MOODY'S
RATING

Credit strengths

» Established market positions in the high-end life insurance markets;

» Broad and balanced independent distribution;

» Good capitalization with a NAIC company action level (CAL) Risk-Based Capital (RBC) ratio of 508% as of year-end 2023.

Credit challenges

» Managing volatility in capital and earnings from capital market movements, especially interest rates;

» Strong competition in core affluent business and professional life insurance markets;

» Above-average exposure to Baa-rated bonds (46% of total bonds as of YE 2023).

Outlook

The outlook on Pacific Life is stable, reflecting strong market position, very good statutory capitalization and a commitment to its mutual philosophy (i.e., focus on policyholder value). Going forward, items to watch for include new business sales as well as the uncertainty in the commercial real estate assets, especially tied to office sub-sector.

Factors that could lead to an upgrade

» Reduced capital and earnings sensitivity to capital market movements;

» GAAP return on capital consistently greater than 8%;

» Financial leverage below 15% (excluding AOCI); and

» Earnings coverage consistently above 8x.

Factors that could lead to a downgrade

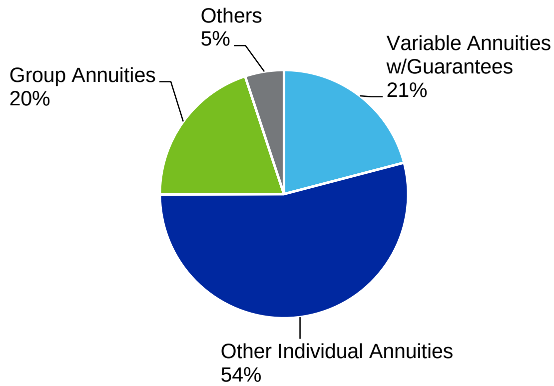
» NAIC company action level RBC ratio falls below 400% (adjusting for captives) and/or lack of organic statutory capital generation;

» GAAP return on capital less than 6%;

» Financial leverage greater than 20% (excluding AOCI); or

» Earnings coverage below 6x.

Statutory revenues by segment shows a diversified business profile
for full-year 2023



Source: Company statutory statements

Detailed credit considerations

Moody's rates Pacific Life Aa3 for insurance financial strength, which is in line with the adjusted scorecard-indicated outcome.

Insurance financial strength

The key factors currently influencing the rating and outlook are:

Market position and brand: Focus on the high-end life insurance and recent product expansions to grow market share

Moody's views Pacific Life's market position and brand as being very strong. The Aa-adjusted score for the company's market position, which is adjusted upward from the unadjusted scorecard score of A, is supported by a strong, focused position in the high-end life insurance market serving the very affluent and businesses. The company holds an often-leading market share in most of the products it sells, including individual life insurance, structured settlements, and annuities. Within its US individual life business, Pacific Life is a top 5 provider of universal life insurance, which includes indexed universal life and variable universal life and within annuities, it holds a top 10 ranking, according to LIMRA. The company, like many of its peers, has benefited from higher interest rates which has driven its annuity sales growth, especially retail fixed annuities. The adjusted score for this factor also reflects Pacific Life's market position internationally, including the UK and Ireland, where it sells life protection and longevity type products and in Australia and Asia, where they market protection and critical illness products.

Distribution: Primarily independent distribution network, but strong relationships with core partners

Pacific Life relies primarily upon a wide variety of third parties such as independent agents, financial advisors, banks and registered representatives for its insurance product distribution. As a result, the company maintains less direct control over its distribution and could see relatively lower persistency and more volatile sales for its third-party sold products than those companies with more control over their distribution systems. However, it benefits from a strong market breadth in most major channels other than career agents, resulting in an A score for diversity of distribution. The company has had long-standing relationships with many key independent distributors, and a reputation for excellent customer service that benefits the company in the market, increasing its sustainability in the independent channels. We have therefore left this factor unchanged, which is the same as the unadjusted scorecard result of A.

Product focus and diversification: Measured approach to diversification reduces overall product risk

Pacific Life has a very diverse set of product offerings in life and annuity markets, including fixed and variable products, as well as institutionally oriented products. The product diversification also benefits from Pacific Life Re, its international, reinsurance and life retrocession operations. In the US, Pacific Life is particularly strong in serving the high net worth life insurance market and benefits from very strong persistency on its products. The middle-market segment helps improve the overall product risk profile (primarily term life insurance products) and creates opportunities to expands its customer base and cross-sell other insurance products, especially through other channels, such as BGAs and direct marketers.

We also believe Pacific Life benefits from a good balance between fixed and variable products, a partial result of its emphasis on risk management and diversification - including growing its institutional business, which has very little sensitivity to equity markets. Since virtually all of the life insurance business is of the nonparticipating variety, which limits its ability to share adverse experience with its policyholders and restricts upward movement for this rating factor, Moody's views Pacific Life's product focus and diversification score to be in-line with the unadjusted score and hence left this factor score unchanged at A.

Asset Quality: Good quality investment portfolio, although high exposure to certain assets, such as mortgage loans and Baa-rated bonds

Pacific Life's general account investment portfolio is diversified and consists primarily of fixed-income securities and commercial mortgages (14% of cash and invested assets). As of the end of 2023, Pacific Life's ratio of high-risk assets as a percentage of shareholders' equity (ex AOCI) was 106%, consistent with a Baa sub-factor score, which primarily emanates from its holdings in below-investment grade bonds, alternative investments, and real estate. We do note that included in high-risk assets are investments related to working capital finance that are primarily investment grade and amounted to $1138 billion as of year-end 2023. We also note that nearly half of Pacific Life's total bonds are rated in the Baa range, which is higher than its peers and could be a source of additional losses in a downturn. In fact, under the baseline scenario, Moody's projects a global speculative grade default rate of 2.8% by May 2025. Under a moderate pessimistic scenario, it reaches 5.1% and under a severe pessimistic scenario it reaches 8.5%.

The company does hold about 15% of total investments in commercial mortgages, with 20% invested in the office sub-sector. Pacific has faced losses on its commercial mortgages in 2024, especially those tied to shopping malls in certain geographies, such as California. We will continue to see some negative pressure on this portfolio which could weaken earnings over the next 12-18 months, although we believe that it will not result in any major calls on capital and will largely be an earnings impact. Although continued deterioration in their holdings can result in a reduction in RBC ratio, its RBC ratio remains strong as of Q2 2024. At year-end 2023, goodwill and other intangibles amounted to 52% of shareholders' equity (ex AOCI), consistent with a Baa score. Looking at the numerator of the metric - we view deferred acquisition costs (DAC), which represents all of the intangibles, as higher quality than goodwill, largely because of the greater likelihood that DAC will eventually be converted into tangible equity, as profits net of DAC amortization flow through income, given the generally consistent policyholder persistency. Despite some of the pressure on asset quality, overall, we view the asset quality to be thus better than the unadjusted score and hence raise the adjusted score for this factor to the A-level.

Capital Adequacy: Very good RBC ratio, but can exhibit volatility from interest rate moves

Pacific Life has very good capital adequacy despite a modest score of 3.8% for shareholders' equity as a percentage of total assets as of year-end 2023, which is impacted by its negative AOCI balance resulting from the rise in interest rates. To assess the capital adequacy of US life insurers' we consider the RBC ratio to be a more reliable measure of capital adequacy. Pacific Life's RBC ratio is strong at 508% as of year-end 2023. It is our expectation that the company will continue to maintain strong RBC ratios going forward, including generating organic capital, which provides a cushion against tail risk events and is a key factor supporting Pacific Life current ratings. We do note that although Pacific Life has taken prudent risk management steps to protect capital in times of stress, its RBC ratio may exhibit some volatility in response to capital market movements, especially from interest rates movements and elevated volatility - although the company has added incremental hedges to protect against this volatility in recent years. As a result, we believe that Pacific Life is best positioned in the Aa range on this factor, given its very good level of reported capital and RBC ratio, somewhat offset by its sensitivity to capital market changes.

Profitability: Diversified earnings, but sensitivity to capital market movements

Moody's views Pacific Life's profitability to be good and benefits from increasing diversification. As of year-end 2023, the company reported very good profitability with a return on average capital (ex AOCI) ratio of 4.9%, which benefitted from a higher net profit in the year. Net income rose in 2023 compared to 2022 as a result of greater net investment income from fixed income maturities and good business growth. Earnings still remain sensitive to equity market movement, particularly in the annuity business, but they are incrementally less so than in the past, particularly as the company implemented newer hedging strategies in recent years and as the older block of guarantees shrinks as newer, more diversified business comes onto the balance sheet. Although we expect the mortality impact to continue to improve in 2024 (as the pandemic is now endemic), the elevated market volatility can lower fee income and impact certain businesses, such as annuities, whose earnings are sensitive to capital markets. Despite that, we have adjusted the score on this factor up to A from the unadjusted scorecard result of Baa, because we believe Pacific Life is well positioned to navigate the market volatility from a risk management and capital perspective.

Liquidity and Asset/Liability Management (ALM): Generally stable liability profile, but VA adds ALM risk

Moody's believes that Pacific Life has excellent liquidity to meet its near-term policyholder obligations based on the unadjusted

In June 2021, Pacific Life amended and extended two existing revolving credit facilities for Pacific LifeCorp and Pacific Life Insurance Company into a single unified $1 billion five year co-borrowed revolving credit facility (RCF) maturing June 2026. The unified RCF replaced standalone five-year revolving credit facilities of $600 million and $400 million for Pacific LifeCorp and Pacific Life Insurance Company, respectively. There were no amounts outstanding as of December 31, 2023 and the facilities contain no material adverse change clauses.

As of December 31, 2023, the company held approximately $761 million in cash and liquid investments at the holding company. Pacific Life's statutory dividend capacity in 2023 is $746 million without requiring special regulatory approval. Total cash needs at the holding company in 2022 include $103 million of interest expense. The company has $567 million in senior notes coming due in 2033 and then no further maturities until 2039.

ESG considerations

Pacific Mutual Holding Company's ESG credit impact score is CIS-2

ESG credit impact score

Support and structural considerations

Rating methodology and scorecard factors

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Rating Factors

Financial Strength Rating Scorecard [1][2]	Aaa	Aa	A	Baa	Ba	B	Caa	Score	Adj Score
$									
Market Position and Brand (15%)									
- t t t									
Distribution (10%)									
- t b t t									
- t t b t									
Product Focus and Diversification (10%)									
- t									
- t t									
Asset Quality (10%)								$	
- t t			1						
- t b t				1					
Capital Adequacy (15%)								$	
- t t t									
Profitability (15%)								$	
- t p t									
- p t									
Liquidity and Asset/Liability Management (10%)									
- t b t									
Financial Flexibility (15%)									
-		1							
- t		1							
-									
-	1								
p t t								-	-
t t									

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t t t t t b t t b p t t t

Source: Moody's Rating's

Ratings

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Category	Moody's Rating
PACIFIC LIFECORP	
t t	
PACIFIC LIFE INSURANCE COMPANY	
t t	
t t	
t t	-1
p t	b
p	-1
PACIFIC LIFE & ANNUITY COMPANY	
t t	
t t	
PACIFIC LIFE GLOBAL FUNDING II	
t t	

Source: Moody's Ratings