



# STANDISH



## Pacific Life Insurance Company

Pacific Life & Annuity Company

**RATING:** Q1  
**Other Ratings as of:** December 2008  
**Moody's:** Aa3  
**S & P:** AA  
**Best:** A++

**State of Domicile:** Nebraska  
**Holding Company:** Pacific Mutual Holding Co.  
**Type:** Mutual Holding Company  
**Incorporated:** 1868

Pacific Life & Annuity Company (PL&A) is a subsidiary of Pacific Life Insurance Company (Pacific Life), which is a subsidiary of intermediate stock holding company, Pacific LifeCorp. Eventually all of these legal entities roll up to Pacific Mutual Holding Company. Pacific Life is one of the few companies in the Standish Stable Value Universe that maintains a mutual holding company ownership structure. In this manner, the majority of the company remains under policyholder ownership, but it allows the parent holding company to tap the equity markets if necessary.

Established in 1868, Pacific Life provides life insurance products, annuities, mutual funds and a variety of institutional investment products. Its much smaller subsidiary, PL&A, focuses on writing life and annuity business in the state of New York. On April 27, 2005, Pacific Life completed the sale of the PL&A group health insurance business to PacifiCare. Pacific Life has recently converted to a Nebraska domicile from its previous California domicile to benefit from reduced premium taxes in many jurisdictions. Standish consolidates the financial statements of both Pacific Life and PL&A in our analysis due to their closely integrated operations.

Pacific Life achieved leading market positions in its core products in 2006; ranking 9th in total life insurance sales in the US, generating \$10.7 billion in variable annuity sales, and its investment management division had \$16.2 billion assets under management. The company also seeks growth and profitability through various other lines of business. One of the company's affiliated entities, Aviation Capital Group (ACG), offers commercial aircraft leasing and management services. In June 2005, ACG acquired Boullion Aviation Services from WestLB AG for approximately \$2.65 billion. With this addition, ACG became a top five operating lessor and increased its portfolio of aircraft owned or under management to over 220 aircraft with a value of over \$5 billion. In mid-2002 the insurer purchased College Savings Bank, providing an entry into the 529 college savings plan market. In early 2008, Pacific Life sold its remaining interest in Pacific Investment Management Company (PIMCO) to Allianz SE.

The Pacific Life companies experienced a 6.9% drop in premiums in 2007, yet the company was able to increase its statutory earnings to \$356 million, up from \$322 million in 2006. The equity and assets of the company grew faster than the earnings, putting a downward pressure on the company's operating ratios. The return on assets and the return on equity fell to 0.91% and 9.51%, respectively from 2006 when they were 0.95% and 10.59%, respectively. These ratios compare adequately to our peer group averages of 0.90% and 11.91%, respectively. Over 75% of the premiums generated by

the Pacific Life companies came from sales of individual annuities, with the remaining premium coming primarily from individual life policies (20%).

In its investment portfolio, the Pacific Life companies had the most significant portion of its invested assets in bonds (77.0%) and commercial mortgages (13.8%). The overall quality of the bond portfolio continued its trend of improving by lowering its exposure to below-investment grade bonds to 3.2%, down from 3.5% in 2006, and better than our peer group average of 5.2%. Besides cash investments and an average allocation to preferred stock holdings (1.8% of invested assets), the Pacific Life companies also invested in alternative investments. These riskier, less liquid assets, which include holdings in limited partnerships and hedge fund investments, grew to 4.4% of invested assets, up from 3.9% in 2006.

At the end of 2007, the Pacific Life companies' capital and surplus totaled an impressive \$3.9 billion, supporting their \$41.1 billion in general account assets. The companies combined for a risk-adjusted surplus ratio of 275.4%, which compared very favorably to our universe average of 163.4%. In early 2008, the Pacific Life companies' sold their interest in Pacific Investment Management Company (PIMCO) to Allianz. The additional capital created by this move will further strengthen the companies' financial position.

The firms have significant liquidity sources with which to tap in times of need. These include a bank credit facility totaling \$400 million, a \$700 million commercial paper program and a line with a Federal Home Loan Bank. The Pacific Life companies also generate a moderate amount of net cash from operations: \$900 million in 2007, up from \$483 million in 2006. On the liability side, the companies have a very low exposure to potential annuity surrender and they issued \$100 million of debt in 2007.

The Pacific Life companies continue to have strong capitalization and liquidity, a relatively conservative investment portfolio, and leading market positions in core products. The firms have also focused on growth with respect to breadth and depth of product offerings, distribution and geographic reach. We believe that the Pacific Life companies deserve our highest credit rating of Q1.

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### Strengths:

- Continued expansion of product offerings, distribution and geographic reach
- Strong cash flows over the past five years, averaging \$1.6 billion per year
- Significant capital and surplus position
- Substantial hidden surplus through residual ownership of PIMCO stake

### Weaknesses:

- Significant sensitivity to performance of equity markets as revenue from variable annuity business is directly tied to the market value of assets under management
- Above average use of less liquid, privately placed bonds

### Key Statistics — Pacific Life Insurance Company

| (\$ millions)               | 2007   | 2006   | 2005   | 2004   | 2003   | CAGR/<br>Average |
|-----------------------------|--------|--------|--------|--------|--------|------------------|
| General Account Assets      | 39,885 | 37,802 | 37,305 | 36,711 | 34,671 | 3.56%            |
| Separate Account Assets     | 56,666 | 48,340 | 37,581 | 31,756 | 24,996 | 22.71%           |
| Total Assets                | 96,551 | 86,142 | 74,886 | 68,467 | 59,667 | 12.79%           |
| Capital and Surplus         | 3,558  | 3,068  | 2,859  | 2,665  | 2,209  | 12.66%           |
| Net GFO                     | 350    | 317    | 200    | 597    | 380    | -2.08%           |
| Net Income                  | 362    | 362    | 234    | 508    | 277    | 6.92%            |
| Return on Assets (Stat.)    | 0.93%  | 0.96%  | 0.63%  | 1.42%  | 0.83%  | 0.96%            |
| Return on Equity (Stat.)    | 10.46% | 11.63% | 8.05%  | 19.63% | 13.76% | 12.71%           |
| Risk Adjusted Surplus Ratio | 259.6% | 244.9% | 225.1% | 189.7% | 168.7% | 217.6%           |

## Pacific Life Insurance Company

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### Key Statistics — Pacific Life and Annuity Company

| (\$ millions)               | 2007   | 2006   | 2005   | 2004   | 2003   | CAGR/<br>Average |
|-----------------------------|--------|--------|--------|--------|--------|------------------|
| General Account Assets      | 1,234  | 1,070  | 1,015  | 1,004  | 989    | 5.69%            |
| Separate Account Assets     | 1,182  | 782    | 491    | 345    | 167    | 63.18%           |
| Total Assets                | 2,415  | 1,852  | 1,506  | 1,349  | 1,155  | 20.24%           |
| Capital and Surplus         | 369    | 365    | 359    | 308    | 272    | 7.94%            |
| Net GFO                     | 6      | 5      | 35     | 40     | 22     | -27.04%          |
| Net Income                  | 2      | 6      | 37     | 35     | 1      | 12.43%           |
| Return on Assets (Stat.)    | 0.16%  | 0.55%  | 3.67%  | 3.48%  | 0.13%  | 1.60%            |
| Return on Equity (Stat.)    | 0.51%  | 1.59%  | 11.11% | 11.95% | 0.43%  | 5.12%            |
| Risk Adjusted Surplus Ratio | 710.5% | 784.1% | 648.9% | 282.1% | 208.8% | 526.9%           |

Source: Annual Regulatory Financial Statements



► A BNY MELLON ASSET MANAGEMENT COMPANY<sup>SM</sup>

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