

Principal Financial(PFG)

\$42.45 (As of 07/30/20)

Price Target (6-12 Months): **\$50.00**

Long Term: 6-12 Months

Zacks Recommendation:

Outperform

(Since: 07/10/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:A

Value: A

Growth: C

Momentum: A

Summary

Principal Financial's second-quarter earnings beat estimates. Focus on fee-based revenue sources should help it earn steadily and limit its exposure to interest rate. The company continues to benefit from strength and leadership in retirement and long-term savings, group benefits and protection in the United States, retirement and long-term savings in Latin America and Asia, and global asset management. The inorganic growth story is impressive with buyouts fortifying its global footprint and adding fee-based businesses. Its shares have underperformed the industry year to date. Nevertheless, it boasts a solid capital position. However, increase in expenses weighs on its margins. Lower ROE pose financial risk. Also, dilution from acquisition is a potential headwind. Given the low rate environment, it expects lower annuity sales in 2020.

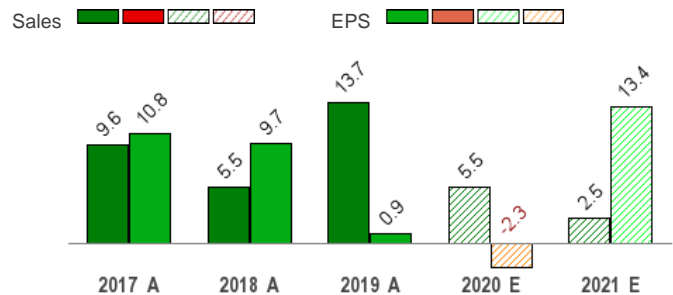
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$59.34 - \$23.31
20 Day Average Volume (sh)	1,355,929
Market Cap	\$12.0 B
YTD Price Change	-20.2%
Beta	1.63
Dividend / Div Yld	\$2.24 / 5.1%
Industry	Financial - Investment Management
Zacks Industry Rank	Top 15% (38 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	11.5%
Last Sales Surprise	-17.0%
EPS F1 Est- 4 week change	7.7%
Expected Report Date	10/22/2020
Earnings ESP	0.0%
P/E TTM	8.4
P/E F1	7.8
PEG F1	1.7
P/S TTM	0.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,412 E	3,979 E	4,297 E	4,087 E	17,602 E
2020	4,430 A	3,181 A	4,176 E	3,964 E	17,174 E
2019	3,659 A	3,977 A		4,138 A	16,275 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.44 E	\$1.41 E	\$1.54 E	\$1.59 E	\$6.18 E
2020	\$1.15 A	\$1.46 A	\$1.42 E	\$1.44 E	\$5.45 E
2019	\$1.43 A	\$1.52 A	\$1.23 A	\$1.41 A	\$5.58 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/30/2020. The reports text is as of 07/31/2020.

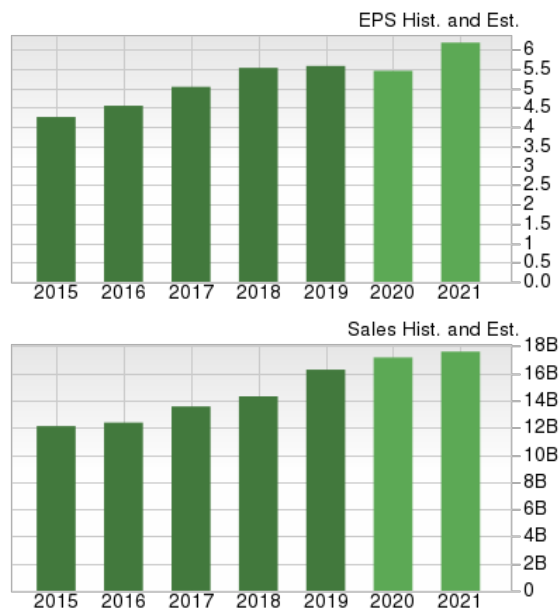
Overview

Ranked among the Fortune 500 companies, Des Moines, IA-based Principal Financial Group Inc. is a leader in global investment management offering businesses, individuals and institutional clients a wide range of financial products and services, including retirement, asset management and insurance through our diverse family of financial services companies. The company was founded in 1879.

The global asset management businesses provide long-term investment strategies to institutional, retirement, high net worth and retail clients by offering a range of capabilities including equity, fixed income, real estate and other alternative investments, as well as fund offerings. In the United States., the company primarily focuses on small and medium-sized businesses by offering a broad array of retirement and employee benefit solutions and individual insurance solutions. Principal Financial reports through four segments.

Retirement and Income Solution (RIS) (54.5% of 2019 revenues) provides pension plan products and services. It now offers a comprehensive portfolio of products and services for retirement savings and retirement income. The company organized Retirement and Income Solutions operations into two business groupings: Retirement and Income Solutions — Fee and Retirement and Income Solutions — Spread. **US Insurance Solution (USIS) (27.1%)** began selling individual life insurance products and now expanded offering to include group insurance products. The company organized this operation into two divisions: Specialty Benefits insurance and Individual Life insurance. **Principal International (PI) (9.3%)** focuses on locations with growing middle classes, favorable demographics and increasing long-term savings, ideally with defined contribution retirement markets. It has operations in Latin America and Asia. **Principal Global Investors (PGI) segment (9.1%)** manages assets for sophisticated investors around the world using a multi-boutique strategy that provides diverse investment capabilities including equity, fixed income, real estate and other alternative investments.

The **Corporate** segment consists of the assets and activities that have not been allocated to any other segments.



Reasons To Buy:

- ▲ Shares of Principal Financial have lost 20.3% year to date compared with the industry's fall of 1.4%. Nevertheless, its solid fundamentals are likely help the stock regain its momentum going forward.
- ▲ Principal Financial continues to benefit from its strength and leadership in retirement and long-term savings, group benefits and protection in the United States, retirement and long-term savings in Latin America and Asia plus global asset management, which help it deliver solid operating earnings. Continued growth in fee, spread and risk businesses boost the company's long-term prospects. However, with the pandemic affecting employment and contributions to employee benefit plans among others, the company estimates growth in group benefits premiums and retirement recurring deposits to be adversely impacted in the rest of 2020, thus weighing on earnings.
- ▲ Principal Financial's AUM is driven by three asset management and asset accumulation segments. AUM as of Jun 30, 2020 was a record \$701.8 billion, up 0.8% year over year, driven by favorable market performance as well as positive net cash flow. Net cash inflow was \$9 billion in the first half of 2020. Further, Principal International generated \$900 million of net cash flow, marking the 47th consecutive positive quarter, of positive cash flow driven by positive flows in Mexico, Chile, Hong Kong and Brazil. We continue to believe that AUM growth will be supported by the company's extensive distribution footprint, best-in-class solutions, strategic buyouts and operational discipline.
- ▲ Investment results at Principal Financial improved in the last five years with the metric rising nearly 31%. However, the same declined 3.5% in the first half of 2020. Also, the company witnessed about \$115 million impact from credit drift and credit losses, with more than \$80 million in the second quarter. Nonetheless, Principal Financial estimates about \$300 million to \$500 million of credit drift and credit losses in 2020, lower than \$400 million to \$800 million expected earlier and believes the losses are manageable, given its superior portfolio quality and sturdy capital position.
- ▲ In order to grow inorganically, management utilizes a significant portion of its operating earnings for mergers and acquisitions and intends to continue to do so. Acquisitions, such as MetLife's Afore business, Internos (known as Principal Real Estate Europe presently), and RobustWealth have helped the company add to its fee-based businesses and expand its global footprint. Its buyout of Wells Fargo Institutional Retirement and Trust businesses on Jul 1, 2019 is expected to generate \$425 million of run-rate revenues, once fully integrated in 2022.
- ▲ Principal Financial boasts a strong capital position, with sufficient cash generation capabilities and liquidity. The company had \$3 billion in cash and liquid assets as well as access to \$800 million of revolving credit facilities available for liquidity purposes at second-quarter 2020 end. Along with over \$2.3 billion of excess and available capital, the company also had access to a contingent capital facility, allowing it to borrow up to \$1 billion, from which Principal Financial aims at least \$800 million to be able to meet the next 12 months of obligations. The company noted average debt service coverage ratio of 2.6. The next debt maturity of \$300 million is scheduled in 2022.
- ▲ Principal Financial's capital deployment through share buybacks and dividend payment look impressive, making it an attractive pick for yield-seeking investors. The 1.8% hike in dividend in January 2020 marked the 13th straight year dividend increases by the company. The company also boasts a solid dividend yield of 5.1%, higher than the industry average of 3.2%. Though the company had \$850 million remaining under its share repurchase authorization, it refrained from share buybacks due to the pandemic. The company estimates capital deployments in 2020 to be in the range of \$800 million to \$1 billion.

Focus on fee-based revenue sources, improving assets under management, spread and risk businesses have been helping Principal Financial earn steadily, besides limiting exposure to low interest rate.

Risks

- Principal Financial's expenses have been increasing since 2013, due to rise in benefits, claims and settlement expenses as well as operating expenses. In the first half of 2020, expenses increased 1.5% year over year. An increase in expenses weighs on its margins. Net margin contracted 120 basis points through 2013-2019 period. It further contracted 310 basis points (bps) in the first quarter and 170 bps in second quarter of 2020. Nonetheless, the company has been undertaking efforts to lower expenses and expects to lower 2020 expenses by \$225 million to \$275 million.
 - Given the low interest rate environment, the company has been experiencing slowdown in its pension risk transfer pipeline. The company expects the same to continue as it anticipates lower annuity sales for the remainder of the year.
 - Principal Financial has been growing inorganically through acquisitions, which increase its debt obligation risks associated with successful integration. In addition, lower-than-expected earnings accretion from the acquisitions might weigh on overall results. Given RobustWealth's acquisition (in Jul 2018), the company expects the transaction to be slightly dilutive for the next several quarters as it continues to expand its investment in the business.
 - Return on equity, a profitability measure, reflecting how effectively the company is utilizing its shareholders fund is lower than the industry average. The company's return on equity is 10.8%, lower than the industry average of 11.1% as well as its year-ago number of 12.4%.
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Last Earnings Report

Principal Financial Q2 Earnings Beat, Revenues Lag

Principal Financial's second-quarter 2020 operating net income of \$1.46 per share beat the Zacks Consensus Estimate by 11.5%. However, the bottom line decreased 3.9% year over year.

Principal Financial witnessed lower revenues across most of its business lines, offset by lower expenses.

Behind the Headlines

Operating revenues decreased 20.5% year over year to nearly \$3.2 billion, primarily due to lower premiums and other considerations, and net investment income. The top line missed the Zacks Consensus Estimate by nearly 17%.

Total expenses decreased 25.7% year over year to \$2.6 billion due to lower benefits, claims and settlement expenses as well as reduced operating expenses.

Principal Financial's AUM as of Jun 30, 2020 was a record \$701.8 billion, up 0.8% year over year.

Segment Update

Retirement and Income Solution: Revenues decreased 31.5% year over year to about \$1.5 billion.

Pretax operating earnings decreased 16.5% year over year to \$213.9 million on account of poor performance at Retirement and Income Solution — Fee as well as Spread business.

Principal Global Investors: Revenues of \$352.9 million were down 1.8% from the prior-year quarter.

Operating earnings declined 6.2% year over year to \$108.4 million primarily due to lower transaction and borrower fees, and higher sales compensation, partially offset by lower operating expenses.

Principal International: Revenues decreased 32.8% year over year to \$276.4 million in the quarter.

Operating earnings increased 1.4% year over year to \$94.5 million primarily due to more favorable encaje performance, partially offset by foreign currency translation headwinds.

U.S. Insurance Solution: Revenues grew 0.1% year over year to \$1.1 billion.

Operating earnings of \$155 million increased 5.9% year over year, driven by strong performance at the Specialty Benefits Insurance business.

Corporate: Operating loss of \$84 million was narrower than \$98.1 million loss incurred a year ago, primarily due to expense management actions.

Financial Update

As of Jun 30, 2020, cash and cash equivalents were \$3.1 billion, down 5% year over year.

At second-quarter end, debt was \$4.2 billion, up 10.6% year over year.

As of Jun 30, 2020, book value per share (excluding AOCI other than foreign currency translation adjustment) was \$44.47, up 1.6% year over year.

Capital Deployment

Principal Financial paid out \$153.5 million in dividends.

The board of directors approved third-quarter dividend of 56 cents per share, up 3% year over year.

Quarter Ending 06/2020

Report Date	Jul 27, 2020
Sales Surprise	-16.98%
EPS Surprise	11.45%
Quarterly EPS	1.46
Annual EPS (TTM)	5.25

Recent News

Principal Financial's Unit Launches Tax-Advantaged Active ETF - Jun 16, 2020

Principal Financial Group, Inc.'s unit Principal Global Investors has unveiled the Principal Spectrum Tax-Advantaged Dividend Active ETF (PQDI), which will enable investors to get access to qualified dividend income. The fund invests in securities from all sectors of the global U.S. dollar capital securities market.

Valuation

Principal Financial shares are down 20.3% in the year-to-date period and 24.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 1.4% and 17.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 3.2% but down 11.9%, respectively.

The S&P 500 index is up 0.12% in the year-to-date period and 8.4% in the past year.

The stock is currently trading at 7.72x forward 12-month earnings, which compares to 13.17x for the Zacks sub-industry, 16.31x for the Zacks sector and 22.44x for the S&P 500 index.

Over the past five years, the stock has traded as high as 13.69x and as low as 4.1x, with a 5-year median of 9.81x. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$50 price target reflects 8.8x forward 12-month earnings.

The table below shows summary valuation data for PFG

Valuation Multiples -PFG					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	7.72	13.17	16.31	22.44
	5-Year High	13.69	14.35	16.31	22.44
	5-Year Low	4.1	9.75	11.59	15.25
	5-Year Median	9.81	12.35	14.16	17.52
P/S F12M	Current	0.69	3.79	6.04	3.54
	5-Year High	1.53	3.79	6.66	3.54
	5-Year Low	0.38	2.3	4.96	2.53
	5-Year Median	1.1	2.98	6.06	3.02
P/B TTM	Current	0.93	2.07	2.4	4.46
	5-Year High	1.79	2.2	2.91	4.56
	5-Year Low	0.46	0.96	1.72	2.83
	5-Year Median	1.31	1.75	2.53	3.71

As of 07/29/2020

Industry Analysis Zacks Industry Rank: Top 15% (38 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Franklin Resources, Inc. (BEN)	Outperform	1
Invesco Ltd. (IVZ)	Outperform	3
T. Rowe Price Group, Inc. (TROW)	Outperform	1
Ameriprise Financial, Inc. (AMP)	Neutral	3
Ares Management L.P. (ARES)	Neutral	3
Grupo Aval Acciones y Valores S.A. (AVAL)	Neutral	3
BlackRock, Inc. (BLK)	Neutral	3
Blackstone Group IncThe (BX)	Neutral	3

Industry Comparison Industry: Financial - Investment Management				Industry Peers		
	PFG	X Industry	S&P 500	AMP	ARES	BLK
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	1	-	-	3	3	3
VGM Score	A	-	-	A	F	D
Market Cap	12.02 B	901.54 M	22.69 B	19.20 B	10.02 B	89.10 B
# of Analysts	4	3	14	2	5	6
Dividend Yield	5.11%	2.31%	1.8%	2.65%	3.95%	2.51%
Value Score	A	-	-	A	D	D
Cash/Price	0.33	0.18	0.07	0.46	0.17	0.05
EV/EBITDA	5.28	6.32	13.11	4.27	12.98	16.48
PEG Ratio	1.66	1.65	3.05	NA	3.51	1.98
Price/Book (P/B)	0.78	1.57	3.15	2.88	5.97	2.69
Price/Cash Flow (P/CF)	5.62	8.42	12.28	8.65	19.96	18.24
P/E (F1)	7.79	10.57	22.27	9.63	24.37	19.76
Price/Sales (P/S)	0.74	1.84	2.46	1.56	7.70	5.93
Earnings Yield	12.42%	9.43%	4.25%	10.39%	4.10%	5.06%
Debt/Equity	0.27	0.21	0.75	0.56	0.75	0.63
Cash Flow (\$/share)	7.81	1.89	6.94	18.13	2.03	31.67
Growth Score	C	-	-	B	F	F
Hist. EPS Growth (3-5 yrs)	6.99%	8.17%	10.85%	16.99%	14.72%	11.24%
Proj. EPS Growth (F1/F0)	-2.28%	-7.30%	-7.70%	1.24%	-0.60%	2.65%
Curr. Cash Flow Growth	4.20%	-4.66%	5.31%	-1.33%	-37.87%	6.72%
Hist. Cash Flow Growth (3-5 yrs)	3.17%	3.83%	8.55%	4.37%	-3.84%	6.05%
Current Ratio	0.09	2.42	1.31	0.86	0.23	4.08
Debt/Capital	22.47%	26.30%	44.23%	35.72%	38.79%	40.11%
Net Margin	7.82%	8.86%	10.45%	20.32%	5.60%	29.55%
Return on Equity	10.12%	12.39%	14.99%	34.99%	15.52%	14.14%
Sales/Assets	0.06	0.35	0.53	0.08	0.11	0.09
Proj. Sales Growth (F1/F0)	5.87%	0.00%	-1.97%	-6.18%	4.39%	4.31%
Momentum Score	A	-	-	F	C	A
Daily Price Chg	1.02%	0.40%	1.52%	1.86%	2.38%	1.21%
1 Week Price Chg	0.58%	0.00%	0.37%	1.23%	-3.82%	-2.91%
4 Week Price Chg	9.25%	1.38%	5.44%	7.60%	2.35%	6.11%
12 Week Price Chg	29.20%	15.26%	15.38%	46.26%	15.60%	19.49%
52 Week Price Chg	-24.41%	-15.66%	-1.61%	7.83%	38.33%	23.50%
20 Day Average Volume	1,355,929	91,670	1,846,377	652,232	612,122	589,558
(F1) EPS Est 1 week change	4.35%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	7.65%	0.24%	0.27%	-2.25%	0.24%	9.41%
(F1) EPS Est 12 week change	9.27%	4.07%	-0.85%	3.82%	4.01%	14.88%
(Q1) EPS Est Mthly Chg	10.84%	1.63%	0.13%	1.63%	0.00%	5.31%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	C
Momentum Score	A
VGM Score	A

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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