



**PRUDENTIAL**

# M&G OVERVIEW

Michael McLintock, Chief Executive, M&G



# DRIVERS OF FUND MANAGEMENT VALUE

## A relatively simple business

---

### Investment performance

41% of M&G funds top quartile over last 3 years

24% of M&G's equity funds top decile over last 3 years

### Net sales

Record net sales in 2005 of £3.9 billion

45% of last year's net sales achieved in Q1 2006

### Profits

Underlying profits up 150% since 2001

Underlying profits in Q1 2006 up 42% on Q1 2005



M&G performing exceptionally

---

# DELIVERING PERFORMANCE AND PROFITS

## Why is M&G consistently delivering?

---

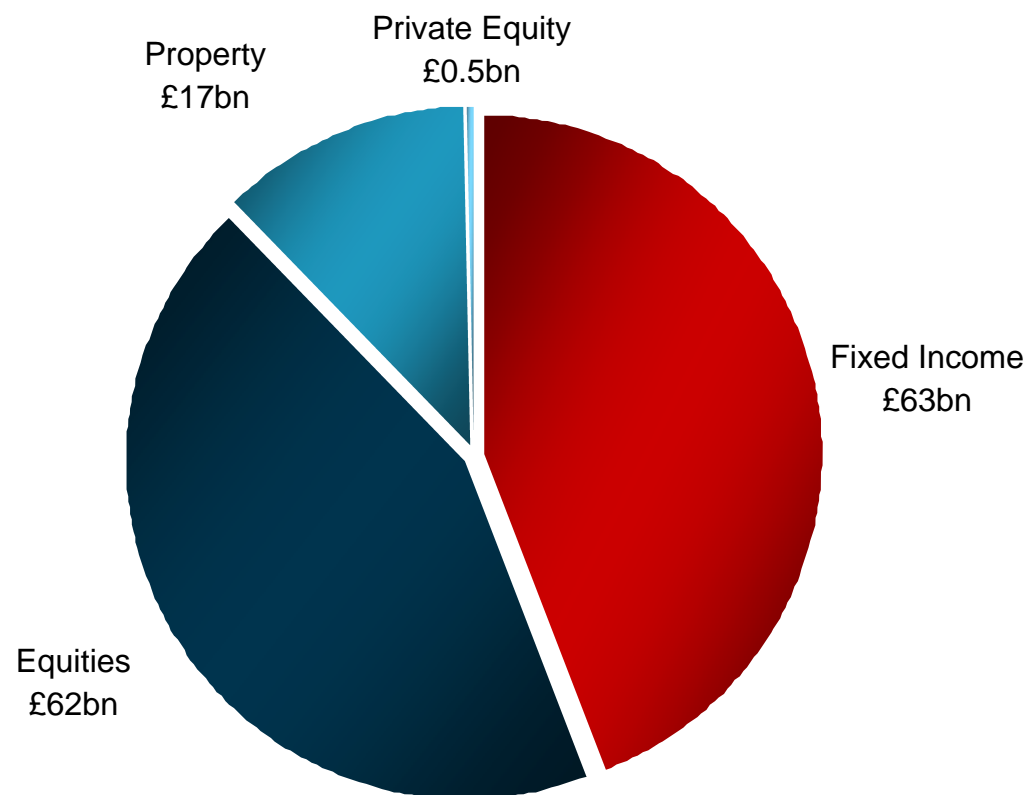
- Attraction and retention of good people
- Investment-led culture
- Devolved management structure
- Entrepreneurial environment
- Well diversified business model

# M&G'S MARKET POSITION

## Significant market share

---

### £149BN ASSETS UNDER MANAGEMENT



- One of the largest fixed income managers in the UK
- Largest active equity manager in the UK (own 2.3% of the UK stock market)
- One of the top two institutional property investors in the UK

# INDUSTRY THEMES

## Some opportunities and challenges

---

### Challenges

- Demand for alpha
- Demand for non-correlated returns
- Boutiques and hedge funds
- Intermediation

### Opportunities

- Shift from opaque to transparent savings vehicles
- Concentration of fund flows
- Open architecture
- Portability of product

# M&G'S STRATEGY

## Distinct strategies for different types of business

---

### Internal

Create value through investment performance and liability matching

Develop skills to facilitate life fund's move into non-correlated assets

### Institutional

Utilise skills developed primarily for internal client to build new business streams and diversify revenues

### Retail

Maximise the leverage offered by investment performance and a single manufacturing hub

### Prudential Finance

Combining the management of Prudential's balance sheet with M&G's market positions to develop a new profit stream

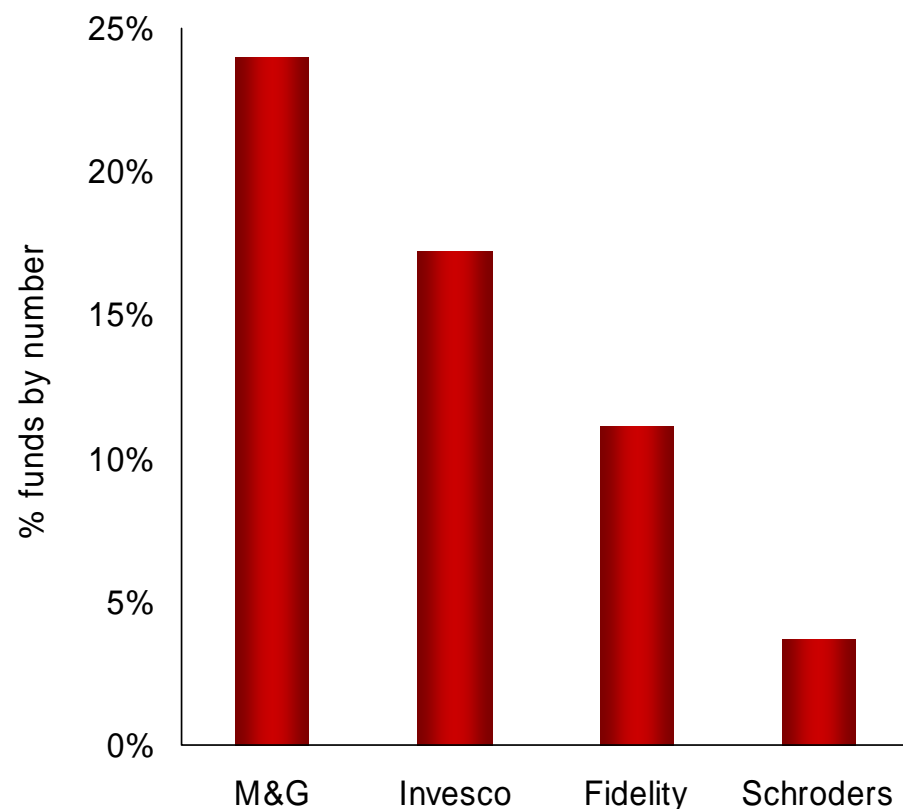
---

# THE RETAIL OPPORTUNITY

## Exceptional performance relative to the competition

---

### PERCENTAGE OF EQUITY FUNDS IN TOP DECILE OVER THREE YEARS



“...without wishing to be too melodramatic about things, there are few investment houses that can currently touch M&G”

*Jeff Prestridge, Bloomberg Money, May 2006*

# **M&G IS PERFORMING EXCEPTIONALLY**

## **Firing on all cylinders**

---

- Reaping the benefits of a consistent, long-term strategy
- Potent combination of exceptional performance and strong profit growth
- Firing on all cylinders





**PRUDENTIAL**

# PHILIP JOHNSON

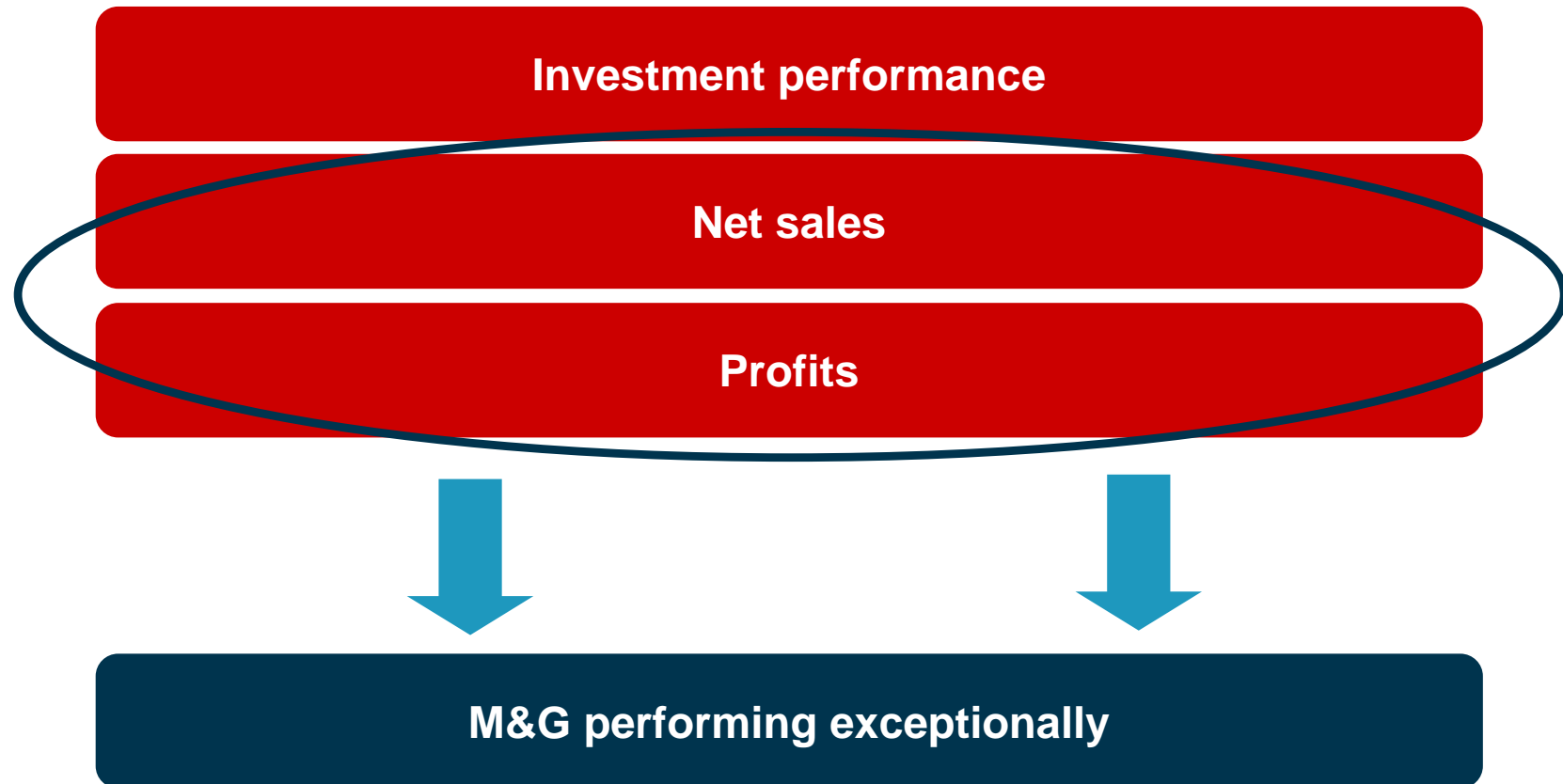
**M&G Group Finance Director**



# OVERVIEW

## Drivers of fund management value

---




# PROFITS

## Significant increase at similar market levels

---

	2001 £m	2002 £m	2003 £m	2004 £m	2005 £m
Underlying profit	56	49	70	110	138
Performance related fees	19	20	8	6	8
Carried interest	-	2	5	20	17
<b>Profit before tax</b>	<b>75</b>	<b>71</b>	<b>83</b>	<b>136</b>	<b>163</b>
Average FTAS	2614	2221	1978	2250	2589

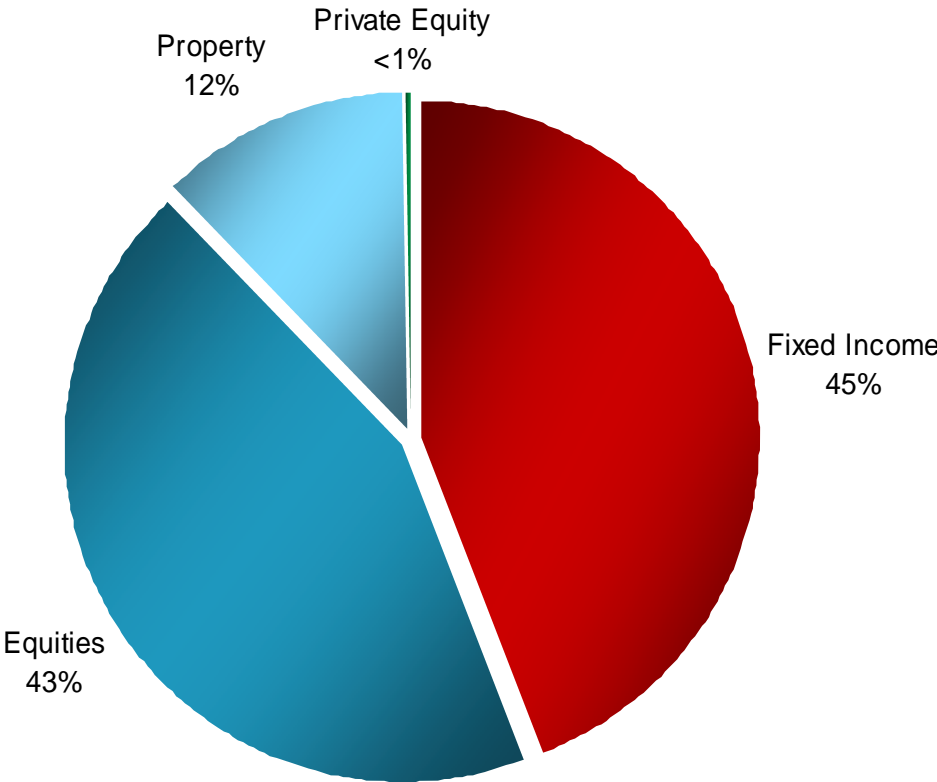


# REVENUES

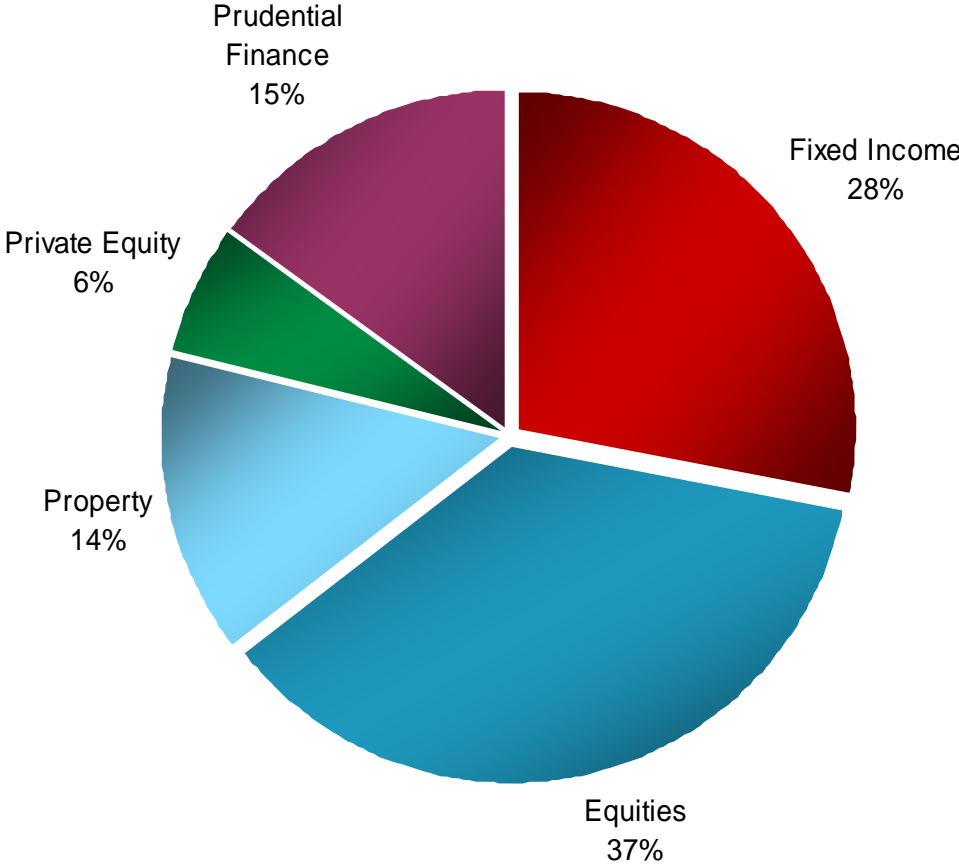
## Broad diversification

---

### FUNDS UNDER MANAGEMENT



### REVENUES

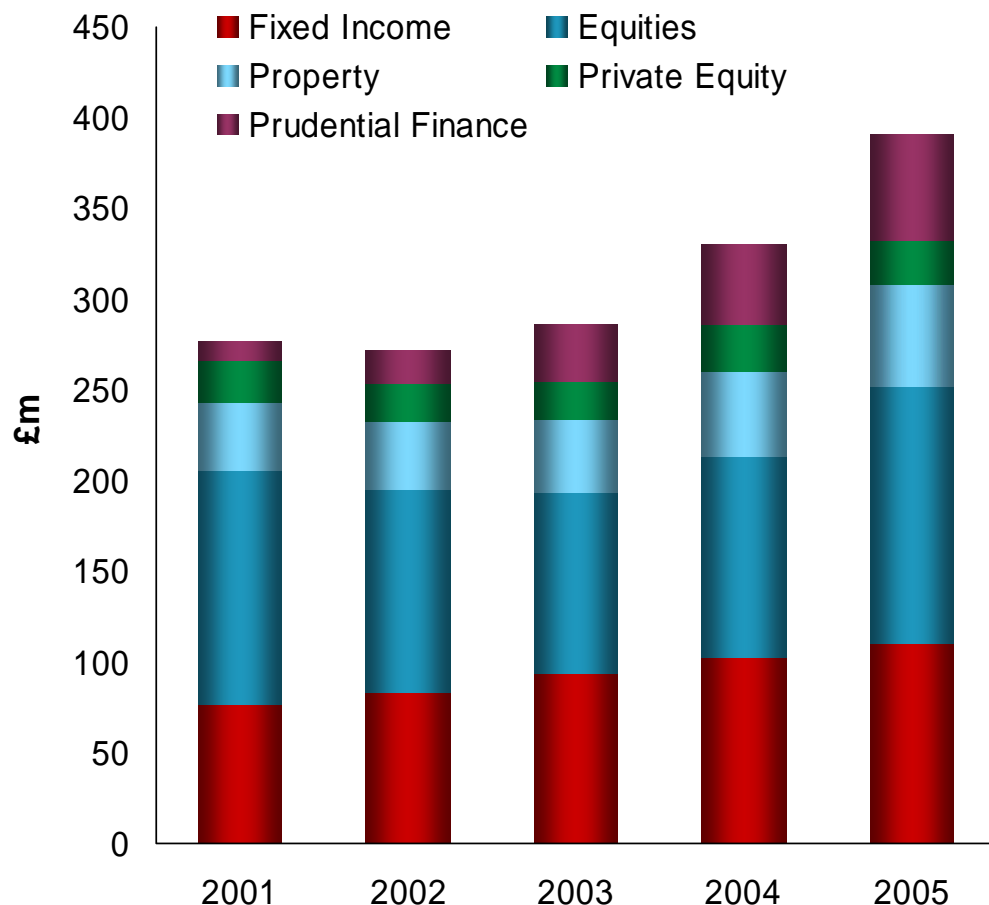


# REVENUE PROGRESSION

## Growing faster than underlying markets

---

### REVENUES BY ASSET CLASS

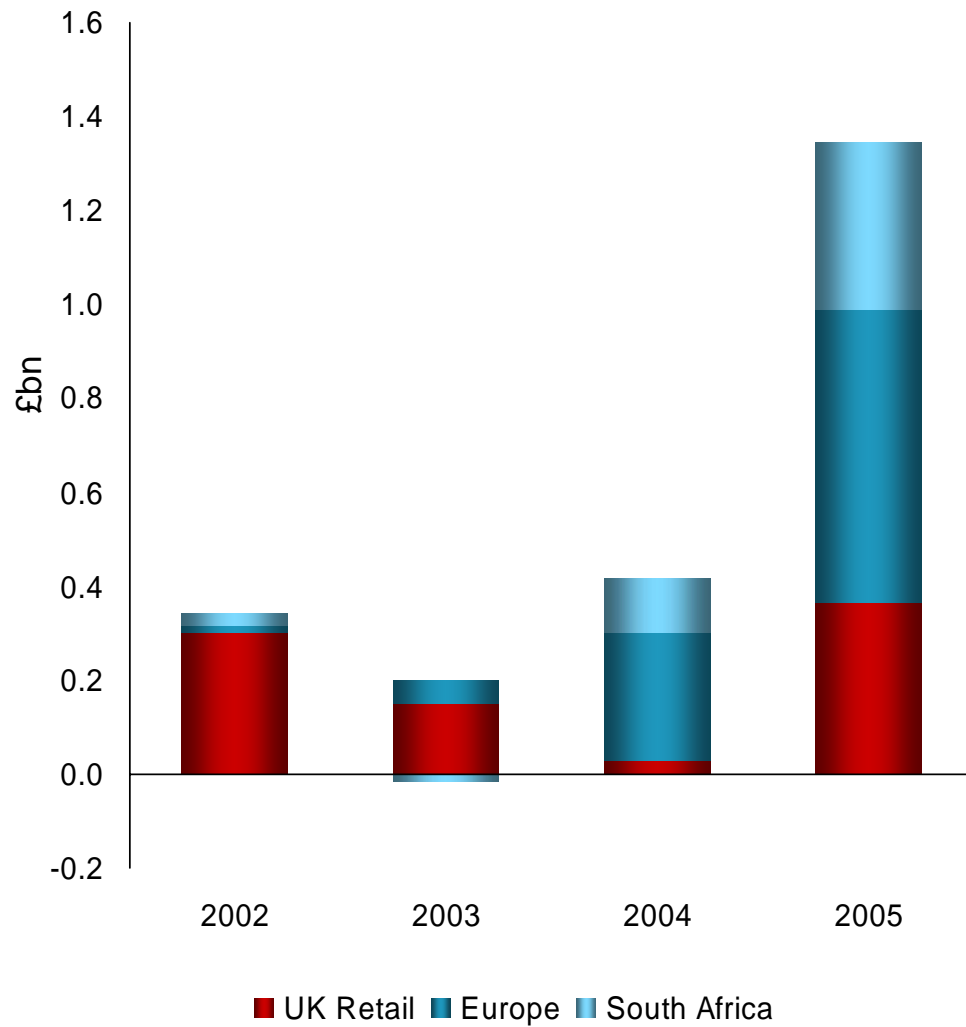


- Market appreciation across all asset classes in 2004 and 2005
- Expansion of Prudential Finance and Securities Lending activities
- Increased retail and pooled fees
- Net new business in all areas accelerating progress

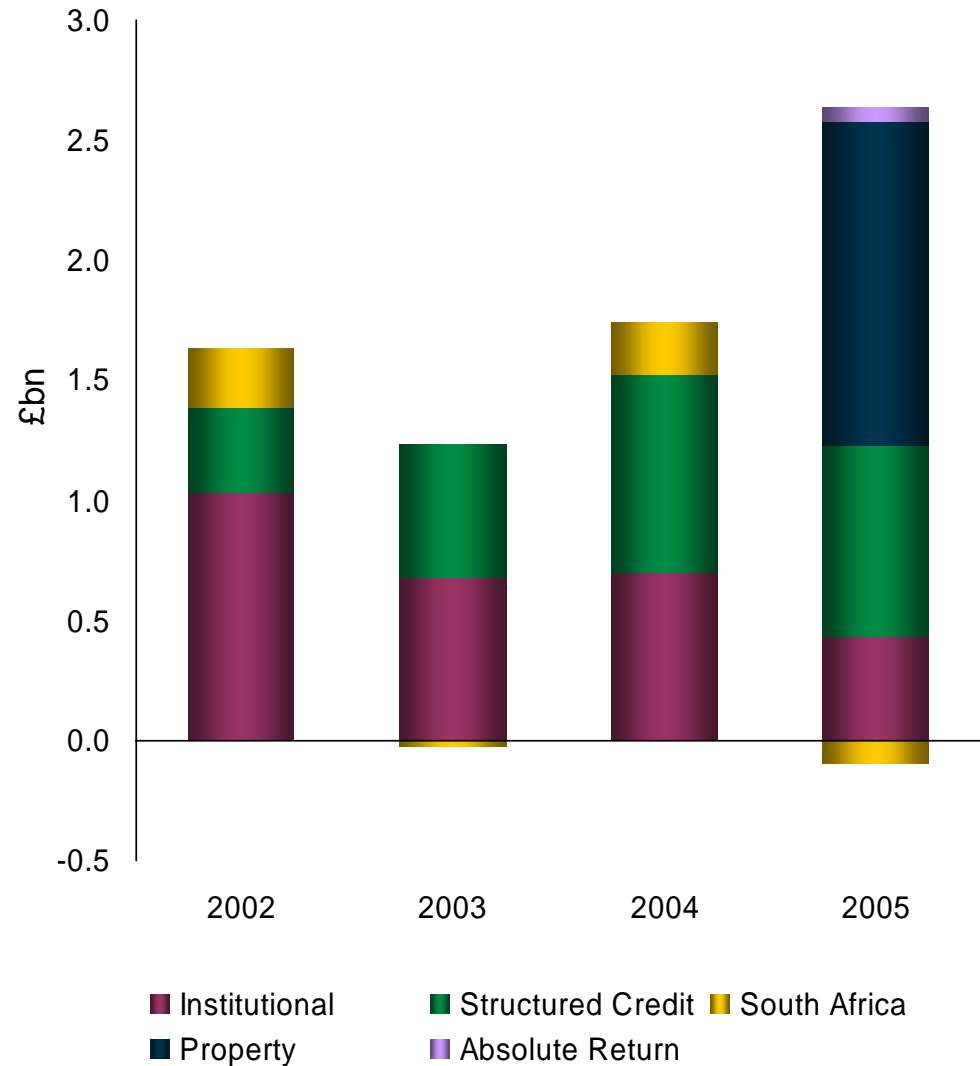
# NET NEW BUSINESS

## Strong progression

### NET RETAIL SALES



### NET INSTITUTIONAL SALES

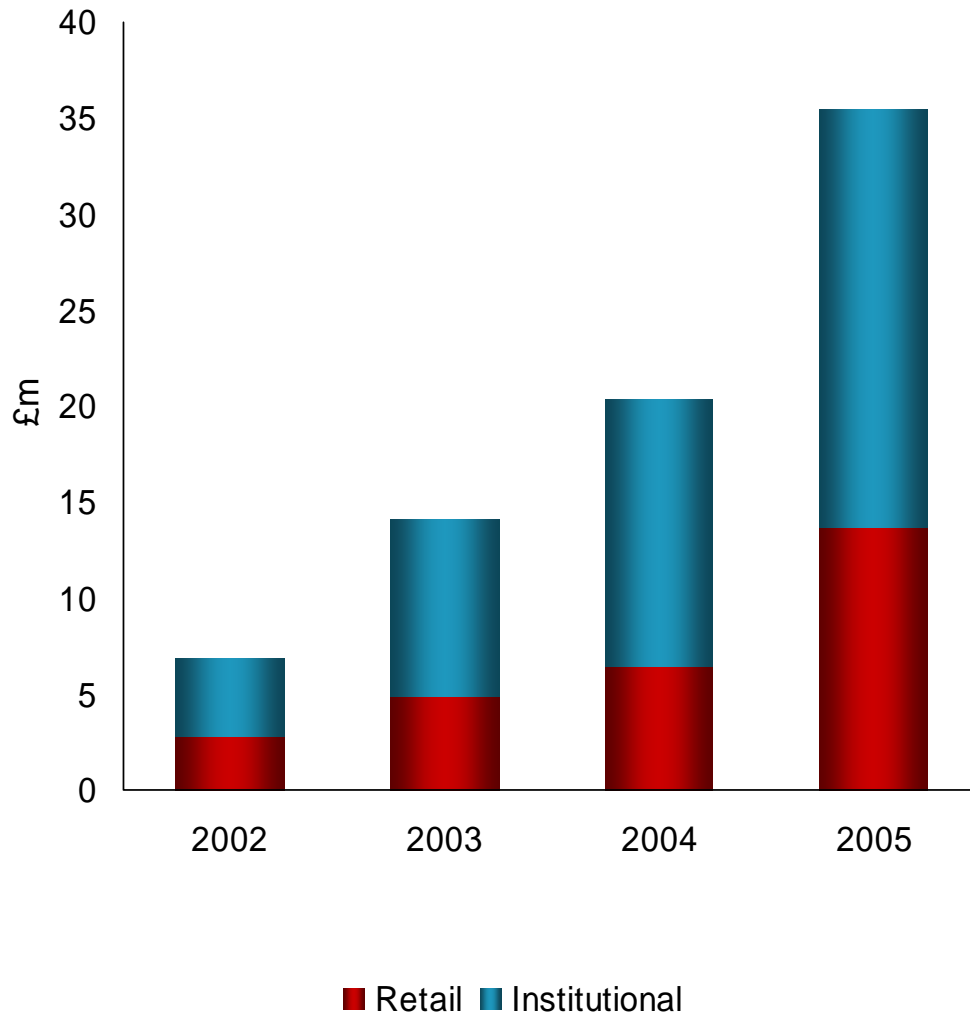


# NET NEW BUSINESS

## Consequent revenues driving bottom line

---

### CUMULATIVE ANNUALISED NEW REVENUES



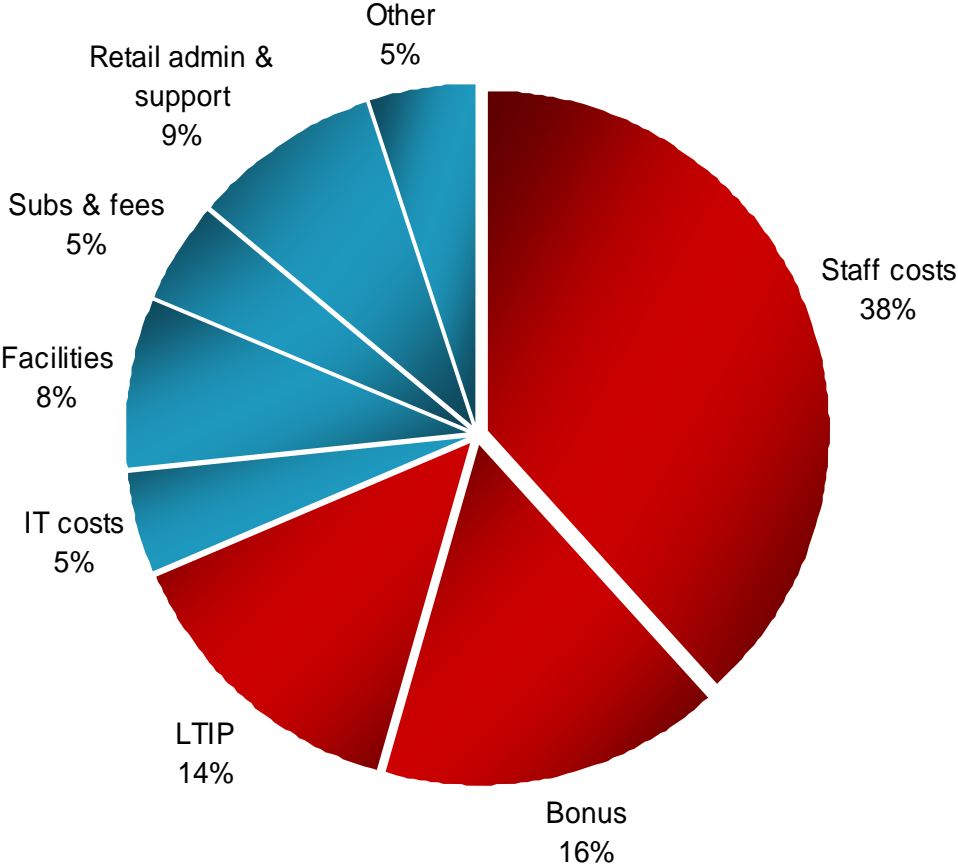
- Importance of net sales to profit growth
- Revenues added from consistent net inflows and development of new business lines

# COSTS

## People are the largest factor

---

### COSTS



- Incentive costs aligned with key metrics of business
  - Profits
  - Investment performance

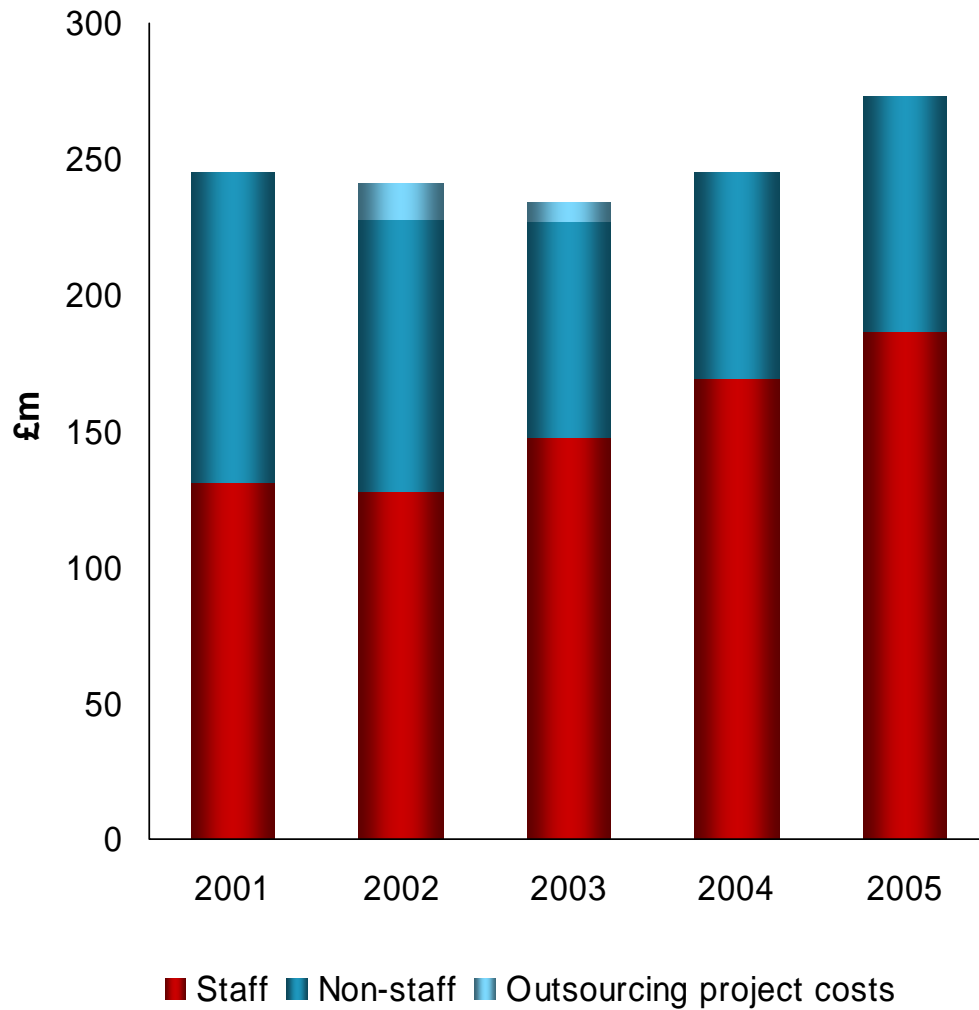


# COST PROGRESSION

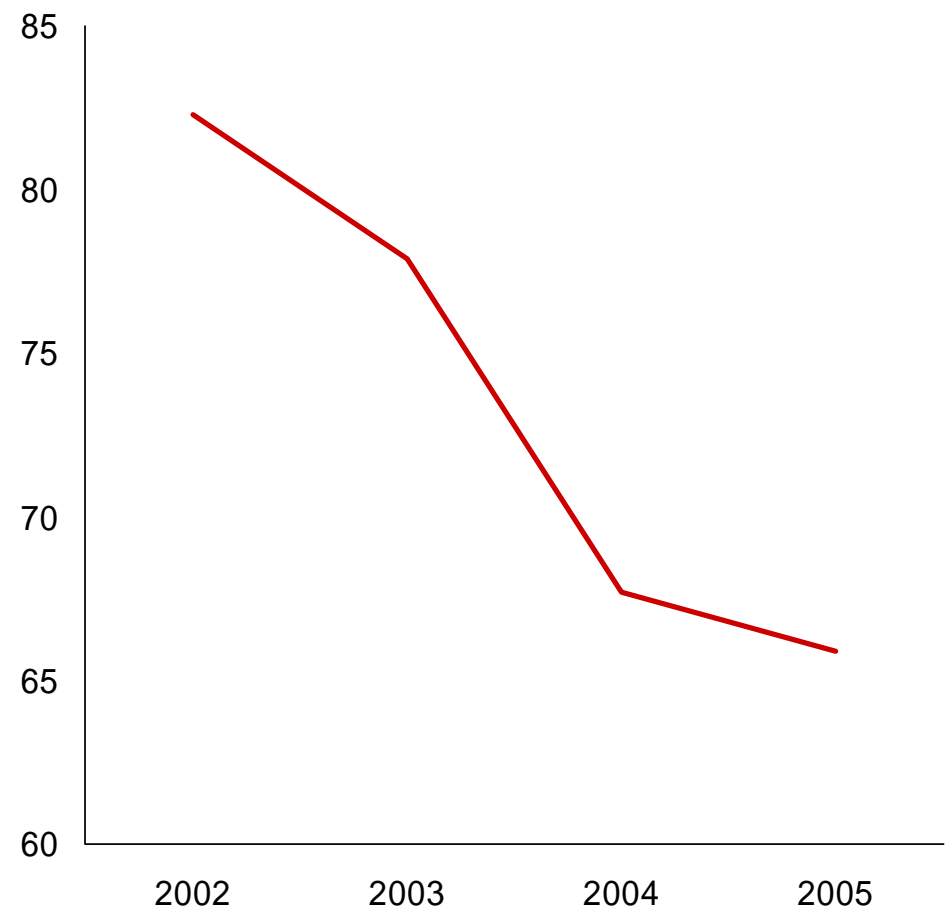
## Disciplined cost management

---

### COSTS BY TYPE



### COST / INCOME RATIO

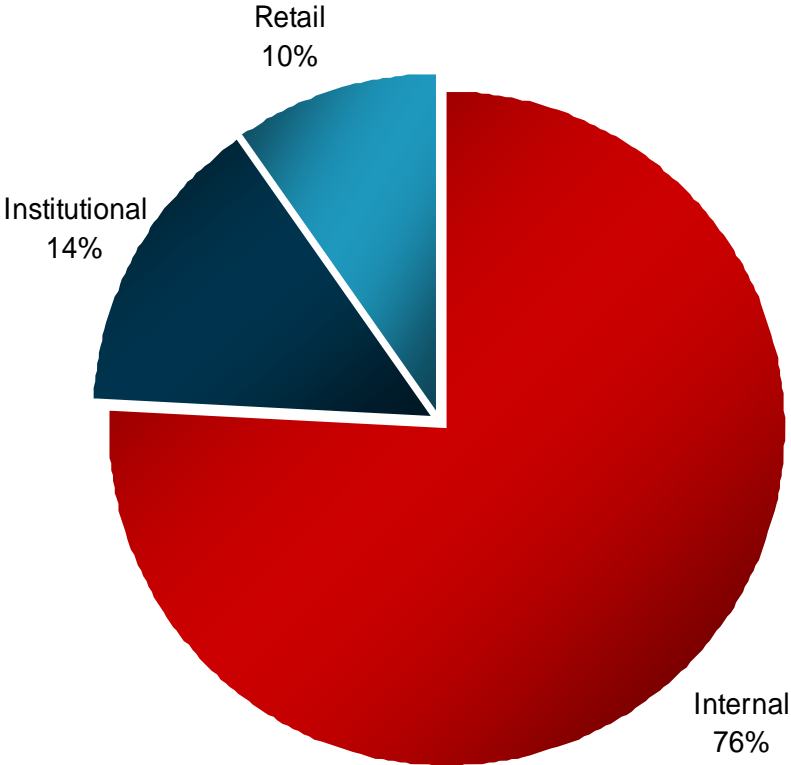


# PROFITS

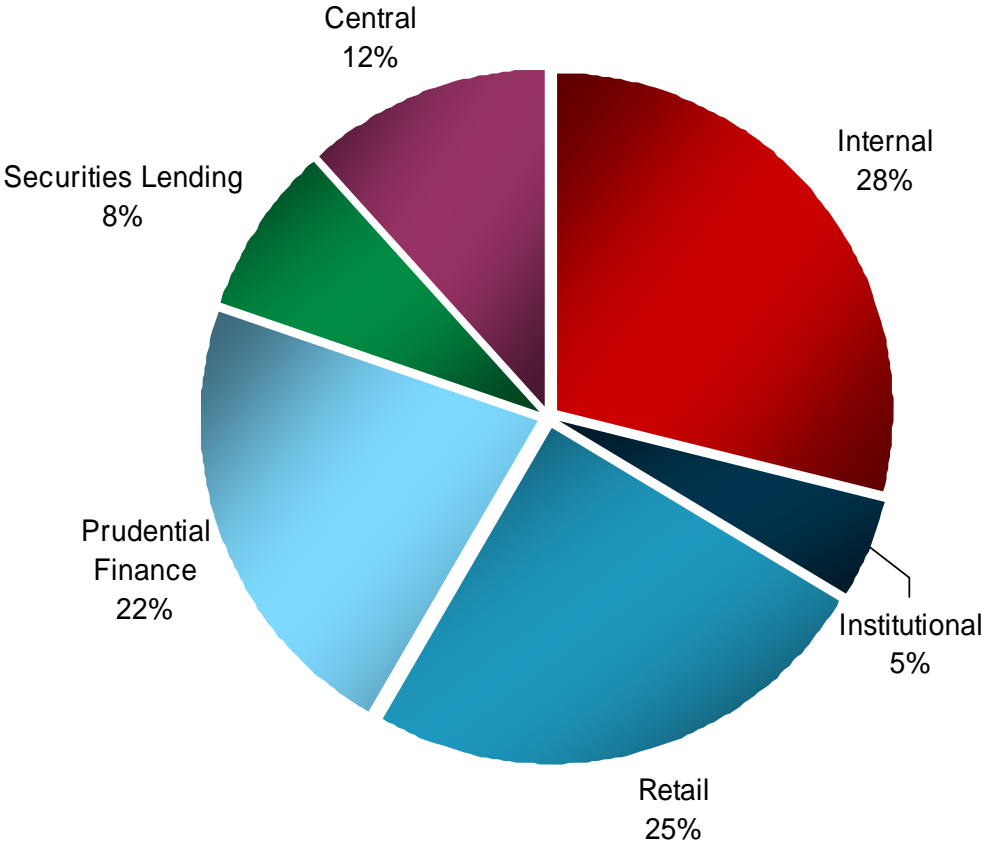
## Diversified sources of earnings

---

### FUNDS UNDER MANAGEMENT



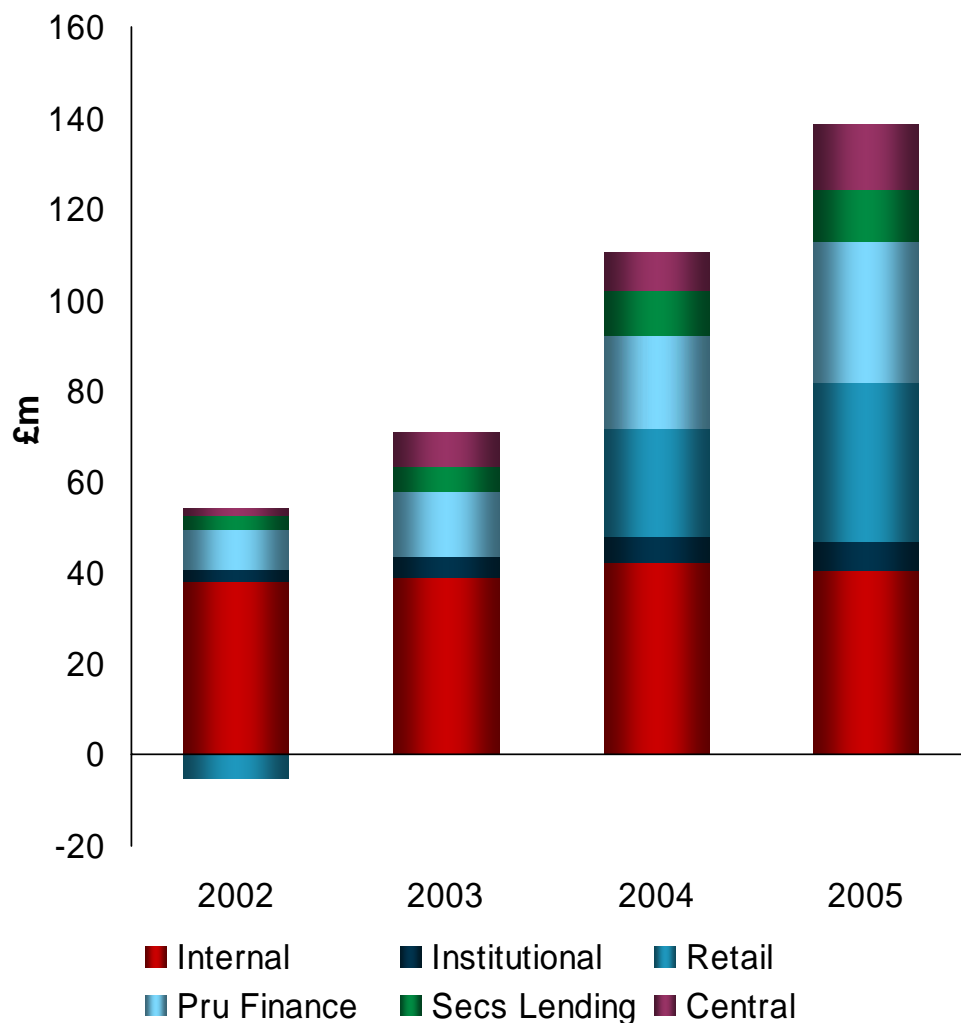
### UNDERLYING PROFITS



# PROFITS PROGRESSION

## Retail and Prudential Finance driving growth

### UNDERLYING PROFITS



- Internal client contribution static
- Retail grown rapidly:
  - Net sales
  - Costs savings from outsourcing retail administration
  - Market appreciation
- Continued expansion of Prudential Finance

# PERFORMANCE RELATED FEES

## Substantial contribution to profits

---

	2001 £m	2002 £m	2003 £m	2004 £m	2005 £m
Underlying profit	56	49	70	110	138
Performance related fees	19	20	8	6	8
Carried interest	-	2	5	20	17
<b>Profit before tax</b>	<b>75</b>	<b>71</b>	<b>83</b>	<b>136</b>	<b>163</b>

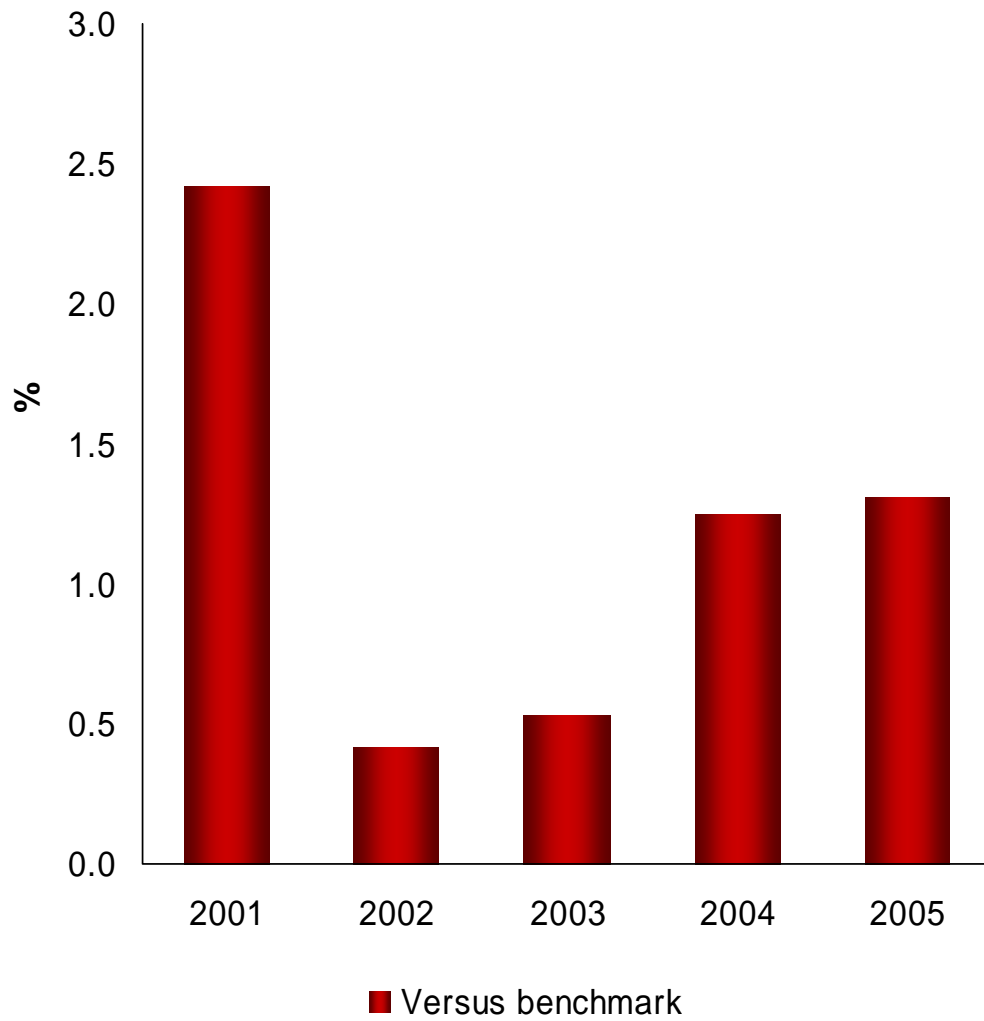
- Life Fund
- Annuities
- Carried interest
- Institutional
- Absolute Return

# VALUE ADDED TO THE LIFE FUND

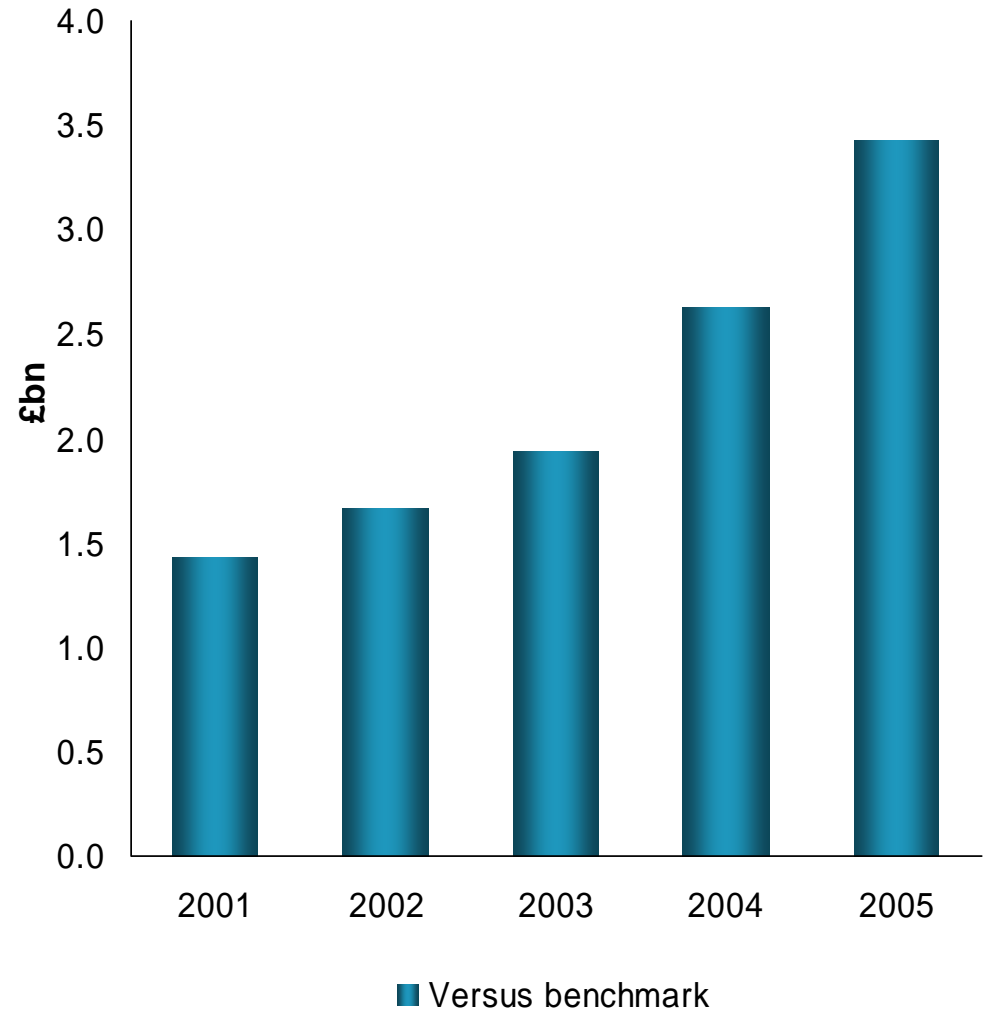
## Unrecognised but hugely important

---

### LIFE FUND RELATIVE PERFORMANCE



### CUMULATIVE VALUE ADDED FROM OUTPERFORMANCE



# BALANCE SHEET

## Light capital requirements and highly cash generative

---

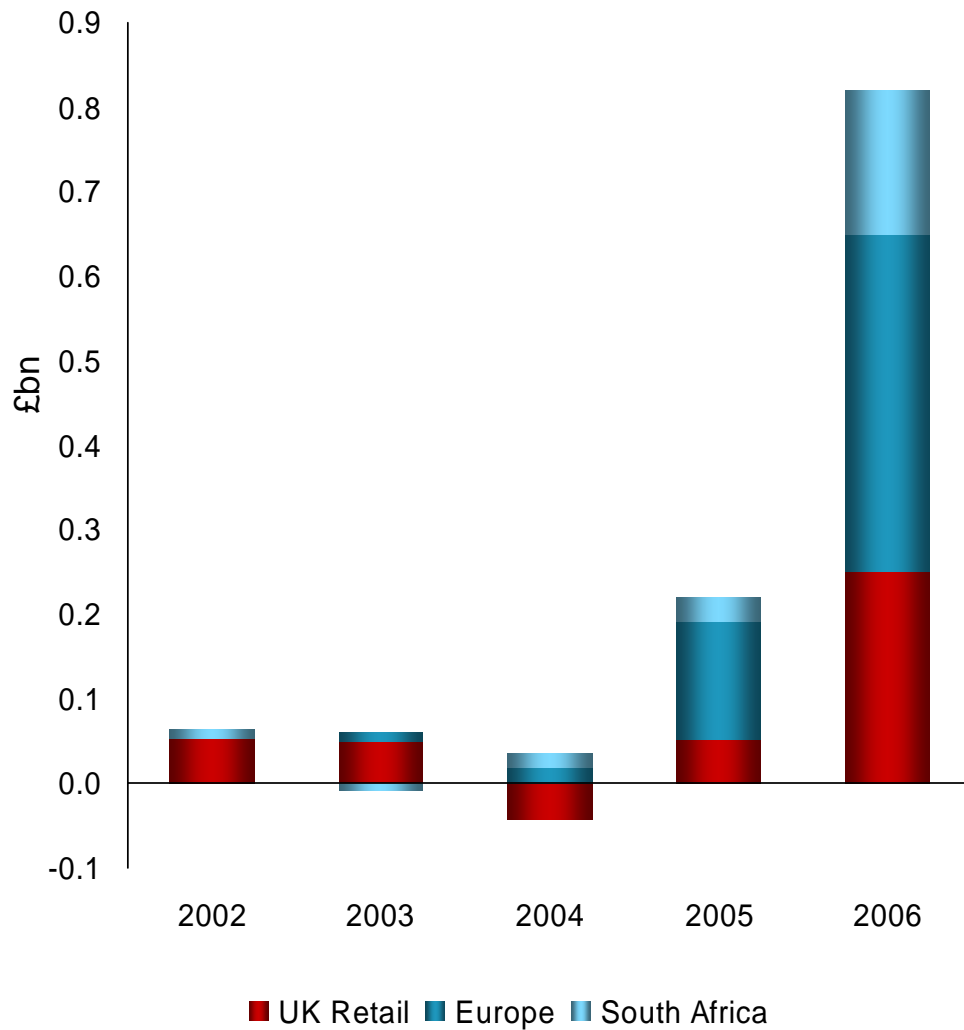
	2004 £m	2005 £m
<b>Cash generated</b>	<b>72</b>	<b>91</b>
Remittance of past surplus	14	-
Available for future remittance	-	(16)
Invested into business	(2)	(13)
<b>Actual cash remitted</b>	<b>84</b>	<b>62</b>

- M&G is not capital-intensive
  - Simple regulatory requirements
  - Growth does not require retentions
- Profits broadly equivalent to cash generation
- Some £20m of cash is generated above the M&G Group level
- Strict criteria for usage of capital

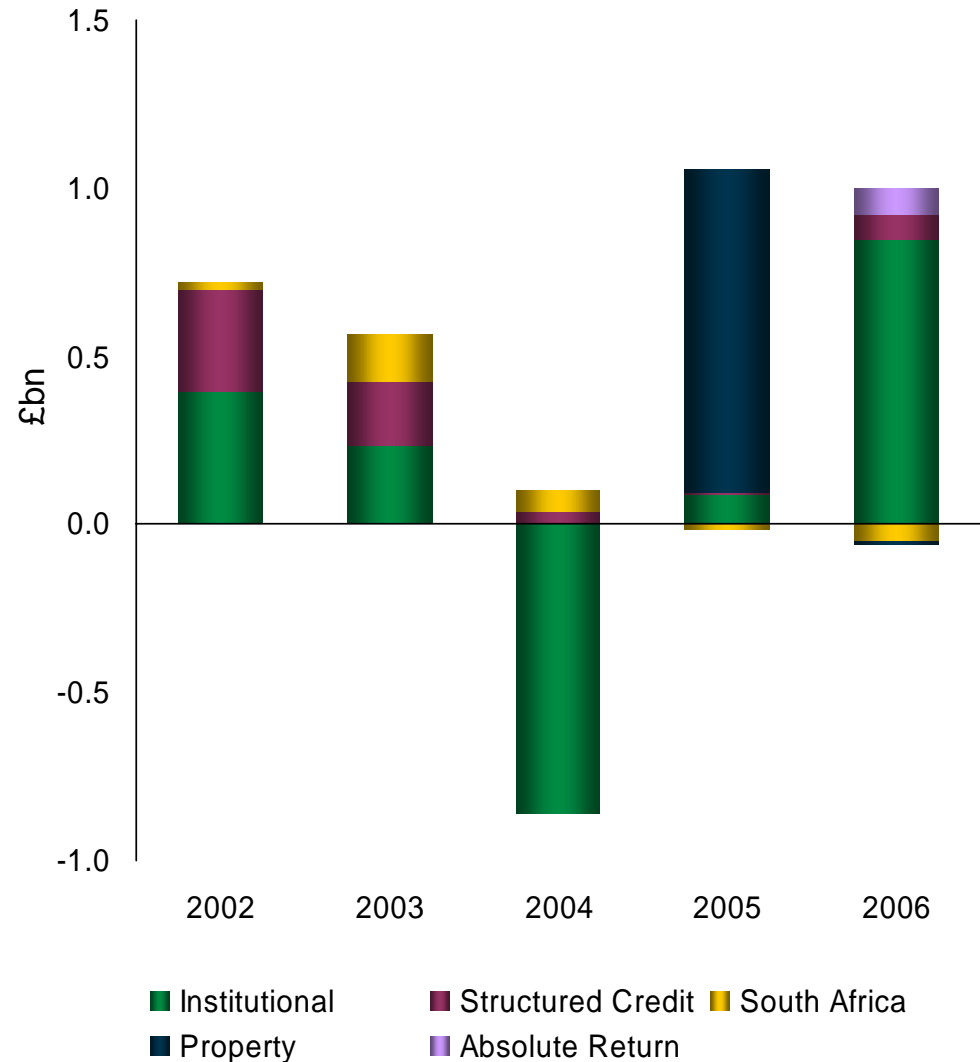
# Q1 NET SALES

## Momentum maintained

### Q1 NET RETAIL SALES



### Q1 NET INSTITUTIONAL SALES

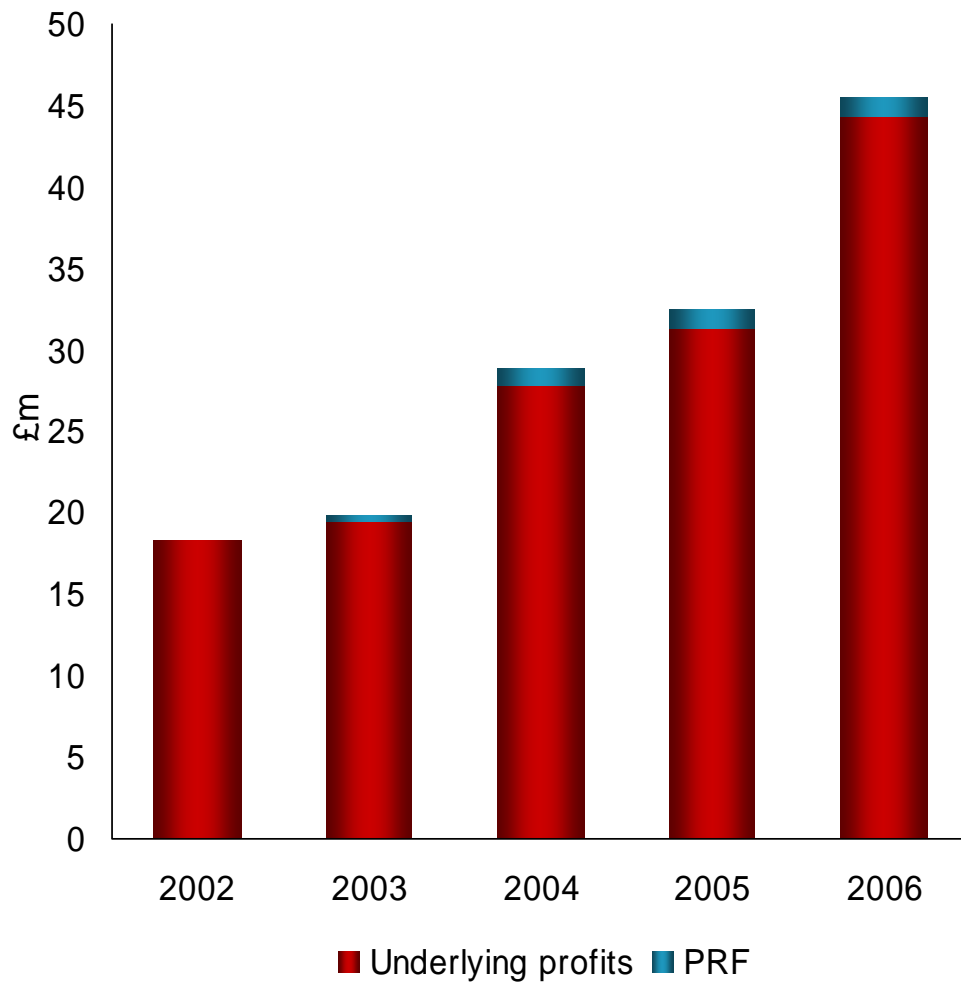


# Q1 PROFITS

## Momentum maintained

---

### Q1 PROFITS BEFORE TAX



- Underlying profits of £44m up 42%
- Result boosted by higher markets, strong net flows and increased retail charges



# SUMMARY

## High quality earnings and strong momentum

---

- Rapidly growing, diverse profit streams
- Significantly outperforming underlying markets
- Good opportunities for continued growth



**PRUDENTIAL**

# FIXED INCOME

**Simon Pilcher, Chief Executive Fixed Income, M&G**

# FIXED INCOME

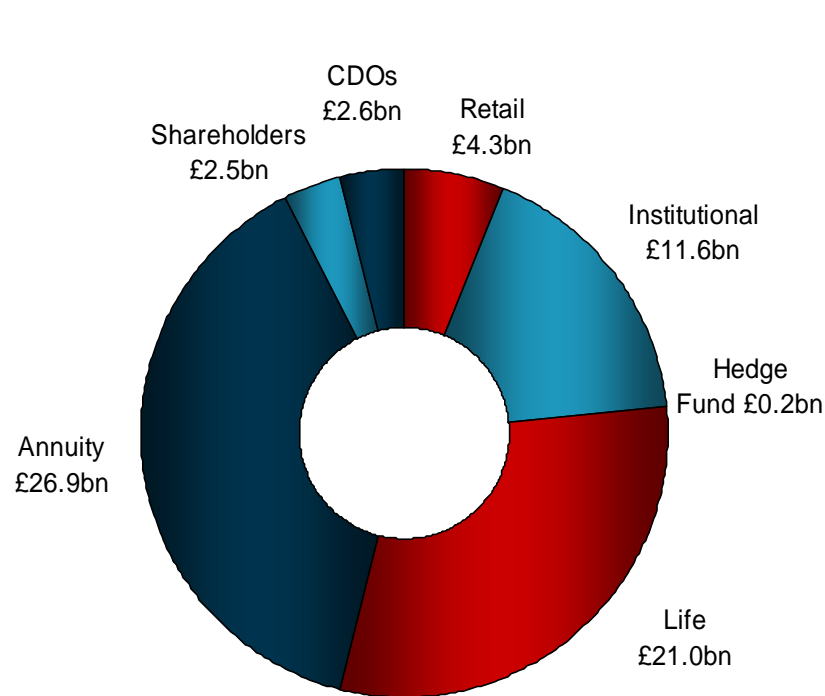
---

- Deliver outstanding investment returns to in-house capital through
  - Investment in innovative and attractive areas of the capital markets
  - Active fund management, particularly credit
- Exploit investment credentials externally
  - Differentiated by capability, not purely reliant on short-term performance
  - More robust business model
  - High marginal fees and profitability

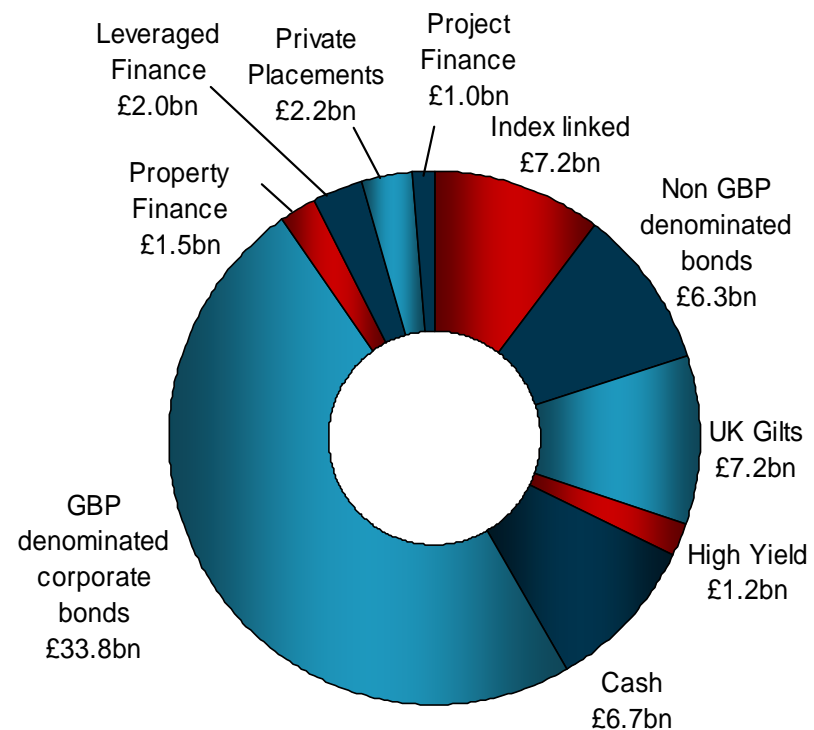
# FIXED INCOME FUNDS UNDER MANAGEMENT

## Breakdown of fixed income client base: £69.1bn total\*

### BY CLIENT TYPE



### BY ASSET CLASS



Source: Prudential M&G as at 31 March 2006. \*Funds managed from the UK by M&G.

# CREDIT ANALYSIS

## At the heart of the business

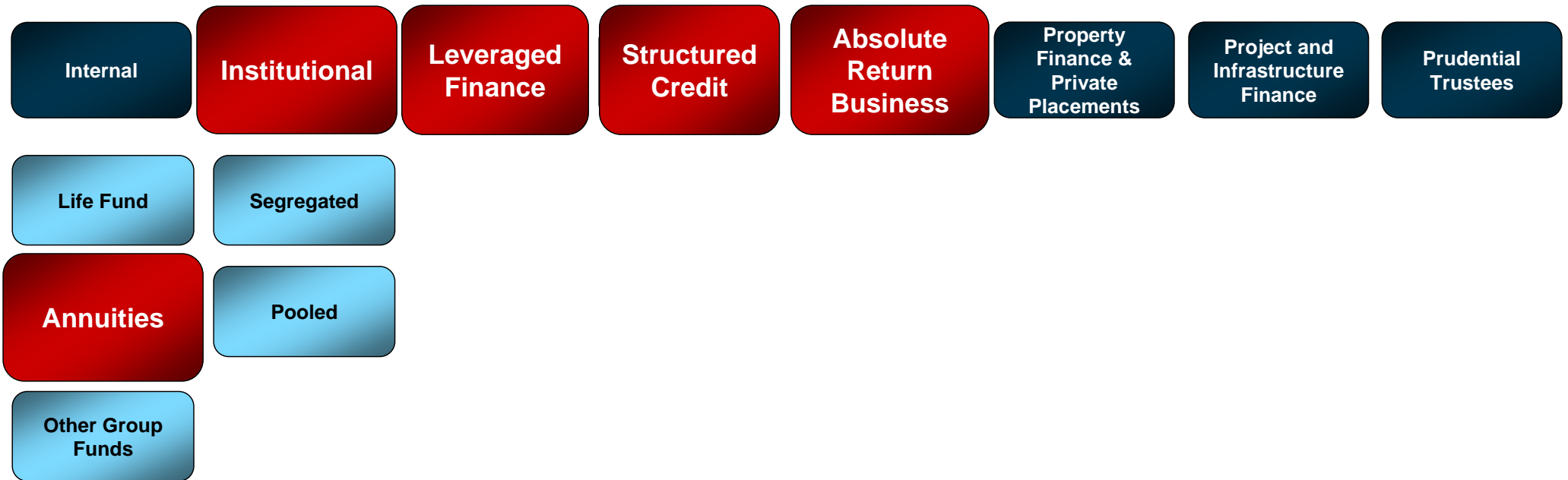
---

- M&G is focused on European Credit
  - Strong liaison with PPM America for US and ‘global’ credits
- Credit analysis is core
  - Dedicated professional career analysts
    - 15 Public analysts with sector specialisation
    - 9 Leveraged Finance
    - 7 Property and Private Placements
    - 9 Project and infrastructure
- Common resource ensures efficiency
  - Supporting different portfolio management teams
  - Key input to PFUK investments

# FIXED INCOME

---

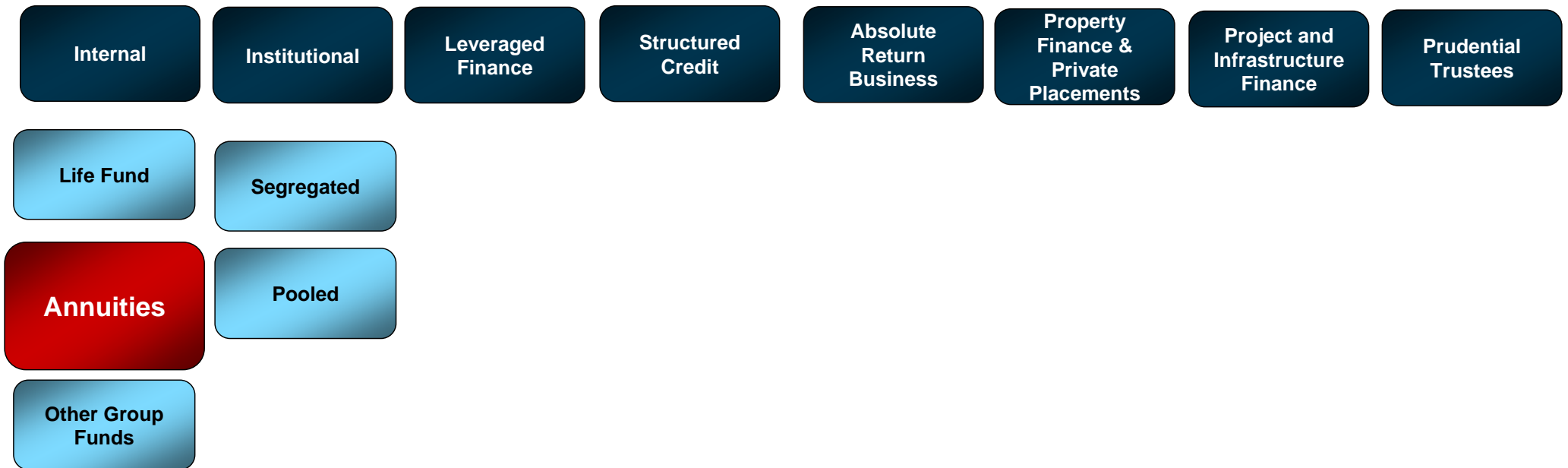
## Head of Fixed Income



# AGENDA: ANNUITIES

---

## Head of Fixed Income



# ANNUITIES

## Close partnership between M&G and the insurance business

---

- £27bn in segregated portfolios with cash flow matching strategy
- Frequent re-pricing of offering dependent on
  - Market conditions
  - Duration of business
- Bespoke pricing for Bulks and Partnership business using case specific liability and asset information
- M&G incentivised to:
  - Maximise new business margins and volumes
  - Improve matching to minimise capital needs
  - Minimise credit losses
  - Enhance yield to maximise value of in-force business



# ANNUITIES

## Significant value added through active credit management

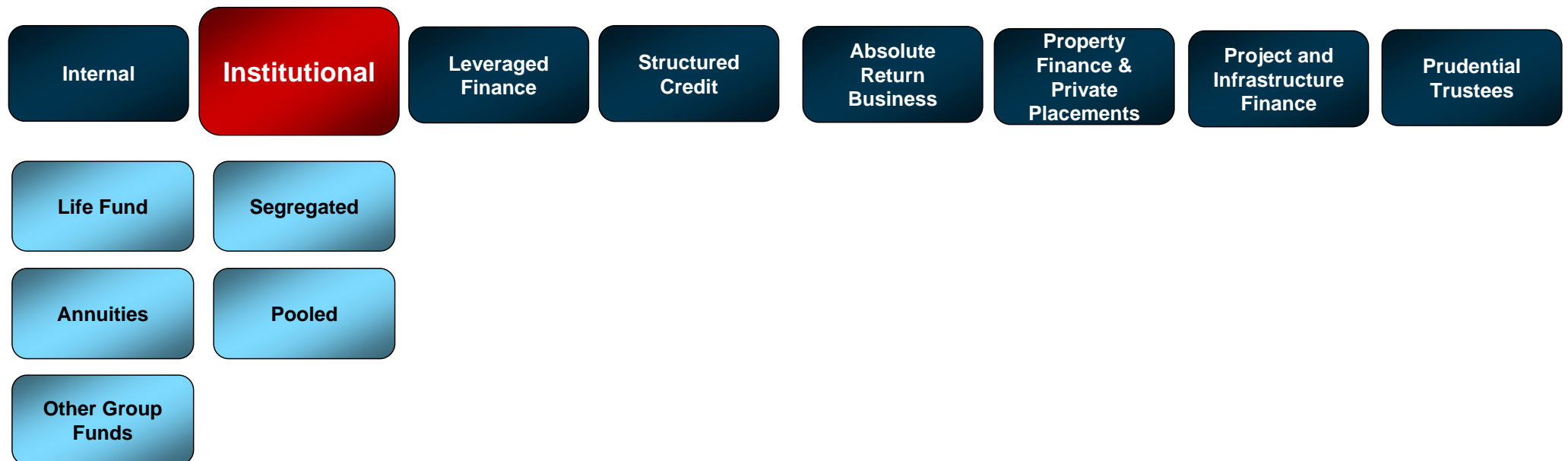
---

- Close matching to minimise interest rate and reinvestment risk
- Active management with every single transaction monitored
  - £44m of surplus generated through matching improvement in 2005
  - £22m generated through yield enhancement
- Flexible derivative strategy to manage risks and synthesize assets
- Attractive assets sought from non-traditional areas, eg:
  - Private finance
  - Property
- Expected credit losses and migration consistently outperformed
  - £32m default provision for 2005: Nil defaults and £1m 'distressed' sales experienced
  - £97m reduction in future years' default provision through credit upgrades
- Performance Related Fees £2m for 2005

# AGENDA: INSTITUTIONAL BUSINESS

---

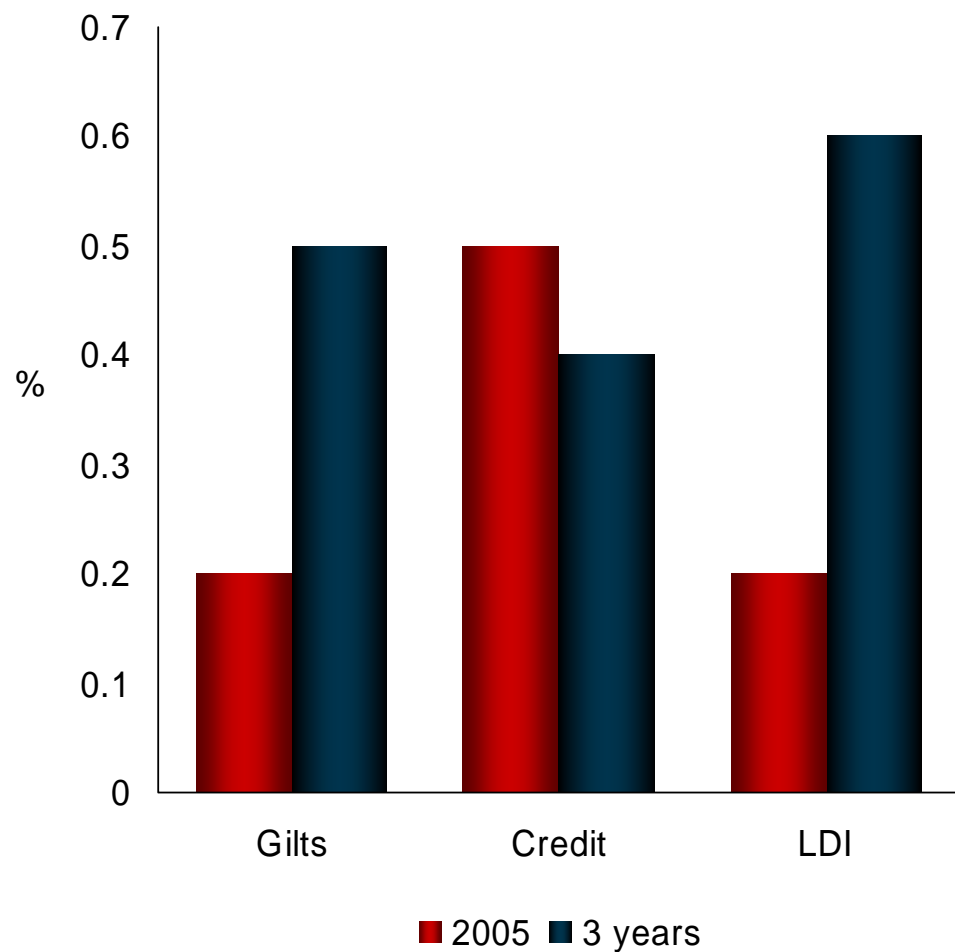
## Head of Fixed Income



# INSTITUTIONAL BUSINESS: SEGREGATED FIXED INCOME

---

## RELATIVE PERFORMANCE OVER 2005 AND 3 YEARS

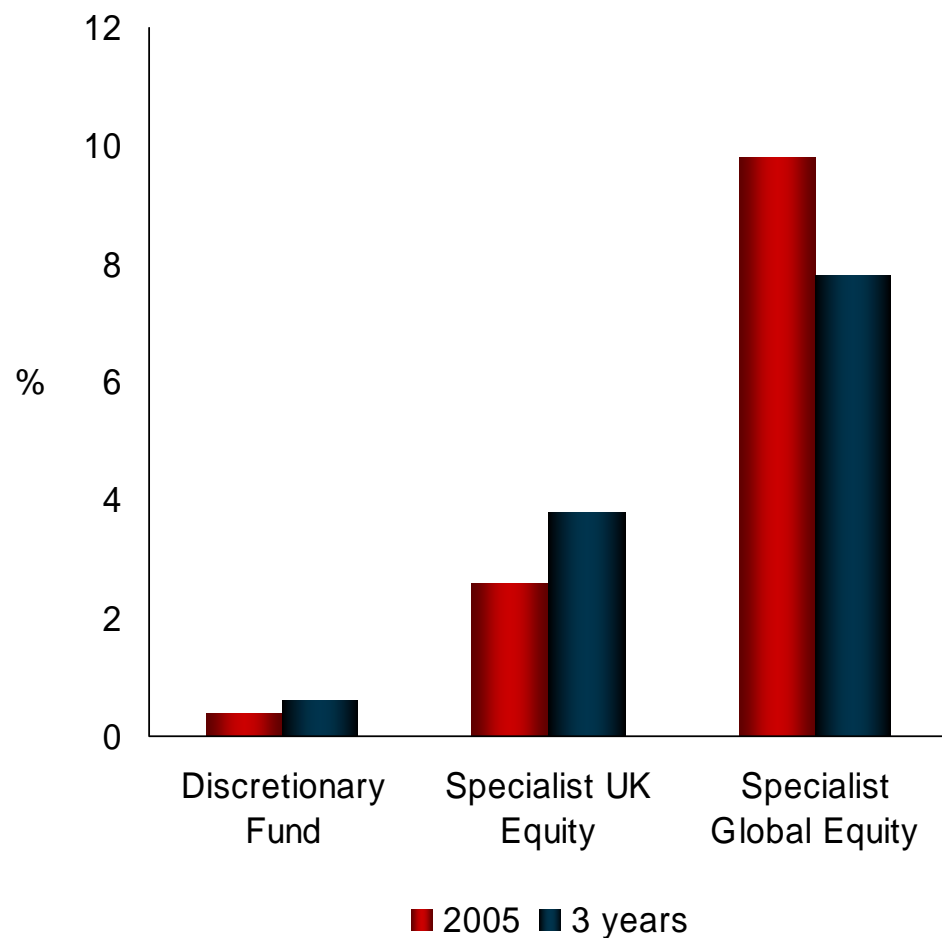


- Solid investment performance in all areas
- Strong start to 2006 for
  - Investment performance
  - New business wins £627m (Year to 31<sup>st</sup> March)
- Alpha opportunities fund under development
  - ‘Best ideas’ fund
  - Core portfolio with overlay portfolios in macro and credit relative value.

# INSTITUTIONAL BUSINESS: POOLED

---

## RELATIVE PERFORMANCE OVER 2005 AND 3 YEARS



- Defined Benefit & Defined Contribution business
- M&G's investment-only product as well as Prudential-sold 'packaged' product
- Consistent 'core' product performance
- Excellent 'new world' product performance
- Strong flows of new business
  - 2005 + £386m
  - 2006 + £43m (to 31<sup>st</sup> March)

# AGENDA: LEVERAGED FINANCE BUSINESS

---

Head of Fixed Income

Internal

Institutional

Leveraged  
Finance

Structured  
Credit

Absolute  
Return  
Business

Property  
Finance &  
Private  
Placements

Project and  
Infrastructure  
Finance

Prudential  
Trustees

Life Fund

Segregated

Annuities

Pooled

Other Group  
Funds

# LEVERAGED FINANCE

## Senior and secured loans to LBOs

---



# LEVERAGED FINANCE

## Playing in Europe's champions league

---

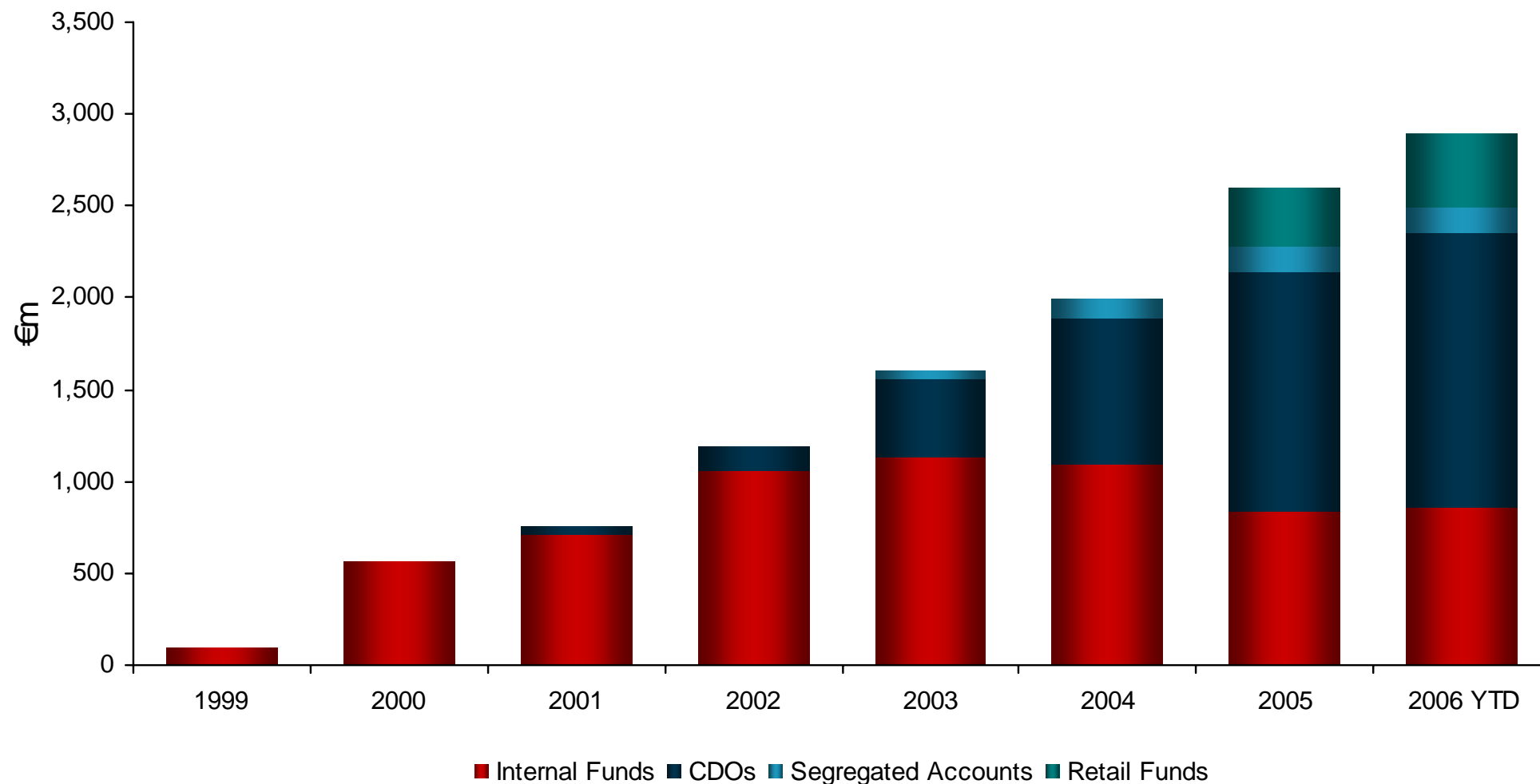
- Long track record, strong relationships with banks and sponsors
  - Gives us early sight of transactions
- One of the largest market participants
  - Permitting big bids and above-market allocations
- Variety of funds under management
  - Creating institutional leverage, flexibility and capability for non-mainstream investments
- Specialisation of team
  - Ensuring superior credit decisions, better structuring, improved relative-value judgements and portfolio management

# LEVERAGED FINANCE: FUNDS UNDER MANAGEMENT

## Controlled expansion of volume and client type

---

### LEVERAGED FINANCE ASSETS MANAGED BY M&G



Source: M&G, 31 March 2006



# AGENDA: STRUCTURED CREDIT

---

Head of Fixed Income

Internal

Institutional

Leveraged  
Finance

Structured  
Credit

Absolute  
Return  
Business

Property  
Finance &  
Private  
Placements

Project and  
Infrastructure  
Finance

Prudential  
Trustees

Life Fund

Segregated

Annuities

Pooled

Other Group  
Funds

# STRUCTURED CREDIT

## A market leader in Europe

---

- Regular issuer of CDOs across multiple asset classes
    - 5 CLOs now priced
    - 3 investment grade arbitrage CDOs
    - 1 ABS arbitrage CDO
    - 6 synthetic investment-grade CDOs (3 public, 3 private)
  - Strong credit performance reflecting conservative credit philosophy
  - Global coordination for CDO issuance and credit management
  - Leading position ensures
    - Improved terms and sharing of ideas from investment banks
    - Low capital commitment (£10.3m)
    - Attractive revenues (£11.6m per annum)
    - Fast growing and sustainable franchise
-

# AGENDA: ABSOLUTE RETURN BUSINESS

---

Head of Fixed Income

Internal

Institutional

Leveraged  
Finance

Structured  
Credit

**Absolute  
Return  
Business**

Property  
Finance &  
Private  
Placements

Project and  
Infrastructure  
Finance

Prudential  
Trustees

Life Fund

Segregated

Annuities

Pooled

Other Group  
Funds

# ABSOLUTE RETURN BUSINESS

## An outstanding long-run track record

---

- Track record of delivering performance
  - Running Global Macro strategy for the Prudential Life fund – AUM of £2.25bn
  - Since 2001 average returns of 18.5% per annum, with average volatility of 9%
- Team in place for six years
- A different perspective and investment approach, applied across a broader universe
  - Discretionary global macro applied within a disciplined framework
  - Equity, fixed income and FX
  - Truly global with both developed and emerging markets
  - Exploiting ‘episodes’ of excess volatility – asset class and geographical mis-pricing

# ABSOLUTE RETURN BUSINESS

## Rapid growth in 3<sup>rd</sup> party business

---

- Episode
  - Cayman domiciled Global Macro Hedge Fund
  - Launched August 2005
  - Funds under management now \$385m
  - Fees 1.5% base, 20% PRF
  - Net returns since inception 13.7% (18.7% annualised)
- Segregated Global Tactical Asset Allocation mandates
  - \$180m now under management
- Capacity estimated at \$1.5billion
  - Expected to be reached H1 2007

## **M&G FIXED INCOME**

### **Attractive prospects for future profits growth**

---

- Unrivalled credit expertise
- Infrastructure established to service life fund and annuity clients, now supporting high growth areas
- Closely integrated with rest of Prudential's business
- Dynamic and innovative, leading market change
- Attractive prospects for future profits growth



**PRUDENTIAL**

# PRUDENTIAL FINANCE

**John Foley, Managing Director**



# PHILOSOPHY

## What is our role?

---

- Internal banker to Group and its subsidiaries
- Leverage Prudential's and M&G's positioning and skills for profit

**HIGH PROFITABILITY, HIGH CAPITAL VELOCITY, LOW CAPITAL**

---



# BACKGROUND

## Who are we?

---

- Formed in 2001
- 20 people – extensive range of financial disciplines
- Economic capital model
- Proprietary investment business

**ENTREPRENEURIAL TEAM EMBEDDED  
IN CORE GROUP BUSINESSES**

---

# PERFORMANCE MEASURES

## Key metrics

---

- Profit
- Return on economic capital
- Velocity of capital
- Symbiotic performance
- Group funding, liquidity and treasury management

**SIMPLE MEASURES – HIGH PERFORMANCE**

---

# BUSINESS DYNAMICS

## How do we do it?

---

- No external clients or customers
- Investment banks are our partners
  - Non-disclosure agreements
  - No market position to protect, e.g. league tables
  - Free to challenge banks, sponsors and business managers
- Centralise bank relationships and deal-flow
- Risk management and oversight

# TOPICS FOR TODAY

---

- Business activities and deal-flow
- Value added examples elsewhere in the Group
- Risk management and oversight
- Key metrics of performance

# **BUSINESS ACTIVITIES AND DEAL-FLOW**

## **Areas of activity**

---

- Bridging transactions
- Property Financing
- Securities Lending
- Funds pre-launch funding
- Arbitrage investments

**COMPLETE CONNECTIVITY WITH GROUP AND SUBSIDIARIES**

---

# BRIDGING INVESTMENTS



# BRIDGING INVESTMENTS

---





# BRIDGING INVESTMENTS

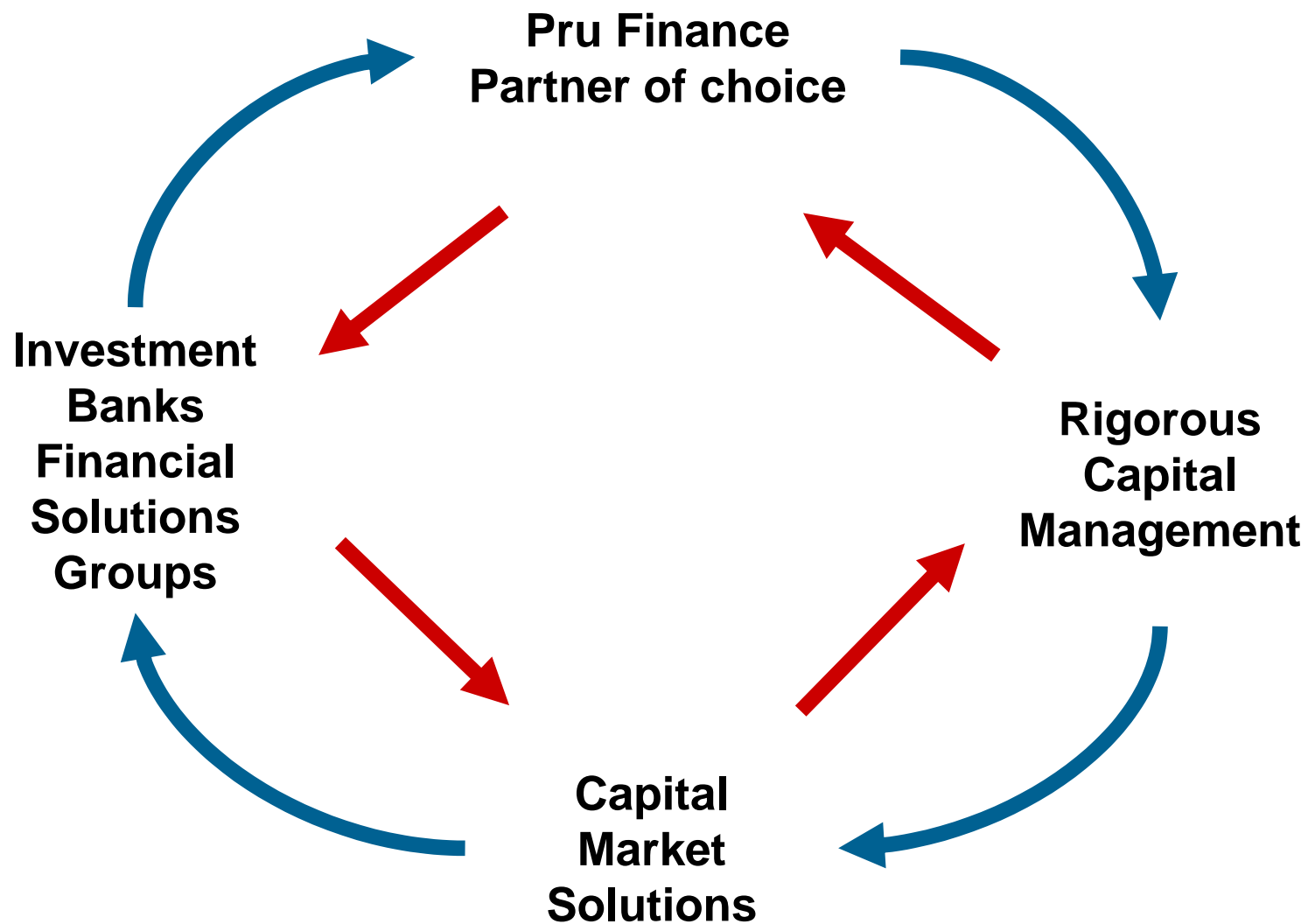




# BUSINESS ACTIVITIES AND DEAL-FLOW

Deal-flow increasingly two way

---



**A SUSTAINABLE PROPOSITION**

---

# BUSINESS ACTIVITIES AND DEAL-FLOW

## A sustainable proposition

---

- Continuity of deal flow
- Power of the relationship
- Maintain quality of analytical and investment skills

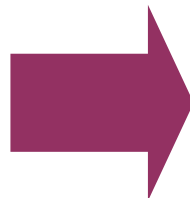
# THE VALUE ADDED REQUIREMENT

## Symbiosis, financial and non-financial value enhancement

---

Demonstrate value added to achieve transaction approval

- Incremental profit
- Investment performance
- Liquidity
- Capital Market solutions



Ensures highly effective “third party” analysis of transactions

Stick to fundamentals

Key to rating agency and regulator “approval” of our strategy

Discipline

# RISK MANAGEMENT AND OVERSIGHT

## Three layers of approval, three layers of monitoring

---

- Prudential Finance Risk Management
  - Daily monitoring
- M&G and Group Risk Departments
  - Daily monitoring
- Prudential Finance Approvals Committee
  - Chaired by Group CFO
  - Deputy chair Group Chief Risk Officer
  - Monthly review

## STRINGENT RISK CONTROL AND REPORTING

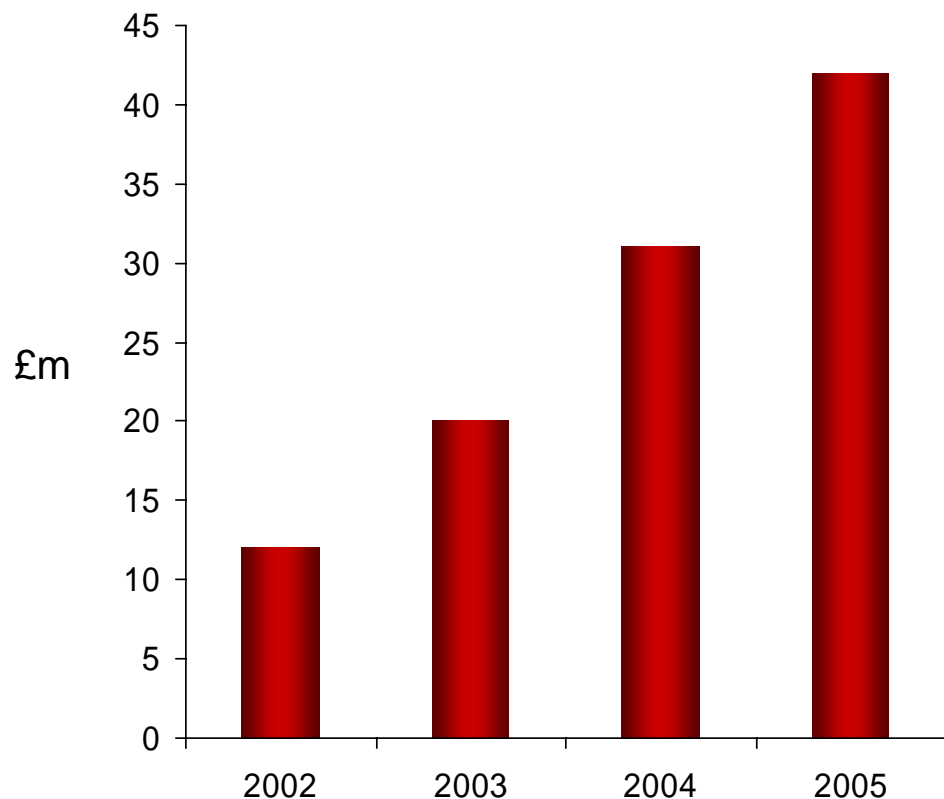
---

# KEY METRICS OF PERFORMANCE

## A cash generator

---

### ROBUST PROFIT STREAMS



- Profit in 2005 of £42 million
- Economic capital £34 million
- Cost/Income ratio 29%
- Velocity of capital >100% pa
- Book size £2.6bn
- Average weighted rating A+
- Average weighted expected duration 1.75 years
- Average weighted margin 112 bps\*

---

\* Not including fee income

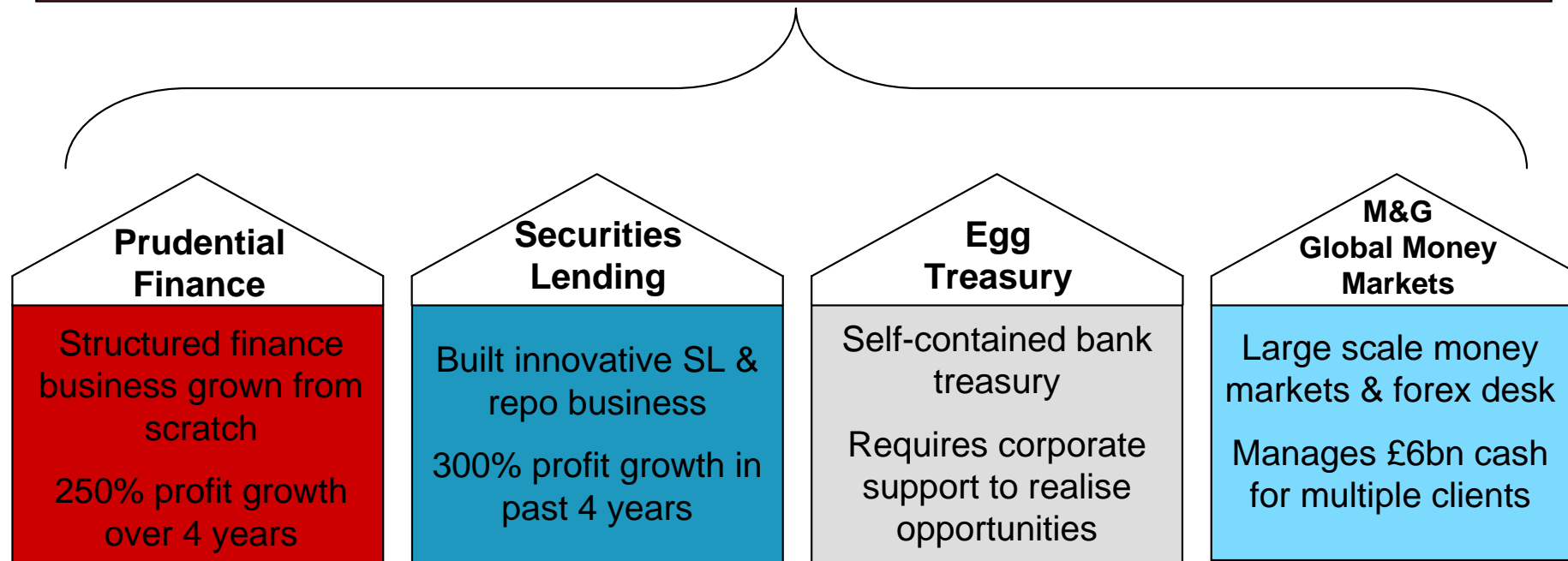
# NEXT PHASE

The opportunity is significant

---

## New Prudential Finance

Internal Group Treasury – Centralised Funding  
Co-ordinated Credit, Liquidity and Interest Rate Management  
Strengthen and Leverage off combined Banking Relationships  
New Regulated Activities – Bank Disintermediation and Principal Securities Lending



**HIGH PROFITABILITY, HIGH CAPITAL VELOCITY, LOW CAPITAL**

---