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Prudential Financial, Inc. (PRU)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

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

I will now turn the call over to Mr. Bob McLaughlin. Please go ahead.

Robert McLaughlin

Vice President-Investor Relations, Prudential Financial, Inc.

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 International Businesses; and PGIM, our Global Investment Manager; Caroline Feeney, Head of US 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 measure and a discussion of factors that could cause actual results to differ materially from those in the forward-looking statements, please see the slides titled Forward-Looking Statements and Non-GAAP Measures in the appendix to today's presentation, and the quarterly financial supplement, both of which can be found on our website at investor.prudential.com.

And now, I'll turn it over to Charlie.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

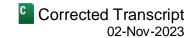
Thank you, Bob, and thanks to everyone for joining us today. Our third quarter results reflect continued momentum across our businesses, including the benefits from strong sales and the fifth consecutive quarter of underlying earnings growth.

We continue to execute on our strategy to become a higher growth, less market-sensitive and more nimble company. This quarter, we increased our capital efficiency and enhanced our capabilities in mutually reinforcing business system.

We are also optimizing our operating model to drive both efficiency and growth. Our strategic progress and financial strength position us well to navigate the current macroeconomic environment and maintain a disciplined approach to capital deployment.

Turning to Slide 3. During the quarter, we launched Prismic, a life and annuity reinsurance company alongside Warburg Pincus and other investors. It is one of our most exciting opportunities to drive sustainable long-term growth across our investment management, insurance and retirement businesses.

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Through Prismic, we can reinsure portions of our life and annuity in-force and new business to reduce market sensitivity, free up capital and invest in growth opportunities. Prismic can also offer its services to other insurance companies in need of reinsurance support, tapping into additional sources of third-party capital to drive further growth.

In addition, Prismic expands PGIM's assets under management. Prismic is a great example of how Prudential can unlock value for customers, shareholders and other stakeholders with our mutually reinforcing business system, which combines the power of our brand, global asset and liability origination capabilities and multi-channel distribution.

We're also growing and investing in our businesses to better serve our customers through both the products and services we offer and through the ways we do business. Our distribution channels continue to evolve and expand to provide more people around the world with our products and services in the way they want them.

I'll provide a few examples from the third quarter. In Brazil, we achieved the second consecutive quarter of record sales, driven by continued expansion in the third-party distribution channel and the strong performance of our Life Planner channel.

In the US, individual retirement strategies posted its strongest sales quarter in three years, driven by the continued success of FlexGuard as well as the expansion of our fixed annuity suite with the launch of our new WealthGuard Multi-Year Guaranteed Annuity.

Within the Institutional Market, retirement strategy secured \$2.5 billion in new pension risk transfer transactions and entered the health savings account space by securing a \$1.2 billion transaction with a top HSA provider, expanding our addressable market.

And in our Prudential Advisors distribution channel, we announced a strategic relationship with LPL Financial, which upon completion in the latter part of next year, will enhance both our advisor and customer experience by leveraging LPL's expertise, industry-leading technology and robust broker dealer and registered investment advisor services.

Alongside these investments in our businesses, we continued to focus on customer service through enhanced sales, service and claims platforms. For example, this year, we have announced seven customer experience technology partnerships within group insurance.

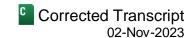
These include Enrollify, an innovative platform transforming the enrollment experience for millions of employees and EvolutionIQ, an Al-driven platform that will streamline the disability claims process.

We're also working to create a leaner, faster and more agile company, so that we can better meet the changing needs and expectations of our customers around the world while driving growth and efficiency to further strengthen our competitive position.

We're taking new steps to simplify our organizational structure by reducing management layers, complexity and costs, while making investments in technology and data platforms. Our goal is to empower faster decision-making and bring our integrated business teams closer to our customers and clients.

Turning now to Slide 4. Prudential's rock solid balance sheet and robust risk and capital management frameworks have allowed us to confidently navigate the current macroeconomic environment.

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Our AA financial strength is supported by our strong capital position, including approximately \$48 billion of unrealized insurance margins, \$4.3 billion in highly liquid assets at the end of the third quarter and a high-quality, well-diversified investment portfolio and disciplined approach to asset liability management.

Moving to Slide 5. Our disciplined approach to capital deployment, coupled with the added capital efficiency from the Prismic transaction enables us to effectively balance investing in the long-term growth of our businesses with returning capital to shareholders. In the third quarter, we returned over \$700 million of capital to shareholders.

And with that, I'll turn it over to Rob.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Thank you, Charlie. I'll provide an overview of our financial results and business performance for our PGIM, US and International businesses. I'll begin on Slide 6 with our financial results for the third quarter of 2023.

Our pre-tax adjusted operating income was \$1.6 billion, with \$3.44 per share on an after-tax basis, up 45% from the year ago quarter. These results reflect underlying business growth, including the benefits from a higher interest rate environment, more favorable variable investment income and underwriting experience, partially offset by lower fee income.

Our GAAP net loss was \$2.1 billion lower than our after-tax adjusted operating income, primarily driven by mark-to-market losses on interest rate derivatives due to the higher rates. Turning to the operating results from our businesses compared to the year ago quarter.

PGIM, our Global Investment Manager, had lower other related revenues driven by lower agency and seed and co-investment earnings and higher expenses. Results of our US businesses primarily reflected higher spread income, including more favorable variable investment income and lower expenses, partially offset by lower fee income and the increase in earnings in our International businesses primarily reflected higher spread income.

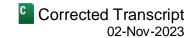
Turning to Slide 7. PGIM, our global active investment manager has diversified capabilities in both public and private asset classes across fixed income, equities and alternatives. PGIM's long-term investment performance remains attractive with 80% or more of assets under management outperforming their benchmarks over the last 5- and 10-year periods.

In addition, our short-term performance continues to improve with 83% of assets exceeding their benchmarks over a one-year period. PGIM experienced third-party net outflows of \$5.7 billion in the quarter.

Institutional outflows were primarily driven by lower than normal fixed income inflows and a large client outflow. Retail outflows were driven by sub-advised equity mandates. As the investment engine of Prudential, the success and growth of PGIM and of our US and International insurance and retirement businesses are mutually reinforcing.

PGIM's asset origination capabilities, investment management expertise and access to institutional and other sources of private capital, including through the recently launched reinsurer of Prismic, our competitive advantage helping our businesses bring enhanced solutions and create more value for our customers.

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Our insurance and retirement businesses, in turn, provide a source of growth for PGIM through affiliated net flows as well as unique access to insurance liabilities. In addition, we continue to grow both organically and through acquisitions.

Our private alternatives and credit business, which has assets of approximately \$230 billion across private, corporate and infrastructure credit, real estate, equity and debt and secondary private equity. Capital deployment across PGIM's private assets platform of \$8 billion during the quarter benefited from robust private placement and direct lending originations.

Turning to Slide 8. Our US businesses produced diversified earnings from fees, net investment spread and underwriting income and benefit from our complementary mix of longevity and mortality businesses.

We continue to drive towards a higher value, higher growth and less market-sensitive mix of earnings, invest in our businesses to deliver best-in-class customer experiences and expand our addressable market with new financial solutions leveraging the capabilities across Prudential.

Retirement strategies generated strong sales of \$6.7 billion in the third quarter across its institutional and individual lines of business. Our Institutional Retirement business has leading market capabilities, which helped to produce third quarter sales of \$4.7 billion, including \$2.5 billion of pension risk transfer transactions as well as strong stable value sales.

Individual Retirement posted \$2 billion in sales, up 40% from the prior year quarter.

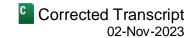
Our product pivots have resulted in continued strong sales of FlexGuard and FlexGuard Income, which represented about two-thirds of sales and fixed annuities that accounted for approximately one-third of sales this quarter.

Our Individual Life sales increased 24% from the year ago quarter, reflecting our earlier product pivot strategy with variable life products representing approximately 73% of sales in the quarter, including the benefit from our recently launched FlexGuard Life product. And in Group Insurance, we continue to execute on our strategy of product and client segment diversification while leveraging technology to increase operating efficiency and enhance the customer experience. Our strong results this quarter included favorable group life underwriting experience, which resulted in a benefits ratio of 82.4%.

Turning to Slide 9. Our International businesses include our Japanese life insurance companies where we have a differentiated multichannel distribution model as well as other businesses aimed at expanding our presence in targeted high-growth emerging markets. In Japan, we are focused on providing high-quality service and expanding our distribution and product offerings. Our needs-based approach and protection product focus continue to provide important value to our customers as we expand our product offerings to meet their evolving needs.

During the third quarter, we launched a new US dollar indexed annuity product and Prudential of Japan was ranked as the number one Japanese life insurer in the Forbes World Best Life Insurance Companies this year. We are proud to be recognized for the value we provide to our customers. In emerging markets, we are focused on creating a select portfolio of businesses in regions where our customer needs are growing, where there are compelling opportunities to build market-leading businesses and where the Prudential enterprise can add value.

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Our International business sales were up 19% compared to the year ago quarter. Life Planner sales were up 18%, driven by our second consecutive quarter of record sales in Brazil as well as higher sales in Japan. Gibraltar sales were up 20%, primarily driven by growth in the bank channel.

As we look ahead, we are well positioned across our businesses to be a global leader in expanding access to investing, insurance and retirement security. We continue to focus on investing in growth businesses and markets, delivering industry-leading customer experiences and creating the next generation of financial solutions to serve the diverse needs of a broad range of customers.

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

Kenneth Yutaka Tanji

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

Thanks, Rob. I'll begin on Slide 10, which provides insight into earnings for the fourth quarter of 2023 relative to our third quarter results. As noted, pre-tax adjusted operating income in the third quarter was \$1.6 billion and resulted in earnings per share of \$3.44 on an after-tax basis. To get a sense of how our fourth quarter results might develop we suggest adjustments for the following items: First, variable investment income was below expectations in the third quarter by \$25 million. Second, we adjust underwriting experience by \$10 million to normalize for third quarter experience. And last, we include an adjustment of \$350 million for expenses and other items.

This includes elevated seasonal expenses and lower international earnings due to timing of seasonal premiums in the fourth quarter. In addition, as Charlie mentioned, we are implementing changes to our organizational structure as part of our continuous improvement process, and we have included an estimated restructuring charge of approximately \$200 million that will be incurred in the fourth quarter.

We expect these actions will create operating efficiencies and provide reinvestment capacity to build capabilities. This will allow us to realize additional efficiencies, strengthen our competitiveness and fuel future growth. These adjustments combined get us to a baseline of \$2.75 per share for the fourth quarter.

I'll note that if you exclude items specific to the fourth quarter, earnings per share would be \$3.48. The key takeaway is that our underlying earnings power continued to improve due to business growth, including the benefit of higher interest rates. While we have provided these items to consider, please note that there may be other factors that affect earnings per share in the fourth quarter.

Turning to Slide 11. Our capital position continues to support our AA financial strength rating. Our cash and liquid assets were \$4.3 billion within our liquidity target range of \$3 billion to \$5 billion. Regulatory capital ratios are above our targets, and we have substantial off-balance sheet resources, including approximately \$9 billion of contingent capital and liquidity facilities. We remain thoughtful in our capital deployment, balancing the preservation of financial strength and flexibility, investing in our businesses for long-term growth and shareholder distributions.

Turning to Slide 12 and in summary. We are transforming our business for sustainable growth. We continue to navigate the current macro environment with the financial strength of our rock solid balance sheet, and we are maintaining a balanced and disciplined approach to capital deployment.

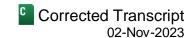
Now I'll turn it to the operator for your questions.



QUESTION AND ANSWER SECTION

Operator: Thank you. We'll now be conducting a question-and-answer session. [Operator Instructions] Our first question is coming from Tom Gallagher from Evercore ISI. Your line is now live. **Thomas Gallagher** Analyst, Evercore ISI Good morning. Just a couple of questions on capital. Did the GAAP net income loss you had this quarter also impacts statutory capital at all? And if so, did that require any contributions to subsidiaries or otherwise? Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc. Hey, Tom, it's Ken. Our GAAP results included the mark-to-market on interest rate hedges and a portion of that increased our negative IMR balance for stat. But our RBC ratios remain above our target and didn't require a capital contribution. Thomas Gallagher Analyst, Evercore ISI Okay. Thanks, Ken. And then the follow-up is when I think about the transition that lies ahead to ESR from SMR in Japan. Do you have enough clarity at this point to know how you should be positioned? Is it likely to consume capital, release capital? What do you think it should mean for Pru? Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc. Yes. Sure. First, let me start with our Japan businesses financial profile, which the businesses are high quality, profitable, financially strong, generating earnings, strong earnings and have good solvency margin ratios under the current regime. The FSA is taking steps to implement new capital standards and that's underway with adoption still now a couple years away. But generally, we still believe our businesses are well capitalized, financially strong, and that would be evident under any reasonable capital standard. We also have ways to manage the outcomes. We can reinsure business internally or externally to better match the economics of the business, if we need to do that. And so we're - it's something that we're looking at and working on. We're also advocating for reasonable and responsible standards and we'll have strategies to adapt to the new potential regime. Thomas Gallagher Analyst, Evercore ISI Okay. Thank you. **Operator**: Thank you. Your next question is coming from Ryan Krueger from KBW. Your line is now live. Ryan Krueger Analyst, Keefe, Bruyette & Woods, Inc.

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Hi. Good morning. My first question was on the restructuring charge. Can you talk a little bit about the potential economic benefits of that on a go-forward basis in terms of potential expense reduction?

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

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Hey, Ryan, it's Charlie. Let me take that at a high level and provide you some context and then turn it over to Ken to specifically answer your question. But in terms of the restructuring program, we made good progress towards becoming a higher growth, less market-sensitive and more nimble company. And if you think about what we've done, that's including releasing a significant amount of capital through the disposition of market-sensitive and/or low-growth businesses and products executing a series of programmatic acquisitions to expand our investment capabilities and growth potential. Launching Prismic, another arrow in our quiver, if you will, enhancing our mutual reinforcing business system and then exceeding our initial expense goal that we established a number of years ago.

But we've also said that we plan to continuously improve and build upon the progress we've made to further accelerate our vision and our growth objectives. We operate in an increasingly competitive environment. And in order to remain competitive and grow sales and earnings, we will continue to focus on further investing in our businesses and technology, reducing our cost of capital, enhancing the risk-adjusted returns we earn on our products and investments and transforming our operations to produce efficiencies while enhancing both our customer and employee experience.

So we're taking steps to create a leaner, faster and more agile company, including simplifying our management structure by reducing management layers, complexities and costs with the goal of bringing our integrated teams closer to our customers and our clients. We're also empowering our employees with faster decision-making in part through investments in technology and data platforms. And as we make progress in each of these areas, we'll update you as we have in the past. So with that as context, Ken, let me turn it over to you to answer the specific question Ryan had.

Kenneth Yutaka Tanii

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



Yeah. So I think, Ryan, we expect, as you just heard from Charlie, a number of benefits in the way we're transforming but also financially, the restructuring will result in annual cost savings that will be greater than the restructuring charge of \$200 million. And those savings will provide expense capacity to invest in capabilities and gain further efficiencies sort of, as Charlie described there, to help offset inflation and also to grow our businesses. And the way we think when we put that all together is we'll be keeping expenses flat over the near term. And that's, again, how we think of things holistically, not just the saves, but also combined with the investments in growing our businesses while keeping operating expenses flat and improving margins. And that's the continuous improvement mindset that we're striving for.

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.

Thank you. And then a question on Prismic, you launched it with \$1 billion of capital. I assume that the structured settlements transaction consumed a good amount of that. Can you give us any color on how much committed capital that you have already in place for future growth?

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

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Hi, Ryan, Rob, maybe let me give a perspective about that. I think, if you're asking that from the perspective of sort of the Prismic standpoint in terms of the appetite there. A couple of thoughts. One is, as Charlie actually indicated in our opening remarks, we see very interesting opportunities, growth opportunities that are at the intersection of asset management and insurance, and we expect Prismic to play a material role in executing against that. And we think the benefit of that is it's going to actually accelerate growth across all of our businesses.

And in the course of doing so, actually help to shift the business mix so that it's higher growth, less market-sensitive and more highly valued at the end of the day. With respect to Prismic itself, I think what we've articulated before is that we and our investors share aspirations that go well beyond the initial \$10 billion structured settlement transaction. So we anticipate that, that will include opportunities to further optimize our balance sheet.

It's going to include what's called flow, so the reserve and capital financing for our new sales across our businesses and importantly, third-party blocks that will be – that we're looking to reinsure into Prismic as well.

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.

Thank you.

Operator: Thank you. Next question is coming from John Barnidge from Piper Sandler. Your line is now live.

John Barnidge

Analyst, Piper Sandler & Co.

Great. Thank you very much. Appreciate the opportunity. The restructuring program, you talked about a portion being there to invest. Can you talk about human capital versus automation and then the offshoring opportunity as well? Thank you.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Sure. It's Charlie again. As part of the continuous improvement process, we'll be simplifying our operating model and organizational structure, as you said, really streamlining decision-making to create a leaner, faster and more agile company so we can better meet the needs of our customers, while driving growth and efficiency.

So we are far more focused on optimizing organizational structure through organizational design and investments in technology as opposed to offshoring. That is the predominant direction in which we're going.

John Barnidge

Analyst, Piper Sandler & Co.

Fantastic. Thank you. And my follow-up question, can you maybe talk about M&A interest? Do you have what you need to grow organically from a product perspective? And is there opportunities for PGIM to get larger in certain products? Thank you.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Yeah. It's Charlie again. Let me take that. We've done many acquisitions that have significantly grown the company over time. And these acquisitions include companies of various sizes as well as teams of specialists.

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And programmatic M&A, to your point, will continue to play a role as we think about the development of the – of what we want to do going forward and a series of well-executed programmatic M&A transactions will become material over time.

As a result, we continue to look at a variety of opportunities in different sizes. But we're continuing to be thoughtful about the deployment of capital, especially in light of the current macroeconomic conditions.

And our M&A interest continue to be focused on mature companies that support our strategy of growing PGIM in emerging markets by which we can expand our capabilities or our distribution and continue to increase the scale of our existing businesses.

But regardless of size, we're going to be thoughtful about evaluating the strategic and the financial merits of each transaction.

Andrew F. Sullivan

Executive Vice President & Head-International Businesses & Global Investment Management, Prudential Financial, Inc.

Hey John, it's Andy. Maybe I'll just add in because you asked about PGIM, we're going to continue to work to globalize the business. And as we've talked about before, focus on higher growth, higher fee areas. So you should think about private alternatives and real asset capabilities.

John Barnidge

Analyst, Piper Sandler & Co.

Thank you very much.

Operator: Thank you. Next question is coming from Wes Carmichael from Wells Fargo. Your line is now live.

Wes Carmichael

Analyst, Wells Fargo Securities LLC

Hey. Good morning. I had a question on RBC. I think your slide showed that PICA's RBC ratio is in excess of 375%. I just wanted to confirm, is the benefit of negative IMR within that RBC ratio? And could you maybe just size that for us?

Kenneth Yutaka Tanji

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

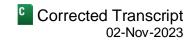
Yeah, sure. It's Ken. Yes, that – the benefit of admitting the negative IMR as part of the new RBC standard is – has been adopted and is in effect for our third quarter results. We were able to admit \$1.3 billion, which is at the cap level relative to our surplus, so that is already reflected in there.

Wes Carmichael

Analyst, Wells Fargo Securities LLC

Thanks, Ken. And maybe just to follow-up on an earlier question on Japan and ESR. Could you maybe just help us understand how your USD-denominated products are proposed to be treated under ESR versus the current SMR framework?

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Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

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Hi. It's Rob. Wes, let me take that question. The – first of all, this is a regulatory framework that's still under development, I want to emphasize that. It's a regulatory framework that to date has been based on the international, the ICS capital standards that have been developed.

And those standards are actually not – don't necessarily reflect the underlying economics of long duration product, particularly in the US. So we continue to work on the international front on the ICS, and we continue to work with Japan as well in terms of how that ultimately gets reflected into their regime, whether it's modified at the international level or not.

But what we found is one of the shortcoming of the current set of proposals is that they don't quite get the economics right when you get into the long – the types of long duration products that are typically sold in the US, both on the life side and on the retirement side. So that's an area where industry continues to work with the regulators and we're hopeful of making progress there.

As Ken mentioned earlier, to the extent that's challenged in any way that we do have alternatives that are available to us to think about how we would then manage that product on a go-forward basis. There's a strong demand for the products in the Japan marketplace.

So for Japanese consumers like the US dollar-denominated products and so the industry will want to continue to sell those products in the marketplace, and we'll come up with solutions for being able to do that and yet be able to finance them on an economic basis.

Andrew F. Sullivan

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Executive Vice President & Head-International Businesses & Global Investment Management, Prudential Financial, Inc.

This is Andy. I was just going to add in. We have a lot of ability and flexibility to navigate those changes that are coming at us. We obviously have incredibly strong distribution, both captive and third-party.

We have a very wide product portfolio from both a yen and US dollar perspective and single premium and recurring premium and we've been very successful at delivering a top-notch, great customer experience that we've been recognized for. So the strength of that business complex will really enable us to navigate the changes that are coming down the road.

Operator: Thank you. Next question is coming from Jimmy Bhullar from JPMorgan. Your line is now live.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

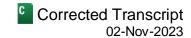
Hi. I first had a question on PGIM flows. If you could just talk about what drove the negative flows in both Retail and Institutional funds? And to what extent do you think it's a function of just industry-wide issues that asset managers are seeing versus maybe the slight dip that you saw in your performance? And then relatedly, the impact on fees, should it be commensurate to the assets, or are the fees lower or higher on the assets that you've lost?

Andrew F. Sullivan

Executive Vice President & Head-International Businesses & Global Investment Management, Prudential Financial, Inc.

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So Jimmy, its Andy. I'll take your question. So this quarter, we experienced third-party outflows of \$5.7 billion. On the retail end, outflows were \$1.9 billion. That was predominantly an equity story.

We've seen clients rebounds for a variety of reasons, including to recognize gains as the funds have performed well. We have produced strong equity performance with 89% of our equity asset outperforming benchmark in the last year.

On the Institutional side, outflows were \$3.8 billion. Net outflows were primarily fixed income. We are seeing a lower level of gross inflows into this asset class. Investors are hesitant to come back in until it's clear rates have stabilized. We also saw one large low fee rate mandate lapse in institutional. As to your question, industry or specific, these are consistent with the industry. And in particular, the fixed income headwinds are consistent. As far as our outlook looking forward, a stable higher rate environment will be good for our flow. So we know that once rates stabilize, we expect to benefit flow-wise.

Your question around fees, obviously, it depends very much on the mix of assets, but we're being very successful in bringing inflows into higher fee rate strategies, in particular, into the private alts areas of our business.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Okay. And then on Individual Life, that's a business where the results have been weak the past several quarters, but this quarter was actually a good quarter. I think you mentioned in the presentation, there's a benefit from lower expenses and a legal reserve release. Can you quantify how much each was so that one gets an idea on sort of the underlying earnings in the business? And what your outlook is for individual Life earnings?

Caroline A. Feeney

Executive Vice President & Head-US Business, Prudential Financial, Inc.

Yeah. So Jimmy, it's Caroline, and I'll take your question. So as you mentioned, this quarter, Individual Life did see favorable expense experience and that includes a number of one-time items, but it also, as you mentioned, does include the release of a legal reserve. So Jimmy, it's our practice to regularly review our legal reserves and then make appropriate adjustments reflecting activity within the quarter. And the release this quarter reflects the results of that review.

In terms of the outlook for life overall, I would say, in addition to what you saw in favorable expenses on the life side, we also saw strong investment results and also underwriting results that were largely aligned to our expectations and overall the fundamentals of the business continue to remain very solid, and we're very optimistic about the growth there.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

And just any color on the size of the legal reserve because that – I'd view that more as sort of a one-time versus expenses tend to move around.

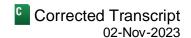
Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Yeah, it would be - that's...



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Caroline A. Feeney

Executive Vice President & Head-US Business, Prudential Financial, Inc.

Jimmy, we would not comment on the specific size of a particular legal reserve, as I said. We saw favorable expenses overall and part of that was the release of a legal reserve, but we do not comment on the specific size of the case.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Okay.

Operator: Thank you. Next question is coming from Tracy Benguigui from Barclays. Your line is now live.

Tracy Benguigui

Analyst, Barclays Capital, Inc.

Thank you. Good morning. I know it's early, but I was wondering if you could just share your thoughts on DOL and the impact on your FIA business.

Caroline A. Feeney

Executive Vice President & Head-US Business, Prudential Financial, Inc.

Sure, Tracy, it's Caroline, and I'll take your question. So, I'll first start off by saying, Tracy, we've been a long-time supporter of regulations that provide consumer protections while ensuring that all Americans continue to have access to the quality advice and the solutions they need for a secure retirement. So the proposal was just released two days ago, and so we're very much still in the midst of thoroughly reviewing and analyzing it, so we can assess any potential impact on our customers and specifically their ability to access critical retirement products.

And you specifically asked, Tracy, about FIA, so we do realize that in the proposal, there appears to be a focus on fixed indexed annuities, which today for us accounts for less than 20% of our total annuity sales, but are also part of our well diversified suite of annuity solutions as we continue to focus on delivering valuable solutions to help our customers meet their retirement savings needs. That being said, I will just reiterate that we're still in the process of reviewing the proposed rule. And finally, I'll just add that under the last proposed rule change, we implemented policies and procedures to comply with the final prohibited transaction exemption in a timely fashion, and we'd expect to do the same here.

Tracy Benguigui

Analyst, Barclays Capital, Inc.

Do you think that evolution also took place in the IMO channel or they could comply with new standards?

Caroline A. Feeney

Executive Vice President & Head-US Business, Prudential Financial, Inc.

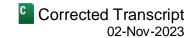
I'm sorry, Tracy, I want to make sure I heard your question.

Tracy Benguigui

Analyst, Barclays Capital, Inc.



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The IMO channel, the independent agents, yeah, would they also be well equipped since the last proposal? So, improve their...

Caroline A. Feeney

Executive Vice President & Head-US Business, Prudential Financial, Inc.

Okay. So, what I couldn't comment on -- Yes. So Tracy, what I couldn't comment on is others in terms of their IMO channels and whether they'd be prepared or not. What I will say, particularly, and I'll just reiterate with the last DOL-proposed rule, we were very much ready as an entire enterprise across all of the various businesses where there was any impact, and we were ready to comply with the rule. And as I mentioned, we would expect to do the same here. That would include all of the distribution channels that would, in any way, be impacted by the new proposed rule.

Tracy Benguigui

Analyst, Barclays Capital, Inc.

Got it. I want to touch on Prismic and thinking about the investor consortium. Could you let me know like what they're thinking in terms of an investment time horizon? Will there be like a call option being arbitrary here, but let's say, like in 10 years, would PRU need to provide liquidity to those investors after a set period of time? Or do you envision raising new funds?

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Tracy, it's Rob. So we're partnering with a group of very large global institutional investors. Their intent is to operate with scale. And their investment horizon very much aligned with our own is quite long term. Prismic itself has an independent Board of Directors, and that will govern the routes toward liquidity, growth and otherwise. But there are no put or call provisions embedded in the agreement that we've got with Prismic.

Tracy Benguigui

Analyst, Barclays Capital, Inc.

Thank you.

Operator: [Operator Instructions] Our next question is coming from Wilma Burdis from Raymond James. Your line is now live.

Wilma Burdis

Analyst, Raymond James & Associates, Inc.

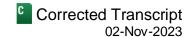
Hey. Good morning. A couple of earnings-related questions. First, I think you guys previously cited \$65 million of deal closing costs with Somerset Re. I just want to know if that would lower the \$2.75 baseline for 4Q? Or maybe just an update on timing there? And then the other is, if you could walk us through the trajectory of benefits from the restructuring. Will we see a benefit in 1Q? Or is it going to take a little bit longer?

Kenneth Yutaka Tanji

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

Yeah. Hey, it's Ken. The deal-related costs for the reinsurance with Somerset Re will be incurred at the time of closing, and those have not been included in the baseline.

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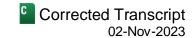


Wilma Burdis Analyst, Raymond James & Associates, Inc. Okay.	Q
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.	A
And I'm sorry. And obviously, I think, your second part of the question was the benefits of the reinsurance will occur subsequent to close, obviously.	e benefits of the restructuring or the
Wilma Burdis Analyst, Raymond James & Associates, Inc.	Q
Yeah, the restructuring, should we start to see some benefits coming in in 1Q	? Or is it going to take some time?
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.	A
Are you saying the organizational restructuring, is that what you're referring to	?
Wilma Burdis Analyst, Raymond James & Associates, Inc.	Q
Yeah.	
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.	A
Or the reinsurer. I'm sorry.	
Wilma Burdis Analyst, Raymond James & Associates, Inc. Yeah.	Q
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.	A
We will see benefits in 2020 for pretty soon thereafter, there will be a portion t first quarter and then thereafter.	hat's highly – that's effective in the
Wilma Burdis Analyst, Raymond James & Associates, Inc.	Q
And could you talk about the impact of Prismic on PICA's RBC $-$ just I know, to impact from the initial investments. So could you just talk about that aspect as	
Kenneth Yutaka Tanji	Λ

Sure. The initial impact of the reinsurance of the structured settlement to Prismic was modest, and that was impact – that was in our RBC ratio for September. And so we had the impact of the initial portion of that. But over time, it will also enable capital benefits as we reallocate the retained investment portfolio. And so it will – we had some impact immediately, but they also will have continued impact as we reallocate the investment portfolio.

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

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Wilma Burdis

Analyst, Raymond James & Associates, Inc.

Okay, Thank you.

Operator: Thank you. Next question today is coming from Suneet Kamath from Jefferies. Your line is now live.

Suneet Kamath

Analyst, Jefferies LLC

Great. Thank you. I wanted to go to Prismic again. Charlie, I think in your prepared remarks, you talked about further optimization of your in-force block. And I think you specifically referred to life and annuity blocks. Is that sort of the extent to where we should be thinking about in terms of where you'd optimize? I guess where I'm going with this is, is there an opportunity for something like a long-term care in terms of your in-force and reinsuring that to Prismic?

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Sure. Let me take a step back and just tell you generally how we're thinking about this. Prismic is really an example of our open architecture solutions and it's a very important additional component of our strategy to become a higher growth, less market-sensitive and more nimble company.

We formed Prismic with Warburg Pincus and other global investors because we see significant opportunities that exist at the intersection, as Rob said, of asset management and insurance. And we're perfectly positioned to take advantage of those opportunities given the business mix we have. And we're excited about our ability to leverage third-party capital and reinsurance to drive the incremental growth in our insurance, retirement and asset management businesses.

And Prismic, to get, to your point, really reinforces and enhances our mutually reinforcing business system in three ways. First, we can reinsure portions of our in-force business like the structural settlements transaction we just completed and have PGIM continue to manage the majority of assets while freeing up capital to become less market sensitive. And to your point, we'll look to our retirement and life businesses for those assets.

Secondly, we can write new business that could be reinsured to Prismic, so forward flow. And since Prismic is mainly supported by third-party capital, we can write additional retirement and insurance business to further accelerate our growth and at the same time, increase PGIM's assets under management.

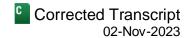
And finally, Prismic can reinsure third-party blocks, which would again increased PGIM's AUM. So there's a lot of potential we see for Prismic, and we're being thoughtful about how we execute against these opportunities and have recently reallocated resources to further optimize and cap our — will further optimize our capabilities since Prismic is such an important component of our mutually reinforcing business system. So it's going to be in the life and retirement businesses mainly that we think about reinsuring other blocks, but we could think about others as we go forward.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Suneet, it's Robert. I'd sort of add as sort of a general market observation to Charlie's remarks is that we've seen investors that are behind many of the reinsurance vehicles in partnership and otherwise, having an increasingly

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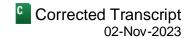
higher appetite for a variety of different products. So this started out very much if you look at the early reinsurance transactions in the sort of very vanilla insurance space and in the very vanilla annuity space, so fixed annuities.

And over time, what you've seen through our own transactions as well as others is that now has expanded into variable annuities. It's expanded into GUL, and we do see that that's a trend that's likely to continue. There's a robust appetite and that appetite as it gets – as investors get more comfortable with the dynamics of the insurance marketplace and business model that their appetite will continue to grow. So we see interesting opportunities, both domestically and I'd add importantly internationally as well.

Suneet Kamath Analyst, Jefferies LLC	C
Okay. Got it. And then I guess on the VA deal, are the proceeds from that transaction still in PICA and is the expectation that they'll just sort of stay there and be used to support organic growth? Or would you expect to take those proceeds up to holdco for other uses?	
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.	A
Yes, it's Ken. So the reinsurance of our variable annuity block closed in April. And so we had the benefit of that effective April 1, and it is one of the considerations we made as we looked at our RBC and our dividend capacity and factored into the dividends that we made in the third quarter, which was \$1 billion from PICA. So we did get the benefit. It's one of the things we thought about when we looked at the overall level of our RBC and then decided to make a dividend to PICA of \$1 billion in the third quarter.	
Suneet Kamath Analyst, Jefferies LLC	Q
Sorry, dividend out of PICA.	
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc. Yes, I'm sorry, yes.	Д
Suneet Kamath Analyst, Jefferies LLC	Q
So just a quick follow-up there. I was just trying to track the holdco cash because it looked like bit sequentially.	it went down a little
Kenneth Yutaka Tanji Chief Financial Officer & Executive Vice President, Prudential Financial, Inc. Yeah.	А
Suneet Kamath Analyst, Jefferies LLC	C
Can you just kind of give us some of the bigger moving pieces there?	
Kenneth Vutaka Tanii	Λ

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

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Sure. Yeah. The bigger moving pieces, like I just mentioned, was the \$1 billion that the holding company received from PICA as a dividend. And then we also made a \$200 million investment in Prismic and then the other would be ordinary course, interest expense and shareholder distributions. And those are the main components that led to a very small change in our HLA.

Suneet Kamath

Analyst, Jefferies LLC

Got it. Okay. Thanks, Ken.

Operator: Thank you. Your next question is coming from Michael Ward from Citi. Your line is now live.

Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.

Hey, guys. Thank you. Good morning. Another one on Prismic. But for the third-party component and the mechanics, if PGIM could get the AUM of new blocks being reinsured, wouldn't the general account of the external blocks go on your balance sheet? Because I wouldn't have thought that you're targeting exposure to third-party capital intensive business.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Mike, it's Rob. So yeah, PGIM will have an appetite for doing both flow and balance sheet from Prudential as well as third parties. We will look to put – and yes, we will get the asset management on those blocks as they're brought into Prismic. So that's part of the arrangement that we have with Prismic. And then separately, we'll make a decision as to how much we invest into Prismic on a go-forward basis.

As of now, our ownership in Prismic is at a 20% level. It's not a contractual obligation for us to stay at that level. But having said that, we think that the returns that we get for a capital that could be deployed through Prismic, when you think about the returns on the underlying blocks enhanced by the fees that we get from our asset management business can be quite attractive on a risk-reward basis.

And so we would have some appetite for continuing to invest in those sorts of business when they significantly enhance the fee components that we get out of that business, which on an overall basis with a reduced risk profile of the earnings stream on a go forward.

Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.

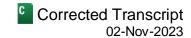
Okay. Thank you. That's helpful. And then maybe one thing, we didn't touch on CRE, commercial real estate. Any developments for you guys in the office area?

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

No, I would say that – it's Rob again. Sorry, Mike, that nothing material to update you on from last quarter. We have a very high-quality overall real estate portfolio, including the office components to that or component of that. And we continue to see resiliency within that portfolio, as you would expect, given the experience that we have there, the dedicated team that we have from an underwriting standpoint and the quality of the overall portfolio.

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So while on the – from a valuation standpoint, we've been updating our valuations and the valuations of the collateral supporting office loans continues to come down, but our LTV still remained quite low on a relative basis, and we feel very comfortable with the overall portfolio exposure there.

Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.

Thanks, Rob.

Operator: Thank you. Our next question is a follow-up from Wes Carmichael from Wells Fargo. Your line is live.

Wes Carmichael

Analyst, Wells Fargo Securities LLC

Hey. Thank you for taking my follow-up. Just had a couple of earnings ones should be quick. But on the baseline for Q4, the \$2.75 that includes normal variable investment income, so I was just hoping if you could help us with your outlook in the near term. It was a pretty modest headwind in the third quarter, but just wondering if you expect that to be a bit challenged going forward.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

From a VII standpoint, Wes, it's Rob. I think about that as having two components to it. One is the returns that we get from our alternatives portfolio and the second being the level of prepayment income that we get from the fixed income portfolio. I think, we've guided to the fact that we expect lower levels of prepayment income on a goforward basis. That was the primary contributor to the below expectations in the current quarter. So I think you should expect to see that.

On a go-forward basis, we generally don't provide an outlook. What I would say is that as evidenced in the current quarter, we have a good portfolio that's very well diversified. And so while there are different components of it that performed up and down in the current quarter, we would expect that to continue in future quarters as well. In this particular quarter, real estate performance was off, as you would expect. But actually, our private equity portfolio performed quite well.

And just to be very clear, within our private equity portfolio, we have a very small exposure to sort of the DC area. So it's more core private equity. And even within that, it's a fairly significant component of that that's in high yield and debt strategies. And so that sort of caused some stabilization within that private equity portfolio. So I think that we will vary as markets do, but we continue to believe that we'll perform on a relevant basis quite well.

Wes Carmichael

Analyst, Wells Fargo Securities LLC

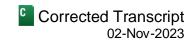
Got it. Thanks. And then on PGIM, I think you lowered your expected range for other related revenues by about \$10 million on a quarterly basis. Just curious if you can provide us some color on what's driving that there.

Andrew F. Sullivan

Executive Vice President & Head-International Businesses & Global Investment Management, Prudential Financial, Inc.

Yeah, Wes, it's Andy. I'll take your question. So ORR came in at the quarter at \$37 million. It was predominantly driven by the real estate space. So this is a pretty consistent story. That's been the last few quarters. Our agency earning decline from the real estate slowdown, and we saw lower real estate valuations and transactions.

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As far as the go-forward look, you are correct. We now expect our ORR to average about \$40 million per quarter. That lower run rate, again, is flowing directly from the slowdown in the real estate markets. We're expecting to see lower agency earnings as well as lower private incentive fees. And while this will vary quarter-to-quarter as always, we expect the patterns that we've been seeing to be more muted in this environment.

Wes Carmichael

Analyst, Wells Fargo Securities LLC

Thank you very much.

Operator: Thank you. We've reached the end of our question-and-answer session. I'd like to turn the floor back over to Mr. Lowrey for any further closing comments.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Okay. Thank you again for joining us today. We're entering into the next chapter of our evolution with a unique business model and growth strategy that positions Prudential to help current and future generation secure their financial future. We are confident that our strategy and mutually reinforcing business model will enable Prudential to be a global leader in expanding access to investing insurance and retirement security. Thank you again, and stay well.

Operator: Thank you. That does conclude today's teleconference and webcast. You may disconnect your lines at this time, and have a wonderful day. We thank you for your participation today.

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