

RatingsDirect®

Pacific LifeCorp

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Pacific LifeCorp

Anchor	aa-	+	Modifiers	0	=	SACP	aa-	AA-/Stable/--
▲		▲		+				
Business Risk	Very Strong		Governance	Neutral		Support	0	Financial strength rating
Competitive position	Very strong							
IICRA	Low		Liquidity	Exceptional		Group support	0	A-/Stable/--
Financial Risk	Very Strong					Government support	0	
Capital and earnings	Very strong		Comparable ratings analysis	0				Holding company ICR
Risk exposure	Moderately low							
Funding structure	Neutral							

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

Overview	
Key strengths	Key risks
Very strong competitive position with solid market positions in the U.S. individual life and annuity markets	Exposure to legacy variable annuity, albeit declining as a percentage of assets
Well-diversified earnings with contributions from life, retirement, institutional, and reinsurance businesses	Meaningful investments in 'BBB' rated corporate bonds and large commercial real estate loans
Excellent capitalization with 'AAA' level redundancy per our year-end 2020 risk-based capital (RBC) model	Elevated mortality and prolonged low interest rates weighing on earnings

We expect Pacific LifeCorp to maintain its solid market positions in life insurance and annuities. It's a leading provider of indexed universal life (IUL) insurance and ranks 17th in fixed annuity, 17th in fixed index annuity (FIA), ninth in variable annuity (VA) sales, and second in structured settlement through year-end 2020 per LIMRA. At year-end 2020, Pacific Life was ranked fourth in total life insurance sales on a recurring premiums basis, and we expect it to maintain its top 10 market position.

Pacific Life's well-diversified earnings are one of its key strengths. The company has earnings contributions from life insurance, retirement, institutional, and reinsurance divisions. In 2020, the company established an institutional division and is focused on growing its reinsurance business. We expect both of these divisions to meaningfully contribute to overall group earnings.

We expect Pacific Life's financial risk profile to remain very strong. Although it has historically held capital redundancy at the 'AAA' level, we expect it to maintain a capital buffer at the 'AA' confidence level on a more sustained basis, consistent with its business growth strategy. Pacific Life also holds sufficient liquidity at the holding company, as demonstrated by more than \$400 million in cash and short-term investments as of year-end 2020.

Outlook: Stable

The stable outlook reflects S&P Global Ratings' view that the group will maintain its very strong business risk and capital redundancy at least at the 'AA' confidence level. We expect its consolidated financial leverage to remain below 20% and fixed-charge coverage above 5x over the longer term.

Downside scenario

We could lower the ratings over the next 12-24 months if Pacific Life's:

- Competitive position deteriorates due to a weakening market position,
- Operating performance declines significantly and is consistently below peers', or
- Earnings become significantly less diversified.

We may also lower our ratings if the group adopts a more-aggressive investment policy or if the quality of its overall investment portfolio deteriorates and capital is no longer redundant at the 'AA' level.

Upside scenario

We are unlikely to raise our ratings in the next 24 months.

Assumptions

- Real GDP growth of 5.5% in 2021 and 3.9% in 2022
- Core Consumer Price Index growth of 3.4% in 2021 and 3.5% in 2022
- Real consumer spending growth of 8.0% in 2021 and 3.8% in 2022
- Unemployment rate of 5.4% in 2021 and 4.0% in 2022
- 10-year Treasury note yield of 1.5% in 2021 and 2.1% in 2022

Source: "Economic Outlook U.S. Q1 2022: Cruising At A Lower Altitude," published on Nov. 29, 2021

Table 1

Pacific LifeCorp--Key Metrics							
(Mil. \$)	2022f	2021f	2020	2019	2018	2017	2016
Net income*	500-700	>600	(658)	864	953	1,374	849
Financial leverage* (%)	<15	<20	15.16	12.9	16.3	13	17.7
EBITDA fixed-charge coverage§ (x)	>5	>5	5.9	10.3	15.1	11.9	9.4
Net investment yield (%)	3.0-4.0	3.0-4.0	3.6	4.8	4	4.6	4.2
Total adjusted capital	12,000-13,500	11,500-12,500	11,842.12	11,261.1	10,661.3	9,929.5	9,246

Table 1

Pacific LifeCorp--Key Metrics (cont.)							
(Mil. \$)	2022f	2021f	2020	2019	2018	2017	2016
S&P Global Ratings' capital adequacy/redundancy	AA	AA	AAA	AAA	AA	AAA	AAA

*Based on consolidated GAAP financial statement. §2020 GAAP EBITDA adjusted for net derivatives losses.

Business Risk Profile: Very Strong

We view Pacific Life's competitive position as very strong based on its well-recognized brand, solid market share, and diversified product offerings. The group primarily caters to the affluent market and relies on a well-diversified distribution network comprising independent producers/planners, financial advisers, and financial institutions (regional banks and wirehouses). At the same time, the company is growing its digital capabilities. Pacific Life is among the top 10 in individual life insurance companies in the U.S. and remains the leading player in IUL, despite regulatory changes (AG 49 and Section 7702 of the IRS tax code) and evolving pricing conditions.

The group has a well-established presence in annuities and institutional offerings. The group also has a strong market presence in life-based long-term care combo (also known as hybrid LTC) products, which have grown significantly in recent years.

Over the past few years, Pacific Life has rebalanced its VA sales to include more investment-only variable annuities as well as some variable annuities with accumulation benefits. It has achieved a strong position in FIA and has a growing presence in term life, but it did experience some slowdown in sales due to challenging business conditions and the low interest rate. Internationally, the company is expanding its presence in the longevity risk market through its Pacific Life Re subsidiary and is one of the top players in this market.

Consistent with other industry players, Pacific Life's operating performance was affected because of COVID-19-related mortality claims but benefited from its longevity exposure. The company's historical operating performance has been stable and in line with peers', with a five-year (2016-2020) average generally accepted accounting principles (GAAP) return on assets (ROA) of about 0.68%. As of year-end 2020, the company reported GAAP ROA of 0.69%.

In the first half of 2021, Pacific Life's overall operating performance improved compared with 2020, but earnings reflect unfavorable mortality claims experience. We expect overall mortality claims to remain elevated in 2022 as well, but overall earnings should benefit from Pacific Life's business diversity. We expect ROA to remain 0.4%-0.8%.

Financial Risk Profile: Very Strong

Pacific Life has maintained very strong capital and earnings at least at the 'AA' confidence level--its statutory RBC ratio was 628% at year-end 2020. Our consolidated capital analysis covers non-U.S. operations, as well as captive entities. We also make adjustments to account for the risk associated with longevity swaps.

The company has boosted capitalization by gradually lowering its exposure to more-capital-intensive products. We expect the group's capital management strategy to remain focused on generating strong statutory retained earnings,

which support our view of the group's capitalization. While the group uses hedging, both GAAP and statutory earnings have shown some volatility. Nevertheless, in the pandemic, the group's very strong capital position should help mitigate the concerns around mortality and asset risk.

In our view, Pacific Life has a well-diversified investment portfolio and no material risks not already captured in our capital and earnings analysis. The group maintains a low level of high-risk assets (speculative-grade bonds, unaffiliated common equities, equity real estate, and alternative investments) relative to capital.

While most of the investment portfolio comprises fixed maturities (63%), the group is exposed to commercial mortgage loans--about 15% of total invested assets. However, any impact from nonperforming commercial whole loans (CWL) should be fairly absorbable given group's very strong capitalization. As of year-end 2020, Pacific Life's overall CWL portfolio's loan-to-value ratio was close to 51% and debt service coverage ratio was about 2.0x.

The company also has a sizable exposure to 'BBB' rated securities--about 62% of total bond portfolio as of year-end 2020. However, we have a favorable view of the group's tight risk controls and believe they will prevent losses above the well-defined tolerances. While we do not anticipate any meaningful changes in general asset allocation or credit quality in the next couple of years, we will continue to monitor the group's investment strategy and the credit quality of its portfolio.

We assess Pacific Life's financial flexibility as adequate based on reported financial leverage of 15.2% and EBITDA fixed-charge coverage (excluding net derivatives gains/losses) of about 5.9x as of year-end 2020. We expect the group to maintain financial leverage below 20% with fixed-charge coverage above 5x for full-year 2021 and 2022.

Other Key Credit Considerations

Governance

In our view, Pacific Life's governance is in line with industry peers. The group has a well-engrained risk management framework and a well-defined risk appetite. It has a clear strategic planning process balanced with a risk appetite for each division.

In August 2021, Jim Morris, chairman, president, and CEO of Pacific Life Group announced his retirement, and Darryl Button will become president and CEO in April 2022. We consider senior management changes, especially at the CEO level, to be meaningful transitions in the leadership of a company. In this instance, Mr. Button has been the chief financial officer since 2017 and comes with broad and deep life insurance industry experience. We view this change in governance to be neutral to the rating.

Liquidity

We assess Pacific Life's liquidity as exceptional, stemming from its diversified invested portfolio, far exceeding liquid liabilities. The group has borrowing capacity under its commercial paper, lines of credit, and Federal Home Loan Bank holdings to access for liquidity during times of stress.

Factors specific to the holding company

Our issuer credit rating on Pacific LifeCorp, the group's intermediary holding company, is three notches lower than our financial strength rating on the group's insurance operating companies, reflecting the structural subordination of the holding company obligations. Pacific LifeCorp relies upon subsidiary interest payments on internal surplus notes, as well as its own cash and short-term investments to meet its fixed charges. It held more than \$400 million in cash and short-term investments as of year-end 2020. Primary subsidiary Pacific Life Insurance Co. can pay up to \$769 million in dividends to Pacific LifeCorp in 2021 without regulatory approval.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Insurance | General: Methodology For Calculating The Convexity Risk In U.S. Insurance Risk-Based Capital Model, April 27, 2011
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

Appendix

Table 2

Pacific LifeCorp--Credit Metrics History						
(Mil. \$)	2020	2019	2018	2017	2016	2015
S&P Global Ratings capital adequacy	AAA	AAA	AA	AAA	AAA	AAA
Total invested assets	97,293	90,526	79,291	71,206	64,882	59,771
Net premiums earned	12,213	14,007	12,799	9,788	8,764	9,381
EBIT	(154.9)	879	775	933	1,048	746
Net income (attributable to all shareholders)	(91.3)	1,749	928	1,247	891	573
Return on revenue (%)	(0.9)	4.7	4.8	6.9	8.6	5.9
Return on assets (excluding investment gains/losses) (%)	(0.1)	0.6	0.6	0.7	0.9	0.6
EBITDA fixed-charge coverage§ (x)	5.9	10.3	15.1	11.9	9.4	8.1
Financial obligations/EBITDA adjusted§	3.9	1.7	1.2	1.1	1.5	1.7
Financial leverage including pension deficit as debt* (%)	15.2	12.9	16.3	13.0	17.7	19.1
Net investment yield (%)	3.6	4.8	4.0	4.6	4.2	4.6

*Based on GAAP financials. §2020 GAAP EBITDA adjusted for net derivatives losses.

Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	Very Strong	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
Strong	aa-/a+	a+/a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bb+	bb/bb-	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of December 13, 2021)*

Pacific LifeCorp

Issuer Credit Rating

Local Currency

A-/Stable/--

Senior Unsecured

A-

Related Entities

Pacific Life & Annuity Co.

Financial Strength Rating

Local Currency

AA-/Stable/--

Issuer Credit Rating

Local Currency

AA-/Stable/--

Pacific Life Global Funding II

Senior Secured

AA-

Pacific Life Insurance Co.

Financial Strength Rating

Local Currency

AA-/Stable/--

Issuer Credit Rating

Local Currency

AA-/Stable/A-1+

Financial Enhancement Rating

Local Currency

AA-/--/--

Commercial Paper

Local Currency

A-1+

Subordinated

A

Pacific Life Re (Australia) Pty Ltd.

Financial Strength Rating

Local Currency

AA-/Stable/--

Pacific Life Re International Ltd.

Financial Strength Rating

Local Currency

AA-/Stable/--

Ratings Detail (As Of December 13, 2021)*(cont.)

Pacific Life Re Ltd.

Financial Strength Rating

Local Currency

AA-/Stable/--

Pacific Life Short Term Funding LLC

Commercial Paper

Local Currency

A-1+

Domicile

Delaware

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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