

07-Feb-2024

Prudential Financial, Inc. (PRU)

Q4 2023 Earnings Call

CORPORATE PARTICIPANTS

Robert McLaughlin

Vice President-Investor Relations, Prudential Financial, Inc.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Kenneth Yutaka Tanji

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

Andrew F. Sullivan

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

Caroline A. Feeney

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

OTHER PARTICIPANTS

Thomas Gallagher

Analyst, Evercore ISI

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.

Alex Scott

Analyst, Goldman Sachs & Co. LLC

Elyse Greenspan

Analyst, Wells Fargo Securities LLC

Suneet Kamath

Analyst, Jefferies LLC

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Joel Robert Hurwitz

Analyst, Dowling & Partners Securities LLC

Wilma Burdis

Analyst, Raymond James & Associates, Inc.

John Barnidge

Analyst, Piper Sandler & Co.

Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.

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 those 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.

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. Before we begin, I'd like to comment on our CFO transition. As you saw from yesterday's news release, Yanela Frias, President of Prudential's Group Insurance Business has been named Executive Vice President and CFO of Prudential, succeeding Ken Tanji. As a 27-year veteran of Prudential, Yanela is a seasoned executive who brings a deep understanding of our business and industry, as well as significant finance, operations and leadership experience. I'm sure you'll enjoy getting to know her as she starts her new role.

Yanela will become CFO effective March 15, and Ken will stay on for a six-month period to ensure a smooth transition. Ken has been a great partner and friend and has had a distinguished 35-year career at Prudential. I don't need to go back far to articulate his impact. Most recently, as CFO, Ken guided Prudential through the financial challenges of the COVID pandemic and the market volatility that followed. During the same time, his leadership on strategic initiatives meaningfully contributed to our goals of becoming less market-sensitive and more nimble. We are grateful to Ken for his many contributions over more than three decades and wish him well.

Now, let's turn to my remarks for the quarter. Our financial results for 2023 reflect continued strong sales momentum across our insurance and retirement businesses and solid underlying earnings growth. The fourth quarter capped a productive year of continued transformation to make Prudential a higher growth, more capital-

efficient and more nimble company. Our strategic progress and financial strength position us well to navigate the current macroeconomic environment, maintain a disciplined approach to capital deployment and deliver long-term sustainable growth.

Turning to slide 3. I will begin today by sharing a few examples of how we are transforming our business to drive future growth and unlock value for all our stakeholders. Over the course of 2023, we executed several attractive transactions adding to our capital efficiency. We reinsure the \$10 billion block of traditional variable annuities, reducing our market sensitivity.

We closed a \$10 billion transaction of structured settlement annuities with Prismic, a life and annuity reinsurance company we launched. Prismic will enhance our mutually reinforcing business system and drive future growth by leveraging our differentiated brands, global asset and liability origination capabilities and multichannel distribution.

In addition, we entered into a reinsurance agreement with Somerset Re for a \$12.5 billion block of guaranteed universal life reserves, which will release capital and increase earnings.

We continue to strengthen the capabilities of our market-leading businesses through strategic M&A, expanded distribution channels and created new products and solutions to meet the evolving needs of our customers across the globe and to support future growth.

In PGIM, we enhanced our capabilities in the attractive area of private credit and direct lending by acquiring a majority stake in Deerpath Capital, which closed in December. To further provide investors with a cohesive offering, we brought together PGIM's private alternatives capabilities into one global team with the formation of PGIM Private Alternatives.

Internationally, we continue to expand third-party distribution in Latin America through Mercado Libre, reaching a milestone of close to 300,000 policies in force last quarter. In Japan, we launched expanded inheritance and new investment products to diversify our portfolio and meet a broader range of customer needs.

Our Institutional Retirement Strategies business secured its second largest longevity risk transfer transaction ever with one of the biggest life insurance companies in the Netherlands. This marks our first international reinsurance deal in the Dutch market.

Retirement strategies also worked with Fidelity Investments to address growing consumer demand for a workplace retirement income solution. Our Prudential SimplyIncome product, a new single premium immediate annuity is now available to employer-based retirement plans administered by Fidelity.

In addition, to solidify our leadership and expand our addressable market and structured settlements, we launched a new index structured settlement annuity product. We also continue to create a more nimble and efficient company to meet the changing needs of our customers and maintain a competitive position in the marketplace. This included evolving our operating model and organizational structure to better support customers at the business level and leveraging technology to bring products to market faster.

Our business and technology teams together launched an average of one new or enhanced product every two weeks in 2023. Additionally, we are strategically leaning into partnerships with cutting-edge technology firms within our group business to increase the speed of innovation, add capabilities and enhance customer experience.

We entered 2024 with momentum and optimism as we have expanded and diversified our product offerings, enhanced customer and client experiences and continued to reinvest in our businesses for sustainable long-term growth.

Moving to slide 4. Our transformation strategy and growth initiatives are supported by Prudential's rock solid balance sheet and robust risk and capital management framework, which have allowed us to confidently navigate the macroeconomic environment.

Our AA rated financial strength, includes a strong capital position, including approximately \$50 billion of unrealized insurance margins, \$4.1 billion in highly liquid assets at the end of the fourth quarter, and a high-quality, well-diversified investment portfolio and disciplined approach to asset liability management.

Turning to slide 5. Our disciplined approach to capital deployment enables us to effectively balance investing in the long-term growth of our businesses with returning capital to shareholders.

In the fourth quarter, we returned over \$700 million of capital to shareholders. For 2024, our board has authorized up to \$1 billion in share repurchases as well as a 4% dividend increase beginning in the first quarter. This represents our 16th consecutive annual dividend increase.

And now, I will 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 fourth quarter and full year of 2023.

Our pre-tax adjusted operating income was \$5.5 billion, or \$11.62 per share for 2023 and \$1.3 billion, or \$2.58 per share in the fourth quarter. These results reflect an increase in the underlying earnings power of our businesses, including the benefits of strong sales growth and higher interest rates. This was partially offset by pressure on variable investment income and higher expenses, primarily due to a \$200 million restructuring charge in the fourth quarter.

Our GAAP net income for the quarter was \$374 million higher than our after-tax AOI primarily driven by net investment gains due to declining rates.

Turning to the quarterly operating results of our businesses compared to the year ago quarter. PGIM, our global investment manager, had lower other related revenues driven by lower incentive fees and agency income and higher expenses. This was partially offset by higher asset management fees, including the benefits from our acquisition of Deerpath Capital and of launching Prismic

Results of our US businesses primarily reflected higher spread income driven by business growth and the benefit of higher interest rates and lower expenses. This was partially offset by lower legacy traditional variable annuity fee income as we pivot to less market-sensitive products. The earnings in our international businesses primarily reflected less favorable underwriting results, including unfavorable policyholder behavior partially offset by lower expenses.

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 strong investment performance over the past year has also driven attractive long-term performance with over 80% of assets under management outperforming their benchmarks over the last 5- and 10-year periods.

PGIM's assets under management increased 6% to \$1.3 trillion from the year ago quarter, primarily resulting from market appreciation. Third-party net outflows in the fourth quarter totaled \$13.5 billion. Institutional outflows of \$6.3 billion were driven primarily by a large redemption of a low fee equity index mandate and redemptions in public fixed income resulting from client rebalancing and liquidity needs.

Retail outflows of \$7.2 billion were primarily driven by equity, sub-advised mandates and fixed income outflows. 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 Prismic, or a competitive advantage, helping our businesses to bring enhanced solutions and create more value for our customers.

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 PGIM Private Alternatives business, which has assets of approximately \$240 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 \$9 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 growth by transforming our capabilities to improve customer experiences and expanding our addressable market with new financial solutions leveraging the capabilities across Prudential.

Retirement strategies generated strong sales of \$16.4 billion in the fourth quarter across its institutional and individual lines of business. Institutional Retirement sales of \$14.3 billion in the fourth quarter were driven by strong international reinsurance sales and our best quarter for structured settlements since 2016. International reinsurance sales included a \$9.2 billion transaction in the Netherlands and with the recently passed Dutch Pension Reform Legislation, we anticipate this market will continue to grow over time.

Individual Retirement posted \$2.1 billion in sales, reaching the highest level since the third quarter of 2019. Our product pivots have resulted in continued strong sales of FlexGuard and FlexGuard Income, which increased about 20% from the year ago quarter, while fixed annuity sales have doubled.

Our Individual Life sales increased 33% from the year ago quarter, reflecting our product pivot strategy towards more capital-efficient products.

Variable life protection and accumulation products represented approximately 70% of sales for the year, including a benefit from our recently launched FlexGuard Life product. 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 full year sales were up 11% compared to the prior year, driven by growth in disability and supplemental health. Group's full year adjusted operating income was the highest in the past 15 years and included favorable underwriting experience. As a result, we are lowering our benefits ratio target range by 2 percentage points to 83% to 87%.

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.

In emerging markets, we are focused on creating a selective portfolio of businesses in regions where customer needs are growing, where there are compelling opportunities to build market-leading businesses and where the Prudential enterprise can add value.

Sales in our international businesses were up 24% compared to the year ago quarter. Life Planner sales were up 21%, including the benefits of recent product launches in Japan to diversify our product offering. In addition, Brazil sales were up 24%, reflecting growth across all channels and leading to a full year record.

Gibraltar sales were up 27%, primarily driven by higher independent agency sales and 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 hand 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 first quarter of 2024 relative to our fourth quarter results. As noted, pre-tax adjusted operating income in the fourth quarter was \$1.3 billion and resulted in earnings per share of \$2.58 on an after-tax basis.

To get a sense for how our first quarter results might develop, we suggest adjustments for the following items: first, variable investment income was below expectations in the fourth quarter by \$95 million. Second, underwriting experience was below expectations by \$15 million in the fourth quarter, and we expect \$30 million of unfavorable seasonality in the first quarter.

And last, we included an adjustment of \$240 million for expenses and other items. This includes the \$200 million restructuring charge related to changes in our organizational structure as well as adjustments for typical seasonality related to the timing of expenses and premium. These adjustments combined get us to a baseline of \$3.36 per share for the first quarter. I'll note that if we exclude items specific to the first quarter, earnings per share would be \$3.50.

The key takeaway is that our underlying earnings power has increased significantly over the past year, while we have also made strategic progress improving our risk profile. While we have provided these items to consider,

please note that there may be other factors that affect earnings per share in the first quarter. As we look forward, we have included other considerations for 2024 in the appendix.

Turning to slide 11. Our capital position continues to support our AA financial strength rating. Our regulatory capital ratios are above our targets, and we expect PICA's year-end RBC ratio to be greater than 425%. Our cash and liquid assets were \$4.1 billion within our liquidity target range of \$3 billion to \$5 billion, and we have substantial off-balance sheet resources. We remain thoughtful in our capital deployment, balancing the preservation of financial strength and flexibility, investment 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 confidently navigate the 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

Q

Good morning, and Ken, good luck. Just looking at the 65% free cash flow conversion, I know that bullet was removed from the capital slides. I just want to make sure that, that's still the target?

And then relatedly, when thinking about Japan economic solvency implementation, can you comment on how you see that impacting sources and uses of capital and capital generation over the next few years? Thanks.

Kenneth Yutaka Tanji

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

A

Yeah. Hey, Tom, it's Ken and thanks for the good luck. I appreciate it. We didn't remove that comment. I think it's pretty well understood that our free cash flow ratio has been about 65% over time and that's reflective of our business mix and our growth. It's going to vary period-to-period, but it will be about – it's been about 65% on average. And we think that's reflective of our approach to balance growth with sustainable and diversified sources of cash flow. Actually, in 2023, you'll see that cash flows were actually higher than that for a variety of reasons, so no change there. In terms of ESR in Japan, again, we believe our businesses in Japan are well capitalized and financially strong. And that would be evident in any reasonable capital standard.

We're certainly working with the FSA, advocating for reasonable and responsible standards, but we also have strategies to adapt to that new regime as well. We could reinsure business internally, to the US or Bermuda, we could reinsure externally. So we have a number of strategies to manage in the new regime. And that's something that we're working on.

Thomas Gallagher

Analyst, Evercore ISI



Got you. Thanks. And then just a follow-up, if I could. The strength in Japan and International sales more broadly, I thought was kind of notable in the quarter.

Can you comment on the competition in those markets, what's driving the stronger sales? And do you think that's going to translate into stronger top-line? Because I know it's been sort of flattish, but do you expect that to inflect at all in 2024 or 2025?

Andrew F. Sullivan

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



So Tom, it's Andy. I'll take your question and thank you for noting that. You've heard me say this before. Sales are an outcome of strong brand, great product and outstanding distribution, we feel that we clearly have a competitive advantage in those areas, particularly as it relates to Japan and Brazil.

As you heard from Rob, we are very pleased that our sales were up 24% year-over-year, up 21% in Life Planner and 27% in Gibraltar. Once again, that success was very broad-based as we saw growth in every channel in Brazil and across life planners, independent agents and the bank channel in Japan.

In Japan, we continue to see lift from higher sales of our US dollar product, really supported by the higher US interest rate. But also clearly, our work on innovating our product designs and enhancing our customer experience, in particular, in digital is paying off.

If you look at Brazil and the results there, we saw double-digit year-over-year growth in every channel. Our Life Planner channel outperformed throughout all of last year with high Life Planner retention and strong productivity.

On top of that, we continue to expand and strengthen our third-party distribution. Once again, we saw really strong results flowing from Itau Bank. And we also remain quite pleased that the expansion of our partnership with Mercado Libre.

So, you asked about the outlook. As always, our priority is going to be to deliver strong value to our customers, while achieving healthy levels of profitability, but we are optimistic about our ability to grow both the top- and bottom-line of our business.

Thomas Gallagher

Analyst, Evercore ISI



Okay. Thanks.

Operator: Thank you. Our next question is coming from Ryan Krueger from KBW. Your line is now live.

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.



Hey. Thanks. Good morning. First, can you provide some more color on the key drivers of the RBC ratio improvement in the quarter? I know you had given us the exact RBC during the year, but it seems like it increased a fair amount in the quarter.

Kenneth Yutaka Tanji

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

A

Yeah. Hey Ryan, it's Ken. Just to remind people, RBC is something that is reported annually and so the greater than 25% is where we believe RBC will be at the end of the year. But again, that will be filed in much greater detail, at the end of the month. And so, yeah, we did have an improvement in our RBC ratio in 2023, and it's really a combination of a few things.

One, our in-force businesses are generating free surplus, that's part of it. We had the benefit of admitting negative IMR with the regulatory change that was adopted during the year. We also had a reduction in our AAT reserves, generally from reaggregation of policies and investment portfolios, which created some efficiency. So, it was a combination of that. And so overall, our capital position and flexibility has improved in 2023. And again, you'll see all that when we file our report at the end of February.

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thanks. And then can you help us understand your sensitivity to short-term interest rates, specifically as we get closer to a potential Fed cutting cycle?

Kenneth Yutaka Tanji

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

A

Yes. Sure, Ryan. The bottom line is, is that there's – we don't expect much net impact from short-term rates. We have cash and collateral balances that earn short-term yields. And that would generally be offset by interest rate derivatives from our investment portfolio, where we're actually paying short-term rates and receiving fixed to manage duration. The two generally offset each other.

Ryan Krueger

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. Thanks.

Operator: Thank you. Our next question today is coming from Alex Scott from Goldman Sachs. Your line is now live.

Alex Scott

Analyst, Goldman Sachs & Co. LLC

Q

Hi. So I wanted to touch on the capital as well. I mean, you're in a much stronger position sort of going into 2024 compared to a year ago. I just wanted to get an update on how you're thinking about priorities for deploying that capital? I know at times you've talked about finding some ways to enhance growth. I mean, certainly, your organic growth across some of your businesses has begun to pick up as well. But how are you thinking about all of that? And how do you look at driving more growth into the business?

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

A

Sure. Alex, it's Charlie. I'll take that. Thanks for the question. We have said that we've always wanted – that we want to be good stewards of capital. And as a result, we want to have a consistent disciplined and balanced approach to redeployment of capital within our businesses, as you said, and to shareholders.

And there are really three aspects to our approach on which we focus. First and foremost is maintaining our rock-solid balance sheet and financial strength, which is critical to fulfilling the promises we make to our customers and clients. Second is investing both organically and through programmatic acquisitions to support sustainable long-term growth of our businesses. And the third is returning excess capital to shareholders as we have in the past.

And in this quarter, we've done all three. We've deployed capital to support strong sales across our businesses, including several new products to meet the evolving needs of our customers. We closed on the Deerpath acquisition for PGIM, and we returned over \$700 million to shareholders. So we'll continue to have this consistent and disciplined approach as we go forward.

Alex Scott

Analyst, Goldman Sachs & Co. LLC

Q

Thank you. The second question I had is on PGIM flows. I was hoping you could just provide a little more color on what you expect going into 2024 as some of these headwinds begin to abate that have driven some outflows?

Andrew F. Sullivan

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

A

Yes. Alex, it's Andy. Thanks for your question. We're not satisfied with the recent flow performance of the business, and we have been, and we're going to continue to take the appropriate actions to restore that performance to historical norms. That really starts with ensuring that we have a range of strategies and vehicles so that we can broadly serve our customers. You've seen us continue to intentionally invest into the business to accomplish just that.

So we've continued our expansion into private alternatives with the acquisitions of Montana Capital Partners and Deerpath. You've also seen us launch new vehicles like exchange traded funds and ESG strategies. All that work adds to an already broad and diversified portfolio.

The second thing I would tell you is, flows and active management are correlated with investment performance. And our performance strengthened throughout all of 2023, but flows can lag. So that's one of the reasons we're constructive on the outlook looking forward. Third, we've continued – we've not taken our foot off the gas on investing in distribution because those three things, product breadth, investment results and distribution lead to active flows over the longer term.

Let me also add, like others, I'm sure you're hearing, we believe that the record money market assets that are sitting on the sideline will flow back into fixed income once inflation and rates are stabilized and the rate trajectory, people are more confident in it. We're ready to capitalize on that given the strength of our investment performance with 81% of our assets outperforming benchmark over 5 and 10 years. So clearly not satisfied about the recent flow performance, but optimistic looking forward. I would just end by noting we saw a pickup in gross inflows towards the end of 4Q, and that has continued into this year. So we're optimistic.

Alex Scott

Analyst, Goldman Sachs & Co. LLC

Q

Thank you.

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

Elyse Greenspan*Analyst, Wells Fargo Securities LLC*

Q

Hi. Thanks. My first question is on, I guess, sticking with PGIM. In the slides, you still call out – you call out programmatic M&A there. Can you just provide an update just on the pipeline of transactions, and what you might be thinking about there?

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

A

So thanks, Elyse. It's Andy. So I won't get obviously specific around pipeline, but maybe just bring it up a level, we've demonstrated our strong ability to grow PGIM organically over a long period of time. So we certainly don't look at it as we need M&A to grow. That said, we do remain interested in augmenting our organic growth with mergers and acquisitions. Montana Capital Partners, PGIM Custom Harvest and then obviously, our closure of Deerpath in December. Those are great examples of us adding capabilities in higher growth, higher fee areas of the industry.

So as we look forward, we're going to continue to look to globalize the business. And we're going to focus on higher growth, higher fee areas. So areas like private alternatives and real asset capabilities. Clearly, periods of time like this that are disruptive can lead to opportunities, so we're making sure that we're in the know and in the flow on what's going on. We've also seen an uptick in activity in the marketplace. But as always, we're going to remain patient and disciplined in our approach.

Elyse Greenspan*Analyst, Wells Fargo Securities LLC*

Q

Thanks. And then my second one is on the RBC. So it's now greater than 425%, right? And you guys saw a nice lift in the quarter. Would you look to maintain [ph] PICA (00:30:29) RBC ratio around this level? Or is that something that you would maybe manage down over time and look to bring more capital [ph] to parent (00:30:38)?

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

A

Yeah, Elyse, it's Ken. We're well within our AA financial objectives on an RBC basis. Now it's not the only thing that matters for our credit rating. But on that measure, we're where we need to be, and we have flexibility. So we – again, we'll balance maintaining financial strength, which is obviously important to our value proposition growth and also distribution to shareholders. So we're balancing all three of those objectives.

Elyse Greenspan*Analyst, Wells Fargo Securities LLC*

Q

Thank you.

Operator: Thank you. [Operator Instructions] Our next question is coming from Suneet Kamath from Jefferies. Your line is now live.

Suneet Kamath*Analyst, Jefferies LLC*

Q

Thanks. Good morning. First of all, thank you to Ken for all of your help over the years. I really appreciate it. My first question is just on the [ph] SGUL (00:31:38) deal with Somerset Re. If I remember correctly, that was

supposed to close in the fourth quarter. Obviously, we haven't seen an announcement on that yet. So, maybe just an update there? And are you still expecting \$450 million of proceeds when that deal closes?

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

A

Suneet, it's Rob. Yes, the deal continues to proceed toward closing. Our counterparty has actually received its regulatory approval. We've got one or two final steps on our end, but we expect a closing in this quarter.

Just a couple reminders. One is, recall it is retrospective to the beginning of the year, so 01/01/2024. And with respect to the financial impacts, annual earnings as well as one-time closing costs and capital, we'll update that in an announcement once we close.

Suneet Kamath

Analyst, Jefferies LLC

Q

Got it. And then I guess on PGIM, totally appreciate the strong 5 and 10-year numbers, but it looks like the 3-year number, 63% outperforming is a little bit lower. Is that something that we should – that could have an impact on kind of the flow dynamics, or is there something maybe that will drop off? Or – I just want to get some color on how you're thinking about that 3-year number?

Andrew F. Sullivan

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

A

Yeah, Suneet, I would focus on how much our investment performance has strengthened here in the near term. We did have a period of time, we're an active manager. We have many high conviction strategies designed to produce alpha. We went through a brief period in 2021, 2022, where we did see a dip in performance, specifically in our fixed income business, but that performance has strengthened quite nicely and is very, very strong right now. So, we don't expect that to have a major impact on us looking forward.

Suneet Kamath

Analyst, Jefferies LLC

Q

Okay. Thanks.

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

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Q

Hey. Good morning. So first, a question for Charlie, maybe on capital and just capital deployment overall. Can you talk about what your priorities are and where do – and how do you think about M&A and/or share buybacks? Because it seems like you certainly have the capacity to do more in buybacks given your capital generation than you've been doing, but not sure if you're prioritizing other things instead as well.

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

A

Sure. As I mentioned to Alex earlier, we do – we have a consistent and balanced approach. And – as a result, Jimmy, we really look for, again, the three things. One is to make sure that we have a very strong balance sheet, which we do, as Ken was talking about. The second is to invest organically in our businesses, and you've seen us do that, and we will continue to do that to support sales growth, to support the growth of all our businesses as we

go forward and then to look for acquisitions that make sense. Those would be in higher growth areas. It could be in distribution, it could be in geography as well.

We also see tremendous opportunities right now in the marketplace in places like PRT, right, where we are one of the leaders in this business. We think there's going to be tremendous volume there, and that's a really good business for us as we go forward. And Caroline, you may want to talk about that in one moment.

The final thing, as we've talked about, is returning excess capital to shareholders. We've done that in the past. And if we think we have excess capital, we'll do so. But we're going to evaluate that relative to our investment in our businesses and the opportunities that come along. And Caroline, you might want to talk about one in particular.

Caroline A. Feeney

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

A

Yes, absolutely. So Jimmy, we did finish another strong year in pensioners transfer. We closed 11 transactions worth almost \$6 billion finishing as the number two pensioners transfer writer.

And we've already built on that positive momentum this year, with a \$5 billion deal with Shell. It's our largest first quarter pensioners' transfer ever. And with this win, Prudential now has completed 7 of the top 10 US PRT transactions on record.

We also see that strong sales trend continuing. It's driven by healthy pipelines due to favorable funding positions of over 100%. And last year's market volume was roughly \$45 billion. And we do expect to see that healthy pipeline continue this year.

And although the market is highly competitive with more new entrants, very few competitors have executed transactions exceeding \$1 billion. And while transactions will continue to be episodic in our PRT business, our expertise and our ability to handle large complex transactions and our leadership position in service delivery, we believe will position us well to remain a leader in the market.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Q

Okay. And then just in Latin America, can you share what your views are in terms of potential pension reform in the Chilean market, and what the reasonable case or sort of a worst-case impact would be on Prudential's business there?

Andrew F. Sullivan

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

A

Yeah. So Jimmy, it's Andy. Thank you for your question. As we've talked about before, our priority is always delivering for our customers day-in and day-out. We're very leaned into what's in their best interest.

As you would expect, because of that, we believe in being very proactive on advocating on their behalf. We're going to continue to advocate for reforms that improve the pension outcomes in Latin America and specifically for the citizens of Chile.

Just to give you an update, in Chile, the constitutional referendum was rejected on December 17, but after two failed attempts. So President Boric really has moved on and is now focused squarely on pension reform.

And there is a proposal that's advancing through Congress. That bill proposes to eliminate AFPs and to increase employer contributions to 6%, we're closely monitoring that situation, as a passage would impact our Habitat JV.

But I would say just a couple things. Our Habitat JV is a high-quality, very well-run business. It's been working to actively diversify across countries and into voluntary savings offerings.

And if you take a step back, just recognize that Joint Venture, while it's obviously a larger component of our emerging markets, it's not a material contributor to PFI earnings. So we'll obviously stay very close to it, and we'll let you know when we have any more clarity.

Jimmy S. Bhullar

Analyst, JPMorgan Securities LLC

Q

Thank you.

Operator: Thank you. Your next question is coming from Joel Hurwitz from Dowling & Partners. Your line is now live.

Joel Robert Hurwitz

Analyst, Dowling & Partners Securities LLC

Q

Hey. Good morning. So I know lapses have periodically been an issue in Japan just given exchange rates. It looks like there's a pretty sizable quarter-over-quarter reduction in the in-force [ph] amount (00:38:36) in both international businesses in the quarter. Can you just talk about what you saw in terms of lapsation there?

Andrew F. Sullivan

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

A

Yeah. So thanks, Joel, it's Andy. So let me just talk about the decline in the in-force. First, as I always start, we're exceptionally proud of our Japanese businesses. They've been very consistent and stable contributors to Prudential for a very long time.

With that, there are a few factors, though, that are impacting the life insurance in-force amounts. First, this is important to note, a significant portion of our recent sales are investment contracts, and that really reflects what customers are looking to buy. Those sales do not include a material life component, but are contributing to our earnings.

Second, we are seeing natural runoff in the older life blocks, particularly in the legacy yen business in Gibraltar. And then as we've talked about in previous quarters, with the recent yen depreciation, we've seen a modestly elevated level of surrenders. But all that said, we are confident in our ability to grow and diversify our Japanese businesses across insurance, investment and retirement security, and we're continuing to invest in them.

Joel Robert Hurwitz

Analyst, Dowling & Partners Securities LLC

Q

Okay. Helpful. And then switching gears to Group. So you reduced the benefit ratio target there. Can you just talk about the overall drivers to the reduction there? And then what's the growth outlook for that business? It looks like top line for full year was roughly flat. So just any color on growth expectations there?

Caroline A. Feeney

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

A

Yes, absolutely, Joel. It's Caroline. Thank you so much for your question. So first of all, I'll start off by saying we had another very strong quarter for Group Insurance and we're very pleased with the full year results of this business. And we believe we're in that strong position in Group given the progress we've made in executing on our strategy and our future earnings power will reflect the efforts we've made to grow in a disciplined and profitable manner.

We continue to focus on diversifying our business by expanding in the under 5,000 live market and the association segments. We're adding new products like supplemental health and continuing our growth in disability. And we made progress in that diversification effort, increasing our disability premiums and fees at a higher rate than before, and our supplemental health premiums also grew at strong double-digit annual growth rates. And this diversification is driving stronger core earnings with higher margins.

So as for our performance, our full year benefits ratio was just over 83 percentage points. It includes very strong performance in our Life block in the second and third quarters of last year and record disability results in the first half of the year. While we don't expect that record performance to continue and definitely, there are certainly other factors to consider.

So overall, Joel, I'd say that our Group business is growing. It's doing so at attractive margins with COVID having transitioned to an endemic state combined with our diversification strategy I just walked you through as well as investments we've made in improving our claims management capabilities and strategic partnerships.

We believe we'll see that underwriting performance and earnings power continue to improve. And then that is why we are confident with our decision in lowering our benefits ratio guidance to be 83% to 87% for the year. And in terms of just future earnings power as well, I gave you some color there as well, Joel. We believe the future earnings power in Group Insurance will continue to be strong as we continue to grow and execute on our strategy.

Joel Robert Hurwitz

Analyst, Dowling & Partners Securities LLC

Q

Very helpful. Thank you.

Operator: Thank you. Our next question today is coming from Wilma Burdis from Raymond James. Your line is now live.

Wilma Burdis

Analyst, Raymond James & Associates, Inc.

Q

Hey. Good morning. I'm just wondering if there's been any activity with Prismic? Seeing that you guys have been focused on the sales of [Technical Difficulty] (00:42:54) and also with this large PRT deal. So if you can give us an update there, please?

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

A

Hey Wilma, it's Rob. So as we've articulated before, we're quite enthusiastic about Prismic and more broadly about what we see to be the opportunities that are coming out of the intersection between asset management and insurance and specifically the role that Prismic can play in helping us to execute against that opportunity.

We believe it will create avenues of growth across our businesses, not specifically for the PRT transaction that we recently announced, but the opportunity to be a source of financing for sales growth, both in the retirement marketplace and our other businesses on a go-forward basis.

Our investors, which are extremely large global institutional investors share our aspirations, both from a directional standpoint and from a quantum standpoint. So our expectation is to go well beyond the initial \$10 billion structured securities or structured settlements transaction that we completed.

It's going to include some level of ongoing balance sheet optimization. It's going to include, as I noted, financing the growth across our businesses. I think what's unique in a way about Prismic is the appetite by it and its investors for longer duration and more complex liabilities. And we're also going to look to do third-party blocks as well in Prismic, all of which will inure to the benefit of increasing the assets under management for our PGIM business.

Wilma Burdis

Analyst, Raymond James & Associates, Inc.



Thank you. And could you talk a little bit about the buyback. I think you guys stuck with the \$1 billion authorization for 2024. Certainly, when you guys sell blocks and run off earnings a little bit, it's good to see more capital returns. So can you just talk about how you guys are thinking through that? Thank you.

Kenneth Yutaka Tanji

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



Yeah, hey, it's Ken. Yeah, we've had a very consistent approach to shareholder distributions using both dividends and share repurchases as a way to return capital. Our share repurchases for this year was approved by the board, and they have considered our capital position, our outlook for free cash flow, but also opportunities to deploy that capital into organic growth, as Charlie discussed, in particular, the very robust PRT market.

So all those things factored into it. We increased our dividend. Again, that's – now we've increased that 16 years in a row. So again, it all factors into what we think is a very consistent approach, balancing all our objectives as well. So hope that color helps.

Wilma Burdis

Analyst, Raymond James & Associates, Inc.



Thank you.

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

John Barnidge

Analyst, Piper Sandler & Co.



Good morning. Thank you for the opportunity. And best of luck, Ken. My first question, I appreciate – if we could go to the Group Insurance business, I appreciate the benefit ratio guidance. But is there an expense savings story in disability coming up, I can't help but notice improvement in administrative expenses in recent quarters. And with COVID moving endemic, the ramping up of expenses, should that fall to the side? Thank you.

Caroline A. Feeney

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

A

Yes. So John, it's Caroline. Thank you so much for your question. In terms of our overall expense management, you may have seen we saw 100 basis point improvement in our admin ratio from the year ago quarter. That is driven by both business growth and continued expense discipline. And we will continue to focus on expense efficiencies and obviously then would regularly adjust our operating models to ensure the appropriate levels of service going forward.

In terms of disability overall, I would say across Group disability results were driven by our focus on effective claims management, including those short and long-term disability as well as absence in family leave. We also benefited from the continued tailwinds of strong employment and high interest rate environment and our disability business had an outstanding year.

I would also just want to point out something else strategically, we're doing on the disability side as we continue to grow that area. We've actually invested, John, in improving our claims management process through a strategic partnership with Evolution IQ. This is a provider of AI-driven technology that provides real-time monitoring leading to increased recoveries.

So overall, I'd say in terms of expense management, we remain highly disciplined and also, obviously, very much focused in terms of our pricing discipline. The evidence there is our ability to accomplish all this growth in maintaining our price competitiveness. But the fact that as we continue to grow our book, we're also not afraid to walk away if the pricing just doesn't make sense on any particular case. So overall, we remain confident in our decision to lower benefits ratio guidance and feel very comfortable with our expense management and our pricing discipline.

John Barnidge

Analyst, Piper Sandler & Co.

Q

Thank you for that answer. My follow-up question. When you talk about globalizing the PGIM business, are there markets you're not large in size that you want to get bigger in? Where does Prismic sit within that growth opportunity for PGIM internationally?

Andrew F. Sullivan

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

A

So John, I'll start out and then, Rob, if you want to tail in, you can jump in. So when we talk about globalizing the business, I think it's important to recognize that a majority of our assets under management today are in the United States. So we've been actively, for many years now, working to expand across Europe and Asia and have invested quite heavily in distribution on both the institutional and retail side of the business. That said, as we look to continue to broaden and diversify our mix of both asset classes, but geographies, we would look to Europe and Asia as key geographies that we're most interested in growing.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

A

John, it's Rob. Just following up on Andy. Within Asia and with respect to Prismic, I think what I'd note is, we see a huge opportunity in Japan, both with regard to, as Ken alluded to earlier, in the call, optimizing our own book, but also with respect to the sort of opportunities we see with third parties in that marketplace as well.

John Barnidge

Analyst, Piper Sandler & Co.



Appreciate that. Thank you.

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

Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.



Thanks, guys. Good morning. Sorry to be the one to ask. Just curious if there's any update on commercial real estate side for you guys. It looked like the LTV deteriorated a little bit. Just kind of wondering how you feel about any kind of watch list or resolutions that you've made last year too.

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.



This is Rob. So I'll take your question, Mike. So a couple thoughts. One, from an overall market standpoint, let me start there. From a peak to trough, what we've seen is across the market, about a 16% correction, and that number relates to, what I'll call, institutional quality real estate, the sort of things that we invest in or we lend against, and that's on an unlevered basis.

Our estimate is that the peak to trough in this cycle across real estate types is going to probably be a little over 20%. So we've got 5% or 6% probably left in the way of price correction yet to experience.

Now within that, office, obviously, has corrected much more severely closer to 30% to-date, and probably has another 10%, 15% yet to go. Because the construction of our portfolio is significantly underweight office, and because the overall quality of the portfolio and the diversification of it across geography and property types, and importantly, because this is a portfolio that's directly originated by PGIM with the team that's deep and averages some 25 years of industry experience, we're actually finding that our portfolio is holding up quite well. So loan-to-values across the portfolio were about 58% and our discount – our debt service coverage ratios remain right around 2.5%.

Within our overall portfolio, our actual valuations increased about 6% during the course of 2023 despite the fact that we saw a double-digit decline in the office component of our portfolio. But again, because that office component is only 2% of our assets or 50% – about 14% of our mortgages, the performance of the rest of the portfolio has offset that. So, with regard to portfolio performance, we're actually feeling quite good.

The last thing that you asked about was sort of what we're seeing in watch list, et cetera. I guess the way I would describe that, Mike, is that, first, if we look at our experience with maturities during 2023, we had about \$2 billion worth of scheduled maturities. Of those, we provided modifications for four – less than \$400 million of that \$2 billion with those modifications providing longer-term extensions. The remainder of all of those maturities was resolved favorably through refinancing payoffs or short-term extensions that then led or leading to subsequent payoffs.

In the upcoming year 2024, we've got about \$3 billion of maturities coming on. That's about 6% of the portfolio that's maturing. And while we don't expect to be immune from this cycle by any means, we do expect that on a relative basis, we'll be quite resilient. We increased our reserves in the real estate portfolio to around \$370 million as of the end of the year and that represents about 72 basis points, and we think that that's well provisioned against the portfolio, again, given that what we've experienced in the underlying quality of that portfolio.



Michael Augustus Ward

Analyst, Citigroup Global Markets, Inc.

Awesome. Really helpful. Thanks, Rob.

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

Charles F. Lowrey

Chairman & Chief Executive Officer, Prudential Financial, Inc.

So thank you again for joining us today. The fourth quarter capped a year of continued growth and evolution for Prudential. Our strategy, coupled with our mutually reinforcing business system positions us well to deliver long-term sustainable growth to all our stakeholders. Our fundamentals are strong, and we are confident about our momentum going into 2024. We will continue to lead the way in expanding access to investing insurance and retirement security across the globe, as we seek to help current and future generations build a secure financial future.

Thank you again for joining us, and have a good day.

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

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2024 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.