



Prudential Financial (PRU)

Updated August 1st, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$93	5 Year CAGR Estimate:	10.8%	Volatility Percentile:	54.9%
Fair Value Price:	\$105	5 Year Growth Estimate:	4.0%	Momentum Percentile:	35.0%
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.5%	Growth Percentile:	25.6%
Dividend Yield:	4.3%	5 Year Price Target	\$128	Valuation Percentile:	76.2%
Dividend Risk Score:	D	Retirement Suitability Score:	C	Total Return Percentile:	66.4%

Overview & Current Events

Prudential Financial, now in business for over 140 years, operates in the United States, Asia, Europe and Latin America, with more than \$1 *trillion* in assets under management. The company provides financial products – including life insurance, annuities, retirement-related services, mutual funds and investment management. Prudential operates in four divisions: PGIM (formerly Prudential Investment Management), U.S. Workplace Solutions, U.S. Individual Solutions, and International Insurance. The \$38 billion market cap company employs 50,000 people.

On July 31st, 2019 Prudential released Q2 2019 results for the period ending June 30th, 2019. For the quarter Prudential reported Net Income of \$708 million (\$1.71 per share) compared to \$197 million (\$0.46 per share) in Q2 2018. After-tax Operating Income totaled \$1.307 billion (\$3.14 per share) compared to \$1.298 billion (\$3.01 per share) in the prior year period. The U.S. Workplace Solutions and International Insurance Divisions showed the greatest improvements for the quarter, posting pre-tax operating income of \$548 million and \$849 million respectively, compared to \$359 million and \$784 million in the year ago period. Adjusted book value per share totaled \$97.15, against \$92.60 in the year-ago quarter. At quarter-end Prudential held \$1.497 billion in assets under management compared to \$1.388 billion in Q2 of 2018.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$5.58	\$6.27	\$6.41	\$6.27	\$9.67	\$9.21	\$10.04	\$9.13	\$10.58	\$11.69	\$12.40	\$15.10
DPS	\$0.70	\$1.15	\$1.45	\$1.60	\$1.73	\$2.17	\$2.44	\$2.80	\$3.00	\$3.60	\$4.00	\$5.28
Shares	462	484	468	463	461	454	447	430	423	411	411	390

The above levels of growth may be a bit optimistic, considering 2009 was a rebounding year from the recession. If you look at 2007 (when the company was earning \$7.31 and paying out \$1.15) through 2018, Prudential has grown earnings-per-share by about 4.4% per year and the dividend has compounded at a rate of roughly 11% per annum for the last decade.

Moving forward we anticipate earnings growth to be in-line with the company's historical average – coming in at 4% annually over the intermediate-term. Higher interest rates and general economic growth can be positives for the company's growth prospects. Of course there are offsetting factors; chief among them being lower rather than higher rates in the short-term. The majority of Prudential's business is in the U.S. and Japan, both of which are mature markets and where we do not anticipate above average growth. Life insurance and annuities are highly competitive industries. Further, insurers do not know the price of the goods sold for years, allowing for the temptation to underprice policies in search for growth. We believe a slow, steady and profitable approach in this industry is prudent.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	6.8	8.9	8.9	8.7	7.4	8.8	8.3	8.7	10.2	8.6	7.5	8.5
Avg. Yld.	1.8%	2.1%	2.5%	2.9%	2.4%	2.5%	2.9%	3.5%	2.8%	3.6%	4.3%	4.1%

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In the last decade shares of Prudential have traded hands with an average P/E ratio of about 8.5 times earnings. This may seem low compared to your average firm, equating to a starting earnings multiple of 11.8%, but this has been typical of insurers. With shares currently trading at 7.5 times expected earnings, this implies a small valuation tailwind. The dividend ought to add meaningfully to shareholder returns as well, as it sits above 4% and yet only takes up about a third of earnings – leaving ample room for growth. Note this payment was recently increased 11.1% to \$1.00 per quarter.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	13%	18%	23%	26%	18%	24%	24%	31%	28%	31%	32%	35%

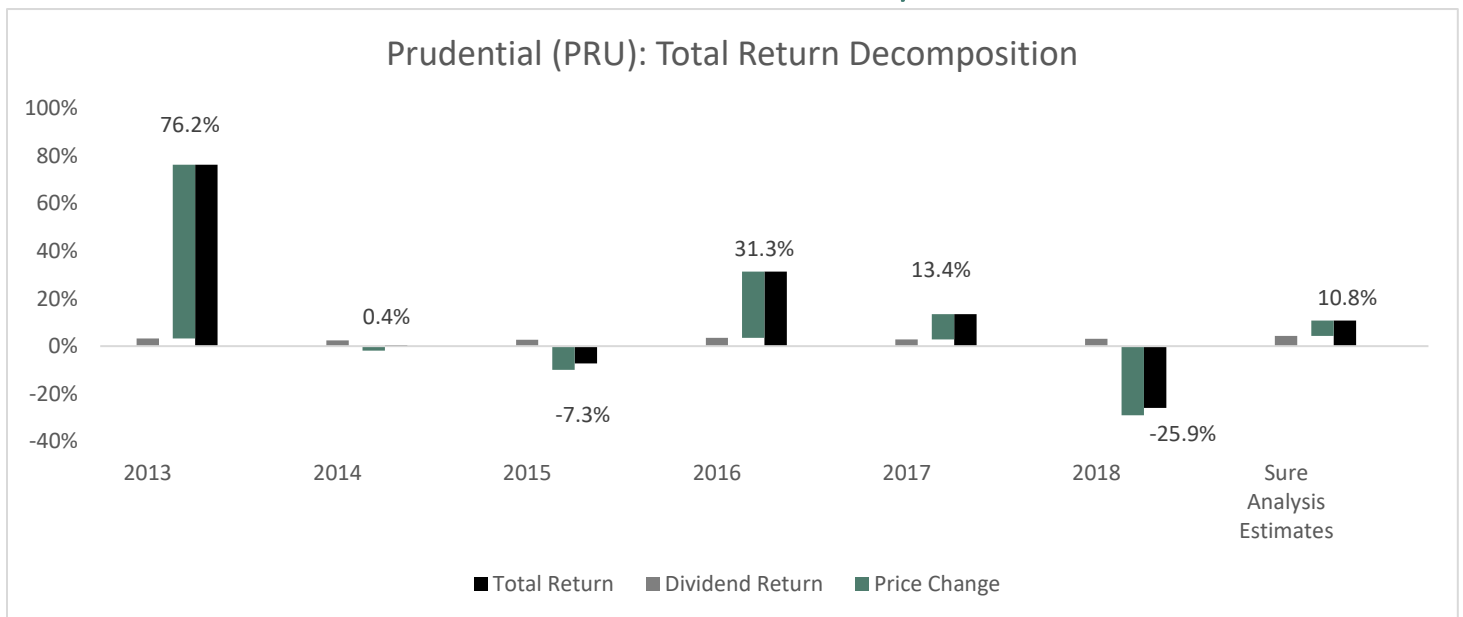
While Prudential is highly profitable and well-known, we do not believe the firm carries a significant competitive advantage over its competitors as the products it sells are highly commoditized.

During the last recession, Prudential generated earnings-per-share of \$7.31 in 2007 followed by \$2.69, \$5.58 and \$6.27 in 2008 through 2010. It wasn't until 2014 that earnings finally eclipsed their pre-recession peak. Similarly, the dividend was slashed from \$1.15 in 2007 down to \$0.58 in 2008 and did not recover until 2010. This sort of cyclicality is certainly possible in the next downturn. Still, the company has a reasonable payout ratio and financial position. We do note that while earnings dipped significantly during the last recession, dilutive activity was not excessive.

Final Thoughts & Recommendation

Shares are down 9% since our last update. Prudential has proven to be a solid business over the years with a variety of positive attributes. We are forecasting 10.8% annual total return potential, stemming from 4% growth, a 4.3% starting dividend yield and a 2.5% valuation tailwind. Further, shares trade near book value, although much like the average valuation, this has been a typical occurrence. There is a lingering negative: even in good times growth is not especially robust and in lesser times the rate of improvement can fall off the rails completely. With shares trading close to our view of fair value, we are reiterating our hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	32566	38217	49085	84847	41461	54105	57119	58779	59689	57570
SG&A Exp.	7392	8309	10605	11094	11011	11807	10912	11779	11915	12967
D&A Exp.	175	104	290	302	411	631	113	318	222	N/A
Net Profit	3124	3001	3632	520	-667	1381	5642	4368	7863	4074
Net Margin	9.6%	7.9%	7.4%	0.6%	-1.6%	2.6%	9.9%	7.4%	13.2%	7.1%
Free Cash Flow	5840	6542	12377	20909	8445	19396	13942	14815	13445	N/A
Income Tax	-54	1243	1515	213	-1058	349	2072	1335	-1438	822

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets (\$B)	480.20	539.85	620.24	709.24	731.78	766.66	757.26	783.96	831.92	815.08
Cash & Equivalents	13164	12915	14251	18100	11439	14918	17612	14127	14490	15353
Goodwill & Int.	N/A	N/A	3845	3248	3675	2836	2828	2314	1591	1850
Total Liab. (\$B)	454.47	506.93	585.40	670.12	695.90	724.31	715.33	737.87	777.58	766.05
Long-Term Debt	24159	25635	27482	28790	29524	29728	29407	21324	20070	20784
Total Equity	25195	32415	34253	38503	35278	41770	41890	45863	54069	48617
D/E Ratio	0.96	0.79	0.80	0.75	0.84	0.71	0.70	0.47	0.37	0.43

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	0.7%	0.6%	0.6%	0.1%	-0.1%	0.2%	0.7%	0.6%	1.0%	0.5%
Return on Equity	16.2%	10.4%	10.9%	1.4%	-1.8%	3.6%	13.5%	10.0%	15.7%	7.9%
ROIC	6.6%	5.5%	6.0%	0.8%	-1.0%	2.0%	7.9%	6.3%	11.1%	5.6%
Shares Out.	462	484	468	463	461	454	447	430	423	426
Revenue/Share	72.66	80.39	100.44	181.26	89.53	115.68	124.06	131.61	136.90	135.08
FCF/Share	13.03	13.76	25.33	44.67	18.24	41.47	30.28	33.17	30.84	N/A

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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