. Impairments are recorded in the income statement.

Presentation of results before tax

The total tax charge for the Group reflects tax that in addition to relating to shareholders' profits is also attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. This is explained in more detail in note F5. Reported profit before the total tax charge is not representative of pre-tax profits attributable to shareholders. Accordingly, in order to provide a measure of pre-tax profits attributable to shareholders the Group has chosen to adopt an income statement

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presentation of the tax charge and pre-tax results that distinguishes between policyholder and shareholder components.

Segmental analysis of results and earnings attributable to shareholders

The Group uses operating profit based on longer-term investment returns as the segmental measure of its results. The basis of calculation is disclosed in section 2(d) below.

For shareholder-backed business, with the exception of debt securities held by Jackson and assets classified as loans and receivables of amortised cost, all financial investments and investment property are designated as assets at fair value through profit and loss. The short-term fluctuations affect the result for the year and the Group provides additional analysis of results before and after short-term fluctuations in investment returns, together with other items that are of a short-term volatile or one-off nature. Short-term fluctuations in investment returns on such assets held by with-profits funds, do not affect directly reported shareholder results. This is because (i) the unallocated surplus of with-profits funds is accounted for as a liability and (ii) excess or deficits of income and expenditure of the funds over the required surplus for distribution are transferred to or from unallocated surplus.

2. Other significant accounting policies

(a) Long-term business contracts

Income statement treatment

Insurance contracts and investment contracts with discretionary participation features (DPF)

Premium and annuity considerations for conventional with-profits policies and other protection type insurance policies are recognised as revenue when due. Premiums and annuity considerations for linked policies, unitised with-profits and other investment type policies are recognised as revenue when received or, in the case of unitised or unit-linked policies, when units are issued. These amounts exclude UK premium taxes and similar duties where Prudential collects and settles taxes borne by the customer.

Policy fees charged on linked and unitised with-profits policies for mortality, asset management and policy administration are recognised as revenue when related services are provided.

Claims paid include maturities, annuities, surrenders and deaths. Maturity claims are recorded as charges on the policy maturity date. Annuity claims are recorded when each annuity instalment becomes due for payment. Surrenders are charged to the income statement when paid and death claims are recorded when notified.

Acquisition costs are deferred and amortised as described in note A4.

Investment contracts other than those with DPF

For investment contracts which do not contain discretionary participating features, the accounting is carried out in accordance with IAS 39 to reflect the deposit nature of the arrangement, with premiums and claims reflected as deposits and withdrawals and taken directly to the statement of financial position as movements in the financial liability balance.

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Under IFRS, investment contracts (excluding those with discretionary participation features) accounted for as financial liabilities in accordance with IAS 39 which also offer investment management services, require the application of IAS 18 for the revenue attached to these services. Incremental, directly attributable acquisition costs relating to the investment management element of these contracts are capitalised and amortised in line with the related revenue. If the contracts involve up-front charges, this income is also deferred and amortised through the income statement in line with contractual service provision.

UK regulated with-profits funds

Prudential's long-term business written in the UK comprises predominantly life insurance policies with discretionary participating features under which the policyholders are entitled to participate in the returns of the funds supporting these policies. Business similar to this type is also written in certain of the Group's Asian operations subject to local market and regulatory conditions. Such policies are called with-profits policies. Prudential maintains with-profits funds within the Group's long-term business funds, which segregate the assets and liabilities and accumulate the returns related to that with-profits business. The amounts accumulated in these with-profits funds are available to provide for future policyholder benefit provisions and for bonuses to be distributed to with-profits policyholders. The bonuses, both annual and final, reflect the right of the with-profits policyholders to participate in the financial performance of the with-profits funds. Shareholders' profits with respect to bonuses declared on with-profits business correspond to the shareholders' share of the cost of bonuses as declared by the Board of directors. The shareholders' share currently represents one-ninth of the cost to the with-profits fund of bonuses declared for with-profits policies.

Annual bonuses are declared and credited each year to with-profits policies. The annual bonuses increase policy benefits and, once credited, become guaranteed. Annual bonuses are charged to the profit and loss account in the year declared. Final bonuses are declared each year and accrued for all policies scheduled to mature and for death benefits expected to be paid during the next financial year. Final bonuses are not guaranteed and are only paid on policies that result from claims through the death of the policyholder or maturity of the policy within the period of declaration or by concession on surrender. No policyholder benefit provisions are recorded for future annual or final bonus declarations.

The policyholders' liabilities of the regulated with-profits funds are accounted for under FRS 27, under which realistic basis liabilities are underpinned by the FSA's Peak 2 basis of reporting. This Peak 2 basis requires the value of liabilities to be calculated as:

a with-profits benefits reserve (WPBR); plus

future policy related liabilities (FPRL); plus

the realistic current liabilities of the fund.

The WPBR is primarily based on the retrospective calculation of accumulated asset shares but is adjusted to reflect future policyholder benefits and other outgoings. Asset shares broadly reflect the policyholders' share of the with-profits fund assets attributable to their policies.

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The FPRL must include a market consistent valuation of costs of guarantees, options and smoothing, less any related charges, and this amount is determined using either a stochastic approach, hedging costs or a series of deterministic projections with attributed probabilities.

The assumptions used in the stochastic models are calibrated to produce risk-free returns on each asset class. Volatilities of, and correlations between, investment returns from different asset classes are as determined by the Group's Portfolio Management Group on a market consistent basis.

The cost of guarantees, options and smoothing is very sensitive to the bonus, market value reduction (MVR) and investment policies the Group employs and therefore the stochastic modelling incorporates a range of management actions that would help to protect the fund in adverse scenarios. Substantial flexibility has been included in the modelled management actions in order to reflect the discretion that the Group retains in adverse investment conditions, thereby avoiding the creation of unreasonable minimum capital requirements. The management actions assumed are consistent with management's policy for with-profits funds and the disclosures made in the publicly available Principles and Practices of Financial Management.

The realistic basis liabilities representing the Peak 2 basis realistic liabilities for with-profits business included in the FSA regulatory returns include the element for the shareholders' share of the future bonuses. For accounting purposes under FRS 27, this latter item is reversed because, consistent with the current basis of financial reporting, shareholder transfers are recognised only on declaration.

Unallocated surplus

The unallocated surplus represents the excess of assets over policyholder liabilities for the Group's with-profits funds. As allowed under IFRS 4, the Group has opted to continue to record unallocated surplus of with-profits funds wholly as a liability. The annual excess (shortfall) of income over expenditure of the with-profits funds, after declaration and attribution of the cost of bonuses to policyholders and shareholders, is transferred to (from) the unallocated surplus each year through a charge (credit) to the income statement. The balance retained in the unallocated surplus represents cumulative income arising on the with-profits business that has not been allocated to policyholders or shareholders. The balance of the unallocated surplus is determined after full provision for deferred tax on unrealised appreciation on investments.

Other insurance contracts (ie contracts which contain significant insurance risk as defined under IFRS 4)

For these contracts 'grandfathered' UK GAAP has been applied, which reflects the MSB. Under this basis the following approach applies:

(i)

Other UK insurance contracts

Other UK insurance contracts that contain significant insurance risk include unit-linked, annuity and other non-profit business. For the purposes of local regulations, segregated accounts are established for linked business for which policyholder benefits are wholly or partly determined by reference to specific investments or to an investment-related index. The interest rates used in establishing policyholder benefit provisions for pension annuities in the course of payment are adjusted each year. Mortality rates

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used in establishing policyholder benefits are based on published mortality tables adjusted to reflect actual experience.

(ii)

Overseas subsidiaries

The assets and liabilities of insurance contracts of overseas subsidiaries are determined initially using local GAAP bases of accounting with subsequent adjustments where necessary to comply with the Group's accounting policies.

Jackson

The future policyholder benefit provisions for Jackson's conventional protection-type policies are determined under US GAAP principles with the locked in assumptions as to mortality, interest, policy lapses and expenses plus provisions for adverse deviations. For non-conventional protection-type policies, the policyholder benefit provision included within policyholder liabilities in the consolidated statement of financial position is the policyholder account balance. Acquisition costs are accounted for as explained in note A4.

Jackson accounts for the majority of its investment portfolio on an available-for-sale basis (see investment policies above) whereby unrealised gains and losses are recognised in other comprehensive income. As permitted by IFRS 4, Jackson has used shadow accounting. Under shadow accounting, to the extent that recognition of unrealised gains or losses on available-for-sale securities causes adjustments to the carrying value and amortisation patterns of deferred acquisition costs (DAC) and deferred income, these adjustments are recognised in other comprehensive income to be consistent with the treatment of the gains or losses on the securities. More precisely, shadow DAC adjustments reflect the change in DAC that would have arisen if the assets held in the statement of financial position had been sold, crystallising unrealised gains or losses, and the proceeds reinvested at the yields currently available in the market.

Asia operations

Except for the operations in India, Japan, Taiwan and until 2012 Vietnam, the future policyholder benefit provisions for Asian businesses are determined in accordance with methods prescribed by local GAAP adjusted to comply, where necessary, with UK GAAP. Refinements to the local reserving methodology are generally treated as change in estimates, dependent on the nature of the change.

For the Asia operations referred to above where local GAAP is not appropriate in the context of the previously applied MSB, accounting for insurance contracts is based on US GAAP. For these operations the business written is primarily non-participating linked and participating business. The future policyholder benefit provisions for non-linked business are determined using the net level premium method, with an allowance for surrenders, maintenance and claim expenses. Rates of interest used in establishing the policyholder benefit provisions vary by operation depending on the circumstances attaching to each block of business. Where appropriate, liabilities for participating business for these three operations include provisions for the policyholders' interest in investment gains and other surpluses that have yet to be declared as bonuses.

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Although the basis of valuation of Prudential's overseas operations is in accordance with the requirements of the Companies Act 2006 and ABI SORP, the valuation of policyholder benefit provisions for these businesses may differ from that determined on a UK MSB for UK operations with the same features. These differences are permitted under IFRS 4.

Liability adequacy

The Group performs liability adequacy testing on its insurance provisions to ensure that the carrying amounts of provisions (less related DAC) and, where relevant, present value of acquired in-force business is sufficient to cover current estimates of future cash flows. Any deficiency is immediately charged to the income statement.

Reinsurance

The measurement of reinsurance assets is consistent with the measurement of the underlying direct insurance contracts.

The treatment of any gains or losses arising on the purchase of reinsurance contracts is dependent on the underlying accounting basis of the entity concerned amongst other things.

Investment contracts (contracts which do not contain significant insurance risk as defined under IFRS 4)

For investment contracts with discretionary participation features, the accounting basis is consistent with the accounting for similar with-profits insurance contracts. Other investment contracts are accounted for on a basis that reflects the hybrid nature of the arrangements whereby part is accounted for as a financial instrument under IAS 39 and the investment management service component is accounted for under IAS 18 'Revenue'.

For those investment contracts in the US with fixed and guaranteed terms, the Group uses the amortised cost model to measure the liability.

Those investment contracts without fixed and guaranteed terms are designated at fair value through profit and loss because the resulting liabilities are managed and their performance is evaluated on a fair value basis. Where the contract includes a surrender option its carrying value is subject to a minimum carrying value equal to its surrender value.

(b) Financial instruments other than financial instruments classified as long-term business contracts

Investment classification

Under IAS 39, subject to specific criteria, financial instruments are required to be accounted for under one of the following categories: financial investments at fair value through profit and loss, financial investments held on an available-for-sale basis, financial investments held-to-maturity or loans and receivables. These IAS 39 classifications have been changed by IFRS 9 'Financial Investments: Classification and Measurement' which is not required to be adopted until 2015 and is still subject to EU endorsement In addition, the International Accounting Standards Board (IASB) continues to consult

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on future possible changes to IFRS 9. This standard has not been adopted by the Group in 2012. The Group holds financial investments on the following bases:

(i) Financial assets and liabilities at fair value through profit and loss this comprises assets and liabilities designated by management as fair value through profit and loss on inception and derivatives that are held for trading. These investments are measured at fair value with all changes thereon being recognised in investment return in the income statement;

(ii) Financial investments on an available-for-sale basis this comprises assets that are designated by management and/or do not fall into any of the other categories. Available-for-sale financial assets are initially recognised at fair value plus attributable transaction costs. For available-for-sale debt securities, the difference between their cost and par value is amortised to the income statement using the effective interest rate. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset.

Available-for-sale financial assets are subsequently measured at fair value. Interest income is recognised on an effective interest basis in the income statement. Except for foreign exchange gains and losses on debt securities, not in functional currency, which are included in the income statement, unrealised gains and losses are recognised in other comprehensive income. Upon disposal or impairment, accumulated unrealised gains and losses are transferred from other comprehensive income to the income statement as realised gains or losses; and

(iii) Loans and receivables Except for those designated as at fair value through profit and loss or available-for-sale, these instruments comprise non-quoted investments that have fixed or determinable payments. These investments include loans collateralised by mortgages, deposits, loans to policyholders and other unsecured loans and receivables. These investments are initially recognised at fair value plus transaction costs. Subsequently, these investments are carried at amortised cost using the effective interest method.

As permitted under IAS 39 the Group has designated certain financial assets as fair value through profit and loss as these assets are managed and their performance is evaluated on a fair value basis. These assets represent all of the Group's financial assets other than those loans and receivables, carried at amortised cost, and debt securities accounted for on an available-for-sale basis by Jackson. The use of the fair value option is consistent with the Group's risk management and investment strategies.

The Group uses the trade date method to account for regular purchases and sales of financial assets.

Use of fair values

The Group uses current bid prices to value its investments with quoted prices. Actively traded investments without quoted prices are valued using prices provided by third parties. If there is no active established market for an investment, the Group applies an appropriate valuation technique such as a discounted cash flow technique. Additional details are provided in note G1.

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Impairments

If, in subsequent periods, an impaired debt security held on an available-for-sale basis or an impaired loan or receivable recovers in value (in part or in full), and this recovery can be objectively related to an event occurring after the impairment, then the previously recognised impairment loss is reversed through the income statement (in part or in full).

Derivatives and hedge accounting

Derivative financial instruments are used to reduce or manage investment, interest rate and currency exposures, to facilitate efficient portfolio management and for investment purposes.

The Group may designate certain derivatives as hedges.

For hedges of net investments in foreign operations, the effective portion of any change in fair value of derivatives or other financial instruments designated as net investment hedges is recognised in other comprehensive income. The ineffective portion of changes in the fair value of the hedging instrument is recorded in the income statement. The gain or loss on the hedging instrument is recognised directly in other comprehensive income while the foreign operation is held.

For fair value hedges, movements in the fair value of the hedged item attributable to the hedged risk are recognised in the income statement.

The Group does not regularly seek to apply fair value or cash flow hedging treatment under IAS 39. The exceptions, where hedge accounting has been applied in 2012 and 2011, are summarised in note G3.

All derivatives that are not designated as hedging instruments are carried at fair value with movements in fair value being recorded in the income statement.

The primary areas of the Group's continuing operations where derivative instruments are held are the UK with-profits funds and annuity business, and Jackson.

For UK with-profits funds the derivative programme derivatives are used for the purposes of efficient portfolio management or reduction in investment risk.

For shareholder-backed UK annuity business the derivatives are held to contribute to the matching as far as practical, of asset returns and duration with those of liabilities to policyholders. The carrying value of these liabilities is sensitive to the return on the matching financial assets including derivatives held.

For Jackson an extensive derivative programme is maintained. Value movements on the derivatives held can be very significant in their effect on shareholder results. Further details on this aspect of the Group's financial reporting are described in note B1 and D3.

Embedded derivatives

Embedded derivatives are present in host contracts issued by various Group companies, in particular Jackson. They are embedded within other non-derivative host financial instruments and insurance contracts to create hybrid instruments. Embedded derivatives meeting the definition of an insurance

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contract are accounted for under IFRS 4. Where economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value with the changes in fair value recognised in the income statement, the embedded derivative is bifurcated and carried at fair value as a derivative in accordance with IAS 39.

In addition, the Group applies the option of IFRS 4 to not separate and fair value surrender options embedded in host contracts and with-profits investment contracts whose strike price is either a fixed amount or a fixed amount plus interest. Further details on the valuation basis for embedded derivatives attaching to Jackson's life assurance contracts are provided in note D3(e).

Securities lending including repurchase agreements

The Group is party to various securities lending agreements under which securities are loaned to third-parties on a short-term basis. The loaned securities are not derecognised; rather, they continue to be recognised within the appropriate investment classification. The Group's policy is that collateral in excess of 100 per cent of the fair value of securities loaned is required from all securities' borrowers and typically consists of cash, debt securities, equity securities or letters of credit.

In cases where the Group takes possession of the collateral under its securities lending programme, the collateral, and corresponding obligation to return such collateral, are recognised in the consolidated statement of financial position.

Derecognition of financial assets and liabilities

The Group's policy is to derecognise financial assets when it is deemed that substantially all the risks and rewards of ownership have been transferred.

The Group derecognises financial liabilities only when the obligation specified in the contract is discharged, cancelled or has expired.

Borrowings

Although initially recognised at fair value, net of transaction costs, borrowings, excluding liabilities of consolidated collateralised debt obligations, are subsequently accounted for on an amortised cost basis using the effective interest method. Under the effective interest method, the difference between the redemption value of the borrowing and the initial proceeds (net of related issue costs) is amortised through the income statement to the date of maturity or for hybrid debt, over the expected life of the instrument.

Financial liabilities designated at fair value through profit and loss

Consistent with the Group's risk management and investment strategy and the nature of the products concerned, the Group has designated under IAS 39 classification certain financial liabilities at fair value through profit and loss as these instruments are managed and their performance evaluated on a fair value basis. These instruments include liabilities related to consolidated collateralised debt obligations and net assets attributable to unit holders of consolidated unit trusts and similar funds.

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(c) Other assets, liabilities, income and expenditure

Basis of consolidation

The Group consolidates those entities it is deemed to control. The degree of control is determined by the ability of the Group to govern the financial and operating policies of an entity in order to obtain benefits. The results of subsidiaries are included in the financial statements from the date control commences to the date control ceases. All inter-company transactions are eliminated on consolidation. Results of asset management activities include those for managing internal funds.

The Group holds investments in internally and externally managed open-ended investment companies (OEICs) and unit trusts. These are consolidated where the Group's percentage ownership level is (i) 50 per cent or greater and(ii) where the Group's ownership of internally managed funds declines marginally below 50 per cent and, the decline in ownership is expected to be temporary.

Where the Group exercises significant influence or has the power to exercise significant influence over an entity, generally through ownership of 20 per cent or more of the entity's voting rights, but does not control the entity, then this is considered to be an investment in an associate. With the exception of those referred to below, the Group's investments in associates are recorded at the Group's share of the associates' net assets including any goodwill and intangibles arising upon initial acquisition. The carrying value of investments in associates is adjusted each year for the Group's share of the entities' profit or loss. This does not apply to investments in associates held by the Group's insurance or investment funds including the venture capital business or mutual funds and unit trusts, which as permitted by IAS 28, 'Investments in Associates', are carried at fair value through profit and loss.

The Group's investments in joint ventures are recognised using proportional consolidation whereby the Group's share of an entity's individual balances are combined line-by-line with similar items into the Group financial statements. Other interests in entities, where significant influence is not exercised, are carried as investments at fair value through profit and loss.

Investment properties

Investments in leasehold and freehold properties not for occupation by the Group, including properties under development for future use as investment properties, are carried at fair value, with changes in fair value included in the income statement. Properties are valued annually either by the Group's qualified surveyors or by taking into consideration the advice of professional external valuers using the Royal Institution of Chartered Surveyors guidelines. Each property is externally valued at least once every three years. Fair value is based on active market prices. If this information is not available, the Group uses alternative valuation methods such as discounted cash flow projections or recent prices in less active markets.

Leases of investment property where the Group has substantially all the risks and rewards of ownership are classified as finance leases (leasehold property). Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased property and the present value of the minimum lease payments.

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Pension schemes

For the Group's defined benefit schemes, if the present value of the defined benefit obligation exceeds the fair value of the scheme assets, then a liability is recorded in the Group's statement of financial position. By contrast, if the fair value of the assets exceeds the present value of the defined benefit obligation then the surplus will only be recognised if the nature of the arrangements under the trust deed, and funding arrangements between the Trustee and the Company support the availability of refunds or recoverability through agreed reductions in future contributions. In addition, if there is a constructive obligation for the Company to pay deficit funding, this is also recognised such that the financial position recorded for the scheme reflects the higher of any underlying IAS 19 deficit and the obligation for deficit funding.

The Group utilises the projected unit credit method to calculate the defined benefit obligation. This method sees each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. Estimated future cash flows are then discounted at a high-quality corporate bond rate, adjusted to allow for the difference in duration between the bond index and the pension liabilities where appropriate, to determine its present value. These calculations are performed by independent actuaries.

The plan assets of the Group's pension schemes exclude several insurance contracts that have been issued by the Group.

These assets are excluded from plan assets in determining the pension obligation recognised in the consolidated statement of financial position.

The aggregate of the actuarially determined service costs of the currently employed personnel and the unwind of discount on liabilities at the start of the period, less the expected investment return on scheme assets at the start of the period, is charged to the income statement. Actuarial gains and losses as a result of changes in assumptions or experience variances are also charged or credited to the income statement.

Contributions to the Group's defined contribution schemes are expensed when due.

Share-based payments

The Group offers share award and option plans for certain key employees and a Save As You Earn plan for all UK and certain overseas employees. Shares held in trust relating to these plans are conditionally gifted to employees.

The compensation expense charged to the income statement is primarily based upon the fair value of the options granted, the vesting period and the vesting conditions. The Company has established trusts to facilitate the delivery of Prudential plc shares under employee incentive plans and savings-related share option schemes. The cost to the Company of acquiring these treasury shares held in trusts is shown as a deduction from shareholders' equity.

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Tax

Current tax expense is charged or credited to operations based upon amounts estimated to be payable or recoverable as a result of taxable operations for the current year. To the extent that losses of an individual UK company are not offset in any one year, they can be carried back for one year or carried forward indefinitely to be offset against profits arising from the same company.

Deferred taxes are provided under the liability method for all relevant temporary differences. IAS 12, 'Income Taxes' does not require all temporary differences to be provided for, in particular, the Group does not provide for deferred tax on undistributed earnings of subsidiaries where the Group is able to control the timing of the distribution and the temporary difference created is not expected to reverse in the foreseeable future. Deferred tax assets are only recognised when it is more likely than not, that future taxable profits will be available against which these losses can be utilised.

The tax charge for long-term business includes tax expense attributable to both the policyholders and the shareholders. Different tax rules apply under UK law depending upon whether the business is life insurance or pension business.

Deferred tax is measured at the tax rates that are expected to apply to the period when the asset is realised or the liability settled, based on tax rates (and laws) that have been enacted or are substantively enacted at the end of the reporting period.

Business acquisitions and disposals

Business acquisitions are accounted for by applying the purchase method of accounting, which adjusts the net assets of the acquired company to fair value at the date of purchase. The excess of the acquisition consideration over the fair value of the assets and liabilities of the acquired entity is recorded as goodwill. Expenses related to acquiring new subsidiaries are expensed in the period in which they are incurred. Income and expenses of acquired entities are included in the income statement from the date of acquisition.

Goodwill

Goodwill arising on acquisitions of subsidiaries and businesses is capitalised and carried on the Group statement of financial position as an intangible asset at initial value less any accumulated impairment losses. Goodwill impairment testing is conducted annually and when there is an indication of impairment. For the purposes of impairment testing, goodwill is allocated to cash generating units.

Intangible assets

Intangible assets acquired on the purchase of a subsidiary or portfolio of contracts are fair valued at acquisition. Other intangible assets, such as software, are valued at the price paid to acquire them. Intangible assets are carried at cost less amortisation and any accumulated impairment losses. Amortisation calculated is charged on a straight-line basis over the estimated useful life of the assets.

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Cash and cash equivalents

Cash and cash equivalents consist of cash at bank and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days maturity from the date of acquisition.

Segments

Under IFRS 8, 'Operating Segments', the Group determines and presents operating segments based on the information that is internally provided to the Group Executive Committee which is the Group's chief operating decision maker.

The operating segments identified by the Group reflect the Group's organisational structure, which is by both geography (Asia, US and UK) and by product line (insurance operations and asset management).

Insurance operations principally comprise of products that contain both significant and insignificant elements of insurance risk. The products are managed together and there is no distinction between these two categories other than for accounting purposes. This segment also includes the commission earned on general insurance business and investment subsidiaries held to support the Group's insurance operations.

Asset management comprises both internal and third-party asset management services, inclusive of portfolio and mutual fund management, where the Group acts as an adviser, and broker-dealer activities. The nature of the products and the managing of the business differ from the risks inherent in the insurance operations segments, and the regulatory environment of the asset management industry differs from that of the insurance operations segments.

The Group's operating segments determined in accordance with IFRS 8, 'Operating Segments', are as follows:

Insurance operations

- Asia
- US (Jackson)
- UK

Asset management operations

- M&G (including Prudential Capital)
- Eastspring Investments

US broker-dealer and asset management (including Curian)

The Group's operating segments are also its reportable segments with the exception of Prudential Capital (PruCap) which has been incorporated into the M&G operating segment for the purposes of segment reporting.

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The performance measure of operating segments utilised by the Company is IFRS operating profit attributable to shareholders based on longer-term investment returns, as described below. This measure excludes the recurrent items of short-term fluctuations in investment returns and the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes. In addition for 2012 this measure excluded a gain arising upon the dilution of the Group's holding in PPM South Africa and the amortisation of the acquisition accounting adjustments arising on the purchase of REALIC as described further in note I1. Further for 2010, this measure excluded costs associated with the terminated AIA transaction and gain arising upon the dilution of the Group's holding in PruHealth. Operating earnings per share is based on operating profit based on longer-term investment returns, after tax and non-controlling interests. Further details on the determination of the performance measure of operating profit based on longer-term investment returns is provided in note below.

Segment results that are reported to the Group Executive Committee include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items are mainly in relation to the Group Head Office and the Asia Regional Head Office.

(d) Operating profit based on longer-term investment returns

The Group provides supplementary analysis of profit before tax attributable to shareholders that distinguishes operating profit based on longer-term investment returns from other constituent elements of the total profit.

Except in the case of the assets backing the UK annuity business, unit-linked and US variable annuity separate account liabilities, operating profit based on longer-term investment returns for shareholder-financed business is determined on the basis of expected longer-term investment returns. In the case of assets backing the UK annuity business, unit-linked and US variable annuity separate account liabilities, the basis of determining operating profit based on longer-term investment returns is as follows:

Assets backing UK annuity business liabilities. For UK annuity business, policyholder liabilities are determined by reference to current interest rates. The value movements of the assets covering liabilities are closely correlated with the related change in liabilities. Accordingly, asset value movements are recorded within the 'operating results based on longer-term investment returns'. Policyholder liabilities include a margin for credit risk. Variations between actual and best estimate expected impairments are recorded as a component of short-term fluctuations in investment returns.

Assets backing unit-linked and US variable annuity business separate account liabilities. For such business, the policyholder unit liabilities are directly reflective of the asset value movements. Accordingly, the operating results based on longer-term investment returns reflect the current period value movements in unit liabilities and the backing assets.

In the case of other shareholder-financed business, the measurement of operating profit based on longer-term investment returns reflects the particular features of long-term insurance business where assets and liabilities are held for the long-term and for which the accounting basis for insurance liabilities under current IFRS is not generally conducive to demonstrating trends in underlying performance of life businesses exclusive of the effects of short-term fluctuations in market conditions. In

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determining the profit on this basis, the following key elements are applied to the results of the Group's shareholder-financed operations as reflected in the segment results shown in note B1.

(i) Debt, equity-type securities and loans

Longer-term investment returns for both debt, equity-type securities and loans comprise longer-term actual income receivable for the period (interest/dividend income) and longer-term capital returns.

In principle, for debt securities and loans, the longer-term capital returns comprise two elements. The first element is a risk margin reserve (RMR) based charge for the expected level of defaults for the period, which is determined by reference to the credit quality of the portfolio. The difference between impairment losses in the reporting period and the RMR charge to the operating result is reflected in short-term fluctuations in investment returns. The second element is for the amortisation of interest-related realised gains and losses to operating results based on longer-term investment returns to the date when sold bonds would have otherwise matured.

Jackson is the shareholder-backed operation for which the distinction between impairment losses and interest-related realised gains and losses is in practice relevant to a significant extent. Jackson has used the ratings by Nationally Recognised Statistical Ratings Organisations (NRSRO) or ratings resulting from the regulatory ratings detail issued by the National Association of Insurance Commissioners (NAIC) developed by external third parties such as PIMCO or BlackRock Solutions to determine the average annual RMR to apply to debt securities held to back general account business. Debt securities held to back separate account and reinsurance funds withheld are not subject to RMR charge. Further details of the RMR charge, as well as the amortisation of interest-related realised gains and losses, for Jackson are shown in note B1(iv).

For debt securities backing non-linked shareholder-financed business of the UK insurance operations (other than the annuity business) and of the Asia insurance operations, the realised gains and losses are principally interest related. Accordingly, all realised gains and losses to date for these operations are being amortised over the period to the date those securities would otherwise have matured, with no explicit RMR charge.

At 31 December 2012, the level of unamortised interest-related realised gains and losses related to previously sold bonds for the Group was a net gain of £498 million (31 December 2011: net gain of £462 million; 31 December 2010: net gain of £373 million).

For equity-type securities, the longer-term rates of return are estimates of the long-term trend investment return for income and capital having regard to past performance, current trends and future expectations. Equity-type securities held for shareholder-financed operations other than the UK annuity business, unit-linked and US variable annuity are of significance for the US and Asia insurance operations. Different rates apply to different categories of equity-type securities.

As at 31 December 2012, the equity-type securities for US insurance non-separate account operations amounted to £1,004 million (31 December 2011: £902 million; 2010: £852 million). For these

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operations, the longer-term rates of return for income and capital applied in 2012, 2011 and 2010, reflects the combination of risk free rates and appropriate risk premiums are as follows:

	2012	2011	2010
Equity-type securities such as common and preferred stock and portfolio holdings in mutual funds	**5.5% to 6.2%**	5.9% to 7.5%	6.5% to 7.9%
Other equity-type securities such as investments in limited partnerships and private equity funds	**7.5% to 8.2%**	7.9% to 9.5%	8.5% to 9.9%

For Asia insurance operations, investments in equity securities held for non-linked shareholder-financed operations amounted to £659 million as at 31 December 2012 (31 December 2011: £590 million; 31 December 2010: £506 million). The rates of return applied in the years 2012 , 2011 and 2010 ranged from 1.0 per cent to 13.8 per cent with the rates applied varying by territory. The investment amounts for 2011 and 2010 of £590 million and £506 million, respectively included the Group's investment in China Life Insurance Company of Taiwan (China Life (Taiwan)) of £88 million and £101 million, respectively which was sold in 2012, as described in note B1.

The longer-term rates of return discussed above for equity-type securities are determined after consideration by the Group's in-house economists of long-term expected real government bond returns, equity risk premium and long-term inflation. These rates are broadly stable from period to period but may be different between countries reflecting, for example, differing expectations of inflation in each territory. The assumptions are for returns expected to apply in equilibrium conditions. The assumed rates of return do not reflect any cyclical variability in economic performance and are not set by reference to prevailing asset valuations.

(ii)

US variable and fixed index annuity business

The following value movements for Jackson's variable and fixed index annuity business are excluded from operating profit based on longer-term investment returns:

Fair value movements for equity-based derivatives;

Fair value movements for embedded derivatives for Guaranteed Minimum Withdrawal Benefit (GMWB) 'not for life' and fixed index annuity business, and Guaranteed Minimum Income Benefit (GMIB) reinsurance (see note);

Movements in accounts carrying value of Guaranteed Minimum Death Benefit (GMDB) and GMWB 'for life' liabilities, for which, under the 'grandfathered' US GAAP applied under IFRS for Jackson's insurance assets and liabilities, the measurement basis gives rise to a muted impact of current period market movements;

Fee assessments and claim payments, in respect of guarantee liabilities; and

Related changes to amortisation of deferred acquisition costs for each of the above items.

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Note: US operations Embedded derivatives for variable annuity guarantee features

The GMIB liability, which is fully reinsured, subject to a deductible and annual claim limits, is accounted for in accordance with FASB ASC Subtopic 944-80 Financial Services Insurance Separate Accounts (formerly SOP 03-1) under IFRS using 'grandfathered' US GAAP. As the corresponding reinsurance asset is net settled, it is considered to be a derivative under IAS 39, 'Financial Instruments: Recognition and Measurement', and the asset is therefore recognised at fair value. As the GMIB benefit is economically reinsured the mark to market element of the reinsurance asset is included as a component of short-term fluctuations in investment returns.

(iii)

Other derivative value movements

Generally, derivative value movements are excluded from operating results based on longer-term investment returns (unless those derivative value movements broadly offset changes in the accounting value of other assets and liabilities included in operating profit). The principal example of non-equity based derivatives (for example interest rate swaps and swaptions) whose value movements are excluded from operating profit arises in Jackson. Non-equity based derivatives are primarily held by Jackson as part of a broadly-based hedging programme for features of Jackson's bond portfolio (for which value movements are booked in the statement of comprehensive income rather than the income statement), product liabilities (for which US GAAP accounting as 'grandfathered' under IFRS 4 does not fully reflect the economic features being hedged), and the interest rate exposure attaching to equity-based embedded derivatives.

(iv)

Other liabilities to policyholders and embedded derivatives for product guarantees

Under IFRS, the degree to which the carrying values of liabilities to policyholders are sensitive to current market conditions varies between territories depending upon the nature of the 'grandfathered' measurement basis. In general, in those instances where the liabilities are particularly sensitive to routine changes in market conditions, the accounting basis is such that the impact of market movements on the assets and liabilities is broadly equivalent in the income statement, and operating profit based on longer-term investments returns is not distorted. In these circumstances, there is no need for the movement in the liability to be bifurcated between the elements that relate to longer-term market conditions and short-term effects.

However, some types of business movements in liabilities do require bifurcation to ensure that at the net level (ie after allocated investment return and change for policyholder benefits) the operating result reflects longer-term market returns.

Examples where such bifurcation is necessary are:

Asia

(i)

Hong Kong

For certain non-participating business, the economic features are more akin to asset management products with policyholder liabilities reflecting asset shares over the contract term. For these products, the charge for policyholder benefits in the operating results should reflect the asset share feature rather

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than volatile movements that would otherwise be reflected if the local regulatory basis (which is applied for IFRS balance sheet purposes) was used.

For other Hong Kong non-participating business, longer term interest rates are used to determine the movement in policyholder liabilities for determining operating results. Similar principles apply for other Asia operations;

(ii)

Japan Guaranteed Minimum Death Benefit (GMDB) product features

For unhedged GMDB liabilities accounted for under IFRS using 'grandfathered' US GAAP, such as in the Japanese business, the change in carrying value is determined under FASB ASC subtopic 944-80, Financial Services Insurance Separate Accounts (formerly SOP 03-1), which partially reflects changes in market conditions. Under the company's segmental basis of reporting the operating profit reflects the change in liability based on longer-term market conditions with the difference between the charge to the operating result and the movement reflected in the total result included in short-term fluctuations in investment returns.

UK shareholder-backed annuity business

The operating result based on longer-term investment returns reflects the impact of value movements on policyholder liabilities for annuity business in PRIL and the PAC non-profit sub-fund after adjustments to allocate the following elements of the movement to the category of 'short-term fluctuations in investment returns' in the Group's supplementary analysis of profit:

The impact on credit risk provisioning of actual upgrades and downgrades during the period;

Credit experience compared to assumptions

Short-term value movements on assets backing the capital of the business.

Credit experience reflects the impact of defaults and other similar experience, such as asset exchanges arising from debt restructuring by issuers that include effectively an element of permanent impairment of the security held. Negative experience compared to assumptions is included within short-term fluctuations in investment returns without further adjustment. This is to be contrasted with positive experience where surpluses are retained in short-term allowances for credit risk for IFRS reporting purposes. The effects of other changes to credit risk provisioning are included in the operating result, as is the net effect of changes to the valuation rate of interest due to portfolio rebalancing to align more closely with management's benchmark.

(v)

Fund management and other non-insurance businesses

For these businesses, the particular features applicable for life assurance noted above do not apply. For these businesses it is inappropriate to include returns in the operating result on the basis described above. Instead, it is appropriate to generally include realised gains and losses (including impairments) in the operating result with unrealised gains and losses being included in short-term fluctuations. For this purpose impairments are calculated as the credit loss determined by comparing the projected cash flows discounted at the original effective interest rate to the carrying value. In some instances it may also be appropriate to amortise realised gains and losses on derivatives and other financial instruments to

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operating results over a time period that reflects the underlying economic substance of the arrangements.

Shareholders' dividends

Interim dividends are recorded in the period in which they are paid. Final dividends are recorded in the period in which they are approved by shareholders.

Share capital

Where there is no obligation to transfer assets, shares are classified as equity. The difference between the proceeds received on issue of the shares, net of share issue costs, and the nominal value of the shares issued, is credited to share premium. Where the Company purchases shares for the purposes of employee incentive plans, the consideration paid, net of issue costs, is deducted from retained earnings. Upon issue or sale any consideration received is credited to retained earnings net of related costs.

Foreign exchange

The Group's consolidated financial statements are presented in pounds sterling, the Group's presentation currency. Accordingly, the results and financial position of foreign subsidiaries must be translated into the presentation currency of the Group from their functional currencies, ie the currency of the primary economic environment in which the entity operates. All assets and liabilities of foreign subsidiaries are converted at year end exchange rates whilst all income and expenses are converted at average exchange rates where this is a reasonable approximation of the rates prevailing on transaction dates. The impact of these currency translations is recorded as a separate component in the statement of comprehensive income.

Foreign currency borrowings that are used to provide a hedge against Group equity investments in overseas subsidiaries are translated at year end exchange rates and movements recognised in other comprehensive income. Other foreign currency monetary items are translated at year end exchange rates with changes recognised in the income statement.

Foreign currency transactions are translated at the spot rate prevailing at the time.

A4: Critical accounting estimates and judgements

In determining the measurement of the Group's assets and liabilities estimates and judgements are required. The critical aspects are described below.

Investments

Determining the fair value of financial investments when the markets are not active

The Group holds certain financial investments for which the markets are not active. These can include financial investments which are not quoted on active markets and financial investments for which markets are no longer active as a result of market conditions e.g. market illiquidity. When the markets are not active, there is generally no or limited observable market data to account for financial

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investments at fair value. The determination of whether an active market exists for a financial investment requires management's judgement.

If the market for a financial investment of the Group is not active, the fair value is determined by using valuation techniques. The Group establishes fair value for these financial investments by using quotations from independent third-parties, such as brokers or pricing services or by using internally developed pricing models. Priority is given to publicly available prices from independent sources when available, but overall the source of pricing and/or the valuation technique is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The valuation techniques include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation and may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these financial investments.

The financial investments measured at fair value are classified into the following three level hierarchy on the basis of the lowest level of inputs that is significant to the fair value measurement of the financial investment concerned:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities

Level 2: Inputs other than quoted prices included within level 1 that are observable either directly or indirectly (i.e. derived from prices).

Level 3: Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At 31 December 2012, £6,660 million (2011: £4,565 million) of the financial investments (net of derivative liabilities) valued at fair value were classified as level 3. Of these £861 million (2011: £800 million) are held to back shareholder non-linked business and so changes to these valuations will directly impact shareholders' equity. Further details of the level 3 investments and the classification of financial instruments are given in note G1.

Determining impairments relating to financial assets

(i)

Available-for-sale securities

The majority of Jackson's debt securities portfolio are accounted for on available-for-sale basis. The consideration of evidence of impairment requires management's judgement. In making this determination the factors considered include, for example:

Whether the decline of the financial investment's fair value is substantial; A substantial decline in fair value might be indicative of a credit loss event that would lead to a measurable decrease in the estimated future cash flows;

The impact of the duration of the security on the calculation of the revised estimated cash flows;

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The duration of a security to maturity helps to inform whether assessments of estimated future cash flows that are higher than market value are reasonable;

The duration and extent to which the amortised cost exceeds fair value; This factor provides an indication of how the contractual cash flows and effective interest rate of a financial asset compares with the implicit market estimate of cash flows and the risk attaching to a 'fair value' measurement. The length of time for which that level of difference has been in place may also provide further evidence as to whether the market assessment implies an impairment loss has arisen; and

The financial condition and prospects of the issuer or other observable conditions that indicate the investment may be impaired.

If a loss event that will have a detrimental effect on cash flows is identified an impairment loss in the income statement is recognised. The loss recognised is determined as the difference between the book cost and the fair value of the relevant impaired securities. This loss comprises the effect of the expected loss of contractual cash flows and any additional market-price-driven temporary reductions in values.

For Jackson's residential mortgage-backed and other asset-backed securities, all of which are classified as available-for-sale, the model used to analyse cash flows, begins with the current delinquency experience of the underlying collateral pool for the structure, by applying assumptions about how much of the currently delinquent loans will eventually default, and multiplying this by an assumed loss severity. Additional factors are applied to anticipate ageing effects. After applying a cash flow simulation an indication is obtained as to whether or not the security has suffered, or is anticipated to suffer, contractual principal or interest payment shortfalls. If a shortfall applies an impairment charge is recorded. The difference between the fair value and book cost for unimpaired securities designated as available-for-sale, is accounted for as unrealised gains or losses, with the movements in the accounting period being included in other comprehensive income.

The Group's review of fair value involves several criteria, including economic conditions, credit loss experience, other issuer-specific developments and future cash flows. These assessments are based on the best available information at the time. Factors such as market liquidity, the widening of bid/ask spreads and a change in cash flow assumptions can contribute to future price volatility. If actual experience differs negatively from the assumptions and other considerations used in the consolidated financial statements, unrealised losses currently in equity may be recognised in the income statement in future periods. Additional details on the impairments of the available-for-sale securities of Jackson are described in notes D3 and G5 .

(ii)

Assets held at amortised cost

Except for certain loans of the UK insurance operations and Jackson National Life, which are accounted for on a fair value through profit and loss basis, and as described below, financial assets classified as loans and receivables under IAS 39 are, except as described below, carried at amortised cost using the effective interest rate method. The loans and receivables include loans collateralised by mortgages, deposits and loans to policyholders. In estimating future cash flows, the Group looks at the expected cash flows of the assets and applies historical loss experience of assets with similar credit risks

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that has been adjusted for conditions in the historical loss experience which no longer exist or for conditions that are expected to arise. The estimated future cash flows are discounted using the financial asset's original or variable effective interest rate and exclude credit losses that have not yet been incurred.

The risks inherent in reviewing the impairment of any investment include: the risk that market results may differ from expectations, facts and circumstances may change in the future and differ from estimates and assumptions, or the Group may later decide to sell the asset as a result of changed circumstances.

Certain mortgage loans of the UK insurance operations and, consequent upon the purchase of REALIC in 2012, policy loans held to back funds withheld under reinsurance arrangements have been designated at fair value through profit and loss as these loan portfolios are managed and evaluated on a fair value basis.

Insurance contracts

Product classification

IFRS 4 requires contracts written by insurers to be classified as either 'insurance contracts' or 'investment contracts' depending on the level of insurance risk transferred. Insurance risk is a pre-existing risk, other than financial risk, transferred from the contract holder to the contract issuer. If significant insurance risk is transferred by the contract then it is classified as an insurance contract. Contracts that transfer financial risk but not significant insurance risk are termed investment contracts. Furthermore, some contracts, both insurance and investment, contain discretionary participating features representing the contractual right to receive additional benefits as a supplement to guaranteed benefits:

(a) that are likely to be a significant portion of the total contract benefits,

(b) whose amount or timing is contractually at the discretion of the insurer, and

(c) that are contractually based on asset or fund performance, as discussed in IFRS 4.

IFRS 4 permits the continued usage of previously applied GAAP for insurance contracts and investment contracts with discretionary participating features. Except for UK regulated with-profits funds, as described subsequently in section A3(2)(a), this basis has been applied by the Group.

For investment contracts that do not contain discretionary participating features, IAS 39 and, where the contract includes an investment management element, IAS 18,'Revenue', apply measurement principles to assets and liabilities attaching to the contract.

Valuation assumptions

(i) Contracts of with-profits funds

For UK regulated with-profits funds, the contract liabilities are valued by reference to the UK Financial Services Authority's (FSA) realistic basis as described in section A3(2)(a). This basis has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and

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current circumstances. An explanation of the basis of liability measurement is contained in section A3(2)(a).

The Group's other with-profits contracts are written in with-profits funds that operate in some of the Group's Asia subsidiaries. The liabilities for these contracts and those of Prudential Annuities Limited, which is a subsidiary company of the PAC with-profits fund, are determined differently. For these contracts the liabilities are estimated using actuarial methods based on assumptions relating to premiums, interest rates, investment returns, expenses, mortality and surrenders. The assumptions to which the estimation of these reserves is particularly sensitive are the interest rate used to discount the provision and the assumed future mortality experience of policyholders.

(ii) Other contracts

Contracts, other than those of with-profits funds, are written by shareholder-backed operations of the Group. The significant shareholder-backed product groupings and the factors that may significantly affect IFRS results due to experience against assumptions or changes of assumptions vary significantly between business units. For some types of business the effect of changes in assumptions may be significant, whilst for others, due to the nature of the product, assumption setting may be of less significance. The nature of the products and the significance of assumptions are discussed in notes D2, D3 and D4.

UK insurance operations

From the perspective of shareholder results the key sensitivity for UK insurance operations are the assumptions for allowance for credit risk and mortality for UK annuity business.

Jackson

With the exception of institutional products and an incidental amount of business for annuity certain contracts, which are accounted for as investment contracts under IAS 39, all of Jackson's contracts are accounted for under IFRS 4 as insurance contracts by applying US GAAP, the previous GAAP used before IFRS adoption. The accounting requirements under these standards and the effect of changes in valuation assumptions are considered below for fixed annuity, variable annuity and traditional life insurance contracts.

Fixed annuity contracts, which are investment contracts under US GAAP terminology, are accounted for by applying in the first instance a retrospective deposit method to determine the liability for policyholder benefits. This is then augmented by potentially three additional amounts, namely deferred income, any amounts previously assessed against policyholders that are refundable on termination of the contract, and any premium deficiency, ie any probable future loss on the contract. These types of contracts contain considerable interest rate guarantee features. Notwithstanding the accompanying market risk exposure, except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of Jackson's fixed annuity products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement.

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Variable annuity contracts written by Jackson may provide for guaranteed minimum death, income, or withdrawal benefit features. In general terms, liabilities for these benefits are accounted for under US GAAP by using estimates of future benefits and fees under best estimate assumptions.

For traditional life insurance contracts, provisions for future policy benefits are determined using assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviation.

Except to the extent of mortality experience, which primarily affects profits through variations in claim payments and the guaranteed minimum death benefit reserves, the profits of Jackson are relatively insensitive to changes in insurance risk. This reflects the principally spread and fee-based nature of Jackson's business.

Asia operations

The insurance products written in the Group's Asia operations principally cover with-profits business, unit-linked business, and other non-participating business. The results of with-profits business are relatively insensitive to changes in estimates and assumptions that affect the measurement of policyholder liabilities. As for the UK business, this feature arises because unallocated surplus is accounted for by the Group as a liability. The results of Asia unit-linked business are also relatively insensitive to changes in estimates or assumptions due to the matching of asset value and liability movements. For other Asia non-participating business the degree of sensitivity of results to changes in interest rates depends upon the degree to which the liabilities under the 'grandfathered' IFRS 4 measurement basis reflects market interest rates from period to period for example, for those countries, such as those applying US GAAP, the results can be more sensitive as the effect of interest rate movements on the backing investments may not be offset by liability movements due to the US GAAP basis of measurement of insurance contracts.

Deferred acquisition costs for insurance contracts

Except for acquisition costs of with-profits contracts of the UK regulated with-profits funds, which are accounted for under the realistic FSA regime, costs of acquiring new insurance business are accounted for in a way that is consistent with the principles of the ABI SORP with deferral and amortisation against margins in future revenues on the related insurance policies. Costs of acquiring new insurance business, principally commissions, marketing and advertising and certain other costs associated with policy insurance and underwriting that are not reimbursed by policy charges, are specifically identified and capitalised as part of deferred acquisition costs (DAC). In general, this deferral is presentationally shown by an explicit carrying value for DAC in the balance sheet. However, in some Asia operations the deferral is implicit through the reserving methodology. The recoverability of the explicitly and implicitly deferred acquisition costs is measured and are deemed impaired if the projected margins are less than the carrying value. To the extent that the future margins differ from those anticipated, then an adjustment to the carrying value will be necessary.

For UK regulated with-profits funds where the realistic FSA regime is applied, the basis of setting liabilities is such that it would be inappropriate for acquisition costs to be deferred, therefore these costs

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are expensed as incurred. The majority of the UK shareholder-backed business is individual and group annuity business where the incidence of acquisition costs is negligible.

The deferral and amortisation of acquisition costs is of most relevance to the Group's results for Jackson and Asia operations. The DAC for Jackson and some Asia operations is determined with reference to US GAAP principles.

Jackson

Under IFRS 4, the Group applies grandfathered US GAAP for measuring the insurance assets and liabilities of Jackson. In the case of Jackson term business, acquisition costs are deferred and amortised in line with expected profits. For interest-sensitive business, the key assumption is the long-term spread between the earned rate on investments and the rate credited to policyholders, which is based on an annual spread analysis. In addition, expected gross profits depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges), all of which are based on a combination of Jackson's actual industry experience and future expectations. A detailed analysis of actual mortality, lapse and expenses experience is performed using internally developed experience studies.

For US variable annuity business the key assumption is the investment return from the separate accounts, which for all years included was 8.4 per cent per annum (after deduction of external fund management fees) determined using a mean reversion methodology. Under the mean reversion methodology, projected returns over the next five years are flexed (subject to capping) so that, combined with the actual rates of return for the current and the previous two years the 8.4 per cent rate is maintained. The projected rates of return are capped at no more than 15 per cent for each of the next five years Further details are explained in note D3(e).These returns affect the level of future expected profits through their effects on the fee income with consequential impact on the amortisation of DAC.

The level of acquisition costs carried in the statement of financial position is also sensitive to unrealised valuation movements on debt securities held to back the liabilities and solvency capital. Further details are explained in notes D3(e) and H1.

As explained in note A5, the Group has adopted the US Financial Accounting Standards Board measurement and recognition requirements in Accounting Standards Update No 2010-26 on 'Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts' from 1 January 2012 into its IFRS reporting for the results of Jackson and those Asia operations whose IFRS insurance assets and liabilities are measured principally by reference to US GAAP principles. Under the Update insurers are required to capitalise only those incremental costs directly relating to acquiring a contract from 1 January 2012. For Group IFRS reporting Prudential has chosen to apply this new basis retrospectively for the results of these operations.

On adoption of the new DAC policy for Jackson the deferred costs balance for business in force at 31 December 2011 was retrospectively reduced from £3,880 million to £3,095 million (31 December 2010: DAC balance reduced from £3,543 million to £2,829 million).

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A: Background and accounting policies (Continued)

Asia operations

For those territories applying US GAAP to insurance assets and liabilities, as permitted by the ABI SORP, principles similar to those set out in the Jackson paragraph above are applied to the deferral and amortisation of acquisition costs. For other territories in Asia, the general principles of the ABI SORP are applied with, as described above, deferral of acquisition costs being either explicit or implicit through the reserving basis.

A5: New accounting pronouncements

The following standards, interpretations and amendments have either been adopted for the first time in 2012 or have been issued but are not yet effective in 2012, including those which have not yet been adopted in the EU. This is not intended to be a complete list as only those standards, interpretations and amendments that could have an impact upon the Group's financial statements have been discussed.

(a) Accounting pronouncements adopted in 2012

Amendments to IFRS 7, 'Financial instruments: Disclosures Transfers of financial assets'

The amendments introduce new disclosure requirements about transfers of financial assets which include disclosures for financial assets that are not derecognised in their entirety and financial assets that are derecognised in their entity but for which the entity retains continuing involvement. The adoption of these amendments did not have a significant impact on the Group's disclosures.

Amendments to IAS 12, 'Income taxes'

These amendments require the measurement of deferred tax assets and liabilities arising from investment properties and plant, property and equipment valued at fair value on the presumption that the carrying amount of the asset will be, normally, recovered through sale. The adoption of these amendments did not have a material effect on the Group's financial statements.

(b) Adoption of updated US GAAP reporting requirements for Group IFRS reporting in 2012

Background

In October 2010, the Emerging Issues Task Force of the US Financial Accounting Standards Board issued update No 2010-26 on 'Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts' (the 'Update'). The Update was issued to address perceived diversity in practices by companies preparing financial statements in accordance with US GAAP as regards the types of acquisition costs being deferred. Under US GAAP, costs that can be deferred and amortised are those that 'vary with and are primarily related to the acquisition of insurance contracts'. The Update requires insurers to capitalise only those incremental costs directly relating to acquiring a contract for financial statements for reporting periods beginning after 15 December 2011. All other indirect acquisition expenses are required to be charged to the income statements as incurred expenses. Accordingly, the main impact of the Update is to disallow insurers from deferring costs that are not directly related to successful sales.

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A: Background and accounting policies (Continued)

The Group's IFRS accounting policies include that under IFRS 4, 'Insurance Contracts', insurance assets and liabilities other than those for UK regulated with-profits funds, are measured using the GAAP basis applied prior to IFRS adoption in 2005. On this basis insurance assets and liabilities are measured under the UK Modified Statutory Basis (MSB) which was codified by the Statement of Recommended Practice (SORP) on accounting for insurance business issued by the Association of British Insurers (ABI) in 2003. The SORP also permits the use of local GAAP subject to the requirement for adjustments to be made to ensure sufficient consistency of measurement under the UK GAAP framework under which the SORP was developed.

In applying this overarching basis, the Group has chosen to apply US GAAP for measuring the insurance assets and liabilities of Jackson. In addition, for the Group's operations in India, Japan, Taiwan and until 2012 Vietnam*, where the local GAAP basis would not be appropriate as the start point for deriving MSB insurance asset and liabilities, the measurement has been determined substantially by reference to US GAAP requirements.

For 2012, the Group had the option to either continue with its current basis of measurement or improve its accounting policy under IFRS4 to acknowledge the issuance of the Update. Prudential has chosen to improve its accounting policy in 2012 to apply the US GAAP update, on a retrospective basis, to the results of Jackson and the affected Asia operations.

The 2011 and 2010 comparatives in these consolidated financial statements have been adjusted accordingly for the retrospective application of this Update.

Effect of the change in accounting policy

(a)

The effect of the change in accounting policy for deferred acquisition costs (DAC) on the income statement, earnings per share, comprehensive income, changes in equity and statement of financial position is shown in the tables below.

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Separately from the DAC change noted above, in Vietnam, the Company has improved its estimation basis for liabilities in 2012 from one determined substantially by reference to US GAAP requirements. After making this change, the estimation basis for Vietnam is aligned substantially with that used in Singapore, Malaysia and some other Asia operations.

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31 December 2012

A: Background and accounting policies (Continued)

Consolidated Income Statements

	Year ended 31 December								
	2012			2011			2010		
	Under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Total revenue, net of reinsurance	**55,476**		**55,476**	36,506		36,506	47,646		47,646
Acquisition costs and other expenditure	**(5,908)**	**(147)**	**(6,055)**	(5,005)	(115)	(5,120)	(4,799)	(190)	(4,989)
Total other charges, net of reinsurance	**(46,233)**		**(46,233)**	(29,575)		(29,575)	(40,775)		(40,775)
Profit before tax *(being tax attributable to shareholders' and policyholders' returns)*	**3,335**	**(147)**	**3,188**	1,926	(115)	1,811	2,072	(190)	1,882
(Less) Add tax (charge) credit attributable to policyholders' returns	**(378)**		**(378)**	17		17	(611)		(611)
Profit before tax attributable to shareholders	**2,957**	**(147)**	**2,810**	1,943	(115)	1,828	1,461	(190)	1,271
Total tax charge	**(1,039)**	**48**	**(991)**	(432)	40	(392)	(636)	65	(571)

attributable to policyholders and shareholders									
Adjustment to remove tax charge (credit) attributable to policyholders' returns	**378**		**378**	(17)		(17)	611		611
Tax charge attributable to shareholders' returns	**(661)**	**48**	**(613)**	(449)	40	(409)	(25)	65	40
Profit for the year	**2,296**	**(99)**	**2,197**	1,494	(75)	1,419	1,436	(125)	1,311
Profit for the year attributable to equity holders of the Company	**2,296**	**(99)**	**2,197**	1,490	(75)	1,415	1,431	(125)	1,311
Earnings per share (in pence)									
Based on profit attributable to the equity holders of the Company:									
Basic	**90.4p**	**(3.9)p**	**86.5p**	58.8p	(3.0)p	55.8p	56.7p	(4.9)p	51.8p
Diluted	**90.3p**	**(3.9)p**	**86.4p**	58.7p	(3.0)p	55.7p	56.6p	(4.9)p	51.7p

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Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

Consolidated Statements of Comprehensive Income and Statements of Changes in Equity

	Year ended 31 December								
	2012			2011			2010		
	Under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Profit for the year	**2,296**	**(99)**	**2,197**	1,494	(75)	1,419	1,436	(125)	1,311
Exchange movements on foreign operations and net investment hedges, net of related tax	**(236)**	**20**	**(216)**	(100)	(5)	(105)	251	(14)	237
Unrealised valuation movements on securities of US insurance operations classified as available-for-sale	**862**		**862**	811		811	1,221		1,221
Related change in amortisation of deferred income and acquisition costs	**(314)**	**44**	**(270)**	(331)	56	(275)	(496)	86	(410)
Related tax	**(190)**	**(15)**	**(205)**	(168)	(19)	(187)	(247)	(31)	(278)
Net unrealised gains	**358**	**29**	**387**	312	37	349	478	55	533
Total comprehensive income for the year	**2,418**	**(50)**	**2,368**	1,706	(43)	1,663	2,165	(84)	2,081
Total comprehensive income for the year attributable to equity holders of the Company	**2,418**	**(50)**	**2,368**	1,702	(43)	1,659	2,160	(84)	2,076
Shareholders' equity:									
Net increase in shareholders' equity	**1,845**	**(50)**	**1,795**	1,086	(43)	1,043	1,760	(84)	1,676

At beginning of year	**9,117**	**(553)**	**8,564**	8,031	(510)	7,521	6,271	(426)	5,845
At end of year	**10,962**	**(603)**	**10,359**	**9,117**	**(553)**	**8,564**	**8,031**	**(510)**	**7,521**

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Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

Consolidated Statements of Financial Position

	31 Dec 2012			31 Dec 2011			31 Dec 2010		
	Under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Assets									
Deferred acquisition costs and other intangible assets attributable to shareholders	**5,173**	**(906)**	**4,267**	5,069	(835)	4,234	4,667	(766)	3,901
Total other assets	**305,986**		**305,986**	268,511		268,511	256,139		256,139
Total assets	**311,159**	**(906)**	**310,253**	273,580	(835)	272,745	260,806	(766)	260,040
Liabilities									
Deferred tax liabilities	**4,273**	**(303)**	**3,970**	4,211	(282)	3,929	4,224	(256)	3,968
Total other liabilities	**295,919**		**295,919**	260,209		260,209	248,507		248,507
Total liabilities	**300,192**	**(303)**	**299,889**	264,420	(282)	264,138	252,731	(256)	252,475
Equity									
Shareholders' equity	**10,962**	**(603)**	**10,359**	9,117	(553)	8,564	8,031	(510)	7,521
Non-controlling interests	**5**		**5**	43		43	44		44
Total equity	**10,967**	**(603)**	**10,364**	9,160	(553)	8,607	8,075	(510)	7,565

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

(b)

The effect of the change in accounting policy for deferred acquisition costs on the Group's supplementary analysis of profit is shown in the table below.

Segment disclosure profit before tax

	Year ended 31 December								
	2012			2011			2010		
	Under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy	As reported under previous policy	Effect of change	Under new policy
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns									
Asia insurance operationsnote (i)	**922**	**(9)**	**913**	704		704	532	(10)	522
US insurance operationsnote (ii)	**1,081**	**(117)**	**964**	694	(43)	651	833	(105)	728
Other operations	**656**		**656**	672		672	576		576
Total	**2,659**	**(126)**	**2,533**	2,070	(43)	2,027	1,941	(115)	1,826
Short-term fluctuations in investment returns on shareholder-backed business	**225**	**(21)**	**204**	(148)	(72)	(220)	(123)	(75)	(198)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	**50**		**50**	21		21	(10)		(10)
Costs of terminated AIA transaction							(377)		(377)
Gain on dilution of Group's holdings	**42**		**42**				30		30
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC	**(19)**		**(19)**						
Profit before tax attributable to shareholders	**2,957**	**(147)**	**2,810**	1,943	(115)	1,828	1,461	(190)	1,271
	80.2p	**(3.4)p**	**76.8p**	63.9p	(1.1)p	62.8p	61.9p	(3.0)p	58.9p

Basic EPS from operating profit based on longer-term investment returns after tax and non-controlling interests									
Basic EPS based on total profit after tax and non-controlling interests	**90.4p**	**(3.9)p**	**86.5p**	58.8p	(3.0)p	55.8p	56.7p	(4.9)p	51.8p

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Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

Notes on the effect of the change in the accounting policy on operating profit based on longer-term investment returns

(i) Asia insurance operations

	2012 Effect of change	2011 Effect of change	2010 Effect of change
	£m	£m	£m
New business			
Acquisition costs on new contracts not deferred under the new policy	**(14)**	(16)	(20)
Business in force at beginning of period			
Reduction in amortisation on reduced DAC balance under the new policy	**5**	16	10
Total	**(9)**		(10)

(ii) US insurance operations

	2012 Effect of change	2011 Effect of change	2010 Effect of change
	£m	£m	£m
New business			
Acquisition costs on new contracts not deferred under the new policy	**(174)**	(156)	(159)
Business in force at beginning of period			
Reduction in amortisation on reduced DAC balance under the new policy	**57**	113	54
Total	**(117)**	(43)	(105)

(c) Accounting pronouncements endorsed by the EU but not yet effective

The following accounting pronouncements potentially relevant to the Group have been issued and endorsed for use in the EU but are not mandatory for adoption for the 31 December 2012 year end.

Amendments to IAS 19, 'Employee benefits'

In June 2011, the IASB published amendments to IAS 19 on accounting for pensions and other post-employment benefits effective from annual periods beginning on or after 1 January 2013. The key revisions to the standard are:

The removal of the corridor option for actuarial gains and losses.
The Group does not apply the corridor option, therefore its removal has no impact to the Group.

Presentation of actuarial gains and losses.

The Group currently presents actuarial gains and losses in the income statement. Under the revised standard actuarial gains and losses will be presented in 'other comprehensive income'. Details of the 2012 and 2011 actuarial gains and losses on the current basis are shown in note I3.

The replacement of the expected return on plan assets with an amount based on the liability discount rate in the determination of pension costs.

This revision alters the pension costs included in the Group's income statement with a corresponding equal and opposite effect on the actuarial gains and losses included in other comprehensive income. The effect of this change for Prudential is not expected to be significant.

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31 December 2012

A: Background and accounting policies (Continued)

Enhanced disclosures, specifically on risks arising from defined benefit plans.

Adoption of the revised IAS19 standard will have no impact on shareholders' equity.

Standards on joint arrangements and disclosures: IFRS 11,'Joint arrangements', IFRS 12,'Disclosures of interest in other entities' and IAS 28,'Investments in associates and joint ventures'

In May 2011, the IASB issued IFRS 11,'Joint arrangements' to replace IAS 31, 'Interests in Joint Ventures'. The standard also incorporates the guidance contained in related interpretation in SIC-13 Jointly Controlled Entities-Non-Monetary Contributions by Venturers. The standard requires a joint venture to be recognised as an investment and be accounted for using the equity method in accordance with IAS 28. The attaching changes to disclosure requirements for parties to joint arrangements are specified in IFRS 12,'Disclosures of interest in other entities', which replaces the disclosure requirements of IAS 28,'Investments in associates and joint ventures' and IAS 31, 'Interests in Joint Ventures'.

The standards are effective from annual periods beginning on or after 1 January 2013 for IFRS as issued by the IASB and 1 January 2014 for IFRS as endorsed by the EU but with early adoption permitted. The Group's investments in joint ventures are currently accounted for using proportionate consolidation. At 31 December 2012 this approach gave rise to consolidated gross assets and liabilities for the joint ventures of £3,946 million and £3,595 million respectively. With the application of IFRS 11, the Group's investments in joint ventures will be accounted for on a single line equity method thus giving rise at 31 December 2012 to a net interest of £351 million included within gross assets.

Similarly, the 2012 gross revenue and charges of £1,040 million and £942 million respectively which are currently included on a line by line basis within the income statement will, after adoption of the standard, be presented as a single net contribution of £98 million. As a consequence, the standard will also have a small impact on profit before tax as the tax on the profits of the joint ventures will no longer be presented in the tax line, instead the tax charges will be required to be netted against the Group's share of Joint Ventures' income included in profit before tax. The tax charges for 2012 for the Group's share of Joint ventures' income was £19 million. Adoption of the standard will have no impact on net of tax profits or shareholders' equity.

Standards on consolidation and disclosures: IFRS 10,'Consolidated financial statements', IFRS 12,'Disclosures of interest in other entities', and IAS 27,'Separate financial statements'

In May 2011, the IASB issued these three standards to replace IAS 27,'Consolidated and separate financial statements' and SIC-12 Consolidation-Special Purpose Entities.

The standards are effective from annual periods beginning on or after 1 January 2013. The standards are expected to have a minor impact on the Group's assessment of its interests in investment funds (including OEICs and unit trusts) and is likely to increase the number of funds consolidated. The Group is currently determining those additional funds that will require consolidation under the requirements of IFRS 10 and the effect of retrospective adjustment to comparative results. The principal effect will be to 'gross up' the consolidated balance sheet for

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

A: Background and accounting policies (Continued)

(i) The difference between the net value of the newly consolidated assets and liabilities and the previous carrying value for the Group's interest; and

(ii) The equal and opposite liability or minority interest for the external parties' interests in the funds.

The grossing up effect on the 2012 statement of financial position is not expected to exceed £1 billion. Adoption of the standard is expected to have an insignificant effect on the retrospectively adjusted comparative 2012 profit and shareholders' equity in the 2013 results.

IFRS 13, 'Fair value measurement'

In May 2011, the IASB issued IFRS 13, 'Fair value measurement' standard which creates a uniform framework to explain how to measure fair value and aims to enhance fair value disclosures, but it does not change when to measure fair value or require additional fair value measurements. The standard requires additional disclosure on the fair value of non-financial assets and liabilities and enhanced disclosures of recurring level 3 fair value measurements.

The standard is effective from annual periods beginning on or after 1 January 2013, with no adjustment to comparative results. The Group is currently assessing the impact of the standard but it is not expected to have a material impact on the fair value measurement of the Group's assets and liabilities. Disclosures will be enhanced in providing detail of the methodology and underlying assumptions used to determine fair value of the Group's assets and liabilities, in line with the new requirements.

Amendments to IAS 1, 'Presentation of financial statements'

These amendments effective on or after 1 January 2013 change the requirement for the disclosure of items presented in other comprehensive income, requiring items to be presented separately based on whether or not they may be recycled to profit or loss in the future. The Group is expecting the amendments to be purely presentational with no significant impact on the Group's results and financial position.

Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32, 'Financial instruments: Presentation' and IFRS 7 'Financial instruments: Disclosures')

The two amendments, effective on or after 1 January 2013 and 2014, respectively clarifies the offsetting criteria for financial assets and financial liabilities in the statement of financial position. The Group is currently assessing the impact of these amendments.

(d) Accounting pronouncements not yet endorsed by the EU

The following accounting pronouncement potentially relevant to the Group has been issued but not yet endorsed for use in the EU.

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31 December 2012

A: Background and accounting policies (Continued)

IFRS 9, 'Financial instruments: Classification and measurement'

The new standard effective on or after 1 January 2015 will automatically replace IAS 39,"Financial Instruments Recognition and measurement". Under the new requirements the classification and hence measurement of financial assets would be on two bases either amortised cost or fair value through profit or loss, rather than the existing four bases of classification. These requirements maintain the existing amortised cost measurement for most liabilities but will require changes in fair value due to changes in the entity's own credit risk to be recognised in the other comprehensive income (OCI) section of the comprehensive income statement, rather than within profit or loss for liabilities measured at fair value. On 28 November 2012, the IASB released an Exposure Draft proposing amendments to IAS 9. The proposed changes would introduce a fair value through other comprehensive income (FVOCI) category which would include certain financial assets that contain contractual cash flows that are solely payments of principal and interest and are held in a business model in which assets are managed both in order to collect contractual cash flows and for sale. The Group is still assessing the full impact of this standard.

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31 December 2012

B: Summary of results

B1: Segment disclosure income statement

The determination of the operating segments and performance measure of the operating segments of the Group are as detailed in note A3(2)(d). Further segmentation of the income statement is provided in note F1 of these financial statements.

	Note	2012	2011*	2010*
		£m	£m	£m
Asia operations				
Insurance operations	note (i), (ii)			
Operating result before gain on sale of stake in China Life of Taiwan		**869**	709	526
Gain on sale of stake in China Life of Taiwan		**51**		
Total Asia insurance operations		**920**	709	526
Development expenses		**(7)**	(5)	(4)
Total Asia insurance operations after development expenses		**913**	704	522
Eastspring Investments		**75**	80	72
Total Asia operations		**988**	784	594
US operations				
Jackson (US insurance operations)	notes (i),(ii),(iii)	**964**	651	728
Broker-dealer and asset management		**39**	24	22
Total US operations		**1,003**	675	750
UK operations				
UK insurance operations:	note (i),(ii)			
Long-term business		**703**	683	673
General insurance commission	note (v)	**33**	40	46
Total UK insurance operations		**736**	723	719
M&G		**371**	357	284
Total UK operations		**1,107**	1,080	1,003
Total segment profit		**3,098**	2,539	2,347
Other income and expenditure				
Investment return and other income		**13**	22	30

Interest payable on core structural borrowings		**(280)**	(286)	(257)
Corporate expenditure		**(231)**	(219)	(223)
Total		**(498)**	(483)	(450)
RPI to CPI inflation measure change on defined benefit pension schemesnote (vi)			42	
Solvency II implementation costs		**(48)**	(55)	(45)
Restructuring costsnote (vii)		**(19)**	(16)	(26)
Operating profit based on longer-term investment returns		**2,533**	2,027	1,826
Short-term fluctuations in investment returns on shareholder-backed businessnote (viii)		**204**	(220)	(198)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemesnote (ix)		**50**	21	(10)
Costs of terminated AIA transactionnote (x)				(377)
Gain on dilution of Group's holdings	**I2**	**42**		30
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC	**I1**	**(19)**		
Profit before tax attributable to shareholders		**2,810**	1,828	1,271

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Notes to the Consolidated Financial Statements

31 December 2012

B: Summary of results (Continued)

Notes

(i)

Operating profit based on longer-term investment returns

The Group provides supplementary analysis of IFRS profit before tax attributable to shareholders so as to distinguish operating profit based on longer-term investment returns from other elements of total profit. Operating profit based on longer-term investment returns is the basis on which management regularly reviews the performance of Prudential's segments as defined by IFRS 8. Further discussion on the determination of operating profit based on longer-term investment returns is provided in note A3(2)(d).

(ii)

Effect of changes to assumptions, estimates and bases of determining life assurance liabilities

The results of the Group's long-term business operations are affected by changes to assumptions, estimates and bases of preparation.

These are described in notes D2(g), D3(g) and D4(g).

(iii)

Jackson operating results based on longer-term investment returns

IFRS basis operating profits for US operations include the following amounts (net of related change in amortisation of deferred acquisition costs, where applicable) so as to derive longer-term investment returns.

	2012	**2011***	**2010***
	£m	**£m**	**£m**
Debt securities:			
Amortisation of interest related realised gains and losses	**72**	67	66
Risk margin reserve charge for longer-term credit related losses (see note (iv) below)	**(66)**	(56)	(58)
Equity type investments:			
Longer-term returns	**54**	51	51

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

(iv)

The risk margin reserve (RMR) charge for longer-term credit-related losses included in operating profit based on longer-term investment returns of Jackson for 2012 is based on an average annual RMR of 26 basis points (2011: 25 basis points; 2010: 26 basis points) on average book values of US$47.6 billion (2011: $44.4 billion; 2010: US$ 44.2 billion) as shown below:

	2012				**2011***				**2010***			
Moody's rating category (or equivalent under NAIC ratings of MBS)	**Average book value**	**RMR**	**Annual expected loss**		**Average book value**	**RMR**	**Annual expected loss**		**Average book value**	**RMR**	**Annual expected loss**	
	US $m	**%**	**US $m**	**£m**	**US $m**	**%**	**US $m**	**£m**	**US $m**	**%**	**US $m**	**£m**
A3 or higher	**23,129**	**0.11**	**(26)**	**(16)**	21,255	0.08	(17)	(11)	20,622	0.06	(12)	(8)
Baa1, 2 or 3	**21,892**	**0.26**	**(56)**	**(36)**	20,688	0.26	(54)	(34)	20,785	0.26	(53)	(34)
Ba1, 2 or 3	**1,604**	**1.12**	**(18)**	**(11)**	1,788	1.04	(19)	(11)	1,935	1.04	(20)	(13)
B1, 2 or 3	**597**	**2.82**	**(17)**	**(11)**	474	3.01	(14)	(9)	500	2.99	(15)	(10)
Below B3	**342**	**2.44**	**(8)**	**(5)**	211	3.88	(8)	(5)	321	3.88	(13)	(8)
Total	**47,564**	**0.26**	**(125)**	**(79)**	44,416	0.25	(112)	(70)	44,163	0.26	(113)	(73)
Related change to amortisation of deferred acquisition costs (see below)			**21**	**13**			22	14			22	14
Risk margin reserve charge to operating profit for longer-term credit related losses			**(104)**	**(66)**			(90)	(56)			(90)	(58)

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

Consistent with the basis of measurement of insurance assets and liabilities for Jackson's IFRS results, the charges and credits to operating profits based on longer-term investment returns are partially offset by related changes to amortisation of deferred acquisition costs.

(v)

General insurance commission

UK operations transferred its general insurance business to Churchill in 2002, with general insurance commission representing the commission received net of expenses for Prudential-branded general insurance products as part of this arrangement.

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31 December 2012

B: Summary of results (Continued)

(vi)

RPI to CPI inflation measure change

During 2011 the Group altered its inflation measure basis for future statutory increases to pension payments for certain tranches of its UK defined benefit pension schemes. This reflected the UK Government's decision to replace the basis of indexation from Retail Prices Index with Consumer Prices Index. This resulted in a credit to the operating profit before tax in 2011 of £42 million.

(vii)

Restructuring costs are incurred in the UK and represent one-off expenses incurred in securing expense savings.

(viii)

Short-term fluctuations in investment returns on shareholder-backed business

	2012	2011*	2010*
	£m	£m	£m
Insurance operations:			
Asia	76	(92)	114
US	(90)	(167)	(453)
UK	136	159	116
Other operations:			
Economic hedge value movement	(32)		
Other	114	(120)	25
Total	204	(220)	(198)

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

General overview of defaults

The Group did not experience any defaults on its shareholder-backed debt securities portfolio in 2012, 2011 or 2010.

Asia insurance operations

The positive short-term fluctuations of £76 million in 2012 reflects unrealised gains on bond assets following a fall in yields in the period. These gains more than offset the impact of falling interest rates in Hong Kong and the transfer to operating profit of previously booked unrealised gains on the sale of the Group's stake in China Life of Taiwan. The realised gain on the sale of the Group's stake in China Life of Taiwan of £51 million is included in the Group's operating profit based on longer-term investment returns as disclosed above.

The fluctuations of negative £(92) million in 2011 in part reflected equity market falls in Taiwan and negative unrealised value movement on the Group's stake in China Life of Taiwan.

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US insurance operations

The short-term fluctuations in investment returns for US insurance operations comprise the following items:

	2012	2011*	2010*
	£m	£m	£m
Short-term fluctuations relating to debt securities			
Charges in the year:			
Defaults			
Losses on sales of impaired and deteriorating bonds	**(23)**	(32)	(99)
Bond write downs	**(37)**	(62)	(124)
Recoveries/reversals	**13**	42	10
Total charges in the yearnote (a)	**(47)**	(52)	(213)
Less: Risk margin charge included in operating profit based on longer-term investment returnsnote (iii)	**79**	70	73
	32	18	(140)
Interest-related realised gains:			
Arising in the year	**94**	158	224
Less: Amortisation of gains and losses arising in current and prior years to operating profit based on longer-term investment returns	**(91)**	(84)	(82)
	3	74	142
Related change to amortisation of deferred acquisition costs	**(3)**	(3)	(2)
Total short-term fluctuations related to debt securities	**32**	89	
Derivatives (other than equity-related): market value movements (net of related change to amortisation of deferred acquisition costs)note (b)	**135**	554	(13)
Net equity hedge results (principally guarantees and derivatives, net of related change to amortisation of deferred acquisition costs)note (c)	**(302)**	(788)	(443)
Equity-type investments: actual less longer-term return (net of related change to amortisation of deferred acquisition costs)note A(d)(i)	**23**		4
Other items (net of related change to amortisation of deferred acquisition costs)	**22**	(22)	(1)

Total	**(90)**	(167)	(453)

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Notes

(a)

The charges on the debt securities of Jackson comprise the following:

	2012	2011	2010
	£m	£m	£m
Residential mortgage-backed securities:			
Prime (including agency)	**(4)**	(25)	(56)
Alt-A	**(1)**	(1)	(54)
Sub-prime	**(3)**		(13)
Total residential mortgage-backed securities	**(8)**	(26)	(123)
Corporate debt securities	**(14)**	(14)	(37)
Other	**(25)**	(12)	(53)
Total	**(47)**	(52)	(213)

(b)

The gain of £135 million (2011: gain of £554 million; 2010: loss of £13 million) is principally for the value movement of non-equity freestanding derivatives held to manage interest rate exposures, and for the GMIB reinsurance asset that is considered to be a derivative under IAS 39.

Under IAS 39, unless hedge accounting is applied value movements on derivatives are recognised in the income statement. For the derivatives programme attaching to the general account business, the Group has continued its approach of not seeking to apply hedge accounting under IAS 39. This decision reflects the inherent constraints of IAS 39 for hedge accounting investments and life assurance assets and liabilities under 'grandfathered' US GAAP under IFRS 4.

(c)

The amount of £(302) million (2011: £(788) million; 2010: £(443) million) relates to the net equity hedge accounting effect of the equity-based derivatives and associated guarantee liabilities of Jackson's variable and fixed index annuity business. The details of the value movements excluded from operating profit based on longer-term investment returns are as described in note C. The principal movements are for (i) value for free standing and GMWB 'not for life' embedded derivatives, (ii) accounting values for GMDB and GMWB 'for life' guarantees (iii) fee assessments and claim payments in respect of guarantee liabilities and (iv) related changes to DAC amortisation. In 2012, the charge of (£302) million principally reflects fair value movements on free standing futures contracts and short-dated options. The movements included within the net equity

hedge result include the effect of lower interest rates for which the movement was particularly significant in 2011. The value movements on derivatives held to manage this and any other interest rate exposure are included in the £135 million (2011: £554 million; 2010: £(13) million) described above in note (b).

In addition to the items discussed above, for US insurance operations, included within the statement of comprehensive income is an increase in net unrealised gains on debt securities classified as available-for-sale of £862 million (2011: increase in net unrealised gains of £811 million; 2010: increase in net unrealised gains of £1,221 million). Temporary market value movements do not reflect defaults or impairments. Additional details on the movement in the value of the Jackson portfolio are included in note D3.

UK Insurance operations

The short-term fluctuations gain for UK insurance operations of £136 million (2011: £159 million; 2010: £116 million) principally reflect net investment gains arising in the year on fixed income assets backing the capital of the shareholder-backed annuity business.

Economic hedge value movement

This item represents the costs on short-dated hedge contracts taken out in the first half of 2012 to provide downside protection against severe equity market falls through a period of particular uncertainty with respect to the Eurozone. The hedge contracts were terminated in the second half of 2012.

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Other operations

Short-term fluctuations of other operations in 2012 of £114 million and in 2010 of £25 million primarily represent unrealised fair value movements on Prudential Capital's bond portfolio. Short-term fluctuations of other operations in 2011 of £(120) million represent unrealised value movements on investments, including centrally held swaps to manage foreign exchange and certain macro-economic exposures of the Group.

(ix)

Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes

	2012	2011	2010
	£m	£m	£m
Actuarial gains and losses			
Actual less expected return on scheme assets	**11**	9	31
Experience gains on scheme liabilities	**15**	19	(5)
(Losses) gains on changes of assumptions for scheme liabilities	**(40)**	12	(41)
	(14)	40	(15)
Less: amount attributable to the PAC with-profits sub-fund	**15**	(18)	5
	1	22	(10)
Other gains and losses			
One-off uplift to recognise a portion of PSPS surplus	**164**		
Movement in the provision for deficit funding of PSPS		(4)	
Less: amount attributable to the PAC with-profits sub-fund	**(115)**	3	
	49	(1)	
Total	**50**	21	(10)

The actuarial gains and losses shown in the table above relate to the Scottish Amicable and M&G schemes. The amounts did not include actuarial gains and losses for the Prudential Staff Pension Scheme, for which the Group has not recognised a substantial portion of its interest in the scheme's underlying surplus.

For the 2011 and 2010 comparatives, the shareholders' share of actuarial and other gains and losses on defined benefit pension schemes comprises the aggregate effect of actual less expected returns on scheme assets, experience gains and losses, the effect of changes in assumptions and altered provisions for deficit funding, where relevant. For 2012, these items also apply. However, the shareholders' share of actuarial and other gains

and losses on defined benefit pension schemes also includes £49 million for the effect of partial recognition of surplus of the main Prudential Staff Pension Scheme. This credit arose from an altered funding arrangement following the 5 April 2011 triennial valuation. Further details on the Group's defined benefit pension schemes are shown in note I3.

(x)

The following costs were incurred in the first six months of 2010 in relation to the proposed, and subsequently terminated, transaction to purchase AIA Group Limited and related rights issue.

	2010
	£m
AIG termination break fee	153
Underwriting fees	58
Costs associated with foreign exchange hedging	100
Adviser fees and other	66
Total costs before tax	377
Associated tax relief	(93)
Total costs after tax	284

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Of the £377 million total costs before tax, the £100 million associated with foreign exchange hedging has been recorded within 'Investment return' and the other £277 million has been recorded as 'Other expenditure' within 'Acquisition costs and other expenditure' in the consolidated income statement.

B2: Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year, excluding those held in employee share trusts and consolidated unit trusts and Open Ended Investment Companies (OEICs), which are treated as cancelled.

For diluted earnings per share, the weighted average number of shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares. The Group's only class of potentially dilutive ordinary shares are those share options granted to employees where the exercise price is less than the average market price of the Company's ordinary shares during the year. No adjustment is made if the impact is anti-dilutive overall.

Earnings per share are calculated based on earnings attributable to ordinary shareholders, after related tax and non-controlling interests.

		2012					
	Note	Before tax note B1	Tax note F5	Non-controlling interests	Net of tax and non-controlling interests	Basic earnings per share	Diluted earnings per share
		£m	£m	£m	£m	pence	pence
Based on operating profit based on longer-term investment returns		2,533	(582)		1,951	76.8p	76.7p
Short-term fluctuations in investment returns on shareholder-backed business	B1	204	(26)		178	7.0p	7.0p
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	B1	50	(12)		38	1.5p	1.5p
Gain on dilution of Group's holdings	I2	42			42	1.7p	1.7p
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC	I1	(19)	7		(12)	(0.5)p	(0.5)p
Based on profit for the year		2,810	(613)		2,197	86.5p	86.4p

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		2011*					
	Note	Before tax note B1	Tax note F5	Non-controlling interests	Net of tax and non-controlling interests	Basic earnings per share	Diluted earnings per share
		£m	£m	£m	£m	pence	pence
Based on operating profit based on longer-term investment returns		2,027	(433)	(4)	1,590	62.8p	62.7p
Short-term fluctuations in investment returns on shareholder-backed business	B1	(220)	29		(191)	(7.6)p	(7.6)p
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	B1	21	(5)		16	0.6p	0.6p
Based on profit for the year		1,828	(409)	(4)	1,415	55.8p	55.7p

	2010*					
	Before tax note B1	Tax note F5	Non-controlling interests	Net of tax and non-controlling interests	Basic earnings per share	Diluted earnings per share
	£m	£m	£m	£m	pence	pence
Based on operating profit based on longer-term investment returns, excluding exceptional tax credit	1,826	(332)	(5)	1,489	59.0 p	58.9 p
Exceptional tax credit*		158		158	6.3 p	6.3 p
Based on operating profit based on longer-term investment return	1,826	(174)	(5)	1,647	65.3 p	65.2 p
Short-term fluctuations in investment returns on shareholder-backed business	(198)	118		(80)	(3.1)p	(3.1)p
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(10)	3		(7)	(0.3)p	(0.3)p
Costs of terminated AIA transaction	(377)	93		(284)	(11.3)p	(11.3)p
Gain on dilution of Group's holdings	30			30	1.2p	1.2p
Based on profit for the year including exceptional tax credit	1,271	40	(5)	1,306	51.8p	51.7p

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Number of shares

A reconciliation of the weighted average number of ordinary shares used for calculating basic and diluted earnings per share is set out as below:

	2012	2011	2010
	£m	£m	£m
Weighted average shares for calculation of basic earnings per share	**2,541**	2,533	2,524
Shares under option at end of year	**9**	13	13
Number of shares that would have been issued at fair value on assumed option exercise	**(6)**	(8)	(8)
Weighted average shares for calculation of diluted earnings per share	**2,544**	2,538	2,529

B3: Dividends

	2012	2011	2010
	£m	£m	£m
Dividends declared and paid in reporting year			
Parent company:			
Interim dividend (2012: 8.40p; 2011: 7.95p; 2010: 6.61p per share)	**215**	203	168
Final dividend for prior period (2012: 17.24p; 2011: 17.24p; 2010: 13.56p per share)	**440**	439	343
Total	**655**	642	511

Dividends paid in cash, as set in the consolidated statement of cash flows for 2012 were £655 million (2011: £642 million; 2010: £449 million).

	2012	2011	2010
	£m	£m	£m
Parent company dividends relating to reporting year:			
Interim dividend (2012: 8.40p; 2011: 7.95p, 2010: 6.61p per share)	**215**	203	168
Final dividend (2012: 20.79p; 2011: 17.24p, 2010: 17.24p per share)	**532**	439	439
Total	**747**	642	607

Dividend per share

Interim dividends are recorded in the period in which they are paid. Final dividends are recorded in the period in which they are approved by shareholders. The final dividend for the year ended 31 December 2011 of 17.24 pence per ordinary share was paid to eligible shareholders on 24 May 2012 and the 2012 interim dividend of 8.4 pence per ordinary share was paid to eligible shareholders on 27 September 2012.

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The Board has decided to rebase the full year dividend upwards by 4 pence, reflecting the strong progress made in both the earnings and free surplus generation of the business and in the delivery of our financial objectives. In line with this, the directors recommend a final dividend of 20.79 pence per share (2011: 17.24 pence), which brings the total dividend for the year to 29.19 pence (2011: 25.19 pence), representing an increase of 15.9 per cent over 2011.

The 2012 final dividend of 20.79 pence per ordinary share will be paid on 23 May 2013 in sterling to shareholders on the principal register and the Irish branch register at 6.00pm BST on Tuesday, 2 April 2013 (Record Date), and in Hong Kong dollars to shareholders on the Hong Kong branch register at 4.30pm Hong Kong time on the Record Date (HK Shareholders). Holders of US American Depositary Receipts (US Shareholders) will be paid their dividends in US dollars on or about 3 June 2013. The final dividend will be paid on or about 30 May 2013 in Singapore dollars to shareholders with shares standing to the credit of their securities accounts with The Central Depository (Pte.) Limited (CDP) at 5.00pm Singapore time on the Record Date (SG Shareholders). The dividend payable to the HK Shareholders will be translated using the exchange rate quoted by the WM Company at the close of business on 12 March 2013. The exchange rate at which the dividend payable to the SG Shareholders will be translated into SG$, will be determined by CDP. The dividend will distribute an estimated £532 million of shareholders' funds.

Shareholders on the principal register and Irish branch register will be able to participate in a Dividend Reinvestment Plan.

B4: Exchange translation

Exchange movement recognised in other comprehensive income

	2012	2011*	2010*
	£m	£m	£m
Asia operations	**(87)**	(28)	162
US operations	**(187)**	35	76
Unallocated to a segment (central funds)	**60**	(44)	(35)
	(214)	(37)	203

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

The movements for Asia and US operations reflect the application of year end exchange rates to the assets and liabilities and average exchange rates to the income statement on translation of these operations into the presentation currency of the Group. The movement unallocated to a segment mainly reflects the translation of currency borrowings and forward contracts which have been designated as a net investment hedge against the currency risk of the net investment in Jackson.

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The exchange rates applied were:

Local currency: £	Closing rate at 31 Dec 2012	Average for 2012	Closing rate at 31 Dec 2011	Average for 2011	Closing rate at 31 Dec 2010	Average for 2010	Opening rate at 1 Jan 2010
Hong Kong	**12.60**	**12.29**	12.07	12.48	12.17	12.01	12.52
Indonesia	**15,665.76**	**14,842.01**	14,091.80	14,049.41	14,106.51	14,033.41	15,171.52
Malaysia	**4.97**	**4.89**	4.93	4.90	4.83	4.97	5.53
Singapore	**1.99**	**1.98**	2.02	2.02	2.01	2.11	2.27
India	**89.06**	**84.70**	82.53	74.80	70.01	70.66	75.15
Vietnam	**33,875.42**	**33,083.59**	33,688.16	33,139.22	30,526.26	29,587.63	29,832.74
US	**1.63**	**1.58**	1.55	1.60	1.57	1.55	1.61

B5: Group statement of financial position

To explain more comprehensively the assets, liabilities and capital of the Group's businesses, it is appropriate to provide analyses of the Group's statement of financial position by operating segment and type of business.

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The tables below aggregate the three asset management segments for ease of presentation and hence should be read in conjunction with the associated tables on asset management in note E2.

(a) Group statement of financial position by operating segment

(i) Position at 31 December 2012

2012

By operating segment	Insurance operations: UK D2	Insurance operations: US D3	Insurance operations: Asia D4	Insurance operations: Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec Group total
	£m	£m	£m	£m	£m	£m	£m	£m
Assets								
Intangible assets attributable to shareholders:								
Goodwill			**239**	**239**	**1,230**			**1,469**
Deferred acquisition costs and other intangible assets	**105**	**3,222**	**908**	**4,235**	**14**	**18**		**4,267**
Total	**105**	**3,222**	**1,147**	**4,474**	**1,244**	**18**		**5,736**
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	**178**			**178**				**178**
Deferred acquisition costs and other intangible assets	**6**		**72**	**78**				**78**
TotalH1	**184**		**72**	**256**				**256**
Total intangible assets	**289**	**3,222**	**1,219**	**4,730**	**1,244**	**18**		**5,992**
Deferred tax assetsH4	**183**	**1,889**	**83**	**2,155**	**107**	**52**		**2,314**
Other non-investment and non-cash assetsH3,H6	**5,424**	**6,792**	**1,117**	**13,333**	**1,051**	**3,766**	**(6,113)**	**12,037**
Investments of long-term business and other operations:								

Investment properties	**10,852**	**24**	**4**	**10,880**				**10,880**
Investments accounted for using the equity method	**72**			**72**	**41**			**113**
Financial investments:								
Loans	**3,373**	**6,235**	**1,014**	**10,622**	**1,199**			**11,821**
Equity securities and portfolio holdings in unit trusts	**36,027**	**49,551**	**14,310**	**99,888**	**70**			**99,958**
Debt securitiesnote B5(c)	**83,862**	**32,993**	**21,402**	**138,257**	**1,846**			**140,103**
Other investments	**4,576**	**2,296**	**957**	**7,829**	**44**	**27**		**7,900**
Deposits	**11,131**	**211**	**1,227**	**12,569**	**84**			**12,653**
Total investmentsG1,H7,H8,	**149,893**	**91,310**	**38,914**	**280,117**	**3,284**	**27**		**283,428**
Properties held for saleH9	**98**			**98**				**98**
Cash and cash equivalentsH10	**2,638**	**513**	**1,668**	**4,819**	**1,083**	**482**		**6,384**
Total assets	**158,525**	**103,726**	**43,001**	**305,252**	**6,769**	**4,345**	**(6,113)**	**310,253**

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Note

Further segmental analysis:

The non-current assets of the Group comprise goodwill, intangible assets other than DAC and present value of acquired in-force business and property, plant and equipment included within 'other non-investment and non-cash assets'. Items defined as financial instruments or related to insurance contracts are excluded. The Group's total non-current assets at 31 December comprise:

	2012	2011
	£m	£m
UK including insurance operations, M&G and central operations	**1,927**	1,906
US	**152**	144
Asia*	**640**	681
Total	**2,719**	2,731

* No individual country in Asia held non-current assets at the end of the year which exceeds 10 per cent of the Group total.

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	2012							
	Insurance operations					Unallocated to a segment (central operations)		
By operating segment	UK D2	US D3	Asia D4	Total insurance operations	Asset management operations E2		Intra-group eliminations	31 Dec Group total
	£m	£m	£m	£m	£m	£m	£m	£m
Equity and liabilities								
Equity								
Shareholders' equity H11	**3,033**	**4,343**	**2,529**	**9,905**	**1,937**	**(1,483)**		**10,359**
Non-controlling interests	**1**		**4**	**5**				**5**
Total equity	**3,034**	**4,343**	**2,533**	**9,910**	**1,937**	**(1,483)**		**10,364**
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Insurance contract liabilities H12	**84,266**	**90,192**	**34,126**	**208,584**				**208,584**
Investment contract liabilities with discretionary participation features G1	**33,464**		**348**	**33,812**				**33,812**
Investment contract liabilities without discretionary participation features G1	**16,182**	**2,069**	**127**	**18,378**				**18,378**
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds) D2, H12	**10,526**		**63**	**10,589**				**10,589**
Total policyholder liabilities and unallocated surplus of with-profits funds	**144,438**	**92,261**	**34,664**	**271,363**				**271,363**
Core structural borrowings of shareholder-financed operations: H13								

Subordinated debt						2,577		2,577
Other		153		153	275	549		977
Total		153		153	275	3,126		3,554
Operational borrowings attributable to shareholder-financed operations	127	26	7	160	1	2,084		2,245
Borrowings attributable to with-profits operations	1,033			1,033				1,033
Other non-insurance liabilities:								
Obligations under funding, securities lending and sale and repurchase agreements	1,461	920	55	2,436				2,436
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	2,307	25	1,851	4,183	162			4,345
Deferred tax liabilities	1,185	2,168	588	3,941	13	16		3,970
Current tax liabilities	237		49	286	8	151		445
Accruals and deferred income	429		110	539	266	28		833
Other creditors	2,766	611	1,601	4,978	3,771	145	(6,113)	2,781
Provisions	291	20	66	377	149	75		601
Derivative liabilities	1,007	645	837	2,489	150	190		2,829
Other liabilities	210	2,554	640	3,404	37	13		3,454
Total	9,893	6,943	5,797	22,633	4,556	618	(6,113)	21,694
Total liabilities	155,491	99,383	40,468	295,342	4,832	5,828	(6,113)	299,889
Total equity and liabilities	158,525	103,726	43,001	305,252	6,769	4,345	(6,113)	310,253

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(ii) Position at 31 December 2011

	2011*							
	Insurance operations							
By operating segment	**UK D2**	**US D3**	**Asia D4**	**Total insurance operations**	**Asset management operations E2**	**Unallocated to a segment (central operations)**	**Intra-group eliminations**	**31 Dec Group total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Assets								
Intangible assets attributable to shareholders:								
Goodwill			235	235	1,230			1,465
Deferred acquisition costs and other intangible assets	113	3,115	977	4,205	16	13		4,234
TotalH1	113	3,115	1,212	4,440	1,246	13		5,699
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	178			178				178
Deferred acquisition costs and other intangible assets	6		83	89				89
TotalH2	184		83	267				267
Total intangible assets	297	3,115	1,295	4,707	1,246	13		5,966
Deferred tax assets	231	1,392	115	1,738	129	409		2,276
Other non-investment and non-cash assetsH3,H6	4,771	1,542	1,024	7,337	1,000	4,532	(6,231)	6,638
Investments of long-term business and other operations:								
Investment properties	10,712	35	10	10,757				10,757
Investments accounted for using the equity method	70			70				70
Financial investments:								

Loans	3,115	4,110	1,233	8,458	1,256			9,714
Equity securities and portfolio holdings in unit trusts	36,722	38,036	11,997	86,755	594			87,349
Debt securitiesBS(c)	77,953	27,022	17,681	122,656	1,842			124,498
Other investments	4,568	2,376	470	7,414	78	17		7,509
Deposits	9,287	167	1,165	10,619	89			10,708
Total investmentsG1,H7,H8	142,427	71,746	32,556	246,729	3,859	17		250,605
Properties held for saleH9		3		3				3
Cash and cash equivalentsH10	2,965	271	1,977	5,213	1,735	309		7,257
Total assets	150,691	78,069	36,967	265,727	7,969	5,280	(6,231)	272,745

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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B: Summary of results (Continued)

2011*

By operating segment	UK D2	US D3	Asia D4	Total insurance operations	Asset management operations E2	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec Group total
	£m	£m	£m	£m	£m	£m	£m	£m
Equity and liabilities								
Equity								
Shareholders' equity H11	2,581	3,761	2,306	8,648	1,783	(1,867)		8,564
Non-controlling interests	33		5	38	5			43
Total equity	2,614	3,761	2,311	8,686	1,788	(1,867)		8,607
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Insurance contract liabilities H12	72,732	67,278	30,353	180,363				180,363
Investment contract liabilities with discretionary participation features G1	29,348		397	29,745				29,745
Investment contract liabilities without discretionary participation features G1	14,944	1,911	112	16,967				16,967
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds) D2, H12	9,165		50	9,215				9,215
Total policyholder liabilities and unallocated surplus of with-profits funds	136,189	69,189	30,912	236,290				236,290
Core structural borrowings of shareholder-financed operations: G1,H13								
Subordinated debt						2,652		2,652
Other		160		160	250	549		959

Total		160		160	250	3,201		3,611
Operational borrowings attributable to shareholder-financed operations	103	127	141	371	13	2,956		3,340
Borrowings attributable to with-profits operations	972			972				972
Other non-insurance liabilities:								
Obligations under funding, securities lending and sale and repurchase agreementsH4,H14,H15	1,945	1,169		3,114				3,114
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	2,043	18	1,101	3,162	678			3,840
Deferred tax liabilities	1,349	1,818	506	3,673	5	251		3,929
Current tax liabilities	553		116	669	106	155		930
Accruals and deferred income	321		103	424	290	22		736
Other creditors	2,829	548	660	4,037	4,493	245	(6,231)	2,544
Provisions	266	13	47	326	133	70		529
Derivative liabilities	1,298	887	480	2,665	182	207		3,054
Other liabilities	209	379	590	1,178	31	40		1,249
Total	10,813	4,832	3,603	19,248	5,918	990	(6,231)	19,925
Total liabilities	148,077	74,308	34,656	257,041	6,181	7,147	(6,231)	264,138
Total equity and liabilities	150,691	78,069	36,967	265,727	7,969	5,280	(6,231)	272,745

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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(b) Group statement of financial position additional analysis by business type

	2012							2011*
	Shareholder-backed business							
	Participating funds	Unit-linked and variable annuity	Non-linked business	Asset management operations	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec Group total	31 Dec Group total
	£m	£m	£m	£m	£m	£m	£m	£m
Assets								
Intangible assets attributable to shareholders:								
Goodwill			**239**	**1,230**			**1,469**	1,465
Deferred acquisition costs and other intangible assets			**4,235**	**14**	**18**		**4,267**	4,234
Total			**4,474**	**1,244**	**18**		**5,736**	5,699
Intangible assets attributable to with-profits funds:								
In respect of acquired subsidiaries for venture fund and other investment purposes	**178**						**178**	178
Deferred acquisition costs and other intangible assets	**78**						**78**	89
Total	**256**						**256**	267
Total intangible assets	**256**		**4,474**	**1,244**	**18**		**5,992**	5,966
Deferred tax assets	**114**		**2,041**	**107**	**52**		**2,314**	2,276
Other non-investment and non-cash assets	**3,133**	**508**	**9,692**	**1,051**	**3,766**	**(6,113)**	**12,037**	6,638
Investments of long-term business and other operations:								
Investment properties	**8,659**	**622**	**1,599**				**10,880**	10,757
Investments accounted for using the equity method			**72**	**41**			**113**	70
Financial investments:								

Loans	**2,709**		**7,913**	**1,199**			**11,821**	9,714
Equity securities and portfolio holdings in unit trusts	**25,105**	**73,860**	**923**	**70**			**99,958**	87,349
Debt securities	**62,002**	**9,504**	**66,751**	**1,846**			**140,103**	124,498
Other investments	**4,745**	**57**	**3,027**	**44**	**27**		**7,900**	7,509
Deposits	**9,470**	**1,396**	**1,703**	**84**			**12,653**	10,708
Total investments	**112,690**	**85,439**	**81,988**	**3,284**	**27**		**283,428**	250,605
Properties held for sale	**98**						**98**	3
Cash and cash equivalents	**1,721**	**1,310**	**1,788**	**1,083**	**482**		**6,384**	7,257
Total assets	**118,012**	**87,257**	**99,983**	**6,769**	**4,345**	**(6,113)**	**310,253**	272,745

* The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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	2012 Shareholder-backed business							2011*
	Participating funds	Unit-linked and variable annuity	Non-linked business	Asset management operations	Unallocated to a segment (central operations)	Intra-group eliminations	31 Dec 2012 Group total	31 Dec 2011 Group total
	£m	£m	£m	£m	£m	£m	£m	£m
Equity and liabilities								
Equity								
Shareholders' equity			**9,905**	**1,937**	**(1,483)**		**10,359**	8,564
Non-controlling interests	**1**		**4**				**5**	43
Total equity	**1**		**9,909**	**1,937**	**(1,483)**		**10,364**	8,607
Liabilities								
Policyholder liabilities and unallocated surplus of with-profits funds:								
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	**97,795**	**85,523**	**77,456**				**260,774**	227,075
Unallocated surplus of with-profits funds	**10,589**						**10,589**	9,215
Total policyholder liabilities and unallocated surplus of with-profits funds	**108,384**	**85,523**	**77,456**				**271,363**	236,290
Core structural borrowings of shareholder-financed operations:								
Subordinated debt					**2,577**		**2,577**	2,652
Other			**153**	**275**	**549**		**977**	959
Total			**153**	**275**	**3,126**		**3,554**	3,611
Operational borrowings attributable to		**1**	**159**	**1**	**2,084**		**2,245**	3,340

shareholder-financed operations								
Borrowings attributable to with-profits operations	**1,033**						**1,033**	972
Deferred tax liabilities	**1,086**	**46**	**2,809**	**13**	**16**		**3,970**	3,929
Other non-insurance liabilities	**7,508**	**1,687**	**9,497**	**4,543**	**602**	**(6,113)**	**17,724**	15,996
Total liabilities	**118,011**	**87,257**	**90,074**	**4,832**	**5,828**	**(6,113)**	**299,889**	264,138
Total equity and liabilities	**118,012**	**87,257**	**99,983**	**6,769**	**4,345**	**(6,113)**	**310,253**	272,745

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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B: Summary of results (Continued)

(b) Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of the Group from the beginning of the year to the end of the year is as follows:

	Insurance operations			
	UK	**US**	**Asia**	**Total**
	£m	**£m**	**£m**	**£m**
At 1 January 2011	135,717	60,523	28,740	224,980
Comprising:				
Policyholder liabilities	125,530	60,523	28,674	214,727
Unallocated surplus of with-profits funds	10,187		66	10,253
Premiums	6,988	12,914	5,079	24,981
Surrenders	(4,255)	(4,270)	(2,237)	(10,762)
Maturities/Deaths	(7,813)	(820)	(664)	(9,297)
Net flows	(5,080)	7,824	2,178	4,922
Shareholders' transfers post tax	(216)		(30)	(246)
Investment-related items and other movements	5,862	136	365	6,363
Foreign exchange translation differences	(94)	706	(341)	271
At 31 December 2011	**136,189**	**69,189**	**30,912**	**236,290**
Comprising:				
Policyholder liabilities	**127,024**	**69,189**	**30,862**	**227,075**
Unallocated surplus of with-profits funds	**9,165**		**50**	**9,215**
At 1 January 2012	**136,189**	**69,189**	**30,912**	**236,290**
Premiums	**8,340**	**14,907**	**5,620**	**28,867**
Surrenders	**(4,785)**	**(4,356)**	**(2,541)**	**(11,682)**
Maturities/Deaths	**(8,009)**	**(954)**	**(658)**	**(9,621)**
Net flows	**(4,454)**	**9,597**	**2,421**	**7,564**
Shareholders' transfers post tax	**(205)**		**(31)**	**(236)**
Investment-related items and other movements	**13,006**	**4,241**	**2,178**	**19,425**
Foreign exchange translation differences	**(98)**	**(3,678)**	**(816)**	**(4,592)**
Acquisition of REALIC[note Z]		**12,912**		**12,912**
At 31 December 2012	**144,438**	**92,261**	**34,664**	**271,363**
Comprising:				

Policyholder liabilities	**133,912**	**92,261**	**34,601**	**260,774**
Unallocated surplus of with-profits funds	**10,526**		**63**	**10,589**
Average policyholder liability balances*				
2012	**130,468**	**77,497**	**32,732**	**240,697**
2011	126,277	64,856	29,768	220,901

* Averages have been based on opening and closing balances and adjusted for acquisitions and disposals in the period and exclude unallocated surplus of with-profits funds.

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The items above represent the amount attributable to changes in policyholder liabilities and unallocated surplus of with-profits funds as a result of each of the components listed. The policyholder liabilities shown include investment contracts without discretionary participation features (as defined in IFRS 4) and their full movement in the year. The items above are shown gross of reinsurance.

The analysis includes the impact of premiums, claims and investment movements on policyholders' liabilities. The impact does not represent premiums, claims and investment movements as reported in the income statement. For example, the premiums shown above will exclude any deductions for fees/charges and claims represent the policyholder liabilities provision released rather than the claim amount paid to the policyholder.

(c) Debt securities and loans

(i) Information on the credit risks of debt securities

	2012						2011
	Insurance operations			Total insurance operations	Asset management	Group total	Group total
	UK	US	Asia				
	£m	£m	£m	£m	£m	£m	£m
S&P AAA	**9,200**	**187**	**785**	**10,172**	**1,046**	**11,218**	12,593
S&P AA+ to AA	**9,623**	**6,343**	**5,523**	**21,489**	**106**	**21,595**	17,038
S&P A+ to A	**23,000**	**7,728**	**3,282**	**34,010**	**206**	**34,216**	31,161
S&P BBB+ to BBB	**17,720**	**10,230**	**1,906**	**29,856**	**235**	**30,091**	25,860
S&P Other	**3,043**	**1,173**	**3,132**	**7,348**	**37**	**7,385**	6,346
	62,586	**25,661**	**14,628**	**102,875**	**1,630**	**104,505**	92,998
Moody's Aaa	**8,446**	**55**	**1,389**	**9,890**	**135**	**10,025**	9,615
Moody's Aa1 to Aa3	**1,420**	**18**	**271**	**1,709**	**36**	**1,745**	806
Moody's A1 to A3	**927**	**21**	**169**	**1,117**		**1,117**	1,352
Moody's Baa1 to Baa3	**1,385**	**56**	**375**	**1,816**	**12**	**1,828**	1,228
Moody's Other	**307**	**13**	**112**	**432**		**432**	318
	12,485	**163**	**2,316**	**14,964**	**183**	**15,147**	13,319
Implicit ratings of MBS based on NAIC valuations (see below)							
NAIC 1		**2,934**		**2,934**		**2,934**	2,577
NAIC 2		**207**		**207**		**207**	147
NAIC 3-6		**321**		**321**		**321**	368
		3,462		**3,462**		**3,462**	3,092

Fitch	**527**	**184**	**533**	**1,244**	**21**	**1,265**	1,039
Other	**8,264**	**3,523**	**3,925**	**15,712**	**12**	**15,724**	14,050
Total debt securities	**83,862**	**32,993**	**21,402**	**138,257**	**1,846**	**140,103**	124,498

In the table above, with the exception of some mortgage-backed securities within Jackson, Standard & Poor's (S&P) ratings have been used where available. For securities where S&P ratings are not immediately available, those produced by Moody's and then Fitch have been used as an alternative. For some mortgage-backed securities within Jackson, the table above includes these securities using the

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B: Summary of results (Continued)

regulatory ratings detail issued by the National Association of Insurance Commissioners (NAIC). These regulatory ratings levels were established by external third parties (PIMCO for residential mortgage-backed securities and BlackRock Solutions for commercial mortgage-backed securities). Notes D2(c), D3(c), D4(c) and E2 provide further details on the credit risks of debt securities by segment.

(ii) Group's exposure to holdings in asset-backed securities

The Group's exposure to holdings in asset-backed securities (ABS), which comprise residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), collateralised debt obligations (CDO) funds and other asset-backed securities, at 31 December 2012 is as follows:

	2012	2011
	£m	£m
Shareholder-backed operations:		
UK insurance operations (2012: 34% AAA, 17% AA)[note (i)]	**1,408**	1,358
US insurance operations[note D3]	**5,626**	5,380
Asia insurance operations[note (ii)]	**144**	176
Asset management operations[note (iii)]	**566**	594
	7,744	7,508
With-profits operations:		
UK insurance operations (2012: 60% AAA, 9% AA)[note (i)]	**5,850**	5,351
Asia insurance operations[note (ii)]	**241**	454
	6,091	5,805
Total	**13,835**	13,313

Notes

(i)

UK insurance operations

All of the exposure of the shareholder-backed business relates to the UK market and primarily relates to investments held by PRIL.

Of the £5,850 million (2011: £5,351 million) relating to with-profit business, £1,697 million (2011: £1,314 million) relates to exposure to the US and with the remaining exposure being primarily to the UK market.

(ii)

Asia insurance operations

The Asia insurance operations' exposure to asset-backed securities is primarily held by the with-profits operations. Of the £241 million, 63 per cent (2011: £454 million, 75 per cent) are investment grade.

(iii)

Asset management operations

Asset management operations' exposure to asset-backed securities is held by Prudential Capital with no sub-prime exposure. Of the £566 million, 77 per cent (2011: £595 million, 77 per cent) are graded AAA.

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(iii) Group sovereign debt exposure

The exposures held by the shareholder-backed business and with-profits funds in sovereign debts and bank debt securities at 31 December 2012 are given within the Risk and Capital Management section of Item 4 'Information on the Company Group Risk Framework' under Credit Risk.

(iv) Loans

Information on the credit quality of the portfolio of loans, which almost wholly is for amounts which are neither past due or impaired is shown in notes D2, D3, D4 and E2. Details of allowances for loans, losses and amounts past due are shown in notes G1 and G2. No additional analysis is provided of the element of loans and receivables that were neither past due nor impaired from those of the total portfolio on the grounds of the immateriality of the difference between the neither past due nor impaired element and the total portfolio.

C: Group risk management

Disclosures concerning the Group's risk framework and the management of the risk attached to the Group's financial instruments and insurance liabilities, together with the inter-relationship with the management of capital have been included in the audited sections of the Risk and Capital Management disclosure in Item 4 'Information on the Company Group Risk Framework'. Additional disclosures are shown in section D1.

D: Life assurance business

D1: Group overview

(a) Products and classification for IFRS reporting

The measurement basis of assets and liabilities of long-term business contracts is dependent upon the classification of the contracts under IFRS. Under IFRS 4, contracts are initially classified as being either 'insurance' contracts, if the level of insurance risk in the contracts is significant, or 'investment' contracts, if the risk is insignificant.

Insurance contracts

Insurance contracts are permitted to be accounted for under previously applied GAAP. The Group has chosen to adopt this approach. However, as an improvement to accounting policy, permitted by IFRS 4, the Group has applied the measurement principles for with-profits contracts of UK regulated entities and disclosures of the UK Standard FRS 27 from 1 January 2005. An explanation of the provisions under FRS 27 is provided in note D2.

Under the previously applied GAAP, UK GAAP, the assets and liabilities of contracts are reported in accordance with the Modified Statutory Basis (MSB) of reporting as set out in the ABI SORP.

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D: Life assurance business (Continued)

The insurance contracts of the Group's shareholder-backed business fall broadly into the following categories:

UK insurance operations

bulk and individual annuity business, and other categories of non-participating UK business;

Jackson

fixed and variable annuity business and life insurance; and

Prudential Corporation Asia

non-participating term, whole life, and unit-linked policies, together with accident and health policies.

Investment contracts

Investment contracts are further delineated under IFRS 4 between those with and without discretionary participation features. For those contracts with discretionary participation features, IFRS 4 also permits the continued application of previously applied GAAP. The Group has adopted this approach, again subject to the FRS 27 improvement.

For investment contracts that do not contain discretionary participation features, IAS 39 and, where the contract includes an investment management element, IAS 18, apply measurement principles to assets and liabilities attaching to the contract that may diverge from those previously applied.

Contracts of the Group, which are classified as investment contracts that do not contain discretionary participation features, can be summarised as:

UK

certain unit-linked savings and similar contracts;

Jackson

Guaranteed Investment Contracts (GICs) and funding agreements - minor amounts of 'annuity certain' contracts; and

Prudential Corporation Asia

minor amounts for a number of small categories of business.

(b) Concentration of risk

(i) Business accepted

The Group's exposure to life assurance risks is well diversified. This is achieved through the geographical spread of the Group's operations and, within those operations, through a broad mix of product types.

As part of the risk management framework, the Group regularly monitors concentration of risk using a variety of risk monitoring tools, including scenario testing and sensitivity analysis of the Group's capital and profitability metrics involving IGD, Group economic capital, EEV and IFRS, to help identify concentrations of risks by risk types, products and business units, as well as the benefits of diversification of risks.

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D: Life assurance business (Continued)

An example of the diversification benefits for Prudential is that adverse scenarios do not affect all business units in the same way, providing natural hedges within the Group. For example, the Group's US business is sensitive to increasing interest rates, whereas, in contrast, several business units in Asia benefit from increasing rates. Conversely, these Asian business units are sensitive towards low interest rates, whereas certain products in the US benefit from falling interest rates. The economic capital framework also takes into account situations where factors are correlated, for example the extent of correlation between UK and US economies.

Business units are also required to disclose to the Group risk function all material risks, along with information on their severity and likelihood, and mitigating actions taken or planned.

Credit risk remains one of the largest risk exposures. This reflects the relative size of exposure in Jackson and the UK shareholder annuities business. The Group manages concentration of credit risks by setting limits on the maximum exposure to each counterparty based on their credit ratings.

(ii) Ceded business

The Group cedes certain business to other insurance companies. Although the ceding of insurance does not relieve the Group of liability to its policyholders, the Group participates in such agreements for the purpose of managing its loss exposure. The Group evaluates the financial condition of its reinsurers and monitors concentration of credit risk from similar geographic regions, activities or economic characteristics of the reinsurers to minimise its exposure from reinsurer insolvencies. At 31 December 2012 the reinsurers' share of insurance contract liabilities was £6,859 million (2011: £1,344 million). The increase arises from the acquisition of REALIC. Further details are shown in note D3(f) and I1. At 31 December 2012, 97 per cent (2011: 91 per cent) of the reinsurance recoverable insurance assets were ceded by the Group's UK and US operations, of which 92 per cent (2011: 94 per cent) of the balance were from reinsurers with Standard & Poor's rating A- and above.

(c) Guarantees

Notes D2(d), D3(d) and D4(d) provide details of guarantee features of the Group's life assurance products. In the UK, guarantees of the with-profits products are valued for accounting purposes on a market consistent basis for 2012 as described in section D2(e)(ii). The UK business also has products with guaranteed annuity option features, mostly within Scottish Amicable Insurance Fund (SAIF), as described in section D2(d). There is little exposure to financial options and guarantees in the shareholder-backed business of the UK operations. The US business annuity products have a variety of option and guarantee features as described in section D3(d). Jackson's derivative programme seeks to manage the exposures as described in section D3(h).

(d) Sensitivity of EEV shareholders' basis profit and equity to market and other risks

The Group prepares supplementary EEV basis financial statements for half-yearly and annual publication. These statements include sensitivity disclosures which are part of the market risk information provided to key management.

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D: Life assurance business (Continued)

(e) Sensitivity of IFRS basis profit or loss and shareholders' equity to market and other risks

(i) Overview of risks by business unit

The financial and insurance assets and liabilities attaching to the Group's life assurance business are, to varying degrees, subject to market and insurance risk and other changes of experience assumptions that may have a material effect on IFRS basis profit or loss and shareholders' equity.

Market risk is the risk that the fair value or future cash flows of a financial instrument or, in the case of liabilities of insurance contracts, their carrying value will fluctuate because of changes in market prices. Market risk comprises three types of risk, namely:

Currency risk: due to changes in foreign exchange rates;

Interest rate risk: due to changes in market interest rates; and

Other price risk: due to fluctuations in market prices (other than those arising from interest rate risk or currency risk).

Policyholder liabilities relating to the Group's life assurance businesses are also sensitive to the effects of other changes in experience, or expected future experience, such as for mortality, other insurance risk and lapse risk.

Three key points are to be noted, namely:

The Group's with-profits and unit-linked funds absorb most market risk attaching to the funds' investments. Except for second order effects, for example on asset management fees and shareholders' share of cost of bonuses for with-profits business, shareholder results are not directly affected by market value movements on the assets of these funds;

The Group's shareholder results are most sensitive to market risks for assets of the shareholder-backed business; and

The main exposures of the Group's IFRS basis results to market risk for its life assurance operations on investments of the shareholder-backed business are for debt securities.

The most significant items for which the IFRS shareholders' profit or loss and shareholders' equity for the Group's life assurance business is sensitive to these variables are shown in the following tables. The distinction between direct and indirect exposure is not intended to indicate the relative size of the sensitivity.

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D: Life assurance business (Continued)

	Market and credit risk			
Type of business	**Investments/ derivatives**	**Liabilities/ unallocated surplus**	**Other exposure**	**Insurance and lapse risk**
UK insurance operations (see also section D2(h))				
With-profits business (including Prudential Annuities Limited)	Net neutral direct exposure (Indirect exposure only)		Investment performance subject to smoothing through declared bonuses	Persistency risk to future shareholder transfers
SAIF sub-fund	Net neutral direct exposure (Indirect exposure only)		Asset management fees earned by M&G	
Unit-linked business	Net neutral direct exposure (Indirect exposure only)		Investment performance through asset management fees	Persistency risk
	Asset/liability mismatch risk			
Shareholder-backed annuity business	Credit risk for assets covering liabilities and shareholder capital			Mortality experience and assumptions for longevity
	Interest rate risk for assets in excess of liabilities ie assets representing shareholder capital			
US insurance operations (see also section D3(h))				
All business	Currency risk			Persistency risk
Variable annuity business	Net effect of market risk arising from incidence of guarantee features and variability of asset management fees offset by derivative hedging programme			
Fixed indexed annuity business	Derivative hedge programme to the extent not fully	Incidence of equity participation features		

	hedged against liability and fund performance			
Fixed indexed annuities, Fixed annuities and GIC business	Credit risk Interest rate risk Profit and loss and shareholders' equity are volatile for these risks as they affect the values of derivatives and embedded derivatives and impairment losses. In addition, shareholders' equity is volatile for the incidence of these risks on unrealised appreciation of fixed income securities classified as available-for-sale under IAS 39		Spread difference between earned rate and rate credited to policyholders	Lapse risk, but the effects of extreme events are mitigated by the application of market value adjustments and by the use of swaption contracts
Asia insurance operations (see also section D4(h))				
All business	Currency risk			Mortality and morbidity risk Persistency risk
With-profits business	Net neutral direct exposure (Indirect exposure only)		Investment performance subject to smoothing through declared bonuses	
Unit-linked business	Net neutral direct exposure (Indirect exposure only)		Investment performance through asset management fees	
	Asset/liability mismatch risk			
Non-participating business	Credit risk	Interest rates for those operations where the basis of insurance liabilities is sensitive to current market		

	movements
Interest rate and price risk	

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(ii) IFRS shareholder results Exposures for market and other risk

Key Group exposures

Detailed analyses of sensitivity of IFRS basis profit or loss and shareholders' equity to key market and other risks are provided in notes D2(h), D3(h), D4(h) and E4. The sensitivity analyses provided show the effect on profit or loss and shareholders' equity to changes in the relevant risk variables, all of which are reasonably possible at the relevant balance sheet date. Other features to note are as follows.

UK

The IFRS operating profit based on longer-term investment returns for UK insurance operations has high potential sensitivity for changes to longevity assumptions affecting the carrying value of liabilities to policyholders for UK shareholder-backed annuity business. At the total IFRS profit level the result is particularly sensitive to temporary value movements on assets backing US and Asia policyholder liabilities (which in general are measured on a basis that is insensitive to current market movements) and shareholder equity.

US

For Jackson at the level of operating profit based on longer-term investment returns, the results are sensitive to market conditions to the extent of income earned on spread-based products and second order equity-based exposure in respect of variable annuity asset management fees. Further information is given below in note D3h(iv).

Jackson's derivative programme is used to manage interest rate risk associated with a broad range of products and equity market risk attaching to its equity-based products. Movements in equity markets, interest rates and credit spreads materially affect the carrying value of derivatives which are used to manage the liabilities to policyholders and backing investment assets. Combined with the use of US GAAP measurement (as 'grandfathered' under IFRS 4) for the insurance contracts assets and liabilities which is largely insensitive to current period market movements, the Jackson total profit (ie including short-term fluctuations in investment returns) is very sensitive to market movements. In addition to these effects the Jackson shareholders' equity is sensitive to the impact of interest rate and credit spread movements on the value of fixed income securities. Movements in unrealised appreciation on these securities are included as movement in shareholders' equity (ie outside the income statement). See D3(h) for details of the hedging.

Asia

For Asia operations, the operating profit based on longer-term investment returns is mainly affected by the impact of market levels on unit-linked business persistency, and other insurance risks.

At the total IFRS profit level the Asia result is affected by short-term value movements on the asset portfolio for non-linked shareholder-backed business.

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Impact of diversification on risk exposure

The Group enjoys significant diversification benefits. This arises because not all risk scenarios will happen at the same time and across all geographic regions. Relevant correlation factors include:

Correlation across geographic regions

- Financial risk factors
- Non-financial risk factors

Correlation across risk factors

- Longevity risk
- Expenses
- Persistency
- Other risks

The effect of Group diversification across the Group's life businesses is to significantly reduce the aggregate standalone volatility risk to IFRS operating profit based on longer-term investment returns. The effect is almost wholly explained by the correlations across risk types, in particular longevity risk.

(f) Duration of liabilities

Under the terms of the Group's contracts, as for life assurance contracts generally, the contractual maturity date is the earlier of the end of the contract term, death, other insurable events or surrender. The Group has therefore chosen to provide details of liability duration that reflect the actuarially determined best estimate of the likely incidence of these factors on contract duration. Details are shown in sections D2(i), D3(i) and D4(i).

In the years 2008 to 2012, claims paid on the Group's life assurance contracts including those classified as investment contracts under IFRS 4 ranged from £17 billion to £21 billion. Indicatively, it is to be expected that, of the Group's policyholder liabilities (excluding unallocated surplus) at 31 December 2012 of £260.8 billion, the amounts likely to be paid in 2013 will be of a similar magnitude.

D2: UK insurance operations

(a) Summary statement of financial position

In order to show the statement of financial position by reference to the differing degrees of policyholder and shareholder economic interest of the different types of fund and business, the analysis below is structured to show separately assets and liabilities of the Scottish Amicable Insurance Fund (SAIF), the PAC with-profits sub-fund (WPSF), unit-linked assets and liabilities and annuity (principally PRIL) and other long-term business.

£97 billion of the £150 billion of investments are held by SAIF and the PAC WPSF. Shareholders are exposed only indirectly to value movements on these assets.

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	31 Dec 2012 £m						31 Dec 2011 £m
		Other funds and subsidiaries					
By operating segment	**Scottish Amicable Insurance Fund note (iii)**	**PAC with-profits fund notes (i), (ii)**	**Unit-linked assets and liabilities**	**Annuity and other long-term business**	**Total**	**UK insurance operations Total**	**UK insurance operations Total**
Assets							
Intangible assets attributable to shareholders:							
Deferred acquisition costs and other intangible assets				**105**	**105**	**105**	113
Total				**105**	**105**	**105**	113
Intangible assets attributable to with-profits funds:							
In respect of acquired subsidiaries for venture fund and other investment purposes		**178**				**178**	178
Deferred acquisition costs		**6**				**6**	6
Total		**184**				**184**	184
Total intangible assets		**184**		**105**	**105**	**289**	297
Deferred tax assets	**1**	**113**		**69**	**69**	**183**	231
Other non-investment and non-cash assets	**369**	**2,440**	**385**	**2,230**	**2,615**	**5,424**	4,771
Investments of long-term business and other operations:							
Investment properties[note (iv)]	**500**	**8,159**	**622**	**1,571**	**2,193**	**10,852**	10,712
Associate investments accounted for using the equity method				**72**	**72**	**72**	70
Financial investments:							
Loans[note (v)]	**116**	**1,993**		**1,264**	**1,264**	**3,373**	3,115
Equity securities and portfolio holdings in unit trusts	**2,070**	**19,875**	**14,071**	**11**	**14,082**	**36,027**	36,722
Debt securities	**3,864**	**46,643**	**6,310**	**27,045**	**33,355**	**83,862**	77,953
Other investments[note (vi)]	**283**	**3,958**	**10**	**325**	**335**	**4,576**	4,568
Deposits	**910**	**8,395**	**822**	**1,004**	**1,826**	**11,131**	9,287

Total investments	**7,743**	**89,023**	**21,835**	**31,292**	**53,127**	**149,893**	142,427
Properties held for sale		**98**				**98**	
Cash and cash equivalents	**120**	**1,077**	**889**	**552**	**1,441**	**2,638**	2,965
Total assets	**8,233**	**92,935**	**23,109**	**34,248**	**57,357**	**158,525**	150,691

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	31 Dec 2012 £m						31 Dec 2011 £m
		Other funds and subsidiaries					
By operating segment	**Scottish Amicable Insurance Fund note (iii)**	**PAC with-profits fund notes (i), (ii)**	**Unit-linked assets and liabilities**	**Annuity and other long-term business**	**Total**	**UK insurance operations Total**	**UK insurance operations Total**
Equity and liabilities							
Equity							
Shareholders' equity				**3,033**	**3,033**	**3,033**	2,581
Non-controlling interests		**1**				**1**	33
Total equity		**1**		**3,033**	**3,033**	**3,034**	2,614
Liabilities							
Policyholder liabilities and unallocated surplus of with-profits funds:							
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	**7,878**	**76,529**	**22,197**	**27,308**	**49,505**	**133,912**	127,024
Unallocated surplus of with-profits funds (reflecting application of 'realistic' basis provisions for UK regulated with-profits funds)		**10,526**				**10,526**	9,165
Total	**7,878**	**87,055**	**22,197**	**27,308**	**49,505**	**144,438**	136,189
Operational borrowings attributable to shareholder-financed operations			**1**	**126**	**127**	**127**	103
Borrowings attributable to with-profits funds	**17**	**1,016**				**1,033**	972
Deferred tax liabilities	**39**	**663**		**483**	**483**	**1,185**	1,349
Other non-insurance liabilities	**299**	**4,200**	**911**	**3,298**	**4,209**	**8,708**	9,464
Total liabilities	**8,233**	**92,934**	**23,109**	**31,215**	**54,324**	**155,491**	148,077
Total equity and liabilities	**8,233**	**92,935**	**23,109**	**34,248**	**57,357**	**158,525**	150,691

Notes

(i)

For the purposes of this table and subsequent explanation, references to the WPSF also include, for convenience, the amounts attaching to the Defined Charges Participating Sub-fund which comprises 3.3 per cent of the total assets of the WPSF and includes the with-profits annuity business transferred to Prudential from the Equitable Life Assurance Society on 1 December 2007 (with assets of approximately £1.7 billion). Profits to shareholders on this with-profits annuity business emerge on a 'charges less expenses' basis and policyholders are entitled to 100 per cent of the investment earnings.

Included in the PAC with-profits fund is £13.3 billion (2011: £12.6 billion) of non-profits annuities liabilities.

(ii)

Excluding policyholder liabilities of the Hong Kong branch of PAC.

(iii)

SAIF is a separate sub-fund within the PAC long-term business fund.

(iv)

Investment properties

At 31 December 2012, the Group's UK insurance operations had £10,852 million (2011: £10,712 million) of investment

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properties. The following table shows the property portfolio by type of investment. The properties are shown at market value below in accordance with the policies described in note A3.

	2012		2011	
	£m	%	£m	%
Office buildings	**4,195**	**38.7**	4,443	41.5
Shopping centres/commercial	**4,389**	**40.4**	4,315	40.3
Retail warehouses/industrial	**1,624**	**15.0**	1,406	13.1
Development	**465**	**4.3**	383	3.6
Other	**179**	**1.6**	165	1.5
Total	**10,852**	**100.0**	10,712	100.0

47.6 per cent (2011: 42.9 per cent) of the UK held investment property is located in London and Southeast England with 35.4 per cent (2011: 41.1 per cent) located throughout the rest of the UK and the remaining 17.0 per cent (2011: 16.0 per cent) located overseas.

(v)

Loans

The loans of the Group's UK insurance operations comprise:

	2012	2011
	£m	£m
SAIF and PAC WPSF:		
Mortgage loans*	**1,311**	1,036
Policy loans	**16**	20
Other loans**	**782**	917
Total SAIF and PAC WPSF loans	**2,109**	1,973
Shareholder-backed:		
Mortgage loans*	**1,259**	1,137
Other loans	**5**	5
Total shareholder-backed loans	**1,264**	1,142
Total UK insurance operations loans	**3,373**	3,115

*

The mortgage loans are collateralised by properties. By carrying value, 86 per cent of the £1,259 million held for shareholder-backed business relates to lifetime (equity release) mortgage business which has an average loan to property value of 29 per cent.

**

Other loans held by the PAC with-profits fund are all commercial loans and comprise mainly syndicated loans.

(vi)

Other investments comprise:

	2012	2011
	£m	£m
Derivative assets*	**1,349**	1,461
Partnerships in investment pools and other**	**3,227**	3,107
	4,576	4,568

*

After including derivative liabilities of £1,007 million (2011: £1,298 million), which are also included in the statement of financial position, the overall derivative position was a net asset of £342 million (2011: £163 million).

**

Partnerships in investment pools and other comprise mainly investments held by the PAC with-profits fund. These investments are primarily investments in limited partnerships and additionally, investments in property funds.

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(b) Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of UK insurance operations from the beginning of the year to the end of the year is as follows:

	SAIF and PAC with-profits sub-fund	Other shareholder-backed funds and subsidiaries: Unit-linked liabilities	Other shareholder-backed funds and subsidiaries: Annuity and other long-term business	Total
	£m	£m	£m	£m
At 1 January 2011	91,773	21,671	22,273	135,717
Comprising:				
Policyholder liabilities	81,586	21,671	22,273	125,530
Unallocated surplus of with-profits funds	10,187			10,187
Premiums	3,413	1,854	1,721	6,988
Surrenders	(2,285)	(1,851)	(119)	(4,255)
Maturities/Deaths	(5,551)	(655)	(1,607)	(7,813)
Net flows[note (a)]	(4,423)	(652)	(5)	(5,080)
Shareholders' transfers post tax	(216)			(216)
Switches	(237)	237		
Investment-related items and other movements[note (b)]	3,338	25	2,499	5,862
Foreign exchange translation differences	(94)			(94)
At 31 December 2011 / 1 January 2012	**90,141**	**21,281**	**24,767**	**136,189**
Comprising:				
Policyholder liabilities	**80,976**	**21,281**	**24,767**	**127,024**

Unallocated surplus of with-profits funds	**9,165**			**9,165**
Premiums	**4,539**	**1,775**	**2,026**	**8,340**
Surrenders	**(2,200)**	**(2,378)**	**(207)**	**(4,785)**
Maturities/Deaths	**(5,664)**	**(658)**	**(1,687)**	**(8,009)**
Net flows[note (a)]	**(3,325)**	**(1,261)**	**132**	**(4,454)**
Shareholders' transfers post tax	**(205)**			**(205)**
Switches	**(236)**	**236**		
Investment-related items and other movements[note (b)]	**8,656**	**1,941**	**2,409**	**13,006**
Foreign exchange translation differences	**(98)**			**(98)**
At 31 December 2012	**94,933**	**22,197**	**27,308**	**144,438**
Comprising:				
Policyholder liabilities	**84,407**	**22,197**	**27,308**	**133,912**
Unallocated surplus of with-profits funds	**10,526**			**10,526**
Average policyholder liability balances*				
2012	**82,691**	**21,739**	**26,038**	**130,468**
2011	81,281	21,476	23,520	126,277

* Averages have been based on opening and closing balances and exclude unallocated surplus of with-profits funds.

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Notes

(a)

Net outflows decreased from £5,080 million in 2011 to £4,454 million in 2012. An improvement in the net outflows of the with-profits business, following increased sales of with-profits bonds in the year, has been greater than the increase in outflows in the unit-linked business. The levels of inflows/outflows for unit-linked business is driven by the activity of corporate pension schemes with transfers in or out from only one or two schemes influencing the level of flows in the year. The net flows of negative £1,261 million in unit-linked business was a result of lower single premiums in and higher transfers out of this business in 2012.

(b)

Investment-related items and other movements of £13,006 million across fund types reflected the continued strong performance of UK equity markets in 2012, as well as investment gains from debt securities following falling bond yields, and other asset classes.

(c) Information on credit risk of debt securities

The following table summarises by rating the securities held by UK insurance operations as at 31 December 2012 and 2011:

(i)

UK insurance operations

	31 Dec 2012 £m						31 Dec 2011 £m
			Other funds and subsidiaries				
	Scottish Amicable Insurance Fund	PAC with-profits fund	Unit-linked assets	PRIL	Other annuity and long-term business	Total	Total
S&P AAA	**441**	**4,716**	**582**	**3,023**	**438**	**9,200**	9,928
S&P AA+ to AA-	**527**	**4,908**	**829**	**3,041**	**318**	**9,623**	8,647
S&P A+ to A-	**1,031**	**12,345**	**1,805**	**6,934**	**885**	**23,000**	21,474
S&P BBB+ to BBB-	**911**	**10,614**	**1,340**	**4,210**	**645**	**17,720**	15,746
S&P Other	**224**	**2,358**	**115**	**307**	**39**	**3,043**	3,175
	3,134	**34,941**	**4,671**	**17,515**	**2,325**	**62,586**	58,970
Moody's Aaa	**241**	**3,780**	**1,239**	**2,557**	**629**	**8,446**	7,945
Moody's Aa1 to Aa3	**41**	**538**	**106**	**622**	**113**	**1,420**	651
Moody's A1 to A3	**32**	**505**	**26**	**321**	**43**	**927**	1,008
Moody's Baa1 to Baa3	**54**	**818**	**113**	**370**	**30**	**1,385**	1,030
Moody's Other	**15**	**224**	**30**	**30**	**8**	**307**	242
	383	**5,865**	**1,514**	**3,900**	**823**	**12,485**	10,876

Fitch	**20**	**295**	**26**	**165**	**21**	**527**	492
Other	**327**	**5,542**	**99**	**2,157**	**139**	**8,264**	7,615
Total debt securities	**3,864**	**46,643**	**6,310**	**23,737**	**3,308**	**83,862**	77,953

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Where no external ratings are available, internal ratings produced by the Group's asset management operation, which are prepared on the Company's assessment of a comparable basis to external ratings, are used where possible. The £8,264 million total debt securities held at 31 December 2012 (2011: £7,615 million) which are not externally rated are either internally rated or unrated. These are analysed as follows:

	2012	2011
	£m	£m
Internal ratings or unrated:		
AAA to A-	**3,150**	2,726
BBB to B-	**3,752**	3,773
Below B- or unrated	**1,362**	1,116
Total	**8,264**	7,615

The majority of unrated debt security investments were held in SAIF and the PAC with-profits sub-fund and relate to convertible debt and other investments which are not covered by ratings analysts nor have an internal rating attributed to them. Of the £2,296 million PRIL and other annuity and long-term business investments which are not externally rated, £6 million were internally rated AAA, £429 million AA, £737 million A, £895 million BBB, £115 million BB and £114 million were internally rated B+ and below or unrated.

During 2011 Standard and Poor's withdrew its ratings of debt securities issued by a number of Sovereigns. Where these are no longer available Moody's ratings have been used. This primarily impacts the UK and Asia insurance operations.

As detailed in note D2(h) below, the primary sensitivity of IFRS basis profit or loss and shareholders' equity relates to non-linked shareholder-backed business which is represented by 'PRIL' and 'other annuity and long-term business' in the table above.

(d) Products and guarantees

Prudential's long-term products in the UK consist of life insurance, pension products and pension annuities.

These products are written primarily in:

One of three separate sub-funds of the PAC long-term fund, namely the with-profits sub-fund (WPSF), SAIF, and the non-profit sub-fund;

Prudential Annuities Limited (PAL), which is owned by the PAC with-profits sub-fund;

Prudential Retirement Income Limited (PRIL), a shareholder-owned subsidiary; or

Other shareholder-backed subsidiaries writing mainly non-profit unit-linked business.

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(i) With-profits products and PAC with-profits sub-fund

Within the statement of financial position of UK insurance operations at 31 December 2012, as shown in note D2(a), there are policyholder liabilities and unallocated surplus of £87.1 billion (2011: £81.6 billion) that relate to the WPSF. These amounts include the liabilities and capital of Prudential Annuities Limited, a wholly owned subsidiary of the fund. The WPSF mainly contains with-profits business but it also contains some non-profit business (unit-linked, term assurances and annuities). The WPSF's profits are apportioned 90 per cent to its policyholders and 10 per cent to shareholders as surplus for distribution is determined via the annual actuarial valuation.

The WPSF held a provision of £47 million at 31 December 2012 (2011: £90 million) to honour guarantees on a small amount of guaranteed annuity products. SAIF's exposure to guaranteed annuities is described below.

With-profits products provide returns to policyholders through bonuses that are 'smoothed'. There are two types of bonuses: 'annual' and 'final'. Annual bonuses are declared once a year, and once credited, are guaranteed in accordance with the terms of the particular product. Unlike annual bonuses, final bonuses are guaranteed only until the next bonus declaration.

The main factors that influence the determination of bonus rates are the return on the investments of the with-profits fund, inflation, taxation, the expenses of the fund chargeable to policyholders and the degree to which investment returns are smoothed. The overall rate of return earned on investments and the expectation of future investment returns are the most important influences on bonus rates.

A high proportion of the assets backing the with-profits business are invested in equities and real estate. If the financial strength of the with-profits business is affected, then a higher proportion of fixed interest or similar assets might be held by the fund.

Further details on the determination of the two types of the bonuses: 'regular' and 'final', the application of significant judgement, key assumptions and the degree of smoothing of investment returns in determining the bonus rates are provided below.

Regular bonus rates

For regular bonuses, the bonus rates are determined for each type of policy primarily by targeting the bonus level at a prudent proportion of the long-term expected future investment return on underlying assets. The expected future investment return is reduced as appropriate for each type of policy to allow for items such as expenses, charges, tax and shareholders' transfers. However, the rates declared may differ by product type, or by the date of payment of the premium, or date of issue of the policy, or if the accumulated annual bonuses are particularly high or low, relative to a prudent proportion of the achieved investment return.

When target bonus levels change the PAC board of directors (PAC Board) has regard to the overall strength of the long-term fund when determining the length of time over which it will seek to achieve the amended prudent target bonus level.

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In normal investment conditions, PAC expects changes in regular bonus rates to be gradual over time. However, the PAC Directors retain the discretion whether or not to declare a regular bonus each year, and there is no limit on the amount by which regular bonus rates can change.

Final bonus rates

A final bonus which is normally declared yearly, may be added when a claim is paid or when units of a unitised product are realised.

The rates of final bonus usually vary by type of policy and by reference to the period, usually a year, in which the policy commences or each premium is paid. These rates are determined by reference to the asset shares for the sample policies but subject to the smoothing approach as explained below.

In general, the same final bonus scale applies to maturity, death and surrender claims except that:

The total surrender value may be impacted by the application of a Market Value Reduction for accumulating with-profits policies and is the surrender bases for conventional with-profits business; and

For the SAIF and Scottish Amicable, the final bonus rates applicable on surrender may be adjusted to reflect expected future bonus rates.

Application of significant judgement

The application of the above method for determining bonuses requires the PAC Board to apply significant judgement in many respects, including in particular the following:

Determining what constitutes fair treatment of customers: Prudential is required by UK law and regulation to consider the fair treatment of its customers in setting bonus levels. The concept of determining what constitutes fair treatment, while established by statute, is not defined;

Smoothing of investment returns: This is an important feature of with-profits products. Determining when particular circumstances, such as a significant rise or fall in market values, warrant variations in the standard bonus smoothing limits that apply in normal circumstances requires the PAC Board to exercise significant judgement; and

Determining at what level to set bonuses to ensure that they are competitive: The overall return to policyholders is an important competitive measure for attracting new business.

Key assumptions

As noted above, the overall rate of return on investments and the expectation of future investment returns are the most important influences in bonus rates, subject to the smoothing described below. Prudential determines the assumptions to apply in respect of these factors, including the effects of reasonably likely changes in key assumptions, in the context of the overarching discretionary and smoothing framework that applies to its with-profits business as described above. As such, it is not possible to specifically quantify the effects of each of these assumptions, or of reasonably likely changes in these assumptions.

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Prudential's approach, in applying significant judgement and discretion in relation to determining bonus rates, is consistent conceptually with the approach adopted by other firms that manage a with-profits business. It is also consistent with the requirements of UK law, which require all UK firms that carry out a with-profits business to define, and make publicly available, the Principles and Practices of Financial Management (PPFM) that are applied in the management of their with-profits funds.

Accordingly, Prudential's PPFM contains an explanation of how it determines regular and final bonus rates within the discretionary framework that applies to all with-profits policies, subject to the general legislative requirements applicable. The purpose of Prudential's PPFM is therefore to:

- explain the nature and extent of the discretion available,
- show how competing or conflicting interests or expectations of different groups and generations of policyholders, and policyholders and shareholders are managed so that all policyholders and shareholders are treated fairly, and
- provide a knowledgeable observer (eg a financial adviser) with an understanding of the material risks and rewards from starting and continuing to invest in a with-profits policy with Prudential.

Furthermore, in accordance with industry-wide regulatory requirements, the PAC Board has appointed:

- an Actuarial Function Holder who provides the PAC Board with all actuarial advice;
- a With-Profits Actuary whose specific duty is to advise the PAC Board on the reasonableness and proportionality of the manner in which its discretion has been exercised in applying the PPFM and the manner in which any conflicting interests have been addressed; and
- a With-Profits Committee of independent individuals, which assesses the degree of compliance with the PPFM and the manner in which conflicting rights have been addressed.

Smoothing of investment return

In determining bonus rates for the UK with-profits policies, smoothing is applied to the allocation of the overall earnings of the UK with-profits fund of which the investment return is a significant element. The smoothing approach differs between accumulating and conventional with-profits policies to reflect the different contract features. In normal circumstances, Prudential does not expect most payout values on policies of the same duration to change by more than 10 per cent up or down from one year to the next, although some larger changes may occur to balance payout values between different policies. Greater flexibility may be required in certain circumstances, for example following a significant rise or fall in market values, and in such situations the PAC Board may decide to vary the standard bonus smoothing limits in order to protect the overall interests of policyholders.

The degree of smoothing is illustrated numerically by comparing in the following table the relatively 'smoothed' level of policyholder bonuses declared as part of the surplus for distribution, with the more

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volatile movement in investment return and other items of income and expenditure of the UK component of the PAC with-profits fund for each year presented.

	2012	2011	2010
	£m	£m	£m
Net income of the fund:			
Investment return	**8,350**	4,094	8,815
Claims incurred	**(6,857)**	(6,411)	(6,390)
Movement in policyholder liabilities	**(3,989)**	(614)	(4,301)
Add back policyholder bonuses for the year (as shown below)	**1,865**	1,945	2,019
Claims incurred and movement in policyholder liabilities (including charge for provision for asset shares and excluding policyholder bonuses)	**(8,981)**	(5,080)	(8,672)
Earned premiums, net of reinsurance	**4,558**	3,404	3,148
Other income	**39**	17	9
Acquisition costs and other expenditure	**(740)**	(696)	(600)
Tax charge	**(292)**	(63)	(528)
Net income of the fund before movement in unallocated surplus	**2,934**	1,676	2,172
Movement in unallocated surplus	**(863)**	485	70
Surplus for distribution	**2,071**	2,161	2,242
Surplus for distribution allocated as follows:			
90% policyholders' bonus (as shown above)	**1,865**	1,945	2,019
10% shareholders' transfers	**206**	216	223
	2,071	2,161	2,242

(ii) Annuity business

Prudential's conventional annuities include level, fixed-increase and inflation-linked annuities, the link being to the Retail Prices Index (RPI) in the majority of cases. They are mainly written within the subsidiaries PAL, PRIL, the PAC non profit sub-fund and the PAC with-profits sub-fund, but there are some annuity liabilities in Prudential Pensions Limited and SAIF.

Prudential's fixed-increase annuities incorporate automatic increases in annuity payments by fixed amounts over the policyholder's life. The RPI annuities that Prudential offers provide for a regular annuity payment to which an additional amount is added periodically based on the increase in the UK RPI.

Prudential's with-profits annuities, which are written in the WPSF, combine the income features of annuity products with the investment smoothing features of with-profits products and enable policyholders to obtain exposure to investment return on the WPSF's equity shares, property and other investment categories over time. Policyholders select a "required smoothed return" bonus from the specific range Prudential offers for the particular product. The amount of the annuity payment each year

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depends upon the relationship between the required smoothed return bonus rate selected by the policyholder when the product is purchased and the smoothed return bonus rates Prudential subsequently declares each year during the term of the product. If the total bonus rates fall below the anticipated rate, then the annuity income falls.

At 31 December 2012, £41.7 billion (2011: £38.3 billion) of investments relate to non-profit annuity business of the PAC WPSF (including PAL) and the annuity business of PRIL. These investments are predominantly in debt securities (including retail price index-linked bonds to match retail price index-linked annuities), loans, deposits and property, and are duration matched with the estimated duration of the liabilities they support.

(iii) SAIF

SAIF is a ring-fenced sub-fund of the PAC long-term fund formed following the acquisition of the mutually owned Scottish Amicable Life Assurance Society in 1997. No new business may be written in SAIF, although regular premiums are still being paid on policies in force at the time of the acquisition and incremental premiums are permitted on these policies.

The fund is solely for the benefit of policyholders of SAIF. Shareholders have no interest in the profits of this fund although they are entitled to asset management fees on this business.

The process for determining policyholder bonuses of SAIF with-profits policies, which constitute the vast majority of obligations of the funds, is similar to that for the with-profits policies of the WPSF. However, in addition, the surplus assets in SAIF are allocated to policies in an orderly and equitable distribution over time as enhancements to policyholder benefits ie in excess of those based on asset share.

Provision is made for the risks attaching to some SAIF unitised with-profits policies that have (Market Value Reduction) MVR-free dates and for those SAIF products which have a guaranteed minimum benefit on death or maturity of premiums accumulated at 4 per cent per annum.

The Group's main exposure to guaranteed annuities in the UK is through SAIF and a provision of £371 million was held in SAIF at 31 December 2012 (2011: £370 million) to honour the guarantees. As SAIF is a separate sub-fund solely for the benefit of policyholders of SAIF, this provision has no impact on the financial position of the Group's shareholders' equity.

(iv) Unit-linked (non-annuity) and other non-profit business

Prudential UK insurance operations also have an extensive book of unit-linked policies of varying types and provide a range of other non-profit business such as credit life and protection contracts. These contracts do not contain significant financial guarantees.

There are no guaranteed maturity values or guaranteed annuity options on unit-linked policies except for minor amounts for certain policies linked to cash units within SAIF.

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(e) Process for setting assumptions and determining contract liabilities

(i) Overview

The calculation of the contract liabilities involves the setting of assumptions for future experience. This is done following detailed review of the relevant experience including in particular mortality, expenses, tax, economic assumptions and, where applicable, persistency.

For with-profits business written in the WPSF or SAIF, a market consistent valuation is performed (as described in section (ii) below). Additional assumptions required are for persistency and the management actions under which the fund is managed. Assumptions used for a market-consistent valuation typically do not contain margins, whereas those used for the valuation of other classes of business do.

Mortality assumptions are set based on the results of the most recent experience analysis looking at the experience over recent years of the relevant business. For non-profit business, a margin for adverse deviation is added. Different assumptions are applied for different product groups. For annuitant mortality, assumptions for current mortality rates are based on recent experience investigations and expected future improvements in mortality. The expected future improvements are based on recent experience and projections of the business and industry experience generally.

Maintenance and, for some classes of business, termination expense assumptions are expressed as per policy amounts. They are set based on the expenses incurred during the year, including an allowance for ongoing investment expenditure and allocated between entities and product groups in accordance with the operation's internal cost allocation model. For non-profit business a margin for adverse deviation is added to this amount. Expense inflation assumptions are set consistent with the economic basis and based on the difference between yields on nominal gilts and index-linked gilts.

The actual renewal expenses incurred on behalf of SAIF by other Group companies are recharged in full to SAIF.

The assumptions for asset management expenses are based on the charges specified in agreements with the Group's asset management operations, plus a margin for adverse deviation for non-profit business.

Tax assumptions are set equal to current rates of taxation.

For non-profit business excluding unit-linked business, the valuation interest rates used to discount the liabilities are based on the yields as at the valuation date on the assets backing the technical provisions. For fixed interest securities the gross redemption yield is used except for the PAL (including the business recaptured by PAC WPSF in 2011) and PRIL annuity business where the internal rate of return of the assets backing the liabilities is used. Properties are valued using the rental yield, and for equities it is the greater of the dividend yield and the average of the dividend yield and the earnings yield. An adjustment is made to the yield on non-risk-free fixed interest securities and property to reflect credit risk. To calculate the non-unit reserves for linked business, assumptions have been set for the gross unit growth rate and the rate of inflation of maintenance expenses, as well as for the valuation interest rate as described above.

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(ii) WPSF and SAIF

The policyholder liabilities reported for the WPSF are primarily for two broad types of business. These are accumulating and conventional with-profits contracts. The policyholder liabilities of the WPSF are accounted for under FRS 27.

The provisions have been determined on a basis consistent with the detailed methodology included in regulations contained in the FSA's rules for the determination of reserves on the FSA's 'realistic' Peak 2 basis. In aggregate, the regime has the effect of placing a value on the liabilities of UK with-profits contracts, which reflects the amounts expected to be paid based on the current value of investments held by the with-profits funds and current circumstances. These contracts are a combination of insurance and investment contracts with discretionary participation features, as defined by IFRS 4.

The FSA's Peak 2 calculation under the realistic regime requirement is explained further in note A3 (2)(a) under the UK regulated with-profits section.

The contract liabilities for with-profits business also require assumptions for persistency. These are set based on the results of recent experience analysis.

(iii) Annuity business

Credit risk provisions

For IFRS reporting, the results for UK shareholder-backed annuity business are particularly sensitive to the allowances made for credit risk. The allowance is reflected in the deduction from the valuation rate of interest for discounting projected future annuity payments to policyholders that would have otherwise applied. Since mid-2007 there has been a significant increase in the actual and perceived credit risk associated with corporate bonds as reflected in the significant widening that has occurred in corporate bond spreads. Although bond spreads over swap rates have narrowed from their peak in March 2009, they are still high compared with the levels seen in the years immediately preceding the start of the dislocated markets in 2007. The allowance that should therefore be made for credit risk remains a particular area of judgement.

The additional yield received on corporate bonds relative to swaps can be broken into the following constituent parts:

(a) the expected level of future defaults,

(b) the credit risk premium that is required to compensate for the potential volatility in default levels,

(c) the liquidity premium that is required to compensate for the lower liquidity of corporate bonds relative to swaps, and

(d) the mark to market risk premium that is required to compensate for the potential volatility in corporate bond spreads (and hence market values) at the time of sale.

The sum of (c) and (d) is often referred to as 'liquidity premium'.

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The allowance for credit risk comprises (i) an amount for long-term best estimate defaults, and (ii) additional provisions for credit risk premium, downgrade resilience and short-term defaults.

The weighted components of the bond spread over swap rates for shareholder-backed fixed and linked annuity business for PRIL at 31 December 2012 , 31 December 2011 and 31 December 2010, based on the asset mix at the relevant balance sheet date are shown below.

31 December 2012	Pillar 1 regulatory basis	Adjustment from regulatory to IFRS basis	IFRS
	(bps)	(bps)	(bps)
Bond spread over swap rates[note (i)]	**161**		161
Credit risk allowance			
Long-term expected defaults[note (ii)]	**15**		15
Additional provisions[note (iii)]	**50**	(23)	27
Total credit risk allowance	**65**	(23)	42
Liquidity premium	**96**	23	119

31 December 2011	Pillar 1 regulatory basis	Adjustment from regulatory to IFRS basis	IFRS
	(bps)	(bps)	(bps)
Bond spread over swap rates[note (i)]	201		201
Credit risk allowance			
Long-term expected defaults[note (ii)]	15		15
Additional provisions[note (iii)]	51	(24)	27
Total credit risk allowance	66	(24)	42
Liquidity premium	135	24	159

31 December 2010	Pillar 1 regulatory basis	Adjustment from regulatory to IFRS basis	IFRS
	(bps)	(bps)	(bps)
Bond spread over swap rates[note (i)]	160		160
Credit risk allowance			
Long-term expected defaults[note (ii)]	16		16
Additional provisions[note (iii)]	52	(26)	26
Total credit risk allowance	68	(26)	42
Liquidity premium	92	26	118

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(i) Bond spread over swap rates reflect market observed data.

(ii) Long-term expected defaults are derived by applying Moody's data from 1970 to 2009 and the definition of the credit rating used is the second highest credit rating published by Moody's, Standard and Poor's and Fitch.

(iii) Additional provisions comprise credit risk premium, which is derived from Moody's data from 1970 to 2009, an allowance for a one-notch downgrade of the portfolio subject to credit risk and an additional allowance for short-term defaults.

The prudent Pillar 1 regulatory basis reflects the overriding objective of maintaining sufficient provisions and capital to ensure payments to policyholders can be made. The approach for IFRS aims to establish liabilities that are closer to 'best estimate'.

Movement in the credit risk allowance for PRIL for the year ended 31 December 2012

The movement during 2012 of the average basis points allowance for PRIL on Pillar 1 regulatory and IFRS bases are as follows:

	Pillar 1 Regulatory basis Total (bps)	IFRS Total (bps)
Total allowance for credit risk at 31 December 2011	**66**	**42**
Credit rating changes	**3**	**2**
Asset trading	**1**	**1**
New business and other	**(5)**	**(3)**
Total allowance for credit risk at 31 December 2012	**65**	**42**

For periods prior to full year 2011, favourable credit experience was retained in short-term allowances for credit risk on both the Pillar 1 and IFRS bases. From full year 2011 onwards the methodology applied is to continue to retain such surplus experience in the IFRS credit provisions but not for Pillar 1.

Overall the movement has led to the credit allowance for Pillar 1 purposes to be 40 per cent (2011: 33 per cent) of the bond spread over swap rates. For IFRS purposes it represents 26 per cent (2011: 20 per cent) of the bond spread over swap rates.

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The reserves for credit risk allowance at 31 December 2012 for the UK shareholder annuity fund were as follows:

	Pillar 1 Regulatory basis Total	IFRS Total
	£bn	£bn
PRIL	**1.9**	**1.2**
PAC non-profit sub-fund	**0.2**	**0.1**
Total 31 December 2012	**2.1**	**1.3**
Total 31 December 2011	**2.0**	**1.3**
Total 31 December 2010	**1.8**	**1.1**

Mortality

The mortality assumptions are set in light of recent population and internal experience. The assumptions used are percentages of standard actuarial mortality tables with an allowance for future mortality improvements. Where annuities have been sold on an enhanced basis to impaired lives an additional age adjustment is made. The percentages of the standard table used are selected according to the source of business.

In 2009, Prudential's annuity business liabilities were determined using the Continuous Mortality Investigation (CMI) medium cohort projections with a floor. Since 2009 new mortality projection models have been released annually by the CMI. The CMI 2009 model was used to produce the 2010 and 2011 results, with calibration to reflect an appropriate view of future mortality improvements. The CMI 2011 model was used to produce the 2012 results, again with calibration to reflect an appropriate view of future mortality improvements.

The tables and range of percentages used are set out in the following tables:

	Non-profit annuities within the WPSF (including PAL)		PRIL	
2012	**Males**	**Females**	**Males**	**Females**
In payment	93% 99% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long-term improvement rate	89% 101% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long-term improvement rate	92% 96% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long-term improvement rate	84% 97% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2011 mortality model, with a long-term improvement rate

	of 2.25%.	of 1.50%.	of 2.25%.	of 1.50%.
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

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2011	Non-profit annuities within the WPSF (including PAL)		PRIL	
	Males	Females	Males	Females
In payment	92% 98% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 2.25%.	88% 100% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 1.25%.	93% 94% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 2.25%.	84% 96% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 1.25%.
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

2010	Non-profit annuities within the WPSF (including PAL)		PRIL	
	Males	Females	Males	Females
In payment	92% 98% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 2.25%.	88% 100% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 1.25%.	94% 95% PCMA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 2.25%.	86% 97% PCFA00 with future improvements in line with Prudential's own calibration of the CMI 2009 mortality model, with a long term improvement rate of 1.25%.
In deferment	AM92 minus 4 years	AF92 minus 4 years	AM92 minus 4 years	AF92 minus 4 years

(iv) Unit-linked (non-annuity) and other non-profit business

The majority of other long-term business written in the UK insurance operations is unit-linked business or other business with similar features. For these contracts the attaching liability reflects the unit value obligation and provision for expenses and mortality risk. The latter component is determined by applying mortality assumptions on a basis that is appropriate for the policyholder profile.

For unit-linked business, the assets covering unit liabilities are exposed to market risk, but the residual risk when considering the unit-linked liabilities and assets together is limited to the effect on fund-based charges.

For those contracts where the level of insurance risk is insignificant, the assets and liabilities arising under the contracts are distinguished between those that relate to the financial instrument liability and acquisition costs and deferred income that relate to the component of the contract that relates to investment management. Acquisition costs and deferred income are recognised consistent with the level of service provision in line with the requirements of IAS 18.

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(f) Reinsurance

The Group's UK insurance business cedes only minor amounts of business outside the Group. During 2012, reinsurance premiums for externally ceded business were £135 million (2011: £132 million; 2010: £128 million) and reinsurance recoverable assets were £608 million (2011: £589 million) in aggregate. The gains and losses recognised in profit and loss for the 2012, 2011 and 2010 contracts were immaterial.

(g) Effect of changes in assumptions used to measure insurance assets and liabilities

Credit risk

There has been no change of approach in the setting of assumption levels.

However, changes in the portfolio have given rise to altered levels of credit risk allowance as set out in note D2 (e)(iii).

2012

Other operating assumption changes

In 2012, for the shareholder-backed business, the net effect of assumption changes other than the allowance for credit risk described above was a charge to shareholder results of £17 million. This comprises the aggregate effect of strengthening of mortality assumptions for the annuity business, offsetting releases of margins and altered expenses and other assumptions.

For the with-profits sub-fund, the aggregate effect of assumption changes in 2012 was a net charge to unallocated surplus of £90 million, relating to changes in mortality and offsetting releases of margins, expense, persistency and economic assumptions.

2011

Other operating assumption changes

In 2011, for the shareholder-backed business, the aggregate effect of assumption changes other than the allowance for credit risk described above was a net charge to the shareholder results of £9 million, comprising a number of individually small assumption changes.

For the with-profits sub-fund, the aggregate effect of assumption changes in 2011 was a net charge to unallocated surplus of £59 million, relating to changes in mortality, expense, persistency and economic assumptions.

2010

Other operating assumptions changes

A new mortality projection model was applied in 2010 to determine Prudential's annuity business.

The net effect of applying the new model, releases of margins, and changes to other related mortality assumptions for shareholder-backed business is a credit of £8 million. With a £38 million

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benefit from altered expense assumptions the overall credit for shareholder-backed business is £46 million.

For the with-profits sub-fund, the aggregate effect of assumption changes in 2010 was a net charge to unallocated surplus of £62 million, relating to changes in mortality, expense, persistency and economic assumptions.

(h) Exposure and sensitivity of IFRS basis profit or loss and shareholders' equity to market and other risks

(i) With-profits business

SAIF

Shareholders have no interest in the profits of the ring-fenced fund of SAIF but are entitled to the asset management fees paid on the assets of the fund.

With-profits sub-fund business

Shareholder UK results of UK with-profits business (including non-participating annuity business of the WPSF and of Prudential Annuities Limited (PAL), which is owned by the WPSF) are only sensitive to market risk through the indirect effect of investment performance on declared policyholder bonuses.

The investment assets of PAC with-profits funds are subject to market risk. Changes in their carrying value, net of related changes to asset-share liabilities of with-profit contracts, affect the level of unallocated surplus of the fund. Therefore, the level of unallocated surplus is particularly sensitive to the level of investment returns on the portion of the assets that represents surplus. The effects for 2012 and 2011 are demonstrated in note D5. However, as unallocated surplus is accounted for as a liability under IFRS, movements in its value do not affect shareholders' profit and equity.

The shareholder results of the UK with-profits fund correspond to the shareholders' share of the cost of bonuses declared on the with-profits business which is currently one-ninth of the cost of bonuses declared. Investment performance is a key driver of bonuses, and hence the shareholders' share of the cost of bonuses. Due to the 'smoothed' basis of bonus declaration, the sensitivity to investment performance in a single year is low relative to movements in the period to period performance. However, over multiple periods, it is important.

Mortality and other insurance risk are relatively minor factors in the determination of the bonus rates. Adverse persistency experience can affect the level of profitability from with-profits but in any given one year, the shareholders' share of cost of bonus may only be marginally affected. However, altered persistency trends may affect future expected shareholder transfers.

(ii) Shareholder-backed annuity business

The principal items affecting the IFRS results of the UK shareholder-backed annuity business are mortality experience and assumptions, and credit risk. The assets covering the liabilities are principally debt securities and other investments that are held to match the expected duration and payment

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characteristics of the policyholder liabilities. These liabilities are valued for IFRS reporting purposes by applying discount rates that reflect the market rates of return attaching to the covering assets.

Asset/liability duration matching is reviewed regularly. Except to the extent of any asset/liability duration mismatch and exposure to credit risk, the sensitivity of the Group's results to market risk for movements in the carrying value of the liabilities and covering assets is broadly neutral on a net basis.

The main market risk sensitivity for the UK shareholder-backed annuity business arises from interest rate risk on the debt securities which substantially represent shareholders' equity. This shareholders' equity comprises the net assets held within the long-term fund of the company that cover regulatory basis liabilities that are not recognised for IFRS reporting purposes, for example contingency reserves, and shareholder capital held outside the long-term fund.

In summary, profits from shareholder-backed annuity business are most sensitive to:

The extent to which the duration of the assets held closely matches the expected duration of the liabilities under the contracts;

Actual versus expected default rates on assets held;

The difference between long-term rates of return on corporate bonds and risk-free rates;

The variance between actual and expected mortality experience;

The extent to which changes to the assumed rate of improvements in mortality give rise to changes in the measurement of liabilities; and

Changes in renewal expense levels.

A decrease in assumed mortality rates of 1 per cent would decrease gross profits by approximately £74 million (2011: £64 million; 2010: £53 million). A decrease in credit default assumptions of five basis points would increase gross profits by £157 million (2011: £137 million; 2010: £119 million). A decrease in renewal expenses (excluding asset management expenses) of 5 per cent would increase gross profits by £25 million (2011: £25 million; 2010: £23 million). The effect on profits would be approximately symmetrical for changes in assumptions that are directionally opposite to those explained above.

(iii) Unit-linked and other business

Unit-linked and other business represents a comparatively small proportion of the in-force business of the UK insurance operations.

Due to the matching of policyholder liabilities to attaching asset value movements the UK unit-linked business is not directly affected by market or credit risk liabilities of other business and are also broadly insensitive to market risk. Profits from unit-linked and similar contracts primarily arise from the excess of charges to policyholders for management of assets under the Company's stewardship, over expenses incurred.

The former is most sensitive to the net accretion of funds under management as a function of new business and lapse and timing of death. The accounting impact of the latter is dependent upon the amortisation of acquisition costs in line with the emergence of margins (for insurance contracts) and amortisation in line with service provision (for the investment management component of investment contracts). By virtue of the design features of most of the contracts which

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provide low levels of mortality cover, the profits are relatively insensitive to changes in mortality experience.

(iv) Shareholder exposure to interest rate risk and other market risk

By virtue of the fund structure, product features and basis of accounting, the policyholder liabilities of the UK insurance operations are, except for pension annuity business, not generally exposed to interest rate risk. At 31 December 2012 pension annuity liabilities accounted for 98 per cent (2011: 98 per cent) of UK shareholder-backed business liabilities. For pension annuity business, liabilities are exposed to interest rate risk. However, the net exposure to the PAC WPSF (for PAL) and shareholders (for annuity liabilities of PRIL and the non-profit sub-fund) is very substantially ameliorated by virtue of the close matching of assets with appropriate duration. The level of matching from period to period can vary depending on management actions and economic factors so it is possible for a degree of mis-matching profits or losses to arise.

The close matching by the Group of assets of appropriate duration to annuity liabilities is based on maintaining economic and regulatory capital. The measurement of liabilities under capital reporting requirements and IFRS is not the same with contingency reserves and some other margins for prudence within the assumptions required under the FSA regulatory solvency basis not included for IFRS reporting purposes. As a result IFRS equity is higher than regulatory capital and therefore more sensitive to interest rate and credit risk.

The estimated sensitivity of the UK non-linked shareholder-backed business (principally pension annuities business) to a movement in interest rates is as follows.

	2012				**2011**			
	A decrease of 2%	**A decrease of 1%**	**An increase of 1%**	**An increase of 2%**	**A decrease of 2%**	**A decrease of 1%**	**An increase of 1%**	**An increase of 2%**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Carrying value of debt securities and derivatives	**9,006**	**3,993**	**(3,265)**	**(5,983)**	7,676	3,426	(2,820)	(5,178)
Policyholder liabilities	**(7,878)**	**(3,513)**	**2,867**	**5,235**	(6,842)	(3,060)	2,510	4,593
Related deferred tax effects	**(259)**	**(110)**	**91**	**172**	(208)	(91)	77	146
Net sensitivity of profit after tax and shareholders' equity	**869**	**370**	**(307)**	**(576)**	626	275	(233)	(439)

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In addition the shareholder-backed portfolio of UK non-linked insurance operations covering liabilities and shareholders' equity includes equity securities and investment property. Excluding any second order effects on the measurement of the liabilities for future cash flows to the policyholder, a fall in their value would have given rise to the following effects on pre-tax profit, profit after tax and shareholders' equity.

	2012		2011	
	A decrease of 20%	A decrease of 10%	A decrease of 20%	A decrease of 10%
	£m	£m	£m	£m
Pre-tax profit	**(316)**	**(158)**	(319)	(160)
Related deferred tax effects	**73**	**36**	80	40
Net sensitivity of profit after tax and shareholders' equity	**(243)**	**(122)**	(239)	(120)

A 10 or 20 per cent increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above. The market risk sensitivities shown above reflect the impact of temporary market movements, and, therefore the primary effect of such movements would, in the Group's segmental analysis of profits, be included within the short-term fluctuations in investment returns.

In the equity risk sensitivity analysis shown above, the Group has considered the impact of an instantaneous 20 per cent fall in equity markets. If equity markets were to fall by more than 20 per cent, the Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Group would be able to put in place mitigating management actions.

(i) Duration of liabilities

With the exception of most unitised with-profits bonds and other whole of life contracts the majority of the contracts of the UK insurance operations have a contract term. However, in effect, the maturity term of contracts reflects the earlier of death, maturity, or lapsation. In addition, with-profits contract liabilities as noted in note D2(e) include projected future bonuses based on current investment values. The actual amounts payable will vary with future investment performance of SAIF and the WPSF.

The tables above show the carrying value of the policyholder liabilities. The tables in the accompanying notes below show the maturity profile of the cash flows for insurance contracts, as defined by IFRS, ie those containing significant insurance risk, and investment contracts, which do not.

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	2012									
	With-profits business			Annuity business (Insurance contracts)		Other				
	Insurance contracts	Investment contracts	Total	Non-profit annuities within WPSF (including PAL)	PRIL	Total	Insurance contracts	Investments contracts	Total	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Policyholders liabilities	37,698	33,486	71,184	13,223	20,114	33,337	13,231	16,160	29,391	133,912
	%	%	%	%	%	%	%	%	%	%
Expected maturity:										
0 to 5 years	45	39	42	30	26	27	35	28	31	36
5 to 10 years	24	25	24	24	22	22	25	23	24	24
10 to 15 years	13	17	15	18	17	18	17	17	17	16
15 to 20 years	8	11	10	12	13	13	10	12	11	11
20 to 25 years	5	6	5	8	9	9	6	9	8	7
over 25 years	5	2	4	8	13	11	7	11	9	6

	2011									
	With-profits business			Annuity business (Insurance contracts)		Other				
	Insurance contracts	Investment contracts	Total	Non-profit annuities within WPSF (including PAL)	PRIL	Total	Insurance contracts	Investments contracts	Total	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Policyholder liabilities	38,974	29,365	68,339	12,637	18,236	30,873	12,885	14,927	27,812	127,024
	%	%	%	%	%	%	%	%	%	%

Expected maturity:										
0 to 5 years	47	32	41	29	25	27	34	28	31	35
5 to 10 years	24	26	25	24	22	22	25	22	24	24
10 to 15 years	13	19	16	18	18	18	18	18	18	17
15 to 20 years	8	14	10	12	13	13	11	12	11	11
20 to 25 years	5	7	6	8	10	9	7	9	7	7
over 25 years	3	2	2	9	12	11	5	11	9	6

Notes

(i)

The cash flow projections of expected benefit payments used in the maturity profile table above are from value of in-force business and exclude the value of future new business, including future vesting of internal pension contracts.

(ii)

Benefit payments do not reflect the pattern of bonuses and shareholder transfers in respect of the with-profits business.

(iii)

Investment contracts under 'Other' comprise certain unit-linked and similar contracts accounted for under IAS 39 and IAS 18.

(iv)

For business with no maturity term included within the contracts, for example with-profits investment bonds such as Prudence Bonds, an assumption is made as to likely duration based on prior experience.

(v)

The maturity tables shown above have been prepared on a discounted basis. Details of undiscounted cash flow for investment contracts are shown in note G2.

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D: Life assurance business (Continued)

D3: US insurance operations

(a) Summary results and statement of financial position

(i) Results and movements in shareholders' equity

	2012	2011*	2010*
	£m	£m	£m
Operating profit based on longer-term investment returns	**964**	651	728
Short-term fluctuations in investment returns	**(90)**	(167)	(453)
Amortisation of acquisition accounting adjustments arising on the purchase of REALIC[note I1]	**(19)**		
Profit before shareholder tax	**855**	484	275
Tax	**(234)**	(127)	(54)
Profit for the year	**621**	357	221

	2012	2011*	2010*
	£m	£m	£m
Profit for the year (as above)	**621**	357	221
Items recognised in other comprehensive income:			
Exchange movements	**(181)**	35	74
Unrealised valuation movements on securities classified as available-for sale:			
Unrealised holding gains arising during the year	**930**	912	1,170
Deduct net gains included in the income statement	**(68)**	(101)	51
Total unrealised valuation movements	**862**	811	1,221
Related change in amortisation of deferred acquisition costs	**(270)**	(275)	(410)
Related tax	**(205)**	(187)	(278)
Total other comprehensive income	**206**	384	607
Total comprehensive income for the year	**827**	741	828
Dividends, interest payments to central companies and other movements	**(245)**	(330)	(97)
Net increase in equity	**582**	411	731
Shareholders' equity at beginning of year:			

As previously reported	**4,271**	3,815	3,011
Effect of change in accounting policy for deferred acquisition costs*	**(510)**	(465)	(392)
After effect of change	**3,761**	3,350	2,619
Shareholders' equity at end of year	**4,343**	3,761	3,350

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Included within the movements in shareholders' equity is a net increase in value of Jackson's debt securities classified as 'available-for-sale' under IAS 39 of £862 million (2011: £811 million; 2010: £2,221 million).

With the exception of debt securities for US insurance operations classified as 'available-for-sale' under IAS 39, unrealised value movements on the Group's investments are booked within the income statement. However, for debt securities classified as 'available-for-sale', unless impaired, fair value movements are recognised in other comprehensive income. Realised gains and losses, including impairments, are recorded in the income statement. This classification is applied for most of the debt securities of the Group's US operations. In 2012, Jackson recorded £37 million (2011: £62 million; 2010: £124 million) of impairment losses arising from:

	2012	2011	2010
	£m	£m	£m
Residential mortgage-backed securities	**8**	21	71
Public fixed income	**2**		1
Other	**27**	41	52
	37	62	124

Jackson's portfolio of debt securities is managed proactively with credit analysts closely monitoring and reporting on the credit quality of its holdings. Jackson continues to review its investments on a case-by-case basis to determine whether any decline in fair value represents an impairment. In addition, investments in structured securities are subject to a rigorous review of their future estimated cash flows, including expected and stress case scenarios, to identify potential shortfalls in contractual payments (both interest and principal). Impairment charges are recorded on structured securities when the Company forecasts a contractual payment shortfall. Situations where such a shortfall would not lead to a recognition of a loss are rare. However, some structured securities do not have a single determined set of future cash flows and instead, there can be a reasonable range of estimates that could potentially emerge. With this variability, there could be instances where the projected cash flow shortfall under management's base case set of assumptions is so minor that relatively small and justifiable changes to the base case assumptions would eliminate the need for an impairment loss to be recognised. The impairment loss reflects the difference between the fair value and book value.

In 2012, there was a movement in the statement of financial position value for debt securities classified as available-for-sale from a net unrealised gain of £2,057 million to a net unrealised gain of £2,807 million. The gross unrealised gain in the statement of financial position increased from £2,303 million at 31 December 2011 to £2,985 million at 31 December 2012 (31 December 2010: £1,580 million), while the gross unrealised loss decreased from £246 million at 31 December 2011 to £178 million at 31 December 2012 (31 December 2010: £370 million).

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Available for sale securities

		Reflected as part of movement in consolidated statement of comprehensive income		
	2012	Changes in unrealised appreciation**	Foreign exchange translation	2011
	£m	£m	£m	£m
Assets fair valued at below book value				
Book value*	**4,551**			2,455
Unrealised (loss) gain	**(178)**	**59**	**9**	(246)
Fair value (as included in statement of financial position)	**4,373**			2,209
Assets fair valued at or above book value				
Book value*	**25,467**			22,504
Unrealised gain (loss)	**2,985**	**803**	**(121)**	2,303
Fair value (as included in statement of financial position)	**28,452**			24,807
Total				
Book value*	**30,018**			24,959
Net unrealised gain (loss)	**2,807**	**862**	**(112)**	2,057
Fair value (as included in statement of financial position)***	**32,825**			27,016

* Book value represents cost/amortised cost of the debt securities.

** Translated at the average rate of $1.5849: £1.00

*** Debt securities for US operations included in the statement of financial position at 31 December 2012 comprise:

	2012	2011
	£m	£m
Available-for-sale	**32,825**	27,016

Fair value through profit and loss:		
Securities of consolidated investment funds		6
Securities held to back liabilities for funds withheld under reinsurance arrangement	**168**	
	32,993	27,022

Included within the movement in gross unrealised losses for the debt securities of Jackson of £59 million (2011: £122 million) as shown above was a net decrease in value of £33 million (2011: £12 million increase) relating to the sub-prime and Alt-A securities as referred to in section B5.

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31 December 2012

D: Life assurance business (Continued)

(ii) Statement of financial position

	31 Dec 2012 £m			31 Dec 2011* £m
	Variable annuity separate account assets and liabilities note (i)	Fixed annuity, GIC and other business note (i)	Total**	Total
Assets				
Intangible assets attributable to shareholders:				
Deferred acquisition costs and other intangibles		**3,222**	**3,222**	3,115
Total		**3,222**	**3,222**	3,115
Deferred tax assets		**1,889**	**1,889**	1,392
Other non-investment and non-cash assets[note (vi)]		**6,792**	**6,792**	1,542
Investments of long-term business and other operations:				
Investment properties		**24**	**24**	35
Financial investments:				
Loans[note (ii)]		**6,235**	**6,235**	4,110
Equity securities and portfolio holdings in unit trusts[note(v)]	**49,298**	**253**	**49,551**	38,036
Debt securities		**32,993**	**32,993**	27,022
Other investments[note (iii)]		**2,296**	**2,296**	2,376
Deposits		**211**	**211**	167
Total investments	**49,298**	**42,012**	**91,310**	71,746
Properties held for sale				3
Cash and cash equivalents		**513**	**513**	271
Total assets	**49,298**	**54,428**	**103,726**	78,069
Equity and liabilities				
Equity				
Shareholders' equity[note (iii)]		**4,343**	**4,343**	3,761
Total equity		**4,343**	**4,343**	3,761
Liabilities				
Policyholder:				
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)[note (iv)]	**49,298**	**42,963**	**92,261**	69,189

Total	**49,298**	**42,963**	**92,261**	69,189
Core structural borrowings of shareholder-financed operations		**153**	**153**	160
Operational borrowings attributable to shareholder-financed operations		**26**	**26**	127
Deferred tax liabilities		**2,168**	**2,168**	1,818
Other non-insurance liabilities[note (vi)]		**4,775**	**4,775**	3,014
Total liabilities	**49,298**	**50,085**	**99,383**	74,308
Total equity and liabilities	**49,298**	**54,428**	**103,726**	78,069

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* The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

** The statement of financial position at 31 December 2012 includes the assets and liabilities of the acquired REALIC business. Details of the acquisition are described in note I1.

Notes

(i) Assets and liabilities attaching to variable annuity business that are not held in the separate account are shown within other business.

(ii) Loans

The loans of the Group's US insurance operations comprise:

	2012	2011
	£m	£m
Mortgage loans	**3,543**	3,559
Policy loans	**2,692**	551
Total US insurance operations loans	**6,235**	4,110

All of the mortgage loans are commercial mortgage loans which are collateralised by properties. The property types are industrial, multi-family residential, suburban office, retail and hotel. The breakdown by property type is as follows:

	2012	2011
	%	%
Industrial	**29**	28
Multi-family residential	**25**	23
Office	**19**	19

Retail	**17**	19
Hotels	**10**	11
	100	100

The US insurance operations' commercial mortgage loan portfolio does not include any single-family residential mortgage loans and is therefore not exposed to the risk of defaults associated with residential sub-prime mortgage loans. The average loan size is £6.3 million (2011: £6.6 million). The portfolio has a current estimated average loan to value of 65 per cent (2011: 68 per cent) which provides significant cushion to withstand substantial declines in value.

At 31 December 2012, Jackson had mortgage loans with a carrying value of £78 million where the contractual terms of the agreements had been restructured. In addition to the regular impairment review afforded all loans in the portfolio, restructured loans are also reviewed for impairment. An impairment will be recorded if the expected cash flows under the newly restructured terms discounted at the original yield (the pre-structured interest rate) are below the carrying value of the loan.

The policy loans are fully secured by individual life insurance policies or annuity policies. The increase in 2012 reflects the purchase of REALIC as explained in note I1. The policy loans from the purchase of REALIC amounted to £1,842 million at 31 December 2012 and are accounted for at fair value through profit and loss as described above. All other policy loans are accounted for at amortised cost, less any impairment.

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(iii) Other investments comprise:

	2012	2011
	£m	£m
Derivative assets*note G3	**1,546**	1,677
Partnerships in investment pools and other**	**750**	699
	2,296	2,376

*

In the US, Prudential uses derivatives:

to reduce interest rate risk;

to facilitate efficient portfolio management to match liabilities under annuity policies, and

for certain equity-based product management activities.

After taking account of the derivative liabilities of £645 million (2011: £887 million), which are also included in Other non-insurance liabilities, the derivative position for US operations is a net asset of £901 million (2011: £790 million).

**

Partnerships in investment pools and other comprise primarily investments in limited partnerships. These include interests in the PPM America Private Equity Fund and diversified investments in 167 (2011: 167) other partnerships by independent money managers that generally invest in various equities and fixed income loans and securities.

(iv) Summary policyholder liabilities (net of reinsurance) and reserves at 31 December 2012

The policyholder liabilities, net of reinsurers' share of £6,076 million (2011: £907 million), reflect balances in respect of the following:

	2012	2011
	£m	£m

Policy reserves and liabilities on non-linked business:		
Reserves for future policyholder benefits and claims payable	**7,663**	518
Deposits on investment contracts (as defined under IFRS 'grandfathered' US GAAP)	**27,425**	28,314
Guaranteed investment contracts	**1,799**	1,617
Unit-linked (variable annuity) business	**49,298**	37,833
	86,185	68,282

In addition to the policyholder liabilities above, Jackson has entered into a programme of funding arrangements under contracts which, in substance, are almost identical to GICs. The liabilities under these funding arrangements totalled £825 million (2011: £1,070 million) and are included in 'other non-insurance liabilities' in the statement of financial position above.

(v)

Equity securities and portfolio holdings in unit trusts includes investments in mutual funds, the majority of which are equity based.

(vi)

Reinsurance balances relating to REALIC

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Included within other non-investment and non-cash assets of £6,792 million (2011: £1,542 million) were balances of £6,076 million (2011: £907 million) for reinsurers' share of insurance contract liabilities. Of the £6,076 million as at 31 December 2012, £5,234 million related to the reinsurance ceded by the newly acquired REALIC business. REALIC holds collateral for certain of these reinsurance arrangements with a corresponding funds withheld liability. As of 31 December 2012, the funds withheld liability of £2,021 million was recorded within other non-insurance liabilities.

(b) Reconciliation of movement in policyholder liabilities

A reconciliation of the total policyholder liabilities of US insurance operations from the beginning of the year to the end of the year is as follows:

US insurance operations

	Variable annuity separate account liabilities	Fixed annuity, GIC and other business	Total
	£m	£m	£m
At 1 January 2011	31,203	29,320	60,523
Premiums	9,176	3,738	12,914
Surrenders	(1,898)	(2,372)	(4,270)
Maturities/Deaths	(300)	(520)	(820)
Net flows[note (b)]	6,978	846	7,824
Transfers from general to separate account	957	(957)	
Investment-related items and other movements	(1,735)	1,871	136
Foreign exchange translation differences[note (a)]	430	276	706
At 31 December 2011/1 January 2012	**37,833**	**31,356**	**69,189**
Premiums	**10,361**	**4,546**	**14,907**
Surrenders	**(2,149)**	**(2,207)**	**(4,356)**
Maturities/Deaths	**(404)**	**(550)**	**(954)**
Net flows[note (b)]	**7,808**	**1,789**	**9,597**
Transfers from general to separate account	**1,577**	**(1,577)**	
Investment-related items and other movements[note (c)]	**4,014**	**227**	**4,241**
Foreign exchange translation differences[note (a)]	**(1,998)**	**(1,680)**	**(3,678)**
Acquisition of REALIC[Notes (d), I1]	**64**	**12,848**	**12,912**
At 31 December 2012	**49,298**	**42,963**	**92,261**

Average policyholder liability balances*			
2012	**43,549**	**33,948**	**77,497**
2011	34,518	30,338	64,856

* Averages have been based on opening and closing balances, and adjusted for acquisitions and disposals in the period.

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D: Life assurance business (Continued)

Notes

(a) Movements in the year have been translated at an average rate of $1.58/£1.00 (2011: $1.60/£1.00). The closing balances have been translated at closing rate of $1.63/£1.00 (2011: $1.55/£1.00). Differences upon retranslation are included in foreign exchange translation differences.

(b) Net flows for the year were £9,597 million compared with £7,824 million in 2011 driven largely by increased new business volumes.

(c) Positive investment-related items and other movements in variable annuity separate account liabilities of £4,014 million for 2012 reflects the increase in the US equity market during the year with the S&P index increasing by 13.4 per cent. Fixed annuity, GIC and other business investment and other movements primarily reflects the interest credited to policyholder account in the year, net of falls in the technical provisions held for the guarantees issued with variable annuity business.

(d) The acquisition of REALIC reflects the liabilities, before reduction for reinsurances ceded, acquired at the date of acquisition.

(c) Information on credit risks of debt securities

Summary	**2012**	**2011**
	£m	**£m**
Corporate and government security and commercial loans:		
Government	**4,126**	2,163
Publicly traded and SEC Rule 144A* securities	**19,699**	16,281
Non-SEC Rule 144A* securities	**3,542**	3,198
Total	**27,367**	21,642
Residential mortgage-backed securities	**2,400**	2,591
Commercial mortgage-backed securities	**2,639**	2,169
Other debt securities	**587**	620
Total US debt securities	**32,993**	27,022

* A 1990 SEC rule that facilitates the resale of privately placed securities that are without SEC registration to qualified institutional investors. The rule was designed to develop a more liquid and efficient institutional resale market for unregistered securities.

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(i)

Credit quality

The following table summarises by rating the debt securities, as at 31 December 2012 and 2011 using Standard and Poor's (S&P), Moody's, Fitch and implicit ratings of mortgage-backed securities (MBS) based on NAIC valuations.*

	2012	2011
	£m	£m
S&P AAA	**187**	133
S&P AA+ to AA-	**6,343**	4,476
S&P A+ to A-	**7,728**	6,382
S&P BBB+ to BBB-	**10,230**	8,446
S&P Other	**1,173**	999
	25,661	20,436
Moody's Aaa	**55**	62
Moody's Aa1 to Aa3	**18**	15
Moody's A1 to A3	**21**	29
Moody's Baa1 to Baa3	**56**	67
Moody's Other	**13**	17
	163	190
Implicit ratings of MBS based on NAIC* valuations (see below)		
NAIC 1	**2,934**	2,577
NAIC 2	**207**	147
NAIC 3-6	**321**	368
	3,462	3,092
Fitch	**184**	184
Other**	**3,523**	3,120
Total debt securities	**32,993**	27,022

*

The Securities Valuation Office of the National Association of Insurance Commissioners (NAIC) classifies debt securities into six quality categories range from Class 1 (the highest) to Class 6 (the lowest). Performing securities are designated as Classes 1 to 5 and securities in or near default are designated Class 6.

**

The amounts within Other which are not rated by S&P, Moody nor Fitch, nor are MBS securities using the revised regulatory ratings, have the following NAIC classifications:

	2012	2011
	£m	£m
NAIC 1	**1,453**	1,258
NAIC 2	**2,022**	1,792
NAIC 3-6	**48**	70
	3,523	3,120

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For some mortgage-backed securities within Jackson, the table above includes these securities using the regulatory ratings detail issued by the NAIC. These regulatory ratings levels were established by external third parties (PIMCO for residential mortgage backed securities and BlackRock Solutions for commercial mortgage backed securities) based on Jackson's carrying value.

(ii) Determining the fair value of debt securities when the markets are not active

Under IAS 39, unless categorised as 'held to maturity' or 'loans and receivables' debt securities are required to be fair valued. Where available, quoted market prices are used. However, where securities do not have an externally quoted price based on regular trades or where markets for the securities are no longer active as a result of market conditions, IAS 39 requires that valuation techniques be applied. IFRS 7 requires classification of the fair values applied by the Group into a three level hierarchy. Note G1 sets out further details of the Group's approach to determining fair value and classifies these fair values into a three level hierarchy as required by IFRS 7. At 31 December 2012, 0.1 per cent of Jackson's debt securities were classified as level 3 (31 December 2011: 0.1 per cent) comprising of fair values where there are significant inputs which are not based on observable market data.

(iii) Asset-backed securities funds exposures

Included within the debt securities of Jackson at 31 December 2012 are exposures to asset-backed securities as follows:

	2012	**2011**
	£m	**£m**
RMBS:		
Sub-prime (2012: 15% AAA, 6% AA)	**261**	207
Alt-A (2012: 4% AAA, 1% AA)	**323**	310
Prime including agency (2012: 0% AAA, 75% AA)	**1,816**	2,074
CMBS (2012: 40% AAA, 24% AA)	**2,639**	2,169
CDO funds (2012: 0% AAA, 27% AA)*, including £nil exposure to sub-prime	**44**	44
Other ABS (2012: 24% AAA, 15% AA), including £nil exposure to sub-prime	**543**	576
Total	**5,626**	5,380

* Including Group's economic interest in Piedmont and other consolidated CDO funds.

Jackson defines its exposure to sub-prime mortgages as investments in residential mortgage-backed securities in which the underlying borrowers have a US Fair Isaac Credit Organisation (FICO) credit score of 680 or lower.

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(iv) Debt securities classified as available-for-sale in an unrealised loss position

The following table shows the fair value of those securities that are in a gross unrealised loss position for various percentages of book value at 31 December:

	2012		2011	
	Fair value	Unrealised loss	Fair value	Unrealised loss
	£m	£m	£m	£m
Between 90% and 100%	**4,214**	**(112)**	1,829	(60)
Between 80% and 90%	**85**	**(13)**	172	(28)
Below 80% *	**74**	**(53)**	208	(158)
Total	**4,373**	**(178)**	2,209	(246)

* The unrealised losses as at 31 December 2012 include £77 million (2011: £183 million) relating to mortgage-backed and other debt securities. The unrealised losses in the portfolio by reference to the length of time 3 years or more as at 31 December 2012 are £36 million (2011: £105 million) in the investment grade and £31 million (2011: £61 million) in non-investment grade.

(d) Products and guarantees

Jackson provides long-term savings and retirement products to retail and institutional customers throughout the US. Jackson offers fixed annuities (interest-sensitive, fixed indexed and immediate annuities), variable annuities (VA), life insurance and institutional products.

(i) Fixed annuities

Interest-sensitive annuities

At 31 December 2012, interest-sensitive fixed annuities accounted for 13 per cent (2011: 16 per cent) of policy and contract liabilities of Jackson. Interest-sensitive fixed annuities are primarily deferred annuity products that are used for asset accumulation in retirement planning and for providing income in retirement. They permit tax-deferred accumulation of funds and flexible payout options.

The policyholder of an interest-sensitive fixed annuity pays Jackson a premium, which is credited to the policyholder's account. Periodically, interest is credited to the policyholder's account and in some cases administrative charges are deducted from the policyholder's account. Jackson makes benefit payments at a future date as specified in the policy based on the value of the policyholder's account at that date.

The policy provides that at Jackson's discretion it may reset the interest rate, subject to a guaranteed minimum. At 31 December 2012, Jackson had fixed interest rate annuities totalling £11.7 billion (US$19.0 billion) (2011: £11.5 billion (US$17.8 billion) in account value with minimum guaranteed rates ranging from 1.0 per cent to 5.5 per cent and a 3.09 per cent average guaranteed rate (2011: 1.0 per cent to 5.5 per cent and a 3.08 per cent average guaranteed rate).

Approximately 50 per cent (2011: 48 per cent) of the interest-sensitive fixed annuities Jackson wrote in 2012 provide for a market value adjustment that could be positive or negative, on surrenders in the surrender period of the policy. This formula-based adjustment approximates the change in value that

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assets supporting the product would realise as interest rates move up or down. The minimum guaranteed rate is not affected by this adjustment.

Fixed indexed annuities

Fixed indexed annuities (FIA) accounted for 8 per cent (2011: 9 per cent) of Jackson's policy and contract liabilities at 31 December 2012. Fixed indexed annuities vary in structure, but generally are deferred annuities that enable policyholders to obtain a portion of an equity-linked return (based on participation rates and caps) but provide a guaranteed minimum return. These guaranteed minimum rates are generally set at 1.0 to 3.0 per cent. Jackson had fixed indexed annuities allocated to indexed funds totalling £5.6 billion (US$9.2 billion) (2011: £5.0 billion (US$7.8 billion) in account value with minimum guaranteed rates on indexed accounts ranging from 1.0 per cent to 3.0 per cent and a 1.82 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 1.76 per cent average guarantee rate). Jackson also offers fixed interest accounts on some fixed indexed annuity products. Fixed interest accounts of fixed indexed annuities totalled £1.5 billion (US$2.3 billion) (2011: £1.4 billion (US$2.1 billion) in account value with minimum guaranteed rates ranging from 1.0 per cent to 3.0 per cent and a 2.53 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 2.50 per cent average guarantee rate).

Jackson hedges the equity return risk on fixed indexed products using futures and options linked to the relevant index as well as through offsetting equity exposure in the VA product. The cost of these hedges is taken into account in setting the index participation rates or caps. Jackson bears the investment and surrender risk on these products.

Immediate annuities

At 31 December 2012, immediate annuities accounted for 1 per cent (2011: 1 per cent) of Jackson's policy and contract liabilities. Immediate annuities guarantee a series of payments beginning within a year of purchase and continuing over either a fixed period of years and/or the life of the policyholder. If the term is for the life of the policyholder, then Jackson's primary risk is mortality risk. The implicit interest rate on these products is based on the market conditions that exist at the time the policy is issued and is guaranteed for the term of the annuity.

(ii) Variable annuities

At 31 December 2012, VAs accounted for 60 per cent (2011: 63 per cent) of Jackson's policy and contract liabilities. VAs are deferred annuities that have the same tax advantages and payout options as interest-sensitive and fixed indexed annuities.

The primary differences between VAs and interest-sensitive or fixed indexed annuities are investment risk and return. If a policyholder chooses a VA, the rate of return depends upon the performance of the selected fund portfolio. Policyholders may allocate their investment to either the fixed or a selection of variable accounts. Investment risk on the variable account is borne by the policyholder, while investment risk on the fixed account is borne by Jackson through guaranteed minimum fixed rates of return. At 31 December 2012, approximately 8 per cent (2011: approximately 10 per cent) of VA funds were in fixed accounts. Jackson had fixed interest rate accounts in variable

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annuities totalling £4.3 billion (US$7.0 billion) (2011: £4.3 billion (US$6.7 billion) in account value with minimum guaranteed rates ranging from 1.0 per cent to 3.0 per cent and a 1.89 per cent average guaranteed rate (2011: 1.0 per cent to 3.0 per cent and a 1.99 per cent average guarantee rate).

Jackson issues VA contracts where it contractually guarantees to the contractholder either a) return of no less than total deposits made to the contract adjusted for any partial withdrawals, b) total deposits made to the contract adjusted for any partial withdrawals plus a minimum return, or c) the highest contract value on a specified anniversary date adjusted for any withdrawals following the contract anniversary. These guarantees include benefits that are payable in the event of death (guaranteed minimum death benefit (GMDB)), annuitisation (guaranteed minimum income benefit (GMIB)), or at specified dates during the accumulation period (guaranteed minimum withdrawal benefit (GMWB) and guaranteed minimum accumulation benefit (GMAB)). Jackson hedges these risks using equity options and futures contracts as described in note D3(h). The GMAB was eliminated from Jackson's product offerings in 2011. The GMIB is no longer offered, with existing coverage being reinsured.

In March 2012, Jackson launched a new variable annuity product, Elite Access, which has no guaranteed benefits and provides tax efficient access to alternative investments. Single premium sales in the period since launch were £849 million.

(iii) Aggregate distribution of account values

The table below shows the distribution of account values for fixed annuities (interest sensitive and fixed indexed) and variable annuities within the range of minimum guaranteed interest rates as described in notes i to ii above as at 31 December 2012 and 2011:

	Account value	
Minimum guaranteed interest rate	**2012**	**2011**
	£m	**£m**
1.0%	**2,534**	1,988
> 1.0% 2.0%	**8,374**	8,321
> 2.0% 3.0%	**9,174**	9,352
> 3.0% 4.0%	**1,236**	841
> 4.0% 5.0%	**1,518**	1,425
> 5.0%	**209**	167
Total	**23,045**	22,094

(iv) Life insurance

Jackson's life insurance products accounted for 15 per cent (2011: 7 per cent) of Jackson's policy and contract liabilities at 31 December 2012. The increase from 2011 was a result of the acquisition of REALIC. Jackson discontinued new sales of life insurance products effective 1 August 2012. The life products included term life, universal life and variable universal life. Term life provides protection for a defined period and a benefit that is payable to a designated beneficiary upon death of the insured. Universal life provides permanent individual life insurance for the life of the insured and includes a

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savings element. Variable universal life is a type of life insurance policy that combines death benefit protection with the ability for the policyholder account to be invested in separate account funds.

At 31 December 2012, Jackson (including the newly acquired REALIC) had interest sensitive life business in force with total account value of £6.0 billion (US$9.7 billion) (2011: £3.3 billion (US$5.1 billion)), with minimum guaranteed interest rates ranging from 2.5 per cent to 6.0 per cent with a 4.67 per cent average guaranteed rate (2011: 3.0 per cent to 6.0 per cent with a 4.88 per cent average guaranteed rate). The table below shows the distribution of the interest-sensitive life business' account values within this range of minimum guaranteed interest rates as at 31 December 2012 and 2011:

	Account value	
Minimum guaranteed interest rate	**2012**	**2011**
	£m	**£m**
1.0%		
> 1.0% 2.0%		
> 2.0% 3.0%	**183**	130
> 3.0% 4.0%	**2,141**	1,145
> 4.0% 5.0%	**2,097**	686
> 5.0%	**1,550**	1,317
Total	**5,971**	3,278

(v) Institutional products

Jackson's institutional products consist of GICs, funding agreements (including agreements issued in conjunction with Jackson's participation in the US Federal Home Loan Bank programme) and medium-term note funding agreements. At 31 December 2012, institutional products accounted for 3 per cent of policy and contract liabilities (2011: 4 per cent). Under a traditional GIC, the policyholder makes a lump sum deposit. The interest rate paid is fixed and established when the contract is issued. If deposited funds are withdrawn earlier than the specified term of the contract, an adjustment is made that approximates a market value adjustment.

Under a funding agreement, the policyholder either makes a lump sum deposit or makes specified periodic deposits. Jackson agrees to pay a rate of interest, which may be fixed but which is usually a floating short-term interest rate linked to an external index. The average term of the funding arrangements is one to two years. In 2012 and 2011, there were no funding agreements terminable by the policyholder with less than 90 days' notice.

Medium-term note funding agreements are generally issued to support trust instruments issued on non-US exchanges or to qualified investors (as defined by SEC Rule 144A). Through the funding agreements, Jackson agrees to pay a rate of interest, which may be fixed or floating, to the holders of the trust instruments.

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(e) Process for setting assumptions and determining contract liabilities

Under the MSB of reporting applied under IFRS 4 for insurance contracts, providing the requirements of the Companies Act, UK GAAP standards and the ABI SORP are met, it is permissible to reflect the previously applied UK GAAP basis. Accordingly, and consistent with the basis explained in note A3, in the case of Jackson the carrying values of insurance assets and liabilities are consolidated into the Group accounts based on US GAAP.

Under US GAAP, investment contracts (as defined for US GAAP purposes) are accounted for by applying in the first instance a retrospective deposit method to determine the liability for policyholder benefits. This is then augmented by potentially three additional amounts. These amounts are for:

any amounts that have been assessed to compensate the insurer for services to be performed over future periods (ie deferred income),

any amounts previously assessed against policyholders that are refundable on termination of the contract, and

any probable future loss on the contract (i.e. premium deficiency).

Capitalised acquisition costs and deferred income for these contracts are amortised over the life of the book of contracts. The present value of the estimated gross profits is generally computed using the rate of interest that accrues to policyholder balances (sometimes referred to as the contract rate). Estimated gross profits include estimates of the following elements, each of which will be determined based on the best estimate of amounts of the following individual elements over the life of the book of contracts without provision for adverse deviation for:

amounts expected to be assessed for mortality less benefit claims in excess of related policyholder balances,

amounts expected to be assessed for contract administration less costs incurred for contract administration,

amounts expected to be earned from the investment of policyholder balances less interest credited to policyholder balances,

amounts expected to be assessed against policyholder balances upon termination of contracts (sometimes referred to as surrender charges), and

other expected assessments and credits.

VA contracts written by Jackson may, as described above, provide for GMDB, GMIB, GMWB and GMAB features. In general terms, liabilities for these benefits are accounted for under US GAAP by using estimates of future benefits and fees under best estimate persistency assumptions.

In accordance with US GAAP, the "grandfathered" basis for IFRS, which specifies how certain guarantee features should be accounted for, the GMDB and the 'for life' portion of GMWB liabilities are not fair valued but are instead determined each period end by estimating the expected value of benefits in excess of the projected account balance and recognising the excess ratably over the life of the contract based on total expected assessments. At 31 December 2012, these liabilities were valued using

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a series of deterministic investment performance scenarios, a mean investment return of 8.4 per cent (2011: 8.4 per cent) and assumptions for lapse, mortality and expense that are the same as those used in amortising the capitalised acquisition costs.

The direct GMIB liability is determined by estimating the expected value of the annuitisation benefits in excess of the projected account balance at the date of annuitisation and recognising the excess ratably over the accumulation period based on total expected assessments.

GMIB benefits are essentially fully reinsured, subject to annual claim limits. As this reinsurance benefit is net settled, it is considered to be a derivative under IAS 39, and is therefore recognised at fair value with the change in fair value included as a component of short-term derivative fluctuations.

The assumptions used for calculating the direct GMIB liability at 31 December 2012 and 2011 are consistent with those used for calculating the GMDB and 'for life' GMWB liabilities. The change in these reserves, along with claim payments and associated fees included in reserves are included along with the hedge results in short-term fluctuations, resulting in removal of the market impact from the operating profit based on longer-term investment returns.

Jackson regularly evaluates estimates used and adjusts the additional GMDB, GMIB and GMWB 'for life' liability balances, with a related charge or credit to benefit expense if actual experience or other evidence suggests that earlier assumptions should be revised.

GMWB 'not for life' features are considered to be embedded derivatives under IAS 39. Therefore, provisions for these benefits are recognised at fair value, with the change in fair value included in short-term fluctuations.

For GMWB and GMIB reinsurance embedded derivatives that are fair valued under IAS 39, Jackson bases its volatility assumptions solely on implied market volatility with no reference to historical volatility levels and explicitly incorporates Jackson's own credit risk in determining discount rates.

Volatility assumptions are based on a weighting of available market data on implied volatility for durations up to ten years, at which point the projected volatility is held constant. Non-performance risk is incorporated into the calculation through the use of discount interest rates sourced from a AA corporate credit curve. Other risk margins, particularly for market illiquidity and policyholder behaviour are also incorporated into the model through the use of explicitly conservative assumptions. On a periodic basis, Jackson rationalises the resulting fair values based on comparisons to other models and market movements.

With the exception of the GMDB, GMIB, GMWB and GMAB features of VA contracts, the financial guarantee features of Jackson's contracts are in most circumstances not explicitly valued, but the impact of any interest guarantees would be reflected as they are earned in the current account value (ie the US GAAP liability).

For traditional life insurance contracts, provisions for future policy benefits are determined under US GAAP using the net level premium method and assumptions as of the issue date as to mortality, interest, policy lapses and expenses plus provisions for adverse deviation.

Institutional products are accounted for as investment contracts under IFRS with the liability classified as being in respect of financial instruments rather than insurance contracts, as defined by

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IFRS 4. In practice there is no material difference between the IFRS and US GAAP basis of recognition and measurement for these contracts.

Certain institutional products representing obligations issued in currencies other than US dollars have been hedged for changes in exchange rates using cross-currency swaps. The fair value of derivatives embedded in funding agreements, as well as foreign currency transaction gains and losses, are included in the carrying value of the trust instruments supported by funding agreements recorded in other non-insurance liabilities.

Deferred acquisition costs

Under IFRS 4, the Group applies grandfathered US GAAP for measuring the insurance assets and liabilities of Jackson. In the case of Jackson term business, acquisition costs are deferred and amortised in line with expected premiums. For annuity and interest-sensitive life business, acquisition costs are deferred and amortised in line with a combination of historical and future expected gross profits on the relevant contracts. For fixed and indexed annuity and interest-sensitive life business, the key assumption is the long-term spread between the earned rate on investments and the rate credited to policyholders, which is based on an annual spread analysis. Expected gross profits also depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges), all of which are based on a combination of actual experience of Jackson, industry experience and future expectations. A detailed analysis of actual mortality, lapse and expense experience is performed using internally developed experience studies.

As with fixed and indexed annuity and interest-sensitive life business, acquisition costs for Jackson's variable annuity products are amortised in line with the emergence of profits. The measurement of the amortisation in part reflects current period fees (including those for guaranteed minimum death, income, or withdrawal benefits) earned on assets covering liabilities to policyholders, and the historical and expected level of future gross profits which depends on the assumed level of future fees, as well as components related to mortality, lapse and expense.

Change of accounting policy

As explained in note A5, the Company has adopted the US Financial Accounting Standards Board requirements in the Emerging Issues Task Force (EITF) Update No. 2010-26 on 'Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts' from 1 January 2012 into Prudential's Group IFRS reporting for the results of Jackson and those Asia operations whose IFRS insurance assets and liabilities are measured principally by reference to US GAAP principles. Under the Update, insurers are required to capitalise only those incremental costs directly relating to successfully acquiring a contract from 1 January 2012. For Group IFRS reporting, the Company has chosen to apply this new basis retrospectively for the results of these operations.

On application of the new policy for Jackson, the deferred costs balance for business in force at 31 December 2011 was retrospectively reduced from £3,880 million to £3,095 million.

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Mean reversion technique

For variable annuity products, under US GAAP (as 'grandfathered' under IFRS 4) the projected gross profits, against which acquisition costs are amortised, reflect an assumed long-term level of equity return which, for Jackson, is 8.4 per cent after deduction of net external fund management fees. This is applied to the period end level of separate account assets after application of a mean reversion technique that removes a portion of the effect of levels of short-term variability in current market returns.

Under the mean reversion technique applied by Jackson, the projected level of return for each of the next five years is adjusted from period to period so that in combination with the actual rates of return for the preceding two years and the current year, the 8.4 per cent annual return is realised on average over the entire eight year period. Projected returns after the mean reversion period revert back to the 8.4 per cent assumption.

However, to ensure that the methodology does not over anticipate a reversion to trend following adverse markets, the mean reversion technique has a cap and floor feature whereby the projected returns in each of the next five years can be no more than 15 per cent per annum and no less than 0 per cent per annum (both gross of asset management fees) in each year. The capping feature was relevant in late 2008, 2009 and 2010 due to the very sharp market falls in 2008. Notwithstanding this capping feature, the mean reversion technique gave rise to a benefit in 2008 of £110 million. This benefit was effectively 'paid back' under the mean reversion technique through charges for accelerated amortisation in 2011, as discussed below.

At 31 December 2012, the projected rate of return for the next five years is materially the same as the long-term assumption of 8.4 per cent, and so the mean reversion technique had little effect at that date.

Sensitivity of amortisation charge

The amortisation charge to the income statement is reflected in operating profit and short-term fluctuations in investment returns. The amortisation charge to the operating profit in a reporting period comprises:

(i) a core amount that reflects a relatively stable proportion of underlying profit; and

(ii) an element of acceleration or deceleration arising from market movements differing from expectations.

In periods where the cap and floor feature of the mean reversion technique are not relevant, the technique operates to dampen the second element above. Nevertheless, extreme market movements can cause material acceleration or deceleration of amortisation in spite of this dampening effect.

Furthermore, in those periods where the cap or floor is relevant, the mean reversion technique provides no further dampening and additional volatility may result.

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2011

In 2011, the DAC amortisation charge to operating profit included £190 million of accelerated amortisation. This amount reflected the combined effect of:

(a) the separate account performance in the year of negative 4 per cent, net of all fees as it compared with the assumed level for the year; and

(b) the reduction in the previously assumed future rates of return for the upcoming five years from 15 per cent, to a level nearer the middle of the corridor (of 0 per cent and 15 per cent), so that in combination with the historical returns, the 8-year average in the mean reversion calculation was the 8.4 per cent assumption.

The reduction in assumed future rates reflected in large part, the elimination from the calculation in 2011 of the 2008 negative returns. Setting aside other complications and the growth in the book, the 2011 accelerated amortisation can be broadly equated as 'paying back' the benefit experienced in 2008.

2012

In 2012, the DAC amortisation charge to operating profit of £356 million was determined after taking credit for decelerated amortisation of £56 million. This amount primarily reflects the separate account performance of 11 per cent, net of all fees, over the assumed level for the year.

2013

The application of the mean reversion formula has the effect of dampening the impact of equity market movements on DAC amortisation while the mean reversion assumption lies within the corridor. It would take a very significant movement in equity markets in 2013 (outside the range of negative 20 per cent to positive 50 per cent) for the mean reversion assumption to move outside the corridor.

Statement of changes in equity 'shadow DAC adjustments'

Consequent upon the positive unrealised valuation movement in 2012 of £862 million (2011: positive £811 million) there is a debit of £270 million (2011: £275 million debit) for altered 'shadow' DAC amortisation booked within other comprehensive income. These adjustments reflect movement from period to period, in the changes to the pattern of reported gross profits that would have happened if the assets reflected in the statement of financial position had been sold, crystallising the unrealised gains or losses, and the proceeds reinvested at the yields currently available in the market. At 31 December 2012, the cumulative 'shadow DAC balance' was negative £952 million (2011: negative £720 million).

(f) Reinsurance

The reinsurance asset for business ceded outside the Group was £6,076 million (2011: £907 million). The increase from 2011 is due to the acquisition of REALIC as described in note I1 whereby certain former REALIC business was retained by Swiss re through 100 per cent reinsurance agreements. Apart from the reinsurance acquired through the purchase of REALIC, the principal reinsurance ceded by Jackson outside the Group is on term life insurance, direct and assumed accident

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and health business and GMIB variable annuity guarantees. In 2012, the premiums for such ceded business amounted to £193 million (2011: £72 million; 2010: £83 million). Net commissions received on ceded business and claims incurred ceded to external reinsurers totalled £24 million and £123 million respectively during 2012 (2011: £9 million and £84 million respectively; 2010: £12 million and £72 million, respectively). There were no deferred gains or losses on reinsurance contracts in either 2012, 2011 or 2010.

(g) Effect of changes in assumptions used to measure insurance assets and liabilities

In 2012, 2011 and 2010, there were no changes of assumptions that had a material impact on the results of US insurance operations.

(h) Exposure and sensitivity of IFRS basis profit and shareholders' equity to market and other risks

Jackson's main exposures are to market risk through its exposure to interest rate risk and equity risk. Approximately 94 per cent (2011: 92 per cent) of its general account investments support interest-sensitive and fixed indexed annuities, life business and surplus and 6 per cent (2011: 8 per cent) support institutional business. All of these types of business contain considerable interest rate guarantee features and, consequently, require that the assets that support them are primarily fixed income or fixed maturity.

Jackson is exposed primarily to the following risks in the US arising from fluctuations in interest rates:

- the risk of loss related to meeting guaranteed rates of accumulation following a sharp and sustained fall in interest rates,
- the risk of loss related to policyholder withdrawals following a sharp and sustained increase in interest rates, and
- the risk of mismatch between the expected duration of certain annuity liabilities and prepayment risk and extension risk inherent in mortgage-backed securities.

Jackson is also exposed to the following risks in the US arising from equity market movements:

- the risk of loss related to the incidence of benefits related to guarantees issued in connection with its VA contracts, and
- the risk of loss related to meeting contractual accumulation requirements in FIA contracts.

Jackson enters into financial derivative transactions, including those noted below to reduce and manage business risks. These transactions manage the risk of a change in the value, yield, price, cash flows or quantity of, or a degree of exposure with respect to assets, liabilities or future cash flows, which Jackson has acquired or incurred.

Jackson uses free-standing derivative instruments for hedging purposes. Additionally, certain liabilities, primarily trust instruments supported by funding agreements, fixed indexed annuities, certain GMWB variable annuity features and reinsured GMIB variable annuity features contain embedded

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derivatives as defined by IAS 39, 'Financial Instruments: Recognition and Measurement'. Jackson does not account for such derivatives as either fair value or cash flow hedges as might be permitted if the specific hedge documentation requirements of IAS 39 were followed. Financial derivatives, including derivatives embedded in certain host liabilities that have been separated for accounting and financial reporting purposes are carried at fair value.

Value movements on the derivatives are reported within the income statement. In preparing Jackson's segment profit as shown in note B1, value movements on Jackson's derivative contracts, are included within short-term fluctuations in investment returns and excluded from operating results based on longer-term investment returns.

The types of derivatives used by Jackson and their purpose are as follows:

Interest rate swaps generally involve the exchange of fixed and floating payments over the period for which Jackson holds the instrument without an exchange of the underlying principal amount. These agreements are used for hedging purposes;

Put-swaption contracts provide the purchaser with the right, but not the obligation, to require the writer to pay the present value of a long-duration interest rate swap at future exercise dates. Jackson purchases and writes put-swaptions with maturities up to 10 years. Put-swaptions hedge against significant movements in interest rates;

Equity index futures contracts and equity index options (including various call, put options and put spreads) are used to hedge Jackson's obligations associated with its issuance of fixed indexed immediate and deferred annuities and certain VA guarantees. These annuities and guarantees contain embedded options which are fair valued for financial reporting purposes;

Total return swaps in which Jackson receives equity returns or returns based on reference pools of assets in exchange for short-term floating rate payments based on notional amounts, are held for both hedging and investment purposes;

Cross-currency swaps, which embody spot and forward currency swaps and additionally, in some cases, interest rate swaps and equity index swaps, are entered into for the purpose of hedging Jackson's foreign currency denominated funding agreements supporting trust instrument obligations; and

Credit default swaps, represent agreements under which Jackson has purchased default protection on certain underlying corporate bonds held in its portfolio. These contracts allow Jackson to sell the protected bonds at par value to the counterparty if a default event occurs in exchange for periodic payments made by Jackson for the life of the agreement. Jackson does not write default protection using credit derivatives.

The estimated sensitivity of Jackson's profit and shareholders' equity to equity and interest rate risks provided below is net of the related changes in amortisation of DAC. The effect on the related changes in amortisation of DAC provided is based on the current 'grandfathered' US GAAP DAC basis but does not include any effect from an acceleration or deceleration of amortisation of DAC. Note A5 provides explanation of the new US GAAP DAC basis adopted by the Company from 1 January 2012. Note D3(e) above provides an explanation of the dynamics that affect the amortisation charge.

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(i) Sensitivity to equity risk

Variable annuity contract related

At 31 December 2012 and 2011, Jackson had variable annuity contracts with guarantees, for which the net amount at risk ('NAR') is generally the amount of guaranteed benefit in excess of current account value, as follows:

31 December 2012

	Minimum return	Account value	Net amount at risk	Weighted average attained age	Period until expected annuitisation
		£m	£m		
Return of net deposits plus a minimum return					
GMDB	0-6%	40,964	1,839	64.4 years	
GMWB Premium only	0%	2,213	91		
GMWB*	0-5%	3,359	88*		
GMAB Premium only	0%	53			
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		4,554	324	64.0 years	
GMWB Highest anniversary only		1,880	245		
GMWB*		697	137*		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0-6%	2,705	348	66.4 years	
GMIB	0-6%	1,588	469		3.3 years
GMWB*	0-8%**	31,167	1,918*		

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31 December 2011

	Minimum return	Account value	Net amount at risk	Weighted average attained age	Period until expected annuitisation
		£m	£m		
Return of net deposits plus a minimum return					
GMDB	0-6%	31,571	2,914	64.2 years	
GMWB Premium only	0%	2,325	195		
GMWB*	0-5%	2,582	582*		
GMAB Premium only	0%	54	2		
Highest specified anniversary account value minus withdrawals post-anniversary					
GMDB		4,002	678	63.7 years	
GMWB Highest anniversary only		1,855	423		
GMWB*		735	217*		
Combination net deposits plus minimum return, highest specified anniversary account value minus withdrawals post-anniversary					
GMDB	0-6%	2,098	479	66.1 years	
GMIB	0-6%	1,661	575		4.2 years
GMWB*	0-8%**	21,902	2,263*		

*

Amounts shown for GMWB comprise sums for the 'not for life' portion (where the guaranteed withdrawal base less the account value equals to the net amount at risk (NAR)), and a 'for life' portion (where the NAR has been estimated as the present value of future expected benefit payment remaining after the amount of the 'not for life' guaranteed benefits is zero).

**

Ranges shown based on simple interest. The upper limits of 5 per cent, or 8 per cent simple interest are approximately equal to 4.1 per cent and 6 per cent respectively, on a compound interest basis over a typical 10-year bonus period. For example $1 + 10 \times 0.05$ is similar to 1.041 growing at a compound rate of 4.01 per cent for a further 9 years.

The GMIB reinsurance guarantees are fully reinsured.

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Account balances of contracts with guarantees were invested in variable separate accounts as follows:

	2012	2011
	£m	£m
Mutual fund type:		
Equity	**38,092**	28,902
Bond	**5,673**	4,251
Balanced	**4,601**	3,846
Money market	**766**	677
Total	**49,132**	37,676

As noted above, Jackson is exposed to equity risk through the options embedded in the fixed indexed liabilities and GMDB and GMWB guarantees included in certain VA benefits as illustrated above. This risk is managed using an equity hedging programme to minimise the risk of a significant economic impact as a result of increases or decreases in equity market levels while taking advantage of naturally offsetting exposures in Jackson's operations. Jackson purchases external futures and options that hedge the risks inherent in these products, while also considering the impact of rising and falling separate account fees.

As a result of this hedging programme, if the equity markets were to increase further in the future, the net effect of Jackson's free-standing derivatives would decrease in value. However, over time, this movement would be broadly offset by increased separate account fees and reserve decreases, net of the related changes to amortisation of deferred acquisition costs. Due to the nature of the free-standing and embedded derivatives, this hedge, while highly effective on an economic basis, may not completely mute in the financial reporting the immediate impact of equity market movements as the free-standing derivatives reset immediately while the hedged liabilities reset more slowly and fees are recognised prospectively. The opposite impact would be observed if the equity markets were to decrease.

At 31 December 2012, the estimated sensitivity of Jackson's profit for VA business, and shareholders' equity to immediate increases and decreases in equity markets is shown below. The sensitivities are shown net of related changes in DAC amortisation.

	2012				2011*			
	Decrease of 20%	Decrease of 10%	Increase of 10%	Increase of 20%	Decrease of 20%	Decrease of 10%	Increase of 10%	Increase of 20%
	£m	£m	£m	£m	£m	£m	£m	£m
Pre-tax profit, net of related changes in amortisation of DAC (excluding impact on future separate account fees)	**326**	**120**	**(86)**	**(215)**	**373**	**196**	**(242)**	**(539)**
Related deferred tax effects	**(114)**	**(42)**	**30**	**75**	**(130)**	**(69)**	**85**	**189**
Net sensitivity of profit after tax and shareholders' equity	**212**	**78**	**(56)**	**(140)**	**243**	**127**	**(157)**	**(350)**

* The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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The above table provides sensitivity movements as at a point in time while the actual impact on financial results would vary contingent upon the volume of new product sales and lapses, changes to the derivative portfolio, correlation of market returns and various other factors including volatility, interest rates and elapsed time.

The directional movements in the sensitivities reflect the hedging programme in place at 31 December 2012.

Other sensitivity to equity risk

In addition to the exposure explained above, Jackson is also exposed to equity risk from its holding of equity securities, partnerships in investment pools and other financial derivatives.

A range of reasonably possible movements in the value of equity securities, partnerships in investment pools and other financial derivatives have been applied to Jackson's holdings at 31 December 2012 and 2011. The table below shows the sensitivity to a 10 and 20 per cent fall in value and the impact that this would have on pre-tax profit, net of related changes in amortisation of DAC, profit after tax and shareholders' equity.

	2012		2011*	
	Decrease of 20%	Decrease of 10%	Decrease of 20%	Decrease of 10%
	£m	£m	£m	£m
Pre-tax profit, net of related changes in amortisation of DAC	**(143)**	**(72)**	(129)	(64)
Related deferred tax effects	**50**	**25**	45	23
Net sensitivity of profit after tax and shareholders' equity	**(93)**	**(47)**	(84)	(41)

* The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

A 10 or 20 per cent increase in their value is estimated to have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above.

In the equity risk sensitivity analysis shown above, the Group has considered the impact of an instantaneous 20 per cent fall in equity markets. If equity markets were to fall by more than 20 per cent, the Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Group would be able to put in place mitigating management actions.

(ii) Sensitivity to interest rate risk

Notwithstanding the market risk exposure previously described, except in the circumstances of interest rate scenarios where the guarantee rates included in contract terms are higher than crediting rates that can be supported from assets held to cover liabilities, the accounting measurement of fixed annuity liabilities of Jackson products is not generally sensitive to interest rate risk. This position derives from the nature of the products and the US GAAP basis of measurement. The GMWB features attaching

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to variable annuity business (other than 'for-life') are accounted for as embedded derivatives which are fair valued and so will be sensitive to changes in interest rate.

Debt securities and related derivatives are marked to fair value. Value movements on derivatives, again net of related changes to amortisation of DAC and deferred tax, are recorded within profit and loss. Fair value movements on debt securities, net of related changes to amortisation of DAC and deferred tax, are recorded within other comprehensive income. The estimated sensitivity of these items and policyholder liabilities to a 1 per cent and 2 per cent decrease (subject to a floor of zero) and increase in interest rates at 31 December 2012 and 2011 is as follows:

	2012				2011*			
	A 2% decrease	A 1% decrease	A 1% increase	A 2% increase	A 2% decrease	A 1% decrease	A 1% increase	A 2% increase
	£m	£m	£m	£m	£m	£m	£m	£m
Profit and loss								
Direct effect								
Derivatives value change	**1,525**	778	(625)	(1,142)	1,549	736	(592)	(1,078)
Policyholder liabilities	**(2,021)**	(871)	610	970	(925)	(446)	395	753
Related effect on amortisation of DAC	**309**	93	(39)	(14)	(132)	(61)	33	46
Pre-tax profit effect	**(187)**		(54)	(186)	492	229	(164)	(279)
Related effect on charge for deferred tax	**65**		19	65	(172)	(80)	57	98
Net profit effect	**(122)**		(35)	(121)	320	149	(107)	(181)
Other comprehensive income								
Direct effect on carrying value of debt securities	**3,873**	2,175	(2,175)	(3,873)	2,679	1,513	(1,513)	(2,679)
Related effect on amortisation of DAC	**(1,332)**	(748)	748	1,332	(954)	(539)	539	954
Related effect on movement in deferred tax	**(889)**	(499)	499	889	(604)	(341)	341	604
Net effect	**1,652**	928	(928)	(1,652)	1,121	633	(633)	(1,121)
Total net effect on shareholders' equity	**1,530**	928	(963)	(1,773)	1,441	782	(740)	(1,302)

* The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

These sensitivities are shown only for interest rates in isolation and do not include other movements in credit risk that may affect credit spreads and valuations of debt securities.

(iii) Currency translation risk

Consistent with the Group's accounting policies, the profits of the Group's US operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2012, the rates were US$1.58 (2011: $1.60 ;2010: US$1.55) and US$1.63 (2011: $1.55; 2010: US$1.57) to £1.00 sterling, respectively. A 10 per cent increase or decrease in these rates would

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reduce or increase profit before tax attributable to shareholders, profit for the year and shareholders' equity attributable to US insurance operations respectively as follows:

	A 10% increase in US$:£ exchange rates		A 10% decrease in US$:£ exchange rates	
	2012	2011*	2012	2011*
	£m	£m	£m	£m
Profit before tax attributable to shareholders note	**(78)**	(44)	**95**	53
Profit for the year	**(56)**	(32)	**69**	39
Shareholders' equity attributable to US insurance operations	**(395)**	(342)	**483**	418

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

Note

Sensitivity on profit before tax ie aggregate of the operating profit based on longer-term investment returns and short-term fluctuations in investment returns.

In addition, the total profit for Jackson is affected by the level of impairment losses on the debt securities portfolio, net effect of market risk arising from the incidence and valuation of guarantee features, guaranteed benefit payments and equity index participation features, offset by variability of benefit related fees and equity derivative hedging performance, short-term value movements on derivatives held to manage the fixed annuity and other general account business, and other temporary value movements on portfolio investments classified as fair value through profit and loss.

(iv) Other sensitivities

As noted in section D1, total profit is very sensitive to market risk on the assets covering liabilities other than variable annuity business segregated in the separate accounts.

As with other shareholder-backed business the profit or loss for Jackson is presented by distinguishing the result for the year between an operating result based on longer-term investment returns and short-term fluctuations in investment returns. In this way the most significant direct effect of market changes that have taken place to the Jackson result are separately identified. The principal determinants of variations in operating profit based on longer-term returns are:

Growth in the size of assets under management covering the liabilities for the contracts in force;

Variations in fees and other income, offset by variations in market value adjustment payments and, where necessary, strengthening of liabilities;

Spread returns for the difference between investment returns and rates credited to policyholders; and

Amortisation of deferred acquisition costs.

For term business, acquisition costs are deferred and amortised in line with expected premiums. For annuity and interest sensitive life business, acquisition costs are deferred and amortised in line with expected gross profits on the relevant contracts. For interest-sensitive business, the key assumption is the expected long-term spread between the earned rate and the rate credited to policyholders, which is

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based on an annual spread analysis. In addition, expected gross profits depend on mortality assumptions, assumed unit costs and terminations other than deaths (including the related charges) all of which are based on a combination of actual experience of Jackson, industry experience and future expectations. A detailed analysis of actual experience is measured by internally developed expense, mortality and persistency studies.

Except to the extent of mortality experience, which primarily affects profits through variations in claim payments and GMDB reserves, the profits of Jackson are relatively insensitive to changes in insurance risk.

Jackson is sensitive to lapse risk. However, Jackson uses swaption derivatives to ameliorate the effect of a sharp rise in interest rates, which would be the most likely cause of a sudden change in policyholder behaviour.

For variable annuity business, the key assumption is the expected long-term level of separate account returns, which for all years included was 8.4 per cent. The impact of using this return is reflected in two principal ways, namely;

through the projected expected gross profits which are used to determine the amortisation of deferred acquisition costs. This is applied through the use of a mean reversion technique which is described in more detail in note D3e above, and;

the required level of provision for guaranteed minimum death benefit claims.

(i) Duration of liabilities

The table below shows the carrying value of policyholder liabilities. The table below also shows the maturity profile of the cash flows used for 2012 and 2011:

	2012			2011		
	Fixed annuity and other business (including GICs and similar contracts)	**Variable annuity**	**Total**	**Fixed annuity and other business (including GICs and similar contracts)**	**Variable annuity**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Policyholder liabilities	**42,963**	49,298	92,261	31,356	37,833	69,189
	%	**%**	**%**	**%**	**%**	**%**
Expected maturity:						
0 to 5 years	**45**	46	46	47	47	47
5 to 10 years	**27**	31	29	27	30	29
10 to 15 years	**12**	13	13	11	13	12

15 to 20 years	**7**	6	6	6	6	6
20 to 25 years	**5**	2	3	5	2	3
Over 25 years	**4**	2	3	4	2	3

The maturity tables shown above have been prepared on a discounted basis. Details of undiscounted cash flows for investment contracts are shown in note G2.

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D4: Asia insurance operations

(a) Summary statement of financial position

	31 December 2012				31 December 2011*
	With-profits businessnote (i)	Unit-linked assets and liabilities	Other business	Total	Total
	£m	£m	£m	£m	£m
Assets					
Intangible assets attributable to shareholders:					
Goodwill			**239**	**239**	235
Deferred acquisition costs and other intangible assets			**908**	**908**	977
Total			**1,147**	**1,147**	1,212
Intangible assets attributable to with-profits funds:					
Deferred acquisition costs and other intangible assets	**72**			**72**	83
Deferred tax assets			**83**	**83**	115
Other non-investment and non-cash assets	**324**	**123**	**670**	**1,117**	1,024
Investments of long-term business and other operations:					
Investment properties			**4**	**4**	10
Financial investments:					
Loansnote (iii)	**600**		**414**	**1,014**	1,233
Equity securities and portfolio holdings in unit trusts	**3,160**	**10,491**	**659**	**14,310**	11,997
Debt securities	**11,495**	**3,194**	**6,713**	**21,402**	17,681
Other investments	**504**	**47**	**406**	**957**	470
Deposits	**165**	**574**	**488**	**1,227**	1,165
Total investments	**15,924**	**14,306**	**8,684**	**38,914**	32,556
Cash and cash equivalents	**524**	**421**	**723**	**1,668**	1,977
Total assets	**16,844**	**14,850**	**11,307**	**43,001**	36,967
Equity and liabilities					

Equity					
Shareholders' equity			**2,529**	**2,529**	2,306
Non-controlling interests			**4**	**4**	5
Total equity			**2,533**	**2,533**	2,311
Liabilities					
Policyholder liabilities and unallocated surplus of with-profits funds:					
Contract liabilities (including amounts in respect of contracts classified as investment contracts under IFRS 4)	**13,388**	**14,028**	**7,185**	**34,601**	30,862
Unallocated surplus of with-profits fundsnote (ii)	**63**			**63**	50
Total	**13,451**	**14,028**	**7,185**	**34,664**	30,912
Operational borrowings attributable to shareholder-financed operations			**7**	**7**	141
Deferred tax liabilities	**384**	**46**	**158**	**588**	506
Other non-insurance liabilities	**3,009**	**776**	**1,424**	**5,209**	3,097
Total liabilities	**16,844**	**14,850**	**8,774**	**40,468**	34,656
Total equity and liabilities	**16,844**	**14,850**	**11,307**	**43,001**	36,967

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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(i) The statement of financial position for with-profits business comprises the with-profits assets and liabilities of the Hong Kong, Malaysia and Singapore with-profits operations. Assets and liabilities of other participating business are included in the column for 'Other business'.

(ii) For the purposes of the presentation of unallocated surplus of with-profits within the statement of financial position, the Hong Kong branch balance is reported within the unallocated surplus of the PAC with-profits sub-fund of the UK insurance operations.

(iii) Asia insurance operations

The loans of the Group's Asia insurance operations comprise:

	2012	2011
	£m	£m
Mortgage loans	**43**	31
Policy loans	**610**	572
Other loans	**361**	630
Total Asia insurance operations loans	**1,014**	1,233

The mortgage and policy loans are secured by properties and life insurance policies respectively.

The majority of the other loans are commercial loans held by the Malaysia operation and which are all investment graded by two local rating agencies.

Summary policyholder liabilities (net of reinsurance) and unallocated surplus

At 31 December 2012, the policyholder liabilities net of reinsurance of £175 million (2011: £151 million) and unallocated surplus for Asia operations of £34.5 billion (2011: £30.8 billion) comprised the following:

2012	2011
£m	£m

Singapore	**10,731**	9,323
Hong Kong	**8,610**	8,279
Malaysia	**3,336**	2,829
Indonesia	**2,110**	1,809
Korea	**2,131**	1,852
Taiwan	**1,931**	1,429
Other countries	**5,640**	5,240
Total Asia operations	**34,489**	30,761

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(b) Reconciliation of movement in policyholder liabilities and unallocated surplus of with-profits funds

A reconciliation of the total policyholder liabilities and unallocated surplus of with-profits funds of Asia insurance operations from the beginning of the year to the end of the year is as follows:

	With-profits business	Unit-linked liabilities	Other business	Total
	£m	£m	£m	£m
At 1 January 2011	11,024	12,724	4,992	28,740
Comprising:				
Policyholder liabilities	10,958	12,724	4,992	28,674
Unallocated surplus of with-profits funds	66			66
Premiums				
New business	162	1,136	723	2,021
In-force	1,110	1,163	785	3,058
	1,272	2,299	1,508	5,079
Surrenders[note (c)]	(502)	(1,490)	(245)	(2,237)
Maturities/Deaths	(431)	(39)	(194)	(664)
Net flows[note (b)]	339	770	1,069	2,178
Shareholders' transfers post tax	(30)			(30)
Investment-related items and other movements	1,274	(1,154)	245	365
Foreign exchange translation differences[note (a)]	36	(325)	(52)	(341)
At 31 December 2011/1 January 2012	**12,643**	**12,015**	**6,254**	**30,912**
Comprising:				
Policyholder liabilities	**12,593**	**12,015**	**6,254**	**30,862**
Unallocated surplus of with-profits funds	**50**			**50**

Premiums				
New business	**216**	**1,336**	**636**	**2,188**
In-force	**1,263**	**1,292**	**877**	**3,432**
	1,479	**2,628**	**1,513**	**5,620**
Surrenders[note (c)]	**(608)**	**(1,675)**	**(258)**	**(2,541)**
Maturities/Deaths	**(432)**	**(30)**	**(196)**	**(658)**
Net flows[note (b)]	**439**	**923**	**1,059**	**2,421**
Shareholders' transfers post tax	**(31)**			**(31)**
Investment-related items and other movements[note (d)]	**639**	**1,451**	**88**	**2,178**
Foreign exchange translation differences[note (a)]	**(239)**	**(361)**	**(216)**	**(816)**
At 31 December 2012	**13,451**	**14,028**	**7,185**	**34,664**
Comprising:				
Policyholder liabilities	**13,388**	**14,028**	**7,185**	**34,601**
Unallocated surplus of with-profits funds	**63**			**63**
Average policyholder liability balances*				
2012	**12,990**	**13,022**	**6,720**	**32,732**
2011	11,775	12,370	5,623	29,768

* Averages have been based on opening and closing balances and exclude unallocated surplus of with-profits funds.

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(a)

Movements in the year have been translated at the average exchange rates for the year ended 31 December 2012. The closing balance has been translated at the closing spot rates as at 31 December 2012. Differences upon retranslation are included in foreign exchange translation differences.

(b)

Net flows have increased by £243 million to £2,421 million in 2012 compared with £2,178 million in 2011 reflecting increased flows from new business and growth in the in-force books.

(c)

In 2012 the rate of surrenders for shareholder-backed business (expressed as a percentage of opening liabilities) was 10.6 per cent (2011: 9.8 per cent). Excluding India where the market has been going through a significant period of change following regulatory changes in 2010, the surrender rate in 2012 was at 9.7 per cent (2011: 9.6 per cent). For with-profits business, surrenders have increased from £502 million in 2011 to £608 million in 2012, primarily as a result of certain products in Hong Kong reaching their five year anniversary, the point at which some product features trigger.

(d)

Positive investment-related items and other movements of £2,178 million in 2012 primarily reflects improvements in the Asia equity market.

(c) Information on credit risks of debt securities

The following table summarises the credit quality of the debt securities of the Asia insurance operations as at 31 December 2012 by rating agency ratings:

	With-profits business	Unit-linked assets	Other business	2012 Total	2011 Total
	£m	£m	£m	£m	£m
S&P AAA	**675**	**19**	**91**	**785**	1,423
S&P AA+ to AA-	**2,960**	**466**	**2,097**	**5,523**	3,843
S&P A+ to A-	**2,059**	**279**	**944**	**3,282**	3,055
S&P BBB+ to BBB-	**1,377**	**112**	**417**	**1,906**	1,451
S&P Other	**1,443**	**815**	**874**	**3,132**	2,137
	8,514	**1,691**	**4,423**	**14,628**	11,909
Moody's Aaa	**700**	**215**	**474**	**1,389**	1,489
Moody's Aa1 to Aa3	**139**	**34**	**98**	**271**	128
Moody's A1 to A3	**93**	**14**	**62**	**169**	304

Moody's Baa1 to Baa3	**196**	**122**	**57**	**375**	131
Moody's Other	**98**	**12**	**2**	**112**	59
	1,226	**397**	**693**	**2,316**	2,111
Fitch	**322**	**93**	**118**	**533**	351
Other	**1,433**	**1,013**	**1,479**	**3,925**	3,310
Total Asia debt securities	**11,495**	**3,194**	**6,713**	**21,402**	17,681

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The following table analyses debt securities of 'Other business' which are not externally rated:

	2012	2011
	£m	£m
Government bonds	**287**	244
Corporate bonds rated as investment grade by local external ratings agencies	**1,069**	776
Other	**123**	45
	1,479	1,065

(d) Products and guarantees

The life insurance products offered by the Group's Asia operations include a range of with-profits and non-participating term, whole life, endowment and unit-linked policies. The Asia operations also offer health, disability, critical illness and accident coverage to supplement its core life products.

The terms and conditions of the contracts written by the Asia operations and, in particular, the products' options and guarantees, vary from territory to territory depending upon local market circumstances.

In general terms, the Asia participating products provide savings and protection where the basic sum assured can be enhanced by a profit share (or bonus) from the underlying fund as determined at the discretion of the insurers. The Asia operations' non-participating term, whole life and endowment products offer savings and/or protection where the benefits are guaranteed or determined by a set of defined market-related parameters. Unit-linked products combine savings with protection, the cash value of the policy depends on the value of the underlying unitised funds. Health and Protection (H&P) policies provide mortality or morbidity benefits and include health, disability, critical illness and accident coverage. H&P products are commonly offered as supplements to main life policies but can be sold separately.

Subject to local market circumstances and regulatory requirements, the guarantee features described in note D2(d) in respect of UK business broadly apply to similar types of participating contracts written in the Hong Kong branch, Singapore and Malaysia. Participating products have both guaranteed and non-guaranteed elements.

Non-participating long-term products are the only ones where the Group is contractually obliged to provide guarantees on all benefits. Unit-linked products have the lowest level of guarantee.

Product guarantees in Asia can be broadly classified into four main categories, namely premium rate, cash value and interest rate guarantees, policy renewability and convertibility options.

The risks on death coverage through premium rate guarantees are low due to appropriate product pricing.

Cash value and interest rate guarantees are of three types:

Maturity values

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Maturity values are guaranteed for non-participating products and on the guaranteed portion of participating products. Declared annual bonuses are also guaranteed once vested. Future bonus rates and cash dividends are not guaranteed on participating products;

Surrender values

Surrender values are guaranteed for non-participating products and on the guaranteed portion of participating products. The surrender value of declared reversionary bonuses are also guaranteed once vested. Market value adjustments and surrender penalties are used where the law permits such adjustments in cash values;

Interest rate guarantees
It is common in Asia for regulations or market-driven demand and competition to provide some form of capital value protection and minimum crediting interest rate guarantees. This would be reflected within the guaranteed maturity and surrender values.

The guarantees are borne by shareholders for non-participating and investment-linked (non-investment guarantees only) products. Participating product guarantees are predominantly supported by the segregated life funds and their estates.

Whole of life contracts with floor levels of policyholder benefits that accrue at rates set at inception and do not vary subsequently with market conditions are written in the Korean life operations though this is not to a significant extent as Korea has a much higher proportion of linked and health business. The Korean business has non-linked liabilities and linked liabilities at 31 December 2012 of £505 million and £1,628 million respectively (2011: £447 million and £1,407 million respectively).

The other area of note in respect of guarantees is the Japanese business where pricing rates are higher than current bond yields. Lapse risk is a feature in that policyholders could potentially surrender their policies on guaranteed terms if interest rates significantly increased leaving the potential for losses if bond values had depreciated significantly. However, the business is matched to a relatively short realistic liability duration.

The method for determining liabilities of insurance contracts for UK GAAP, and IFRS, purposes for some Asia operations is based on US GAAP principles and this method applies to contracts with cash value and interest rate guarantees. Following standard US GAAP procedure, premium deficiency reserve calculations are performed each year to establish whether the carrying values of the liabilities are sufficient.

On the US GAAP basis the calculations are deterministic, that is to say based on a single set of projections, and expected long-term rates of return are applied.

(e) Process for setting assumptions and determining liabilities

The future policyholder benefit provisions for Asia businesses in the Group's IFRS accounts and previously under the MSB, are determined in accordance with methods prescribed by local GAAP adjusted to comply, where necessary, with UK GAAP.

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For some countries in Asia where local GAAP is not well established and in which the business written is primarily non-participating and linked business, US GAAP is used as the most appropriate reporting basis. This basis is applied in India, Japan, Taiwan and until 2012, Vietnam. Under this basis, the future policyholder benefit provisions for non-linked business are determined using the net level premium method, with an allowance for surrenders, maintenance and claims expenses. Rates of interest used in establishing the policyholder benefit provisions vary by operation depending on the circumstances attaching to each block of business. In Vietnam, the Company improved its estimation basis for liabilities in 2012 from one determined substantially by reference to US GAAP requirements. After making this change, the estimation basis for Vietnam is aligned substantially with that used in Singapore, Malaysia and some other Asia operations.

(f) Reinsurance

The Asia businesses cede only minor amounts of business outside the Group with immaterial effects on reported profit. During 2012, reinsurance premiums for externally ceded business were £178 million (2011: £226 million; 2010: £146 million) and the reinsurance assets were £175 million (2011: £151 million) in aggregate.

(g) Effect of changes in bases, estimates and assumptions used to measure insurance assets and liabilities

In 2012, the IFRS operating profit based on longer-term investment returns for Asia insurance operations included a net £48 million credit (2011: £38 million) representing a small number of non-recurring items that are not anticipated to re-occur in subsequent periods.

Separately, the IFRS policyholder liabilities of the shareholder-backed non-linked business of the Group's Hong Kong operation are measured on a prospective net premium valuation approach with zero allowance for lapses. In 2012, the basis of determining the valuation rate of interest has been altered to align with a permitted practice of the Hong Kong authorities for regulatory reporting. The main change is to apply a valuation rate of interest that incorporates a reinvestment yield that is weighted by reference to current and the historical three year average rather than the year end rate. The change reduced the carrying value of policyholder liabilities at 31 December 2012 by £95 million. This benefit is included within the short-term fluctuations in investment returns in the Group's supplementary analysis of profit.

In 2010, one-off changes made to reserving assumptions resulted in a release from liabilities of £19 million.

(h) Exposure and sensitivity of IFRS basis profit and shareholders' equity to market and other risks

The Asia operations sell with-profits and unit-linked policies and, although the with-profits business generally has a lower terminal bonus element than in the UK, the investment portfolio still contains a proportion of equities. Non-participating business is largely backed by debt securities or deposits. The exposure to market risk of the Group arising from its Asia operations is therefore at modest levels. This

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arises from the fact that the Asia operations have a balanced portfolio of with-profits, unit-linked and other types of business.

In Asia, adverse persistency experience can impact the IFRS profitability of certain business written in the region. This risk is managed at a business unit level through regular monitoring of experience and the implementation of management actions as necessary. These actions could include product enhancements, increased management focus on premium collection as well as other customer retention efforts. The potential financial impact of lapses is often mitigated through the specific features of the products, eg surrender charges.

(i) Sensitivity of profit and shareholders' equity to risks other than currency translation risk

With-profits business

Similar principles to those explained for UK with-profits business apply to profit emergence for the Asia with-profits business.

Correspondingly, the profit emergence reflects bonus declaration and is relatively insensitive to period by period fluctuations in insurance risk or interest rate movements.

Unit-linked business

As for the UK insurance operations, for unit-linked business, the main factor affecting the profit and shareholders' equity of the Asia operations is investment performance through asset management fees. The sensitivity of profits and shareholders' equity to changes in insurance risk, interest rate risk and credit risk are not material.

Other business

Interest rate risk

Asia operations offer a range of insurance and investment products, predominantly with-profits and non-participating term, whole life endowment and unit-linked. Excluding with-profit and unit-linked business, the results of the Asia business are sensitive to the vagaries of routine movements in interest rates.

For the purposes of analysing sensitivity to variations in interest rates, reference has been made to the movements in the 10-year government bond rates of the territories. At 31 December 2012, 10-year government bond rates vary from territory to territory and range from 0.60 per cent to 9.50 per cent (2011: 0.99 per cent to 12.88 per cent).

For the sensitivity analysis as at 31 December 2011 as shown in the table below, for the majority of the territories, a movement of 1 per cent in the 10-year government bond rate has been used. Exceptions to this approach are for Japan and Taiwan where a movement of 0.5 per cent has been used. Following falls in interest rates in many of the territories during 2012, the approach was altered such that the reasonably possible interest rate movement used is one per cent for all territories but subject to a floor of zero where the bond rates are currently below 1 per cent. This revised approach was applied in estimating the sensitivity at 31 December 2012.

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The estimated sensitivity to the decrease and increase in interest rates at 31 December 2012 and 2011 is as follows:

	2012		2011	
	Decrease of 1%	Increase of 1%	Decrease of 1% *	Increase of 1% *
	£m	£m	£m	£m
Pre-tax profit	**216**	**(269)**	73	(159)
Related deferred tax (where applicable)	**(56)**	**53**	(22)	34
Net effect on profit and shareholders' equity	**160**	**(216)**	51	(125)

* Except for Japan and Taiwan using 0.5 per cent sensitivity.

The pre-tax impacts, if they arose, would mostly be recorded within the category short-term fluctuations in investments returns in the Group's segmental analysis of profit before tax.

The degree of sensitivity of the results of the non-linked shareholder-backed business of the Asia operations to movements in interest rates depends upon the degree to which the liabilities under the 'grandfathered' IFRS 4 measurement basis reflects market interest rates from period to period. For example for those countries, such as those applying US GAAP, the results can be more sensitive as the effect of interest rate movements on the backing investments may not be offset by liability movements.

Equity price risk

The non-linked shareholder business has limited exposure to equity and property investment (£663 million at 31 December 2012). Generally changes in equity and property investment values are not directly offset by movements in policyholder liabilities.

The estimated sensitivity to a 10 and 20 per cent change in equity and property prices for shareholder-backed Asia other business, which would be reflected in the short-term fluctuation component of the Group's segmental analysis of profit before tax, at 31 December 2012 and 2011 would be as follows:

	2012		2011	
	Decrease of 20%	Decrease of 10%	Decrease of 20%	Decrease of 10%
	£m	£m	£m	£m
Pre-tax profit	**(134)**	**(67)**	(120)	(60)
Related deferred tax (where applicable)	**31**	**15**	24	12
Net effect on profit and shareholders' equity	**(103)**	**(52)**	(96)	(48)

A 10 or 20 per cent increase in their value would have an approximately equal and opposite effect on profit and shareholders' equity to the sensitivities shown above. The market risk sensitivities shown above reflect the impact of temporary market movements and, therefore, the

primary effect of such movements would, in the Group's segmental analysis of profits, be included within the short-term fluctuations in investment returns.

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In the equity risk sensitivity analysis shown above, the Group has considered the impact of an instantaneous 20 per cent fall in equity markets. If equity markets were to fall by more than 20 per cent, the Group believes that this would not be an instantaneous fall but rather this would be expected to occur over a period of time during which the Group would be able to put in place mitigating management actions.

Insurance risk

Many of the territories in Asia are exposed to mortality/morbidity risk and provision is made within policyholder liabilities on a prudent regulatory basis to cover the potential exposure. If these prudent assumptions were strengthened by 5 per cent then it is estimated that post tax profit would be decreased by approximately £30 million (2011: £27 million). Mortality and morbidity has a symmetrical effect on the portfolio and any weakening of these assumptions would have a similar equal and opposite impact.

(ii) Sensitivity of IFRS basis profit and shareholders' equity to currency translation risk

Consistent with the Group's accounting policies, the profits of the Asia insurance operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. For 2012, the rates for the most significant operations are given in note B4.

A 10 per cent increase or decrease in these rates would have reduced or increased profit before tax attributable to shareholders, profit for the year and shareholders' equity, excluding goodwill, attributable to Asia operations respectively as follows:

	A 10% increase in local currency to £ exchange rates		**A 10% decrease in local currency to £ exchange rates**	
	2012	**2011**	**2012**	**2011**
	£m	**£m**	**£m**	**£m**
Profit before tax attributable to shareholders [note]	**(90)**	(57)	**110**	70
Profit for the year	**(75)**	(46)	**92**	56
Shareholders' equity, excluding goodwill, attributable to Asia operations	**(243)**	(228)	**297**	278

Note

Sensitivity on profit (loss) before tax ie aggregate of the operating profit based on longer-term investment returns and short-term fluctuations in investment returns.

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(i) Duration of liabilities

The table below shows the carrying value of policyholder liabilities. The table below also shows the maturity profile of the cash flows, taking account of expected future premiums and investment returns for 2012 and 2011:

	2012	2011
	£m	£m
Policyholder liabilities	**34,601**	30,862
Expected maturity:	%	%
0 to 5 years	**23**	22
5 to 10 years	**19**	19
10 to 15 years	**17**	15
15 to 20 years	**13**	13
20 to 25 years	**9**	10
Over 25 years	**19**	21

D5: Capital position statement for life assurance businesses

The primary purpose of this section is to meet the disclosure requirements of FRS 27, the UK GAAP Standard on Life Assurance. Prudential, together with other major UK life assurers undertook to the UK Accounting Standards Board in 2004 to adopt this standard for Group IFRS reporting. Under the disclosure requirements of FRS 27 the capital position statement and related footnotes are prepared by reference to local regulation.

(a) Summary statement

The Group's estimated capital position for life assurance businesses with reconciliations to shareholders' equity is shown below. As noted above, available capital for each fund or group of

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companies has been determined by reference to local regulation at 31 December 2012 and 2011. Group capital requirements also apply as discussed in note D5(b)(iv).

	2012									
	SAIF	WPSF note (ii)	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note (ii)	Jackson	Asia life assurance subsidiaries	Total life assurance operations	M&G (including Prudential Capital)	Parent company and other subsidiaries and funds	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Group shareholders' equity										
Held outside long-term funds:										
Net assets				**920**	**4,343**	**2,290**	**7,553**	**393**	**(1,143)**	**6,803**
Goodwill						**239**	**239**	**1,153**	**77**	**1,469**
Total				**920**	**4,343**	**2,529**	**7,792**	**1,546**	**(1,066)**	**8,272**
Held in long-term fundsnote (iii)				**2,087**			**2,087**			**2,087**
Total Group shareholders' equity				**3,007**	**4,343**	**2,529**	**9,879**	**1,546**	**(1,066)**	**10,359**
Adjustments to regulatory basis										
Unallocated surplus of with-profits fundsnote (v)		**10,526**	**10,526**			**63**	**10,589**			
Shareholders' share of realistic liabilities		**(2,469)**	**(2,469)**				**(2,469)**			
Deferred acquisition costs of non-participating business not recognised for regulatory reporting purposes and goodwill		**(6)**	**(6)**	**(103)**	**(3,199)**	**(893)**	**(4,201)**			

Jackson surplus notesnote (iv)				**153**		**153**
Investment and policyholder liabilities valuation differences between IFRS and regulatory basis for Jacksonnote (viii)				**696**		**696**
Adjustment from IAS 19 basis pension deficit attributable to WPSF to pension liability for regulatory purposesnote (vii)	**(107)**	**(107)**				**(107)**
Valuation difference on PAL between IFRS basis and regulatory basis	**(215)**	**(215)**				**(215)**
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis)note (v)	**(729)**	**(729)**	**(534)**	**906**	**(78)**	**(435)**
Total adjustments	**7,000**	**7,000**	**(637)**	**(1,444)**	**(908)**	**4,011**
Total available capital resources of life assurance businesses on local regulatory bases	**7,000**	**7,000**	**2,370**	**2,899**	**1,621**	**13,890**

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	2012						
	SAIF	WPSF note (i)	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note (ii)	Jackson	Asia life assurance subsidiaries	Total life assurance operations
	£m	£m	£m	£m	£m	£m	£m
Policyholder liabilities							
With-profits liabilities of UK Regulated with-profits funds:							
Insurance contracts	**7,217**	**29,353**	**36,570**			**6,696**	**43,266**
Investment contracts (with discretionary participation features)	**352**	**33,112**	**33,464**			**95**	**33,559**
Total	**7,569**	**62,465**	**70,034**			**6,791**	**76,825**
Other liabilities:							
Insurance contracts:							
With-profits liabilities of non-UK regulated funds						**6,597**	**6,597**
Unit-linked, including variable annuity		**29**	**29**	**6,086**	**49,298**	**14,028**	**69,441**
Other life assurance business	**309**	**14,013**	**14,322**	**27,259**	**40,894**	**7,058**	**89,533**
Investment contracts without discretionary participation features (principally unit-linked and similar contracts in the UK and GIC liabilities of Jackson)[note vi]		**22**	**22**	**16,160**	**2,069**	**127**	**18,378**
Total	**309**	**14,064**	**14,373**	**49,505**	**92,261**	**27,810**	**183,949**
Total policyholder liabilities shown in the consolidated statement of financial position	**7,878**	**76,529**	**84,407**	**49,505**	**92,261**	**34,601**	**260,774**

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	2011*									
	SAIF	WPSF note (i)	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note (ii)	Jackson	Asia life assurance subsidiaries	Total life assurance operations	M&G (including Prudential Capital)	Parent company and shareholders' equity of other subsidiaries and funds	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Group shareholders' equity										
Held outside long-term funds:										
Net assets				930	3,761	2,071	6,762	229	(1,514)	5,477
Goodwill						235	235	1,153	77	1,465
Total				930	3,761	2,306	6,997	1,382	(1,437)	6,942
Held in long-term fundsnote (iii)				1,622			1,622			1,622
Total Group shareholders' equity				2,552	3,761	2,306	8,619	1,382	(1,437)	8,564
Adjustments to regulatory basis										
Unallocated surplus of with-profits fundsnote (v)		9,165	9,165			50	9,215			
Shareholders' share of realistic liabilities		(2,394)	(2,394)				(2,394)			
Deferred acquisition costs of non-participating business not recognised for regulatory reporting purposes and goodwill		(6)	(6)	(111)	(3,095)	(929)	(4,141)			
Jackson surplus notesnote (iv)					160		160			
Investment and policyholder liabilities valuation differences between IFRS and regulatory basis for Jacksonnote (vii)					1,002		1,002			

Adjustment from IAS 19 basis pension deficit attributable to WPSF to pension liability for regulatory purposes	16	16				16
Valuation difference on PAL between IFRS basis and regulatory basis	(640)	(640)				(640)
Other adjustments to restate these amounts to a regulatory basis (with SAIF and the WPSF on a Peak 2 realistic basis)note (v)	(2)	(2)	(504)	699	66	259
Total adjustments	6,139	6,139	(615)	(1,234)	(813)	3,477
Total available capital resources of life assurance businesses on local regulatory bases	6,139	6,139	1,937	2,527	1,493	12,096

*

The 2011 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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	2011						
	SAIF	WPSF note (i)	Total PAC with-profits fund	Other UK life assurance subsidiaries and funds note (ii)	Jackson	Asia life assurance subsidiaries	Total life assurance operations
	£m	£m	£m	£m	£m	£m	£m
Policyholder liabilities							
With-profits liabilities of UK Regulated with-profits funds:							
Insurance contracts[note (viii)]	7,934	30,077	38,011			6,777	44,788
Investment contracts (with discretionary participation features)	412	28,936	29,348			397	29,745
Total	8,346	59,013	67,359			7,174	74,533
Other liabilities:							
Insurance contracts:							
With-profits liabilities of non-UK regulated funds						5,419	5,419
Unit-linked, including variable annuity[note (viii)]		26	26	6,387	37,833	12,015	56,261
Other life assurance business	209	13,365	13,574	24,734	29,445	6,142	73,895
Investment contracts without discretionary participation features (principally unit-linked and similar contracts in the UK and GIC liabilities of Jackson)[note (vi)]		17	17	14,927	1,911	112	16,967
Total	209	13,408	13,617	46,048	69,189	23,688	152,542
Total policyholder liabilities shown in the consolidated statement of financial position	8,555	72,421	80,976	46,048	69,189	30,862	227,075

Notes

(i) WPSF unallocated surplus includes amounts related to the Hong Kong branch. Policyholder liabilities of the Hong Kong branch are included in the amounts of Asian life assurance subsidiaries.

(ii) Excluding PAC shareholders' equity that is included in 'parent company and shareholders' equity of other subsidiaries and funds'.

(iii)

The term shareholders' equity held in long-term funds refers to the excess of assets over liabilities attributable to shareholders of funds which are required by law to be maintained ring-fenced with segregated assets and liabilities.

(iv)

For regulatory purposes the Jackson surplus notes are accounted for as capital.

(v)

Other adjustments to shareholders' equity and unallocated surplus include amounts for the value of non-participating business for UK regulated with-profits funds, deferred tax, admissibility and other items measured differently on the regulatory basis. For Jackson the principal reconciling item is deferred tax related to the differences between IFRS and regulatory basis as shown in the table above and other methodology differences.

(vi)

Insurance business accounted for as financial instruments under IAS 39.

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(vii) The investment and policyholder liabilities valuation difference between IFRS and regulatory bases for Jackson is mainly due to not all investments being carried at fair value under the regulatory basis and also due to the valuation difference on annuity reserves.

(viii) The allocation between the with-profits liabilities and unit-linked liabilities within the WPSF column have been adjusted for those previously published to align with the basis of presentation applied in 2012.

(b) Basis of preparation, capital requirements and management

Each of the Group's long-term business operations is capitalised to a sufficiently strong level for its individual circumstances. Details of the Group's major operations are shown below.

(i) UK insurance operations

The FSA rules which govern the Prudential regulation of insurance form part of the Prudential Sourcebook for Insurers, the General Prudential Sourcebook and Interim Prudential Sourcebook for Insurers. Overall, the net requirements of the General Prudential Sourcebook are intended to align the capital adequacy requirements for insurance business more closely with those of banking and investment firms and building societies, for example, by addressing tiers of capital, rather than looking at net admissible assets. An insurer must hold capital resources equal at least to the Minimum Capital Requirement (MCR).

The Prudential Sourcebook for Insurers also contains rules on Individual Capital Assessments. Under these rules and the rules of the General Prudential Sourcebook all insurers must assess for themselves the amount of capital needed to back their business. If the FSA views the results of this assessment as insufficient, it may draw up its own Individual Capital Guidance for a firm, which can be superimposed as a requirement.

PAC WPSF and SAIF

Under FSA rules, insurers with with-profits liabilities of more than £500 million must hold capital equal to the higher of the MCR and the Enhanced Capital Requirement (ECR). The ECR is intended to provide a more risk responsive and 'realistic' measure of a with-profit insurer's capital requirements, whereas the MCR is broadly speaking equivalent to the previous required minimum margin under the Interim Prudential Sourcebook and satisfies the minimum EU Standards.

Determination of the ECR involves the comparison of two separate measurements of the firm's resources requirement, which the FSA refers to as the 'twin peaks' approach.

The two separate peaks are:

(i) The requirement comprised by the mathematical reserves plus the 'Long-Term Insurance Capital Requirement' (LTICR), together known as the 'regulatory peak'; and

(ii)

a calculation of the 'realistic' present value of the insurer's expected future contractual liabilities together with projected 'fair' discretionary bonuses to policyholders, plus a risk capital margin, together known as the 'realistic peak'.

Available capital of the WPSF and SAIF of £7.0 billion (2011: £6.1 billion) represents the excess of assets over liabilities on the FSA realistic basis. Unlike the previously discussed FRS 27 basis, realistic

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liabilities on the regulatory basis include the shareholders' share of future bonuses. These amounts are shown before deduction of the risk capital margin (RCM) which is estimated to be £1.5 billion at 31 December 2012 (2011: £2.0 billion).

The FSA's basis of setting the RCM is to target a level broadly equivalent to a Standard & Poor's credit rating of BBB and to judge this by ensuring there are sufficient assets to absorb a one in 200 year event. The RCM calculation achieves this by setting rules for the determination of margins to cover defined stress changes in asset values and yields for market risk, credit risk and termination risk for with-profits policies.

PAC has discretion in its management actions in the case of adverse investment conditions. Management actions encompass, but are not confined to, investment allocation decisions, levels of reversionary bonuses, crediting rates and total claim values.

Other UK life assurance subsidiaries and funds

The available capital of £2,370 million (2011: £1,937 million) reflects the excess of regulatory basis assets over liabilities of the subsidiaries and funds, before deduction of the capital resources requirement of £1,376 million (2011: £1,194 million).

The capital resources requirement for these companies broadly reflects a formula which, for active funds, equates to a percentage of regulatory reserves plus a percentage of death strains. Death strains represent the payments made to policyholders upon death in excess of amounts explicitly allocated to fund the provisions for policyholders' claims and maturities.

(ii) Jackson

The regulatory framework for Jackson is governed by the requirements of the US NAIC approved risk-based capital standards. Under these requirements life insurance companies report using a formula-based capital standard that they calculate by applying factors to various asset, premium and reserve items and separate model based calculations of risk associated primarily with variable annuity products. The risk-based capital formula takes into account the risk characteristics of a company, including asset risk, insurance risk, interest rate risk, market risk and business risk.

The available capital of Jackson shown above of £2,899 million (2011: £2,527 million) reflects US regulatory basis assets less liabilities including asset valuation reserves. The asset valuation reserve is designed to provide for future credit-related losses on debt securities and losses on equity investments. Available capital includes a reduction for the effect of the interest maintenance reserve, which is designed by state regulators to defer recognition of non-credit related realised capital gains and losses and to recognise them rateably in the future.

Jackson's risk-based capital ratio is significantly in excess of regulatory requirements. At 31 December 2012, Jackson had a permitted practice in effect as granted by the local regulator allowing Jackson to carry certain interest rate swaps at book value, as if statutory hedge accounting were in place, instead of at fair value as would have been otherwise required. Jackson was also required to demonstrate the effectiveness of its interest rate swap programme pursuant to the Michigan Insurance

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Code. The total effect of this permitted practice net of tax was to decrease statutory surplus by £357 million at 31 December 2012.

Michigan insurance law specifically allows value of business acquired ("VOBA") as an admitted asset as long as certain criteria are met. US NAIC standards limit the admitted amount of goodwill/VOBA generally to 10 per cent of capital and surplus. At 31 December 2012, Jackson reported £289 million of statutory basis VOBA as a result of the REALIC acquisition, which is fully admissible under Michigan insurance law.

(iii) Asia operations

The available capital shown above of £1,621 million (2011: £1,493 million) represents the excess of local regulatory basis assets over liabilities before deduction of required capital of £661 million (2011: £608 million). These amounts have been determined applying the local regulations in each of the operations.

The businesses in Asia are subject to local capital requirements in the jurisdictions in which they operate. The Hong Kong business branch of PAC and its capital requirements are subsumed within those of the PAC long-term fund. For the other material Asia operations, the details of the basis of determining regulatory capital and regulatory capital requirements are as follows:

Singapore

A risk-based regulatory framework applies in Singapore.

For participating business, a gross premium reserve, determined using prudent best estimate assumptions and which makes allowance for future bonus, is held. The amount held is subject to a minimum of the higher of the assets attributed to participating business and a gross premium reserve calculated on specified assumptions, but without allowance for future bonus, that include prescribed provisions for adverse deviations (PADs).

For non-participating business, gross premium reserves are held. For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

Indonesia

Solvency capital is determined using risk-based capital approach. Insurance companies in Indonesia are expected to maintain the level of net assets above 120 per cent of solvency capital. Due to the 2008 financial crisis, the local regulator provided relief in solvency capital and the measure continued until 1 January 2012 when it was withdrawn. The withdrawal of this temporary relief did not have a significant impact on the Group's Indonesia business.

Japan

Mathematical reserves for traditional business are determined on a net premium basis using prescribed mortality and interest rates. Interest rates reflect the original pricing assumptions.

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For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

Solvency capital is determined using a risk-based capital approach. The adjusted solvency capital assets of the Company must exceed 200 per cent of the risk related capital requirement value at risk. A number of changes to the risk-based capital rules in Japan were effective in April 2012 but the changes did not have a significant impact on the Group's Japan business.

Malaysia

A risk-based capital framework applies in Malaysia.

For participating business, a gross premium reserve on the guaranteed and non-guaranteed benefits determined using best estimate assumptions is held. The amount held is subject to a minimum of a gross premium reserve on the guaranteed benefits, determined using best estimate assumptions along with provisions of risk margin for adverse deviations discounted at the risk-free rate.

For non-participating business, gross premium reserves determined using best estimate assumptions along with provisions of risk margin for adverse deviations discounted at the risk-free rate are held. For linked business the value of units is held together with a non-unit reserve calculated in accordance with standard actuarial methodology.

Participating fund surplus is not allowed to be used to support deficit (if any) and capital requirement of the non-participating business. The capital requirement is calculated based on a prescribed series of risk charges. The local regulator has set a Supervisory Target Capital Level of 130 per cent below which supervisory actions of increasing intensity will be taken. Each insurer is also required to set its own Individual Target Capital Level to reflect its own risk profile and this is expected to be higher than the Supervisory Target Capital Level.

Vietnam

Mathematical reserves are calculated using a modified net premium approach, set using assumptions agreed with the regulator.

The capital requirement is determined as four per cent of reserves plus a specified percentage of 0.1 per cent of sums at risk for policies with original term less than or equal to five years or 0.3 per cent of sums at risk for policies with original term of more than five years. An additional capital requirement of Vietnamese Dong 200 billion is also required for companies transacting unit-linked business.

Korea

Policy reserves for traditional business are determined on net premium reserve basis using pricing mortality and prescribed standard interest rates.

For linked business, the value of units is held together with the non-unit reserves calculated in accordance with regulatory standard actuarial methodology.

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A risk-based capital framework applies in Korea. Under this risk based framework, insurance companies in Korea are expected to maintain a level of free surplus in excess of the capital requirements with the general target level of solvency margin being in excess of 150 per cent of the risk-based capital.

(iv) Group capital requirements

In addition to the requirements at individual company level, FSA requirements under the IGD apply additional prudential requirements for the Group as a whole. Discussion of the Group's estimated IGD position at 31 December 2012, together with market risk sensitivity disclosure provided to key management, is provided in the Risk and Capital Management section under Group Risk Framework in Item 4 'Information on the Company.

(c) Movements in total available capital

Total available capital for the Group's life assurance operations has changed as follows:

	2012				
	WPSF note (i)	Other UK life assurance subsidiaries and funds note (iii)	Jackson note (ii)	Asia life assurance subsidiaries note (iv)	Group total
	£m	£m	£m	£m	£m
Available capital at 31 December 2011	**6,139**	**1,937**	**2,527**	**1,493**	**12,096**
Changes in assumptions	**(136)**	**(145)**		**30**	**(251)**
Changes in management policy	**500**			**(24)**	**476**
Changes in regulatory requirements				**27**	**27**
New business and other factors[note (v)]	**497**	**578**	**372**	**95**	**1,542**
Available capital at 31 December 2012	**7,000**	**2,370**	**2,899**	**1,621**	**13,890**

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	2011				
	WPSF note (i)	Other UK life assurance subsidiaries and funds note (iii)	Jackson note (ii)	Asian life assurance subsidiaries note (iv)	Group total
	£m	£m	£m	£m	£m
Available capital at 31 December 2010	6,800	1,707	2,907	1,378	12,792
Changes in assumptions	(60)	38		(32)	(54)
Changes in management policy	(15)				(15)
Changes in regulatory requirements				17	17
New business and other factors note (v)	(586)	192	(380)	130	(644)
Available capital at 31 December 2011	6,139	1,937	2,527	1,493	12,096

Notes

(i)

WPSF

The increase in 2012 of £861 million reflects primarily the positive impact of investment returns earned on the opening available capital. The decrease in 2011 of £661 million reflects primarily the negative effect of the lower interest rate used to value projected policyholder benefit payments, partially offset by the positive impact of investment returns earned on the opening available capital.

(ii)

Jackson

The increase of £372 million in 2012 reflects an underlying increase of £483 million (applying the 2012 year end exchange rate of $1.63:£1.00) and £111 million of exchange translation loss.

The decrease of £380 million in 2011 reflects an underlying decrease of £402 million (applying the 2011 year end exchange rate of $1.55:£1.00) and £22 million of exchange translation gains.

(iii)

Other UK life assurance subsidiaries and funds

The effect from the changes in assumptions of valuation interest rates on insurance liabilities is broadly matched by the corresponding effect on assets leaving no significant impact on the available capital.

(iv)

Asia life assurance subsidiaries

The increase of £128 million in 2012 reflects an underlying increase of £177 million (applying the relevant 2012 year end exchange rates) and £49 million of exchange translation loss.

The increase of £115 million in 2011 reflected an underlying increase of £134 million (applying the relevant 2011 year end exchange rates) and £19 million of exchange translation loss.

(v)

New business and other factors comprise the effect of changes in new business, valuation interest rate, investment return, foreign exchange and other factors.

(d) Transferability of available capital

For PAC and all other UK long-term insurers, long-term business assets and liabilities must, by law, be maintained in funds separate from those for the assets and liabilities attributable to non-life insurance business or to shareholders. Only the 'established surplus', the excess of assets over liabilities in the

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D: Life assurance business (Continued)

long-term fund determined through a formal valuation, may be transferred so as to be available for other purposes. Distributions from the with-profits sub-fund to shareholders reflect the shareholders' one-ninth share of the cost of declared policyholders' bonuses.

Accordingly, the excess of assets over liabilities of the PAC long-term fund is retained within that company. The retention of the capital enables it to support with-profits and other business of the fund by, for example, providing the benefits associated with smoothing and guarantees. It also provides investment flexibility for the fund's assets by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of significant events or fundamental changes in its long-term business without affecting the bonus and investment policies.

For other UK long-term business subsidiaries, the amounts retained within the companies are at levels which provide an appropriate level of capital strength in excess of the regulatory minimum.

For Jackson, capital retention is maintained at a level consistent with an appropriate rating by Standard & Poor's. Currently Jackson is rated AA. Jackson can pay dividends on its capital stock only out of earned surplus unless prior regulatory approval is obtained. Furthermore, dividends which exceed the greater of statutory net gain from operations for the prior year or 10 per cent of Jackson's statutory surplus require prior regulatory approval.

For Asian subsidiaries, the amounts retained within the companies are at levels that provide an appropriate level of capital strength in excess of the local regulatory minimum. For ring-fenced with-profits funds, the excess of assets over liabilities is retained with distribution tied to the shareholders' share of bonuses through declaration of actuarially determined surplus. The Singapore and Malaysian businesses may, in general, remit dividends to the UK, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations.

Available capital of the non-insurance business units is transferable to the life assurance businesses after taking account of an appropriate level of operating capital, based on local regulatory solvency targets, over and above basis liabilities.

(e) Sensitivity of liabilities and total capital to changed market conditions and capital management policies

Prudential manages its assets, liabilities and capital locally, in accordance with local regulatory requirements and reflecting the different types of liabilities Prudential has in each business. As a result of the diversity of products offered by Prudential and the different regulatory requirements in which it operates, Prudential employs differing methods of asset/liability and capital management, depending on the business concerned.

Stochastic modelling of assets and liabilities is undertaken in the UK, Jackson and Asia to assess the economic capital requirements.

A stochastic approach models the inter-relationship between asset and liability movements, taking into account asset correlation, management actions and policyholder behaviour under a large number of alternative economic scenarios.

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D: Life assurance business (Continued)

In addition, reserve adequacy testing under a range of scenarios and dynamic solvency testing is carried out, including under certain scenarios mandated by the UK, US and Asian regulators.

The sensitivity of liabilities and other components of total capital vary depending upon the type of business concerned and this conditions the approach to asset/liability management.

For example, for businesses that are most sensitive to interest rate changes, such as immediate annuity business, Prudential uses cash flow analysis to create a portfolio of debt securities whose value changes in line with the value of liabilities when interest rates change. This type of analysis helps protect profits from changing interest rates. This type of analysis is used in the UK for annuity business and by Jackson for its interest-sensitive and fixed indexed annuities and stable value products.

For businesses that are most sensitive to equity price changes, Prudential uses stochastic modelling and scenario testing to look at the future returns on its investments under different scenarios which best reflect the large diversity in returns that equities can produce. This allows Prudential to devise an investment and with-profits policyholder bonus strategy that, on the model assumptions, allows it to optimise returns to its policyholders and shareholders over time while maintaining appropriate financial strength. Prudential uses this methodology extensively in connection with its UK with-profits business.

(f) Intragroup arrangements in respect of SAIF

Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations of the policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency in the first instance. The directors believe that the probability of either the PAC long-term fund or the Group's shareholders' funds having to contribute to SAIF is remote.

E: Asset management (including US broker-dealer) and other operations

E1: Income statement for asset management operations

The Group's asset management operations are based in the UK, Asia and the US where they operate different models and under different brands tailored to their markets.

Asset management in the UK and Europe is undertaken through M&G which is made up of three distinct businesses being Retail, Institutional and Finance. M&G's investment expertise covers all key asset classes, equities, fixed interest and commercial real estate, and includes a number of specialist fixed income and real estate strategies. M&G manages its own retail fund operations, funds for pensions, insurance companies and third-party entities.

Asset management in the US is undertaken through PPM America which manages assets for the Group's UK, Asia and US affiliates plus also provides investment services to other affiliated and unaffiliated institutional clients including collateralised debt obligations (CDOs), private investment funds, institutional accounts and mutual funds. In addition, broker-dealer activities are undertaken in the US where trades in securities are carried out for both third-party customers and for its own account.

Eastspring Investments in Asia serves both the life companies in Asia by managing the life funds and funds underlying the investment linked products and third-party customers through mutual fund

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E: Asset management (including US broker-dealer) and other operations (Continued)

business. Asia offers mutual fund investment products in a number of countries within the region, allowing customers to participate in debt, equity and money market investments.

Other operations cover unallocated corporate activities and includes the head office functions.

(a) The profit included in the income statement in respect of asset management operations for the year is as follows:

	M&G	Eastspring Investments US	Eastspring Investments note (iii)	Total 2012	Total 2011	Total 2010
	£m	£m	£m	£m	£m	£m
Revenue (excluding revenue of consolidated investment funds and NPH broker-dealer fees)	**1,234**	**296**	**282**	**1,812**	1,583	1,423
Revenue of consolidated investment funds[note (i)]	**(11)**			**(11)**	9	11
NPH broker-dealer fees[note (i)]		**435**		**435**	405	369
Gross revenue*	**1,223**	**731**	**282**	**2,236**	1,997	1,803
Charges (excluding charges of consolidated investment funds and NPH broker-dealer fees)	**(713)**	**(257)**	**(207)**	**(1,177)**	(1,147)	(1,003)
Charges of consolidated investment funds[note (i)]	**11**			**11**	(9)	(11)
NPH broker-dealer fees[note (i)]		**(435)**		**(435)**	(405)	(369)
Gross charges	**(702)**	**(692)**	**(207)**	**(1,601)**	(1,561)	(1,383)
Profit before tax	**521**	**39**	**75**	**635**	436	420
Comprising:						
Operating profit based on longer-term investment returns[note (b)]	**371**	**39**	**75**	**485**	461	378
Short-term fluctuations in investment returns[note (ii)]	**93**			**93**	(29)	47
Shareholder's share of actuarial gains and losses on defined benefit pension schemes	**15**			**15**	4	(5)
Gain on dilution of Group's holdings	**42**			**42**		
Profit before tax	**521**	**39**	**75**	**635**	436	420

* For 2012, gross revenue includes the Group's share of results from the associate PPM South Africa. In prior years, PPM South Africa was treated as a subsidiary and accounted for accordingly.

Notes

(i)

Under IFRS, disclosure details of segment revenue are required. The segment revenue of the Group's asset management operations are required to include two items that are for amounts which, reflecting their commercial nature, are also wholly

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E: Asset management (including US broker-dealer) and other operations (Continued)

reflected as charges within the income statement. After allowing for these charges, there is no effect on profit from these two items which are:

(a) Investment funds which are managed on behalf of third parties and are consolidated under IFRS in recognition of the control arrangements for the funds. The gains and losses of these funds are non-recourse to M&G and the Group; and

(b) NPH broker-dealer fees which represent commissions received, that are then paid on to the writing brokers on sales of investment products.

The presentation in the table above shows the amounts attributable to these two items so that the underlying revenue and charges can be seen.

(ii) Short-term fluctuations in investment returns for M&G are primarily in respect of unrealised fair value movements on Prudential Capital's bond portfolio.

(iii) Included within Eastspring Investments revenue and charges are £42 million of commissions (2011: £44 million; 2010: £60 million).

(b) M&G operating profit based on longer-term investment returns:

	2012	**2011***	**2010***
	£m	**£m**	**£m**
Asset management fee income	**728**	662	575
Other income	**6**	4	3
Staff costs	**(289)**	(270)	(254)
Other costs	**(147)**	(134)	(112)
Underlying profit before performance-related fees	**298**	262	212
Share of associate results	**13**	26	20
Performance-related fees	**9**	13	14
Operating profit from asset management operations	**320**	301	246
Operating profit from Prudential Capital	**51**	56	38
Total M&G operating profit based on longer-term investment returns	**371**	357	284

* Following the divestment in the first half of 2012 of M&G's holding in PPM South Africa from 75 per cent to 49.99 per cent and its treatment from 2012 as an associate, M&G's operating income and expense no longer include any element from PPM South Africa, with the share of associates results being presented in a separate line. The table above reflects the retrospective application of this basis of presentation for the 2011 and 2010 results. Total profit remains the same.

The difference between the fees and other income shown above in respect of asset management operations, and the revenue figure for M&G shown (excluding consolidated investment funds) in the main table primarily relates to the total revenue of Prudential Capital (including short-term fluctuations) of £218 million (2011: £96 million; 2010: £136 million) and commissions which have been netted off in arriving at the fee income of £728 million (2011: £662 million; 2010: £612 million) in the table above. The difference in the presentation of commission is aligned with how management reviews the business.

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E: Asset management (including US broker-dealer) and other operations (Continued)

E2: Statement of financial position for asset management operations

Assets, liabilities and shareholders' equity included in the Group consolidated statement of financial position in respect of asset management operations are as follows:

	M&G note (iii)	US	Eastspring Investments	Total 31 Dec 2012	Total 31 Dec 2011
	£m	£m	£m	£m	£m
Assets					
Intangible assets:					
Goodwill	**1,153**	**16**	**61**	**1,230**	1,230
Deferred acquisition costs and other intangibles assets	**10**	**2**	**2**	**14**	16
Total	**1,163**	**18**	**63**	**1,244**	1,246
Other non-investment and non-cash assets	**901**	**174**	**83**	**1,158**	1,129
Associate investments accounted for using the equity method	**41**			**41**	
Financial investments:					
Loans[note (i)]	**1,199**			**1,199**	1,256
Equity securities and portfolio holdings in unit trusts	**50**		**20**	**70**	594
Debt securities[note (ii)]	**1,839**		**7**	**1,846**	1,842
Other investments	**38**	**6**		**44**	78
Deposits	**3**	**33**	**48**	**84**	89
Total investments	**3,170**	**39**	**75**	**3,284**	3,859
Cash and cash equivalents	**909**	**48**	**126**	**1,083**	1,735
Total assets	**6,143**	**279**	**347**	**6,769**	7,969
Equity and liabilities					
Equity					
Shareholders' equity	**1,545**	**124**	**268**	**1,937**	1,783
Non-controlling interests					5
Total equity	**1,545**	**124**	**268**	**1,937**	1,788
Liabilities					
Core structural borrowing of shareholder-financed operations	**275**			**275**	250
Intra-group debt represented by operational borrowings at Group level[note (iv)]	**2,084**			**2,084**	2,956
Net asset value attributable to external holders of consolidated unit trusts and similar funds	**162**			**162**	678

Other non-insurance liabilities[note (v)]	**2,077**	**155**	**79**	**2,311**	2,297
Total liabilities	**4,598**	**155**	**79**	**4,832**	6,181
Total equity and liabilities	**6,143**	**279**	**347**	**6,769**	7,969

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E: Asset management (including US broker-dealer) and other operations (Continued)

Notes

(i)

Loans

The M&G loans relate to loans and receivables managed by Prudential Capital. These assets are generally secured but most have no external credit ratings. Internal ratings prepared by the Group's asset management operations as part of the risk management process are:

	2012	2011
	£m	£m
Loans and receivables internal ratings:		
A+ to A-		129
BBB+ to BBB-	**836**	1,000
BB+ to BB-	**339**	89
B+ to B-	**24**	38
Total M&G loans	**1,199**	1,256

(ii)

Debt securities

Of the £1,846 million total debt securities at 31 December 2012 (2011: £1,842 million) for asset management operations, the following amounts were held by M&G.

	2012	2011
	£m	£m
M&G:		
AAA to A- by Standard & Poor's or Aaa rated by Moody's	**1,493**	1,547
Other	**346**	287
Total M&G debt securities	**1,839**	1,834

(iii)

The M&G statement of financial position includes the assets and liabilities in respect of Prudential Capital.

(iv)

Intra-group debt represented by operational borrowings at Group level

Operational borrowings for M&G are in respect of Prudential Capital's short-term fixed income security programme and comprise:

	2012	2011
	£m	£m
Commercial paper	**1,535**	2,706
Medium-Term Notes	**549**	250
Total intra-group debt represented by operational borrowings at Group level	**2,084**	2,956

(v)

Other non-insurance liabilities consists primarily of intra-group balances, derivative liabilities and other creditors.

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E: Asset management (including US broker-dealer) and other operations (Continued)

E3: Regulatory and other surplus for asset management operations

Certain asset management operations are subject to regulatory requirements. The movement in the year of the surplus regulatory capital position of these operations, combined with the movement in the IFRS basis shareholders' funds for unregulated asset management operations, is as follows:

	Asset management operations				
	2012				2011
	M&G	US Eastspring Investments		Total	Total
	£m	£m	£m	£m	£m
Regulatory and other surplus					
Beginning of year	**156**	**129**	**127**	**412**	432
Gains during the year	**356**	**8**	**52**	**416**	326
Movement in capital requirement	**(3)**		**6**	**3**	(14)
Capital injection			**9**	**9**	8
Distributions made	**(254)**	**(8)**	**(56)**	**(318)**	(342)
Exchange movement		**(5)**	**(4)**	**(9)**	2
End of year	**255**	**124**	**134**	**513**	412

The movement in the year reflects gains driven by profits generated during the year and also changes in regulatory requirements. Distributions consist of dividends paid up to the parent company.

The M&G figures include those for Prudential Capital.

E4: Sensitivity of profit and shareholders' equity to market and other financial risk

(i) Currency translation

Consistent with the Group's accounting policies, the profits of Eastspring Investments and US asset management operations are translated at average exchange rates and shareholders' equity at the closing rate for the reporting period. The rates for the functional currencies of most significant operations are shown in note B4.

A 10 per cent increase in the relevant exchange rates would have reduced reported profit before tax attributable to shareholders and shareholders' equity, excluding goodwill attributable to Eastspring Investments and US asset management operations, by £10 million (2011: £9 million) and £29 million (2011: £30 million) respectively.

(ii) Sensitivities to other financial risks for asset management operations

The principal sensitivities to other financial risk of asset management operations are credit risk on the bridging loan portfolio as described in note E2 of the Prudential Capital operation and the indirect effect of changes to market values of funds under management. Due to the nature of the asset management operations there is limited direct sensitivity to movements in interest rates. Total debt securities held at 31 December 2012 by asset management operations were £1,846 million (2011: £1,842 million), the majority of which are held by the Prudential Capital

operation. Debt securities held

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by M&G and Prudential Capital are in general variable rate bonds and so market value is limited in sensitivity to interest rate movements and consequently any change in interest rates would not have a material impact on profit or shareholders' equity. The Group's asset management operations do not hold significant investments in property or equities.

E5: Other operations

Other operations consist of unallocated corporate activities relating to Group Head Office and the Asia regional head office, with net expenditure for the year of £498 million (2011: £483 million; 2010: negative £450 million) as detailed in note B1. An analysis of the assets and liabilities of other operations is shown in note B5.

The Group holds certain derivatives that are used to manage foreign currency movements and macroeconomic exposures. The fair value of these derivatives is sensitive to the combined effect of movements in exchange rates, interest rates and inflation rates. The possible permutations cover a wide range of scenarios. For indicative purposes, a reasonably possible range of fair value movements could be plus or minus £17 million.

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F: Income statement notes

F1: Segmental information

	Year ended 31 December 2012								
	Insurance operations			Asset management(note E1)					
	UK	US	Asia	M&G	Eastspring Investments		Total segment	Unallocated corporate	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Gross premiums earned	7,020	14,660	8,230				29,910		29,910
Outward reinsurance premiums	(135)	(193)	(178)				(506)		(506)
Earned premiums, net of reinsurance	6,885	14,467	8,052				29,404		29,404
Investment returnnote(ii)	14,495	6,193	3,112	251	6	8	24,065	(14)	24,051
Other income	213	(2)	153	972	725	274	2,335	(314)	2,021
Total revenue, net of reinsurance	21,593	20,658	11,317	1,223	731	282	55,804	(328)	55,476
Benefits and claims	(18,253)	(18,703)	(7,875)				(44,831)		(44,831)
Outward reinsurers' share of benefits and claimsnote(iv)	159	(8)	108				259		259
Movement in unallocated surplus of with-profits fundsnote(iii)	(863)		(518)				(1,381)		(1,381)
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	(18,957)	(18,711)	(8,285)				(45,953)		(45,953)
Acquisition costs and other operating expenditurenote F3	(1,478)	(1,079)	(1,965)	(686)	(692)	(207)	(6,107)	52	(6,055)
Finance costs: interest on core structural borrowings of shareholder-financed operations		(13)		(16)			(29)	(251)	(280)
Total charges, net of reinsurance	(20,435)	(19,803)	(10,250)	(702)	(692)	(207)	(52,089)	(199)	(52,288)

Profit (loss) before tax *(being tax attributable to shareholders' and policyholders' returns)*note(i)	**1,158**	**855**	**1,067**	**521**	**39**	**75**	**3,715**	**(527)**	**3,188**
Tax charge attributable to policyholders' returns	**(300)**		**(78)**				**(378)**		**(378)**
Profit (loss) from continuing operations before tax attributable to shareholders	**858**	**855**	**989**	**521**	**39**	**75**	**3,337**	**(527)**	**2,810**

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31 December 2012

F: Income statement notes (Continued)

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Year ended 31 December 2012								
	Insurance operations		Asset management						
	UK	US	Asia	M&G	Eastspring UK	Eastspring US Investments	Total segment	Unallocated corporate	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	736	964	913	371	39	75	3,098	(565)	2,533
Short-term fluctuations in investment returns on shareholder-backed business	136	(90)	76	93			215	(11)	204
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(14)			15			1	49	50
Gain on dilution of Group holdings				42			42		42
Amortisation of acquisition accounting adjustments arising on purchase of REALIC		(19)					(19)		(19)
Profit (loss) from continuing operations before tax attributable to shareholders	858	855	989	521	39	75	3,337	(527)	2,810

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F: Income statement notes (Continued)

	Year ended 31 December 2011*								
	Insurance operations			Asset management(note E1)					
	UK	US	Asia	M&G	Eastspring Investments	Total segment	Unallocated to corporate	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Gross premiums earned	5,678	12,650	7,378				25,706		25,706
Outward reinsurance premiums	(131)	(72)	(226)				(429)		(429)
Earned premiums, net of reinsurance	5,547	12,578	7,152				25,277		25,277
Investment return[note(ii)]	7,604	1,447	283	128	1	2	9,465	(105)	9,360
Other income	193	(62)	155	923	653	290	2,152	(283)	1,869
Total revenue, net of reinsurance	13,344	13,963	7,590	1,051	654	292	36,894	(388)	36,506
Benefits and claims	(12,048)	(12,931)	(6,081)				(31,060)		(31,060)
Outward reinsurers' share of benefits and claims[note(iv)]	290	280	176				746		746
Movement in unallocated surplus of with-profits funds[note(iii)]	485		540				1,025		1,025
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	(11,273)	(12,651)	(5,365)				(29,289)		(29,289)
Acquisition costs and other operating expenditure[note F3]	(1,239)	(815)	(1,562)	(704)	(630)	(212)	(5,162)	42	(5,120)
Finance costs: interest on core structural borrowings of shareholder-financed operations		(13)		(15)			(28)	(258)	(286)
Total charges, net of reinsurance	(12,512)	(13,479)	(6,927)	(719)	(630)	(212)	(34,479)	(216)	(34,695)
Profit (loss) before tax *(being tax attributable to shareholders' and policyholders' returns)*[note(i)]	832	484	663	332	24	80	2,415	(604)	1,811
Tax charge attributable to policyholders' returns	68		(51)				17		17
Profit (loss) from continuing operations before tax attributable to shareholders	900	484	612	332	24	80	2,432	(604)	1,828

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F: Income statement notes (Continued)

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Year ended 31 December 2011*								
	Insurance operations		Asset management						
	UK	US	Asia	M&G	Eastspring Investments		Total segment	Unallocated corporate	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	723	651	704	357	24	80	2,539	(512)	2,027
Short-term fluctuations in investment returns on shareholder-backed business	159	(167)	(92)	(29)			(129)	(91)	(220)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	18			4			22	(1)	21
Profit (loss) from continuing operations before tax attributable to shareholders	900	484	612	332	24	80	2,432	(604)	1,828

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F: Income statement notes (Continued)

	Year ended 31 December 2010*								
	Insurance operations			Asset management(note E1)					
	UK	US	Asia	M&G	Eastspring Investments	PAC	Total segment	Unallocated to corporate	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Gross premiums earned	6,371	11,817	6,380				24,568		24,568
Outward reinsurance premiums	(128)	(83)	(146)				(357)		(357)
Earned premiums, net of reinsurance	6,243	11,734	6,234				24,211		24,211
Investment return[note(ii)]	14,374	4,576	2,744	186	1	3	21,884	(115)	21,769
Other income	233	(24)	139	768	597	248	1,961	(295)	1,666
Total revenue, net of reinsurance	20,850	16,286	9,117	954	598	251	48,056	(410)	47,646
Benefits and claims	(18,674)	(15,472)	(6,462)				(40,608)		(40,608)
Outward reinsurers' share of benefits and claims	243	49	43				335		335
Movement in unallocated surplus of with-profits funds[note(iii)]	70		(315)				(245)		(245)
Benefits and claims and movements in unallocated surplus of with-profits funds, net of reinsurance	(18,361)	(15,423)	(6,734)				(40,518)		(40,518)
Acquisition costs and other operating expenditure[note F4]	(1,093)	(575)	(1,672)	(628)	(576)	(179)	(4,723)	(266)	(4,989)
Finance costs: interest on core structural borrowings of shareholder-financed operations		(13)					(13)	(244)	(257)
Total charges, net of reinsurance	(19,454)	(16,011)	(8,406)	(628)	(576)	(179)	(45,254)	(510)	(45,764)
Profit (loss) before tax *(being tax attributable to shareholders' and policyholders' returns)*[note(i)]	1,396	275	711	326	22	72	2,802	(920)	1,882
Tax charge attributable to policyholders' returns	(536)		(75)				(611)		(611)
Profit (loss) from continuing operations before tax attributable to shareholders	860	275	636	326	22	72	2,191	(920)	1,271

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F: Income statement notes (Continued)

This is represented in the segmental analysis of profit from continuing operations before tax attributable to shareholders in note B1 as follows:

	Year ended 31 December 2010*								
	Insurance operations		Asset management						
	UK	US	Asia	M&G	Eastspring Investments	PAI	Total segment	Unallocated corporate	Group total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Operating profit based on longer-term investment returns	719	728	522	284	22	72	2,347	(521)	1,826
Short-term fluctuations in investment returns on shareholder-backed business	116	(453)	114	47			(176)	(22)	(198)
Shareholders' share of actuarial and other gains and losses on defined benefit pension schemes	(5)			(5)			(10)		(10)
Costs of terminated AIA transaction								(377)	(377)
Gain on dilution of Group's holdings	30						30		30
Profit (loss) from continuing operations before tax attributable to shareholders	860	275	636	326	22	72	2,191	(920)	1,271

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

Notes

(i) This measure is the formal profit (loss) before tax measure under IFRS but is not the result attributable to shareholders.

(ii) Investment return principally comprises:

Interest and dividends;

Realised and unrealised gains and losses on securities and derivatives classified as fair value through profit and loss under IAS 39; and

Realised gains and losses, including impairment losses, on securities classified as available-for-sale under IAS 39.

(iii)

The movement in unallocated surplus of with-profits funds for Asia above includes movement relating to the Hong Kong branch of PAC. For the purpose of the presentation of unallocated surplus of with-profits funds within the statement of financial position, the Hong Kong branch balance is shown within the unallocated surplus of the PAC with-profits sub-fund.

(iv)

The increase in the credit for outwards reinsurers' share of benefits and claims for Jackson from 2010 to 2011 arises from the fair value movements on the GMIB reinsurance in 2011. As the GMIB reinsurance is net settled it is considered to be a derivative under IAS 39. The movement was particularly high in 2011 due to the reduction in US interest rates in 2011.

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F: Income statement notes (Continued)

F2: Revenue

	2012	2011	2010
	£m	£m	£m
Long-term business premiums			
Insurance contract premiums	**27,447**	23,705	22,595
Investment contracts with discretionary participation feature premiums	**2,243**	1,861	1,802
Inwards reinsurance premiums	**220**	140	171
Less: reinsurance premiums ceded	**(506)**	(429)	(357)
Earned premiums, net of reinsurance[note(iv)]	**29,404**	25,277	24,211
Investment return			
Realised and unrealised gains and losses on securities at fair value through profit and loss	**15,338**	866	14,728
Realised and unrealised losses and gains on derivatives at fair value through profit and loss	**75**	86	(891)
Realised losses on available-for-sale securities, previously recognised in other comprehensive income	**68**	101	(51)
Realised losses on loans	**(51)**	(43)	(12)
Interest[notes(i), (ii)]	**6,600**	6,440	5,976
Dividends	**1,462**	1,304	1,394
Other investment return	**559**	606	625
Investment return	**24,051**	9,360	21,769
Fee income from investment contract business and asset management[notes(iii), (iv)]	**2,021**	1,869	1,666
Total revenue	**55,476**	36,506	47,646

Notes

(i) The segmental analysis of interest income is as follows:

	2012	2011	2010
	£m	£m	£m
Insurance operations:			
UK	4,310	4,286	4,371
US	1,778	1,717	1,014
Asia	403	339	412
Asset management operations:			

M&G	114	110	127
US	1	1	
Eastspring Investments	3	3	2
Total segment	6,609	6,456	5,926
Unallocated corporate	(9)	(16)	50
Total	6,600	6,440	5,976

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(ii)

Interest income includes £13 million (2011: £8 million; 2010: £8 million) accrued in respect of impaired securities.

(iii)

Fee income includes £35 million (2011: £13 million; 2010: £11 million) relating to financial instruments that are not held at fair value through profit and loss.

These fees primarily related to prepayment fees, late fees and syndication fees.

(iv)

The following table provides additional segmental analysis of revenue from external customers:

	2012				
	Asia	**US**	**UK**	**Intragroup**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Revenue from external customers:					
Insurance operations	**8,205**	14,465	7,098		29,768
Asset management	**274**	725	972	(333)	1,638
Unallocated corporate			19		19
Intragroup revenue eliminated on consolidation	**(84)**	(77)	(172)	333	
Total revenue from external customers	**8,395**	15,113	7,917		31,425

	2011				
	Asia	**US**	**UK**	**Intragroup**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Revenue from external customers:					
Insurance operations	7,307	12,516	5,740		25,563
Asset management	290	653	923	(323)	1,543
Unallocated corporate			40		40
Intragroup revenue eliminated on consolidation	(93)	(68)	(162)	323	
	7,504	13,101	6,541		27,146

Total revenue from external customers

	2010				
	Asia	**US**	**UK**	**Intragroup**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Revenue from external customers:					
Insurance operations	6,373	11,710	6,476	(10)	24,549
Asset management	248	597	768	(314)	1,299
Unallocated corporate			29		29
Intragroup revenue eliminated on consolidation	(77)	(72)	(175)	324	
Total revenue from external customers	6,544	12,235	7,098		25,877

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Revenue from external customers is made up of the following:

	2012	2011	2010
	£m	£m	£m
Earned premiums, net of reinsurance	**29,404**	25,277	24,211
Fee income from investment contract business and asset management (presented as 'Other income')	**2,021**	1,869	1,666
Total revenue from external customers	**31,425**	27,146	25,877

In their capacity as fund managers to fellow Prudential Group subsidiaries, M&G, Eastspring Investments and US asset management businesses generate fees for investment management and related services. These services are charged at appropriate arm's length prices, typically priced as a percentage of funds under management. Intragroup fees included within asset management revenue were earned by the following asset management segment:

	2012	2011	2010
	£m	£m	£m
Intragroup revenue generated by:			
M&G	**172**	162	165
Eastspring Investments	**84**	93	77
US broker-dealer and asset management (including Curian)	**77**	68	72
Total intragroup fees included within asset management segment	**333**	323	314

In 2010 a further £10 million of intragroup revenue was recorded between UK insurance operations for services, typically charged as a percentage of funds under management.

Revenue from external customers of Asia, US and UK insurance operations shown above are net of outwards reinsurance premiums of £178 million, £193 million, and £135 million respectively (2011: £226 million, £72 million and £131 million respectively; 2010: £146 million, £83 million, and £128 million respectively).

In Asia, revenue from external customers from no individual country exceeds 10 per cent of the Group total. The largest country is Hong Kong with a total revenue from external customers of £1,745 million (2011: Singapore £1,383 million; 2010: Hong Kong £1,246 million).

Due to the nature of the business of the Group, there is no reliance on any major customers.

F3: Acquisition costs and other expenditure

	2012	2011*	2010*
	£m	£m	£m
Acquisition costs incurred for insurance policies	**(2,649)**	(2,264)	(2,024)
Acquisition costs deferred less amortisation of acquisition costs for insurance policies	**480**	520	728
Administration costs and other expenditure	**(3,728)**	(3,524)	(3,496)
Movements in amounts attributable to external unit holders	**(158)**	148	(197)
Total acquisition costs and other expenditure	**(6,055)**	(5,120)	(4,989)

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Notes

Notes

(i)

Acquisition costs in 2012 comprise amounts related to insurance contracts of £(1,949) million (2011: £(1,679) million; 2010: £(941) million), and investment contracts and asset management contracts of £(220) million (2011: £(65) million; 2010: £(165) million).

(ii)

There were no fee expenses relating to financial liabilities held at amortised cost included in acquisition costs in 2012, 2011 and 2010.

(iii)

The total depreciation and amortisation expense of £(731) million (2011: £(584) million; 2010: £(320) million) relates to amortisation of deferred acquisition costs of insurance contracts and asset management contracts.

The segmental analysis of total depreciation and amortisation expense is as follows:

	2012	**2011***	**2010***
	£m	**£m**	**£m**
Insurance operations:			
UK	**(65)**	(55)	(35)
US	**(302)**	(237)	(15)
Asia	**(332)**	(270)	(248)
Asset management operations:			
M&G	**(6)**	(7)	(8)
US	**(1)**	(1)	(2)
Eastspring Investments	**(4)**	(4)	(4)
Total segment	**(710)**	(574)	(312)
Unallocated corporate	**(21)**	(10)	(8)
Total	**(731)**	(584)	(320)

*The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

(iv)

Interest expense, excluding interest on core structural borrowings of shareholder-financed operations, amounted to £(140) million (2011: £(123)million) and is included within total acquisition costs and other operating expenditure as part of investment management expenses. The segmental analysis of this interest expense is as follows:

	2012	2011	2010
Insurance operations:			
UK	**(62)**	(49)	(28)
US	**(28)**	(31)	(33)
Asia	**(7)**	(10)	(13)
Asset management operations:			
M&G	**(18)**	(11)	(19)
Total segment	**(115)**	(101)	(93)
Unallocated corporate	**(25)**	(22)	(20)
Total	**(140)**	(123)	(113)

(v)

Movements in amounts attributable to external unit holders are in respect of those OIECS and unit trusts which are required to be consolidated and comprises a charge of £(195) million (2011: a credit of £28 million; 2010: £(61) million) for UK insurance operations and a credit of £37 million (2011: £120 million; 2010: £(136) million) for Asia insurance operations.

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(vi)

The total amounts for acquisition costs and other expenditure shown above includes Corporate Expenditure shown in note B1 (Segment disclosure income statement). The charge for Corporate Expenditure comprises:

	2012	2011	2010
	£m	£m	£m
Group Head Office	**(168)**	(168)	(175)
Asia Regional Office:			
Gross costs	**(99)**	(86)	(90)
Recharges to Asia operations	**36**	35	42
	(63)	(51)	(48)
Total	**(231)**	(219)	(223)

F4: Finance costs: Interest on core structural borrowings of shareholder-financed operations

Finance costs of £280 million (2011: £286 million; 2010: £257 million) comprise £251 million (2011: £258 million; 2010: £244 million) interest on core debt of the parent company, £13 million (2011: £13 million; 2010: £13 million) on US insurance operations' surplus notes and £16 million (2011: £15 million; 2010: nil) on PruCap's bank loan.

F5: Tax

(a) Total tax charge by nature of expense

An analysis of the total tax benefit (expense) of continuing operations recognised in the income statement by nature of benefit (expense) is as follows:

	2012	2011*	2010*
	£m	£m	£m
Current tax expense:			
Corporation tax	**(950)**	(775)	(378)
Adjustments in respect of prior years	**143**	33	287
Total current tax	**(807)**	(742)	(91)
Deferred tax arising from:			
Origination and reversal of temporary differences	**(178)**	293	(453)
	(6)	57	(27)

(Expense) credit in respect of a previously unrecognised tax loss, tax credit or temporary difference from a prior period			
Total deferred tax (charge) credit	**(184)**	350	(480)
Total tax charge	**(991)**	(392)	(571)

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The total tax expense arises as follows:

	2012	2011*	2010*
	£m	£m	£m
Current tax expense:			
UK	**(393)**	(475)	(61)
Foreign	**(414)**	(267)	(30)
	(807)	(742)	(91)
Deferred tax (charge) credit:			
UK	**(45)**	455	(252)
Foreign	**(139)**	(105)	(228)
	(184)	350	(480)
Total	**(991)**	(392)	(571)

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

The current tax charge of £807 million includes £18 million (2011: charge of £16 million; 2010: charge of £13 million) in respect of the tax charge for Hong Kong. The Hong Kong current tax charge is calculated as 16.5 per cent for all periods on either (i) 5 per cent of the net insurance premium or (ii) the estimated assessable profits, depending on the nature of the business written.

In the UK, life insurance companies are taxed on both their shareholders' profits and on their policyholders' investment returns on certain insurance and investment products. Tax on shareholders' profits is calculated at the standard corporation tax rate, and tax on policyholders' investment returns is calculated at the basic rate of income tax. Although both types of tax are included in the total tax charge in the Group's consolidated income statement, they are presented separately in the income statement to provide the most relevant information about tax that the Group pays on its profits.

Until the end of 2012 for the Group's UK life insurance companies, shareholders' profits were calculated using regulatory surplus as a starting point, with appropriate deferred tax adjustments for IFRS. Beginning in 2013, under new UK life tax rules, shareholders' profits will be calculated using accounting profit or loss as a starting point.

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The total tax charge comprises tax attributable to policyholders and unallocated surplus of with-profits funds, unit-linked policies and shareholders as shown below.

	2012			2011*	2010*
Tax charge	**Current tax**	**Deferred tax**	**Total**	**Total**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Tax (charge) credit to policyholders' returns	**(488)**	110	(378)	17	(611)
Tax charge attributable to shareholders	**(319)**	(294)	(613)	(409)	40
Total tax charge	**(807)**	(184)	(991)	(392)	(571)

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

The principal reason for the increase in the tax charge attributable to policyholders' returns is an increase in deferred tax on unrealised gains and losses on investments.

The total deferred tax (charge)/credit arises as follows:

	2012	2011*	2010*
	£m	**£m**	**£m**
Unrealised gains and losses on investments	**(91)**	129	(217)
Balances relating to investment and insurance contracts	**467**	148	37
Short-term timing differences	**(226)**	66	(431)
Capital allowances		2	(8)
Unused tax losses	**(334)**	5	139
Deferred tax (charge)/credit	**(184)**	350	(480)

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

In 2012, a deferred tax charge of £198 million (2011: charge of £187 million; 2010: charge of £287 million) has been taken through other comprehensive income. Other movements in deferred tax totalling a £378 million credit mainly arises as a result of bringing a deferred tax asset in respect of the acquired REALIC business on to the balance sheet. When these amounts are taken with the deferred tax charge shown above

there is no significant change in the Group's net deferred tax liability (2011: decrease of £0.1 billion; 2010: increase of £0.9 billion).

(b) Reconciliation of effective tax rate

The total tax charge is attributable to shareholders and policyholders as summarised in the income statement.

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F: Income statement notes (Continued)

(i) Summary of pre-tax profit and tax (charge)

The income statement includes the following items:

	2012	2011*	2010*
	£m	£m	£m
Profit before tax	**3,188**	1,811	1,882
Tax (charge) credit attributable to policyholders' returns	**(378)**	17	(611)
Profit before tax attributable to shareholders	**2,810**	1,828	1,271
Tax attributable to shareholders' profits:			
Tax charge	**(991)**	(392)	(571)
Less: tax attributable to policyholders' returns	**378**	(17)	611
Tax charge attributable to shareholders' returns	**(613)**	(409)	40
Profit for the year	**2,197**	1,419	1,311

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

(ii) Overview

For the purposes of explaining the relationship between tax expense and accounting profit, it is appropriate to consider the sources of profit and tax by reference to those that are attributable to shareholders and policyholders, as follows:

	2012			2011*			2010*		
	Attributable to shareholders	Attributable to policyholders**	Total	Attributable to shareholders	Attributable to policyholders**	Total	Attributable to shareholders	Attributable to policyholders**	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Profit (loss) before tax	**2,810**	**378**	**3,188**	1,828	(17)	1,811	1,271	611	1,882
Taxation charge:									
Expected tax rate	**27%**	**100%**	**27%**	28%	100%	28%	27%	100%	51%

Expected tax (charge) credit	**(763)**	**(378)**	**(1,141)**	(519)	17	(502)	(341)	(611)	(952)
Variance from expected tax chargenote v(ii)	**150**		**150**	110		110	381		381
Actual tax (charge) credit	**(613)**	**(378)**	**(991)**	(409)	17	(392)	40	(611)	(571)
Average effective tax rate	**22%**	**100%**	**31%**	22%	100%	22%	-3%	100%	30%

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

**

For the column entitled 'Attributable to policyholders', the profit (loss) before tax represents income, before tax attributable to policyholders and unallocated surplus of with-profits funds and unit-linked policies. This income has been determined after deduction of charges for policyholder benefits and movements on unallocated surplus which are determined net of tax. Hence, the pre-tax results attributable to policyholders is the inverse of the tax charge attributable to policyholders.

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Due to the requirements of the financial reporting standards IAS 1 'Presentation of Financial Statements' and IAS 12 'Income Taxes', the profit (loss) before tax and tax charge reflect the aggregate of amounts that are attributable to shareholders and policyholders.

Profit (loss) before tax comprises profit attributable to shareholders and pre-tax profit attributable to policyholders of linked and with-profits funds and unallocated surplus of with-profits funds.

The total tax charge for linked and with-profits business includes tax expense on unit-linked and with-profits funds attributable to policyholders, the unallocated surplus of with-profits funds and the shareholders' profits. This feature arises from the basis of taxation applied to life and pension business, principally in the UK, but with similar bases applying in certain Asia operations, and is explained in note (iii) below.

Furthermore, the basis of preparation of Prudential's financial statements incorporates the additional feature that, as permitted under IFRS 4, the residual equity of the Group's with-profits funds, ie unallocated surplus, is recorded as a liability with transfers to and from that liability reflected in pre-tax profits. This gives rise to anomalous effective tax rates for profits attributable to policyholders (as described in note (iv) below).

In meeting the reconciliation requirements set out in paragraph 81(c) of IAS 12, the presentation shown in this disclosure note seeks to ensure that the explanation of the relationship between tax expense and accounting profit draw properly the distinction between the elements of the profit and tax charge that are attributable to policyholders and shareholders as explained below in notes (iv) and (v) respectively. Due to the nature of the basis of taxation of UK life and pension business (as described in note (iii) below), and the significance of the results of the business to the Group, it is inappropriate to seek to explain the effective tax rate on profit before tax by the traditional approach that would apply for other industries.

The shareholder elements are the components of the profit and tax charge that are of most direct relevance to investors, and it is this aspect that the IAS 12 reconciliation requirement is seeking to explain for companies that do not need to account for both with-profits and unit-linked funds, where tax is borne by the Company on the policyholders' behalf and which is not contemplated by the IFRS requirement.

(iii) Basis of taxation for UK life and pension business

Different rules apply under UK tax law for taxing pension business and life insurance business and there are detailed rules for apportioning the investment return and profits of the fund between the types of business.

The investment return referable to pension business, and some other less significant classes of business, is exempt from taxation, but tax is charged on the profit that shareholders derive from writing such business at the corporate rate of tax. The rules for taxing life insurance business are more complex. Initially, the UK regime seeks to tax the regulatory basis investment return less management expenses (I-E) on this business as it arises. However, in determining the actual tax charge, a calculation of the shareholder profits for taxation purposes from writing life insurance business also has to be made and compared with the I-E profit.

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If the shareholder profit is higher than the I-E amount, extra income is attributable to the I-E calculation until the I-E profit equals the shareholder profit. If on the other hand, the I-E profit is the greater, then an amount equal to the shareholder profit is taxed at the corporate rate of tax, with the remainder of the I-E profit being taxed at the lower policyholder rate of tax.

The purpose of this approach is to ensure that the Company is always at a minimum taxed on the profit, as defined for taxation purposes by reference to the Company's regulatory returns (rather than IFRS basis results), that it has earned. The shareholders' portion of the long-term business is taxed at the shareholders' rate, with the remaining portion taxed at rates applicable to the policyholders.

It is to be noted that the calculations described are determined using data from the regulatory basis returns rather than the IFRS basis results. Beginning in 2013, under new UK life tax rules, shareholders' profits will be calculated using accounting profit or loss as a starting point.

(iv) Profits attributable to policyholders and related tax

As noted above, it is necessary under IFRS requirements to include the total tax charge of the Company (both policyholder and shareholder elements) in the tax charge disclosed in the income statement.

The tax expense attributable to policyholders is a combination of current and deferred tax charges and reflects the nature of the income and expenditure of the with-profits and unit linked funds. The current tax charge element reflects the element for the funds, determined on the I-E basis (as described in note (iii) above) that is attributable to policyholders. For policyholder deferred tax, normally the most significant element reflects the movement on unrealised appreciation on investments. These investments are accounted for under IAS 39 on a fair value through profit or loss basis with attaching deferred tax charges or credits.

For with-profits business, total pre-tax profits reflect the aggregate of profits attributable to policyholders and shareholders. However, amounts attributable to the equity of with-profits funds are carried in the liability for unallocated surplus. Also, as described in note (iii), UK with-profits business is taxed on a basis that affects policyholders' unallocated surplus of with-profits funds and shareholders. For the PAC with-profits sub-fund, transfers to and from unallocated surplus are recorded in the income statement, so that after charging the total tax borne by the fund, the net balance reflects the statutory transfer from the fund for the year. The statutory transfer represents 10 per cent of the actuarially determined surplus for the year that is attributable to shareholders.

For SAIF, similar transfers are made. However, in the case of SAIF, a net nil balance is derived, reflecting the lack of shareholder interest in the financial performance of the fund (other than through asset management arrangements).

The accounting anomaly that arises under IFRS is that due to the fact that the net of tax profit attributable to with-profits policyholders is zero, the Company's presentation of pre-tax profit attributable to policyholders reflects an amount that is the mirror image of the tax charge attributable to policyholders.

For unit-linked business, pre-tax profits also reflect the aggregate of profits attributable to policyholders and shareholders. The pre-tax profits attributable to policyholders represent fees earned

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that are used to pay tax borne by the Company on policyholders' behalf. The net of tax profit attributable to policyholders for unit-linked business is thus zero.

The combined effect of these features is such that providing a reconciliation of the tax charge attributable to policyholders to an expected charge based on the standard corporate rate of tax on IFRS basis profits attributable to policyholders is not relevant.

In summary, for accounting purposes, in all cases and for all reporting periods, the apparent effective rate for profit attributable to policyholders and unallocated surplus is 100 per cent. However, it is to be noted that the 100 per cent rate does not reflect a rate paid on the profits attributable to policyholders. It instead reflects the basis of accounting for unallocated surplus coupled with the distinction made for performance reporting between sources of profit attributable to shareholders, policyholders and unallocated surplus and IFRS requirements in respect of reporting of all pre-tax profits and all tax charges irrespective of policyholder or shareholder economic interest.

(v) Reconciliation of effective tax rate

The total tax charge is attributable to shareholders and policyholders as summarised in the income statement.

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Reconciliation of tax charge on profit attributable to shareholders for continuing operations:

2012	Asia insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m (Except for tax rates)				
Operating profit (loss) based on longer-term investment returns	913	964	736	(80)	2,533
Non-operating profit (loss)	76	(109)	122	188	277
Profit before tax attributable to shareholders	989	855	858	108	2,810
Expected tax rate:*	23%	35%	25%	25%	27%
Tax at the expected tax rate	227	300	210	26	763
Effects of:					
Adjustment to tax charge in relation to prior years	(11)	10	(26)	(10)	(37)
Movements in provisions for open tax matters		(3)		32	29
Income not taxable or taxable at concessionary rates	(87)			(2)	(89)
Deductions not allowable for tax purposes	30			3	33
Different local basis of tax on overseas profits		(68)			(68)
Impact of changes in local statutory tax rates			(39)	9	(30)
Deferred tax adjustments	(6)		8	(1)	1
Irrecoverable withholding taxes				14	14
Other	5	(5)	8	(11)	(3)
Total actual tax charge	158	234	161	60	613
Analysed into:					
Tax on operating profit based on longer-term investment returns	142	272	126	42	582
Tax on non-operating profit	16	(38)	35	18	31
Actual tax rate:					
Operating profit based on longer-term investment returns	16%	28%	17%	(53)%	23%
Total profit	16%	27%	19%	56%	22%

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2011**	Asia insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m (Except for tax rates)				
Operating profit (loss) based on longer-term investment returns	704	651	723	(51)	2,027
Non-operating profit	(92)	(167)	177	(117)	(199)
Profit (loss) before tax attributable to shareholders	612	484	900	(168)	1,828
Expected tax rate:*	25%	35%	27%	27%	28%
Tax at the expected tax rate	151	170	243	(45)	519
Effects of:					
Adjustment to tax charge in relation to prior years	(7)		33	(19)	7
Movements in provisions for open tax matters				(44)	(44)
Income not taxable or taxable at concessionary rates	(36)		(1)		(37)
Deductions not allowable for tax purposes	12			4	16
Different local basis of tax on overseas profits		(37)			(37)
Impact of changes in local statutory tax rates			(32)	1	(31)
Deferred tax adjustments	7				7
Irrecoverable withholding taxes				13	13
Other	(3)	(6)	(14)	19	(4)
Total actual tax charge (credit)	124	127	229	(71)	409
Analysed into:					
Tax on operating profit based on longer-term investment returns	122	185	190	(64)	433
Tax on non-operating profit	2	(58)	39	(7)	(24)
Actual tax rate:					
Operating profit based on longer-term investment returns	17%	28%	26%	125%	21%
Total profit	20%	26%	25%	42%	22%

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F: Income statement notes (Continued)

2010**	Asia insurance operations	US insurance operations	UK insurance operations	Other operations	Total
	£m (Except for tax rates)				
Operating profit based on longer-term investment returns	522	728	719	(143)	1,826
Non-operating profit	114	(453)	141	(357)	(555)
Profit (loss) before tax attributable to shareholders	636	275	860	(500)	1,271
Expected tax rate:*	23%	35%	28%	28%	27%
Tax at the expected tax rate	144	97	240	(140)	341
Effects of:					
Adjustment to tax charge in relation to prior years			(26)	(12)	(38)
Movement in provisions for open tax matters				(158)	(158)
Income not taxable or taxable at concessionary rates	(158)		(4)	(5)	(167)
Deductions not allowable for tax purposes	33		5		38
Different local basis of tax on overseas profits		(36)			(36)
Impact of changes in local statutory tax rates			(16)	5	(11)
Deferred tax adjustment	44		20	(38)	26
Other	1	(7)	(5)	(24)	(35)
Total actual tax charge/(credit)	64	54	214	(372)	(40)
Analysed into:					
Tax on operating profit based on longer-term investment returns, excluding exceptional tax credit	56	212	183	(119)	332
Exceptional tax credit***				(158)	(158)
Tax on operating profit based on longer-term investment returns	56	212	183	(277)	174
Tax on non-operating profit	8	(158)	31	(95)	(214)
Actual tax rate:					
Operating profit based on longer-term investment returns	11%	29%	25%	194%	10%
Total profit	10%	20%	25%	74%	(3%)
Actual tax rate (excluding exceptional tax credit***):					
Operating profit based on longer-term investment returns	11%	29%	25%	83%	18%
Total profit	10%	20%	25%	43%	9%

*

The expected tax rates shown in the table above (rounded to the nearest whole percentage) reflect the corporation tax rates generally applied to taxable profits of the relevant country jurisdictions. For Asia

operations the expected tax rates reflect the corporation tax rates weighted by reference to the source of profits of operations contributing to the aggregate business result. The expected tax rate for Other operations reflects the mix of business between UK and overseas non-insurance operations, which are taxed at a variety of rates. The rates will fluctuate from year to year dependent on the mix of profits.

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F: Income statement notes (Continued)

**

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

***

The tax charge attributable to shareholders' return included an exceptional tax credit of £158 million which primarily related to the impact of settlement agreed with the UK tax authorities.

(c) Taxes paid

In 2012 Prudential remitted £2.2 billion (2011: £1.6 billion) of tax to Revenue authorities, this includes £925 million (2011: £561 million) of corporation tax, £184 million of other taxes and £1,078 million collected on behalf of employees, customers and third parties.

The geographical split of taxes remitted by Prudential is as follows:

	2012				**2011**			
	Corporation taxes*	**Other taxes**	**Taxes Collected**	**Total**	**Corporation taxes***	**Other taxes**	**Taxes Collected**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Asia	**221**	**37**	**152**	**410**	170	32	64	266
US	**181**	**25**	**264**	**470**	131	20	221	372
UK	**522**	**121**	**662**	**1,305**	260	112	595	967
Other	**1**	**1**		**2**		1		1
Total tax paid	**925**	**184**	**1,078**	**2,187**	561	165	880	1,606

*

In certain countries such as the UK, the corporation tax payments for the Group's life insurance businesses are based on taxable profits which include policyholder investment returns on certain life insurance products.

Other taxes paid includes property taxes, withholding taxes, customs duties, stamp duties, employer payroll taxes and irrecoverable indirect taxes.

Taxes collected are other taxes that Prudential remits to tax authorities which it is obliged to collect from employees, customers and third parties which includes sales/VAT/GST taxes, employee and annuitant payroll taxes.

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G: Financial assets and liabilities

G1: Financial instruments Designation and fair values

The Group designates all financial assets as at fair value, either through profit and loss or on an available-for-sale, or as loans and receivables on an amortised cost basis, net of impairment basis. Financial liabilities are designated as either fair value through profit and loss, amortised cost, or as investment contracts with discretionary participation features accounted for under IFRS 4 as described in note A3.

	2012				
	Fair value through profit and loss	Available-for-sale	Loans and receivables at amortised cost	Total carrying value	Fair value
	£m	£m	£m	£m	£m
Financial assets					
Cash and cash equivalents			**6,384**	**6,384**	**6,384**
Deposits			**12,653**	**12,653**	**12,653**
Equity securities and portfolio holdings in unit trusts	**99,958**			**99,958**	**99,958**
Debt securities[note (i)]	**107,278**	**32,825**		**140,103**	**140,103**
Loans[note (ii)]	**2,068**		**9,753**	**11,821**	**12,333**
Other investments[note (iii)]	**7,900**			**7,900**	**7,900**
Accrued investment income			**2,798**	**2,798**	**2,798**
Other debtors			**1,361**	**1,361**	**1,361**
	217,204	**32,825**	**32,949**	**282,978**	

	2012				
	Fair value through profit and loss note (v)	Amortised cost	IFRS 4 basis value	Total carrying value	Fair value
	£m	£m	£m	£m	£m
Financial liabilities					
Core structural borrowings of shareholder-financed operations[notes (i), H13]		**3,554**		**3,554**	**4,133**
		2,245		**2,245**	**2,245**

Operational borrowings attributable to shareholder-financed operations[H13]					
Borrowings attributable to with-profits funds[H13]	**40**	**993**		**1,033**	**1,042**
Obligations under funding, securities lending and sale and repurchase agreements		**2,436**		**2,436**	**2,455**
Net asset value attributable to unit holders of consolidated unit trust and similar funds	**4,345**			**4,345**	**4,345**
Investment contracts with discretionary participation features[note (iv)]			**33,812**	**33,812**	
Investment contracts without discretionary participation features	**16,309**	**2,069**		**18,378**	**18,419**
Other creditors	**259**	**2,522**		**2,781**	**2,781**
Derivative liabilities	**2,829**			**2,829**	**2,829**
Other liabilities	**2,021**	**1,433**		**3,454**	**3,453**
	25,803	**15,252**	**33,812**	**74,867**	

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G: Financial assets and liabilities (Continued)

	Fair value through profit and loss	Available-for-sale	2011 Loans and receivables at amortised cost	Total carrying value	Fair value
	£m	£m	£m	£m	£m
Financial assets					
Cash and cash equivalents			7,257	7,257	7,257
Deposits			10,708	10,708	10,708
Equity securities and portfolio holdings in unit trusts	87,349			87,349	87,349
Debt securities[note (i)]	97,482	27,016		124,498	124,498
Loans[note (ii)]	279		9,435	9,714	9,828
Other investments[note (iii)]	7,509			7,509	7,509
Accrued investment income			2,710	2,710	2,710
Other debtors			987	987	987
	192,619	27,016	31,097	250,732	

	2011				
	Fair value through profit and loss note (v)	Amortised cost	IFRS 4 basis value	Total carrying value	Fair value
	£m	£m	£m	£m	£m
Financial liabilities					
Core structural borrowings of shareholder-financed operations[notes (i), H13]		3,611		3,611	3,815
Operational borrowings attributable to shareholder-financed operations[H13]		3,340		3,340	3,340
Borrowings attributable to with-profits funds[H13]	39	933		972	978
Obligations under funding, securities lending and sale and repurchase agreements		3,114		3,114	3,144

Net asset value attributable to unit holders of consolidated unit trust and similar funds	3,840			3,840	3,840
Investment contracts with discretionary participation features[note (iv)]			29,745	29,745	
Investment contracts without discretionary participation features	15,056	1,911		16,967	17,008
Other creditors	281	2,263		2,544	2,544
Derivative liabilities	3,054			3,054	3,054
Other liabilities		1,249		1,249	1,249
	22,270	16,421	29,745	68,436	

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G: Financial assets and liabilities (Continued)

Notes

(i) As at 31 December 2012 £525 million (2011: £523 million) of convertible bonds were included in debt securities and £673 million (2011: £702 million) were included in borrowings.

(ii) Loans and receivables are reported net of allowance for loan losses of £83 million (2011: £89 million).

(iii) See note G3 for details of the derivative assets included. The balance also contains the PAC with-profits fund's participation in various investment funds and limited liability property partnerships.

(iv) It is impractical to determine the fair value of investment contracts with discretionary participation features due to the lack of a reliable basis to measure such features.

(v) For financial liabilities designated as fair value through profit and loss, the impact on profit from movements in credit risk during 2012 and 2011 was negligible.

Determination of fair value

The fair values of the financial instruments for which fair valuation is required under IFRS are determined by the use of current market bid prices for exchange-quoted investments, or by using quotations from independent third-parties, such as brokers and pricing services or by using appropriate valuation techniques. Investments valued using valuation techniques include financial investments which by their nature do not have an externally quoted price based on regular trades and financial investments for which markets are no longer active as a result of market conditions eg market illiquidity. The valuation techniques used include comparison to recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option adjusted spread models and, if applicable, enterprise valuation. These techniques may include a number of assumptions relating to variables such as credit risk and interest rates. Changes in assumptions relating to these variables could positively or negatively impact the reported fair value of these instruments. When determining the inputs into the valuation techniques used priority is given to publicly available prices from independent sources when available, but overall the source of pricing is chosen with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date.

The fair value estimates are made at a specific point in time, based upon available market information and judgments about the financial instruments, including estimates of the timing and amount of expected future cash flows and the credit standing of counterparties. Such estimates do not reflect any premium or discount that could result from offering for sale at one time the Group's entire holdings of a particular financial instrument, nor do they consider the tax impact of the realisation of unrealised gains or losses from selling the financial instrument being fair valued. In some cases the disclosed value cannot be realised in immediate settlement of the financial instrument.

The loans and receivables have been shown net of provisions for impairment. The fair value of loans has been estimated from discounted cash flows expected to be received. The rate of discount used was the market rate of interest.

The estimated fair value of derivative financial instruments reflects the estimated amount the Group would receive or pay in an arm's length transaction. This amount is determined using quoted prices if exchange listed, quotations from independent third-parties or valued internally using standard market

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G: Financial assets and liabilities (Continued)

practices. In accordance with the Group's risk management framework, all internally generated valuations are subject to assessment against external counterparties' valuations.

For investment contracts in the US with fixed and guaranteed terms the fair value is determined based on the present value of future cash flows discounted at current interest rates.

The fair value of other financial liabilities is determined using discounted cash flows of the amounts expected to be paid.

Level 1, 2 and 3 fair value measurement hierarchy of Group financial instruments

The table below includes financial instruments carried at fair value analysed by level of the IFRS 7 'Financial Instruments: Disclosures' defined fair value hierarchy. This hierarchy is based on the inputs to the fair value measurement and reflects the lowest level input that is significant to that measurement.

The classification criteria and its application to Prudential can be summarised as follows:

Level 1 quoted prices (unadjusted) in active markets for identical assets and liabilities

Level 1 includes financial instruments where there is clear evidence that the valuation is based on a quoted publicly traded price in an active market (eg exchange listed equities, mutual funds with quoted prices and exchange traded derivatives.)

Level 2 inputs other than quoted prices included within level 1 that are observable either directly (ie as prices) or indirectly (ie derived from prices)

Level 2 includes investments where a direct link to an actively traded price is not readily apparent, but which are valued using inputs which are largely observable either directly (ie as prices) or indirectly (ie derived from prices). A significant proportion of the Group's level 2 assets are corporate bonds, structured securities and other non-national government debt securities. These assets, in line with market practice, are generally valued using independent pricing services or third-party broker quotes. These valuations are determined using independent external quotations from multiple sources and are subject to a number of monitoring controls, such as monthly price variances and analysis on prices achieved on subsequent trades.

Pricing services, where available, are used to obtain the third-party broker quotes. Where pricing services providers are used, a single valuation is obtained and applied.

When prices are not available from pricing services, quotes are sourced directly from brokers. Prudential seeks to obtain a number of quotes from different brokers so as to obtain the most comprehensive information available on their executability. Where quotes are sourced directly from brokers, the price used in the valuation is normally selected from one of the quotes based on a number of factors, including the timeliness and regularity of the quotes and the accuracy of the quotes considering the spreads provided. The selected quote is the one which best represents an executable quote for the security at the measurement date.

Generally, no adjustment is made to the prices obtained from independent third parties. Adjustment is made in only limited circumstances, where it is determined that the third-party valuations obtained do

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G: Financial assets and liabilities (Continued)

not reflect fair value (eg either because the value is stale and/or the values are extremely diverse in range). These are usually securities which are distressed or that could be subject to a debt restructure or where reliable market prices are no longer available due to an inactive market or market dislocation. In these instances, prices are derived using internal valuation techniques including those as described above in this note with the objective of arriving at a fair value measurement which reflects the price at which an orderly transaction would take place between market participants on the measurement date. The techniques used require a number of assumptions relating to variables such as credit risk and interest rates. Examples of such variables include an average credit spread based on the corporate bond universe and the relevant duration of the asset being valued. Prudential measures the input assumptions based on the best available information at the measurement dates. Securities valued in such manner are classified as level 3 where these significant inputs are not based on observable market data.

Of the total level 2 debt securities of £105,839 million at 31 December 2012 (31 December 2011: £94,378 million), £8,248 million are valued internally (31 December 2011: £6,847 million). The majority of such securities are valued using matrix pricing, which is based on assessing the credit quality of the underlying borrower to derive a suitable discount rate relative to government securities of a comparable duration. Under matrix pricing, the debt securities are priced taking the credit spreads on comparable quoted public debt securities and applying these to the equivalent debt instruments factoring in a specified liquidity premium. The majority of the parameters used in this valuation technique are readily observable in the market and, therefore, are not subject to interpretation.

Level 3 Significant inputs for the asset or liability that are not based on observable market data (unobservable inputs)

Level 3 includes investments which are internally valued or subject to a significant number of unobservable assumptions (eg private equity funds and certain derivatives which are bespoke or long-dated).

At 31 December 2012 the Group held £6,660 million (2011: £4,565 million), 3 per cent of the fair valued financial investments, net of derivative liabilities (2011: 2 per cent), within level 3.

Of these amounts £3,916 million (2011: £3,732 million) was held by the Group's participating funds and therefore shareholders' profit and equity are not impacted by movements in the valuation of these financial instruments. At 31 December 2012, the £3,916 million (2011: £3,732 million) represented 4.3 per cent (2011: 4.3 per cent) of the total fair valued financial instruments, net of derivative liabilities of the participating funds.

Included within the £2,703 million level 3 fair valued financial investments, net of derivative liabilities at 31 December 2012 (2011: £800 million) held to support non-linked shareholder-backed business were loans of £1,842 million, attaching to the purchase of REALIC in 2012 held to back the liabilities for funds withheld under reinsurance arrangement. The funds withheld liability, which was also accounted for on a fair value basis and classified as level 3, amounted to £2,021 million at 31 December 2012. This liability is included within Other financial liabilities held at fair value in the table below.

Excluding the financial investments of £1,842 million held to back the funds withheld liability under REALIC's reinsurance arrangement, the level 3 fair valued financial investments, net of derivative liabilities, supporting non-linked shareholder-backed business at 31 December 2012 were £861 million

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(2011: £800 million) (representing 1.2 per cent of the total fair valued financial investments net of derivative liabilities backing this business (2011: 1.3 per cent)). Of this amount, £837 million of net assets are externally valued and £24 million of net liabilities are internally valued (2011: net assets of £757 million and £43 million respectively). Internal valuations, which represent 0.03 per cent of the total fair valued financial investments net of derivative liabilities supporting non-linked shareholder-backed business at 31 December 2012 (2011: 0.1 per cent), are inherently more subjective than external valuations.

If the value of all level 3 investments backing non-linked shareholder-backed business valued internally was varied downwards by 10 per cent, the change in valuation would be £2 million (2011: £4 million), which would reduce shareholders' equity by this amount before tax. Of this amount a £1 million increase (2011: £1 million decrease) would pass through the income statement substantially as part of short-term fluctuations in investment returns outside of operating profit and a £3 million decrease (2011: £3 million decrease) would be included as part of other comprehensive income, being unrealised movements on assets classified as available-for-sale.

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G: Financial assets and liabilities (Continued)

	31 Dec 2012			
	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
Analysis of financial investments, net of derivative liabilities by business type				
With-profits				
Equity securities and portfolio holdings in unit trusts	22,129	2,496	480	25,105
Debt securities	15,910	45,550	542	62,002
Other investments (including derivative assets)	108	1,743	2,894	4,745
Derivative liabilities	(61)	(1,072)		(1,133)
Total financial investments, net of derivative liabilities	38,086	48,717	3,916	90,719
Percentage of total	42%	54%	4%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	73,632	189	39	73,860
Debt securities	3,843	5,659	2	9,504
Other investments (including derivative assets)	47	10		57
Derivative liabilities		(1)		(1)
Total financial investments, net of derivative liabilities	77,522	5,857	41	83,420
Percentage of total	93%	7%	0%	100%
Non-linked shareholder-backed				
Loans		226	1,842*	2,068
Equity securities and portfolio holdings in unit trusts	937	7	49	993
Debt securities	13,721	54,630	246	68,597
Other investments (including derivative assets)	31	2,306	761	3,098
Derivative liabilities	(16)	(1,484)	(195)	(1,695)
Total financial investments, net of derivative liabilities	14,673	55,685	2,703	73,061
Percentage of total	20%	76%	4%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans		226	1,842*	2,068
Equity securities and portfolio holdings in unit trusts	96,698	2,692	568	99,958
Debt securities	33,474	105,839	790	140,103
Other investments (including derivative assets)	186	4,059	3,655	7,900
Derivative liabilities	(77)	(2,557)	(195)	(2,829)
Total financial investments, net of derivative liabilities	130,281	110,259	6,660	247,200
Borrowings attributable to the with-profits fund held at fair value		(40)		(40)
Investment contracts liabilities without discretionary participation features held at fair value		(16,309)		(16,309)

Net asset value attributable to unit holders of consolidated unit trusts and similar funds	**(3,309)**	**(430)**	**(606)**	**(4,345)**
Other financial liabilities held at fair value		**(259)**	**(2,021)***	**(2,280)**
Total financial instruments at fair value	**126,972**	**93,221**	**4,033**	**224,226**
Percentage of total	**57%**	**41%**	**2%**	**100%**

*

The level 3 loans and other financial liabilities held by the non-linked shareholder-backed business include amounts of £1,842 million and £(2,021) million, respectively relating to the reinsurance arrangements attaching to the purchase of REALIC as described in note 11.

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G: Financial assets and liabilities (Continued)

	31 Dec 2011			
	Level 1	Level 2	Level 3	Total
	£m	£m	£m	£m
Analysis of financial investments, net of derivative liabilities by business type				
With-profits				
Equity securities and portfolio holdings in unit trusts	24,001	1,762	284	26,047
Debt securities	13,298	43,279	655	57,232
Other investments (including derivative assets)	252	1,378	2,793	4,423
Derivative liabilities	(214)	(1,127)		(1,341)
Total financial investments, net of derivative liabilities	37,337	45,292	3,732	86,361
Percentage of total	43%	53%	4%	100%
Unit-linked and variable annuity separate account				
Equity securities and portfolio holdings in unit trusts	59,662	198	30	59,890
Debt securities	4,160	4,698	3	8,861
Other investments (including derivative assets)	18	95		113
Derivative liabilities	(2)	(7)		(9)
Total financial investments, net of derivative liabilities	63,838	4,984	33	68,855
Percentage of total	93%	7%	0%	100%
Non-linked shareholder-backed				
Loans		279		279
Equity securities and portfolio holdings in unit trusts	1,175	176	61	1,412
Debt securities	11,753	46,401	251	58,405
Other investments (including derivative assets)	30	2,237	706	2,973
Derivative liabilities	(78)	(1,408)	(218)	(1,704)
Total financial investments, net of derivative liabilities	12,880	47,685	800	61,365
Percentage of total	21%	78%	1%	100%
Group total analysis, including other financial liabilities held at fair value				
Group total				
Loans		279		279
Equity securities and portfolio holdings in unit trusts	84,838	2,136	375	87,349
Debt securities	29,211	94,378	909	124,498
Other investments (including derivative assets)	300	3,710	3,499	7,509
Derivative liabilities	(294)	(2,542)	(218)	(3,054)
Total financial investments, net of derivative liabilities	114,055	97,961	4,565	216,581
Borrowings attributable to the with-profits fund held at fair value		(39)		(39)
Investment contracts liabilities without discretionary participation features held at fair value		(15,056)		(15,056)

Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(2,586)	(805)	(449)	(3,840)
Other financial liabilities held at fair value		(281)		(281)
Total financial instruments at fair value	111,469	81,780	4,116	197,365
Percentage of total	57%	41%	2%	100%

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G: Financial assets and liabilities (Continued)

Reconciliation of movements in level 3 financial instruments measured at fair value

The following tables reconcile the value of level 3 financial instruments at 1 January 2012 to that presented at 31 December 2012 and at 1 January 2011 to that presented at 31 December 2011.

Total investment return recorded in the income statement represents interest and dividend income, realised gains and losses, unrealised gains and losses on financial instruments classified at fair value through profit and loss and foreign exchange movements on an individual entity's overseas investments.

Total gains and losses recorded in other comprehensive income includes unrealised gains and losses on debt securities held as available-for-sale within Jackson and foreign exchange movements arising from the retranslation of the Group's overseas subsidiaries and branches.

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G: Financial assets and liabilities (Continued)

The transfers in and out of level 3 during 2012 represent sundry individual financial investments, none of which are materially significant as highlighted in the table below.

	2012										
	At 1 Jan	Total gains/ losses recorded in income statement	Total gains/ losses recorded in other comprehensive income	Acquisition of REALIC	Purchases	Sales	Settled	Issued	Transfers into level 3	Transfers out of Level 3	At 31 Dec
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
2012											
Loans		(46)	(42)	1,858			(12)	84			1,842
Equity securities and portfolio holdings in unit trusts	375	49	44		255	(98)			6	(63)	568
Debt securities	909	65	(3)		260	(217)	(73)		18	(169)	790
Other investments (including derivative assets)	3,499	250	(61)		482	(515)					3,655
Derivative liabilities	(218)	13								10	(195)
Total financial investments, net of derivative liabilities	4,565	331	(62)	1,858	997	(830)	(85)	84	24	(222)	6,660
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(449)	(20)	(47)		2	1		(93)			(606)
Other financial investments		41	46	(2,075)			73	(106)			(2,021)
Total	4,116	352	(63)	(217)	999	(829)	(12)	(115)	24	(222)	4,033
2011											
Equity securities and portfolio holdings in unit trusts	576	50	(1)		62	(278)				(34)	375
Debt securities	1,117	46	5		274	(490)	(21)		51	(73)	909
	3,106	224	(50)		691	(417)				(55)	3,499

Other investments (including derivative assets)									
Derivative liabilities	(226)	(17)						25	(218)
Total financial investments, net of derivative liabilities	4,573	303	(46)	1,027	(1,185)	(21)	51	(137)	4,565
Net asset value attributable to unit holders of consolidated unit trusts and similar funds	(379)	(78)		(10)	18				(449)
Total	4,194	225	(46)	1,017	(1,167)	(21)	51	(137)	4,116

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G: Financial assets and liabilities (Continued)

Of the total gains and losses in the income statement of £357 million (2011: £225 million), £126 million (2011: £99 million) relates to financial instruments still held at the end of the year, which can be analysed as follows:

	2012	2011
	£m	£m
Equity securities	**27**	49
Debt securities	**51**	20
Other investments	**48**	176
Derivative liabilities		(68)
Net asset value attributable to unit holders of consolidated unit trusts and similar funds		(78)
Total	**126**	99

Transfers between level 1 and level 2

During 2012, the transfers between levels within the Group's portfolio were primarily transfers from level 1 to 2 of £600 million (2011: £335 million) and transfers from level 2 to level 1 of £227 million (2011: nil). These transfers which relate to equity securities and debt securities arose to reflect the change in the observability of the inputs used in valuing these securities.

Interest income and expense

The interest income on financial assets not at fair value through profit and loss for the year ended 31 December 2012 from continuing operations was £1,886 million (2011: £1,814 million; 2010: £1,994 million).

The interest expense on financial liabilities not at fair value through profit and loss for the year ended 31 December 2012 from continuing operations was £420 million (2011: £456 million; 2010: £427 million).

G2: Market risk

Interest rate risk

The following table shows an analysis of the classes of financial assets and liabilities except for cash and cash equivalents and their direct exposure to interest rate risk. Each applicable class of the Group's

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financial assets or liabilities is analysed between those exposed to fair value interest rate risk, cash flow interest rate risk and those with no direct interest rate risk exposure:

	2012			
	Fair value Interest rate risk	Cash flow Interest rate risk	Not directly exposed to Interest rate risk	Total
	£m	£m	£m	£m
Financial assets				
Deposits	**1,021**	**11,445**	**187**	**12,653**
Debt securities	**131,732**	**7,851**	**520**	**140,103**
Loans	**8,992**	**2,809**	**20**	**11,821**
Other investments (including derivatives)	**1,896**	**1,126**	**4,878**	**7,900**
	143,641	**23,231**	**5,605**	**172,477**
Financial liabilities				
Core structural borrowings of shareholder-financed operations	**3,279**	**275**		**3,554**
Operational borrowings attributable to shareholder-financed operations	**574**	**1,670**	**1**	**2,245**
Borrowings attributable to with-profits funds	**379**	**562**	**92**	**1,033**
Obligations under funding, securities lending and sale and repurchase agreements	**403**	**2,033**		**2,436**
Investment contracts without discretionary participation features	**1,179**	**894**	**16,305**	**18,378**
Derivative liabilities	**974**	**576**	**1,279**	**2,829**
Other liabilities	**165**	**116**	**3,173**	**3,454**
	6,953	**6,126**	**20,850**	**33,929**

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	2011			
	Fair value Interest rate risk	Cash flow Interest rate risk	Not directly exposed to Interest rate risk	Total
	£m	£m	£m	£m
Financial assets				
Deposits	790	9,439	479	10,708
Debt securities	117,988	5,788	722	124,498
Loans	6,424	3,091	199	9,714
Other investments (including derivatives)	1,912	1,077	4,520	7,509
	127,114	19,395	5,920	152,429
Financial liabilities				
Core structural borrowings of shareholder-financed operations	3,362	249		3,611
Operational borrowings attributable to shareholder-financed operations	3,114	213	13	3,340
Borrowings attributable to with-profits funds	120	743	109	972
Obligations under funding, securities lending and sale and repurchase agreements	580	2,534		3,114
Investment contracts without discretionary participation features	1,011	903	15,053	16,967
Derivative liabilities	1,426	615	1,013	3,054
Other liabilities	158	142	949	1,249
	9,771	5,399	17,137	32,307

Liquidity analysis

(i) Contractual maturities of financial liabilities

The following table sets out the contractual maturities for applicable classes of financial liabilities, excluding derivative liabilities and investment contracts that are separately presented. The financial liabilities are included in the column relating to the contractual maturities at the undiscounted cash flows

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(including contractual interest payments) due to be paid assuming conditions are consistent with those of year end.

					2012				
	Total carrying value	1 Year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Financial liabilities									
Core structural borrowings of shareholder-financed operationsH13	**3,554**	**140**	**791**	**603**	**958**	**1,038**	**691**	**1,753**	**5,974**
Operational borrowings attributable to shareholder-financed operationsH13	**2,245**	**1,708**	**558**						**2,266**
Borrowings attributable to with-profits fundsH13	**1,033**	**115**	**542**	**199**	**71**	**12**	**73**	**194**	**1,206**
Obligations under funding, securities lending and sale and repurchase agreements	**2,436**	**2,436**							**2,436**
Other liabilities	**3,453**	**945**	**45**	**5**				**2,458**	**3,453**
Net asset value attributable to unit holders of consolidated unit-trusts and similar funds	**4,345**	**4,345**							**4,345**
Other creditors	**2,781**	**2,515**	**23**	**36**	**73**	**70**	**406**		**3,123**
	19,847	**12,204**	**1,959**	**843**	**1,102**	**1,120**	**1,170**	**4,405**	**22,803**

				2011				
	Total carrying value	1 Year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	No stated maturity	Total

	£m	£m	£m	£m	£m	£m	£m	£m	£m
Financial liabilities									
Core structural borrowings of shareholder-financed operationsH13	3,611	245	624	606	840	1,243	737	1,834	6,129
Operational borrowings attributable to shareholder-financed operationsH13	3,340	2,971	394						3,365
Borrowings attributable to with-profits fundsH13	972	199	418	158	100	5	97	139	1,116
Obligations under funding, securities lending and sale and repurchase agreements	3,114	3,114							3,114
Other liabilities	1,249	842	106	5				296	1,249
Net asset value attributable to unit holders of consolidated unit-trusts and similar funds	3,840	3,840							3,840
Other creditors	2,544	2,268	20	27	36	45	148		2,544
	18,670	13,479	1,562	796	976	1,293	982	2,269	21,357

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G: Financial assets and liabilities (Continued)

(ii) Maturity analysis of derivatives

The following table provides a maturity analysis of derivative assets and liabilities:

	2012					
	Total carrying value	1 Year or less	After 1 year to 3 years	After 3 years to 5 years	After 5 years	Total
	£m	£m	£m	£m	£m	£m
Net derivative position	**1,033**	**1,025**	**(22)**	**(14)**	**(50)**	**939**

	2011					
	Total carrying value	1 Year or less	After 1 year to 3 years	After 3 years to 5 years	After 5 years	Total
	£m	£m	£m	£m	£m	£m
Net derivative position	601	731	(18)	(11)	(31)	671

The net derivative positions as shown in the table above comprise the following derivative assets and liabilities:

	2012	2011	2010
	£m	£m	£m
Derivative assets	**3,862**	3,655	2,039
Derivative liabilities	**(2,829)**	(3,054)	(2,037)
Net derivative position	**1,033**	601	2

The majority of derivative assets and liabilities have been included at fair value within the one year or less column, representing the basis on which they are managed (ie to manage principally asset or liability value exposures). Contractual maturities are not considered essential for an understanding of the timing of the cash flows for these instruments and, in particular, the Group has no cash flow hedges. The only exception is certain identified interest rate swaps which are fully expected to be held until maturity solely for the purposes of matching cash flows on separately held assets and liabilities. For these instruments the undiscounted cash flows (including contractual interest amounts) due to be paid under the swap contract assuming conditions are consistent with those at year end are included in the column relating to the contractual maturity of the derivative.

The table below shows the maturity profile for investment contracts on an undiscounted basis to the nearest £ billion. This maturity profile has been based on the cash flow projections of expected benefit payments as part of the determination of the value of in-force business when

preparing EEV basis results.

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	2012							
	1 Year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	Total undis-counted value	Total carrying value
	£bn	£bn	£bn	£bn	£bn	£bn	£bn	£bn
Life assurance investment contracts	4	16	15	11	8	10	64	52

	2011							
	1 Year or less	After 1 year to 5 years	After 5 years to 10 years	After 10 years to 15 years	After 15 years to 20 years	Over 20 years	Total undis-counted value	Total carrying value
	£bn	£bn	£bn	£bn	£bn	£bn	£bn	£bn
Life assurance investment contracts	3	12	13	11	9	10	58	47

Most investment contracts have options to surrender early, albeit these are often subject to surrender or other penalties. It is therefore the case that most contracts could be said to have a contractual maturity of less than one year, but in reality the additional charges and term of the contracts means these are unlikely to be exercised in practice and the more useful information is to present information on expected payment.

The maturity profile above excludes certain corporate unit-linked business with gross policyholder liabilities of £12 billion (2011: £11 billion) which has no stated maturity but which is repayable on demand.

This table has been prepared on an undiscounted basis and accordingly the amounts shown for life assurance investment contracts differ from those disclosed on the statement of financial position. Durations of long-term business contracts, covering insurance and investment contracts, on a discounted basis are included in section D.

The vast majority of the Group's financial assets are held to back the Group's policyholder liabilities. Although asset/liability matching is an important component of managing policyholder liabilities (both those classified as insurance and those classified as investments), this profile is mainly relevant for managing market risk rather than liquidity risk. Within each business unit this asset/liability matching is performed on a portfolio by portfolio basis.

In terms of liquidity risk a large proportion of the policyholder liabilities contain discretionary surrender values or surrender charges, meaning that many of the Group's liabilities are expected to be held for the long term. Much of the Group's investment portfolios is in marketable securities, which can therefore be converted quickly to liquid assets.

For the reasons above an analysis of the Group's assets by contractual maturity is not considered necessary to evaluate the nature and extent of the Group's liquidity risk.

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G: Financial assets and liabilities (Continued)

Market and other financial risks

The Group's maximum exposure to credit risk of financial instruments before any allowance for collateral or allocation of losses to policyholders is represented by the carrying value of financial instruments on the balance sheet that have exposures to credit risk. These assets comprise cash and cash equivalents, deposits, debt securities, loans and derivative assets, and other debtors, the carrying value of which are disclosed at the start of this note and note G3 for derivative assets. The collateral in place in relation to derivatives is described in G4. Notes D2a(iv), D3a(ii)(ii) and D4a(iii), describe the security for these loans held by the Group, as disclosed at the start of this note.

Of the total loans and receivables held, £25 million (2011: £39 million) are past their due date but have not been impaired. Of the total past due but not impaired, £18 million is less than one year past their due date (2011: £3 million). The Group expects full recovery of these loans and receivables.

No further analysis has been provided of the element of loans and receivables that was neither past due nor impaired for the total portfolio. This is on the grounds of immateriality of the difference between the neither past due nor impaired elements and the total portfolio.

Financial assets that would have been past due or impaired had the terms not been renegotiated amounted to £86 million (2011: £90 million).

In addition, during the year the Group took possession of £16 million (2011: £13 million) of other collateral held as security, which mainly consists of assets that could be readily convertible into cash.

Further details of collateral and pledges are provided in note G4.

Currency risk

As at 31 December 2012, the Group held 19 per cent (2011: 21 per cent) and 7 per cent (2011: 9 per cent) of its financial assets and financial liabilities respectively, in currencies, mainly US dollar and Euro, other than the functional currency of the relevant business unit.

Financial assets, of which 56 per cent (2011: 55 per cent) are held by the PAC with-profits fund, allow the PAC with-profits fund to obtain exposure to foreign equity markets.

Financial liabilities, of which 28 per cent (2011: 28 per cent) are held by the PAC with-profits fund, mainly relate to foreign currency borrowings.

The exchange risks inherent in these exposures are mitigated through the use of derivatives, mainly forward currency contracts (note G3 to the consolidated financial statements in Item 18).

The amount of exchange loss recognised in the income statement in 2012, except for those arising on financial instruments measured at fair value through profit and loss, is £213 million (2011: £1 million gain; 2010: £82 million loss). This constitutes £1 million loss (2011: £11 million loss; 2010: £16 million loss) on Medium Term Notes (MTN) liabilities and £212 million of net loss (2011: £12 million net gain;2010: £98 million loss), mainly arising on investments of the PAC with-profits fund. The gains/losses on MTN liabilities are fully offset by value movements on cross-currency swaps, which are measured at fair value through profit and loss.

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G3: Derivatives and Hedging

Derivatives

The Group enters into a variety of exchange traded and over-the-counter derivative financial instruments, including futures, options, forward currency contracts and swaps such as interest rate swaps, cross-currency swaps, swaptions and credit default swaps.

All over-the-counter derivative transactions, with the exception of some Asia transactions, are conducted under standardised ISDA (International Swaps and Derivatives Association Inc) master agreements and the Group has collateral agreements between the individual Group entities and relevant counterparties in place under each of these market master agreements. The total fair value balances of derivative assets and liabilities as at 31 December 2012 were as follows:

	UK insurance operations	US insurance operations	Asia insurance operations	Asset management	Unallocated to a segment	Group total
	£m	£m	£m	£m	£m	£m
Derivative assets	**1,349**	**1,546**	**927**	**38**	**2**	**3,862**
Derivative liabilities	**(1,007)**	**(645)**	**(837)**	**(150)**	**(190)**	**(2,829)**
	342	**901**	**90**	**(112)**	**(188)**	**1,033**

2011

	UK insurance operations	US insurance operations	Asia insurance operations	Asset management	Unallocated to a segment	Group total
	£m	£m	£m	£m	£m	£m
Derivative assets	1,461	1,677	444	71	2	3,655
Derivative liabilities	(1,298)	(887)	(480)	(182)	(207)	(3,054)
	163	790	(36)	(111)	(205)	601

The above derivative assets are included in 'other investments' in the primary statements.

These derivatives are used for efficient portfolio management to obtain cost effective and efficient exposure to various markets in accordance with the Group's investment strategies and to manage exposure to interest rate, currency, credit and other business risks. See also note D3 for use of derivatives by the Group's US operations.

The Group uses various interest rate derivative instruments such as interest rate swaps to reduce exposure to interest rate volatility.

The UK with-profits funds use derivatives for the purposes of efficient portfolio management or reduction in investment risks. For UK annuity business derivatives are used to assist with asset and liability cash flow matching.

Some of the Group's products, especially those sold in the US, have certain guarantee features linked to equity indexes. A mismatch between guaranteed product liabilities and the performance of the underlying assets backing them, exposes the Group to equity index risk. In order to mitigate this risk,

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the relevant business units purchase swaptions, equity options and futures to match asset performance with liabilities under equity-indexed products.

The US operations and some of the UK operations hold large amounts of interest-rate sensitive investments that contain credit risks on which a certain level of defaults is expected. These entities have purchased some swaptions in order to manage the default risk on certain underlying assets and hence reduce the amount of regulatory capital held to support the assets.

Hedging

The Group has formally assessed and documented the effectiveness of the following hedges under IAS 39.

Fair value hedges

The Group has chosen to designate as a fair value hedge certain fixed to floating rate swaps which hedge the fair value exposure to interest rate movements of certain of the Group's operational borrowings.

The fair value of the derivatives designated as fair value hedges above at 31 December 2012, was an asset of less than £1 million (2011: asset of £3 million). Movements in the fair value of the hedging instruments of a net loss of £3 million (2011: net loss of £2 million) and the hedged items of a net gain of £3 million (2011: net gain of £2 million) are recorded in the income statement in respect of the fair value hedges above.

Net investment hedges

The Group has designated perpetual subordinated capital securities totalling US$2.85 billion (2011: US$2.85 billion) as a net investment hedge to hedge the currency risks related to the net investment in Jackson. The carrying value of the subordinated capital securities was £1,746 million as at 31 December 2012 (2011: £1,823 million; 2010: £1,462 million). The foreign exchange loss of £81 million (2011: loss of £18 million; 2010: gain of £45 million) on translation of the borrowings to pounds sterling at the statement of financial position date is recognised in the translation reserve in shareholders' equity.

This net investment hedge was 100 per cent effective.

Cash flow hedges

The Group has no cash flow hedges in place.

G4: Derecognition and collateral

Securities lending and reverse repurchase agreements

The Group has entered into securities lending (including repurchase agreements) whereby blocks of securities are loaned to third-parties, primarily major brokerage firms. The amounts above the fair value of the loaned securities required to be held as collateral by the agreements depend on the quality of the collateral, calculated on a daily basis. The loaned securities are not removed from the Group's

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consolidated statement of financial position, rather they are retained within the appropriate investment classification. Collateral typically consists of cash, debt securities, equity securities and letters of credit. At 31 December 2012, the Group had lent £3,015 million (2011: £7,843 million) of securities of which £2,047 million (2011: £5,820 million) was lent by the PAC with-profits fund and held collateral under such agreements of £3,137 million (2011: £8,160 million) of which £2,138 million (2011: £6,108 million) was held by the PAC with-profits fund.

At 31 December 2012, the Group had entered into reverse repurchase transactions under which it purchased securities and had taken on the obligation to resell the securities for the purchase price of £943 million (2011: £1,607 million), together with accrued interest.

Collateral and pledges under derivative transactions

At 31 December 2012, the Group had pledged £754 million (2011: £840 million) for liabilities and held collateral of £1,964 million (2011: £1,953 million) in respect of over-the-counter derivative transactions.

These transactions are conducted under terms that are usual and customary to collateralised transactions including, where relevant, standard securities lending and repurchase agreement.

G5: Impairment of financial assets

In accordance with the Group's accounting policy set out in note A3, impairment reviews were performed for available-for-sale securities and loans and receivables. In addition, impairment reviews were undertaken for the reinsurers' share of insurance contract liabilities.

During the year ended 31 December 2012, impairment losses of £50 million (2011: £126 million; 2010: £145 million) were recognised for available-for-sale securities and loans and receivables analysed as shown in the attached table.

	2012	2011	2010
	£m	£m	£m
Available-for-sale securities held by Jackson	**37**	62	124
Loans and receivables*	**13**	64	21
	50	126	145

* Relates to loans held by the UK with-profits fund and mortgage loans held by Jackson

Impairment losses recognised on available-for-sale securities amounted to £37 million (2011: £62 million; 2010: £124 million). Of this amount, 22 per cent (2011: 34 per cent; 2010: 90 per cent) has been recorded on structured asset-backed securities, primarily due to reduced cash flow expectations on such securities that are collateralised by diversified pools of primarily below investment grade securities. Of the losses related to the impairment of fixed maturity securities, the top five individual corporate issuers made up 74 per cent (2011: 75 per cent; 2010: 32 per cent), reflecting a deteriorating business outlook of the companies concerned. The impairment losses have been recorded in 'investment return' in the income statement.

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In 2012, the Group realised gross losses on sales of available-for-sale securities of £44 million (2011: £43 million; 2010: £160 million) with 64 per cent (2011: 64 per cent; 2010: 45 per cent) of these losses related to the disposal of fixed maturity securities of 10 (2011: 10; 2010: 15) individual issuers, which were disposed of as part of risk reduction programmes intended to limit future credit loss exposure. Of the £44 million (2011: £ 43 million; 2010: £160 million), £23 million (2011: £32 million; 2010: £99 million) relates to losses on sales of impaired and deteriorating securities.

The effect of those reasonably likely changes in the key assumptions that underpin the assessment of whether impairment has taken place depends on the factors described in note A4. A key indicator of whether such impairment may arise in future, and the potential amounts at risk, is the profile of gross unrealised losses for fixed maturity securities accounted for on an available-for-sale basis by reference to the time periods by which the securities have been held continuously in an unrealised loss position and by reference to the maturity date of the securities concerned.

For 2012, the amount of gross unrealised losses for fixed maturity securities classified as available-for-sale under IFRS in an unrealised loss position was £178 million (2011: £246 million; 2010: £370 million). Notes B1 and D3 provide further details on the impairment charges and unrealised losses of Jackson's available-for-sale securities.

H: Other information on statement of financial position items

H1: Intangible assets attributable to shareholders

(a) Goodwill

	2012	2011
	£m	£m
Cost		
At beginning of year	**1,585**	1,586
Additional consideration paid on previously acquired business	**2**	
Exchange differences	**2**	(1)
At end of year	**1,589**	1,585
Aggregate impairment	**(120)**	(120)
Net book amount at end of year	**1,469**	1,465

Goodwill attributable to shareholders comprises:

	2012	2011
	£m	£m
M&G	**1,153**	1,153
Other	**316**	312
	1,469	1,465

'Other' represents goodwill amounts across cash generating units (CGUs) in Asia and US operations. Other goodwill amounts are not individually material.

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Impairment testing

Goodwill does not generate cash flows independently of other groups of assets and thus is assigned to CGUs for the purposes of impairment testing. These CGUs are based upon how management monitors the business and represent the lowest level to which goodwill can be allocated on a reasonable basis.

Assessment of whether goodwill may be impaired

Goodwill is tested for impairment by comparing the CGUs carrying amount, including any goodwill, with its recoverable amount.

With the exception of M&G, the goodwill attributable to shareholders in the statement of financial position mainly relates to acquired life businesses. The Company routinely compares the aggregate of net asset value and acquired goodwill on an IFRS basis of acquired life business with the value of the business as determined using the EEV methodology, as described in note D1. Any excess of IFRS over EEV carrying value is then compared with EEV basis value of current and projected future new business to determine whether there is any indication that the goodwill in the IFRS statement of financial position may be impaired.

M&G

The recoverable amount for the M&G CGU has been determined by calculating its value in use. This has been calculated by aggregating the present value of future cash flows expected to be derived from the M&G operating segment (based upon management projections).

The discounted cash flow valuation has been based on a three-year plan prepared by M&G, and approved by management, and cash flow projections for later years.

The value in use is particularly sensitive to a number of key assumptions as follows:

(i) The set of economic, market and business assumptions used to derive the three-year plan. The direct and secondary effects of recent developments, eg changes in global equity markets, are considered by management in arriving at the expectations for the financial projections for the plan.

(ii) The assumed growth rate on forecast cash flows beyond the terminal year of the plan. A growth rate of 2.5 per cent (2011: 2.5 per cent) has been used to extrapolate beyond the plan period representing management's best estimate view of the long-term growth rate of the business after considering the future and past growth rates and external sources of data.

(iii) The risk discount rate. Differing discount rates have been applied in accordance with the nature of the individual component businesses. For retail and institutional business, a risk discount rate of 12 per cent (2011: 12 per cent) has been applied to post-tax cash flows. The pre-tax risk discount rate was 15 per cent (2011: 15 per cent). Management have determined the risk discount rate by reference to an average implied discount rate for comparable UK listed asset managers calculated by reference to risk-free rates, equity risk premiums of 5 per cent and an average 'beta' factor for relative market risk of comparable UK listed asset managers. A similar approach has been applied for the other component businesses of M&G.

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(iv) That asset management contracts continue on similar terms.

Management believes that any reasonable change in the key assumptions would not cause the recoverable amount of M&G to fall below its carrying amount.

Japanese life company

The aggregate goodwill impairment of £120 million at 31 December 2012 and 2011 relates to the goodwill held in relation to the Japanese life operation which was impaired in 2005.

(b) Deferred acquisition costs and other intangible assets attributable to shareholders

The deferred acquisition costs (DAC) and other intangible assets in the Group consolidated statement of financial position attributable to shareholders comprise:

	2012	2011*	2010*
	£m	£m	£m
Deferred acquisition costs related to insurance contracts as classified under IFRS 4	**3,866**	3,805	3,550
Deferred acquisition costs related to investment management contracts, including life assurance contracts classified as financial instruments and investment management contracts under IFRS 4	**100**	107	110
	3,966	3,912	3,660
Present value of acquired in-force policies for insurance contracts as classified under IFRS 4 (PVIF)	**64**	64	70
Other intangibles	**237**	258	171
	301	322	241
Total of deferred acquisition costs and other intangible assets	**4,267**	4,234	3,901

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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H: Other information on statement of financial position items (Continued)

	2012 £m						2011* £m	2010* £m
	Deferred acquisition costs							
	UK	US[note (i)]	Asia	Asset management	PVIF and other intangibles	Total	Total	Total
Balance at 1 Jan								
As previously reported	**111**	**3,880**	**744**	**12**	**322**	**5,069**	4,667	4,097
Effect of change in accounting policy[note B]		**(785)**	**(50)**			**(835)**	(766)	(651)
After effect of change	**111**	**3,095**	**694**	**12**	**322**	**4,234**	3,901	3,446
Additions	**12**	**798**	**249**	**3**	**31**	**1,093**	1,117	968
Acquisition of REALIC in 2012 and UOB Life Assurance Ltd in 2010					**5**	**5**		12
Amortisation to the income statement:								
Operating profit	**(20)**	**(356)**	**(277)**	**(5)**	**(51)**	**(709)**	(792)	(515)
Amortisation related to short-term fluctuations in investment returns		**76**				**76**	287	283
	(20)	**(280)**	**(277)**	**(5)**	**(51)**	**(633)**	(505)	(232)
Exchange differences		**(144)**	**(12)**		**(6)**	**(162)**	(2)	129
Change in shadow DAC related to movement in unrealised appreciation of Jackson's securities classified as available-for-sale**		**(270)**				**(270)**	(275)	(410)
Disposals							(2)	(5)
Dilution of Group's holdings								(7)
Balance at 31 December	**103**	**3,199**	**654**	**10**	**301**	**4,267**	4,234	3,901

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

** (See note D3(e) for explanation)

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US operations DAC

Summary balances

(i) The DAC amount in respect of US insurance operations comprises amounts in respect of:

	2012	2011*	2010*
	£m	£m	£m
Variable annuity business	**3,330**	2,960	2,283
Other business	**821**	855	980
Cumulative shadow DAC (for unrealised gains/losses booked in other comprehensive income)	**(952)**	(720)	(434)
Total DAC for US operations	**3,199**	3,095	2,829

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

Deferred acquisition costs related to insurance and investment contracts attributable to shareholders

The movement in deferred acquisition costs relating to insurance and investments contracts attributable to shareholders are as follows:

	2012		2011*		2010*	
	Insurance contracts	Investment Management	Insurance contracts	Investment Management	Insurance contracts	Investment Management
	£m	£m	£m	£m	£m	£m
DAC at 1 January	**3,805**	**105**	3,550	110	3,172	107
Additions	**1,048**	**12**	982	17	710	21
Amortisation	**(563)**	**(17)**	(450)	(20)	(19)	(18)
Exchange differences	**(154)**				104	
Change in shadow DAC related to movement in unrealised appreciation of Jackson's securities classified as available-for-sale	**(270)**		(275)		(410)	
Dilution of holding in PruHealth					(7)	
DAC at 31 December	**3,866**	**100**	3,807	107	3,550	110

* The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

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Note

All of the additions are through internal development. The carrying amount of the balance comprises the following gross and accumulated amortisation amounts:

	31 Dec 2012	31 Dec 2011	31 Dec 2010
	£m	£m	£m
Gross amount	**210**	200	183
Accumulated amortisation	**(110)**	(93)	(73)
Net book amount	**100**	107	110

Present value of acquires in-force (PVIF) and other intangibles attributable to shareholders

	2012				2011			
	PVIF note (i)	Other intangibles note (ii) Distribution rights	Software	Total	PVIF note (i)	Other intangibles note (ii) Distribution rights	Software	Total
	£m	£m	£m	£m	£m	£m	£m	£m
At 1 January								
Cost	**212**	**235**	**163**	**610**	203	136	144	483
Accumulated amortisation	**(148)**	**(36)**	**(104)**	**(288)**	(133)	(23)	(86)	(242)
	64	**199**	**59**	**322**	70	113	58	241
Additions (including amounts arising on acquisition of subsidiaries)	**5**		**31**	**36**		96	24	120
Amortisation charge	**(5)**	**(17)**	**(29)**	**(51)**	(5)	(9)	(21)	(35)
Disposals							(2)	(2)
Exchange differences		**(5)**	**(1)**	**(6)**	(1)	(1)		(2)
At 31 December	**64**	**177**	**60**	**301**	64	199	59	322
Comprising:								
Cost	**217**	**230**	**193**	**640**	200	235	163	598
Accumulated amortisation	**(153)**	**(53)**	**(133)**	**(339)**	(136)	(36)	(104)	(276)
	64	**177**	**60**	**301**	64	199	59	322

Note

(i)

All of the PVIF balances relate to insurance contracts and is accounted for under UK GAAP as permitted by IFRS 4. Investment contracts have been fully amortised. Amortisation is charged to the 'acquisition costs and other operating expenditure' line in the income statement over the period of provision of asset management services as those profits emerge.

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(ii)

Other intangibles comprise distribution and software rights. Distribution rights relate to facilitation fees paid in respect of the bancassurance partnership arrangements in Asia for the bank distribution of Prudential's insurance products for a fixed period of time. The distribution rights amounts are amortised over the term of the distribution contracts. Software is amortised over its useful economic life, which generally represents the licence period of the software acquired. Amortisation is charged to the 'acquisition costs and other expenditure' line in the income statement.

H2: Intangible assets attributable to with-profits funds

(a) Goodwill in respect of acquired investment subsidiaries for venture fund and other investment purposes

	2012	2011
	£m	£m
At 1 January	**178**	166
Additions in the year		12
At 31 December	**178**	178

All the goodwill relates to the UK insurance operations segment.

The venture fund investments consolidated by the Group relates to investments by PAC with-profits fund managed by M&G. The goodwill shown in the table above relates to these venture fund investments. Goodwill is tested for impairment of these investments by comparing the investment's carrying value including goodwill with its recoverable amount. The recoverable amount of the investments is determined by calculating their fair value less costs to sell. The fair value is determined by using a discounted cash flow valuation. The valuations are based on cash flow projections to 2016 prepared by management after considering the historical experience and future growth rates of the business. The key assumption applied in the calculations is the risk discount rate ranging from 10 per cent to 14 per cent derived by reference to risk-free rates and an equity premium risk. In 2012, no goodwill was deemed to be impaired following the impairment testing carried out.

(b) Deferred acquisition costs and other intangible assets

Other intangible assets in the Group consolidated statement of financial position attributable to with-profits funds consist of:

	2012	2011
	£m	£m
Deferred acquisition costs related to insurance contracts attributable to the PAC with-profits fund	**6**	6
Distribution rights attributable to with-profits funds of the Asia insurance operations	**70**	83
Computer software attributable to with-profits funds of the Asia insurance operations	**2**	
	78	89

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Deferred acquisition costs related to insurance contracts attributable to the PAC with-profit fund

The movement in deferred acquisition costs relating to insurance contracts attributable to the PAC with-profits fund is as follows:

	2012	2011
	£m	£m
At 1 January	**6**	13
Amortisation charge		(7)
At 31 December	**6**	6

The above costs relate to non-participating business written by the PAC with-profits sub-fund.

No deferred acquisition costs are established for the participating business.

Distribution rights attributable to with-profit funds of the Asia insurance operations

Distribution rights relate to facilitation fees paid in relation to the bancassurance partnership arrangements in Asia for the bank distribution of Prudential's insurance products for a fixed period of time. The distribution rights amounts are amortised over the term of the distribution contracts.

	2012	2011
	£m	£m
At 1 January		
Gross amount	**96**	108
Accumulated amortisation	**(13)**	(11)
	83	97
Amortisation charge	**(9)**	(5)
Exchange differences	**(4)**	1
Reclassification		(10)
At 31 December	**70**	83
Comprising:		
Gross amount	**92**	96
Accumulated amortisation	**(22)**	(13)
	70	83

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H3: Reinsurers' share of insurance contract liabilities

	2012	2011
	£m	£m
Insurance contract liabilities	**6,079**	1,486
Claims outstanding	**780**	161
	6,859	1,647
Comprising amounts in respect of:		
UK insurance operations[note D2(f)]	**608**	589
US insurance operations[note D3(f)]	**6,076**	907
Asia insurance operations[note D4(f)]	**175**	151
	6,859	1,647

The movement on reinsurers' share of insurance contract liabilities is as follows:

	2012	2011
	£m	£m
At 1 January	**1,486**	1,167
Acquisition of REALIC	**4,810**	
Other movements in the year	**(55)**	303
Foreign exchange translation differences	**(162)**	16
At 31 December	**6,079**	1,486

H4: Tax assets and liabilities

Assets

Of the £254 million (2011: £546 million) current tax recoverable, the majority is expected to be recovered in one year or less.

Deferred tax asset

	2012	2011
	£m	£m
Unrealised losses on investments	**102**	297

Balances relating to investment and insurance contracts	**1**	13
Short-term timing differences	**2,097**	1,513
Capital allowances	**15**	15
Unused deferred tax losses	**99**	438
Total	**2,314**	2,276

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The deferred tax asset at 31 December 2012 and 2011 arises in the following parts of the Group:

	2012	2011
	£m	£m
UK insurance operations:		
SAIF	**1**	1
PAC with-profits fund (including PAL)	**113**	78
Other	**69**	153
US insurance operations	**1,889**	1,392
Asia insurance operations	**83**	114
Other operations	**159**	538
Total	**2,314**	2,276

The increase in the deferred tax asset primarily relates to additional short term timing differences on US insurance reserves following the REALIC acquisition partially offset by the utilisation of tax losses across the Group.

Deferred tax assets are recognised to the extent that they are regarded as recoverable, that is to the extent that, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted.

The taxation regimes applicable across the Group often apply separate rules to trading and capital profits and losses. The distinction between temporary differences that arise from items of either a trading or capital nature may affect the recognition of deferred tax assets. Accordingly, for the 2012 results and financial position at 31 December 2012 the possible tax benefit of approximately £158 million (31 December 2011: £158 million), which may arise from capital losses valued at approximately £0.8 billion (31 December 2011: £0.7 billion), is sufficiently uncertain that it has not been recognised. In addition, a potential deferred tax asset of £122 million (31 December 2011: £147 million), which may arise from trading tax losses and other potential temporary differences totalling £0.5 billion (31 December 2011: £0.6 billion) is sufficiently uncertain that it has not been recognised. Of these, losses of £105 million will expire within the next 7 years. The remaining losses have no expiry date. Until the end of 2012, for the Group's UK life insurance companies, shareholders' profits were calculated using regulatory surplus as a starting point, with appropriate deferred tax adjustments for IFRS. Beginning in 2013, under new UK life tax rules, shareholders' profits will be calculated using accounting profit or loss as a starting point. As the 2012 Finance Act had been enacted at the balance sheet date, the effects of these changes are reflected in the financial statements for the year ended 31 December 2012 but with no material impact on the Group's net assets.

The two tables that follow provide a breakdown of the recognised deferred tax assets set out above for both the short-term timing differences and unused tax losses split by business unit. The table also shows the period of estimated recoverability for each respective business unit. For these and each category of deferred tax asset recognised their recoverability against forecast taxable profits is not significantly impacted by any current proposed changes to future accounting standards.

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Short-term timing differences

	2012 £m	Expected period of recoverability
Asia	**42**	**1 to 3 years**
JNL	**1,800**	**With run-off of in-force book**
UK long-term Business	**151**	**1 to 10 years**
Other	**104**	**1 to 10 years**
Total	**2,097**	

Unused tax losses

	2012 £m	Expected period of recoverability
Asia	**36**	**3 to 5 years**
UK long-term Business	**18**	**1 to 3 years**
Other	**45**	**1 to 3 years**
Total	**99**	

Liabilities

The current tax liability decreased to £445 million (2011: £930 million) reflecting the settlement of prior year balances in the UK and Asia following the agreement of tax positions.

Deferred tax liability

	2012 £m	2011* £m	2010* £m
Unrealised gains on investments	**1,814**	1,566	1,678
Balances relating to investment and insurance contracts	**432**	667	801
Short-term timing differences	**1,715**	1,687	1,477
Capital allowances	**9**	9	12
Total	**3,970**	3,929	3,968

*

The 2011 and 2010 comparative results have been adjusted from those previously published for the retrospective application of the change in accounting policy described in note A5.

Under IAS 12, 'Income Taxes', deferred tax is measured at the tax rates that are expected to apply to the period when the asset is realised or the liability settled, based on the tax rates (and laws) that have been enacted or are substantively enacted at the end of the reporting periods.

The UK government's tax rate change to 23 per cent (from the 24 per cent effective from 1 April 2012) has had the effect of reducing the UK with-profits and shareholder-backed business element of

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the net deferred tax balances as at 31 December 2012 by £52 million. The tax change to 23 per cent is effective from 1 April 2013 but has been enacted at 31 December 2012.

The subsequent proposed phased rate changes to 21 per cent are expected to have the effect of reducing the UK with-profits and shareholder-backed business elements of the net deferred tax balances at 31 December 2012 by £52 million.

H5: Accrued investment income and other debtors

	2012	2011
	£m	£m
Accrued investment income		
Interest receivable	**2,015**	1,919
Other	**783**	791
Total	**2,798**	2,710
Other debtors		
Amounts due from:		
Policyholders	**271**	227
Intermediaries	**27**	27
Reinsurers	**23**	11
Other	**1,040**	722
Total	**1,361**	987
Total accrued investment income and other debtors	**4,159**	3,697

Of the £4,159 million (2011: £3,697 million) of accrued investment income and other debtors, £538 million (2011: £162 million) is expected to be settled after one year or more.

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H6: Property, plant and equipment

Property, plant and equipment comprise Group occupied properties and tangible assets. A reconciliation of the carrying amount of these items from the beginning of the year to the end of the year is as follows:

	2012			2011		
	Group occupied property	Tangible assets	Total	Group occupied property	Tangible assets	Total
	£m	£m	£m	£m	£m	£m
At 1 January						
Cost	**262**	**915**	**1,177**	197	764	961
Accumulated depreciation	**(29)**	**(400)**	**(429)**	(24)	(383)	(407)
Net book amount	**233**	**515**	**748**	173	381	554
Year ended 31 December						
Opening net book amount	**233**	**515**	**748**	173	381	554
Exchange differences	**(9)**	**(8)**	**(17)**	(2)	(7)	(9)
Depreciation charge	**(10)**	**(80)**	**(90)**	(5)	(69)	(74)
Additions	**4**	**135**	**139**	5	119	124
Arising on acquisitions of subsidiaries		**(1)**	**(1)**	69	99	168
Disposals and transfers	**(2)**	**(12)**	**(14)**	(7)	(8)	(15)
Closing net book amount	**216**	**549**	**765**	233	515	748
At 31 December						
Cost	**255**	**999**	**1,254**	262	915	1,177
Accumulated depreciation	**(39)**	**(450)**	**(489)**	(29)	(400)	(429)
Net book amount	**216**	**549**	**765**	233	515	748

Capital expenditure: property, plant and equipment by segment

The capital expenditure of £135 million (2011: £124 million) arose as follows: £80 million in UK, £24 million in US and £20 million in Asia in insurance operations with the remaining balance of £11 million arising from asset management operations and unallocated corporate expenditure (2011: £69 million in UK, £20 million in US, £21 million in Asia in insurance operations and £14 million in other).

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H: Other information on statement of financial position items (Continued)

H7: Investment properties

Investment properties principally relate to the PAC with-profits fund and are carried at fair value. A reconciliation of the carrying amount of investment properties at the beginning and end of the year is set out below:

	2012	2011
	£m	£m
At 1 January	**10,757**	11,247
Additions:		
Resulting from acquisitions	**1,025**	393
Resulting from expenditure capitalised	**118**	45
Disposals	**(695)**	(1,439)
Net (loss) gain from fair value adjustments	**(175)**	522
Net foreign exchange differences	**(53)**	(41)
Transfers (to)/from held for sale assets	**(97)**	25
Transfers from owner occupied properties		5
At 31 December	**10,880**	10,757

The income statement includes the following items in respect of investment properties:

	2012	2011	2010
	£m	£m	£m
Rental income from investment properties	**559**	606	625
Direct operating expenses (including repairs and maintenance expenses) arising from investment properties that generated rental income during the year	**64**	128	125

Further information on the investment property held by the UK insurance operations further information is included in note D2(a).

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Investment properties of £3,845 million (2011: £3,439 million) are held under finance leases. A reconciliation between the total of future minimum lease payments at the statement of financial position date, and their present value is shown below:

	2012	2011
	£m	£m
Future minimum lease payments at 31 December	**988**	1,071
Future finance charges on finance leases	**(877)**	(944)
Present value of minimum lease payments	**111**	127
Future minimum lease payments are due as follows:		
Less than 1 year	**6**	7
1 to 5 years	**23**	26
Over 5 years	**959**	1,038
Total	**988**	1,071
The present values of these minimum lease payments are:		
Less than 1 year	**6**	6
1 to 5 years	**19**	23
Over 5 years	**86**	98
Total	**111**	127

Contingent rent is that portion of the lease payments that is not fixed in amount but is based on the future value of a factor that changes other than with the passage of time. There was no contingent rent recognised as income or expense in 2012 and 2011.

The Group's policy is to rent investment properties to tenants through operating leases. Minimum future rentals to be received on non-cancellable operating leases of the Group's freehold investment properties are receivable in the following periods:

	2012	2011
	£m	£m
Less than 1 year	**451**	430
1 to 5 years	**1,541**	1,407
Over 5 years	**3,785**	3,304
Total	**5,777**	5,141

The total minimum future rentals to be received on non-cancellable sub-leases for the Group's investment properties held under finance leases at 31 December 2012 are £2,439 million (2011: £2,553 million).

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H8: Investments in associates and joint ventures

Investments in associates

The Group had two associates at 31 December 2012 (31 December 2011: one) that were accounted for under the equity method. The Group's associates at 31 December 2012 are a 25 per cent interest in PruHealth Holdings Limited and a 49.99 per cent interest in PPM South Africa, following the dilution of the Group's holding in the period (see note I2). The Group's share of the profit during the year was a profit of £8 million (full year 2011: a loss of £3 million). The total carrying value of these associates are £113 million (2011: £70 million). This is reflected in the Group's profit after tax attributable to equity holders during the year.

Associates accounted for using the equity method

A summary of the movements in investments in associates accounted for using the equity method in 2012 and 2011 is set out below:

	Share of share capital and share premium	Share of retained earnings	Share of net assets	Goodwill	Total carrying value
	£m	£m	£m	£m	£m
Balance at 1 January 2010	1		1	2	3
Transfer of PruHealth to associates(note I2)	91	(25)	66		66
Acquisition/capital injection in PruHealth	9		9		9
Goodwill write off				(1)	(1)
Share of loss for the year after tax		(6)	(6)		(6)
Balance as at 31 December 2010	**101**	**(31)**	**70**	**1**	**71**
Capital injection	4		4		4
Disposals	(1)		(1)		(1)
Goodwill write off				(1)	(1)
Share of loss for the year after tax		(3)	(3)		(3)
Balance at 31 December 2011	**104**	**(34)**	**70**		**70**
Transfer of PPMSA as an associate(note I2)		**39**	**39**		**39**
Exchange translation and other movements		**(6)**	**(6)**		**(6)**
Share of profit for the year after tax		**10**	**10**		**10**
Balance at 31 December 2012	**104**	**9**	**113**		**113**

There have been no changes recognised in the other comprehensive income of associates that would also be recognised in the other comprehensive income by the Group.

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The Group's share of the assets, liabilities, revenues and profit and loss of associates accounted for using the equity method at 31 December 2012 and 2011 is as follows:

	2012	2011
	£m	£m
Financial position		
Total assets (excluding goodwill)	**162**	109
Total liabilities	**(49)**	(39)
Net assets	**113**	70

	2012	2011	2010
	£m	£m	£m
Results of operations			
Revenue	**96**	81	39
Profit (Loss) in the year	**10**	(3)	(6)

There are several minor service agreements in place between the associates and the Group. During 2012, the aggregate amount of the transactions was £42 million (2011: £33 million) and the balance due to the Group as at 31 December 2012 was £73.2 million (2011: £74.2 million).

Associates and joint ventures carried at fair value through profit and loss

In addition to the above the Group has associates that are carried at fair value through profit and loss, as allowed under IAS 28, that comprise investments in Open-Ended Investment Companies (OEICs), unit trusts, funds holding collateralised debt obligations, property unit trusts and venture capital investments of the PAC with-profits funds where the Group has significant influence. These investments are incorporated both in the UK and overseas, and some have year ends which are non-coterminous with that of the Group. In these instances, the investments are recorded at fair value at 31 December 2012 based on valuations or pricing information at that specific date. The aggregate fair value of associates carried at fair value through profit and loss where there are published price quotations is approximately £0.8 billion (2011: £4.8 billion) at 31 December 2012.

The aggregate assets of these associates are approximately £2.2 billion (2011: £3.4 billion). Aggregate liabilities, excluding liabilities to unit holders and shareholders for unit trusts and OEICs, are approximately £0.8 billion (2011: £1.1 billion). Fund revenues, with revenue arising in unit trusts and OEICs deemed to constitute the investment return for these vehicles, were approximately £0.1 billion (2011: £0.3 billion) and net profit in the year, excluding unit trusts and OEICs where all investment returns accrue to unit holders or shareholders respectively, was approximately £0.1 billion (2011: profit of £0.2 billion).

Investments in joint ventures

The Group owns a number of joint ventures. Joint ventures represent activities over which the Group exercises joint control through contractual agreement with one or more parties. The Group's

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significant joint ventures, which are accounted for using proportionate consolidation, comprise following interests:

Investment	% held	Principal activity	Country
CITIC Prudential Life Insurance Company Limited	50	Life assurance	China
CITIC-Prudential Fund Management Company Limited	49	Asset management	China
ICICI Prudential Asset Management Company Limited	49	Asset management	India
Prudential BSN Takaful Berhad	49	General and life insurance	Malaysia
BOCI-Prudential Asset Management Limited	36	Asset management	China (Hong Kong)
ICICI Prudential Life Insurance Company Limited	26	Life assurance	India

The investments noted in the table above have the same accounting year end as the Group, except for ICICI Prudential Life Insurance Company Limited and ICICI Prudential Asset Management Company Limited. Although these investments have reporting periods ending 31 March, 12 months of financial information up to 31 December is recorded. Accordingly, the information covers the same period as that of the Group.

Joint ventures contributed £98 million (31 December 2011: £54 million) to profit after tax attributable to equity holders during the period. The year-on-year movement in these contributions reflect the growth in their operating profit based on longer-term investment returns and the increase in short-term fluctuations in investment returns by these joint ventures.

Further, in June 2012, the PAC with-profits fund, via its venture fund holdings and as part of its investment portfolio, entered into a joint venture to acquire control of Veolia Water RegCo (now renamed Affinity Water), the UK regulated water business of Veolia Environnement S.A. This joint venture investment is carried at fair value through profit and loss in the Group's financial statements, as allowed under IAS 28. The results of this operation are reflected in the movement in the unallocated surplus of the PAC with-profits fund and therefore do not affect shareholders' results.

The summarised financial data for the Group's share of investments in joint ventures is as follows:

	2012	2011
	£m	£m
Financial position		
Current assets	**442**	706
Non-current assets	**3,504**	2,757
Total assets	**3,946**	3,463
Current liabilities	**(375)**	(301)
Non-current liabilities	**(3,220)**	(2,799)
Total Liabilities	**(3,595)**	(3,100)
Net equity	**351**	363

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	2012	2011	2010
	£m	£m	£m
Results of operations			
Revenue	**1,040**	1,056	1,195
Expenses	**(942)**	(1,002)	(1,135)
Net profit	**98**	54	60

The joint ventures have no significant contingent liabilities or capital commitments to which the Group is exposed nor does the Group have any significant contingent liabilities or capital commitments in relation to its interest in the joint ventures.

H9: Properties held for sale

Investment properties are classified as held for sale when contracts have been exchanged but the sale has not been completed at the period end. At 31 December 2012 the value of assets held for sale was £98 million (2011: £3 million).

Gains on disposal of held for sale assets are recorded in 'investment return' within the income statement.

H10: Cash and cash equivalents

Cash and cash equivalents consist of cash at bank and in hand, deposits held at call with banks, treasury bills and other short-term highly liquid investments with less than 90 days maturity from the date of acquisition. Cash and cash equivalents included in the cash flow statement comprise the following statement of financial position amounts:

	2012	2011
	£m	£m
Cash	**4,884**	6,338
Cash equivalents	**1,500**	919
Total cash and cash equivalents	**6,384**	7,257

Cash and cash equivalents held centrally are considered to be available for general use by the Group. These funds amount to £482 million and £309 million at 31 December 2012 and 2011, respectively. The remaining funds are considered not to be available for general use by the Group, and include funds held for the benefit of policyholders.

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H: Other information on statement of financial position items (Continued)

H11: Shareholders' equity: share capital, share premium and reserves

A summary of the ordinary shares in issue is set out below:

Share capital and share premium

	Number of ordinary shares	Share capital £m	Share premium £m
Issued shares of 5p each fully paid:			
At 1 January 2011	2,545,594,506	127	1,856
Shares issued under share option schemes	2,444,824		17
Shares issued in lieu of cash dividends			
At 31 December 2011	**2,548,039,330**	**127**	**1,873**
Shares issued under share option schemes	**9,203,022**	**1**	**16**
Reserve movements in respect of shares issued in lieu of cash dividends			
At 31 December 2012	**2,557,242,352**	**128**	**1,889**

Amounts recorded in share capital represent the nominal value of the shares issued. The difference between the proceeds received on issue of shares, net of issue costs, and the nominal value of shares issued is credited to the share premium account.

At 31 December 2012, there were options outstanding under Save As You Earn schemes to subscribe for shares as follows:

	Number of shares to subscribe for	Share price range from	to	Exercisable by year
31 December 2012	**9,396,810**	**288p**	**629p**	**2018**
31 December 2011	13,329,709	288p	572p	2017

Transactions by Prudential plc and its subsidiaries in Prudential plc shares

The Group buys and sells Prudential plc ('own shares') either in relation to its employee share schemes or via transactions undertaken by authorised investment funds that the Group is deemed to control. Further information about these transactions is set out below.

The cost of own shares of £97 million as at 31 December 2012 (2011: £109 million) is deducted from retained earnings. The Company has established trusts to facilitate the delivery of shares under employee incentive plans and savings-related share option schemes. At 31 December 2012, 8.0 million (2011: 8.1 million) Prudential plc shares with a market value of £69 million (2011: £52 million) were held in such trusts. Of this total, 8.0 million (2011: 8.0 million) shares were held in trusts under employee incentive plans.

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In 2012, the Company purchased the following number of shares in respect of employee incentive plans.

	Number of shares purchased (in millions)*	Cost £m
2012	**9.4**	**76.1**
2011	8.2	54.7

*

The maximum number of shares held in 2012 was 8.0 million which was in December 2012.

Of the total shares held in trust no shares were held by a qualifying employee share ownership trust (2011: 0.1 million).

The shares purchased each month are as follows:

	2012 Share Price				2011 Share Price			
	Number of shares	Low	High	Cost	Number of shares	Low	High	Cost
		£	£	£		£	£	£
January	**15,573**	**6.40**	**6.40**	**99,589**	12,723	6.83	6.83	86,834
February	**12,678**	**7.33**	**7.33**	**92,930**	11,688	7.13	7.13	83,376
March	**4,022,002**	**7.10**	**8.03**	**32,058,297**	2,106,702	7.04	7.14	15,253,240
April	**368,901**	**7.27**	**7.67**	**2,712,460**	263,361	7.40	7.49	1,960,300
May	**939,541**	**6.80**	**7.26**	**6,407,556**	174,614	7.46	7.53	1,307,410
June	**482,377**	**6.61**	**6.84**	**3,208,338**	1,418,209	7.07	7.18	10,141,069
July	**15,047**	**7.26**	**7.26**	**109,166**	98,334	6.89	7.34	683,084
August	**28,488**	**7.88**	**8.12**	**228,176**	1,520,620	5.77	6.32	9,051,804
September	**712,649**	**8.16**	**8.25**	**5,829,154**	19,273	5.85	6.00	115,022
October	**12,549**	**8.39**	**8.39**	**105,329**	15,385	6.07	6.07	93,310
November	**492,993**	**8.55**	**9.15**	**4,502,129**	110,951	6.15	6.33	692,501
December	**2,277,012**	**8.86**	**9.27**	**20,706,597**	2,456,692	6.07	6.55	15,226,106
Total	**9,379,810**			**76,059,721**	8,208,552			54,694,056

The Group has consolidated a number of authorised investment funds where it is deemed to control these funds under IFRS. Some of these funds hold shares in Prudential plc. The total number of shares held by these funds at 31 December 2012 was 4.5 million (2011: 8.6 million) and the cost of acquiring these shares of £27 million (2011: £52 million) is included in the cost of own shares. The market value of these shares as at

31 December 2012 was £39 million (2011: £54 million).

During 2012, these funds made net disposals of 4,143,340 Prudential shares (2011: net disposals of 1,171,635) for a net decrease of £25.1 million to book cost (2011: net increase of £4.8 million).

All share transactions were made on an exchange other than the Stock Exchange of Hong Kong.

Other than set out above the Group did not purchase, sell or redeem any Prudential plc listed securities during 2012 or 2011.

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Reserves

The translation reserve of £66 million (2011: £282 million) represents cumulative foreign exchange translation differences taken directly to equity in accordance with IFRS, net of related tax. In accordance with IFRS 1, cumulative translation differences are deemed to be zero at 1 January 2004, the date of transition to IFRS.

The available-for-sale reserve represents gains or losses arising from changes in the fair value of available-for-sale securities of Jackson, net of the related change in amortisation of deferred income and acquisition costs and of the related tax.

H12: Insurance contract liabilities and unallocated surplus of with-profits funds

Movement in year

	Insurance contract liabilities	Unallocated surplus of with-profits funds
	£m	£m
At 1 January 2011	171,291	10,253
Income and expense included in the income statement	8,748	(1,025)
Foreign exchange translation differences	324	(13)
At 1 January 2012	**180,363**	**9,215**
Income and expense included in the income statement	**32,760**	**1,381**
Foreign exchange translation differences	**(4,539)**	**(7)**
At 31 December 2012	**208,584**	**10,589**

Notes B5, D2b, D3b and D4b provide further analysis of the movement in the year of the Group's policyholder liabilities and unallocated surplus of the with-profits funds.

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H: Other information on statement of financial position items (Continued)

H13: Borrowings

Core structural borrowings of shareholder-financed operations

	2012				2011
	Innovative Tier 1*	Lower Tier 2*	Senior**	Total	Total
	£m	£m	£m	£m	£m
Central operations					
Subordinated debt:					
€20m Medium-Term Subordinated Notes 2023[note (i)]		**16**		**16**	17
£435m 6.125% Subordinated Notes 2031		**429**		**429**	428
£400m 11.375% Subordinated Notes 2039		**386**		**386**	384
US$1,000m 6.5% Perpetual Subordinated Capital Securities	**615**			**615**	644
US$250m 6.75% Perpetual Subordinated Capital Securities[note (ii)]	**154**			**154**	161
US$300m 6.5% Perpetual Subordinated Capital Securities[note (ii)]	**185**			**185**	193
US$750m 11.75% Perpetual Subordinated Capital Securities	**458**			**458**	477
US$550m 7.75% Perpetual Subordinated Capital Securities[note (ii)]	**334**			**334**	348
	1,746	**831**		**2,577**	2,652
Senior debt:					
£300m 6.875% Bonds 2023			**300**	**300**	300
£250m 5.875% Bonds 2029			**249**	**249**	249
			549	**549**	549
Total central operations	**1,746**	**831**	**549**	**3,126**	3,201
£275m bank loan[note (iii)]			**275**	**275**	250
US$250m 8.15% Surplus Notes 2027[note (iv)]		**153**		**153**	160
Total[notes (v), (vi)]	**1,746**	**984**	**824**	**3,554**	3,611

*

These debt classifications are consistent with the treatment of capital for regulatory purposes, as defined in the FSA handbook. In January 2011, the Company issued US$550 million 7.75 per cent Tier 1 subordinated debt, primarily to retail investors. The proceeds, net of costs, were US$539 million (£340 million) and were used to finance the repayments of the €500 million Tier 2 subordinated debt in December 2011.

The Group has designated US$2.85 billion (2011: US$2.85 billion) of its Tier 1 subordinated debt as a net investment hedge under IAS 39 to hedge the currency risks related to the net investment in Jackson.

**

The senior debt ranks above subordinated debt in the event of liquidation.

Notes

(i)

The €20 million borrowings were issued at 20-year Euro Constant Maturity Swap (capped at 6.5 per cent). These have been swapped into borrowings of £14 million with interest payable at three month £LIBOR plus 1.2 per cent.

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H: Other information on statement of financial position items (Continued)

(ii)

The US$250 million 6.75 per cent borrowings, the US$300 million 6.5 per cent borrowings and the US$550 million 7.75 per cent borrowings can be converted, in whole or in part, at the Company's option and subject to certain conditions, on any interest payment date, into one or more series of Prudential preference shares.

(iii)

The PruCap bank loan was increased from £250 million to £275 million on 20 December 2012. The loan has been made in two tranches: a £160 million loan maturing in June 2014, currently drawn at a cost of 12 month £LIBOR plus 0.6 per cent and a £115 million loan maturing on 20 December 2017 and currently drawn at a cost of 12 month £LIBOR plus 0.79 per cent.

(iv)

The Jackson borrowings are unsecured and subordinated to all present and future indebtedness, policy claims and other creditor claims of Jackson.

(v)

Maturity analysis

The following table sets out the contractual maturity analysis of the Group's core structural borrowings:

	2012	**2011**
	£m	**£m**
Less than 1 year	**115**	115
1 to 2 years	**160**	
2 to 3 years		135
3 to 4 years		
4 to 5 years		
Over 5 years	**3,279**	3,361
Total	**3,554**	3,611

(vi)

Management analyses the net core structural borrowings position as follows:

	2012	**2011**
	£m	**£m**

Total core structural borrowings (as above)	**3,554**	3,611
Less: Holding company cash and short-term investments (recorded within the consolidated statement of financial position)	**(1,380)**	(1,200)
Net core structural borrowings of shareholder-financed operations	**2,174**	2,411

(vii)

In January 2013, the Company issued core structural borrowings of US$700 million Tier 1 perpetual subordinated capital securities. The proceeds, net of costs, were US$689 million.

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H: Other information on statement of financial position items (Continued)

Operational borrowings attributable to shareholder-financed operations

	2012	2011
	£m	£m
Borrowings in respect of short-term fixed income securities programmes		
Commercial paper	**1,535**	2,706
Medium-Term Notes 2013[note (vi)]	**250**	250
Medium-Term Notes 2015	**299**	
	2,084	2,956
Borrowings of US operations		
Investment subsidiaries (non-recourse)[note (i)]	**19**	20
Piedmont and CDO funds (non-recourse)[notes (i), (ii)]	**1**	1
	20	21
Other borrowings		
Bank loans and overdrafts	**1**	13
Obligations under finance leases	**1**	1
Other borrowings[note (iii)]	**139**	349
	141	363
Total	**2,245**	3,340

Notes

(i) In all instances the holders of the debt instruments issued by these subsidiaries and funds do not have recourse beyond the assets of those subsidiaries and funds.

(ii) Piedmont is an investment trust investing in certain asset-backed and mortgage-backed securities in the US. These borrowings pertain to debt instruments issued to external parties.

(iii) Other borrowings mainly include amounts whose repayment to the lender is contingent upon future surplus emerging from certain contracts specified under the arrangement. If insufficient surplus emerges on those contracts, there is no recourse to other assets of the Group and the liability is not payable to the degree of shortfall.

The Group has chosen to designate as a fair value hedge under IAS 39 certain fixed to floating rate swaps which hedge the fair value exposures to interest rate movements of these borrowings.

In addition, other borrowings include senior debt issued through the Federal Home Loan Bank of Indianapolis (FHLB), secured by collateral posted with the FHLB by Jackson.

(iv)

In addition to the debt listed above, £200 million Floating Rate Notes were issued by Prudential plc in October 2012 which will mature in April 2013. These Notes have been wholly subscribed by a Group subsidiary and accordingly have been eliminated on consolidation in the Group financial statements. These notes were originally issued in October 2008 and have been reissued upon their maturity.

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H: Other information on statement of financial position items (Continued)

(v)

Maturity analysis

The following table sets out the contractual maturity analysis of the Group's operational borrowings attributable to shareholder-financed operations:

	2012	2011
	£m	£m
Less than 1 year	**1,920**	3,169
1 to 2 years	**6**	140
2 to 3 years	**309**	10
3 to 4 years	**9**	10
4 to 5 years	**1**	11
Over 5 years		
Total	**2,245**	3,340

(vi)

In January 2013 the Company repaid on maturity, £250 million Medium Term Notes included within borrowings in respect of short-term fixed income securities in the table above.

Borrowings attributable to with-profits operations

	2012	2011
	£m	£m
Non-recourse borrowings of consolidated investment funds [note (i)]	**823**	747
£100m 8.5% undated subordinated guaranteed bonds of Scottish Amicable Finance plc[note (ii)]	**100**	100
Other borrowings (predominantly obligations under finance leases)	**110**	125
Total[note (iii)]	**1,033**	972

Notes

(i)

In all instances the holders of the debt instruments issued by these funds do not have recourse beyond the assets of those funds.

(ii)

The interests of the holders of the bonds issued by Scottish Amicable Finance plc, a subsidiary of the Scottish Amicable Insurance Fund, are subordinate to the entitlements of the policyholders of that fund.

(iii)

Maturity analysis

The following table sets out the contractual maturity analysis of the Group's borrowings attributable to with-profits operations:

	2012	**2011**
	£m	**£m**
Less than 1 year	**288**	297
1 to 2 years	**82**	75
2 to 3 years	**124**	30
3 to 4 years	**46**	110
4 to 5 years	**61**	31
Over 5 years	**432**	429
Total	**1,033**	972

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H: Other information on statement of financial position items (Continued)

H14: Provisions and contingencies

Provisions

	2012	2011
	£m	£m
Provision in respect of defined benefit pension schemes:[I3]		
Surplus (deficit), gross of deferred tax, based on scheme assets held, including investments in Prudential insurance policies:		
Attributable to PAC with-profits fund	**37**	41
Attributable to shareholder-financed operations	**(1)**	23
	36	64
Add back investments in Prudential insurance policies	**169**	165
Provision after elimination of investments in Prudential insurance policies and matching policyholder liabilities from Group statement of financial position	**205**	229
Other provisions (see below)	**396**	300
Total provisions	**601**	529

Analysis of other provisions:

	2012	2011
	£m	£m
At 1 January[I3]	**300**	282
Charged to income statement:		
Additional provisions	**237**	144
Unused amounts released	**(12)**	(29)
Used during the year	**(124)**	(97)
Exchange differences	**(5)**	
At 31 December	**396**	300
Comprising:		
Legal provisions	**20**	14
Restructuring provisions	**27**	23
Other provisions	**349**	263
Total	**396**	300

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Other provisions

The movement in other provisions is shown in the table below:

	2012			2011		
	Legal provisions note (i)	**Restructuring provisions note (ii)**	**Other Provisions note (iii)**	**Legal provisions note (i)**	**Restructuring provisions note (ii)**	**Other Provisions note (iii)**
At 1 January	**14**	**23**	**263**	20	26	236
Charged to income statement:						
Additional provisions	**10**	**14**	**213**		5	139
Unused amounts released	**(1)**	**(4)**	**(7)**		(5)	(24)
Used during the year	**(2)**	**(6)**	**(116)**	(6)	(3)	(88)
Exchange differences	**(1)**		**(4)**			
Total at 31 December	**20**	**27**	**349**	14	23	263

Notes

(i) Total legal provisions at 31 December 2012 of £20 million related to Jackson. Jackson has been named in civil proceedings, which appear to be substantially similar to other class action litigation brought against many life insurers in the US, alleging misconduct in the sale of insurance products. Of the £20 million legal provision as at 31 December 2012, £18 million has been established to cover this potential litigation and is expected to be utilised over the next five years.

(ii) Restructuring provisions primarily relate to restructuring activities of UK insurance operations. The provisions pertain to property liabilities resulting from the closure of regional sales centres and branches and staff terminations and other transformation costs to enable streamlining of operations.

(iii) Other provisions comprise staff benefits provisions of £286 million, provisions for onerous contracts of £61 million and regulatory and other provisions of £2 million. Staff benefits are generally expected to be paid out within the next three years.

The provision balance is expected to be paid out within the next five years.

Contingencies and related obligations

In addition to the legal proceedings relating to Jackson mentioned under the legal provisions section above, the Group is involved in other litigation and regulatory issues.

Whilst the outcome of such litigation and regulatory issues cannot be predicted with certainty, the Company believes that their ultimate outcome will not have a material adverse effect on the Group's financial condition, results of operations, or cash flows.

Pension mis-selling review

The pensions review by the UK insurance regulator of past sales of personal pension policies required all UK life insurance companies to review their cases of potential mis-selling and record a provision for the estimated costs. The Group met the requirement of the FSA to issue offers to all cases by 30 June 2002.

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At 31 December 2012 the pension mis-selling provision was £306 million (31 December 2011: £362 million).

The pension mis-selling provision is included within the liabilities in respect of investment contracts with discretionary participation features under IFRS 4. The pension mis-selling provision at 31 December 2012 of £306 million is stochastically determined on a discounted basis. The average discount rate implied in the movement in the year is 2.3 per cent (2011: 2.6 per cent).

The directors believe that, based on current information, the provision, together with future investment return on the assets backing the provision, will be adequate to cover the costs of pension mis-selling including administration costs. Such provision represents the best estimate of probable costs and expenses. However, there can be no assurance that the current provision level will not need to be increased.

The costs associated with the pension mis-selling review have been met from the inherited estate (see below). Accordingly, these costs have not been charged to the asset shares used in the determination of policyholder bonus rates. Hence policyholders' pay-out values have been unaffected by pension mis-selling.

In 1998, Prudential stated that deducting mis-selling costs from the inherited estate would not impact its bonus or investment policy and it gave an assurance that if this unlikely event were to occur, it would make available support to the fund from shareholder resources for as long as the situation continued, so as to ensure that policyholders were not disadvantaged. The assurance was designed to protect both existing policyholders at the date it was announced, and policyholders who subsequently purchased policies while the pension mis-selling review was continuing.

This review was completed on 30 June 2002. The assurance will continue to apply to any policy in force at 31 December 2003, both for premiums paid before 1 January 2004, and for subsequent regular premiums (including future fixed, retail price index or salary related increases and Department of Work and Pensions rebate business). The assurance has not applied to new business since 1 January 2004. New business in this context consists of new policies, new members to existing pension schemes plus regular and single premium top-ups, transfers and switches to existing arrangements. The maximum amount of capital support available under the terms of the assurance will reduce over time.

The bonus and investment policy for each type of with-profits policy is the same irrespective of whether or not the assurance applies and this is expected to continue for the foreseeable future. Hence removal of the assurance for new business has had no impact on policyholder returns.

Guaranteed annuities

Prudential Assurance used to sell guaranteed annuity products in the UK and at 31 December 2012 held a provision of £47 million (2011: £90 million) within the main with-profits fund within policyholder liabilities to honour guarantees on these products. The Group's main exposure to guaranteed annuities in the UK is through SAIF and at 31 December 2012 a provision of £371 million (2011: £370 million) was held in SAIF to honour the guarantees. As SAIF is a separate sub-fund of the Prudential Assurance long-term business fund, wholly attributable to the policyholders of the fund, the movement in this provision has no impact on shareholders.

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Other matters

Inherited estate of the PAC long-term fund

The assets of the with-profits sub-fund (WPSF) within the long-term insurance fund of The Prudential Assurance Company Limited (PAC) comprise the amounts that it expects to pay out to meet its obligations to existing policyholders and an additional amount used as working capital. The amount payable over time to policyholders from the WPSF is equal to the policyholders' accumulated asset shares plus any additional payments that may be required by way of smoothing or to meet guarantees. The balance of the assets of the WPSF is called the 'inherited estate' and has accumulated over many years from various sources.

The inherited estate, as working capital, enables PAC to support with-profits business by providing the benefits associated with smoothing and guarantees, by providing investment flexibility for the fund's assets, by meeting the regulatory capital requirements that demonstrate solvency and by absorbing the costs of certain significant events or fundamental changes in its long-term business without affecting the bonus and investment policies. The size of the inherited estate fluctuates from year to year depending on the investment return and the extent to which it has been required to meet smoothing costs, guarantees and other events.

Support for long-term business funds by shareholders' funds

As a proprietary insurance company, PAC is liable to meet its obligations to policyholders even if the assets of the long-term funds are insufficient to do so. The assets, represented by the unallocated surplus of with-profits funds, in excess of amounts expected to be paid for future terminal bonuses and related shareholder transfers ('the excess assets') in the long-term funds could be materially depleted over time by, for example, a significant or sustained equity market downturn, costs of significant fundamental strategic change or a material increase in the pension mis-selling provision. In the unlikely circumstance that the depletion of the excess assets within the long-term fund was such that the Group's ability to satisfy policyholders' reasonable expectations was adversely affected, it might become necessary to restrict the annual distribution to shareholders or to contribute shareholders' funds to the long-term funds to provide financial support.

In 1997, the business of Scottish Amicable Life Assurance Society (SALAS), a mutual society, was transferred to PAC. In effecting the transfer, a separate sub-fund, Scottish Amicable Insurance Fund (SAIF), was established within PAC's long-term business fund. This sub-fund contains all the with-profits business and all other pension business that was transferred. No new business has been or will be written in the sub-fund and the sub-fund is managed to ensure that all the invested assets are distributed to SAIF policyholders over the lifetime of SAIF policies. With the exception of certain amounts in respect of the unitised with-profits life business, all future earnings arising in SAIF are retained for SAIF policyholders. Any excess (deficiency) of revenue over expense within SAIF during a period is attributable to the policyholders of the fund. Shareholders have no interest in the profits of SAIF but are entitled to the asset management fees paid on this business.

SAIF with-profits policies contain minimum levels of guaranteed benefit to policyholders. In addition, as mentioned earlier in this note, certain pensions products have guaranteed annuity rates at retirement. Should the assets of SAIF be inadequate to meet the guaranteed benefit obligations of the

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policyholders of SAIF, the PAC long-term fund would be liable to cover any such deficiency in the first instance. The directors believe that the probability of either the PAC long-term fund or the Group's shareholders' funds having to contribute to SAIF is remote.

Unclaimed Property Provision

Jackson has received regulatory inquiries on an industry-wide matter relating to claims settlement practices and compliance with unclaimed property laws. Concurrently, some regulators and state legislatures have required and others are considering proposals that would require life insurance companies to take additional steps to identify unreported deceased policy and contract holders. Additionally, numerous states are contracting with independent firms to perform specific unclaimed property audits or targeted market conduct examinations covering claims settlement practices and procedures for escheating unclaimed property. One such firm has been contracted by treasury departments of 26 states to perform an examination of the Jackson's practices for handling unclaimed property. Any regulatory audits, related examination activity and internal reviews may result in additional payments to beneficiaries, escheatment of funds deemed abandoned under state laws, administrative penalties and changes in the Jackson's procedures for the identification of unreported claims and handling of escheatable property.

In 2011, Jackson initiated a project to compare its entire policy master file to vendors' databases of known deaths and accrued a £16 million provision for potential claims at 31 December 2011. In 2012, Jackson recognised a charge of £18 million, net of policy reserves released upon death, as a result of the project. At 31 December 2012, based on its current analysis, Jackson has accrued £17 million for estimated remaining claims that have not yet been positively identified.

Guarantees and commitments

Guarantee funds in both the UK and the US provide for payments to be made to policyholders on behalf of insolvent life insurance companies. These guarantee funds are financed by payments assessed on solvent insurance companies based on location, volume and types of business. The Group estimated its reserve for future guarantee fund assessments for Jackson, included within other liabilities to be £31 million at 31 December 2012 (2011: £17 million). Similar assessments for the UK businesses were not significant. The directors believe that the reserve is adequate for all anticipated payments for known insolvencies.

At 31 December 2012, Jackson has unfunded commitments of £325 million (2011: £341 million) related to its investments in limited partnerships and of £86 million (2011: £77 million) related to commercial mortgage loans. These commitments were entered into in the normal course of business and the directors do not expect a material adverse impact on the operations to arise from them.

Jackson owns debt instruments issued by securitisation trusts managed by PPM America. At 31 December 2012, the support provided by certain forbearance agreements Jackson entered into with the counterparty to certain of these trusts could potentially expose Jackson to maximum losses of £31 million (2011: £71 million), if circumstances allowed the forbearance period to cease. Jackson believes that, so long as the forbearance period continues, the risk of loss under the agreements is remote.

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The Group has provided other guarantees and commitments to third-parties entered into in the normal course of business but the Company does not consider that the amounts involved are significant.

H15: Other liabilities

	2012	2011
	£m	£m
Creditors arising from direct insurance and reinsurance operations	**1,134**	970
Interest payable	**62**	67
Other items*	**2,258**	212
Total	**3,454**	1,249

* Of the £2,258 million other items as at 31 December 2012, £2,021 million related to liabilities for funds withheld under reinsurance arrangement of the Group's US operations from the purchase of REALIC, as discussed in note I1.

I: Other notes

I1: Acquisition of subsidiaries

(a) Acquisition of Reassure America Life Insurance Company (REALIC)

On 4 September 2012, the Group through its indirect wholly-owned subsidiary, Jackson National Life Insurance Company (JNLI) completed the acquisition of 100 per cent issued share capital of SRLC America Holding Corp. (SRLC), and its primary operating subsidiary, Reassure America Life Insurance Company (REALIC). The purchase consideration which remains subject to final agreement under the terms of the transaction with Swiss Re, is £370 million (US$587 million). The acquisition increases the scale of the Group's life business in the US, helping Jackson to diversify earnings by increasing the amount of income from underwriting activities thereby enhancing the quality of earnings in a capital efficient manner. Immediately prior to the acquisition, SRLC entered into a reinsurance arrangement with Swiss Re, the former ultimate parent company facilitating Swiss Re to retain a portion of the REALIC business. As collateral for this reinsurance arrangement, REALIC holds £2.1 billion of policy loans, bonds and short-term investments, which are offset by a funds withheld liability.

REALIC was a US-based insurance company whose business model was to acquire, through purchase or reinsurance, closed blocks of insurance business, primarily life assurance risks. REALIC did not write new business.

The purchase consideration paid is equivalent to the fair value of the identifiable acquired assets and liabilities assumed and accordingly no goodwill is recognised under IFRS on the date of completion of the acquisition.

In addition to the purchase consideration, the Group incurred £9 million of acquisition related costs that have been recognised as an expense during the year, in the consolidated income statement.

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The provisional fair value of the acquired assets and liabilities are shown in the table below.

	Fair value recognised at acquisition date
	£m
Identifiable assets	
Intangible assets attributable to shareholders:	
Acquired value of in-force business	**5**
Other non-investment and non-cash assets:	
Reinsurers' share of insurance contract liabilities	**5,444**
Deferred tax	**390**
Current tax recoverable	**44**
Accrued investment income	**58**
Other debtors	**38**
Investments of long-term business and other operations:	
Loans	**2,204**
Equity securities and portfolio holdings in unit trusts	**69**
Debt securities	**7,177**
Cash and cash equivalents	**147**
Total identifiable assets	**15,576**
Identifiable liabilities	
Policyholder liabilities:	
Insurance contract liabilities	**12,912**
Other non-insurance liabilities	**2,294**
Total identifiable liabilities	**15,206**
Net identifiable assets acquired and liabilities assumed	**370**
Purchase consideration	**370**

At the date the financial statements were approved the fair value of the identifiable acquired assets and liabilities and the consideration were subject to finalisation. In accordance with accounting guidance for business combinations, the Company will continue to review the balance sheet and record required adjustments, for up to a twelve month period following the acquisition close date, in order to reflect updated information on certain accruals, related expenses, or other potential valuation adjustments, if further information becomes available about facts and circumstances that existed as of the acquisition date. Any measurement period adjustments determined to be material will be applied retrospectively to the acquisition date in the Company's consolidated financial statements and depending on the nature of the adjustment, the Company's results subsequent to the acquisition period could be affected.

Reserves were initially valued consistent with existing IFRS guidance. Accordingly, as for the Group's measurement of Jackson's insurance assets and liabilities, under IFRS 4, a 'grandfathered' US GAAP basis has been applied. For instance the traditional products were valued using standard modelling techniques with assumptions updated to match current interest rate environment or be

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consistent with Jackson's assumptions where appropriate. Base reserves on interest sensitive products were set equal to the account value and the reserves accounted for under FASB ASC Subtopic 944-80 Financial Services Insurance Separate Accounts (formerly SOP 03-1) were adjusted to reflect Jackson's assumptions where appropriate. In addition, provision has been made for the effects of fair valuing the acquired policyholder liabilities and value of in force business in accordance with IFRS 3.

Included within the identifiable assets as shown above are loans and other debtors acquired with fair values of £2,204 million and £38 million, respectively. These values represent the gross contractual amounts all of which are expected to be collected. The majority of the loans of £2,204 million were held to back liabilities for funds withheld under reinsurance arrangements as described above.

The consolidated statement of cash flows contains a £224 million net cash outflow in respect of this acquisition representing cash consideration of £371 million (based on the preliminary purchase price of £417 million with a deferred consideration of £46 million) less cash and cash equivalents acquired of £147 million.

Impact of acquisition on the results of the Group

	Actual Post acquisition period from 4 Sept to 31 Dec 2012	Estimated Full Year 2012 (note i)
	£m	£m
Revenue	**184**	**695**
Operating profit based on longer-term investment returns	**67**	
Short-term fluctuations in investment returns	**13**	
Amortisation of acquisition accounting on the purchase of REALIC[note (ii)]	**(19)**	
Profit before tax	**61**	**123**

Notes

(i) Estimation of the REALIC business' contribution to the Group's consolidated revenue and profit before tax for the year if the acquisition had occurred on 1 January 2012. In determining these amounts, it has been assumed that the fair value adjustments which arose on the date of acquisition would have been the same if the acquisition had occurred on 1 January 2012.

(ii)

The profit of £61 million for the period has been determined after a charge of £(19) million for amortisation of acquisition accounting adjustments. This charge reflects the net effect of:

(a)

The difference between the yield on the acquired debt securities (excluding those held to back funds withheld for reinsurance contracts) determined by reference to their market value at acquisition as required by the IFRS 3 purchase GAAP purposes and the book yield on a historic GAAP basis;

(b)

Amortisation of the fair value adjustments on policyholder liabilities, and

(c)

Amortisation of the acquired value of in-force business.

This charge has been shown separately within Group's supplementary analysis of profit, as explained in note B1.

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(b) Acquisition of Thanachart Life Assurance Company Limited

On 5 November 2012, Prudential plc, through its subsidiary Prudential Life Assurance (Thailand) Public Company Limited ('Prudential Thailand') entered into an agreement to acquire 100 per cent of Thanachart Life Assurance Company Limited ('Thanachart Life'), a wholly-owned life insurance subsidiary of Thanachart Bank Public Company limited ('Thanachart Bank'). The consideration for Thanachart Life is THB 17.5 billion (£352 million at the year end exchange rate) settled in cash on completion, with a further payment of THB 0.5 billion (£10 million) payable 12 months after completion, subject to a post-completion adjustment to reflect the net asset value as at the completion date. The transaction was approved by the regulator in March 2013 and is expected to close in the second quarter of 2013. Upon completion of the transaction, Thanachart Life will become a wholly-owned subsidiary of Prudential Thailand.

As part of the deal, Prudential Thailand and Thanachart Bank have entered into an agreement to establish an exclusive 15-year partnership to develop jointly their bancassurance business in Thailand. This transaction builds on Prudential's strategy of focusing on the highly attractive markets of South-east Asia and is in line with the group's multichannel distribution strategy.

(c) PAC with-profits funds acquisitions

2012:

The PAC with-profits fund, via its venture fund holdings and as part of its investment portfolio, has made an acquisition of a joint venture, see note H8. There were no acquisitions of subsidiaries made during the year.

2011:

The PAC with-profits fund, via its venture fund holdings and as part of its investment portfolio, made acquisitions during the period. These were acquisitions for a 100 per cent interest of Earth & Wind Energias Renovables SL, a company which invests in solar panel parks, in March 2011 and a 100 per cent interest of Alticom Holdings BV, a company investing in telecommunication towers, in June 2011. The Earth & Wind portfolio of solar panel parks was further expanded with the acquisition of a 100 per cent interest in Promociones Fotovoltaicas Betula SL, Promociones Fotovoltaicas Castanea SL, Promociones Fotovoltaicas Corylus SL and Promociones Fotovoltaicas Fagus SL in July 2011 and a 50 per cent controlling interest in Sarinena Solar SL in October 2011.

As these transactions are within the with-profits fund, they have no impact on shareholders' profit or equity for the year ended 31 December 2011. The impact on the Group's consolidated revenue, including investment returns, is not material. Had the acquisitions been effected at 1 January 2011, the revenue and profit of the Group for the year ended 31 December 2011 would not have been materially different.

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A summary of the consideration, goodwill and net assets acquired relating to these four acquisitions is provided in the table below:

	2011 Total
	£m
Cash consideration paid	67
Net assets acquired:	
Property, plant and equipment	190
Other non-investment and non-cash assets	16
Cash and cash equivalents	14
Borrowings attributable to with-profits funds	(114)
Derivative liabilities	(2)
Other non-insurance liabilities	(49)
Fair value of net assets acquired	55
Total goodwill arising on acquisition attributable to the with-profits fund	12

I2: Changes to Group's holdings

PPM South Africa

On 22 February 2012, M&G completed transactions to (i) exchange bonus share rights for equity holdings with the employees of PPM South Africa and (ii) the sale of a 10 per cent holding in the majority of the business to Thesele Group, a minority shareholder, for cash. Following these transactions M&G's majority holding in the business reduced from 75 per cent to 49.99 per cent. Under IFRS requirements, the divestment is accounted for as the disposal of the 75 per cent holding and an acquisition of a 49.99 per cent holding at fair value resulting in a reclassification of PPM South Africa from a subsidiary to an associate. As a consequence of the IFRS application, the transactions gave rise to a gain on dilution of £42 million. This amount is shown separately and in the Group's 2012 supplementary analysis of profit excluded from the Group's IFRS operating profit based on longer-term investment returns. The net cash outflow arising from this change to the Group's holdings, as shown in the consolidated statement of cash flows, of £23 million, comprised the net effect of cash and cash equivalents no longer consolidated and the cash proceeds received.

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I3: Staff and pension plans

(a) Staff and employment costs

The average number of staff employed by the Group during the year was:

	2012	2011	2010
Business operations:			
Asia operations	**18,584**	17,001	17,988
US operations	**4,000**	3,785	3,545
UK operations	**5,035**	4,628	4,459
Total	**27,619**	25,414	25,992

The costs of employment were:

	2012	2011	2010
	£m	£m	£m
Business operations:			
Wages and salaries	**1,204**	1,101	1,052
Social security costs	**85**	75	69
Other pension costs:			
Defined benefit schemes*:			
Defined benefit schemes PSPS**	**17**	22	27
Defined benefit schemes Other schemes*	**21**	(34)	31
Defined contribution schemes:			
Defined contribution schemes Domestic	**12**	12	11
Defined contribution schemes Overseas	**35**	29	26
Pension actuarial and other (gains) losses charged to income statement*	**(145)**	(37)	26
	(60)	(8)	121
Total	**1,229**	1,168	1,242

*

The derivation of these amounts is shown in note (b)(i)4(i).

**

Consistent with the derecognition of the Company's interest in the underlying IAS 19 surplus of Prudential Staff Pension Scheme (PSPS) as described in note (b)(i)1 below, the other pension costs for PSPS represents

the cash cost of contributions for ongoing service of active members and the unwind of discount on the opening provision for deficit funding for PSPS.

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(b) Pension plans

(i) Defined benefit plans

1 Summary

The Group asset/liability in respect of defined benefit pension schemes is as follows:

	2012			2011
	PSPS	Other schemes	Total	Total
	£m	£m	£m	£m
Underlying economic surplus[note (ii)]	**1,174**	**(36)**	**1,138**	1,543
Less: unrecognised surplus and adjustment for obligation under IFRIC 14 for deficit funding (2011 only)[note (ii)]	**(1,010)**		**(1,010)**	(1,607)
Economic surplus (deficit) (including investment in Prudential insurance policies)[note (ii)]	**164**	**(36)**	**128**	(64)
Attributable to:				
PAC with-profits fund	**115**	**(37)**	**78**	(41)
Shareholder-backed operations	**49**	**1**	**50**	(23)
Consolidation adjustment against policyholder liabilities for investment in Prudential insurance policies		**(169)**	**(169)**	(165)
IAS 19 pension asset (liability) on the Group statement of financial position[as explained in note 7 below]	**164**	**(205)**	**(41)**	(229)

*

At 31 December 2012, the PSPS pension asset of £164 million and the other schemes' pension liabilities of £205 million were included within 'Other debtors' and 'Provisions' respectively on the consolidated statement of financial position. The comparative liabilities of £229 million as at 31 December 2011 were included within 'Provisions'.

The Group's businesses operate a number of pension schemes. The specific features of these plans vary in accordance with the regulations of the country in which the employees are located, although they are, in general, funded by the Group and based either on a cash balance formula or on years of service and salary earned in the last year or years of employment. The largest defined benefit scheme is the principal UK scheme, namely the Prudential Staff Pension Scheme (PSPS), which PSPS accounts for 86 per cent (2011: 86 per cent) of the underlying scheme liabilities of the Group defined benefit schemes.

The Group also operates two smaller defined benefit schemes for UK employees in respect of Scottish Amicable and M&G. For all three schemes, the projected unit method was used for the most recent full actuarial valuations. There is also a small defined benefit scheme in Taiwan

with a negligible deficit.

Triennial actuarial valuations

Defined benefit schemes in the UK are generally required to be subject to full actuarial valuation every three years in order to assess the appropriate level of funding for schemes in relation to their

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commitments. These valuations include assessments of the likely rate of return on the assets held within the separate trustee administered funds.

The last completed actuarial valuation of PSPS was as at 5 April 2011 by CG Singer, Fellow of the Institute of Actuaries, of Towers Watson Limited. This valuation was finalised in the first half of 2012 and demonstrated the scheme to be 111 per cent funded by reference to the Scheme Solvency Target that forms the basis of the scheme's funding objective. As a result of this valuation, future contributions into the scheme have been reduced to the minimum level of contributions required under the scheme rules effective from July 2012. Excluding expenses, the contributions fell to approximately £6 million per annum from the £50 million per annum paid previously. The new contributions are only for ongoing service of current employees that are active members of the scheme. No deficit type funding is required. Deficit funding for PSPS, where applicable, as applied in 2011, is apportioned in the ratio of $^{70}/_{30}$ between the PAC with-profits fund and shareholder-backed operations following detailed consideration in 2005 of the sourcing of previous contributions. Employer contributions for ongoing service of current employees are apportioned in the ratio relevant to current activity. In 2012, total contributions paid in the year including expenses were £36 million (2011: £54 million).

The market value of PSPS scheme assets as at the 5 April 2011 valuation was £5,255 million. The actuarial assumptions used in determining benefit obligations and the net periodic benefit costs for the purposes of the 2011 valuation were as follows:

Rate of increase in salaries	Nil
Rate of inflation:	
Retail Prices Index (RPI)	3.7
Consumer Prices Index (CPI)	3.0
Rate of increase of pensions in payment for inflation:	
Guaranteed (maximum 5%)	3.0
Guaranteed (maximum 2.5%)	2.5
Discretionary	Nil
Expected returns on plan assets	4.2

Mortality assumptions:

The tables used for PSPS pensions in payment at 5 April 2011 were:

Base post retirement mortality

For current male (female) pensioners 113% (108%) of the mortality rates of the 2000 series mortality tables (PNMA00/PNFA00), published by the Continuous Mortality Investigation Bureau (CMI).

For male (female) non-pensioners 107% (92%) of the 2000 series rates (PNMA00/PNFA00).

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Allowance for future improvements to post retirement mortality

For males (females) 100% (75%) of Medium Cohort subject to a minimum rate of improvement of 2.00% (1.25%) up to the age of 90, decreasing linearly to zero by age of 120 with a long-term rate of 1.75% pa (1.5% pa) but adjusted as follows:

period improvements are blended between ages 60 to 80 to the long-term improvement rate over a 15 year period (compared with a 20 year period in the core CMI model) and;

cohort improvements are assumed to dissipate over a 30 year period, or by age 90 if earlier (compared with a 40 year period, or by age 100 if earlier, in the core CMI model).

The last completed actuarial valuation of the Scottish Amicable Pension Scheme (SAPS) was as at 31 March 2011 by Jonathan Seed, Fellow of the Institute and Faculty of Actuaries, of Xafinity Consulting. This valuation was finalised in the second half of 2012 and demonstrated the scheme to be 85 per cent funded. Based on this valuation, it was agreed with the Trustees that the existing level of deficit funding of £13.1 million per annum continues to be paid into the scheme over the next six years, to eliminate the actuarial deficit.

The last completed actuarial valuation of the M&G pension scheme was as at 31 December 2011 by Paul Belok, Fellow of the Institute and Faculty of Actuaries, of AON Hewitt Limited. This valuation was finalised in the second half of 2012 and demonstrated the scheme to be 83 per cent funded. Based on this valuation, deficit funding amounts designed to eliminate the actuarial deficit over a three year period are being made from January 2013 of £18.6 million per annum for the first two years and £9.3 million in the third year. This compares to the £10.5 million of deficit funding paid by the Group in 2012.

Summary economic and IAS 19 financial positions

Under the IAS 19 'Employee Benefits' valuation basis, the Group applies IFRIC 14, 'IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. Under IFRIC 14, a surplus is only recognised to the extent that the Company is able to access the surplus either through an unconditional right of refund to the surplus or through reduced future contributions relating to ongoing service, which have been substantively enacted or contractually agreed. Further, the IFRS financial position recorded, reflects the higher of any underlying IAS 19 deficit and any obligation for committed deficit funding where applicable.

For PSPS, the Group does not have an unconditional right of refund to any surplus of the scheme. Accordingly, prior to the finalisation of the 5 April 2011 triennial valuation, the Group had not recognised the underlying surplus of PSPS (31 December 2011: £1,588 million gross of deferred tax) and had recognised an economic liability for deficit funding (31 December 2011: £19 million gross of deferred tax).

The underlying IAS 19 surplus for PSPS at 31 December 2012 was £1,174 million. The finalisation of the 5 April 2011 triennial valuation was accompanied by an agreement with the Trustees that additional deficit type funding would no longer be necessary and furthermore, the level of contributions for ongoing service of current employees was reduced to the minimum level required by the scheme rules. As a consequence, a portion of the surplus, being £164 million, is now recognised as recoverable.

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The £164 million represents the present value of the economic benefits available from the reductions to future ongoing contributions to the scheme. Accordingly, a net surplus of £164 million gross of deferred tax was recognised at 31 December 2012. Of this amount, £115 million was allocated to the PAC with-profits fund and £49 million was allocated to the shareholders' fund.

The IAS 19 deficit of the Scottish Amicable Pension Scheme at 31 December 2012 was £74 million (31 December 2011: deficit of £55 million) and has been allocated approximately 50 per cent to the PAC with-profits fund and 50 per cent to the shareholders' fund.

The IAS 19 surplus of the M&G pension scheme on an economic basis at 31 December 2012 was £38 million (31 December 2011: surplus of £10 million) and is wholly attributable to shareholders. The underlying position on an economic basis reflects the assets (including investments in Prudential insurance policies that are offset against liabilities to policyholders on the Group consolidation) and the liabilities of the schemes. As at 31 December 2012, the M&G pension scheme has invested £169 million in Prudential insurance policies (31 December 2011: £165 million). After excluding these investments that are offset against liabilities to policyholders, the IAS 19 basis position of the M&G pension scheme is a deficit of £131 million (31 December 2011: deficit of £155 million).

2 Corporate governance

The rules of the Group's largest pension arrangement, the defined benefit section of PSPS, a final salary scheme, specify that, in exercising its investment powers, the Trustee's objective is to achieve the best overall investment return consistent with the security of the assets of the scheme. In doing this, consideration is given to the nature and duration of the scheme's liabilities. The Trustee sets the benchmark for the asset mix, following analysis of the liabilities by the Scheme's Actuary and, having taken advice from the Investment Managers, then selects benchmark indices for each asset type in order to measure investment performance against a benchmark return.

The Trustee reviews strategy, the asset mix benchmark and the Investment Managers' objectives every three years, to coincide with the Actuarial Valuation, or earlier if the Scheme Actuary recommends. Interim reviews are conducted annually based on changing economic circumstances and financial market levels.

The Trustee sets the general investment policy and specifies any restrictions on types of investment and the degrees of divergence permitted from the benchmark, but delegates the responsibility for selection and realisation of specific investments to the Investment Managers. In carrying out this responsibility, the Investment Managers are required by the Pensions Act 1995 to have regard to the need for diversification and suitability of investments. Subject to a number of restrictions contained within the relevant asset management agreements, the Investment Managers are authorised to invest in any class of investment asset. However, the Investment Managers will not invest in any new class of investment asset without prior consultation with the Trustee.

The Trustee consults the Principal Employer, the Prudential Assurance Company, on these investment principles, but the ultimate responsibility for the investment of the assets of the scheme lies with the Trustee.

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The investment policies and strategies for the other two UK defined benefit schemes, the M&G Group Pension Scheme and the Scottish Amicable Staff Pension Scheme, which are both final salary schemes, follow similar principles, but have different target allocations reflecting the particular requirements of the schemes.

3 Assumptions

The actuarial assumptions used in determining benefit obligations and the net periodic benefit costs for the years ended 31 December were as follows:

	2012	2011	2010
	%	%	%
Discount rate*	**4.4**	4.7	5.45
Rate of increase in salaries	**2.7**	2.9	5.55
Rate of inflation**			
Retail prices index (RPI)	**2.7**	2.9	3.55
Consumer prices index (CPI)	**2.0**	1.9	n/a
Rate of increase of pensions in payment for inflation:			
Guaranteed (maximum 5%)	**2.5**	2.5	3.55
Guaranteed (maximum 2.5%)	**2.5**	2.5	2.5
Discretionary	**2.5**	2.5	2.5
Expected returns on plan assets	**3.1**	5.1	5.9

* The discount rate has been determined by reference to an 'AA' corporate bond index, adjusted where applicable, to allow for the difference in duration between the index and the pension liabilities.

** The rate of inflation reflects the long-term assumption for the UK RPI or CPI depending on the tranche of the schemes.

The rates of 2.5 per cent are those for PSPS. Assumed rates of increase of pensions in payments for inflation for all other schemes are 2.7 per cent in 2012 (2011: 2.9 per cent; 2010: 3.55 per cent).

The calculations are based on current actuarially calculated mortality estimates with a specific allowance made for future improvements in mortality. The specific allowance for 2012 and 2011 is in line with a custom calibration of the 2009 mortality model from the Continuous Mortality Investigation Bureau of the Institute and Faculty of Actuaries (CMI). The tables used for PSPS immediate annuities in payment at 31 December 2012 and 2011 were:

Male: 108.6 per cent PNMA00 with improvements in line with a custom calibration of the CMI's 2009 mortality model, with a long-term mortality improvement rate of 1.75 per cent per annum; and

Female: 103.4 per cent PNFA00 with improvements in line with a custom calibration of the CMI's 2009 mortality model, with a long-term mortality improvement rate of 1.00 per cent per annum.

The assumed life expectancies on retirement at age 60, based on the mortality table used was:

	2012 years		**2011 years**		**2010 years**	
	Male	**Female**	**Male**	**Female**	**Male**	**Female**
Retiring today	**28.0**	**29.1**	27.8	29.0	27.7	29.0
Retiring in 20 years' time	**30.6**	**31.2**	30.5	31.1	30.3	31.1

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The mean term of the current PSPS liabilities is around 17 years.

Using external actuarial advice provided by the scheme actuaries being Towers Watson for the valuation of PSPS, Xafinity Consulting for SAPS and Aon Hewitt Limited for the M&G scheme, the most recent full valuations have been updated to 31 December 2012, applying the principles prescribed by IAS 19.

4 Group economic and IAS 19 financial position

This section illustrates the financial position of the Group's defined benefit pension schemes on an economic basis and the IAS 19 basis. The underlying position on an economic basis reflects the assets (including investments in Prudential policies that are offset against liabilities to policyholders on the Group consolidation) and the liabilities of the schemes. At 31 December 2012, the investments in Prudential insurance policies comprise £123 million (2011: £112 million) for PSPS and £169 million (2011: £165 million) for the M&G scheme.

Separately, the economic financial position also includes the effect of the application of IFRIC 14, 'IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. For PSPS, where there are constraints in the trust deed to prevent the company access, the surplus is not recognised and a liability to additional funding is established, where relevant (as previously described).

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(i) Estimated pension scheme deficit economic basis

Movements on the pension scheme deficit (determined on the economic basis) are as follows, with the effect of the application of IFRIC 14 being shown separately:

	Surplus (deficit) in scheme at 1 January 2012	2012 (Charge) credit to income statement: Operating results (based on longer-term investment returns)	2012 (Charge) credit to income statement: Actuarial and other gains and losses	Contributions paid	Surplus (deficit) in scheme at 31 Dec 2012
	£m	£m	£m	£m	£m
All schemes					
Underlying position (without the effect of IFRIC 14)					
Surplus	1,543	(166)	(311)	72	1,138
Less: amount attributable to PAC with-profits fund	(1,083)	105	222	(31)	(787)
Shareholders' share:					
Gross of tax surplus	460	(61)	(89)	41	351
Related tax	(117)	25	20	(9)	(81)
Net of shareholders' tax	343	(36)	(69)	32	270
Effect of IFRIC 14					
Derecognition of surplus and set up of additional funding obligation (1 Jan 2012 only)	(1,607)	136	461		(1,010)
Less: amount attributable to PAC with-profits fund	1,124	(93)	(322)		709
Shareholders' share:					
Gross of tax deficit	(483)	43	139		(301)
Related tax	123	(22)	(32)		69
Net of shareholders' tax	(360)	21	107		(232)
With the effect of IFRIC 14					
(Deficit) surplus	(64)	(30)	150	72	128
Less: amount attributable to PAC with-profits fund	41	12	(100)	(31)	(78)
Shareholders' share:					
Gross of tax (deficit) surplus	(23)	(18)	50	41	50

Related tax	**6**	**3**	**(12)**	**(9)**	**(12)**
Net of shareholders' tax	**(17)**	**(15)**	**38**	**32**	**38**

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Underlying investments and liabilities of the schemes

On the 'economic basis', after including the underlying assets represented by the investments in Prudential insurance policies as scheme assets, the plan's net assets at 31 December comprise the following investments and liabilities:

	2012				2011			
	PSPS	Other schemes	Total	%	PSPS	Other schemes	Total	%
	£m	£m	£m		£m	£m	£m	
Equities	**43**	321	364	5	210	273	483	7
Bonds	**5,440**	418	5,858	81	5,547	407	5,954	83
Properties	**290**	40	330	5	297	20	317	4
Other assets[note (i)]	**627**	18	645	9	378	31	409	6
Total value of assets	**6,400**	797	7,197	100	6,432	731	7,163	100

Note

(i) The PSPS scheme has entered into a derivatives based strategy to match the duration and inflation profile of its liabilities. This involved a reallocation from other investments to other assets with an interest and inflation swap overlay. In broad terms, the scheme is committed to making a series of payments related to LIBOR on a nominal amount and in return the scheme receives a series of fixed and inflation-linked payments which match a proportion of its liabilities. As at 31 December 2012, the nominal value of the interest and inflation-linked swaps amounted to £0.9 billion (2011: £0.9 billion) and £2.0 billion (2011: £2.0 billion) respectively.

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(ii) IAS 19 basis financial position as consolidated

The movements in the pension schemes' surplus and deficit between scheme assets and liabilities as consolidated in the financial statements were:

	2012					
	PSPS	Other schemes		Total		Total
	Asset/liability	Plan assets	Present value of benefit obligations	Economic basis net surplus (deficit)	Adjust for investments in Prudential insurance policies	IAS 19 basis net deficit
	£m	£m	£m	£m	£m	£m
Net deficit, beginning of year	(19)	731	(776)	(64)	(165)	(229)
Current service cost			(11)	(11)		(11)
Other finance income		35	(37)	(2)	(8)	(10)
Cash costs and unwind of discount on opening provision for deficit funding for PSPS	(17)			(17)		(17)
Benefit payments		(17)	17			
Contributions	36	36		72		72
Actuarial and other gains and losses	164	12	(26)	150	(5)	145
Transfer out of investment in Prudential insurance policies					9	9
Net surplus (deficit), end of year	164	797	(833)	128	(169)	(41)

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	2011					
	PSPS	Other schemes		Total		Total
	Provision of deficit funding	Plan assets	Present value of benefit obligations	Economic basis net deficit	Adjust for investments in Prudential insurance policies	IAS 19 basis net deficit
	£m	£m	£m	£m	£m	£m
Net deficit, beginning of year	(47)	653	(826)	(220)	(227)	(447)
Current service cost			(13)	(13)		(13)
Negative past service cost (RPI to CPI inflation measure change)			66	66		66
Other finance income		41	(45)	(4)	(15)	(19)
Cash costs and unwind of discount on opening provision for deficit funding for PSPS	(22)			(22)		(22)
Benefit payments		(15)	15		5	5
Contributions	54	40	(1)	93	(21)	72
Actuarial and other gains and losses	(4)	12	28	36	1	37
Transfer out of investment in Prudential insurance policies					92	92
Net deficit, end of year	(19)	731	(776)	(64)	(165)	(229)

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	2010					
	PSPS	Other schemes		Total		Total
	Provision of deficit funding	Plan assets	Present value of benefit obligations	Economic basis net deficit	Adjust for investments in Prudential insurance policies	IAS 19 basis net deficit
	£m	£m	£m	£m	£m	£m
Net deficit, beginning of year	(75)	563	(738)	(250)	(187)	(437)
Current service cost			(13)	(13)		(13)
Other finance income		38	(43)	(5)	(13)	(18)
Cash costs and unwind of discount on opening provision for deficit funding for PSPS	(27)			(27)		(27)
Benefit payments		(15)	15		5	5
Contributions	55	36	(1)	90	(21)	69
Actuarial and other gains and losses		31	(46)	(15)	(11)	(26)
Net deficit, end of year	(47)	653	(826)	(220)	(227)	(447)

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The IAS 19 basis pensions deficit can be summarised as follows:

	2012		2011		2010		2009		2008	
	£m	%	£m	%	£m	%	£m	%	£m	%
Plan assets (IAS 19 basis before effect of IFRIC 14):										
Equities	**202**	**5**	336	5	610	11	917	18	875	17
Bonds	**5,728**	**84**	5,826	85	4,095	72	3,587	69	2,619	52
Properties	**330**	**5**	317	4	206	4	278	5	290	6
Other assets	**645**	**6**	407	6	748	13	442	8	1,273	25
Fair value of plan assets, end of year*	**6,905**	**100**	6,886	100	5,659	100	5,224	100	5,057	100
Present value of benefit obligation	**(6,059)**		(5,620)		(5,438)		(4,951)		(4,493)	
Funded status (wholly or partly funded)	**846**		1,266		221		273		564	
Present value of unfunded obligations (M&G scheme)***					(254)		(223)		(180)	
	846		1,266		(33)		50		384	
Effect of the application of IFRIC 14 for pension schemes										
Derecognition of PSPS' surplus	**(1,010)**		(1,588)		(485)		(513)		(728)	
Set up obligation for deficit funding for PSPS			(19)		(47)		(75)		(65)	
Adjustment in respect of investment of PSPS in Prudential policies	**123**		112		118		101		103	
Deficit recognised in the statement of financial position	**(41)**		(229)		(447)		(437)		(306)	

Experience adjustments:					
Experience adjustments on scheme liabilities**	**4**	314	(4)	76	145
Percentage of scheme liabilities at 31 December	**(0.07%)**	(5.59%)	(0.07%)	1.47%	3.10%
Experience adjustments on scheme assets (IAS 19 basis)	**(39)**	998	287	100	(277)
Percentage of scheme assets at 31 December	**(0.57%)**	14.49%	5.07%	1.91%	(5.48%)

*

The IAS 19 basis plan assets at 31 December 2012 of £6,905 million is different from the economic basis plan assets of £7,197 million as show in section 4(i) above due to the exclusion of investment in Prudential insurance policies of £292 million comprising £123 million for PSPS and £169 million for the M&G scheme.

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The experience adjustments on scheme liabilities in 2011 of £314 million related mainly to the 'true-up' reflecting improvements in data consequent upon the ongoing 2011 triennial valuations of PSPS and the Scottish Amicable pension scheme. The experience adjustments on scheme liabilities in 2008 of a gain of £145 million related mainly to the 'true up' reflecting improvements in data consequent upon the 2008 triennial valuation of PSPS.

***

The M&G pension scheme invests in Prudential insurance policies. On Prudential Group consolidation these assets are eliminated against liabilities in the statement of financial position of UK insurance operations. Up until 2011 all of the M&G scheme assets were invested in this way thus giving rise to an unfunded status on a Prudential Group consolidated basis. At 31 December 2012 and 2011, only £169 million (2011: £165 million) out of the M&G scheme assets of £297 million (2011: £257 million) was invested in Prudential insurance policies, thereby switching its status to a partly funded scheme.

The long-term expected rate of return has been taken to be the weighted average (by market value) of the long-term expected rates of return on each major asset class shown above.

	2012	**2011**
	%	**%**
Long-term expected rate of return		
Equity	**6.8**	8.2
Bonds	**3.0**	4.6
Properties	**5.6**	6.9
Other assets	**2.0**	4.8
Weighted average long-term expected rate of return	**3.1**	5.1

The expected rates of return have been determined by reference to long-term expectations, the carrying value of the assets and equity and other market conditions at the statement of financial position date.

The actual return on scheme assets was a gain of £189 million (gain of 2011: £1,290 million) on an IAS 19 basis.

None of the scheme assets included shares in Prudential plc or property occupied by the Prudential Group.

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(iii) Credit (charge) to the income statement

The components of the credit (charge) for the net periodic pension cost (comprising amounts attributable to the PAC with-profits fund and shareholder-backed operations) are as follows:

	2012	2011	2010
	£m	£m	£m
Pension cost			
Current service cost	**(32)**	(35)	(38)
Past service cost:[note (a)]			
RPI to CPI inflation measure change in 2011		282	
Exceptional discretionary pension increase for PSPS in 2012	**(106)**		
Finance (expense) income:			
Interest cost	**(263)**	(299)	(294)
Expected return on assets IAS 19 basis	**227**	283	304
Add: expected return on investments of scheme assets in Prudential insurance policies	**8**	25	21
Expected return on assets economic basis	**235**	308	325
Total (charge) credit without the effect of IFRC 14	**(166)**	256	(7)
Effect of the application of IFRIC 14	**136**	(229)	(38)
Pension cost economic basis[note (i) above and note (b)]	**(30)**	27	(45)
Adjustment for investments in Prudential insurance policies[note (d)]	**(8)**	(15)	(13)
Pension cost IAS 19 basis (as recognised in the income statement and referred to in note I3a)	**(38)**	12	(58)
Actuarial and other gains and losses			
Actual less expected return on assets	**(34)**	982	306
Losses on changes of assumptions for plan liabilities	**(273)**	(414)	(411)
Experience (losses) gains on liabilities	**(4)**	314	(4)
Total (charge) credit without the effect of IFRC 14	**(311)**	882	(109)
Effect of the application of IFRIC 14	**461**	(846)	94
Actuarial gains and losses economic basis[note (i) above and note (c)]	**150**	36	(15)
Adjustment for investments in Prudential insurance policies[note (d)]	**(5)**	1	(11)
Actuarial gains and losses IAS 19 basis (as recognised in the income statement and referred to in note I3a)	**145**	37	(26)

Net periodic pension cost (included within acquisition and other operating expenditure in the income statement)	**107**	49	(84)

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Notes

(a)

Past service cost

RPI/CPI inflation measure change in 2011

During 2011 the Group altered its inflation measure basis for future statutory increases to pension payments for certain tranches of its UK defined benefit pension schemes. This reflected the UK Government's decision to replace the basis of indexation from RPI with CPI.

The £282 million credit in 2011 shown above comprised £216 million for PSPS and £66 million for other schemes. As noted earlier, the PSPS scheme surplus was not recognised for accounting purposes due to the application of IFRIC 14. The £66 million for other schemes was allocated as £24 million to PAC with-profits fund and £42 million to shareholders as referred to in note C.

Exceptional discretionary pension increase for PSPS in 2012

During the first half of 2012, an exceptional discretionary increase to pensions in payment of PSPS was awarded which resulted in a past service cost of £106 million.

As the PSPS scheme surplus is substantially not recognised for accounting purposes, these two items had negligible impact on the Group's results.

(b)

Consistent with the derecognition of a substantial portion of the Company's interest in the underlying IAS 19 surplus of PSPS, the charge to operating profit based on longer-term investment returns for PSPS reflects the cash cost of contributions for ongoing service of active members (2012: £17 million; 2011: £20 million; 2010: £23 million). In addition, the charge to the operating results also includes a charge for the unwind of discount on the opening provision for deficit funding for PSPS (2012: £nil; 2011: £2 million; 2010: £4 million).

(c)

The net credit (charge) for actuarial and other gains and losses is recorded within the income statement. Within the Group's supplementary analysis of profit, the shareholders' share of actuarial and other gains and losses (ie net of allocation of the share to the PAC with-profits funds) of £50 million as shown in note ii above (2011: £21 million; 2010: £(10) million) is excluded from operating profit based on longer-term investment returns as shown in note B1.

The 2012 actuarial and other gains reflects the positive impact of inflation rate movements in the period, offset by lower discount rates as interest rate falls, and partial recognition of actuarial surplus in PSPS described above.

(d)

The adjustments for investments in Prudential insurance policies are consolidation adjustments with no net impact to the operating results.

Total employer contributions expected to be paid into the Group defined benefit schemes for the year ending 31 December 2012 amounts to £56 million (2011: £94 million).

5 Sensitivity of the pension scheme liabilities to key variables

The total underlying Group pension scheme liabilities of £6,059 million (2011: £5,620 million) comprise £5,226 million (2011: £4,844 million) for PSPS and £833 million (2011: £776 million) for the

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other schemes. The table below shows the sensitivity of the underlying PSPS and the other scheme liabilities at 31 December 2012 and 2011 to changes in discount rates, inflation rates and mortality rates.

	Assumption applied		Sensitivity change in assumption	Impact of sensitivity on scheme liabilities on IAS 19 basis		
	2012	2011			2012	2011
Discount rate	**4.4%**	4.7%	**Decrease by 0.2%**	**Increase in scheme liabilities by:**		
				PSPS	**3.3%**	3.3%
				Other schemes	**4.9%**	4.8%
Discount rate	**4.4%**	4.7%	**Increase by 0.2%**	**Decrease in scheme liabilities by:**		
				PSPS	**3.1%**	3.1%
				Other schemes	**4.6%**	4.5%
Rate of inflation	**RPI: 2.7%**	RPI: 2.9%	**RPI: Decrease by 0.2%**	**Decrease in scheme liabilities by:**		
	CPI: 2.0%	CPI: 1.9%	**CPI: Decrease by 0.2% with consequent reduction in salary increases**	**PSPS**	**0.6%**	0.6%
				Other schemes	**4.3%**	4.1%
Mortality rate			**Increase life expectancy by 1 year**	**Increase in scheme liabilities by:**		
				PSPS	**2.6%**	2.7%
				Other schemes	**2.4%**	2.4%

The sensitivity of the underlying pension scheme liabilities to changes in discount, inflation and mortality rates as shown above does not directly equate to the impact on the profit or loss attributable to shareholders or shareholders' equity due to the effect of the application of IFRIC 14 on PSPS and the allocation of a share of the interest in financial position of the PSPS and Scottish Amicable schemes to the PAC with-profits fund as described above.

The sensitivity to the changes in the key variables as shown in the table above has no significant impact on the pension costs included in the Group's operating results. This is due to the pension costs charged in each of the periods presented being derived largely from market conditions at the beginning of the period. After applying IFRIC 14 and to the extent attributable to shareholders, any residual impact from the changes to these variables is reflected as actuarial gains and losses on defined benefit pension schemes within the supplementary analysis of profits.

6 Transfer value of PSPS scheme

At 31 December 2012, it is estimated that the assets of the scheme are broadly sufficient to cover the liabilities of PSPS on a 'buyout' basis including an allowance for expenses. The 'buyout' basis refers to a basis that might apply in the circumstance of a transfer to another appropriate financial institution. In making this assessment, it has been assumed that a more conservative investment strategy applies together with a more prudent allowance for future mortality improvements and no allowance for discretionary pension increases.

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ii Other pension plans

The Group operates various defined contribution pension schemes including schemes in Jackson an Asia. The cost of the Group's contributions for continuing operations to these schemes in 2012 was £47 million (2011: £40 million).

I4: Share-based payments

(a) Description of the plans

The Group maintains a number of main share award and share option plans relating to Prudential plc shares, which are described below.

(i) Group Performance Share Plan, previously Restricted Share Plan

The Group Performance Share Plan (GPSP) is the incentive plan in which all executive directors and other senior executives within the Group can participate. This scheme was established as a replacement for the Restricted Share Plan (RSP) under which no further awards could be made after March 2006. Awards are granted either in the form of a nil cost option, conditional right over shares, or such other form that shall confer to the participant an equivalent economic benefit, with a vesting period of three years. The performance measure for the awards is that Prudential's Total Shareholder Return (TSR) outperforms an index comprising of peer companies. Vesting of the awards between each performance point is on a straight-line sliding-scale basis. Participants are entitled to the value of reinvested dividends that would have accrued on the shares that vest. Beginning in 2010, newly issued shares have been used in settling the awards that vest and are released.

The RSP was, until March 2006, the Group's long-term incentive plan for executive directors and other senior executives designed to provide rewards linked to shareholder return. Each year participants were granted a conditional option to receive a number of shares. There was a deferment period of three years, at the end of which the award vested to an extent that depended on the performance of the Group's shares including notional reinvested dividends and on the Group's underlying financial performance. After vesting, the option may be exercised at zero cost at any time, subject to closed period rules, in the balance of a 10-year period. Shares are purchased in the open market by a trust for the benefit of qualifying employees.

(ii) Business Unit Performance Plan

The Business Unit Performance Plan (BUPP) is an incentive plan created to provide a common framework under which awards would be made to senior employees in the UK, Jackson and Asia, including the chief executive officers. Awards under this plan were based on growth in shareholder capital value on the European Embedded Value basis with performance measured over three years. All awards made are settled in shares after vesting. Participants are entitled to receive the value of reinvested dividends over the performance period for those shares that vest. The growth parameters for the awards are relevant to each region, and vesting of the awards between each performance point is on a straight-line sliding-scale basis. Beginning in 2010, newly issued shares will be used in settling the awards that vest and are released. The BUPP awards for the UK business unit are based on the same

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relative TSR measure applied to GPSP awards. As a result, awards made under the UK BUPP reflect those TSR conditions applied to GPSP awards.

(iii) Savings-related options

The Group maintains four share option schemes satisfied by the issue of new shares: UK-based executive directors and eligible employees are eligible to participate in the Prudential HM Revenue & Customs (HMRC) approved UK savings-related share option scheme. Asia-based executive directors and eligible employees can participate in the equivalent International savings-related share option scheme. Dublin-based employees are eligible to participate in the Prudential International Assurance sharesave plan and Hong Kong-based agents can participate in the non-employee savings-related share option scheme.

The options are normally exercisable during the six month period following either the third or fifth anniversary of the start of the relevant savings contract. No options may be granted under the schemes if the grant would cause the number of shares which have been issued, or which remain issuable pursuant to options granted in the preceding 10 years under the scheme and other share option schemes operated by the Company, or which have been issued under any other share incentive scheme of the Company, to exceed 10 per cent of the Company's ordinary share capital at the proposed date of grant.

(iv) Share Incentive Plan

UK-based executive directors and employees are also eligible to participate in the Company's HMRC-approved Share Incentive Plan (SIP), which allows all UK-based employees to purchase shares of Prudential plc (partnership shares) on a monthly basis out of gross salary. For every four partnership shares bought, an additional matching share is awarded, purchased on the open market. Dividend shares accumulate while the employee participates in the plan. Partnership shares may be withdrawn from the scheme at any time. If the employee withdraws from the plan within five years, the matching shares are forfeit, and if within three years, dividend shares are forfeit.

(v) Performance-related share awards

Jackson operates a performance-related share award which, subject to the prior approval of the Jackson Remuneration Committee, may grant share awards to eligible Jackson employees in the form of a contingent right to receive shares or a conditional allocation of shares. These share awards have vesting periods of four years and are at nil cost to the employee. Award holders do not have any right to dividends or voting rights attaching to the shares. The shares are held in the employee share trust in the form of American Depository Receipts which are tradable on the New York Stock Exchange.

(vi) Long-term Incentive Plan

The Prudential Corporation Asia Long-Term Incentive Plan (PCA LTIP) is an incentive plan created in 2008 for senior employees and chief executive officers. Awards under this plan will vest after three years subject to the employee being in employment at the time of vesting without any performance conditions. Awards are discretionary and on a year-by-year basis determined by Prudential's full year

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financial results and the employee's contribution to the business. All awards will be in Prudential shares except for countries where share awards are not feasible due to securities and/or tax reasons, where awards will be replaced by the cash value of the shares that would otherwise have been transferred.

(vii) Annual Incentive Plan

Certain senior executives have Annual Incentive Plans (AIP) with awards paid in cash up to the target level of their plan. The portion of any award for above-target performance is made in the form of awards of shares deferred for three years, with the release of shares subject to close periods. The shares are held in the employee share trust and shares equivalent to dividends otherwise payable will accumulate for the benefit of award holders during the deferral period up to the release date.

(viii) Other Share awards

In addition, there are other share awards, including the Prudential Corporation Asia Deferred Bonus Plan (PCA DBP), Prudential Capital Deferred Bonus Plan (PruCap DBP) and other arrangements. There are no performance conditions attaching to these deferred bonus plans, and awards vest in full subject to the individual being employed by Prudential at the end of the vesting period. The other arrangements relate to various awards that have been made without performance conditions to individual employees, typically in order to secure their appointment or ensure retention.

(b) Outstanding options and awards

The following table shows movement in options outstanding under the Group's share-based compensation plans at 31 December 2012 and 2011:

	2012		2011		2010	
Options outstanding under SAYE schemes	**Number of options**	**Weighted average exercise price**	**Number of options**	**Weighted average exercise price**	**Number of options**	**Weighted average exercise price**
	millions	**£**	**millions**	**£**	**millions**	**£**
Beginning of year:	**13.3**	**3.55**	12.8	3.4	12.2	3.2
Granted	**2.4**	**6.29**	2.1	4.66	2.2	4.61
Exercised	**(5.7)**	**2.99**	(0.6)	3.98	(0.6)	3.15
Forfeited	**(0.2)**	**4.29**	(0.2)	3.17	(0.2)	3.44
Cancelled	**(0.2)**	**4.32**	(0.4)	3.56	(0.5)	3.37
Lapsed	**(0.2)**	**4.39**	(0.4)	3.94	(0.3)	3.89
End of year	**9.4**	**4.54**	13.3	3.55	12.8	3.4
Options immediately exercisable, end of year	**0.2**	**3.88**	0.4	4.54	0.2	5.52

The weighted average share price of Prudential plc for the year ended 31 December 2012 was £7.69 compared to £6.86 for the year ended 31 December 2011 and £5.68 for the year ended 31 December 2010.

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Movements in share awards outstanding under the Group's share-based compensation plans relating to Prudential plc shares at 31 December 2012, 2011 and 2010 were as follows:

Awards outstanding under incentive plans including conditional options	2012 Number of awards	2011 Number of awards	2010 Number of awards
	millions	millions	millions
Beginning of year:	**26.7**	23.9	19.2
Granted	**8.8**	10.3	11.2
Exercised	**(9.4)**	(4.2)	(4.7)
Forfeited	**(1.4)**	(0.1)	(1.2)
Expired	**(1.0)**	(3.2)	(0.6)
End of year	**23.7**	26.7	23.9

The following table provides a summary of the range of exercise prices for Prudential plc options outstanding at 31 December 2012.

	Outstanding			Exercisable	
Range of exercise prices	Number Outstanding	Weighted average remaining contractual life	Weighted average exercise prices	Number exercisable	Weighted average exercise prices
	millions	years	£	years	£
Between £2 and £3	**2.8**	**2.0**	**2.88**	**0.1**	**2.88**
Between £4 and £5	**4.1**	**2.3**	**4.61**	**0.1**	**4.24**
Between £5 and £6	**0.1**	**0.6**	**5.60**		**5.67**
Between £6 and £7	**2.4**	**3.6**	**6.29**		
	9.4	**2.6**	**4.54**	**0.2**	**3.88**

The following table provides a summary of the range of exercise prices for Prudential plc options outstanding at 31 December 2011.

	Outstanding			Exercisable	
Range of exercise prices	Number Outstanding	Weighted average remaining contractual life	Weighted average exercise prices	Number exercisable	Weighted average exercise prices
	millions	years	£	years	£
Between £2 and £3	8.2	1.6	2.88		

Between £3 and £4		0.8	3.73		3.43
Between £4 and £5	5.0	3.1	4.58	0.3	4.40
Between £5 and £6	0.1	0.9	5.58	0.1	5.53
	13.3	2.2	3.55	0.4	4.54

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The following table provides a summary of the range of exercise prices for Prudential plc options outstanding at 31 December 2010.

	Outstanding			Exercisable	
Range of exercise prices	Number Outstanding	Weighted average remaining contractual life	Weighted average exercise prices	Number exercisable	Weighted average exercise prices
	millions	years	£	millions	£
Between £2 and £3	9.0	2.6	2.88		
Between £3 and £4	0.1	1.3	3.59		3.67
Between £4 and £5	3.3	3.3	4.51		4.07
Between £5 and £6	0.4	1.0	5.59	0.2	5.63
	12.8	2.8	3.4	0.2	5.52

The years shown above for weighted average remaining contractual life include the time period from end of vesting period to expiration of contract.

c Fair value of options and awards

The weighted average fair values of Prudential plc options and awards granted during the period are as follows:

2012 Weighted average fair value			2011 Weighted average fair value			2010 Weighted average fair value		
GPSP	SAYE Options	Awards	GPSP	SAYE Options	Awards	GPSP	SAYE Options	Awards
£	£	£	£	£	£	£	£	£
3.91	**2.28**	**6.72**	3.88	2.63	6.28	2.74	2.91	5.14

The fair value amounts estimated on the date of grant relating to all options including conditional nil cost options above were determined using the Black-Scholes and the Monte Carlo option-pricing models using the following assumptions:

	2012		2011		2010	
	GPSP	SAYE Options	GPSP	SAYE Options	GPSP	SAYE Options
Dividend yield (%)		**3.63**		3.33		3.43
Expected volatility (%)	**33.03**	**34.33**	28.90	62.67	42.69	64.65
Risk-free interest rate (%)	**0.31**	**0.39**	1.32	0.89	1.7	1.07

Expected option life (years)		**3.24**		3.48		3.49
Weighted average exercise price (£)		**6.29**		4.66		4.61
Weighted average share price (£)	**6.78**	**8.26**	7.32	6.06	5.7	6.38

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Compensation costs for all share-based compensation plans are determined using the Black-Scholes model, Monte Carlo model or other market consistent valuation methods. The compensation costs for all awards and options are recognised in net income over the plans' respective vesting periods. The Group uses the Black-Scholes model to value all options and awards other than the GPSP and UK BUPP, for which the Group uses a Monte Carlo model in order to allow for the impact of the TSR performance conditions. These models are used to calculate fair values for share options and awards at the grant date based on the quoted market price of the stock at the measurement date, the amount, if any, that the employees are required to pay, the dividend yield, expected volatility, risk-free interest rates and exercise prices.

For the SAYE options, the expected volatility is based on the market implied volatilities for Prudential shares as quoted on Bloomberg. This change (from an estimate based on historic volatility) brings the methodology into line with the approach used to determine the volatility for the GPSP and UK BUPP awards. The Prudential specific at-the-money implied volatilities are adjusted to allow for the different term and discounted exercise price on SAYE options by using information on the volatility surface of the FTSE 100.

Risk-free interest rates are UK gilt rates with projections for three-year and five-year terms to match corresponding vesting periods. Dividend yield is determined as the average yield over a period of 12 months up to and including the date of grant. For the GPSP, volatility and correlation between Prudential and an index constructed from a simple average of the TSR growth of 10 companies is required. For grants in 2012, an average index volatility and correlation of 32 per cent and 76 per cent respectively, were used. For the GPSP, market implied volatilities are used for both Prudential and the components of the index. Changes to the subjective input assumptions could materially affect the fair value estimate.

(d) Share-based payment expense charged to the income statement

Total expense recognised in the year in the consolidated financial statements related to share-based compensation is as follows:

	2012	2011	2010
	£m	£m	£m
Share-based compensation expense	**58**	48	47
Amount accounted for as equity-settled	**42**	44	37
Carrying value at 31 December of liabilities arising from share-based payment transactions	**24**	15	17
Intrinsic value of above liabilities for which rights had vested at 31 December	**16**	6	6

I5: Key management remuneration

Key management constitutes the directors of Prudential plc as they have authority and responsibility for planning, directing and controlling the activities of the Group.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

I: Other notes (Continued)

Total key management remuneration can be broken down in the following table:

	2012	2011	2010
	£	£	£
Salaries and short-term benefits	**13,793,000**	12,192,000	9,594,000
Post-employment benefits	**1,206,000**	1,189,000	926,000
Share-based payments	**11,787,000**	9,734,000	11,157,000
	26,786,000	23,115,000	21,677,000

Post-employment benefits comprise the change in the transfer value of the accrued benefit relating to directors' defined benefit pension schemes in the year and the total contributions made to directors' other pension arrangements.

The share-based payments charge is the sum of £7,992,000 (2011: £6,571,000; 2010: £7,320,000), which is determined in accordance with IFRS 2, 'Share-Based Payments' (see note I4) and £3,795,000 (2011: £3,163,000; 2010: £3,837,000) of deferred share awards.

Total key management remuneration includes total directors' emoluments of £18,505,000 (2011: £16,212,000; 2010: £14,225,000) as shown in Item 6 'Directors, Senior Management and Employees and additional amounts in respect of pensions and share-based payments. Further information on directors' remuneration is given in Item 6 'Directors, Senior Management and Employees.

I6: Fees payable to auditor

	2012	2011	2010
	£m	£m	£m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	**2.0**	2.1	1.9
Fees payable to the Company's auditor and its associates for other services:			
Audit of subsidiaries pursuant to legislation	**6.5**	6.1	6.1
Audit-related assurance services	**3.2**	2.6	2.5
Tax compliance services	**0.5**	0.6	0.4
Other assurance services	**0.5**	0.5	0.6
Other assurance services excluding the AIA transaction	**0.5**	0.5	0.6
Services relating to corporate finance transactions	**0.4**	0.5	0.1
All other services	**1.2**	0.3	0.4
Total	**14.3**	12.7	17.5

In addition, there were fees incurred of £0.1 million (2011: £0.1 million; 2010: £0.1 million) for the audit of pension schemes.

The above audit fees for 2012 and 2011, reflect the new disclosure requirements of SI2011/2198 The Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) (Amendment) Regulations 2011.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

I: Other notes (Continued)

The Audit Committee regularly monitors the non-audit services provided to the Group by its auditor and has developed a formal Auditor Independence Policy which sets out the types of services that the auditor may provide, consistent with the guidance in Sir Robert Smith's report 'Audit Committees Combined Code Guidance' and with the provisions of the US Sarbanes-Oxley Act.

The Audit Committee annually reviews the auditor's objectivity and independence.

I7: Related party transactions

Transactions between the Company and its subsidiaries are eliminated on consolidation.

In addition, the Company has transactions and outstanding balances with certain unit trusts, Open-Ended Investment Companies (OEICs), collateralised debt obligations and similar entities which are not consolidated and where a Group company acts as manager. These entities are regarded as related parties for the purposes of IAS 24. The balances are included in the Group's statement of financial position sheet at fair value or amortised cost in accordance with their IAS 39 classifications. The transactions are included in the income statement and include amounts paid on issue of shares or units, amounts received on cancellation of shares or units and paid in respect of the periodic charge and administration fee. Further details of the aggregate assets, liabilities, revenues, profits or losses and reporting dates of entities considered to be associates under IFRS are disclosed in note H8.

Executive officers and directors of the Company may from time to time purchase insurance, asset management or annuity products marketed by Group companies in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with other persons.

In 2012 and 2011, other transactions with directors were not deemed to be significant both by virtue of their size and in the context of the directors' financial positions. As indicated above, all of these transactions are on terms broadly equivalent to those that prevail in arm's length transactions.

Apart from these transactions with directors, no director had interests in shares, transactions or arrangements that require disclosure, other than those given in Item 6 'Directors, Senior management and Employees'. Key management remuneration is disclosed in note I5.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

I: Other notes (Continued)

I8: Subsidiary undertakings

(i) Principal subsidiaries

The principal subsidiary undertakings of the Company at 31 December 2012, all wholly owned were:

	Main activity	Country of incorporation
The Prudential Assurance Company Limited	Insurance	England and Wales
Prudential Annuities Limited*	Insurance	England and Wales
Prudential Retirement Income Limited (PRIL)*	Insurance	Scotland
M&G Investment Management Limited*	Asset management	England and Wales
Jackson National Life Insurance Company*	Insurance	US
Prudential Assurance Company Singapore (Pte) Limited*	Insurance	Singapore

* Owned by a subsidiary undertaking of the Company.

Each subsidiary has one class of ordinary shares and operates mainly in its country of incorporation, except for PRIL which operates mainly in England and Wales.

Details of all Prudential subsidiaries, joint ventures and associates will be annexed to the next Annual Returns of Prudential plc filed with the UK Registrar of Companies.

(ii) Dividend restrictions and minimum capital requirements

Certain Group subsidiaries are subject to restrictions on the amount of funds they may transfer in the form of cash dividends or otherwise to the parent company. UK insurance companies are required to maintain solvency margins which must be supported by capital reserves and other resources, including unrealised gains on investments. Jackson can pay dividends on its capital stock only out of earned surplus unless prior regulatory approval is obtained. Furthermore, without the prior regulatory approval, dividends cannot be distributed if all dividends made within the preceding 12 months exceed the greater of Jackson's statutory net gain from operations or 10 per cent of Jackson's statutory surplus for the prior year. In 2013, the maximum amount of dividends that could be paid by the US insurance sub-group, subject to the availability of earned surplus, without prior regulatory approval is US$352 million (£216 million) (in 2012: US$411 million (£264 million)). The Group's subsidiaries in Asia may remit dividends to the Group, in general, provided the statutory insurance fund meets the capital adequacy standard required under local statutory regulations and has sufficient distributable reserves.

The Group capital position statement for life assurance businesses is set out in note D5, showing the available capital reflecting the excess of regulatory basis over liabilities for each fund or group of companies determined by reference to the local regulation of the subsidiaries. In addition, disclosure is also provided in note D5 of the local capital requirement of each of the fund or group of companies.

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Prudential plc and Subsidiaries

Notes to the Consolidated Financial Statements

31 December 2012

I: Other notes (Continued)

I9: Commitments

(i) Operating leases

The Group leases various offices to conduct its business. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

	2012	2011	2010
	£m	£m	£m
Future minimum lease payments for non-cancellable operating leases fall due during the following periods:			
Not later than 1 year	**74**	66	70
Later than 1 year and not later than 5 years	**199**	173	236
Later than 5 years	**116**	72	120

The total minimum future sublease rentals to be received on non-cancellable operating leases for land and buildings for the year ended 31 December 2012 were £18 million (2011: £18 million; 2010: £nil).

Minimum lease rental payments for the year ended 31 December 2012 of £73 million (2011: £74 million; 2010: £92 million) are included in the consolidated income statement.

(ii) Capital commitments

The Group has provided, from time to time, certain guarantees and commitments to third-parties including funding the purchase or development of land and buildings and other related matters. The contractual obligations to purchase or develop investment properties at 31 December 2012 were £5 million (2011: £9 million; 2010: £28 million).

I10: Cash flows

Structural borrowings of shareholder-financed operations comprise of core debt of the parent company, the PruCap bank loan and Jackson surplus notes. Core debt excludes borrowings to support short-term fixed income securities programmes, non-recourse borrowings of investment subsidiaries of shareholder-financed operations and other borrowings of shareholder-financed operations. Cash flows in respect of these borrowings are included within cash flows from operating activities.

Structural borrowings of with-profits operations relate solely to the £100 million 8.5 per cent undated subordinated guaranteed bonds which contribute to the solvency base of the Scottish Amicable Insurance Fund (SAIF), a ring-fenced sub-fund of the PAC with-profits fund. Cash flows in respect of other borrowings of with-profits funds, which principally relate to consolidated investment funds, are included within cash flows from operating activities.

I11: Post balance sheet events

In January 2013, the Company issued US$700 million 5.25 per cent Tier 1 perpetual subordinated capital securities. The proceeds, net of costs, were US$689 million. The Company also repaid on maturity, the £250 million Medium Term Notes 2013, included within operational borrowings in note H13 in January 2013.

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Profits and Loss Accounts (UK GAAP Basis)

Years ended 31 December	2012	2011	2010
	£m	£m	£m
Investment income, including dividends from subsidiary undertakings	**641**	4,457	1,746
Investment expenses and charges	**(383)**	(508)	(696)
Other charges:			
Corporate expenditure	**(247)**	(216)	(161)
Costs of terminated AIA transaction			(262)
Provision against loans			(10)
Foreign currency exchange losses		(1)	(90)
Profit on ordinary activities before tax	**11**	3,732	527
Tax (charge) credit on profit on ordinary activities	**(227)**	(12)	354
(Loss) profit for the financial year	**(216)**	3,720	881

The accompanying notes are an integral part of this condensed financial information

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Balance Sheets (UK GAAP Basis)

	2012	2011
	£m	£m
Fixed assets		
Investments:		
Shares in subsidiary undertakings	**11,929**	10,902
Loans to subsidiary undertakings	**1,164**	1,200
	13,093	12,102
Current assets		
Debtors:		
Amounts owed by subsidiary undertakings	**3,208**	6,122
Deferred tax	**47**	364
Other debtors	**3**	11
Derivative assets	**3**	3
Cash at bank and in hand	**193**	152
	3,454	6,652
Less liabilities: amounts falling due within one year		
Commercial paper	**(1,535)**	(2,706)
Other borrowings	**(450)**	(200)
Derivative liabilities	**(190)**	(207)
Amounts owed to subsidiary undertakings	**(1,705)**	(1,049)
Tax payable	**(103)**	(198)
Sundry creditors	**(19)**	(19)
Accruals and deferred income	**(46)**	(46)
	(4,048)	(4,425)
Net current (liabilities) assets	**(594)**	2,227
Total assets less current liabilities	**12,499**	14,329
Less liabilities: amounts falling due after more than one year		
Subordinated liabilities	**(2,577)**	(2,652)
Debenture loans	**(549)**	(549)
Other borrowings	**(299)**	(250)
Amounts owed to subsidiary undertakings	**(2,576)**	(3,560)
	(6,001)	(7,011)
Total net assets (excluding pension)	**6,498**	7,318
Pension asset (net of related deferred tax)	**38**	39
Total net assets (including pension)	**6,536**	7,357

Capital and reserves		
Share capital	**128**	127
Share premium	**1,889**	1,873
Profit and loss account	**4,519**	5,357
Shareholders' funds	**6,536**	7,357

The accompanying notes are an integral part of this condensed financial information

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Statements of Total Recognised Gains and Losses (UK GAAP Basis)

Years ended 31 December	2012	2011	2010
	£m	£m	£m
(Loss) profit for the financial year	**(216)**	3,720	881
Actuarial gains (losses) recognised in respect of the pension scheme (net of related deferred tax)	**27**	(12)	(10)
Reserve movements in respect of share based payments	**6**	7	6
Total recognised (losses) gains relating to the financial year	**(183)**	3,715	877

The accompanying notes are an integral part of this condensed financial information

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Reconciliation of Movements in Shareholders' Capital And Reserves (UK GAAP Basis)

	Number of Ordinary Shares	Ordinary Share Capital	Share Premium	Retained Profit and Loss Reserve	Total
	m	£m	£m	£m	£m
1 January 2010	2,532	127	1,843	1,856	3,826
Total recognised gains relating to 2010				877	877
Dividends				(511)	(511)
New share capital subscribed	14		75		75
Reserve movements in respect of shares issued in lieu of cash dividends			(62)	62	
1 January 2011	2,546	127	1,856	2,284	4,267
Total recognised gains relating to 2011				3,715	3,715
Dividends				(642)	(642)
New share capital subscribed	2		17		17
1 January 2012	**2,548**	**127**	**1,873**	**5,357**	**7,357**
Total recognised losses relating to 2012				**(183)**	**(183)**
Dividends				**(655)**	**(655)**
New share capital subscribed	**9**	**1**	**16**		**17**
31 December 2012	**2,557**	**128**	**1,889**	**4,519**	**6,536**

The accompanying notes are an integral part of this condensed financial information

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Statements of Cash Flows (UK GAAP Basis)

Years ended 31 December	2012	2011	2010
	£m	£m	£m
Operations			
Net cash inflow from operating activities before interest and tax	**475**	4,156	1,347
Interest paid	**(421)**	(427)	(443)
Taxes paid	**(14)**		(3)
Acquisitions and disposals			
Sale of (investment in) shares in subsidiary undertakings	**2**	(1,600)	421
Equity dividends paid	**(655)**	(642)	(449)
Net cash (outflow) inflow before financing	**(613)**	1,487	873
Financing			
Issue of ordinary share capital	**17**	17	13
Issue of borrowings, net of repayment	**299**	7	
Movement in commercial paper and other borrowings to support a short-term fixed income securities program	**(1,171)**	395	522
Movement in net amount owed by subsidiary undertakings	**1,509**	(1,916)	(1,606)
Net cash inflow (outflow) from financing	**654**	(1,497)	(1,071)
Net cash inflow (outflow) for the year	**41**	(10)	(198)
Reconciliation of profit on ordinary activities before tax to net cash inflow from operating activities			
Profit on ordinary activities before tax	**11**	3,732	527
Add back: interest charged	**435**	433	433
Adjustments for non-cash items:			
Fair value adjustments on derivatives	**(17)**	75	29
Pension scheme	**37**	(12)	(17)
Foreign currency exchange movements	**1**	(61)	104
Provisions against investments and loans			10
Loss on intragroup transfer of subsidiary			244
Decrease (increase) in debtors	**8**	(5)	1
(Increase) decrease in creditors		(6)	16
Net cash inflow from operating activities	**475**	4,156	1,347

The accompanying notes are an integral part of this condensed financial information

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Notes to the Condensed Financial Statement Schedule

31 December 2012

1 Basis of preparation and significant accounting policies

The financial statements of the parent company are prepared in accordance with applicable accounting standards under UK Generally Accepted Accounting Practice (UK GAAP), including Financial Reporting Standards (FRS) and Statements of Standard Accounting Practice (SSAP). This is in line with the parent company's UK statutory basis of reporting.

Significant accounting policies

Shares in subsidiary undertakings

Shares in subsidiary undertakings are shown at the lower of cost and estimated realisable value.

Loans to subsidiary undertakings

Loans to subsidiary undertakings are shown at cost, less provisions.

Derivatives

Derivative financial instruments are held to manage interest rate and currency profiles. Derivative financial instruments are carried at fair value with changes in fair value included in the profit and loss account.

Under FRS 26 'Financial Instruments: Recognition and Measurement', hedge accounting is permissible only if certain criteria are met regarding the establishment of documentation and continued measurement of hedge effectiveness. For derivative financial instruments designated as fair value hedges, the movements in the fair value are recorded in the profit and loss account with the accompanying change in fair value of the hedged item attributable to the hedged risk.

Borrowings

Borrowings are initially recognised at fair value, net of transaction costs, and subsequently accounted for on an amortised cost basis using the effective interest method. Under the effective interest method, the difference between the redemption value of the borrowing and the initial proceeds, net of transaction costs, is amortised through the profit and loss account to the date of maturity, or, for hybrid debt, over the expected life of the instrument.

Dividends

Interim dividends are recorded in the period in which they are paid. Final dividends are recorded in the period in which they are approved by shareholders.

Share premium

The difference between the proceeds received on issue of shares and the nominal value of the shares issued is credited to the share premium account.

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Notes to the Condensed Financial Statement Schedule (Continued)

31 December 2012

1 Basis of preparation and significant accounting policies (Continued)

Foreign currency translation

Foreign currency borrowings that have been used to finance or provide a hedge against Group equity investments in overseas subsidiaries are translated at year-end exchange rates. The impact of these currency translations is recorded within the profit and loss account for the year.

Other assets and liabilities denominated in foreign currencies are also converted at year end exchange rates with the related foreign currency exchange gains or losses reflected in the profit and loss account for the year.

Tax

Current tax expense is charged or credited to operations based upon amounts estimated to be payable or recoverable as a result of taxable operations for the current year. To the extent that losses of an individual UK company are not offset in any one year, they can be carried back for one year or carried forward indefinitely to be offset against profits arising from the same company.

Deferred tax assets and liabilities are recognised in accordance with the provisions of FRS 19, 'Deferred tax'. The parent Company has chosen not to apply the option available of recognising such assets and liabilities on a discounted basis to reflect the time value of money. Except as set out in FRS 19, deferred tax is recognised in respect of all timing differences that have originated but not reversed by the balance sheet date. Deferred tax assets are recognised to the extent that it is regarded as more likely than not that they will be recovered.

The Group's UK subsidiaries each file separate tax returns. In accordance with UK tax legislation, where one domestic UK company is a 75 per cent owned subsidiary of another UK company or both are 75 per cent owned subsidiaries of a common parent, the companies are considered to be within the same UK tax group. For companies within the same tax group, trading profits and losses arising in the same accounting period may be offset for the purposes of determining current and deferred taxes.

Pensions

The Company assumes a portion of the pension surplus or deficit of the Group's main pension scheme, the Prudential Staff Pension Scheme ('PSPS') and applied the requirements of FRS 17 'Retirement Benefits' (as amended in December 2006) to its interest in the PSPS surplus or deficit.

A pension surplus or deficit is recorded as the difference between the present value of the scheme liabilities and the fair value of the scheme assets. The Company's share of pension surplus is recognised to the extent that the Company is able to recover a surplus either through reduced contributions in the future or through refunds from the scheme.

The assets and liabilities of the defined benefit pension schemes of the Prudential Group are subject to a full triennial actuarial valuation using the projected unit method. Estimated future cash flows are then discounted at a high quality corporate bond rate, adjusted to allow for the difference in duration between the bond index and the pension liabilities where appropriate, to determine its present value. These calculations are performed by independent actuaries.

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Notes to the Condensed Financial Statement Schedule (Continued)

31 December 2012

1 Basis of preparation and significant accounting policies (Continued)

The aggregate of the actuarially determined service costs of the currently employed personnel and the unwind of the discount on liabilities at the start of the period, gains and losses on settlements and curtailments, less the expected investment return on the scheme assets at the start of the period, is recognised in the profit and loss account. To the extent that part or all of the Company's interest in the pension surplus is not recognised as an asset, the unrecognised surplus is initially applied to extinguish any past service costs, losses on settlements or curtailments that would otherwise be included in the profit and loss account. Next, the expected investment return on the scheme's assets is restricted so that it does not exceed the total of the current service cost, interest cost and any increase in the recoverable surplus. Any further adjustment for the unrecognised surplus is treated as an actuarial gain or loss.

Actuarial gains and losses as a result of the changes in assumptions, the difference between actual and expected investment return on scheme assets and experience variances are recorded in the statement of total recognised gains and losses. Actuarial gains and losses also include adjustment for unrecognised pension surplus as described above.

Share-based payments

The Group offers share award and option plans for certain key employees and a SAYE plan for all UK and certain overseas employees. The share-based payment plans operated by the Group are mainly equity-settled plans with a few cash-settled plans.

Under FRS 20 'Share-based payment', where the Company, as the parent company, has the obligation to settle the options or awards of its equity instruments to employees of its subsidiary undertakings, and such share-based payments are accounted for as equity-settled in the Group financial statements, the Company records an increase in the investment in subsidiary undertakings for the value of the share options and awards granted with a corresponding credit entry recognised directly in equity. The value of the share options and awards granted is based upon the fair value of the options and awards at the grant date, the vesting period and the vesting conditions.

2 Dividends declared in the reporting period from subsidiary undertakings

	2012	**2011**	**2010**
	£m	**£m**	**£m**
The Prudential Assurance Company Limited	**246**	224	800
Prudential Holdings Limited		3,479	115
M&G Group Limited	**196**	213	150
Prudential Five Limited			251
Prudential Capital Holding Company Limited	**58**	67	2
Prudential Group Holdings Limited	**1**		
Prudential Four Limited		19	
Total dividends	**501**	4,002	1,318

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Notes to the Condensed Financial Statement Schedule (Continued)

31 December 2012

2 Dividends declared in the reporting period from subsidiary undertakings (Continued)

Included within the 2011 dividends of £4,002 million was £2,734 million relating to gains made by an intermediate holding company following the transfer at fair value of certain of its subsidiaries to other parts of the Group as part of an internal restructuring exercise in 2011.

3 Reconciliation from UK GAAP to IFRS

The parent company financial statements are prepared in accordance with UK GAAP and the consolidated financial statements are prepared in accordance with IFRS as issued by the IASB and endorsed by the EU. The tables below provide a reconciliation between UK GAAP and IFRS.

	2012	2011	2010
	£m	£m	£m
Profit after tax			
(Loss) profit for the financial year of the Company in accordance with UK GAAP	**(216)**	3,720	881
IFRS adjustment *	**71**	(5)	(8)
(Loss) profit for the financial year of the Company (including dividends from subsidiaries) in accordance with IFRS	**(145)**	3,715	873
Share in the IFRS result of the Group, net of distributions to the Company **	**2,342**	(2,300)	558
Profit after tax of the Group attributable to shareholders in accordance with IFRS	**2,197**	1,415	1,431

	2012	2011
	£m	£m
Net equity		
Shareholders' equity of the Company in accordance with UK GAAP	**6,536**	7,357
IFRS adjustment *		(44)
Shareholders' equity of the Company in accordance with IFRS	**6,536**	7,313
Share in the IFRS net equity of the Group **	**3,823**	1,251
Shareholders' equity of the Group in accordance with IFRS	**10,359**	8,564

*

'IFRS adjustment' in the above tables represent the difference in the accounting treatment for pension schemes between UK GAAP and IFRS.

**

The 'shares in the IFRS result and net equity of the Group' lines represent the parent company's equity in the earnings and net assets of its subsidiaries and associates.

The (loss) profit for the financial year of the parent company in accordance with UK GAAP and IFRS includes dividends declared in the year from subsidiary undertakings of £501 million, £4,002 million and £1,318 million for the years ended 31 December 2012 and 2011 and 2010, respectively (see note 2).

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Schedule II

Condensed Financial Information of Registrant Prudential plc

Notes to the Condensed Financial Statement Schedule (Continued)

31 December 2012

3 Reconciliation from UK GAAP to IFRS (Continued)

As stated in note 1, under UK GAAP, the parent company accounts for its investments in subsidiary undertakings at the lower of cost and estimated realisable value. For the purpose of this reconciliation, no adjustment is made to the parent company in respect of any valuation adjustments to shares in subsidiary undertakings which would be eliminated on consolidation.

4 Guarantees provided by the parent company

In certain instances the parent company has guaranteed that its subsidiaries will meet their obligations when they fall due for payment.

5 Post balance sheet events

In January 2013, the Company issued US$ 700 million 5.25 per cent Tier 1 perpetual subordinated capital securities. The proceeds, net of costs, were US$ 689 million. Also in January 2013, the Company repaid £250 million Medium-Term Notes 2013 on maturity.

Subject to shareholders' approval, in May 2013 the Company will pay a final dividend for the year ended 31 December 2012. Further details are provided in note B3 "Dividends" of the Prudential's consolidated financial statements.

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SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorised the undersigned to sign this annual report on its behalf.

PRUDENTIAL PLC

By: /s/ TIDJANE THIAM

16 April 2013

Name: Tidjane Thiam
Title: Group Chief Executive

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Item 19. Exhibits

Documents filed as exhibits to this Form 20-F:

Exhibit Number	Description
1.	Memorandum[7] and Articles of Association of Prudential.[8]
2.1	Form of Deposit Agreement among Prudential, Morgan Guaranty Trust Company of New York, as depositary, and holders and beneficial owners from time to time of ADRs issued there under, including the form of ADR.[1]
2.2	The total amount of long-term debt securities of Prudential plc authorised under any instrument does not exceed 10 per cent of the total assets of the Company on a consolidated basis. Prudential plc hereby agrees to furnish to the Securities and Exchange Commission, upon its request, a copy of any instrument defining the rights of holders of long-term debt of Prudential plc or of its subsidiaries for which consolidated or unconsolidated financial statements are required to be filed.
4.1	Group Performance Share Plan, Business Unit Performance Plan and M&G Executive Long-Term Incentive Plan[6]
4.2	Executive Directors' Service Contracts: Robert Devey[8] John Foley[9] Michael McLintock[2] Nic Nicandrou[8] Barry Stowe[5] Tidjane Thiam[6][7] Michael Wells[9]
4.3	Other benefits between the Prudential Group and Executive Directors: Robert Devey[8] John Foley[9] Michael McLintock[6] Nic Nicandrou[8] Barry Stowe[6] Tidjane Thiam[6] Michael Wells[9]
4.4	Chairman's Letter of Appointment
4.5	Other benefits between Prudential and the Chairman
4.6	Non-executive Directors' Letters of Appointment: Keki Dadiseth[3] Sir Howard Davies[9] Michael Garrett[3] Ann Godbehere[6] Alexander Johnston[10] Kaikhushru Nargolwala[10] Philip Remnant Lord Turnbull[4]

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Exhibit Number	Description
4.7	Other benefits between Prudential and the non-executive Directors: Keki Dadiseth[6] Sir Howard Davies[9] Michael Garrett[6] Ann Godbehere[6] Alexander Johnston[10] Kaikhushru Nargolwala[10] Philip Remnant Lord Turnbull[6]
6.	Statement re computation of per share earnings (set forth in Note B2 to the consolidated financial statements included in this Form 20-F).
8.	Subsidiaries of Prudential (set forth in Note I8 to the consolidated financial statements included in this Form 20-F).
12.1	Certification of Prudential plc's Group Chief Executive pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
12.2	Certification of Prudential plc's Chief Financial Officer pursuant to Section 302 of the Sarbanes Oxley Act of 2002.
13.1	Annual certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
14.1	Consent of KPMG Audit Plc.
15.1	Prudential's Code of Business Conduct.[9]

(1) As previously filed with the Securities and Exchange Commission on 22 June 2000 as an exhibit to Prudential's Form F-6.

(2) As previously filed with the Securities and Exchange Commission on 24 June 2003 as an exhibit to Prudential's Form 20-F.

(3) As previously filed with the Securities and Exchange Commission on 24 June 2005 as an exhibit to Prudential's Form 20-F.

(4) As previously filed with the Securities and Exchange Commission on 28 June 2006 as an exhibit to Prudential's Form 20-F.

(5) As previously filed with the Securities and Exchange Commission on 28 June 2007 as an exhibit to Prudential's Form 20-F.

(6) As previously filed with the Securities and Exchange Commission on 15 May 2008 as an exhibit to Prudential's Form 20-F.

(7)

As previously filed with the Securities and Exchange Commission on 18 May 2009 as an exhibit to Prudential's Form 20-F.

(8)

As previously filed with the Securities and Exchange Commission on 22 June 2010 as an exhibit to Prudential's Form 20-F.

(9)

As previously filed with the Securities and Exchange Commission on 11 May 2011 as an exhibit to Prudential's Form 20-F.

(10)

As previously filed with the Securities and Exchange Commission on 30 March 2012 as an exhibit to Prudential's Form 20-F.