

Chesnara plc

Condensed Consolidated Financial Statements

for the Six Months Ended

30 June 2008

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Note on Terminology

On 30 June 2006 the long-term business of City of Westminster Assurance Company Limited, a Group subsidiary acquired on 2 June 2005, was transferred, under the provisions of Part VII of the Financial Services and Markets Act 2000, to the Group's other principal operating subsidiary, Countrywide Assured plc, in which the whole of the Life operations of the Group now subsist. However, within this document reference is made to 'CWA' and to 'CA' to continue to identify respectively the long-term business which had been conducted within the respective companies prior to the transfer.

Chesnara plc

Condensed Consolidated Financial Statements for the six months ended 30 June 2008

Financial Highlights

	Unaudited 6 months ended 30 June		Year ended 31 December
	2008	2007	2007
IFRS basis			
Operating profit	10.4	13.0	28.8
Financing costs	(0.4)	(0.6)	(1.1)
Profit before income taxes	£10.0m	£12.4m	£27.7m
Basic earnings per share	7.71p	9.68p	24.32p
Dividend per share	5.5p	5.25p	15.1p
Shareholders' net equity	£123.5m	£116.0m	£125.8m
European Embedded Value basis (EEV)			
Operating (loss) / profit	(4.7)	6.0	9.7
Investment variances and economic assumption changes	(0.5)	5.1	(3.3)
(Loss)/profit before tax	£(5.2)m	£11.1m	£6.4m
Profit for the period, net of tax	£2.0m	£7.7m	£12.1m
Covered Business			
Shareholder net worth	57.1	77.1	77.6
Value of in-force business	85.9	105.6	94.0
Embedded value	143.0	182.7	171.6
Acquired embedded value financed by debt	(8.3)	(12.6)	(12.4)
Shareholders' equity in other Group companies	44.3	18.3	28.1
Shareholders' equity on EEV basis	£179.0m	£188.4m	£187.3m
Life annual premium income (AP)	£47.4m	£52.3m	£102.3m
Life single premium income (SP)	£13.3m	£17.8m	£32.0m
Life annualised premium income (AP + 1/10 SP)	£48.7m	£54.1m	£105.5m

In contrast with the IFRS basis of reporting, the EEV basis recognises the discounted value of the expected future cash flows arising from the long-term business contracts in force at the period-end, as a component of shareholder equity. Accordingly, the EEV result recognises, within profit, the movement in this component, which, for the six months ended 30 June 2008, was adversely impacted by global investment market conditions, giving rise to an operating loss at the pre-tax level. This was offset by associated reductions in the estimate of future tax payable within expected future cash flows, so that the EEV result reflects a profit at the net of tax level.

Chairman's Statement

I am pleased to present the fifth interim statements of Chesnara plc ('Chesnara').

Background

Chesnara was listed on the London Stock Exchange in May 2004. Originally formed to become the holding company of Countrywide Assured plc on its demerger from Countrywide plc, in June 2005 it acquired City of Westminster Assurance Company Limited, a further closed life assurance company, the long-term business of which was transferred to Countrywide Assured plc on 30 June 2006.

Countrywide Assured plc now manages a portfolio of some 195,000 life assurance and pension policies and is substantially closed to new business. It writes a small amount of new business and accepts top-ups to existing contracts. As a substantially closed book it is expected that the embedded value of the business will decline over time as the number of policies in force reduces and as the surplus emerging in the business is distributed by way of dividends. As the portfolio runs off, the regulatory capital supporting it may also be reduced and returned to shareholders.

In order to prolong the yield delivery Chesnara seeks to acquire similar businesses. We believe, however, that such potential acquisitions should not detract from our key objective of delivering a steady and attractive dividend yield.

Review of the Business

In the first half of the year, none of the acquisition opportunities reviewed by the Company proved compelling. Therefore, we have concentrated our efforts on enhancing shareholder value within the business. Although investment market performance has had an adverse effect, our long-standing prudent approach to the business has enabled the posting of a result, which in the prevailing circumstances, can be described as resilient.

Investment market falls have depressed projected future earnings, and hence overall company value, as part of our profit flow emanates from the charges on policyholder investment funds. However, we have seen further improvements in policy persistency with lower lapse rates than expected. With mortality experience remaining in line with expectations and the mortgage endowment misselling reserve proving adequate we are able to report a strong set of results.

On the IFRS basis of reporting we have posted a pre-tax profit of £10.0m for the half-year ended 30 June 2008 compared with £12.4m for the corresponding period in 2007.

On the European Embedded Value ('EEV') basis of reporting, the Group recognises a pre-tax loss of £5.2m for the half-year ended 30 June 2008 compared to a profit of £11.1m for the same period in 2007. This arises largely from the impact of falls in global investment markets and is offset by associated reductions in the estimate of future tax so that we are able to post a positive post-tax result, in a difficult climate, of £2.0m.

Total shareholder equity, as stated on an EEV basis, pre interim dividend appropriation, has reduced, albeit not as much as one might expect from the reduction in the policy base and investment market performance, from £187.3m (£1.79 per share) at 31 December 2007 to £179.0m (£1.71 per share) at 30 June 2008.

Countrywide Assured plc's capital solvency ratio at 227% remains at a healthy premium to the target set by the Board of 150%. It has reduced from 267% at the corresponding point last year due to significant dividend transfers to Chesnara. The Group's solvency position, post the proposed dividend, has strengthened significantly from 267% as at 30 June 2007 to 348% as at 30 June 2008.

Based on these results the Board is pleased to recommend an interim dividend of 5.5p (2007: 5.25p), which represents an increase of 4.8% and equates to a total interim dividend of £5.8m.

Outlook

Experience in all the key areas affecting the business, with the exception of investment market performance, has proved to be on target, if not better. The fact that, overall, we have increased the net value of the Group, in the face of a challenging environment, is very positive and bodes well for the future.

We continue to search for acquisitions, both in the life assurance and related sectors, and remain expectant that suitable opportunities will arise and that, with our strong capital base, we are well placed to take advantage of the right opportunity.

We remain well placed to continue to fulfil our stated objective of continuing to deliver a reliable and progressive dividend flow and wish to thank our employees for their contribution to the Group in realising this aim.

Christopher Sporborg
Chairman
28 August 2008

Directors' Information

Christopher H Sporborg CBE is the Non-executive Chairman of Chesnara plc. He is also Chairman of the Nomination Committee. He was formerly Deputy Chairman of Hambros PLC, Deputy Chairman of Hambros Bank Limited and Chairman of Hambro Insurance Services Group PLC. At Hambros he was responsible for the acquisition of Bairstow Eves PLC in 1986 and the formation of Hambro Countrywide plc and, in 1988, the creation of the life company then called Hambro Guardian Assurance plc and now part of the Chesnara plc group of companies. He is also a director of Getty Images Inc.

Graham Kettleborough is the Chief Executive of Chesnara plc. He joined Countrywide Assured plc in July 2000 with responsibility for marketing and business development and was appointed as Managing Director and to the Board in July 2002. Prior to joining Countrywide Assured plc, he was Head of Servicing and a Director of the Pension Trustee Company at Scottish Provident. He has lifetime experience in the financial services industry, primarily in customer service, marketing, product and business development, gained with Scottish Provident, Prolific Life, City of Westminster Assurance and Target Life.

Ken Romney is the Finance Director and Company Secretary of Chesnara plc. He joined Countrywide Assured plc in 1989 and became a member of the Board in 1997. He has worked in the life assurance industry for the last 24 years. He was Chief Accountant at Laurentian Life (formerly Imperial Trident) up to 1987 and was Financial Controller at Sentinel Life between 1987 and 1989. He worked for Price Waterhouse in their audit division until 1983 in both the UK and South Africa. He is a Fellow of the Institute of Chartered Accountants in England and Wales.

Frank Hughes is the Business Services Director of Chesnara plc. He joined Countrywide Assured plc in November 1992 as an IT Project Manager and was appointed to the Board as IT Director in May 2002. He has 23 years' experience in the life assurance industry gained with Royal Life, Norwich Union and CMG.

Peter Mason is the Senior Independent Non-executive Director of Chesnara plc and is Chairman of the Audit Committee. He also serves on the Remuneration and Nomination Committees. He is currently a Non-executive Director of Homeowners Friendly Society and Countrywide Assured plc. He is the Investment Director and Actuary of Neville James Group, an investment management company. He was admitted as a Fellow of the Institute of Actuaries in 1979.

Mike Gordon is an Independent Non-executive Director of Chesnara plc and is Chairman of the Remuneration Committee. He also serves on the Audit Committee and the Nomination Committee. He spent 12 years as Group Sales Director of Skandia Life Assurance Holdings. He is Chairman of Bankhall Investment Management Limited, a Skandia-owned subsidiary.

Terry Marris is a Non-executive Director of Chesnara plc and serves on the Audit Committee, the Remuneration Committee and the Nomination Committee. He joined Countrywide Assured Group plc in 1992 and was Managing Director of Countrywide Assured plc until July 2002. Previous roles included senior management positions at Lloyds Bank and General Accident.

Interim Management Report

Background

Chesnara seeks to participate in the consolidation of the closed life business sector in the UK. In 2004, at the same time that we listed on the London Stock Exchange, we acquired Countrywide Assured plc on its effective demerger from the estate agency business which now forms the core of the operations of Countrywide plc, while in 2005 we acquired City of Westminster Assurance Company Limited from Irish Life and Permanent plc. In 2006 we merged the long-term business of the two companies in order to realise significant financial and operational synergies.

As Countrywide Assured plc is substantially closed to new business its primary focus is on the efficient run-off of the existing life and pension portfolios. This gives rise to the emergence of surplus which supports our primary aim of delivering an attractive long-term dividend yield to our shareholders. By the very nature of the life business assets the surplus arising will deplete over time as the policies mature, expire or are the subject of a claim. Therefore, to prolong the yield delivery we seek to acquire similar businesses.

Review of the Business

During the first half of 2008 Chesnara has continued, in the absence of any compelling acquisition opportunities, to concentrate on its policy of delivering enhanced value to shareholders through focusing on the efficient run-off of its Life business.

The continued strength of the emergence of surplus has underpinned the overall financial performance of the business and enabled the delivery of a strong profit on the IFRS basis of reporting and the maintenance of a healthy regulatory solvency position.

Whilst the result has, inevitably, been negatively affected by conditions prevailing in the investment markets these have been mitigated by a contribution from new business and tight control over expenses. There have been no new regulatory issues that have given rise to any significant concerns or costs.

These key areas are reviewed in more detail in the following sections.

Investment Funds

Strong performance in the unit-linked funds helps promote policy retention and increases the embedded value of the Group as future management charges will be of a higher magnitude. The CA Managed Fund, which represents a significant proportion of the CA policyholder funds under management, returned –6.41% during the twelve months ended 30 June 2008 while the CWA Global Managed Fund, which represents a significant proportion of CWA policy funds under management, returned –8.56% over the same period. These returns, on balance, compare favourably with the average of –7.86% achieved by the ABI Life Balanced Managed Funds sector.

These results reflect the poor performance of the equity markets consequent upon developments in the credit markets and the general economic climate. Shareholders do not have any direct exposure to the sub-prime market. However, recent market performance does affect fund values and consequently, the embedded value. Guidance as to the sensitivity of embedded value to market movements is provided on page 30.

The Board continue to have a prudent approach to the investment of shareholder funds, which underpins our strong solvency position. The benchmark of 70% cash and 30% fixed interest has been maintained.

Policy Attrition

The longer a policy stays in force the greater the profit that accrues to the Group. We have continued to maintain a strong focus on the retention of policies where it is in the interests of customers to continue with their arrangements. At the 2007 year-end we reported that the rate of policy attrition had decreased. This improvement has been sustained and further reduction in policy cessation rates has been evident. However, this benefit has not been reflected in the assumptions underpinning the EEV at the half year. Should this persist, despite the current economic climate, through to the year-end then a positive re-rating of the value of the in-force policies, and consequently of the embedded value, through a restatement of persistency assumptions, is possible.

Financial Exposures

The Group pays particular attention to any area where it has potentially significant financial exposure. In life and pensions these typically arise in the areas of onerous policy options and guarantees and of compensation claims for past mis-selling of products. Whilst the Group's portfolios have very little exposure to the impact of investment market performance on options and guarantees, it does have some ongoing exposure to potential mis-selling of

policies sold in connection with an endowment mortgage. We are required to make redress to a subset of mortgage endowment policyholders who have been mis-sold their product and to write to policyholders on a biennial basis setting out their potential returns based on specified growth rates. In the past there has been significant media attention and aggressive advertising by claims management firms on this issue. This activity has continued to decline in the first half of the year as more potential claims become time-barred from making a successful complaint. At the present time, over 80% of relevant mortgage endowments are time-barred with the balance of the population carrying little potential liability to compensation. We are pleased to report that, during the first half of 2008, the number of complaints we have received has continued to reduce. However this has been offset, to a degree, by slightly higher uphold rates. Based on current experience we believe that the reserve we hold will prove adequate.

As disclosed in previous statements we identified an error in an old unit pricing system which had resulted in incorrect capital gains tax being deducted from unit linked funds. A project is in place to provide recompense to affected policyholders in line with Treating Customers Fairly ('TCF') principles and the provision created in 2007 (net of estimated recoveries) of £2.5m (£1.8m net of tax) is still considered to be adequate.

Regulatory Issues

The key focus on the regulatory front in the first part of the year was to ensure we met the FSA's target of the development of suitable management information in order to evidence our compliance with TCF requirements by March 2008. I am pleased to say that we met that target and have made significant progress in embedding TCF into the business. The next target is being able to demonstrate full TCF compliance by December 2008 and we believe we are in good shape to meet this requirement.

We continue to receive and review Good Practice Guides as issued by the Association of British Insurers and, where we believe it appropriate to our business, amend our practice to comply with the guidance.

Expense Base

Operational and outsourcer costs are being kept under control and our policy attrition rate is better than assumed. The result is that there are more policies in force over which fixed costs can be allocated, leading to cost efficiencies reflected in lower per policy costs.

Key to our strategy of expense base management is the outsourcing of our back office functions to professional outsourcing organisations. This results in predictable levels of per policy cost each year for the term of the relevant contract and removes cost inefficiencies that can occur as a result of a diminishing policy base.

As reported at the last year-end we finalised an arrangement with Capita Life and Pensions Limited ('Capita') for the outsourcing of the administration of the CWA book early in 2007.

The systems migration project undertaken by Capita, which aimed to transfer the CWA business to their systems, resulted in a successful migration on 21 July 2008. We have now closed the inherited Luton operation and consequently reduced the cost base further.

Service levels from both Capita and Liberata Financial Services Limited, who are managing the CA book of business, are in line with agreed standards.

IFRS Result

The following summarises information reflected in the IFRS Income Statement, showing the contribution from the constituent members of the Group

	CA	CWA	Parent	Amortisation	Total
	£000	£000	company	of AVIF	£000
			£000	£000	
Six months ended 30 June 2008					
Operating profit	7,886	3,176	1,121	(1,751)	10,432
Financing costs	-	-	(455)	-	(455)
Profit before income taxes	7,886	3,176	666	(1,751)	9,977
Six months ended 30 June 2007					
Operating profit	8,892	5,803	30	(1,751)	12,974
Financing costs	-	-	(579)	-	(579)
Profit before income taxes	8,892	5,803	(549)	(1,751)	12,395

Year ended 31 December 2007

Operating profit	18,566	12,674	1,071	(3,502)	28,809
Financing costs	-	-	(1,089)	-	(1,089)
Profit before income taxes	18,566	12,674	(18)	(3,502)	27,720

Notes

- (1) Financing costs relate to a bank loan raised to part finance the acquisition of CWA.
- (2) Amortisation of Acquired Value In-Force ('AVIF') represents a post acquisition charge to profits of the write-down of the acquired value of CWA in-force business, as measured at the acquisition date. The pattern of amortisation is broadly intended to match the pattern of surplus arising from the run-off of the underlying CWA insurance and investment contract portfolios.

Overall, the result for the six months ended 30 June 2008 reflects the continuing strong emergence of surplus in both CA and CWA, as the underlying insurance and investment contracts run off. However, the impact of investment market conditions over the period has adversely impacted the result by some £2m and this is in sharp contrast to benign investment market conditions which, together with favourable mortality experience, benefited the comparative period for the six months ended 30 June 2007. The resilience of the result in difficult trading conditions has been underpinned by a new business contribution and continuing tight control over expenses, together £0.8m better than expected.

The significant increase in parent company operating profit for the six months ended 30 June 2008 compared with the comparative period for 2007 reflects the increased return on investment assets following dividend transfers from the Life subsidiary.

EEV Result

Supplementary information prepared in accordance with EEV principles and set out in the financial information on pages 22 to 31 is presented to provide alternative information to that presented under IFRS. EEV principles recognise profits as they are earned over the life of insurance and investment contracts and assist in identifying the value being generated by the life businesses. The result determined under this method represents principally the movement in the life businesses' embedded value, before transfers made to the Parent Company and ignoring any capital movements. As the Group's life assurance operations are now substantially closed to new business, the principal underlying components of the EEV result are the expected return from the business in force (being the yield at the risk discount rate on the related policy cash flows as they fall into surplus) together with (1) variances of actual experience from that assumed for each component of the policy in force cash flows and (2) the impact of resetting assumptions for each component of the prospective cash flows.

The following is a summarised statement of the EEV result:

	6 months ended 30 June		Year ended 31 December
	2008	2007	2007
	£000	£000	£000
Operating (loss)/profit before tax	(4,669)	5,949	9,662
Variation from longer term investment return	428	(571)	824
Economic assumption changes	(950)	5,697	(4,043)
(Loss)/profit before tax	(5,191)	11,075	6,443
Tax			
- current	(2,500)	(3,355)	(4,379)
- deferred	9,726	5	10,053
Profit for the period after tax	2,035	7,725	12,117

Investment markets suffered significant falls over the six months ended 30 June 2008, with leading UK equity market indices, for example, recording a 13% decrease over the period. The capital values of fixed interest securities also incurred significant reductions as interest rates eased up over the second half of the period. These conditions affect the result both through the impact on estimated future deductions from unit-linked funds and on the impact on returns from non-linked policyholder and shareholder funds.

These adverse impacts have been offset, to a degree, by:

- (i) the expected return (unwind of the risk discount rate at 7.7%) of £5.4m;
- (ii) favourable lapse experience of £3.2m; and
- (iii) favourable new business and expense variances of £0.8m

resulting in a net pre-tax loss of some £5.2m during the period.

The impact of investment market losses is further mitigated to the extent of some £8m as a result of the associated reduction in the estimate of future tax payable, which is dependent, to a significant extent, on investment returns and on the estimated level of franked investment income, and this is included in the deferred tax credit of £9.7m shown above, so that the Group has achieved a positive net of tax result in the period.

Overall, these positive factors have maintained the value of the Company in a difficult and challenging trading environment.

Shareholders' Equity and Embedded Value of Covered Business – EEV Basis

The consolidated balance sheet prepared in accordance with EEV principles may be summarised as:

	30 June		31 December
	2008	2007	2007
	£000	£000	£000
Value of in-force business	85,939	105,607	94,007
Other net assets	93,109	82,807	93,308
	179,048	188,414	187,315
Represented by:			
Embedded value ('EV') of covered business	143,005	182,669	171,639
Less: amount financed by borrowings	(8,326)	(12,600)	(12,469)
EV of covered business attributable to shareholders	134,679	170,069	159,170
Net equity of other Group companies	44,369	18,345	28,145
Shareholders' equity	179,048	188,414	187,315

Subsequent to 31 December 2007, a dividend of £30m was paid to Chesnara plc from the Life business. This reduced the EV of the covered business, while increasing the net equity of other Group companies.

The tables below, set out the components of the value of in-force business by major product line at each period end:

	30 June		31 December
	2008	2007	2007
	000	000	000
Number of policies			
Endowment	62	70	66
Protection	70	80	75
Annuities	4	4	4
Pensions	50	52	51
Other	9	9	9
Total	195	215	205

	30 June		31 December
	2008	2007	2007
	£m	£m	£m
Value in-force			
Endowment	51.4	68.1	58.3
Protection	55.0	70.3	63.0
Annuities	2.3	2.7	2.0
Pensions	34.1	41.9	38.1
Other	0.2	0.3	1.4
Total at product level	143.0	183.3	162.8

Valuation adjustments			
Holding company expenses	(20.5)	(21.2)	(20.7)
Other	(20.5)	(16.0)	(21.4)
Cost of capital	(5.1)	(3.0)	(5.5)
Value in-force pre-tax	96.9	143.1	115.2
Taxation	(11.0)	(37.5)	(21.2)
Value in-force post-tax	85.9	105.6	94.0

Principal Risks and Uncertainties

The Group's management of insurance risk is a critical aspect of the business. The primary insurance activity carried out by the Group comprises the assumption of the risk of loss from persons that are directly subject to the risk. Such risks in general relate to life, accident, health and financial perils that may arise from an insurable event, with the majority of the Group's exposure relating to mortality risk on individual lives, predominantly in the UK. As such, the Group is exposed to the uncertainty surrounding the timing and severity of claims under the related contracts.

The Group is also exposed to a range of financial risks through its life assurance contracts, financial assets, financial liabilities, including investment contracts and borrowings, and its reinsurance assets. In particular, the key financial risk is that in the long-term its investment proceeds are not sufficient to fund the obligations arising from its insurance and investment contracts. The most important components of this financial risk are market risk (interest rate risk and equity price risk), and credit risk, including the risk of reinsurer default. The Group has procedures for setting and monitoring the Group's assets and liability position with the objective of ensuring that the Group can always meet its obligations without undue cost and in accordance with the Group's internal and regulatory capital requirements.

Detailed information on the characteristics and management of insurance and financial risks borne by the Group is provided in Notes 4 and 5 respectively of the Company's published consolidated financial statements for the year ended 31 December 2007.

In addition, insofar as the Group makes estimates and assumptions that affect the reported amounts of the following assets and liabilities, there is uncertainty as to the amounts at which they may eventually be settled or realised and as to the timing of settlement or realisation:

- (i) estimates of future benefits payments arising from long-term insurance contracts;
- (ii) fair value of investment contracts;
- (iii) liability for redress in respect of mortgage endowment misselling complaints and of unit pricing error;
- (iv) deferred acquisition costs and deferred income; and
- (v) amortisation of acquired value of in-force business.

Detailed information on these items is provided in Note 3 of the Company's published consolidated financial statements for the year ended 31 December 2007.

There have been no changes in the nature and incidence of the principal risks and uncertainties, referred to above, during the six months ended 30 June 2008, except in relation to volatility in global investment markets. The impact of this on reported results for the six months ended 30 June 2008 is set out in the commentary under 'IFRS Result' and 'EEV Result' above. Clearly there is continuing significant uncertainty with regard to the direction of investment markets over the remaining six months of the current financial year and attention is drawn particularly to the sensitivity of the reported embedded value of the Company to investment market and interest rate movements set out in Note 7 to the European Embedded Value Basis Supplementary Information on page 30.

Related Party Transactions

There have been no related party transactions that have occurred during the first six months of the financial year that have materially affected the financial position or performance of the Group during that period and there have been no changes in the related party transactions described in the last annual report that could do so.

Solvency and Regulatory Capital

Regulatory Capital Resources and Requirements

The regulatory capital of life insurance companies in the UK is calculated by reference to FSA prudential regulations. The rules are designed to ensure that companies have sufficient assets to meet their liabilities in specified adverse circumstances. As such, there is a restriction on the full transfer of surplus from the long-term business fund to shareholder funds of the Life company and on the full distribution of reserves from the Life company to Chesnara.

The following summarises the capital resources and requirements of the Life company for regulatory purposes after making provision for dividend payments from the Life company to Chesnara, which were approved after the respective period ends. There were no such dividends relating to 30 June 2008 or 30 June 2007.

	30 June 2008 £m	2007 £m	31 December 2007 £m
Available capital resources ('CR')	57.1	77.1	47.6
Long-term insurance capital requirement ('LTICR')	23.6	26.9	25.1
Resilience capital requirement ('RCR')	1.5	2.0	1.5
Total capital resources requirement ('CRR')	25.1	28.9	26.6
Target capital requirement cover	37.0	42.4	39.1
Excess of CR over target requirement	20.1	34.7	8.5
Ratio of available CR to CRR	227%	267%	179%

It can be seen from this information that Chesnara, which relies on dividend distributions from its Life company, is currently in a favourable position to service its loan commitments and to continue to pursue a progressive dividend policy.

Insurance Group Directive

In accordance with the EU Insurance Group Directive, the Group calculates the excess of the aggregate of regulatory capital employed over the aggregate minimum solvency requirement imposed by local regulators. The following sets out these calculations after the recognition of interim and final dividends for the financial year, approved by the Board and paid to Group shareholders after the respective dates:

	30 June 2008 £m	2007 £m	31 December 2007 £m
Available group capital resources	87.3	77.3	82.9
Group regulatory capital requirements	(25.1)	(28.9)	(26.6)
Excess	62.2	48.4	56.3
Cover	348%	267%	312%

The regulatory requirement is that available group capital resources should be at least 100% of capital requirements.

Individual Capital Assessments

The FSA Prudential Sourcebooks require an insurance company to make its own assessment of its capital needs to a required standard (a 99.5% probability of being able to meet its liabilities to policyholders after one year). In the light of scrutiny of this assessment, the FSA may impose its own additional individual capital guidance. The Individual Capital Assessment is based on a realistic liability assessment, rather than on the statutory mathematical reserves, and involves stress testing the resultant realistic balance sheet for the impact of adverse events.

CA completed a further annual assessment during 2007 as a result of which it was concluded that the effective current- and medium-term capital requirement constraints on distributions to Chesnara will continue to be on the basis set out under "Regulatory capital resources and requirements" above.

Developments

In the second half of the year Chesnara will continue to search for consolidation or other value-enhancing acquisition opportunities and work with our outsource partners to ensure continuing delivery of acceptable service levels. We will also continue to progress the Treating Customers Fairly project and maintain our focus on mortgage endowment and persistency issues.

Consolidation

Whilst there has been more activity at the top end of the market, as measured by Embedded Value, there has been little, if any, opportunity in our target range. However, we continue to expect that opportunities for consolidation of suitably sized life assurance companies will arise.

Regulatory

With our TCF project on track, our Individual Capital Assessment indicating that, at present, we have no requirement to hold additional regulatory capital and no other significant regulatory challenges emerging we will look to build on our progress to date and to ensure that we maintain strong and focussed management of our regulatory and risk programmes.

Financial Reporting

The CFO Forum, representing leading European insurers, published its 'Market Consistent Embedded Value (MCEV) Principles and Guidance' during June 2008. We will be assessing the new principles and guidance with a view to implementation in 2009 and we anticipate that the application of the principles will make no material difference to our published EEV, as we already adopt a market-consistent approach.

Mortgage Endowments and Persistency

Notwithstanding the acceptable mortgage endowment experience and the positive persistency result in the first half of the year we remain aware that they are both significant drivers of both current and future profitability. Therefore they will, necessarily, receive ongoing focussed management attention.

Outlook

The results for the first six months have, whilst being affected by investment market performance, benefited from ongoing improvement in policy attrition rates, a new business contribution and strong expense management. We believe that the results demonstrate a level of ongoing resilience to the rigours of adverse market conditions.

Within the mortgage endowment misselling redress provision we still retain an element of prudence: both this, and our currently strong persistency experience could be adversely affected by the wider economic climate. Accordingly, we have not recognised the full financial effects of the improvement in the policy attrition rate as it is too early to assess the mid to longer-term effects in this uncertain climate.

We will continue to seek other opportunities that could leverage value from our existing capabilities. If no clearly superior investment alternative is identified the possibility of, and preferred methodology for, a return of surplus capital will be considered.

We continue to believe we are well placed to fulfil our stated objective of delivering a reliable and progressive dividend flow.

The Board wishes to extend its thanks to all its employees for their continued contribution to the Group.

Dividend

We have signalled that we aim to provide a reliable and progressive dividend payment. With the continuing healthy emergence of surplus from the underlying product base, the improving situation in the key areas of mortgage endowment and persistency and the strong solvency position of the business, the Board are pleased to be able to recommend an interim dividend of 5.5p, which represents an increase of 4.8% over the 2007 interim payment.

Graham Kettleborough
Chief Executive Officer
28 August 2008

Statement of Directors' Responsibilities in respect of the Half Yearly Financial Report

The Directors confirm that, to the best of their knowledge:

- the condensed set of consolidated financial statements has been prepared in accordance with IAS 34 *Interim Financial Reporting* as adopted by the EU;
- the interim management report includes a fair view of the information required by:
 - (a) DTR 4.2.7R of the Disclosure and Transparency Rules, being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements and a description of the principal risks and uncertainties for the remaining six months of the year; and
 - (b) DTR 4.2.8R of the Disclosure and Transparency Rules in respect of
 - (I) transactions that have taken place in the first six months of the current financial year that have materially affected the financial position or performance of the Group during that period; and
 - (II) any changes in the related party transactions described in the last annual report that could do so.

On behalf of the Board:

Ken Romney
Finance Director
28 August 2008

Condensed Consolidated Income Statement for the six months ended 30 June 2008

		Unaudited 6 months ended 30 June		Year ended 31 December
	Note	2008 £000	2007 £000	2007 £000
Insurance premium revenue		48,183	52,669	103,554
Insurance premium ceded to reinsurers		(8,779)	(9,453)	(18,716)
Net insurance premium revenue		39,404	43,216	84,838
Fee and commission income				
Insurance contracts		17,905	19,770	38,032
Investment contracts		4,907	4,570	9,149
Investment income	4	(114,296)	83,290	90,210
Total revenue (net of reinsurance payable)		(52,080)	150,846	222,229
Other operating income		1,031	543	1,298
Net income		(51,049)	151,389	223,527
Policyholder claims and benefits incurred		25,384	(102,809)	(157,114)
Reinsurers' share of claims and benefits incurred		(4,011)	15,837	26,518
Net policyholder claims and benefits incurred	4	21,373	(86,972)	(130,596)
Change in investment contract liabilities		51,632	(40,875)	(50,697)
Reinsurers' share of investment contract liabilities		(2,352)	1,341	11,534
Net change in investment contract liabilities	4	49,280	(39,534)	(39,163)
Fees, commission and other acquisition costs		(601)	(790)	(1,546)
Administrative expenses		(6,531)	(8,750)	(15,955)
Other operating expenses				
Charge for amortisation of intangible assets		(1,740)	(1,889)	(3,734)
Other		(300)	(480)	(3,724)
Total expenses	4	61,481	(138,415)	(194,718)
Operating profit		10,432	12,974	28,809
Financing costs		(455)	(579)	(1,089)
Profit before tax		9,977	12,395	27,720
Income tax expense		(1,917)	(2,275)	(2,281)
Profit for the period	3	8,060	10,120	25,439
Basic earnings per share	2	7.71p	9.68p	24.32p
Diluted earnings per share	2	7.71p	9.68p	24.32p

The Group considers that it has no product or distribution based segmentation and, as it only has significant business activity within the UK, it has no geographic segmentation. Accordingly, no segmented reporting is presented.

Condensed Consolidated Balance Sheet at 30 June 2008

		Unaudited 30 June		31 December
		2008	2007	2007
	Note	£000	£000	£000
Assets				
Intangible assets				
Deferred acquisition costs		9,158	10,088	9,542
Acquired value of in-force business				
Insurance contracts		18,197	20,762	19,427
Investment contracts		12,118	13,135	12,627
Reinsurers' share of insurance contract provisions		197,763	211,097	212,353
Amounts deposited with reinsurers		24,876	62,126	27,558
Investment properties		3,673	19,935	4,983
Financial assets				
Equity securities at fair value through income		443,155	850,876	743,670
Holdings in collective investment schemes at fair value through income		634,228	411,083	508,857
Debt securities at fair value through income		247,457	312,775	247,152
Loans and receivables including insurance	5	13,277	49,847	15,415
Derivative financial instruments		8,338	25,610	9,525
Total financial assets		1,346,455	1,650,191	1,524,619
Reinsurers' share of accrued policyholder claims		4,356	5,631	4,661
Income taxes		-	153	-
Cash and cash equivalents		244,810	247,802	225,127
Total assets		1,861,406	2,240,920	2,040,897
Liabilities				
Bank Overdrafts		1,506	-	1,229
Insurance contract provisions		1,009,868	1,134,689	1,110,848
Financial liabilities				
Investment contracts at fair value through income		650,061	798,671	726,503
Borrowings	6	8,326	12,425	12,469
Derivative financial instruments		2,474	367	265
Total financial liabilities		660,861	811,463	739,237
Provisions		3,494	537	3,575
Deferred tax liabilities		11,263	12,862	11,847
Reinsurance payables		1,942	2,192	1,622
Payables related to direct insurance and investment		24,023	25,974	22,859
Deferred income		15,576	17,276	16,362
Income taxes		2,643	4,626	743
Other payables	5	6,688	115,345	6,791
Total liabilities		1,737,864	2,124,964	1,915,113
Net assets		123,542	115,956	125,784
Shareholders' equity				
Share capital		41,501	41,501	41,501
Share premium		20,458	20,458	20,458
Other reserves		50	50	50
Retained earnings	3	61,533	53,947	63,775
Total shareholders' equity		123,542	115,956	125,784

Condensed Consolidated Statement of Cash Flows for the six months ended 30 June 2008

	Unaudited 6 months ended 30 June		Year ended 31 December
	2008	2007	2007
	£000	£000	£000
Profit for the year	8,060	10,120	25,439
Adjustments for:			
Amortisation of deferred acquisition costs	384	599	1,145
Amortisation of acquired in-force value	1,739	1,891	3,734
Tax expense	1,917	2,275	2,281
Interest receivable	(13,825)	(12,357)	(26,650)
Dividends receivable	(15,908)	(17,681)	(35,997)
Interest expense	455	579	1,089
Change in fair value of investment properties	(10)	(1,682)	(1,873)
Fair value losses on financial assets	146,777	918	31,768
Interest received	10,639	9,876	28,707
Dividends received	18,399	19,107	37,810
Changes in operating assets and liabilities			
Decrease/(increase) in financial assets	30,569	(129,760)	(54,327)
Decrease/(increase) in reinsurers' share of insurance contract provisions	14,895	(5,258)	(5,544)
Decrease in amounts deposited with reinsurers	2,682	1,595	36,163
Decrease / (increase) in other loans and receivables	2,833	(31,482)	(1,975)
(Decrease) / increase in insurance contract provisions	(100,980)	19,492	(4,349)
(Decrease) in investment contract liabilities	(76,442)	(14,308)	(86,476)
(Decrease) / increase in provisions	(81)	(60)	2,978
Increase / (decrease) in reinsurance payables	320	(867)	(1,437)
Increase / (decrease) in payables related to direct insurance and investments contracts	1,164	1,047	(2,068)
Increase / (decrease) in other payables	1,353	106,518	(3,060)
Cash generated from / (utilised by) operations	34,940	(39,438)	(52,642)
Income tax paid	(600)	(645)	(5,399)
Net cash generated from / (utilised by) operating activities	34,340	(40,083)	(58,041)
Cash flows from financing activities			
Repayment of borrowings	(4,200)	(4,200)	(4,200)
Dividends paid	(10,302)	(8,419)	(13,910)
Interest paid	(432)	(714)	(1,169)
Net cash utilised by financing activities	(14,934)	(13,333)	(19,279)
Net increase / (decrease) in cash and cash equivalents	19,406	(53,416)	(77,320)
Cash and cash equivalents at beginning of period	223,898	301,218	301,218
Cash and cash equivalents at end of period	243,304	247,802	223,898

Condensed Consolidated Statement of Changes in Equity for the six months ended 30 June 2008

Unaudited Six months ended 30 June 2008					
	Share capital £000	Share premium £000	Capital redemption reserve £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2008	41,501	20,458	50	63,775	125,784
Profit for the period representing total recognised income and expenses	-	-	-	8,060	8,060
Dividends paid	-	-	-	(10,302)	(10,302)
Equity shareholders' funds at 30 June 2008	41,501	20,458	50	61,533	123,542

Unaudited Six months ended 30 June 2007					
	Share capital £000	Share premium £000	Capital redemption reserve £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2007	41,501	20,458	50	52,246	114,255
Profit for the period representing total recognised income and expenses	-	-	-	10,120	10,120
Dividends paid	-	-	-	(8,419)	(8,419)
Equity shareholders' funds at 30 June 2007	41,501	20,458	50	53,947	115,956

Year ended 31 December 2007					
	Share capital £000	Share premium £000	Capital redemption reserve £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2007	41,501	20,458	50	52,246	114,255
Profit for the period representing total recognised income and expenses	-	-	-	25,439	25,439
Dividends paid	-	-	-	(13,910)	(13,910)
Equity shareholders' funds at 31 December 2007	41,501	20,458	50	63,775	125,784

Notes to the Condensed Consolidated Financial Statements (Unaudited)

1. Basis of preparation

This condensed set of consolidated financial statements has been prepared in accordance with IAS 34 '*Interim Financial Reporting*' as adopted by the EU. As required by the Disclosure and Transparency Rules of the Financial Services Authority, the condensed set of consolidated financial statements has been prepared applying the accounting policies and presentation that were applied in the preparation of the Group's published consolidated financial statements for the year ended 31 December 2007, which were prepared in accordance with IFRS as adopted by the EU. Any judgements and estimates applied in the condensed set of financial statements are consistent with those applied in the preparation of the Group's published consolidated financial statements for the year ended 31 December 2007

The financial information shown in this half-year review is unaudited and does not constitute statutory accounts within the meaning of Section 240 of the Companies Act 1985.

The comparative figures for the financial year ended 31 December 2007, are not the company's statutory accounts for that financial year. Those accounts have been reported on by the company's auditors and delivered to the Registrar of Companies. The report of the auditors was (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and (iii) did not contain a statement under Section 237 (2) or (3) of the Companies Act 1985.

2. Earnings per share

Earnings per share is based on the following:

	Unaudited 6 months ended 30 June		Year ended 31 December
	2008	2007	2007
Profit for the period (£000)	8,060	10,120	25,439
Weighted average number of ordinary shares	104,588,785	104,588,785	104,588,785
Basic earnings per share	7.71p	9.68p	24.32p
Diluted earnings per share	7.71p	9.68p	24.32p

The weighted average number of ordinary shares in respect of the six months ended 30 June 2008, the six months ended 30 June 2007 and the year ended 31 December 2007 is based on 104,588,785 shares in issue at the beginning and end of all related periods.

There were no share options outstanding during the periods covered by these financial statements. Accordingly, there is no dilution of the average number of ordinary shares in issue in respect of the periods reported.

3. Retained earnings

	Unaudited 6 months ended 30 June		Year ended 31 December
	2008	2007	2007
	£000	£000	£000
Balance at 1 January	63,775	52,246	52,246
Profit for Period	8,060	10,120	25,439
Dividends			
Final approved and paid for 2006	-	(8,419)	(8,419)
Interim approved and paid for 2007	-	-	(5,491)
Final approved and paid for 2007	(10,302)	-	-
Balance at 30 June/31 December	61,533	53,947	63,775

The final dividend in respect of 2006, approved and paid in 2007, was paid at the rate of 8.05p per share.

The interim dividend in respect of 2007, approved and paid in 2007, was paid at the rate of 5.25p per share.

The final dividend in respect of 2007, approved and paid in 2008, was paid at the rate of 9.85p per share, so that the total dividend paid to the equity shareholders of the parent company in respect of the year ended 31 December 2007 was 15.1p per share.

An interim dividend of 5.5p per share in respect of the year ending 31 December 2008, payable on 10 October 2008 to equity shareholders of the parent company registered at the close of business on 12 September 2008, the dividend record date, was approved by the Directors after 30 June 2008. The resulting interim dividend of £5.8m has not been provided in these financial statements.

The following summarises dividend per share information in respect of the year ended 31 December 2007 and the year ending 31 December 2008:

	2008	2007
Interim dividend	5.5p	5.25p
Final dividend		9.85p
Total for the year		15.10p

4. Investment income, net policyholder claims and benefits incurred, net changes in investment contract liabilities and total expenses

Investment income for the six months ended 30 June 2008 is stated after taking into account unrealised investment losses of approximately £168m arising as a result of global investment market falls. This has had the effect of generating negative total revenue (net of reinsurance payable) and negative net income. As this amount arises principally within policyholder unit-linked funds there is a corresponding decrease in net policyholder claims and benefits incurred and in the net change in investment contract liabilities, such that these amounts are reflected as net credits to the income statement, giving rise to negative total expenses for the six months ended 30 June 2008.

5. Loans and Receivables / Other Payables

Included in loans and receivables and other payables as at 30 June 2007 are amounts of £30,071,000 and £109,745,000 respectively, which resulted from a change in investment policy whereby the Group repositioned a significant portion of its financial assets portfolio. These amounts were subsequently settled for cash.

6. Borrowings

	Unaudited 30 June		31 December
	2008 £000	2007 £000	2007 £000
Bank Loan	8,326	12,425	12,469

The bank loan, which was drawn down on 2 June 2005 under a facility made available on 4 May 2005, is unsecured and is repayable in five equal annual amounts on the anniversary of the draw-down date. The outstanding principal on the loan bears interest at a rate based on the London Inter-bank Offer Rate and is payable in arrears over a period which varies between one and six months at the option of the borrower.

The fair value of the bank loan at 30 June 2008 was £8,400,000 (30 June 2007 and 31 December 2007: £12,600,000).

7. Forward-looking statements

This document may contain forward-looking statements with respect to certain of the plans and current expectations relating to future financial condition, business performance and results of Chesnara plc. By their nature, all forward-looking statements involve risk and uncertainty because they relate to future events and

circumstances that are beyond the control of Chesnara plc including, amongst other things, UK domestic and global economic and business conditions, market-related risks such as fluctuations in interest rates, inflation, deflation, the impact of competition, changes in customer preferences, delays in implementing proposals, the timing, impact and other uncertainties of future acquisitions or other combinations within relevant industries, the policies and actions of regulatory authorities, the impact of tax or other legislation and other regulations in the jurisdiction in which Chesnara plc and its subsidiaries operate. As a result, Chesnara plc's actual future condition, business performance and results may differ materially from the plans, goals and expectations expressed or implied in these forward-looking statements.

8. Approval of condensed consolidated report for the six months ended 30 June 2008

This condensed consolidated report was approved by the Board of Directors on 28 August 2008. A copy of the report will be available to the public at the company's registered office, Harbour House, Portway, Preston PR2 2PR, UK and at www.chesnara.co.uk.

Supplementary Information – European Embedded Value Basis

Summarised Consolidated Interim Income Statement for the six months ended 30 June 2008

		Unaudited Six months ended 30 June		Year ended 31 December
		2008	2007	2007
	Note	£000	£000	£000
Operating (loss) / profit of covered business	6	(5,334)	6,498	9,678
Other operational result		665	(549)	(16)
Operating (loss) / profit		(4,669)	5,949	9,662
Variation from longer-term investment return		428	(571)	824
Effect of economic assumption changes		(950)	5,697	(4,043)
(Loss) / profit before tax		(5,191)	11,075	6,443
Tax		7,226	(3,350)	5,674
Profit for the period		2,035	7,725	12,117
Earnings per share				
Based on profit for the period		1.95p	7.39p	11.59p
Diluted earnings per share				
Based on profit for the period		1.95p	7.39p	11.59p

Supplementary Information – European Embedded Value Basis

Summarised Consolidated Interim Balance Sheet as at 30 June 2008

		Unaudited 30 June		31 December
	Note	2008 £000	2007 £000	2007 £000
Assets				
Value of in force business	5,8	85,939	105,607	94,007
Reinsurers' share of insurance contract provisions		177,575	186,853	187,486
Amounts deposited with reinsurers		24,039	61,230	26,702
Investment properties		3,673	19,935	4,983
Deferred tax assets		82	122	88
Financial assets				
Equity securities at fair value through income		443,155	850,876	743,670
Holdings in collective investment schemes at fair value through income		634,228	411,083	508,857
Debt securities at fair value through income		247,457	312,775	247,152
Loans and receivables including insurance receivables		13,277	49,847	15,415
Derivative financial instruments		8,338	25,610	9,525
Total financial assets		<u>1,346,455</u>	<u>1,650,191</u>	<u>1,524,619</u>
Reinsurers' share of accrued policy claims		4,356	5,631	4,660
Income taxes		-	153	-
Cash and cash equivalents		244,810	247,802	225,127
Total assets		<u>1,886,929</u>	<u>2,277,524</u>	<u>2,067,672</u>
Liabilities				
Bank Overdrafts		1,506	-	1,229
Insurance contract provisions		989,974	1,111,109	1,086,581
Financial liabilities				
Investment contracts at fair value through income		666,811	816,535	744,222
Borrowings		8,326	12,425	12,469
Derivative financial instruments		2,474	367	265
Total financial liabilities		<u>677,611</u>	<u>829,327</u>	<u>756,956</u>
Provisions		3,494	537	3,575
Reinsurance payables		1,942	2,192	1,622
Payables related to direct insurance and investment contracts		24,023	25,974	22,859
Income taxes		2,643	4,626	743
Other payables		6,688	115,345	6,792
Total liabilities		<u>1,707,881</u>	<u>2,089,110</u>	<u>1,880,357</u>
Net assets		<u>179,048</u>	<u>188,414</u>	<u>187,315</u>
Shareholders' equity				
Share capital		41,501	41,501	41,501
Share premium		20,458	20,458	20,458
Other reserves		50	50	50
Retained earnings		117,039	126,405	125,306
Total shareholders' equity	5,8	<u>179,048</u>	<u>188,414</u>	<u>187,315</u>

Supplementary Information – European Embedded Value Basis

Summarised Consolidated Interim Statement of Changes in Equity for the six months ended 30 June 2008

	Unaudited Six months ended 30 June		Year Ended 31 December
	2008 £000	2007 £000	2007 £000
Shareholders' equity at 1 January	187,315	189,108	189,108
Profit for the period representing total recognised income and expense	2,035	7,725	12,117
Dividends paid	(10,302)	(8,419)	(13,910)
Shareholders' equity at 30 June/31 December	179,048	188,414	187,315

Supplementary Information – European Embedded Value Basis

Notes to the Supplementary Information (unaudited)

1. Basis of presentation

This section sets out the detailed methodology followed for producing this Group financial information which is supplementary to the Group's primary financial statements which have been prepared using accounting policies consistent with International Financial Reporting Standards ('IFRS') and in accordance with International Accounting Standard 34 as adopted by the EU.. This financial information has been prepared in accordance with the European Embedded Value ('EEV') principles issued in May 2004 by the European CFO Forum and supplemented by Additional Guidance on EEV Disclosures issued by the same body in October 2005. The principles provide a framework intended to improve comparability and transparency in embedded value reporting across Europe.

2. Covered business

The Group uses EEV methodology to value its individual life assurance, pension and annuity business, which has been written, with only insignificant exceptions, in the UK ('covered business'). This business comprises the Group's long-term business operations, being those contracts falling under the definition of long-term insurance business for UK regulatory purposes.

The Group has no business activities other than those relating to the covered business. In particular, the operating activities of the holding company, Chesnara plc, are treated as an integral part of the covered business. Under EEV principles no distinction is made between insurance and investment contracts, as there is under IFRS, which accords these classes of contracts different accounting treatments.

3. Methodology

a) Embedded Value

Overview

Shareholders' equity comprises the embedded value of the covered business, together with the net equity of other Group companies, including that of the holding company which is stated after writing down fully the carrying value of the covered business.

The embedded value of the covered business is the aggregate of the shareholder net worth ('SNW') and the present value of future shareholder cash flows from in-force covered business (value of in-force business) less any deduction for the cost of required capital. It is stated after allowance has been made for aggregate risks in the business. SNW comprises those amounts in the long-term business, which are either regarded as required capital or which represent surplus assets within that business.

New business

Much of the covered business is in run-off and is, accordingly, substantially closed to new business. The Group does still sell guaranteed bonds but, overall, the contribution from new business to the results established using EEV methodology is not material. Accordingly, not all of those items related to new business values, which are recommended by the EEV guidelines, are reported in this supplementary financial information.

Value of in-force business

The cash flows attributable to shareholders arising from in-force business are projected using best estimate assumptions for each component of cash flow.

The present value of the projected cash flows is established by using a discount rate which reflects the time value of money and the risks associated with the cash flows which are not otherwise allowed for. There is a deduction for the cost of holding the required capital, as set out below.

Taxation

The present value of the projected cash flows arising from in-force business takes into account all tax which is expected to be paid under current legislation, including tax which would arise if surplus assets within the covered business were eventually to be distributed.

The value of the in-force business has been calculated on an after-tax basis and is grossed up to the pre-tax level for presentation in the income statement. The amount used for the grossing up is the amount of shareholder tax payable in the policyholder fund plus any direct tax charge within the shareholder fund.

Cost of capital

The cost of holding the required capital to support the covered business (see 3b below) is reflected as a deduction from the value of in-force business and is determined as the difference between the amount of the required capital and the projected release of capital and investment income.

Financial options and guarantees

The principal financial options and guarantees are (i) guaranteed annuity rates offered on some unit-linked pension contracts and (ii) a guarantee offered under Timed Investment Funds that the unit price available at the selected maturity date (or at death, if earlier) will be the highest price attained over the policy's life. The cost of these options and guarantees has been assessed, in principle, on a market-consistent basis, but, in practice, this has been carried out on approximate bases, which are appropriate to the level of materiality of the results.

Allowance for risk

Allowance for risk within the covered business is made by:

- 1) Setting required capital levels by reference to the Directors' assessment of capital needs;
- 2) Setting the risk discount rate, which is applied to the projected cash flows arising on the in-force business, at a level which includes an appropriate risk margin; and
- 3) Explicit allowance for the cost of financial options and guarantees and, where appropriate, for reinsurer default.

b) Level of Required Capital

The level of required capital of the covered business reflects the amount of capital that the Directors consider necessary and appropriate to manage the business. In forming their policy the Directors have regard to the minimum statutory requirements and an internal assessment of the market, insurance and operational risks inherent in the underlying products and business operations. The capital requirement resulting from this assessment represents 150% of the long-term insurance capital requirement ('LTICR') together with 100% of the resilience capital requirement ('RCR'), as set out in FSA regulations.

The required capital is provided by the retained surplus in the long-term business fund and the retained earnings and issued share capital in the shareholder fund.

c) Risk Discount Rate

The risk discount rate ('RDR') is a combination of the risk-free rate and a risk margin. The risk-free rate reflects the time value of money and the risk margin reflects any residual risks inherent in the covered business and makes allowance for the risk that future experience will differ from that assumed. In order to reduce the subjectivity when setting the RDR, the Board has decided to adopt a 'bottom up' market-consistent approach to allow explicitly for market risk.

Using the market-consistent approach each cash flow is valued at a discount rate consistent with that used in the capital markets: in accordance with this, equity-based cash flows are discounted at an equity RDR and bond-based cash flows at a bond RDR. In practice a short-cut method known as the 'certainty equivalent' approach has been adopted. This method assumes that all cash flows earn the risk-free rate of return and are discounted at the risk-free rate. In general, and consistent with the market's approach to valuing financial instruments for hedging purposes, the risk-free rate is based on swap yields. Where, however, non-linked business is substantially backed by government bonds, the yields on these assets have been taken.

Within the risk margin, allowance also needs to be made for non-market risks. For some of these risks, e.g. mortality and expense risk, it is assumed that the shareholder can diversify away any uncertainty where the impact of variations in experience on future cash flows is symmetrical. For those risks that are assumed to be diversifiable no adjustment to the risk margin has been made. For any remaining risks that are considered to be non-diversifiable risks there is no risk premium observable in the market and therefore a constant margin of 50 basis points has been added to the risk margin. The RDR is determined by equating the results from the traditional embedded value approach, including the assumed actual investment returns and traditional cost of capital, to that derived using the market-consistent method, this process being known as calibration of the RDR. The risk margin is then the difference between the derived RDR and the risk-free rate. The selection of the assumed actual investment returns and the reported cost of capital will have no impact on the reported result, as changes in these produce corresponding changes in the RDR.

A market-consistent valuation approach also generally requires consideration of 'frictional' costs of holding shareholder capital: in particular, the cost of tax on investment returns and the impact of investment management fees can reduce the face value of shareholder funds. In the Group's case, the expenses relating to corporate governance functions eliminate any taxable investment return in shareholder funds, while investment management fees are not material.

The risk margin established on the basis set out above is normally calculated at each financial year-end. At interim periods, the discount rate normally remains consistent with the investment return assumptions. The margin over investment return assumptions is, however, reassessed if market conditions change significantly.

d) Analysis of Profit

The contribution to operating profit, which is identified at a level which reflects an assumed longer-term level of investment return, arises from three sources:

- (i) New business;
- (ii) Return from in-force business; and
- (iii) Return from shareholder net worth.

Additional contributions to profit arise from:

- (i) Variances between the actual investment return in the period and the assumed long-term investment return; and
- (ii) The effect of economic assumption changes.

The contribution from new business represents the value recognised at the end of each period in respect of new business written in that period, after allowing for the cost of acquiring the business, the cost of establishing the required technical provisions and after making allowance for the cost of capital.

The return from in-force business is calculated using closing assumptions and comprises:

- (i) The expected return, being the unwind of the discount rate over the period applied to establish the value of in-force business, at the beginning of the period;
- (ii) Variances between the actual experience over the period and the assumptions made to establish the value of business in force at the beginning of the period; and
- (iii) The net effect of changes in future assumptions, made prospectively at the end of the period, from those used in establishing the value of business in-force at the beginning of the period, other than changes in economic assumptions.

The contribution from shareholder net worth comprises the actual investment return on residual assets in excess of the required capital.

e) Assumption Setting

There is a requirement under EEV methodology to use best estimate demographic assumptions and to review these at least annually with the economic assumptions being determined at each reporting date. The current practice is detailed below.

Each year the demographic assumptions are reviewed as part of year-end processing and hence were last reviewed in December 2007. For mid-year reporting, the previous year-end assumptions are usually considered in light of recent experience, particularly persistency, to ensure robustness, but are not necessarily expected to change.

The detailed projection assumptions, including mortality, morbidity, persistency and expenses reflect recent operating experience. Allowance is made for future improvement in annuitant mortality based on experience and externally published data. Favourable changes in operating experience, particularly in relation to expenses and persistency, are not anticipated until the improvement in experience has been observed. Holding company expenses (for the Chesnara Group such expenses relate largely to listed company functions) are allocated to the covered business as the whole business of the Chesnara Group is the transaction of life assurance business through the subsidiary companies. Hence the expense assumptions used for the cash flow projections include the full cost of servicing this business.

The economic assumptions are reviewed and updated at each reporting date based on underlying investment conditions at the reporting date. The assumed discount rate and inflation rates are consistent with the investment return assumptions.

In addition, the demographic assumptions used at December 2007 are considered to be best estimate and, consequently, no further adjustments are required. The assumptions required in the calculation of the value of the annuity rate guarantee on pension business have been set equal to best-estimate assumptions.

4. Assumptions

a) Investment Returns (pre tax)

The assumed future pre-tax returns on fixed interest and RPI linked securities are set by reference to redemption yields available in the market at the end of the reporting period. The corresponding return on equities and property is equal to the fixed interest gilt assumptions plus an appropriate risk margin; for equities, the return is split between franked income and capital gains based on current dividend yield. For linked business the aggregate return has been determined by reference to the benchmark asset mix within the Managed Funds.

	30 June		31 December
	2008	2007	2007
Equity risk premium	2.7%	2.7%	2.7%
Property risk premium	2.7%	2.7%	2.7%
Investment return			
Fixed Interest	5.2%	5.3%	4.6%
Equities	7.9%	8.0%	7.3%
Property	7.9%	8.0%	7.3%
UK equities dividend yield	4.1%	2.8%	3.0%
Inflation			
RPI	3.9%	3.2%	3.1%

b) Actuarial Assumptions

The demographic assumptions used to determine the value of the in-force business have been set at levels commensurate with the underlying operating experience identified in the periodic actuarial investigations.

c) Taxation

Projected tax has been determined assuming current tax legislation and rates continue unaltered, except where future tax rates or practices have been announced.

d) Expenses

The expense levels are based on internal expense analysis investigations and are appropriately allocated to the new business and policy maintenance functions. These have been determined by reference to:

- i) The outsourcing agreements in place with our third-party business process administrators;
- ii) Anticipated revisions to the terms of such agreements as they fall due for renewal; and
- iii) Corporate governance costs relating to the covered business.

The expense assumptions also include the expected future holding company expenses which will be recharged to the covered business.

No allowance has been made for future productivity improvements in the expense assumptions.

e) Risk Discount Rate

The risk-free rate is set by reference to the sterling mid swap rates available in the market at the end of the reporting period. Where, however, non-linked business is substantially backed by government bonds, the yields on these assets have been used.

An explicit constant margin of 50 basis points is added to the risk-free rate to cover any remaining risks that are considered to be non-market, non-diversifiable risks, as there is no risk premium observable in the market. This margin gives due recognition to the fact that:

- i) The covered business is substantially closed to new business;
- ii) There is no significant exposure in the with-profits business, which is wholly reassured;
- iii) Expense risk is limited as a result of the outsourcing of substantially all policy administration functions to third-party business process administrators; and
- iv) For much of the Life business the Group has the ability to vary risk charges made to policyholders.

	30 June		31 December
	2008	2007	2007
Risk-free rate	5.6%	5.6%	5.0%
Non-diversifiable risk	0.5%	0.5%	0.5%
Risk margin	2.2%	0.7%	2.2%
Risk discount rate	8.3%	6.8%	7.7%

The risk margin is derived as a result of the calibration of the RDR, as explained in Note 3c above. The significant increase from 30 June 2007 to 31 December 2007 and 30 June 2008 reflects a change in the projected long-term tax position of the covered business. As at 30 June 2007, there were differences in the projected tax basis and, hence, in the absolute level of projected tax as between the market-consistent approach and the traditional embedded value approach: these differences were, effectively, eliminated by the calibration process and this resulted in an apparently lower level of derived risk margin. As at 31 December 2007 and 30 June 2008, the projected tax position between the two approaches is consistent so that there are no differences which are eliminated by the calibration process and this results in a higher level of derived risk margin.

5 Analysis of shareholders' equity

	30 June		31 December
	2008	2007	2007
	£000	£000	£000
Covered business			
Required capital	36,962	42,314	39,149
Free surplus	20,104	34,748	38,483
Shareholder net worth	57,066	77,062	77,632
Value of in-force business	85,939	105,607	94,007
Embedded value of covered business	143,005	182,669	171,639
Less: amount financed by borrowings	(8,326)	(12,600)	(12,469)
Embedded value of covered business attributable to shareholders	134,679	170,069	159,170
Net equity of other Group companies	44,369	18,345	28,145
Total shareholders' equity	179,048	188,414	187,315
The movement in the value of in-force business comprises:			
Value at beginning of period	94,007	109,941	109,941
Amount charged to operating profit	(8,068)	(4,334)	(15,934)
Value at end of period	85,939	105,607	94,007

On 2 June 2005, the Group drew down £21m on a bank loan facility, in order to part fund the acquisition of CWA Life Holdings plc. This effectively represented, by way of debt finance, a purchase of part of the underlying value in force within that company, which was subsequently transferred to Countrywide Assured plc on 30 June 2006 under the provisions of Part VII of the Financial Services and Markets Act 2000. It follows that the embedded value of the covered business is not attributable to equity shareholders of the Group to the extent of the outstanding balance on the loan account at each balance sheet date. The loan is repayable in five equal annual instalments on the anniversary of the draw-down date, the funds for the repayment effectively being provided by way of the realisation of the underlying value of in-force business of the covered business. In accordance with this, a further £4.2m of the loan was repaid on 2 June 2008, leaving principal outstanding at that date of £8.4m.

6. Analysis of profit of covered business

	Six months ended 30 June		Year Ended 31 December
	2008	2007	2007
	£000	£000	£000
New business contribution	549	615	1,261
Return from in-force business			
Expected return	5,389	5,217	10,206
Experience variances	(9,894)	4,092	394
Operating assumption changes	-	(4,242)	(4,236)
Return on shareholder net worth	(1,378)	816	2,053
Operating profit	(5,334)	6,498	9,678
Variation from longer-term investment return	428	(571)	824
Effect of economic assumption changes	(950)	5,697	(4,043)
Profit before tax	(5,856)	11,624	6,459
Tax	7,232	(3,350)	5,677
Profit after tax	1,376	8,274	12,136

The profit of covered business varies from amounts presented in the summarised consolidated income statement in respect of the pre-tax result of the holding company presented as 'other operational result', and in respect of any tax pertaining thereto, which is included in 'other tax'.

Experience variances for the six months ended 30 June 2008 reflect the impact of significant adverse global investment market conditions over that period. There has been a significant reduction in the estimate of future tax payable, as this is dependent, to a significant extent, on the associated projection of investment returns and franked investment income.

7. Sensitivities to alternative assumptions

The following table shows the sensitivity of the embedded value of the covered business at relevant period end dates to variations in the assumptions adopted in the calculation of the embedded value. Sensitivity analysis is not provided in respect of the new business contribution for the six months ended 30 June 2008 as the reported level of new business contribution is not considered to be material (see Note 3(a) above). It largely relates to guaranteed bond business, where a close asset/liability matching approach leaves values largely insensitive to changes in experience.

	30 June		31 December
	2008	2007	2007
	£143.0m	£182.7m	£171.6m
Embedded Value ('EV') of covered business			
Change in EV	£m	£m	£m
Economic sensitivities			
100 basis point increase in risk discount rate	(4.8)	(5.1)	(4.7)
100 basis point reduction in yield curve	2.2	(3.3)	2.9
10% decrease in equity and property values	(5.1)	(2.8)	(5.2)
Operating sensitivities			
10% decrease in maintenance expenses	2.2	2.4	1.9
10% decrease in lapse rates	3.6	3.3	3.7
5% decrease in mortality/morbidity rates			
Assurances	1.6	2.0	1.8
Annuities	(0.8)	(0.5)	(0.8)
Reduction in the required capital to statutory minimum	1.9	0.8	1.8

The key assumption changes represented by each of these sensitivities are as follows:

Economic sensitivities

- 100 basis point increase in the risk discount rate. The 8.3% RDR increases to 9.3%;
- 100 basis point reduction in the yield curve. The fixed interest return is reduced by 1% and the equity/property returns are also reduced by 1%, thus maintaining constant equity/property risk premiums. The rate of future inflation has also been reduced by 1% so that real yields remain constant. In addition the risk discount rate has also reduced by 1%; and

- iii) 10% decrease in the equity and property values. This gives rise to a situation where, for example, a Managed Fund unit liability with a 60% equity holding would reduce by 6% in value.

Operating sensitivities

- i) 10% decrease in maintenance expenses, giving rise to, for example, a base assumption of £20 per policy pa reducing to £18 per policy pa;
- ii) 10% decrease in persistency rates giving rise to, for example, a base assumption of 10% of policy base lapsing pa reducing to 9% pa;
- iii) 5% decrease in mortality/morbidity rates giving rise to, for example, a base assumption of 100% of the parameters in a selected mortality/morbidity table reducing to 95% of the parameters in the same table; and
- iv) The sensitivity to the reduction in the required capital to the statutory minimum shows the effect of reducing the required capital from 150% of the LTICR plus 100% RCR to the amounts of 100% LTICR plus 100% RCR, being the minimum requirement prescribed by FSA regulation.

In each sensitivity calculation all other assumptions remain unchanged except where they are directly affected by the revised economic conditions: for example, as stated, changes in interest rates will directly affect the risk discount rate.

The sensitivities to changes in the assumptions in the opposite direction will result in changes of similar magnitude to those shown in the above table but in the opposite direction.

8. Reconciliation of shareholders' equity on the IFRS basis to shareholder equity on the EEV basis

	30 June		31 December
	2008	2007	2007
	£000	£000	£000
Shareholders' equity on the IFRS basis	123,542	115,956	125,784
Adjustments			
Deferred acquisition costs			
Investment contracts	(8,595)	(9,488)	(8,961)
Deferred income	14,674	16,309	15,426
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	(17,248)	(18,393)	(18,220)
Adjustments to provisions on insurance contracts, net of reinsurers' share	(294)	(664)	(600)
Acquired in-force value	(22,386)	(24,544)	(23,785)
Deferred tax	3,416	3,631	3,664
Group shareholder net worth	93,109	82,807	93,308
Value of in-force business	85,939	105,607	94,007
Shareholders' equity on the EEV basis	179,048	188,414	187,315

Group shareholder net worth comprises:

Shareholder net worth in covered business	57,066	77,062	77,632
Shareholder's equity in other Group companies	44,369	18,345	28,145
Debt finance	(8,326)	(12,600)	(12,469)
Total	93,109	82,807	93,308

Independent review report by KPMG Audit Plc to Chesnara plc

Introduction

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2008, which comprises the Condensed Consolidated Income Statement, the Condensed Consolidated Balance Sheet, the Condensed Consolidated Statement of Cash Flows, the Condensed Consolidated Statement of Changes in Equity and the related explanatory notes and to review the European Embedded Value Basis Supplementary Information for the six months ended 30 June 2008 which comprises the Summarised Consolidated Interim Income Statement, the Summarised Consolidated Interim Balance Sheet, the Summarised Consolidated Interim Statement of Changes in Equity and the related explanatory notes ("the Supplementary Information").

We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements or the Supplementary Information.

This report is made solely to the Company in accordance with the terms of our engagement to assist the Company in meeting the requirements of the Disclosure and Transparency Rules ("the DTR") of the UK's Financial Services Authority ("the UK FSA") and also to provide a review conclusion to the Company on the Supplementary Information. Our review of the condensed set of financial statements has been undertaken so that we might state to the Company those matters we are required to state to it in this report and for no other purpose. Our review of the Supplementary Information has been undertaken so that we might state to the Company those matters we have been engaged to state in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our review work, for this report, or for the conclusions we have reached.

Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the DTR of the UK FSA. The directors have accepted responsibility for preparing the Supplementary Information contained in the half-yearly financial report in accordance with the European Embedded Value Principles issued in May 2004 by the European CFO Forum and supplemented by the Additional Guidance on European Embedded Value Disclosures issued in October 2005 (together the 'EEV Principles') and for determining the methodology and assumptions used in the application of those principles.

As disclosed in Note 1 to the Condensed Consolidated Financial Statements, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the EU. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with IAS 34 *Interim Financial Reporting* as adopted by the EU.

The Supplementary Information has been prepared in accordance with the EEV Principles, using the methodology and assumptions set out in Notes 3 to 4 to the Supplementary Information. The Supplementary Information should be read in conjunction with the Group's condensed set of financial statements which are set out on pages 15 to 21.

Our responsibility

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

Scope of review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2008 is not prepared, in all material respects, in accordance with IAS 34 as adopted by the EU and the DTR of the UK FSA.

Based on our review, nothing has come to our attention that causes us to believe that the Supplementary Information for the six months ended 30 June 2008 is not prepared, in all material respects, in accordance with the EEV Principles, using the methodology and assumptions set out in notes 3 to 4 to the Supplementary Information.

KPMG Audit Plc
Chartered Accountants
St James Square
Manchester M2 6DS

28 August 2008