Notes on the EEV basis supplementary information

1 Basis of preparation

The EEV basis results have been prepared in accordance with the EEV Principles issued by the CFO Forum of European Insurance Companies in May 2004 and expanded by the Additional Guidance on EEV Disclosures published in October 2005. Where appropriate the EEV basis results include the effects of adoption of International Financial Reporting Standards (IFRS).

The EEV results for the Group are prepared for 'covered business' as defined by the EEV Principles. Covered business represents the Group's long-term insurance business for which the value of new and in-force contracts is attributable to shareholders. The EEV basis results for the Group's covered business are then combined with the IFRS basis results of the Group's other operations. These other operations include the results of discontinued banking operations, following the sale of Egg on 1 May 2007.

The definition of long-term business operations is consistent with previous practice and comprises those contracts falling under the definition of long-term insurance business for regulatory purposes together with, for US operations, contracts that are in substance the same as guaranteed investment contracts (GICs) but do not fall within the technical definition. Under the EEV Principles, the results for covered business incorporate the projected margins of attaching internal asset management.

With two principal exceptions, covered business comprises the Group's long-term business operations. The principal exceptions are for the closed Scottish Amicable Insurance Fund (SAIF) and for the presentational treatment of the financial position of two of the Group's defined benefit pension schemes. A very small amount of UK group pensions business is also not modelled for EEV reporting purposes.

SAIF is a ring-fenced sub-fund of the Prudential Assurance Company (PAC) long-term fund, established by a Court approved Scheme of Arrangement in October 1997. SAIF is closed to new business and the assets and liabilities of the fund are wholly attributable to the policyholders of the fund. In 2006, a bulk annuity arrangement between SAIF and Prudential Retirement Income Limited (PRIL), a shareholder-owned subsidiary, took place as explained in note 5a. Reflecting the altered economic interest for SAIF policyholders and Prudential shareholders, this arrangement represents a transfer from long-term business of the Group that is not 'covered' to business that is 'covered' with consequential effect on the EEV basis results.

As regards the Group's defined benefit pension schemes, the surplus or deficit attaching to the Prudential Staff Pension Scheme (PSPS) and Scottish Amicable Pension Scheme are excluded from the EEV value of UK operations and included in the total for Other operations. The surplus and deficit amounts are partially attributable to the PAC with-profits fund and shareholder-backed long-term business and partially to other parts of the Group. In addition to the IFRS basis surplus or deficit, the shareholders' 10 per cent share of the PAC with-profits fund's interest in the movement on the financial position of the schemes is recognised for EEV reporting purposes.

The directors are responsible for the preparation of the supplementary information in accordance with the EEV Principles.

2 Methodology

a Embedded value

Overview

The embedded value is the present value of the shareholders' interest in the earnings distributable from assets allocated to covered business after sufficient allowance has been made for the aggregate risks in that business. The shareholders' interest in the Group's long-term business comprises:

— present value of future shareholder cash flows from in-force covered business (value of in-force business), less a deduction for the cost of locked-in (encumbered) capital;
— locked-in (encumbered) capital; and
— shareholders' net worth in excess of encumbered capital.

The value of future new business is excluded from the embedded value.

Notwithstanding the basis of presentation of results (as explained in notes 4 and 6) no smoothing of market or account balance values, unrealised gains or investment returns is applied in determining the embedded value or the profit before tax.

Value of in-force business

The embedded value results are prepared incorporating best estimate assumptions about all relevant factors including levels of future investment returns, expenses, persistency and mortality. These assumptions are used to project future cash flows. The present value of the future cash flows is then calculated using a discount rate which reflects both the time value of money and the non-diversifiable risks associated with the cash flows that are not otherwise allowed for.

The total profit that emerges over the lifetime of an individual contract as calculated using the embedded value basis is the same as that calculated under the IFRS basis. Since the embedded value basis reflects discounted future cash flows, under this methodology the profit emergence is advanced thus more closely aligning the timing of the recognition of profits with the efforts and risks of current management actions, particularly with regard to business sold during the year.

2 Methodology continued

Cost of capital

A charge is deducted from the embedded value for the cost of capital supporting the Group's long-term business. This capital is referred to as encumbered capital. The cost is the difference between the nominal value of the capital and the discounted value of the projected releases of this capital allowing for investment earnings (net of tax) on the capital.

The annual result is affected by the movement in this cost from year to year which comprises a charge against new business profit and generally a release in respect of the reduction in capital requirements for business in force as this runs off.

Where capital is held within a with-profits long-term fund, the value placed on surplus assets in this fund is already discounted to reflect their release over time and no further adjustment is necessary in respect of encumbered capital. However, where business is funded directly by shareholders, the capital requires adjustment to reflect the cost of that capital to shareholders.

Financial options and guarantees

Nature of options and guarantees in Prudential's long-term business

Asian operations

Subject to local market circumstances and regulatory requirements, the guarantee features described below in respect of UK business broadly apply to similar types of participating contracts principally written in the PAC 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 insurer is contractually obliged to provide guarantees on all benefits. The most significant book of non-participating business in the Group's Asian operations is Taiwan's whole of life contracts. For these contracts there are floor levels of policyholder benefits that accrue at rates set at inception by reference to minimum returns established by local regulation. These rates do not vary subsequently with market conditions. Under these contracts the cost of premiums are also fixed at inception based on a number of assumptions at that time, including long-term interest rates, mortality assumptions and expenses. The guaranteed maturity and surrender values reflect the pricing basis.

US operations (Jackson)

The principal options and guarantees in Jackson are associated with the fixed annuity and Variable Annuity (VA) lines of business.

Fixed annuities provide that, at Jackson's discretion, it may reset the interest rate credited to policyholders' accounts, subject to a guaranteed minimum. The guaranteed minimum return varies from 1.5 per cent to 5.5 per cent (2006: 1.5 per cent to 5.5 per cent), depending on the particular product, jurisdiction where issued, and date of issue. At 31 December 2007, 80 per cent (2006: 70 per cent) of the fund relates to policies with guarantees of three per cent or less. The average guarantee rate is 3.1 per cent (2006: 3.2 per cent).

Fixed annuities also present a risk that policyholders will exercise their option to surrender their contracts in periods of rapidly rising interest rates, possibly requiring Jackson to liquidate assets at an inopportune time.

Jackson issues VA contracts where it contractually guarantees to the contract holder 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.

These guarantees generally protect the policyholder's value in the event of poor equity market performance.

Jackson also issues fixed index annuities that enable policyholders to obtain a portion of an equity-linked return while providing a guaranteed minimum return. The guaranteed minimum returns would be of a similar nature to those described above for fixed annuities.

UK insurance operations

The only significant financial options and guarantees in the UK insurance operations arise in the with-profits fund and SAIF. 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 with-profits fund held a provision on the Pillar I Peak 2 basis of £45 million (2006: £47 million) at 31 December 2007 to honour guarantees on a small amount of guaranteed annuity option products.

Beyond the generic features and the provisions held in respect of guaranteed annuities described above, there are very few explicit options or guarantees of the with-profits fund such as minimum investment returns, surrender values, or annuity values at retirement and any granted have generally been at very low levels.

The Group's main exposure to guaranteed annuity options in the UK is through SAIF and a provision on the Pillar I Peak 2 basis of £563 million (2006: £561 million) was held in SAIF at 31 December 2007 to honour the guarantees.

2 Methodology continued

Time value

The value of financial options and guarantees comprises two parts. One is given by a deterministic valuation on best estimate assumptions (the intrinsic value). The other part arises from the variability of economic outcomes in the future (the time value).

Where appropriate, a full stochastic valuation has been undertaken to determine the value of the in-force business including the cost of capital. A deterministic valuation of the in-force business is also derived using consistent assumptions and the time value of the financial options and guarantees is derived as the difference between the two.

The economic assumptions used for the stochastic calculations are consistent with those used for the deterministic calculations. Assumptions specific to the stochastic calculations such as equity volatility and credit losses reflect local market conditions and are based on a combination of actual market data, historic market data and an assessment of long-term economic conditions. Common principles have been adopted across the Group for the stochastic asset models, for example, separate modelling of individual asset classes but with an allowance for correlation between the various asset classes. Details of the key characteristics of each model are given in note 3.

b Level of encumbered capital

In adopting the EEV Principles, Prudential has based encumbered capital on its internal targets for economic capital subject to it being at least the local statutory minimum requirements. Economic capital is assessed using internal models but, when applying the EEV Principles, Prudential does not take credit for the significant diversification benefits that exist within the Group. For with-profits business written in a segregated life fund, as is the case in Asia and the UK, the capital available in the fund is sufficient to meet the encumbered capital requirements.

- Asian operations: the economic capital requirement is substantially higher than local statutory requirements in total. Economic capital requirements vary by territory, but in aggregate, the encumbered capital is equivalent to the amount required under the Insurance Groups Directive (IGD).
- US operations: the level of encumbered capital has been set to an amount at least equal to 235 per cent of the risk-based capital required by the National Association of Insurance Commissioners at the Company Action Level (CAL), which is sufficient to meet the economic capital requirement.
- UK insurance operations: the economic capital requirements for annuity business are fully met by Pillar I requirements being four per cent of mathematical reserves, which are also sufficient to meet Pillar II requirements.

c Risk discount rates

Overview

Under the EEV Principles, discount rates used to determine the present value of future cash flows are set equal to risk-free rates plus a risk margin. The risk margin should reflect any non-diversifiable risk associated with the emergence of distributable earnings that is not allowed for elsewhere in the valuation. Prudential has selected a granular approach to better reflect differences in market risk inherent in each product group. The risk discount rate so derived does not reflect a market beta but instead reflects the expected volatility associated with the cash flows in the embedded value model.

Since financial options and guarantees are explicitly valued under the EEV methodology, discount rates under EEV are set excluding the effect of these product features.

As Prudential's UK shareholder-backed annuity business is predominantly backed by fixed interest securities, the beta methodology described above is not appropriate. We have therefore used a market consistent embedded value (MCEV) approach to derive an implied risk discount rate which is then applied to the projected cash flows.

In the annuity MCEV calculations, the future cash flows were discounted using the gilt yield curve plus 84 basis points for fixed annuities and 24 basis points for inflation-linked annuities (2006: gilt yield curve plus 34 basis points for both products). The 84 basis points and 24 basis points for 2007 were based on our assessment of the liquidity premium available in the yield on the assets backing the annuity liabilities.

Allowance for risk

The risk allowance in the risk discount rate is determined as follows:

Market risk

Under the Capital Asset Pricing Methodology (CAPM) the discount rate is determined as:

Discount rate = risk-free rate + (beta x equity risk premium)

Under CAPM, the beta of a portfolio or product measures its relative market risk.

The risk discount rates reflect the market risk inherent in each product group and hence the volatility of product cash flows.

They are determined by considering how the profits from each product are affected by changes in expected returns on various asset classes. By converting this into a relative rate of return it is possible to derive a product specific beta.

2 Methodology continued

Product level betas are calculated each year. They are combined with the most recent product mix to produce appropriate betas and risk discount rates for each major product grouping.

CAPM does not include any allowance for non-market risks since these are assumed to be fully diversifiable. For EEV purposes, however, a risk margin is added for non-diversifiable non-market risks and to cover Group level risks.

Diversifiable non-market risks

No allowance is required for non-market risks where these are assumed to be fully diversifiable. The majority of non-market risks are considered to be diversifiable.

Non-diversifiable, non-market risks

Finance theory cannot be used to determine the appropriate component of beta for non-diversifiable non-market risks since there is no observable risk premium associated with it that is akin to the equity risk premium. Recognising this, a pragmatic approach has been used.

Except for UK shareholder-backed annuity business, a constant margin of 50 basis points (2006: 50 basis points) has been added to the risk margin derived for market risk to cover the non-diversifiable non-market risks associated with the business. For UK shareholder-backed annuity business, a margin of 100 basis points was used (2006: 100 basis points).

d Management actions

In deriving the time value of financial options and guarantees, management actions in response to emerging investment and fund solvency conditions have been modelled. Management actions encompass, but are not confined to, the following areas:

— investment allocation decisions;
— levels of reversionary bonuses and credited rates; and
— total claim values.

Bonus rates are projected from current levels and varied in accordance with assumed management actions applying in the emerging investment and fund solvency conditions.

In all instances, the modelled actions are in accordance with approved local practice and therefore reflect the options actually available to management. For the PAC with-profits fund, the actions assumed are consistent with those set out in the Principles and Practices of Financial Management.

e With-profits business and the treatment of the estate

For the PAC with-profits fund, the shareholders' interest in the estate is derived by increasing final bonus rates so as to exhaust the estate over the lifetime of the in-force with-profits business. In those few extreme scenarios where the total assets of the life fund are insufficient to meet policyholder claims in full, the excess cost is fully attributed to shareholders.

f Pension costs

The Group operates three defined benefit schemes in the UK. The principal scheme is the Prudential Staff Pension Scheme (PSPS). The other two, much smaller, schemes are the Scottish Amicable and M&G schemes. There is also a small scheme in Taiwan.

Under IFRS the surpluses or deficits attaching to these schemes are accounted for in accordance with the provisions of IAS 19. The surpluses or deficits represent the difference between the market value of the schemes' assets and the discounted value of projected future benefit payments to retired members and deferred pensioners and, to the extent of service to date, current employed members.

For PSPS the surplus or deficit at the reporting date is allocated between the PAC with-profits fund and shareholder-backed operations by reference to the activities of the members of the scheme during their period of service. At 31 December 2005, the deficit of PSPS was apportioned in the ratio 70/30 between the with-profits fund and shareholder-backed operations following detailed consideration of the sourcing of previous contributions. This ratio was applied to the base deficit position at 1 January 2006 for the purposes of determining the allocation of the movement in that position up to 31 December 2007. The IAS 19 service charge and ongoing employer contributions are allocated by reference to the cost allocation for current activity.

Under the EEV basis the IAS 19 basis surplus or deficit is initially allocated in the same manner. The shareholders' 10 per cent interest in the PAC with-profits fund estate is determined after inclusion of the portion of the IAS 19 basis surplus or deficit attributable to the fund. Adjustments under EEV in respect of accounting for surpluses or deficits on defined benefit schemes are reflected as part of 'Other operations', as shown in note 15.

Separately, the projected cash flows of in-force covered business include contributions to the defined benefit schemes for future service based on the contribution basis applying to the schemes at the time of the preparation of the results.

2 Methodology continued

g Debt capital
Core structural debt liabilities are carried at market value.

3 Assumptions

a Best estimate assumptions
Best estimate assumptions are used for the cash flow projections, where best estimate is defined as the mean of the distribution of future possible outcomes. The assumptions are reviewed actively and changes are made when evidence exists that material changes in future experience are reasonably certain.

Assumptions required in the calculation of the value of options and guarantees, for example relating to volatilities and correlations, or dynamic algorithms linking liabilities to assets, have been set equal to the best estimates and, wherever material and practical, reflect any dynamic relationships between the assumptions and the stochastic variables.

b Principal economic assumptions
Deterministic
In most countries, the long-term expected rates of return on investments and risk discount rates are set by reference to period end rates of return on cash or fixed interest securities. This 'active' basis of assumption setting has been applied in preparing the results of all the Group's US and UK long-term business operations. For the Group's Asian operations, the active basis is appropriate for business written in Japan, Korea and US dollar denominated business written in Hong Kong.

An exception to this general rule is that for countries where long-term fixed interest markets are less established, investment return assumptions and risk discount rates are based on an assessment of longer-term economic conditions. Except for the countries listed above, this basis is appropriate for the Group's Asian operations.

Expected returns on equity and property asset classes in respect of each territory are derived by adding a risk premium, also based on the long-term view of Prudential's economists, to the risk-free rate. In Asia, equity risk premiums range from 3.0 per cent to 6.0 per cent (2006: 3.0 per cent to 5.8 per cent). In the US and the UK, the equity risk premium is 4.0 per cent above risk-free rates for both 2007 and 2006. Best estimate assumptions for other asset classes, such as corporate bond spreads, are set consistently.

Assumed investment returns reflect the expected future returns on the assets held and allocated to the covered business at the valuation date.

The tables below summarise the principal financial assumptions:

Asian operations	31 Dec 2007 %						31 Dec 2006 %					
	China	Hong Kong notes iii,iv,v	India	Indonesia	Japan	Korea	China	Hong Kong notes iii,iv,v	India	Indonesia	Japan	Korea
Risk discount rate:												
New business	11.75	5.7	15.75	16.75	5.1	9.7	12.0	6.6	16.5	17.5	5.3	9.5
In force	11.75	6.0	15.75	16.75	5.1	9.7	12.0	6.8	16.5	17.5	5.3	9.5
Expected long-term rate of inflation	4.0	2.25	5.0	6.0	0.0	2.75	4.0	2.25	5.5	6.5	0.0	2.75
Government bond yield	8.25	4.1	9.25	10.25	2.0	5.8	9.0	4.7	10.5	11.5	2.1	5.0

	31 Dec 2007 %						31 Dec 2006 %					
	Malaysia notes iv,v	Philippines	Singapore notes iv,v	Taiwan notes ii,v	Thailand	Vietnam	Malaysia notes iv,v	Philippines	Singapore notes iv,v	Taiwan notes ii,v	Thailand	Vietnam
Risk discount rate:												
New business	9.3	15.75	6.4	9.1	13.0	16.75	9.5	16.5	6.9	8.8	13.75	16.5
In force	9.1	15.75	6.8	9.8	13.0	16.75	9.2	16.5	6.9	9.3	13.75	16.5
Expected long-term rate of inflation	2.75	5.0	1.75	2.25	3.0	6.0	3.0	5.5	1.75	2.25	3.75	5.5
Government bond yield	6.5	9.25	4.25	5.5	6.75	10.25	7.0	10.5	4.5	5.5	7.75	10.5

3 Assumptions continued

	31 Dec 2007 % Asia total	31 Dec 2006 % Asia total
Weighted risk discount rate:note i		
New business	9.5	9.8
In force	8.7	8.8

Notes

i The weighted risk discount rates for Asian operations shown above have been determined by weighting each country's risk discount rates by reference to the EEV basis operating result for new business and the closing value of in-force business.

ii For traditional business in Taiwan, the economic scenarios used to calculate the 2007 and 2006 EEV basis results reflect the assumption of a phased progression of the bond yields from the current rates applying to the assets held to the long-term expected rates.

The projections assume that in the average scenario, the current bond yields at 31 December 2007 of around 2.5 per cent (2006: around 2 per cent) trend towards 5.5 per cent at 31 December 2013.

In projecting forward the Fund Earned Rate, allowance is made for the mix of assets in the fund, future investment strategy, and further market value depreciation of bonds held as a result of assumed future yield increases. These factors, together with the assumption of the phased progression in bond yields, give rise to an average assumed Fund Earned Rate that trends from 0.5 per cent for 2007 to 6.4 per cent for 2014. The assumed Fund Earned Rate increases to 2.5 per cent in 2008 and then increases to 3.3 per cent by 2013. Thereafter, the assumed Fund Earned Rate fluctuates around a target of 6.4 per cent. This projection compares with that applied for the 2006 results of a grading from an assumed rate of 2.1 per cent for 2006 to 5.7 per cent for 2014.

Consistent with the EEV methodology applied, a constant discount rate has been applied to the projected cash flows.

iii The assumptions shown are for US dollar denominated business which comprises the largest proportion of the in-force Hong Kong business.

iv The mean equity return assumptions for the most significant equity holdings in the Asian operations were:

	31 Dec 2007 %	31 Dec 2006 %
Hong Kong	8.1	8.7
Malaysia	12.5	12.8
Singapore	9.3	9.3

To obtain the mean, an average over all simulations of the accumulated return at the end of the projection period is calculated. The annual average return is then calculated by taking the root of the average accumulated return minus 1.

v For 2007, cash rates rather than government bond yields were used in setting the risk discount rates for Malaysia, Singapore, Taiwan and for Hong Kong dollar denominated business. For 2006, cash rates were used for these operations and for all Hong Kong business (i.e. including US dollar denominated business).

US operations (Jackson)	31 Dec 2007 %	31 Dec 2006 %
Risk discount rate:*		
New business	7.0	7.6
In force	6.0	6.7
Expected long-term spread between earned rate and rate credited to policyholders for single premium deferred annuity business	1.75	1.75
US 10-year treasury bond rate at end of period	4.1	4.8
Pre-tax expected long-term nominal rate of return for US equities	8.1	8.8
Expected long-term rate of inflation	2.4	2.5

* The risk discount rates at 31 December 2007 for new business and business in force for US operations reflect weighted rates based on underlying rates of 8.1 per cent for variable annuity business and 4.8 per cent for other business. The decrease in the weighted discount rates reflects the decrease in the US 10-year treasury bond rate.

3 Assumptions continued

UK insurance operations	31 Dec 2007 %	31 Dec 2006 %
Risk discount rate:[note i]		
New business	7.3	7.8
In force	7.85	8.0
Pre-tax expected long-term nominal rates of investment return:		
UK equities	8.55	8.6
Overseas equities	8.1 to 10.2	8.6 to 9.3
Property	6.8	7.1
Gilts	4.55	4.6
Corporate bonds – with-profits funds[note ii]	6.0	5.3
– other business	6.25	5.3
Expected long-term rate of inflation	3.2	3.1
Post-tax expected long-term nominal rate of return for the PAC with-profits fund:		
Pension business (where no tax applies)	7.85	7.5
Life business	6.9	6.6
Pre-tax expected long-term nominal rate of return for annuity business:[note iii]		
Fixed annuities	5.4 to 5.6	5.0 to 5.1
Linked annuities	5.0 to 5.2	4.8 to 5.0

Notes
i The risk discount rates for new business and business in force for UK insurance operations reflect weighted rates based on the type of business.
ii The assumed long-term rate for corporate bonds for 2007 for with-profits business reflects the purchase of credit default swaps.
iii The pre-tax rates of return for annuity business are based on the gross redemption yield on the backing assets net of a best estimate allowance for future defaults.

Stochastic
The economic assumptions used for the stochastic calculations are consistent with those used for the deterministic calculations described above. Assumptions specific to the stochastic calculations, such as the volatilities of asset returns, reflect local market conditions and are based on a combination of actual market data, historic market data and an assessment of longer-term economic conditions. Common principles have been adopted across the Group for the stochastic asset models, for example, separate modelling of individual asset classes but with allowance for correlation between the various asset classes.

Details are given below of the key characteristics and calibrations of each model.

Asian operations
The same asset return models as used in the UK, appropriately calibrated, have been used for the Asian operations as described for UK insurance operations below. The principal asset classes are government and corporate bonds. Equity holdings are much lower than in the UK whilst property holdings do not represent a significant investment asset.

The stochastic cost of guarantees is primarily only of significance for the Hong Kong, Malaysia, Singapore and Taiwan operations.

The mean stochastic returns are consistent with the mean deterministic returns for each country. The expected volatility of equity returns for both 2007 and 2006 ranges from 18 per cent to 25 per cent and the volatility of government bond yields ranges from 1.3 per cent to 2.5 per cent (2006: 1.4 per cent to 2.5 per cent).

US operations (Jackson)
— Interest rates are projected using a log-normal generator calibrated to actual market data;
— Corporate bond returns are based on Treasury securities plus a spread that has been calibrated to current market conditions and varies by credit quality; and
— Variable annuity equity and bond returns have been stochastically generated using a regime-switching log-normal model with parameters determined by reference to historical data. The volatility of equity fund returns for both 2007 and 2006 ranges from 18.6 per cent to 28.1 per cent, depending on risk class, and the standard deviation of bond returns ranges from 1.4 per cent to 1.7 per cent (2006: 1.4 per cent to 2.0 per cent).

3 Assumptions continued

UK insurance operations

- Interest rates are projected using a two-factor model calibrated to actual market data;
- The risk premium on equity assets is assumed to follow a log-normal distribution;
- The corporate bond return is calculated as the return on a zero-coupon bond plus a spread. The spread process is a mean reverting stochastic process; and
- Property returns are modelled in a similar fashion to corporate bonds, namely as the return on a riskless bond, plus a risk premium, plus a process representative of the change in residual values and the change in value of the call option on rents.

Mean returns have been derived as the annualised arithmetic average return across all simulations and durations. For each projection year, standard deviations have been calculated by taking the square root of the annualised variance of the returns over all the simulations. These have been averaged over all durations in the projection. For equity and property, the standard deviations relate to the total return on these assets. The standard deviations applied to both years are as follows:

	%
Equities:	
UK	18.0
Overseas	16.0
Property	15.0

c Demographic assumptions

Persistency, mortality and morbidity assumptions are based on an analysis of recent experience but also reflect expected future experience. Where relevant, when calculating the time value of financial options and guarantees, policyholder withdrawal rates vary in line with the emerging investment conditions according to management's expectations.

d Expense assumptions

Expense levels, including those of service companies that support the Group's long-term business operations, are based on internal expense analysis investigations and are appropriately allocated to acquisition of new business and renewal of in-force business. Exceptional expenses are identified and reported separately.

Asia development and Regional Head Office expenses are charged to EEV basis results as incurred. No adjustment is made to the embedded value of covered business as the amounts of expenditure that relate to operating expenses are not material. Similarly, corporate expenditure for Group Head Office (GHO), to the extent not allocated to the PAC with-profits fund, is charged to the EEV basis result as incurred.

e Inter-company arrangements

The EEV results for covered business incorporate the effect of the reinsurance arrangement of non-profit immediate pension annuity liabilities of SAIF to PRIL, as described in note 5a. In addition, the analysis of free surplus and value of in-force business takes account of the impact of contingent loan arrangements between Group companies.

f Taxation and other legislation

Current taxation and other legislation have been assumed to continue unaltered except where changes have been announced and the relevant legislation passed.

g Asset management and service companies

The value of future profits or losses from asset management and service companies that support the Group's covered businesses are included in the profits for new business and the in-force value of the Group's long-term business.

4 Accounting presentation

a Analysis of profit before tax

To the extent applicable, presentation of the EEV profit for the year is consistent with the basis that the Group applies for analysis of IFRS basis profits before shareholder taxes between operating and non-operating results. Operating results reflect the underlying results of the Group's continuing operations including longer-term investment returns. Operating results include the impact of routine changes of estimates and non-economic assumptions. Non-operating results include certain recurrent and exceptional items that primarily do not reflect the performance in the year of the Group's continuing operations.

4 Accounting presentation continued

b Investment return

Profit before tax

With the exception of debt securities held by Jackson, investment gains and losses during the year (to the extent that changes in capital values do not directly match changes in liabilities) are included directly in the profit for the year and shareholders' funds as they arise.

The results for any covered business conceptually reflects the aggregate of the IFRS results and the movements on the additional shareholders' interest recognised on the EEV basis. Thus the start point for the calculation of the EEV results for Jackson, as for other businesses, reflects the market value movements recognised on the IFRS basis.

However, in determining the movements on the additional shareholders' interest the basis for calculating the Jackson EEV result acknowledges that for debt securities backing liabilities the aggregate EEV results reflect the fact that the value of in-force business instead incorporates the discounted value of future spread earnings. This value is not affected generally by short-term market movements on securities that are broadly speaking held with the intent and ability to be retained for the longer term.

Separately, from 31 December 2006, fixed income securities backing the free surplus and required capital are accounted for at fair value. However, consistent with the treatment applied under IFRS for securities classified as available-for-sale, movements in unrealised appreciation on these securities are accounted for in equity rather than in the income statement.

Operating profit

Investment returns, including investment gains, in respect of long-term insurance business are recognised in operating results at the expected long-term rate of return. For the purpose of calculating the longer-term investment return to be included in the operating results of UK operations, where equity holdings are a significant proportion of investment portfolios, values of assets at the beginning of the reporting period are adjusted to remove the effects of short-term market volatility.

For the purposes of determining the long-term returns for debt securities of shareholder-backed operations, a risk margin charge is included which reflects the expected long-term rate of default based on the credit quality of the portfolio. For Jackson, interest-related realised gains and losses are amortised to the operating results over the maturity period of the sold bonds and for equity-related investments, a long-term rate of return is assumed, which reflects the aggregation of risk-free rates and equity risk premium.

c Pension costs

Profit before tax

Movements on the shareholders' share of surplus or deficit of the Group's defined benefit pension schemes adjusted for contributions paid in the year are recorded within the income statement. Consistent with the basis of distribution of bonuses and the treatment of the estate described in notes 2d and 2e, the shareholders' share incorporates 10 per cent of the proportion of the surplus or deficit attributable to the PAC with-profits fund. The surplus or deficit is determined by applying the requirements of IAS 19.

Actuarial gains and losses

Actuarial gains and losses comprise:

— the difference between actual and expected return on the scheme assets;
— experience gains and losses on scheme liabilities; and
— the impact of altered economic and other assumptions on the discounted value of scheme liabilities.

These items are recorded in the income statement but, consistent with the IFRS basis of presentation, are excluded from operating results.

d Effect of changes in economic assumptions and time value of cost of options and guarantees

Movements in the value of in-force business caused by changes in economic assumptions and the time value of cost of options and guarantees resulting from changes in economic factors are recorded in non-operating results.

e Results for asset management operations

The results of the Group's asset management operations include the profits from management of internal and external funds. For EEV basis reporting, Group shareholders' other income is adjusted to deduct the expected margin for the year on management of covered business. The deduction is on a basis consistent with that used for projecting the results for covered business. Group operating profit accordingly includes the variance between actual and expected profit in respect of covered business.

4 Accounting presentation continued

f Capital held centrally for Asian operations

In adopting the EEV Principles, Prudential has decided to set encumbered capital at its internal targets for economic capital. In Asia, the economic capital target is substantially higher than the local statutory requirements in total. Accordingly, capital is held centrally for Asian operations. For the purpose of the presentation of the Group's operating results, it is assumed that the centrally held capital is lent interest free to the Asian operations. In turn, the results of the Asian operations include the return on that capital and Group shareholders' other income for EEV basis reporting is consequently reduced.

g Taxation

The EEV profit for the year for covered business is in most cases calculated initially at the post-tax level. The post-tax profit is then grossed up for presentation purposes at the effective rate of tax. In general, the effective rate corresponds to the corporation tax rate on shareholder profits of the business concerned.

h Foreign currency translation

Foreign currency profits and losses have been translated at average exchange rates for the year. Foreign currency assets and liabilities have been translated at year end rates of exchange. The purpose of translating the profits and losses at average exchange rates, notwithstanding the fact that EEV profit represents the incremental value added on a discounted cash flow basis, is to maintain consistency with the methodology applied for IFRS basis reporting.

The principal exchange rates applied are:

Local currency: £	Closing rate at 31 Dec 2007	Average for 2007	Closing rate at 31 Dec 2006	Average for 2006	Opening rate at 1 Jan 2006
Hong Kong	15.52	15.62	15.22	14.32	13.31
Japan	222.38	235.64	233.20	214.34	202.63
Malaysia	6.58	6.88	6.90	6.76	6.49
Singapore	2.87	3.02	3.00	2.93	2.85
Taiwan	64.56	65.75	63.77	59.95	56.38
US	1.99	2.00	1.96	1.84	1.72

The exchange movements in 2007 and 2006 recorded within the movements in shareholders' equity (and for 2007, in note 16) for long-term business and other operations comprise amounts in respect of:

	2007 £m	2006 £m
Long-term business operations:		
Asian operations	80	(169)
US operations	(53)	(432)
Other operations	37	242
Total	64	(359)

5. Premiums, operating profit and margins from new business

a Premiums and contributions[note i]

	Single		Regular		Annual Premium and Contribution Equivalents (APE)		Present Value of New Business Premiums (PVNBP)	
	2007 £m	2006 £m	2007 £m	2006 £m	2007 £m	2006 £m	2007 £m	2006 £m
Asian operations								
China[note iv]	72	27	40	36	47	39	268	198
Hong Kong	501	355	117	103	167	139	1,196	933
India (Group's 26% interest)	26	20	177	105	180	107	728	411
Indonesia	118	31	109	71	121	74	494	269
Japan	122	68	22	7	34	14	214	97
Korea	179	103	241	208	259	218	1,267	1,130
Malaysia	41	4	78	72	82	72	472	418
Singapore	593	357	67	72	126	108	1,047	803
Taiwan	132	92	218	139	231	148	1,121	743
Other	36	15	55	36	59	37	200	130
Total Asian operations	1,820	1,072	1,124	849	1,306	956	7,007	5,132
US operations								
Fixed annuities	573	688	–	–	57	69	573	688
Fixed index annuities	446	554	–	–	45	55	446	554
Variable annuities	4,554	3,819	–	–	455	382	4,554	3,819
Life	7	8	19	17	20	18	158	147
Guaranteed Investment Contracts	408	458	–	–	41	46	408	458
GIC – Medium Term Notes	527	437	–	–	53	44	527	437
Total US operations	6,515	5,964	19	17	671	614	6,666	6,103
UK insurance operations								
Product summary								
Internal vesting annuities	1,399	1,341	–	–	140	134	1,399	1,341
Direct and partnership annuities	842	780	–	–	84	78	842	780
Intermediated annuities	589	592	–	–	59	59	589	592
Total individual annuities	2,830	2,713	–	–	283	271	2,830	2,713
Equity release	156	89	–	–	16	9	156	89
Individual pensions	38	21	1	–	5	2	42	21
Corporate pensions	283	318	84	66	112	98	737	490
Unit-linked bonds	243	388	–	–	24	39	243	388
With-profit bonds	297	139	–	–	30	14	297	139
Protection	–	11	5	9	5	10	26	63
Offshore products	434	540	4	–	47	54	455	540
Total retail retirement	4,281	4,219	94	75	522	497	4,786	4,443
Corporate pensions	198	261	115	100	135	126	604	643
Other products	190	232	25	26	44	49	276	347
DWP rebates	143	161	–	–	14	16	143	161
Total mature life and pensions	531	654	140	126	193	191	1,023	1,151
Total retail	4,812	4,873	234	201	715	688	5,809	5,594
Wholesale annuities[notes ii,iii]	1,799	1,431	–	–	180	143	1,799	1,431
Credit life	21	687	–	–	2	69	21	687
Total UK insurance operations	6,632	6,991	234	201	897	900	7,629	7,712
Channel summary								
Direct and partnership	2,385	2,543	209	174	448	428	3,288	3,133
Intermediated	2,284	2,169	25	27	253	244	2,378	2,300
Wholesale[notes ii,iii]	1,820	2,118	–	–	182	212	1,820	2,118
Sub-total	6,489	6,830	234	201	883	884	7,486	7,551
DWP rebates	143	161	–	–	14	16	143	161
Total UK operations	6,632	6,991	234	201	897	900	7,629	7,712
Group total	14,967	14,027	1,377	1,067	2,874	2,470	21,302	18,947

5 Premiums, operating profit and margins from new business continued

Notes

i The tables 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 not intended to be, reflective of premium income recorded in the IFRS income statement.

APEs are calculated as the aggregate of regular new business amounts and one-tenth of single new business amounts. PVNBPs are calculated as equalling single premiums plus the present value of expected premiums of new regular premium business, allowing for lapses and other assumptions made in determining the EEV new business contribution. New business premiums reflect those premiums attaching to covered business, including premiums for contracts classified as investment products for IFRS basis reporting. New business premiums for regular premium products are shown on an annualised basis. Department of Work and Pensions (DWP) rebate business is classified as single recurrent business. Internal vesting business is classified as new business where the contracts include an open market option.

ii The tables above include the transfer of 62,000 with-profit annuity policies from Equitable Life on 31 December 2007 with assets of approximately £1.7 billion. The transfer represented an APE of £174 million.

iii The tables for 2006 include a bulk annuity transaction with the Scottish Amicable Insurance Fund (SAIF) with a premium of £560 million. The transaction reflects the arrangement entered into in June 2006, for the reinsurance of non-profit immediate pension annuity liabilities of SAIF to Prudential Retirement Income Limited (PRIL) a shareholder owned subsidiary of the Group. SAIF is a closed ring-fenced sub-fund of the PAC long-term fund established by a Court approved Scheme of Arrangement in October 1997, which is solely for the benefit of SAIF policyholders. Shareholders have no interest in the profits of this fund and, accordingly, it is not part of covered business for EEV reporting purposes. Consistent with this treatment, and the transfer of longevity risk, requirement for capital support and entitlement to profits on this block of business from SAIF to Prudential shareholders, the transaction has been accounted for as new business for EEV basis reporting purposes.

iv Subsequent to 29 September 2007, following expiry of the previous management agreement, CITIC-Prudential Life Insurance Company Ltd (CITIC-Prudential), the Group's life operation in China, has been accounted for as a joint venture. Prior to this date, CITIC-Prudential was consolidated as a subsidiary undertaking. The amounts in the table above include 100 per cent of the total premiums for this operation up to 29 September 2007 and 50 per cent thereafter, being the Group's share after this date.

b Operating profit

	2007 £m			2006 £m		
	Pre-tax	Tax	Post-tax Notes 17ii,iii	Pre-tax	Tax	Post-tax Note 17ii
Asian operations	653	(173)	480	514	(141)	373
US operations[note i]	285	(100)	185	259	(91)	168
UK insurance operations	277	(77)	200	266	(80)	186
Total	1,215	(350)	865	1,039	(312)	727

Note

i US Operations net of tax profit:

	2007	2006
Before capital charge	197	182
Capital charge	(12)	(14)
After capital charge	185	168

In determining the EEV basis value of new business written in the year the policies incept, premiums are included in projected cash flows on the same basis of distinguishing annual and single premium business as set out for statutory basis reporting. Included within pre-tax new business profits shown in the table above are profits arising from asset management business falling within the scope of covered business of:

	2007 £m	2006 £m
Asian operations	44	23
US operations	1	2
UK insurance operations	11	9
Total	56	34

5 Premiums, operating profit and margins from new business continued

c Margins

	2007 £m					2007 %	
	New business premiums		Annual premium and contribution equivalent	Present value of new business premiums	Pre-tax new business contribution	New business margin	
	Single	Regular	(APE)	(PVNBP)		(APE)	(PVNBP)
Asian operations	1,820	1,124	1,306	7,007	653	50	9.3
US operations	6,515	19	671	6,666	285	42	4.3
UK insurance operations	6,632	234	897	7,629	277	31	3.6
Total	14,967	1,377	2,874	21,302	1,215	42	5.7

	2006 £m					2006 %	
	New business premiums		Annual premium and contribution equivalent	Present value of new business premiums	Pre-tax new business contribution	New business margin	
	Single	Regular	(APE)	(PVNBP)		(APE)	(PVNBP)
Asian operations	1,072	849	956	5,132	514	54	10.0
US operations	5,964	17	614	6,103	259	42	4.2
UK insurance operations	6,991	201	900	7,712	266	30	3.4
Total	14,027	1,067	2,470	18,947	1,039	42	5.5

	New business margin (APE) 2007 %	New business margin (APE) 2006 %
Asian operations:		
Hong Kong	73	69
Korea	37	35
Taiwan	58	55
India	12	23
China	50	43
Other	61	72
Weighted average for all Asian operations	50	54

New business margins are shown on two bases, namely the margins by reference to the Annual Premium and Contribution Equivalents (APE) and the Present Value of New Business Premiums (PVNBP).
New business contributions represent profits determined by applying the economic and non-economic assumptions as at the end of the year.
The table of new business premiums and margins above excludes SAIF DWP rebate premiums.

6 Operating profit from business in force

	2007 £m	2006 £m
Asian operations[note ii]		
Unwind of discount and other expected returns[note i]	340	254
Changes in operating assumptions[note iia]	54	45
Experience variances and other items[note iib]	(1)	16
	393	315
US operations[note iii]		
Unwind of discount and other expected returns:[note i]		
On value of in-force business and required capital	187	202
On surplus assets	53	49
Spread experience variance	99	118
Amortisation of interest-related realised gains and losses	37	45
Changes in operating assumptions	(24)	(7)
Other[note iii]	(10)	42
	342	449
UK insurance operations[note iv]		
Unwind of discount and other expected returns[note i]	592	530
Effect of change in the UK corporate tax rate[note iva]	67	–
Annuity business:[note ivb]		
Mortality strengthening	(312)	–
Release of margins	312	–
	0	–
Other items[notes ivc,ivd]	(77)	(110)
	582	420
Total	1,317	1,184

Notes

i For Asian operations and UK insurance operations, unwind of discount and other expected returns is determined by reference to the value of in-force business, required capital and surplus assets at the start of the year as adjusted for the effect of changes in economic and operating assumptions reflected in the current year. For the unwind of discount for UK insurance operations included in operating results based on longer-term returns a further adjustment is made. For UK insurance operations the amount represents the unwind of discount on the value of in-force business at the beginning of the year (adjusted for the effect of current year assumption changes), the expected return on smoothed surplus assets retained within the PAC with-profits fund and the expected return on shareholders' assets held in other UK long-term business operations. Surplus assets retained within the PAC with-profits fund are smoothed for this purpose to remove the effects of short-term investment volatility from operating results. In the balance sheet and for total profit reporting, asset values and investment returns are not smoothed. For US operations the return on surplus assets is shown separately.

ii Asian operations

a Changes in operating assumptions

The £54 million profit from the effect of changes in operating assumptions for 2007 includes a benefit arising from reductions in corporate tax rates in China, Malaysia and Singapore. After grossing up the net of tax benefits totalling £25 million for notional tax of £7 million, the effect on the pre-tax operating result based on longer-term investment returns for Asian operations for 2007 is a credit of £32 million. Also included is a credit of £51 million for the effect of changes in expense assumptions, mainly relating to Singapore (£37 million) and Korea (£21 million) both due to increases in investment margins, a further credit of £17 million for the effect of changes in mortality and morbidity assumptions, offset by a charge of £51 million for the effect of changes in persistency assumptions mainly arising in Singapore (£29 million) as a result of changes in a number of product-related features and updated maturity assumptions and in Taiwan (£15 million) from an increase in lapse rates, reflecting recent experience.

The £45 million profit from the effect of changes in operating assumptions for 2006 for Asian operations includes £24 million in respect of higher assumed investment management margins based on current experience, a further £24 million for the net effect of altered lapse rates across a number of territories and similarly a net £20 million for changes to mortality and morbidity assumptions offset by a charge of £23 million for other items.

b Experience variances and other items

Experience variances and other items, a net charge of £1 million for 2007 (2006: credit of £16 million), include a credit of £47 million (2006: £35 million) for mortality and morbidity experience variance relating to better than expected experience across most territories and a charge of £27 million (2006: £26 million) for expense experience variances in China of £12 million (2006: £14 million) and India of £15 million (2006: £12 million). The negative expense variances in China and India are primarily a reflection of the expenses for new business being in excess of the target levels factored into the valuation of new business for these operations which are at a relatively early stage of development. On the basis of current plans, the target level for India and existing China operations are planned to be attained in 2011. Also for 2007 there is a charge of £11 million in respect of Vietnam for higher than expected investment fees payable on asset managers' performance, a credit of £4 million (2006: £18 million) in respect of the investment return on capital held centrally in respect of Taiwan and £14 million (2006: £11 million) of other charges.

6 Operating profit from business in force continued

Notes continued

iii US operations

The principal component of the £42 million credit in 2006 for other items is £31 million of favourable mortality experience variance.

iv UK insurance operations

a Effect of change in UK corporate tax rate

At 31 December 2007, a change to reduce the UK corporate tax rate from 30 per cent to 28 per cent in 2008 had been enacted in the legislative process. Accordingly, the 2007 results incorporate the effects of this change in projecting the tax cash flows attaching to in force business. Under the convention applied for EEV basis reporting, profits are generally determined on a post-tax basis and then grossed up at the prevailing corporate tax rates to derive pre-tax results. The effect of the change in the UK corporate tax rate is to give rise to a benefit to the value of business in force at 1 January 2007 of £48 million. After grossing up this amount for notional tax of £19 million, the effect on the pre-tax operating results based on longer-term investment returns for UK insurance operations for 2007 is a credit of £67 million.

b Annuity business

For UK insurance operations there is a net nil charge or credit for both the 2007 and 2006 results. However, the 2007 results for annuity business have been determined after a strengthening of explicit mortality assumptions and the release of excess margins in the aggregate liabilities that had previously been set aside as an indirect extra allowance for longevity related risks.

The overall impact of the assumption changes and release of margins for 2007 is as follows:

		£m
Strengthening of mortality assumptions[note 1]		(312)
Release of margins:		
Projected benefit related[note 2]	144	
Investment related[note 3]	82	
Expense related[note 4]	29	
Other[note 5]	57	
		312
		0

1 The mortality assumptions have been strengthened such that the previous future improvement assumptions of medium cohort for males and 75 per cent of medium cohort for females are now subject to a minimum level of improvement in future years.
2 The release of projected benefit related margins relates to modelling improvements that have been made during 2007 and the effect of hedging inflationary increases on certain deferred annuity business.
3 The release of investment related margins predominantly relates to £38 million in respect of default margins and £43 million for adjustments to the assumed liquidity premium. The resulting assumptions for expected defaults and liquidity premium, after allowing for the release of margins, remain appropriate given economic conditions at 31 December 2007.
4 A release of expense reserves has been made following recent expense reductions, on which the related cost of capital on the EEV basis is £29 million.
5 This amount reflects the release of other additional margins in the liabilities that are no longer appropriate in light of the explicit strengthening of the mortality assumptions.

c UK insurance operations other items represent:

	2007 £m	2006 £m
Cost of development of new products and distribution capabilities (and costs associated with regulatory requirements for 2006)	(36)	(32)
Annual licence fee payments[notes 1, 3]	(13)	(14)
Expense overruns in respect of tariff agreement with SAIF[notes 2, 3]	(14)	(16)
Adjustments to the policyholder and shareholder taxes for non-participating business of the PAC long-term fund, after grossing up for notional tax	–	(26)
Other items[note 4]	(14)	(22)
	(77)	(110)

1 The licence fee payments are made by shareholder-backed subsidiaries of UK insurance operations, via a service company, to the PAC with-profits fund for the right to use trademarks and for the goodwill associated with the purchase of the business of the Scottish Amicable Life Assurance Society in 1997. The licence fee arrangements run to 2017.
2 The charge of £14 million (2006: £16 million) in respect of SAIF, which is not covered business, is borne by a service company and arises from a tariff arrangement which ran to the end of 2007 and was onerous to shareholders.
3 Charges in respect of items 1 and 2 above are reflected in the EEV and IFRS results on an annual basis.
4 The charge for other items includes a positive persistency experience variance of £1 million (2006: negative variance of £9 million).

6 Operating profit from business in force continued

Notes continued

d Expense assumptions

The 2006 EEV basis financial statements included note disclosure which explained that in determining the appropriate expense assumptions account had been taken of the cost synergies that were expected to arise with some certainty from the initiative announced in December 2005 from UK insurance operations working more closely with Egg and M&G and the effect of the end to end review of the UK business, which was under way at the time.

On 29 January 2007 the Company announced the sale of Egg to Citi and on 15 March 2007 the Company announced the actions necessary to implement the reassessed plans in light of this transaction and additional initiatives. In preparing the 2006 results, account was taken of the effect of expense savings that were expected to arise with some certainty. Without this factor the effect on the 2006 results would have been a charge of £44 million for the net effect of revised assumptions in line with 2006 unit costs. For the 2007 results the unit costs are in line with assumptions and no anticipation of savings has been incorporated.

7 Investment return and other income

	2007 £m	2006 £m
IFRS basis	86	58
Less: allocation of investment return on centrally held capital in respect of Taiwan business to the operating result of Asian operations	(4)	(18)
Less: projected asset management result in respect of covered business incorporated in opening EEV value of in-force business	(37)	(32)
EEV basis	45	8

8 Restructuring costs

Restructuring costs have been incurred as follows:

	2007 £m	2006 £m
UK insurance operations	8	34
M&G	0	2
Unallocated corporate	12	5
Total	20	41

The charge of £20 million (2006: £41 million) comprises £19 million (2006: £38 million) recognised on the IFRS basis and an additional £1 million (2006: £3 million) recognised on the EEV basis for the shareholders' share of costs incurred by the PAC with-profits fund.

9 Short-term fluctuations in investment returns

	2007 £m	2006 £m
Long-term business:		
Asian operations[note i]	226	286
Jackson[note ii]	(9)	63
UK insurance operations[note iii]	(43)	378
Share of investment return of funds managed by PPM America that are consolidated into Group results but attributable to external investors	1	1
Share of profits of venture investment companies and property partnerships of the PAC with-profits fund that are consolidated into Group results but are attributable to external investors	1	0
Other operations[note iv]	(2)	10
Total	174	738

Notes

i The short-term fluctuations for Asian operations of £226 million (2006: £286 million) arose mainly from favourable equity investment performance in most territories, principally in Hong Kong of £102 million (2006: £73 million), Vietnam £66 million (2006: £108 million) and Singapore £38 million (2006: £41 million) offset by a negative fluctuation in Taiwan of £26 million principally due to a £30 million value reduction for an investment in a CDO fund (2006: favourable variance of £46 million).

Notes on the EEV basis supplementary information
continued

9 Short-term fluctuations in investment returns continued

Notes continued

ii Short-term fluctuations for Jackson comprise:

	2007 £m	2006 £m
Actual investment return on investments less long-term returns included within operating profit:		
Actual realised (losses) gains less default assumption and amortisation of interest-related realised gains and losses for fixed maturity securities and related swap transactions	(44)	20
Actual less long-term return on equity-based investments and other items	51	26
Investment return related (loss) gain due primarily to changed expectation of profits on in-force variable annuity business in future periods based on current period equity returns*, net of related hedging activity	(16)	17
	(9)	63

*This adjustment arises due to market returns being (lower) higher than the assumed long-term rate of return. This gives rise to (lower) higher than expected year end values of variable annuity assets under management with a resulting effect on the projected value of future account values, and hence future profitability.

iii The charge for UK insurance operations for 2007 of £43 million primarily reflects value movements on the bond holdings of PRIL's shareholders' funds due to the net effect of widened credit spreads and reduced interest rates together with the difference between the actual investment return for the with-profits life fund of 7.2 per cent and the gross long-term assumed rate of 7.85 per cent. For 2006, the credit of £378 million reflects the PAC life fund investment return of 12.4 per cent.

iv Comparative figures for 2006 have been adjusted from those previously published to exclude discontinued banking operations.

10 Mark to market value movements on core borrowings

	2007 £m	2006 £m
US operations	9	3
Other operations	214	82
Total	223	85

Core borrowings of the Group are marked to market value under EEV. The figures in the table above reflect the movement in the difference between market and IFRS carrying values. As the liabilities are generally held to maturity or for the long term, no deferred tax asset or liability has been established on the difference (compared to IFRS) in carrying value. Accordingly, no deferred tax charge is recorded in the results in respect of the 2007 credit of £223 million (2006: £85 million).

11 Actuarial gains and losses on defined benefit pension schemes

The gain of £116 million (2006: gain of £207 million) included within profit before tax reflects the shareholders' share of actuarial gains and losses on the Group's defined benefit pension schemes. On the EEV basis, this gain includes a 10 per cent share of the actuarial gains and losses on the share attributable to the PAC with-profits fund for the Prudential Staff and Scottish Amicable Pension Schemes. The 2007 gains mainly reflect gains due to changes in economic assumptions, partly offset by the effect of strengthened mortality assumptions. The very high level of shareholders' actuarial gains in 2006 reflected the excess of market returns over the long-term assumption and the increase in discount rate applied in determining the present value of projected pension payments from 4.8 per cent at 31 December 2005 to 5.2 per cent at 31 December 2006.

12 Effect of changes in economic assumptions and time value of cost of options and guarantees

The profits (losses) on changes in economic assumptions and time value of cost of options and guarantees resulting from changes in economic factors for in-force business included within the profit from continuing operations before tax (including actual investment returns) arise as follows:

	2007 £m			2006 £m		
	Change in economic assumptions	Change in time value of cost of options and guarantees	Total	Change in economic assumptions	Change in time value of cost of options and guarantees	Total
Asian operations[note i]	201	9	210	(132)	14	(118)
US operations[note ii]	81	8	89	(51)	6	(45)
UK insurance operations[note iii]	466	(17)	449	182	40	222
Total	748	0	748	(1)	60	59

12 Effect of changes in economic assumptions and time value of cost of options and guarantees continued

Notes

i The principal components of the effect of changes in economic assumptions in 2007 of £201 million for Asian operations are credits of £110 million in Taiwan and £80 million in Hong Kong. The increase for Taiwan reflects the combined effect of changes to the projected fund earned rate (as explained in note 3), and to economic capital (versus projected), offset by the effect of an increase in the risk discount rate. The increase for Hong Kong reflects a reduction in the risk discount rate for all product lines and an increase in the projected fund earned rate for participating and linked business. The charge of £132 million for 2006 mainly relates to Taiwan where there was a charge of £101 million arising from the delay in the assumed long-term yield projection and the associated effect of this delay on the economic capital requirement.

ii The credit of £81 million for US operations in 2007 arises from the decrease in risk discount rate, partially offset by the negative effect of a reduction in the assumed future rate of return for separate account variable annuity business. Both changes reflect the 0.7 per cent decrease in the 10-year treasury bond rate (as shown in note 3).

iii The effect of changes in economic assumptions in 2007 of £466 million for UK insurance operations reflects a 0.35 per cent increase in the fund earned rate arising from the increase in assumed returns on non-UK equities and corporate bond rates which more than offsets the slight reduction in gilt rates (as shown in note 3), a partial offset from the cost of credit default swaps of £41 million and the effect of the risk discount rate for business in force reducing slightly by 0.15 per cent in a similar way to the fall in gilt rates as also shown in note 3.

13 Tax attributable to shareholders' profit

The tax charge comprises:

	2007 £m	2006 £m
Tax charge (credit) on operating profit from continuing operations based on longer-term investment returns		
Long-term business:[note i]		
Asian operations[notes ii,iii]	252	222
US operations[note v]	197	251
UK insurance operations[notes ii,iii]	236	178
	685	651
Other operations	9	(17)
Total tax charge on operating profit from continuing operations based on longer-term investment returns	694	634
Tax charge (credit) on items not included in operating profit		
Tax charge on short-term fluctuations in investment returns	22	212
Tax charge on shareholders' share of actuarial gains and losses on defined benefit pension schemes	32	62
Tax charge (credit) on effect of changes in economic assumptions and time value of cost of options and guarantees[note iv]	213	(4)
Total tax charge on items not included in operating profit from continuing operations	267	270
Tax charge on profit from continuing operations (including tax on actual investment returns)[note vi]	961	904

Notes

i The profit for the year for covered business is in most cases calculated initially at the post-tax level. The post-tax profit for covered business is then grossed up for presentation purposes at the effective rates of tax applicable to the countries and periods concerned. For Asia, this is subject to the availability of taxable profits. For Jackson, the US federal tax rate of 35 per cent is applied to gross up movements on the value of in-force business. Effects on statutory tax for the period affect the overall tax rate. In the UK, the effective rate is the UK corporation tax rate of 28 per cent which will take effect from 1 April 2008 (2006: 30 per cent).

ii Including tax relief on Asia development expenses and restructuring costs borne by UK insurance operations.

iii The 2007 tax charge incorporates the notional tax gross up of £26 million attaching to the change of corporate tax rates in China, Malaysia, Singapore and the UK as detailed in notes 6[ii a] and 6[iv a].

iv The tax credit for 2006 on the effect of changes in economic assumptions includes a credit of £9 million in respect of a change in the tax rate for Malaysia.

v The 2006 tax charge for US operations of £251 million includes a charge in respect of prior years of £29 million and a charge of £26 million in respect of a change in valuation of deferred tax under EEV to reflect discounting over a period of four to 11 years depending upon the type of business concerned. These adjustments also resulted in a reallocation from free surplus to the value of in-force business of £44 million.

vi Comparative results for 2006 have been adjusted from those previously published to exclude discontinued banking operations.

Notes on the EEV basis supplementary information
continued

14 Earnings per share (EPS)

	2007 £m	2006 £m
Operating EPS from continuing operations:		
Operating profit before tax	2,542	2,133
Tax	(694)	(634)
Minority interests	(17)	(1)
Operating profit after tax and minority interests from continuing operations	1,831	1,498
Operating EPS from continuing operations	74.9p	62.1p
Total EPS from continuing operations:		
Total profit before tax	3,803	3,222
Tax	(961)	(904)
Minority interests	(21)	(3)
Total profit after tax and minority interests from continuing operations	2,821	2,315
Total EPS from continuing operations	115.3p	96.0p
Average number of shares (millions)	2,445	2,413

The average number of shares reflects the average number in issue adjusted for shares held by employee trusts and consolidated unit trusts and OEICs which are treated as cancelled.

15 Shareholders' funds – segmental analysis

	2007 £m	2006 £m
Asian operations		
Long-term business:[note i]		
Net assets of operations – EEV basis shareholders' funds	3,726	2,548
Acquired goodwill[note ii]	111	111
Asset management:[note iii]		
Net assets of operations	111	89
Acquired goodwill[note ii]	61	61
	4,009	2,809
US operations		
Jackson (net of surplus note borrowings of £147m (2006: £158m):[note iv]		
Shareholders' funds before capital charge	3,689	3,420
Capital charge[note v]	(84)	(117)
EEV basis shareholders' funds	3,605	3,303
Broker-dealer and asset management operations[note iii]	81	57
	3,686	3,360
UK operations		
Long-term business operations:[notes i,vi]		
Smoothed shareholders' funds[note vii]	6,031	5,155
Actual shareholders' funds less smoothed shareholders' funds	466	658
EEV basis shareholders' funds	6,497	5,813
M&G:[note iii]		
Net assets of operations	271	230
Acquired goodwill[note ii]	1,153	1,153
Egg[notes iii,viii]	–	292
	7,921	7,488
Other operations		
Holding company net borrowings at market value[note iv]	(873)	(1,542)
Other net assets (liabilities)[note iii]	36	(232)
	(837)	(1,774)
Total	14,779	11,883

15 Shareholders' funds – segmental analysis continued

Notes

i A charge is deducted from the annual result and embedded value for the cost of capital supporting the Group's long-term business operations. This capital is referred to as encumbered capital. The cost is the difference between the nominal value of the capital and the discounted value of the projected releases of this capital allowing for investment earnings (net of tax) on the capital. Where encumbered capital is held within a with-profits fund, the value placed on surplus assets in the fund is already discounted to reflect its release over time and no further adjustment is necessary in respect of encumbered capital.

ii Under IFRS, goodwill is not amortised but is subject to impairment testing. Goodwill attaching to venture fund investment subsidiaries of the PAC with-profits fund that are consolidated under IFRS is not included in the table above as the goodwill attaching to these companies is not relevant to the analysis of shareholders' funds.

iii With the exception of the share of pension scheme surplus attributable to the PAC with-profits fund which is included in Other operations' net assets (liabilities), and the borrowings as described in note iv, the amounts shown for the items in the table above that are referenced to this note have been determined on the statutory IFRS basis. The overall pension scheme surplus, net of tax, attributable to shareholders relating to the Prudential Staff Pension and Scottish Amicable Pension Schemes are determined as shown below:

	2007 £m	2006 £m
IFRS basis surplus (relating to shareholder-backed operations)	98	19
Additional EEV surplus (relating to shareholders' 10 per cent share of the IFRS basis surplus (deficit) attributable to the PAC with-profits fund)	31	6
EEV basis	129	25

iv Net core structural borrowings of shareholder-financed operations comprise:

	IFRS basis 2007 £m	Mark to market value adjustment £m	EEV basis 2007 £m	IFRS basis 2006 £m	Mark to market value adjustment 2006 £m	EEV basis 2006 £m
Holding company* cash and short-term investments	1,456	–	1,456	1,119	–	1,119
Core structural borrowings – central funds (at market value)	(2,367)	38	(2,329)	(2,485)	(176)	(2,661)
Holding company net borrowings	(911)	38	(873)	(1,366)	(176)	(1,542)
Core structural borrowings – Jackson (at market value)	(125)	(22)	(147)	(127)	(31)	(158)
	(1,036)	16	(1,020)	(1,493)	(207)	(1,700)

*Including central finance subsidiaries.
In accordance with the EEV Principles, core borrowings are carried at market value.

v In determining the cost of capital for Jackson, it has been assumed that an amount at least equal to 235 per cent of the risk-based capital required by the National Association of Insurance Commissioners (NAIC) at the Company Action Level must be retained. The impact of the related capital charge is to reduce Jackson's shareholders' funds by £84 million (2006: £117 million).

vi The proportion of surplus allocated to shareholders from the UK with-profits business has been based on the present level of 10 per cent. Future bonus rates have been set at levels which would fully utilise the assets of the with-profits fund over the lifetime of the business in force.

vii UK long-term business smoothed shareholders' funds reflect an adjustment to the assets of the PAC with-profits fund, for the purposes of determining the unwind of discount included in operating profits, to remove the short-term volatility in market values of assets. Shareholders' funds in the balance sheet are determined on an unsmoothed basis.

viii On 1 May 2007, the Company sold Egg.

16 Reconciliation of movement in shareholders' funds

	2007 £m					
	Long-term business operations					
	Asian operations	US operations	UK insurance operations	Total long-term business operations	Other operations	Group total
Operating profit from continuing operations (based on longer-term investment returns)						
Long-term business:						
New business[5]	653	285	277	1,215		1,215
Business in force[6]	393	342	582	1,317		1,317
	1,046	627	859	2,532		2,532
Asia development expenses	(15)			(15)		(15)
M&G					254	254
Asian asset management operations					72	72
US broker-dealer and asset management					13	13
Curian					(5)	(5)
Other income and expenditure					(289)	(289)
Restructuring costs[8]			(8)	(8)	(12)	(20)
Operating profit from continuing operations based on longer-term investment returns	1,031	627	851	2,509	33	2,542
Short-term fluctuations in investment returns[9]	226	(9)	(42)	175	(1)	174
Mark to market value movements on core borrowings[10]		9		9	214	223
Shareholders' share of actuarial gains and losses on defined benefit pension schemes[11]					116	116
Effect of changes in economic assumptions and time value of cost of options and guarantees[12]	210	89	449	748		748
Profit from continuing operations before tax (including actual investment returns)	1,467	716	1,258	3,441	362	3,803
Tax (charge) credit attributable to shareholders' profit:[13]						
Tax on operating profit	(252)	(197)	(236)	(685)	(9)	(694)
Tax on short-term fluctuations in investment returns	(43)	3	12	(28)	6	(22)
Tax on shareholders' share of actuarial gains and losses on defined benefit pension schemes					(32)	(32)
Tax on effect of changes in economic assumptions and time value of cost of options and guarantees	(56)	(31)	(126)	(213)		(213)
Total tax charge	(351)	(225)	(350)	(926)	(35)	(961)
Discontinued operations, net of tax					241	241
Minority interests	(15)		(1)	(16)	(5)	(21)
Profit for the year	1,101	491	907	2,499	563	3,062
Unrealised valuation movements on Egg securities classified as available-for-sale					(2)	(2)
Movement on cash flow hedges					(3)	(3)
Exchange movements[note i]	80	(53)		27	37	64
Related tax					3	3
Intra group dividends (including statutory transfer)	(98)	(123)	(286)	(507)	507	
External dividends					(426)	(426)
Reserve movements in respect of share-based payments					18	18
Investment in operations[note ii]	103		95	198	(198)	
Other transfers[note iv]	(8)	0	(32)	(40)	40	
Movement in own shares in respect of share-based payment plans					7	7
Movement on Prudential plc shares purchased by unit trusts consolidated under IFRS					4	4
New share capital subscribed					182	182
Mark to market value movements on Jackson assets backing surplus and required capital		(13)		(13)		(13)
Net increase in shareholders' equity	1,178	302	684	2,164	732	2,896
Shareholders' equity at 1 January 2007	2,548	3,303	5,813	11,664	219	11,883
Shareholders' equity at 31 December 2007[note iii,15]	3,726	3,605	6,497	13,828	951	14,779

16 Reconciliation of movement in shareholders' funds continued

Notes

i Profits are translated at average exchange rates, consistent with the method applied for statutory IFRS basis results. The amounts recorded above for exchange rate movements reflect the difference between 2006 and 2007 exchange rates as applied to shareholders' funds at 1 January 2007 and the difference between 31 December 2007 and average 2007 rates for profits.

ii Investment in operations reflects increases in share capital. This includes certain non-cash items as a result of timing differences.

iii For the purposes of the table above, goodwill related to Asia long-term operations (as shown in note 15) is included in Other operations.

iv Other transfers (from) to long-term business operations to other operations represent:

	Asian operations £m	US operations £m	UK insurance operations £m	Total long-term business operations £m
Adjustment for net of tax asset management projected profits of covered business	(9)	(2)	(16)	(27)
Adjustment for investment return, net of related tax, on economic capital for Taiwan operations held centrally	(3)			(3)
Other adjustments	4	2	(16)	(10)
	(8)	0	(32)	(40)

EEV basis shareholders' equity at 31 December 2007	Long-term business operations: Asian operations £m	US operations £m	UK insurance operations £m	Total long-term business operations £m	Other operations £m	Group total £m
Analysed as:						
Statutory IFRS basis shareholders' equity	1,258	2,690	1,364	5,312	889	6,201
Additional retained profit on an EEV basis	2,468	915	5,133	8,516	62	8,578
EEV basis shareholders' equity at 31 December 2007	3,726	3,605	6,497	13,828	951	14,779
Comprising:						
Free surplus	49	1,147	272	1,468		
Required capital	907	1,072	891	2,870		
Value of in-force business before deduction of cost of capital and of guarantees	3,245	1,612	5,641	10,498		
Cost of capital	(472)	(84)	(251)	(807)		
Cost of time value of guarantees	(3)	(142)	(56)	(201)		
	3,726	3,605	6,497	13,828		

EEV basis shareholders' equity at 1 January 2007	Long-term business operations: Asian operations £m	US operations £m	UK insurance operations £m	Total long-term business operations £m	Other operations £m	Group total £m
Analysed as:						
Statutory IFRS basis shareholders' equity	1,176	2,656	1,263	5,095	393	5,488
Additional retained profit on an EEV basis	1,372	647	4,550	6,569	(174)	6,395
EEV basis shareholders' equity at 1 January 2007	2,548	3,303	5,813	11,664	219	11,883
Comprising:						
Free surplus	(42)	910	147	1,015		
Required capital	962	1,073	831	2,866		
Value of in-force business before deduction of cost of capital and of guarantees	2,156	1,578	5,129	8,863		
Cost of capital	(521)	(117)	(254)	(892)		
Cost of time value of guarantees	(7)	(141)	(40)	(188)		
	2,548	3,303	5,813	11,664		

Notes on the EEV basis supplementary information
continued

17 Reconciliation of net worth and value of in-force business

Reconciliation of net worth and value of in-force business for 2007 note i	Free surplus note vii	Required capital	Total net worth note iv	Value of in-force business note viii	Total long-term business
	2007 £m				
Shareholders' equity at 1 January 2007 note ix	1,015	2,866	3,881	7,783	11,664
New business contribution notes ii,iii	(544)	308	(236)	1,101	865
Existing business – transfer to net worth note v	963	(225)	738	(738)	0
Other movements note vi					
Expected return on existing business note vi	99	48	147	706	853
Changes in operating assumptions and experience variances note vi	89	(24)	65	41	106
Changes in non-operating assumptions and experience variances and minority interests note vi	136	(77)	59	616	675
	324	(53)	271	1,363	1,634
Profit for the year from long-term business operations	743	30	773	1,726	2,499
Exchange movements	9	(26)	(17)	44	27
Intra-group dividends (including statutory transfer) and investment in operations	(246)	–	(246)	(63)	(309)
Mark to market value movements on Jackson assets backing surplus and required capital	(13)	–	(13)	–	(13)
Other transfers from net worth note x	(40)	–	(40)	–	(40)
Shareholders' equity at 31 December 2007 note ix	1,468	2,870	4,338	9,490	13,828

Notes

i All figures are shown net of tax.

ii The movements arising from new business contribution are as follows:

	2007 note iii £m	2006 £m
Free surplus	(544)	(554)
Required capital	308	383
Total net worth	(236)	(171)
Value of in-force business	1,101	898
Total long-term business [5]	865	727

iii The new business contribution arises as follows:

	Free surplus note vii £m	Required capital £m	Total net worth note iv £m	Value of in-force business note viii £m	Total long-term business £m
Asian operations	(194)	21	(173)	653	480
US operations	(200)	183	(17)	202	185
UK insurance operations	(150)	104	(46)	246	200
	(544)	308	(236)	1,101	865

iv Net worth is based on statutory solvency capital (or economic capital where higher) and unencumbered capital.

v Existing business transfer to net worth

	Free surplus note vii £m	Required capital £m	Total net worth note iv £m	Value of in-force business note viii £m	Total long-term business £m
Asian operations	216	(27)	189	(189)	0
US operations	326	(178)	148	(148)	0
UK insurance operations	421	(20)	401	(401)	0
	963	(225)	738	(738)	0

17 Reconciliation of net worth and value of in-force business continued

vi Other movements

	Free surplus note vii £m	Required capital £m	Total net worth note iv £m	Value of in-force business note viii £m	Total long-term business £m
Asian operations					
Expected return on existing business	28	9	37	231	268
Changes in operating assumptions and experience variances	(61)	2	(59)	90	31
Changes in non-operating assumptions and experience variances and minority interests	83	(52)	31	291	322
	50	(41)	9	612	621
US operations					
Expected return on existing business	34	40	74	82	156
Changes in operating assumptions and experience variances	194	(28)	166	(77)	89
Changes in non-operating assumptions and experience variances and minority interests	32	0	32	29	61
	260	12	272	34	306
UK insurance operations					
Expected return on existing business	37	(1)	36	393	429
Changes in operating assumptions and experience variances	(44)	2	(42)	28	(14)
Changes in non-operating assumptions and experience variances and minority interests	21	(25)	(4)	296	292
	14	(24)	(10)	717	707
Total long-term business					
Expected return on existing business	99	48	147	706	853
Changes in operating assumptions and experience variances	89	(24)	65	41	106
Changes in non-operating assumptions and experience variances and minority interests	136	(77)	59	616	675
	324	(53)	271	1,363	1,634

vii Movements in free surplus arising from profit for the year from long-term business operations are as follows:

	Cost of acquiring new business note iii £m	Total in-force transfer to net worth note v £m	Other movements note vi £m	Increase in free surplus arising from profit in the year £m
Asian operations	(194)	216	50	72
US operations	(200)	326	260	386
UK insurance operations	(150)	421	14	285
	(544)	963	324	743

viii Value of in-force business includes the value of future margins from current in-force business less the cost of holding encumbered capital.

ix Included in the EEV basis shareholders' funds of long-term business operations of £13,828 million (2006: £11,664 million) is £349 million (2006: £257 million) in respect of asset management business falling within the scope of covered business as follows:

	2007 £m	2006 £m
Asian operations	**204**	120
US operations	**12**	12
UK insurance operations	**133**	125
	349	257

x Other transfers from net worth

	2007 16iv £m
Adjustment for net of tax asset management projected profits of covered business	(27)
Adjustment for investment return, net of related tax, on economic capital for Taiwan operations held centrally	(3)
Other adjustments	(10)
	(40)

Notes on the EEV basis supplementary information
continued

18 Sensitivity of results to alternative assumptions

a Sensitivity analysis – economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2007 (31 December 2006) and the new business contribution after the effect of encumbered capital for 2007 and 2006 to:

— One per cent increase in the discount rates;
— one per cent increase and decrease in interest rates, including all consequential changes (assumed investment returns for all asset classes, market values of fixed interest assets, risk discount rates);
— one per cent rise in equity and property yields;
— 10 per cent fall in market value of equity and property assets (not applicable for new business contribution); and
— holding company statutory minimum capital (by contrast to economic capital).

In each sensitivity calculation, all other assumptions remain unchanged except where they are directly affected by the revised economic conditions.

	2007 £m			
	Asian operations	US operations	UK insurance operations	Total long-term business operations
New business profit for 2007				
As reported[5]	653	285	277	1,215
Discount rates – 1% increase	(77)	(29)	(36)	(142)
Interest rates – 1% increase	(16)	5	(5)	(16)
Interest rates – 1% decrease	13	(18)	5	0
Equity/property yields – 1% rise	33	30	15	78
Embedded value of long-term operations at 31 December 2007				
As reported[16]	3,726	3,605	6,497	13,828
Discount rates – 1% increase	(386)	(129)	(534)	(1,049)
Interest rates – 1% increase[note i]	(29)	(120)	(95)	(244)
Interest rates – 1% decrease[note i]	2	17	113	132
Equity/property yields – 1% rise	234	58	405	697
Equity/property market values – 10% fall	(136)	(63)	(519)	(718)
Statutory minimum capital	315	59	8	382

	2006 £m			
	Asian operations	US operations	UK insurance operations	Total long-term business operations
New business profit for 2006				
As reported[5]	514	259	266	1,039
Discount rates – 1% increase	(56)	(28)	(46)	(130)
Interest rates – 1% increase	(9)	3	4	(2)
Interest rates – 1% decrease	7	(17)	(11)	(21)
Equity/property yields – 1% rise	23	28	16	67
Embedded value of long-term operations at 31 December 2006				
As reported[16]	2,548	3,303	5,813	11,664
Discount rates – 1% increase	(271)	(127)	(480)	(878)
Interest rates – 1% increase[notes i,ii]	42	(190)	(66)	(214)
Interest rates – 1% decrease[notes i,ii]	(115)	116	69	70
Equity/property yields – 1% rise	154	46	382	582
Equity/property market values – 10% fall	(99)	(58)	(502)	(659)
Statutory minimum capital	391	82	8	481

18 Sensitivity of results to alternative assumptions continued

Notes

i Asian operations

2007	Embedded value of long-term operations £m	Interest rates 1% increase £m	Interest rates 1% decrease £m
Asian operations			
Established markets	2,704	(77)	83
Taiwan*	(12)	67	(91)
Korea	304	(7)	7
Vietnam	234	(5)	5
Other	496	(7)	(2)
	3,726	(29)	2

* Taiwan sensitivity to starting bond rate (i.e. the starting bond rate for the progression to the assumed long-term rate):

	Embedded value at 31 Dec 2007 £m	1% increase in the starting bond rate £m	1% decrease in the starting bond rate £m
Taiwan	(12)	73	(57)

If it had been assumed in preparing the 2007 results for Taiwan that interest rates remained at the current level of around 2.5 per cent until 31 December 2008 and the progression period in bond yields was delayed by a year so as to end on 31 December 2014, there would have been a reduction in the Taiwan embedded value of £70 million.

2006	Embedded value of long-term operations £m	Interest rates 1% increase £m	Interest rates 1% decrease £m
Asian operations			
Established markets	2,039	(55)	45
Taiwan*	(216)	107	(165)
Korea	191	(5)	5
Vietnam	198	(1)	1
Other	336	(4)	(1)
	2,548	42	(115)

* Taiwan sensitivity to starting bond rate (i.e. the starting bond rate for the progression to the assumed long-term rate):

	Embedded value at 31 Dec 2006 £m	1% increase in the starting bond rate £m	1% decrease in the starting bond rate £m
Taiwan	(216)	116	(125)

ii UK insurance operations
2006 comparatives for the sensitivity to interest rate changes have been adjusted from previously published data for the effect of revisions to the calculation for the with-profits fund.

b Sensitivity analysis – non-economic assumptions

The tables below show the sensitivity of the embedded value as at 31 December 2007 (31 December 2006) and the new business contribution after the effect of encumbered capital for 2007 and 2006 to:

— 10 per cent proportionate decrease in maintenance expenses (a 10 per cent sensitivity on a base assumption of £10 per annum would represent an expense assumption of £9 per annum);
— 10 per cent proportionate decrease in lapse rates (a 10 per cent sensitivity on a base assumption of five per cent would represent a lapse rate of 4.5 per cent per annum); and
— five per cent proportionate decrease in base mortality and morbidity rates (i.e. increased longevity).

	2007 £m			
	Asian operations	US operations	UK insurance operations	Total long-term business operations
New business profit for 2007				
As reported[5]	653	285	277	1,215
Maintenance expenses – 10% decrease	20	6	8	34
Lapse rates – 10% decrease	62	19	8	89
Mortality and morbidity – 5% decrease	21	4	(14)	11
Change representing effect on:				
Life business	21	4	0	25
Annuity business	0	0	(14)	(14)
Embedded value of long-term operations at 31 December 2007				
As reported[16]	3,726	3,605	6,497	13,828
Maintenance expenses – 10% decrease	54	30	36	120
Lapse rates – 10% decrease	142	123	87	352
Mortality and morbidity – 5% decrease	98	74	(103)	69
Change representing effect on:				
Life business	98	74	9	181
Annuity business	0	0	(112)	(112)

	2006 £m			
	Asian operations	US operations	UK insurance operations	Total long-term business operations
New business profit for 2006				
As reported[5]	514	259	266	1,039
Maintenance expenses – 10% decrease	13	6	10	29
Lapse rates – 10% decrease	42	21	8	71
Mortality and morbidity – 5% decrease	14	6	(27)	(7)
Change representing effect on:				
Life business	14	6	1	21
Annuity business	0	0	(28)	(28)
Embedded value of long-term operations at 31 December 2006				
As reported[16]	2,548	3,303	5,813	11,664
Maintenance expenses – 10% decrease	45	32	33	110
Lapse rates – 10% decrease	93	110	75	278
Mortality and morbidity – 5% decrease	77	75	(87)	65
Change representing effect on:				
Life business	77	75	7	159
Annuity business	0	0	(94)	(94)