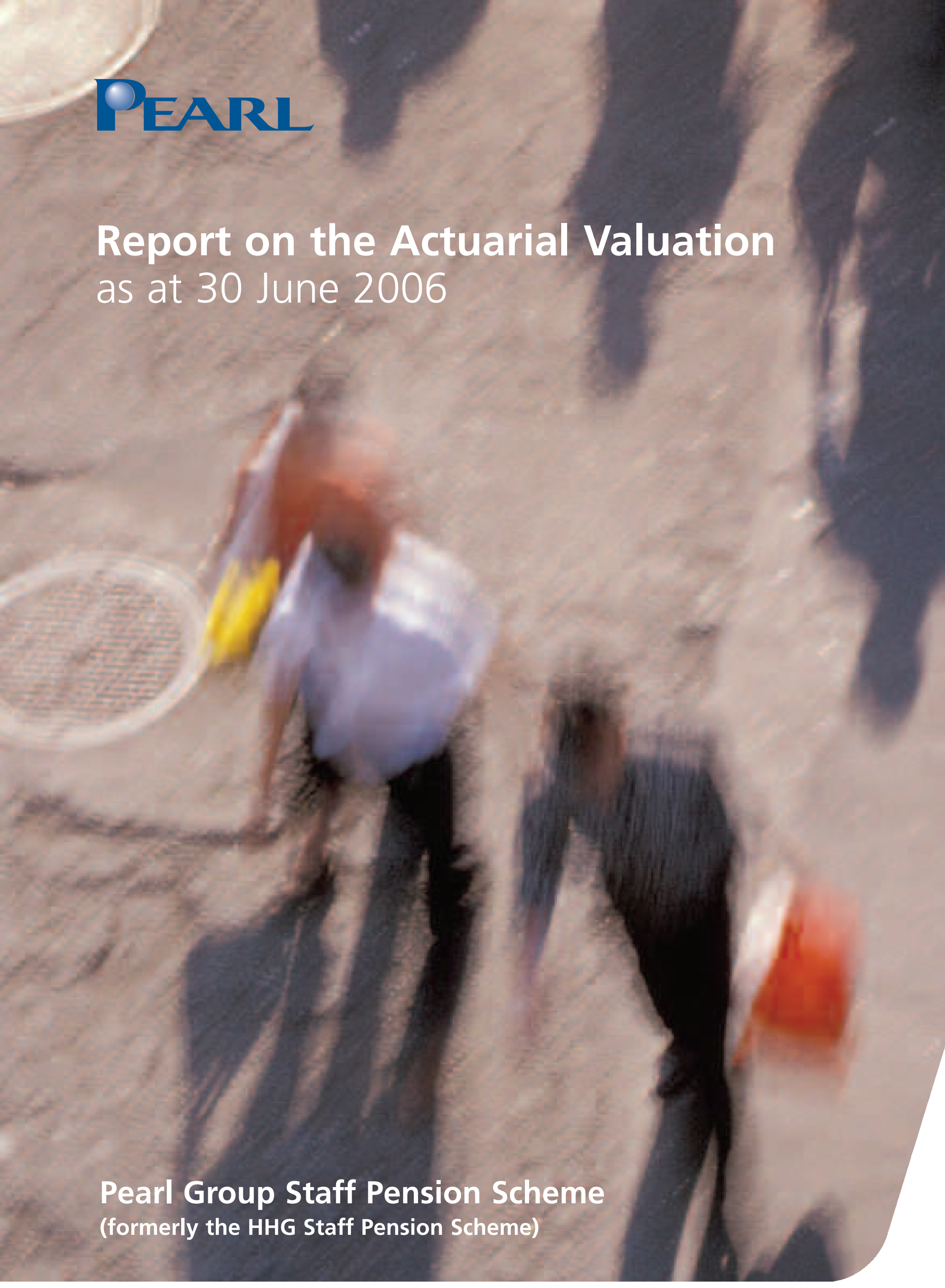


PEARL

Report on the Actuarial Valuation
as at 30 June 2006

Pearl Group Staff Pension Scheme
(formerly the HHG Staff Pension Scheme)

Contents

Welcome

Welcome to the Pearl Group Staff Pension Scheme Actuarial Valuation Report. This report contains a summary of the actuarial valuation carried out by Watson Wyatt Limited as at 30 June 2006.

Originally planned for 31 December 2006, the date of the valuation was brought forward, following discussions between the Company and the Trustee around the future funding of the Scheme.

Inside we explain:

- The new funding agreement
- The new scheme-specific funding requirements
- The membership and demographic information used
- The financial assumptions used
- The conclusions of the valuation

The summary funding statement (for Final Salary section members only) is also included in this report.

Funding agreement

The Trustee Board is delighted to advise that it has negotiated an agreement with the Company, which will help to ensure the long-term security of the Pearl Group Staff Pension Scheme and create a strong collaborative relationship to manage the investments of the Scheme.

- The Trustee has secured the Company's agreement to a new and significantly more conservative basis of valuation. Valuing the Scheme's liabilities in this way means that we take less credit than previously for expected future investment returns. Under the new basis, the amount we would need to earn on our assets to pay for those benefits will be in line with Government bond yields (known as a 'Gilts' basis). At the same time we have taken the opportunity to make increased allowances for the lengthening lifespans of our members. By choosing this valuation approach, the apparent value of the Scheme's liabilities significantly increases. This in turn means that the Company has agreed indirectly to provide greatly increased amounts of funding for the Scheme to make up this gap over time.

- The Trustee has established a Funding Guarantee with the Company. The Company will guarantee returns on the Scheme's assets sufficient to remove the funding shortfall by 30 June 2027. If investment returns are below the guaranteed return, the Company will make additional contributions after each triennial valuation. Any investment returns achieved above the guaranteed return will be retained within an escrow account to provide additional contingent security until the Gilt funding target is reached.

- As part of the agreement, the oversight of the management of the assets of the Final Salary sections of the Scheme will be transferred to Axial, Pearl Group's in-house investment company, who will place the investments with a range of diversified specialist fund managers.

Money Purchase/Defined Contribution (DC) members

The changes to the management of the assets are in respect of the funding of the Final Salary sections of the Scheme only. There are currently no changes planned for members of the Money Purchase section, although the Trustee will continue to keep the funds under review.

Key elements of the funding agreement

The following provides more detail on the key elements of the agreement that the Trustee has secured with the Company:

1. A target of 100% 'Gilt' funding by 30 June 2027
2. Target improved funding levels for each three-year point to 30 June 2027
3. A guarantee from the Company to provide funds to meet these three-year targets should investment performance of the funds not achieve required levels
4. A new diversified and innovative investment strategy agreed with the Company's investment arm (Axial) and implemented by them
5. £50 million of payments by the Company into an escrow fund to improve short-term security which will be retained in that fund (together with any excess investment returns) until 30 June 2027
6. An undertaking that, during the lifetime of the agreement, further payments may be made to the escrow fund to guard against diminution in the 'embedded value' of the remainder of the Life Company's business
7. The continued independence of the Trustee Board (any changes to the board membership to be agreed with the Trustee)
8. The administrative and non-investment expenses of the Scheme during the period to 30 June 2027 will be met directly by the Company

The new scheme-specific funding requirements

The main responsibility of the Scheme Actuary, Neil Wearing of Watson Wyatt, is to carry out regular funding valuations of the Scheme, called actuarial valuations, normally every three years.

This involves him checking that the amount of money invested in the Scheme (the assets) is sufficient to pay for benefits earned (the liabilities). He also calculates the rate of future contributions needed to ensure the financial health of the Scheme in future years. Finally, he provides input to help the Trustee and its investment adviser to set the Scheme's investment policy.

The actuarial valuation as at 30 June 2006 was the first to be carried out under the new funding regime established by the Pensions Act 2004. This system, based on a Statutory Funding Objective (SFO), has been developed by the Pensions Regulator through a series of regulations and codes of practice. The Pensions Regulator has powers to enforce these regulations.

Unlike the Minimum Funding Requirement (MFR), which it has replaced, the new Statutory Funding Objective is specific to the Scheme. This essentially means that the Scheme must hold sufficient and appropriate assets to meet its 'technical provisions' – the target level of assets that the Trustee and the Company decide is appropriate to meet all the promised Scheme benefits both now and in the future.

The Trustee has prepared a 'Statement of Funding Principles', which sets out its policy for meeting the SFO, which was agreed with the Company. The Statement of Funding Principles sets out the Trustee's choice of methods and assumptions for determining the Scheme's technical provisions, after taking advice from the Actuary.


clean up?

The underlying assumptions

In carrying out the valuation, the Actuary has to make certain assumptions about future events, for example, future investments returns, rates of inflation, salaries, average lifespan and so on, as they will all have an effect on the value of the Scheme's liabilities in five, 10 or even 50 years' time.

Scheme demographics

Demographic assumptions concern the likelihood of events such as death, retirement and leaving service taking place at different ages. At each valuation the experience over the period since the previous valuation is reviewed to assess if the assumptions adopted previously remain appropriate. The results of the analysis on this occasion were as follows:

- *Pensioner mortality*
  The improvements in mortality rates anticipated in the 2003 valuation have proved true. Future improvements in mortality have also been allowed for.

- *Family statistics*
  The 2003 valuation assumptions regarding proportion married and age differences have been updated for consistency over membership classes for the 2006 valuation.

- *In-service demographics (including such considerations as employee turnover, mortality, early and ill-health retirement, and salary increases)*
  For the purpose of the 2006 valuation, the Actuary retained the 2003 valuation assumptions.

Scheme benefits

The Pension Scheme has four sections with different benefit structures, and the Actuary took these into account when valuing the Scheme benefits. A summary of the Scheme benefits is available on the website (www.pearlstaffpensionscheme.co.uk) or by calling the Scheme Administrators (contact details on page 20).

Financial assumptions

The Actuary takes into account the current and expected future distribution of assets and makes assumptions about what will happen to investments, salaries and pensions in the future. He uses an assumed rate of price inflation and from that makes relative assumptions about other important financial data.

Basis	**Assumptions used at 30 June 2006**	
	Real (relative to price inflation) % per annum	**Absolute % per annum**
Long-term rate of:		
Price inflation (RPI)	0.0	3.0
Salary increases	1.5	4.5
Pension increases in payment		
- 5% per annum or RPI if lower	0.0	3.0
- 3% per annum or RPI if lower	-0.25	2.75
Discount rate	Varying by duration reflecting yields on Gilts	Varying by duration reflecting yields on Gilts

Membership information

The Actuary takes into account the membership at the valuation date. He considers members' ages and their salaries or pensions. Some of the data used for this valuation is shown below.

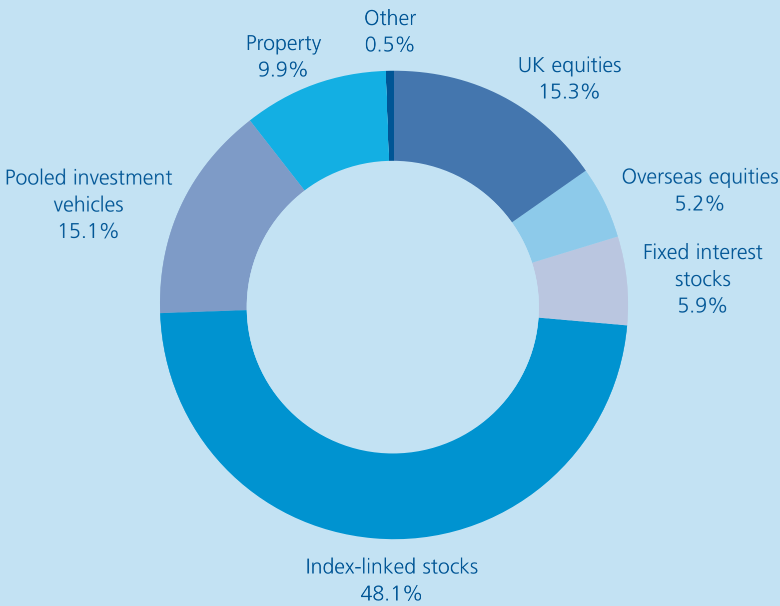
Active members (final salary sections, including hybrids)	Number	Pensionable earnings p.a.
Men	40	£2.2m
Women	28	£1.0m
Total	**68**	**£3.2m**
Deferred pensioners	**Number**	**Annual deferred pensions p.a.**
Men	8,902	£30.8m
Women	5,950	£13.5m
Total	**14,852**	**£44.3m**
Pensioners	**Number**	**Annual pensions p.a.**
Men	5,014	£46.7m
Women	1,877	£5.7m
Dependants	2,063	£9.7m
Total	**8,954**	**£62.1m**

Notes:

- Hybrid members are members who have Final Salary benefits but switched to accrue future benefits on a Money Purchase basis
- The Final Salary sections' active membership at 30 June 2006 includes nine hybrid members with pensionable earnings of £0.4 million
- The deferred pensioner membership includes 698 hybrid members with a total final salary pension of £3 million
- There are 110 pure Money Purchase active members with a total salary roll of £5.3 million
- Fourteen active members who transferred to First Actuarial plc after the valuation date have been included in the deferred pensioner membership

Assets

Actual assets held at 30 June 2006



Axial Investment Management

Pearl Group Limited has invested heavily to create a new top-flight asset and risk management business, Axial Investment Management.

Axial Investment Management is an FSA regulated fund manager and a division of Pearl Group responsible for the investment and oversight of the Group's funds. It oversees the management of more than £28 billion in client assets. The majority of Axial's funds are externally managed. You can find out more at www.pearlgrouplimited.co.uk

Valuing the Scheme's liabilities

In the valuation, the Scheme's Actuary compares the assets the Scheme is building up (through its investments, in its bank balances and any money owed to the Scheme), with the liabilities the Scheme has to pay, including administrative expenses and benefits for members and their families.

Previous valuation basis

This is the basis used in the previous valuation as at 31 December 2003 and reflected the expected return on the Scheme's assets (a mixture of equities, bonds and property). The funding level at this time was 101% (a surplus of £9 million). A summary of how this position has changed to the new valuation basis is shown on the following page.

Our new valuation basis

The table below shows the results of the valuation on the new 'Gilts' basis as at 30 June 2006. This is the amount that would be likely to enable the Trustee to meet the Scheme's future liabilities without further support from the Company.

Past service liabilities

Value of past service liabilities in respect of:

Pensioners and dependants	£1,045m
Deferred pensioners	£1,015m
Active members	£20m
Money purchase and AVCs	£40m
Expenses	£19m
Total past service liabilities	**£2,139m**
Market value of assets	**£1,756m**
Excess of liabilities over assets	**£383m**
Funding level	**82%**

Summary of changes from the position in 2003 to the position in 2006

Surplus (£9 million) brought forward with interest	£10m
Payments from escrow account	£20m
Better-than-assumed investment returns	£165m
Effect of more active members leaving than assumed	£20m
Miscellaneous, including pensioner mortality experience	£19m
Surplus on 2003 assumptions	**£234m**
Effect of updated demographic assumptions	(£70m)
Surplus allowing for changed demographics only	**£164m**
Effect of updated financial assumptions	(£547m)
Deficit as at 30 June 2006	**(£383m)**

Scheme year-end change

To tie in with the funding agreement, the Scheme year-end has been changed to 30 June. The next set of audited accounts will be for the 18-month period from 1 January 2007 to 30 June 2008. The Short Report to members will now be issued in the first quarter of each year with the next report due in Spring 2008.

Conclusions

- The Scheme's liabilities as at the valuation date totalled £2,139 million. This means that the assets (including Money Purchase funds and AVCs) would have covered 82% of the Scheme's liabilities in respect of benefits for service up to 30 June 2006.

- In accordance with the new scheme-specific funding requirements, stemming from the Pensions Act 2004, the Trustee and Company have agreed that the employer's contributions in respect of future service will be paid to the Scheme as follows:
  - Final Salary sections: 48.8% of pensionable earnings
  - Hybrid members: 19.1% of pensionable earnings
  - Money Purchase section: 12.4% of pensionable earnings

- The Company and the Trustee have entered into a contract under which the Company will guarantee returns on the Scheme's assets sufficient to remove the funding shortfall by 30 June 2027 (see page 4).

- There is one remaining payment due from the escrow account set up under the Escrow Deed dated 29 March 2005. This will be made in June 2008.

- In addition, to provide additional security in the unlikely event of the Company becoming insolvent, an escrow account has been set up by the Company with an initial contribution of £10 million. Further contributions of £8 million p.a. will be made to the escrow account by the Company from 2010 to 2014 inclusive.

- Had the Scheme discontinued on the valuation date, then overall the Scheme's assets would have been about 75% of the estimated discontinuance liabilities. However, allowing for the statutory priority order, the assets would have been sufficient to cover 100% of the Pension Protection Fund (PPF) liabilities but only around 20% of the Scheme benefits above the PPF benefits. At the valuation date the assets of the Scheme were equal to 119% of the PPF liabilities.

Summary Funding Statement*

Final Salary sections only

As part of the discussions around the future funding of the Scheme, the valuation due at 31 December 2006 was brought forward and carried out by the Scheme Actuary as at 30 June 2006. This valuation of the Scheme showed that on 30 June 2006 the funding position (excluding Money Purchase section and AVC assets and liabilities) was as follows:

Assets	£1,716 million
Amount needed to provide benefits (technical provisions)	£2,099 million
Shortfall	£383 million
Funding level	82%

As a result, the Trustee and Pearl Group Limited have entered into an agreement to reduce this deficit over the next 20 years to reach the target of 100% 'Gilt' funding by 30 June 2027.

The cost of accrual of future service benefits allowing for contributions to be paid annually in December is:

Final Salary section members	48.8% of pensionable earnings
Hybrid members	19.1% of pensionable earnings
Money Purchase members	12.4% of pensionable earnings

If the Scheme had started winding up (full solvency), it is estimated that the assets available would have been sufficient to secure, on average, 75% of benefits for members of the Final Salary sections.

Inclusion of this information does not imply that Pearl Group Limited is thinking of winding-up the Scheme.

*After first scheme-specific funding valuation under the Pensions Act 2004.

Payment to Pearl Group Limited

There has not been any payment to Pearl Group Limited out of Scheme funds since the last statement was issued.

Change in funding position since the previous statement

The results show that the assets were 82% of the amount needed to cover the technical provisions, with a shortfall of assets of £383 million. This compares with asset cover at the previous valuation of 101%, with a surplus of assets of £9 million. The reasons for the change since the previous valuation are the updated demographic and financial assumptions, which have more than offset any gains that have been made through better-than-assumed investment returns and the effect of more active members leaving than assumed.

Important: If you are thinking of leaving the Scheme for any reason, you should consult a professional adviser, such as an independent financial adviser, before taking any action.

How the Scheme operates

How is my pension paid for?

The assets of the Scheme are held in a common fund which is used to pay pensions and other benefits to Scheme members as they fall due. Pearl Group Limited pays contributions into this fund as required. The money to pay for the Final Salary benefits is held in a common fund. It is not held in separate funds for each individual.

How is the amount the Scheme needs worked out?

The Trustee has a funding plan (the Statement of Funding Principles) agreed with Pearl Group Limited, which aims to make sure there is enough money in the Scheme to pay for pensions now and in the future. The amount of money that Pearl Group Limited pays into the Scheme may go up or down following regular funding checks by our Actuary (called actuarial valuations).

The importance of Pearl Group Limited's support

The Trustee's objective is to have enough money in the Scheme to pay pensions now and in the future. However, the success of the Scheme relies on Pearl Group Limited continuing to support it because:

- Pearl Group Limited will be paying the future expenses of running the Scheme on an annual basis

- the funding level can fluctuate, and when there is a funding shortfall, Pearl Group Limited will usually need to put in more money

- if the target funding level should turn out not to be enough, Pearl Group Limited will need to put in more money

What would happen if the Scheme started to wind up?

Whilst the Scheme remains ongoing, even though funding may temporarily be below target, benefits will continue to be paid in full. If the Scheme winds up, you might not get the full amount of pension you have built up. If the Scheme were to start to wind up, Pearl Group Limited is required to pay enough into the Scheme to enable the members' benefits to be completely secured with an insurance company.

It may be, however, that Pearl Group Limited would not be able to pay this full amount. If Pearl Group Limited became insolvent, the Pension Protection Fund might be able to take over the Scheme and pay compensation to members. Further information and guidance is available on the Pension Protection Fund's website at **www.pension protectionfund.org.uk.** Or you can write to the Pension Protection Fund at Knollys House, 17 Addiscombe Road, Croydon, Surrey, CR0 6SR.

Why does the funding plan not call for full solvency at all times?

The full solvency position assumes that benefits will be secured by buying insurance policies. Insurers are obliged to take a very cautious view of the future and need to make a profit. The cost of securing pensions in this way also incorporates the future expenses involved in administration. By contrast, our funding plan assumes that Pearl Group Limited will continue in business and support the Scheme.

What is the Scheme invested in?

The Trustee's policy is to invest in a broad range of assets. During 2008 Axial will organise the transition of the assets previously held from those classes shown on the left to the categories shown on the right in the table below. The terms 'quantitative' and 'fundamental' relate to types of approaches to managing assets and relate to strategies to achieve outperformance whilst not taking significant market risks.

	Current (prices as at 3.10.07)		Max % after 12 months
	£m	**%**	
Equity	279	15	10
Overseas Equity	293	16	10
Fixed Income/ Index Linked Gilts	1,022	57	10
Private Equity	3	0	10
Property	201	11	20
Cash	25	1	7.5
Quantitative	0	0	45
Fundamental	0	0	65
Commodity	0	0	10
Total	**1,823**		

Where can I get more information?

If you have any other questions, or would like any more information, please contact the Scheme Administrators. A list of more detailed documents that provide further information is listed below. If you want us to send you any of these documents please let us know.

Please help us to keep in touch with you by telling us if you change address.

Additional documents available on request

The *Statement of Funding Principles,* which sets out the Scheme's funding plan.

The Recovery Plan, which explains how the funding shortfall is being made up.

The Statement of Investment Principles, which explains how the Trustee invests the money paid into the Scheme.

The Schedule of Contributions, which shows how much money is being paid into the Scheme.

The Annual Report and Accounts of the Pearl Group Staff Pension Scheme, which shows the Scheme's income and expenditure in the year up to 31 December 2006.

The full Report on the Actuarial Valuation following the Actuary's check of the Scheme's financial situation as at 30 June 2006.

An Annual Benefit Statement – If you are an active member of the Scheme (and have not received a benefit statement in the previous 12 months), you can ask for a statement that provides an illustration of your likely pension.

A 'Frequently Asked Questions' handout – A copy was issued with this booklet but further copies are available on the pension scheme website (www.pearlstaffpensionscheme.co.uk) or by contacting the Scheme Administrators (contact details on page 20).

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Next review

The financial position of the Scheme and the level of contributions required will be reviewed at the next actuarial valuation, which is expected to be carried out no later than 30 June 2009.

Get in touch

If members have any queries concerning their benefits or the valuation, they should contact First Actuarial, the Scheme Administrators.

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