Prudential Financial

William Infante
10 June 2020

Qualitative Analysis – Management, Prospects, Competition

Competitive Comparison

Item	AIG (AIG)	Allstate (ALL)	Berkshire (BRK.B)	Chubb (CB)
Market Price	40	100	200 (B-Shares)	140
Free Cash Flow	$3 (*d*)	$6	$111	$6
ROTA	0.66%	4.29%	12.54%	2.96%
Revenue	$49,778,000,000	$44,675,000,000	$69,147,000,000	$34,230,000,000
Debt:Equity	0.59	0.27	0.28	0.29
Earning Coverage	5.98	14.82	20.6	8.1
M-Score	2.48 (*d*)	2.58 (*d*)	3.85 (*d*)	2.61 (*d*)
Market Share	3.6%	5%	9.3%	3.3%
Consensus	VIII	III	I	VI

Item	Metlife (MET)	Progressive (PGR)	Prudential (PRU)	Travelers (TRV)
Market Price	40	80	70	130
Free Cash Flow	$17	$13	$16	$7
ROTA	0.84%	7.94%	0.49%	2.55%
Revenue	$69,620,000,000	$38,997,000,000	$64,710,000,000	$31,581,000,000
Debt:Equity	0.26	0.38	0.4	0.26
Earning Coverage	6.18	20.93	2.72	7.62
M-Score	3.60 (*d*)	2.71 (*d*)	2.72 (*d*)	2.59 (*d*)
Market Share	13%	5.6%	7.7%	4.1%
Consensus	II	V	IV	VII

*Shares outstanding is always 890 million

Overall, Prudential Financial is ranked 4/8 compared to it’s competitors. It has ample cash flow, and revenue, yet it seems that it struggles with its expenses, as it has low earning coverage and Return-on-tangible asset numbers. Overall,

NYSE:PRU

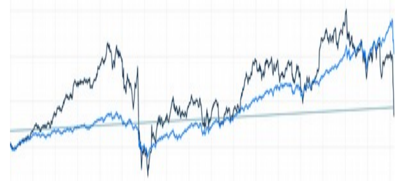
Price: $71.76

Price Target: $500

Secondary Price Target: $158

Consensus: HOLD

Price Performance



S&P 500 – 177% (2002-C), 140% (2002-2018)

Prudential – 131% (2002-C), 318% (2002-2018)

Company Data	
Price ($)	71.76
Date of Price	9 June 20
52-week Range ($)	38.62-103.56
Market Cap ($ bn)	28.35
Fiscal Year End	Dec
Shares O/S (bn)	29.52
Price Target ($)	500
Secondary Price Target ($)	158

Other Metrics	
Price-to-Owner-Earnings	5.57
Cash-to-Debt	1.32
Net Margin (%)	4.72
ROE (%)	4.81
ROA (%)	0.34
Cash per Share ($)	80
Working Capital Per Share ($)	115

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Prudential is doing modestly compared to its competitors. Prudential should have

a 50% rating on its competitive conditions, as it was ranked at a moderate 4/8. One last note from this is that it is unlikely that Prudential manipulates its earnings, as it's M-Score is lower than -2.2. This company will grow in the long term.

Management Analysis

The management seems satisfactory. To begin, 77% of its employees approved of the CEO, and about 60% approved of the management in general. The CEO seems favorable. Mr. Lowrey, the CEO, is a long term investor by character, as he mentions of 'seizing opportunities that may arise during periods of stress'. He also went to both Yale and Harvard, where he studied Business and Architecture. He also worked as a real estate banker for J.P. Morgan Chase. Despite this, the CEO is still not very proven. One way to see this is if Mr. Lowrey is able follow through with his plan to eliminate 500 million of expenses by 2022.

Future Prospects

As mentioned before, Prudential will most likely prosper for years to come, as the insurance industry is a stable one, and Prudential is a strong company. There is no need for explaination, as stable industries survive anything, and along with this, insurance is a necessary business. However, it earns little. This business should receive a 60% rating on its future prospects.

Quantitative Analysis – Income Statement & Balance Sheet, Sources of Income

Income Statement Analysis (2016-2019)

Item	2019	2018	2017	2016	Average	Trend
ROTA	0.49%	0.50%	0.98%	0.57%	0.64%	Bad
ROE	7.41%	7.83%	15.52%	9.84%	10.2%	Bad
Premium(mn)	$34,202	$35,779	$32,091	$30,964	$33,259	OK
Net Income, adjusted (mn)	$1,854	$1,801	$4,800	$2,491	$2,737	Bad
Interest Expenses Earned	1.59	1.55	4.13	2.16	2.4	Bad

Owner Earnings (mn)	$11,516	$17,772	$6,495	$10,897	$11,670	OK

Balance Sheet Analysis (2017-2019)

Item	2019	2018	2017	% Change
Cash Per Share	$0.6	$0.5	$0.5	12%
Liability:Asset	93%	94%	93%	0.54% (*d*)
Debt:Equity	57%	71%	60%	5% (*d*)
Book Value Per Share	$158	$118	$128	23%
Liquidation Value (mn)	$30,235	$18,610	$24,244	24.7%
Acid Test (Intangibles)	PASS	PASS	PASS	N/A
Surplus (mn)	$32,991	$30,470	$28,671	15.1%

Conclusions from 2017-2019 Study of Financial Statements

To begin, PRU's low ROTA is justified by its vast tangible assets, which dilute this metric. The ROTA is being diluted, since the ROE is good. These metrics, along with the income, show stability, and most likely slow growth in the longer term. The net income always covered the interest expenses, which allows this business to at least qualify for bond investment. Despite having a less-than par income statement, the business successfully retains their earnings over time, and does will in their business of earning premiums from policy-holders. PRU's balance sheet was acceptable. Although the Liability:Asset ratio is high, it is most likely justified by the fact that like banks, insurance companies have people that put their money into it. This is what makes PRU's balance sheet seem less than par, but when in fact, it is above par! Their balance sheet passed the acid test for every period studied, and their liquidation value seems to cover the market price. Lastly, the one thing that stuck out to me was the fact that the business was selling for below its book value by a generous margin. This allows for opportunity, and safety. Overall, this business looks like it will survive for years to come. Now, a quantitative study will be conducted for the years of the financial crisis, 2007-2009. This will determine what PRU can withstand.

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Income Statement Analysis (2007-2009)

Item	2009	2008	2007	% Change
ROE (avg)	0.85% (*d*)	5.5%	16.9%	105% (*d*)
Premiums (mn)	$16,545	$15,468	$14,351	15%
Net Income, adjusted (mn)	$3,124	$1,604 (*d*)	$3,662	15 (*d*)
Interest Expenses Earned	6.6	None	7.7	15%

Balance Sheet Analysis (2007-2009)

Item	2009	2008	2007	% Change (Max Drawdown)
Cash Per Share	0.44	0.51	0.38	16%
Liability:Asset	95%	97%	95%	0%
Debt:Equity	110%	97%	50%	120%
Book Value Per Share	$43	$40	$50	20% (*d*)
Liquidation Value (mn)	$1,656	$17,091 (*d*)	$3,295 (*d*)	400% (*d*)

Acid Test (Intangibles)	Border Line	Border Line	Border Line	N/A
Surplus (mn)	$13,787	$10,502	$11,841	11% (*d*)

PRU's income account deemed somewhat satisfactory, given the situation. Despite of a net loss in 2008 (due to a decline in client investment), their premiums grew by 15%. Their earning coverage also rebounded significantly in 2009. Conclusively, PRU will consistently earn profits over time. PRU's balance sheet also seemed somewhat satisfactory, given the situation. They kept their liabilities essentially consistent at around 96% of their assets. Speaking of assets, they spent little cash during the crisis, unlike other companies. Also, when accounting for large client account liabilities, the company would pass the 'Acid Test', which is Liabilities:Assets excluding intangible assets. Without accounting for this, PRU just about passes. The most important thing to look at when observing a company is whether they can move rebound from downturns. Despite the liquidation value being negative pre-2009, it rebounded, and to this day holds a good liquidation value. Additionally, Prudential consistently obtained surplus throughout the crisis, with the surplus only going down by 11% during 2008, before rebounding past the 2007 surplus. Lastly, when looking at book value, Prudential was overvalued in 2009 and 2007, while being undervalued in 2008. This can show that the stock will grow slowly for the long term, as it may become overvalued directly after the beginning of a bull market. Overall, Prudential is strong, and it will last for years to come. It has proven to be able to grow during both bear and bull markets.

Sources of Income

Prudential Financial has 3 sources of income, which are insurance premiums, insurance and asset management fees, and investments. These sources of income are mostly from cash flow, including most of the investments (which are in bonds). This shows that Prudential can earn money consistently through cash flow rather than the pain-staking process of capital gains, which is taxed more.

Intrinsic Value Model

Growth	
Tangible Assets	**$854,300**
Recurring Net Income (Deflation)	**$1,854**
Recurring Net Income (Inflation)	**-$1,604**
ROTA (Deflation)	**0.22%**
ROTA (Inflation)	**-0.19%**
Long-term ROTA	**0.01%**
Owner Earnings	
Recurring Net Income	**$4,238.00**
Depreciation + Amortization	**$460.00**
Other Non-Cash Charges	**$3,587.00**
Changes in Working Capital	**$0.00**
Capital Expenditures (Avg)	**-$2,483.00**
Owner Earnings	**$5,802.00**
Confidence Factor	
Management	70
Competitive Conditions	50
Future Prospects	60
Confidence Factor	60

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Intrinsic Value

Shares Outstanding	411
Government Risk Free Rate	1.52%

FCF Growth (Long Term)

Period 1	Period 2	Period 3	Period 4
$5,802.85	$5,803.70	$5,804.55	$5,805.40

Terminal Value	$381,933.98
Total Company Value	$381,925.74
Intrinsic Value	$557.56

Closing Statements

Pros

- The stock is undervalued in terms of the FCF Model, and book value. This provides a big opportunity, especially if the market falls farther.
- Both the industry and Prudential are stable. Prudential has been around since about 1890, and therefore has been through a few debt crises.
- Prudential has a surplus of free cash flow. That allows for a higher intrinsic value, and safety for the company.
- Prudential also controls its debt very well, which is a characteristic of an insurance company. As of now, they have a Debt:Equity of about 40%. Also, the debt is covered by their cash, and the many securities it holds.
- Their management seems respectable.
- The CEO is new to the CEO job, which could mean that he is not a corrupted one
- They earn a satisfactory Return on Equity. Again, their low ROTA is justified by lots of tangible assets
- The company generates money mostly from cash flow rather than capital gains.

Cons

- The CEO is unproven. However, if Prudential ends up getting rid of 500 million in expenses by 2022, (Mr. Lowreys plan) then that will prove that Mr. Lowrey is capable.

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Conclusion

Overall, this stock should be ranked at 'HOLD'. The only reason it should not be ranked 'BUY' right now is because the market are headed down, and why acquire shares of a company right before the stock falls? Current shareholders should hold onto their shares of this company, as there is an adequate margin of safety between the intrinsic value and the market price, and the company is strong and consistent. This stock can be ranked as a 'BUY' for new investors as soon as the CEO has proven himself a little bit more, and as soon as the economy has bottomed, which is expected to be in around the year 2023.