Corrected Transcript

31-Oct-2024

Prudential Financial, Inc. (PRU)

Q3 2024 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.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

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

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.

OTHER PARTICIPANTS

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

Suneet Kamath
Analyst, Jefferies LLC

Thomas Gallagher
Analyst, Evercore ISI

Nicholas M. Annitto
Analyst, Wells Fargo Securities LLC

John Barnidge
Analyst, Piper Sandler & Co

Wes Carmichael
Analyst, Autonomous Research US LP

Wilma Burdis
Analyst, Raymond James & Associates, Inc.

Alex Scott
Analyst, Barclays Capital, 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 would 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; Yanela Frias, Chief Financial Officer; and Rob Axel, Controller and Principal Accounting Officer. We will start with prepared comments by Charlie, Rob and Yanela, and then we will take your questions.

Today's discussion may include forward-looking statements. It is possible that actual results may differ materially from the predictions we make today. In addition, our presentation includes references to non-GAAP measures for reconciliation of such measures to the comparable GAAP measures, 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 of 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 all of you for joining us today. Our third quarter performance reflects continued positive momentum in growing our businesses, increasing capital efficiency, and pivoting our product suite to address the investing, insurance, and retirement needs of our customers and clients around the world.

We reported robust sales across our US and international insurance and retirement businesses, as well as strong investment performance and private credit originations in PGIM. We also maintained our disciplined approach to capital deployment, while continuing to invest in our businesses and returning excess capital to shareholders. Our strategic progress and performance are backed by our financial strength.

Turning to slide 3. This morning, I will highlight how we continue to become a higher growth, more capital efficient company. We are growing our market-leading businesses while increasing our capital flexibility. Let's start by taking a closer look at how our Retirement Strategies business is benefiting from the global retirement opportunity. On the institutional side, our continued leadership in pension risk transfer was reinforced through a second transaction with IBM, this time to ensure $6 billion of pension liabilities. With this latest transaction, we have now closed 7 out of the 10 largest pension risk transfer deals in the US. On the individual side, five of our annuity products have exceeded $1 billion in sales so far this year, validating our product diversification strategy.

Our Japan business is another great example of how we're addressing the growing demand for retirement products. While life insurance has traditionally comprised the bulk of our business in Japan, year-to-date sales of retirement and savings products are up 30% compared to the prior year. Meanwhile, PGIM is well positioned to help plan sponsors deliver benefits to millions of retirement beneficiaries through its diversified investment solutions. As a market leader, with nearly $0.5 trillion of assets under management supporting defined benefit and defined contribution plans, PGIM serves more than half of the world's 300 largest pension funds.

Now, let's look at how we are further growing our market-leading businesses by diversifying our products and expanding our global distribution networks. In our Retirement Strategies business, we're increasing the number of individual annuity solutions and adding new workplace partnerships, like the relationship we recently announced with J.P. Morgan Asset Management. In our Group Insurance business, we are expanding our disability and supplemental health products and growing our position in the under 5,000 lives and Association market segments.

Turning to our Individual Life business, we continue to launch innovative, more capital efficient products and we have positive momentum across our distribution channels. In our international businesses, we're benefiting from recent product launches and our strong multichannel distribution in both Japan and Brazil. And lastly, PGIM continues to benefit from our deeply connected and reinforcing business mix, resulting in strong affiliated flows on a year-to-date basis. In addition, private alternatives capital deployment has increased 24% year-to-date, underscoring the demand in the market and PGIM's private credit capabilities.

PGIM is also well-positioned to continue to capture the growing retail demand for fixed income products. In addition, our investments in technology across our insurance, retirement and asset management businesses is helping us to deliver exceptional sales, service and claims experiences supporting our growth strategy.

At the same time, we're improving the quality of earnings from the continued shift of our business mix. This quarter, we announced a transaction with Wilton Re to reinsure an $11 billion guaranteed universal life block. Following this transaction, we will have reduced our guaranteed universal life reserves by 60%, advancing our strategic progress to become a higher growth, more capital efficient company.

Turning to slide 4, our continued investments in our businesses are supported by our disciplined approach to capital deployment, which included returning more than $700 million to shareholders during the third quarter.

Turning to slide 5, our growth strategy is further supported by our financial strength and our risk and capital management framework. We maintain a AA rating, which reflects a healthy capital position, including more than $4 billion in highly liquid assets at the end of the third quarter. We also maintain a well-diversified, high-quality portfolio and disciplined approach to asset liability management. In closing, we're operating from a position of strength, with confidence in our strategy, our capabilities, and our path to deliver long-term sustainable value for all our stakeholders.

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

Robert Michael Falzon

Vice Chairman, Prudential Financial, Inc.

Thanks, 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. Our pre-tax adjusted operating income was $1.6 billion or $3.48 per share on an after-tax basis for the third quarter of 2024 and $9.98 on a year-to-date basis, which is up 6%. These results reflect the execution of our strategy to grow our market-leading businesses and were driven by higher spread and fee income due to continued strong sales and the benefit of higher interest rates and equity markets, net of increased expenses to support the growth of our businesses.

Year-to-date adjusted operating return on equity of 13.7% has improved a 0.5 percentage point from the prior year. This reflects the strength of our businesses, the benefits from the deliberate actions we have taken to pivot to more capital efficient and higher growth products.

Turning to the operating results from our businesses compared to the year-ago quarter. PGIM, our global investment manager, had higher asset management fees, driven by favorable investment performance, contributions from the Deerpath Capital acquisition and market appreciation. This was partially offset by higher expenses to support business growth.

Earnings growth in our US businesses reflected more favorable underwriting results from better-than-expected mortality experience in Individual Life and higher spread income driven by business growth and the benefit of higher interest rates. This was partially offset by lower legacy traditional variable annuity fee income as we intentionally pivot to less market-sensitive products, as well as higher expenses to support business growth.

Results of our international businesses included less favorable underwriting results, primarily reflecting elevated US dollar product surrenders with a weakness in the yen, and higher expenses to support business growth, partially offset by higher joint venture earnings driven by encaje performance in Chile and higher spread income due to higher yields from reinvestment of the portfolio.

Turning to slide 7, PGIM, our global investment manager, has diversified capabilities in both public and private asset classes across fixed income, equities, and alternatives. PGIM's strong investment performance continues to improve with 86% of assets under management exceeding their benchmarks over the past year. This has contributed favorably to strong long-term performance with 79% and 85% of assets under management outperforming their benchmarks over the last 5- and 10-year periods respectively.

PGIM's assets under management increased by 15% to $1.4 trillion from the year-ago quarter driven by market appreciation, investment performance, and net flows. Total net flows in the quarter of $3.2 billion included affiliated net flows of $6.4 billion driven by strong retirement strategy sales, partially offset by $3.2 billion of third-party net outflows. On a year-to-date basis, total net flows were $29 billion, including $15 billion in affiliated flows and $14 billion from third-party clients. These inflows reflect the net benefit from large episodic institutional pension plan activity.

As the investment engine of Prudential, PGIM's capabilities support the success and growth of our US and international businesses in retirement, asset management, and insurance. PGIM's asset origination capabilities, investment management expertise, and access to institutional and other sources of private capital, including through our sponsored reinsurer, Prismic, are a competitive advantage, helping our businesses 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, our diversified PGIM Private Alternatives platform, which has assets under management of over $250 billion, experienced strong private credit origination activity driven by our direct lending businesses, including the benefit from our recent acquisition of Deerpath Capital.

Turning to slide 8, our US businesses produce diversified earnings from fees, net investment spread, and underwriting income and benefit from our complementary mix of longevity and mortality businesses and diversified sources of earnings. We continue to focus on growing our market-leading businesses by expanding our addressable market with new financial solutions delivered through a broader distribution footprint, leveraging capabilities across Prudential and enhancing those capabilities to improve the experience of our customers and distribution partners while driving operating efficiencies.

Retirement Strategies generated strong sales of nearly $15 billion in the third quarter across its institutional and individual lines of business. Institutional Retirement sales totaled $11 billion in the quarter. US-funded pension risk transfer transactions of $6.3 billion included the second PRT transaction with IBM. Additionally, longevity risk transfer sales totaled $2.8 billion for the quarter. Year-to-date, Institutional Retirement sales were over $26 billion as we have captured about 40% of the PRT market.

Individual Retirement posted $3.6 billion in sales, its best quarter of sales in over a decade. Our product pivots and innovation have resulted in continued strong sales of our registered indexed linked annuities, and fixed annuity products have more than doubled from the prior year. Additionally, we continue to reduce market sensitivity by running off our legacy variable annuities.

Group Insurance sales primarily occur in the first quarter of the year based on annual enrollments. On a year-to-date basis, sales increased 3% compared to the prior year driven by growth and supplemental health. We are executing our strategy of both product and client segment diversification while leveraging technology to increase operating efficiency and enhance the customer experience. These actions to improve profitability and performance resulted in a benefits ratio of 83.4% which is the low end of our target range.

In Individual Life, sales increased 13% from the year-ago quarter and 9% year-to-date. These increases include the benefit from the strength and breadth of our distribution capabilities and expansion of our product offerings, including our pivot towards more capital efficient products like FlexGuard Life which reached its highest sales quarter since its launch in 2022.

Turning to slide 9, our international businesses include our Japanese life insurance companies where we have a differentiated multi-channel 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 selling approach and protection and retirement 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 25% compared to the year-ago quarter. Higher sales in Japan are benefiting from recent product launches as we expand our retirement and savings offerings, which are gaining traction with customers and represented 75% of the current quarter sales.

In addition, emerging market sales were also higher, driven by growth in Brazil, as we continue to expand third-party distribution and benefit from the strong performance of our world-class Life Planners. 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 and client 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 Yanela.

Yanela del Carmen Frias

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

Thank you, Rob. I will begin on slide 10, which provides insight into earnings for the fourth quarter of 2024 relative to our third quarter results. The pre-tax adjusted operating income for the third quarter was $1.6 billion and resulted in earnings per share of $3.48 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 by $50 million in the third quarter, driven by lower private equity returns. Beginning next quarter, we plan to pre-announce our estimated variable investment income results. Next, underwriting experience was above expectations by $15 million in the third quarter. And last, we include an adjustment of $100 million for expenses and other items.

Higher expenses in the third quarter reflect the timing of investments in enterprise initiatives to support growth. We expect higher initiative investments to continue in the fourth quarter and maintain the full year 2024 expected loss in corporate and other of $1.8 billion. We also expect seasonally lower annual premiums of $50 million in international in the fourth quarter. These adjustments combined get us to a baseline of $3.34 per share for the fourth quarter. I will note that if you exclude items specific to the fourth quarter, earnings per share would be $3.67.

The key takeaway is that our underlying earnings power increased and reflects the improved quality of earnings from intentionally shifting our business mix and continued investment in the growth of our market-leading businesses. While we have provided these items to consider, please note that there may be other factors that affect earnings per share in the future. A few items that I would highlight.

We continue to benefit from new money rates that were higher than our portfolio yield in the third quarter, and we do not expect a significant impact from the potential decline in short-term rates. We have cash at the holding company, floating rate assets across our businesses, and collateral in Individual Retirement Strategies that earn short-term yields, which is generally offset by interest rate derivatives that manage duration across our businesses, where we pay short-term rates and receive fixed.

The earnings benefit from the recent pension risk transfer transactions grows over time as we reposition the investment portfolio and is muted by in-force runoff. In addition, our legacy variable annuities in-force is running off at $3 billion to $4 billion per quarter, and we have been experiencing an elevated level of surrenders in our businesses in Japan associated with US dollar products as the yen has weakened relative to the US dollar. The exchange rate hit a 38-year low in the second quarter. And while we have experienced a reduction in surrender levels as the yen strengthened during the third quarter, we expect some continued near-term pressure on earnings before surrenders normalize.

Also of note, in order to provide greater insight into our financial outlook and to better align with the longer-term nature of our business, we plan to introduce new intermediate-term financial targets. These targets will replace our quarterly baseline disclosure, concurrent with the release of our fourth quarter earnings results.

Turning to slide 11, our regulatory capital ratios are strong and above levels that we believe represent AA financial strength as we continue to maintain margins to support strong organic growth prospects and are prepared for the potential impacts of market-driven volatility. Our cash and liquid assets were $4.3 billion, which is above our minimum liquidity target of $3 billion, and we have substantial off-balance sheet resources. We remain thoughtful in our capital deployment, preserving financial strength and flexibility, investing in our businesses for long-term growth, and returning capital to shareholders.

Turning to slide 12, and in summary, we are becoming a higher-growth, more capital efficient company. We are maintaining a disciplined approach to capital deployment, and our growth is supported by the strengths of our balance sheet.

And with that, we will be happy to take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We'll now be conducting a question-and-answer session. [Operator Instructions] Our first question today is coming from Ryan Krueger from KBW. Your line is now live.

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

Q

Hey. Thanks. Good morning. I guess, one question and kind of a related follow-up would be, one, can you give an update on Prismic and potential activity there? And then the second one was just how you plan to use capital that you free up from both external and internal reinsurance transactions going forward? Because I think you've freed up some capital from various transactions, but what are your key priorities for returning that over time?

Robert Michael Falzon
Vice Chairman, Prudential Financial, Inc.

A

Ryan, it's Rob. I'll take the first part of your question, and I think Charlie will probably jump in and handle the second part of that. So, I guess, what I'd start with, Ryan, is I would reiterate what we said last quarter, which is we'd be disappointed if we've not entered into an additional transaction that we could announce before year-end. We're continuing our work on a very active pipeline. It's got multiple reinsurance transactions across a spectrum of types, so it's ongoing looking at our own balance sheet optimization. It's looking at opportunities for flow or new sales financing as well as third-party blocks. And there, we have a particular focus on Japan. And as you may have seen, we actually made – Prismic actually made an announcement that we've stood up a dedicated licensed team in Tokyo in order to be able to advance that opportunity.

While they're all in play, I think we would say that the likely next transaction is going to be back-book amongst the variety of things that we're working on and potentially in Japan. The interest in that is in particularly that it would help establish the plumbing and the precedent for doing third-party transactions from that market, which we think is an interesting market in which we have a competitive advantage. If I was – stepping back, Ryan, I would say, we have a visible pipeline. We have capital available to us. We've got the right underwriting expertise and the staffing at Prismic, and all of that combines to give us confidence in our ability to scale Prismic in a way that's consistent with our aspirations and the aspirations of our investors.

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

A

And Ryan, this is Charlie. Let me add on to what Rob said in terms of capital deployment. We've always said that we want to be good stewards of capital and that we have a consistent disciplined and balanced approach to the redeployment of that capital within our businesses and to our shareholders. And there are really three aspects to our approach on which we focus. The first is just maintaining our rock-solid balance sheet and financial strength, which is fundamental to us in terms of fulfilling our promises, which we've done for almost 150 years. The second is investing, both organically and through programmatic acquisitions to support the sustainable long-term growth of our businesses.

And finally, returning excess capital to shareholders, as we've done in the past. And in this quarter, we deployed capital to support strong sales across our businesses, including several new products to meet the evolving needs of our customers, and we returned over $700 million to shareholders. So, we have a consistent process, and we're going to follow that through.

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

Great. Thank you.

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

Suneet Kamath
Analyst, Jefferies LLC
Q

Hi. Thanks. Good morning. I wanted to start with Japan. Can you talk about how the margins or the returns on these retirement products that you're selling compare to the protection products, death protection products that you used to sell? I mean, my recollection is those death protection products have very attractive margins. And I just want to get a sense of the new business that you're writing and how that compares.

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

Yeah, Suneet, good morning. It's Andy. I'll take the question. So, we're pleased with the profitability of the sales that we're seeing in Japan. And we do not expect an impact on the margins, given the mix shift between the product types. We're actually quite excited. We see a long-term opportunity to help the citizens in Japan prepare for and enjoy their retirement. Given the longevity aspects of Japan and the low bank savings yields, we believe that we're going to see a continued strengthening of demand for a broader set of retirement products.

While we already have a broad product portfolio there, we've been methodically diversifying and expanding our capabilities to really lean into this opportunity. And you saw that – success of that strategy in third quarter with our retirement investment product sales increasing about 30% year-to-date versus the prior year. And those sales accounted for the majority of Japan sales in the quarter. So, we don't expect an impact on the margins given that mix shift, and we're very excited as we see this as early days in what should be a very long-term opportunity tailwind.

Suneet Kamath
Analyst, Jefferies LLC
Q

Okay. That makes sense. Thanks for that. And then I guess for Caroline, it looks like your prediction that 2024 would be another record year for annuity sales is playing out. Just curious, if you can give us some color around like where the growth is kind of coming from. Is it coming out of 401(k) plan rollovers or product exchanges? And how sustainable do you think this level of sales is as we think about moving into 2025? Thanks.

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.
A

Yes, sure. Thanks for your question, Suneet. So, first of all, let me say, we are extremely pleased with our individual retirement results. And as you saw in the third quarter, we drove over $3.5 billion of sales, making our best quarter in over a decade. And this strong performance is the direct result of our efforts over the past few years to diversify our annuity portfolio, allowing us to meet more of the consumer need for protected savings and income. In fact, we now have the broadest individual product portfolio we've ever had. And to put that in perspective, Suneet, as Charlie mentioned in his opening comments, just two years ago, we had only one product that generated over $1 billion in sales. Now, we already have five products that have exceeded that mark this year.

So, in terms of your question on sustainability, the outlook for our individual annuity franchise remains strong. Beyond our diversified portfolio, what we see is a clear tailwind coming from aging demographics. That's over 11,000 Americans turning 65 every day, and 30 million Americans turning 65 between now and 2030. So, a lot of that growth, Suneet, is coming from that tailwind. We're also seeing increased demand in the marketplace for protected savings and income solutions. So, combining those factors, the industry is on pace for a third sequential record-setting sales year, as you say, with year-to-date sales outpacing last year by more than 25%. And we'll meet that demand head-on with our diverse portfolio solutions and the strength of our brand and our distribution.

Suneet Kamath
Analyst, Jefferies LLC
Q

Got it. Okay. Thanks for that.

Operator: Thank you. Next question today is coming from Tom Gallagher from Evercore ISI. Your line is now live.

Thomas Gallagher
Analyst, Evercore ISI
Q

Good morning. First question back on Japan. Can you talk about your sales mix between yen products, foreign currency products? I know foreign currency has been a big part of what's gone on, but just given the move higher in rates in Japan, are you starting to see a pivot back into yen-oriented products? And how do you see that going forward? Thanks.

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

Yeah, Tom. It's Andy. I'll take the question. So, in the third quarter, we saw about 30% of our sales in Japan were yen-based sales. The fact is our level of yen-based sales has nearly doubled over the last three years, and this has been based on what have been a series of very intentional actions on our part. We believe in having a broadly diversified product portfolio in every geography that we operate. So for Japan, that means having good diversification across life insurance, retirement, and savings products, and having a nice balance between US dollar and yen offerings.

So we've been intentionally strengthening the choices that our customers have for yen-based products over the last year or so. And these new product introductions have been a material contributor to the 29% year-over-year sales increase. So, we believe in a broad portfolio. We've been expanding the yen-based offerings, and we're seeing the success of that strategy.

Thomas Gallagher
Analyst, Evercore ISI
Q

Got you. Thanks. And then my follow-up is, I guess, a broader industry question, but I think Swiss Re research institute put out a report recently on how they expect excess mortality to persist for another 5 to 10 years. And hard to know exactly what the degrees they're referring to is, but is that – and particularly, it mentioned the US and Japan, which are obviously two big exposures for Pru. Curious, do you share that view, broadly speaking? If that does come to pass, do you feel like you have enough prudence in your reserves to handle it? And any additional thoughts you would have on that topic. Thanks.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

Hey, Tom. It's Yanela. And yeah, let me take that question. So, yes, the observations and the expectations from the report are consistent with our internal view and with the approach that we have taken for our mortality assumptions. So, our assumptions reflect some continued excess mortality through 2028 before returning to the pre-pandemic trend line. And obviously, we regularly monitor mortality trends and advances and adjust accordingly every year during our annual assumption process in the second quarter.

I would remind you that we have a diversified mix of businesses providing natural mortality hedges, right, so life insurance, and PRT, and also throughout globally within the US and other significant insurance markets such as Japan and the UK. And so, a few data points on what we are seeing. In Individual Life, we have experienced mortality that is broadly in line with expectations since updating our mortality-based table assumptions in 2022, and this quarter, we saw favorable experience.

Now, the Individual Life insured population is less impacted by COVID than the general population. Our PRT mortality experience has trended heavier in 2023 that is consistent with continued excess mortality, and what I would say is that our PRT population tends to be more closely correlated to the general population.

Thomas Gallagher
Analyst, Evercore ISI

Q

That's great. Thanks.

Operator: Thank you. Next question today is coming from Nick Annitto from Wells Fargo. Your line is now live.

Nicholas M. Annitto
Analyst, Wells Fargo Securities LLC

Q

Hey. Good morning. Thanks. I just wanted to hit on PGIM first. Maybe could you talk about what went on in institutional in the quarter, what drove the outflows and maybe how you're expecting them to come into 2025? I mean, I know it's episodic, but any color there would be helpful. Thanks.

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

A

Sure, Nick. It's Andy. And let me actually comment on institutional and retail. So, starting on institutional, I'd reiterate what I said last quarter. We expect to continue experiencing more near-term variability in our institutional fixed income flows. We are the sixth largest manager of DB assets globally, and many of these DB plans remain overfunded and we're seeing these clients derisk. That is leading to more money in motion creating this near-term variation. But as the rate curve normalizes, money will flow back more consistently into institutional fixed income, and we obviously expect to benefit from that, given our world-class business.

Stepping back from that dynamic, we believe in analyzing our flows over a longer timeframe and looking inclusively at affiliated flows. Affiliated flows stem from when we win pension risk transfer transactions as well as from flow from asset-intensive annuities and life insurance. In the pension space, often the activity within third-party and affiliated are linked, so you're really talking about the same universe of DB plans. So, the bottom line is you have to look at both third-party and affiliated to get the full picture on our PGIM assets under management. If you look across 2024 year-to-date, our third-party institutional flows are a positive $14 billion and our affiliated institutional flows are a positive $15 billion. So we like that track record of success.

Just a minute on retail. On the retail side of the business, we continue to achieve improving results, and in the quarter, we saw a positive $1.3 billion in inflows. We are seeing, in retail, the investors return to fixed income strategies, and we would expect that will accelerate, given the anticipated Fed direction. So, really, if you step back, the strength of our fixed income franchise is very, very strong, and we think over time we're going to experience significant tailwinds and we'll be a net winner over the long term.

Nicholas M. Annitto
Analyst, Wells Fargo Securities LLC

Q

Thanks. That's helpful. And then, maybe just more of a higher level one, I guess following the GUL deal that you guys just did and some of the other deals that you guys have done, is there any block in the business that you guys kind of view non-core that can be shopped?

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

A

Hey, Nick, it's Charlie. Let me take that one, and I'll take a step back and then directly answer your question. But we feel really good about the considerable progress we've made in shifting our business mix to be more capital efficient and the fact that we're well positioned to capture market opportunities for higher growth. We've executed on several transactions that have driven a 50% reduction in our traditional variable annuities portfolio and also a 60% reduction in the guaranteed universal life reserves, following the transaction we announced in the third quarter with Wilton Re. And while we've been quite successful in increasing our capital efficiency as part of our strategy, we've been equally focused on investing in our market-leading businesses to drive growth with some of those proceeds.

Having said that, and this gets to your question, we will consider additional opportunities as long as they meet our strategic and financial objectives and make sense for all our stakeholders. So, we'll continue to review our portfolios, but it needs to meet the strategic and financial objectives that we talked about.

Nicholas M. Annitto
Analyst, Wells Fargo Securities LLC

Q

That's helpful. Thanks.

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

John Barnidge
Analyst, Piper Sandler & Co

Q

Thank you for the opportunity. On the variable investment income pre-announcement that you're going to do for disclosure going forward, will that be a wholly separate pre-announcement from the AUM one that comes out as an 8-K? Thanks.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Hey, John. It's Yanela. That will be included in the current disclosure that we provide on AUM, so it'll be all-inclusive.

John Barnidge
Analyst, Piper Sandler & Co
Q

Thank you for that. And then it sounded like you were upbeat about the growth opportunity in workplace solutions. Can you maybe talk about partnerships there that you're working on? Thank you.

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.
A

Yeah. Hi, John. It's Caroline. Thank you for your question. And yes, we are very much upbeat and confident in terms of our group results going forward. And we have a number of strategic partnerships that we've recently executed. And most of these are very much focused on elevating the customer enrollment experience, but they're also going to be a key contributor to our overall focus on things like claims management. And I'll just give you a few examples, John.

One of those is a partnership with a leading-edge technology firm that's really transforming the benefits experience for millions of people. And essentially, their innovative platform walks employees through the enrollment process, connecting them with Prudential's counselors for one-on-one support. Another partnership we have is with EvolutionIQ. This is an AI-driven platform that leverages data to expedite claim examiner evaluations in short as well as long-term disability claims. And the platform is going to help us eliminate manual work. It's going to help us provide better outcomes for customers overall for disability claims.

And I would just say in terms of how we're feeling about our group business overall, John, it is growing nicely, as we've demonstrated another strong quarter, driven by solid underlying fundamentals. We're growing at attractive markets – margins. And when I think about our overall diversification strategy, improving claims management capabilities and investments in those strategic partnerships I just mentioned, we're very much positioned to continue to see that profitable growth and solid earnings.

John Barnidge
Analyst, Piper Sandler & Co
Q

Thank you.

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

Wes Carmichael
Analyst, Autonomous Research US LP
Q

Hey. Thanks. Good morning. My first question, I guess, was on the comments regarding moving away from the quarterly EPS baseline and moving towards new financial targets. Is there any more color you can provide us on what you're considering for those? And realize it's still maybe in flux.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Hi, Wes. This is Yanela. And so, yes, let me start with just kind of reaffirming what we're doing. So, we plan to introduce new intermediate term financial targets beginning for 2025. And really, we're making this change to provide greater insight into our financial outlook and to better align with the longer term nature of our business where the economics emerge over a longer period of time. We also think it will help investors better understand our business outlook and earnings power. So, that is really what we're doing. We will be replacing the quarterly baseline. And again, as we shared, also we will be pre-announcing VII. We plan to implement these changes beginning with the release of the fourth quarter earnings results. So, we will share the targets and the information at that time.

Wes Carmichael
Analyst, Autonomous Research US LP

Q

Okay. Got it. Thanks, Yanela.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

You're welcome.

Wes Carmichael
Analyst, Autonomous Research US LP

Q

My second question, I guess, was on – sorry, was there something else?

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.

A

No, sorry.

Wes Carmichael
Analyst, Autonomous Research US LP

Q

My second question was on the group business. I saw a press release, I think, last quarter that Pru's entering the stop loss business. I guess, just curious how meaningful that could be over time and kind of what that business brings through.

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.

A

Yes, of course, Wes. It's Caroline, and I'll take your question. So, our entry into the medical stop loss builds upon our strategy to diversify our portfolio across both client segments and products. And this move allows us to better serve the evolving needs of our clients by offering a broader range of solutions, particularly, Wes, in the mid-market. As you know, employers frequently purchase medical stop loss in conjunction with other group products, making it attractive from a portfolio perspective and allowing us to leverage our deep customer and our broker relationships.

In the near term, Wes, we plan to take a thoughtful approach to scaling with a disciplined underwriting process and robust reinsurance program with experienced partners. And given the size of our total book, we expect it to be a small portion of our business mix. Our longer-term success will be guided by a disciplined approach to scale. We're committed to sustainable growth and ensuring that our expansion in this area is both strategic and measured.

Wes Carmichael
Analyst, Autonomous Research US LP
Q

Thank you.

Operator: Thank you. [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.
Q

Hey. Good morning. Could you talk a little bit more about the Prismic team, the Prismic Japan team that you're building out and maybe give us some examples of the types of deals that could make sense and the size of the market? Thanks.

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

Wilma, it's Rob. Sure. So, in order for us to be able to effectively do reinsurance transactions in Japan, we need to have an agency licensed business on the ground there dedicated to Prismic. And so, that's what we've put into place in response to what we see as a very large opportunity there. If you think about the discussions we've had even on this call about the US dollar and other foreign currency denominated products that are sold in Japan and had historically been sold in Japan, with the upcoming ESR, so the new economic solvency regime that's going to be adopted in Japan, that solvency regime is really punitive with respect to long-duration liabilities and foreign currency denominated liabilities in very much what we believe to be a non-economic way. And we think that that's going to give rise and be a catalyst to ongoing desire by insurers in that marketplace to continue to meet the customer demand for those products, because Japanese customers continue to have an interest in dollar-denominated products and the returns that they can get on those.

But to be able to square that off with being able to economically finance the reserves and capital against that business in a way that continues to create a compelling economic proposition for the Japanese customer. So, we're actually quite excited about that opportunity. We think the brand and quality and scale of our own business there gives us incredible credibility with the other insurers in that marketplace that would be interested in doing things, as I described before, that would follow a pattern of what we're able to do with our own book from an optimization standpoint.

Wilma Burdis
Analyst, Raymond James & Associates, Inc.
Q

Okay. Thank you. And then my understanding is that there are some tailwinds for UK longevity blocks. Is that something you're seeing? And maybe just talk a little bit about why that market's attractive. Thanks.

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.
A

Yes. Of course, Wilma. It's Caroline and I'll take your question. So in the near term, for our longevity reinsurance, our overall international reinsurance, we remain focused on the US, the UK, and the Netherlands. But what I would say, specifically to your question on the UK, we continue to see very strong funding levels there, actually reaching 113%. And when we look at the market size in the UK, we do expect a size of around $70 billion in pension risk transfer for the year, most of which will seek reinsurance solutions. So, this is why we are pleased that we're not only a leader in this business in the US, but also in UK. And obviously, Wilma, you also saw our expansion last year in the Netherlands. And so, for the time being, those are very much our three areas of focus, and we're pleased to remain a leader.

Wilma Burdis
Analyst, Raymond James & Associates, Inc.

Q

Thank you.

Operator: Thank you. Next question is coming from Alex Scott from Barclays. Your line is now live.

Alex Scott
Analyst, Barclays Capital, Inc.

Q

Hi. Good morning. First one I had for you was on the comments that were made on, I guess, surrenders in foreign currency products being a bit elevated. And it was noted that there was some earnings pressure from that. I wanted to also get a feel for what kind of revenue pressure is that exhibiting on the international franchise, particularly Life Planner?

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

A

So, Alex, it's Andy. I'll take your question, and maybe just let's start by explaining the dynamics to make sure everyone has it clear. So, the weaker yen is leading to an enhanced level of US dollar policy surrenders. That's really kind of flowing from two things. First, on US dollar recurring premium products, affordability has become an issue for customers as it takes more yen to pay the premium. Second, some customers in our US dollar investment products are looking to monetize their gains.

So, with this, they either reduce their level of coverage or they turn the policy in. That obviously has some influence on our sales. But I think the best way to think about this is, had it not been for this surrender experience over this recent period, we would have seen, instead of being flat, low-single-digit earnings growth across our PII business segment. So, it's influencing both, obviously, the premium and the AOI.

Alex Scott
Analyst, Barclays Capital, Inc.

Q

Yeah, that's helpful. And then, I had a follow-up on the potential for reinsurance in Japan and the comments on Prismic. When I think about Pru's business, it very much aligns with what was described in terms of longer duration, a lot of foreign currency denominated in USD, et cetera. If you were to engage in a transaction involving your own business, should we think about that more as like mitigating whatever impact would have been there from the economic solvency regime or does it go further than that? I mean, should we think about it as potentially releasing capital that could be redeployed elsewhere in your business?

Robert Michael Falzon
Vice Chairman, Prudential Financial, Inc.

A

So, let me answer that question. Sorry, it's Rob. Let me answer that question. Let me say more broadly, when we think about reinsurance and whether that be to Prismic or be to sort of other opportunities that we have for reinsurance within our portfolio, we really think about reinsurance as an opportunity to, one, derisk and grow our portfolio. So, financing for growth and – by reinsuring, diversifying against risk. We also think about that as an opportunity for optimizing our back book, and that would be in response to things like you're alluding to, the TSR regime – the economic solvency regime, excuse me, in Japan.

And when we look at the benefits from that reinsurance, we then say, okay, from an economic and business strategy standpoint, what is the optimal outcome for us? So, as we're thinking about that, there are going to be instances where we're looking to do reinsurance or to be able to deliver products to the marketplace with a compelling value proposition. There are going to be other times when we're looking to ensure that we've got an optimization of our own capital against the regimes as they're being modified. And there are other times when we just see a dislocation between how blocks of business are being valued within our franchise in a public basis versus what we see is the opportunity to transact in the private marketplace where they would be valued differently, obviously at a higher valuation and provide, therefore, to our investors, shareholders, a better risk-adjusted return by being able to monetize those.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

And Alex, maybe if I could add specifically to Japan and our business and ESR, I did share in the first quarter that we reinsured $3 billion of US dollar-denominated whole life products from Japan to our Bermuda affiliate, Gibraltar Re. And in the second quarter, we executed a transaction for US dollar new business from Gibraltar to PICA. So, definitely is a tool that will help us stabilize capital in all of our operating entities, including in Japan.

Alex Scott
Analyst, Barclays Capital, Inc.
Q

Thank you.

Operator: Thank you. Our next question is a follow up from Wes Carmichael from Autonomous. Your line is now live.

Wes Carmichael
Analyst, Autonomous Research US LP
Q

Hey, thanks for taking the follow-up. I guess I just really wanted to follow up on this particular topic on ESR, and Rob, your comments that this regime is punitive and perhaps uneconomic for long-duration liabilities. I guess, I think about – I understand that you have levers for reinsurance for your own book, but is this transition to ESR, like is this ex-reinsurance, like would this be somewhat problematic in terms of Pru needing to capitalize the business to a greater degree or something? I'm just trying to understand the issue that maybe you and both Japanese insurers are facing here.

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

Yeah. No, Wes, it's – you want to start, Yanela, and then I'll add in?

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Yeah, Wes, let me start in terms of the impact to our capital position. So, I'll reiterate that we believe our Japan businesses are well capitalized and financially strong. And that strength would be reflected under any reasonable capital standard, including the new ESR framework. Like, as we mentioned, we have tools like reinsurance, we have transacted in a couple blocks of business, but we expect that upon implementation of our capital levels, we'll continue to be above target levels that would support a AA financial strength ratings in Japan.

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

Yeah, Wes. And it's Andy. I was just going to add, we've managed changing capital regimes at Prudential over a very long period of time. In Japan, we have a very broad product portfolio that meets the needs of our customers. We've continued to innovate and expand that portfolio, including with ESR friendly type products. So, the bottom line is, as a management team, between the product capabilities combined with our strong underwriting, our ALM capabilities, hedging and reinsurance, we believe we have everything we need to continue to profitably grow in Japan and navigate these changes.

Wes Carmichael
Analyst, Autonomous Research US LP
Q

Got it. That's all very helpful. And I guess, my follow-up would be, just any help with the outlook for the pension risk transfer market into the fourth quarter? I know the third quarter was a big one with IBM. But as you look to this quarter and maybe even to 2025, any thoughts there?

Caroline A. Feeney
Executive Vice President & Head-US Businesses, Prudential Financial, Inc.
A

Yes, of course, Wes. It's Caroline, and I'll take that one. So with over $16 billion and a 40% market share in PRT sales this year, clearly we're continuing to demonstrate our strong market leadership. And as we look forward to 2025, we continue to view the US PRT market as highly attractive, with $3 trillion in outstanding US corporate pension liabilities, favorable funding positions and a robust long-term pipeline of opportunities. And while the market remains highly competitive, we believe we are uniquely positioned to execute. Of course, our scale, our depth of underwriting experience as well as our ability to originate attractive assets enable us to price competitively, while generating attractive returns for our shareholders.

We also deliver deep expertise, have a demonstrated ability to handle complex deals and provide industry-leading service. And, Wes, we believe that combination is evident in our sales this year, where over half of our transactions have been with existing clients. And those traits are exactly why Prudential remains one of the few companies to have successfully executed transactions over $1 billion and why we continue to feel very confident about our go-forward business.

Wes Carmichael
Analyst, Autonomous Research US LP
Q

Great. Thank you.

Operator: Thank you. [Operator Instructions] Our next question is a follow-up from Tom Gallagher from Evercore ISI. Your line is now live.

Thomas Gallagher
Analyst, Evercore ISI
Q

Thanks. Yanela, just would you mind reiterating what you said you're going to change to quarterly disclosure? Did you say you were going to eliminate the quarterly bridge that you typically provide on the next quarter out? And I think I heard you say you were going to start pre-announcing alternatives. Any other changes you're planning on making. Thanks.

Yanela del Carmen Frias
Chief Financial Officer & Executive Vice President, Prudential Financial, Inc.
A

Yes, Tom. So, we are eliminating the quarterly baseline disclosure. And we're replacing that with intermediate term financial targets, starting with 2025, and pre-announcing variable investment income. Those are the two key changes we're making. We are still going to speak to unique items in the quarter, really to help you understand what's happening. But that's the extent of the changes.

Thomas Gallagher
Analyst, Evercore ISI
Q

Okay. Thank you.

Operator: Thank you. Our next question is a follow-up from Suneet Kamath from Jefferies. Your line is now live.

Suneet Kamath
Analyst, Jefferies LLC
Q

Hi. Thanks. I just wanted to circle back on this concept of doing a back-book deal with Prismic. I just want to make sure I'm thinking about it right. So if you were to do a deal with a block of business from Japan, is it fair to say that there might be some initial EPS pressure because you're giving up some of the earnings that you're now – you own 100% of it, and obviously you'll give up some of those earnings to your Prismic partners. Presumably, you'll free up some capital, which you can then deploy in new business. But there might be a little bit of a lag between when you lose the earnings on the back-book versus when you deploy the capital that's being freed. Is that the right way to think about it, or is there some sort of offset that I'm missing there?

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

No, Suneet, I think you've – I'm sorry. It's Rob. I think you've captured it well, which is that's not unique to doing the back-book deal in Japan, that you could use that same description and apply it to each of the reinsurance transactions that we've done to-date, which is that, by virtue of reinsuring, we unlock capital and embedded value. And in Japan, in particular, we think that our products there have very high levels of margins in the reserves that we have. And so, we're able to release those reserves and capital associated with it. By virtue of reinsuring, then the AOI associated with that block will no longer appear on our earnings. However, our analysis looks at what the economics of that translate into with the freed-up capital and our ability to redeploy that capital.

Suneet Kamath
Analyst, Jefferies LLC
Q

And does PGIM manage all of the assets that back the Japanese liabilities already? Or is there a portion of assets that they don't manage that if it went into Prismic, it would start to earn fees on?

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

The assets that we have within our business today are – the vast, vast majority of them are managed by PGIM. There's a selective – a couple of instances where we do have some third-party managers in specific areas that PGIM is not focused on. But I would say, by and large, it would be accurate to characterize that those liabilities – excuse me, those assets that are backing the liabilities are being managed by PGIM today. When they transferred into Prismic, they would be managed – continue to be managed by PGIM, but on sort of a third-party set of economics as opposed to the economic range that we have with the general account, and that generally is accretive to PGIM.

Suneet Kamath
Analyst, Jefferies LLC

Q

Got it. Okay. Thanks.

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, and thank you again for joining us today. We've entered the last quarter of this year pleased with the progress we've made to become a higher growth and more capital efficient company. We are well positioned to address the growing needs of our customers and clients around the world as they seek to protect their life's work and live better lives longer.

So, thank you again, and enjoy the rest of the 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.