



Chesnara plc

Condensed Consolidated Financial Statements
for the Six Months Ended
30 June 2010

Financial Calendar

26 August 2010.....	Interim results for the six months ended 30 June 2010 announced
8 September 2010.....	Ex dividend date
10 September 2010.....	Dividend record date
12 October 2010.....	Dividend payment date
19 November 2010.....	Interim Management Statement for the quarter ending 30 September 2010
March 2011	Results for the year ending 31 December 2010 announced

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, Swedish 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 jurisdictions 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.

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	Page
Condensed Consolidated Financial Statements for the six months ended 30 June 2010	
Financial Highlights	4
Chairman's Statement.....	5
Directors' Information.....	7
Interim Management Report	8
Directors' Responsibility Statement in respect of the Half Yearly Financial Report.....	23
Independent Auditor's Review Report to the Members of Chesnara plc in respect of the Half Yearly Financial Report	24
Condensed Consolidated Statement of Comprehensive Income (unaudited).....	25
Condensed Consolidated Balance Sheet (unaudited)	26
Condensed Consolidated Statement of Cash Flows (unaudited).....	27
Condensed Consolidated Statement of Changes in Equity (unaudited)	28
Notes to the Condensed Consolidated Financial Statements (unaudited).....	29
Statement of Directors' Responsibilities in respect of the EEV Basis Supplementary Information ..	40
Independent Auditor's Review Report to the Directors of Chesnara plc on the EEV Basis Supplementary Information	41
Supplementary Information – European Embedded Value Basis (unaudited).....	42
Notes to the Supplementary Information (unaudited)	44

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 UK operating subsidiary, Countrywide Assured plc, in which the whole of the UK-based 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 this transfer.

This document refers throughout to the 'UK Business' and the 'Swedish Business'. As explained in Note 5 to these Condensed Consolidated financial statements, these are the business segments of the Group, comprising, for the UK Business, Countrywide Assured Life Holdings Limited and its subsidiary companies and, for the Swedish Business, Moderna Försäkringar Liv AB ('Moderna') and its subsidiary and associated companies.

Condensed Consolidated Financial Statements for the six months ended 30 June 2010

Financial Highlights

	Unaudited Six months ended 30 June		Year ended 31 December
	2010	2009	2009
IFRS basis			
Operating profit/(loss)			
UK Business	16.8	11.6	24.7
Swedish Business	(4.3)	–	(2.1)
Other group activities	(0.7)	(0.3)	(2.3)
Profit arising on business combinations	0.9	–	25.1
	<u>12.7</u>	<u>11.3</u>	<u>45.4</u>
Financing costs	(0.7)	(0.1)	(0.7)
Profit before tax	<u>£12.0m</u>	<u>£11.2m</u>	<u>£44.7m</u>
Basic earnings per share	7.71p	8.17p	45.26p
Dividend per share	5.80p	5.65p	15.95p
Shareholders' net equity	<u>£156.8m</u>	<u>£124.5m</u>	<u>£159.8m</u>
European Embedded Value basis (EEV)			
Operating (loss)/profit			
UK Business	10.0	10.1	22.0
Swedish Business	(16.5)	–	(2.9)
Other group activities	(0.8)	0.1	0.9
	<u>(7.3)</u>	<u>10.2</u>	<u>20.0</u>
Investment variances and economic assumption changes			
UK Business	(4.9)	(2.4)	(6.1)
Swedish Business	7.2	–	10.1
(Loss)/profit before tax and before exceptional items	<u>(5.0)</u>	<u>7.8</u>	<u>24.0</u>
Exceptional items			
Profit recognised on business combinations	0.9	–	54.2
Effect of modelling improvements	10.4	–	–
	<u>6.3</u>	<u>7.8</u>	<u>78.2</u>
Profit before tax	<u>6.3</u>	<u>7.8</u>	<u>78.2</u>
Tax	(2.4)	(1.4)	12.1
Profit for the period	<u>£3.9m</u>	<u>£6.4m</u>	<u>£90.3m</u>
Shareholders' equity on EEV basis			
Embedded value			
UK Business	132.1	135.2	157.8
Swedish Business	93.7	–	91.5
	<u>225.8</u>	<u>135.2</u>	<u>249.3</u>
Embedded value of covered business	225.8	135.2	249.3
Acquired embedded value financed by debt	–	(4.2)	(4.2)
Shareholders' equity in other Group companies	29.3	47.9	17.5
	<u>£255.1m</u>	<u>£178.9m</u>	<u>£262.6m</u>
EEV per share	251.3p	176.3p	258.7p
UK business			
Life annual premium income (AP)	£40.2m	£43.5m	£85.5m
Life single premium income (SP)	£12.3m	£13.2m	£23.3m
Life annualised premium income (AP + 1/10 SP)	£41.4m	£44.8m	£87.8m
Swedish business			
New business premium income (AP + 1/10 SP)	£33.1m	–	£49.9m
Total premium income (AP + SP)	£138.2m	–	£269.4m

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 shareholders' equity. Accordingly, the EEV result recognises, within profit, the movement in this component.

The Swedish Business was acquired on 23 July 2009. Accordingly, certain of the premium income amounts shown above relate to the pre-acquisition period and are presented here for illustrative purposes.

I am pleased to present the seventh interim financial statements of Chesnara plc ('Chesnara'). In the light of continuing economic uncertainty and investment market volatility, it is pleasing that our results continue to show a high degree of resilience, allowing us to maintain a reliable and progressive dividend policy, while being in a good position to pursue further value-enhancing acquisitions as they arise.

Review of the Business

Global investment market volatility continues to have a significant impact on the Group's results, with the leading UK market indices, for example, posting gains of 5% in the first quarter rising to 8% by mid-April, only to fall back sharply to levels at the end of June which represented a 9% reduction from the prior year-end closing position. In addition, a reduction in swap yields, which are used to both set the rate of investment return and the discount rate for future cash flows, together with little corresponding changes in market values of our fixed interest securities and future inflation expectations, also gave rise to negative influences. On a more positive note, we completed the acquisition of the business of Aspis Försäkrings Liv AB ('Aspis') in Sweden and thereby acquired the capability to write significantly higher volumes of Risk and Health business which represents an excellent strategic fit with the existing Swedish Pensions and Savings business.

On the IFRS basis, we have posted a pre-tax profit of £12.0m for the half-year ended 30 June 2010 compared with £11.2m for the corresponding period in 2009. The UK Business generated a pre-tax profit of £16.8m arising from the continuing strong emergence of surplus from its run off book, enhanced by the release of a claims reserve of some £3.2m. The Swedish Business posted a loss before tax of £4.1m: overall this is in line with expectations as the business builds scale. However, competition for transfer business and subdued investment sales have inhibited progress, this being partially offset by gains arising from the Aspis acquisition.

On the EEV basis of reporting we have posted a pre-tax profit of £6.3m compared with £7.8m for the corresponding period in 2009. The UK Business benefited from favourable lapse and mortality experience which gave rise to a pre-tax increase of £3.9m in embedded value. The result was further enhanced by £3.2m in respect of the release to income of certain claims liabilities as mentioned above. These favourable effects were offset by adverse investment market impacts of some £6.0m, so that the net pre-tax result at £5.1m is close to management expectations.

The Swedish Business contributed £2.0m to the pre-tax EEV profit. This primarily resulted from adjustments to expense and transfer rate assumptions amounting to some £11m adverse, countered by the positive effects resulting from refinements to modelling systems, which together with profit arising from the acquisition of Aspis amounted to £11.3m, the balance being generated from the core trading result.

Shareholder Value and Returns to Shareholders

Total shareholder equity on the EEV basis, pre appropriation of the proposed interim dividend, is £255.1m (251.3p per share) compared with £262.6m (258.7p per share) as at 31 December 2009. As mentioned earlier this demonstrates the resilience of the business in a difficult economic, trading and investment environment.

The capacity of the Group to pursue its dividend policy relies on the continuing emergence of surplus in the UK Business and in the ability to distribute that surplus which, in turn, depends on the regulatory solvency position of Countrywide Assured plc ('CA plc'), the principal operating subsidiary of the UK Business. I am pleased to report that CA plc's solvency ratio, post proposed dividends, at 263% (197% as at 31 December 2009) remains in excess of the target of 150% set by the CA plc Board.

The Group's dividend policy now has to take account of the competing need for funds of the developing Swedish Business which, in turn, depends on the underlying regulatory solvency ratio of the Swedish Life Business. This was 220% as at 30 June 2010 which is comfortably in excess of the target of 150% set by the Moderna Board. The combined Group post dividend solvency ratio remains at a healthy 330% as at 30 June 2010 (31 December 2009: 316%).

Based on the strength of our results and of our capital solvency ratios, the Board has decided to declare an interim dividend of 5.8p per share (2009 interim dividend: 5.65p per share) which represents a 2.65% increase and equates to a total dividend payable to shareholders of £5.9m.

Outlook

In line with our primary aim of delivering an attractive and reliable dividend yield, we remain focused on the efficient management of our businesses.

Whilst Group performance has been relatively robust through the economic crisis and, indeed it was the catalyst which generated the value-enhancing acquisition of Moderna, the ongoing effects still bring challenges to our businesses. Macroeconomic and industry-related factors will continue to challenge the Group and, provided we can continue to navigate a successful path through these areas, the short- to medium-term outlook is positive for the ongoing emergence of surplus and, accordingly, for dividend support.

We continue to see a reasonable flow of potential acquisition opportunities and, as demonstrated with the Moderna and Aspis transactions, we will readily progress these where we see value and a clear strategic fit. We remain open-minded as to location in the UK and Western Europe, and will continue to apply strict financial and risk criteria in assessing them.

Peter Mason

Chairman

25 August 2010

Peter Mason was the Senior Independent Non-executive Director of Chesnara plc and Chairman of the Audit Committee during 2008. He was appointed as Chairman of Chesnara plc and Chairman of the Nomination Committee on 1 January 2009. He was re-appointed as a member of the Remuneration and Audit Committees with effect from 22 December 2009 and was appointed as Chairman of Moderna Försäkringar Liv AB with effect from 23 July 2009. He is currently a Non-executive Director of Homeowners Friendly Society and 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.

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. He was appointed as a Non-executive Director of Moderna Försäkringar Liv AB and as Chairman of Moderna Fonder & Analys AB with effect from 23 July 2009. 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 27 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 26 years' experience in the life assurance industry gained with Royal Life, Norwich Union and CMG.

Mike Gordon is an Independent Non-executive Director of Chesnara plc and is Chairman of the Remuneration Committee. He was appointed as Senior Independent Non-executive Director of Chesnara plc on 1 January 2009. He also serves on the Audit Committee and the Nomination Committee and was appointed as a Non-executive Director of Moderna Försäkringar Liv AB with effect from 23 July 2009. He spent 12 years as Group Sales Director of Skandia Life Assurance Holdings.

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.

Peter Wright is an Independent Non-executive Director who was appointed to the Chesnara plc Board on 1 January 2009. At the same date he was appointed as Chairman of the Audit Committee and as a member of the Remuneration Committee. He was appointed as a member of the Nomination Committee with effect from 9 July 2009. He retired as a Principal of Towers Perrin on 1 January 2008 and is a former Vice President of the Institute of Actuaries, having been admitted as a Fellow in 1979.

Interim Management Report

Background

Chesnara continues to seek to acquire life assurance and pensions businesses in the UK and Western Europe. When the Company was listed on the London Stock Exchange in 2004, we acquired Countrywide Assured plc ('CA') on its demerger from Countrywide plc. In 2005 we acquired City of Westminster Assurance Company Limited ('CWA') from Irish Life and Permanent plc and in 2006 we merged the long-term business of the two companies. In early 2009, following a period where valuations had increased to unattractive levels following which significant uncertainty arose due to the disruption in financial markets, we acquired an open Swedish life assurance and pensions company – Moderna Försäkringar Liv AB ('Moderna') – at a very attractive discount to its embedded value. The acquisition was completed in July 2009. In December 2009 we announced that Moderna had agreed to take over the in-force business, personnel, expertise and systems of Aspis Försäkrings Liv AB ('Aspis'), a small Swedish life and health risk insurer, which complements Moderna's focus on pensions and savings contracts. Completion of the acquisition of Aspis took place on 16 February 2010. The acquisitions of Moderna and Aspis add a growth element to Chesnara's proposition to shareholders. Whilst requiring capital in the early years, the prospect for the creation of value for shareholders in the medium to longer term remains significant.

The UK Business is substantially closed to new business and its primary focus remains on the efficient run-off of its existing life and pensions 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.

The Swedish Business remains open to new business and its primary aim is to develop profits through regaining market share in the company-paid and individual pensions market, whilst developing business in other areas. Writing new business requires funding to support the initial costs incurred: this is provided either by way of financial reinsurance or by way of cash contributions from Chesnara. As the in-force business portfolio grows in scale the income generated by it eventually allows the business to self fund and become a net generator of cash. Moderna is targeted to reach this pivotal point in the next three to four years.

Following the acquisition of Moderna, and in order to prolong the yield delivery to investors, we continue to examine opportunities to acquire businesses, primarily in the small to medium sector of the life assurance and pensions market in the UK and Western Europe. The experience gained from the acquisition of Moderna and Aspis leads us to believe that we can leverage further value from our existing, and acquired, capabilities. As a consequence of changes in the wider financial market environment sellers' expectations of value have moderated to levels where transactions may provide the returns we are seeking. Whilst the environment is now more challenging, due to market uncertainty and possible higher solvency capital requirements, potentially attractive opportunities are emerging.

We primarily target acquisitions with a value of between £50m and £200m, although other opportunities are considered. All opportunities are assessed against a number of key criteria including size, risk (including actual or potential product and financial liabilities), discount to embedded value, capital requirements and the pattern and quality of predicted profit emergence. Our strategic approach, however, remains that such potential acquisitions should not detract significantly from the primary aim of delivering a steady and attractive dividend yield although opportunities which present a significant value uplift or growth opportunity will also be evaluated.

Developments during 2010

UK Business

In the UK this has been a relatively quiet period for the business. Effort has been directed to the sourcing and initial review of potential acquisition opportunities and the advancement of longer-term corporate issues. Of these the implementation of Solvency II, which also applies to the Swedish Business, is key and this is described in more detail on page 21.

Swedish Business

In Sweden we completed the acquisition of the business operations of Aspis on 16 February 2010. This has enabled us to progress the integration of the Aspis personnel and develop plans for integrating the product ranges, begin rationalisation of the systems and initiate reorganisation of the business, both in terms of structure and operational location, consequent upon the utilisation of the administrative capabilities brought to us by Aspis.

Review of the Business

In addition to finalising the acquisition of Aspis, the Group has continued to concentrate on its policy of delivering enhanced value to shareholders through focusing on the efficient run-off of its UK Life business.

The continued strength of the emergence of surplus has underpinned the overall financial performance of the business and enabled the delivery of an improved profit on the IFRS basis of reporting, a positive outturn in EEV profit and the maintenance of a healthy regulatory solvency position.

The result has, inevitably, been affected by the volatility prevailing in the investment markets with good performance in the first quarter being more than eroded in the second quarter. The performance of investment markets and wider economic concerns have restricted Moderna's ability to make significant inroads into its recapture of its former market share. The sales effort has been reorganised and this is beginning to show some positive improvement in new business figures compared to prior year comparative periods. On the Risk and Health side we are pleased to report that the renewals being generated from the Aspis portfolio are ahead of expectations and are delivering profitable returns.

There have been no new regulatory issues that have given rise to any significant concerns or costs.

The key performance areas in the UK and Swedish businesses are reviewed in more detail in the following sections.

UK Business

Per Policy Expenses

Management of the expenses incurred in the servicing of the in-force life and pensions policy base remains a key area of focus for the UK Business. Through our outsourcing contracts we have maximised the proportion of expenses which vary with policy volume and we maintain a small focused governance team to minimise non-policy-related expense. This, together with further continued improvement in policy lapse experience, which leads to a favourable impact in per policy costs (as the fixed expenses are spread over a larger policy base), has resulted in per policy expenses being slightly lower than expectations.

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 2009 year-end we reported that the rate of policy attrition had decreased. This improvement has been sustained and a further slight 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 as we believe that the current economic climate may, at least temporarily, stall the improvements we have seen historically.

Number of in-force policies ('000's)	Unaudited 6 months ended 30 June		Year ended 31 December
	2010	2009	2009
Beginning of period	176	192	192
End of period	169	184	176
Rate of attrition (annualised)	8.0%	8.3%	8.3%

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 Pension Managed Fund, which represents a significant proportion of the CA policyholder funds under management, returned 19.74% during the twelve months ended 30 June 2010 and the CWA Balanced Managed Pension Fund, which represents a significant proportion of CWA policy funds under management, returned 17.53% over the same period. These returns, on balance, compare favourably with the average of 17.77% achieved by the ABI Pension Balanced (up to 85% Equity) Managed Funds sector.

As these are Managed Funds the returns reflect the performance of the equity, fixed interest and property markets consequent upon the general economic climate. Market performance does affect fund values and, consequently, embedded value. Guidance as to the sensitivity of embedded value to market movements is provided on pages 54 and 55.

The Board continues 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.

Mortgage Endowments

We continue to carry potentially significant exposure to mortgage endowment misselling complaints, which may become subject to redress payments to policyholders. Three of the key statistics which define and limit the extent of this exposure are set out below:

	Unaudited 6 months ended 30 June		Year ended 31 December
	2010	2009	2009
Number of complaints received	348	660	1,210
% of complaints assessed upheld	26%	27%	27%
% of complaints assessed time barred	57%	53%	62%

As can be seen the number of complaints continues to reduce whilst the upheld and time barred percentages have stabilised.

Swedish Business

Premium Income and Market Share

	Unaudited 6 months ended 30 June		Year ended 31 December
	2010 £m	2009 £m	2009 £m
Total premium income*			
Pensions and savings	121.9	126.2	244.2
Risk insurance	17.4	10.1	25.2
Total	139.3	136.3	269.4
New Business premium income*			
Pensions and savings	26.2	27.4	46.8
Risk insurance	6.2	0.8	3.1
Total	32.4	28.2	49.9

	Unaudited 6 months ended 30 June		Unaudited Year ended 31 December
	2010	2009	2009
Market share of unit-linked pensions business			
Total business	4.7%	8.0%	5.7%
Company-paid business	6.1%	10.4%	7.4%

Note: Information in respect of the half-year ended 30 June 2009 and the year ended 31 December 2009 includes performance prior to the acquisition of the Swedish Business on 23 July 2009 and is presented for illustrative purposes.

* Translated into sterling at a constant rate of SEK11.5 = £1.

Moderna Försäkringar Liv AB ('Moderna') has continued to seek to re-establish its sales and market share in Sweden. Recently, pensions and savings income has recovered with single premium income for the six months well ahead of the comparative period last year. Risk insurance premiums have surged following the acquisition of the operations of Aspis.

Policy Attrition

As with the UK Business, the longer a policy stays in force the greater the profit that accrues to the Group. The economic climate in Sweden and the uncertainty regarding Moderna ownership during 2008/9 led to some historically high attrition rates. We are seeing some improvement in the discontinuance rates but the relatively newly opened transfer market where, in particular, banks are targeting their customers with related offers, remains challenging.

Annualised rate of attrition	Unaudited 6 months ended 30 June		Year ended 31 December
	2010	2009	2009
Surrenders	13.3%	—	21.7%
Transfers	5.3%	—	5.6%

Assets under Management

	Unaudited 30 June	Unaudited 31 March	31 December
	2010 £m	2010 £m	2009 £m
Assets under management*	1,036.6	1,043.0	962.3

* Translated into sterling at a constant rate of SEK11.5 = £1.

The above illustrates the growth in assets being managed and the effects of the positive market performance in the first quarter countered by the falls in the second quarter. Comparing the end of period figure with the year end figure demonstrates a 7.7% growth despite the markets being lower at the end of the period.

Fund Performance

Relative fund performance is as follows:

Number of funds	Unaudited 6 months ended 30 June		Year ended 31 December
	2010	2009	2009
Outperformed against relevant index	9	—	19
Underperformed against relevant index	19	—	14
No relevant index	3	—	2

The decline in relative performance is a consequence of the investment style which focuses on a value-driven approach. The funds advanced in the first quarter as markets improved. As markets retreated in the second quarter, opportunities were taken to reposition in order to regain comparative performance when values increased and this has produced good performance post the reporting period. As part of the ongoing search for attractive investment opportunities two new funds were added in the first half of the year and their comparative performance to the end of the reporting period is above that of the relevant indices.

IFRS Result

The results analysed below relate to profit for the period and, therefore, exclude foreign exchange translation differences.

The IFRS result for the six months ended 30 June 2010 comprises:

	Unaudited six months ended 30 June 2010		
	Pre-tax £000	Tax £000	Post-tax £000
UK Business result	16,795	(4,238)	12,557
Swedish Business result	(4,060)	44	(4,016)
Other group activities result	(757)	—	(757)
Total result	11,978	(4,194)	7,784
Non-controlling interest			40
Total result attributable to shareholders			7,824

	Unaudited six months ended 30 June 2009		
	Pre-tax £000	Tax £000	Post-tax £000
UK Business result	11,650	(2,927)	8,723
Swedish Business result	—	—	—
Other group activities result	(439)	5	(434)
Total result	11,211	(2,922)	8,289
Non-controlling interest			—
Total result attributable to shareholders			8,289

	Year ended 31 December 2009		
	Pre-tax £000	Tax £000	Post-tax £000
Profit arising on acquisition of Swedish Business	25,056	—	25,056
UK Business result	24,784	948	25,732
Swedish Business result	(2,626)	(148)	(2,774)
Other group activities result	(2,473)	392	(2,081)
Total result	44,741	1,192	45,933
Non-controlling interest			7
Total result attributable to shareholders			45,940

The result of the UK Business, which is net of an amortisation charge of £1.8m in respect of the acquired value of in-force business, continues to be dominated by the strong emergence of surplus from its life and pensions contracts, which are in run-off. Fixed interest yields reduced, with consequent increases in asset values in the first six months of 2010, which resulted in favourable experience of some £5m, compared with £2.3m previously reported at the first quarter position. Pre-tax earnings were significantly enhanced by the release of £3.2m in respect of amounts previously set aside in respect of policyholder claims. A thorough review has determined that the business has no further liability in respect of these claims.

The pre-tax loss attributable to the Swedish Business of £4.1m is stated net of an amortisation charge of £3.8m in respect of the acquired value of in-force business and of an associated write back of £1.4m of deferred acquisition costs. However, the current period loss is also net of a profit of £0.9m recognised on the acquisition of the Aspis business, which has, accordingly, sheltered an underlying loss on core trading in excess of £2.6m.

The Swedish Business is expected to incur trading losses for up to a further three years as it continues to build scale and until profits from an increasing base of in-force investment contracts outweigh the front-end strain of writing new business. That said, conditions in the Swedish economy continue to be challenging, while transfers out of business are higher than expected. Key performance indicators relating to the Swedish Business are set out above.

EEV Result

Supplementary information prepared in accordance with EEV principles and set out in the financial statements on pages 42 to 57 is presented to provide alternative information to that presented under IFRS. EEV principles assist in identifying the value being generated by the UK and Swedish Life Businesses. The result determined under this method represents principally the movement in the UK and Swedish Businesses' embedded value, before transfers made to the parent company and ignoring any capital movements. Through including the in-force value of insurance and investment contracts, EEV recognises the discounted profit stream expected to arise from those contracts. The principal underlying components of the EEV result are the expected return from existing business, in both the UK and Swedish businesses, being the unwind of the rate used to discount the related cash flows, and the value added by the writing of new business in the Swedish Business. Adjustments are made to the result for variations in actual experience from that assumed for each component of policy cash flows arising in the period and for the impact of restating assumptions for each component of the prospective cash flows.

The movement in Group European Embedded Value may be summarised as:

	Unaudited 6 months ended 30 June				Year ended 31 December	
	2010		2009		2009	
	£000	£000	£000	£000	£000	£000
EEV at beginning of period		262,585		182,708		182,708
Effect of modelling improvements		10,363		—		—
EEV at beginning of period restated		272,948		182,708		182,708
Profit arising on acquisition of Swedish Business		—		—		54,187
Profit arising on acquisition of Aspis business		989		—		—
Result for the period						
UK Business						
New business	383		188		1,482	
Existing business	4,720		7,470		14,438	
Tax	(2,428)		(1,392)		11,893	
Post-tax		2,675		6,266		27,813
Swedish Business						
New business	288		—		783	
Existing business	(9,635)		—		6,437	
Tax	—		—		—	
Post-tax		(9,347)		—		7,220
Other group activities net of tax		(762)		111		1,052
Foreign exchange reserve movement		(918)		—		5,539
Dividends paid		(10,454)		(10,200)		(15,934)
EEV at end of period		255,131		178,885		262,585

The effect of the modelling improvements set out above, which is in the nature of an exceptional profit, arises from the fact that, during the first half of 2010, the Swedish Business introduced a new system for modelling the value of its in-force policies. This provided a capability for (i) more accurately modelling the impact on commission paid on policies becoming paid-up and (ii) for determining future fee income on a case-by-case investment mix basis, whereas previously it had been necessary to adopt high-level estimates. These factors led to an increase in the measure of embedded value of £6.3m and £4.1m respectively.

These gains have been virtually offset by the net impact of a number of other significant variances affecting the Swedish Business. The expected return (unwind of the risk discount rate) of just over £1.5m was enhanced by favourable investment market performance in the period of just over £2.5m. This, however, displayed a weaker position than the previously-reported more robust result at the end of the first quarter and is one indication of the condition of the Swedish economy, which has contributed to lower new business volumes. These in turn gave rise to associated expense overruns of some £1.6m as the business did not reach its planned scale. In view of this and additional adverse effects of some £2.6m arising from worsening lapse experience (principally arising from transfers out on pensions savings products), it was decided to take the opportunity to adopt a more cautious stance and to strengthen key assumptions used to value the in-force business. Accordingly, maintenance expense assumptions were strengthened, giving rise to a reduction of £7.7m in embedded value, while the adoption of a more conservative transfer rate assumption has led to a reduction of £3.4m in embedded value. All of the factors set out above, including the impact of model improvements of £10.4m and the profit arising on the acquisition of Aspis as referred to under 'IFRS Result' above, have led to an EEV pre-tax profit of £2m in respect of the Swedish Business.

The UK Business, while being influenced by a degree of economic and investment market uncertainty, has posted a result closer to expectations. It has, however, also displayed a less positive picture than the previously reported first quarter position, largely driven by equity market movements, with a number of leading indices reflecting a fall of approximately 9% over the half-year. On the positive side, favourable lapse and mortality experience gave rise to a pre-tax increase of some £3.9m in embedded value and the result was further enhanced by £3.2m in respect of the release to income of certain claims liabilities as explained in 'IFRS Result' above. These favourable effects were offset by adverse investment market impacts of some £6m, so that the net pre-tax result at £5.1m is close to expectations. The underlying volatility in investment markets has been reflected through declining swap yields, without a corresponding decline in fixed interest rates of return, particularly in the first quarter and through the sharp rise and fall in equity markets referred to above. It is worthy of note that the greater part of the equity market decline experienced over the first half of the year had reversed by mid August 2010.

At the net-of-tax position, the UK Business is slightly behind expectations as the exposure of the £3.2m release to income of claims liabilities to tax at the full rate has increased the marginal rate of tax on the overall result, as there is no corresponding release of deferred tax within the value in-force.

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

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

	Unaudited 30 June 2010			
	UK business £000	Swedish business £000	Other group activities £000	Total £000
Value of in-force business	73,581	114,493	–	188,074
Other net assets	58,523	(22,970)	31,504	67,057
	132,104	91,523	31,504	255,131
Represented by:				
Embedded value ('EV') of regulated entities	132,104	93,717	–	225,821
Less: amount financed by borrowings	–	–	–	–
EV of regulated entities attributable to shareholders	132,104	93,717	–	225,821
Net equity of other Group companies	–	(2,194)	31,504	29,310
Shareholders' equity	132,104	91,523	31,504	255,131

	Unaudited 30 June 2009			
	UK business £000	Swedish business £000	Other group activities £000	Total £000
Value of in-force business	80,153	—	—	80,153
Other net assets	50,828	—	47,904	98,732
	130,981	—	47,904	178,885
Represented by:				
Embedded value ('EV') of regulated entities	135,175	—	—	135,175
Less: amount financed by borrowings	(4,194)	—	—	(4,194)
EV of regulated entities attributable to shareholders	130,981	—	—	130,981
Net equity of other Group companies	—	—	47,904	47,904
Shareholders' equity	130,981	—	47,904	178,885

	31 December 2009			
	UK business £000	Swedish business £000	Other group activities £000	Total £000
Value of in-force business	85,559	112,753	—	198,312
Other net assets	68,098	(22,323)	18,498	64,273
	153,657	90,430	18,498	262,585
Represented by:				
Embedded value ('EV') of regulated entities	157,854	91,478	—	249,332
Less: amount financed by borrowings	(4,197)	—	—	(4,197)
EV of regulated entities attributable to shareholders	153,657	91,478	—	245,135
Net equity of other Group companies	—	(1,048)	18,498	17,450
Shareholders' equity	153,657	90,430	18,498	262,585

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

	Unaudited 30 June 2010		
	UK business 000	Swedish business 000	Total 000
Number of policies			
Endowment	52	15	67
Protection	55	—	55
Annuities	5	—	5
Pensions	50	74	124
Other	7	—	7
Total	169	89	258

	Unaudited 30 June 2009		
	UK business 000	Swedish business 000	Total 000
Number of policies			
Endowment	58	—	58
Protection	61	—	61
Annuities	5	—	5
Pensions	52	—	52
Other	8	—	8
Total	184	—	184

	31 December 2009		
	UK business 000	Swedish business 000	Total 000
Number of policies			
Endowment	55	15	70
Protection	58	—	58
Annuities	5	—	5
Pensions	51	70	121
Other	7	—	7
Total	176	85	261

	Unaudited 30 June 2010		
	UK business £m	Swedish business £m	Total £m
Value of in-force			
Endowment	36.6	12.7	49.3
Protection	46.3	—	46.3
Annuities	(0.2)	—	(0.2)
Pensions	33.3	102.0	135.3
Other	—	—	—
Total at product level	116.0	114.7	230.7
Valuation adjustments			
Holding company expenses	(10.1)	—	(10.1)
Other	(27.7)	—	(27.7)
Cost of capital	(0.9)	(0.2)	(1.1)
Value in-force pre-tax	77.3	114.5	191.8
Taxation	(3.7)	—	(3.7)
Value in-force post-tax	73.6	114.5	188.1

Value of in-force	Unaudited 30 June 2009		
	UK business £m	Swedish business £m	Total £m
Endowment	46.5	—	46.5
Protection	47.3	—	47.3
Annuities	5.3	—	5.3
Pensions	32.7	—	32.7
Other	—	—	—
Total at product level	131.8	—	131.8
Valuation adjustments			
Holding company expenses	(8.8)	—	(8.8)
Other	(23.1)	—	(23.1)
Cost of capital	(4.4)	—	(4.4)
Value in-force pre-tax	95.5	—	95.5
Taxation	(15.3)	—	(15.3)
Value in-force post-tax	80.2	—	80.2

Value of in-force	31 December 2009		
	UK business £m	Swedish business £m	Total £m
Endowment	40.2	15.2	55.4
Protection	48.1	—	48.1
Annuities	3.9	—	3.9
Pensions	36.2	98.6	134.8
Other	0.7	—	0.7
Total at product level	129.1	113.8	242.9
Valuation adjustments			
Holding company expenses	(9.8)	—	(9.8)
Other	(26.5)	—	(26.5)
Cost of capital	(0.8)	(1.0)	(1.8)
Value in-force pre-tax	92.0	112.8	204.8
Taxation	(6.4)	—	(6.4)
Value in-force post-tax	85.6	112.8	198.4

The value-in-force represents the discounted value of the future surpluses arising from the insurance and investment contracts in force at each respective period end. The future surpluses are calculated by using realistic assumptions for each component of the cash flow.

Other valuation adjustments in the UK Business principally comprise expenses of managing policies which are not attributed at product level.

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 5 and 6 respectively of the Company's published consolidated financial statements for the year ended 31 December 2009.

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;
- (iv) deferred acquisition costs and deferred income;
- (v) amortisation of acquired value of in-force business;
- (vi) insurance claim reserves; and
- (vii) insurance claim reserves – reinsurance recoverable.

In addition, in respect of the Swedish Business, commission payable and receivable from fund managers in respect of the unit-linked business have been included as part of the unit-linked funds and subject to fund yield tax. Management is aware that the Swedish tax authority has questioned, in respect of another unit-linked business, whether such commissions receivable from fund managers should be part of the Group's income and be subject to corporation tax of 26.3% (the Swedish corporation tax rate for the year 2010). Management consider that the current accounting treatment remains appropriate.

Detailed information on these items is provided in Note 3 of the Company's published consolidated financial statements for the year ended 31 December 2009.

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 2010, except in relation to continuing volatility in global investment markets. The impact of this on reported results for the six months ended 30 June 2010 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 pages 54 and 55.

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 both the UK and Swedish Businesses is calculated by reference to regulations established and amended from time to time by the FSA in the UK and by Finansinspektionen in Sweden. The rules are designed to ensure that companies have sufficient assets to meet their liabilities in specified adverse circumstances. As such, there is, in the UK, a restriction on the full transfer of surplus from the long-term business fund to shareholder funds of Countrywide Assured plc ('CA plc'), and on the full distribution of reserves from CA plc to Chesnara and, in Sweden, on distributions from shareholder funds.

Within the UK, the regulations include minimum standards for assessing the value of liabilities, including making an appropriate allowance for default risk on corporate bonds held to match liabilities when assessing the valuation discount rates used for valuing these liabilities. Market turmoil in 2008 led to significant widening of spreads on corporate bonds above gilts, through changed assessment of default risk and liquidity issues, and therefore, with the widening spreads, this issue was of concern to the industry. CA plc continues to maintain a prudent approach of limiting the assumed liquidity premium in corporate bonds to a maximum of 50bps as at 30 June 2010 (30 June 2009 and 31 December 2009: 50bps). Additionally, the CA plc Board continues to maintain their stance that permissive changes to regulations introduced in 2006, in FSA policy statement PS06/14, that would allow a reduction in liabilities are not appropriate for CA plc at this time.

The following summarises the capital resources and requirements of CA plc for UK regulatory purposes, after making provision for dividend payments from CA plc to Chesnara, which were approved after the respective period ends:

	Unaudited 30 June		31 December
	2010 £m	2009 £m	2009 £m
Available capital resources ('CR')	58.2	55.0	43.6
Long-term insurance capital requirement ('LTICR')	19.2	21.2	19.8
Resilience capital requirement ('RCR')	2.9	1.6	2.3
Total capital resources requirement ('CRR')	22.1	22.8	22.1
Target capital requirement cover	31.7	33.5	32.0
Ratio of available CR to CRR	263%	241%	197%
Excess of CR over target requirements	<u>£26.5m</u>	<u>£21.5m</u>	<u>£11.6m</u>

The CA plc Board, as a matter of policy, continues to target CR cover for total CRR at a minimum level of 150% of the LTICR and 100% of the RCR. To the extent that the target capital requirement cover of £31.7m as at 30 June 2010 falls short of the £40m share capital component of CR, so it follows that £8.3m of the reported excess of CR over target requirement is not available for distribution to shareholders except by way of a capital reduction.

It can be seen from this information that Chesnara, which relies on dividend distributions from CA plc, is currently in a favourable position to continue to pursue a progressive dividend policy.

In contrast to the UK Business, the Swedish Business, which is open to new business, is, in the short to medium term, a net consumer of capital. The ratio of capital resources to capital resource requirements is a key indicator of the capital health of the business as it expands and provides the context in which further capital contributions are made by the parent company to finance that expansion in a predictable and orderly manner.

The following summarises the capital resources and requirements of Moderna Försäkringar Liv AB ('Moderna') for Swedish regulatory purposes:

	Unaudited 30 June		31 December
	2010 £m	2009 £m	2009 £m
Available capital resources (CR) represented by:			
Share capital	1.1	–	1.1
Additional equity contributions	33.6	–	33.6
Accumulated deficit	(14.5)	–	(10.2)
	<u>20.2</u>	<u>–</u>	<u>24.5</u>
Regulatory capital resource requirement (CRR)	9.2	–	8.1
Target requirement	13.8	–	12.1
Ratio of CR to CRR	220%	–	302%
Excess of CR over target requirements	<u>£6.4m</u>	<u>–</u>	<u>£12.4m</u>

The Moderna Board, as a matter of policy, sets a minimum target of 150% of the regulatory capital requirement. Swedish solvency regulation requires that, to be fully admissible, a certain proportion of assets are to be held in the form of cash. The operation of this requirement may, from time to time, act as the operative constraint in determining the level of additional funding requirements, thereby causing the solvency ratio to rise above what it would otherwise have been, had the form of assets matching capital resources not been a constraint.

Insurance Groups Directive

In accordance with the EU Insurance Groups Directive, the Group calculates the excess of the aggregate of regulatory capital employed over the aggregate minimum solvency requirement imposed by local regulators for all of the constituent members of the Group, all of which are based in Europe. The following sets out these calculations after the recognition of interim or final dividends for the respective financial periods, but approved by the Board and paid to Group shareholders after the respective dates:

	Unaudited 30 June		31 December
	2010 £m	2009 £m	2009 £m
Available group capital resources	106.9	93.0	99.7
Group regulatory capital requirement	(32.4)	(22.8)	(31.6)
Excess	<u>74.5</u>	<u>70.2</u>	<u>68.1</u>
Cover	<u>330%</u>	<u>408%</u>	<u>316%</u>

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

Individual Capital Assessments

The FSA Prudential Sourcebooks require UK insurance companies to make their own assessment of their capital needs to a required standard (a 99.5% probability of being able to meet 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, including such market effects as significant falls in equity values, interest rate increases and decreases, bond defaults and further widening of bond spreads.

CA plc completed a further full annual assessment during 2009 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. This assessment is subject to quarterly high-level updates until the next full annual assessment.

We are currently developing the Swedish Business's ability to produce similar assessments, so that the determination of risk-based capital is more clearly aligned with UK best practice. In the meantime, the Swedish Business, in accordance with local regulatory requirements, continues to make quarterly assessments of the risk-based capital requirements of its business: these indicate that capital resources currently provide a comfortable margin over capital resource requirements.

EU Solvency II Framework

Over the year, we have continued to monitor developments in the EU Solvency II framework which will impact both the UK and Swedish Businesses. We have established a Steering Group to oversee our implementation of the regulations, which are currently due to become effective on 31 October 2012. Besides ensuring that there are robust processes for the calculation of technical reserves and solvency capital, the implementation will embrace wide-ranging changes in risk management processes on a Group-wide basis. In the meantime, we have continued internal quantitative analysis and continue to assess the impact on the Group of the content of the numerous Consultation Papers which have been issued by the Committee of European Insurance and Occupational Pensions Supervisors ('CEIOPS').

Going Concern Statement

After making appropriate enquiries, the Directors confirm that they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. Accordingly, they continue to adopt the going concern basis in the preparation of the financial statements.

Outlook

In line with our primary aim of delivering an attractive and reliable dividend yield, we remain focused on the efficient management of our businesses.

Whilst Group performance has been relatively robust through the economic crisis and, indeed it was the catalyst which generated the value-enhancing acquisition of Moderna, the ongoing effects still bring challenges to our businesses. Macroeconomic and industry-related challenges include:

- (i) Ongoing volatility in investment markets – which affects surplus generation and embedded value as customers' propensity to invest further or, indeed, maintain their exposure to equity and related markets is challenged;
- (ii) Historically low interest rates – which diminish the returns we can achieve on our significant cash holdings;
- (iii) Economic environment – whilst low inflation and interest rates help policy affordability, any significant increase in unemployment will have an inevitable effect although we have factored this prospect into our discontinuance rates;
- (iv) Regulatory or legislative change – Solvency II is providing a significant operational challenge. However, we are not currently expecting any significant capital threats. On the legislation front we have a new government in the UK which is keen to raise funds to cut the deficit and an election is imminent in Sweden. That said, there appear to be no immediate issues other than a tax consultation paper issued in the UK where we currently believe the outcomes will not have any significant effects on the UK business; and
- (v) Exchange rates – which may affect the cost of funding Moderna and give rise to fluctuations in the reported embedded value of the Swedish Business.

Provided that these areas do not adversely impact the prospects of the Group significantly, the short-to medium-term outlook is positive for the ongoing emergence of surplus and, accordingly, for dividend support.

On the more positive side, we continue to see a reasonable flow of potential acquisition opportunities (at least in part generated by some of the issues noted above) and, as demonstrated with the Moderna and Aspis transactions, we will readily progress these where we see value and a clear strategic fit. As regards other opportunities, while we remain open-minded as to location in the UK and Western Europe, we will continue to apply strict financial and risk criteria in assessing them.

Dividend

We have signalled that we aim to provide a reliable and progressive dividend payment. With the continuing healthy cash flow generated by the emergence of surplus from the underlying UK product base and the strong solvency position of the business, the Board is pleased to be able to declare an interim dividend of 5.8p, which represents an increase of 2.65% over the 2009 interim payment.

Graham Kettleborough
Chief Executive Officer
25 August 2010

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

Responsibility statement

We confirm that to the best of our knowledge:

- (a) the condensed set of financial statements has been prepared in accordance with IAS 34 'Interim Financial Reporting';
- (b) the interim management report includes a fair review of the information required by DTR 4.2.7R (indication of important events during the first six months and description of principal risks and uncertainties for the remaining six months of the year); and
- (c) the interim management report includes a fair review of the information required by DTR 4.2.8R (disclosure of related parties' transactions and changes therein).

By order of the Board

Peter Mason
Chairman
25 August 2010

Graham Kettleborough
Chief Executive Officer
25 August 2010

Independent Auditor's Review Report to the Members of Chesnara plc in respect of the Half Yearly Financial Report

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 2010 which comprises the condensed consolidated statement of comprehensive income, the condensed consolidated balance sheet, the condensed consolidated statement of cash flows, the condensed consolidated statement of changes in equity and related Notes 1 to 7. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

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

Directors' responsibilities

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

As disclosed in Note 1, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting," as adopted by the European Union.

Our responsibility

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

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2010 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

Deloitte LLP

Chartered Accountants and Statutory Auditors
Manchester, United Kingdom

25 August 2010

Condensed Consolidated Statement of Comprehensive Income for the six months ended 30 June 2010

	Note	Unaudited Six months ended 30 June		Year ended 31 December
		2010 £000	2009 £000	2009 £000
Insurance premium revenue		59,044	44,577	100,105
Insurance premium ceded to reinsurers		(18,999)	(8,110)	(24,997)
Net insurance premium revenue		40,045	36,467	75,108
Fee and commission income				
Insurance contracts		18,915	17,573	35,864
Investment contracts		14,943	3,299	15,256
Net investment return		(150)	9,145	326,680
Total revenue (net of reinsurance payable)		73,753	66,484	452,908
Other operating income		7,028	1,498	4,689
Total income		80,781	67,982	457,597
Insurance contract claims and benefits incurred				
Claims and benefits paid to insurance contract holders		(64,345)	(60,417)	(129,557)
Net (increase)/decrease in insurance contract provisions		14,006	9,809	(127,840)
Reinsurers' share of claims and benefits		15,049	7,287	47,897
Net insurance contract claims and benefits		(35,290)	(43,321)	(209,500)
Change in investment contract liabilities		(465)	(3,658)	(199,748)
Reinsurers' share of investment contract liabilities		(303)	193	4,710
Net change in investment contract liabilities		(768)	(3,465)	(195,038)
Fees, commission and other acquisition costs		(7,630)	(661)	(5,167)
Administrative expenses		(13,272)	(6,322)	(18,245)
Other operating expenses				
Charge for amortisation of acquired value of in-force business		(5,636)	(1,863)	(6,953)
Charge for amortisation of acquired value of customer relationships		(442)	–	(188)
Other		(6,003)	(1,027)	(2,195)
Total expenses		(69,041)	(56,659)	(437,286)
Total income less expenses		11,740	11,323	20,311
Share of (loss)/profit of associates		(101)	–	39
Profit recognised on business combinations	4	989	–	25,056
Operating profit		12,628	11,323	45,406
Financing costs		(650)	(112)	(665)
Profit before income taxes	5	11,978	11,211	44,741
Income tax (expense)/credit		(4,194)	(2,922)	1,192
Profit for the period		7,784	8,289	45,933
Attributable to:				
Shareholders	2,5	7,824	8,289	45,940
Non-controlling interest		(40)	–	(7)
		7,784	8,289	45,933
Foreign exchange translation differences arising on the revaluation of foreign operations		(329)	–	3,381
Total comprehensive income for the period		7,455	8,289	49,314
Attributable to:				
Shareholders		7,495	8,289	49,321
Non-controlling interest		(40)	–	(7)
		7,455	8,289	49,314
Basic earnings per share (based on profit for the period attributable to shareholders)	2	7.71p	8.17p	45.26p
Diluted earnings per share (based on profit for the period attributable to shareholders)	2	7.71p	8.17p	45.26p

Condensed Consolidated Balance Sheet at 30 June 2010

	Note	Unaudited 30 June		31 December
		2010 £000	2009 £000	2009 £000
Assets				
Intangible assets				
Deferred acquisition costs		10,914	8,116	9,327
Acquired value of in-force business				
Insurance contracts		13,484	15,512	14,937
Investment contracts		66,864	11,101	71,526
Acquired value of customer relationships		3,498	–	2,682
Internally-developed software		5,456	–	4,060
Property and equipment		681	–	491
Investment in associates		943	–	1,051
Investment properties		3,355	3,272	3,355
Reinsurers' share of insurance contract provisions		239,078	181,769	236,866
Amounts deposited with reinsurers		26,571	22,339	27,056
Financial assets				
Equity securities at fair value through income		397,509	356,387	454,970
Holdings in collective investment schemes at fair value through income		1,537,247	589,530	1,612,861
Debt securities at fair value through income		380,057	258,410	247,836
Policyholders' funds held by the Group		44,336	–	41,107
Insurance and other receivables		27,477	9,812	19,822
Prepayments		3,396	2,920	3,784
Derivative financial instruments		7,405	2,410	7,964
Total financial assets		2,397,427	1,219,469	2,388,344
Reinsurers' share of accrued policyholder claims		3,996	3,519	4,728
Income taxes		941	–	395
Cash and cash equivalents		174,183	178,789	155,241
Total assets	5	2,947,391	1,643,886	2,920,059
Liabilities				
Bank overdrafts		1,590	2,074	2,312
Insurance contract provisions		1,065,147	910,174	1,077,033
Financial liabilities				
Investment contracts at fair value through income		1,564,816	535,536	1,529,221
Liabilities relating to policyholders' funds held by the Group		44,336	–	41,107
Borrowings	6	22,452	4,194	28,996
Derivative financial instruments		1,542	746	54
Total financial liabilities		1,633,146	540,476	1,599,378
Provisions		1,696	2,580	1,452
Deferred tax liabilities		9,558	9,647	10,366
Reinsurance payables		22,105	1,772	15,039
Payables related to direct insurance and investment contracts		29,139	24,948	30,433
Deferred income		12,254	13,779	13,132
Income taxes		7,543	6,956	1,313
Other payables		8,417	7,023	9,833
Total liabilities	5	2,790,595	1,519,429	2,760,291
Net assets		156,796	124,457	159,768
Shareholders' equity				
Share capital		41,501	41,501	41,501
Share premium		20,458	20,458	20,458
Treasury shares		(3,379)	(3,379)	(3,379)
Other reserves		3,102	50	3,431
Retained earnings	3	95,114	65,827	97,744
Total shareholders' equity		156,796	124,457	159,755
Non-controlling interest		–	–	13
Total equity		156,796	124,457	159,768

Condensed Consolidated Statement of Cash Flows for the six months ended 30 June 2010

	Unaudited Six months ended 30 June		Year ended 31 December
	2010 £000	2009 £000	2009 £000
Profit for the year	7,824	8,289	45,940
Adjustments for:			
Depreciation of property and equipment	148	–	65
Amortisation of deferred acquisition costs	3,040	474	2,080
Amortisation of acquired value of in-force business	5,637	1,863	6,953
Amortisation of acquired value of customer relationships	442	–	188
Amortisation of internally-developed software	527	–	414
Tax expense/(recovery)	4,194	2,922	(1,192)
Interest receivable	(6,752)	(8,558)	(17,959)
Dividends receivable	(13,749)	(15,266)	(24,048)
Interest expense	650	112	665
Change in fair value of investment properties	–	160	77
Fair value losses/(gains) on financial assets	31,095	3,824	(284,739)
(Profit)/loss on sale of property and equipment	(2)	–	21
Profit arising on business combination	(989)	–	(25,056)
Share of loss of associate net of impairment	101	–	122
Interest received	6,363	8,627	20,893
Dividends received	13,064	15,024	23,304
Increase in intangible assets related to insurance and investment contracts	(4,479)	–	(3,157)
Changes in operating assets and liabilities			
(Increase)/decrease in financial assets	(44,764)	14,494	(58,028)
(Increase)/decrease in reinsurers' share of insurance contract provisions	(1,859)	1,505	(27,211)
Decrease/(increase) in amounts deposited with reinsurers	485	(158)	(4,875)
(Increase)/decrease in insurance and other receivables	(6,983)	1,417	(4,671)
Decrease/(increase) in prepayments	376	(1,320)	(1,293)
(Decrease)/increase in insurance contract provisions	(14,575)	(13,332)	120,648
Increase/(decrease) in investment contract liabilities	50,682	(23,006)	219,609
Increase/(decrease) in provisions	244	(817)	(2,229)
Increase in reinsurance payables	7,422	375	3,629
(Decrease)/increase in payables related to direct insurance and investment contracts	(1,119)	1,057	3,604
Increase/(decrease) in other payables	4,564	427	(970)
Cash generated from/(utilised by) operations	41,587	(1,887)	(7,216)
Income tax (paid)/recovered	(4,694)	1,811	(2,371)
Net cash generated from/(utilised by) operating activities	36,893	(76)	(9,587)
Cash flows from investing activities			
Acquisition of business net of cash acquired	1,830	–	(5,944)
Investment in associates	–	–	(334)
Development of software	(1,079)	–	(918)
Purchases of property and equipment	(193)	–	(180)
Net cash generated from/(utilised by) investing activities	558	–	(7,376)
Cash flows from financing activities			
Repayment of borrowings	(6,177)	(4,200)	(5,759)
Dividends paid	(10,454)	(10,200)	(15,934)
Interest paid	(853)	(96)	(821)
Net cash utilised by financing activities	(17,484)	(14,496)	(22,514)
Net increase/(decrease) in cash and cash equivalents	19,967	(14,572)	(39,477)
Cash and cash equivalents at beginning of the year	152,929	191,287	191,287
Effect of exchange rate changes on cash and cash equivalents	(303)	–	1,119
Cash and cash equivalents at end of the period	172,593	176,715	152,929

Condensed Consolidated Statement of Changes in Equity for the six months ended 30 June 2010

	Unaudited Six months ended 30 June 2010					
	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2010	41,501	20,458	3,431	(3,379)	97,744	159,755
Profit for the period attributable to shareholders	–	–	–	–	7,824	7,824
Dividends paid	–	–	–	–	(10,454)	(10,454)
Foreign exchange translation reserve	–	–	(329)	–	–	(329)
Equity shareholders' funds at 30 June 2010	<u>41,501</u>	<u>20,458</u>	<u>3,102</u>	<u>(3,379)</u>	<u>95,114</u>	<u>156,796</u>

	Unaudited Six months ended 30 June 2009					
	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2009	41,501	20,458	50	(3,379)	67,738	126,368
Profit for the period attributable to shareholders	–	–	–	–	8,289	8,289
Dividends paid	–	–	–	–	(10,200)	(10,200)
Equity shareholders' funds at 30 June 2009	<u>41,501</u>	<u>20,458</u>	<u>50</u>	<u>(3,379)</u>	<u>65,827</u>	<u>124,457</u>

	Year ended 31 December 2009					
	Share capital £000	Share premium £000	Other reserves £000	Treasury shares £000	Retained earnings £000	Total £000
Equity shareholders' funds at 1 January 2009	41,501	20,458	50	(3,379)	67,738	126,368
Profit for the year attributable to shareholders	–	–	–	–	45,940	45,940
Dividends paid	–	–	–	–	(15,934)	(15,934)
Foreign exchange translation reserve	–	–	3,381	–	–	3,381
Equity shareholders' funds at 31 December 2009	<u>41,501</u>	<u>20,458</u>	<u>3,431</u>	<u>(3,379)</u>	<u>97,744</u>	<u>159,755</u>

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 2009, 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 2009.

The financial information shown in this half-year review is unaudited and does not constitute statutory accounts within the meaning of section 435 of the Companies Act 2006.

The comparative figures for the financial year ended 31 December 2009 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 298(2) or (3) of the Companies Act 2006.

2. Earnings per share

Earnings per share are based on the following:

	Unaudited Six months ended 30 June		Year ended 31 December
	2010	2009	2009
Profit for the year attributable to shareholders (£000)	7,824	8,289	45,940
Weighted average number of ordinary shares	101,492,591	101,492,591	101,492,591
Basic earnings per share	7.71p	8.17p	45.26p
Diluted earnings per share	7.71p	8.17p	45.26p

The weighted average number of ordinary shares in respect of the six months ended 30 June 2010, the six months ended 30 June 2009 and the year ended 31 December 2009 is based on 104,588,785 shares in issue at the beginning and end of the period less 3,096,194 own shares held in treasury at the beginning and end of the period.

There were no share options outstanding during the periods under review. Accordingly, there is no dilution of the average number of ordinary shares in issue in respect of these periods.

Earnings per share for the year ended 31 December 2009 includes the impact of £25,056,000 of profit recognised on the acquisition of Moderna. Excluding this item both the basic and diluted earnings per share for the year ended 31 December 2009 would have been 20.58p per share.

Notes to the Condensed Consolidated Financial Statements (Unaudited) (continued)

3. Retained earnings

	Unaudited Six months ended 30 June		Year ended 31 December
	2010 £000	2009 £000	2009 £000
Retained earnings attributable to equity holders of the parent company comprise			
Balance at 1 January	97,744	67,738	67,738
Profit for the period	7,824	8,289	45,940
Dividends			
Final approved and paid for 2008	–	(10,200)	(10,200)
Interim approved and paid for 2009	–	–	(5,734)
Final approved and paid for 2009	(10,454)	–	–
Balance at 30 June/31 December	95,114	65,827	97,744

The final dividend in respect of 2008, approved and paid in 2009, was paid at the rate of 10.05p per share.

The interim dividend in respect of 2009, approved and paid in 2009, was paid at the rate of 5.65p per share.

The final dividend in respect of 2009, approved and paid in 2010, was paid at the rate of 10.3p per share so that the total dividend paid to the equity shareholders of the Parent Company in respect of the year ended 31 December 2009 was made at the rate of 15.95p per share.

An interim dividend of 5.80p per share in respect of the year ending 31 December 2010, payable on 12 October 2010 to equity shareholders of the parent company registered at the close of business on 10 September 2010, the dividend record date, was approved by the Directors after 30 June 2010. The resulting interim dividend of £5.9m has not been provided in these financial statements.

The following summarises dividends per share in respect of the year ended 31 December 2009 and 31 December 2010:

	2010	2009
Interim dividend	5.80p	5.65p
Final dividend		10.30p
Total		15.95p

4. Business combinations

Business combination relating to Aspis Försäkringar Liv AB

On 16 February 2010, Chesnara plc's Swedish subsidiary, Moderna Försäkringar Liv AB ('Moderna'), entered into an agreement with the Swedish Regulatory Authority, Finansinspektionen ('FI') to take over the operational management and certain of the assets and liabilities of Aspis Försäkringar Liv AB ('Aspis') for a total consideration of SEK 20.75m (£1.8m), paid in cash. This followed the FI's decision to take control of Aspis on 26 November 2009 after revoking Aspis' licence as it was unable to demonstrate its solvency. Moderna has acquired the in force business, the personnel, expertise and systems of Aspis and will also manage, but not be responsible for, the payment of in-force claims that had occurred up to 12 November 2009. Moderna had previously, under the terms of an asset transfer agreement entered into on 10 December 2009, acquired the right to offer renewal policies to Aspis policyholders from 12 November 2009.

The acquisition of this business has given rise to a profit on acquisition of £989,257 calculated as follows:

The estimated book and fair values of the assets and liabilities at the date of acquisition were:

	Book value £000	Fair value and accounting policy adjustments £000	Fair value £000
Assets			
Intangible assets			
Value of in-force insurance contracts	–	235	235
Software assets	–	927	927
Value of customer relationships	–	1,306	1,306
Deferred acquisition costs	235	(235)	–
Property and equipment	154	–	154
Cash and cash equivalents	3,651	–	3,651
Total assets	4,040	2,233	6,273
Liabilities			
Insurance contract provisions	3,298	–	3,298
Other payables	154	–	154
Total liabilities	3,452	–	3,452
Net assets	588	2,233	2,821
Net assets acquired			2,821
Total consideration			(1,832)
Profit arising on acquisition of subsidiary			989

The assets and liabilities as at the acquisition date in the table above are stated at their provisional fair values and may be amended for 12 months after the date of acquisition in accordance with paragraph 45 of IFRS 3 (2008), *Business Combinations*.

The results of Aspis have been included in the consolidated financial statements of the Group with effect from 16 February 2010, and have contributed revenue of £3.0 million over this period, whilst contributing £0.6 million loss to the overall consolidated profit before tax.

Had Aspis been consolidated from 1 January 2010 the consolidated statement of comprehensive income would have included revenue of £4.1 million, and the results would have contributed £0.8 million loss to the overall consolidated profit before tax.

Notes to the Condensed Consolidated Financial Statements (Unaudited) (continued)

5 Operating segments

The Group considers that it has no product or distribution-based business segments. It reports segmental information on the same basis as reported internally to the Chief Operating Decision Maker, which is the Board of Directors of Chesnara plc.

There were no changes to the basis of segmentation or the measurement basis for segment profit during the periods under review.

UK Business

This segment comprises the UK insurance and investment operation, Countrywide Assured Life Holdings Limited ('CAHL'), which holds the Group's UK insurance and investment assets and liabilities, and is responsible for managing both unit-linked and non-linked business.

Swedish Business

This segment comprises the Swedish insurance and investment operation, Moderna Försäkringar Liv AB ('Moderna'), which holds the Group's Swedish insurance and investment assets and liabilities, and is responsible for managing both unit-linked and non-linked business.

Other Group Activities

The functions performed by the holding company, Chesnara plc, are defined under the operating segment analysis as Other Group Activities. Also included therein are consolidation and elimination adjustments.

Measurement basis

The accounting policies of the segments are the same as those for the Group as a whole. Any transactions between the business segments are on normal commercial terms and market conditions. The Group evaluates performance of operating segments on the basis of the profit before tax attributable to shareholders and the total assets and liabilities of the reporting segments and the Group.

(i) **Segmental income statement for the six months ended 30 June 2010 (unaudited)**

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Insurance premium revenue	41,851	17,193	–	59,044
Insurance premium ceded to reinsurers	(7,391)	(11,608)	–	(18,999)
Net insurance premium revenue	34,460	5,585	–	40,045
Fee and commission income				
Insurance contracts	16,255	2,660	–	18,915
Investment contracts	5,124	9,819	–	14,943
Net investment return	(7,947)	7,689	108	(150)
Total revenue (net of reinsurance payable)	47,892	25,753	108	73,753
Other operating income	1,560	5,468	–	7,028
Segmental income	49,452	31,221	108	80,781
Insurance contract claims and benefits incurred				
Claims and benefits paid to insurance contract holders	(58,361)	(5,984)	–	(64,345)
Net decrease/(increase) in insurance contract provisions	18,318	(4,312)	–	14,006
Reinsurers' share of claims and benefits	7,888	7,161	–	15,049
Net insurance contract claims and benefits incurred	(32,155)	(3,135)	–	(35,290)
Change in investment contract liabilities	7,673	(8,138)	–	(465)
Reinsurers' share of investment contract liabilities	(303)	–	–	(303)
Net change in investment contract liabilities	7,370	(8,138)	–	(768)
Fees, commission and other acquisition costs	(711)	(6,919)	–	(7,630)
Administrative expenses	(4,723)	(7,659)	(890)	(13,272)
Other operating expenses				
Charge for amortisation of acquired value of in-force business	(1,847)	(3,789)	–	(5,636)
Charge for amortisation of customer relationships	–	(442)	–	(442)
Other	(591)	(5,466)	54	(6,003)
Segmental expenses	(32,657)	(35,548)	(836)	(69,041)
Segmental income less expenses	16,795	(4,327)	(728)	11,740
Share of profit from associates	–	(101)	–	(101)
Profit recognised on acquisition of subsidiary	–	989	–	989
Segmental operating profit/(loss)	16,795	(3,439)	(728)	12,628
Financing costs	–	(621)	(29)	(650)
Profit/(loss) before tax	16,795	(4,060)	(757)	11,978
Income tax (expense)/credit	(4,238)	44	–	(4,194)
Non-controlling interest	–	40	–	40
Profit/(loss) after tax attributable to shareholders	12,557	(3,976)	(757)	7,824

Notes to the Condensed Consolidated Financial Statements (Unaudited) (continued)

(ii) Segmental income statement for the six months ended 30 June 2009 (unaudited)

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Insurance premium revenue	44,577	–	–	44,577
Insurance premium ceded to reinsurers	(8,110)	–	–	(8,110)
Net insurance premium revenue	36,467	–	–	36,467
Fee and commission income				
Insurance contracts	17,573	–	–	17,573
Investment contracts	3,299	–	–	3,299
Net investment return	8,745	–	400	9,145
Total revenue (net of reinsurance payable)	66,084	–	400	66,484
Other operating income	1,498	–	–	1,498
Segmental income	67,582	–	400	67,982
Insurance contract claims and benefits incurred				
Claims and benefits paid to insurance contract holders	(60,417)	–	–	(60,417)
Net decrease in insurance contract provisions	9,809	–	–	9,809
Reinsurers' share of claims and benefits	7,287	–	–	7,287
Net insurance contract claims and benefits incurred	(43,321)	–	–	(43,321)
Change in investment contract liabilities	(3,658)	–	–	(3,658)
Reinsurers' share of investment contract liabilities	193	–	–	193
Net change in investment contract liabilities	(3,465)	–	–	(3,465)
Fees, commission and other acquisition costs	(661)	–	–	(661)
Administrative expenses	(5,378)	–	(944)	(6,322)
Other operating expenses				
Charge for amortisation of acquired value of in-force business	(1,863)	–	–	(1,863)
Other	(1,244)	–	217	(1,027)
Segmental expenses	(55,932)	–	(727)	(56,659)
Segmental income less expenses	11,650	–	(327)	11,323
Share of profit from associates	–	–	–	–
Profit recognised on acquisition of subsidiary	–	–	–	–
Segmental operating profit/(loss)	11,650	–	(327)	11,323
Financing costs	–	–	(112)	(112)
Profit/(loss) before tax	11,650	–	(439)	11,211
Income tax (expense)/credit	(2,927)	–	5	(2,922)
Profit/(loss) after tax attributable to shareholders	8,723	–	(434)	8,289

(iii) Segmental income statement for the year ended 31 December 2009

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Insurance premium revenue	88,469	11,636	–	100,105
Insurance premium ceded to reinsurers	(15,831)	(9,166)	–	(24,997)
Net insurance premium revenue	72,638	2,470	–	75,108
Fee and commission income				
Insurance contracts	34,285	1,579	–	35,864
Investment contracts	8,258	6,998	–	15,256
Net investment return	233,926	92,239	515	326,680
Total revenue (net of reinsurance payable)	349,107	103,286	515	452,908
Other operating income	4,689	–	–	4,689
Segmental income	353,796	103,286	515	457,597
Insurance contract claims and benefits incurred				
Claims and benefits paid to insurance contract holders	(126,737)	(2,820)	–	(129,557)
Net (increase)/decrease in insurance contract provisions	(128,064)	224	–	(127,840)
Reinsurers' share of claims and benefits	45,630	2,267	–	47,897
Net insurance contract claims and benefits incurred	(209,171)	(329)	–	(209,500)
Change in investment contract liabilities	(107,524)	(92,224)	–	(199,748)
Reinsurers' share of investment contract liabilities	4,710	–	–	4,710
Net change in investment contract liabilities	(102,814)	(92,224)	–	(195,038)
Fees, commission and other acquisition costs	(1,116)	(4,051)	–	(5,167)
Administrative expenses	(9,806)	(5,276)	(3,163)	(18,245)
Other operating expenses				
Charge for amortisation of acquired value of in-force business	(3,688)	(3,265)	–	(6,953)
Charge for amortisation of customer relationships	–	(188)	–	(188)
Other	(2,417)	(110)	332	(2,195)
Segmental expenses	(329,012)	(105,443)	(2,831)	(437,286)
Segmental income less expenses	24,784	(2,157)	(2,316)	20,311
Share of profit from associates	–	39	–	39
Profit recognised on acquisition of subsidiary	–	–	25,056	25,056
Segmental operating profit/(loss)	24,784	(2,118)	22,740	45,406
Financing costs	–	(508)	(157)	(665)
Profit/(loss) before tax	24,784	(2,626)	22,583	44,741
Income tax credit/(expense)	948	(148)	392	1,192
Non-controlling interest	–	7	–	7
Profit/(loss) after tax attributable to shareholders	25,732	(2,767)	22,975	45,940

Notes to the Condensed Consolidated Financial Statements (Unaudited) (continued)

(iv) Segmental balance sheet as at 30 June 2010 (unaudited)

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Intangible assets	30,093	70,123	–	100,216
Property and equipment	–	681	–	681
Investment in associates	–	943	–	943
Reinsurers' share of insurance contract provisions	208,715	30,363	–	239,078
Amounts deposited with reinsurers	26,571	–	–	26,571
Investment properties	3,355	–	–	3,355
Financial assets	1,350,351	1,046,773	303	2,397,427
Reinsurers' share of accrued policyholder claims	3,996	–	–	3,996
Income tax	546	–	395	941
Cash and cash equivalents	123,603	19,125	31,455	174,183
Total assets	1,747,230	1,168,008	32,153	2,947,391
Bank overdrafts	1,590	–	–	1,590
Insurance contract provisions	1,023,893	41,254	–	1,065,147
Investment contracts at fair value through income	584,921	979,895	–	1,564,816
Liabilities relating to policyholders' funds held by the Group	–	44,336	–	44,336
Borrowings	–	22,452	–	22,452
Derivative financial instruments	1,542	–	–	1,542
Provisions	1,696	–	–	1,696
Deferred tax liabilities	8,870	686	2	9,558
Reinsurance payables	2,476	19,629	–	22,105
Payables related to direct insurance and investment contracts	19,975	9,164	–	29,139
Deferred income	12,254	–	–	12,254
Income taxes	4,600	2,943	–	7,543
Other payables	3,178	4,261	978	8,417
Total liabilities	1,664,995	1,124,620	980	2,790,595
Net assets	82,235	43,388	31,173	156,796
Non-controlling interest	–	–	–	–
Net assets attributable to shareholders	82,235	43,388	31,173	156,796

(v) Segmental balance sheet as at 30 June 2009 (unaudited)

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Intangible assets	34,729	–	–	34,729
Reinsurers' share of insurance contract provisions	181,769	–	–	181,769
Amounts deposited with reinsurers	22,339	–	–	22,339
Investment properties	3,272	–	–	3,272
Financial assets	1,218,955	–	514	1,219,469
Reinsurers' share of accrued policyholder claims	3,519	–	–	3,519
Cash and cash equivalents	130,429	–	48,360	178,789
Total assets	1,595,012	–	48,874	1,643,886
Bank overdrafts	2,074	–	–	2,074
Insurance contract provisions	910,174	–	–	910,174
Investment contracts at fair value through income	535,536	–	–	535,536
Borrowings	–	–	4,194	4,194
Derivative financial instruments	746	–	–	746
Provisions	2,580	–	–	2,580
Deferred tax liabilities	9,647	–	–	9,647
Reinsurance payables	1,772	–	–	1,772
Payables related to direct insurance and investment contracts	24,948	–	–	24,948
Deferred income	13,779	–	–	13,779
Income taxes	7,102	–	(146)	6,956
Other payables	5,487	–	1,536	7,023
Total liabilities	1,513,845	–	5,584	1,519,429
Net assets	81,167	–	43,290	124,457
Non-controlling interest	–	–	–	–
Net assets attributable to shareholders	81,167	–	43,290	124,457

Notes to the Condensed Consolidated Financial Statements (Unaudited) (continued)

(vi) Segmental balance sheet as at 31 December 2009

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Intangible assets	32,471	70,061	–	102,532
Property and equipment	–	491	–	491
Investment in associates	–	1,051	–	1,051
Reinsurers' share of insurance contract provisions	209,604	27,262	–	236,866
Amounts deposited with reinsurers	27,056	–	–	27,056
Investment properties	3,355	–	–	3,355
Financial assets	1,413,798	974,475	71	2,388,344
Reinsurers' share of accrued policyholder claims	4,728	–	–	4,728
Income tax	–	–	395	395
Cash and cash equivalents	120,830	14,776	19,635	155,241
Total assets	1,811,842	1,088,116	20,101	2,920,059
Bank overdrafts	2,312	–	–	2,312
Insurance contract provisions	1,044,680	32,353	–	1,077,033
Investment contracts at fair value through income	610,930	918,291	–	1,529,221
Liabilities relating to policyholders' funds held by the Group	–	41,107	–	41,107
Borrowings	–	24,799	4,197	28,996
Derivative financial instruments	54	–	–	54
Provisions	1,452	–	–	1,452
Deferred tax liabilities	9,613	751	2	10,366
Reinsurance payables	2,064	12,975	–	15,039
Payables related to direct insurance and investment contracts	24,751	5,682	–	30,433
Deferred income	13,132	–	–	13,132
Income taxes	854	459	–	1,313
Other payables	3,825	3,990	2,018	9,833
Total liabilities	1,713,667	1,040,407	6,217	2,760,291
Net assets	98,175	47,709	13,884	159,768
Non-controlling interest	–	(13)	–	(13)
Net assets attributable to shareholders	98,175	47,696	13,884	159,755

6. Borrowings

	Unaudited 30 June		31 December
	2010 £000	2009 £000	2009 £000
Bank loan	–	4,194	4,197
Amount due in relation to financial reinsurance	22,340	–	24,686
Other	112	–	113
Total	22,452	4,194	28,996

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

The fair value of the bank loan at 30 June 2010 was £nil (30 June 2009: £4,200,000).

The fair value of amounts due in relation to financial reinsurance was £22,885,000 (30 June 2009: £nil).

The fair value of other borrowings was not materially different from its carrying value at any of the period ends under review.

7 Approval of consolidated report for the six months ended 30 June 2010

This condensed consolidated report was approved by the Board of Directors on 25 August 2010. 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.

Statement of Directors' Responsibilities in respect of the European Embedded Value (EEV) Basis Supplementary Information

The Directors have chosen to prepare Supplementary Information in accordance with the EEV Principles issued in May 2004 by the CFO Forum of European Insurance Companies and expanded by the Additional Guidance on European Embedded Value Disclosures issued in October 2005.

When compliance with the EEV Principles is stated, those principles require the Directors to prepare supplementary information in accordance with the Embedded Value Methodology ('EVM') contained in the EEV Principles and to disclose and explain any non-compliance with the EEV guidance included in the EEV Principles.

In preparing the EEV supplementary information, the Directors have:

- Prepared the supplementary information in accordance with the EEV Principles;
- Identified and described the business covered by the EVM;
- Applied the EVM consistently to the covered business;
- Determined assumptions on a realistic basis, having regard to past, current and expected future experience and to any relevant external data, and then applied them consistently;
- Made estimates that are reasonable and consistent; and
- Described the basis on which business that is not covered business has been included in the supplementary information, including any material departures from the accounting framework applicable to the Group's financial statements.

Independent Auditor's Review Report to the Directors of Chesnara plc on the EEV Basis Supplementary Information

We have been engaged by the Company to review the Supplementary Information – European Embedded Value Basis in the half-yearly financial report for the six months ended 30 June 2010 which comprises the summarised EEV consolidated income statement, the summarised EEV consolidated balance sheet, the summarised EEV consolidated statement of changes in equity and the related notes 1 to 9. 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 Supplementary Information – European Embedded Value Basis.

We have reported separately on the condensed financial statements of Chesnara plc for the six months ended 30 June 2010. The information contained in the Supplementary Information – European Embedded Value Basis should be read in conjunction with the condensed set of financial statements prepared on an IFRS basis. This information is described within the Chesnara plc condensed set of financial statements in the half-yearly financial report as having been reviewed.

This report is made solely to the Company's directors in accordance with our engagement letter and solely for the purpose of expressing an opinion as to whether anything has come to our attention that causes us to believe that the Supplementary information – European Embedded Value Basis for the six months ended 30 June 2010 is not prepared, in all material respects, 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. Our work has been undertaken so that we might state to the Company's directors those matters we are required to state to them in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company's directors, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The Supplementary Information – European Embedded Value Basis is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the Supplementary Information – European Embedded Value Basis 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.

Our responsibility

Our responsibility in relation to the Supplementary Information – European Embedded Value Basis is to express to the Company a conclusion on the Supplementary Information – European Embedded Value Basis based on our review.

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the Supplementary information – European Embedded Value Basis for the six months ended 30 June 2010 is not prepared, in all material respects, 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.

Deloitte LLP

Chartered Accountants and Statutory Auditors
Manchester, United Kingdom

25 August 2010

Supplementary Information – European Embedded Value Basis

Summarised Consolidated Interim Income Statement for the six months ended 30 June 2010

	Note	Unaudited Six months ended 30 June		Year ended 31 December
		2010 £000	2009 £000	2009 £000
Operating (loss)/profit of covered business	6	(6,579)	10,075	19,120
Other operational result		(762)	152	868
Operating (loss)/profit		(7,341)	10,227	19,988
Variation from longer-term investment return	6	8,169	(2,710)	13,750
Effect of economic assumption changes	6	(5,834)	293	(9,730)
(Loss)/profit before tax and before exceptional item		(5,006)	7,810	24,008
Exceptional items				
Profit recognised on business combinations	6	989	–	54,187
Effect of modelling improvements	6	10,363	–	–
Profit before tax		6,346	7,810	78,195
Tax	6	(2,399)	(1,433)	12,070
Profit for the period		3,947	6,377	90,265
Attributable to:				
Shareholders		3,947	6,377	90,272
Non-controlling interest		–	–	(7)
		3,947	6,377	90,265
Earnings per share				
Based on profit for the period attributable to shareholders		3.89p	6.28p	88.94p
Diluted earnings per share				
Based on profit for the period attributable to shareholders		3.89p	6.28p	88.94p

Supplementary Information – European Embedded Value Basis

Summarised Consolidated Balance Sheet as at 30 June 2010

	Note	Unaudited Six months ended 30 June		31 December
		2010 £000	2009 £000	2009 £000
Assets				
Value of in force business	5,8	188,074	80,153	198,312
Deferred acquisition costs arising on unmodelled business		640	–	197
Acquired value of customer relationships		1,416	–	346
Internally-developed software		5,456	–	4,060
Property and equipment		681	–	491
Investment in associate		943	–	1,051
Reinsurers' share of insurance contract provisions		209,555	165,377	209,537
Amounts deposited with reinsurers		25,299	21,584	26,240
Investment properties		3,355	3,272	3,355
Deferred tax assets		1,638	–	1,972
Financial assets				
Equity securities at fair value through income		397,509	356,387	454,970
Holdings in collective schemes at fair value through income		1,537,247	589,530	1,612,861
Debt securities at fair value through income		380,057	258,410	247,836
Insurance and other receivables		27,477	9,812	19,822
Prepayments		3,396	2,920	3,784
Policyholders' funds held by the Group		44,336	–	41,107
Derivative financial instruments		7,405	2,410	7,964
Total financial assets		2,397,427	1,219,469	2,388,344
Reinsurers' share of accrued policy claims		3,996	3,519	4,728
Income taxes		941	–	395
Cash and cash equivalents		174,183	178,789	155,241
Total assets		3,013,604	1,672,163	2,994,269
Liabilities				
Bank overdraft		1,590	2,074	2,312
Insurance contract provisions		1,035,702	893,908	1,049,906
Financial liabilities				
Investment contracts at fair value through income		1,578,342	549,063	1,543,915
Borrowings		28,558	4,194	36,307
Derivative financial instruments		1,542	746	54
Liabilities relating to policyholders' funds held by the Group		44,336	–	41,107
Total financial liabilities		1,652,778	554,003	1,621,383
Provisions		1,696	2,580	1,452
Deferred tax liabilities		–	14	–
Reinsurance payables		21,608	1,772	15,039
Payables related to direct insurance and investment contracts		29,139	24,948	30,433
Income taxes		7,543	6,956	1,313
Other payables		8,417	7,023	9,833
Total liabilities		2,758,473	1,493,278	2,731,671
Net assets		255,131	178,885	262,598
Equity				
Share capital		41,501	41,501	41,501
Share premium		20,458	20,458	20,458
Treasury shares		(3,379)	(3,379)	(3,379)
Other reserves		4,642	–	5,589
Retained earnings		191,909	120,255	198,416
Total shareholders' equity		255,131	178,885	262,585
Non-controlling interest		–	–	13
Total equity		255,131	178,885	262,598

Notes to the Supplementary Information (unaudited)

1. Basis of preparation

This section sets out the detailed methodology followed for producing these Group financial statements which are supplementary to the Group's primary financial statements which have been prepared in accordance with International Financial Reporting Standards ('IFRS'). These financial statements have 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.

In order to improve understanding of the Group's financial position and performance, certain of the information presented in these financial statements is presented on a segmental basis: the business segments are the same as those described in Note 5 to the condensed consolidated interim financial statements prepared on the IFRS basis. The Swedish Business was acquired on 23 July 2009: accordingly, the results relating thereto, as reflected in segmental analysis for prior year information in respect of the financial position as at 31 December 2009 and for the year then ended in respect of the Swedish Business, are for a period just in excess of five months.

2 Covered business

The Group uses EEV methodology to value the bulk of its long-term business (the 'covered business'), which is written primarily in the UK and Sweden, as follows:

- (i) for the UK Business, the covered business comprises the business's long-term business being those individual life insurance, pensions and annuity contracts falling under the definition of long-term insurance business for UK regulatory purposes. The operating expenses of the holding company, Chesnara plc, are treated as an integral part of the UK covered business.
- (ii) for the Swedish Business, the covered business comprises the business's long-term pensions and savings unit-linked business. Group life and sickness business, including waiver of premium and non-linked individual life assurance policies are not included in the covered business: the result relating to this business is established in accordance with IFRS principles and is included within 'other operational result' within the consolidated summarised income statement.

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

UK Business

Much of the covered business is in run-off and is, accordingly, substantially closed to new business. The UK Business does still sell a small amount of new business 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.

Swedish Business

New business, in relation to the pensions and savings covered business is taken as all business where contracts are signed and new premiums paid during the reporting period, for both new policies and premium increases on existing business, but excluding standard renewals. New business premium volume for the period is as follows:

New business premium income relating to pensions and savings covered business,	£12.9m *
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*Basis: annualised premium plus 1/10 single premium translated into sterling at the average rate of SEK 11.2608 = £1.

The new business contribution has been assessed as at the end of the period, using opening assumptions.

Value of in-force business

The cash flows attributable to shareholders arising from in-force business are projected using 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.

The estimates used for projecting the components of the cash flow are best estimate assumptions for the non-economic assumptions and risk free market consistent assumptions for the investment returns.

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. For the UK business, allowance has been made for planned reductions in corporation tax, as announced by the Chancellor in his budget speech on 22 June 2010.

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, excluding those payments made on behalf of policyholders, being policyholder tax in the UK Business and yield tax in the Swedish Business.

Cost of capital

The cost of holding the required capital to support the covered business (see 3(b) 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

UK Business

The principal financial options and guarantees in the UK Business 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.

Swedish Business

In respect of the Swedish Business, some contracts provide policyholders with an investment guarantee, whereby a minimum rate of return is guaranteed for the first 5 years of the policy, at a rate of 3% per annum. As at 30 June 2010, the total amount guaranteed was approximately £0.5m. Thus, due to low volumes and the limited exposure, the value of the guarantee is ignored as not material to the results.

Allowance for risk

Allowance for risk within the covered business is made by:

- (i) setting required capital levels by reference to the assessment of capital needs made by the directors of the regulated entities within the UK and Swedish Businesses (the 'Directors');

Notes to the Supplementary Information (unaudited) (continued)

- (ii) 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
- (iii) explicit allowance for the cost of financial options and guarantees.

Internal Group Company

EEV Guidance requires that actual and expected profit or loss incurred by an internal group company on services provided to the covered business should be included in allowances for expenses. The covered business in the Swedish Business is partially managed by an internal group fund management company. Not all relevant future income and expenses of that company have been included in the calculation of embedded value. However, the effect is not considered to be material.

(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 respective businesses. 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 (a) for the UK Business, 150% of the long-term insurance capital requirement ('LTICR') together with 100% of the resilience capital requirement ('RCR'), as determined by the regulations of the Financial Services Authority in the UK and (b) for the Swedish Business, 150% of the regulatory solvency requirement as determined by Finansinspektionen in Sweden.

The required level of regulatory capital is provided as follows:

- (i) for the UK Business, by the retained surplus within the long-term business fund and by share capital and retained earnings within the shareholder funds of the regulated entity; and
- (ii) for the Swedish Business, by share capital and additional equity contributions from the parent company, net of the accumulated deficit in the regulated entity, these components together comprising shareholder's equity.

The Swedish Business is reliant, in the medium term, on further equity contributions from the parent company, Chesnara plc.

(c) Discount Rates

The discount rates are a combination of the reference rate and a risk margin. The reference 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 discount rates, the Group 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 discount rate and bond-based cash flows at a bond discount rate. In practice a short-cut method known as the 'certainty equivalent' approach has been adopted. This method assumes that all cash flows earn the reference rate of return and are discounted at the reference rate.

In general, and consistent with the market's approach to valuing financial instruments for hedging purposes, the reference rate is based on swap yields. These have been taken as mid swap yields available in the market at the end of the reporting period.

Allowance also needs to be made for non-market risks. For some of these risks, such as 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 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 has been added. The margin added reflects the assumed risks within the businesses and is 50 basis points for the UK Business and 70 basis points for the Swedish Business.

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. For the UK Business, the expenses relating to corporate governance functions eliminate any taxable investment return in shareholder funds, while investment management fees are not material. For the Swedish Business, appropriate allowance is made for the cost of tax on locked-in capital and the cost for an investor of owning an asset indirectly via an investment policy rather than by direct investment into the underlying assets.

(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, calculated on opening assumptions.

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

- (i) the expected return, being the unwind of the discount rates 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 reported at each reporting date. The current practice is detailed below.

Each year the demographic assumptions are reviewed as part of year-end processes and hence were reviewed in December 2009.

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 UK covered business, except for a relatively small amount of expense, which is assumed to relate to business development functions, to reflect effort expended within the holding company relating to 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.

Notes to the Supplementary Information (unaudited) (continued)

In addition, the demographic assumptions used at December 2009 are considered to be best estimate for both the UK and Swedish business except for, in respect of the Swedish Business, the rate at which pensions business transfers out, where it has been considered appropriate to increase the assumed rate of withdrawal. In respect of the UK Business, 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.

(f) Pension Schemes

In the Swedish Business, where the Group participates in a combined defined benefit and defined contribution scheme, future contributions to the scheme are reflected in the value of in-force business.

(g) Financial Reinsurance

In the Swedish Business the Group uses financial reinsurance to manage the impact of its new business strain. Whilst this liability is valued at fair value within the IFRS statements, allowing for an option which provides the Group with the right to settle the liability early on beneficial terms, when valuing the shareholder net worth within the EEV it is considered more appropriate to assess this liability at a higher cost, reflecting the likelihood of the option not being utilised.

4. Assumptions

(a) Investment Returns (pre-tax)

Investment returns are assumed to be equal to the reference rate, as covered in note 3(c) above. For linked business, the aggregate return has been determined by the reference rate less an appropriate allowance for tax.

	UK Business	Swedish Business
Unaudited 30 June 2010		
Investment return	2.8%	3.05%*
Inflation		
RPI	2.7%	2.0%

	UK Business	Swedish Business
Unaudited 30 June 2009		
Investment return	4.3%	n/a
Inflation		
RPI	2.4%	n/a

	UK Business	Swedish Business
31 December 2009		
Investment return	3.8%	3.74%*
Inflation		
RPI	2.9%	2.0%

* A full swap rate curve is used: the rate quoted is for a term of ten years and is presented as an indicative rate.

(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, for the UK business, allows for changes in corporation tax announced by the Chancellor in his budget speech of 22 June 2010 and therefore reflects a reduction from the current 28% to 24% in steps of 1%.

(d) Expenses

The expense levels are based on internal expense analysis investigations and are appropriately allocated to the new business and policy maintenance functions.

For the UK Business, 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.

For the Swedish Business, these have been determined by reference to:

- (i) an expense analysis in which all expenses were allocated to covered and uncovered business, with expenses for the covered business being allocated to acquisition and maintenance activities; and
- (ii) expense drivers, being, in relation to acquisition costs, the number of policies sold during the period and, in relation to maintenance expenses, the average number of policies in force during the period.

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

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

(e) Discount Rate

An explicit constant margin is added to the reference 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, which is 50 basis points for the UK Business and 70 basis points for the Swedish Business, gives due recognition to the fact that:

(a) For the UK Business:

- (i) the covered business is substantially closed to new business;
- (ii) there is no significant exposure in the with profit business, which is wholly reinsured;
- (iii) expense risk is limited as a result of the outsourcing of substantially all policy administration and related 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.

(b) For the Swedish Business:

- (i) the covered business remains open;
- (ii) the in-force business is relatively small;
- (iii) reinsurance is used to significantly reduce insurance risks; and
- (iv) a number of the risks provide diversification benefits within the Chesnara Group, in relation to reinsurance counterparties, market exposures and policyholder populations.

The sensitivity of the value of in-force business to the discount rate is greater for the Swedish Business than for the UK Business and the relative margins provided by these adjustments are more material (more than twice) for the Swedish Business than for the UK Business, which reflects these different risks.

Notes to the Supplementary Information (unaudited) (continued)

	UK Business	Swedish Business
Unaudited 30 June 2010		
Reference rate	2.9%	3.05%*
Non-diversifiable risk	0.5%	0.7%
Discount rate	3.4%	3.75%*

	UK Business	Swedish Business
Unaudited 30 June 2009		
Reference rate	4.3%	—
Non-diversifiable risk	0.5%	—
Discount rate	4.8%	—

	UK Business	Swedish Business
31 December 2009		
Reference rate	3.8%	3.74%*
Non-diversifiable risk	0.5%	0.7%
Discount rate	4.3%	4.44%*

*A full swap curve is used: the rate quoted is for a term of ten years and is presented as an indicative rate.

5 Analysis of shareholders' equity

	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Unaudited 30 June 2010				
Regulated entities				
Capital required	31,712	10,608	—	42,320
Free surplus	26,811	11,552	—	38,363
Shareholders' net worth of regulated entities	58,523	22,160	—	80,683
Adjustments to shareholder net worth				
Deferred acquisition costs	—	(44,576)	—	(44,576)
Financial reinsurance liability	—	(5,232)	—	(5,232)
Other asset/liability adjustments	—	6,872	—	6,872
Adjusted shareholder net worth	58,523	(20,776)	—	37,747
In-force value of covered business	73,581	114,493	—	188,074
Embedded value of regulated entities	132,104	93,717	—	225,821
Net equity of other Group companies	—	(2,194)	31,504	29,310
Total shareholders' equity	132,104	91,523	31,504	255,131

Unaudited 30 June 2009	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Regulated entities				
Capital required	33,494	–	–	33,494
Free surplus	21,528	–	–	21,528
Shareholders' net worth of regulated entities	55,022	–	–	55,022
Adjustments to shareholder net worth				
Deferred acquisition costs	–	–	–	–
Financial reinsurance liability	–	–	–	–
Other asset/liability adjustments	–	–	–	–
Adjusted shareholder net worth	55,022	–	–	55,022
In-force value of covered business	80,153	–	–	80,153
Embedded value of regulated entities	135,175	–	–	135,175
Less: amount financed by borrowings	(4,194)	–	–	(4,194)
Embedded value of regulated entities attributable to shareholders	130,981	–	–	130,981
Net equity of other Group companies	–	–	47,904	47,904
Total shareholders' equity	130,981	–	47,904	178,885

Unaudited 30 June 2009	UK Business £000	Swedish Business £000	Other Group Activities £000	Total £000
Regulated entities				
Capital required	32,042	12,123	–	44,165
Free surplus	40,253	12,337	–	52,590
Shareholders' net worth of regulated entities	72,295	24,460	–	96,755
Adjustments to shareholder net worth				
Deferred acquisition costs	–	(44,721)	–	(44,721)
Financial reinsurance liability	–	(5,313)	–	(5,313)
Other asset/liability adjustments	–	4,299	–	4,299
Adjusted shareholder net worth	72,295	(21,275)	–	51,020
In-force value of covered business	85,559	112,753	–	198,312
Embedded value of regulated entities	157,854	91,478	–	249,332
Less: amount financed by borrowings	(4,197)	–	–	(4,197)
Embedded value of regulated entities attributable to shareholders	153,657	91,478	–	245,135
Net equity of other Group companies	–	(1,048)	18,498	17,450
Total shareholders' equity	153,657	90,430	18,498	262,585

Notes to the Supplementary Information (unaudited) (continued)

6 Summarised statement of changes in equity and analysis of profit

(a) *Changes in equity may be summarised as:*

	Unaudited Six months ended 30 June		Year ended 31 December
	2010 £000	2009 £000	2009 £000
Shareholders' equity at beginning of period	262,585	182,708	182,708
Effect of modelling improvements	10,363	–	–
Shareholders' equity at beginning of period restated	272,948	182,708	182,708
Profit for the period attributable to shareholders	(6,416)	6,377	90,272
Foreign exchange reserve movement	(947)	–	5,539
Dividends paid	(10,454)	(10,200)	(15,934)
Shareholders' equity at end of period	255,131	178,885	262,585

During the first half of 2010 the Swedish Business introduced a new system for modelling value-in-force, which provided the capability for (i) more accurately modelling the impact on commission paid of policies becoming paid-up and (ii) for determining future fee income on a case-by-case investment mix basis, whereas previously it had been necessary to adopt high-level estimates.

The effect of the modelling improvements is classified as an exceptional credit in the consolidated income statement and is presented after operating (loss)/profit.

(b) *The profit for the period is analysed as:*

	UK Business	Swedish Business	Total
Unaudited six months ended 30 June 2010	£000	£000	£000
Covered business			
New business contribution	383	288	671
Return from in-force business			
Expected return	2,688	1,529	4,217
Experience variances	7,204	(5,374)	1,830
Operating assumption changes	(853)	(11,074)	(11,927)
Return on shareholder net worth	530	(1,900)	(1,370)
Operating profit/(loss) of covered business	9,952	(16,531)	(6,579)
Variation from longer-term investment return	4,069	4,100	8,169
Effect of economic assumption changes	(8,918)	3,084	(5,834)
Profit on covered business before tax	5,103	(9,347)	(4,244)
Tax thereon	(2,428)	29	(2,399)
Profit/(loss) on covered business after tax	2,675	(9,318)	(6,643)
Results of non-covered business and of other group companies			
Profit before tax, and exceptional item			(762)
Exceptional profit recognised on business combination			989
Tax			–
Profit after tax			(6,416)

The determination of profit recognised on business combination relates to the acquisition by the Swedish Business of certain of the net assets of Aspis Försäkringar Liv AB and is set out in Note 4 to the IFRS financial statements.

	UK Business	Swedish Business	Total
Unaudited six months ended 30 June 2009	£000	£000	£000
Covered business			
New business contribution	188	–	188
Return from in-force business			
Expected return	3,965	–	3,965
Experience variances	6,651	–	6,651
Operating assumption changes	(218)	–	(218)
Return on shareholder net worth	(511)	–	(511)
Operating profit	10,075	–	10,075
Variation from longer-term investment return	(2,710)	–	(2,710)
Effect of economic assumption changes	293	–	293
Profit on covered business before tax	7,658	–	7,658
Tax thereon	(1,392)	–	(1,392)
Profit on covered business after tax	6,266	–	6,266
Results of non-covered business and of other group companies			
Profit before tax			152
Tax			(41)
Profit after tax			6,377
Non-controlling interest			–
Profit for the period attributable to shareholders			6,377

	UK Business	Swedish Business	Total
Year ended 31 December 2009	£000	£000	£000
Covered business			
New business contribution	1,482	783	2,265
Return from in-force business			
Expected return	7,357	1,682	9,039
Experience variances	4,499	2,060	6,559
Operating assumption changes	8,862	(7,405)	1,457
Return on shareholder net worth	(200)	–	(200)
Operating profit	22,000	(2,880)	19,120
Variation from longer-term investment return	6,206	7,544	13,750
Effect of economic assumption changes	(12,286)	2,556	(9,730)
Profit on covered business before tax	15,920	7,220	23,140
Tax thereon	11,893	–	11,893
Profit on covered business after tax	27,813	7,220	35,033
Results of non-covered business and of other group companies			
Profit before tax, and exceptional item			868
Exceptional profit recognised on business combination			54,187
Tax			177
Profit after tax			90,265
Non-controlling interest			7
Profit for the period attributable to shareholders			90,272

Notes to the Supplementary Information (unaudited) (continued)

The results of the non-covered business and of other Group companies before tax and before exceptional item are presented as 'other operating income' in the consolidated income statement. For UK Business, the result of the covered business includes the expenses of the holding company, with an equal and opposite adjustment to the result of the non-covered business and of other Group companies.

Included within the effect of economic assumption changes in respect of the UK Business for the year ended 31 December 2009 is an amount of £5,620,000 being a reduction of pre-tax profit relating to a change in the basis of taxation of overseas dividends. This change leads to a reduction in the estimate of future deductions for taxation from policyholder linked funds and is matched by a broadly offsetting reduction in the estimate of future tax payable. This is a significant component of the tax credit of £11,893,000 in respect of tax for the UK Business for the year ended 31 December 2009 as shown above.

7 Sensitivities to alternative assumptions

The following tables show the sensitivity of the embedded value as reported at 30 June 2010, and of the new business contribution of the Swedish Business, 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 of the UK Business for the period ended 30 June 2010 as the reported level of new business contribution is not considered to be material (see Note (3a) above).

	Unaudited Embedded Value		Unaudited New Business Contribution
	UK Business £m	Swedish Business £m	Swedish Business £m
Published value as at 30 June 2010	132.1	91.5	0.3
Changes in embedded value/new business contribution arising from:			
Economic sensitivities			
100 basis point increase in yield curve	(4.7)	6.5	0.3
100 basis point reduction in yield curve	1.2	(7.4)	(0.4)
10% decrease in equity and property values	(3.4)	(7.4)	(0.3)
Operating sensitivities			
10% decrease in maintenance expenses	2.1	6.3	0.3
10% decrease in lapse rates	2.0	7.9	0.4
5% decrease in mortality/morbidity rates			
Assurances	1.2	0.2	—
Annuities	(1.5)	n/a	n/a
Reduction in the required capital to statutory minimum	0.2	—	—

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

Economic sensitivities

- (i) 100 basis point increase in the yield curve. The reference rate is increased by 1%. The rate of future inflation has also been increased by 1% so that real yields remain constant;
- (ii) 100 basis point reduction in the yield curve. The reference rate is reduced by 1%. The rate of future inflation has also been reduced by 1% so that real yields remain constant; 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 95% of the parameters in a selected mortality/morbidity table reducing to 90.25% 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 that defined in Note 3(b) above to the minimum requirement prescribed by 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 reference rate.

Excluding the sensitivities relating to a 100 basis point increase and reduction in the yield curve, both of which are presented, 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 shareholders' equity on the EEV basis

Unaudited 30 June 2010	Swedish Business £000	UK Business £000	Other Group Activities £000	Total £000
Shareholders' equity on the IFRS basis	43,388	81,904	31,504	156,796
Adjustments				
Deferred acquisition costs				
Investment contracts	(3,121)	(6,656)	–	(9,777)
Deferred income	–	11,465	–	11,465
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	–	(14,009)	–	(14,009)
Adjustments to provisions on insurance contracts, net of reinsurers' share	–	(78)	–	(78)
Acquired in-force value	(57,408)	(16,909)	–	(74,317)
Acquired value of customer relationships	(2,082)	–	–	(2,082)
Adjustment to borrowings	(6,106)	–	–	(6,106)
Deferred tax	2,359	2,806	–	5,165
Shareholder net worth	(22,970)	58,523	31,504	67,057
Value of in-force business	114,493	73,581	–	188,074
Shareholders' equity on the EEV basis	91,523	132,104	31,504	255,131
Shareholder net worth comprises:				
Shareholder net worth in regulated entities	(20,776)	58,523	–	37,747
Shareholders' net equity in other Group companies	(2,194)	–	31,504	29,310
Debt finance	–	–	–	–
Total	(22,970)	58,523	31,504	67,057

Notes to the Supplementary Information (unaudited) (continued)

Unaudited 30 June 2009	Swedish Business £000	UK Business £000	Other Group Activities £000	Total £000
Shareholders' equity on the IFRS basis	–	76,553	47,904	124,457
Adjustments				
Deferred acquisition costs				
Investment contracts	–	(7,590)	–	(7,590)
Deferred income	–	12,938	–	12,938
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	–	(13,967)	–	(13,967)
Adjustments to provisions on insurance contracts, net of reinsurers' share	–	(126)	–	(126)
Acquired in-force value	–	(19,636)	–	(19,636)
Acquired value of customer relationships	–	–	–	–
Adjustment to borrowings	–	–	–	–
Deferred tax	–	2,656	–	2,656
Shareholder net worth	–	50,828	47,904	98,732
Value of in-force business	–	80,153	–	80,153
Shareholders' equity on the EEV basis	–	130,981	47,904	178,885
Shareholder net worth comprises:				
Shareholder net worth in regulated entities	–	55,022	–	55,022
Shareholders' net equity in other Group companies	–	–	47,904	47,904
Debt finance	–	(4,194)	–	(4,194)
Total	–	50,828	47,904	98,732

31 December 2009	Swedish Business £000	UK Business £000	Other Group Activities £000	Total £000
Shareholders' equity on the IFRS basis	47,696	93,561	18,498	159,755
Adjustments				
Deferred acquisition costs				
Investment contracts	(1,447)	(7,173)	–	(8,620)
Deferred income	–	12,319	–	12,319
Adjustment to provisions on investment contracts, net of amounts deposited with reinsurers	–	(15,038)	–	(15,038)
Adjustments to provisions on insurance contracts, net of reinsurers' share	–	(238)	–	(238)
Acquired in-force value	(61,675)	(18,282)	–	(79,957)
Acquired value of customer relationships	(2,336)	–	–	(2,336)
Adjustment to borrowings	(5,073)	–	–	(5,073)
Deferred tax	512	2,949	–	3,461
Shareholder net worth	(22,323)	68,098	18,498	64,273
Value of in-force business	112,753	85,559	–	198,312
Shareholders' equity on the EEV basis	90,430	153,657	18,498	262,585
Shareholder net worth comprises:				
Shareholder net worth in regulated entities	(21,275)	72,295	–	51,020
Shareholders' net equity in other Group companies	(1,048)	–	18,498	17,450
Debt finance	–	(4,197)	–	(4,197)
Total	(22,323)	68,098	18,498	64,273

9 Foreign exchange translation reserve

A foreign exchange translation reserve arises on the translation of the financial statements of the Swedish Business, the functional currency of which is the Swedish Krona, into pounds sterling, which is the presentational currency of the Group financial statements. Items in the consolidated income statement are translated at the average exchange rate of SEK 11.2608 = £1 ruling in the reported period (31 December 2009: SEK 11.5594 = £1), while all items in the balance sheet are stated at the closing rates ruling at the reported balance sheet date, being SEK 11.6438 = £1 at 30 June 2010 (31 December 2009: 11.5305). The differences arising on translation using this methodology are recognised directly in shareholders' equity within the foreign exchange translation reserve.

The reported embedded value is sensitive to movements in the SEK:£ exchange rate. Had the exchange rate as at 30 June 2010 been 10% higher at SEK 12.8082 = £1, then the reported embedded value of £255.1m as at 30 June 2010 would have been reported as £246.8m.

