M&G Group

Pillar 3 Disclosures

As at 31 December 2017

Contents

Glossary – Abbreviations

AUM	Assets Under Management
BIPRU	Prudential Sourcebook for Banks, Building Societies and Investment Firms
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CRD	Capital Requirements Directive
CRM	Credit Risk Mitigation
CRO	Chief Risk Officer
DAC	Deferred Acquisition Costs
DB	Defined Benefit (Pension Scheme)
DIR	Deferred Initial Revenue
ECAIs	External Credit Assessment Institutions
FCA	Financial Conduct Authority
FOR	Fixed Overhead Requirement
FX	Foreign Exchange
GENPRU	General Prudential Sourcebook
GRC	M&G Group Risk Committee
GwIA	Group-wide Internal Audit
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IRB	Internal ratings-based approach
KI	Key Indicator
LTIP	Long-term incentive plan
M&G	M&G Group Ltd, along with its direct and indirect subsidiaries
M&GP	M&G Prudential
MAGAIM	M&G Alternatives Investment Management Ltd
MAGIM	M&G Investment Management Ltd
MGII	M&G International Investments Ltd
MGSL	M&G Securities Limited
OEIC	Open Ended Investment Company
PRA	Prudential Regulation Authority
PRR	Position Risk Requirement
RAS	Risk Appetite Statement
RCSA	Risk and Control Self-assessment
S&P	Standard and Poor's
SYSC	Senior Management Arrangements, Systems and Controls
SREP	Supervisory Review and Evaluation Process
ToR	Terms of Reference
TSR	Total Shareholder Return
UT	Unit Trust

1. Overview

1.1. Introduction

This document sets out the M&G Group Pillar 3 disclosures on risk management and capital adequacy as at 31 December 2017.

M&G Group Limited, along with its direct and indirect subsidiaries, form the M&G Group ("M&G").

M&G is regulated by the Financial Conduct Authority ("FCA"). It is subject to rules set out in the FCA's General Prudential Sourcebook ("GENPRU") and Prudential Sourcebook for Banks, Building Societies and Investment Firms ("BIPRU"). This disclosure is prepared in accordance with the Capital Requirements Directive ("CRD") III.

The capital requirements framework consists of three Pillars:

- Pillar 1: Sets out minimum capital requirements;
- Pillar 2: Sets out the process for assessing capital adequacy in relation to a firm's actual risk profile and for determining whether additional capital is required to cover these risks. This is achieved through the Internal Capital Adequacy Assessment Process ("ICAAP") undertaken by M&G and the Supervisory Review and Evaluation Process ("SREP") performed by the FCA; and
- Pillar 3: Requires public disclosure of a firm's risks, risk management and capital.

1.2. M&G overview

M&G is an asset management firm with more than 90 years of experience investing on behalf of individuals and institutions. M&G's aim is to help its customers prosper by putting their investments to work through the active and careful allocation of capital. In doing so, M&G has a conviction-led, long-term approach to asset management applied across the full range of asset types: cash, equities, bonds, real estate and alternatives. M&G offers products across diverse geographies, asset classes and investment strategies aimed at delivering value for clients through the generation of long-term capital growth and / or income.

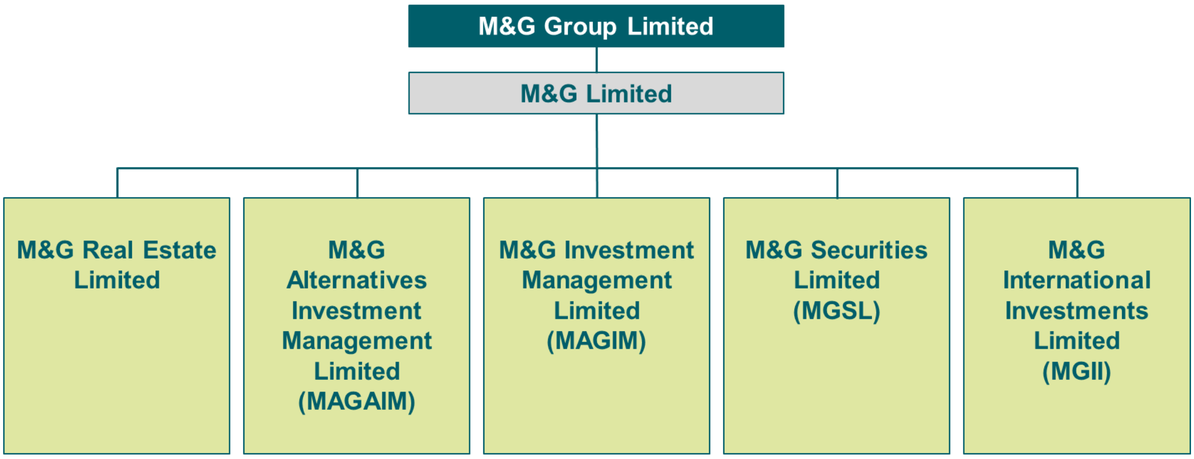
M&G is a 100% owned subsidiary of Prudential plc, a Prudential Regulation Authority ("PRA") regulated group with shares listed on the London, Hong Kong, Singapore & New York Stock Exchanges and an external credit rating of A, A2, A- (long-term senior – Standard and Poor's ("S&P"), Moody's, Fitch) as at 28 June 2018.

In August 2017, the formation of M&G Prudential ("M&GP") was announced through the combination of M&G and Prudential plc's UK and European insurance and savings business. On 14 March 2018, Prudential plc announced its intention to demerge M&GP and to float it as an independent firm on the London Stock Exchange in the belief that this will strengthen both businesses and enhance value to shareholders and customers.

1.3. Scope

The Pillar 3 disclosures relate to M&G, which is subject to supervision by the FCA on a consolidated basis. An overview of M&G's main trading statutory entities and the material UK regulated entities included in the scope of the consolidation are shown in Figure 1.1.

Figure 1.1: M&G's main trading entities (as at 31 December 2017)



M&G Group Limited, M&G Limited and M&G Real Estate Limited do not undertake any regulated investment activity.

1.4. Accounting consolidation

The basis of consolidation for the purpose of statutory financial accounting under International Financial Reporting Standards ("IFRS") is described in the annual financial statements. It is based on the inclusion of all entities controlled by M&G at 31 December each year.

1.5. Prudential consolidation

M&G used the same basis for its prudential and accounting consolidations.

Treatment of significant investments in the prudential consolidation

Significant investments are deducted from regulatory capital resources under the heading material holdings. Material holdings are an associate and insurance related entity investment, refer Table 1.2 below.

Table 1.2: Entitles deducted in calculating capital resources

Entity	Treatment in accounting consolidation
Prudential Portfolio Managers (South Africa) (Pty) Limited	Investment in associate
Furnival Insurance Company PCC Limited	Available-for-sale financial asset

A reconciliation of regulatory capital resource items to the balance sheet in the audited financial statements as at 31 December 2017 is disclosed in Section 6 Appendix I. The reconciliation identifies items that are components of, or are deducted from, capital resources.

There is no current or foreseen material, practical or legal impediment to the prompt transfer of capital resources or repayment of liabilities among the parent undertaking and its subsidiaries.

1.6. Materiality

As per the BIPRU rules, an entity may omit one or more of the required disclosures if it believes that the information is immaterial. A disclosure is deemed to be material if the omission or misstatement of that information would be likely to change or influence the assessment or decision of a user relying on that information for the purposes of making economic decisions. Where a disclosure is considered to be immaterial, this has been noted.

1.7. Frequency

M&G has an accounting reference date of 31 December and disclosures are published annually in conjunction with the date of publication of the M&G Group Limited financial statements. However, disclosures may be published more frequently in light of any material changes.

1.8. Location and verification

These disclosures have been approved by the M&G Group Limited Board ("the Board"). These disclosures are not subject to audit and have been produced solely for the purposes of satisfying the Pillar 3 regulatory requirements.

The disclosures are made available on the M&G corporate website.

2. Risk management

M&G is exposed to strategic, financial, business environment and operational risks and these are defined in Section 2.2. M&G's risk management governance and processes are defined in the M&G risk framework document and supporting risk policies. M&G's risk appetite is set out in the M&G Risk Appetite Statement ("RAS"), which is approved by the Board. M&G monitors its risk profile against risk appetite and reports are provided to the Board and to relevant governance bodies on a regular basis.

2.1. Risk management objective

The key risk objective for the Board is to facilitate continued controlled growth, within agreed risk appetite, that will meet the requirements of M&G's customers, shareholder and regulators. In order to achieve this M&G:

- Identifies the significant risks that it faces by pursuing its business plan;
- Articulates a risk appetite statement for each category of material risk;
- Establishes formal processes to manage risks in the context of M&G's risk appetite;
- Regularly re-assesses the capital requirements and liquidity impacts implied by these risk exposures; and
- Ensures a robust risk governance structure and risk culture is maintained.

2.2. Identification of significant risks

M&G is exposed to a number of risks. Some are industry-wide and inherent in running an investment management business; others are idiosyncratic and unique to M&G and result from the strategy, size and structure of the business.

M&G's categorisation of its material business risks is aligned with Prudential plc's risk categorisation framework. The high-level risk categories are as follows:

- **Strategic risk:** the risk that M&G is unable to generate profitable medium-term growth as a result of inadequate execution of strategy.
- **Financial risk:** the risk that M&G is unable to maintain adequate capital and liquidity to meet its customers' and stakeholders' requirements.
- **Business environment risk:** the risk that M&G is unable to generate profitable medium-term growth as a result of Prudential plc's and M&G's business structure or M&G's exposure to the external environment.
- **Operational risk**: the risk of loss or unintended gain arising from inadequate or failed internal processes and systems, from failures by personnel or from external events.

The high-level risks are driven by a number of underlying risks. M&G's assessment of its risk profile highlights that most of M&G's significant risk exposures are operational in nature. This is also reflected in M&G's capital assessment with operational risk being the most significant risk for M&G under Pillar 2.

The operational risk categories for M&G are set out in Table 2.1.

Table 2.1: List of operational risks categories

List of M&G's operational risks categories	
• People management and culture	• Business continuity
• Financial crime	• Regulatory and legislative compliance
• Operations processes	• Social, environmental, brand and external communications
• Finance processes	• Risk management / controls
• IT information and cyber security	• Change management and strategy
• Outsourcing and third-party management	

Client interests are central to M&G's business model. Therefore, M&G's approach to conduct, culture and treating customers fairly is considered throughout its RAS.

Conduct risk

M&G defines conduct risk as the risk that the acts or omissions of the firm, or individuals within the firm, deliver poor or unfair outcomes for customers or affect market integrity. Managing conduct risk is a key focus of the business and M&G has low appetite for outcomes resulting from poor conduct.

Following a high-level assessment of M&G readiness to answer the 5 FCA conduct questions, M&G

implemented a number of initiatives to further develop its conduct risk framework. M&G's conduct risk framework demonstrates how M&G drives conduct using a top down and bottom up process.

2.3. Risk appetite

Risk appetite is defined as the type and level of risk that M&G is willing to accept to achieve its strategic goals as referred to in its RAS.

M&G's risk appetite statement

There is a statement for each risk category that directionally outlines whether M&G has "high"; "low" or "no" risk appetite. Some statements also include quantitative thresholds where required / appropriate.

M&G's risk appetite key indicators

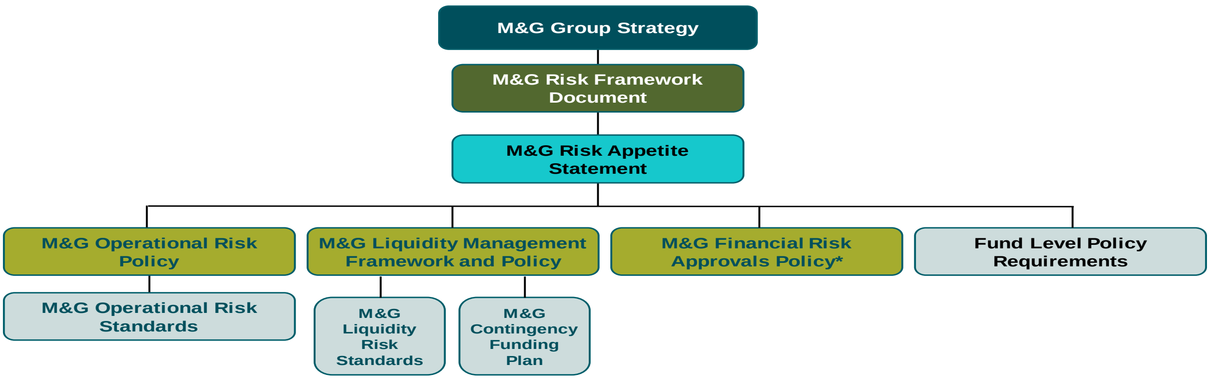
M&G's KIs measure whether M&G is inside or outside of appetite for each RAS and act as a prompt for senior management to discuss whether management action is required to reduce risk exposures.

2.4. Strategies and processes to manage risks

Risk policies for each separate category of risk

Prudential plc, and where appropriate, M&G policies are in place and cover each category of risk. Where necessary, these policies are supported by standards (refer Figure 2.1).

Figure 2.1 – M&G's risk policies and standards



* Covers strategic and corporate financial risk exposures such as credit and market risk.

Strategic risk management

M&G's key strategic risks are in relation to profit volatility, investment performance and revenue concentration. M&G has established KIs and associated threshold limits for each of these risks and re-evaluates these limits on an annual basis in the context of M&G's business strategy and risk appetite. A trigger of one of these limits would result in discussion by established governance forums over potential management action.

Financial risk management

M&G is exposed to capital, liquidity, pension, securitisation, credit and market risk.

- Capital and liquidity - M&G expects to hold sufficient capital and liquidity to ensure the continuity of its business under normal and stressed conditions. Senior management review details of regulated entities' capital adequacy on a monthly basis and performs stress and scenario testing at least annually (refer section 2.5 for further details).

- Pension - M&G has established monitoring arrangements in place to identify and report on Defined Benefit ("DB") scheme obligations.
- Securitisation - M&G has not invested in securitisations post-crisis (2008) on-balance sheet and there are currently no plans to use balance sheet for either investment or originating securitisations.
- Credit and market - In addition to its Pillar 1 calculations of credit and market risk (refer section 4) M&G has internal processes to measure these risk exposures against risk appetite.
- Processes for hedging and mitigating risks - To protect the solvency of M&G, the Board is reluctant to take market risk on to the balance sheet. Therefore, M&G's appetite is to restrict the balance sheet exposure to a limited set of activities. These activities are managed in line with M&G's RAS and risk policies and standards. M&G has low appetite for foreign exchange ("FX") exposures arising from its seed investments and M&G may seek to hedge these exposures.

Business environment risk management

M&G is exposed to regulatory relationship; legal; and group risk.

- Regulatory relationship - It is the responsibility of all staff to ensure M&G remains regulatory compliant. M&G has in place a suitably resourced Compliance function, which assists the business to ensure ongoing compliance with new and existing regulations.
- Legal - M&G requires all of its agreements with third parties are properly documented with legal advice taken internally or, where appropriate, from one of the law firms on M&G's approved panel by an authorised individual.
- Group - As M&G is a member of Prudential plc, an event occurring at Prudential plc level could impact M&G. M&G includes consideration of group risk in its stress and scenario testing as part of the ICAAP.

Operational risk management

All areas of M&G are exposed to operational risk through their day-to-day operations. Any control absence or failure associated with processes, people, systems or any external events can result in direct or indirect financial and non-financial consequences to M&G.

In order to support the management of operational risks, the Board has established processes, proportionate to the nature, scale and complexity of its operations. These include but are not necessarily limited to:

- Regular cycle of review of risk policies and standards;
- Regular cycle of risk appetite setting and KIs monitoring and reporting;

- Risk and Control Self-assessments ("RCSA");
- Management, reporting and review of operational incidents, including impact assessment of relevant external incidents; and
- Operational Risk Scenario Analysis to assess capital requirements of high impact, low likelihood operational events.

Risk reporting and measurement systems

Risk reporting requirements are set out in the M&G risk policies as separate documents.

The M&G Boards and risk committee each have approved Terms of Reference ("ToR") which support clear segregation of roles and responsibilities with respect to risk reporting. The ToR are reviewed and updated annually or more frequently if there are changes to roles and responsibilities or membership.

A number of key ratios and metrics are reviewed by M&G Risk to monitor risk exposures on an ongoing basis. Regular reports of risk exposure relative to risk appetite and other risk management information are provided to business divisions and M&G's management bodies.

2.5. Assessment of capital requirements and liquidity impacts

M&G continually assesses its capital and liquidity adequacy relative to its current and future risk profile under normal and severe conditions. M&G recalculates its current and forecast capital adequacy position on a monthly, quarterly and annual basis in response to movements, actual or projected, in its balance sheet assets.

2.6. Risk governance

Risk governance is used to describe the organisational structure, delegation of authority, and roles and responsibilities that M&G and the business divisions establish to make decisions and manage their activities.

M&G's risk governance is based on the three lines of defence model, in which risk management, risk oversight and independent assurance are distinct activities that are carried out by different individuals, committees and departments for any particular risk. The key roles and responsibilities are illustrated by Figure 2.2.

Figure 2.2 – Risk responsibilities across the three lines of defence as at 31 December 2017

	M&G Group Limited Board		
	First Line	Second Line	Third Line
Activity	Risk management	Risk oversight	Assurance
Responsible Committee	Executive Committees*	M&G Group Risk Committee M&G Risk & Compliance Committee M&G Investment Performance & Risk Committee M&G Corporate Capital & Liquidity Sub-Committee / other Sub-Committees**	M&G Audit Committee
Responsible Personnel	Business division heads Senior management All M&G personnel	M&G Chief Risk Officer M&G Risk M&G Compliance Director M&G Compliance	Group-wide Internal Audit

*Executive Committee, Product Management Committee, Marketing & Distribution Committee, Dealing Management Committee and Operations & Technology Committee
**CASS Sub-Committee, Employee Sub-Committee, Valuations Sub-Committee and Liquidity Management Sub-Committee

The three lines of defence are described as follows:

Risk management (First Line)

- Identifying risks that could threaten the achievement of business objectives;
- Assessing and managing these risks in line with M&G's policies, standards and risk appetite;
- Ensuring business processes have in place appropriate controls that remain effective;
- Identifying and promptly escalating significant emerging risk issues; and
- Reporting operational incidents in line with the operational risk standards.

Business division heads and senior managers have primary accountability for business risk management.

Oversight and challenge (Second Line)

- Assisting the Board with the formulation and subsequent communication of M&G’s risk appetite, risk policies and limits;
- Overseeing and objectively challenging the identification, measurement, management, monitoring and reporting of risks;
- Providing independent validation of management’s risk and control assessments, and assessing the design and operational effectiveness of controls;
- Analysing risk information and producing risk reports for relevant risk committees; and
- Supporting the implementation of M&G's risk policies, standards and risk appetite.

The Chief Risk Officer ("CRO") has primary accountability for risk oversight, with support from risk committees and risk teams.

Independent assurance (Third Line)

This comprises the provision of independent assurance on the design and effectiveness of the overall system of internal control, including risk oversight and compliance. Independent assurance is provided by Group-wide internal audit ("GwIA") and via external audits, as required.

Governance as at 31 December 2017

The responsibilities of the Board include oversight of M&G business strategy, structure, capital and financial reporting.

Oversight of the governance

Oversight of the governance of M&G is undertaken by the Nomination & Governance Committee of the Board of Prudential plc, comprised of its Chairman, its Senior Independent Director, and the Chairs of each of its Audit, Risk and Remuneration committees. The Nomination & Governance Committee has set out processes for the selection of independent members and processes for the annual evaluation of the effectiveness of the Board. As part of its responsibility for appointing independent members to the Board, Prudential plc's Nomination & Governance Committee takes into account the Prudential's diversity and inclusion policy as referenced in the Prudential's Material Subsidiary Corporate Governance Manual which governs the operation of the Board.

2.7. Equal opportunity / diversity

M&G recognises, respects and values difference and diversity. Its equal opportunities and diversity policy promotes equal opportunity for all employees or potential employees and ensures that M&G attracts, retains and develops the best available talent. M&G values the benefits of different skills, experience, backgrounds and perspectives and harness these things to create a better business and lead to a stronger investment performance, as well as building a workplace where everyone can achieve their potential.

3. Capital resources

3.1. Capital resources

M&G's capital resources are primarily constituted of share capital and retained earnings and therefore are considered to be a high quality of capital resource, referred to as Tier 1 capital.

Tier 2 capital for M&G comprises of the fair value revaluation reserve, which arises from investments held in the available-for-sale financial asset category.

Deductions in arriving at capital resources as at 31 December 2017 consist of intangible assets, DB fund asset, deferred acquisition cost ("DAC"), deferred initial revenue ("DIR") and material holdings.

Table 3.1: M&G Group Capital Resources as at 31 December 2017

Capital resources	31 December 2017 £ millions
Share capital (A)	0.1
Retained earnings (B)	691
Other reserves (C)	(19)
Deductions from share capital and reserves:	
Deferred acquisition costs (DACs/DIRs) (net of associated deferred tax)	(7)
Defined benefit asset (net of associated deferred tax)	(91)
Less intangible assets	
Intangible assets	0
Core tier 1 capital	**574**
Tier 2 - revaluation reserves (D)	8
Deductions from total of tiers 1 and 2 capital:	
Material holdings	(46)
Total tier 1 plus tier 2 capital after deductions	**537**

Note: Numbers in all tables have been rounded so do not always sum.

M&G's eligible share capital and reserves reconcile to the equity of M&G disclosed in the Annual Report as shown in Table 3.2 below. Capital and reserves are considered eligible after they have been verified by external auditors.

Table 3.2: Reconciliation of eligible capital and reserves to equity as at 31 December 2017

Reconciliation of eligible capital and reserves to equity	31 December 2017 £ millions
Eligible share capital and reserves *(Table 3.1 - A+B+C+D)*	680
Add unverified profits and gains in the period	72
Capital and reserves	**752**

4. Capital adequacy

4.1. Calculation of capital requirements

M&G's capital requirement is calculated as the higher of the Pillar 1 capital requirement (as per table 4.1 below) and the Pillar 2 capital requirement. The Pillar 2 requirement is M&G's own assessment of the minimum amount of capital deemed adequate to be held against the identified risks.

The Pillar 1 capital requirement for regulatory reporting is the higher of:

- The Fixed Overhead Requirement ("FOR"); and
- The sum of the credit and market risk requirements.

Table 4.1: Pillar 1 capital requirement as at 31 December 2017

Pillar 1 capital requirement	31 December 2017 £ millions
(A) Credit risk	80
(B) Market risk	15
(C) Sum of (A) & (B)	95
(D) Fixed Overhead Requirement (FOR)	119
Pillar 1 capital requirement - higher of (C) & (D)	119

As at 31 December 2017, the capital requirement for M&G under Pillar 1 was the FOR.

4.2. Pillar 1 assessment[1]

FOR

The deductions in the calculation of FOR under CRD IV are more restrictive than under CRD III. Whereas under CRD III (GENPRU rules) 'other variable expenditure' is an allowable deduction, the CRD IV tightens this definition allowing only the deduction of specific items or 'non-recurring expenses from non-ordinary activities'. Following the transition back to CRD III, M&G has not revised the deductions around variable expenditure and has continued to calculate FOR in line with the stricter deduction rules for prudence and consistency within the M&G regulatory group.

Credit risk[2]

M&G has adopted the standardised approach for credit risk for calculating the minimum credit risk requirement under Pillar 1 of CRD III.

Credit risk is the exposure to loss arising from a counterparty's failure to meet its contractual obligations, either as a result of business failure or intentional withholding of amounts due. An exposure is classified as impaired when the carrying value exceeds the amount expected to be recovered through use or sale. M&G assesses its financial assets for indication of impairment on an on-going basis.

The External Credit Assessment Institutions ("ECAIs") used by M&G are Fitch, Moody's and S&P. These

[1] M&G does not use the internal ratings-based ("IRB") and the credit risk mitigation ("CRM") for the calculation of the Pillar 1 capital requirement.
[2] M&G does not make any value adjustments in its credit risk Pillar 1 capital requirement.

are all recognised as eligible ECAIs and are used to assess the credit quality of all exposure classes, where applicable, using the credit quality assessment scale set out in BIPRU.

M&G's credit risk exposures arise from both on and off-balance sheet items. In terms of the on-balance sheet items, these exposures are in the form of cash balances held at banks, Open Ended Investment Company ("OEIC") and Unit Trust ("UT") debtors, annual charges and exposures to other Prudential Plc companies. M&G's off-balance sheet items are in relation to financial guarantees and undrawn commitments provided by M&G.

Financial assets are considered to be past due if a counterparty has not made payment by the contractually due date. The impairment of assets is calculated as the amount by which the carrying amount of an asset exceeds its recoverable amount.

As at 31 December 2017, M&G had not applied any credit risk mitigation techniques in the calculation of the Pillar 1 capital requirement.

Table 4.2: Credit risk – risk weighted asset exposures by class and maturity

Credit risk exposure amounts by class and maturity	**Maturity**		**Total**
£ millions	**<1 year**	**>1year**	
Institutions	129	-	129
Corporates	486	7	493
Collective investment undertakings (CIU)	261	61	322
Central governments or central banks	0	-	0
Past due	5	-	5
Other items	18	30	48
Total	898	99	997

Market risk

Market risk is the exposure to loss arising from movements in market risk factors such as equity prices, FX rates, interest rates and commodity prices. M&G's exposures to market risk arise from its seed investments, the retail fund book of units and FX positions as a result of overseas operations. These exposures give rise to capital requirements. M&G also has a second exposure to market risk through its investment management activities, as the income earned will vary dependent on the value of assets under management ("AUM"). However, this second exposure does not give rise to a capital requirement.

Pillar 1 market risk for M&G is related to FX position risk. M&G is exposed to FX risk as a result of transactional FX exposures in its operating entities. These are primarily US Dollar, Euro and Singapore Dollar positions.

M&G is exposed to structural FX risk as a result of its net investment in overseas operations which contribute to capital resources. These investments are recorded in the functional currencies of the individual entities and are subsequently translated to M&G's presentational currency (GBP). FX differences arising on the translation of the foreign operations are recorded in the FX translation reserve through other comprehensive income and give rise to movements in M&G's capital resources.

M&G does not have a trading book. M&G does not issue debt instruments or other liabilities and, as a result, is not exposed to excessive leverage risk. The leverage ratio is therefore not applicable.

M&G does not use its balance sheet to originate or invest in securitised assets. Securitisation risk is therefore not applicable.

4.3. Other assessment items

Operational risk

Operational risk is defined within M&G's risk framework and operational risk policy as the risk of loss or unintended gain arising from inadequate or failed internal processes, or from personnel and systems, or from external events. There is no operational risk consideration under Pillar 1 but this is the most significant risk for the M&G under Pillar 2.

M&G has an established operational risk scenario analysis process that ensures:

- Completeness of scenario identification: operational risk scenarios are reviewed for completeness in the context of M&G's key risk reporting and are subject to review and challenge using established governance arrangements.
- Forward looking assessment of exposures: Each scenario leverages on both subjective assessments by business specialists and use of objective data and analysis. This analysis includes use of both internal and external data sources. All scenario assessments are subject to review and challenge via established governance arrangements.
- Risk based aggregation: M&G considers correlations between scenarios to determine the potential for concurrency of events.

Non-trading book exposures to equity

M&G holds seed investments across various underlying asset class on the balance sheet. The investments are undertaken, usually at the inception of a new fund, to ensure that investment capital is available to the fund in the short-term, until sufficient third-party client assets are forthcoming and to assist funds with building their track records.

M&G also runs a retail 'book' of units for its fund ranges which invest across a range of underlying asset types. The 'book' is a stock of units that is used as a buffer to smooth pricing basis movements (to keep the funds on a consistent pricing basis as far as possible and to reduce price volatility).

Non-trading book exposure to equities[3] are carried at the balance sheet date fair value and recognised at fair value through profit or loss.

As at 31 December 2017, non-trading book exposures to equity have been treated in line with the requirements of CRD III and are considered immaterial.

Interest rate risk in the non-trading book

[3] An overview of the accounting basis is included in note 11, Other financial assets, within the M&G Group Limited financial statements.

M&G has no debt and is not directly exposed to interest rate risk from an interest expense perspective. Cash deposits are primarily held with a short maturity date and no fixed rate liabilities exist. Additionally, M&G does not hedge interest rate risk. M&G is not exposed to interest rate risk in the non-trading book, with the exception of the book of units and capital investment in funds, which is considered immaterial.

5. Remuneration policy

5.1. Pillar 3 remuneration disclosure for M&G for the year ending 31 December 2017

The following remuneration disclosure is made in accordance with the requirements of the FCA's 'Prudential Sourcebook for Banks, BIPRU, specifically BIPRU 11.5.18 R. This disclosure is available on the M&G's website.

5.2. Decision making process for remuneration policy

M&G has a Remuneration Committee (the "Committee"), which meets at least twice a year to consider issues relating to the remuneration policy and structures for all employees of M&G, including the terms of annual bonus and long-term incentive plans and individual remuneration packages for Directors and other senior employees (including all those in positions of significant influence and those having an impact on M&G's risk profile).

The Committee's membership comprises the Prudential Group's Chief Executive, Chief Financial Officer ("CFO") and HR Director and the M&G CEO and HR Director. Appropriate input is provided by the Finance, Compliance and Risk Directors of M&G to assist the Committee in setting remuneration policy, ensuring that these take appropriate account of all relevant current and future risks and in managing remuneration outcomes. The Committee received independent advice in respect of the firm's remuneration policy from PwC. Other consultants are used from time to time to advise on specific issues. The Committee is accountable to the Prudential PLC Remuneration Committee. No individual is involved in decisions relating to their own remuneration. Decisions in respect of the M&G Chief Executive are within the remit of the Prudential PLC Remuneration Committee.

The Committee takes full account of the Company's strategic objectives in setting remuneration policy. The Committee seeks to ensure the successful retention, recruitment and motivation of employees.

5.3. Code Staff criteria

Code Staff are identified in accordance with the BIPRU Remuneration Code (Senior Management Arrangements, Systems and Controls ("SYSC") 19C.3.4R of the FCA Handbook) which establishes qualitative criteria to identify categories of staff whose professional activities have a material impact on the firm's risk profile. These categories broadly include the relevant Board of Directors, senior management, senior control function staff and other key risk takers.

The Committee approves the list of Code Staff on an annual basis. In addition, Code Staff are notified of their status and the implications of this annually.

5.4. The link between pay and performance for Code Staff

Remuneration is made up of fixed pay (salary and benefits) and performance–related pay. Performance-related pay aligns the interests of participants with the business objectives of the firm and the investment objectives of its clients.

M&G operates a number of discretionary annual bonus arrangements. In most cases, consideration is given to a range of financial and non-financial measures relating to individual, business division / team and M&G's performance. The extent to which each aspect of performance affects the overall payment level depends on the role and responsibilities of the individual. M&G's performance measure used is its profit (the M&G CEO also has Group financial targets). M&G profit is driven by investment returns delivered to clients since revenue mainly comprises charges on funds under management. For key individuals, an element of the bonus is deferred for a period of three years. Deferral is normally into M&G long-term incentive plan units, fund units or Prudential Plc shares (or a combination of these) to ensure appropriate alignment to the long-term sustainable performance of the business. Typically, the rate of deferral will be set so as to ensure that those in receipt of higher amounts of performance pay are required to defer more.

M&G's long-term incentive plans are designed to link reward with its sustained performance. Awards are made at the discretion of the Committee. Awards vest after three years with vesting subject to continued employment. The value of awards is determined at the end of the three-year performance period. All Code Staff participate in a long-term incentive plan.

This plan conditionally awards Prudential shares to participants, with vesting subject to Group International Financial Reporting Standards ("IFRS") profit or business unit IFRS profit, relative Total Shareholder Return ("TSR") and / or a balanced scorecard of strategic measures over a three-year performance period.

Malus provisions[4] may be applied to deferred awards or awards made under one of M&G's long-term incentive plans to support the risk management objective of the firm.

M&G operates a fully flexible policy on variable remuneration, which enables it to award no variable remuneration should individual, business division / team and / or Company performance warrant this (including with relation to financial and non-financial (including against risk and compliance objectives) performance).

The remuneration policies are designed to ensure that any relevant conflicts of interest can be managed appropriately at all times and that the remuneration of its staff is in line with the risk policies and objectives. No individual is involved in decisions relating to their own remuneration. The appraisal and remuneration processes for control function staff, including Risk and Compliance, ensure that their performance management is based on the objectives of the function and individual. All remuneration decisions for such staff are taken independently of the businesses they support.

[4] Contractual arrangement to revise of refuse payments in certain conditions.

5.5. Code Staff remuneration

M&G is required to disclose quantitative remuneration information for its Code Staff population in a manner that is appropriate to its size, internal organisation and the nature, scope and complexity of its activities.

There were 13 Code Staff categorised as Senior Management, including the Chief Executive, M&G, and 11 other Code Staff. On the basis that M&G is one business unit, aggregate remuneration expenditure in respect of Code Staff was as follows:

Table 5.1: Aggregate remuneration expenditure in respect of Code Staff

	Aggregate remuneration awarded in 2017	***Fixed remuneration***	***Variable remuneration***
Senior management	£21,115,265	*£3,965,695*	*£17,149,570*
Other Code Staff	£2,902,759	*£1,427,052*	*£1,475,706*
TOTAL	**£24,018,024**	***£5,392,747***	***£18,625,276***

Aggregate remuneration consists of base salary, directors' fees, benefits, annual bonus, deferred bonus and long-term incentive awards. Pension is excluded.

6. Appendix

6.1. Appendix I – Balance sheet & capital resources as at 31 December 2017

Balance sheet and capital resources as at 31 December 2017	M&G Group Limited Balance Sheet (audited)	Group Capital resources items	Comment
Non-current assets	**£m**	**£m**	
Property, plant and equipment	3.5		
Intangible assets	0.0	(0.0)	Intangible assets deduction
Trade and other receivables	11.9	(6.5)	DAC/DIR adjustment *
Investments in associates	40.3	(39.9)	Material holdings deduction
Other financial assets	68.0	(6.0)	Material holdings deduction
Deferred tax assets	26.0		
Pension scheme surplus	106.5	(90.6)	Pension asset deduction net of deferred tax
Current Assets			
Other financial assets	312.6		
Trade and other receivables	717.2		
Cash and cash equivalents	434.4		
Current liabilities	(838.2)		
Non-current liabilities	(130.0)		
Net assets	**752.2**		
Equity attributable to equity holders of the parent			
Share capital	0.1	0.1	
Fair value reserve	10.8	8.2	
Other reserves	4.2	(21.3)	**
Retained earnings	733.7	691.3	**
Non-controlling interest	3.4	1.9	**
Total equity / capital resources	**752.2**	**537.2**	

Numbers have been rounded to the nearest decimal point so may not always sum correctly.

*Deferred acquisition cost / deferred initial revenue adjustment

** The difference between the audited balance sheet and capital resource amounts is due to unverified gains at the reporting date of 31 December 2017 for regulatory capital purposes; these are subsequently verified by external auditors after the reporting date.