

Prudential Financial Inc. (PRU)

Updated August 5th, 2020 by Eli Inkrot

Key Metrics

Current Price:	\$67	5 Year CAGR Estimate:	13.0%	Market Cap:	\$26 B
Fair Value Price:	\$76	5 Year Growth Estimate:	5.0%	Ex-Dividend Date:	08/19/20 ¹
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.7%	Dividend Payment Date:	09/12/20 ¹
Dividend Yield:	6.6%	5 Year Price Target	\$97	Years Of Dividend Growth:	12
Dividend Risk Score:	C	Retirement Suitability Score:	B	Last Dividend Increase:	10.0%

Overview & Current Events

Prudential Financial, now in business for over 140 years, operates in the United States, Asia, Europe and Latin America, with \$1.6 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 \$26 billion market cap company employs approximately 50,000 people.

On August 4th, 2020 Prudential released Q2 2020 results for the period ending June 30th, 2020. For the quarter Prudential reported a net loss of -\$2.409 billion or -\$6.12 per share compared to net income of \$708 million or \$1.71 per share in Q2 2019. However, these results included substantial investment losses. On an adjusted basis, operating income totaled \$742 million or \$1.85 per share compared to \$1.262 billion or \$3.03 in the year ago quarter. While results declined, the per share metrics continue to be aided by a lower share count. Adjusted book value per share totaled \$92.07 against \$97.15 in Q2 2019. At quarter-end Prudent held \$1.605 trillion in assets under management compared to \$1.497 trillion in the year ago period.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$6.27	\$6.41	\$6.27	\$9.67	\$9.21	\$10.04	\$9.13	\$10.58	\$11.69	\$11.69	\$9.50	\$12.12
DPS	\$1.15	\$1.45	\$1.60	\$1.73	\$2.17	\$2.44	\$2.80	\$3.00	\$3.60	\$4.00	\$4.40	\$5.62
Shares²	484	468	463	461	454	447	430	423	411	399	396	370

If you look at 2007 (when the company was earning \$7.31 and paying out \$1.15) through 2019, Prudential has grown earnings-per-share by about 4.0% per year and the dividend has compounded at a rate of roughly 11.8% per annum.

Higher interest rates and general economic improvement could be positives for the company's growth prospects over the long-term. 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 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.

In addition, the current COVID-19 pandemic is set to impact the business. We again reduced our expectation for 2020 earnings and presume a slightly higher 5% growth rate; still implying lower expectations over the intermediate term.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	8.9	8.9	8.7	7.4	8.8	8.3	8.7	10.2	8.6	8.0	7.0	8.0
Avg. Yld.	2.1%	2.5%	2.9%	2.4%	2.5%	2.9%	3.5%	2.8%	3.6%	4.3%	6.6%	5.2%

¹ Estimate

² In millions.

Disclosure: This analyst is long the security discussed in this research report

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In the last decade shares of Prudential have traded hands with an average P/E ratio between 8- and 9-times earnings. This may seem low compared to your average firm, but this has been typical of insurers. With shares currently trading at 7 times expected earnings, this implies the potential for a moderate valuation tailwind.

The dividend ought to add meaningfully to shareholder returns as well, as it sits above 6% and takes up less than half of earnings – leaving ample room for growth. Note the payment was increased 10% to \$1.10 per quarter earlier this year.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	18%	23%	26%	18%	24%	24%	31%	28%	31%	34%	46%	46%

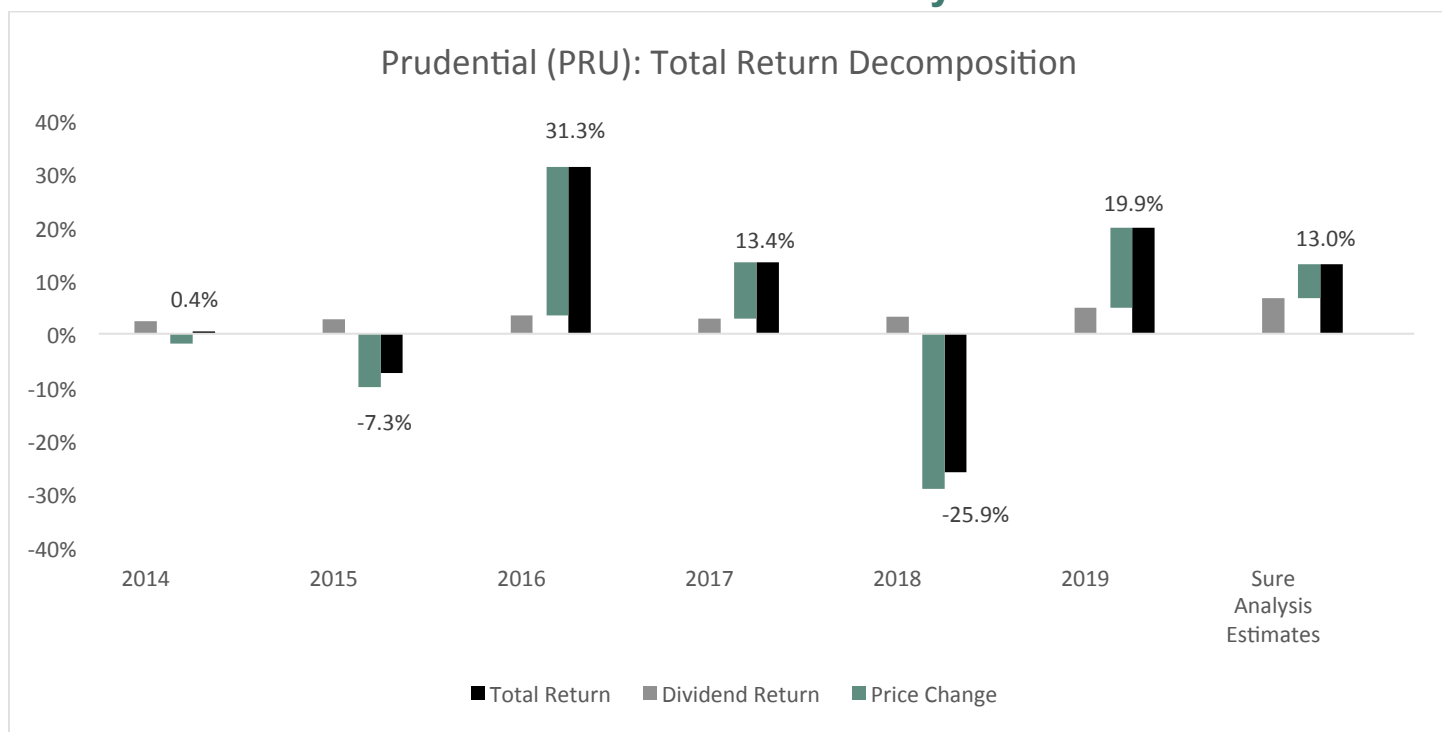
While Prudential is highly profitable and well-known, we do not believe the firm carries a significant competitive advantage over its competitors as the products it sells are highly commoditized.

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 cyclical nature 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

After being down -40% in our last report, shares are up 18% in the last three months. Prudential has proven to be a solid business over the years with a variety of positive attributes. We are forecasting 13.0% annual total return potential, stemming from 5% growth, a 6.6% starting dividend yield and a valuation tailwind. 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. Still, the valuation remains compelling and the security continues to earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	38217	49085	84847	41461	54105	57119	58779	59689	57570	57243
SG&A Exp.	8309	10605	11094	11011	11807	10912	11779	11915	12967	14520
D&A Exp.	104	290	302	411	631	113	318	222		
Net Profit	3001	3632	520	-667	1381	5642	4368	7863	4074	4186
Net Margin	7.9%	7.4%	0.6%	-1.6%	2.6%	9.9%	7.4%	13.2%	7.1%	7.3%
Free Cash Flow	6542	12377	20909	8445	19396	13942	14815	13445		
Income Tax	1243	1515	213	-1058	349	2072	1335	-1438	822	947

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets (\$B)	539.85	620.24	709.24	731.78	766.66	757.26	783.96	831.92	815.08	896.55
Cash & Equivalents	12915	14251	18100	11439	14918	17612	14127	14490	15353	16327
Goodwill & Int.	N/A	3845	3248	3675	2836	2828	2314	1591	1850	1110
Total Liab. (\$B)	506.93	585.40	670.12	695.90	724.31	715.33	737.87	777.58	766.05	832.83
Long-Term Debt	25635	27482	28790	29524	29728	29407	21324	20070	20784	21853
Total Equity	32415	34253	38503	35278	41770	41890	45863	54069	48617	63115
D/E Ratio	0.79	0.80	0.75	0.84	0.71	0.70	0.47	0.37	0.43	0.35

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	0.6%	0.6%	0.1%	-0.1%	0.2%	0.7%	0.6%	1.0%	0.5%	0.5%
Return on Equity	10.4%	10.9%	1.4%	-1.8%	3.6%	13.5%	10.0%	15.7%	7.9%	7.5%
ROIC	5.5%	6.0%	0.8%	-1.0%	2.0%	7.9%	6.3%	11.1%	5.6%	5.4%
Shares Out.	484	468	463	461	454	447	430	423	411	411
Revenue/Share	80.39	100.44	181.26	89.53	115.68	124.06	131.61	136.90	135.08	139.31
FCF/Share	13.76	25.33	44.67	18.24	41.47	30.28	33.17	30.84		

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

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