Preliminary results for Partnership Assurance Group plc

For the Year ended 31 December 2013

19 March 2014

PARTNERSHIP ASSURANCE GROUP PLC ANNOUNCES 17% INCREASE IN OPERATING PROFIT AND ROBUST NEW BUSINESS MARGINS IN A DISRUPTED MARKET

Profitability

- **Total Operating Profit [i] £131m up 17% (2012: £112m)**
- **New Business Operating Profit [ii] of £86m (2012: £94m) with margins of 7.0% for the full year, up from 6.0% at the half year (2012: 7.4%)**
- **In-force Operating Profit of £34m (2012: £14m) including £21m of gains reflecting realised expense reductions for the in-force block**
- **Return on Surplus Assets of £11m (2012: £4m) reflecting increased surplus assets and improved investment returns**
- **Group IFRS Profit Before Tax up 24% to £83m (2012: £67m)**

New Business

- **Total new business premiums [iii] down 3% to £1,229m (2012: £1,265m)**
- **Total retirement new business flat at £1,160m; external non-standard annuity market down 18%**
- **Established market leading position in underwritten Defined Benefit (DB) bulk annuity market with sales of £84m; pipeline remains strong**
- **Care annuity sales of £66m (2012: £94m); some improvement in sales in H2**

Operational update

- **Continued development of proprietary Intellectual Property delivering enhanced pricing and risk selection**
- **Enhanced automated quote capability, facilitating greater access to growing web-based distribution**
- **Expanded administrative capability for wider range of DB scheme features, expanding the DB de-risking proposition reach**
- **Senior management strengthened to improve technical and operational capability**
- **Continued industry recognition for product and service quality; Financial Adviser 5 Star service award for fourth consecutive year**

Capital

- **Increased Economic Capital position with a coverage ratio of 159%**
- **Maiden dividend of 3.0 pence per share proposed, in line with our stated policy at IPO**

Outlook

- **Confident of medium and long term drivers of growth, although uncertainty remains over timing of return to growth**
- **We expect total sales in Q1 to be lower than Q4 2013**
- **Focus on pricing discipline and risk selection, leaving business well positioned for the market's return to growth**

Commenting on these results, Steve Groves, Group Chief Executive, said:

"Trading conditions in the second half of 2013 remained difficult. The regulatory changes that occurred at the end of 2012 have had a deeper and longer impact on the retirement and care annuity markets than we foresaw. In these challenging conditions we have maintained our pricing discipline, and have chosen only to compete in those segments of the market offering attractive returns to shareholders. We have deployed our proprietary IP advantage to select the better rewarded risks, resulting in improved new business profitability in the second half of the year.

Over the twelve month period, we focussed on leveraging Partnership's key strengths and developing further our capability. We have continued to enhance our market-leading underwritten Defined Benefit de-risking proposition, where the opportunities are significant, and we have improved our automated underwriting capability to access the increasingly active web-based distribution channels. Our senior management team has been expanded to provide the level of resource and expertise needed to capitalise on the opportunities open to Partnership.

Elsewhere, the initial conclusions from the Financial Conduct Authority's thematic review into the annuity market further increase our confidence that Partnership will have improved access to the retirement annuity market over time.

Although trading conditions continue to be challenging, the medium and long term drivers of growth remain intact. Meanwhile, the strength of our proprietary IP allows us to bring our expertise into developing areas, including Defined Benefit de-risking. We will continue to build upon our capabilities to position the business for the market's return to growth."

Notes:

i. 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").

ii. New Business Operating Profit is profit generated from new business completed in the period, calculated using assumptions applicable at the time the new business was written.

iii. New Business Premiums represent the value, measured as single premium equivalent ("SPE"), of new insurance contracts completed during the reporting period.

New Business sales by quarter

	3 months to:							
	31/12/13	30/9/13	30/6/13	31/3/13	31/12/12	30/9/12	30/6/12	31/3/12
	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Retirement	275.3	282.8	242.9	358.6	380.8	268.6	210.5	307.6
Care	21.0	16.8	13.3	14.8	25.8	23.4	19.5	25.7
Protection	0.8	0.8	1.1	0.7	0.4	0.5	0.8	1.0
Total	297.1	300.3	257.3	374.1	407.0	292.5	230.8	334.3

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A presentation for analysts will take place at 8.30am today at

Bishopsgate & Chancery Rooms

Andaz Hotel Liverpool Street

London EC2M 7QN

The presentation will be webcast live on www.partnership-group.com and a copy of this announcement, webcast of the presentation and the presentation slides will be available on the website **thereafter**.

Financial calendar

7 May 2014	Ex-dividend date – Final dividend
9 May 2014	Record date to be eligible for the final dividend
14 May 2014	Quarter 1 Interim Management Statement
22 May 2014	Annual General Meeting (11.30 a.m.)
30 May 2014	Final dividend payment date for the year to 31 December 2013
14 August 2014	Results – Half Year
12 November 2014	Quarter 3 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.

How we are performing

Performance review

Total new business premiums were £1,229m for the year ended 31 December 2013, a decrease of 3% on the same period last year.

	2013 £m	2012 £m
Retirement annuities	**1,160**	1,168
Care annuities	**66**	94
Protection	**3**	3
New business premiums	**1,229**	1,265

Retirement annuities

Retirement annuities form the majority of our business. New business premiums for retirement annuities decreased by 1% to £1,160m (2012: £1,168m) and within this we sold £84m (2012: £nil) of defined benefit buy in/buy out business.

The retirement new business level is particularly encouraging in the context of the disruption seen in the non-standard annuity market through much of 2013, which saw a fall of 18% in total premiums sold through the open market.

This slowdown has been caused by two principal factors: the introduction of gender neutral pricing in December 2012 caused acceleration of sales into the second half of 2012 and early 2013 that would typically have completed in 2013; and the implementation of changes for advisers under the Retail Distribution Review (RDR), which came into force on 1 January 2013, which again accelerated some sales to 2012. This appears to have reduced adviser engagement with customers for the sale of annuities.

We have continued to invest in the development of our defined benefit de-risking proposition in 2013, and we have completed a number of buy-in and buy-out transactions in the year with total premiums of £84m. This is proving the benefits of our proposition for pensioners, trustees and sponsoring companies. As this is a new market for Partnership, we continue to learn a significant amount, and see new opportunities, enabling us to further enhance our proposition.

Care annuities

Sales of Care annuities reduced by 30% to £66m (2012: £94m).

The sale of annuities for funding long-term care has fallen behind expectations in 2013. The impact of the outcome of the RDR on advisers selling care annuities has been more significant and this led to a reduction in the level of activity in the first half of 2013. Advisers do appear to be returning to the market with quote activity gradually improving in the second half of the year, though the conversion from quote to policy for INAs can be lengthy and unpredictable.

Protection

Protection sales remained flat at £3m (2012: £3m). 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.

Whilst a small component of our business in 2013, there are significant opportunities to grow in the future.

Financial headlines

Total operating profit in 2013 was £131m (2012: £112m), an increase of 17%. Within this overall result, we have delivered new business operating profits of £86m (2012: £94m), achieving a new business operating margin of 7.0% (2012: 7.4%).

The fall in new business margin compared to 2012 is due to an increase in expenses. In 2013, we invested in the business to increase scalability and efficiency, and incurred costs associated with our transition from private to public ownership. Whilst this investment is now largely complete, we expect to see a further increase in 2014 as the full annualised costs are realised.

Profits emerging from the in-force book in 2013 were £34m (2012: £14m), and benefited from economies of scale realised on in-force business. This was in part due to the transfer of the administration of a significant block of in-force annuities onto our in-house administration platform. This was the primary driver behind a total positive contribution from assumption and other changes in 2013 of £21m.

We recorded an increase in return on surplus assets to £11m (2012: £4m), reflecting the growth in the period and the allocation of surplus assets out of cash and into higher-yielding assets.

The level of excess economic capital at 31 December 2013 was £173m (2012: £104m), giving a capital coverage ratio of 158% (2012: 141%), 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, demonstrating the close matching of assets and liabilities, efficient use of reinsurance, and monitoring of risk levels against our Board tolerances.

Assets under management have increased to £4.1bn (2012: £3.3bn), including accrued interest but excluding £272m (2012: £330m) of assets that the Group manages on behalf of reinsurers under certain reinsurance arrangements. Our focus remains on seeking superior risk-adjusted yields and capital efficiency for the benefit of policyholders and shareholders.

Our investment portfolio (excluding equity release investments) is of high overall quality with in excess of 66% invested in bonds rated A or better and 99% rated BBB or better.

We continue to source equity release loans through a combination of newly originated loans and bulk purchases. Newly originated loans in 2013 totalled £129m (2012: £87m). In the second half of the year we completed two bulk acquisitions, acquiring loans with a value of £287m (2012: £62m). The level of equity release mortgage assets as a proportion of total assets under management at 31 December 2013 increased to 21% (2012: 15%).

In June 2013, we issued our first loans, using shareholder assets, to facilitate Commodity Trade Finance ("CTF"), in line with our strategy of seeking to maximise risk-adjusted returns on shareholder capital. Whilst we gain experience of this asset class, allocations to it will remain relatively low. We are actively investigating other alternative assets that can provide superior risk-adjusted returns for the benefit of shareholders or to match insurance liabilities.

Total market consistent embedded value (MCEV) as at 31 December 2013 was £520m, which compares to a pro-forma MCEV at 31 December 2012 of £417m. New business value generated in 2013 was £100m (2012: £117m), gross of tax.

Investing in our future

In 2013 we continued to invest in the business, with 85 new positions created over the full year taking total staff numbers to 580 at 31 December 2013.

A number of new senior roles were created to meet the requirement of public ownership (for example Deputy Chief Financial Officer and Director of Investor Relations) and to enable Partnership to capitalise on future growth in its markets (for example Chief Pricing Officer, Chief Technology Officer and Director of Defined Benefit Solutions).

We also continued with major projects on infrastructure to support, in particular, our data platforms, and successfully deployed the first significant modules of our new valuation data and reporting database. Our automated underwriting engine is continuing to deliver efficiency gains, in particular with respect to speed and accuracy, which has improved our customer experience. It has also improved the timeliness and granularity of information on new business quotes used to manage the business.

This investment in both human capital and technology enables the continued improvement in Partnership's IP, underpinning our core competitive advantage in the NSA market.

In line with our strategy of expanding and diversifying distribution, our arrangement with Virgin Money, which commenced during the first half of the year, has now benefited from the launch of marketing activity with Virgin customers. The quality of our products and service continues to be recognised in the industry; we won the FT Adviser 5 star online service award for 2013; were voted as Investment Life & Pensions Moneyfacts "Best Enhanced Annuity Provider" for the fourth year in a row; and retained our Financial Adviser "5 Star" rating also for the fourth straight year.

Current trading and outlook

The disruption to the market for NSAs in 2013 has continued into 2014. However there are signs that market activity is improving, but it is too early to confirm whether this will translate into higher sales.

However, we believe that the core drivers of growth in the UK are firmly embedded and we are confident in our ability to capitalise on these opportunities. Each year more people are reaching retirement with their savings in a defined contribution pension scheme, and are therefore in need of annuities to secure an income for their retirement. The political and regulatory pressures for people to save more for their retirement and shop around for the best deal when they do retire will expand the market that we serve. Underwritten Defined Benefit solutions are increasingly an option for Trustees to consider as they develop de-risking strategies for their schemes. As the population continues to grow older, more individuals will require increasing levels of care and could benefit from the financial security that an INA can bring.

All these factors point to strong new business growth opportunities over time.

Segmental information

The consolidated segment Information provides information about the performance of the Group analysed on the basis of segment information provided to the Board.

Details of significant movements in the year are set out below:

IFRS operating profit before tax

For the year ended 31 December	2013 £000's	2012 £000's
New business operating profit	**85,678**	93,871
In-force operating profit	**34,278**	14,263
Long-term expected return on surplus assets	**11,435**	3,997
Operating profit	**131,391**	112,131
Investment variances	**8,643**	(3,289)
Non-recurring expenditure	**(30,769)**	(5,735)
Other	**(1,201)**	(1,156)
Interest on borrowings	**(25,403)**	(34,472)
Profit from continuing operations before tax	**82,661**	67,479

Total operating profit

Total operating profit in the year to 31 December 2013 of £131.4m is up £19.3m from the £112.1m reported for 2012 as the increase in in-force operating profit more than offsets lower new business profits as explained below.

New business operating profit

New business operating profit has decreased 8.7% from £93.9m in 2012 to £85.7m in 2013. This decrease is primarily as a result of the increased cost base following investment in the Group's personnel and infrastructure, and investment in distribution arrangements, that commenced in H2 2012. This investment in the business is necessary to prepare the Group for future growth. New business operating profit was also impacted by the reduction in overall sales compared to 2012. Offsetting this, gross margins increased in the year as we maintained our pricing discipline in a competitive market. The combination of these factors resulted in a decline in the new business operating margin to 7.0% for 2013 (2012: 7.4%).

In-force operating profit

In-force operating profit amounted to £34.3m for the year ended 31 December 2013 compared to £14.3m for 2012. The result in 2013 included a £21m benefit from assumption and other changes, primarily driven by economies of scale achieved during the year producing an expense assumption profit. In addition, we benefited in the second half of the year from an assumption change due to lower investment fees. This level of assumption change is not expected to reoccur. Underlying profits emerging from the in-force book were in line with our expectations and reflect the growth of the in-force book as a whole.

During the year, a full review of the mortality basis for annuity business was undertaken. The overall impact of the resulting change in basis on the IFRS liabilities was not material.

Long-term return on surplus assets

Long-term expected return on surplus assets for the year ended 31December 2013 was up by £7.4m to £11.4m (2012: £4.0m) predominantly as a result of an increase in surplus funds and the allocation of these out of cash and into higher yielding assets.

Investment variances

The positive investment variance in the period reflects an increase in risk-free yields and a narrowing spread between risk-free yields and the yields achieved on the Group's corporate bonds in 2013.

Non-recurring expenditure

Non-recurring expenditure of £30.8m for the year (2012: £5.7m) comprises:

- £15.8m expenses in respect of the Group's restructuring and IPO (2012: £2.3m);
- £9.8m charge related to the Group's staff share option plan which vested in full as a result of the IPO (2012: £1.5m);
- £4.1m of costs relating to regulatory projects (Solvency II) and re-engineering of financial processes (2012: £1.9m);
- £1.1m of other costs including redundancy, office relocation costs and other professional fees (2012: £nil).

Other losses

Other losses relate to sundry income and costs arising in the distribution subsidiaries of the Group and holding company expenses.

Interest on borrowings

Interest on borrowings is £9.1m lower than the amount for 2012 as during 2013 the loan notes were converted into equity as part of the IPO and related group restructuring and the £70m bank loan drawn down in 2012 was repaid on 21 August 2013 using proceeds from the IPO.

IFRS Profit before tax

IFRS profit before tax amounted to £82.7m compared to £67.5m for 2012. The increase is due to higher operating profits, an investment profit for the year and lower interest expense following repayment of debt in the year.

Capital information

Capital Management

The Group's Economic Capital and IGD capital ratios as at 31 December 2013 are strong. The Economic Capital and IGD capital positions as at 31 December 2013 are calculated at the Group's top holding company, PAG plc.

	Economic Capital		IGD[2]	
	2013 £m	2012[1] £m	**2013 £m**	2012 £m
Total Capital Available	**467**	356	**469**	328
Capital Required	**294**	252	**193**	163
Excess Surplus	**173**	104	**276**	165
Coverage Ratio (%)	**159%**	141%	**243%**	201%

1 Calculated at PLACL level.

2 The IGD calculated at EEA Group Parent level being Partnership Holdings Limited at 31 December 2012 and PAG plc at 31 December 2013.

Excess Capital surplus on both an Economic Capital and IGD basis showed an improvement from the position as at 31 December 2012. The key drivers for these are: additional capital raised during the IPO; expense efficiencies relating to the growing in-force book; positive investment performance; profits earned during the year and equity release assets acquired.

Stress and scenario testing

The Group undertakes stress and scenario tests to ensure the robustness of the Economic Capital 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, 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 on the economic capital ratio of the stress and scenario tests for the most material risks are set out below:

	Economic Capital Ratio	
	2013	2012
Basic coverage ratio	**159%**	151%
Credit spread widening + 100 bps	**157%**	149%
Credit spread widening + 200 bps	**153%**	146%
Euro zone crisis[3]	**151%**	142%
"Lehman" crisis[3]	**145%**	139%
Longevity – 5/10% deterioration	**152%**	134%
Property – 10% price fall	**151%**	143%

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

The interim guidance on Solvency 2 published recently by the European Insurance and Occupational Pensions Authority (EIOPA) brings us closer to the implementation of this new EU-wide capital regime which looks likely to come into force in 2016. While it remains uncertain how the new rules will be introduced into the UK regulatory framework, we believe that the group is well placed to accommodate the changes.

The marketplace context

Long-term structural growth expected in non-standard annuities

A growing market

Annuities currently represent a significant and growing proportion of the at-retirement market in the UK, accounting for £11.9bn in premiums in 2013 (on a single premium equivalent (“SPE”) basis), an increase of 138% since 2000.

We believe the total annuity market will grow strongly in the near future, with the market growth underpinned by several structural growth drivers as set out below.

Changing demographics

The UK population is living longer, with the number of people in the population who are age 65 and over forecast to grow from an estimated 10.5m in 2011 to 18.7m in 2041 (source: Office for National Statistics (“ONS”)).

Switching from defined benefit to defined contribution pensions

In recent years, there has been a shift from defined benefit (“DB”) scheme membership to defined contribution (“DC”) scheme membership as DB schemes close to new members. This shift is expected to continue, so that DC and DB assets represent equal proportions by 2019, with DC schemes representing an estimated 96% of total pension assets under management by 2030 (source: Oliver Wyman).

Various factors have driven this trend, including DB scheme members living longer and the closure of DB schemes. The number of private sector DB schemes in the UK that are open to new members is decreasing and most DB schemes are not accruing further benefits and are in run-off.

The UK Government has also promoted greater access to and use of DC schemes, including stakeholder pensions, in order to increase pension saving. In 2012, the UK Government further encouraged pension savings into DC pension funds through the introduction of ‘auto-enrolment’, requiring all employers over a certain size to enrol all employees into a DC pension savings plan, unless the employees actively request non-participation.

Government activity and regulatory pressure

The UK Government is progressively seeking to reduce reliance on state-funded pensions by implementing plans such as increasing the age at which an individual is entitled to receive a state pension and promoting personal retirement saving through schemes such as the National Employment Savings Trust (“NEST”), participation in which is expected to grow substantially over the next decade (source: Oliver Wyman).

Pension funding gap

The significant pension funding gap (which represents the difference between the income needed to live comfortably in retirement and the actual income individuals can currently expect from existing savings levels) in the UK (estimated at approximately £318bn per annum as of 2010 (source: Aviva)) and government encouragement for individuals to save for retirement should act as a catalyst for retirement savings growth.

Finally, the size of the annuity market is also driven by income growth, contribution changes and investment returns on accumulated pension assets.

Increasing pressure to exercise open market option

There continues to be regulatory and consumer group pressure, most recently in the findings of the FCA's Thematic Review of the UK annuity market, for more people to explore the annuity rates available to them from companies other than their pension savings company when they retire. The majority of people will secure a better retirement income if they shop around for their annuity. Whilst progress has been made in this area, with 49% of people in 2013 exercising their open market option ("OMO"), there remains scope for more people to do so.

Market size – annual £m

	Total external annuity sales	Total NSA Market
2009	5,438	1,735
2010	5,986	2,423
2011	6,337	3,079
2012	8,470	4,523
2013	**6,880**	**3,832**

Increasing penetration of enhanced annuities in the open market option market

Over the past few years, the proportion of enhanced annuities sold as a proportion of all OMO business has increased rapidly, driven by the growth of specialist providers, including Partnership. The market disruption we have experienced in 2013 has resulted in OMO business decreasing in the year as a proportion of the total market. The non-standard annuity market has been similarly affected, with around 32% of all annuities sold being non-standard, the same proportion as 2012. In 2010, this proportion was 22%.

We welcome the adoption of the Association of British Insurers Code of Conduct on Retirement Choices in 2013 and the findings of the FCA Annuity Review in 2014, both of which should help to ensure that all customers are aware of and have considered an enhanced annuity. We believe that these factors should result in a continued increase in the proportion of people exercising the OMO and increase penetration of enhanced annuities going forward.

The corporate market

There are a number of annuity-based initiatives being considered by trustees of DB schemes in response to the challenge of managing increasing liabilities. This remains a significant and long-term challenge for corporate sponsors and has led to an increasing focus on active deficit management strategies. There are two strategies currently undertaken at the scheme level and at the member-level, both of which replace DB scheme liabilities with annuity purchases:

- Bulk risk transfer solutions which involve the substitution of annuities provided by a third party insurer which replicate some or all of the sponsor's payment obligations under its DB scheme. These risk transfer solutions are designed to provide an equivalent guaranteed retirement income to scheme members whilst removing or reducing future pension liabilities and uncertainty for the corporate sponsor; and
- Member-level risk transfer solutions include the Total Pension Income Exchange ("TPIE") process, whereby a population of scheme members is offered the opportunity to purchase an annuity in exchange for the transfer to the annuity provider of the cash equivalent transfer value of their DB schemes. Because such processes allow an analysis of individual scheme member longevity, we are able to offer a non-standard annuity product to some scheme members, potentially increasing the attractions of the TPIE solution for both scheme members and corporate sponsors.

We believe that the market opportunity from DB liability management exercises has the potential for significant growth, particularly bulk transactions.

Care

The market for sales of annuity funding solutions for long-term care remains a relatively small one in the UK, and, as a result, our strategy continues to focus on ways in which the substantial number of privately funded individuals entering residential and nursing care in the UK can access these annuity products.

The core market of self-funded care residents is a market estimated by Partnership at circa £7bn per year, but the provision of financial advice and take-up of Immediate Needs Annuities ("INA") product remains low.

Based on the most recent market data, the underlying trend and demographic drivers would indicate that the outlook for INA sales in the UK remains positive. The core demographic of 85+ year olds is projected by the ONS to be the fastest growing segment of UK population in coming years, and underlying its projections is an annual average growth in this segment of the population of circa 3% per year. The cost of care, a key driver of the level of INA premium, has also shown above inflation levels of growth historically.

Offsetting this is the impact of continued uncertainty over Government Care policy and continuing disruption caused by the introduction of the RDR.

Protection

The protection market in the UK is mature and, for standard and mildly impaired lives, well-served by providers with mature medical underwriting capability.

However, there are customers for whom the mainstream providers do not provide a price for protection. Our proprietary Intellectual Property ("IP") on impaired lives means that we are able to provide protection insurance where other providers cannot and this represents a small but significant market in which Partnership currently takes a small share.

Our place in the market

A market leader in enhanced and care annuities

Individual annuities

The majority of annuities sold by us are impaired annuities designed for customers with reduced life expectancy as a result of health conditions such as cancer.

We also provide “lifestyle” annuities, PA Lite and Smoker annuities, where underwriting is more straightforward.

Since 2010 our growth in this part of the annuity market has been significant, with our market share in 2013 at 31%. The sales recorded in 2013 put us in a leading position in this market.

Corporate defined benefit

We participate in the DB market through an enhanced buy-in/buy-out proposition which involves a bulk transfer of annuity liability from pension schemes.

We focus on smaller DB schemes where our individual underwriting of members with medical conditions can offer scheme trustees an attractive liability transfer price.

We have been successful in developing these new markets and see significant opportunities for future growth.

Care annuities

During 2013 we were one of only two providers of care (immediate needs) annuities in the UK. Whilst we have had success in this market, growth is constrained by a lack of advice to self-funding entrants into care. To help address this issue, we have established “Paying For Care” – a not-for-profit organisation that is designed to provide information and enable self-funding care entrants to access qualified financial advisers.

We are also actively engaged with local authorities and care homes to help ensure people are obtaining appropriate advice and to help drive market growth.

Protection

We also write a limited amount of non-standard life protection business for individuals who are unable to obtain cover elsewhere. Protection products pay out a pre-determined amount on death of the policyholder in exchange for regular premium payments over the life of the policy.

Whilst not a large component of our business, the non-standard life protection market is attractive to us because it serves an important customer need and there are opportunities for growth in the future.

Directors' Responsibility Statement to Disclosure and Transparency Rule 4 (extracted from the 2013 Annual Report and Accounts)

The Annual Report and Accounts contains the following statements regarding responsibility for the financial statements and business review included in the Annual Report and accounts.

We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with the IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial positions and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- The Directors' report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a descriptions of the principal risk and uncertainties that they face; and
- The Board confirms that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the performance, strategy and business model of the Company.

By order of the Board

Steve Groves

Chief Executive Officer

Consolidated statement of comprehensive income

For the year ended 31 December 2013

	Note	**2013 £000's**	2012 2 £000's
Gross premiums written	1	**1,159,562**	1,468,008
Outward reinsurance premiums		**(733,849)**	(554,620)
Net premiums earned before restructure of reinsurance treaty		**425,713**	913,388
Reinsurance premium related to restructure of treaty		**–**	(495,803)
Net premiums earned		**425,713**	417,585
Net investment income	3	**137,762**	290,738
Share of results of joint venture		**(162)**	(40)
Other income		**219**	180
Total income		**563,532**	708,463
Gross claims paid		**(341,124)**	(273,655)
Reinsurers' share of claims paid		**225,277**	188,462
Recovery related to recapture of reinsurance treaty		**–**	99,748
Net claims (paid)/recovered		**(115,847)**	14,555
Change in insurance liabilities:			
Gross amount		**(624,290)**	(1,564,761)
Reinsurers' share not related to restructure and recapture		**428,197**	663,452
Reinsurers' share related to restructure and recapture	7	**–**	396,213
Net change in insurance liabilities		**(196,093)**	(505,096)
Acquisition costs		**(13,036)**	(34,566)
Investment expenses and charges		**(13,270)**	(8,178)
Interest on subordinated debt		**–**	(496)
Interest on external borrowings		**(25,403)**	(33,976)
Administrative and other expenses		**(117,223)**	(73,227)
Total expenses		**(168,931)**	(150,443)
Total claims, change in insurance liabilities and expenses		**(480,872)**	(640,984)
Profit from continuing operations before tax		**82,661**	67,479
Income tax charge from continuing operations		**(23,240)**	(17,245)
Profit for the year from continuing operations		**59,421**	50,234
Loss for the year from discontinued operations		**–**	(28)
Profit for the period		**59,421**	50,206
Profit/(loss) attributable to:			
- Owners of the Parent		**59,465**	50,193
- Non-controlling interest		**(44)**	13
Profit for the period		**59,421**	50,206
Basic earnings per ordinary share	4	**£0.17**	£0.18
Diluted earnings per ordinary share	4	**£0.17**	£0.18

Consolidated statement of changes in equity

For the year ended 31 December 2013

	Note	Share Capital £000's	Share Premium £000's	Capital Redemption Reserve £000's	Merger Reserve £000's	Shares held by Employee Benefit Trust £000's	Retained profit £000's	Total £000's	Non-controlling interest £000's	Total £000's
		Attributable to Owners of the Parent								
At 1 January 2013		**36**	**182**	**3,297**	**–**	**(33)**	**78,901**	**82,383**	**(22)**	**82,361**
PAGH shares exchanged for ordinary shares	14	**28,250**	**(182)**	**(3,297)**	**(24,521)**	**(250)**	**–**	**–**	**–**	**–**
Loan Notes exchanged for ordinary shares	14	**8,462**	**317,288**	**–**	**–**	**–**	**–**	**325,750**	**–**	**325,750**
Shares issued for cash	14	**3,252**	**121,993**	**–**	**–**	**(46)**	**526**	**125,725**	**–**	**125,725**
Share issue costs		**–**	**(4,032)**	**–**	**–**	**–**	**–**	**(4,032)**	**–**	**(4,032)**
Share-based payments		**–**	**–**	**–**	**–**	**271**	**9,053**	**9,324**	**–**	**9,324**
Profit for the year		**–**	**–**	**–**	**–**	**–**	**59,465**	**59,465**	**(44)**	**59,421**
At 31 December 2013		**40,000**	**435,249**	**–**	**(24,521)**	**(58)**	**147,945**	**598,615**	**(66)**	**598,549**

	Note	Share Capital £000's	Share Premium £000's	Capital Redemption Reserve £000's	Merger Reserve £000's	Shares held by Employee Benefit Trust £000's	Retained profit £000's	Total £000's	Non-controlling interest £000's	Total £000's
		Attributable to Owners of the Parent								
At 1 January 2012		3,330	182	–	–	(33)	27,208	30,687	(35)	30,652
Shares issued/										
(bought back) for cash	14	(3,294)	–	3,297	–	–	–	3	–	3
Share-based payments		–	–	–	–	–	1,500	1,500	–	1,500
Profit for the year		–	–	–	–	–	50,193	50,193	13	50,206
At 31 December 2012		36	182	3,297	–	(33)	78,901	82,383	(22)	82,361

Consolidated statement of financial position

As at 31 December 2013

	Note	**2013 £000's**	2012 £000's
Assets			
Property, plant and equipment		**15,459**	3,688
Goodwill		**126,207**	126,207
Other intangible assets	5	**16,401**	12,343
Financial assets	6	**3,950,443**	3,159,001
Investment in joint ventures		**206**	368
Reinsurance assets		**2,840,749**	2,412,551
Insurance and other receivables		**64,476**	94,881
Prepayments and accrued income		**70,817**	63,123
Deferred tax assets		**424**	158
Cash and cash equivalents		**112,741**	166,273
Total assets		**7,197,923**	6,038,593
Equity			
Share capital	14	**40,000**	36
Share premium	14	**435,249**	182
Capital redemption reserve	14	**–**	3,297
Merger reserve	14	**(24,521)**	–
Shares held by Employee Benefit Trust	14	**(58)**	(33)
Retained profit		**147,945**	78,901
Total equity attributable to owners of the Parent		**598,615**	82,383
Non-controlling interest		**(66)**	(22)
Total equity		**598,549**	82,361
Liabilities			
Insurance liabilities	7	**4,347,588**	3,723,298
Insurance and other payables		**32,088**	62,948
Financial liabilities	8	**2,201,500**	1,778,765
External borrowings	9	**–**	380,367
Current tax liabilities		**18,198**	10,854
Total liabilities		**6,599,374**	5,956,232
Total equity and liabilities		**7,197,923**	6,038,593

Consolidated cash flow statement

For the year ended 31 December 2013

	Note	**2013 £000's**	2012 £000's
Cash (used in)/from operations		**(56,851)**	46,171
Corporation tax paid		**(17,000)**	(17,074)
Net cash (used in)/from operating activities		**(73,851)**	29,097
Cash flows from investing activities:			
Purchase of property, plant and equipment		**(13,657)**	(3,058)
Purchase of other intangible assets		**(7,696)**	(7,385)
Net cash used in investing activities		**(21,353)**	(10,443)
Cash flows from financing activities:			
Proceeds from issuance of share capital		**121,693**	3
Repayment of subordinated debt	9	**–**	(16,000)
Repayment of loan notes	9	**(7,656)**	–
(Repayment)/receipt of bank loan	9	**(70,000)**	50,000
Proceeds from issuance of bank loan	9	**–**	68,075
Interest on subordinated debt		**–**	(496)
Interest payable on external borrowings		**(2,365)**	(829)
Net cash from financing activities		**41,672**	100,753
Net (decrease)/increase in cash and cash equivalents		**(53,532)**	119,407
Cash and cash equivalents brought forward		**166,273**	46,866
Cash and cash equivalents carried forward		**112,741**	166,273

Cash flows related to the sale and purchase of financial investments are included in operating cash flows as they are associated with the origination of insurance contracts and payment of insurance claims.

1. Segmental analysis

The operating segments reflect the level within the Group at which key strategic and resource allocation decisions are made and the way in which operating performance is reported internally to the chief operating decision makers in the Group, being the Board.

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 plus ten times the annual regular premium for new contracts written during the year. These revenue measures are monitored by the Board separately for each core target market.

a) Segmental analysis of profit

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

For the year ended 31 December	2013 £000's	2012 £000's
New business operating profit	**85,678**	93,871
In-force operating profit	**34,278**	14,263
Long-term expected return on surplus assets	**11,435**	3,997
Operating profit	**131,391**	112,131
Investment variances	**8,643**	(3,289)
Non-recurring expenditure	**(30,769)**	(5,735)
Other	**(1,201)**	(1,156)
Interest on borrowings	**(25,403)**	(34,472)
Profit from continuing operations before tax	**82,661**	67,479

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 comprises:

- £15.8m expenses in respect of the Group’s restructuring and IPO (2012: £2.3m);
- £9.8m charge related to the Group’s staff share option plan which vested in full as a result of the IPO (2012: £1.5m);
- £4.1m of costs relating to regulatory projects (Solvency II) and re-engineering of financial processes (2012: £1.9m);
- £1.1m of other costs including redundancy, office relocation costs and other professional fees (2012: £nil).

Other losses relate to the Group’s interest in distribution subsidiaries and holding company expenses.

The profit measure used by the 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 that are 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:

For the year ended 31 December	**2013 % pa**	2012 % pa
Cash	**0.5**	0.5
Gilts	**3.0**	3.0
Corporate bonds	**4.5**	4.5
Commodity trade finance	**10.0**	n/a

b) Segmental analysis of new business revenue by target market

For the year ended 31 December	**2013 £000's**	2012 £000's
Retirement	**1,159,616**	1,167,537
Care	**65,854**	94,362
Protection	**3,389**	2,738
Total single premium equivalent	**1,228,859**	1,264,637

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

Premiums are recognised in the accounting period in which an insurance contract commences, gross of any commission paid. Single premium retirement policies commence at the point that the policyholder accepts a quote. Other policies commence on the date set out in the individual policy contracts. Premiums which have been received and for which no contract is yet in-force are classified as payables arising from insurance contracts and are included within insurance and other payables in the Consolidated Statement of Financial Position. Where a contract has been issued but premiums have not yet been received, a debtor arising out of direct insurance operations is recognised for the expected premiums due. Reinsurance premiums and recoveries are accounted for in the accounting period in accordance with the contractual terms of the reinsurance treaties. Premiums exclude any taxes or duties based on premiums.

New business revenue by target market reconciles to gross premiums as follows:

For the year ended 31 December	**2013 £000's**	2012 £000's
Total single premium equivalent	**1,228,859**	1,264,637
Adjustment in respect of regular premium business	**(5)**	–
Premiums received in respect of equity release longevity insurance	**–**	2,522
Premiums arising from change to contract terms in 2012	**(69,335)**	109,580
Reinsurance premiums received	**43**	91,269
Gross premiums written	**1,159,562**	1,468,008

Premiums are written at the point an insurance contract comes into force. In November 2012, the Group changed the terms of its offer to potential retirement policyholders such that an insurance contract would come into force at the point of their acceptance of the offered terms. Previously a contract only came into force when all funds had been received from the policyholder. For management purposes SPE continues to be recorded when all funds have been received from the policyholder. £109.6m of premium recognised in 2012 would otherwise have been

recognised in 2013 and £40.3m of the premium recognised in 2013 would otherwise have been recognised in 2014 so that total premium recognised in 2013 was £69.3m lower than would otherwise have been recognised. This also gives rise to amounts due from policyholders for premiums not yet received.

d) Product revenue information

The following table illustrates revenue by product as required by IFRS 8 “Operating Segments”. All revenues from external customers are 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:

For the year ended 31 December	2013 £000’s	2012 £000’s
Retirement annuity	**1,090,282**	1,277,177
Care annuity	**65,979**	94,508
Protection life assurance	**3,258**	3,433
Other	**43**	92,950
Total gross premiums written	**1,159,562**	1,468,008

2. Basis of preparation and adoption of new and revised standards

Partnership Assurance Group (PAG) plc (the "Company") was incorporated and registered in England and Wales on 26 February 2013 as a public company limited by shares. The Company's registered office address is Heron Tower, 110 Bishopsgate, London, EC2N 4AY. The Company and the entities controlled by the Company (its "subsidiaries") are collectively "the Group".

The results included in this announcement have been extracted from the audited consolidated annual financial statements of the Group made up to 31 December 2013. The consolidated financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and endorsed by the European Union ("EU"), and those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The Group has adopted the following new and amended standards which became effective for financial years beginning 1 January 2013:

- Amendments to IFRS 7 "Offsetting Financial Assets and Financial Liabilities"
- IFRS 13 "Fair Value Measurement"
- Amendments to IAS 1 "Presentation of Items of Other Comprehensive Income"
- Amendments to IAS 12 "Income Taxes"

None of these standards and amendments has a material impact on these financial statements.

This announcement does not constitute statutory accounts as defined in Section 434 of the Companies Act 2006.

The auditors have reported on the consolidated financial statements. Their report was unqualified, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

The Directors have undertaken a going concern assessment in accordance with 'Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009', published by the Financial Reporting Council in October 2009. The Directors have adopted the going concern basis in preparing the consolidated financial statements.

3. Net investment income

Investment income comprises interest received on financial investments, realised investment gains and losses and movements in unrealised gains and losses.

Expenses and charges are included on an accruals basis.

Realised gains and losses on investments are calculated as the difference between net sales proceeds less costs of sale and original cost. Unrealised gains and losses on investments represent the difference between the valuation at the balance sheet date and their purchase price or if they have been previously valued their valuation at the last balance sheet date. The movement in unrealised gains and losses recognised in the year also includes the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

For the year ended 31 December	2013 £000's	2012 £000's
Interest receivable from financial assets	**138,533**	113,479
Interest payable from financial liabilities	**(71,596)**	(58,970)
Movement in fair value of financial assets	**26,616**	247,126
Movement in fair value of financial liabilities	**17,382**	(38,787)
Realised gains on financial assets	**72,604**	65,531
Realised losses on financial liabilities	**(45,777)**	(37,641)
Total net investment income	**137,762**	290,738

All financial assets and liabilities at 31 December 2013 are classified at fair value through profit and loss.

4. Earnings per share

Basic earnings per share is calculated using the earnings attributable to ordinary equity holders of the parent, divided by the weighted average number of ordinary shares in issue during the period.

For diluted earnings per share, the weighted average number of ordinary shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares, including share options.

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:

For the year ended 31 December	2013 £000's	2012 £000's
Profit for the year	**59,421**	50,206
Less non-controlling interests	**44**	(13)
Profit attributable to equity holders of the Parent	**59,465**	50,193
Effect of dilutive potential ordinary shares:		
Share options	**–**	–
Diluted profit attributable to equity holders of the Parent	**59,465**	50,193

All of PAGH's A, B and C shares (see note 13) were exchanged for PAG plc shares on 12 June 2013. For the purpose of the earnings per share calculation, the weighted average number of share shown below has been calculated as if the exchange of these PAGH shares had occurred at the beginning of the comparative period.

For the year ended 31 December	2013 Number of Shares	2012 Number of Shares
Basic weighted average number of shares	**346,138,910**	279,527,196
Effect of dilutive potential ordinary shares:	**–**	–
Share options	**1,276,243**	2,133,025
Diluted weighted average number of shares	**347,415,153**	281,660,221

The options granted by the PAGH trust in respect of the ESOP scheme have a dilutive effect, up to the date of the IPO when these options vested.

The Group implemented a number of new employee share-based plans following admission on the London Stock Exchange. The Share Incentive Plan (SIP) has a potential dilutive effect.

No decisions have been made as to the method of settlement of the Long Term Incentive Plan (LTIP) or the share element of the Deferred Share Bonus Plan (DSBP). 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 with shares bought externally from the market and hence will not be dilutive.

5. Other intangible assets

Other intangible assets comprise intellectual property and software development costs.

The intellectual property asset comprises of specific mortality tables derived from data collected over an extended period and are deemed to have an indefinite life. Consequently no amortisation is charged against its carrying value.

Development costs that are directly attributable to the design and testing of identifiable software products, controlled by the Group, are recognised as intangible assets when it can be demonstrated that it is technically feasible to complete the product so that it is available for use and will generate probable future economic benefits. Software development costs have a finite useful life and are amortised using the straight-line method over three to five years.

Impairment review of other intangible assets

The carrying amounts of intangible assets with finite expected useful economic lives are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. A review for indicators of impairment is conducted annually. The carrying amounts of intangible assets with indefinite expected useful economic lives are tested for impairment at least annually, or when circumstances or events indicate there may be uncertainty over this value. An impairment loss is recognised in the Consolidated Statement of Comprehensive Income for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount of an asset is the greater of its net selling price (fair value less selling costs) and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit, or company of units, to which the asset belongs.

	2013 £000's	2012 £000's
Intellectual property cost and carrying amount:		
At 1 January	**3,100**	3,100
At 31 December	**3,100**	3,100
Software development cost:		
At 1 January	**11,750**	4,365
Additions at cost	**7,696**	7,385
Assets written off	**(1,641)**	–
At 31 December	**17,805**	11,750
Software development accumulated amortisation:		
At 1 January	**2,507**	1,244
Charge for the year	**1,997**	1,263
Eliminated on disposals	**–**	–
At 31 December	**4,504**	2,507
Total intangible assets at 1 January	**12,343**	6,221
Total intangible assets at 31 December	**16,401**	12,343

The value of intellectual property has been determined based upon an estimate of the costs to employ adequately skilled individuals over an appropriate period of time to develop intellectual property of a similar nature sufficient to enable the Group to replicate the estimated future cash flows and profits deriving from that intellectual property.

The intellectual property is continually updated through the collection of further data, updated analyses, and conversion into new and more detailed underwriting manuals and mortality tables. For this reason, the intangible asset is deemed to have an indefinite life, and consequently, no amortisation is provided against the value of the intangible asset. The carrying value of the intangible asset is tested for impairment at each reporting date, and is allocated to the "new business" cash-generating unit, the scope of which is identical to the "new business" operating segment described in note 1. The method and assumptions used in this test are identical to those applied in the goodwill impairment test.

No impairment of intellectual property has been recognised in 2012 or 2013.

The amortisation period for software development costs is three to five years. During the year the intangible assets relating to software development were reviewed for impairment. As a result of this certain software assets were identified as no longer being expected to generate economic benefits for the Group. No other indicators of impairment existed in respect of software development costs as at the balance sheet date.

6. Financial assets

Financial assets classification

The Group classifies its financial assets as financial investments, loans secured by mortgages and derivative financial assets at fair value through profit and loss. The category of fair value through profit and loss has two sub-categories: those that meet the definition as being held for trading; and those that the Group chooses to designate as fair value. The fair value through profit and loss is selected as the Group's strategy is to manage its financial assets, as a portfolio, on a fair value basis.

Financial investments

Purchases and sales of debt securities and other fixed income securities are recognised on the trade date, which is the date that the Group commits to purchase or sell the assets, at their fair values. Transaction costs are expensed as incurred. These investments are derecognised when the contractual rights to receive cash flows from the investments expire, or where the investments have been transferred, together with substantially all the risks and rewards of ownership.

Debt securities and other fixed income securities are subsequently carried at fair value with changes in fair value included in the Consolidated Statement of Comprehensive Income in the period in which they arise.

The fair values of debt securities are based on quoted bid prices, or based on modelled prices (using observable market inputs) where quoted bid prices are not available.

Investments in Commodity Trade Finance loans are carried at fair value on initial recognition and are recognised when the cash is advanced for the trade. Commodity Trade Finance loans are subsequently carried at fair value with changes in fair value included in the Consolidated Statement of Comprehensive Income in the period in which they arise. The fair value of these investments is not based on observable market data.

Loans secured by mortgages

Loans secured by mortgages are recognised when the cash is advanced to borrowers at their fair values. These loans are derecognised when the contractual rights to receive cash flows from the investments expire, or where the investments have been transferred, together with substantially all the risks and rewards of ownership.

Loans secured by mortgages are subsequently carried at fair value with changes in fair value included in the Consolidated Statement of Comprehensive Income in the period in which they arise.

The fair value of loans secured by mortgages is initially deemed to be the transaction price and subsequently marked to model. The underlying model follows the methodology used to establish transaction prices. It uses longevity assumptions to derive expected cash flows and the Black Scholes option pricing methodology to establish the value of the no negative equity guarantee that is embedded in the product. The discount rates that are applied to cash flows to produce fair value are based on long dated swaps adjusted so that they would produce transaction date prices on the date of transaction.

Derivative financial instruments

The Group enters into a variety of derivative financial instruments to manage its exposure to interest rates, inflation, credit default and foreign exchange rate risk, including foreign exchange forward contracts, interest rate swaps, credit default swaps and inflation swaps.

Derivative contracts are traded either through an exchange or over the-counter ("OTC"). OTC derivative contracts are individually negotiated between contracting parties and can include options, swaps, caps and floors.

Derivatives are initially recognised at fair value at the date that a derivative contract is entered into and are subsequently remeasured to fair value at each balance sheet date. The resulting gain or loss is recognised in the Consolidated Statement of Comprehensive Income. The fair values are obtained from quoted market prices or, if these are not available, by using standard valuation techniques based on discounted cash flow models or option pricing models. All derivatives are carried as assets when the fair value is positive and liabilities when the fair values are negative. Premiums paid for derivatives are recorded as an asset in the Consolidated Statement of Financial Position at the date of purchase representing their fair value at that date.

Fair value at 31 December	**2013** **£000's**	2012 £000's
Financial investments	**3,073,964**	2,645,997
Loans secured by mortgages	**840,066**	478,097
Derivative assets	**36,413**	34,907
Total financial assets	**3,950,443**	3,159,001

Cost at 31 December	**2013** **£000's**	2012 £000's
Financial investments	**2,991,196**	2,464,790
Loans secured by mortgages at cost	**796,788**	414,500
Derivative assets	**–**	–
Total financial assets	**3,787,984**	2,879,290

The methodology used to derive the fair values is set out in note 10.

7. Insurance liabilities and reinsurance assets

Insurance liabilities

Insurance contracts are defined as those containing significant insurance risk if, and only if, an insured event would cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire.

The Group's long-term insurance contracts include annuities to fund retirement income, annuities to fund care fees (immediate needs and deferred), long-term care insurance and whole of life and term protection insurance. These contracts are expected to remain in force for an extended period of time, and insure events associated with human life.

One of the purposes of insurance is to enable policyholders to protect themselves against future uncertain events such as death or specific types of illness. Insurance companies accept the transfer of uncertainty from policyholders and seek to add value through the aggregation and management of these risks. As a consequence of this uncertainty, estimation techniques are employed by suitably qualified personnel in computing the levels of provisions held against such uncertainty.

The insurance liabilities, which are also referred to as the long-term business provision and policyholder reserves elsewhere in this report, are determined by the Partnership Board on the advice of the Group's Actuarial Function Holder on the modified statutory basis using recognised actuarial methods with due regard to the actuarial principles set out in the PRA's (formerly the FSA's) Insurance Prudential Sourcebook. In particular, a prospective gross premium valuation method has been adopted for major classes of business.

Although the process for the establishment of insurance liabilities follows specified rules and guidelines, the provisions that result from the process remain uncertain. As a consequence of this uncertainty, the eventual value of claims could vary from the amounts provided to cover future claims. The Group seeks to provide for appropriate levels of contract liabilities taking known facts and experiences into account but nevertheless such provisions remain uncertain.

The estimation process used in determining insurance liabilities involves projecting future annuity payments and the costs of maintaining the contracts. For non-annuity contracts, the long-term business provision is determined as the sum of the discounted value of future benefit payments and future administration expenses less the expected value of premiums payable under the contract. The key sensitivities are the assumed level of interest rates and the mortality experience.

At the balance sheet date, provision is made for all notified claims plus an estimate for those claims that have been incurred but not reported.

Reinsurance assets

Long-term business is ceded to reinsurers under contracts to transfer part or all of one or more of the following risks: mortality, morbidity, investment, persistency and expenses. The benefits to which the Group are entitled under its reinsurance contracts held are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers (classified within "Insurance and other receivables") as well as longer-term receivables that are dependent on the expected benefits arising under the related reinsured contracts.

Amounts recoverable from reinsurers are estimated in a consistent manner with insurance liabilities, and are classified as "reinsurance assets".

Some contracts, which provide for the transfer of significant risk, are also structured to provide financing. When, under such contracts, financing components are to be repaid in future accounting periods, the amount outstanding under the contract at the balance sheet date are classified as "payables arising from reinsurance contracts" and included within insurance and other payables in the Consolidated Statement of Financial Position.

If the reinsurance asset were impaired, the Group would adjust the carrying amount accordingly and recognise that impairment loss in the Consolidated Statement of Comprehensive Income. A reinsurance asset is impaired if there is objective evidence, as a result of an event that occurred after initial recognition of the reinsurance asset, that the Group may not receive all amounts due to it under the terms of the contract, and the event has a reliably measurable impact on the amounts that the Group will receive from the reinsurer

Liability adequacy test

At the end of each reporting period, liability adequacy tests are performed to ensure the adequacy of the insurance liabilities. In performing these tests, current best estimates of future contractual cash flows and claims handling and

administration expenses, as well as investment income from assets backing such liabilities, are used. Any deficiency is immediately charged to the Consolidated Statement of Comprehensive Income.

Claims

Maturity claims and annuities are charged against revenue when due for payment. Death claims and all other claims are accounted for when notified. Claims reinsurance recoveries are accounted for in the same period as the related claim. Where reinsurance treaties are recaptured, amounts received to compensate for the transfer of risk from the reinsurer are accounted for when received or, if earlier, on the date the treaty ceases to be included within the calculation of the reinsurers' share of long-term business provision.

As at 31 December	**2013 £000's**	2012 £000's
Long term business provision	**4,347,588**	3,723,298
Reinsurers' share of long term business provision	**(2,840,749)**	(2,412,551)
Net provision	**1,506,839**	1,310,747

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	2013	Modified E&W Population Mortality with CMI 2012u (1.75%) and CMI 2012F (1.50%)	4.31%
	2012	Modified PML/PFL92 (U=2013) modified ave MC & LC floor 1.5%	3.76%
Other annuity products	2013	Modified PCMA/PCFA00u2014 p-spline	1.70%
	2012	Modified PCMA/PCFA00u2013 p-spline	2.26%
Term and whole of life products	2013	86.25% TM/TF00Select	1.44%
	2012	86.25% TM/TF00Select	1.07%

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 47% (2012: 37%) 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 year ended 31 December 2013	**Gross £000's**	**Reinsurance £000's**	**Net £000's**
At 1 January 2013	**3,723,298**	**(2,412,551)**	**1,310,747**
Increase in liability from new business	**1,038,011**	**(678,827)**	**359,184**
Release of in-force liability	**(111,110)**	**75,012**	**(36,098)**
Release of liability due to recorded deaths	**(69,967)**	**31,040**	**(38,927)**
Economic changes	**(209,299)**	**144,164**	**(65,135)**
Non-economic changes	**(25,847)**	**1,609**	**(24,238)**
Other	**2,502**	**(1,196)**	**1,306**
At 31 December 2013	**4,347,588**	**(2,840,749)**	**1,506,839**

For the year ended 31 December 2012	Gross £000's	Reinsurance £000's	Net £000's
At 1 January 2012	2,158,537	(1,352,886)	805,651
Increase in liability from new business	1,324,979	(532,265)	792,714
Release of in-force liability	(48,465)	30,083	(18,382)
Release of liability due to recorded deaths	(61,815)	36,098	(25,717)
Recapture and restructure of reinsurance treaties*	–	(396,213)	(396,213)
Economic changes	335,573	(200,464)	135,109
Non-economic changes	11,266	–	11,266
Other	3,223	3,096	6,319
At 31 December 2012	3,723,298	(2,412,551)	1,310,747

* The impact of the recapture and restructure of reinsurance treaties has been calculated as if both transactions occurred on 31 December 2012 before the impact of year end basis changes.

c) Analysis of expected maturity

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

	Expected cash flows (undiscounted)				
At 31 December 2013	**less than one year £000's**	**one to five years £000's**	**five to ten years £000's**	**more than ten years £000's**	**Carrying value (discounted) £000's**
Gross	373,419	1,360,968	1,450,164	3,829,024	4,347,588
Reinsurance	(241,692)	(903,711)	(985,311)	(2,544,018)	(2,840,749)
Net	131,727	457,257	464,853	1,285,066	1,506,839

	Expected cash flows (undiscounted)				
At 31 December 2012	less than one year £000's	one to five years £000's	five to ten years £000's	more than ten years £000's	Carrying value (discounted) £000's
Gross	300,885	1,080,196	1,122,562	2,998,611	3,723,298
Reinsurance	(191,170)	(711,459)	(767,756)	(2,028,997)	(2,412,551)
Net	109,715	368,737	354,806	969,614	1,310,747

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:	**2013** **£000's**	2012 £000's
Interest rates + 1%	**2,954**	1,362
Interest rates - 1%	**(3,308)**	(8,610)
Credit spreads + 0.5%	**(10,917)**	(7,305)
Expenses + 10%	**(9,962)**	(8,894)
Mortality - 5%	**(22,140)**	(19,791)
Property Prices - 10%	**(25,313)**	(11,093)
Voluntary redemptions + 10%	**(2,402)**	2,871

8. Financial liabilities

As well as derivative financial liabilities, the Group carries financial liabilities where assets under specific reinsurance treaties are legally and physically deposited back to the Group by reinsurers. Financial liabilities are classified as at fair value through profit and loss. As such, financial liabilities are initially recognised at fair value on the same date that the value of underlying deposited assets is recognised and are subsequently remeasured at fair value at each balance sheet date. The resulting gain or loss is recognised in the Consolidated Statement of Comprehensive Income. The net gain or loss recognised incorporates any interest paid on the financial liability. Fair value is determined as the amount payable discounted from the first date that the amount is required to be paid.

A financial liability (including subordinated debt and external borrowings) is generally derecognised when the contract that gives rise to it, is settled, sold, cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, such that the difference in the respective carrying amounts together with any costs or fees incurred are recognised in the Consolidated Statement of Comprehensive Income.

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into.

As at 31 December	**2013** **£000's**	2012 £000's
Payables arising from reinsurance contracts	**2,169,109**	1,728,998
Derivative liabilities	**32,391**	49,767
Total financial liabilities	**2,201,500**	1,778,765

Payables arising from reinsurance contracts at fair value through profit and loss are designated as such on initial recognition. Derivative liabilities are carried at fair value through profit and loss.

9. External borrowings

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.

As at 31 December	**2013 £000's**	2012 £000's
Due in more than five years:		
Loan notes issued, repayable otherwise than by instalments (unsecured)	–	299,823
Less capitalised debt issuance costs on loan notes	–	(2,519)
Interest payable on loan notes	–	14,458
Due in one to five years:		
Bank loan	–	70,000
Less capitalised debt issuance costs on bank loan	–	(1,765)
Interest payable on bank loan	–	370
Total external borrowings	–	380,367

- A and B Loan notes totalling £151,667,000 were issued by PAGF, a Group company, to the Fourth Cinven Fund and other third parties on 5 August 2008. The interest rate on these notes was 12% per annum and was payable at six monthly intervals starting on 30 June 2009 at the discretion of the Group. In the event that interest payments were not made, the amounts due accrued interest at the same rate from the date payment was due. Additional loan notes totalling £6.9m were issued during the period (31 December 2012: £25.6m) in settlement of interest accrued.
- On 21 August 2012, C Loan notes totalling £50.0m were issued by the Group to the Fourth Cinven Funds. The interest rate was fixed at 22% per annum and was payable at six monthly intervals starting 30 June 2013. In the event that interest payments were not made, the amounts due began to accrue interest at the same rate from the date payment was due.
- Vendor loan notes totalling £5.0m were issued by the Group on 5 August 2008 in connection with the acquisition of the former Group by the Cinven funds. The interest rate was fixed at 9% per annum and was payable at six monthly intervals starting 30 June 2009. In the event that interest payments were not made, the amounts due began to accrue interest at the same rate from the date payment was due.
- A bank loan of £70m was taken out on 21 August 2012. The bank loan carried a fixed interest rate at LIBOR plus 4% per annum. Debt issuance costs of £1,925,000 were capitalised, of which £1,491,000 was amortised in the period (2012: £160,000).
- As set out in note 13, as a result of the reorganisation steps undertaken before the admission of the Company to the London Stock Exchange, the A,B,C and Vendor loan notes, the bank loan and accrued interest were settled in the period.

The Group hedged its exposure to LIBOR, using an interest rate swap, whereby LIBOR payments were swapped for a fixed interest payment of 0.7% per annum for two years from the date the loan was taken. Interest was payable at three monthly instalments, in advance, starting 21 November 2012. Effective 21 June 2013, this interest rate swap arrangement was terminated.

10. Financial instruments – fair value methodology

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 31 December 2013 and 31 December 2012.

At 31 December 2013	**Level 1 £000's**	**Level 2 £000's**	**Level 3 £000's**	**Total £000's**
Financial investments (a)	**3,063,140**	**–**	**10,824**	**3,073,964**
Loans secured by mortgages (b)	**–**	**–**	**840,066**	**840,066**
Derivative assets (c)	**–**	**36,413**	**–**	**36,413**
Total financial assets held at fair value	**3,063,140**	**36,413**	**850,890**	**3,950,443**
Payables arising from reinsurance contracts (d)	**–**	**–**	**2,169,109**	**2,169,109**
Derivative liabilities (c)	**–**	**32,391**	**–**	**32,391**
Total financial liabilities held at fair value	**–**	**32,391**	**2,169,109**	**2,201,500**

At 31 December 2012	Level 1 £000's	Level 2 £000's	Level 3 £000's	Total £000's
Financial investments (a)	2,645,997	–	–	2,645,997
Loans secured by mortgages (b)	–	–	478,097	478,097
Derivative assets (c)	–	34,907	–	34,907
Total financial assets held at fair value	2,645,997	34,907	478,097	3,159,001
Payables arising from reinsurance contracts (d)	–	–	1,728,998	1,728,998
Derivative liabilities (c)	–	49,767	–	49,767
Total financial liabilities held at fair value	–	49,767	1,728,998	1,778,765

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.

During 2012, all the financial investments, with the exception of Commodity Trade Finance ("CTF") loans were reclassified from Level 2 to Level 1. Since the financial crisis in 2008, there has been a continual improvement in the level of liquidity in the fixed and variable rate securities markets, and having considered this during 2012, the Directors considered that the market is sufficiently active to allow classification of these financial investments as Level 1. There are no transfers between Levels 1, 2 and 3 during the period to 31 December 2013.

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

For the year ended 31 December 2013	Payables arising out of reinsurance contracts £000's	Commodity Trade Finance Loans £000's	Loans secured by mortgages £000's
At 1 January 2013	**(1,728,998)**	**–**	**478,097**
Loans (received)/advanced	**(733,849)**	**23,990**	**416,473**
Total (losses)/gains in Consolidated Statement of Comprehensive Income excluding reinsurance restructure	**(155,522)**	**(3,135)**	**(25,695)**
Redemptions made/(received)	**528,119**	**(11,306)**	**(34,187)**
(Interest payable accrued)/interest receivable accrued	**(78,859)**	**1,275**	**5,378**
At 31 December 2013	**(2,169,109)**	**10,824**	**840,066**

For the year ended 31 December 2012	Payables arising out of reinsurance contracts £000's	Commodity Trade Finance Loans £000's	Loans secured by mortgages £000's
At 1 January 2012	(809,641)	–	316,729
Loans (received)/advanced	(1,050,424)	–	148,030
Total (losses)/gains in Consolidated Statement of Comprehensive Income excluding reinsurance restructure	(75,427)	–	7,246
Total gains in Consolidated Statement of Comprehensive Income from reinsurance restructure	35,186	–	–
Redemptions made/(received)	224,083	–	(13,847)
(Interest payable accrued)/interest receivable accrued	(52,775)	–	19,939
At 31 December 2012	(1,728,998)	–	478,097

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 and loans secured by mortgages for the period to 31 December 2013 are £105.6m, £118.3m and £(14.1)m respectively (31 December 2012: £(40.2)m, £nil and £27.2m respectively). These unrealised gains and losses are included within net investment income in the Consolidated Statement of Comprehensive Income.

Level 3 Sensitivity Analysis

As at 31 December 2013		Reasonably Possible Alternative Assumptions		
		Current fair value £000's	Increase in fair value £000's	Decrease in fair value £000's
Assets				
Commodity Trade Finance Loans	Expected defaults	**10,824**	**350**	**(528)**
Loans secured by mortgages	Discount Rate, Value of no-negative equity guarantee	**840,066**	**100,863**	**(86,046)**
Liabilities				
Payables arising out of reinsurance contracts	Discount Rate	**(2,169,109)**	**(182,645)**	**161,733**

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 31 December 2013 and 31 December 2012, 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 includes 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 estimating the fair value of the CTF loans as at 31 December 2013 was 12.0% p.a. (31 December 2012: not applicable).

b) Loans secured by 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 various estimates, it is considered that only the discount rate and no-negative equity guarantee assumptions would have significant impact 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 31 December 2013 was 6.24% (31 December 2012: 5.89%).

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 31 December 2013 were 5.5% (31 December 2012: 5.5%) and 13% (31 December 2012: 13%) respectively. The over-valuation assumption used as at 31 December 2013 was 22% (31 December 2012: 17%). The value of the no negative equity guarantee as at 31 December 2013 was £67.3m (31 December 2012: £27.6m).

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.

c) 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 31 December 2013 and 31 December 2012 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 historical 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 historical 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.

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 31 December 2013, the Group had pledged £10.1m (31 December 2012: £13.8m) and held collateral of £0.9m (31 December 2012: £0.5m) in respect of over-the-counter derivative transactions.

d) Payables arising from reinsurance contracts

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 rate used as at 31 December 2013 for Retirement and Care was 4.95% and 1.97% respectively (31 December 2012: 4.53% and 2.45% respectively).

11. Management of insurance and financial risk

The Group issues contracts that accept insurance risk in return for a premium. In addition the Group is exposed to financial risk through its financial assets, financial liabilities, reinsurance assets and insurance liabilities. In particular, the key financial risk is that the proceeds from financial assets are not sufficient to fund the obligations arising from contracts with policyholders. The most important components of this financial risk are interest rate risk and credit risk. The Group is not exposed to any equity price risk and to currency risk only to an immaterial extent.

a) Insurance risk

a1) Underwriting, pricing and reserving risk

Underwriting and pricing risk is the risk that inappropriate business will be written, or an inappropriate premium will be charged for that business. Reserving risk is the risk that the insurance liabilities have been calculated incorrectly, or the assumptions used in the calculations are incorrect.

As the Group's insurance business is specifically targeted at people with medical 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 tailored underwriting manuals designed to specifically cover a large array of medical conditions.

The Group has developed its own proprietary underwriting manuals for retirement annuity business and those seeking care funding, based on industry standard mortality tables modified to take account of experience data recorded by the Group and its predecessor organisations.

The assumptions used in the reserving for future policyholder payments are set based on available market and experience data, on the advice of the Actuarial Function Holder. The assumptions are approved by the Partnership Board. The insurance liabilities are calculated using recognised actuarial methods with due regard to the actuarial principles set out in the Prudential Regulation Authority's Prudential sourcebooks.

a2) Specific insurance risk

Insurance risk on the 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 protection policies arises through higher than expected mortality levels. 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 also reduced significantly through the use of reinsurance. Expense risk is managed through regular assessment of expenses incurred against budgets and overall impact on profitability of the insurance contracts.

a3) Concentration of insurance risk

The Group writes annuity contracts for the provision of retirement income or care fees and protection insurance contracts, primarily for individuals in the UK with one or more medical conditions or lifestyle factors that are likely to reduce their overall life expectancy. The Group's insurance risk is therefore concentrated on longevity and mortality risk. These risks are significantly reduced through the Group's use of external reinsurance arrangements.

b) Interest rate and other market risk

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 insurance liabilities.

The Group manages its interest rate risk within an asset liability management (ALM) framework that has been developed to achieve long-term investment returns in excess of its obligations under insurance and investment contracts. The principal technique of the Group's ALM framework is to match assets to the liabilities arising from insurance contracts by reference to the type of benefits payable to policyholders.

The Group monitors interest rate risk by calculating the mean duration and cash flow profile of the investment portfolio and the liabilities. The mean duration is an indicator of the sensitivity of the assets and insurance liabilities to changes in current interest rates but is not sufficient in isolation. The mean duration of the liabilities is determined by means of projecting expected cash flows from the contracts using best estimates of mortality and voluntary terminations. No future discretionary supplemental benefits are assumed to accrue. The mean duration of the assets is calculated in a consistent manner. Any gap between the mean duration of the assets and the mean duration of the liabilities is minimised by means of buying and selling fixed interest securities of different durations or purchasing interest rate swap derivatives to alter the effective mean duration of the assets. Periodically the cash flow matching is reviewed and rebalanced.

At 31 December 2013, the mean duration of the assets was 7.5 years (2012: 7.7 years) measured with reference to a gross redemption yield and the mean duration of the liabilities was at 9.0 years (2012: 8.9 years) measured with reference to the valuation interest rate.

The Group has reinsurance arrangements in place which provide for fixed payments to the reinsurer over future periods. In assessing the fair value of this liability, the Directors have used a discount rate derived from current market yields earned on assets held to fund the future cash outflows, adjusted for the risk of default on those assets. No further adjustment to the discount rate to reflect any risk of the Group defaulting on those payments to the reinsurer was deemed appropriate.

c) Credit risk

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. Key areas where the Group is exposed to credit risk are exposure to:

- the issuer of corporate bonds;
- counterparties in derivative contracts;
- reinsurers in respect of their share of insurance liabilities; and
- reinsurers in respect of claims already paid.

The Group places limits on its exposures to a single counterparty, or groups of connected counterparties.

With respect to its investment in corporate bonds, the credit rating is derived from the Standard & Poor's, Moody and Fitch ratings for each individual stock, if two or more ratings are available the second highest rating is used otherwise the single available rating is used. The Group places limits on the exposure to bond issuers with different credit ratings. Credit default swaps are also used to manage exposure to single issuers. Current restrictions do not allow investment in any corporate bond with a rating below "BBB" (or equivalent). Where investments already held are subsequently downgraded, the Directors will review each holding to determine whether to retain that exposure.

At 31 December 2013, £0.5m of collateral (2012: £8.6m) had been pledged to the Group to mitigate the credit risk exposure associated with the derivative assets held at that time.

Reinsurance is used to manage insurance risk. This does not, however, discharge the Group's liability as primary insurer, and consequently, if a reinsurer fails to pay a claim, the Group remains liable for the payment to the policyholder. As a result, the Group is exposed to credit risk in relation to the reinsurers' ability to fulfil its obligations to the Group. The creditworthiness of reinsurers is considered by reviewing their financial strength prior to finalisation of any contract and then subsequently at least on an annual basis.

We seek to place new business with reinsurers with a minimum credit rating of "A".

For certain reinsurance treaties, the reinsurers share of annuity insurance liabilities is backed by investments deposited back with the Group, or held in trust for the beneficial ownership of the Group. In this way, the Group's exposure to the credit risk relating to the reinsurer is significantly reduced. The investment risk on investments deposited back with the Group, or held in trust for the beneficial ownership of the Group, is borne by the reinsurers. The following table analyses the credit exposure of the Group by type of asset and includes the credit risk arising out of reinsurance exposures, based on the credit ratings of the reinsurer, as published by Standard & Poors, or an equivalent rating from another recognised rating agency.

At 31 December 2013	AAA £000's	AA £000's	A £000's	BBB £000's	Credit rating Below BBB/Unrated £000's	Total £000's
Financial Investments	**601,351**	**257,263**	**1,170,898**	**1,033,628**	**10,824**	**3,073,964**
Derivative assets	**–**	**–**	**–**	**–**	**36,413**	**36,413**
Loans backed by mortgages	**–**	**–**	**–**	**–**	**840,066**	**840,066**
Reinsurance assets	**–**	**1,240,280**	**1,600,469**	**–**	**–**	**2,840,749**
Insurance and other receivables	**–**	**29**	**9,010**	**–**	**55,437**	**64,476**
Total	**601,351**	**1,497,572**	**2,780,377**	**1,033,628**	**942,740**	**6,855,668**

At 31 December 2012	AAA £000's	AA £000's	A £000's	BBB £000's	Credit rating Below BBB/Unrated £000's	Total £000's
Financial Investments	621,927	220,684	1,036,267	759,049	8,070	2,645,997
Derivative assets	–	–	–	–	34,907	34,907
Loans backed by mortgages	–	–	–	–	478,097	478,097
Reinsurance assets	–	1,353,220	1,059,331	–	–	2,412,551
Insurance and other receivables	–	–	5,627	–	89,254	94,881
Total	621,927	1,573,904	2,101,225	759,049	610,328	5,666,433

The following table presents an aging analysis of financial assets by payment due status:

As at 31 December 2013	Not past due	Past due but not impaired Less than 1 month £000's	1-3 months £000's	3-6 months £000's	More than 6 months £000's	Impaired	Total
Commodity Trade Finance	**6,350**	**–**	**742**	**3,732**	**–**	**–**	**10,824**
Loans secured by mortgages	**840,066**	**–**	**–**	**–**	**–**	**–**	**840,066**
Other financial assets	**6,008,985**	**–**	**–**	**–**	**–**	**–**	**6,008,985**

No other financial assets were past due at 31 December 2012.

d) Liquidity risk

Liquidity risk is the risk that cash may not be available to pay obligations when due at a reasonable cost. The Partnership Board sets limits on the minimum amount of highly liquid assets to be available to meet such obligations.

Short-term cash requirements are monitored on a daily basis to ensure sufficient funds are available to meet immediate payments. The nature of the Group's business means that, in general, cash flows into the Group (through up-front premium payments) before annuity payments become due. Annuity payments are substantially fixed in nature, and consequently the cash requirements are not subject to excessive uncertainty.

In accordance with PRA (formerly the FSA) regulations, the Group's assets are reviewed to ensure they are of sufficient amount and of an appropriate currency and term to ensure that the cash inflows from those assets will meet the expected cash outflows from the Group's insurance and other financial liabilities.

In the following table expected cash outflows for:

- net insurance liabilities have been modelled with reference to underlying mortality and longevity assumptions;
- payables arising from reinsurance include interest and payments due under the terms of reinsurance treaties;
- derivative liabilities have been modelled with reference to the yield curves that existed at the balance sheet date and assumed to be held to maturity; and

- subordinated debt is assumed to be repaid in accordance with the terms set out in the loan agreement.

The following table includes insurance and financial liabilities that are exposed to liquidity risk.

	Expected cash flows (undiscounted)				
At 31 December 2013	**less than one year £000's**	**one to five years £000's**	**five to ten years £000's**	**more than ten years £000's**	**Carrying value (discounted) £000's**
Net insurance liabilities	**131,727**	**457,257**	**464,853**	**1,285,066**	**1,506,839**
Payables arising from reinsurance contracts	**1,831,083**	**735,336**	**792,792**	**1,934,163**	**2,169,109**
Derivative liabilities	**584**	**10,252**	**14,381**	**15,596**	**32,391**
Total	**1,963,394**	**1,202,845**	**1,272,026**	**3,234,825**	**3,708,339**

	Expected cash flows (undiscounted)				
At 31 December 2012	less than one year £000's	one to five years £000's	five to ten years £000's	more than ten years £000's	Carrying value (discounted) £000's
Net insurance liabilities	109,715	368,737	354,809	969,614	1,310,747
Payables arising from reinsurance contracts	114,153	576,795	619,048	1,496,027	1,728,998
External borrowings	–	–	–	365,539	365,539
Derivative liabilities	8,406	27,856	5,142	11,971	49,767
Total	232,274	973,388	978,999	2,843,151	3,455,051

The maximum exposure to credit risk is equal to the balance sheet value of debt instruments/derivatives

e) Property risk

Property risk is the risk that property values do not rise sufficiently to recover the full value of equity release loans made plus accrued interest. The initial loan value is restricted to a maximum "loan to value" ratio that limits the risk exposure for the Group.

Loans backed by mortgages represent little credit risk as the debt is ultimately repayable from the proceeds of the sale of the property on death of the policyholder or on their transfer to long-term care.

12. Available capital resources

The Group manages its capital to ensure that entities within the Group will be able to continue to operate as going concerns, and to ensure that where a subsidiary is subject to regulatory capital requirements, that entity maintains an adequate capital surplus to ensure compliance with those requirements. The Group's capital consists of equity attributable to equity holders of the Parent Company. For the purposes of regulatory capital requirements, certain assets are restricted, or are inadmissible.

One subsidiary, Partnership Life Assurance Company Limited, is required to comply with minimum capital requirements calculated at the level of its EEA Parent Company level, as well as its own single entity level. It must also calculate its available capital at the ultimate Parent Company level, but as failure to cover the minimum capital requirement at this level has no consequence for the entity, or the Group, it is not a measure used to manage capital and hence is not disclosed in this note. The table below shows the available capital resources at the level of the EEA Parent Company as this is the number by which we assess the Group's capital adequacy. These capital requirements are determined in accordance with the PRA regulations and the EU directives, for insurance and other PRA regulated business. Any changes or release of capital from long-term funds is subject to there being an established surplus shown by an actuarial investigation.

As at 31 December	2013 £000's	2012 £000's
Total Equity of EEA parent company	**598,549**	457,703
Minority Interest in equity for regulated business	**(66)**	–
Adjustments in respect of regulatory capital basis:		
Inadmissible intangible assets	**(16,401)**	(12,343)
Inadmissible goodwill	**(126,207)**	(126,207)
Inadmissible deferred tax asset	**(424)**	(158)
Equity and reserves related to non-regulated entities (excluded from regulatory capital calculation), adjusted for inadmissible assets already adjusted above	**13,031**	9,157
Total available capital resources (regulatory basis)	**468,483**	328,152
Group minimum capital requirement (regulatory basis)	**(191,630)**	(163,213)
Surplus over regulatory capital requirement	**276,853**	164,939

Movements in equity are shown in the Consolidated Statement of Changes in Equity.

Throughout the year, each regulated subsidiary has maintained capital resources in excess of the minimum required by the PRA regulations and the EU directives.

13. Reorganisation

As part of the "Global Offer" and admission of the Company to the London Stock Exchange on the 12 June 2013, the Group has undertaken certain reorganisation steps as detailed below.

Immediately prior to admission on 12 June 2013:

- the A and B loan notes, previously issued by PAG Finance Limited ("PAGF"), a Group company, together with accrued but unpaid interest, were exchanged on a pound-for-pound basis for the allotment and issue of 69,212,294 ordinary shares in the Company which had a value of £266.5m;
- the C loan notes, previously issued by PAGH, together with accrued but unpaid interest, were exchanged on a pound-for-pound basis for the allotment and issue of 15,397,726 ordinary shares in the Company which had a value of £59.3m; and
- the A, B, and C ordinary shares in PAGH were exchanged for the allotment and issue of 282,358,446 ordinary shares in the Company. A merger reserve of £(24.5)m arose on consolidation as a result of this share exchange to maintain parity of the consolidated net assets of the Group before and after these share exchanges.

As a result of the above steps the company obtained control of PAGH and its subsidiaries. Also as a result of the above steps Cinven Funds, certain Directors, certain members of Senior Management and other individuals hold ordinary shares in each case in proportion to the value of the shareholder instruments in the Group held by them immediately prior to the reorganisation.

Pursuant to the Global Offer and following admission on 12 June 2013:

- the Company issued 32,467,532 new ordinary shares raising gross proceeds of £125.0m;
- £7.7m of these proceeds were used to repay in full the Vendor loan notes ("VLN"), together with accrued unpaid interest;
- the remainder of these proceeds were used in part to fund transaction costs, to repay the £70m external borrowing facility on 21 August 2013 and for general corporate purposes; and
- the Company also issued 51,948 new ordinary shares to certain of the independent non-executive Directors and 12,025 new ordinary shares to the employee benefit trust raising £246,000.

The transaction costs relating to the Global Offer in the six months period to 30 June 2013 amounted to £19.6m. £4.0m of these costs are directly associated with the issue of new shares and have therefore been set-off against the share premium associated with those shares. £3.8m of these costs have been paid during the period to 30 June 2013.

14. Share Capital

The Group has issued ordinary shares which are classified as equity. Incremental external costs that are directly attributable to the issue of the ordinary shares are recognised in equity, net of tax.

On 12 June 2013, immediately prior to admission on the London Stock Exchange, the Company acquired a 100% shareholding in PAGH, the top holding company of the Group at that point in time.

The allocated and issued share capital of PAGH and PAG plc, the top holding companies of the Group as at 31 December 2012 and 31 December 2013 respectively are detailed below:

At 31 December 2012	Share Capital £000's	Share Premium £000's
The authorised share capital of the Company is:		
'A" ordinary shares of £0.01 each	25	–
'B" ordinary shares of £0.01 each	3	–
'C" ordinary shares of £0.01 each	5	182
'D" ordinary shares of £1 each	3	–
Total	36	182

In the year to 31 December 2012,

- 2,834 ordinary D shares of PAGH of £1 each were issued at par for cash;
- the A, B and C ordinary shares of PAGH were converted into new A, B and C ordinary shares of £0.01 each and new deferred shares of £0.99 each;
- PAGH repurchased the deferred ('DEF') shares of £0.99 each, for a total consideration of £1; and
- a Capital Redemption Reserve of £3,296,860 was created on repurchase of the deferred shares.

As detailed in note 13, immediately prior to admission on 12 June 2013, all of the A, B and C ordinary shares in PAGH were transferred to the Company in exchange for the allotment and issue of ordinary shares in the Company of £0.10 each. This resulted in the creation of the Merger Reserve as a result of the Group electing to account for the acquisition of its 100% shareholding in PAGH as a group reconstruction as described under the UK GAAP accounting standard, Financial Reporting Standard 6, "Acquisitions and Mergers". In addition, the Capital Redemption Reserve was transferred to this Merger Reserve as part of the same transaction

As at 31 December 2013	**Number of shares**	**Share Capital £'000s**	**Share Premium £'000s**
The allotted and issued Share Capital of PAG plc:			
On incorporation, ordinary shares of £1.00 each	**50,000**	**50**	**–**
On 12 June 2013:			
Shares subdivided into 500,000 ordinary shares of £0.10 each	**450,000**	**–**	**–**
Exchange of the A and B loan notes	**69,212,294**	**6,921**	**259,547**
Exchange of C loan notes	**15,397,726**	**1,540**	**57,742**
Share for share exchange of A, B and C ordinary shares in PAGH			
for ordinary shares in PAG plc	**282,358,446**	**28,236**	**–**
New issue of shares as part of Global Offer	**32,467,532**	**3,247**	**121,752**
New ordinary shares issued to senior management	**51,948**	**5**	**195**
New ordinary shares issued to EBT	**12,025**	**1**	**45**
Share issue costs	**–**	**–**	**(4,032)**
As at 31 December 2013, ordinary shares of £0.10 each	**399,999,971**	**40,000**	**435,249**

The Company was incorporated on 26 February 2013 with an issued share capital of £50,000 divided into 50,000 ordinary shares of 100 pence each. On 12 June 2013, the 50,000 ordinary shares of 100 pence each were subdivided into 500,000 ordinary shares of 10 pence each. Immediately following the completion of the Global Offer, and as a result of a number of steps undertaken prior to admission described in note 13, the issued share capital of the Company was increased to £39,999,997, comprising 399,999,971 ordinary shares of 10 pence each, all of which will be fully paid or credited as fully paid.

The ordinary share entitles the holder to dividends declared by the Board which are not cumulative. The ordinary share entitles the holder to one vote for every share held.

Shares held by the employee trust

Where an employee trust acquires shares in the Company or obtains rights to purchase its shares, the consideration paid (including attributable transaction costs, net of tax) is shown as a deduction from the owners' equity. Gains and losses on sales of shares held by the employee trust are charged or credited to the own shares account in equity.

As at 31 December	**2013 £000's**	2012 £000's
Employee benefit trust	**(58)**	(33)

Prior to the Global Offer, the PAGH Employee Benefit trust ("PAGH trust"), which was established in 2008, and is a discretionary employee benefit trust, held shares to satisfy awards granted to employees of the Group.

As part of the Group restructuring prior to the Global Offer, the shares in PAGH held by the EBT were exchanged for £283,000 of ordinary shares in PAG plc. Following the admission of the Group onto the London Stock Exchange via a Premium Listing, £271,000 of these shares were sold to fund the vesting of the options under the Group's previous Employee Share Option Plan with the remainder of the shares transferred to a new employee benefit trust.

In addition, during the year, £46,000 of new shares were issued by the Company to the new employee benefit trust. The number of shares held by the new employee trust as at 31 December 2013 was 136,884 (31 December 2012: PAGH trust: 33,000).

15. 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

Prior to the Group reorganisation in 2013 and as described in note 13, the Fourth Cinven Fund was the ultimate shareholder of the Group.

The Group issued a number of loan notes to the Fourth Cinven Fund. These included the A, B and C loan notes. Details of these loan notes are described in note 13 above and the outstanding balances at the end of each reporting period are disclosed in the table below:

As at 31 December	**2013 £000's**	2012 £000's
A and B Loan notes	**–**	232,702
C Loan notes	**–**	53,978
Total	**–**	286,680

During the year, as described in note 13 above, the A, B and C loan were transferred on a pound-for-pound basis to the Company in exchange for the allotment and issue of ordinary shares in the Company.

The amounts accruing to the Fourth Cinven Funds in respect of these loan notes are detailed below:

As at 31 December	**2013 £000's**	2012 £000's
Interest accrued on loan notes	**18,629**	29,640
Monitoring fee payments	**216**	450
Total	**18,845**	30,090

The monitoring fee payments up to February 2013 include fees for two of the Group's non-executive directors who are also employees of Cinven Capital Management.

In addition, as part of the IPO, ordinary shares in the Company were issued to Cinven and Directors as explained in note 13.

b) Remuneration of key management personnel

Key management personnel consist of the directors of the Company. The key management personnel changed during the year 2013 reflecting the Group reorganisation. The remuneration of the directors, who are the key management personnel of the Group, is set out below:

As at 31 December	**2013 £000's**	2012 £000's
Short-term employee benefits	**2,060**	2,129
Post-employment benefits	**55**	114
Share based payments		
Total	**2,115**	2,243

c) Directors' loans

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

As at 31 December	2013 £000's	2012 £000's
Amounts owed to directors:		
B loan notes	–	12,216
Vendor loan notes	–	878
Total	–	13,094
Amounts owed by directors:		
Loan advances	**289**	378
Total	**289**	378

The terms of the B and Vendor loan notes are detailed in note 13, and, as set out in that note, the loan notes were exchanged for ordinary shares in the Company as part of the IPO.

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

The amounts accruing to/from the directors in respect of these loan notes are detailed below:

As at 31 December	2013 £000's	2012 £000's
Interest accrued on B and Vendor loan notes	**663**	1,421
Interest accrued on Directors' loan advances	**6**	–
Total	**669**	1,421

d) Other related party transactions

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

As at 31 December	2013 £000's	2012 £000's
Transaction expense (services received)	**558**	–
Total	**558**	–

e) Ultimate controlling party

As at 31 December 2013 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 adviser to the Cinven Funds.

16. Events after the balance sheet date

Dividend

Subsequent to 31 December 2013, the directors proposed a final dividend for 2013 of 3.0 pence per ordinary share (2012: nil), amounting to £12.0m (2012: nil) in total. Subject to approval by shareholders at the AGM, the dividend will be paid on 30 May 2014 and will be accounted for as an appropriation of retained earnings in the year ending 31 December 2014.

Group MCEV analysis of earnings (net of tax)

For the year ended 31 December 2013

			2013		2012
	Note	**Covered business MCEV £000's**	**Non covered business MCEV £000's**	Total MCEV £000's	Total MCEV £000's
Opening Group MCEV		**383,600**	**(373,710)**	9,890	(58,554)
Opening adjustments		**–**	**–**	–	–
Adjusted opening Group MCEV		**383,600**	**(373,710)**	9,890	(58,554)
Operating MCEV earnings	3	**107,236**	**–**	107,236	120,433
Non-operating MCEV earnings	3	**(2,342)**	**(51,883)**	(54,225)	(40,562)
Total MCEV earnings		**104,894**	**(51,883)**	53,011	79,871
Other movements in IFRS net equity	4	**–**	**481,732**	481,732	–
Closing adjustments	3	**(25,000)**	**–**	(25,000)	(11,427)
Closing Group MCEV		**463,494**	**56,139**	519,633	9,890

Covered business analysis of movement in embedded value (net of tax)

For the year ended 31 December 2013

	Note	VIF £000's	Required capital £000's	Free surplus £000's	2013 MCEV £000's	2012 MCEV £000's
Opening MCEV		**56,814**	**287,078**	**39,708**	383,600	166,273
Opening adjustments		**–**	**–**	**–**	–	–
Adjusted opening MCEV		**56,814**	**287,078**	**39,708**	383,600	166,273
New business value	3	**10,428**	**104,055**	**(33,389)**	81,094	94,800
Expected existing business contribution (reference rate)	3	**2,800**	**–**	**–**	2,800	3,504
Transfers from VIF and required capital to free surplus		**(5,902)**	**(16,183)**	**27,311**	5,226	2,306
Experience variances	3	**(343)**	**389**	**(347)**	(301)	(178)
Assumption changes	3	**(9,631)**	**(11,544)**	**30,974**	9,799	(599)
Other operating variances	3	**1,269**	**(16,200)**	**23,549**	8,618	20,570
Operating MCEV earnings		**(1,379)**	**60,517**	**48,098**	107,236	120,403
Economic variances	3	**(5,373)**	**6,735**	**372**	1,734	(4,551)
Other non-operating variances	3	**262**	**–**	**(4,338)**	(4,076)	784
Total MCEV earnings		**(6,490)**	**67,252**	**44,132**	104,894	116,636
Closing adjustments	3	**–**	**–**	**(25,000)**	(25,000)	100,691
Closing MCEV		**50,324**	**354,330**	**58,840**	463,494	383,600

Reconciliation of Group IFRS net assets to MCEV

As at 31 December 2013

	2013			2012		
	Covered Business Adjusted Net Worth £000's	**Non Covered Business Adjusted Net Worth £000's**	**Group £000's**	Covered Business Adjusted Net Worth £000's	Non Covered Business Adjusted Net Worth £000's	Group £000's
Group Net Assets as reported under IFRS	**415,501**	**183,114**	**598,615**	329,118	(246,735)	82,383
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)
MCEV Net Worth	**413,169**	**56,139**	**469,308**	326,786	(373,710)	(46,924)
VIF	**50,325**	**–**	**50,325**	56,814	–	56,814
MCEV (net of taxation)	**463,494**	**56,139**	**519,633**	383,600	(373,710)	9,890

Notes to the MCEV financial statements

For the period ended 31 December 2013

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 6 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 value of external debt, at the outstanding face value, within the net worth of Group companies outside of PLACL. The Group does not make use of any financial reinsurance.

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 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 no negative equity guarantee. The time value of this option and guarantee is allowed for in the asset valuation using closed form calculations.

c) 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.

d) 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. The unwind of new business from point of sale to the valuation date is included as part of the expected existing business contribution. 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
31 December 2013	**180 bps**
31 December 2012	217 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
31 December 2013	**216 bps**
31 December 2012	270 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 each period end. These rates have been supplied by PLACL's investment manager.

							Swap curves
	6 months	1 year	2 years	5 years	10 years	15 years	20 years
31 December 2013	**0.71%**	**0.71%**	**1.03%**	**2.17%**	**3.10%**	**3.47%**	**3.57%**
31 December 2012	0.67%	0.67%	0.71%	1.02%	1.92%	2.57%	2.57%

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.

Exceptional 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 amounted to £5.2m for the year to 31 December 2013 (31 December 2012: £2.4m in relation to Solvency II).

Best estimate expense inflation as at 31 December 2013 was 4.8% p.a. (31 December 2012: 4.3%)

Taxation

The current and future tax rates are those corporation tax rates as published by HM Treasury and take into account both taxes enacted by legislation and those disclosed in budget announcements. Tax losses in Group companies, resulting mainly from accrued interest on debt, are fully relieved to PLACL resulting in a reduction in the effective tax rate. The effective tax rate for the year to 31 December 2013 was 17.1% (31 December 2012: 16.2%).

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

The corporation tax rates used were as follows:

	Blended corporation tax rate	
	2013	2012
2011	**26.50%**	26.50%
2012	**24.50%**	24.50%
2013	**23.25%**	23.25%
2014	**21.50%**	21.50%
2015	**20.25%**	21.00%
2016+	**20.00%**	21.00%

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 on equity release assets. As at 31 December 2013 the assumption was set to 12% (31 December 2012: 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 1.2% (31 December 2012: 1.2%) has been applied to the non-hedgeable capital required for a 1-in-200 year basis 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 185% of the capital resources requirement (31 December 2012: 176%). 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 0.8% as at 31 December 2013 (31 December 2012: 1.1%).

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

Covered business

The key driver of MCEV earnings was the value of new business written over the period.

The decrease in the New business value in 2013 is due to lower volumes of new business and higher expenses.

The total expected existing business contribution and transfers from VIF and required capital to free surplus has increased in the period as a result of continued growth in the portfolio. There has been a refinement in the allocation of the unwind of FCoRC between the two lines.

Experience variances in the period are negligible in aggregate and there were no significant individual components.

The changes in assumptions include an expense assumption profit due to a reduction in per policy expenses, partially offset by mortality assumption changes.

Other operating variances largely consist of expected long-term return on excess assets.

The small economic variance is immaterial in the context of the investment portfolio.

Non-operating variance in free surplus consists of exceptional expenses in respect of the Group's expenditure on regulatory projects, such as the necessary system and process developments required to comply with the proposed Solvency II capital regime. The VIF impact represents benefit of the reduction of corporation tax changes to 20% effective from 1 April 2015.

On 13 December 2013 Partnership Life Assurance Company Limited declared and paid a dividend to Partnership Group Holdings Limited (PAGHL) of £25 million.

Non-covered business

The non-operating MCEV loss principally comprises transaction costs relating to the IPO and Global Offer and interest payable on loan notes and bank borrowings.

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

The other movements in IFRS net equity are predominantly as a direct result of the “Global Offer”, the admission of the Company to the London Stock Exchange on 12 June 2013 and certain internal reorganisation steps undertaken in the lead up to these transactions. These have resulted in an increase in the net worth of £455.5m.

Immediately prior to admission on 12 June 2013:

- the A and B loan notes, previously held by PAG Finance Limited (“PAGF”), a Group company, together with accrued but unpaid interest, were exchanged on a pound-for-pound basis for the allotment and issue of 69,212,294 ordinary shares in the Company resulting in an increase of net worth of £266.5m; and
- the C loan notes, previously held by PAGH, together with accrued but unpaid interest, were exchanged on a pound-for-pound basis for the allotment and issue of 15,397,726 ordinary shares in the Company resulting in an increase in net worth of £59.3m.

Pursuant to the Global Offer and following admission on 12 June 2013:

- the Company issued 32,467,532 new ordinary shares raising £125.0m; and
- the Company issued 51,948 new ordinary shares to senior management and 12,025 new ordinary shares to the employee benefit trust raising £246,000.

£4.0m of transactions costs relating to the Global Offer in the year to 31 December 2013 are directly associated with the issue of new shares and have therefore been set off against share premium associated with those shares resulting in a reduction in net worth by that amount. In addition, following admission on the London Stock Exchange, the awards under the ESOP vested in full and were exercised immediately. This resulted in an increase in net worth of £8.5m as a result the utilisation of the share-based payment reserves.

5. Covered business analysis of movement in gross of tax embedded value

Covered business is the PLACL legal entity which holds all the long-term insurance business within the Group. The analysis of movement for covered business is shown in the table below. All earnings are shown on a gross of tax basis with attributed tax shown separately.

				2013		2012
For the year ended 31 December	Note	**VIF £000's**	**Required capital £000's**	**Free surplus £000's**	MCEV £000's	MCEV £000's
Opening MCEV (net of tax)		**56,814**	**287,078**	**39,708**	383,600	166,273
Tax adjustments		**21,711**	**–**	**–**	21,711	15,451
Adjusted opening MCEV (gross of tax)		**78,525**	**287,078**	**39,708**	405,311	181,724
New business value		**15,198**	**104,055**	**(18,796)**	100,457	116,657
Expected existing business contribution (reference rate)		**3,774**	**–**	**–**	3,774	4,504
Transfers from VIF and required capital to free surplus		**(7,707)**	**(16,183)**	**29,609**	5,719	2,741
Experience variances		**(403)**	**389**	**(338)**	(352)	(278)
Assumption changes		**(12,361)**	**(11,544)**	**34,986**	11,081	(927)
Other operating variances		**1,064**	**(16,201)**	**25,066**	9,929	24,453
Operating MCEV earnings		**(435)**	**60,516**	**70,527**	130,608	147,150
Economic variances		**(6,036)**	**6,736**	**1,838**	2,538	(4,250)
Other non-operating variances		**–**	**–**	**(5,233)**	(5,233)	(2,914)
Total MCEV earnings		**(6,471)**	**67,252**	**67,132**	127,913	139,986
Closing adjustments		**–**	**–**	**(25,000)**	(25,000)	100,691
Closing MCEV before tax		**72,054**	**354,330**	**81,840**	508,224	422,401
Tax		**(21,730)**	**–**	**(23,000)**	(44,730)	(38,801)
Closing MCEV after tax		**50,324**	**354,330**	**58,840**	463,494	383,600

6. 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**	
2013 Sensitivity	**Impact on MCEV £000's**	**Change in MCEV %**	**Impact on MCEV £000's**	**Change in MCEV %**
Embedded Value (Base)	**463,494**		**81,094**	
Interest rate environment +100 bps	**760**	**0%**	**n/a**	**n/a**
Interest rate environment -100 bps	**(4,802)**	**–1%**	**n/a**	**n/a**
Swaption implied volatilities + 25%	**n/a**	**n/a**	**n/a**	**n/a**
Property volatilities +25%	**(23,601)**	**–5%**	**(4,100)**	**–5%**
Property Values -10%	**(17,364)**	**–4%**	**n/a**	**n/a**
Lapses -10% (including equity release)	**1,861**	**0%**	**n/a**	**n/a**
Mortality -5% (annuities)	**(16,892)**	**–4%**	**(3,179)**	**–4%**
Expenses -10%	**5,842**	**1%**	**1,322**	**2%**
Mortality improvements +0.25%	**(7,149)**	**–2%**	**(1,986)**	**–2%**
Decrease in liquidity premium 25 bps	**(60,529)**	**–13%**	**(17,363)**	**–22%**
Required capital set to be 100% of CRR	**16,813**	**4%**	**6,466**	**8%**

	In force		New business	
2012 Sensitivity	Impact on MCEV £000's	Change in MCEV %	Impact on MCEV £000's	Change in MCEV %
Embedded Value (Base)	383,600		94,800	
Interest rate environment +100 bps	(7,287)	–2%	n/a	n/a
Interest rate environment -100 bps	7,091	2%	n/a	n/a
Swaption implied volatilities + 25%	n/a	n/a	n/a	n/a
Property volatilities +25%	(14,469)	–4%	(4,200)	–4%
Property Values -10%	(8,241)	–2%	n/a	n/a
Lapses -10% (including equity release)	2,026	1%	n/a	n/a
Mortality -5% (annuities)	(11,419)	–3%	(3,043)	–3%
Expenses -10%	5,629	1%	1,190	1%
Mortality improvements +0.25%	(5,121)	–1%	(1,685)	–2%
Decrease in liquidity premium 25 bps	(47,649)	–12%	(16,113)	–17%
Required capital set to be 100% of CRR	12,755	3%	3,190	3%

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 90% * 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. This equates to an increase in best-estimate credit defaults of 34bps per annum for corporate bond holdings.
- The required capital sensitivity is modelled by reducing capital from 186% to 100% of the capital resource requirement. This has no impact on net worth and reduces 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.