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Prudential Financial, Inc. (PRU)

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. Welcome to Prudential Quarterly Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. Instructions will be given at that time. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Darin Arita. Please go ahead.

Darin Arita

Senior Vice President, Head of Investor Relations, Prudential Financial, Inc.

Thank you, Greg. Good morning, and thank you for joining our call. Representing Prudential on today's call are Charlie Lowrey, Chairman and CEO; Rob Falzon, Vice Chairman; Andy Sullivan, Head of US Businesses; Scott Sleyster, Head of International Businesses; Ken Tanji, Chief Financial Officer; and Rob Axel, Controller and Principal Accounting Officer. We will start with prepared comments by Charlie, Rob and Ken, and then we will take your questions.

Today's presentation may include forward-looking statements. It is possible that actual results may differ materially from the predictions we make today. In addition, this presentation may include references to non-GAAP measures. For a reconciliation of such measures to the comparable GAAP measures and the discussion of factors that could cause actual results to differ materially from those in the forward-looking statements, please see the slide titled Forward-Looking Statements and Non-GAAP Measures in the appendix to today's presentation, which can be found on our website at investor.prudential.com.

With that, I'll hand it over to Charlie.

Charlie F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Thank you, Darin. Good morning, everyone, and thank you for joining us today. Yesterday, we reported fourth quarter earnings per share of $2.33. We also reported an adjusted operating return on equity of 12.1% for the full year. Looking back on 2019, we implemented a number of important actions to enhance our business and financial performance for the long-term. As a result, we have begun 2020 with a clear set of initiatives against which we will execute with a renewed confidence that our businesses can deliver increased earnings performance.

I'll begin this morning by sharing a few accomplishments from 2019. First, we launched a process, talent and technology transformation initiative, which is on track to realize $500 million in run-rate cost savings by 2022. As part of this program, we initiated a Voluntary Separation Program for segments of our US workforce during the fourth quarter, which is reducing our cost base over the course of 2020, and creating a more agile and competitive workforce.

Second, we returned approximately $4 billion to shareholders via dividends and share repurchases. The 10% increase in our dividend represents the 12th consecutive year of dividend increases and produces a yield on book value in excess of 4%. Third, we completed our acquisition of Assurance IQ in October, adding a leading direct-to-consumer financial wellness solutions platform. We're encouraged by the growth in customer demand, the interest from carriers wanting to put their products on the platform, and the level of talent we are attracting from well-known technology companies.

Finally, we made progress in our ongoing efforts to reduce the variability of our quarterly earnings pattern, and we added transparency to our quarterly financial performance. In 2019, our financial performance was impacted by a low interest rate environment, the annual assumption update in our Individual Life business, and higher than typical expenses in our International Businesses. In 2020, we're implementing a number of initiatives to drive improved financial performance in the years ahead. We're focused on executing three key initiatives. First, we remain focused on enhancing the customer experience to produce long-term sustainable growth, while generating $140 million in cost savings this year.

Second, in our International Businesses, we continue to focus on increasing the percentage of earnings coming from growth markets. Supporting this objective, this quarter, we closed on the acquisition of a Colombian pension fund manager with Habitat, expanding our presence in Latin America. We also completed the sale of our Italian insurance business and are exploring strategic options for operations in other markets, including Korea. We'll share further details at the appropriate time. And third, we're continuing to take steps to mitigate the effects of the low interest rate environment such as adjusting the mix and pricing of our products.

Turning to slide 3, I'll briefly touch upon some of the key drivers of our fourth quarter results, which Rob will cover in more detail. Our US Businesses benefited from record account values in Retirement and Individual Annuities. Earnings increased from the prior-year quarter, reflecting higher net investment spread results, partly offset by lower fees in our Annuities business. PGIM, our global asset manager, reported record assets under management of $1.3 trillion as well as higher net asset management fees and other related revenues. Our International Businesses increased earnings, driven by higher net investment spread results and business growth partly offset by higher than typical expenses.

Turning to slide 4, I'd like to touch briefly on four ways we generate value to our stakeholders in a sustainable way. First, we are a purpose-driven company. We strive to make lives better by solving the financial challenges of our changing world and do so for a broad array of stakeholders. Second, in December, our board introduced a multi-stakeholder framework that extends the board's accountability to investors, employees, customers, and society at large, reinforcing the board's commitment and ours to enabling positive change as well as strong financial returns. Third, this multi-stakeholder framework is reflected in our continued pursuit of exemplary environmental, social, and governance practices.

Finally, we provide transparency so investors can measure our progress. We disclose metrics and targets related to the Financial Stability Board's task force on climate-related financial disclosures. This includes quantifying greenhouse gas emissions, recycling, and water usage. In addition, we publish metrics in accordance with the Sustainability Accounting Standards Board.

We continue to be recognized for our commitment and standards we uphold. Just last month, FORTUNE included us on its list of World's Most Admired Companies for the fifth consecutive year. We are proud to have earned the first place distinction in the Life and Health Insurance category each year. In closing, we continue to move quickly and with conviction to execute on our strategy that we put into place including the three initiatives I have outlined for 2020.

With that, I'll turn it over to Rob for a closer look at our business performance for the quarter, and our earnings outlook.

Robert M. Falzon
Vice Chairman, Prudential Financial, Inc.

Thank you, Charlie. I'll provide more color on how we are executing on our strategy within our US, PGIM, and International Businesses and in our near-term earnings growth outlook.

Turning to slide 5, our US Businesses consist of the Workplace Solutions, Individual Solutions, and Assurance IQ divisions that produce a diversified source of earnings from fees, investment spread and underwriting income. Our US Businesses have three key priorities for growth. First, we're investing in transforming our capabilities and the way we work to deliver a better customer experience, while realizing efficiencies that will improve our margins. Second, we will continue to pursue targeted growth opportunities including, by way of example, the non-jumbo Corporate segment of the Full Service Retirement market and the Premier segment of involuntary products offered by our Group Insurance business. And third, we remain committed to expanding our addressable market, including through workplace financial wellness and Assurance IQ.

As a result of the continued thoughtful execution of these priorities, over time, we expect higher earnings growth and improved returns. In the near-term, we expect underlying earnings in the US Businesses to be relatively consistent with current levels as underlying business growth in Retirement, Group Insurance, and Assurance IQ offset the impact from low interest rates and the net outflows in our Individual Annuities business as we maintain pricing discipline. We have included a slide in the appendix that provides our expected underlying earnings outlook by business.

Now, turning to slide 6, PGIM, our asset management business, continues to leverage its diversified multimanager model with global distribution and affiliated flows to grow in higher value-added strategies that serve investors globally. With a record $1.3 trillion of assets under management as of year-end, PGIM is a top-10 global asset manager. It is the fifth largest investor in fixed income globally, and one of the largest in alternative investments with significant real estate and private investment platforms.

We continue to broaden and globalize our products and capabilities by developing and launching private and alternative investment strategies and expanding in both retail and international markets. And as the investment engine of Prudential, PGIM benefits from a symbiotic relationship with our US and International Businesses.

Our investment performance is a key driver of our business success. More than 80% of assets under management have outperformed their benchmarks over the last three-, five- and 10-year periods. This performance helped us to generate $1.9 billion of net third-party flows during the fourth quarter including $1.2 billion of institutional and $700 million of retail net flows. In addition, PGIM rose to the seventh-highest ranking mutual fund franchise based on 2019 net flows, up from 14th in 2018. PGIM's adjusted operating margin of 32% in the fourth quarter was 180 basis points higher than the year-ago quarter and has grown over the last three years as we balance business reinvestment with margin expansion. For the full year 2019, PGIM had a record level of adjusted operating income that was 4% higher than 2018 and 6% higher after adjusting for business acquisition-related costs.

Looking ahead, we believe PGIM is well positioned to deliver mid-to-high single digit earnings growth across the cycle driven by its deep asset class expertise, while leveraging its scale and reach as a global asset manager, and we expect to grow earnings in 2020 despite the absence of the Wells Fargo fee arrangement that ended last year.

Turning to slide 7, our International Businesses continued to benefit from our world-class Japanese life insurance operation where we have a differentiated business model with unique distribution as well as from our focus on other operations in high-growth markets. Life Planner sales increased by 17% compared to the year-ago quarter. This increase was driven by record Life Planner count and higher sales in Brazil, Korea and Taiwan. Sales for Gibraltar were 14% lower than the year-ago quarter. This primarily reflects lower single-pay US dollar fixed annuity sales in our Life Consultant and Independent Agency channels as the recent decline in US interest rates led us to lower crediting rates.

In addition, we continued to focus on quality distribution. The number of Life Planners as a result has declined. The lower Life Consultant sales were partially offset by higher bank channel sales. We continued to innovate new products and implement pricing actions to maintain both sales and our targeted level of profitability. Total inforce for International increased by 3% from the prior year, including a 5% increase in Life Planner and a 1% increase in Gibraltar. In the near-term, we expect total inforce to grow at a similar level. We expect underlying earnings to be relatively consistent with current levels as business growth will offset the impact of low interest rates.

And with that, I'll hand it over to Ken.

Kenneth Yutaka Tanji

Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

Thanks, Rob. I'll begin on slide 8, which provides insight into the earnings for first quarter 2020 relative to our fourth quarter 2019 results.

We begin with pre-tax adjusted operating income in the fourth quarter, which was $1.2 billion and resulted in earnings per share of $2.33 on an after-tax basis. Then we adjust for the following items. First, in the fourth quarter, we had favorable variable investment income driven by equity market performance and prepayment income, which was a benefit of $135 million. Second, the first quarter is expected to have lower seasonal expenses and implementation costs, which will result in a net benefit of $435 million or $0.85 per share and is comprised of two items. The fourth quarter included $160 million of seasonally higher expenses, and $365 million of implementation costs, including the impact from the Voluntary Separation Program.

As indicated in the 8-K filing on December 17, we expect implementation costs of $175 million in 2020 with about $20 million of these costs in the first quarter. And long-term compensation expense for retiree eligible employees is recognized when awards are granted, which is typically in the first quarter of each year. In the first quarter of 2020, we expect this expense to be about $70 million split between PGIM and Corporate & Other. These items net to $0.85 per share.

Third, there are other considerations that we expect will have a $20 million more favorable impact in the first quarter relative to the fourth quarter. And fourth, we anticipate net investment income will be reduced by $10 million, assuming reinvestment rates are held flat with the fourth quarter. Combined, this gets us to a baseline of $2.95 per share for the first quarter of 2020 before including the impact of share repurchases, business growth, and market impacts in 2020. The baseline also includes items specific to the first quarter that reduces EPS by approximately $0.15 per share. While we have provided these items to consider, there may be other factors that affect earnings per share in the first quarter of 2020.

I'd also like to bring your attention to a few additional items that are included in the appendix. On slide 18, we have provided additional information that shows the adjusted operating income roll-forward by business. And on slide 19, we provided updated information regarding seasonal items by business. In addition, we have included some other considerations for 2020 on slide 21, regarding Corporate & Other net costs, the yen foreign exchange rate, and the effective tax rate.

Now, turning to slide 9, I'll provide an update on capital deployment, liquidity, and leverage. We feel very good about the overall strength of our capital position. We returned $900 million to shareholders during the fourth quarter through dividends and share repurchases, which were largely funded by the cash flows generated by our businesses. On December 19, we announced the board's authorization to repurchase up to $2 billion of common stock in 2020. In addition, we increased the first quarter dividend to $1.10 per share, which represents a 10% increase from our dividend in the fourth quarter of 2019, and a 4.4% yield on our adjusted book value.

We also continued to maintain a rock-solid balance sheet. Our regulatory capital ratios continue to be above our AA financial strength targets and our financial leverage ratio remains better than our target. Our cash and liquid assets at the parent company were $4.1 billion at the end of the quarter and at the midpoint of our $3 billion to $5 billion liquidity target range. We will continue to invest in the growth of our businesses, assess acquisition opportunities to build scale or gain capabilities, and return capital to shareholders.

Turning to slide 10, and in summary, we had numerous accomplishments in 2019. We are focused on executing our key initiatives in 2020, leading to greater earnings in 2021.

Now, I'll turn it to the operator for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from the line of Nigel Dally from Morgan Stanley. Please go ahead.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks and good morning. I had a question on Annuities. It's one of the areas that you do expect a decline in earnings in 2020, so I just wanted to check, is that just because of a modest decline in AUM because of the anticipated outflows overwhelming market appreciation, or is there also an underlying element of some deterioration in the return on assets? And if it is the latter, what's driving that?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.

A

So, Nigel, thanks for your question. This is Andy. There's really two major impacts that we're seeing in the Annuities business. One, as you pointed out, is the outflow. That really is coming from we are being very disciplined in our pricing of product and in our return on new sales. And if you look backward, we had some pretty sizable blocks back in the 2010 to 2012 range, so that's creating that outflow. The other thing I would point to though is as that business is rolling across its surrender period, we are seeing business go to lower fee tiers and getting fee pressure from that effect.

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Yeah, Nigel, this is Ken. I'd just add, I know there's been some questions about the ROA. Our primary objective with the profitability of our annuity business is to achieve a high ROE, and our variable annuity business is very profitable and that is evident by the high ROE that's in the high-teens. And that high ROE reflects our unique product design, our robust risk management, and disciplined pricing. And our hedging program is highly effective and it results in very stable earnings, capital and cash flow, even with significant market moves.

So, as a result, our earnings, capital and cash flow will be less sensitive to markets than the account values, and the ROA may move as market moves, but again, our earnings, capital and cash flow will be stable and ROA is simply an outcome. So, the decline in rates and the increase in the equity markets, while it had an increase in account values, had a less meaningful impact on our earnings, again, due to our robust risk management.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Okay, I got it. Second question was just on dividends. Good to see the incremental dividends again this quarter. I think that brings the payout ratio to around 35%. Is there a limit to how high you'd like to go, or is there incremental upside there?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Yeah, sure. So maybe just a little bit of reflection of our capital management and shareholder distribution philosophy that's been very consistent over time, and it starts with our free cash flow which is about 65% of after-tax earnings. This year a little bit better than that. And we then distribute in both the forms of dividends and share repurchases. Our dividends have increased actually 12 years in a row now, and if you looked at the average increase over the last five years, it's been 11%. And now that dividend represents, as I mentioned in my opening comments, a 4.4% yield on book value.

Our board has also authorized $2 billion of share repurchases for 2020, so generally a very consistent approach to our shareholder distributions which balances both dividends and returns of excess capital through share repurchases.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Very helpful. Thank you.

Operator: Your next question comes from the line of Andrew Kligerman from Credit Suisse. Please go ahead.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Q

Hey, good morning. So maybe a question on interest rates. On last quarter's call, you increased your guided interest rate sensitivity to $0.30 of EPS impact for a 50 basis point drop in rates, and now we've seen in 2020 – well, maybe not today, but I was estimating 30 basis points so far in 2020.

So I just want to make sure there are no changes. Should we expect a $0.15 to $0.20 negative impact on 2020 EPS based on that, or are there some other factors at work? And with that, maybe you could tell us what your new money yields are too on the portfolio.

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Yeah, sure. So the sensitivity that we gave to interest rates of 50 basis points at $0.30, that's still good. So that rough rule of thumb and how you applied it, I think that still is appropriate.

Our new money yields in the second half of the year were about 3.65% and you can think of that relative to our – and that's in the US – relative to our US portfolio yield of about 4.2%.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. Thank you. And then just shifting over to the Individual Life segment and kind of thinking back, second quarter you had that $200-plus million charge, third quarter there was about $30 million of underwriting income below expectations, and in 4Q it was about $15 million now below expectations.

So I'm wondering if as we look forward, are you comfortable with underwriting assumptions into the year? And your sales were really robust at $209 million. You cited it as a record since 2013. So what are you selling there that you're excited about?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.

A

Yeah, so, Andrew, it's Andy. Thanks for your question. So we would consider our actual to expected in the fourth quarter, as in line with our expectations. The result was 103%. And I would encourage you to think of there's a [ph] quarter around that – (23:29) plus or minus a couple percent. So we really think that's in line. As far as you referenced the assumption updates. We're seeing that our business performance has been consistent with the updates that we made in the second quarter.

Shifting over to the new business sales, we are very, very pleased with the performance of sales in the Individual Life business. As you cited, it's best quarter in five years. We're probably even more pleased versus the absolute level in the mix of sales. The mix has shifted pretty meaningfully away from guaranteed universal life which obviously is highly interest rate sensitive and over to where almost half of the sales are variable life, which has much, much less sensitivity to interest rates.

So pleased with what we're seeing. The success is really coming from we have a very, very strong brand name. We believe our product portfolio is very strong and our distribution system is top-notch.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Q

And term life, is that the balance of the sales largely?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.

A

Yes.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Q

Awesome. Thanks so much.

Operator: Your next question comes from the line of Tom Gallagher from Evercore ISI. Please go ahead.

Thomas Gallagher
Analyst, Evercore ISI

Q

Good morning. Just the first question on the Assurance IQ deal in terms of how are you thinking about the results so far? It looks to me, based on the disclosure that the revenues are coming in below what was projected initially. I think it was $500 million was the 2019 guide, and it looks closer to maybe $300 million on a full year basis. I guess first question, is that right? And secondly, does that cause you to rethink revenue and earnings projections 2020, 2021?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.

A

So maybe Tom, this is Andy, I'll start, and then I'll hand it off to Ken. So as you'd imagine, these are early days, we just closed the acquisition in October. But I'd tell you, there's a lot of things that we're excited about. We're as we sit here today even more excited about the strategic growth potential of this business.

In fourth quarter, we saw very, very strong consumer demand flow across the platform. We saw 6.5 million shoppers, and just to define that for you, we define a shopper as an individual that has an absolute intention to buy a financial service product and that's willing to share their contact information with us. So we saw 6.5 million shoppers across the platform in 4Q. That's compared against 3.5 million in the year ago quarter. So we're very pleased with the level of consumer flow and consumer demand.

A very positive for us on that is we have product providers literally lining up of every shape and size that want to go ahead and get on the platform. So from a revenue potential perspective, we're every bit as strong as we were. Kind of where we're focused right now is getting those additional products onto the platform.

As far as your numbers around revenue, yeah, our revenue for the year came in just north of $300 million. And really what I would tell you there is we had a lot more consumer demand than we had appointed agents, we'll call it capacity on the platform. We learned some lessons in the quarter around the effort and energy and timeline it takes to get the Medicare Advantage and under 65 health care agents onto the platform. I will tell you that we're already well underway in getting those agents appointed for 4Q of 2020. So that's a completely rectifiable situation and we're well out in front of it.

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Yeah, the only thing I'd add there is as you had heard from Andy describe, this business is in a very high growth phase and we were not expecting meaningful earnings in the near-term or in 2020 as a result. And so it's early days, and we'll report this information to you each quarter, and just as Andy indicated, just a reminder that is a seasonal business primarily fourth quarter loaded.

Thomas Gallagher
Analyst, Evercore ISI

Q

Got it. And Ken, would you say you're sticking to the $700 million revenue projection for 2020 still, or is that sort of TBD?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Yeah. Given the high-growth nature of this business, we don't want to get into the practice of updating each and every quarter. So again, we're going to – you're going to see the results as they occur in a separate segment.

Thomas Gallagher
Analyst, Evercore ISI
Q

Okay. Thanks. And then just my follow-up is, is PRU planning on early adopting variable annuity reform at yearend 2019? And if not, is the plan to do a full implementation in 2020, or a three-year phase-in?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

We're going to adopt on the effective date, which is January 1, 2020. But remind you that we made some big structural changes that were very much aligned with the new reform many years ago, so we're well positioned and expect to be very well capitalized before the reform and after the reform.

Thomas Gallagher
Analyst, Evercore ISI
Q

Okay. And Ken, no three-year phase-in? You'd fully adopt in 2020?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Fully adopt January 1.

Thomas Gallagher
Analyst, Evercore ISI
Q

Okay. Thanks.

Operator: [Operator Instructions] Next, we'll go to the line of Erik Bass from Autonomous Research. Please go ahead.

Erik Bass
Analyst, Autonomous Research
Q

Hi. Thank you. So you've clearly taken some big steps to accelerate the timing of realizing the expense savings you talked about. Can you just help us think about when we'll start to see these in results and where they'll come through, I guess whether in terms of the business segments or in corporate?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Yeah, sure. In our 8-K that we filed, we gave some information of our belief of the progression of the saves. They were modest in 2019 and we provided an estimate for 2020 that $140 million would be realized in the P&L in the year.

Those results you can expect to build as we go through the year, and you can expect to see them emerge with primarily in the US businesses and in corporate, but throughout those businesses, again, because it's a company – it's a US business-wide program.

Erik Bass
Analyst, Autonomous Research
Q

Got it. And when you're giving sort of your walk-through in the slides of kind of future earnings trajectory, am I right that there's nothing really explicitly contemplated there from savings in the businesses?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

No, only what was accomplished through 2019 or the first – or the fourth quarter. And then any future improvement, whether it's from business growth or share repurchases or additional expense saves – incremental expense saves would not be included in that baseline. That's all in the future.

Erik Bass
Analyst, Autonomous Research

Q

Got it. And then you mentioned in the remarks potential actions to continue streamlining your business portfolio, and realize it's premature to say much specific, but how would you think of redeploying any proceeds that you potentially generate? Would you look to reinvest these in the businesses, or potentially would they be available to return to shareholders?

Charlie F. Lowrey
Chairman & Chief Executive Officer, Prudential Financial, Inc.

A

The answer is yes. So, what we mean is, we'll cross that bridge when we come to it, but let me take a step back for a moment and make a more general comment on how we think about capital, in particular the optimization of our capital, which I think we've been doing for years.

So we always look across our businesses, both domestically and internationally, to ensure that we're optimizing capital deployment. And when we see attractive opportunities, you've seen us invest in growth and make acquisitions. And you've also seen us scale back or look for divestitures over the years when there are better uses of capital and then put that capital to use either in growing the franchise or if there aren't opportunities, returning it to shareholders.

So we'll continue to look for ways to optimize capital deployment and to maximize outcomes for our shareholders, whether that be in investing in new business opportunities, which again, you've seen us do, or return capital to shareholders.

Erik Bass
Analyst, Autonomous Research

Q

Thank you.

Operator: Your next question comes from the line of Ryan Krueger from KBW. Please go ahead.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Hi. Good morning. I guess, first, have you completed the yearend cash flow testing analysis? And if so, can you give us any indication of the impact?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

The statutory filings will come out at the end of the month, and so, yes, that will include our updated cash flow testing, our asset adequacy testing. You'll see those results when we report them.

What I'd offer you now is given lower rates, we would expect some strengthening in our AAT reserves, or cash flow testing, but we have derivative gains or interest rate hedges that offset that and we expect to have RBC ratios that are above our AA financial strength objectives.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Got it. Thanks. And then when you did the second quarter assumption review and had some impacts to the Individual Life business, at the time you talked about reinsurance as being a potential option to improve returns in that business. Is that something that you're still contemplating, and can you give us any update there?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.

A

Yeah, Ryan, this is Andy. So I would broaden your question and say we're taking a number of actions to strengthen the performance of our Life business. First and foremost, we are working diligently on expense efficiencies, and you can think about that in the context of the broader work going on at the company and the $500 million in outcomes we expect over the next couple years.

We already talked about the sales which we think is a meaningful – will be a meaningful contributor to giving earnings lift over time in the business. And then, yes, you are correct, we have been looking at options and we'll continue to look at options from a reinsurance perspective with the block, and what we're looking for there obviously is the right partner and the right terms that make economic sense for us. There's nothing currently that we want to report, but we'll keep you posted as we go forward.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

All right. Thank you.

Operator: Your next question comes from the line of Suneet Kamath from Citi. Please go ahead.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc.

Q

Thanks. Just focusing on slide 20 of your deck, in the international businesses, it looks like at least over the next 12 months Life Planner and Gibraltar are expected to be flat, which is lower than that intermediate earnings growth guidance you gave at Investor Day of mid-single digits. So just want to get a sense of, if we stay in this interest rate environment, what kind of gets us from flat back up to the mid-single digits and sort of over what timeframe?

Scott Garrett Sleyster
Executive Vice President and Head of International Businesses, Prudential Financial, Inc.

A

Hi, Suneet. This is Scott. Let me take that. So as you pointed out, the underlying business fundamentals for our international businesses actually look quite strong. As Rob pointed out, our in-force block is growing at about 4%, 4% to 5% in LP, and about 1% in Gibraltar.

Unfortunately, given the low rate environment, for the most part, we're giving back a lot of the earnings growth associated in the block and we're continuing to make some portfolio investments on technology and the like. So right now, I would say over the – certainly looking out to this year, we think we're going to be closer to flat. We hope over time as we make adjustments that will start to build, but I would say even right now looking at the intermediate term, we'd say we're looking at low-single digit growth.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc.
Q

Okay. Thanks. And then the follow-up is just on Assurance IQ. I think, it was mentioned that there are about 6.5 million shoppers in the fourth quarter. What should we expect to be the conversion rate of that balance? In other words, of the 6.5 million, how many would you expect to actually buy a product?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.
A

So, Suneet, it's Andy. I'll take your question. Conversion rate is a very complex topic, so it very much depends on the product mix that's on the platform, and as we talked about, we are in a phase of rapidly looking out – looking to roll new products onto the platform. So the conversion rates that we're currently experiencing are going to change quite a bit with that product mix shift, as well as, as you can imagine, with the shopper demand we had. But the mismatch with our agent capacity, our conversion was lower than we would expect going forward.

At this point, we're not going to put out explicit numbers, but hopefully that gives you a way to think about it.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc.
Q

And have you put any PRU products on that platform yet? I know that was one of your objectives when you announced the deal.

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.
A

Yeah, so it absolutely is one of our primary objectives. We have been working diligently to get our Simply Term Life product onto the platform. We are ahead of schedule on those plans and we will get that product on the platform in the second quarter of this year. And we're very encouraged with our brand name and the quality of our products that that will give both Assurance and obviously mother Prudential some lift.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc.
Q

Okay. Thanks.

Operator: [Operator Instructions] Next, we'll go to the line of John Barnidge from Sandler O'Neill. Please go ahead.

John Barnidge
Analyst, Piper Sandler & Co.
Q

Thank you. Have you seen any meaningful acceleration in PGIM's UK business post-election or demand for product from that market in Continental Europe?

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.
A

So John, this is Andy. I'll take that question. So what I would tell you is in the short term with all the flux that's been going on, we haven't seen any meaningful change or lift. I would kind of frame it as in many ways the marketplace is a bit hunkered down. So as an example, on the real estate side, we haven't seen a whole lot of capital fund raising and deployment.

We are absolutely ready no matter how that plays out. We have licenses in all the right places and people in all the right places to continue not only serving our current clients but to capitalize on potential opportunities if and when the dust settles.

John Barnidge
Analyst, Piper Sandler & Co.
Q

Okay. And then my follow-up, as we look back to SARS over 15 years ago in light of the coronavirus, do you see any increased demand for your products on the benefits side to note?

Scott Garrett Sleyster
Executive Vice President and Head of International Businesses, Prudential Financial, Inc.
A

Hi. This is Scott. Again, on the specific question, I would say history would show that any time there's a widespread illness, it creates a greater sensitivity among the customer base about the kinds of products that we sell. In particular, as you know, on the international side especially we're very focused on death protection products, and so any time you have something like this that goes on, you're very concerned about your employees and your customers and you're taking lots of actions there. But I do think there is a follow-on effect of greater sensitivity to the products that we offer.

John Barnidge
Analyst, Piper Sandler & Co.
Q

Great. Thank you.

Operator: Your next question comes from the line of Humphrey Lee from Dowling & Partners. Please go ahead.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

Good morning. Thank you for taking my questions. A question related to PGIM. So looking at your retail flows, it looks very strong from an inflows perspective. I think it may be even a record number. But then at the same time, it seems like you have record withdrawals as well.

I was just wondering if you can provide some color in terms of where you see the inflows and what happened in the outflows and how you're thinking about it in 2020.

Andrew Sullivan
Executive Vice President and Head of U.S. Businesses, Prudential Financial, Inc.
A

So, yeah, this is Andy, Humphrey. So we are very pleased and proud of the retail flows that we saw, as I think Rob mentioned in his opening. We moved up to number seven in the quarter. The retail flows are really coming from an expansion of our product portfolio on that platform as well as the work that we've done around UCITS.

From an outflow perspective, what I would say is that will tend to be episodic and I think over the long term we feel very, very good that due to our investment performance and our range of strategies, that we will see a continued upward trend over time.

Robert M. Falzon
Vice Chairman, Prudential Financial, Inc.
A

And Humphrey, I would just add on the institutional side that those flows can be a little bit lumpy, and we saw a couple of clients who wanted to consolidate this year and sometimes we're the beneficiary of consolidation, sometimes we're not and a couple of dominoes tilted against us this year. But that doesn't affect how we think about our institutional capability or the quality of flows that we can have going forward.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

That makes sense. And then just a clarification regarding Assurance IQ. So I think Ken was talking about given the growth that you're expecting and that you're not necessarily expecting any earnings from Assurance IQ in 2020. I just wanted to make sure that I heard that correctly because I think originally at the time of the announcement you were expecting maybe a $0.10 EPS accretion for 2020. So I just wanted to bridge the – any differences.

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Yeah, no, I didn't mean to say no earnings. I said not meaningful earnings, again, because of the high growth nature of the phase that they're going through.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

So the $0.10 is still coming – I understand you're not going to update guidance or anything like that, but is the $0.10 still a reasonable expectation?

Kenneth Yutaka Tanji
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Again, we don't want to get in the practice of having to update this every quarter.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

Okay. All right. Fair enough. Thank you.

Operator: And I'd now like to turn the call back to Charlie Lowrey for any closing comments.

Charlie F. Lowrey
Chairman & Chief Executive Officer, Prudential Financial, Inc.

Okay. Thank you very much. So in closing, I hope you all walk away from this call with a clear picture of our progress and priorities, our continued sense of conviction and urgency, and our path forward to deliver meaningful outcomes for all of our stakeholders including investors.

So thanks, again, for joining us today, and have a nice day.

Operator: Ladies and gentlemen, that does conclude your conference for today. Thank you for your participation and for using AT&T Teleconferencing. You may now disconnect.