Interim Results for Partnership Assurance Group plc ('Partnership')
For the six months ending 30 June 2015

11 August 2015

Individual annuity sales starting to recover post implementation of the Pension Freedoms in April 2015; growing Defined Benefit market activity points to transactions increasing in H2

Financial highlights

- Total new business premiums of £231 million comprising:
  - £128 million of individually underwritten annuities; Q2 sales post implementation of the Pension Freedoms increased by over a third vs. Q1, as advisers and customers started to return to the market
  - £68 million of medically underwritten Defined Benefit ('DB') bulk annuity sales, including £42 million from the largest individually underwritten DB whole of scheme transaction to date
  - £33 million of care annuities and £2 million of protection sales
- Total operating profits of £18 million comprising:
  - A loss of £(2) million on new business; pricing discipline has been maintained in the period to ensure new business covers its capital requirement. However, as previously highlighted, since over 90% of operating expenses are allocated to new business, profits and margin continue to be impacted by current operational gearing and will remain compressed in the short term until sales volumes recover
  - £13 million of in-force operating profits, reflecting positive mortality experience, particularly on in-force care business, and £7 million return on surplus assets, representing a yield of 3.0%
- IFRS profit before tax £3 million after £7 million of negative investment variances, £6 million of other non-recurring expenses and £3 million of interest on the Tier 2 bond issued in March 2015
- MCEV increased 2% to £590 million or 147 pence per share at 30 June 2015
- Estimated economic capital surplus of £223 million at 30 June 2015, representing coverage of 156% vs. the Board's minimum target of 125%
- Assets under management increased by £94 million to £5.0 billion at 30 June 2015
- 2015 interim dividend of 0.5p per share

Operational highlights

- Continued focus on developing innovative new products and enhancing existing proposition to meet evolving customer needs. Retirement account development progressing well with launch planned for H2 2015
- Partnerships Defined Benefit proposition continues to develop and recognised in H1 with industry award for "Buyout Firm of the Year" at the European Pensions Awards 2015.
- Well placed to deliver targeted c. £75 million cost base for FY15 with £34 million of operating expenses incurred in H1
- Solvency II matching adjustment and transitional measures applications submitted to the PRA for approval. Based on our current interpretation of the draft regulations, we expect to remain well capitalised on a Solvency II basis
- Preferred partner for launch of US Care annuity selected. Operational build to support launch commenced. Implementation timetable to be provided when negotiations have concluded

Outlook

- The long term structural drivers of the individual annuity market remain intact. Quote levels for individual annuities continue to increase gradually but customer behaviour and conversion trends have not yet stabilised. Whilst it is too early to be certain, based on current activity levels, we continue to expect individual annuity sales volumes to grow in H2 15 relative to H2 14 and H1 15
- Defined Benefit industry-wide had a slow start to 2015 but market feedback points to trustee and Employee Benefit Consultants (EBCs) activity growing into H2. Our pipeline comprises transactions across a wide selection of EBCs, reflecting both the increasing recognition of medical underwriting in bulk de-risking and the stronger and broader relationships with EBCs
- Defined Benefit completions remain lumpy but our recent activity and current pipeline provides confidence in our ability to achieve our target of at least £200 million in FY15
- As individual annuity volumes increase and the targeted DB dales are delivered, both the absolute level of new business profits and the new business margins are expected to recover

Steve Groves, CEO, commented:

“Sales of individual annuities in the second quarter, post implementation of the Pension Freedoms in April, increased by over a third compared to the first quarter. Although customer behaviour has not yet stabilised, the structural drivers for growth in this market remain intact and I continue to be positive about its outlook over the long term. We welcome the commitment of Regulators and Government to delivering good outcomes for customers, including the recently announced review into how financial advice could work better for all consumers.

In the first half of this year, we completed the largest individually underwritten Defined Benefit whole of scheme transaction to date. Greater awareness of Medical Underwriting for bulk annuities among Employee Benefit Consultants and Trustees, recent market activity, and our pipeline provide confidence in our ability to achieve our target of at least £200 million of Defined Benefit sales in 2015.

We remain focused on our clear three-pronged strategy to diversify and grow our business based on the recovery in the core retail market, growth in Defined Benefits and US care, and opportunities to leverage our Intellectual Property in product innovation.

Recommended all-share merger of Just Retirement Group plc and Partnership Assurance Group plc

The Boards of Just Retirement Group plc (‘Just Retirement’) and Partnership Assurance Group plc (‘Partnership’) have announced today that they have reached agreement on the terms of a recommended all-share merger to create JRP Group plc (the "Merger"). Please refer to the separate announcement released today for further details.

Commenting on the Merger, Chris Gibson-Smith, Chairman of Partnership, said:

"I am delighted to announce the recommended all-share merger of Just Retirement and Partnership. Both businesses have at their core a focus on using outstanding intellectual property and underwriting expertise to deliver better value products and improved customer outcomes within defined benefit, UK retail retirement income and international markets. This transaction represents a unique opportunity to accelerate the existing strategy of both businesses, which we believe will allow us to deliver better returns to both policyholders and shareholders."

Summary of results

	HY15	HY14	FY14
Total new business premiums[1] (£m)	231	409	791
New business operating (loss)/ profit (£m)	(2)	18	39
New business margin	(1.0)%	4.4%	4.9%
Total operating profit (£m)	18	33	64
Economic capital ratio[2]	156%	153%	159%
MCEV per share	147p	136p	144p
Assets under management (£bn)	5.0	4.4	4.9

New business sales by quarter (£m)[1]

3 months to:	30-Jun-15	31-Mar-15	31-Dec-14	30-Sep-14	30-Jun-14
Individual annuities	74	54	62	69	135
DB bulk annuities	44	24	210	-	3
Care	13	20	19	20	16
Protection	1	1	1	1	1
Total new business	132	99	291	89	155

New business sales (£m)[1]

6 months to:	30-Jun-15	30-Jun-14
Individually underwritten annuities	128	334
DB bulk annuities	68	37
Care	33	36
Protection	2	2
Total new business	231	409

Notes:

(1) New business sales are Single Premium Equivalent sales completed in the period. These are recorded when funds have been received from the policyholder quarterly and at half year. Totals are subject to rounding.

(2) Economic capital was 134% at FY14 year end. Proforma economic capital position, taking into account £100m bond issue in Q1 2015, was 159%.

Enquiries

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Further information

A presentation for analysts and investors will take place at 8am (BST) today to discuss the Merger and Partnership's interim results in the Auditorium at Deutsche Bank, Winchester House, 1 Great Winchester Street, London EC2N 2DB

Participants may also dial in as follows:

+44 (0)20 3059 8125
Please quote "JRP" to access the call.

A copy of the presentation will be available on our website **www.partnership-group.co.uk**

A transcript and replay of the call will also be available on the website in due course.

Financial calendar

20 August 2015	Ex-dividend date – interim dividend
21 August 2015	Record date to be eligible for the final dividend
30 October 2015	Interim dividend payment date
5 November 2015	2015 Q3 Interim Management Statement

Forward looking statements

This announcement in relation to Partnership Assurance Group Plc and its subsidiaries (the ‘Group’) contains, and we may make other statements (verbal or otherwise) containing, forward-looking statements about the Group’s current plans, goals and expectations relating to future financial conditions, performance, results, strategy and/or objectives.

Statements containing the words: ‘believes’, ‘intends’, ‘expects’, ‘plans’, ‘seeks’, ‘targets’, ‘continues’ and ‘anticipates’ or other words of similar meaning are forward-looking (although their absence does not mean that a statement is not forward-looking). Forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that are beyond the Group’s control. For example, certain insurance risk disclosures are dependent on the Group’s choices about assumptions and models, which by their nature are estimates. As such, actual future gains and losses could differ materially from those that we have estimated.

Other factors which could cause actual results to differ materially from those estimated by forward-looking statements include but are not limited to: domestic and global economic and business conditions; asset prices; market related risks such as fluctuations in interest rates and exchange rates, and the performance of financial markets generally; the policies and actions of governmental and/or regulatory authorities, including, for example, new government initiatives related to the provision of retirement benefits or the costs of social care and the effect of the European Union’s “Solvency II” requirements on the Group’s capital maintenance requirements; the impact of inflation and deflation; market competition; changes in assumptions in pricing and reserving for insurance business (particularly with regard to mortality and morbidity trends, gender pricing and lapse rates); risks associated with arrangements with third parties, including joint ventures and distribution partners; inability of reinsurers to meet obligations or unavailability of reinsurance coverage; the impact of changes in capital, solvency or accounting standards, and tax and other legislation and regulations in the jurisdictions in which the Group operates.

As a result, the Group’s actual future financial condition, performance and results may differ materially from the plans, goals and expectations set out in the forward-looking statements within this announcement. The Group undertakes no obligation to update any of the forward-looking statements contained within this announcement or any other forward-looking statements it may make. Nothing in this announcement should be construed as a profit forecast.

Performance review

Total new business premiums were £231m for the half year ended 30 June 2015, a decrease of 44% on the same period last year.

SPE	**Half year ended 30 June 2015 £m**	Half year ended 30 June 2014 £m	Year ended 31 December 2014 £m
Individual retirement annuities	**128**	334	466
Defined benefit buy-in/ buy-out annuities	**68**	37	247
Individual care annuities	**33**	36	76
Individual protection	**2**	2	3
Total new business premiums	**231**	409	791

Individual retirement annuities

New business premiums for retirement annuities sold to individuals decreased by 62% to £128m (HY 2014: £334m).

The sales result in the first half of the year continues to be affected by lower annuity market activity and sales when compared to the pre-2014 Budget position. The comparative result for 2014 included pre-budget sales results and the completion of the majority of our pipeline cases at the time of the Budget announcement.

The second quarter of 2015 achieved sales of £74m, up from £54m in the first quarter which represents an increase over Q1 of 37%.

The second quarter has seen a modest increase in market activity after the Pension Freedom changes came into force in early April. We have seen an increase in the level of new quotations and a more marked increase in re-quote activity, which indicates that previously deferred cases may be coming back to the annuity market.

Whilst this improvement in market conditions is reflected, in part, in the sales performance in the quarter there remains significant uncertainty over the near-term level of annuity sales as customers and advisers continue to adapt to the new pensions tax rules. The recently announced Government review of the financial advice market is a welcome step in identifying how more consumers could benefit from proper advice when making a decision on their retirement income.

As the Pension Freedoms came into force the media commentary has focussed more on people's retirement income needs and the risks that the new freedoms posed to the security of pension income. It is clear that a guaranteed income for life to cover regular expenditure is a consumer priority, and that the purchase of an annuity to satisfy this need continues to be an attractive retirement option. It is also clear that longevity risk cannot be managed on an individual basis.

At the beginning of the second quarter, to help customers and advisers to better understand their retirement options, we launched new features on our retirement annuities to offer 'benefit based quotes' where advisers can obtain a quotation based on the level of income that their customer is targeting, together with extended value protection and longer guarantee periods. The take up of these options across the market has been relatively slow in the first weeks after launch, as advisers continue to get to grips with the new retirement income landscape.

The revisions to our proposition noted above were a first step towards delivery of our Retirement Account and we have made good progress in the development of the overall proposition, which we expect to launch later in the year. This will enable advisers and customers to produce a bespoke retirement income solution, combining investment, drawdown and guaranteed income in one account.

In the longer term, we continue to see the potential for our addressable share of the market increasing as more retirees are encouraged to shop-around through the impartial guidance process.

The long-term structural drivers behind the growth of the defined contribution pension market remain intact. The new regulations create the opportunity to develop new products where our unrivalled intellectual property and nimble product development capability mean we are well positioned for success in the future.

Defined benefit buy-in/ buy-out annuities

Defined benefit bulk annuity (DB) sales have grown to £68m up from £37m in the first half of 2014 which represents an 84% increase over the equivalent period last year.

Competition for the deals that are coming to market has been strong in the first half of the year, and we are pleased with the progress that we are making in the developing market for underwritten DB transactions

The investments that we have made, and continue to make, in the development of our defined benefit de-risking proposition into our support infrastructure and our sales capability are beginning to pay off. This will continue to ensure that we are best placed to succeed in this growing and potentially material market, which for our core target market of sub-£100m schemes has been estimated at £100 billion of liabilities.

Our focus remains on increasing the proportion of deals that are medically underwritten. Our distribution network and Employee Benefits Consultant (EBC) relationships are strong and the acceptance of medically underwritten transactions amongst EBCs, Scheme Trustees and sponsoring companies is growing. Indeed, we were delighted that the strength of our proposition was recognised in the period with Partnership receiving an industry award for "Buyout Firm of the Year" at the European Pension Awards.

The DB market has seen an industry-wide slow start to 2015 but market feedback points to trustee and EBC activity growing into the second half. Our pipeline comprises transactions across a wide selection of EBCs, reflecting both the increasing recognition of medical underwriting in bulk de-risking and stronger and broader relationships with EBCs.

The timing and size of future DB deals will be difficult to accurately predict and sales are likely to be lumpy, however, our current pipeline provides confidence in our ability to achieve our target of at least £200m in 2015.

In the longer term we are confident that our market-leading experience and track record in medical underwriting provides the opportunity for significant growth.

Individual care annuities

Sales of care annuities decreased by 8% to £33m down from £36m in the first half of 2014.

In general through 2014 and into 2015 we have seen advisers selling care annuities returning to the market after a period of uncertainty surrounding Government Care policy.

The recent announcement by the Government of the delay to the introduction of the 'care cap' leaves consumers exposed to uncapped care liabilities. It remains the case that those who are looking to cap their liabilities but secure a guaranteed income for life, while in care, have the option to choose an immediate needs care annuity.

Whether this delay leads to an increase in market activity remains to be seen, however, the conversion from quote to policy for care annuities can be lengthy and unpredictable and the impact on sales can take time to be seen.

Despite a modest fall in sales of care annuities in the first half of the year we remain optimistic about the medium term outlook for this proposition.

Individual protection

Protection sales remained flat at £2m (HY 2014: £2m). Partnership regards protection as an opportunity to leverage our proprietary Intellectual Property (IP) to be able to provide protection cover for people that other insurers cannot quote for.

While a small component of our business in 2015, there are significant opportunities to grow in the future.

Operating profit before tax

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
New business operating (loss)/ profit	**(2,425)**	17,803	38,962
In-force operating profit	**13,476**	6,840	8,477
Long-term expected return on surplus assets	**7,241**	8,746	16,328
Operating profit	**18,292**	33,389	63,767

Total operating profit

Total operating profit is considered by the Board to be the core measure of underlying performance for the Group.

Total operating profit in the half year to 30 June 2015 was £18.3m (HY 2014: £33.4m), a decrease of 45%.

Total operating expenses of £34m were incurred reflecting the impact of cost management actions taken in H2 2014 in response to the 2014 Budget. This represents a 19% reduction versus H1 2014 expenses. Over 90% of our total operating expenses are allocated to new business, reflecting the level of resource required to support new business vs inforce business. We remain well placed to achieve our targeted c. £75m cost base for FY15.

The decrease in operating profit reflects a lower contribution from new business and lower contribution from expected return on surplus assets, partially offset by a higher in-force profit.

The component parts of the total operating profit and the movements in each are set out below:

New business operating profit

New business operating profit indicates the level of profit generated on the business sold in the period.

The new business operating loss was £(2.4)m (HY 2014: profit £17.8m), representing a new business margin of (1.0)% (HY 2014: 4.4%).

We have maintained our disciplined approach to pricing through the recent market disruption ensuring that new business covers its capital requirement.

The decrease in new business operating profit compared to 2014 is therefore largely due to the lower volumes of annuity sales and the leveraged impact of the expense base. While expenses have been reduced, this has not been sufficient to offset the impact of the lower sales volumes.

We anticipate that the new business margin, net of expenses, will increase in the second half of the year as the level of individual annuity volumes increases and as we deliver the expected level of defined benefit sales.

In-force operating profit

In-force operating profit shows the profits earned in the management of the in-force business and demonstrates the robustness of the key operating assumptions made at point-of-sale.

Profits emerging from the in-force book in the half year to 30 June 2015 were £13.5m (HY 2014: £6.8m).

The underlying level of in-force operating profits reflects the increased size of the business and higher planned margins on mortality as we decided to increase the level of retained risk, particularly in respect of DB business, as well as positive longevity experience on care business.

Long-term expected return on surplus assets

Long-term expected return on surplus assets measures the success of our investment strategy for surplus assets and contributes towards our objective of maximising risk-adjusted returns.

We recorded a decrease in expected return on surplus assets to £7.2m (HY 2014: £8.7m), reflecting a change in the asset mix in the period away from bonds and into cash, coupled with lower longer term expected rates of return on bonds.

The long-term expected return is derived from applying an average expected yield appropriate to the category of surplus assets held, and is adjusted for the best-estimate expected level of defaults on those investments. The risk-adjusted annual yields applied to surplus assets during the period were:

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
Cash	**0.5%**	0.5%	0.5%
Gilts	**3.0%**	3.0%	3.0%
Corporate bonds	**4.0%**	4.5%	4.5%
Equity Release mortgages	**6.0%**	6.0%	6.0%

IFRS profit before tax

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
New business operating (loss)/ profit	**(2,425)**	17,803	38,962
In-force operating profit	**13,476**	6,840	8,477
Long-term expected return on surplus assets	**7,241**	8,746	16,328
Operating profit	**18,292**	33,389	63,767
Investment variances	**(6,532)**	(9,043)	(23,491)
Non-recurring expenditure	**(6,445)**	(9,656)	(16,348)
Other	**167**	321	139
Interest on borrowings	**(2,554)**	-	-
Profit from continuing operations before tax	**2,928**	15,011	24,067

IFRS profit before tax represents the (pre-tax) level of profit potentially available for distribution to shareholders and includes the impact of non operating items on profit. Non operating items comprise investment and economic variances against assumptions, investment and economic assumption changes, non recurring expenditure, interest on external borrowings and other non operating items.

Investment variances

The impact of changes in risk free rates and credit spreads was broadly neutral. There were minor adverse variances between expected and achieved rates of investment return in the period.

Non-recurring expenditure

Non-recurring expenditure of £6.4m for the period (HY 2014: £9.7m) includes costs relating to Solvency II developments, development of our Defined Benefit proposition, our Retirement Account proposition and the International Care business. The 2014 non-recurring expenditure included restructuring costs of £1.2m and £6.0m due to impairment of distribution assets following the Budget announcement in addition to regulatory and proposition developments.

Other items

Other items of £0.2m (HY 2014: £0.3m) relate to interest on cash holdings at the holding company, sundry income and costs arising in the distribution subsidiaries of the Group and holding company expenses.

Interest on borrowings

The company issued a £100m Solvency II tier 2 qualifying debt instrument at par in March 2015 with a maturity date of March 2025 and a coupon of 9.5%. Prior to this point the company was debt free.

The interest charge in respect of the period since issue was £2.6m (HY 2014: £nil).

Earnings per share

Basic earnings per share was 1 pence (HY 2014: 3 pence). The decrease in earnings per share reflects the lower profit for the period. The basic weighted average number of shares was largely unchanged. Diluted earnings per share was equivalent to basic earnings per share as the dilutive impact of instruments potentially giving rise to additional ordinary shares does not have a material impact.

Dividends

Dividends will be recognised in the Consolidated Statement of Changes in Equity in the period in which they are declared. As set out in note 12, an interim dividend of 0.5 pence per share, at an expected total cost of £2.0m was declared on 10 August 2015 for payment in October 2015 and will be reflected in the Statement of Changes in Equity in the second half of the year.

MCEV

	Half year ended 30 June 2015			Half year ended 30 June 2014	Year ended 31 December 2014
	Covered business	**Non covered business**	**Total Group MCEV**	Total Group MCEV	Total Group MCEV
	£000's	**£000's**	**£000's**	£000's	£000's
Opening Group MCEV	**557,532**	**18,754**	**576,286**	519,633	519,633
Opening adjustments	**-**	**-**	**-**	-	-
Adjusted opening Group MCEV	**557,532**	**18,754**	**576,286**	519,633	519,633
Operating MCEV earnings	**18,608**	**-**	**18,608**	41,862	86,502
Non-operating MCEV earnings	**(2,629)**	**156**	**(2,473)**	(5,185)	(17,071)
Total MCEV earnings	**15,979**	**156**	**16,135**	36,677	69,431
Other movements in IFRS net equity	**-**	**1,366**	**1,366**	239	1,222
Dividends	**-**	**(4,000)**	**(4,000)**	(12,000)	(14,000)
Closing Group MCEV	**573,511**	**16,276**	**589,787**	544,549	576,286

Total market consistent embedded value (MCEV) as at 30 June 2015 was £589.8m, which compares to MCEV at 31 December 2014 of £576.3m. This represents £1.47 per share (31 December 2014: £1. 44 per share).

MCEV movements in the period

The MCEV growth in the period was driven by the MCEV operating profit, offset by dividends and non-operating losses. The result for the year included the benefit of lower UK corporate taxes and a lower effective future tax rate due to the issue of the Tier 2 bond during the period.

The principal change in the value of the non-covered business is due to the payment of the 2014 final dividend of £4m.

Further details of MCEV and its movements in the period are set out in MCEV Supplementary Information which follows IFRS Financial Information.

Assets under management

Assets by credit rating[1]:

	Half year ended 30 June 2015 £m	Year ended 31 December 2014 £m
AAA	***676***	*816*
AA	***326***	*235*
A	***1,138***	*1,251*
BBB	***1,308***	*1,281*
BB	***37***	-
Total Fixed Interest Securities	**3,485**	3,583
Commodity Trade Finance loans	**-**	2
Loans secured by residential mortgages	**1,247**	1,212
Loans secured by commercial mortgages	**38**	38
Cash	**246**	87
Assets under management	**5,016**	4,922

Our investment strategy is to invest in assets that produce superior risk-adjusted yields and are efficient from an economic capital perspective.

Assets under management have increased to £5,016m (31 December 2014: £4,922m), including accrued interest, excluding £242m (31 December 2014: £270m) of assets that the Group manages on behalf of reinsurers under certain reinsurance arrangements.

Our fixed income security portfolio is of high overall quality with in excess of 61% (31 December 2014: 64%) invested in bonds rated A or better and near 100% rated BBB or better.

During the first half of the year, the proportion of the assets invested in BBB rated bonds increased due to out-performance relative to our more highly rated bonds and due to normal investment trading activity.

We have continued to source newly originated equity release loans and, whilst we continue to seek out attractive bulk purchases, we have not completed any in the year to date. Newly originated loans in 2015 totalled £60m (HY 2014: £80m). The level of equity release mortgage assets as a proportion of total assets under management at 30 June 2015 was 25% (31 December 2014: 25%).

We have invested £38m into commercial mortgage assets to date out of a mandate for £150m held by NM Rothschild & Sons Ltd and have a high quality pipeline of transactions. Partnership benefits from Rothschild's extensive experience of managing this asset class and Rothschild is co-investing alongside Partnership.

We are actively investigating other alternative assets that can provide superior risk-adjusted returns.

[1] Median rating of Standard and Poor's, Moody's and Fitch, where available.

Capital management

Economic capital (EC) is the principal risk-based capital measure used by the Board. EC is based on the Board's view of the available capital and required capital calibrated to a 1 in 200 year risk event. The coverage ratio expresses the available capital as a percentage of the required capital.

The level of excess economic capital at 30 June 2015 was £223m (31 December 2014: £132m or £232m when including the £100m external debt raised on 2 March 2015). This represents a capital coverage ratio of 156% at 30 June 2015 (31 December 2014: 134% or 159% including external debt on 2 March 2015), well in excess of our targeted minimum of 125% (under normal economic circumstances).

The stress and scenario tests we perform, which reflect the key risks borne by the Group, continue to show a robust capital position. This demonstrates the close matching of assets and liabilities, efficient use of reinsurance, and monitoring of risk levels against our Board tolerances.

The EC surplus (before final dividend) decreased by £9m in the period due to new business required capital increasing by more than the post-dividend surplus.

The EC and IGD capital positions as at 30 June 2015 are calculated at the Partnership Assurance Group plc level.

	Economic capital		IGD	
	Half year ended 30 June 2015	Year ended 31 December 2014 proforma[1]	**Half year ended 30 June 2015**	Year ended 31 December 2014 proforma[1]
	£m	£m	**£m**	£m
Total Capital Available	**622**	625	**563**	568
Capital Required	**399**	393	**225**	224
Excess Surplus	**223**	232	**338**	344
Coverage (%)	**156%**	159%	**250%**	254%

[1] Proforma before final dividend and including £100m bond agreed on 2 March 2015

Stress and scenario testing

The Group undertakes stress and scenario tests to ensure the robustness of the EC solvency position, having regard to the material financial and non-financial risks that the Group is exposed to. The most material risks to the level of capital adequacy on an economic basis arise from the Group's investment in assets with credit risk exposure, interest rate risk, residential property risk exposure, and longevity risk. Other risks are either not material or are appropriately hedged to leave minimal exposure for the Group.

The impact of the stress and scenario tests for the most material balance sheet risks are set out below:

	Economic Capital Ratio Sensitivities			
	Half year ended 30 June 2015		Year ended 31 December 2014 proforma[1]	
	£m	**%**	£m	%
Economic capital surplus/ coverage	**223**	**156%**	232	159%
Impact on surplus/ revised coverage				
Interest +1%	**42**	**176%**	31	176%
Interest -1%	**(46)**	**138%**	(46)	141%
Credit spread widening +100bps	**(4)**	**158%**	(8)	159%
"Lehman" crisis*	**(36)**	**160%**	(49)	157%
Eurozone crisis*	**(20)**	**159%**	(31)	158%
Property -10% price fall	**(51)**	**142%**	(44)	147%
Longevity +5% deterioration	**(33)**	**147%**	(30)	151%

[1] Proforma including £100m bond completed on 23 March 2015

*Eurozone crisis and "Lehman" crisis scenarios have been modelled by applying the credit spreads of 7 October 2011 and 5 December 2008 respectively.

Solvency II

Our Solvency II programme is designed to ensure that the Group meets the Solvency II requirements when they go live on 1 January 2016.

Our programme is planned so as to deliver the standard formula approach to capital measurement. We continue to keep the option of developing an internal model under review, with a view to being ready to apply for an internal model for certain risks if and when it is considered appropriate.

Although the way that the regulations will be applied in practice is still uncertain, based on our interpretation of the Solvency II regulations, the Group is expected to remain well capitalised. We are putting in place plans to mitigate risks in the regulations, such as the treatment of equity release assets in the matching adjustment calculation.

Risk Management and Internal Control

The Group has a risk management framework in place comprising formal committees, a suite of formal policies, a common risk assessment process and risk review functions. The Group's risk management framework remains as set out on pages 34 and 35 of the 2014 Annual Report and Accounts.

Principal risks and uncertainties

The principal risks and uncertainties faced by the Group remain consistent with those set out on pages 36 to 39 of the 2014 Annual Report and Accounts. The following table summarises the changes to the principal risks since the start of 2015.

Risk Management and Internal Control

Risk	Strategic objective	Description	How we manage the risk	Description of risk change
Underwriting, pricing and reserving risk	Leveraging Partnership's proprietary IP	Underwriting and pricing risk is the risk that insurance contracts will be written that are not within the Board's risk appetite, or that the premium charged for that business is not adequate to cover the risks borne by the Group. The accurate pricing of non-standard annuities is dependent on the Group's assessment of the impact on prospective customers' longevity of various medical and lifestyle factors and an estimate of future investment yields and credit default. The actual timing of deaths and investment income experience may be inconsistent with the assumptions and pricing models used in underwriting and setting prices for its products. Reserving risk is the risk that the reserves have been calculated incorrectly, or the assumptions used in the calculations are inappropriate.	As the Group's insurance business is targeted at people with conditions affecting their life expectancy, or people seeking to fund domiciliary or residential care, the underwriting risk is managed through the use of highly trained, and qualified underwriting staff, together with detailed underwriting manuals designed to cover a large range of medical conditions. We have developed our own proprietary underwriting manuals for retirement annuity business and those seeking care funding, based on industry standard mortality tables modified to take account of our experience data. The assumptions used in the reserving for future policyholder payments are set based on available market and experience data, on the advice of our Actuarial Function Holder. The assumptions are approved by the Board. The reserves are calculated using recognised actuarial methods with due regard to the actuarial principles set out in the PRA's sourcebooks, including appropriate levels of prudential margin against future adverse experience.	No change in first half of 2015.

Risk Management and Internal Control

Risk	Strategic objective	Description	How we manage the risk	Description of risk change
Specific insurance risk	Maximising risk adjusted returns	Insurance risk on the Group's annuity contracts arises through longevity risk and through the risk that operating factors, such as administration expenses, are worse than expected. Insurance risk on the Group's protection policies arises through higher than expected mortality levels.	The Group's longevity and mortality experience is monitored on a regular basis and compared to the underlying assumptions used to reserve for future insurance payments. The exposure to longevity and mortality risk is reduced through the use of reinsurance. Expense risk is managed through regular assessment and quarterly reforecasting of expenses incurred against budgets.	There has been variation in the financial consequence of this risk as long-term risk free rates have varied. As these rates rise the consequence of longevity risk (should that risk materialise) decreases.
Interest rate and spread risk	Maximising risk adjusted returns	Interest rate risk arises from open positions in fixed and variable rate stock issued by government and corporate bodies that are exposed to general and specific market movements. The Group is exposed to the market movements in interest rates to the extent that the asset value movement is different to the accompanying movement in the value of its insurance liabilities. The difference between asset and liability movements can arise from both a change in the absolute level of interest rates, and from a change in the 'spread' (that is the level of interest rates applying to an asset in excess of the risk-free interest rate).	The Group manages its interest rate risk within an asset liability management (ALM) framework that has been developed to achieve investment returns in excess of its obligations under insurance contracts. The principal technique of the ALM framework is to match assets to the liabilities arising from insurance contracts by reference to the type of benefits payable to policyholders.	No change in the first half of 2015.
Market credit risk	Maximising risk adjusted returns	Market credit risk is the risk that the Group invests in assets that may default. If an asset fails to repay either interest or capital, or that payment is significantly delayed, the Group may make losses and be unable to meet liabilities as they fall due.	The Group's Investment Management Guidelines set out maximum exposure to bonds issued by a single, or related group of, counterparty(/ies) and to credit ratings. The allowance made for issuer default in the Group's valuation is regularly monitored and kept up to date.	No change in the first half of 2015.

Risk Management and Internal Control

Risk	Strategic objective	Description	How we manage the risk	Description of risk change
Property risk	Maximising risk adjusted returns	Property risk arises from the provision of a protected equity guarantee on the mortgages underlying the equity release assets purchased. The Group is exposed to the risk that property values do not rise sufficiently, or that the property is not maintained properly, to recover the full value of the loan made plus accrued interest.	The Group manages its purchase of loan assets to a level appropriate to its liability profile and ensures that the purchase prices of loan assets reflect a prudent assessment of future property price growth. Appropriate limits are applied to the "loan to value ratio" in order to limit the risk exposure to the Group. The Group seeks to avoid excess concentration of property holdings in any geographical area.	No change in the first half of 2015.
Liquidity risk	Maximising risk adjusted returns	Liquidity risk arises where cash flows from investments and from new premiums prove insufficient to meet our obligations to policyholders and other third parties as they fall due.	The Group's ALM framework ensures that cash flows are sufficient to meet both long- and short-term liabilities. The Group maintains a minimum level of cash and highly liquid assets such that, in the extreme scenario of new business cash flows being insufficient to meet current obligations, those obligations can continue to be met.	No change in the first half of 2015.
Counterparty credit risk (excluding investment assets)	Maximising risk adjusted returns	Credit risk arises if another party fails to honour its obligations to the Group including failure to honour these obligations in a timely manner. The Group's primary credit risk exposure arises from the inability of the reinsurers to meet their claim payment obligations.	The Group has arrangements with its reinsurers whereby most reinsurance premiums are either deposited back to the Group or held by a third party in a trust arrangement. In addition, the Group's reinsurance policy is to seek to choose companies with a minimum 'A' credit rating.	No change in the first half of 2015.

Risk Management and Internal Control

Risk	Strategic objective	Description	How we manage the risk	Description of risk change
Distribution risk	Improving access for customers	Distribution risk arises from adverse changes in customer need for the Group's products, the Group's competitive landscape or its relationships with intermediaries.	The Group derives competitive advantage from its proprietary underwriting intellectual property which it considers to be unique in the non-standard annuity and individual care annuity markets. It is the Group's strategy to continue to innovate and introduce new products and propositions that meet customer needs and leverage this intellectual property to protect its competitive position. The Group maintains a multi-channel distribution strategy in order to diversify and reduce concentration risk.	Sales in the first half of 2015 continued to be affected by lower annuity market activity when compared to the pre-2014 Budget position. Whilst the second quarter of 2015 saw a modest increase in market activity there remains significant uncertainty over the near-term level of annuity sales as customers and advisors adapt to the new pension tax rules. Alongside the development of its UK retirement account proposition, the successful acceleration of the Group's Defined Benefit proposition and the launch of its US care opportunity are critical to the Group's ability diversify its product portfolio.
Operational risk	Maximising risk adjusted returns	Operational risk arises from inadequate or failed internal processes, people and systems or from external events	The Group maintains a suite of risk management tools to help manage its operational risks including facilitated risk and control self-assessments, risk event management and loss reporting. Underlying and informing the operation of these tools is a framework of formal policies and controls which govern the management and oversight of the risks faced by the Group. These include business continuity and disaster recovery arrangements. Operational risk is overseen by the Executive Operational Risk Committee.	No change in the first half of 2015.

Risk Management and Internal Control

Risk	Strategic objective	Description	How we manage the risk	Description of risk change
Regulatory, legal and political environment risk	Maximising risk adjusted returns	Regulatory, legal and political environment risk arises where changes in regulation or legislation may result in a detrimental effect on the Group's strategy and profitability.	The Group's strategic planning process sets a medium term strategy based on our understanding of the regulatory, legal and political risks inherent in the markets in which it operates. This is informed by active and constructive engagement with policymakers and regulators both directly and indirectly through trade associations. Our planning and response capability is supported by continued monitoring of the regulatory, legal and political landscape.	No change in the first half of 2015. The Group continues to work with the Prudential Regulation Authority in preparation for the incoming Solvency II regime (binding on insurers from 1st January 2016) and take steps to mitigate any potentially adverse effects of the regulation, including restructuring assets where necessary.

Directors’ Responsibilities Statement

Each of the Directors of the Company confirms that to the best of their knowledge:

(a) the condensed set of financial statements has been prepared in accordance with IAS 34: *Interim financial reporting* as adopted by the European Union;

(b) the interim management report includes a fair review of the information required by Disclosure and Transparency Rule 4.2.7, namely important events that have occurred during the period and their impact on the condensed set of financial statements, as well as a description of the principal risks and uncertainties faced by the Company and the undertakings included in the condensed consolidated financial statements taken as a whole for the remaining six months of the financial year; and

(c) the interim management report includes a fair review of material related party transactions and any material changes in the related party transactions described in the last annual report as required by Disclosure and Transparency Rule 4.2.8.

By order of the Board

Steve Groves
Chief Executive Officer
London
10 August 2015

David Richardson
Chief Financial Officer

Note:

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial information differs from legislation in other jurisdictions.

Independent review report to Partnership Assurance Group plc

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2015 which comprises the condensed consolidated statement of comprehensive income, the condensed consolidated statement of changes in equity, the condensed consolidated statement of financial position, the condensed consolidated cash flow statement and the related notes 1 to 12. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the Company those matters we are required to state to it in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our review work, for this report, or for the conclusions we have formed.

Directors’ responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom’s Financial Conduct Authority.

As disclosed in note 2, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34 “Interim Financial Reporting” as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2015 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom’s Financial Conduct Authority.

Deloitte LLP
Chartered Accountants and Statutory Auditor
10 August 2015
London, United Kingdom

IFRS FINANCIAL INFORMATION

Condensed consolidated statement of comprehensive income

For the half year ended 30 June 2015

	Note	**Half year ended 30 June 2015 £000's**	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Gross premiums written	3	**242,778**	385,340	760,638
Outward reinsurance premiums		**(76,987)**	(230,974)	(307,959)
Net premiums earned		**165,791**	154,366	452,679
Net investment income		**6,648**	108,616	299,232
Share of results of joint ventures & associates accounted for using the equity method		**1**	(166)	(179)
Profit on loss of control of subsidiary		**-**	-	158
Other income		**55**	275	207
Total income		**172,495**	263,091	752,097
Gross claims paid		**(204,230)**	(191,080)	(390,570)
Reinsurers' share of claims paid		**130,393**	125,660	255,957
		(73,837)	(65,420)	(134,613)
Change in insurance liabilities:				
Gross amount		**59,141**	(305,833)	(883,524)
Reinsurers' share		**(103,149)**	185,179	405,259
		(44,008)	(120,654)	(478,265)
Acquisition costs		**(1,334)**	(3,480)	(4,997)
Investment expenses and charges		**(6,906)**	(6,995)	(14,352)
Interest on external borrowings		**(2,554)**	-	-
Other operating expenses		**(40,928)**	(51,531)	(95,803)
		(51,722)	(62,006)	(115,152)
Total claims and expenses		**(169,567)**	(248,080)	(728,030)
Profit from continuing operations before tax		**2,928**	15,011	24,067
Income tax charge from continuing operations	4	**(692)**	(3,950)	(5,213)
Profit for the period		**2,236**	11,061	18,854
Profit attributable to:				
- Owners of the Parent		**2,236**	11,059	18,852
- Non-controlling interest		**-**	2	2
Basic earnings per ordinary share	6	**£0.01**	£0.03	£0.05
Diluted earnings per ordinary share	6	**£0.01**	£0.03	£0.05

Condensed consolidated statement of changes in equity

For the half year ended 30 June 2015

	Attributable to Owners of the Parent						Non-controlling interest	Total
	Share Capital	Share Premium	Merger Reserve	Shares held by Employee Benefit Trust	Retained profit	Total		
	£000's	£000's	£000's	£000's	£000's	£000's	£000's	£000's
At 1 January 2014	40,000	435,249	(24,521)	(58)	147,945	598,615	(66)	598,549
Share-based payments	-	-	-	-	239	239	-	239
Profit for the period	-	-	-	-	11,059	11,059	2	11,061
Disposal of subsidiary	-	-	-	-	-	-	64	64
Dividends paid	-	-	-	-	(12,000)	(12,000)	-	(12,000)
At 30 June 2014	40,000	435,249	(24,521)	(58)	147,243	297,913	-	597,913
At 1 January 2014	40,000	435,249	(24,521)	(58)	147,945	598,615	(66)	598,549
Share-based payments	-	-	-	(78)	1,301	1,223	-	1,223
Disposal of subsidiary	-	-	-	-	-	-	64	64
Dividends paid	-	-	-	-	(14,000)	(14,000)	-	(14,000)
Profit for the year	-	-	-	-	18,852	18,852	2	18,854
At 31 December 2014	40,000	435,249	(24,521)	(136)	154,098	604,690	-	604,690
At 1 January 2015	**40,000**	**435,249**	**(24,521)**	**(136)**	**154,098**	**604,690**	**-**	**604,690**
Share-based payments	**-**	**-**	**-**	**14**	**1,351**	**1,365**	**-**	**1,365**
Profit for the period	**-**	**-**	**-**	**-**	**2,236**	**2,236**	**-**	**2,236**
Dividends paid	**-**	**-**	**-**	**-**	**(4,000)**	**(4,000)**	**-**	**(4,000)**
At 30 June 2015	**40,000**	**435,249**	**(24,521)**	**(122)**	**153,685**	**604,291**	**-**	**604,291**

Condensed consolidated statement of financial position

As at 30 June 2015

	Note	Half year ended 30 June 2015 £000's	Year ended 31 December 2014 £000's
Assets			
Property, plant and equipment		**10,702**	12,557
Goodwill		**126,207**	126,207
Other intangible assets		**14,255**	15,219
Financial assets	**8**	**4,840,070**	4,910,904
Investment in joint ventures and associates		**233**	233
Reinsurance assets	**7**	**3,142,859**	3,246,008
Insurance and other receivables		**30,651**	39,167
Prepayments and accrued income		**3,761**	3,615
Deferred tax assets		**937**	519
Cash and cash equivalents		**245,890**	87,251
Total assets		**8,415,565**	8,441,680
Equity			
Share capital		**40,000**	40,000
Share premium		**435,249**	435,249
Merger reserve		**(24,521)**	(24,521)
Shares held by Employee Benefit Trust		**(122)**	(136)
Retained profit		**153,685**	154,098
Total equity attributable to owners of the Parent		**604,291**	604,690
Liabilities			
Insurance liabilities	**7**	**5,171,970**	5,231,112
Insurance and other payables		**24,655**	29,527
Financial liabilities	**8**	**2,506,413**	2,571,288
External borrowings	**9**	**102,464**	-
Current tax liabilities		**4,567**	3,735
Deferred tax liability		**1,205**	1,328
Total liabilities		**7,811,274**	7,836,990
Total equity and liabilities		**8,415,565**	8,441,680

Condensed consolidated cash flow statement

For the half year ended 30 June 2015

	Note	**Half year ended 30 June 2015**	Half year ended 30 June 2014	Year ended 31 December 2014
		£000's	£000's	£000's
Cash from operations	**10**	**63,548**	41,228	11,664
Corporation tax received/ (paid)		**36**	(13,457)	(19,705)
Net cash from/ (used in) operating activities		**63,584**	27,771	(8,041)
Cash flows from investing activities:				
Investment in associate		**-**	(48)	(48)
Purchase of property, plant and equipment		**(193)**	(22)	(1,308)
Purchase of other intangible assets		**(662)**	(1,462)	(2,093)
Net cash used in investing activities		**(855)**	(1,532)	(3,449)
Cash flows from financing activities:				
Proceeds from issuance of Subordinated Debt	**9**	**99,910**	-	-
Dividends paid to shareholders	**6**	**(4,000)**	(12,000)	(14,000)
Net cash from/ (used in) financing activities		**95,910**	(12,000)	(14,000)
Net increase/ (decrease) in cash and cash equivalents		**158,639**	14,239	(25,490)
Cash and cash equivalents at beginning of period		**87,251**	112,741	112,741
Cash and cash equivalents at end of period		**245,890**	126,980	87,251

Notes to the condensed consolidated financial statements for the period ended 30 June 2015

1. Activities of business and legal structure of the Company

Partnership Assurance Group (PAG) plc (the "Company") is incorporated in the United Kingdom and registered in England and Wales as a public company limited by shares. The Company's registered office address is 5th Floor, 110 Bishopsgate, London, EC2N 4AY.

The principal activity of the Company is that of a holding company. The Company and the entities controlled by the Company (its "subsidiaries") are collectively "the Group".

The share capital of the Company consists of 399,999,971 shares of 10 pence each. The Company has a Premium Listing on the London Stock Exchange.

2. Basis of preparation

The condensed consolidated financial statements for the six months to 30 June 2015 have been prepared in accordance with IAS 34, Interim Financial Reporting, as issued by the International Accounting Standards Board and adopted by the European Union, and the Disclosure and Transparency Rules of the Financial Conduct Authority.

The accounting policies applied in the condensed consolidated financial statements are the same as those applied in the Partnership Assurance Group plc Annual Report and Accounts 2014 ("2014 Report and Accounts"), with the exception of the changes detailed below.

The results for the six months to 30 June 2015 and 2014 are unaudited. The results for the year to 31 December 2014 full year IFRS basis results have been taken from the 2014 Report and Accounts. The auditor has reported on the 2014 Report and Accounts which have been delivered to the Registrar of Companies. The auditor's report was (i) unqualified, (ii) did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying their report, and (iii) did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

The presentation currency of the Group is Sterling. Unless otherwise stated, the amounts shown in the condensed consolidated financial statements are in thousands of pounds Sterling (£'000).

The Directors have undertaken a going concern assessment in accordance with 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting', published by the Financial Reporting Council in September 2014. After making appropriate enquiries, the Directors consider the adoption of the going concern basis of accounting appropriate.

Changes in accounting policy

The Group has adopted the following new or revised standards that became effective (as adopted by the EU) as of 1 January 2015:

An amendment to IAS 19 Employee benefits clarifying the requirements on attributing to periods of service contributions from employees or third parties that are linked to service. The amendment has no impact on the financial statements in the current or prior periods.

Minor amendments to various standards arising from the Annual Improvements 2010 - 2012 and 2011 – 2013 cycles have no impact on the financial statements in the current or prior periods.

Other changes in accounting policy are:

External Borrowings – During the period the Group issued a £100m bond and applied the following policy to the resulting liability: External borrowings are recorded at the proceeds received, net of direct issue costs. Issue costs are capitalised and charged to the consolidated statement of comprehensive income over the life of the loan using the effective interest method. Interest payable is accounted for on an accruals basis in the consolidated statement of comprehensive income. Gains and losses on the repurchase, settlement or otherwise cancellation of external borrowings are recognised respectively in the income and interest expenses and charges.

3. Segmental analysis

Information is provided to the Board, which identifies operating profit split between that achieved on new business written in the period, that which derives from in-force policies and that relating to the long-term expected return on surplus assets, and therefore this split forms the reportable operating segments in accordance with IFRS 8 “Operating Segments”.

New business revenue is reported as Single Premium Equivalent (“SPE”), being the actual single premium for single premium business, and ten times the annual premium for a regular premium business written during the year. These revenue measures are monitored by the Board separately for each core target market.

The table below shows operating profit for each year, together with a reconciliation to profit before tax:

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
New business operating (loss)/ profit	**(2,425)**	17,803	38,962
In-force operating profit	**13,476**	6,840	8,477
Long-term expected return on surplus assets	**7,241**	8,746	16,328
Operating profit	**18,292**	33,389	63,767
Investment variances	**(6,532)**	(9,043)	(23,491)
Non-recurring expenditure	**(6,445)**	(9,656)	(16,348)
Other	**167**	321	139
Interest on borrowings	**(2,554)**	-	-
Profit from continuing operations before tax	**2,928**	15,011	24,067

Investment variances reflect:

a) the difference between actual performance on investment assets (e.g. cash, gilts, corporate bonds and equity release) over the reporting period and the investment yield allowed for in the calculation of in-force liabilities at the start of the reporting period;

b) the difference between the yield on investment assets allowed for in the calculation of new business profits and the actual investment performance including differences arising from investing at different yields and asset allocations than those expected when pricing new business;

c) the difference between actual performance on investment assets and long-term assumed return on surplus assets; and

d) the impact of changes in the best-estimate credit default allowance made against the Group’s invested assets.

Non-recurring expenditure of £6.4m for the period (HY 2014: £9.7m) includes costs relating to Solvency II developments, development of our defined benefit proposition, our Retirement Account proposition and the International Care business.

Other operating expenses, in the Condensed consolidated statement of comprehensive income, includes underlying operating expenses and non-recurring expenditure.

The profit measure used by the Group Board to monitor performance is operating profit before tax, analysed between new business operating profit, in-force operating profit and the long-term expected return on surplus assets. Each component of operating profit is explained as:

- New business operating profit is profit generated from new business completed in the period, calculated using actuarial assumptions applicable at the time the new business was written, and utilising a discount rate based upon investment yields on investment assets (e.g. cash, gilts, corporate bonds and loans secured by mortgages) used to generate the annuity quotation, net of expenses allocated against new business.
- In-force operating profit is generated from the actual experience measured against the assumed experience in the actuarial basis. The actuarial basis includes a number of assumptions, the most material of which are mortality levels, levels of default on investments, expense levels (to

maintain the business in-force), levels of inflation, and lapse rates (for regular premium business). In-force operating profit also includes the effect recognised in the IFRS profit arising from changes to the reported value of insurance (and associated financial) liabilities resulting from changes to the actuarial assumptions, valuation methods, or underlying data, made subsequent to the point of sale.

- Return on surplus assets is the long-term, risk adjusted, expected return on investments surplus to those investments that are used to back insurance liabilities. The long-term expected return is derived from applying an average expected yield appropriate to the category of surplus assets held and is adjusted for the best estimate expected level of defaults on those investments. The risk adjusted annual yields applied to surplus assets during the period were:

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
Cash	**0.5%**	0.5%	0.5%
Gilts	**3.0%**	3.0%	3.0%
Corporate bonds	**4.0%**	4.5%	4.5%
Equity Release mortgages	**6.0%**	6.0%	6.0%

a) Segmental analysis of new business revenue by target market

SPE	**Half year ended 30 June 2015 £000's**	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Individual retirement annuities	**127,971**	334,313	465,840
Defined benefit buy-in/ buy-out annuities	**67,930**	36,837	246,573
Individual care annuities	**33,269**	36,354	75,741
Individual protection	**2,141**	1,537	3,083
Total SPE	**231,311**	409,041	791,237

b) Reconciliation of new business revenue by target market to gross premiums written

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Total SPE	**231,311**	409,041	791,237
Adjustment in respect of regular premium business	**(406)**	100	135
Change in premiums receivable - not included in SPE	**11,873**	(23,801)	(30,734)
Gross premiums written	**242,778**	385,340	760,638

Product revenue information

The following table illustrates revenue by product as required by IFRS 8 'Operating Segments'. All revenues from external customers are predominantly derived from business originated in the UK, and as such no geographical information is disclosed.

The Board consider the Group's external customers to be the individual policyholders. As such, the Group is not reliant on any individual customer.

An analysis of gross premiums written by product is set out below:

Gross premiums written	**Half year ended 30 June 2015 £000's**	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Individual retirement annuities	**139,843**	310,512	435,106
Defined benefit buy-in/ buy-out annuities	**67,930**	36,837	246,573
Individual care annuities	**33,335**	36,422	75,864
Individual protection	**1,670**	1,569	3,095
Total gross premiums written	**242,778**	385,340	760,638

4. Income tax charge

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Current taxation:			
Tax charge for the year	**1,233**	3,234	6,015
Adjustment in respect of prior periods	**-**	-	(2,035)
	1,233	3,234	3,980
Deferred taxation:			
Tax (credit)/ charge for the year	**(541)**	716	1,233
Net taxation charge	**692**	3,950	5,213

The income tax charge for all periods presented is in respect of continuing operations.

The actual tax charge of the Group differs from the expected tax charge, computed by applying the average rate of UK corporation tax for the year of 20.25% (30 June 2014: 21.5%, 31 December 2014: 21.5%), as follows:

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 £000's	Year ended 31 December 2014 £000's
Profit before tax	**2,928**	15,012	24,067
Current taxation at 20.25% (2014: 21.5%)	**593**	3,227	5,173
Disallowable expenses	**19**	21	51
Adjustment in respect of prior periods	**-**	-	(2,035)
Adjustments to deferred tax in respect of prior periods	**6**	448	1,903
Rate change impact	**8**	(1)	55
Non-qualifying depreciation	**51**	93	106
Share-based payment charge on which deferred tax not recognised	**15**	162	(40)
Net taxation charge	**692**	3,950	5,213

5. Dividends

The final dividend for 2014 of 1.0 pence per ordinary share, amounting to £4m in total was paid on 28 May 2015 and is reflected as an appropriation of earnings in the statement of changes in equity for the period.

6. Earnings per share

Basic earnings per share amounts are calculated by dividing profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the profit attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

The calculation of the basic and diluted earnings per share from continuing operations is based on the following data:

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	£000's	£000's	£000's
Profit for the year	**2,236**	11,061	18,854
Less non-controlling interests	**-**	(2)	(2)
Profit attributable to equity holders of the Parent	**2,236**	11,059	18,852
Diluted profit attributable to equity holders of the Parent	**2,236**	11,059	18,852

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	Number of Shares	Number of Shares	Number of Shares
Basic weighted average number of shares	**399,999,971**	399,999,971	399,870,568
Effect of dilutive potential ordinary shares:			
Share options	**5,748,110**	929,557	2,780,521
Diluted weighted average number of shares	**405,748,081**	400,929,528	402,651,089

It is current intention that the Long Term Incentive Plan (LTIP) and the share element of the Deferred Share Bonus Plan (DBSP) be settled by fresh issue of shares when the awards vest. The weighted average number of shares calculation above has been derived on the assumption that the vesting of shares in respect of the LTIP and DSBP awards will be settled by a fresh issue of shares when the awards vest and hence will be dilutive.

7. Insurance liabilities and reinsurance assets

	Half year ended 30 June 2015 £000's	Year ended 31 December 2014 £000's
Long term business provision	**5,171,970**	5,231,112
Reinsurers' share of long term business provision	**(3,142,859)**	(3,246,008)
Net provision	**2,029,111**	1,985,104

a) Principal assumptions

The principal assumptions underlying the calculation of the long-term business provision are as follows:

		Mortality tables	Valuation discount rates
Medically underwritten annuity products	**Half year ending 30 June 2015**	**Modified E&W Population Mortality with CMI 2013m (1.25%) and CMI 2013f (1.00%)**	**3.85%**
	Year ending 31 December 2014	Modified E&W Population Mortality with CMI 2013m (1.25%) and CMI 2013f (1.00%)	3.53%
Other annuity products	**Half year ending 30 June 2015**	**Modified PCMA/PCFA00u bespoke**	**1.55%**
	Year ending 31 December 2014	Modified PCMA/PCFA00u bespoke	1.35%
Term and whole of life products	**Half year ending 30 June 2015**	**86.25% TM/TF00Select**	**1.13%**
	Year ending 31 December 2014	86.25% TM/TF00Select	1.00%

Valuation discount rate assumptions are set with regards to yields on supporting assets. An allowance for risk is included by making an explicit deduction from the yields on debt and other fixed income securities based on historical default experience and expected experience of each asset class. The allowance for credit risk has been set at 42% (31 December 2014: 42%) of the spread on the yield of the corporate bonds over the yield on gilts.

The changes in the valuation discount rates at each period end reflect changes in yields on the supporting assets and changes made to the allowance for risk.

The mortality tables used have been adjusted to reflect additional mortality based on the proprietary data held by the Group developed from actual experience incurred. The valuation basis used to calculate the long-term business provisions includes an allowance for future expenses.

b) Movements

Movements in the carrying amount of insurance liabilities and reinsurance assets are explained as follows:

For the half year ended 30 June 2015	**Gross £000's**	**Reinsurance £000's**	**Net £000's**
At 1 January 2015	**5,231,112**	**(3,246,008)**	**1,985,104**
Increase in liability from new business	**226,436**	**(69,171)**	**157,265**
Release of in-force liability	**(83,242)**	**54,045**	**(29,197)**
Release of liability due to recorded deaths	**(44,868)**	**21,379**	**(23,489)**
Economic changes	**(157,261)**	**96,437**	**(60,824)**
Non-economic changes	**-**	**-**	**-**
Other	**(207)**	**459**	**252**
At 30 June 2015	**5,171,970**	**(3,142,859)**	**2,029,111**

For the year ended 31 December 2014	£000's	£000's	£000's
At 1 January 2014	4,347,588	(2,840,749)	1,506,839
Increase in liability from new business	692,005	(266,845)	425,160
Release of in-force liability	(130,286)	87,709	(42,577)
Release of liability due to recorded deaths	(67,743)	31,799	(35,944)
Economic changes	332,956	(211,434)	121,522
Non-economic changes	912	-	912
Other	55,680	(46,488)	9,192
At 31 December 2014	5,231,112	(3,246,008)	1,985,104

c) Analysis of expected maturity

The following table analyses insurance liabilities and reinsurance assets by duration.

	Expected cash flows (undiscounted)				**Carrying value (discounted)**
At 30 June 2015	**less than one year £000's**	**one to five years £000's**	**five to ten years £000's**	**more than ten years £000's**	**£000's**
Long-term business provision	**417,864**	**1,537,112**	**1,654,164**	**4,435,156**	**5,171,970**
Reinsurers' share of long-term business provision	**(259,225)**	**(967,808)**	**(1,049,726)**	**(2,641,911)**	**(3,142,859)**
Net	**158,639**	**569,304**	**604,438**	**1,793,245**	**2,029,111**

	Expected cash flows (undiscounted)				Carrying value (discounted)
At 31 December 2014	less than one year £000's	one to five years £000's	five to ten years £000's	more than ten years £000's	£000's
Long-term business provision	411,885	1,510,716	1,624,201	4,367,492	5,231,112
Reinsurers' share of long-term business provision	(258,539)	(966,479)	(1,053,161)	(2,699,933)	(3,246,008)
Net	153,346	544,237	571,040	1,667,559	1,985,104

d) Sensitivity analysis

Life insurance results are inherently uncertain due to actual experience being different to modelled assumptions. Sensitivity analysis is provided below to illustrate the impact of changes in key assumptions.

Sensitivity factor	Description of sensitivity factor applied
Interest rate & investment return	The impact of a change in the market interest rates by +/– 1% (e.g. if a current interest rate is 5%, the impact of an immediate change to 4% and 6% respectively). The test allows consistently for similar changes to investment returns and movements in the market backing fixed interest securities.
Credit spreads	The impact of credit spreads widening by 50bps with a corresponding pro-rated change to defaults.
Expenses	The impact of an increase in maintenance expenses by 10%.
Mortality rates	The impact of a decrease in mortality rates by 5%.
Property values	The impact of an immediate decrease in the value of properties by 10%. The test allows for the impact on the annuity liabilities arising from any change in yield on the equity release assets used to back the liabilities.
Voluntary redemptions	The impact of an increase in voluntary redemption rates on equity release loans by 10%. The test allows for the impact on the annuity liabilities arising from any change in yield on the equity release assets used to back the liabilities.

The table below demonstrates the effect of a change in a key assumption whilst other assumptions remain unchanged. In reality, such an occurrence is unlikely due to correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results. The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed and may vary at the time that any actual market movement occurs.

	Increase / (decrease) in profit before tax	
Change in assumption:	**Half year ended 30 June 2015 £000's**	Year ended 31 December 2014 £000's
Interest rates + 1%	**1,355**	2,866
Interest rates - 1%	**(135)**	(5,993)
Credit spreads + 0.5%	**(10,816)**	(11,621)
Expenses + 10%	**(10,504)**	(10,906)
Mortality - 5%	**(29,857)**	(32,027)
Property prices - 10%	**(36,950)**	(38,583)
Voluntary redemptions + 10%	**(3,691)**	(6,412)

8. Financial instruments – fair value disclosures

All financial instruments, with the exception of external borrowings are classified at fair value through profit and loss. In accordance with IFRS 13 Fair Value measurement, financial instruments at fair value have been classified into three categories.

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices)

Level 3: Inputs for the assets or liabilities that are not based on observable market data (that is, unobservable inputs)

An analysis of financial assets and liabilities held at fair value in accordance with the fair value hierarchy is set out below. All these financial assets and liabilities relate to recurring fair value measurements. There are no non-recurring fair value measurements as at 30 June 2015 and 31 December 2014.

At 30 June 2015	**Level 1 £000's**	**Level 2 £000's**	**Level 3 £000's**	**Total £000's**
Financial investments (a)	**3,484,710**	**-**	**86**	**3,484,796**
Loans secured by residential mortgages (b)	**-**	**-**	**1,246,967**	**1,246,967**
Derivative assets (c)	**-**	**70,599**	**-**	**70,599**
Loans secured by commercial mortgages (d)	**-**	**-**	**37,708**	**37,708**
Total financial assets held at fair value	**3,484,710**	**70,599**	**1,284,761**	**4,840,070**
Deposits from reinsurers (e)	**-**	**-**	**2,440,419**	**2,440,419**
Derivative liabilities (c)	**-**	**65,994**	**-**	**65,994**
Total financial liabilities held at fair value	**-**	**65,994**	**2,440,419**	**2,506,413**

At 31 December 2014	Level 1 £000's	Level 2 £000's	Level 3 £000's	Total £000's
Financial investments (a)	3,583,183	-	1,637	3,584,820
Loans secured by residential mortgages (b)	-	-	1,212,324	1,212,324
Derivative assets (c)	-	75,892	-	75,892
Loans secured by commercial mortgages (d)	-	-	37,868	37,868
Total financial assets held at fair value	3,583,183	75,892	1,251,829	4,910,904
Deposits from reinsurers (e)	-	-	2,491,795	2,491,795
Derivative liabilities (c)	-	79,493	-	79,493
Total financial liabilities held at fair value	-	79,493	2,491,795	2,571,288

The Group's policy is to recognise transfers into and transfers out of levels 1, 2 and 3 as of the date at which the Consolidated Statement of Financial Position is prepared.

There are no transfers between Levels 1, 2 and 3 during the period to 30 June 2015.

The table below reconciles the opening and closing recorded amount of level 3 of recurring financial liabilities and financial assets which are stated at fair value.

	Deposits from reinsurers £000's	Loans secured by commercial mortgages £000's	Commodity trade finance investments £000's	Loans secured by residential mortgages £000's
At 1 January 2015	**(2,491,795)**	**37,868**	**1,637**	**1,212,324**
Loans (received)/advanced	**(76,987)**	**4,258**	**-**	**60,114**
Total gains/ (losses) in Consolidated Statement of Comprehensive Income	**63,072**	**(4,586)**	**73**	**(29,045)**
Redemptions made/(received)	**111,415**	**-**	**(1,624)**	**(26,783)**
(Interest payable accrued)/interest receivable accrued	**(46,124)**	**168**	**-**	**30,357**
At 30 June 2015	**(2,440,419)**	**37,708**	**86**	**1,246,967**

	Deposits from reinsurers £000's	Loans secured by commercial mortgages £000's	Commodity trade finance investments £000's	Loans secured by residential mortgages £000's
At 1 January 2014	(2,182,350)	-	11,568	840,066
Loans (received)/advanced	(307,959)	37,480	6,321	232,519
Total (losses)/gains in Consolidated Statement of Comprehensive Income	(139,376)	263	(884)	139,973
Redemptions made/(received)	229,082	-	(16,386)	(51,273)
(Interest payable accrued)/interest receivable accrued	(91,192)	125	1,018	51,039
At 31 December 2014	(2,491,795)	37,868	1,637	1,212,324

The gains and losses are included within net investment income in the Consolidated Statement of Comprehensive Income.

The unrealised gains/ (losses) in respect of payables arising out of reinsurance contracts, commodity trade finance loans, loans secured by residential mortgages and loans secured by commercial mortgages for the period to 30 June 2015 are £63.1m, £nil, £1.3m and £(4.6)m respectively (30 June 2014: £(20.8)m, £0.4m, £40.9m and £nil respectively: 31 December 2014: £(139.4)m, £(0.9)m, £191.0m and £0.2m respectively). These unrealised gains and losses are included within net investment income in the Consolidated Statement of Comprehensive Income.

Level 3 Sensitivity Analysis

At 30 June 2015	Significant assumption	Current fair value £000's	Impact of alternative assumptions Increase in fair value £000's	Decrease in fair value £000's
Assets				
CTF Investments	**Expected defaults**	**86**	**71**	**(86)**
Loans secured by commercial mortgages	**Discount Rate**	**37,708**	**2,652**	**(2,424)**
Loans secured by residential mortgages	**Discount Rate**	**1,223,596**	**157,695**	**(132,791)**
Liabilities				
Deposits from reinsurers	**Discount Rate**	**(2,440,419)**	**(214,621)**	**183,435**

At 31 December 2014	Significant assumption	Current fair value £000's	Impact of alternative assumptions Increase in fair value £000's	Decrease in fair value £000's
Assets				
CTF Investments	Expected defaults	1,637	289	(353)
Loans secured by commercial mortgages	Discount Rate	37,868	2,744	(2,501)
Loans secured by residential mortgages	Discount Rate	1,212,324	156,367	(132,186)
Liabilities				
Deposits from reinsurers	Discount Rate	(2,491,795)	(220,538)	192,268

The impacts of reasonably possible alternative assumptions are estimated by modelling alternative scenarios for the key assumptions for each valuation model.

a) Financial investments

All financial investments are designated at fair value through profit and loss. All financial investments excluding commodity trade finance are listed.

In assessing the fair value of the debt securities and other fixed income securities, the Directors have relied upon values provided by an independent third-party which specialises in providing such values to companies. The third-party provides prices based upon quoted market prices, or where not available, modelled prices using observable market inputs. At 30 June 2015 and 31 December 2014, 100% of the values provided were based on quoted market prices that are observable for the asset or liability.

Due to the short-term nature of the commodity trade finance (“CTF”) loans, the fair value of these instruments is estimated as the principal amount borrowed plus accrued interest from the date of acquisition, adjusted for incurred and expected defaults. These CTF loans are considered to be Level 3 within the valuation category prescribed by IFRS 13 as the inputs to the fair value calculation are not based on observable market data, and include the Company’s own assumptions.

The change in the fair value of level 3 financial instruments from period to period is analysed into loans advanced, loans repaid/redemptions, and interest accrued, with the remaining balance representing fair value measurement gains and losses recognised in the Statement of Comprehensive Income.

Interest rate: The interest rate used in deriving the fair value of the CTF loans as at 30 June 2015 was nil% p.a. (30 June 2014:13.0% p.a.: 31 December 2014:nil% p.a.).

b) Loans secured by residential mortgages

The fair value recognised in the financial statements for loans secured by mortgages is determined using a marked to model valuation technique where a significant proportion of inputs are not based on observable market data and so these assets are considered to be Level 3 within the valuation category prescribed by IFRS 13.

The valuation model discounts the expected future cash flows using an interest rate swap curve with an additional spread or yield factor minus the cost of the no-negative equity guarantee. The no-negative equity guarantee represents an embedded guarantee that the repayment of the loan cannot exceed the value of the property at the time of repayment.

Although such valuations are sensitive to estimates, it is the discount rate and no-negative equity guarantee assumptions have a significant impact on the fair value.

Discount rate: Loans secured by mortgages are valued using the swap rate appropriate to the term of each contract with adjustment to reflect the credit and liquidity risk associated with such long-dated contracts. The risk adjusted swap rate for the portfolio weighted by average value at 30 June 2015 was 5.25% (31 December 2014: 5.05%).

No-negative equity guarantee: The fair value of loans secured by mortgages takes into account an explicit provision in respect of the no-negative equity guarantee which is calculated using a variant of the Black Scholes option pricing model. The key assumptions used to derive the value of the no-negative equity guarantee include property growth, volatility and over-valuation. The property growth and volatility assumed at 30 June 2015 were 5.5% (31 December 2014: 5.5%) and 13% (31 December 2014: 13% respectively). The over-valuation assumption used as at 30 June 2015 was 26.7% (31 December 2014: 27.4%). The value of the no-negative equity guarantee as at 30 June 2015 was £113.2m (31 December 2014: £112.5m).

c) Loans secured by commercial mortgages

The valuation technique that the Group uses to assess the fair value of loans secured by mortgages is consistent with that used to derive the prices applied at the initial transaction. As such, there is no difference between the fair value of loans secured by equity release mortgages at initial recognition and the amount that would have been determined at that date using the valuation technique.

The fair value recognised in the financial statements for loans secured by commercial mortgages is determined using a marked to model valuation technique where a significant proportion of inputs are not based on observable market data and so these assets are considered to be Level 3 within the valuation category prescribed by IFRS 13.

The valuation model produces a series of projected future cash flows for each mortgage, based on a range of simulations of changes in property prices drawn from a distribution based on historic observed changes. Potential changes in property tenancy (e.g. tenant default, exercise of break clause or non-renewal of lease) are also modelled in a range of simulations. A risk adjusted cash flows is calculated as the average across the range of simulations.

The risk adjusted cash flows are discounted using a swap curve with an additional spread. The additional spread is the increase in swap discount rates required so that the initial discounted risk adjusted cash flows equal the initial purchase price. This uplift is reviewed if there is evidence that market has moved materially.

The discount rate and changes in property prices and tenancy are the most significant assumptions applied in calculating the fair value of the loans.

d) Derivative assets and liabilities

The estimated fair value of derivative instruments reflects the estimated amount the Group would receive or pay in an arm's length transaction. All the derivatives held at 30 June 2015 and 31 December 2014 were purchased over the counter.

The Group’s derivative assets and liabilities largely relate to forward currency positions, interest rate swaps and inflation swaps.

Forward currency positions: Forward currency exchange contracts are priced from independent third parties.

Interest rate swaps: The fair value of the interest rate swaps is derived using an interest rate swap pricing model, using a time series of historic Libor rates, an applicable zero coupon interest rate swap curve to derive future cash flows ('forward curve') and an applicable zero coupon interest rate swap curve to discount future cash flows ('discount curve') as inputs. The forward curve is used by the pricing model to determine the future Libor rates to be applied in the calculation of the floating leg cash flow(s). The discount curve is used to calculate the present value of the future cash flow(s) of both the fixed and floating legs of the swap and its composition is driven by the terms of the Credit Support Annex under which the swap is traded.

Inflation swaps: The fair value of the inflation swaps is derived using the inflation swap pricing model, using a time series of historic inflation index levels, a zero coupon swap inflation expectation curve, an inflation seasonality model and a zero coupon interest rate swap curve as inputs. The inflation swap pricing model generates a future cash flow for both the fixed and inflation legs of a swap for which a present value is determined using zero coupon interest rate swap curve.

Interest Rate Swaptions: The fair value of these instruments is derived using a Black option pricing model. Significant inputs to the model are 'at the money' volatilities and swaption skews. 'At the money' volatilities are sourced from a market pricing provider. Swaption skew information is sourced from counterparty data.

The derivative assets and liabilities are presented on a gross basis in the Consolidated Statement of Financial Position. All over-the-counter derivative transactions are conducted under standardised ISDA (International Swaps and Derivatives Association Inc.) master agreements and the Group has collateral agreements between the individual group entities and relevant counterparties in place under each of these market master agreements. As at 30 June 2015, the Group had pledged £28.5m (31 December 2014: £29.9m) and held collateral of £29.5m (31 December 2014: £19.0m) in respect of over-the-counter derivative transactions.

e) Deposits from reinsurers

The fair value recognised in the financial statements is determined using a marked to model valuation technique where not all inputs are based on observable market data and so these liabilities are considered to be Level 3 within the valuation category prescribed by IFRS 13.

The valuation model discounts the expected future cash flows using a discount rate, derived from the assets hypothecated to back these liabilities at a product level.

As payables arising from reinsurance contracts do not have a single fixed maturity date it is not possible to determine an amount that would be contractually required to pay at maturity.

Discount rate: The key inputs to the derivation of the discount rate include market observable gross redemption yields, contractual investment expenses and an allowance for credit risk on a best estimate basis. The discount rates used as at 30 June 2015 for Retirement and Care were 4.42% and 1.79% respectively (31 December 2014: 4.16% and 1.67% respectively)

9. External Borrowings

	At 30 June 2015	At 31 December 2014
Amounts payable within 10 years:	**£000's**	£000's
Sub-ordinated debt	**99,913**	-
Interest Payable	**2,551**	-
Total	**102,464**	**-**

On 2 March 2015 the Group entered into an agreement to issue a £100m bond to funds managed by Cinven Capital Management ("Cinven"), its majority shareholder. The issue completed on 23 March 2015. The bond is repayable after a 10 year term with possible redemption, at option of the Group, at the fifth anniversary or on any interest payment date thereafter, in each case subject to PRA consent. The bond has an annual interest rate of 9.5% payable annually in arrears from the issue date. The bond issue cost was £0.1m, which is being amortised over the 10 year term. The bond is a Tier 2 qualifying regulatory capital instrument under existing solvency regulations and Solvency II compliant following implementation of the Solvency II regime on 1 January 2016. The bond is issued by Partnership Assurance Group plc with a guarantee provided by Partnership Life Assurance Company Limited.

10. Notes to the Condensed Cash Flow Statement

	Half year ended 30 June 2015 £000's	Half year ended 30 June 2014 restated £000's	Year ended 31 December 2014 restated £000's
Profit before income tax including discontinued operations	**2,928**	15,011	24,067
Non-cash movements in profit before income tax:			
Depreciation of property, plant and equipment	**1,779**	1,585	3,238
Amortisation of intangible assets	**1,626**	1,596	3,275
Assets written off	**270**	-	971
Investment in associate- Eldercare	**-**	-	(27)
Profit on the reclassification of subsidiary to associate	**-**	(94)	(94)
Share of loss of joint venture	**(1)**	166	206
Profit of subsidiary before disposal	**-**	-	2
Share based payment charge	**1,365**	239	1,223
Share of profits in associate	**-**	(8)	-
Interest and amortised cost on Subordinated Debt	**2,554**	-	-
(Increase)/ decrease in financial assets	**70,834**	(326,833)	(900,635)
(Decrease)/ increase in financial liabilities	**(64,875)**	198,245	356,547
Decrease/ (increase) in reinsurance assets	**103,149**	(185,179)	(405,259)
Decrease in insurance and other receivables excluding Corporation Tax	**7,454**	26,556	42,557
(Increase)/ decrease in prepayments and accrued income	**(146)**	7,665	7,376
(Decrease)/ increase in insurance liabilities	**(59,142)**	305,833	883,524
Decrease in insurance and other payables	**(4,872)**	(2,851)	(4,477)
Increase/ (decrease) in other taxes and social security payables	**625**	(704)	(830)
Cash from operations	**63,548**	41,227	11,664

11. Related party transactions

Balances and transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

During the period, the Group entered into transactions, in the ordinary course of business, with other related parties. Transactions entered into and balances outstanding at the end of each reporting date are detailed below.

a) Financing transactions

On 23 March 2015 the Group completed the issue of £100m of subordinated debt to Cinven's funds. Further details of this transaction can be found in note 9.

b) Remuneration of key management personnel

Key management personnel consist of the directors of the Company. The remuneration of the Directors, who are the key management personnel of the Group, is set out below:

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	£000's	£000's	£000's
Short-term employee benefits	**1,007**	995	2,850
Post-employment benefits	**-**	14	16
Total	**1,007**	1,009	2,866

c) Directors' loans

A number of directors who are defined as key management personnel of the Company held loans during the period. The amounts owed by the Directors are detailed as follows:

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	£000's	£000's	£000's
Amounts owed by directors:			
Loan advances	**314**	302	302
Total	**314**	302	302

The loan advances to directors accrue interest fixed at 4% per annum and are repayable in whole or in part at any time.

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	£000's	£000's	£000's
Interest receivable accrued on Directors' loan advances	**6**	6	12
Total	**6**	6	12

d) Other related party transactions

During the period the group entered into transactions with other entities controlled by Cinven Limited as set out below. All transactions were on a commercial basis.

	Half year ended 30 June 2015	Half year ended 30 June 2014	Year ended 31 December 2014
	£000's	£000's	£000's
Costs paid to entities related to the ultimate parent controlling party	**34**	68	122
Group's share of losses of joint venture investment	**-**	-	6
Loans advanced to associate and fees on loans	**3**	-	187
Total	**37**	68	315

e) Ultimate controlling party

As at 30 June 2015 a majority of the Company's ordinary shares are held by the partnerships comprising the Fourth Cinven Funds (the "Cinven Funds"), being funds managed and advised by Cinven Limited, a company incorporated under the laws of England and Wales. Accordingly, the Directors consider the Company's ultimate controlling party to be Cinven Limited, the manager and advisor to the Cinven Funds.

12. Post balance sheet events

On 10 August 2015, the Board proposed an interim dividend for 2015 of 0.5 pence per share. The total cost of this will be £2.0m and the dividend will be paid in October 2015 and recorded in the Statement of Changes in Equity in the second half of the year.

Statement of Directors’ Responsibilities in respect of the Market Consistent Embedded Value (‘MCEV’) basis

The MCEV methodology adopted by the Group is in accordance with the CFO Forum MCEV principles (© Stitching CFO Forum foundation 2008) published in October 2009. When compliance with the MCEV Principles is stated, those principles require the Directors to prepare supplementary information in accordance with the methodology contained in the MCEV Principles and to disclose and explain any non-compliance in the guidance included in the MCEV Principles.

In preparing the MCEV supplementary information, the Directors have:

- determined assumptions on a realistic basis, having regard to past, current and expected future experience and to relevant external data, and then applied them consistently;
- made estimates that are reasonable and consistent;
- provided additional disclosure when compliance with the specific requirements of the MCEV principles is insufficient to enable users to understand the impact of particular transactions, other events and conditions and the Group’s financial position and financial performance; and
- described the basis on which business that is non-covered has been included in the supplementary information, including any material departures from the accounting framework applicable to the Group condensed consolidated IFRS financial statements.

By order of the Board

Steve Groves
Chief Executive Officer
London
10 August 2015

David Richardson
Chief Financial Officer

Note:

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial information differs from legislation in other jurisdictions.

Independent Review Report to the Directors of Partnership Assurance Group plc on the Consolidated Partnership Group Market Consistent Embedded Value (MCEV) Supplementary Information

We have been engaged by the Company to review the Consolidated Partnership Group Market Consistent Embedded Value supplementary information (MCEV supplementary information) in the half-year financial report for the six months ended 30 June 2015 which comprises the Group MCEV analysis of Earnings (net of tax), Covered business Analysis of Movements in Embedded Value (net of tax), Reconciliation of Group IFRS net assets to MCEV and the related notes 1 to 5. We have read the other information contained in the half-year financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the MCEV supplementary information.

This report is made solely to the Company's Directors in accordance with our engagement letter and solely for the purpose of expressing an opinion as to whether anything has come to our attention that causes us to believe that the MCEV supplementary information for the six months ended 30 June 2015 is not prepared, in all material respects, in accordance with the Market Consistent Embedded Value principles issued in June 2008 by the European CFO Forum and supplemented by an amendment to the MCEV principles issued by the same body in October 2009.

Our work has been undertaken so that we might state to the Company's Directors those matters we are required to state to them in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company's Directors, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The MCEV supplementary information is the responsibility of, and has been approved by, the Directors. The Directors are responsible for preparing the MCEV supplementary information in accordance with the Market Consistent Embedded Value principles issued in June 2008 by the European CFO Forum as supplemented by an amendment to the MCEV principles issued by the same body in October 2009.

Our responsibility

Our responsibility in relation to the MCEV supplementary information is to express to the Company a conclusion on the MCEV supplementary information based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the MCEV supplementary information for the six months ended 30 June 2015 has not been properly prepared, in all material respects, in accordance with the MCEV principles using the methodology and assumptions set out in notes 1 and 2.

Other matter

We have reported separately on the condensed financial statements of Partnership Assurance Group for the six months ended 30 June 2015. The information contained in the MCEV supplementary information should be read in conjunction with the condensed set of financial statements prepared on an IFRS basis. This information is described within the Partnership Assurance Group plc condensed set of financial statements in the half-year financial report as having been reviewed.

Deloitte LLP
Chartered Accountants and Statutory Auditor
London, United Kingdom
10 August 2015

MCEV FINANCIAL INFORMATION

Group MCEV analysis of Earnings (net of tax)

For the half year ended 30 June 2015

					Half year ended 30 June 2014	Year ended 31 December 2014
		Half year ended 30 June 2015				
	Note	**Covered business MCEV £000's**	**Non covered business IFRS £000's**	**Total Group MCEV £000's**	Total Group MCEV £000's	Total Group MCEV £000's
Opening Group MCEV		**557,532**	**18,754**	**576,286**	519,633	519,633
Opening adjustments		**-**	**-**	**-**	-	-
Adjusted opening Group MCEV		**557,532**	**18,754**	**576,286**	519,633	519,633
					-	-
Operating MCEV earnings	**3**	**18,608**	**-**	**18,608**	41,862	86,502
Non-operating MCEV earnings	**3**	**(2,629)**	**156**	**(2,473)**	(5,185)	(17,071)
Total MCEV earnings		**15,979**	**156**	**16,135**	36,677	69,431
Other movements in IFRS net equity	**4**	**-**	**1,366**	**1,366**	239	1,222
Closing adjustments	**3**	**-**	**(4,000)**	**(4,000)**	(12,000)	(14,000)
Closing Group MCEV		**573,511**	**16,276**	**589,787**	544,549	576,286

Covered business Analysis of Movement in Embedded Value (net of tax)

For the half year ended 30 June 2015

	Note	Half year ended 30 June 2015 Free Surplus £000's	Required Capital £000's	VIF £000's	MCEV £000's	Half year ended 30 June 2014 MCEV £000's	Year ended 31 December 2014 MCEV £000's
Opening MCEV		**30,834**	**418,238**	**108,460**	**557,532**	463,494	463,494
Opening adjustments		**-**	**-**	**-**	**-**	-	-
Adjusted opening MCEV		**30,834**	**418,238**	**108,460**	**557,532**	463,494	463,494
New business value	**3**	**(24,602)**	**22,574**	**8,347**	**6,319**	18,295	56,072
Expected existing business contribution (reference rate)	**3**	**-**	**-**	**2,458**	**2,458**	2,006	4,106
Transfers from VIF and required capital to free surplus		**12,165**	**(5,725)**	**(5,042)**	**1,398**	1,765	3,469
Experience variances	**3**	**3,095**	**543**	**(797)**	**2,841**	(633)	(1,087)
Assumption changes	**3**	**(1,825)**	**1,825**	**(101)**	**(101)**	2,433	(481)
Other operating variances	**3**	**3,274**	**3,168**	**(749)**	**5,693**	17,996	24,423
Operating MCEV earnings		**(7,893)**	**22,385**	**4,116**	**18,608**	41,862	86,502
Economic variances	**3**	**12,822**	**(22,802)**	**604**	**(9,376)**	2,695	(3,994)
Other non-operating variances	**3**	**(8,573)**	**1,371**	**13,949**	**6,747**	(7,517)	(11,470)
Total MCEV earnings		**(3,644)**	**954**	**18,669**	**15,979**	37,040	71,037
Closing adjustments	**3**	**-**	**-**	**-**	**-**	-	23,000
Closing MCEV		**27,190**	**419,192**	**127,129**	**573,511**	500,534	557,532

Reconciliation of Group IFRS net assets to MCEV

As at 30 June 2015

Adjusted Net Worth	Half year ended 30 June 2015			Year ended 31 December 2014		
	Covered Business £000's	Non Covered Business £000's	Group £000's	Covered Business £000's	Non Covered Business £000's	Group £000's
Group Net Assets as reported under IFRS	**461,040**	**143,251**	**604,291**	458,959	145,729	604,688
Goodwill	**(1,332)**	**(124,875)**	**(126,207)**	(1,332)	(124,875)	(126,207)
Intangibles	**(1,000)**	**(2,100)**	**(3,100)**	(1,000)	(2,100)	(3,100)
Adjustments to IFRS	**(12,325)**	**-**	**(12,325)**	(7,555)	-	(7,555)
MCEV Net Worth	**446,383**	**16,276**	**462,659**	449,072	18,754	467,826
VIF	**127,128**	**-**	**127,128**	108,460	-	108,460
MCEV (net of taxation)	**573,511**	**16,276**	**589,787**	557,532	18,754	576,286

Notes to the MCEV financial statements for the period ended 30 June 2015

1. Basis of preparation

The supplementary information which comprises the Group MCEV analysis of Earnings (net of tax), Covered business Analysis of Movement in Embedded Value (net of tax), Reconciliation of Group IFRS net assets to MCEV and the related notes 1 to 5 has been prepared on a Market Consistent Embedded Value (MCEV) basis and results for non-covered business on the International Financial Reporting Standards (IFRS) basis.

The MCEV methodology adopted is in accordance with the MCEV Principles published by the CFO Forum in October 2009.

Covered business

The MCEV calculations cover all lines of insurance business within PLACL. No other Group companies contain any covered business and the value of these companies has been included in the Group MCEV at IFRS net asset value, less the value of goodwill and intangibles, to the extent that their recovery is supported by future profits.

Group financing

The Group MCEV includes the fair value of the external debt that was completed on 23 March 2015. The group did not make use of any financial reinsurance during the first half of 2015.

MCEV methodology

Overview

Under the MCEV methodology, profit is recognised as it is earned over the life of products defined within covered business. The total profit recognised over the lifetime of a policy is the same under MCEV and IFRS, but the timing of recognition is different.

Embedded value

The embedded value is the sum of the adjusted net worth of the Group companies plus the value of in-force on the covered business, this being the present value of profits that will emerge over time.

The embedded value is calculated net of the impacts of reinsurance and allows for taxation based on current legislation and known future changes.

i) Net worth

The net worth is the market value of the shareholders’ funds and the shareholders’ interest in the surplus held in the long-term business fund. This is the Net Assets on a regulatory basis for the life company and the IFRS net asset value for other Group companies, less the value of goodwill and intangibles, to the extent that their recovery is supported by future profits.

The net worth is equal to the sum of the required capital and free surplus in the Group.

ii) Required capital

Required capital is the market value of assets attributed to the covered business in excess of assets required to back liabilities for covered business, and for which distribution to shareholders is restricted. The level of required capital is set equal to the higher of:

- The level of capital at which the regulator is empowered to take action;
- The capital requirement under the Group’s Economic Capital framework; and
- The target capital level

This methodology reflects the level of capital considered by the directors to be appropriate to manage the business, and includes any additional shareholder funds not available for distribution. The same definition of required capital is used for both existing and new business.

The level of required capital is disclosed as the percentage of the EU minimum capital requirement (Capital Resources Requirement).

The free surplus is the market value of any assets allocated to, but not required to support, the in-force covered business at the valuation date.

iii) Value of in-force covered business (VIF)

The value of in-force covered business consists of the following components:

- present value of future profits;
- time value of financial options and guarantees;
- frictional costs of required capital; and
- cost of residual non-hedgeable risk.

a) Present value of future profits (PVFP)

The PVFP is the present value of the distributable profits to shareholders arising from the in-force covered business projected on a best estimate basis. Distributable profits generally arise when they are released following actuarial valuations. These valuations are carried out in accordance with PRA statutory requirements designed to ensure and demonstrate solvency in long-term business funds. Future distributable profits will depend on experience in a number of areas such as investment return, mortality, lapse rates and administration costs. Releases to shareholders arising in future years from the in-force covered business and associated required capital can be projected using assumptions of future experience.

Future profits are projected using best estimate non-economic assumptions and market consistent economic assumptions. In principle, each cash flow is discounted at a rate that appropriately reflects the riskiness of that cash flow, so higher risk cash flows are discounted at higher rates. In practice, the PVFP is calculated using the 'certainty equivalent' approach, under which the reference rate is used for both the investment return and the discount rate. This approach ensures that asset cash flows are valued consistently with the market prices of assets without options and guarantees. Further information on the risk-free rates is in the following pages.

b) Time value of financial options and guarantees (TVOG)

The PVFP calculation is based on a single (base) economic scenario; however, a single scenario cannot appropriately allow for the effect of certain asset features. If an option or guarantee affects shareholder cash flows in the base scenario, the impact is included in the PVFP and is referred to as the intrinsic value of the option guarantee; however, future investment returns are uncertain and the actual impact on shareholder profits may be higher or lower. The covered business does not contain any significant policyholder options or guarantees and therefore the TVOG is zero.

The assets backing the covered business include mortgages secured against individual domestic property (Equity release mortgages). The mortgages contain guarantees where if the value of the property is lower than the mortgage balance at the time of death or entry into a care home, then the lower of the property value and mortgage balance is repaid. The time value of this option and guarantee is allowed for in the asset valuation using closed form calculations.

In the first half of 2015 swaptions were acquired as part of a strategy to protect its solvency position of the covered business against a significant decrease in the risk free rate. The MCEV for covered business includes a provision against the current and potential maximum future cost of this strategy, which effectively results in no value being recognised for the time values of these options in the total MCEV.

Frictional costs of required capital (FCoRC)

The additional costs to a shareholder of holding the assets backing required capital within an insurance company rather than directly in the market are called frictional costs. They are explicitly deducted from the PVFP. The additional costs allowed for are the taxation costs and any additional investment expenses on the assets backing the required capital. The level of required capital has been set out in the net worth section.

Frictional costs are calculated by projecting forwards the future levels of required capital. The projection of the required capital has been based on an approximate method assuming that the required capital is a constant proportion of the Long Term Insurance Capital Requirement. Tax on investment return and investment expenses are payable on the assets backing required capital, up until the point that they are released to shareholders.

c) Cost of residual non-hedgeable risks (CoNHR)

The cost of residual non-hedgeable risks (CoNHR) covers risks not already allowed for in the time value of options and guarantees or the PVFP. The allowance includes the impact of both non-hedgeable financial and non-financial risks. The most significant risks not included in the PVFP are operational risks and equity release property risks.

Asymmetric risks allowed for in the PVFP are described earlier in the basis of preparation. No allowance has been made within the cost of non-hedgeable risk for symmetrical risks as these are diversifiable by investors. The CoNHR includes an allowance for non-modelled non-hedgeable risks. For ease of comparison the CoNHR is expressed as percentage cost of non-hedgeable capital.

New business

All annuity business is written on a single premium basis. Premium increments received following policy issue are excluded from the value of new business. Single and regular premium protection business is included in new business.

Point of sale economic and non-economic assumptions are used to value the new business. Any variances or changes in assumptions after the point of sale are recorded within the analysis of the MCEV earnings as operating experience variances or operating assumption changes.

Participating business

The Group does not contain any policies where the policyholders participate in the profits of the business.

2. Assumptions

Reference rates

Reference rates are calculated using corporate bond and equity release liquidity premiums added to the swap curve. The liquidity premium on corporate bond assets is calculated by deducting an allowance for credit default, individually assessed for each bond based on credit rating, and comparing the resulting risk adjusted internal rate of return on the portfolio to the swap curve.

The equity release assets are valued using a mark to model approach that allows for the cost of the no negative equity guarantee, where relevant, with the liquidity premium calculated on a consistent basis.

For protection business, cash flows are assumed to be liquid and as such are discounted with no allowance for a liquidity premium.

The liquidity premiums used for the annuity in-force business are as follows:

	Liquidity premium
30 June 2015	**215 bps**
31 December 2014	211 bps
30 June 2014	179 bps

The liquidity premium on new business is determined using an approach consistent with that for the in-force business. For new business, the liquidity premium in excess of swaps is derived on a daily basis using the prevailing market conditions.

The weighted average liquidity premiums used for the new business MCEV calculations are as follows:

	Liquidity premium
30 June 2015	**257 bps**
31 December 2014	273 bps
30 June 2014	247 bps

Swap rates

The swap curve is constructed from cash rates, future strips, and semi-annual swap rates sourced from a variety of counterparties and brokers with flat interpolation beyond 50 years.

The table below sets out the swap rates used for the MCEV valuations as at period end. These rates have been supplied by PLACL's investment manager.

	6 months	1 year	2 years	5 years	10 years	15 years	20 years
30 June 2015	**0.83%**	**0.83%**	**1.11%**	**1.73%**	**2.20%**	**2.39%**	**2.43%**
31 December 2014	0.74%	0.74%	0.93%	1.46%	1.87%	2.11%	2.24%
30 June 2014	0.90%	0.90%	1.34%	2.20%	2.85%	3.17%	3.32%

Operating earnings

For operating earnings, PLACL uses the risk adjusted yield on the asset portfolio backing liabilities in order to determine the total existing business contribution. This represents management's long-term expectations of total return on the portfolio.

The expected return has been calculated by reference to the internal rate of return on the backing assets less an appropriate risk margin.

Mortality rates

Assumed future mortality, morbidity and lapse rates have been derived from PLACL's historical experience data. The assumption is set as a best estimate of future experience. Improvements in annuitant longevity have been included in this best estimate.

Expenses

Maintenance expenses are based on the costs allocated or recharged to the PLACL in-force business. No credit for future productivity gains or economies of scale has been included in the MCEV.

Non-recurring expenses, associated with the covered business, are charged to the non-operating earnings in the year incurred and are excluded from the per policy maintenance expense assumptions. These amounted to £6.4m for the 6 month period to 30 June 2015 (30 June 2014: £9.7m, 31 December 2014: £16.4m).

Best estimate expense inflation applied as at 30 June 2014 was 4.6% p.a. (30 June 2014: 4.7%, 31 December 2014: 4.5%).

Taxation

The current and future tax rates are corporation tax rates as published by HM Treasury and take into account both taxes enacted by legislation and those disclosed in budget announcements. The effective tax rate in PLACL in first half of 2015 is consistent with the current corporation tax rate. The effective tax rate for the 6 months to 30 June 2015 was 20.3% (30 June 2014: 21.5%, 31 December 2014: 13.4%).

For the purposes of modelling tax on future profits, a calendar year assumption is set using a pro rata method based on months at each effective rate. This is implemented as prescribed by HMRC.

On 23 March 2015, the group completed an issue of £100 million of subordinated debt to Cinven's funds. Future interest payments due on this subordinated debt reduce the future profits to which the effective tax rate is applied, resulting in an increase in VIF by an amount equal to the value of the future interest payments.

The blended corporation tax rates used are as follows:

	Half year ended 30 June 2015	Year ended 31 December 2014	Half Year ended 30 June 2014
2014	**21.50%**	21.50%	21.50%
2015	**20.25%**	20.25%	20.25%
2016	**20.00%**	20.00%	20.00%
2017	**19.25%**	20.00%	20.00%
2018	**19.00%**	20.00%	20.00%
2019	**19.00%**	20.00%	20.00%
2020	**18.25%**	20.00%	20.00%
2021+	**18.00%**	20.00%	20.00%

Volatilities and correlations

Residential property volatility is the only direct volatility input to the MCEV calculations and is used in the evaluation of the "No Negative Equity Guarantee ("NNEG") on Equity release assets. As at 30 June 2015 the assumption was set to 12% (30 June 2014: 12%, 31 December 2014: 12%).

Correlations between the risks inherent in the business are used for the calculation of the CoNHR total non-hedgeable risk capital. The correlations are consistent with the Group's Economic Capital assumptions which are based on historic correlations with adjustment for prudence as required.

Non-hedgeable risk

For the balance sheet and operating profit, a charge of 0.9% (30 June 2014: 1.1%, 31 December 2014: 0.9%) has been applied to the non-hedgeable capital required for a 1-in-200 year risk over the remaining lifetime of in-force business. The charge includes an allowance for all material non-hedgeable risks identified which are not already included in the PVFP calculation.

The capital levels used are consistent with those used in the Economic Capital calculation for those risks covered. Diversification benefits are included between non-hedgeable risks of the covered business. No diversification credit has been taken with hedgeable risks in the covered or non-covered business. The capital has been projected as running off over the remaining lifetime of the covered business in line with the capital resources requirement.

Frictional cost of required capital

The required capital has been set to be 187% of the capital resources requirement (30 June 2014: 176%, 31 December 2014: 190%). The required capital has been projected as running off over the remaining lifetime of the covered business in line with the capital resources requirement.

The total frictional cost allowance for investment expenses and tax on investment income earned on the required capital is 0.5% as at 30 June 2015 (30 June 2014: 0.7%, 31 December 2014: 0.5%).

3. Commentary on the analysis of movement in embedded value (net of tax)

Covered business

New business volumes and profit margins in the first half of 2015 are less than in the first half of 2014 reducing MCEV earnings from the value of new business written.

The total expected existing business contribution, transfers from VIF and required capital to free surplus have increased in the period as a result of continued growth in the portfolio.

Experience variances in the period are positive in aggregate as a result of heavier than expected mortality experience.

Other operating variances also include expected long-term return on excess assets (after tax) of £5.8m (£12.8m at 31 December 2014 and £6.8m at 30 June 2014).

The £(9.4)m economic variance on MCEV includes a provision against the current and potential maximum future cost of our interest rate hedging strategy and a smaller negative variance on IFRS net worth offset by the lower valuation of the subordinated debt under MCEV which is valued at fair value compared to IFRS which is valued at amortised cost.

The impact of economic variances on the economic capital balance sheet has contributed to the movement in the allocation of required capital and free surplus in the economic variances line but has no net impact on MCEV. The main driver of this is the rise in risk-free rates which has reduced required capital and increased free surplus on an economic basis.

Non-operating variance free surplus predominantly consists of non-recurring expenses of £6.4m, further detail of which is provided in note 3 to the consolidated financial statements presented with this supplementary information. The increase in VIF from non-operating variances arises since future interest payments due on the subordinated debt reduce future profits. Therefore, future profit with value equivalent to the value of the future interest payments will be tax exempt.

Non-covered business

The non-operating MCEV loss in the period has arisen in the non-insurance companies in the group.

The principal changes in the value of non-covered business are a £4.0m reduction due to the payment of the 2014 final dividend offset by a £1.4m increase as share based payment reserve has accumulated in PAG plc.

4. Commentary on the movements in IFRS net equity (net of tax)

The other movements in IFRS net equity have arisen as the share based payment reserve has been increased to reflect the charge arising from the Group’s non-cash employee benefits.

5. Sensitivities

No future management actions are modelled following the change to the assumptions. The results are shown net of tax. The Required Capital has not been recalculated in each scenario and is modelled as a level percentage of the Capital Resources Requirement (CRR) (although the CRR will have increased or decreased as a result of any change in IFRS reserves and will impact on the FCoRC).

The sensitivity of the embedded value and the value of new business to changes in economic and non-economic assumptions is as follows:

	In-force		**New business**	
	Impact on MCEV	**Change in MCEV**	**Impact on MCEV**	**Change in MCEV**
30 June 2015 Sensitivity	**£'000**	**%**	**£'000**	**%**
Embedded Value (Base)	**573,511**		**6,319**	
Interest rate environment +100 bps	**(626)**	**0%**	**n/a**	**n/a**
Interest rate environment -100 bps	**3,580**	**1%**	**n/a**	**n/a**
Swaption implied volatilities + 25%	**-**	**0%**	**n/a**	**n/a**
Property volatilities +25%	**(43,204)**	**-8%**	**(1,611)**	**-25%**
Property Values -10%	**(28,966)**	**-5%**	**n/a**	**n/a**
Lapses -10% (including equity release)	**2,694**	**0%**	**n/a**	**n/a**
Mortality -5% (annuities)	**(24,663)**	**-4%**	**(874)**	**-14%**
Expenses -10%	**6,557**	**1%**	**49**	**1%**
Mortality improvements +0.25% (best estimate only)	**(12,365)**	**-2%**	**(713)**	**-11%**
Decrease in liquidity premium 25 bps	**(77,535)**	**-14%**	**(3,640)**	**-58%**
Required capital set to be 100% of CRR	**10,396**	**2%**	**593**	**9%**

	In-force		New business	
	Impact on MCEV	Change in MCEV	Impact on MCEV	Change in MCEV
31 December 2014 Sensitivity	£'000	%	£'000	%
Embedded Value (Base)	557,532		56,072	
Interest rate environment +100 bps	(5,714)	-1%	n/a	n/a
Interest rate environment -100 bps	828	0%	n/a	n/a
Swaption implied volatilities + 25%	-	0%	n/a	n/a
Property volatilities +25%	(39,445)	-7%	(5,339)	-10%
Property Values -10%	(29,763)	-5%	n/a	n/a
Lapses -10% (including equity release)	4,771	1%	n/a	n/a
Mortality -5% (annuities)	(21,603)	-4%	(1,825)	-3%
Expenses -10%	6,663	1%	180	0%
Mortality improvements +0.25% (best estimate only)	(11,254)	-2%	(1,747)	-3%
Decrease in liquidity premium 25 bps	(79,212)	-14%	(12,595)	-22%
Required capital set to be 100% of CRR	10,995	2%	2,927	5%

Notes to the sensitivities:

- Interest rate environment +/-100 bps – this sensitivity is modelled as a 100bp change to the yield on each asset. The sensitivity allows for the resulting change in asset value and the change in liability value that follows from the change in risk adjusted internal rate of return on the portfolio. In the -100bp sensitivity the reference rate has a floor of 0%.
- No sensitivity to swaption implied volatilities has been shown as swaption volatilities are not used in any part of the MCEV calculation for PLACL.
- 25% increase in property volatility – this sensitivity allows for the change in equity release asset value as a result of the change in the cost of the "No Negative Equity Guarantee" and the corresponding change in liabilities as a result of the yield change.
- 10% fall in property values – this sensitivity allows for the change in asset value arising from an immediate fall of 10% in property prices, thereby increasing the cost of the "No Negative Equity Guarantee" and the change in liabilities as a result of the consequent change in yield on the equity release asset.
- 10% proportionate change in lapses (e.g. base lapse rate of 5% becomes 4.5%) - equity release repayment rates are also adjusted, the IFRS reserves are changed in this scenario as a result of changing yields on equity release mortgages
- 5% decrease in base mortality – this sensitivity is modelled for the annuity business only. Remaining products are not material. This is modelled as a change in the best estimate mortality level and the prudent margins remain unchanged.
- 10% decrease in maintenance expenses – modelled as a 10% change in the expense reserve. There is no change to expense inflation and no change to valuation interest rates.
- Mortality improvements +0.25% - this sensitivity is modelled as an additional 0.25% improvement in each future year within the best estimate basis. Prudent margins are unchanged.
- 25bps decrease in liquidity premiums – this sensitivity is modelled as a 25bp parallel shift in the reference rates used for annuity business.
- The required capital sensitivity is modelled by reducing capital from 187% to 100% of the capital resource requirement. This has no impact on net worth and increases the VIF as a result of lower frictional costs of capital.
- Interest rate and property value sensitivities are not modelled for new business as the group actively reviews its pricing, and in the event of a sudden movement in asset values the pricing of new business would be changed.

Glossary

"Board"	the board of directors of the Company
"Company"	Partnership Assurance Group plc
"DB"	defined benefit pension scheme
"DC"	defined contribution pension scheme
"Directors"	the Executive Directors and the Non-executive Directors of PAG plc
"Economic Capital"	is based on the Boards view of capital required to withstand a 1 in 200 year risk event.
"Economic Capital Coverage Ratio"	the ratio of economic capital surplus over economic capital requirements assessed at the Group level.
"Economic Capital Surplus"	surplus capital of the Group in excess of an assessment of the level of capital that would be required for the Group to withstand the impact of an event that is commensurate with a level of severity of a 1 in 200 year event.
"EU"	the European Union
"Group"	Partnership Assurance Group plc and its subsidiaries and subsidiary undertakings from time to time
"GWP"	gross written premium or gross premiums written, the line item on the Group's consolidated income statement which reflects the revenue recognised in respect of premiums paid for its policies
"IGD surplus capital resources"	The IGD surplus capital resources are defined by the FCA in the Insurance Groups Directive. It is calculated as the surplus of the available capital resources over the capital resources requirement. It excludes the surplus capital held within the long-term funds.
"INA"	immediate needs annuity, otherwise known as a care annuity, which is designed to provide income for life to fund care costs in return for a one-off premium and is designed for adults requiring immediate financial support with their long-term care costs
"In-force Operating Profit"	profit generated from the actual experience measured against the assumed experience in the actuarial basis. The actuarial basis includes a number of assumptions, the most material of which are mortality levels, levels of defaults on investments, expense levels (to maintain the business in-force), levels of inflation, and lapse rates (for regular premium business). In-force Operating Profit also includes the effect recognised in the IFRS profit arising from changes in the reported value of insurance (and associated financial) liabilities resulting from changes to the actuarial assumptions, valuation methods, or underlying data, made subsequent to the point of sale.
"Longevity risk"	the risk that on average annuitants will live longer than expected
"Long-term expected return on surplus assets"	the long-term, risk adjusted, expected return on investments surplus to those investments that are used to back insurance liabilities. The long-term expected return is derived from applying an average expected yield appropriate to the category of surplus assets held and is adjusted for the best estimate expected level of defaults on those investments

Glossary

"Mortality risk"	the risk that on average protection policyholders will not live as long as expected
"New Business Margin"	the ratio of New Business Operating Profit to New Business Premiums
"New Business Operating Profit"	profit generated from new business completed in the period, calculated using actuarial assumptions applicable at the time the new business was written, utilising a discount rate based upon expected investment yields on investment assets (e.g. cash, gilts, corporate bonds and loans secured by equity release mortgages) used to generate the annuity quotation, net of expenses allocated against new business
"New Business Premiums"	New Business Premiums represent the value, measured as single premium equivalent ("SPE"), of new insurance contracts completed during the reporting period.
"PLACL"	Partnership Life Assurance Company Limited
"PRA"	the Prudential Regulation Authority
Surplus assets"	investments held by the Group that are not required to back insurance liabilities
"SPE"	single premium equivalent, which is calculated as total single premiums plus 10 times annual regular premiums; an industry accepted measure of revenue
"Total Operating Profit"	Total Operating Profit is the sum of New Business Operating Profit and In-force Operating Profit, together with the long-term expected return from investments held by the Group that are not required to back insurance liabilities (termed "surplus assets").
"VIF"	"Value of In-Force" represents the current value of future profits expected to emerge from the in-force insurance liabilities