

Principal Financial Group - Where Should the Next Dollar Go?

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Decision date and information cutoff: 21 February 2021, 8:00 p.m. ET

Decision scope: Portfolio priorities and capital deployment across PFG's existing businesses

Case convention: This is an author-created board decision exercise. The alternatives are hypothetical; company disclosures are historical. No private board proposal or deliberation is represented.

The decision

Principal Financial Group (PFG) entered 2021 with a broad financial-services portfolio and a difficult allocation question. In 2020, company-defined operating earnings fell while total assets under management and net cash flows reached records. Results varied sharply across retirement, asset management, international retirement and investment, and U.S. insurance. PFG also reported a substantial capital cushion, while facing low interest rates, market uncertainty and COVID-related claims. [S1], Items 1, 7 and 8; [S2], full-year highlights and segment tables.

For this classroom exercise, assume you advise PFG's board on 21 February 2021. The board asks how to set portfolio priorities and deploy capital over the next planning cycle. Should PFG preserve its broad model and invest across the businesses, concentrate additional investment in fee-oriented retirement and asset management, reduce exposure to selected U.S. retail insurance products, or increase shareholder distributions? A combination is possible, but the board wants explicit priorities and conditions.

The cited public disclosures do not identify a specific transaction or budget proposal at the cutoff. This assignment is hypothetical. Use only information available by 8:00 p.m. ET on 21 February 2021. Do not assume a business has a particular standalone value or that the company can deploy all reported capital without legal-entity, regulatory, rating or liquidity constraints.

A portfolio of different businesses

PFG served individuals, employers, institutions and intermediaries through several businesses. Retirement and Income Solutions (RIS) included fee-based recordkeeping and administration as well as spread-based retirement products. Principal Global Investors (PGI) managed investment products and client assets. Principal International (PI) served retirement and investment markets outside the United States. U.S. insurance included Specialty Benefits and Individual Life. These businesses did not have interchangeable revenue, risk or capital profiles. [S1], Item 1, "Business," and Item 7, segment discussions.

The portfolio had recently expanded in retirement services. PFG acquired Wells Fargo's Institutional Retirement & Trust business (IRT) for \$1.2 billion in cash, plus an earn-out of up to \$150 million tied to revenue retention through 31 December 2020. The acquisition closed on 1 July 2019. [S3], acquisition announcement; [S1], Item 8, acquisition note. In January 2021, management said final customer migrations remained underway. [S2], CEO remarks. The acquisition demonstrated prior willingness to invest for platform scale, but its purchase price and the subsequent growth of the combined business do not by themselves establish the investment's return.

PFG described its diversification and capital position as sources of resilience. The board could ask whether different businesses truly shared customers, distribution, data or investment capabilities-or whether diversification mainly made a complex portfolio harder to govern. [S2], management commentary. The available disclosures did not quantify profitable cross-selling among all the businesses.

A mixed year

PFG reported 2020 GAAP net income attributable to the company of \$1.396 billion, nearly unchanged from 2019. Non-GAAP operating earnings were \$1.366 billion, down from \$1.569 billion. The company's operating measure excludes adjusted net realized capital gains and losses and certain after-tax items; PFG cautioned that some adjustments can recur. Neither measure alone resolves whether 2020 represented a temporary shock or a change in the portfolio's earning power. [S2], "Principal Financial Group, Inc. Results" and non-GAAP reconciliation.

Exhibit 1. Selected 2020 company and segment measures

USD millions unless noted. Segment figures are company-defined pre-tax operating earnings. They are not directly comparable returns on invested or statutory capital.

Business / measure	2020	2019	Change / context
GAAP net income attributable to PFG	\$1,395.8	\$1,394.2	Broadly level
Non-GAAP operating earnings	\$1,366.4	\$1,569.1	Down 13%
Total company AUM	\$806.6bn	-	Record; includes \$13.7bn net cash flow in 2020
RIS-Fee operating earnings	\$456.3	-	Down 1%; net revenue \$1,987.7, up 13%; pre-tax return on net revenue 23.0% vs 26.3%
RIS-Spread operating earnings	\$510.6	-	Up 24%; net revenue \$664.8, up 8%; pre-tax return on net revenue 76.8% vs 66.8%
PGI operating earnings	\$512.9	-	Up 6%; \$5.6bn sourced net cash flow; \$502.1bn managed AUM
PI operating earnings	\$243.6	-	Down 38%; net revenue at PFG share \$826.6, down 18%; net cash flow \$4.2bn

Business / measure	2020	2019	Change / context
Specialty Benefits operating earnings	\$292.3	-	Down 17%; premiums and fees \$2,364.8, up 2%; pre-tax return on premiums and fees 12.4% vs 15.1%
Individual Life operating earnings (loss)	\$(52.4)	\$169.4	Premiums and fees \$1,227.5 vs \$1,245.0

Source: [S2], “Full Year 2020” highlights, PFG results and segment tables. Percentages are company-reported or calculated from reported values as described in the release. RIS-Fee and RIS-Spread returns use different revenue bases; none is a capital return. Company AUM includes client assets managed or administered and is not corporate capital. PGI managed AUM is a separate measure. PI’s reported \$165.2bn AUM excludes \$118.4bn of China AUM; do not add unlike scopes. Segment comparisons reflect differing markets, acquisitions, currencies and product economics.

The detail offers competing readings. RIS-Fee revenue grew while its operating earnings were slightly lower. RIS-Spread earnings rose, but spread economics were exposed to investment income, reserves and rates. PGI’s earnings and cash flows were positive, though AUM can rise with markets and does not equal fee revenue or profit. PI combined positive flows with a marked earnings decline; management cited currency, inflation in Brazil and “encaje” performance among influences on results. Specialty Benefits experienced weaker earnings during a year of COVID-related claims and other experience. Individual Life reported a loss even as PFG highlighted strong term sales. [S2], segment tables and management explanations.

These figures do not identify which products earned attractive risk-adjusted returns. They also do not isolate the effects of pandemic claims, market movements, foreign exchange, acquisition timing or accounting differences. A board choosing among businesses would need more than a ranking of reported annual earnings.

Capital and competing uses

At year-end, PFG reported \$2.9 billion of “excess and available capital” in holding companies and other subsidiaries and estimated Principal Life statutory risk-based capital (RBC) at 440%, above a 400% target. In 2020, PFG deployed \$907.3 million to shareholders: \$614.5 million in dividends and \$292.8 million to repurchase 5.7 million shares. It restarted repurchases in the fourth quarter with \$75 million and announced a \$0.56-per-share first-quarter 2021 dividend. [S2], “Continued strong financial position” and company highlights.

The \$2.9 billion was a company-reported estimate, not necessarily unrestricted parent cash. Statutory RBC is not GAAP equity; capital is held in legal entities subject to regulatory and rating considerations. Low interest rates, market volatility, credit spreads, product guarantees, customer behavior, COVID-19 and insurer dividend restrictions all mattered to capital resilience. [S1], Item 1A, risk factors, and Item 7, liquidity and capital resources. The board therefore faced a choice among growth investment, preserving flexibility, reducing risk exposure and returning capital—not a simple allocation of a fully fungible cash balance.

Exhibit 2. The board's alternatives

Direction	Strategic case for it	Questions and risks to resolve
Preserve breadth; invest selectively	Maintain access across employer, institutional, intermediary and individual channels; keep potential diversification and customer-service benefits.	What evidence shows shared relationships or capabilities create value? How should leaders compare unlike segment requests?
Concentrate investment in fee-oriented businesses	RIS-Fee and PGI had scale, positive revenue/flow signals and less direct spread exposure than some insurance products.	Are flows durable and profitable? What capital, technology and integration costs are required? Does the evidence support shifting resources away from other businesses?
Reduce selected U.S. retail insurance exposure	Product run-off, reinsurance or sale could reduce rate-sensitive guarantees and focus management attention.	Which products and obligations are involved? What are the block's risk-adjusted economics, transaction price, policyholder effects and retained liabilities? No product-level exit valuation is supplied.
Return more capital to shareholders	Dividends and repurchases provide a direct use for capital when incremental projects do not clear a disciplined hurdle.	What capital buffer is needed under adverse scenarios? How much is actually distributable? Would a larger payout foreclose attractive investment or resilience?

These are directions, not mutually exclusive announced plans. A staged policy could set common return and risk hurdles, fund limited commitments, and delay irreversible choices pending product-level evidence. Whether that is prudent discipline or costly indecision is for the board to judge.

Assignment

Prepare a board memo recommending a portfolio and capital-allocation direction for the next planning cycle. State which activities should receive incremental attention, which should maintain or reduce exposure, and how much capital should be retained versus distributed. You may recommend a staged decision or combine alternatives, but explain the sequence and decision rules. Identify the evidence you would require before approving a sale, reinsurance transaction, material new investment or payout increase. State what would make you change your recommendation.

Discussion questions

1. What does the 2020 evidence say about PFG's portfolio-and what can't it establish?
2. Which potential scope benefits are plausible across PFG's businesses? What evidence would distinguish them from management's broad diversification claim?
3. Should the board favor fee-oriented growth, reduce selected insurance exposure, preserve breadth, or return more capital? What is the strongest counterargument?
4. How should PFG compare unlike segment earnings, client flows, risk capital and strategic options on a common basis?
5. What information and governance safeguards should be required before an irreversible portfolio action?

Sources and conventions

S1. Principal Financial Group, [2020 Form 10-K](#), year ended 31 December 2020; SEC accession 0001104659-21-022074, accepted 12 February 2021, 5:00:44 p.m. ET. Relevant sections: Item 1, Business; Item 1A, Risk Factors; Item 7, MD&A and Liquidity and Capital Resources; Item 8, audited statements and notes.

S2. Principal Financial Group, [Fourth Quarter and Full Year 2020 Results](#), 28 January 2021. Segment tables, full-year highlights, capital position and non-GAAP reconciliation.

S3. Principal Financial Group, [announces agreement to acquire Wells Fargo Institutional Retirement & Trust](#), 9 April 2019. Transaction scope and announced terms; closing and accounting cross-checked to S1.

All amounts are historical reported figures unless marked otherwise. USD shown. "Operating earnings" refers to PFG's non-GAAP measure or segment pre-tax operating earnings as explicitly labeled. No later event or outcome is included.