# 2020 KBW Insurance Conference

## Company Participants

- Robert Falzon, Vice Chair
- Ryan Krueger, Analyst

## Presentation

### Ryan Krueger {BIO 15132646 <GO>}

Good morning, everyone. It's Ryan Krueger from KBW.

Really pleased to have Prudential Financial with us at the conference virtually this year.

With me is Rob Falzon, who is Vice Chairman. Previously to that, Rob was the CFO for several years. And prior to that, he was Treasurer.

Rob, I wanted to kick it to you just to provide some opening remarks. Then we'll get into the Q&A.

### Robert Falzon {BIO 4770408 <GO>}

Great. Thanks, Ryan, and thank you, everyone, for participating today.

I thought what I would do is, I know, Ryan, you're going to want to cover a number of topics.

But I thought I'd just share a couple of reflections that I have on the current environment -- and three specifically that I just wanted to sort of share with everyone.

The first is that while we're finding ourselves in a challenging sort of macroeconomic environment, so the pandemic, the recession that's been caused by the pandemic, the associated impacts on the credit cycle and noninterest rates, I'd like to remind people that this is what we were built for. This is actually what we planned for.

We have a whole series of playbooks that we've devised after the Great Recession and that would anticipate a range of things that could happen, both from a pandemic and from a recession standpoint, and range of things that are far worse than what we're experiencing.

The intent is to continue to be resilient through that and we have been.

We feel really good about how well we're capitalized.

We feel really good about the quality of the portfolio.

We feel really good about our operational integrity and how we've been able to continue to have a good experience for our employees and for our customers throughout this period of time. Having said that, I think to the extent we have a concern, the concern is actually about customers.

What's been exposed during the course of this experience in this relatively short period of time is just how fragile the economic and their own financial resiliency is for many Americans and even outside of our own country. And for that, we're particularly concerned. They're unprepared for disruptions and dislocations.

So they don't have enough savings for those sort of things. They are unprepared for retirement.

In many instances, now actually dipping into some of that retirement savings in order to be able to support themselves in current times. And many are woefully underinsured from a life standpoint. The -- I don't want to call the silver lining, but the -- from our standpoint and from an industry standpoint, the opportunity that, that creates is the level of awareness about the benefits of what we do about -- we are in fact able to do, are all the more present and visible to our customer base.

So as we look at this, we look at this as the opportunity to execute on what we're talking about before, which is expanding our adjustable market by providing more customers with more products and services going across the entire socioeconomic spectrum and not just being focused on sort of the very high net worth that the -- that we and many of the industry are -- have been particularly focused on.

So that's kind of my first and second observation.

With regard to that second piece, I think we view ourselves as being very well positioned to execute against the opportunity that's in front of us.

We think to do that well it really requires that you think differently about distribution, you think differently about product, and you think differently about your cost structure. From a distribution standpoint, I'd like to use the phrase, sort of, omni. Distribution is not about multichannel, distribution is actually around omni-distribution that's having a complete continuum that goes from digital to fully advised and with hybrid type experiences that fall in between that. From a product standpoint, as you go deeper into the market, it requires that you pivot to things that are, frankly, more simple, so less complex products that meet the needs of that expanded marketplace and sort of then, segueing into the third component of that, cost efficiency, you also need to be priced appropriately for that marketplace.

So that means that we need to think about our cost structure in a way that continues to make us competitive in the marketplace and allows us to mitigate some of the impacts that are occurring as a result of the low rates and the headwinds that, that creates to our own profitability.

I think the third and last thing I'd share about the current environment is that as a result of what we're all going through, we've seen this really sort of quantum acceleration.

We know we used to label the future work and the future of the workplace. And for us, that's meant sort of a much more rapid adoption of technology and the digitization of the experience for the customer. It's been helped because in a crisis, regulators removed some of the impediments to our ability to do that.

So that's been helpful. But we removed some of our own impediments to do that. And as we were looking at how do we meet surging demand at our call centers and other -- and for -- and claims and other types of inquiries coming in, digitizing that experience and creating chats and online resources for people as opposed to their need to speak to directly to wait on the phone on hold to speak to a human, there's been a massive acceleration in that and a good experience for our customers as a result as well.

That's gone through the entire food chain.

So it's about creating that experience everywhere from underwriting through claims payment. That has, from our own standpoint, not only accelerated our ability to execute on the customer experience and efficiency initiatives that we had already outlined at the beginning of last year, but it's also part of what's allowed us to think more expansively about that as we've institutionalized that capability, thinking about how we can go further in terms of creating those kind of experiences for our customers and enhancing the margins associated with our businesses.

So three observations, just kind of where we are in the environment.

I think that while a challenging environment, we feel as if we're extremely well capitalized and positioned from a portfolio and operational standpoint.

We have a set of initiatives that we're very much focused on that I think are well aligned with serving the needs of customers as they've experienced this, both pandemic and economic scenario that we've been under.

We also think that the initiatives that we're doing around our efficiencies will position us to be able to execute on that and improve the profitability of the firm for our investors.

So thanks for the opportunity to do that, Ryan.

I'll turn it over to your questions.

## Questions And Answers

### A - Ryan Krueger {BIO 15132646 <GO>}

Thanks, Rob.

Some of my questions will build off of those opening comments. To start, it's been almost two years now since you became Vice Chairman and Charlie Lowrey became CEO, and Prudential's strategy has evolved some during that time. Can you discuss some of the key changes that you've made as well as the reasons for doing so?

### A - Robert Falzon {BIO 4770408 <GO>}

Yes.

So that really gets to sort of the pivot we made, I think in the Second Quarter from the First Quarter, around the narrative in the First Quarter being very much around resiliency and all the things I talked about, and the Second Quarter really being around how are we going to enhance shareholder value and returns to our shareholders.

I think there were three things that we identified as sort of the priorities that we had, that were impacted by the economic environment we find ourselves in. You go back to beginning of 2019, when Charlie and I kind of stepped into our positions, the interest rates have declined around 200 basis points on the 10-year over that period of time.

So it's breathtaking in a way.

So as we think about how do we deal with a low interest rate environment and what are the opportunities in front of us and how we execute against that. The first thing that we really were focused on is that we need to improve the quality of our earnings is how I kind of like to describe it.

So from a quality standpoint, what that means is that you have a less interest rate and market sensitivity in our businesses and that those underlying businesses, producers had financial outcomes that are more consistent and predictable.

We think if we're able to do that, that leads to a reduction on our cost of capital or extension in our multiple, sort of think about it that way.

So we've used the phrase in the Second Quarter of simplifying and derisking, and that's sort of what that was meant to capture.

The second pieces have been around, our focus has been, okay, improved quality of earnings, now improve the profitability of our businesses. And from a profitability standpoint, that gets very much around the initiatives that we announced in 2019, the $700 million of investments we're making in order to generate $0.5 billion of margin enhancement. And as we talked about in the Second Quarter, and I mentioned earlier, the ability to, we think expand on that as we've institutionalized that capability in our firm, we see sort of more opportunities.

So that's sort of our second focus, get quality of earnings up, get margins up and then growth.

I think growth will come about by virtue of what we're doing from the profitability, obviously but from a longer-term growth standpoint, it's really very much about the expanded addressable markets that we see for each of our businesses.

To the extent, like, we can talk about those but both in our investment management business, international business and in our U.S. businesses, we see an opportunity to accelerate our growth by expanding the number of individuals that we can serve.

The -- probably the other thing that doesn't get noticed enough, I guess the thing I'd like to say that we spend a lot of time on is our leadership team.

We have -- since we've taken the reins, we've -- most of our -- the leadership of most of our U.S. businesses have changed over that period of time.

So we've had succession planning that have put in place the leaders for those businesses.

We stood up a transformation office.

We took one of our most successful business leaders and put that person in charge of that capability, that's leading to our ability to have accelerated the execution of the $0.5 billion of benefits and to think about how we can do that more expansively.

We hired a new Chief Information and Technology Officer, Stacey Goodman, a little over a year ago.

Significantly redesigned our technology organization, pivoting it away from sort of the traditional focus on maintenance and operations and toward business enablement and development applications. And under Stacey, if you look at the 10 next most senior leaders there, half of those individuals are new to position from outside the company.

In fact, from outside the industry.

So a big investment from a technology standpoint. That's been helpful to what we're already accomplishing on our initiatives and we think will be additive to that on a go-forward basis as well.

Then we've selectively -- we put a new Head of Strategy in place and other selective hiring.

So we spent a fair amount of time on our leadership as well.

We think all of that is paying dividends.

And if you just give me one more minute, Ryan, just sort of a couple of things that I want to tick off.

So if I think about -- if I just sort of think about PGIM international, our U.S. businesses, from PGIM's standpoint, the company had a record level of AUM in the Second Quarter. Positive flows in that quarter, strong flows from a retail standpoint, number one, mutual fund flows to retail in the first half of the year. But also institutional has been strong as well as, it gets masked because we had a single large client in the Second Quarter. That was an indexed low fee, so not very significant from a revenue standpoint, exit out, but otherwise had good institutional flows.

So performance continues to be good there. Flows continue to be good.

We continue to build and invest in our international capability, our retail capability and our alternatives capability, those are the levers for growth within that business and we've done something on relatively recently in all three of those areas that are helping to produce the kind of results that you're seeing within PGIM.

From an international standpoint, we've talked about the way which we want to expand our addressable market there is, in Japan we have a phenomenal franchise. It continues to grow faster than the overall market does.

We see an opportunity to capitalize on that franchise by providing more products into that marketplace than the traditional protection -- life protection-type products that we sold.

So we can -- as that demographic ages, meeting the new needs of that aged demographic through our existing distribution, which is incredibly strong.

Outside of Japan, we wanted to do a major pivot to say, okay, we're going to have -- if we're going to have a big play to develop market in the U.S. and in Japan, we want to have more of an exposure to emerging markets outside of that.

So what you've seen is we've exited out of Italy, we exited out of Poland, we exited out of Korea, we've announced the sale of our business in Taiwan as well.

So those more mature markets we've exited out of. And pretty much below the radar, but not uninteresting, we've expanded what we're doing in Brazil.

We had done the Group acquisition a little while back, but more recently, we did a bancassurance agreement in order to expand on our very, very strong Life Planner platform that we have in Brazil. In our Afore in Chile, we've done acquisitions through that business, most recently in Colombia, we're trying to create sort of a pan-LatAm for a capability out of that business, a small expansion in our Africa presence.

So building in -- exiting out of the things that are slower growth and more developed and selectively looking to build on where we have an existing presence in emerging markets that give a growth to your -- sort of complexion to our international business.

Then finally, from the U.S. business standpoint, a number of things there.

We continue to execute well on the Financial Wellness platform in the workplace. We've talked about that, that's a longer-term growth strategy for us. But we think important to our competitiveness in that space on a direct basis, institutional competitiveness, but then also the ability to get to the underlying employee and provide more solutions to them to grow our business. We've been -- we bought the Assurance business at the end of last year, which has added to our -- that distribution capability that I spoke to.

So a big presence in digital and then they do hybrid as well. Distribution, so we feel as if we've got now a leading-edge capability on the digital side. And an ability to provide more products on sort of a pure distribution brokerage standpoint into our customer base.

And then as I mentioned, the success that we've had in accelerating both the costs associated with our initiatives.

So through the middle of this year, we've already incurred $450 million of the $700 million that we said would be needed in order to generate the $0.5 billion worth of economies.

We disclosed at the end of last year that we expected to be able to accelerate also the realization of those operating margin improvements from what we're talking about as well.

Our performance in the Second Quarter, I think kind of reaffirms our ability to do that.

Then looking, as I said, to see how we might be able to expand on that in the future.

So those are the things that are our priorities, and that's the progress, I think we're actually making against those priorities.

## A - Ryan Krueger {BIO 15132646 <GO>}

Thanks.

On the cost saves, as you talked about, you have this $500 million plan for -- by 2022, but you've also talked about the potential to do more. Can you just discuss where you see additional opportunities?

And then also when you anticipate that you might quantify the potential there?

## A - Robert Falzon {BIO 4770408 <GO>}

Yes.

So we'll be pulling -- so first, in terms of where we are.

I think in the first half of the year, in period we realized $75 million of in-period savings.

We -- the number we put out there was expectation of $140 million for the full period.

So we were sort of ahead of pace on that. Expectation would be that we would get to a run rate by the end of the year of somewhere between $250 million and $300 million, and then the $0.5 billion number by the end of 2022.

So the run rate benefit in -- as of the end of the Second Quarter, trying to think of I don't know -- let me not go by memory because I'm not sure what the number is, but it's well on the way to the objective for the full year.

So we feel good about where we are both in terms of in-period savings and our run rate.

As we look to expand on that, I think the single most important thing I'd point out is what I mentioned when we talked about -- when I talked about leadership, is that we've actually institutionalized this capability.

So we set up a transformation unit office.

We took one of our strongest business leaders out of position to put them in charge of that capability.

We're obviously working with consultants and bringing them in as well but we've staffed that.

Their task has been to not only look at the acceleration and execution of what we had in pipeline, but to look across our businesses and opportunities to go further.

I think as we think about that, we think within our existing businesses using the existing levers we have.

So it's the classic set of levers you have around automation, digitization, use of technology, location strategies including outsourcing, process redesign, all those sorts of things, organizational redesign. And continue to use those tools and just sort of push them further in areas where we've already focused, which has been primarily around sort of our U.S. business and functions.

While we had included both our investment management and international and some look at that, the reality is we have a lot more opportunity, both in investment management and in international, when -- vis-à-vis the very robust process we went through with our U.S. businesses and functions.

So we think there's more opportunity there to take the same set of tools and apply them across our entire business complex.

So more broadly than we did before. The other thing I'd mention is, I think we've just scratched the surface on technology. With the new team installed, most of which were put into place this year, maybe end of last year, the -- we've only begun to scratch the surface on what we think are the availabilities there, particularly from an infrastructure standpoint and how we think about the spend that we have there, and can use it not only to produce better outcomes but produce better outcomes at a lower cost.

## A - Ryan Krueger {BIO 15132646 <GO>}

Thanks.

On the Second Quarter call, you had also discussed potential in force derisking actions for variable annuities and universal life with secondary guarantees. A couple of questions there. I guess, one, just what led to that decision?

Then secondly, when you're considering reinsurance transactions, how do you balance the -- I guess, potential outcomes that differ from your view of the economic value of those businesses, but do achieve the desired derisking impact that you're looking for?

## A - Robert Falzon {BIO 4770408 <GO>}

Yes.

So I'd say, Ryan, we talked about the products pivoting that we're doing and repricing that we're doing that -- think about that as really just the first step in this broader issue of simplifying and derisking.

So stepping back from HDI and from single life GUL and looking at things like FlexGuard annuities as products that have significantly less market sensitivity. And also associated with that, more predictable and system financial outcomes, both on an AOI and a GAAP basis because we're sensitive to both those metrics. The -- as we've thought about that, I think the -- sort of related to what I spoke about earlier, we are -- we believe that if we can reduce the market sensitivity of our business, and in conjunction with doing that, improve the consistency and predictability of financial results that, that will have a very direct impact on our multiple, on our valuation.

I think that there are certain product lines that we have, and I think HDI would be maybe a poster child for that, to be completely frank about it, where we think the economics are actually incredibly compelling. It's a very high ROE business. It has good cash flow that's associated with it. It's extremely well capitalized and it's well hedged.

Having said that, the market's perception of that business -- the public market valuation of that business is not synced up with what we would think would be our own valuation or a private valuation for that business.

We try to be more transparent to try to get that sinking to occur. But it's not.

I think there's a reality of -- even with all that hedging and good outcomes, the reality is it does have some market sensitivity associated with it, and does have some accounting volatility that's associated with it, sort of below the line or outside of AOI.

Those become, from a valuation standpoint, I think headwinds from our overall value.

The challenge we face is that it seems that it's not just applied to that sleeve of the business, but rather to the totality of our businesses, when you sort of look at the valuation of the company in total, it seems to be overly influenced by the variable annuity component of our business.

So we've recognized that this isn't just a matter of transparency, this is just a matter of valuation differentials that exist in the marketplace, and we need to be responsive to that.

So from our standpoint, that was sort of part of the catalyst of recognizing that overall and then using HDI as a very specific example of that. How we can improve valuation by being more thoughtful about. How we continue to -- we can continue to serve the needs of consumers around life protection and around retirement protection, but do it in a way which where -- has less market sensitivity and more predictable and consistent financial outcomes associated with it.

So those were kind of the catalysts that were associated with it.

In terms of how we think about it, obviously we've already taken actions on the new business side.

We have blocks of those business, which will continue to generate earnings.

When we look at that, we have the option of just running them down and harvesting the cash that's coming off those, and that's one viable option. But we are and will continue to look at other alternatives that can range from selling pieces of those business or reinsuring pieces of those business to getting rid of entire blocks, either through reinsurance or sale as a way to sort of accelerate that transformation.

We'll be economic about it. We'll look at the trade-offs to value in the market that we can achieve today or at other points in time against what we think the implication of that would be on the valuation of the stock in the marketplace and hopefully make an execution there that optimizes the outcome for our shareholders.

## A - Ryan Krueger {BIO 15132646 <GO>}

Thank you. I guess on -- I think it was exactly a year ago, it was actually at our -- the same day of our conference last year, you announced the acquisition of Assurance IQ, which is an insurtech distribution platform for those unfamiliar. They got off to a bit of a slower start than expected, but how are things progressing now?

And to what extent are you, I guess, more broadly integrating it into Prudential?

## A - Robert Falzon {BIO 4770408 <GO>}

Yes.

So if I think about Assurance IQ, first, it is a proven model for digital distribution.

That was what was very attractive to us about that. They kind of cracked the code on digital distribution linked with this sort of hybrid adviser capability and was actually quite -- has been quite successful in a relatively short period of time as an insurgent.

That capability, we thought would leapfrog others in the marketplace from the standpoint of us having that capability.

So we continue to be quite enthusiastic about it strategically from that standpoint. We've talked about the Fourth Quarter of last year. The Fourth Quarter of last year was -- I think about it as a bottleneck issue for us. The good news for us is that the fundamental indicators of the strength of that platform continue to be quite good. The shoppers to the site continue to grow at double digits.

The demand by insurers to get on to the platform continues to be really strong as well.

So you sort of think about, you just need to make sure that we have the operational capability to close that gap, and we had a couple of hiccups in the Fourth Quarter that Andy and team have been addressing with the Assurance team to make sure that we're well positioned for the Fourth Quarter of this year, when you've got the big driver being the Medicaid -- Medicare enrollment period.

So we feel really good about drivers to the business and about having that capability in terms of making us more successful at providing a broad range of products, not all of which we want to provide, we'd rather take health solutions and P&C solutions from other providers, we don't want to get into that business, but they're important solutions for the customers that we're serving, and so to be able to do that on a third-party through a distribution or brokerage arrangement is actually quite attractive to us.

With regard to our own products, we put our simply life term product on their platform, which was actually transformational for both them and for us, transformation being significant, it hasn't transformed anything yet, but it's been -- it was a significant milestone, I guess I should say, for both of us. The fact that we were able to do that actually well ahead of schedule speaks to sort of the rate at which we're learning to adapt to the new world and pivot and change. And from their standpoint, having our brand and our product on their platform significantly enhances the pull-through of that life product to their customer base vis-à-vis the other life products that they have on the platform already.

So good mutual outcome there.

We think we're licensed in, I think 49 states at this point in time, we'll be licensed across all states by end of this year, beginning of next year.

So we're pretty close to that if we're not there already.

So we feel good, again about having gotten that capability in place. From a financial standpoint, it will be a Fourth Quarter story, and we'll be prepared to talk about that when we get into the Fourth Quarter.

## A - Ryan Krueger {BIO 15132646 <GO>}

Got it. What's your level of interest in additional M&A at this point?

And are -- I guess, what areas would you view as most compelling?

## A - Robert Falzon {BIO 4770408 <GO>}

I think about our M&A, I describe it as being programmatic M&A, meaning that it's really about where we can do it on an incremental basis to lever existing strong capabilities that we have.

So think about that in the PGIM context, I talked about retail, international and alternatives being areas of growth and focus for us.

So what we've been doing are making small, what I call, bolt-on acquisitions -- often not just look like team lift-outs, they're acquisitions, but they look more like team lift-outs to add to our multi-manager model.

We did that with the Wadhwani acquisition, which was a U.K.-based futures manager, a year plus ago or so.

Those are the kind of things that we're looking to do is continue to build those kind of capabilities on sort of an incremental basis. By bringing those small shops on, we can get great economies from that.

So it's a way in which -- for us to continue to grow flows and maintain profitability.

Without -- we obviously [ph] see multiple concerns when you're doing those kind of acquisitions and if you're doing a large asset management acquisition, by way of example.

The second area would be in international, and that's leveraging our emerging market presence that we already have.

So of both Chile and Afore platform and the Brazilian life platform being perfect examples of that, where what we've done is taken a strong capability, but frankly, not large enough yet that it's changing the complexion of PFI, so we want to grow it and think about how do we leverage that capability in that market by growing our footprint.

So in Brazil, we built over the course of a decade and half, a really strong proprietary distribution capability, life planner model, similar to what we have in Japan. Number one, sort of non-bank life seller now in Japan.

Then we added to that a Group capability and then bancassurance, and we have other third-party distribution now as well.

So building multi-distribution capability in a market in which we have a strong brand and good success.

The same thing with the Afore business we have, it's quite successful. We're sort of the leading Afore in each of the markets in which we're serving.

We want to continue to build on that, and that could involve selective acquisition.

Now having said all of that, I would say, Ryan, there's a high hurdle to any M&A that we would do. And hence, these sort of things are small, where we can get very good economics by leveraging existing capabilities and platforms.

As we think about deployment of capital, given where our -- particularly where our share price is these days, buybacks create a very compelling alternative to doing M&A, and we're very conscious of that to the extent that we're looking at M&A at any point in time.

When and as we get to the point where we're ready to take a look at our capital capacity and feel as if we've got enough visibility on recovery that we want to redeploy that capacity, we would think about how we redeploy that cognizant of the very attractive economics that will be associated with buybacks at this point in time.

## A - Ryan Krueger {BIO 15132646 <GO>}

Can you delve into that a little bit more?

You have a good capital position. The Korea sale has now closed.

So I guess how are you thinking about the key indicators that would get you comfortable resuming buybacks?

## A - Robert Falzon {BIO 4770408 <GO>}

So I'd sort of dial back and look at the same set of indicators that caused us to put it on pause. Now since we're going into the pandemic, we're anticipating what the recession might look like and what specifically the credit cycle associated with that recession might look like.

That said, okay, we should, at this point in time, be conservative, maintain flexibility and sit on our capital position. And as you noted, we still have -- we have $4.5 billion worth of highly liquid assets, cash.

Then at the end of the Second Quarter, and then we received about $1.7 billion, I think on the sale of Korea relatively recently as well.

So we do have a very strong capital and liquid position. But we'd be looking at that same dashboard set of metrics that caused us to put it on pause to take our finger off the pause button, where I think the observation would be that the recession, specifically, again the credit cycle has been relatively benign to date. The -- if you looked at the framework that we laid out in the First Quarter and you compared actual experience against that framework, it's been very benign, a relatively modest credit cycle. Now that -- we're not necessarily convinced that, that means that the credit cycle will remain benign during the entire recession.

So we're keeping our eye on that.

So while there's a host of metrics that are on our dashboard, probably the one that's largest and in the center of that dashboard is credit.

We're looking at things around ratios of upgrades and downgrades and trends in that indicators around the financial health of corporate America. And as indicators as to when we think we'll either be through the cycle or that, in fact, the cycle is not going to manifest itself as being as severe as we might otherwise think it might be -- would be indicated by history and the framework that we laid out in the First Quarter.

So as we think about, Ryan, restarting, I've said in the past that we don't want to start and stop. If we begin, we want to begin so that we can do it programmatically and with conviction.

That means we're going to be cautious to ensure that we're very comfortable that we've seen the worst of the credit cycle.

Then depending on how severe that's been, we'll define how much excess capital we have. If it's this benign, we'll have a fair amount of excess capital. If it turns out to be more severe, we'll need some of that capital in order to respond to the impairments that will happen in a more severe credit cycle.

Then what's left after that would be what we really think about redeploying.

## A - Ryan Krueger {BIO 15132646 <GO>}

Got it. At your 2019 Investor Day, you guided to a 12% to 14% intermediate term ROE obviously have had a significant change in the environment. Since then, as you think about that now, do you still think the lower end of that range is achievable in the current interest rate environment?

Or how are you viewing the return profile of the company?

## A - Robert Falzon {BIO 4770408 <GO>}

Yes.

I think the walk-through that we provide now quarterly, which I think is very helpful to the market.

I think probably the best way I can go about answering that, Ryan.

So in that walk through, the baseline -- so we do adjustments that take sort of the results in the current quarter and try to give you an idea, if you remove some of the unusual stuff, so we did the Second Quarter assumption update.

Then we had the COVID experience both from a mortality standpoint, although it's positive in the Second Quarter, we're removing that experience and the costs associated with that in the customer and efficiency initiatives. Then you get to a number that was our baseline for the beginning of the Third Quarter, that was around $2.85 a share.

Then with respect to that number, I think is actually -- actually, I think it was like closer to $2.90, but we assumed some level of ongoing initiative spending and that gets you down to $2.85.

So if you take that $2.85, and you adjust that, it doesn't reflect the seasonality in our expenses. We've talked about that number.

So we've said that our -- in the Fourth Quarter, we have elevated expenses that generally ranged $125 million and $175 million.

So you have to adjust the number for -- it doesn't reflect the seasonality of expenses, the biggest one being that in the Fourth Quarter.

Then you'd have to adjust that for the -- with the guidance we've given around the headwinds associated with interest rates, the $0.03 per quarter compounding against some opportunity for business growth and the savings that are coming about by virtue of the initiatives now, we've incurred $450 million of the $700 million of initiatives we were to spend.

So that number is coming down fairly rapidly as the run rate benefit of those is climbing fairly rapidly.

I think in next year, you see there's actually a crossover in that where the benefits, the in-year benefits exceed the in-year expenses as contrasted to what we've experienced last year and this year.

So the -- I think that if you do that math, I think that depending on your own view of what market growth opportunities are out there, probably get you to a view of what the ROE -- near-term ROE potential of the company might be.

In the longer term, we'll be -- have to look sort of through this recession through COVID and then how well we can execute against the -- on the broader growth objectives that we have.

## A - Ryan Krueger {BIO 15132646 <GO>}

Got it. All right, there, look, I guess, two questions. What's -- do you think that the GAAP accounting changes that are coming, I guess, now in 2023 will actually change how you operate the business at all?

And then somewhat related to that, are there any other regulatory issues that you're paying particularly close attention to at this point?

## A - Robert Falzon {BIO 4770408 <GO>}

The -- so targeted improvements will -- it's gotten delayed.

There's a discussion around advanced adoption.

We haven't decided yet, Ryan, whether we're going to advance adopt it yet.

So that's kind of still out there. I'm not anticipating that we have necessarily changed -- any changes from what we've already talked about as a result of targeted improvements.

I think the interest rate and market sensitivity that we're already looking to reduce will be further exacerbated under targeted improvements, but that's something we've already talked about doing.

So I don't -- targeted improvements in and of itself is not a catalyst to, I think further change in how we're thinking about our business mix.

I think there's some real benefits that will come out of targeted improvements. We're going to have to deal with the DAC unlocking. It will just be sort of smooth, just be locked in and amortized out. You have -- having a mark-to-market on both the asset and the liability side, I think there's a benefit to that. Instead of just having AOCI one side and then people sort of guessing about what's happening.

We saw that in the crisis, which is assets getting marked down. There was no corresponding mark on the liability.

So that was creating a little bit of a panic. The -- and so I think having symmetry on that is actually beneficial. Incidentally, from a very parochial standpoint, I think it's really great that everyone's got to do the same accounting on annuities. We've always had this market accounting that we've been sort of alone in that and so everyone will be switching over to that, it'll make the results on that, I think a little bit more comparable.

The -- so I think those were good outcomes from it. It will introduce more volatility in the way that FASB has chosen to introduce this, and some of that volatility will be counterintuitive.

That's a frustration.

We tried to -- the industry tried to -- and people that are on this phone may have been part of that effort, tried to get FASB to think very differently about how they were going to do this, this idea of retrospective versus prospective in order to match up better with cash flows. They chose not to do that.

I think that's a shortcoming.

I think the industry is continuing to dialogue on how do we at least figure out as an industry to provide supplemental information that may help to at least get through that volatility on a consistent basis between companies.

So that's something I know our CFO and other CFOs are working on.

So I don't -- that's the first part of your question, I've wandered on so much that I -- sure I remember the second part of your question, that was targeted -- what was the second part, Ryan, I apologize?



## A - Ryan Krueger {BIO 15132646 <GO>}

I said are there any other key regulatory developments there –

## A - Robert Falzon {BIO 4770408 <GO>}

Oh, key regulatory. Yes, from a capital standpoint, there's a bunch of stuff that's going on, nothing that's particularly problematic for us. They're looking at the C1 charges, so the credit charges.

We don't think they have quite -- that quite right. They're still working on it. But there's nothing there that would cause us to invest differently than we're currently investing, although, we do think it rewards bad behavior in a marginal way that we'd rather not see be there. The VA accounting that they're rolling out is something we adopted a number of years ago, with both New Jersey and Arizona, our regulators.

So while the details of that are always sort of a little different, by and large, that's a construct that we have in place, and we're well capitalized under that construct.

Then there are change around the capital construct using discount rates around fixed annuity, so the PRT, pension risk transfer, business will be affected by that. But again we've already adopted that. That was something we struck with our regulators that we would account for using those current interest rates several years ago.

So that's not new accounting for us.

So while there are a number of initiatives going on there, and we're paying attention to all of them and highly engaged, there's nothing that we find that would be disruptive or would change our own -- the way we think about executing against our business. We're also paying a lot of attention to what's happening on a holding company in systemic basis, and we're highly engaged in that, both here in the U.S. and abroad.

I think for us, Ryan, probably the things we're paying more attention to are the things that are sort of across the economy.

So the two things I'd probably point out would be initiatives around retirement.

So we had the SECURE Act, and there's work being done on SECURE 2.0, and we're putting an ore in on that.

I think that will be net beneficial to consumers and to the industry.

We're looking at consumer connection stuff. That's everything from the DOL rules and the SEC rules to privacy issues to make sure that, that gets done in a proper way as well which is mainly around sort of the administration of whatever comes out of those regulations. Those are areas we're paying more attention to than anything that might be specifically happening from an insurance standpoint.

## A - Ryan Krueger {BIO 15132646 <GO>}

Got it. Well I think we are, unfortunately, out of time.

So I really appreciate you participating again this year.

I don't know if you want to make any closing comments. But otherwise, we'd kind of wrap it up.

## A - Robert Falzon {BIO 4770408 <GO>}

No, I thank to everyone for their interest and support. Ryan, thanks for the opportunity to do this. And look forward to our ongoing engagement and talking to everyone in the -- when we come up with the Third Quarter results.

## A - Ryan Krueger {BIO 15132646 <GO>}

Great. Thank you.

## A - Robert Falzon {BIO 4770408 <GO>}

Okay. Bye now.